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State-Owned Enterprises and International Investment Treaties

When are State-Owned Entities and their Investments Protected?

PAUL BLYSCHAK*

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I. Introduction

The activity of Sovereign Wealth Funds (SWFs) and State-Owned Companies (SOCs), referred to collectively here as State-Owned Enterprises (SOEs), has been attracting intense scrutiny in recent years.¹ This is due in

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¹ Phillip Riblett, "A Legal Regime for State-Owned Companies in the Modern Era" (2008) 18:1 *J. Transnat'l L. & Pol'y* 1.

part to the remarkably rapid growth in their size, number and influence as they participate with increasing significance in industries of political, economic and strategic importance. The increased scrutiny can also be partially attributed to the fact that many SOEs hail from regions that have at times experienced strained relationships with the Western states in which they conduct much of their investment. Consequently, while Western states are interested in attracting SOE investment, they are simultaneously intent on ensuring that this investment is conducted in a politically neutral manner.

Investment by SOEs is regulated in multiple ways, and at multiple levels. At the international level a number of guidelines have been developed by supra-national organizations. Aimed at easing the concerns of national regulators and politicians, these prescribe best practices for SOEs, including transparency mechanisms and disclosure practices.² At the national level various countries have amended their foreign investment legislation to account for SOE activity by inserting tests relating to national security that must be met by inbound foreign investment. SOE investment is also subject to a third form of law and regulation that in its application to SOEs has gone largely overlooked to this point,³ namely international investment law of the kind contained in Bilateral or Multilateral Investment Treaties (BITs or MITs) such as Chapter Eleven of the *North American Free Trade Agreement (NAFTA)*⁴ and the *Energy Charter Treaty (ECT)*.⁵

The lack of scholarship on this point deserves remediation. While national investment review procedures screen proposed foreign SOE investment *ex ante*, international investment law applies to SOE investment *ex post*, when circumstances relating to the investment itself and to relevant national security issues may have changed substantially. Furthermore, international investment law was largely originally conceived and constructed to apply to foreign private investment rather than the foreign public investment carried out by SOEs. The application of international investment law to SOEs can therefore give rise to various legal ambiguities and conceptual difficulties. This is particularly the case with respect to the standing of SOEs to bring investment arbitration claims under International Investment Treaties (IITs) such as BITs and MITs. While the growing body of international investment law has generally been well received, it has also been the subject of controversy, not least for the often inconsistent rulings of

² See section II.1, below.

³ At the time of writing the author is aware of only a handful of other publications dealing with the relationship between international investment law and SOE investment. While these articles contribute greatly to current discussions of the regulation of SOE activity, they pay only cursory attention to the jurisdictional law applicable to that activity. See Mathius Audit, "Is the Erecting of Barriers against Sovereign Wealth Funds Compatible with International Investment Law?" (2009) 10 J. World Investment & Trade 617; Locknie Hsu, "Multi-Sourced Norms Affecting Sovereign Wealth Funds: A Comparative View of National Laws, Cross-Border Treaties and Non-binding 'Codes'" (2009) 10 J. World Investment & Trade 793 [Hsu, "Comparative View"]; Locknie Hsu, "Sovereign Wealth Funds, Recent US Legislative Changes, and Treaty Obligations" (2009) 43 J. World Trade 451.

⁴ 17 December 1992, Can. T.S. 1994 No. 2, 32 I.L.M. 289 and 32 I.L.M. 605 (entered into force 1 January 1994).

⁵ 17 December 1994, 2080 U.N.T.S. 100, 34 I.L.M. 360 (entered into force 16 April 1998).

investment arbitration tribunals.⁶ It is therefore important that the law pertaining to the jurisdiction of investment arbitration tribunals over claims brought by SOEs is developed in a consistent and comprehensive fashion that respects the rights and obligations of not only the States parties to IITs, but also the SOEs intended to benefit from them.

This article will attempt to lay the framework for such a body of law.⁷ In particular, as a roadmap for practitioners of international investment law, it will focus on some of the jurisdictional issues most likely to arise where SOEs pursue investment arbitration under IITs. This analysis will be composed of three parts. The next section will provide additional background on SOEs. It will examine their activities, the concerns that they have typically inspired in Western nations, and the domestic investment laws applicable to foreign SOEs that have been enacted partially in response to these concerns. Section three will then briefly review several concepts fundamental to the jurisdiction of investor-state tribunals, including the basic features and rationale of international investment law and arbitration. Section four then turns to the central analysis of the paper, focusing on two of the more problematic jurisdictional issues posed by SOEs' investment arbitration claims.

The first issue that may arise is whether or not investment by SOEs is protected by a particular IIT. Many IITs inadequately distinguish between privately and publically owned foreign investors. As such, in many instances it will not be immediately clear from the ordinary meaning of the IIT's terms whether a SOE has standing to bring arbitration. Where this is the case the relevant IIT must be interpreted on its own merits. The level of protection granted to SOEs is assessed by interpreting the jurisdictional provisions' ordinary meaning within the broader context of the IIT, as well as the larger objects and purposes underlying the agreement. This may include consideration of asymmetrical definitions of "investor" contained in the IIT, references to "public" or "private" investment in the IIT, and other provisions directly or indirectly referencing the participation of States parties or their agencies.

The second issue that may arise is whether the SOE has standing to bring its investment arbitration claim before the forum of its choice—typically the International Centre for the Settlement of Investment Disputes (ICSID),

⁶ See Susan D. Franck, "The Legitimacy Crisis in Investment Treaty Arbitration: Privatizing Public International Law Through Inconsistent Decisions" (2005) 73 Fordham L. Rev. 1521.

⁷ It must be noted that, although the regulation of SOEs under international investment law certainly raises a number of other very significant issues—such as the changing meaning of sovereignty and the division between the public and private domains—such issues are beyond the scope of the current paper. For enlightened discourse in this regard, see e.g. Larry Catá Backer, "Sovereign Investing in Times of Crisis: Global Regulation of Sovereign Wealth Funds, State-Owned Enterprises, and the Chinese Experience" (2010) 19 Transnat'l L. & Contemp. Probs. 3 at 20 ("Responses to sovereign investment have focused on law and policy to protect the integrity and workings of domestic and international markets by decentering the sovereign element of sovereign investment. However, this response lacks much of a plausible conceptual center."); Micah Schwab, "International Law & State Corporatism" (1 May 2008) at 73, online: <http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1350609> (Arguing that state corporatism is properly the subject of both "international and domestic law, and that international law must... evolve to recognize this particular aspect of international relations.").

pursuant to the *Washington Convention on the Settlement of Investment Disputes between States and Nationals of other States* (ICSID Convention).⁸ While investment arbitration before the ICSID has its advantages, it is also accompanied by added jurisdictional requirements. Most importantly for this article, ICSID arbitration is subject to the “Broches test” for jurisdiction, and is therefore unavailable to an SOE either “discharging an essentially governmental function” or “acting as an agent” of its home state. Moreover, although this two-pronged inquiry has been the accepted standard governing the availability of ICSID arbitration to SOEs for over 40 years, further analysis will reveal that its parameters remain rather insufficiently defined. This creates uncertainty as to the availability in different circumstances of ICSID arbitration to SOEs, demanding a review of the applicable law and commentary. In particular, these uncertainties demand a thorough inquiry into when a SOE will be considered to be “discharging essentially governmental functions,” when a SOE will be considered to be “acting as an agent” of its home state, and which entities will be considered SOEs in respect of ICSID arbitration in the first place.

II. State-Owned Enterprises and Domestic Investment Law

This section will discuss how the growth of SOEs during recent decades, and the accompanying rise in concerns regarding their influence, has resulted in increasing domestic regulation of their activities. It will explain the increasingly significant scale of SOEs’ activities, the intense domestic politics surrounding these activities, and the notable degree of ambiguity in much domestic investment law concerning SOEs. The discussion below does not directly relate to the jurisdictional issues in international investment law that are the focus of this article, but it does place these issues in context, and is essential to understanding why it is important to identify reliable legal principles to govern the standing of SOEs to bring investment claims under IITs.

1. The Increasing Significance of Sovereign Wealth Funds and State-Owned Companies

Sovereign wealth funds are defined by the United Nations Conference on Trade and Development (UNCTAD) as “a fund which is owned by the State or the Government and which is composed of financial assets such as stocks, bonds, property, gold, currencies and other investment vehicles.”⁹

⁸ 18 March 1965, 575 U.N.T.S. 159, 4 I.L.M. 532 (entered into force 14 October 1966). Investment arbitration tribunals can be constituted before a number of different international arbitration institutions, or under such independent arbitration rules such as the United Nations Commission on International Trade Law (UNCITRAL) *Model Law on International Commercial Arbitration*, U.N. Doc. A/40/17, Annex 1 (1985), 24 I.L.M. 1312. For a number of procedural reasons, the *ICSID Convention* is typically preferred by disaffected foreign investors. For further analysis of these considerations, please see sub-sections IV.1 and IV.3, below.

⁹ “The Protection of National Security in IIAs: UNCTAD Series on International Investment Policies for Development” (New York and Geneva: United Nations, 2009) at 19, online: <http://www.unctad.org/en/docs/diaeia20085_en.pdf> [UNCTAD, “National Security”]. See

The first SWFs were based in Middle Eastern countries,¹⁰ but these have recently been joined by similar investment vehicles from China, Russia, Brazil, Algeria, Libya and Venezuela.¹¹ As this history suggests, the growth of most SWFs can be tied to the rapid escalation of oil prices over the last decade and the increasing foreign reserves accumulated by oil and gas exporting nations as a result.¹² The Abu Dhabi Investment Authority, thought to be the world's largest SWF, was in 2007 estimated to hold over US\$875 billion in assets.¹³ In total, in 2007 the world's SWFs were estimated to hold over US\$15 trillion in assets, at least two thirds of which were international in nature.¹⁴ Indeed, SWFs now collectively control more capital than the international hedge fund industry.¹⁵

The goals pursued by SWFs vary but may include securing access to natural resources (including energy and minerals), growing national brands into global leaders, and strengthening international relationships.¹⁶ Specific interests prized by SWFs have traditionally included oil and gas properties, financial services, mining ventures and technology companies, but they have been diversifying their holdings as of late with ventures into the education, health and entertainment sectors.¹⁷ The type of assets pursued by SWFs has also evolved, moving from bonds and other financial instruments to real estate, hedge funds and, most noticeably, to equity investments.¹⁸ This includes greater participation in the mergers and acquisitions market, and lately the distressed assets markets, where high profile SWF action has included investments in Morgan Stanley, Merrill Lynch and Citigroup.¹⁹ The moves made by SWFs have at times been dramatic and have involved some major Western institutions. In 2008 the investment and real estate arms of Dubai World acquired a 20% stake in Cirque du Soleil, the world's largest live entertainment business.²⁰ In 2007 Borse Dubai purchased a 19.9% share

also Julius Melnitzer, "Cash Rules" *Lexpert: The Business Magazine for Lawyers* (October 2009) 83 at 83 (defining SWFs as "discrete pools of government-owned or controlled entities whose portfolios include international assets.").

¹⁰ The first SWF is believed to have been established in Kuwait in the 1950s. See Hsu, Comparative View, *supra* note 3 at 793.

¹¹ See Gerard Lyons, "State Capitalism: The Rise of Sovereign Wealth Funds" (2008) 14 L. & Bus. Rev. Am. 179.

¹² Charles Kovacs, "Sovereign Wealth Funds: Much Ado About Some Money" (1 October 2009) 14 Columbia FDI Perspectives, online: <<http://www.vcc.columbia.edu/content/sovereign-wealth-funds-much-adobt-about-some-money>>.

¹³ Audit, *supra* note 3 at 618. See also UNCTAD, "National Security", *supra* note 9 at 18-19. Some of the other largest SWFs include those hailing from Kuwait, China, Singapore and Norway. See also UNCTAD, *World Investment Report 2008: Transnational Corporations and the Infrastructure Challenge* (New York and Geneva: United Nations, 2008) at 20-26, online: <http://www.unctad.org/en/docs/wir2008_en.pdf>.

¹⁴ Melnitzer, *supra* note 9 at 83.

¹⁵ Laura Badian & Gregory Harrington, "The Politics of Sovereign Wealth: Global Financial Markets Enter a New Era" *The International Economy* (Winter 2008) 52 at 52.

¹⁶ Melnitzer, *supra* note 4 at 84.

¹⁷ *Ibid.* at 83.

¹⁸ *Ibid.*; See also Audit, *supra* note 3 at 618; Kovacs, *supra* note 12.

¹⁹ Melnitzer, *ibid.*

²⁰ *Ibid.*

in the NASDAQ Stock Market while simultaneously acquiring NASDAQ's 28% interest in the London Stock Exchange.²¹

The emergence of SWFs has seen a roughly parallel growth in the size and importance of State-Owned Companies. These are not pools of sovereign capital, but commercial corporate entities controlled or owned by sovereign states and engaged in specific sectors of strategic importance to those states.²² Unlike SWFs, SOCs are not a recent phenomenon and have experienced varying degrees of utilization across different historical and political boundaries.²³ However, like SWFs, the SOCs currently attracting the most attention are those involved in the energy sector.

This is the case for a number of reasons. First, national oil companies (NOCs) have grown into truly sophisticated international market players no longer dependent on the major international oil companies (IOCs) for the type of external technology, expertise and financing that they once were.²⁴ This has led to concern among certain economists that IOCs face an irreversible decline in size, number and clout.²⁵ Secondly, NOCs now hold over 90% of the world's known oil and gas reserves, while the four largest privately held and operated IOCs collectively hold less than 4%.²⁶ This has sparked anxiety among some economists that too much of conventional energy reserves rests in too few hands, and that politics rather than business interests could be the deciding factor in how and when these reserves are exploited.²⁷ Finally, certain NOCs, particularly those connected to China,²⁸

²¹ Badian & Harrington, *supra* note 15 at 55. See also Chris Lalonde, "Dubai or not Dubai?: A Review of Foreign Investment and Acquisition Laws in the U.S. and Canada", Note, (2008) 41 Vand. J. Transnat'l L. 1475 at 1492-1494.

²² Badian & Harrington, *ibid.* at 52.

²³ The US, for instance, has almost no tradition of government ownership and has historically looked upon direct public participation in the economy with scepticism and suspicion. See David E.M. Sappington & J. Gregory Sidak, "Competition Law for State-Owned Enterprises" (2003) 71 Antitrust L. J. 479; Mark E. Plotkin, "Foreign Direct Investment by Sovereign Wealth Funds: Using the Market and the Committee on Foreign Investment in the United States Together to Make the United States More Secure" (2008) 118 Yale L.J. Pocket Part 88 at 91. For a history of the Canadian government's participation in its oil industry through the creation and control of Petro-Canada, see Peter McKenzie Brown, "Melting Away" *Oilweek: Canada's Oil & Gas Authority* (November 2009) 58.

²⁴ Riblett, *supra* note 1 at 3, 25, citing Valérie Marcel, *Oil Titans: National Oil Companies in the Middle East* (Washington, D.C.: Brookings Institution Press, 2006) at 77, 80, 85, 228; Daniel Johnston, "Changing fiscal landscape" (2008) 1 J. World Energy L. Bus. 31 at 32.

²⁵ Carola Hoyos, "The New Seven Sisters: Oil and Gas Giants Dwarf Western Rivals" *Financial Times* (11 March 2007).

²⁶ Marcel, *supra* note 24; "National Oil Companies: Really Big Oil", *The Economist* (10 August 2006). Other sources claim that NOCs control only approximately 75% of the world's remaining oil reserves, depending on the calculation methods used. See Johnston, *supra* note 24. See also Hoyos, *supra* note 20 (The four largest IOCs in 2007 were, in decreasing order of reserves, ExxonMobil, BP, Chevron, and Royal Dutch Shell); Eric Reguly, "Mighty Big Oil No Match for Big Nationals" *The Globe and Mail* (12 January 2011).

²⁷ See Amy Myers Jaffe & Ronald Soligo, "Militarization of Energy: Geopolitical Threats to the Global Energy System" (Houston: The James A. Baker III Institute for Public Policy of Rice University, May 2008), online: <<http://www.rice.edu/energy/publications/WorkingPapers/IEJMilitarization.pdf>>.

²⁸ Chinese NOCs include China National Petroleum Corporation (CNPC), PetroChina, China National Offshore Oil Corporation (CNOOC) and China Petrochemical Corporation (Sinopec), among others. Other prominent NOCs include NIOC (Iran), ADNOC (Abu Dhabi), Rosneft and

have recently begun an invigorated campaign to increase their reserve holdings by acquiring stakes in major oil and gas projects, including those in the United States and Canada.²⁹ This has given rise to concerns that these investments are made in furtherance of geopolitical interests rather than profit.³⁰

It is difficult to ignore the increasingly heavy footsteps of these oil giants.³¹ The Seven Sisters, the privately owned and run IOCs that dominated global energy trade following the Second World War, have been usurped by the new sovereign “Seven Sisters” of Saudi Aramco, Gazprom, CNPC/PetroChina, the National Oil Company of Iran, Petrobras, Petronas and Petróleos de Venezuela.³² Saudi Aramco is widely considered to be the world’s largest company but, as it is not publically traded, this cannot be verified.³³ Thirteen separate NOCs control more reserves than does ExxonMobil, the world’s largest private oil company.³⁴ Some NOCs have grown so large they have been termed “states within states” at times capable of so dominating national politics that, rather than defending government interests, their agendas have come to direct government affairs.³⁵

2. Primary Concerns Regarding Sovereign Wealth Funds and State-Owned Companies

As the activities of SOEs have grown in scale and expanded into an increasing number of industries of political, economic and strategic importance, their activities have in many states become (at least until quite recently) the focus of a rising level of political and regulatory concern. Because of their ties to their home states, investments made by SWFs and SOCs raise different considerations among regulators compared to those raised when purely private enterprises pursue similar investments. Chief among these considerations is that in conducting their business, SOEs might

Gazprom (Russia), PDVSA (Venezuela), Kufpec (Kuwait), Petrobras (Brasil), Petronas (Malaysia), Sonatrach (Algeria), Statoil and Norsk Hydro (Norway), ONGC (India), ENI (Italy), Nippon Oil (Japan), CPC (Taiwan), EGPC (Egypt) and TPAO (Turkey).

²⁹ Sizhi Guo, “The Business Development of China’s National Oil Companies: The Government to Business Relationship in China” (Houston: The James A. Baker III Institute for Public Policy of Rice University, March 2007), online: <http://www.rice.edu/energy/publications/docs/NOCs/Papers/NOC_Guo%20China.pdf>; Eurasia Group, “China’s Overseas Investment in Oil and Gas Production” (New York: Eurasia Group, 16 October 2006), online: U.S.-China Economic and Security Review Commission, <www.uscc.gov/researchpapers/2006/oil_gas.pdf>; Maria Kielmas, “China’s Foreign Energy Asset Acquisitions: From Shopping Spree to Fire Sale?” (2005) 3:3 The China and Eurasia F.Q. 27.

³⁰ Johnston, *supra* note 24 at 33. See also Jaffe & Soligo, *supra* note 27.

³¹ See Marcel, *supra* note 24.

³² Hoyos, *supra* note 25; Reguly, *supra* note 26.

³³ For a discussion of the sometimes opaque operating practices of Saudi Aramco, see Matthew R. Simmons, *Twilight in the Desert: The Coming Saudi Oil Shock and the World Economy* (Hoboken, NJ: John Wiley & Sons, 2005).

³⁴ Johnston, *supra* note 24 at 32.

³⁵ Paul Stevens, “National Oil Companies and International Oil Companies in the Middle East: Under the Shadow of Government and the Resource Nationalism Cycle” (2008) 1 J. World Energy L. Bus. 5 at 18 (referring to Mexico’s Pemex). See also Backer, *supra* note 7 at 59 (arguing that sovereign investment has the potential to accomplish political goals through economic means).

consider subjugating market interests to political goals. As explained by the OECD:

when governments undertake commercial activities, they remain answerable to a wide range of societal pressures that their governance structures are designed to take into account. For this reason, governments may encounter difficulties in making credible commitments to pursue only “commercial” objectives, since their *raison d'être* involves being sensitive to political pressures and to pursuing non-commercial objectives.³⁶

Politicians, regulators, and other commentators are also concerned that politically motivated operations could lead to market inefficiencies, and that government linkages can increase the capacity of firms to act anti-competitively because they may not be fully exposed to market pressures.³⁷ In the case of SOCs, additional concerns are that these entities may pursue goals such as vertical integration, wealth distribution, and energy security, even if these specific government agendas conflict with the maximization of shareholder value.³⁸

These apprehensions, whether reasonable or not, have manifested themselves in several high profile political controversies in the United States and Canada surrounding recent attempted acquisitions. Dubai Ports World, owned by the government of Dubai, attempted in 2007 to acquire various US port terminals owned by P&O Ports, a private international conglomerate. This alarmed some members of the U.S. Congress, who viewed the proposed transaction as a threat to national security. The deal was eventually withdrawn.³⁹ Members of Congress responded with similar apprehension in 2005 to the attempt of the China National Offshore Oil Corporation (CNOOC) to purchase Unocal, a US based oil and gas company with diverse natural gas holdings, including fields in Southeast Asia.⁴⁰ Although

³⁶ Kathryn Gordon & April Tash, “Foreign Government-Controlled Investors and Recipient Country Investment Policies: A Scoping Paper” (Paris: OECD Investment Division, January 2009) at 10, online: <www.oecd.org/dataoecd/1/21/42022469.pdf>. For further discussion of the fears surrounding SWFs, see William Miracky *et al.*, “Assessing the Risks: The Behaviors of Sovereign Wealth Funds in the Global Economy” (Cambridge, MA: Monitor Group, June 2008), online: <http://www.monitor.com/Portals/0/MonitorContent/imported/MonitorUnitedStates/Articles/PDFs/Monitor_SWF_report_final.pdf>.

³⁷ Badian & Harrington, *supra* note 15 at 55-56, 84; Antonio Capobianco, “Competition Law and Foreign-Government Controlled Investors” (Paris: OECD Investment Division, January 2009) at 3; Gordon & Tash, *ibid.* at 8; Plotkin, *supra* note 24 at 89; Kara Scannell, “Cox Cites Concerns over Sovereign Wealth Funds” *Wall Street Journal* (25 October 2007) A8; Ronald J. Gilson & Curtis J. Milhaupt, “Sovereign Wealth Funds and Corporate Governance: A Minimalist Response to the New Mercantilism” (2008) 60 Stan. L. Rev. 1345 at 1362.

³⁸ Robert Pirog, “The Role of National Oil Companies in the International Oil Market: CRS Report for Congress” (Washington, D.C.: Congressional Research Service, 21 August 2007), online: Federation of American Scientists, <<http://www.fas.org/sgp/crs/misc/RL34137.pdf>>.

³⁹ These concerns focused on primarily on issues related to territorial security and the desirability of allowing a company controlled by a foreign state to have direct control over importation into the US of people and goods. See Lalonde, *supra* note 21 at 1491-1492; Deborah M. Mostaghel, “Dubai Ports World under Exon-Florio: A Threat to National Security or a Tempest in a Seaport?” (2007) 70 Alb. L. Rev. 583; Bashar H. Malkawi, “The Dubai Ports World Deal and U.S. Trade and Investment Policy in an Era of National Security” (2006) 7 J. World Investment & Trade 443. See also Bill Mongelluzzo, “Financial Crisis May Let DP World In” *The Journal of Commerce* (19 November 2008).

⁴⁰ See Joshua W. Casselman, “China’s Latest ‘Threat’ to the United States: The Failed CNOOC-

CNOOC's offer exceeded ChevronTexaco's by US\$2.1 billion and exceeded Unocal's value by approximately \$1.5 billion (based on its share listing price on the New York Stock Exchange), the fierce opposition the bid inspired among members of the House of Representatives eventually caused it to be withdrawn.⁴¹ In 2007 a similar reaction occurred amongst Canadian lawmakers when TAQA, Abu Dhabi's national energy company, sought to acquire Canadian based PrimeWest Energy Trust.⁴² Although eventually approved, the deal "ignited concerns that the current system operated too leniently and curbed consideration of national security concerns under the ICA review process."⁴³

Such controversies have recently become less common. While many governments still view SWFs and SOCs with distrust, the international economic downturn beginning in 2008, which was characterized by the tightening of credits markets and a dramatic decrease in investment flows, has caused many to re-evaluate their attitude toward inbound SOE capital,⁴⁴ and come to the conclusion that SOEs are capable of playing entirely positive roles in the global economy by providing equity injections into troubled institutions and stabilizing financial markets.⁴⁵ Indeed, rather than discouraging SOE international investment, leading Western-based corporations and governments are aggressively pursuing sovereign direct investment and "public calls for opening financial markets to SWFs now abound."⁴⁶ Many analysts argue that this correction is overdue and that SOEs have long been receiving an amount of attention disproportionate to their

Unocal Merger and its Implications for Exon-Florio and CFIUS", Note, (2007) 17 Ind. Int'l & Comp. L. Rev. 155. See also Pirog, *supra* note 38 at 8-9; Friedrich Wu, "The Globalization of Corporate China" (2005) 16:3 NBR Analysis, online: National Bureau of Asian Research, <<http://www.nbr.org/publications/issue.aspx?id=162>> (describing the suspicion and hostility, predicated on national and economic security concerns, that often accompanies the activities of Chinese corporations).

⁴¹ In this case, concerns related to possible negative effects on U.S. energy security. Guo, *supra* note 29 at 21-22; Steve Lohr, "Unocal Bid Denounced at Hearing" *The New York Times* (14 July 2005); "China Bashing: Giving China a Bloody Nose" *The Economist* (4 August 2005); David Olive, "US Seeing China Inc.: Reaction of US Lawmakers to Chinese Company's Bid to Buy Unocal is Not Only Hysterical, It's Foolhardy" *The Toronto Star* (3 July 2005) A18.

⁴² Lalonde, *supra* note 39 at 1494-1496. For earlier discussion the ICA review process, see Steven Chase & Simon Tuck, "National Security Bill Not Aimed at Energy Takeovers: Emerson" *The Globe and Mail* (15 July 2005) B1; Simon Tuck & Steven Chase, "Feds Eye New Hand on Foreign Ownership" *The Globe and Mail* (15 May 2006) B1.

⁴³ Lalonde, *ibid.* at 1495. These concerns have been repeated by Canada's federal government as recently as April 2011. See Steve Chase, "Harper Cautious About Future Chinese Resource Bids" *The Globe and Mail* (6 April 2011).

⁴⁴ Veljko Fotak & William Megginson, "Are SWFs Welcome Now?" (21 July 2009) 9 Columbia FDI Perspectives, online: <<http://www.vcc.columbia.edu/pubs/documents/FotakandMegginson-Final.pdf>> (describing how in early 2008 SWFs contributed to a temporary rescue of the international financial system by buying approximately \$60 billion of new equity issued by European and US banks).

⁴⁵ See Lyons, *supra* note 11.

⁴⁶ Fotak & Megginson, *supra* note 44, citing OECD, Investment Committee, "Sovereign Wealth Funds and Recipient Country Policies" (4 April 2008), online: <<http://www.oecd.org/dataoecd/34/9/40408735.pdf>>; Warren E. Buffet, "2008 Letter to the Shareholders of Berkshire Hathaway Inc." (27 February 2009), online: <<http://www.berkshirehathaway.com/letters/2008ltr.pdf>>. See also Luca Schicho, "Pride and Prejudice: How the Financial Crisis Made Us Reconsider SWFs" (2010) 2 Göttingen J. Int'l L. 63.

actual size and holdings in relation to the global economy at large.⁴⁷ Nevertheless, the political controversies triggered by SOE investment continue to play a critical role in SOE investment strategy and in the potential disputes that may arise between SOEs and host states.⁴⁸

3. National Investment Review Acts – the United States and Canada

Numerous entities and scholars have sought to promote guidelines and policies dealing with SOE activity. All of these try to respond to the domestic political concerns and controversies discussed above by striking a balance between the need to attract capital, and the goal of avoiding undesired interference by foreign governments in the operation of domestic markets.⁴⁹ Some scholars advocate a minimalist approach that focuses exclusively on corporate governance and shareholder voting rights.⁵⁰ Other commentators have advocated making the commercial activity of sovereigns an issue of global trade law.⁵¹ The Santiago Principles, developed by the International Monetary Fund together with the International Working Group of Sovereign Wealth Funds, are a code of conduct for SWFs themselves: a set of 24 voluntary principles that include basic governance and transparency standards.⁵² These have since been embraced by many of the major SWFs and the principal Western nations that now seek SWF capital.⁵³ The OECD

⁴⁷ See Kovacs, *supra* note 12 (argues that SWFs make good copy for the media due to their mysterious nature, the fact that they tend to hail from distant dictatorial regimes, and the fact that many of their transactions are otherwise newsworthy.).

⁴⁸ It has become increasingly common for SOEs to pursue alternatives to direct acquisitions, including joint venture arrangements. For example, when Sinochem considered mounting a rival bid to BHP Billiton's takeover attempt of Potash Corporation, speculation immediately began on whether the Chinese SOC would seek a local partner. See Jeffrey McCracken and Zachary Mider, "Sinochem Said to Be Likeliest Rival to BHP Potash Bid" *Bloomberg News* (27 September 2010), online: <<http://www.bloomberg.com/news/2010-09-27/sinochem-said-to-emerge-as-likeliest-rival-to-bhp-s-potash-bid.html>>. Unsurprisingly, the suggestion that the former Crown corporation could fall under the control of a foreign state also immediately sparked political concern. See "Sinochem Readyng PotashCorp Bid: Report" *Associated Press* (16 September 2010), online: <<http://www.cbc.ca/canada/saskatchewan/story/2010/09/16/potash-sinochem.html>>.

⁴⁹ Anna Gelpern, "A Sovereign Wealth Turn" (Rutgers School of Law-Newark Research Paper Series No. 025, 23 September 2008), online: <<http://ssrn.com/abstract=1272395>> (Draft, cited with permission of author). For a review of some of these mechanisms, see Yvonne C.L. Lee, "A Reversal of Neo-Colonialism: The Pitfalls and Prospects of Sovereign Wealth Funds" (2008-2009) 40 Geo. J. of Int'l L. 1103; Yvonne C.L. Lee, "The Governance of Contemporary Sovereign Wealth Funds" (2010) 6 Hastings Bus. L.J. 197.

⁵⁰ Gilson & Milhaupt, *supra* note 37 (Suggesting that where SOEs obtain shares of private corporations in non-controlling amounts, the voting rights of those shares should be suspended so long as they remain the property of the SOE.).

⁵¹ See Paul Rose, "Sovereigns as Shareholders" (2008) 87 N.C.L. Rev. 101 at 148-151 [Rose, "Sovereigns"]. For critical surveys of arguments that SWF investment should be made a matter of international trade regulation, see Bob Davis, "How Trade talks Could Tame Sovereign Wealth Funds" *Wall Street Journal* (29 October 2007) A2; Badian & Harrington, *supra* note 15 at 53.

⁵² *Sovereign Wealth Funds: Generally Accepted Principles and Practices – The "Santiago Principles"* (October 2008), online: <<http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf>>. See Rose, "Sovereigns", *ibid.* at 153-165 (an evaluation of the likely effectiveness of the Santiago Principles.)

⁵³ Fotak & Megginson, *supra* note 44. It is also important to note that the Santiago Principles were

has advised SOEs seeking to increase confidence in their operations to establish autonomous management structures, to list on stock exchanges, to allow partial private ownership, and to adopt transparent board nomination procedures and transparent disclosure and reporting practices.⁵⁴ The OECD Council has also sought to influence domestic regulations through its *Guidelines for Recipient Country Investment Policies Relating to National Security*.⁵⁵

However, the vast majority of regulation targeted at SOEs is maintained at a national level.⁵⁶ Under U.S. law, for example,⁵⁷ screening for national security purposes of foreign investment into the United States is a presidential power, and includes the authority to prohibit or suspend any foreign merger, acquisition or takeover of a U.S. enterprise that is identified as a threat to national security.⁵⁸ This power was delegated in 1988 to the Committee on Foreign Investment in the United States (CFIUS), a responsibility that remains with this administrative body.⁵⁹ In 1993 the responsibilities of CFIUS were expanded to include additional investigations where the acquiring entity is acting on behalf of or controlled by a foreign sovereign and the acquisition "could result in control of a person engaged in interstate commerce in the US that could affect the national security of the US."⁶⁰ In 2007 the *Foreign Investment and National Security Act*⁶¹ (FINSA) extended the scope of national security reviews to include "transactions involving critical infrastructure and energy, and requires a second-stage review investigation of most proposed acquisitions by state-owned companies."⁶² Notably, the 2008 Treasury Department regulations

crafted to apply to SWFs, and not necessarily to SOEs. See Backer, *supra* note 7 at 72.

⁵⁴ See OECD, *OECD Guidelines on Corporate Governance of State-owned Enterprises* (Paris, 2005), online: <<http://www.oecd.org/dataoecd/46/51/34803211.pdf>>.

⁵⁵ Recommendation adopted by the OECD Council (25 May 2009), online: <www.oecd.org/dataoecd/11/35/43384486.pdf>. For a discussion of foreign investment laws and codes see Ray August, *International Business Law: Texts, Cases, and Readings*, 4th ed. (Upper Saddle River, NJ: Prentice Hall/Pearson Education, 2004) at 244-265.

⁵⁶ Audit, *supra* note 3 at 621.

⁵⁷ This sub-section will examine examples of such regulation in the United States and Canada. However, these countries are not alone in integrating concerns over national security into legislation dealing with foreign investment. Germany, Australia, China and Russia, among others, have all adopted similar regulatory regimes. See Hsu, "Comparative View", *supra* note 3 at 804-817.

⁵⁸ See *Omnibus Trade and Competitiveness Act of 1988*, Pub. L. No. 100-418, §502, 102 Stat. 1107, amending *Defense Production Act of 1950*, Pub. L. No. 81-774, §721, 64 Stat. 698 (codified as amended at 50 U.S.C. App. §2061 *et seq.*). For a detailed history of CFIUS and investment law in the United States see David Bailey, "U.S. Policy Towards Inward FDI: CFIUS and Extension of the Concept of 'National Security'" (2003) 4 J. World Investment & Trade 867 (featuring at 872-878 a discussion of the Exon-Florio Amendment). See also Jose E. Alvarez, "Political Protectionism and United States International Investments Obligations in Conflict: The Hazards of Exon-Florio" (1989) 30 Va. J. Int'l L. 1 (critiques at 142-144 the failure of the CFIUS to subject Greenfield Investments to review).

⁵⁹ See *National Defense Authorization Act for Fiscal Year 1993*, Pub. L. No. 102-484, §837(a), 106 Stat. 2639 (1992), amending *Defense Production Act of 1950*, §721, *ibid*. See also Bailey, *ibid*. at 878-884.

⁶⁰ Audit, *supra* note 3 at 622, fn. 18.

⁶¹ *Foreign Investment and National Security Act*, Pub. L. No. 110-49, §2, 121 Stat. 246 (2007) (codified at 50 U.S.C. App. §2170).

⁶² Audit, *supra* note 3 at 622, fn. 18. See also Mark E. Plotkin & David N. Fagan, "The Revised National Security Review Process for FDI in the US" (7 January 2009) 2 Columbia FDI

implementing the *Act* define neither the concept of “control” by a foreign person, nor the contours of “national security.”⁶³

In Canada, the *Investment Canada Act*⁶⁴ (*ICA*) applies to the establishment of a new Canadian business, the direct acquisition of a Canadian business or the acquisition of an interest in or establishment of an entity carrying on all or any of its operations in Canada. The *ICA* is concerned with assessing whether a proposed transaction is “of net benefit to Canada,” and requires authorities to consider whether a proposed transaction is likely to result in further economic growth and employment opportunities.⁶⁵ In December of 2007 the Canadian government issued special guidelines to be followed by authorities reviewing transactions involving state-owned enterprises.⁶⁶ Recommended considerations include the SOE’s adherence to Canadian standards of corporate governance and transparency, as well as the nature and extend of foreign state control. The federal Minister of Energy at the time stated to the press that the government’s concern with investment by SOEs was not “with the ownership of the foreign capital being invested in Canada; but, rather, with how that capital behaves in the marketplace and the issue of reciprocity among nations as to whether state owned enterprises are allowed to invest.”⁶⁷ Like the *FINSA*, the *ICA* does not define “national security.”

The evolution of these statutes has inspired lively discussion, reflecting the complex mixture of political and commercial concerns captured by the activities of SOEs. Many critics contend that the lack of definitions for the crucial concepts of “control” and “national security” injects too much uncertainty into the review process in the amount of discretion it bestows upon reviewing authorities.⁶⁸ Others note that it “opens the door” to the imposition of political pressure “under the guise of the national security

Perspectives, online: <<http://www.vcc.columbia.edu/pubs/documents/Perspective2-PlotkinandFagan.pdf>>; George Stephanov Georgiev, “The Reformed CFIUS Regulatory Framework: Mediating Between Continued Openness to Foreign Investment and National Security” (2008) 25 Yale J. on Reg. 125.

⁶³ Plotkin & Fagan, *ibid*. For a discussion of the operations of CFIUS under the Obama administration, see Mark E. Plotkin & David N. Fagan, “Foreign Direct Investment and U.S. National Security: CFIUS under the Obama Administration” (7 June 2010) 24 Columbia FDI Perspectives, online: <http://www.vcc.columbia.edu/files/vale/print/Fagan_and_Plotkin-Final_0.pdf>.

⁶⁴ R.S.C. 1985, (1st Supp.), c. 28, ss. 11(a), 11(b).

⁶⁵ *Ibid.*, s. 2. For a discussion of the *ICA*, see Christopher C. Nicholls, *Mergers, Acquisitions, and Other Changes of Corporate Control* (Toronto: Irwin Law, 2007) at 47-54. Note that, unlike the *FINSA*, the *ICA* can apply to Greenfield Investments: *ICA*, *ibid.*, s. 11(a). Competition issues related to Canadian investment transactions, whether or not foreign in nature, are reviewed under the *Competition Act*, R.S.C. 1985, c. C-34. For a discussion of this statute, see Nicholls, *ibid.* at 30-47.

⁶⁶ Issued pursuant to s.38 of the *ICA*, by the Minister responsible for the statute’s administration. See “Investment Canada Act: All Guidelines” (updated 5 May 2011), online: Industry Canada, <www.ic.gc.ca/eic/site/ica-lic.nsf/eng/lk00064.html>.

⁶⁷ Robert T. Booth & Donald E. Greenfield, “Energy (Oil & Gas) – Corporate: Recent Developments of Importance,” reprinted from the 2008 *Lexpert/ALM Guide to the Leading 500 Lawyers in Canada*, online: <<http://www.bennettjones.com/Images/Guides/update3331.pdf>>.

⁶⁸ Rose, “Sovereigns”, *supra* note 51 at 130-137. See also W. Robert Shearer, “The Exon-Florio Amendment: Protectionist Legislation Susceptible to Abuse”, Comment, (1993) 30 Houston L. Rev. 1729.

rubric.”⁶⁹ After all, “national security” is an amorphous concept that can plausibly be raised in a number of industry sectors, including military, pipelines, ports, aviation and anything energy related.⁷⁰ These criticisms highlight the potential for the unpredictable or even arbitrary application of such ambiguous standards.

Still others are concerned that the guidelines do not go far enough and subject foreign acquisitions to too little scrutiny. Certain acquisitions, it is argued, although significant in the influence they bestow on SWFs and SOCs, will not necessarily be subject to review guidelines because they will not immediately result in control of a company.⁷¹ As described by the OECD, “minority shareholdings can have negative effects on competition, either by “reducing the minority shareholder’s incentives to compete” or “by facilitating collusion.”⁷² How will the inevitable gray zone between “pure commercial motives and unacceptable political motives” be handled, others ask.⁷³ They emphasize that governments have various means of exercising control and that government participation can take many forms and can evolve over time.⁷⁴ This second set of criticisms highlights the risk that the regulatory regime applicable to SOE investment, with its perceived lacunae, may yet undergo significant changes aimed at subjecting SOE investment to considerably stricter supervision.

Therefore, in sum, foreign investment by SOEs occurs in a highly uncertain context. Due to their participation in strategically important economic sectors, including the energy sector, SOE investment is frequently the focus of intense political controversy. On the other hand, the domestic regulation of SOE investment activity remains characterized by a number of ambiguous tests and subjective standards. Together, the result is the

⁶⁹ Melnitzer, *supra* note 9 at 85, quoting George Addy of Davies Ward Phillips & Vineberg LLP.

⁷⁰ *Ibid.* at 86, quoting Catherine Pawluch of Gowling Lafleur Henderson LLP; Audit, *supra* note 3 at 618.

⁷¹ Badian & Harrington, *supra* note 15 at 54. Note also that certain foreign investment regulators and regulations recognize that “lack of control”, as defined by securities law, does not mean a total absence of influence or “soft” power. The new rules regulating CFIUS examinations, for instance, provide for such power by stipulating that SWF control may be identified where the fund directs the company to engage in “certain important matters,” including inducing a decision to reorganize, merge, sell assets, issue securities, or causing the appointment or dismissal of officers or senior managers. As such, even if a SWF doesn’t attract CFIUS scrutiny upon its initial entry into the U.S., the possibility of a CFIUS investigation nonetheless constantly hovers above its interests so long as they remain. Furthermore, CFIUS has the ability to require that SOEs enter into “mitigation agreements” that may stipulate special audits or even that SWFs forego filling boardroom seats. See Paul Rose, “Sovereign Wealth Funds: Active or Passive Investors?” (2008) 118 Yale L.J. Pocket Part 104. [Rose, “Active or Passive”]; Rose, “Sovereigns”, *supra* note 51 at 126-128.

⁷² Capobianco, *supra* note 37 at 5-6.

⁷³ Gordon & Tash, *supra* note 36 at 9.

⁷⁴ *Ibid.* at 4, citing International Working Group of Sovereign Wealth Funds, “Sovereign Wealth Funds: Current Institutional and Operational Practices” (15 September 2008), online: <<http://www.iwg-swf.org/pubs/eng/swfsurvey.pdf>>. It has also been argued that, while countries such as the US and Canada have the ability to police the operation of SOEs within their borders, these same countries may nonetheless be indirectly harmed by SOE activity and the market distortions they can create in less regulated foreign jurisdictions. As Paul Rose highlights, strategic purchases of vital overseas energy reserves or commodity producers have the potential to threaten North American security interests more drastically than similar activity within the continent: “Sovereigns”, *supra* note 51 at 106-107, 165.

continued and constant possibility that SOEs may be subject to discriminatory or arbitrary governmental, regulatory or administrative treatment motivated more by political considerations than by genuine cause to be concerned with the nature, scope or purpose of their operations. In this light, it is of immediate importance to determine the standing of SOEs to bring investment arbitration claims so that, where such illegitimate treatment is alleged to have occurred, the entitlement of SOEs to seek recourse under international law is clear.

III. International Investment Law in a Nutshell

Before turning to the specific jurisdictional issues in international investment law that are the focus of this paper, it is necessary to review some of the basic history and characteristics of this often complex area of law. The history of international investment law does not read completely dissimilarly to that of SOEs. Like the first SWF, the BITs and MITs that compose the body of contemporary international investment law first appeared in the late 1950s.⁷⁵ Following the Second World War a main concern of Western nations was to rebuild the international economy in a manner that would safeguard against renewed global conflict. Increasing the amount of international investment and trade was seen as central to this assignment, as this would lead to increased political and economic interdependence and act as a natural deterrent to aggressive actions.⁷⁶ At first it was hoped that a broadly signed multilateral treaty on investment could be achieved that would create a uniform body of international investment law.⁷⁷ However, when this proved to be too ambitious a diplomatic endeavour those nations most committed to the project fell back on bilateral and smaller multilateral efforts.⁷⁸ In time the investment treaty movement gathered momentum, with over 2600 BITs having been signed by the end of 2008.⁷⁹

⁷⁵ The first BIT was signed between West Germany and Pakistan in 1959. See *Treaty for the Protection of Investment*, 25 November 1959, 457 U.N.T.S. 23.

⁷⁶ Bernardo M. Cremades & David J.A. Cairns, "The Brave New World of Global Arbitration" (2002) 3 J. World Investment 173 at 175.

⁷⁷ See Franziska Tschofen, "Multilateral Approaches to the Treatment of Foreign Investment" (1992) 7 ICSID Rev. – F.I.L.J. 384.

⁷⁸ See *ibid*. For a discussion of multilateral approaches to investment in the context of international trade, see also Michael J. Trebilcock & Robert Howse, *The Regulation of International Trade*, 3d ed. (London: Routledge, 2005); Cremades & Cairns, *supra* note 76 at 180; Glen Kelly, "Multilateral Investment Treaties: A Balanced Approach to Multinational Corporations" (2001) 39 Colum. J. Transnat'l L. 483; S. Gudgeon, "US Bilateral Investment Treaties: Comments on Their Origins, Purposes and General Treatment Standards" (1986) 4 Int'l Tax & Bus. Law. 105 at 111.

⁷⁹ UNCTAD, "Recent Developments in International Investment Agreements (2008-June 2009)", IIA Monitor No.3 (2009), U.N. Doc. UNCTAD/WEB/DIAE/IA/2009/8, online: <http://www.unctad.org/en/docs/webdiaeia20098_en.pdf>. See also Zachary Elkins, Andrew T. Guzman & Beth A. Simmons, "Competing for Capital: The Diffusion of Bilateral Investment Treaties, 1960-2000" (2006) 60 Int'l Org. 811. Note that while investment treaties have been popular for several decades, it is only within the last 10 years that the arbitration provisions of these treaties have been relied on consistently by foreign investors.

Like the development of the largest SWFs and SOEs, much of the development of the investment treaty regime can be linked to the needs of the oil and gas industry. IITs are designed to promote cross-border investment flows in two main ways. First, they obligate host governments to provide certain protections to foreign investors. These include guarantees of National Treatment, Most Favoured Nation treatment, treatment in accordance with the International Minimum Standard, Fair and Equitable treatment, protection against performance requirements, and compensation in the event of expropriation or actions tantamount to expropriation.⁸⁰ Second, they provide a neutral and reliable forum for the settlement of disputes in which an investor alleges that a host government has breached one of these standards of protection.⁸¹ Disputes are resolved by tribunals of independent arbitrators in neutral sites and not in the courts of the host state. The home state of the investor need not be involved in any way.⁸² Such guarantees of protection and reliability of enforcement are of particular value in international energy projects, characterized as they are by long time horizons, large and immovable assets, and acute sensitivity to economic and political cycles.⁸³ Indeed, approximately 30% of investment disputes involve this sector.⁸⁴ These characteristics are, for similar reasons, also of particular value to SOEs—particularly in comparison to the relatively political domestic regulatory regimes discussed in the previous section.

Investment arbitrations can be conducted pursuant to the UNCITRAL Model Law or according to the Arbitration Rules of the ICSID,⁸⁵ a forum specifically dedicated to investor-State disputes.⁸⁶ Arbitrations may also take place under the auspices of a number of other arbitral institutions, including

⁸⁰ The consistent appearance of these provisions across different IITs is primarily due to the popularity of standard form BITs, developed by international organizations such as the OECD. Furthermore, the protective provisions contained in these model treaties originate primarily in disputed principles of customary international law on foreign investment. See Rudolf Dolzer & Margrete Stevens, *Bilateral Investment Treaties* (The Hague: Kluwer Law International, 1995); Jeswald W. Salacuse, "BIT by BIT: The Growth of Bilateral Investment Treaties and their Impact on Foreign Investment in Developing Countries" (1990) 24 Int'l Law. 655.

⁸¹ Foreign investors have generally been concerned that local courts, particularly those located in developing or underdeveloped countries, would be unable to safeguard their concerns in a fair manner. They worried that the legal systems in these countries would lack the sophistication to handle in a predictable and timely manner the complex matters investment disputes can raise. They also worried that they could not rely on these forums to impartially decide their dispute without showing favour to the host government. See Ibrahim F.I. Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Role of ICSID and MIGA* (Washington: ICSID, 1993); Gudgeon, *supra* note 78.

⁸² Prior to the advent of investor-state arbitration the only recourse available to foreign investors was state-to-state adjudication before international courts, such as the ICJ. This required the investor to petition its home government for such advocacy, which was by no means guaranteed and in fact quite rare. See Andrew Newcombe & Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (The Hague: Kluwer Law International, 2009) at 3-18. [Newcombe & Paradell]

⁸³ See Thomas W. Waelde, "International Energy Investment" (1996) 17 Energy L. J. 191.

⁸⁴ L.A. Ahee & R.E. Walck, "Investment Arbitration Update (As Of December 31, 2008)" [2009] 1 Transnat'l Disp. Management.

⁸⁵ See *ICSID Convention*, *supra* note 8.

⁸⁶ For a comparison of some of the differences between these systems of arbitration see Giorgio Sacerdoti, "Investment Arbitration under ICSID and UNCITRAL Rules: Prerequisites, Applicable Law, Review of Awards" (2004) 19 ICSID Review – F.I.L.J. 1.

the International Chamber of Commerce in Paris and the Stockholm Chamber of Commerce. Each forum and set of rules has its own particular characteristics and related appeal for disputing parties,⁸⁷ but the ICSID system incorporates two particular advantages for investors that are unmatched by its peers. First, ICSID awards are not subject to review by the courts of the jurisdiction in which they have been rendered.⁸⁸ Secondly, awards rendered by ICSID tribunals are enforceable in countries that have signed the *ICSID Convention* as though they are final awards of such states' domestic legal systems.⁸⁹ For these reasons, investors will typically elect to pursue investment arbitration before an ICSID tribunal over another arbitral forum, where ICSID arbitration is available to them. However, for this to be the case both the home government of the investor and the host government must have ratified the *ICSID Convention*.⁹⁰

In discussing the application of international investment law to transactions involving SWFs and SOCs it is necessary to distinguish between the pre-investment and post-investment phases.⁹¹ Most IITs afford protection only to post-investment activities.⁹² This means that, generally speaking, the decision made by national investment authorities screening proposed inbound foreign investment by SWFs and SOCs will not be subject to review by investment arbitration tribunals. This may be explicitly stated in an IIT. For example, under NAFTA Art. 2102 the States parties have the right to deny inward bound foreign investment on the ground of national security concerns. Furthermore, pursuant to Art. 1138(1), such a decision is exempt from review. Other IITs, such as the *ECT*, distinguish between pre-investment and post-investment phases to impose binding obligations on

⁸⁷ For example, Stockholm has historically been a popular venue for disputes between Western nations and states from the former Communist bloc, particularly for the latter.

⁸⁸ This effectively protects ICSID awards from review at the point of execution. See Sacerdoti, *supra* note 86.

⁸⁹ This effectively protects ICSID awards from review at the point of enforcement. See *ibid*.

⁹⁰ Investment arbitration awards rendered by non-ICSID tribunals are almost always enforced pursuant to the terms of the *New York Convention on the Recognition and Enforcement of Arbitral Awards*, 10 June 1958, 330 U.N.T.S. 38 (entered into force 7 June 1959).

⁹¹ The distinction between pre- and post-investment activities is not always easy to draw. For example, in *Mihaly International Corporation v. Sri Lanka* (Award of 15 March 2002), ICSID Case No. ARB/00/2, 17 ICSID Rev. 142, 41 I.L.M. 867, the facts required the tribunal to decide whether expenditures made in preparation for a "build-own-transfer" contract for a power plant constituted an investment made in Sri Lanka. See also Robert N. Hornick, "The Mihaly Arbitration Pre-Investment Expenditure as a Basis for ICSID Jurisdiction" (2003) 20 J. Int'l Arb. 189; C. Chatterjee, "When Pre-investment or Development Costs May or May Not be Regarded as Part of 'Investment' under Article 25(1) of the ICSID Convention – The Mihaly Case" (2003) 4 J. World Investment 909.

⁹² See Anna Joubin-Bret, "Admission and Establishment in the Context of Investment Protection" in A. Reinisch, ed., *Standards of Investment Protection* (New York: Oxford University Press, 2008) 9 at 10-11; UNCTAD, "National Security", *supra* note 9 at 28-29. Where IITs do protect pre-establishment activities, they normally do so through similar provisions used to protect post-establishment assets and activities, including non-discrimination, national treatment and most-favoured nation treatment. Note that it has been argued that, regardless of whether or not an IIT protects pre-investment expenditures, disputes based on these actions cannot be brought before ICSID due to the *ICSID Convention's* internal 'definition' of investment. See Christoph H. Schreuer, *The ICSID Convention: A Commentary*, 1st ed. (Cambridge: Cambridge University Press, 2001) at Art. 25, para 101.

host states solely in relation to the latter.⁹³ The situation is similar under customary international law. Absent any binding commitment to the contrary it is the sovereign right of states to decide who and what, including capital and legal entities, is allowed entry into their territory, whether physically or otherwise.⁹⁴

Therefore, should SOEs consider bringing international investment arbitration claims against the states in which they have invested, it is far more likely that they will bring such claims in relation to government actions that have occurred some time into that investment's lifespan rather than at the point of entry. As mentioned, depending on the terms of the particular IIT at play, this could be, *inter alia*, for treatment the SOE believes is discriminatory, for treatment that the SOE believes is less favourable than that afforded to similar national enterprises, or for treatment that is less than fair and equitable.⁹⁵ In fact, because of the broad nature of most foreign investment protection provisions, the possible range of government action capable of triggering an investment claim is beyond description.⁹⁶

In contrast, the range of jurisdictional issues raised by potential investment arbitration claims by SOEs is far more capable of precise portrayal. Every such dispute will inevitably be unique, but the jurisdictional requirements encountered by them will not. IITs have developed a standard form over time from which only relatively moderate deviation is made,⁹⁷ and SOEs have to date been addressed by these in a relatively limited number of ways. That does not mean that the jurisdictional issues raised by SOEs are simple, however. The remainder of this article is devoted to addressing these clearly defined—yet significantly complex—jurisdictional issues.

IV. State-Owned Enterprises and the Jurisdiction of Investment Arbitration Tribunals

This section will focus on two of the more problematic jurisdictional issues that arise under IITs in connection with investment claims brought by SOEs. Before turning to each of these issues, however, the section will review the basic principles of arbitration tribunal jurisdiction and the complex preliminary issue of investor standing—whether a tribunal arbitrating pursuant to a particular IIT will have jurisdiction over a particular SOE.

⁹³ The former is only subject to a “soft” regime of “best endeavour” obligations. See *ECT, supra* note 5, Art. 10(1), (2); Kaj Hobér, “The Energy Charter Treaty: An Overview” (2003) 8 J. World Investment & Trade 323 at 325, 327–328.

⁹⁴ See Joubin-Bret, *supra* note 92 at 10.

⁹⁵ For a comprehensive treatment of the various standards of protection included in IITs, see Newcombe & Paradell, *supra* note 82.

⁹⁶ International investors tend to applaud this reality. Others are far more critical. In particular, opponents of international investment law frequently cite the “regulatory chill” that can result from administrators fearful of infringing obligations assumed in investment treaties. See generally Gus van Harten, “Private Authority and Transnational Governance: The Contours of the International System of Investor State Protection” (2005) 12 Rev. of Int’l Pol. Economy 600; Lyuba Zarsky, “From Regulatory Chill to Deep Freeze?” (2006) 6 Int’l Envtl. Agreements 395.

⁹⁷ See Dolzer & Stevens, *supra* note 80 at 54. See also Kenneth J. Vandeveld, “A Brief History of International Investment Agreements” (2005) U.C. Davis J. Int’l L. & Pol’y 162.

1. SOEs and International Investment Treaties

IITs typically contain two main jurisdictional requirements. First, the investor must have made an investment in the territory of the host state. This provides an investment tribunal with jurisdiction *ratione materiae*, also known as subject matter jurisdiction. The definition of "investment" included in most IITs is typically broad and encompasses such interests as shares, contractual rights, and rights to profits.⁹⁸ Secondly, the investor must be a national of a State party to the IIT under which the investor is making its claim. This provides an investment tribunal with jurisdiction *ratione personae*, or jurisdiction over the person. In the case of an investor that is a natural person, most IITs will generally focus on whether or not that person is a citizen of the home state.⁹⁹ In the case of an investor that is a juridical entity, such as a corporation, most IITs will focus on certain characteristics of that entity's formation.¹⁰⁰ Some treaties require simply that the entity is constituted in accordance with the laws of a state.¹⁰¹ Other treaties may require that the entity is both incorporated in the jurisdiction and have its place of effective management there.¹⁰²

The particular tests for both jurisdiction *ratione materiae* and jurisdiction *ratione personae*—the tests each "investment" and "investor" will respectively have to meet—will depend on the wording of each particular IIT. However, if arbitration with respect to a particular IIT is pursued under the *ICSID Convention*, the additional definitions of "investment" and "investor" under that treaty will also have to be met.¹⁰³ Conversely, if the investor wishes to avoid the added jurisdictional requirements of the *ICSID Convention* it can simply proceed under or before any alternative rules or forum available.¹⁰⁴

When an SOE is involved in an investment dispute under an IIT, questions surrounding the jurisdiction *ratione personae* of a tribunal are likely

⁹⁸ Barton Legum, "Defining Investment and Investor: Who is Entitled to Claim?" (2006) 22 Arb. Int'l 521. For a description of some of the more controversial issues to arise in relation to "investment" requirements see Sébastien Manciaux, "The Notion of Investment: New Controversies" (2008) 9 J. World Investment & Trade 443.

⁹⁹ Catharine Yannaca-Small, "Definition of Investor and Investment in International Investment Agreements", in *International Investment Law: Understanding Concepts and Tracking Innovations* (Paris: OECD, 2008) 7 at 10-17, online: <<http://www.oecd.org/dataoecd/3/7/40471468.pdf>>.

¹⁰⁰ *Ibid.* at 17-38.

¹⁰¹ For example, the Greece-Cuba BIT defines investors with regard to either Contracting Party as "legal persons constituted in accordance with the laws of that Contracting Party." See *Agreement between the Government of the Hellenic Republic and the Government of the Republic of Cuba on the Promotion and Reciprocal Protection of Investments*, 18 June 1996, Art. 1(3), online: <<http://www.unctadxi.org/templates/DocSearch.aspx?id=779>>.

¹⁰² For example, article 3(b) the Germany-China BIT defines German investors to include "any juridical person as well as any commercial or other company or association with or without legal personality having its seat in the territory of the Federal Republic of Germany." See *Agreement between the Federal Republic of Germany and the People's Republic of China concerning the encouragement and reciprocal protection of investments*, 7 October 1983, 1475 U.N.T.S. 262, online: <http://untreaty.un.org/unts/60001_120000/23/21/00045007.pdf>. This more robust requirement effectively prohibits shell companies from gaining standing under such treaties.

¹⁰³ Yannaca-Small, *supra* note 99 at 14-17, 33-38, and 59-61.

¹⁰⁴ Although, as mentioned, this would mean sacrificing the benefits of the *ICSID Convention* regarding the enforcement and execution of awards as well as the judicial review of awards.

to raise more complicated issues than questions surrounding its jurisdiction *ratione materiae*. Definitions of investment in IITs turn on the nature of participation in the domestic economy by a purported foreign investor; the nature of the participant is typically irrelevant.¹⁰⁵ Since the nature of SOEs' investments is largely indistinguishable from that of purely private entities, the issue of a tribunal's jurisdiction *ratione materiae* should thus not be complicated by the fact that the investment at issue was engaged in by a state-owned entity.

By contrast, the fact that an investor is owned or controlled by a sovereign state could very well prove decisive in determining whether the tribunal has jurisdiction *ratione personae*. IITs were not originally designed with SOEs in mind. Attracting and protecting private investment was at the forefront of negotiators' minds, rather than facilitating transnational flows of sovereign capital.¹⁰⁶ This is particularly the case in regards to the *ICSID Convention*, one of the express purposes of which was to depoliticize investment disputes.¹⁰⁷ As a result, IITs, including their definitions of "investor," are often ambiguous with respect to the standing of SOEs and claims levied by such entities will do much to test the limits of investment arbitration under these treaties and the *ICSID Convention*.¹⁰⁸

Practitioners will therefore face a number of uncertainties in assessing the jurisdiction *ratione personae* of an arbitration tribunal over a particular SOE. First, what steps should be followed in interpreting the extent of a tribunal's jurisdiction *ratione personae* pursuant to an IIT in respect of a SOE claimant? In particular, how should contextual sources be deployed in the event an IIT does not clearly provide for claims by SOEs? Secondly, in what circumstances will an SOE be denied standing to bring an investment arbitration claim before the ICSID, due to the operation of either branch of the "Broches test"? In particular, which SOEs will be considered to be "discharging an essentially governmental function" of their home states, in what circumstances will an SOE be considered to be "acting as an agent" of its home state, and when will an entity be considered an SOE for the purpose

¹⁰⁵ See e.g. *NAFTA*, *supra* note 4, Art. 1139 (defines investment through reference to a list of various means of participating in economic activity, including equity, debt, loans, real estate or other property, and various forms of contractual relations such as concessions. The nature of the investor involved in the transaction is not material.).

¹⁰⁶ "Report of the Executive Directors on the Convention of the Settlement of Investment Disputes between States and Nationals of Other States, 1965" (1993) 1 ICSID Rep. 23.

¹⁰⁷ See Shihata, *supra* note 81; Schreuer, *supra* note 92, Art. 25, para 270.

¹⁰⁸ For a brief treatment of these issues, see Michael D. Nolan & Frédéric G. Sourges, "State-controlled Entities as Claimants in International Investment Arbitration: An Early Assessment" (2 December 2010) 32 Columbia FDI Perspectives, online: <http://www.vcc.columbia.edu/files/vale/print/Perspectives_-_Nolan_Sourges_Final_0.pdf>. As noted by the authors, SOEs already frequently act as claimants in contractual commercial arbitrations. However, examples of SOEs as claimants in investment arbitration are to date far less common, and raise complex issues. See *Telenor Mobile Communications A.S. v. Republic of Hungary* (Award of 13 September 2006), ICSID Case No. ARB/04/15, online: <http://www.iisd.org/pdf/2006/itn_telenor_hungary.pdf>; *CDC Group plc v. Republic of the Seychelles* (Award of 17 December 2003) ICSID Case No. ARB/02/14. In both of these cases the investor had close ties to the government of the home state; in neither case, however, did the Respondent state object to these ties at the jurisdictional phase of the proceedings.

of these tests in the first place? The remainder of this article is dedicated to addressing in detail these important jurisdictional uncertainties.

2. Jurisdictional Issue #1: Does an SOE have Standing under an IIT?

According to Art. 31(1) of the *Vienna Convention on the Law of Treaties* (*VCLT*),¹⁰⁹ “a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.” Where an investment tribunal is tasked with determining whether an SOE has standing to institute investment arbitration under a particular IIT, this interpretive analysis will not always be a difficult exercise. Many IITs do contain express provisions protecting SOE investment.

Article 201(1) of *NAFTA*, for example, defines “enterprise” as “any entity constituted or organized under applicable law, whether or not for profit, and whether privately-owned or governmentally-owned, including any corporation, trust, partnership, sole proprietorship, joint venture or other association” [emphasis added]. Identical language also appears in both the 2004 *Model U.S. Bilateral Investment Treaty*,¹¹⁰ and Canada’s 2004 model for Foreign Investment Promotion and Protection Agreements.¹¹¹ Similarly, Art. 13(a)(iii) of the *Convention establishing the Multilateral Investment Guarantee Agency*¹¹² includes within the definition of investor legal entities “whether or not privately owned.” Other IITs specifically extend protection not only to government controlled entities but also to the home government itself. The BIT between the Czech Republic and Kuwait, for example, defines “investor” to include, “with respect to either Contracting State, the Government of that Contracting State.”¹¹³ Furthermore, this express inclusion of the States parties in the definition of “investor” is in addition to a host of other possible government organs or appendages, including “institutions, development funds, authorities, foundations, establishments [and] agencies.”¹¹⁴

Where the protection of an IIT is expressly extended to SOEs, the ordinary meaning of the IIT pursuant to Art. 31 *VCLT* will largely settle the interpretive issue. Further examination of the IIT’s context and object and purpose will rarely (if ever) over-ride the effect of explicit provisions protecting SOEs. Absent any express provision to the contrary the SOE will be entitled to the exact same treatment as a purely private investor, regardless of its quasi-public nature. However, this is not the case where an IIT is more ambiguous as to its treatment of investors of a sovereign nature—in other words, where the plain meaning of the IIT is less informative. In

¹⁰⁹ (23 May 1969), 1155 U.N.T.S. 331, 8 I.L.M. 679 (entered into force 27 January 1980) [*VCLT*].

¹¹⁰ Online: <<http://www.state.gov/documents/organization/117601.pdf>>.

¹¹¹ Online: <<http://www.international.gc.ca/trade-agreements-accords-commerciaux/assets/pdfs/2004-FIPA-model-en.pdf>>.

¹¹² 11 October 1985, 24 I.L.M. 1598 (entered into force 12 April 1988).

¹¹³ *Agreement between the Czech Republic and the State of Kuwait for the Promotion and Protection of Investments*, 8 January 1996, Art. 1(2)(b), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/czech_kuwait.pdf>.

¹¹⁴ *Ibid.*

these circumstances, it will be necessary to rely on the latter two interpretive sources set out in Art. 31(1) of the *VCLT*, and assess whether protection for SOE investors is implied either by the context or by the object and purpose of the IIT.¹¹⁵ This may prove a thorny undertaking.

It has been suggested by UNCTAD that a presumption in favour of extending protection to SOEs should apply.¹¹⁶ This interpretation is said to follow from a “plain meaning” approach to the term “legal entity”: according to UNCTAD, the term “is usually broadly understood as any kind of juridical entity constituted or organized under the applicable laws of a party. This means that, unless the [IIT] states something to the contrary, State enterprises... are normally protected under the [IIT].”¹¹⁷ However, further investigation reveals this simplifying proposition to be of somewhat limited utility in the highly context-dependent area of international investment law. While it is reasonably arguable that the mere term “legal entity” should be construed to include state-owned legal entities, it is important to recognize that IITs can contradict this proposition in ways not immediately apparent: locating express and implied contradictions of SOE standing will often require consideration of various other provisions commonly included in IITs, including not only those related to the definition of “investor,” but also those not immediately related to this term. A brief review of several IITs concluded by various countries is illustrative of provisions that potentially contradict the proposed UNCTAD presumption, as well as the interpretive issues they raise.

One possibility is that an IIT may contain multiple definitions of investor that diverge significantly in their treatment of SOEs. The BIT between China and Qatar, for example, defines “investor” in respect of Qatar to include “legal persons including companies, general corporations, *public organizations, public and semi-public entities* constituted in accordance with the legislation of... Qatar and domiciled in its territory.”¹¹⁸ However, the same article defines “investor” in respect of China to include only “economic entities established in accordance with the laws... of China and domiciled in the territory of... China.”¹¹⁹ A similar asymmetry exists in China’s BIT with Ghana, where an identical definition of “investor” in respect of China is provided while a Ghanaian “investor” is defined to include “*state corporations*

¹¹⁵ For example, the “intentions” school was relied on to determine the scope of consent in both *Inceysa Vallisoletana S.L. v. Republic of El Salvador* (Decision on Jurisdiction of 2 August 2006), ICSID Case No. ARB/03/26 at paras. 177-178 [*Inceysa v. El Salvador*], and *Amco Asia Corp. v. Republic of Indonesia* (Award of 25 September 1983) ICSID Case No. ARB/81/1 at para 14. See also *The Rompetrol Group N.V. v. Romania*, (Decision on Respondent’s Preliminary Objections on Jurisdiction and Admissibility, 18 April 2008), ICSID Case No. ARB/06/3 [*Rompetrol v. Romania*] at para. 107 (holding that where confusion as to the intention of the parties arises, the best means available to attempt to safeguard those intentions is “the unequivocal terms of the treaty text on which they formally agreed” as “that is the approach which the Vienna Convention requires.”).

¹¹⁶ UNCTAD, “National Security”, *supra* note 9 at 43.

¹¹⁷ *Ibid.*

¹¹⁸ *Agreement Between the Government of the People’s Republic of China and the Government of the State of Qatar Concerning the Encouragement and Reciprocal Protection of Investments*, April 1999, Art. 1(2)(b), online: <http://www.unctad.org/sections/dite/iia/docs/bits/china_qatar.pdf> [emphasis added].

¹¹⁹ *Ibid.*

and agencies and companies registered under the laws of Ghana which invest or trade abroad.”¹²⁰ Therefore, while the definitions of Chinese investors under these treaties do nothing to expressly exclude the standing of Chinese SOEs, the express inclusion of SOEs within the definitions of Qatari and Ghanaian investors suggests that perhaps Chinese SOEs were not intended to be granted standing. Stated differently, the express inclusion of SOEs within the definitions of Qatari and Ghanaian investors suggests that, had the parties intended to give standing to Chinese SOEs, they would have included similar language in respect of these entities.

Another possibility is that an IIT may contain multiple definitions of “investor” that diverge significantly in their construction, but which are all immediately silent as to their treatment of SOEs. The BIT between China and Peru, for example, defines “investor” in respect of Peru to include “all juridical persons established in accordance with the laws of... Peru and domiciled in... Peru, including civil and commercial companies and other associations with or without a legally acknowledged existence that perform an economic activity within the sphere of this Agreement and which are directly or indirectly controlled by nationals of... Peru.”¹²¹ On the other hand, the same article defines “investor” in respect of China to include merely “economic entities established in accordance with the laws of... China and domiciled in... China.”¹²²

These two asymmetrical approaches can be contrasted with BITs which provide the exact same definition of “investors” for each party, such as in China’s BIT with Trinidad and Tobago.¹²³ Therefore, where such a divergent approach is taken to the definitions of “investor” included in an IIT, an investment tribunal should pause to examine why this is the case, including the possibility that the parties intended to include or exclude different types of investors from the provisions of the BIT, including SOEs. Such an investigation could include a comparison of the different definitions of

¹²⁰ *Agreement between the Government of the People's Republic of China and the Government of the Republic of Ghana Concerning the Encouragement and Reciprocal Protection of Investments*, 12 October 1989, Art. 1(b), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/china_ghana.pdf> [emphasis added].

¹²¹ *Agreement between the Government of the Republic of Peru and the Government of the People's Republic of China Concerning the Encouragement and Reciprocal Protection of Investments*, 8 June 1994, Art. 1(2), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/peru_china.pdf>.

¹²² *Ibid.* For another Chinese BIT defining “investor” differently in respect of China and its counterparty state, but which is also silent as to the inclusion of SOEs within these, see *Agreement between the Government of the People's Republic of China and the Government of the Oriental Republic of Uruguay Concerning the Encouragement and Reciprocal Protection of Investments*, 2 December 1993, Art. 1(2), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/china_uruguay.pdf>.

¹²³ This BIT defines “investors” other than natural persons—in respect of both parties—to include “economic entities, including companies, corporations, associations, partnerships and other organizations, incorporated and constituted under the laws and regulations of either Contracting Party and which have their seats in that Contracting Party.” See *Agreement between the Government of the Republic of Trinidad and Tobago and the Government of the People's Republic of China on the Reciprocal Promotion and Protection of Investments*, Art. 1(2), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/china_trinidad.pdf> (date of signature not available).

investor included in the BIT to the domestic law and legislation of the two parties dealing with companies and their incorporation, including the parties' domestic law and legislation dealing with SOEs. For example, it could be that the domestic laws of Peru specifically provide for "civil and commercial companies and other associations" in a manner which excludes SOEs or similar entities from the ambit of these terms.

An investigation into the standing of SOEs in the face of otherwise neutral definitions of "investor" could also include consideration of various other provisions included in an IIT that are capable of indirectly evidencing the parties' intentions. Like the BIT between China and Trinidad and Tobago, China's agreements with Uganda¹²⁴ and with Egypt¹²⁵ both adopt uniform definitions of "investor" which are silent as to the standing of SOEs. However, each of these three treaties also contains another provision potentially indirectly relevant to the standing of SOEs. This is the "subrogation clause," which establishes the right of an investor to allow a third party to bring a claim on its behalf, in respect of matters to which the subrogation applies.¹²⁶ These clauses are often constructed to extend subrogation rights only to private entities, such as an investor's insurance company.¹²⁷ However, subrogation clauses in the three treaties identified above take a different approach: they extend subrogation rights to Contracting Parties or any "designated agency." This strict focus on the subrogation rights of contracting states and any "designated agencies" is of potential significance. In particular, it suggests that where the States parties intended to provide standing to states and certain state "agencies," they did so expressly. It therefore also suggests that when the IIT does not expressly extend standing to states and certain "state agencies," this was intentional, and such entities were not intended to be given standing to bring investment arbitration claims. Of course, whether or not an implied intention to deny standing to state *agencies* except in certain circumstances can be extended to equal an implied intention not to give similar standing to state-owned

¹²⁴ *Agreement between the Government of the People's Republic of China and the Government of the Republic of Uganda on the Reciprocal Promotion and Protection of Investments*, 27 May 2004, Art. 1(2), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/Uganda_China.pdf> (defines "investor" in respect of both States parties to include "legal entities, including company, association, partnership and other organization, incorporated or constituted under the laws and regulations of either Contracting Party and having their headquarters in that Contracting Party").

¹²⁵ *Agreement between the Government of the Arab Republic of Egypt and the Government of the People's Republic of China Concerning the Encouragement and Reciprocal Protection of Investments*, 21 April 1994, Art. 1(2)(b), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/egypt_china.pdf> (defines "investor" in respect of both States parties to include "economic entities established in accordance with the laws of that Contracting Party and domiciled in its territory").

¹²⁶ See China-Egypt BIT, *ibid.* Art. 7; China-Uganda BIT, *supra* note 124, Art. 6; China-Trinidad and Tobago BIT, *supra* note 123, Art. 9.

¹²⁷ See *Agreement on reciprocal promotion and protection of investments between the Government of the Republic of Kazakhstan and the Government of the Islamic Republic of Iran*, January 1996, Art. 9(1), online: <http://www.unctad.org/sections/dite/iiia/docs/bits/egypt_china.pdf>. For a subrogation clause which specifically establishes subrogation rights in respect of both private entities as well as home governments and their agencies see the Czech Republic-Kuwait BIT, *supra* note 113, Art. 8(1).

enterprises is an entirely different proposition, and one which would likely require significantly more support.

Depending on the IIT, such further evidence may be available in the Preamble, which under Art. 31(2) *VCLT* forms part of the interpretive context of a treaty. Take the BIT between Germany and Iran.¹²⁸ Here, the definitions provision defines German investing “companies” as including “any juristic person as well as any commercial or other company or association.” On the other hand, Iranian investing “companies” are defined to include “any legal personality or corporation or institution.” Both of these are wide and inclusive definitions which can very reasonably be argued to provide standing to SOEs. This is particularly the case in respect of Iranian companies because of the inclusion of the term “institution,” an expression often invoked to refer to public rather than private bodies. However, any implied standing of German or Iranian SOEs to bring investment claims under the Germany-Iran BIT is partially contradicted by the Preamble to the BIT, which specifically provides that the Treaty was intended to “stimulate *private* business initiative.”¹²⁹ This is not an outright rejection of the ability of SOEs from either country to bring claims under the BIT, but it does imply that any “public” investment made by such entities was not intended to be afforded protection.

In total, there is merit to UNCTAD’s abovementioned argument that a presumption in favour of the standing of SOEs should apply in the absence of evidence to the contrary: where an IIT definition of “investor” speaks solely of any or all “legal entities” it is reasonable to conclude that this should include both privately and publically held companies. However, two important caveats to this analysis must be raised. First, presumptions in favour of jurisdiction are inappropriate in investment arbitration. As held in *Inceysa Vallisoletana, S.L. v. Republic of El Salvador*, respecting the will of the States parties to an IIT requires that the scope of their consent to arbitration is scrutinized on an individual basis, free and clear of any presumption either for or against jurisdiction.¹³⁰ Secondly, evidence arguing against the standing of SOEs to bring arbitration under an IIT need not necessarily appear in the relevant definition of investor in the IIT, nor need it be express. It may be found in any other provision of the IIT. It may be either express or arise by implication. It may also bear on the relevant definition of investor

¹²⁸ *Treaty between the Federal Republic of Germany and the Empire of Iran concerning the Promotion and Reciprocal Protection of Investments*, 11 November 1965, online: <http://www.unctad.org/sections/dite/iaa/docs/bits/germany_iran_eng_gr.pdf>.

¹²⁹ *Ibid.*, Preamble [emphasis added].

¹³⁰ A similar IIT-specific approach to intention has been followed in other areas. According to the tribunal in *Inceysa v. El Salvador*, *supra* note 115 at para. 176, any investigation into the scope of consent to arbitration given by the States parties to an IIT should proceed free from any presumptions in favour of or against jurisdiction. See also *Noble Energy, Inc. and Machalapower Cia. Ltda. v. The Republic of Ecuador and Consejo Nacional de Electricidad* (Decision on Jurisdiction, 5 March 2008), ICSID Case No. ARB/05/12 at paras. 195-197 [*Noble v. Ecuador*]; *RosInvestCo UK Ltd. v. The Russian Federation* (Award on Jurisdiction, October 2007), SCC Case No. Arb. V079/2005 at para. 44 (Arbitration Institute of the Stockholm Chamber of Commerce) [*RosInvestCo v. Russia*].

either directly or indirectly. Therefore, while at first glance an otherwise neutral definition of “investor” may appear to grant standing to a SOE, it is important to verify that such standing is not substantially contradicted by other provisions of the IIT either expressly or by implication. Not all such contradictory evidence will be of identical persuasive value, however. A reference to “private” investment in a Preamble or the asymmetrical treatment of SOEs in two definitions of “investor,” for example, may weigh somewhat heavily against SOE standing. A state-centred subrogation clause, on the other hand, will likely hold minimal weight at best. Nonetheless, it is clear that in sufficient strength, evidence of this kind could amount to a persuasive implication that SOEs were not intended to be granted standing under an IIT otherwise silent on this point.

Considering these realities of interpretation, a presumption in favour of standing risks being of limited utility at best, and—to the extent that it could distract from real interpretive deliberation—counter-productive at worst. Perhaps it would be more useful instead to specify a general foundation for understanding the object and purpose of IITs. Tribunals should proceed in this inquiry on the basis that, as reviewed above, the general goal of the international investment arbitration regime is to stimulate cross border flows of capital. However, this should be balanced with the fact that many investment protection treaties, at least initially, were also designed with the intention of depoliticizing disputes between states. Once again, these considerations would only be a general framework for each particular IIT: tribunals should take into account the fact that different states likely placed different emphases on these separate goals at different times in their respective histories.

However, at no time during this inquiry should investment arbitration tribunals exceed the interpretive boundaries prescribed by the *VCLT*. While it is important to outline which interpretive practices a Tribunal should adopt when considering the standing of SOEs, attention should also be drawn to interpretive practices which should be avoided. One such undesirable practice is the attribution of undue importance to other IITs executed by the same States parties to the present dispute. In circumstances where even after Art. 31 *VCLT* interpretation the meaning of an IIT is “ambiguous or obscure,” Art. 32 *VCLT* calls for tribunals to refer to supplementary means of interpretation, “including the preparatory work of the treaty and the circumstances of its conclusion.” This may include numerous sources, including drafts of the IIT and related official correspondence between the States parties. Therefore, where the standing of an SOE under an IIT is unclear, tribunals may be tempted in their consideration of supplementary sources to compare the IIT before them to other IITs signed by the same States parties. For example, were a Tribunal investigating the standing of a Saudi Arabian SOE to bring a claim under the BIT between Saudi Arabia and the Belgo-Luxembourg Economic Union (BLEU),¹³¹ it might consider turning for guidance to the terms of Saudi

¹³¹ *Agreement between the Kingdom of Saudi Arabia and the Belgo-Luxembourg Economic Union (B.L.E.U.) Concerning the Reciprocal Promotion and Protection of Investments*, 22 April 2001, online:

Arabia's BIT with Malaysia.¹³² In particular, it might seek to compare the former's definition of a Saudi Arabian investor, which includes "any legal entity *having or not having legal personality*"¹³³, with the latter's definition of a Saudi Arabian investor, which includes merely "any legal entity"¹³⁴, to establish that Saudi Arabia intended to provide for a wider class of Saudi investors in the later *Saudi Arabia-BLEU BIT* than it did in the earlier *Saudi Arabia-Malaysia BIT*. However, any such attempt would be misguided. As stated by the tribunal in *Aguas del Tunari, S.A. v. Republic of Bolivia*:

[t]he practice of a state as regards the conclusion of BITs other than the particular BIT involved in a dispute is not of direct value to the task of interpretation under Article 31 of the Vienna Convention. The fact that a pattern might exist in the content of the BITs entered into by a particular state does not mean that a specific BIT by that state should be understood as necessarily conforming to that pattern rather than constituting an exception to that pattern.¹³⁵

This warning is repeated by the Tribunal in *Rompetrol v. Romania*, where it held that there is "nothing in the Vienna Convention that would authorize an interpreter to bring in as interpretive aids when constructing the meaning of one bilateral treaty the provisions of other treaties concluded with other partner States."¹³⁶

3. Jurisdictional Issue #2: Does an SOE have standing under the ICSID Convention?

Even after an investment tribunal determines that an IIT *does* in fact extend its protection to SOEs, additional barriers will exist where the tribunal has been constituted pursuant to the *ICSID Convention*. The *ICSID Convention* does not allow for the arbitration of disputes between states.¹³⁷ Allowing for the arbitration of such disputes was expressly considered by the drafters of the Convention and firmly rejected.¹³⁸ Furthermore, while the drafters of the Convention decided to grant access to ICSID arbitration to

<http://www.unctad.org/sections/dite/iia/docs/bits/saudi_belg_lux.pdf> [Saudi-BLEU BIT].

¹³² *Agreement between the Government of the Kingdom of Saudi Arabia and the Government of Malaysia Concerning the Promotion and Reciprocal Protection of Investments*, 25 October 2000, online: <http://www.unctad.org/sections/dite/iia/docs/bits/saudi_malaysia.pdf> [Saudi-Malaysia BIT].

¹³³ *Saudi-BLEU BIT*, supra note 131, Art. 1(3)(a)(II) [emphasis added].

¹³⁴ *Saudi-Malaysia BIT*, supra note 132, Art. 1(3)(b)(ii).

¹³⁵ (Decision on Jurisdiction, 21 October 2005), ICSID Case No. ARB/02/3 at para. 291, online: <http://www.iisd.org/pdf/2005/AdT_Decision-en.pdf> [*AdT v. Bolivia*]. However, the tribunal does go on to note that a state's practice in negotiating BITs may be of assistance in "testing the assertions of parties as to the general policies" of an IIT's States parties and in "testing assumptions a tribunal may make regarding BITs." See *ibid.* at para. 292.

¹³⁶ *Supra* note 115 at para. 108. However, one must question whether the situation is the same with Model BITs used by states in negotiating investment agreements, such as the 2004 *Model U.S. Bilateral Investment Treaty*, *supra* note 110, and Canada's 2004 model for Foreign Investment Promotion and Protection Agreements, *supra* note 111. In particular, as both of these model treaties include publicly-owned entities within their definition of investor, the absence of such language in later BITs could indicate that they did not intend to extend protection to state-owned businesses in these later instruments.

¹³⁷ See *ICSID Convention*, *supra* note 8, Art. 25.

¹³⁸ Schreuer, *supra* note 92, Art. 25, para. 270.

SOEs, they simultaneously decided to limit the circumstances in which this would be done.¹³⁹ The remainder of this article will explore the parameters of such constraints. Sub-section (i) will examine the circumstances in which the application of the “Broches test” will deny standing to an SOE under *ICSID Convention* Art. 25: what does it mean for an SOE to “discharge an essentially governmental function,” or “act as an agent for the government”? Sub-section (ii) will examine how SOEs are defined and/or identified for the purposes of the *ICSID Convention* and the Broches test—the ultimate question being how a tribunal will determine whether or not the Broches test should be applied in the first place. Both of these analyses will be made with reference to previous investment arbitration case law as well as other relevant sources of international law. Both of these analyses will also criticize such precedent where it has been lacking in either substance or scope.

Art. 25 of the *ICSID Convention* and the “Broches Test”

As mentioned, a tribunal constituted in relation to an investment dispute under an IIT must confirm its jurisdiction not only under the IIT but also under the arbitration rules specific to it. Therefore, where the tribunal has been constituted before the International Chamber of Commerce’s International Court of Arbitration or under the UNCITRAL Model Rules, it will be necessary for the tribunal to determine whether the jurisdictional provisions of these rules have been complied with. As these forums were designed to administer commercial disputes between private parties, their jurisdictional provisions are generally concerned with confirming that the parties have properly consented to arbitration and that the arbitral tribunal has been properly formed. However, tribunals constituted under the *ICSID Convention* will not only have to address these same issues of consent and formation; they will also have to deal with issues specific to ICSID’s role as a forum designed to adjudicate disputes between private investors and sovereign states. Art. 25 of the *ICSID Convention* establishes the jurisdictional requirements for ICSID tribunals. Under Art. 25(1), “The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State... and a national of another Contracting State.”

The leading decision in respect of the standing of SOEs to bring arbitration under the *ICSID Convention* is currently the award of the Tribunal in *Ceskoslovenska Obchodni Banka, A.S. v. The Slovak Republic*.¹⁴⁰ At the time of the claim, CSOB was a bank owned by the government of the Czech Republic.¹⁴¹ In 1993, CSOB entered into a series of agreements with the Slovak Republic, the Czech Republic, and two collection companies: one established in each of the involved states. In addition, CSOB entered into a loan agreement with the Slovak collection company; the obligations of the collection company were guaranteed by the Slovak Republic. When the

¹³⁹ *Ibid.*, Art. 25, paras. 270-271.

¹⁴⁰ (Decision on Jurisdiction, 24 May 1999), ICSID Case No. ARB/97/4, 14 ICSID Rev.-F.I.L.J. 25, online: <http://ita.law.uvic.ca/documents/CSOB-Jurisdiction1999_000.pdf> [CSOB v. Slovak Republic].

¹⁴¹ *Ibid.* at para. 18.

Slovak collection company failed to honour its obligations under the loan and the Slovak Republic in turn failed to fulfil its guarantee, CSOB filed a claim for arbitration by an ICSID tribunal under the BIT between the Czech Republic and the Slovak Republic.¹⁴² Several objections to the tribunal's jurisdiction under the BIT and the *ICSID Convention* were raised by the Slovak Republic.¹⁴³ Most important here, it was argued that CSOB did not qualify as an *ICSID Convention* Art. 25 "national of another Contracting State," and was in fact an organ of the Czech state.¹⁴⁴

The tribunal in *CSOB v. Slovakia* began its analysis of the Slovak Republic's objection by stating that Art. 25 leaves no doubt that ICSID tribunals have no jurisdiction over disputes between two Contracting States.¹⁴⁵ However, this did not mean that the *ICSID Convention* was available only to privately owned companies.¹⁴⁶ Rather, citing the legislative history of the *ICSID Convention* and a study made by its principal drafter, Aron Broches, the Tribunal held that "for purposes of the Convention a mixed economy company or government-owned corporation should not be disqualified as a 'National of another Contracting State' unless it is acting as an agent for the government or is discharging an essentially governmental function."¹⁴⁷ Notably, both the Claimant and the Respondent accepted that this test—which has subsequently come to be known as the "Broches test"—was determinative.¹⁴⁸

The Broches Test: "discharging an essentially governmental function"

In applying the Broches test to the facts of the case, the Tribunal made two observations. First, the Tribunal noted that 65% of CSOB was owned by the Czech Republic and that, according to the respondent, this majority ownership resulted in the bank being under the "absolute control" of its home state.¹⁴⁹ Second, the Tribunal took note of the fact that over the course of its existence most of the CSOB's work was undertaken on behalf of the Czech Republic, including facilitating foreign commercial operations and executing international banking transactions at the State's behest.¹⁵⁰

¹⁴² *Agreement between the Government of the Slovak Republic and the Government of the Czech Republic Regarding the Promotion and Reciprocal Protection of Investments*, 23 November 1992; *CSOB v. Slovak Republic*, *ibid.* at paras. 1-3.

¹⁴³ *Ibid.* at paras. 10-12.

¹⁴⁴ *Ibid.* at paras. 10, 15.

¹⁴⁵ *Ibid.* at para. 16. This assertion is now generally accepted: *Emilio Agustín Maffezini v. The Kingdom of Spain* (Decision of the Tribunal on Objections to Jurisdiction, 25 January 2000), ICSID Case No. ARB/97/7 at para. 74, online: <http://ita.law.uvic.ca/documents/Maffezini-Jurisdiction-English_001.pdf> [Maffezini v. Spain].

¹⁴⁶ *CSOB v. Slovak Republic*, *supra* note 140 at para. 16.

¹⁴⁷ *Ibid.* at para. 17, citing Aron Broches, *The Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (1972) 135 Hague Rec. d. Cours 331 at 354-355. Mr. Broches served as both General Counsel to the World Bank, and as Secretary General of the ICSID.

¹⁴⁸ *CSOB v. Slovak Republic*, *supra* note 140 at para. 17.

¹⁴⁹ *Ibid.* at para. 18.

¹⁵⁰ *Ibid.* at para. 20.

However, the Tribunal emphasized that, in light of the Broches test, these observations could not be determinative. Rather, it held that assessing whether SOE investment represented the discharge of an “essentially governmental function” necessitated a focus on the *nature* of the acts rather than their *purpose*.¹⁵¹ In other words, the Tribunal held that regardless of whether or not CSOB’s actions functioned to “promote the government policies or purposes” of the Czech Republic, the ultimately crucial issue was whether the actions themselves “were essentially commercial rather than governmental in nature.”¹⁵²

Focussing exclusively on how to characterize the nature of the particular investment activity at issue, the Tribunal concluded that it mattered little that CSOB was publically owned and controlled.¹⁵³ Such public ownership and control was already provided for and accommodated by the *ICSID Convention* itself, as discussed above. What mattered was whether, in conducting its investment, the activities of CSOB ever crossed the line between those exercised by private commercial entities, and those exercised primarily by entities of a public nature. Therefore, it mattered not that CSOB’s actions might be “driven by state policies,”¹⁵⁴ nor that CSOB’s activities were benefitting from the Czech government’s policies and subsidies.¹⁵⁵ Instead, the determinative fact was that CSOB was not itself engaged in policy making or development, or in legislative or administrative action;¹⁵⁶ rather, its actions, strictly speaking and divorced from their greater context, were within the competency of a private commercial entity. Since they were not within the special and exclusive competency of a sovereign, its sub-state entities or state organs, it could not be said that CSOB’s investments were the discharge of an essentially governmental function.

The Tribunal’s decision in *CSOB v. Slovak Republic* represents a significant expansion of established international investment law, elaborating substantially on the requirements of Article 25 of the *ICSID Convention*. By concentrating entirely on the nature of the entity’s activities without any consideration of their purpose, the Tribunal elevated form over substance, presumably in search of a bright-line test. This approach does have its advantages, among them greater certainty and predictability. The nature of an entity’s investments will often be more easily determined than the purpose underlying those investments. This is particularly the case where one seeks merely to categorize investments as either public or private. It would appear that most if not all actions undertaken by a private entity that are not accompanied by some sort of *puissance publique* or public authority will be just that—private. The motivations or purposes behind investment, on the other hand, can be much more difficult to decipher: they can be masked, and there will often be multiple motivations underlying any one action. The issue of underlying motivation can also pose serious

¹⁵¹ *Ibid.*

¹⁵² *Ibid.*

¹⁵³ *Ibid.* at para. 18.

¹⁵⁴ *Ibid.* at para. 21.

¹⁵⁵ *Ibid.* at para. 23.

¹⁵⁶ *Ibid.*

evidentiary problems, since much of the most pertinent information will be controlled by the entity that is the subject of the inquiry.

Nonetheless, for two reasons the bright-line "nature" test established in *CSOB v. Slovak Republic* should not receive unconditional acceptance by tribunals as the appropriate test for Art. 25 jurisdiction over SOEs. First, the decision is not entirely persuasive. The "commercial transaction" test has long been the accepted standard in the domestic law of many states for determining the jurisdiction of courts over the actions of foreign states and their instrumentalities: only where the activities of such entities are deemed to be "commercial" or non-sovereign (*jure gestionis*) rather than sovereign (*jure imperii*) will courts exercise jurisdiction over them.¹⁵⁷ The aim of this inquiry is in many respects analogous to the Broches test and its "essentially governmental function" limb. The "commercial transaction" test prevents courts from exercising jurisdiction over a state entity except where it is acting in a non-sovereign or commercial manner. Similarly, the "essentially governmental function" restricts the standing of SOEs before the ICSID to those circumstances where their investments have been conducted in a comparably non-sovereign or commercial manner. While it has previously been customary for courts to solely consider the nature of a state-controlled entity's activities when applying the "commercial transaction" test, it has more recently become the norm to consider both the nature *and* purpose of the entity's activities where appropriate. Article 2(2) of the United Nations *Convention on Jurisdictional Immunities of States and their Property*,¹⁵⁸ which has not yet entered into force but is nevertheless considered by many to be an expression of international consensus on the matter,¹⁵⁹ provides that:

In determining whether a contract or transaction is a "commercial transaction" ... reference should be made primarily to the nature of the contract or transaction, but its purpose should also be taken into account if the parties to the contract have so agreed, or if, in the practice of the state of the forum, that purpose is relevant to determining the non-commercial character of the contract or transaction.

This follows the approach of many notable domestic courts in recent decades, which have increasingly recognized that consideration of the greater context in which activities take place, including their purpose, may

¹⁵⁷ Malcolm N. Shaw, *International Law*, 6th ed. (New York: Cambridge University Press, 2008) at 708-714. For earlier treatments of this topic see e.g. Bernard Fensterwald, Jr., "Sovereign Immunity and Soviet State Trading" (1949-1950) 63 Harv. L. Rev. 614; "Sovereign Immunity of States Engaged in Commercial Activities", Unsigned Note, (1965) 65 Colum. L. Rev. 1086.

¹⁵⁸ New York, 2 December 2004, U.N. Doc. A/59/508 (Not yet in force. As of 30 April 2011, 28 signatories and 11 States parties).

¹⁵⁹ Hazel Fox, *The Law of State Immunity*, 2d ed. (New York: Oxford University Press, 2008) at 167 (The Convention is an "authoritative written codification of the international law relating to state immunity" that "represents a coherent statement of the current international law based on State practice"); David Gaukrodger, "Foreign State Immunity and Foreign Government Controlled Investors" (2010) 2 *OECD Working Papers on International Investment* (Paris: OECD Publishing) at 12, online: <<http://www.oecd.org/dataoecd/21/32/45036449.pdf>>, citing *Jones v. Ministry of Interior of Saudi Arabia*, [2006] UKHL 26, [2007] 1 A.C. 270 ("[d]espite its embryonic status, this Convention is the most authoritative statement available on the current international understanding of the limits of state immunity in civil cases.").

be necessary to accurately determine their sovereign or non-sovereign nature.¹⁶⁰ As held by the Supreme Court of Canada, “an antiseptic distillation of a ‘once-and-for-all’ characterization of the activity in question, entirely divorced from its purpose,” is “to attempt the impossible.”¹⁶¹ According to the U.S. Court of Appeals for the Fifth Circuit, in *De Sanchez v. Banco Central de Nicaragua and Others*, “unless we can inquire into the purpose of [certain] acts, we cannot determine their nature.”¹⁶² Similarly, the Australian Law Commission has written that the conceptual distinction between the purpose and nature of an activity is impossible to sustain: “It is not possible to classify the nature of any human activity without reference to its purpose... The classifications 'governmental' and 'commercial' are themselves purposive.”¹⁶³

In this light, the difficulty involved in investigating the purpose behind the activities of an SOE operating in a foreign state does not diminish the potential relevance of such purpose in determining the jurisdiction of an ICSID tribunal. In fact, contemporary concerns related to SOEs reveal that the potential relevance of an SOE’s motivations is quite high, and there will be political pressures to take these motivations into account. As discussed, the main concern surrounding modern SOEs is that they may engage in behaviour motivated by political concerns rather than strictly commercial concerns—in other words, adopt the appearance of a private enterprise in order to further otherwise political objectives. These concerns are not related to the type or nature of activity that SOEs may engage in. They are related to the purposes and objections behind such activities. As such, they are not addressed in the test adopted by the *CSOB* tribunal. This is a deficiency that is not likely to sit well with countries interested in closely policing the activity of SWFs and SOEs within their borders. They will rightly argue that SOEs and the governments that control them are entirely capable of cloaking politically motivated decisions and strategies in otherwise commercial actions, and that the test advocated in *CSOB v. Slovak Republic* would allow such behaviour to be protected by the *ICSID Convention* even where the end goal is one contrary to the interests of the host state. ICSID tribunals should not overlook this.

Second, there are numerous reasons why future tribunals may feel free to expand on the inadequate reasoning of the Tribunal in *CSOB v. Slovak Republic*. Like all international investment arbitration decisions, it is not binding on future investment tribunals.¹⁶⁴ It is true that there is very good cause to consider and give great weight to the determinations of previous

¹⁶⁰ See Shaw, *supra* note 157 at 710-712.

¹⁶¹ *United States of America v. The Public Service Alliance of Canada and others (Re Canada Labour Code)*, [1992] 2 S.C.R. 50 at para. 28 [Re *Canada Labour Code*]. See also the ruling of Wilberforce L.J. in *I Congreso del Partido*, [1983] 1 A.C. 244 (H.L.) (heavily relied on in *Re Canada Labour Code*).

¹⁶² *De Sanchez v. Banco Central de Nicaragua and Others*, 770 F.2d 1385 at 1393 (5th Cir. 1985), 88 I.L.R. 75 at 83.

¹⁶³ Australian Law Reform Commission, *Report No. 24: Foreign State Immunity* (1984), online: <<http://www.austlii.edu.au/au/other/alrc/publications/reports/24/>>.

¹⁶⁴ See *RosInvestCo v. Russia*, *supra* note 130 at para. 49; *Noble v. Ecuador*, *supra* note 130 at paras. 49-50; Gabrielle Kaufmann-Kohler, “Arbitral Precedent: Dream, Necessity or Excuse?” (2007) 23 Arb. Int’l 357; Jeffrey P. Commission, “Precedent in Investment Treaty Arbitration: A Citation Analysis of a Developing Jurisprudence” (2007) 24 J. Int’l Arb. 129.

investment tribunals. As noted in *Burlington Resources Inc. v. Republic of Ecuador*, tribunals should “pay due consideration to earlier decisions of international tribunals” and, “subject to compelling contrary grounds... [should] adopt solutions established in a series of consistent cases.”¹⁶⁵ This is in order to “contribute to the harmonious development of investment law” and to thereby “meet the legitimate expectations of the community of States and investors towards the certainty of the rule of law.”¹⁶⁶ However, as recognized by the *Burlington Resources* tribunal, “compelling contrary grounds” should cause a tribunal to depart from this approach. The decision of the tribunal in *CSOB v. Slovak Republic* is one such case. As argued above, the argument articulated by the tribunal is not particularly persuasive in its outright dismissal of the relevance of “purpose” when examining SOE activities. Furthermore, the decision’s lack of comprehensiveness will make it easier for other tribunals to depart from the tribunal’s approach. *CSOB* was one of the earliest decisions on jurisdiction by an ICSID tribunal. It followed only a handful of previous awards and was decided without the benefit of the avalanche of investment arbitration awards and associated academic discussion that has since ensued. Whereas contemporary decisions on jurisdiction in investment disputes consistently result in lengthy awards numbering hundreds of pages and citing large numbers of authorities and legal instruments, the *CSOB* decision on this point produced only twelve paragraphs and referenced only a single source. Perhaps most importantly, *CSOB v. Slovak Republic* was also decided prior to the recent increase in the size, number and influence of SWFs and SOCs, and the effect of these SOEs on the investment policies of many IIT States parties.

In this regard, it is clear that a more balanced approach is needed to determine whether or not an SOE is “discharging an essentially governmental function” for the purpose of ICSID tribunal Art. 25: one that represents the likely intention of the jurisdictional provision, that recognizes the legitimate concerns with respect to SOEs of the States parties to the *ICSID Convention*, that reflects the increasing comprehensiveness of ICSID jurisprudence and academic commentary, and that is designed to deal with the current realities of complex SOE investment.

It is submitted that such a test for “essentially governmental functions” is one that considers the nature of an SOE’s activities as well as the purpose behind those activities where appropriate. While it is true that this will involve a more extensive examination than focusing merely on the nature of an SOE’s activities, and that the result of this examination may be more

¹⁶⁵ (Decision on Jurisdiction, 2 June 2010), ICSID Case No. ARB/08/05 at para. 100, online: <http://ita.law.uvic.ca/documents/BurlingtonResourcesInc_v_Ecuador_Jurisdiction_Eng.pdf> [*Burlington Resources*]. See also *Saipem S.p.A. v. The People's Republic of Bangladesh* (Decision on Jurisdiction, 21 March 2007), ICSID Case No. ARB/05/07 at paras. 66-67, online: <<http://ita.law.uvic.ca/documents/Saipem-Bangladesh-Jurisdiction.pdf>>; *Saba Fakes v. Republic of Turkey* (Award, 14 July 2010), ICSID Case No. ARB/07/20 at para. 96; *Victor Pey Casado and President Allende Foundation v. Republic of Chile* (Award, 9 May 2008), ICSID Case No. ARB/98/2 at para. 119.

¹⁶⁶ *Burlington Resources*, *ibid*.

difficult for disputing parties to predict beforehand, it is nonetheless the analysis which is the most likely to produce a fair and reasonable outcome.

The benefits of this alternative approach can be seen by returning to the example of *CSOB v. Slovak Republic*. The dispute arose in unique circumstances. The Soviet Bloc had only recently collapsed and Eastern Europe, including the Czech Republic, was hurtling through a drastic transformation from state-controlled economies to free markets. The agreements entered into by CSOB were directly related to this transition, concluded in major part for the purpose of privatizing CSOB itself.¹⁶⁷ This aspect of public or governmental purpose underlying CSOB's activities appeared to trouble both the bank and the tribunal. In particular, it appears from the text of the award that CSOB was concerned that if its participation in the loan agreement could be framed as the implementation of government policy, the obedience of the bank in this regard would be sufficient to characterize its actions as "essentially governmental." As such, CSOB seemed eager to dissociate its actions from the greater political, economic and ideological shift in which they occurred by concentrating on the fundamentally private nature of the financial transactions themselves. But CSOB's concerns in this regard would not necessarily be justified under the alternative approach proposed here. While it is true that CSOB was taking its orders from the Czech state when it negotiated the loan agreement, the fundamental objective of those directives was the disconnection and disassociation of CSOB from the Czech state.¹⁶⁸ Stated differently, the true purpose of CSOB's actions was not to advance government policy but to ensure that, going forward, it could in no way function as or be considered to be an arm of the Czech state. This is hardly an agenda that threatens the philosophy of the ICSID system or the principles of its foundation. Therefore, had the tribunal in *CSOB v. Slovak Republic* been willing to depart from a formalistic analysis to examine both the nature and purpose of CSOB's activities in the larger context in which they occurred, and to consider the ultimate goal of the government objectives being advanced, it could have been sensitive to these realities.

A test that considers both nature and purpose is also the approach best suited to analyze the potentially complex operations of today's large and often very powerful SOEs. If the *ICSID Convention* is not intended to protect SOEs operating as an appendage of their home states, then it is only appropriate that the totality of an SOE's operations be evaluated to decide whether or not they represent an extension of those states' policy or agenda. This approach will allow tribunals to determine the true geopolitical or economic ramifications of otherwise superficially commercial transactions. More so than the CSOB test, this approach will allow tribunals to determine whether an SOE has crossed the line from behaviour motivated purely by

¹⁶⁷ For a critical analysis of the Czech Republic's privatization program at this time, see George Bogdan, "The Economic and Political Logic of Mass Privatization in Czechoslovakia and Poland" (1996) 4 Cardozo J. Int'l & Comp. L. 43.

¹⁶⁸ The CSOB Tribunal even seemed to recognize this argument. See *CSOB v. Slovak Republic*, *supra* note 140 at para. 23.

commercial objectives to behaviour motivated totally or in part by the greater political, economic and social concerns of the state that created and controls it.

The Broches Test: “acting as an agent for the government”

In addition to the deficiencies of the CSOB Tribunal’s ruling on the “essentially governmental function” limb of the Broches test, the decision suffers from another notable weakness: the Tribunal’s failure to sufficiently address the “government agent” prong of the Broches test. As discussed, the Broches test provides that “for purposes of the Convention a mixed economy company or government-owned corporation should not be disqualified as a ‘National of another Contracting State’ unless it is acting as an agent for the government or is discharging an essentially governmental function.”¹⁶⁹ The two branches of the test are disjunctive, being separated by the word “or”; therefore, the test clearly imposes two separate and distinct inquiries. First it asks whether the claimant SOE is acting as an “agent for the government.” It then asks whether the claimant SOE is “discharging an essentially governmental function.” If either of these branches are satisfied, then the *ICSID Convention* will not apply to protect the relevant SOE investment. The *CSOB v. Slovak Republic* Tribunal clearly turned its attention to the second of these limbs (although its analysis on this point should be questioned, as argued above). However, its treatment of the “government agent” branch of the Broches test is even more suspect.

The Tribunal acknowledges twice that the Slovak Republic contends that the “CSOB is... an agent of the Czech Republic,”¹⁷⁰ but ultimately does not give the “government agent” limb the same attention accorded to the “essentially governmental function” limb. Rather, it appears to conflate the two, failing to recognize that the “government agent” branch is a conceptually distinct component of the Broches test. It does this in two separate passages.¹⁷¹ First, it states that:

It cannot be denied that for much of its existence, CSOB *acted on behalf* of the State in facilitating or executing the international banking transactions and foreign commercial operations the State wished to support and that *the State’s control of CSOB required it to do the State’s bidding* in that regard. But in determining whether CSOB, in discharging these functions, exercised governmental functions, the focus must be on the nature of these activities and not their purpose.

Second, it states that:

... even if one were to conclude that the non-performing assets derived from *activities conducted by CSOB as an agent of the State*, the measures taken by CSOB to remove them from its books in order to improve its balance and consolidate its financial position in accordance with the provisions of the Consolidation Agreement, *must be deemed to be commercial in character*.

¹⁶⁹ Broches, *supra* note 147.

¹⁷⁰ *CSOB v. Slovak Republic*, *supra* note 140 at para 10. See also para. 19.

¹⁷¹ *Ibid.* at paras. 20-21 [emphases added].

This confusion is unfortunate. There is no suggestion inherent to the Broches test that either limb is superior to the other: they are put on exactly level ground. There is therefore no reason why the CSOB Tribunal should have predominantly focused its reasoning on the “essentially governmental function” limb to the exclusion of the “government agent” limb. There is also therefore no reason why the tribunal should have implied, as it did in the passages cited above, that an *ICSID Convention* tribunal can take jurisdiction as long as the SOE is not performing an “essentially governmental function.” This was a disservice to the Slovak Republic. It remains a distinct possibility that, had the Tribunal given both limbs equal attention and significance, it would have held that the “acting as an agent for the government” branch was an independent basis to deny jurisdiction over CSOB’s claims.

This raises the following two critical and interrelated questions. First, under what circumstances will an SOE be “acting as an agent of the government” for the purpose of *ICSID Convention* Art. 25? Secondly, how is this test conceptually distinct from the “essentially governmental function” branch that was the focus of the Tribunal in *CSOB v. Slovak Republic*?

One readily available source for understanding what it means to act as a government agent may be Art. 8 of the International Law Commission’s *Draft Articles on the Responsibility of States for Internationally Wrongful Acts*.¹⁷² Similar to the latter branch of the Broches test, Art. 8 is concerned with whether the conduct of a non-state actor should be attributed to a state. According to Art. 8:

The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on the instructions of, or under the direction or control of, that State in carrying out the conduct.¹⁷³

The official ILC Commentary to Art. 8 explains that while, “as a general principle, the conduct of... entities is not attributable to [a] State under international law... [c]ircumstances may arise... where such conduct is nevertheless attributable to the State because there exists a specific factual relationship between the... entity engaging in the conduct and the State.”¹⁷⁴ The ILC Commentary further explains that Art. 8 is intended to apply to two different situations. The first is where private persons or entities act “on the instructions of the State in carrying out the... conduct.”¹⁷⁵ The second is “the more general situation where private persons act under the State’s direction or control.”¹⁷⁶ The ILC Commentary also makes clear that, in “the text of

¹⁷² Report of the ILC on the Work of its Fifty-third Session, UN GAOR, 56th Sess., Supp. No. 10, UN Doc. A/56/10 (2001) 43 [Draft Articles]. Articles 4, 5 and 8 of the *Draft Articles* are considered a codification of the customary international law of attribution: Srilal M. Perera, “State Responsibility: Ascertaining the Liability of States in Foreign Investment Disputes” (2005) 6 J. World Investment & Trade 499.

¹⁷³ *Draft Articles*, *ibid.*, Art. 8.

¹⁷⁴ International Law Commission, “Responsibility of States for Internationally Wrongful Acts: General Commentary”, in *Report of the International Law Commission on the work of its fifty-third session*, UN GAOR, 56th Sess., Supp. No. 10, UN Doc. No. A/56/10 (2001) 31 at 47, online: <<http://untreaty.un.org/ilc/reports/2001/2001report.htm>> [ILC Commentary].

¹⁷⁵ *Ibid.*

¹⁷⁶ *Ibid.* at 48.

article 8, the three terms ‘instructions’, ‘direction’ and ‘control’ are disjunctive; it is sufficient to establish any one of them.”¹⁷⁷

These inquiries share obvious parallels with the “government agent” limb of the Broches test: all are on their face concerned with establishing whether or not an entity should be considered an agent of a state in certain circumstances. As such, case law and commentary developed in connection with ILC Art. 8 should serve as a valuable reference to any tribunal tackling the “government agent” limb of the Broches test for a number of reasons.

First, they provide valuable insight into a number of questions that can arise when investigating the relationship between a state and a purported state agent under the “government agent” limb of the Broches test. These include the degree of specificity a state’s directions to a purported agent must meet, whether states are responsible for acts that go beyond the scope of the state’s authorization of an agent, and the degree of control a state must exercise over an agent’s activities.¹⁷⁸ For example, the ILC Commentary confirms that the “attribution to the State of conduct in fact authorized by it is widely accepted in international jurisprudence.”¹⁷⁹ The ILC Commentary also explains that, where questions arise as to whether “conduct was carried out ‘under the direction or control’ of a State... such conduct will be attributable to the State only if it directed or controlled the specific operation and the conduct complained of was an integral part of that operation.”¹⁸⁰

Secondly, the ILC Commentary specifically contemplates the operation of Art. 8 in the context of SOEs, and thereby provides some valuable first principles: “[b]earing in mind the important role played by the principle of effectiveness in international law, it is necessary to take into account in both cases the existence of a real link between the person or group performing the act and the State machinery.”¹⁸¹ In this regard, the ILC Commentary makes a clear distinction between establishing agency between a state and entities unrelated to the state and establishing agency between a state and “companies or enterprises which are State-owned and controlled.”¹⁸² The ILC Commentary first confirms that “international law acknowledges the general separateness of corporate entities at the national level, except in those cases where the ‘corporate veil’ is a mere device or a vehicle for fraud or evasion.”¹⁸³ As such, the ILC Commentary then goes on to confirm that the mere “fact that [a] State initially establishes a corporate entity... is not a sufficient basis for the attribution to the State of the subsequent conduct of that entity.”¹⁸⁴ However, it is simultaneously recognized that where there is evidence that a “State was using its ownership interest in or control of a

¹⁷⁷ *Ibid.*

¹⁷⁸ *Ibid.* at 47-49.

¹⁷⁹ *Ibid.* at 47, citing, among others, the *Zafiro Case* (*D. Earnshaw and Others (Great Britain) v. United States*) (1925), 6 R.I.A.A. 160, (1926) 20 Am. J. Int’l L. 385.

¹⁸⁰ ILC Commentary, *ibid.*

¹⁸¹ *Ibid.*

¹⁸² *Ibid.* at 48.

¹⁸³ *Ibid.*

¹⁸⁴ *Ibid.*

corporation specifically in order to achieve a particular result" the conduct in question may be attributable to the State.¹⁸⁵

Lastly, the utility of Art. 8 for international investment law has already been acknowledged—and further developed—in a growing body of arbitration case law invoking ILC Art. 8 when considering the conduct of state-owned or controlled entities. The following examples are illustrative. The tribunal in *EDF (Services) Limited v. Romania* referred to Art. 8 when considering whether Romania was liable for the acts of two separate entities owned by the Romanian government, including the country's national airline company, Compania de Transportationuri Aeriene Romane Tarom S.A. (TAROM).¹⁸⁶ The state entities had entered into joint ventures with the claimant, EDF, in respect of duty free services at a Romanian international airport as well as during flights to and from the airport. In bringing the claim before the ICSID Convention tribunal, EDF accused Romania of acting through the state-owned entities to indirectly undermine its investment.¹⁸⁷ The tribunal agreed, attributing the conduct of the state-owned entities to Romania with reference to the principles of Art. 8.¹⁸⁸ In particular, it held that Romania had, through a number mandates and directives, effectively used its ownership and control of the entities to achieve results within its own interests.¹⁸⁹

In *Bayindir v. Pakistan*, the Tribunal applied Art. 8 to hold Pakistan responsible for the activities of that country's National Highway Authority (NHA).¹⁹⁰ Bayindir had been commissioned by the NHA to provide construction services in respect of new a six-lane motorway between Islamabad and Peshawar, and works ancillary to it. After several delays and revisions to the project, Bayindir instituted arbitration claiming that Pakistan had, *inter alia*, failed to provide it fair and equitable treatment through illegitimate pressure, coercion, the denial of due process and a government conspiracy to expel the corporation and transfer the work to local competitors.¹⁹¹ The Tribunal recognized that the NHA was a public corporation and body corporate under Pakistani law, created by statute with the right to sue and be sued in its own name.¹⁹² However, as various

¹⁸⁵ *Ibid.* On this point the ILC commentary refers to two decisions of the Iran-United States Claims Tribunal: *Foremost Tehran, Inc. v. The Government of the Islamic Republic of Iran* (1986), 10 Iran-U.S. C.T.R. 228 (Iran was ultimately responsible for the non-payment of dividends to American shareholders of an Iranian dairy company indirectly controlled by it through various state agencies); *American Bell International Inc. v. The Islamic Republic of Iran* (1986), 12 Iran-U.S. C.T.R. 170 (Iran was responsible for the failure of an Iranian private telecommunications company controlled by it to pay invoices and other costs incurred by a local subsidiary of AT&T).

¹⁸⁶ *EDF (Services) Limited v. Romania* (Award, 8 October 2009), ICSID Case No. ARB/05/13, online: <<http://ita.law.uvic.ca/documents/EDFAwardandDissent.pdf>> [*EDF v. Romania*].

¹⁸⁷ *Ibid.* at paras. 45-64, 66-111.

¹⁸⁸ *Ibid.* at para. 213.

¹⁸⁹ *Ibid.* at paras. 201-214.

¹⁹⁰ *Bayindir Insaat Turizm Ticaret ve Sanayi A.S. v. Islamic Republic of Pakistan* (Award, 27 August 2009), ICSID Case No. ARB/03/29, online: <<http://ita.law.uvic.ca/documents/Bayandiraward.pdf>> [*Bayindir v. Pakistan*].

¹⁹¹ *Ibid.* at paras. 96-100.

¹⁹² *Ibid.* at para. 9.

pertinent decisions of the Pakistan government were implemented through the NHA, and as various important decisions of the NHA were not executed prior to express governmental approval, the Tribunal concluded that the actions of the NHA could be attributed to Pakistan for the purposes of Bayindir's claims.¹⁹³

However, regardless of these parallels, it should be remembered that investigations under the "government agent" limb of the Broches test arise in substantially different circumstances than do investigations under Art. 8 of the ILC *Draft Articles* and the question of state attribution in general. This distinction may reduce the value of the Art. 8 jurisprudence to interpretations and applications of the Broches test. International tribunals turn to the principles of state attribution when trying to determine whether or not a state should be held responsible for the conduct of a third party entity. In other words, the attribution problem arises when a defendant state has been accused of infringing through a third party agent the rights of another entity or another state. Such reference to the principles of state attribution may occur in a number of institutional contexts: before the International Court of Justice, in assessing state responsibility for the conduct of foreign guerrilla forces,¹⁹⁴ before special purpose international tribunals, such as the Iran-U.S. Claims Tribunal, in assessing state responsibility for various public and private liabilities,¹⁹⁵ and in investment arbitration convened before an ICSID tribunal or some other arbitral body, in assessing whether the actions of an SOE can be attributed to the investor's host state.¹⁹⁶

On the other hand, the Broches test is designed to be invoked where an SOE attempts to bring an investment arbitration claim before a tribunal instituted under the *ICSID Convention*, and the respondent state seeks to deny the standing of the investor SOE because of its state-owned or state-

¹⁹³ *Ibid.* at paras. 114, 125-128. Note, however, that while the Tribunal found that the NHA's conduct could be attributed to Pakistan, it did not find the attributed conduct to amount to a breach of Pakistan's obligations. See page 140. Interestingly, the tribunal further noted that certain principles applicable in attributing conduct to states under Art. 8 of the ILC *Draft Articles* will not necessarily be applicable to the investment activities of SOEs. It particular, it distinguished between situations where attribution is being claimed amid commercial relations and in other situations such as political conflict. It commented at para. 130 that:

The Tribunal is aware that the levels of control required for a finding of attribution under Article 8 in other factual contexts, such as foreign armed intervention or international criminal responsibility, may be different. It believes, however, that the approach developed in such areas of international law is not always adapted to the realities of international economic law and that they should not prevent a finding of attribution if the specific facts of an investment dispute so warrant.

While the Tribunal clearly offers that different considerations may be warranted in these circumstances, it does not go so far as to opine on whether the corresponding standard of attribution applied would be any higher or lower.

¹⁹⁴ *Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States of America)*, [1986] I.C.J. Rep. 51 at para. 86.

¹⁹⁵ *Foremost Tehran*, *supra* note 185; *American Bell International*, *supra* note 185. For a discussion of the relevance of the jurisprudence of the Iran-United States Claims Tribunal to international investment arbitration, see Christopher S. Gibson and Christopher R. Drahoszal, "Iran-U.S. Claims Tribunal Precedent in Investor-State Arbitration", in Drahoszal & Gibson, eds., *The Iran-U.S. Claims Tribunal at 25: The Cases Everyone Needs to Know for Investor-State & International Arbitration* (New York: Oxford University Press, 2007) 1.

¹⁹⁶ *EDF v. Romania*, *supra* note 186; *Bayindir v. Pakistan*, *supra* note 190.

controlled nature. This is different than arguing agency for liability purposes and may involve significantly different considerations. When agency is argued for liability purposes, it may only be necessary to link certain specific conduct back to the purportedly controlling state—that conduct which constituted a violation of an entity’s rights. In *EDF v. Romania*, for example, it was only necessary for EDF to attribute the cancellation of the duty-free contract by TAROM back to Romania. It was not necessary for EDF to tie the general operations, or other specific operations, of TAROM back to Romania. Similarly, in *Bayindir v. Pakistan* it was only necessary for Bayindir to connect back to Pakistan the actions of NHA related to the Islamabad-Peshawar highway contract and its eventual demise. It was not necessary for Bayindir to address the involvement of Pakistan in any other project undertaken by the NHA.

However, where the “government agent” limb of the Broches test is invoked, a far broader analysis may be warranted. In particular, it may not be sufficient in order to deny standing to an SOE to merely establish that certain aspects of a SOE’s investment activities and behaviour are attributable to its home state. Rather, as occurred in *CSOB v. Slovak Republic*, it will likely be necessary to engage in a more general analysis of the SOE’s activities and objectives. Foreign investment projects can easily be large and complicated endeavours with multiple interdependent operations. They may involve long times frames with multiple stages. They may also evolve significantly over time to take on characteristics and operations different from those initially intended. As such, tribunals applying the “government agent” limb of the Broches test may be forced to make difficult decisions regarding which periods of an investment’s history the “government agent” test should be applied to. Should the test be applied to the circumstances of the SOE’s initial investment decision and entry and/or establishment? Should the test be applied to the entirety of the SOE investment’s lifecycle in a more general manner? Or, should the test be more selectively applied to certain periods of the SOE’s investment or certain important decisions taken by the SOE in relation thereto? The answers are not immediately apparent. It is likely that whichever direction a tribunal takes on these decisions will be at least moderately context-dependent. However, it is also clear that questions such as these do not immediately arise in the context of state attribution, which generally involves sovereign liability for more discrete conduct.¹⁹⁷

¹⁹⁷ This alone is an important ground on which to proceed with caution in the application of principles developed in connection with Art. 8 of the ILC *Draft Articles* to the ‘government agent’ limb of the Broches test. However, it is also important to note that various tribunals and publicists have already balked at the idea that the ILC *Draft Articles*, including Art. 8, are appropriate in contexts other than the attribution of conduct for determining state liability under international law.

For example, investors and publicists have on a number of occasions argued that, in addition to the attribution of liability, the ILC *Draft Articles* may be used to attribute other matters to states such as contractual undertakings. These arguments have arisen when investors have sought to establish privity between themselves and a state purportedly standing behind the named counterparty to a contract, in order to bring a breach of contract claim against the state rather than, or in addition to, the named counterparty. See Newcombe & Paradell, *supra* note 82 at 461, fn. 133; Nick Gallus, “An Umbrella Just for Two? BIT Obligations Observance Clauses and the

Nonetheless, reference to ILC Art. 8 and related case law and commentary begins to provide a basic framework for the application of the “government agent” limb of the Broches test. First, as international law clearly acknowledges the separate status of corporate entities at the national level, a relatively strict standard is likely warranted to find an SOE to be acting as an agent of the state. This conclusion is reinforced by the fact that, as foreign investments may be complex undertakings with long time horizons, a tribunal will want to ensure that agency is identified in respect of the wider investment itself rather than merely in respect of non-material discrete actions or decisions taken or made within the larger investment venture. From this starting point, the framework developed in connection to Art. 8 can guide the analysis. A tribunal should then aspire to unequivocally confirm that the SOE was acting on the instructions of or under the direct control of its home state in making and steering the investment. It should look to identify specific directions evidencing a high degree of control over critical investment decisions. It should look to identify clear manifestations of the links between the SOE and its home state and the means through which control over the investment is exercised. It should also look to identify whether such control was exercised to achieve a particular important result in respect of the investment. Similar to *EDF v. Romania*, such agency may be manifested by state mandates, directives, legislation or decrees specifically directing the investment. On the other hand, similar to *Bayindir v. Pakistan*, such agency may be manifested by significant guiding decisions made by senior members of the home state’s executive or by the requirement of senior executive approval of such decisions.

These considerations target a relationship between a SOE and its home state that is different than what is addressed by the “essentially governmental function” limb of the Broches test. In particular, while the “essentially governmental function” limb focuses on the degree to which a SOE may be performing investment activities with elements of governmental or regulatory authority, the “government agent” limb focuses on the degree to which the state has directed a SOE’s investment actions or investment activities. This does not mean that a SOE investment cannot satisfy both of these standards simultaneously. For example, in *EDF v. Romania*, even though the tribunal had determined that TAROM had been acting as an agent of the state in respect of the duty free contracts, it was also careful to consider whether or not the SOE could also be considered to be exercising

Parties to a Contract” (2008) 24 Arb. Int’l 157 at 167. See also *EDF v. Romania*, *supra* note 186 at paras. 317-319; *Consortium Groupement L.E.S.I.-DIPENTA v. Algeria* (Award, 10 January 2005), ICSID Case No. ARB/03/08 at II.2.3, para. 16; *Nykomb Synergies Technology Holding A.B. v. Republic of Latvia* (Award, 16 December 2003), S.C.C. Case No. 118/2003 at para. 4.2 (Arbitration Institute of the Stockholm Chamber of Commerce).

However, others strongly disagree with this analysis and maintain that attribution and privity are different things. They highlight that the fact that the actions of an entity may be attributable to a state for liability purposes does not mean that contracts entered into by such entities are state contracts. See James Crawford, “Treaty and Contract in Investment Arbitration” (2008) 24 Arb. Int’l 351 at 356. The ILC Commentary, to which Crawford contributed, also clearly supports this proposition. See ILC Commentary, *supra* note 174 at 39, para. 5.

“essentially governmental functions” in respect of its overall engagement of EDF in the project.¹⁹⁸ However, the conceptual distinction between the “essentially governmental function” and the “government agent” limbs of the Broches test does mean that the Tribunal in *CSOB v. Slovak Republic* made an error. Where an ICSID tribunal is confronted by a SOE claimant, care should be taken to adequately and distinctly engage with both of these standards.

State Ownership and State Control under the Broches Test

As the above discussions illustrate, much remains to be resolved in respect of the proper application of both the “essentially governmental function” and the “government agent” limbs of the Broches test. Clearly, this article cannot discuss all of these ambiguities. However, there remains one further issue that should be addressed here in respect of the Broches test. This is not *how* the Broches test should be applied, but *when* it should be applied. More specifically, is the Broches test activated solely by state-owned entities, or is it equally activated by entities which, although not necessarily owned by a state, are none the less *controlled* by the state? Furthermore, what sources of state control should be considered? The remainder of this article will be dedicated to answering these questions.

Ownership and Control

As discussed, it is clear that the drafters of the *ICSID Convention* did not intend to give standing to investor states. However, as noted by Schreuer, “[t]he situation is less clear when it comes to wholly or partly government controlled companies (or other entities, such as funds responsible for investing sovereign wealth).” The official comment to the preliminary draft of the *ICSID Convention* stated:

It will be noted that the term “national” is not restricted to privately-owned companies, thus permitting a wholly or partially government-owned company to be a party to proceedings brought by or against a foreign State.¹⁹⁹

However, as noted by Schreuer, this position was not repeated in the executive director’s report to the Convention.²⁰⁰ Therefore, when examining the circumstances in which the Broches test will be triggered we are not immediately left with more than the test itself. In other words, immediate guidance is limited to Broches’ employment of the expression “mixed economy company or government-owned corporation.”

¹⁹⁸ *EDF v. Romania*, *supra* note 186 at paras. 191-198. However, it must again be noted that the EDF tribunal was considering these matters in respect of attributing conduct potentially in breach of Romania’s obligations under an IIT by a SOE to Romania rather than in respect of attributing an investment by a Romanian SOE to Romania in connection with the “essentially governmental function” limb of the Broches test.

¹⁹⁹ *History of the ICSID Convention: Documents Concerning the Origin and the Formulation of the Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (Washington, DC: ICSID, 1968) vol. 2 at 230 [History].

²⁰⁰ Schreuer, *supra* note 92, Art. 25, para. 271.

At first glance this articulation may appear to limit the application of the Broches test to entities owned by the government. It expressly refers to government ownership, and the term “mixed economy” also appears to refer to the nature of the capital underlying the entity; i.e. a mixture of public and private investment. However, there is good cause to strongly doubt this analysis and conclude that government controlled entities are caught as well. First, that Broches employed the term “mixed economy company” in addition to the term “government-owned corporation” implies that it was intended to capture entities that are not strictly “government-owned corporations.” This can be taken to mean that the expression was being used not to refer to entities composed of both public and private capital, but rather to government-related entities of a broader species, perhaps including government-controlled entities.

This conclusion—that the Broches test should be engaged by government controlled entities as well as government-owned entities—is also generally supported by related international law and investment arbitration state case law. The author is unaware of any case law specifically examining what will constitute a state-owned or state-controlled entity for the purposes of the Broches test and Art. 25 of the *ICSID Convention*. However, for other purposes under international investment law, there are a number of cases which have examined both state ownership and state control in determining whether the business activities of a non-state entity should be attributed to the state.

Perhaps the best known of these is *Maffezini v. Spain*.²⁰¹ Maffezini had incorporated a Spanish company to engage in the production and distribution of chemical products in the Galicia region of Spain. Maffezini owned 70% of the company, and the remaining 30% was owned by the Sociedad para el Desarrollo Industrial de Galicia (SODIGA), an entity charged with furthering economic development in Galicia. When the project floundered because of large cost overruns, Maffezini instituted proceedings against SODIGA under the *ICSID Convention*, alleging that SODIGA’s ill conceived advice in the planning of the enterprise directly lead to its demise, in a fashion which violated his rights under the Argentine-Spain BIT. Spain contested the jurisdiction of the ICSID tribunal, arguing that Maffezini’s dispute lay not with it but solely with SODIGA. The tribunal therefore undertook to determine “whether or not SODIGA is a State entity for the purpose of determining the jurisdiction of the Centre and the competence of the Tribunal.”²⁰²

The tribunal first noted that the *ICSID Convention* itself provided no “guiding principles” on this issue. As such, the tribunal held there was no other recourse but to consult “the applicable rules of international law.” These, it noted, “have evolved and been applied in the context of the law of State responsibility,” and required consideration of “various factors,”

²⁰¹ *Supra* note 145.

²⁰² *Ibid.* at para. 75.

including both “ownership” and “control.”²⁰³ To do this it would examine SODIGA from a “formal or structural point of view”: if SODIGA was held to be either directly or indirectly owned by Spain, or directly or indirectly controlled by Spain, this would “give rise to a rebuttable presumption that it is a State entity.”²⁰⁴

The approach of the tribunal in *Maffezini v. Spain* was endorsed in 2001 by the tribunal in *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco*.²⁰⁵ In this case two Italian construction companies submitted a joint tender for the construction of a section of a planned highway in Morocco from Rabat to Fès following an international invitation by the Société Nationale des Autoroutes du Maroc (the ADM), a limited liability company active in the construction of building, maintaining and operating roadways in accordance with a concession agreement concluded with the Minister of Infrastructure.²⁰⁶ The companies were awarded the contract and proceeded to complete the planned construction, though four months behind schedule.²⁰⁷ When ADM failed to satisfy all amounts due on the basis of the delay, the Italian parties commenced investment arbitration.²⁰⁸ Asked to decide whether ADM was a state entity, the *Salini v. Morocco* tribunal referred favourably to the *Maffezini* decision and held that, “[g]enerally, any commercial entity dominated or predominantly controlled by the State or by State institutions, whether it has legal personality or not, is considered to be a State-owned company.”²⁰⁹

Although some investment arbitration tribunals have declined to refer to international law to determine whether an entity qualifies as state-owned or state-controlled, these decisions are of limited relevance to ICSID Convention claims grounded in violations of BITs or MITs. For example, in *Impregilo S.p.A. v. Islamic Republic of Pakistan*,²¹⁰ the Tribunal referred to the municipal law of Pakistan to determine whether Pakistan’s Water and Power Development Authority (WAPDA) was sufficiently owned or controlled by

²⁰³ *Ibid.* at para. 76, referring to Ian Brownlie, *System of the Law of Nations – State Responsibility, Part I* (Oxford: Clarendon Press, 1983) at 132. This attention to control in addition to ownership was again emphasized by the *Maffezini* tribunal at the Merits stage of the proceedings, where it noted that: “The structural test, however, is but one element to be taken into account. Other elements to which international law looks are, in particular, the control of the company by the State or State entities and the objectives and functions for which the company was created. As the Tribunal emphasized in its decision on jurisdiction, many of these elements point in the instant case to its public nature.” See *Emilio Agustín Maffezini v. The Kingdom of Spain* (Award, 13 November 2000), ICSID Case No. ARB/97/7 at para. 50, online: <<http://ita.law.uvic.ca/documents/Maffezini-Award-English.pdf>>.

²⁰⁴ *Maffezini v. Spain*, *supra* note 145 at para. 77.

²⁰⁵ (Decision on Jurisdiction, 23 July 2001) ICSID Case No. ARB/00/4, (2003) 42 I.L.M. 609, online: <<http://ita.law.uvic.ca/documents/Salini-English.pdf>> [*Salini v. Morocco*].

²⁰⁶ *Ibid.* at para. 2.

²⁰⁷ *Ibid.* at paras. 2-4.

²⁰⁸ *Ibid.* at para. 6.

²⁰⁹ *Ibid.* at para. 31 (emphasis added), referring also to L.J. Bouchez, “The Prospect for International Arbitration: Disputes Between States and Private Enterprises” (1991) 8 J. Int’l Arb. 81; Jan Paulsson, Book Review of *Arbitration and State Enterprises: Survey on the National and International State of Law and Practice* by Karl-Heinz Böckstiegel, (1985) 1 Arb. Int’l 195.

²¹⁰ (Decision on Jurisdiction, 22 April 2005), ICSID Case No. ARB/03/3, online: <<http://ita.law.uvic.ca/documents/impregilo-decision.pdf>> [*Impregilo v. Pakistan*].

the state. However, this was the case only in the context of Impregilo's breach of contract claims against WAPDA, which were necessarily to be determined under the law of the contract, namely Pakistani law.²¹¹ The Tribunal distinguished between alleged breaches of international law and alleged breaches of the municipal law of a contract, and specifically distinguished the facts before it from the circumstances of the decision in *Salini v. Morocco* on this basis.²¹² This distinction was also recognized by the tribunal in *Maffezini* when it held that, while the classification of an entity under domestic law could be considered by a tribunal examining the nature of a purported state-owned or state-controlled entity under international law, it will neither be determinative nor binding on the tribunal's analysis.²¹³

In total, the consensus that emerges from *Maffezini v. Spain*, *Salini v. Morocco* and *Impregilo v. Pakistan* is reasonably clear: where a question arises as to the status of an alleged SOE in respect of an international instrument the answer to this question should be sought under international law, and likely must include consideration of both the ownership and *control* of the entity. Furthermore, there is no reason why this should not be the case in respect of the Broches test and *ICSID Convention* Art. 25. The Broches test seeks to identify investors that are either acting as "government agents" or are discharging "essentially governmental functions" to prevent claims that essentially amount to disputes between states rather than disputes between states and purely private entities.²¹⁴ Therefore, the focus of the test is on identifying extensions and arms of the state that, while they are not state entities in a formal sense, are acting directly *on behalf of the state* as an "agent of the state" or *in place of the state* through the exercise of "essentially governmental functions."

As such, it would be absurd for the Broches test to be engaged exclusively by state-owned entities: state ownership is required neither for an entity to act as an arm of a state, nor for an entity to act in place of that state. However, state *control* is fundamentally necessary if an entity is to act either on behalf of a state or in place of a state at the direction of that state. Therefore, if the mischief that the Broches test seeks to prevent is the abuse of the ICSID forum by an investor that is essentially an arm of a state, then interpreting the Broches test to require government ownership of an investor in addition to government control of that investor represents an impermissibly strict reading of that test.

²¹¹ *Ibid.* at para. 210. For further discussion on this point, see Eduardo Silva Romero, "ICC Case Law" in Emmanuel Gaillard & Jennifer Younan, eds., *State Entities in International Arbitration*, IAI Series on International Arbitration No. 4 (Huntington, NY: Juris, 2008) 31.

²¹² *Impregilo v. Pakistan*, *ibid.* at paras. 210, 213.

²¹³ *Maffezini v. Spain*, *supra* note 145 at para. 82.

²¹⁴ Schreuer, *supra* note 92, Art. 25, paras. 165-169.

Sources of Ownership and Control

Once it is accepted that the Broches test will be activated by a claimant that is either owned or controlled by a state, the next question becomes what sources of such ownership and control should be considered. The *ICSID Convention*, its drafting history, related case law and commentary are again helpful in this pursuit. Together, they suggest that there can be no bright-line test for state ownership and control: the particular circumstances of each entity will need to be uniquely evaluated with a view to any relevant contextual factors.

The Tribunal in *CSOB v. Slovak Republic* decided that the issue of CSOB's standing engaged the Broches test, since it accepted that more than 65% of CSOB's shares were owned "in one form or another by the Czech Republic" and that this was sufficient to give the Czech Republic "absolute control" over the bank.²¹⁵ This exclusive focus on shareholding is understandable given the clear ability of the Czech Republic in the circumstances of the case to dictate CSOB's conduct, and follows the approach of other ICSID tribunals asked to examine the control of investors.²¹⁶ However, an exclusive reliance on control through the prism of shareholding does not appear appropriate upon examination of the *ICSID Convention*, its drafting history and further case law.

ICSID Convention Art. 25(2)(b) partly defines a "National of another Contracting State" to include "any juridical person which had the nationality of the Contracting State party to the dispute... and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purposes of this Convention (emphasis added)."²¹⁷ Although this does not speak directly to the question of state control, it has provided much useful discussion as to "control" in the context of Art. 25. This body of commentary and law clearly establishes that tribunals should approach issues of Art. 25 "control" with a wide lens.

At least in the context of Art. 25(2)(b), the drafters of the *ICSID Convention* recognized that "a mere majority holding of shares would not necessarily be [a] decisive [indicator of control]."²¹⁸ Not only was it not meant to be decisive, it was not even meant to be necessary: the drafters recognized that "even a minority holding of as little as 25% or even 15% might amount to control through a capacity to block major changes or otherwise."²¹⁹ In this regard, as noted by Schreuer:

[c]ontrol over a juridical person is not a simple phenomenon. Participation in the company's stock or share ownership, while relatively simple to ascertain,

²¹⁵ *CSOB v. Slovak Republic*, *supra* note 140 at para. 18.

²¹⁶ See e.g. *Klöckner v. Republic of Cameroon* (Award, 21 October 1983), ICSID Case No. ARB/81/2, 2 ICSID Rep. 3 at 15-16.

²¹⁷ The purpose of this provision is to allow companies incorporated in state A to bring investment claims against state A where they are controlled by investors from state B. This provision is therefore an acknowledgement of, and a response to, the fact that it is common for national foreign investment laws to require inbound foreign investment to be made through locally incorporated vehicles. See Schreuer, *supra* note 92, Art. 25, paras. 760-763.

²¹⁸ *Ibid.*, Art. 25, para. 851, referring to *History*, *supra* note 199 at 359-360, 396, 447-448, 538.

²¹⁹ Schreuer, *ibid.*, referring to *History*, *ibid.* at 447-448, 538.

is not necessarily a reliable indicator of control. Different voting rights attached to different types of shares, decision-making procedures and the exercise of management all contribute to a complex picture of control.²²⁰ He concludes that the existence of adequate control for the purpose of Article 25 "is a complex question requiring examination of several factors" and that, "for purposes of ICSID's jurisdiction, the concept of control should be treated with some flexibility."²²¹

Various investment tribunals have likewise recognized the complexity of inquiries into control. In *Vacuum Salt Products Limited v. Government of the Republic of Ghana*,²²² the Tribunal had to determine whether a Ghanaian company 80% owned by Ghanaian nationals and 20% owned by a Greek national could for the purpose of Art. 25(2)(b) be considered to be controlled by the latter. The Tribunal concluded that there is no strict "formula" for determining control and that each case "must be viewed in its own particular context, on the basis of all the facts and circumstances."²²³ The Tribunal decided it "reasonable" to conclude that "100% ownership would almost certainly result in... control, by whatever standard," and that a total absence of shareholding would "virtually preclude the existence of such control."²²⁴ However, how much control would be "enough" control, the tribunal reasoned, could not be "determined abstractly" and it recommended in addition to ownership such criteria as voting rights and management powers. It also emphasized that, the less shareholding was present, the more such various other indicators of control would be required.²²⁵

The Tribunal in *International Thunderbird Gaming Corporation v. The United Mexican States*²²⁶ also examined what factors other than share ownership could result in control. Although Thunderbird owned less than 50% of the shares in certain Mexican investment vehicles, the tribunal nonetheless held that there was sufficient *de facto* control. The tribunal noted that:

It is quite common in the international corporate world to control a business activity without owning the majority voting rights in shareholder meetings. Control can also be achieved by the power to effectively decide and implement the key decisions of the business activity of an enterprise and, under certain circumstances, control can be achieved by the existence of one or more factors such as technology, access to supplies, access to markets, access to capital, know how, and authoritative reputation. Ownership and legal control may assure that the owner or legally controlling party has the ultimate right to determine key decisions. However, if in practice a person exercises that position with an expectation to receive an economic return for

²²⁰ Schreuer, *ibid.*, Art. 25, para. 850.

²²¹ *Ibid.*, Art. 25, paras. 864-865.

²²² *Vacuum Salt Products Limited v. Government of the Republic of Ghana* (Award, 16 February 1994), ICSID Case No. ARB/92/1, 9 ICSID Rev. – F.I.L.J. 72 [*Vacuum Salt v. Ghana*].

²²³ *Ibid.* at para. 43.

²²⁴ *Ibid.*

²²⁵ *Ibid.* at paras. 43-44.

²²⁶ (Award, 26 January 2006), (Arbitral Tribunal constituted under Chapter Eleven of NAFTA, conducted under the UNCITRAL Arbitration Rules) at para. 107, online: <http://www.iisd.org/pdf/2006/itn_award.pdf>. Note that, as this case proceeded under the UNCITRAL arbitration rules, the tribunal was not discussing the concept of control expressly in relation to the ICSID Convention.

his efforts and eventually be held responsible for improper decisions, one can conceive the existence of a genuine link yielding the control of the enterprise to that person.²²⁷

This formulation had much merit. However, it is important to note that, as it takes a broad and rather inclusive approach to defining the ability to control, it also simultaneously creates the possibility that an entity may have multiple “controllers.”

The Tribunal in *Vacuum Salt v. Ghana* was conscious of this proposition and questioned whether “control” within the meaning of Art. 25 “means exclusive control, or whether it allows for the possibility that more than one shareholder or group or shareholders may enjoy control.”²²⁸ However, it reached no conclusion on the matter as it found that it need not address the issue in the circumstances at hand.²²⁹ Schreuer is of the opinion that the existence of multiple controllers should not preclude an investment tribunal from focusing on one such controller in particular, and making a conclusive decision on jurisdiction on that basis.²³⁰ In other words, he argues that the fact that one controller can be said to exercise a higher degree of control than a second controller need not necessarily require dismissing the second controller as a true or real controller.²³¹ Accepting this proposal requires distinguishing between “absolute control” and “a reasonable amount of control” without immediately discriminating against or disregarding the latter.²³² However, he also cautions that “not every substantial minority participation should be accepted as control.”²³³ On the other hand, Schreuer further contends that, in principle, tribunals should not ignore the collective control exercised by two or more sources. He finds support for this proposition in the rulings in *Sempra Energy International v. The Argentine Republic*²³⁴ and *Camuzzi International S.A. v. The Argentine Republic*²³⁵ in which the respective Tribunals allowed control influenced by multiple minority foreign investors to combine to satisfy the control requirements of ICSID Convention Art. 25(2)(b). In the case of an alleged SOE, this would allow a tribunal to consider not just the cumulative effect of various means of state influence, but also the cumulative effect of multiple sources of such state influence, including various different government officials, bodies, agencies, organs or otherwise.

Another important question arises as to whether control must be in fact be exercised, or whether its mere presence and potential to be exercised is sufficient.²³⁶ In *AdT v. Bolivia*, for example, the Tribunal noted that the

²²⁷ *Ibid.* at para. 108.

²²⁸ *Vacuum Salt v. Ghana*, *supra* note 222 at para. 43, fn. 21.

²²⁹ *Ibid.*

²³⁰ Schreuer, *supra* note 92, Art. 25, para. 865.

²³¹ *Ibid.*

²³² *Ibid.*

²³³ Schreuer, *supra* note 92, Art. 25, para. 865.

²³⁴ (Decision on Objections to Jurisdiction, 11 May 2005), ICSID Case No. ARB/02/16 at para. 51, online: <<http://ita.law.uvic.ca/documents/sempira-en.pdf>>.

²³⁵ (Decision on Objections to Jurisdiction, 11 May 2005), ICSID Case No. ARB/03/2, online: <<http://ita.law.uvic.ca/documents/camuzzijurisdiction.pdf>>.

²³⁶ Schreuer, *supra* note 92, Art. 25, paras. 859-863.

ordinary meaning of “control” can “encompass both actual exercise of powers or direction and the rights arising from the ownership of shares.”²³⁷ Stated differently, the Tribunal distinguished between the “power to control” and “the actual exercise of control.”²³⁸ AdT had instituted ICSID arbitration under the Bolivia-Netherlands BIT and sought to satisfy the control requirements of Art. 25(2)(b) on the basis of its ownership by a series of Dutch holding companies.²³⁹ However, Bolivia objected to the jurisdiction of the Tribunal on this basis, arguing that the holding companies were mere shells without any actual control over AdT and that all such actual control resided with the large Italian and American parents of the holding companies.²⁴⁰ As such, Bolivia argued that any assertion of control required proof of actual control.²⁴¹ The Tribunal disagreed, deciding that “it is almost impossible to discern precisely at what stage mere formal control through ownership might transform and become actual or effective control.”²⁴² It therefore concluded that control is “a quality of the ownership interest” that exists regardless of its actual exercise.²⁴³ It decided that “an entity may be said to control another entity [merely] if it possesses the legal capacity to control it” even in the “absence of its overt exercise” of such control.²⁴⁴

Altogether, these authorities combine to sketch a broad portrait of the various possible manifestations of control for Tribunals to consider. A majority shareholding may be considered very strong proof of control but should not necessarily be considered decisive. Nor should control through ownership be automatically dismissed where only a minority position is held. No rigid formula for determining control should be mapped and each case should be viewed in the totality of its particular circumstances. Control may be weighed via a multiplicity of criteria, including voting rights, management powers, executive influence, access to capital and other resources, and unofficial but authoritative sources of power. There can be multiple controllers, and the presence of a controller with greater influence than a second controller will not necessarily diminish the significance of the authority of such second controller. Nor should a tribunal be barred from considering the cumulative effect of multiple different sources of influence in addition to multiple different means of influence. On the other hand, control need not necessarily be exercised in order to be recognized; potential control in the form of legal capacity can be sufficient.

The flexibility of these considerations is a good thing. The size, complexity and dynamism of contemporary SOEs defy simple categorization and demand the application of an extensive set of analytical tools to be

²³⁷ *Supra* note 135 at para. 227.

²³⁸ Schreuer, *supra* note 92, Art. 25, para. 859, referring to *AdT v. Bolivia*, *ibid.* at para. 232.

²³⁹ *AdT v. Bolivia*, *ibid.* at paras. 210-213.

²⁴⁰ *Ibid.* at paras. 206-209.

²⁴¹ *Ibid.* at para. 207.

²⁴² Schreuer, *supra* note 92, Art. 25, para. 860, referring to *AdT v. Bolivia*, *ibid.* at para. 247.

²⁴³ *AdT v. Bolivia*, *ibid.* at para. 242.

²⁴⁴ Schreuer, *supra* note 92, Art. 25, paras. 861-862, referring to *AdT v Bolivia*, *ibid.* at paras. 242, 264.

properly appreciated and understood,²⁴⁵ and this is no less the case in respect of investigations into the control of SOEs. Tribunals determining the standing of a purported SOE to bring arbitration under *ICSID Convention* Art. 25 should be conscious of the many means of implementing control over an SOE and should not refrain from the investigation of each. Nor should they necessarily refrain from setting a moderate standard in respect of what should be considered a SOE for the purposes of *ICSID Convention* Art. 25. As acknowledged by the Tribunal in *CSOB v. Slovak Republic*, Art. 25 does not absolutely bar the participation of SOEs as claimants under the *ICSID Convention*. It merely bars SOEs “acting as an agent” for their home government or SOEs “discharging an essential governmental function” in place of their home government. Therefore, the identification of a purported SOE as an actual SOE is not the end of the inquiry but in many respects the beginning of the real inquiry: whether the entity is or has been in fact behaving in a fashion which would infringe the intentions of the *ICSID Convention*’s drafters. In this regard, while it is arguable that tribunals should adopt a relatively rigorous standard in respect of the type of activity that will bar an SOE from standing under Art. 25, it is where the two limbs under the Broches test are actually being applied that such a rigorous standard would be most appropriate. Either way, what is clear is that significant further analysis of the relationship between *ICSID Convention* Art. 25 and SOEs by investment arbitration tribunals is to be welcomed.²⁴⁶

V. Conclusion

This article has attempted to address a number of difficult questions that may arise where an investor owned or controlled by a state institutes an investment arbitration claim. In particular, it has examined how investment tribunals should proceed when deciding whether a SOE has standing to

²⁴⁵ For an in depth analysis of the structure, function and control of Chinese SWFs and SOEs, for example, see Backer, *supra* note 7. For a similar review of various state-owned oil companies, see Marcel, *supra* note 24.

²⁴⁶ Unfortunately, not all tribunals have met this obligation. See e.g. *Rumeli Telekom A.S. and Telsim Mobil Telekomunikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (Award, 29 July 2008), ICSID Case No. ARB/05/16 at paras. 280-300, 327, online: <<http://ita.law.uvic.ca/documents/Telsimaward.pdf>>.

Kazakhstan raised several objections to the jurisdiction of the tribunal, based on the control of a Turkish state agency (TSDIF) over the Claimants. In particular, Kazakhstan argued that TSDIF’s control of Rumeli and Telsim prevented the claim from satisfying the restrictions in *ICSID Convention* Art. 25 on the standing of state-owned investors. Kazakhstan conceded that the shares of the Claimants remained in private hands, and not in the hands of TSDIF. However, Kazakhstan argued that corporate control under the *ICSID Convention* is not viewed exclusively through the lens of share ownership, but includes consideration of such elements as management and decision-making structure. In this regard, while the Claimants were not owned by TSDIF, Kazakhstan argued that by virtue of recent legislation the Claimants remained under the complete control of TSDIF and were thus “effectively State-owned corporations”. According to Kazakhstan, this required the application of the Broches test to the claimant’s operation and activities, including the act of bringing the investment arbitration claim itself. However, Kazakhstan’s efforts in this regard were lost upon the tribunal. Rather than dealing with the assertion that the Claimants were “effectively state owned corporations” for the purposes of Art. 25, the tribunal appeared to brush aside Kazakhstan’s argument simply by asserting that the “record... confirms that the TSDIF is not the owner of Claimants’ shares.”

arbitrate under a particular IIT and when deciding whether a SOE has standing to arbitrate under the Art. 25 of the *ICSID Convention*.

However, this survey is not exhaustive and a number of other important issues may arise. For example, it is important to note that a Most Favoured Nation (MFN) clause, contained in the IIT under which a SOE brings its claims, may impact on the standing of the SOE under the IIT. It has become common practice for investors to employ MFN clauses in IITs to access more favourable provisions in other IITs signed by the same host state against which they are bringing their claim.²⁴⁷ In the context of a SOE claim, this could affect a tribunal's investigation of the broader treatment of SOEs by an IIT.²⁴⁸ On the other hand, it is important to recognize that many IITs contain national security exceptions that exempt the States parties from liability where their otherwise unlawful actions are in response to a threat to their security. Therefore, even where an SOE is clearly protected under an IIT, it may not be entitled to protection or compensation under the treaty if its actions can be interpreted by a tribunal as threatening the security of its host state.²⁴⁹

All of these issues are deserving of further study and analysis. Different countries have different histories with public ownership, but going forward SWFs and SOCs are only expected to grow in number and influence in what may very well become an increasingly turbulent world.²⁵⁰ Furthermore, while there is not yet any known instance of SWFs behaving in an overtly political manner rather than in pursuit of purely benign commercial objectives²⁵¹ and while the International Energy Agency has very recently announced that Chinese state oil companies, for example, should not be

²⁴⁷ See, for example, *Maffezini v. Spain*, *supra* note 145; *Plama Consortium Limited v. Bulgaria* (Decision on Jurisdiction, 8 February 2005), ICSID Case No. ARB/03/24, online: <<http://ita.law.uvic.ca/documents/plamavbulgaria.pdf>>; *RosInvestCo v. Russia*, *supra* note 130. For one of a number of academic discussions of the role and use of MFN clauses in investor-State arbitration, see Dana H. Freyer & David Herlihy, "Most-Favoured-Nation Treatment and Dispute Settlement in investment Arbitration: Just How 'Favored' is 'Most-Favored'?" (2005) 20 *ICSID Rev.* – F.I.L.J. 58.

²⁴⁸ Note that, as the *ICSID Convention* does not contain a MFN clause, this issue will not occur in the context of SOE standing under the *Convention*.

²⁴⁹ See UNCTAD, "National Security", *supra* note 9; William W. Burke-White & Andreas von Staden, "Investment Protection in Extraordinary Times: The Interpretation and Application of Non-Precluded Measures Provisions in Bilateral Investment Treaties" (2008) 48 *Va. J. Int'l L.* 307; Susan Rose-Ackerman & Benjamin Billa, "Treaties and National Security" (2008) 40 *N.Y.U.J. Int'l L. & Pol.* 437; Andrea K. Bjorklund, "Emergency Exceptions: State of Necessity and Force Majeure" in Peter Muchlinski, Federico Ortino & Christoph Schreuer, eds., *Oxford Handbook of International Investment Law* (New York: Oxford University Press, 2008) 459.

²⁵⁰ Kovacs, *supra* note 12. The reality is that the future permutations of an emerging "state capitalism" cannot accurately be predicted. See Jeffrey Garten, "The Unsettling Zeitgeist of State Capitalism" *Financial Times* (14 January 2008); "A Special Report on Globalisation: The Rise of State Capitalism" *The Economist* (20 September 2008); Rose, "Sovereigns", *supra* note 51 at 149 ("we may yet see the day when SWFs are viewed not merely as commercial tools, but also as economic and political tools used by all sovereigns in the normal course of international affairs.")

²⁵¹ Rose, "Active or Passive", *supra* note 71. See also Gordon & Tash, *supra* note 36 at 4; Fotak & Megginson, *supra* note 44.

considered “puppets” of their home state,²⁵² this is not necessarily the case in respect of SOCs.²⁵³ Moreover, while the interests of capital importing states and SOEs are currently aligned, it does not take much imagination to imagine circumstances, such as a prolonged global energy crisis,²⁵⁴ where this might be less the case. Should this occur, it is easy to imagine foreign SOEs becoming the target of heightened political suspicion and controversy, whether justified or not, as well as the target of focused regulatory intervention, whether arbitrary or discriminatory or not. Broadly worded domestic investment legislation such as the FINSA gives regulatory bodies such as the CFIUS and the executive behind it the power to force the divestiture of foreign investment at any point in its lifetime. This power will always be vulnerable to capture by forces and sentiment beyond the control of individual investors and sometimes even individual administrations.²⁵⁵ The fear of foreign competitors and foreign governments is an often powerful stimulant. This can lead to overreactions by host governments that result in legitimate international investment arbitration claims by state-owned or state-controlled foreign investors.

To mitigate these risks that are perhaps inherent in international investment by SOEs, two steps can be taken. One of the surest ways to safeguard against such abuses and unnecessary confusion regarding the jurisdiction of investment arbitration tribunals to hear cases brought by SOEs is clearer drafting in national legislation and international investment treaties. In addition, building on the framework set out in this article would result in the elaboration of principles for international investment law that better serve all interested parties, regulators and investors alike: principles that would be more clearly agreed-upon among stakeholders, more predictable in their application, and therefore more capable of serving as the basis for informed investment decision-making.

²⁵² Peter O’Neil, “Chinese oil companies aren’t ‘puppets,’ report says” *Calgary Herald* (17 February 2011).

²⁵³ Perhaps the most glaring example of politically motivated activity by SOCs (again, as opposed to by SWFs) is the politically charged operations of Russia’s Gazprom and Transneft. These SOCs have repeatedly been used to send strong messages to Eastern and Central European states. In particular, Russia has directed Gazprom to turn off gas supplies to Ukraine a number of times following disagreements between the two states regarding foreign policy. Russia has also directed Transneft to slow oil pipeline flows to the Czech Republic following that country’s talks with the US regarding the installation of missile defence technology in the Czech Republic. See Ribblett, *supra* note 1 at 26. Chinalco’s direct involvement in the scuttling of Rio Tinto’s proposed merger with BHP Billiton has raised suspicion that the company was acting on behalf of China, which sought to preserve a diversity of mineral suppliers. See Schwalb, *supra* note 7.

²⁵⁴ See Hon. Richard D. Cudahy, “The Bell Tolls for Hydrocarbons: What’s Next?” (2008) 29 Energy L.J. 381.

²⁵⁵ For a discussion of some of the most recent foreign investment proposals attracting intense scrutiny by CFIUS, see Eric Lipton, “Questions on Security Mar Foreign Investments” *New York Times* (18 December 2009) B1.

Crafting a Multilateral Solution for North Korean Refugee Settlement

What American Policymakers Can Learn from the Indochinese Refugee Crisis

YUAN JI*

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I. Introduction

A pressing humanitarian crisis is ongoing but lacks an adequate solution. Food shortages and human rights violations have driven many North Korean asylum seekers to cross the border into China. Once there, they are given no legal protection, categorically defined as illegal economic migrants, and subject to forced repatriation. The severity of the food shortage has been compared to that of the North Korean famine in the mid-1990s, which killed between one and three million people.¹ As of 2007, it is estimated that 300,000 North Korean migrants reside in China,² and those forcibly returned to North Korea "routinely face prison, torture, and sometimes execution."³ The majority of North Korean refugees⁴ in China do not wish to remain there permanently. The Peterson Institute for International Economics and the United States Committee for Human Rights in North Korea conducted a survey of these refugees in 2008. Out of a sample of 1247, the majority (64.3%) wished to resettle in South Korea and 19.1% wished to resettle in the United States.⁵

The United States is home to the largest Korean population outside of Northeast Asia and many in the Korean-American community have family ties to North Korea.⁶ In 2004, the US Congress passed the *North Korean Human Rights Act (NKHRA)*.⁷ The enactment of the *NKHRA* was motivated by a concern both for human rights abuses that are pervasive in North Korea and for human rights issues facing North Korean refugees when they arrive in the United States.⁸ The *NKHRA* grants refugee status to all eligible North

¹ House Committee on Foreign Affairs, *North Korean Human Rights Reauthorization Act of 2008* (H.R. Rep. No. 110-628) (Washington, D.C.: United States Government Printing Office, 2008) at 5 [House Committee, 2008 Reauthorization Act Report].

² Congressional Research Service, *North Korean Refugees in China and Human Rights Issues: International Response and U.S. Policy Options* (26 September 2007) at CRS-4, online: <<http://www.fas.org/spp/crs/row/RL34189.pdf>> [2007 CRS Report]. Press reports typically estimate the number of North Korean migrants residing in China to be anywhere between 100,000 and 300,000. The estimates used by the Chinese government, the U.S. State Department, and UNHCR have been significantly smaller than 300,000 but there are reasons to doubt the accuracy of the official estimates, such as UNHCR's lack of access to conduct a systematic survey.

³ House Committee, 2008 Reauthorization Act Report, *supra* note 1 at 5.

⁴ The term "refugee" is defined by the two key international instruments governing refugee protection: *Convention relating to the Status of Refugees*, 28 July 1951, 189 U.N.T.S. 150 (entered into force 22 April 1954) [*1951 Refugee Convention*]; *Protocol relating to the Status of Refugees*, 31 January 1967, 606 U.N.T.S. 267, 19 U.S.T. 6223 (entered into force 4 October 1967) [*1967 Protocol*].

⁵ Congressional-Executive Commission on China, "North Korea Executes 15 Attempting Escape, China Arrests 40 Refugees" (25 June 2008), online: <<http://www.cecc.gov/pages/virtualAcad/index.php?showsingl=105687>>.

⁶ House Committee, 2008 Reauthorization Act Report, *supra* note 1 at 2.

⁷ *North Korean Human Rights Act of 2004*, Pub. L. 108-333, 118 Stat. 1287, 22 U.S.C. 7801 et seq. [NKHRA].

⁸ See e.g. *NKHRA*, *ibid.*, s. 302(a) (clarifying that "North Koreans are not barred from eligibility for refugee status or asylum in the United States on account of any legal right to citizenship they may enjoy under the Constitution of [South Korea]").

Koreans⁹ and, for fiscal years 2005-2008, authorized an annual budget of up to \$20 million for the assistance of North Korean refugees.¹⁰

However, implementation of the NKHRA has been ineffective and slow in the resettlement of North Korean refugees. In 2006, a bipartisan group of nine members of Congress expressed their concern over this issue as follows: “despite the fact that the [NKHRA] calls for the Department of State to facilitate the submission of North Korean refugee applications, not one North Korean has been offered asylum or refugee status in the 16 months since the unanimous passage of the legislation.”¹¹ Indeed, the first North Korean refugees did not arrive in the United States until May 2006, nineteen months after the passage of the NKHRA, and as of 2009, the asylum claims of only 81 North Koreans have been recognized by the American government.¹²

In 2008, Congress passed the *North Korean Reauthorization Act* (2008 *Reauthorization Act*) to renew the NKHRA for the years 2009-2012, on the basis of its “longstanding commitment ... to refugee and human rights advocacy.”¹³ The renewal furthered Congress’ intentions for the United States to “pursue an international agreement to adopt an effective ‘first asylum’ policy, modeled on the first asylum policy for Vietnamese refugees, that guarantees safe haven and assistance to North Korean refugees.”¹⁴

“Vietnamese refugees” refers to the outpour of refugees, beginning in 1975, from Vietnam, Laos, and Cambodia. These refugees sought temporary first asylum—primarily in Thailand but also in Malaysia, Singapore, Indonesia, the Philippines, and Hong Kong—before moving to the United States and other countries for permanent resettlement. This mass exodus, known as the Indochinese refugee crisis, followed the end of the Vietnam War and the Communist takeovers in Vietnam, Laos, and Cambodia during the 1970s. Close to two million people fled their homelands in Southeast Asia for political or economic reasons. The resettlement of Indochinese refugees during this humanitarian crisis was achieved through international burden-sharing, with Thailand and the United States taking respective leadership in providing first asylum and permanent resettlement.

One important lesson from the Indochinese episode is that a multilateral solution to a humanitarian problem does not require all parties to share the same motivations, and a purely humanitarian rhetoric that fails to consider the national interests of the parties involved is not likely to effect actual change. Thailand served as the primary first asylum country in the

⁹ Eligibility for North Koreans seeking refugee and asylum status under the NKHRA is defined respectively by ss. 207 and 208 of the *Immigration and Nationality Act*, 8 U.S.C. 1157, Pub. L. No. 82-414, 66 Stat. 163. See *NKHRA*, *ibid.*, s. 302(b).

¹⁰ Congressional Research Service, *Congress and U.S. Policy on North Korean Human Rights and Refugees: Recent Legislation and Implementation* (22 October 2008) at CRS-2, online: <<http://fpc.state.gov/documents/organization/112040.pdf>>.

¹¹ House Committee, *2008 Reauthorization Act Report*, *supra* note 1 at 5-6.

¹² “No. of N.Korean Refugees in U.S. ‘Reaches 81’” *Chosun Ilbo* (7 May 2009), online: Arirang News <http://english.chosun.com/site/data/html_dir/2009/05/07/2009050700644.html>.

¹³ *North Korean Human Rights Reauthorization Act of 2008*, Pub. L. 110-346, 122 Stat. 3939.

¹⁴ House Committee on International Relations, *North Korean Human Rights Act of 2004* (H.R. Rep. No. 108-478) (Washington, D.C.: United States Government Printing Office, 2004) at 7.

Indochinese crisis, and China is the natural candidate to assume similar leadership in the current North Korean crisis. An evaluation of Thailand's interests and motivations with respect to the Indochinese crisis reveals insights on how American policymakers can more effectively persuade China to take leadership in providing first asylum to North Korean refugees. Of course, there are limits to this analogy, and these limits will be canvassed in Part IV.

To the extent that the analogy between the two refugee crises is appropriate, this article will argue that even if motivated by humanitarian concerns, American policymakers should nevertheless take a pragmatic approach to the negotiation and implementation of a multilateral solution for the North Korean refugee crisis. Specifically, this article proposes policies for the current US administration by focusing on two key and related themes: i) as demonstrated by the Indochinese refugee crisis, successful negotiation and implementation of a multilateral solution requires a pragmatic awareness of the partner states' national interests; and ii) successful resettlement of North Korean refugees must engage China, a key partner, by understanding its interests and burdens arising from the provision of first asylum. American diplomatic dialogue with China might make more progress on the issue if it focuses less on human rights and more on, for example, the financial benefits that could potentially result if China were willing to recognize refugee status for qualifying North Korean refugees. Part of the NKHRA's annual budget should also be pledged to the development of an effective domestic screening program, which would assure China that the rate of permanent resettlement in the United States would not lag behind China's admission of North Koreans.

As demonstrated by its role in the six-party talks over nuclear nonproliferation, China is a crucial player in any multilateral collaboration regarding North Korea. In the refugee context, China's importance derives from various factors including its negotiating power over North Korea, its partnership with South Korea, and its status as the primary first stop for North Korean refugees. The NKHRA, while well-intended, has made little progress in resettling North Korean refugees because, among other shortcomings, it has failed to garner China's partnership. While South Korea is bound to play an important role in any multilateral resettlement of North Korean refugees and should not be sidelined, this article will primarily focus on the potential progress that bilateral US-China leadership can make in resettlement efforts.

Part II will reflect on the lessons from Indochinese refugee resettlement, during which the United States and Thailand took respective leadership roles in providing permanent resettlement and first asylum. Thailand, like China, viewed refugees as illegal economic migrants and for the most part did not base its asylum policy on humanitarian concerns. A primary lesson from the Indochinese crisis is that a successful multilateral solution does not require the states that assume leadership roles to have completely identical motives. Rather, it is sufficient for them to have an overlap of interests, which is certainly conceivable in the North Korean scenario. Such an overlap of

interests is illustrated, for example, by the modern US-China cooperation in pressuring North Korea to abandon its nuclear program.

Part III will explain why it is crucial for the NKHRA or any future American foreign policy to engage China's partnership in the resettlement of North Korean refugees. It will examine the national interests that shape China's current policy of denying refugee status to all North Korean defectors. This will reveal that those crafting American foreign policy must address China's national interests first if they wish to be effective in seeking Chinese collaboration.

Part IV will point out the NKHRA's shortcomings as well as the imperfections in current international law's protection of economic refugees. It proposes that effective US-China leadership in North Korean refugee resettlement should work with rather than in criticism of the Chinese legal system. This approach is adopted from the lessons offered by the Thai experience during the Indochinese refugee crisis. Part V will address the challenges in implementing these policy proposals and the difference in circumstances between the Indochinese episode and the North Korean situation at present.

II. Lessons from the Indochinese Refugee Crisis: US-China Leadership in Forming a Multilateral Resettlement Solution for North Korean Refugees

The 1990s saw a global trend of increasingly restrictive asylum policies and a general failure to comply with international treaty obligations toward refugees.¹⁵ International burden-sharing schemes that allocate refugees to recipient states for permanent resettlement, such as the ones proposed for the Haitian refugee crisis of 1994, have been revived as solutions to this problem.¹⁶ The last successful multilateral resettlement of a large Asian refugee population was that of the Vietnamese refugees following the end of the Vietnam War in 1975. Although small numbers of Laotians and Khmers were resettled as well during this period, the outflow primarily originated from Vietnam: roughly 700,000 Vietnamese resettled in Western developed countries during the 1980s and the early 1990s.¹⁷

Burden-sharing aims to distribute the burdens of refugee protection fairly among the members of the international community. It is rooted in broad participation by states, consent of participating states, and proportionality in each state's share of burdens relative to other states.¹⁸ The principle of burden-sharing was key to the resettlement program for Indochinese refugees, for which countries like Thailand, Malaysia, and Indonesia agreed to grant first asylum as long as permanent resettlement

¹⁵ Astri Suhrke, "Burden-sharing during Refugee Emergencies: The Logic of Collective versus National Action" (1998) 11 J. Refugee S. 396 at 396 [Suhrke, "Burden-sharing"].

¹⁶ *Ibid.* at 396-97.

¹⁷ *Ibid.* at 405.

¹⁸ Peter H. Schuck, "Refugee Burden-Sharing: A Modest Proposal" (1997) 22 Yale J. Int'l L. 243 at 276-77.

would be provided elsewhere. Another distinctive feature of this resettlement program was the hegemonic role played by the United States, which rallied collective action among participating states while doing its own "fair share" of resettlement out of humanitarian and political considerations.¹⁹

Granted, past American leadership in the resettlement of Indochinese refugees is not indicative of future success with North Korean refugees; the circumstances underlying the Indochinese refugee outflow were very different from those corresponding to the North Korean refugee problem. The former was the result of war and political repression, while the latter was brought about by the North Korean famine during the 1990s. Also, the United States has different interests with respect to the two scenarios. Without an analogous sense of responsibility like that resulting from American involvement in the Vietnam War, the United States' interests in the successful resettlement of North Korean refugees are arguably less compelling. Thus, it cannot be claimed that a comparison of the two situations alone would provide a sufficient solution to the North Korean refugee crisis.

However, to the extent that effective implementation of the *NKHRA* complements the American tradition of humanitarianism and "voting with your feet" foreign policy,²⁰ the Indochinese refugee crisis offers valuable lessons for North Korean refugee resettlement. The passing of the *NKHRA* indicates that the United States is willing to take leadership in the permanent resettlement of North Korean refugees in a manner similar to what it did during the Indochinese refugee crisis of the late 1970s.²¹ But to do so effectively, it must coordinate its policies and diplomacy with China in order to form a multilateral solution. The *Immigration and Nationality Act*,²² which was amended by the *Refugee Act of 1980*,²³ authorizes the admission of refugees of special humanitarian concern to the United States based on the President's determination in consultation with Congress.²⁴

¹⁹ Suhrke, "Burden-sharing", *supra* note 15 at 405, 413. For examples of burden-sharing schemes for refugee resettlement, see *ibid.* at 397.

²⁰ The American facilitation and encouragement of Cuban immigration following the Cuban revolution, for example, was based on humanitarian concerns and the wish to show the world that the revolution had failed democratic ideals. See Maria de los Angeles Torres, "The Politics of Cuban Emigrés in the United States" in Felix Padilla, ed., *Handbook of Hispanic Cultures in the United States: Sociology*, vol. 3 (Houston: Arte Publico, 1994) 133 at 136.

²¹ Even though various US-based organizations like Human Rights Watch and North Korean Freedom Coalition have urged President Obama to take a stance on the North Korean human rights issue, the Obama administration has remained silent on the topic: Human Rights Watch, "US/South Korea: Obama Should Raise North Korea Rights Issues" (17 November 2009), online: <<http://www.hrw.org/en/news/2009/11/17/usssouth-korea-obama-should-raise-north-korea-rights-issues>>; "Obama pressed to raise NK refugee plight with Hu" *The Korea Times* (12 January 2011), online: <http://www.koreatimes.co.kr/www/news/nation/2011/01/116_79563.html>.

²² *Supra* note 9.

²³ *Refugee Act of 1980*, Pub. L. No. 96-212, 94 Stat. 102.

²⁴ U.S. Department of State, Bureau for Refugee Programs, *Report of the Indochinese Refugee Panel* 7 (1986) [Report of the Indochinese Refugee Panel].

One of Congress's goals in renewing the 2004 NKHRA is the following: [T]he United States should make it a priority to seek broader permission and greater cooperation from foreign governments to allow the United States to process North Korean refugees overseas for resettlement in the United States, through persistent diplomacy by senior officials of the United States, including United States ambassadors to Asia-Pacific nations[.]²⁵

The 2008 *Reauthorization Act* provides a similar statutory solution specific to the North Korea refugee crisis. Citing China's "increasingly aggressive campaign to locate and forcibly return border-crossers to North Korea," the House Committee Report accompanying the Bill called for the Chinese government to stop forcible repatriation of North Korean refugees, fulfill international treaty obligations, and allow the United Nations High Commissioner for Refugees (UNHCR) into its territory for refugee status assessments.²⁶

This can be accomplished if the United States engages China to take leadership in serving as a temporary first asylum country and coordinates the permanent resettlement of North Korean refugees with South Korea. Before discussing the implementation of such a multilateral solution, it is necessary to first give an overview of the United States' involvement in the Indochinese refugee crisis of the late 1970s, which bears similarities to the present North Korean situation.

1. Background of the Indochinese refugee crisis

The end of the Vietnam War and subsequent communist takeovers in Vietnam, Laos, and Cambodia caused close to two million people to flee from their home countries and seek asylum in nearby ASEAN countries.²⁷ The influx of Indochinese refugees fled predominantly to Thailand, whose history of accepting Vietnamese refugees dates back to the Indochina Wars in the 1940s. Although some of the individuals who took part in the Indochinese exodus were genuine political refugees who feared imprisonment or execution under the communist regimes in their home countries, a significant number were economic migrants who escaped in order to avoid the deteriorating quality of life under the new regimes.²⁸

During the decade following the fall of Saigon in April 1975, the United States led, more than any other country, the process of receiving Indochinese refugees for permanent resettlement. Between April 1975 and February 1986, 1.7 million refugees were recorded as reaching first asylum and over half

²⁵ 2008 *Reauthorization Act*, *supra* note 13, s. 3(1).

²⁶ House Committee, 2008 *Reauthorization Act Report*, *supra* note 1, ss. 2(4) and 3(5).

²⁷ Valerie O'Connor Sutter, *The Indo-Chinese Refugee Dilemma* (Baton Rouge: Louisiana State University Press, 1990) at 4 (Thailand served as the primary first asylum country, but other ASEAN (The Association of Southeast Asian Nations) countries such as Malaysia, Singapore, Indonesia, and the Philippine participated as well).

²⁸ Astrid Suhreke, "Indochinese Refugees: The Law and Politics of First Asylum" (1983) 467 Annals Am. Acad. Pol. & Soc. Sci. 102 at 106, fn.4 (noting that State Department officials have estimated economic refugees to be somewhere between 40 to 60 percent of recent Indochinese refugee arrival at various times) [Suhreke, "Law and Politics of First Asylum"].

were received by the United States, which has continued its commitment to Indochinese refugees through generous admissions since 1986.²⁹

Before 1979, however, the United States, France, and other countries had adopted selective resettlement policies that preferred only the most highly educated and skilled of the Indochinese refugees. Meanwhile, an increasing influx of refugees led the Thai government to adopt tougher deterrence measures, such as closing the Thai-Laotian border in September 1977 and turning large groups of Vietnamese boat people back to the sea in late 1977.³⁰ The July 1979 UN Geneva Conference on Refugees and Displaced Persons in South East Asia elevated the issue to the international spotlight; the international community felt that this was not a problem for the first asylum countries to cope with alone, but rather a humanitarian crisis that could only be solved through international cooperation and burden-sharing.³¹

The United States' response appeared to be consistent with the American tradition of humanitarianism, but it is naïve to evaluate any country's decisions without taking its national interests into consideration.³² America's foreign policy since World War II has consistently encouraged "voting with your feet" in order to isolate Communist regimes. This trend is reflected in the liberal admission policies it has extended to refugees from the Soviet Bloc,³³ and in this light it is not surprising that the United States was willing to accept Indochinese refugees after the Communist unification of Vietnam.

In addition to the isolation of Vietnam, the United States' refugee policy was also motivated by strategic interests in the ASEAN countries' political and economic stability. The ASEAN countries had the fastest growing economies among developing states and, by 1984, collectively ranked as the fifth largest trading partner of the United States.³⁴ This alliance proved to be particularly important during the 1973 oil crisis, when Indonesia chose not to

²⁹ Report of the Indochinese Refugee Panel, *supra* note 24 at 4; Sutter, *supra* note 27 at 53.

³⁰ Phuwadol Songprasert, *Thailand: A First Asylum Country for Indochinese Refugees* (Bangkok: Institute for Asian Studies, Chulalongkorn University, 1988) at 39-40. Vietnamese boat refugees arrived at the rate of roughly 1,000 per month in Thailand during 1977.

³¹ Report of the Indochinese Refugee Panel, *supra* note 24 at 3-4.

³² see David Kennedy, *The Dark Sides of Virtue: Reassessing International Humanitarianism* (Princeton: Princeton University Press, 2004) at 232 (notes that most foreign policy experts fall somewhere between the two extremes of realism and idealism, and that the default mode for the foreign policy establishment is realism). See also Kathleen Newland, "The Impact of U.S. Refugee Policies on U.S. Foreign Policy: A Case of the Tail Wagging the Dog?" in Michael S. Teitelbaum & Myron Weiner, eds., *Threatened Peoples, Threatened Borders: World Migration and U.S. Policy* (New York: The American Assembly, 1995) at 190, 192 (notes that even though the *Refugee Act of 1980* eliminated geographical and ideological grounds for granting refugee status, thereby changing the legal basis of refugee admission from political realism to humanitarianism, U.S. refugee admission changed very little in practice.).

³³ See e.g. Edwin Harwood, "American Public Opinion and U.S. Immigration Policy" (1986) 487 Annals Am. Acad. Pol. & Soc. Sci. 201 at 201, 204; Norman L. Zucker, "Refugee Resettlement in the United States: Policy and Problems" (1983) 467 Annals Am. Acad. Pol. & Soc. Sci. 172 at 172, 175-76.

³⁴ Kishore Mahbubani, "The Kampuchean Problem: A Southeast Asian Perception" (1983/1984) 62 Foreign Affairs 407 at 421.

participate in the OPEC boycott and continued to deliver its contracts to America.³⁵

The United States also had a geo-strategic interest in ASEAN stability, due to the fact that the Philippines was hosting American military bases, which, in turn, covered significant sea straits.³⁶ In ASEAN and Hong Kong, the refugee flow was perceived as both economically and developmentally adverse. Refugees were potential recruits for local Communist insurgency groups and therefore a threat to domestic stability. Thailand, where the largest number of refugees sought asylum, was most concerned with spies who arrived under the guise of refugees but with the real purpose of infiltration, and a screening process was eventually set up to filter out such saboteurs.³⁷ The arrival of ethnically Chinese refugees from Vietnam fed existing racial tensions in Malaysia and Indonesia. Hong Kong and Singapore had high-density populations on limited physical space, which confined their ability to dispense housing, employment, and other services to refugees.³⁸

It was in the United States' strategic interest to secure the goodwill of these countries by taking leadership in permanent resettlement efforts, especially since it was viewed as partially responsible for the refugee problem to begin with. The Indochinese migration began, after all, following the collapse of pro-American governments in Vietnam, Laos, and Cambodia—it was the result of a failed American military intervention.³⁹

One important lesson from the Indochinese refugee episode was that a multilateral solution to a humanitarian crisis could be implemented without requiring all parties involved to share the same assumptions underlying their actions. The ASEAN countries provided first asylum primarily out of political rather than humanitarian concerns and did not deem it important that the refugees should have a non-Communist alternative.⁴⁰ The United States, in contrast, was driven by humanitarian concerns, "voting with your feet" foreign policy, and strategic interests in the ASEAN countries' political and economic stability. It also felt a certain sense of responsibility because the first waves of refugees out of Indochina were affiliated with the American-supported *anciens régimes* in Vietnam, Laos and Cambodia, and consequentially ASEAN countries saw the Indochinese refugee problem as ultimately an American problem.

The United States was the wealthiest non-Communist country with resources for permanent refugee resettlement, whereas ASEAN was made up of developing countries with limited means.⁴¹ Like China's view on North

³⁵ Sutter, *supra* note 27 at 97.

³⁶ *Ibid.*

³⁷ Songprasert, *supra* note 30 at 35, 38-39.

³⁸ *Ibid.* at 99.

³⁹ Jeremy Hein, *States and Migrants: The Incorporation of Indochinese Refugees in the United States and France* (Boulder, CO: Westview Press, 1993) at 19.

⁴⁰ See Astrid Suhrke, *Indochinese Refugees: The Impact on First Asylum Countries and Implications For American Policy: a study prepared for the use of the Joint Economic Committee, Congress of the United States* (Washington, D.C.: United States Government Printing Office, 1981) at 3 [Suhrke, *Impact*].

⁴¹ *Ibid.*

Korean refugees, Thailand saw the displaced Indochinese who had fled to its borders as illegal and economic migrants rather than refugees.⁴² Thus, despite its concern over reducing the number of asylum seekers on its soil, Thailand was reluctantly willing to adopt a liberal refugee policy. This can be explained because of America's emphasis on the availability of first asylum, which was sufficiently persuasive to Thailand given the increasing importance of good US-Thai relations particularly with respect to security issues. Other factors that help explain the Thai policy are the influx of relief assistance from the international community,⁴³ the fact that a refusal to offer first asylum would violate international humanitarian principles,⁴⁴ and the international condemnation that could be expected to result from such a breach.

2. Past US-China Leadership in Multilateral Collaborations Regarding North Korea

The United States is now in a position to engage China's leadership in a multilateral resettlement solution to the present North Korean refugee problem. The United States and South Korea both have the capabilities to receive North Korean refugees for permanent resettlement, but China is the most significant first asylum country.⁴⁵ Indeed, Chinese consent to providing first asylum and UNHCR access to North Korean asylum seekers living near its border are essential to a multilateral solution.

The first instance of successful US-China collaboration regarding North Korea was in the application of pressure to prevent North Korean nuclear proliferation.⁴⁶ China's mediation through its facilitation of trilateral talks was not only crucial in opening a dialogue of negotiations between North Korea and the United States but also set the multilateral framework for the six-party talks that came later.⁴⁷

Like the Indochinese refugee crisis, the US-China partnership on the North Korean nuclear issue demonstrates an important lesson: multilateral cooperation requires a sufficient overlap, but not a complete convergence, of

⁴² See Sutter, *supra* note 27 at 101; Suhrke, *ibid.* at 7, fn. 4.

⁴³ The UN conference in July 1979 on the plight of Indochinese refugees was held specifically in response to pleas of assistance from ASEAN countries. The economic costs of maintaining refugee camps were borne by foreign sources and the UNHCR.

⁴⁴ Suhrke, *Impact*, *supra* note 40 at 8-9.

⁴⁵ Paul Wolfowitz, "How to Help North Korea's Refugees" *The Wall Street Journal* (16 June 2009) A15.

⁴⁶ Bonnie S. Glaser & Wan Liang, "North Korea: The Beginning of a China-U.S. Partnership?" (2008) 31 Wash. Q. 165 at 165.

⁴⁷ See *ibid.* at 169-70. For a description of China's leadership in mediation since North Korea first disclosed its highly enriched uranium program in October 2002, see Cheng Qian & Xiaohui Wu, "The Art of China's Mediation during the Nuclear Crisis on the Korean Peninsula" (2009) 36 Asian Aff.: Am. Rev. 79 at 82. The fourth round of six-party talks in September 2005 produced a joint statement in which North Korea agreed to give up its nuclear programs. In return, the United States confirmed that it had no interest in attacking North Korea; China, Japan, Russia, South Korea, and the United States also agreed to provide energy assistance to Pyongyang. Even though its terms were vague enough to give rise to later disagreements, the joint statement was still the first of its kind to be accomplished at a six-party talk.

motives among participating states. Former Secretary of State Colin Powell had similar sentiments:

American and Chinese interests on the Korean Peninsula may not overlap completely, but they do so considerably. Neither side wishes to see nuclear weapons developed and deployed there. Neither side enjoys the spectacle of the dilapidated North Korean economy. *Neither side wants the refugee crisis on China's border to worsen* nor relishes a North Korean regime that smuggles drugs and weapons, counterfeits currencies, and engages in the periodic extortion of its neighbors through brinkmanship. And neither side, to be sure, has any interest in another Korean war.⁴⁸

The United States and China both considered the nuclear disarmament of Pyongyang a priority but differed in their preferred methods of deterrence. The American strategy of deterrence focused on hard-line economic sanctions such as cutting off Pyongyang's energy supply from foreign sources. The US policy was shaped by the threat that North Korea's nuclear development would pose to its allies in the region, the security risk of nuclear material ending up in the hands of terrorist groups, and the Bush administration's overall aversion to the North Korean regime.⁴⁹

China, on the other hand, was strongly opposed to economic sanctions. It considered its regular supply of oil and food to North Korea to be a small premium to pay for ensuring stability on its northeastern border. This is consistent with Chinese diplomacy more generally, which has historically focused on noninterference, avoidance of direct conflict, and neutrality as long as it does not sacrifice the Chinese national interest.⁵⁰ However, China took on the uncharacteristic role of mediator on the North Korean nuclear issue for several reasons. First, North Korea's nuclear program was a direct security threat to China and other countries in the region. Nonproliferation was viewed as the ideal state for economic development; and China had additional motivation to intervene in order to stymie the escalating US-North Korea tension, which could accelerate the collapse of the North Korean regime and trigger an unwanted mass influx of refugees. Second, in addition to security concerns, mediation also provided an opportunity for China to improve its relationship with the United States, and China was a valuable partner in this regard because of the political and economic leverage that it had over Pyongyang. Lastly, China has a history of friendly relations with North Korea that goes back to the Korean War and therefore is well positioned to serve as a neutral third-party broker between the United States

⁴⁸ Colin L. Powell, "A Strategy of Partnerships" (January / February 2004) 83 Foreign Affairs 22 at 32 (emphasis added).

⁴⁹ Glaser & Liang, *supra* note 46 at 173.

⁵⁰ See Qian & Wu, *supra* note 47 at 81. The Five Principles of Peaceful Coexistence, a set of international relations guidelines initiated by China, India, and Myanmar in 1954 and widely recognized as norms in the region since then, stresses the importance of mutual non-interference and peaceful coexistence in international affairs. See "Backgrounder: Five Principles of Peaceful Coexistence" (14 June 2004), online: China View, <http://news.xinhuanet.com/english/2005-04/08/content_2803638.htm>.

and North Korea—two ideologically divergent countries with a legacy for hostility and mistrust that has lasted for decades.⁵¹

III. China's Leadership Role in the North Korean Refugee Problem: International Obligations, Current Policy, and Negotiating Power

China shares a 1,300 km border with North Korea and has perhaps the most significant interest in the North Korean crisis. Moreover, Northeast China is the first stop for most North Korean defectors, who either remain in China or go on to Southeast Asia before obtaining transportation and travel documents to South Korea. Others are smuggled from China on boats to the area surrounding South Korea or depart directly from Chinese cities with forged passports and plane tickets.⁵²

Despite its indispensable role in any multilateral solution to the North Korean refugee problem, China does not recognize refugee status for any North Korean defectors and categorizes them as economic migrants instead.⁵³ The Chinese government regularly repatriates them back to North Korea, where the punishment awaiting them can vary anywhere from a few months of “labor correction” to execution.⁵⁴ It follows that Beijing’s cooperation is crucial if the United States wants to implement the *NKHRA* in ways that would make a meaningful contribution to the resolution of the North Korean refugee crisis.

1. International Obligations Towards Refugees

China is a state party to both the 1951 *Refugee Convention*⁵⁵ and the 1967 *Protocol*⁵⁶—the two key guidelines for refugee protection in the international arena today. Article 1(A)(2) of the 1951 *Refugee Convention* in combination with Art. I(2) of the 1967 *Protocol* define “refugee” as someone who:

[in] fear of being persecuted for reasons of race, religion, nationality, membership of a particular social group or political opinion, is outside the country of his nationality and is unable or, owing to such fear, is unwilling to avail himself of the protection of that country; or who, not having a nationality and being outside the country of his former habitual residence ... is unable or, owing to such fear, is unwilling to return to it.⁵⁷

Often referred to as the bedrock principle of international refugee law, *nonrefoulement* is codified in Art. 33 of the 1951 *Refugee Convention*, which

⁵¹ Qian & Wu, *supra* note 47 at 81-82.

⁵² Stephan Haggard & Marcus Noland, eds., *The North Korea Refugee Crisis: Human Rights and International Response* (Washington, DC: US Committee on Human Rights in North Korea, 2006) at 61.

⁵³ See *infra* notes 58-59 and accompanying text for discussion of the UNHCR’s distinction between “economic migrants” and “refugees”.

⁵⁴ Haggard & Noland, *supra* note 52, “Summary”.

⁵⁵ *Supra* note 4.

⁵⁶ *Ibid.*

⁵⁷ 1951 *Refugee Convention*, *supra* note 4, Art. 1(A)(2). The original time limit of “before 1 January 1951” in the 1951 *Refugee Convention*’s definition of refugees was eliminated later by the 1967 *Protocol*, *supra* note 4, Art. I(2).

obligates member parties not to “expel or return (‘refouler’) a refugee . . . [to territories] . . . where his life or freedom would be threatened on account of his race, religion, nationality, membership of a particular social group or political opinion.”

Guidelines released by the UNHCR distinguish between “economic migrants” and “refugees”: one who “voluntarily leaves his country . . . exclusively . . . [for] economic consideration . . . is an economic migrant and not a refugee.”⁵⁸ However, economic migrants who were not refugees at the time of departure from their own countries are still eligible to claim *sur place* refugee status if their subsequent actions or events arising in their home countries during their absences “justify a well-founded fear of persecution.”⁵⁹

China’s current policy systematically views North Korean defectors as illegal economic migrants rather than refugees. This practice is at odds with China’s obligations under Art. 33 of the 1951 *Refugee Convention*, which, according to the UNHCR guidelines, would normally require refugee status to be assessed on an “individual basis” before a potential refugee is returned to his/her home country.⁶⁰ Admittedly, there is no explicit requirement for individual assessment of refugee status in the text of the 1951 *Refugee Convention* or of the 1967 *Protocol*. Neither instrument requires specific procedures to be adopted for the determination of refugee status; each State is left with the discretion to establish its own procedures.⁶¹ China’s failure to conduct individual assessments of refugee status for North Koreans, therefore, is a violation of non-binding “soft law” norms as established by the UNHCR guidelines, but not an outright violation of binding international law.⁶²

China’s conduct does, however, violate Art. 35 of the 1951 *Refugee Convention* and Art. II of the 1967 *Protocol*, which require member states to cooperate with the UNHCR. In a 1995 bilateral agreement,⁶³ China further pledged its commitment to UNHCR’s purpose of “providing international

⁵⁸ *Handbook on Procedures and Criteria for Determining Refugee Status under the 1951 Convention and the 1967 Protocol relating to the Status of Refugees*, U.N. Doc. HCR/IP/4/Eng/REV.1 (January 1992) at para. 62 [UNHCR Handbook] (emphasis added).

⁵⁹ *Ibid.* at paras. 94-96. Particularly relevant to this article’s focus on the Indochinese refugee crisis, groups of Vietnamese asylum seekers also faced forcible repatriation after Hong Kong had determined that they were economic migrants: Josh Briggs, “*Sur Place* Refugee Status in the Context of Vietnamese Asylum Seekers in Hong Kong”, Comment, (1993) 42 Am. U.L. Rev. 433 (“Screening officials in Hong Kong apply an excessively narrow definition of ‘refugee’ in the case of individuals and subgroups of Vietnamese asylum seekers because they fail to consider *sur place* refugee claims adequately. The result is an unwarranted denial of refugee status to many of the Vietnamese asylum seekers screened out as economic migrants.”).

⁶⁰ See *UNHCR Handbook*, *supra* note 58 at para. 44.

⁶¹ *Ibid.* at para. 189.

⁶² See Michael Alexander, “Refugee Status determination conducted by UNHCR” (1999) J. Int’l Refugee L. 251 at 284 (argues that individual refugee status determination is expensive and that it is the UNHCR’s role to persuade governments to allocate to it the necessary resources, thereby implying that individual refugee status determination is not binding international law.)

⁶³ *Agreement on the Upgrading of the UNHCR Mission in the People’s Republic of China to UNHCR Branch Office in the People’s Republic of China*, United Nations High Commissioner for Refugees and China, 1 December 1995, 1899 U.N.T.S. 61, online: <http://untreaty.un.org/unts/120001_144071/6/9/00004988.pdf>.

protection and humanitarian assistance to refugees”⁶⁴ by upgrading the UNHCR Mission in China to a local branch office.⁶⁵ The agreement obligates China to allow UNHCR personnel “unimpeded access to refugees and to the sites of UNHCR projects” in consultation and cooperation with the Chinese government.⁶⁶ Contrary to these obligations, China currently does not allow the UNHCR meaningful access to determine the refugee status of North Koreans living in China.⁶⁷

Generally, sovereign states that are parties to the 1951 *Refugee Convention* are given discretion in establishing processes for the evaluation of refugee claims within their own legal systems.⁶⁸ The UNHCR offers guidance on refugee status determination procedures but only plays a non-binding supervisory role in this regard.⁶⁹ China currently does not have a national refugee system or legislation specifically designed for the fulfillment of its obligations under the 1951 *Refugee Convention*. However, the 1986 *Law of the People's Republic of China on Entry and Exit of Aliens* does permit political asylum seekers to reside in China upon approval by the Chinese government.⁷⁰

China is certainly capable of tolerance in its treatment of refugees. Indeed, it allows the UNHCR to take the lead role in refugee status determinations with respect to all asylum seekers other than those originating from North Korea. The Chinese government allows non-North Korean asylum seekers to approach the UNHCR offices in China, seek refugee status there, and remain on Chinese soil while they wait for third-country resettlement.⁷¹ Upon the arrival of Vietnamese persons of Chinese ethnicity who fled Vietnam during the 1979 China-Vietnam Border War, roughly 260,000 Vietnamese refugees were given asylum in China, and that community has now grown to over 300,000. Although they do not possess formal citizenship, many are integrated into Chinese society and entitled to

⁶⁴ *Ibid.*, Art. IV(1).

⁶⁵ *Ibid.*

⁶⁶ *Ibid.*, Art. III(5).

⁶⁷ *The North Korean Human Rights Act of 2004: Issues and Implications: Joint Hearing Before the Subcommittee on Asia and the Pacific and the Subcommittee on Africa, Global Human Rights and International Operations of the Committee on International Relations* *Tribal Energy Self-Sufficiency Act and the Native American Energy and Self-Determination Act*, 109th Cong. (2005) at 13-14 (Arthur E. “Gene” Dewey, Assistant Secretary, Bureau of Population, Refugees, and Migration, U.S. Department of State) [2005 NKHRA Joint Hearing] (pointing out that the UNHCR’s Beijing office is hard to find, and that the UNHCR does not have access to North Koreans living at the China-North Korea border).

⁶⁸ *UNHCR Handbook*, *supra* note 58 at para 189.

⁶⁹ The *UNHCR Handbook* offers guidance on status determination procedures that is an authoritative interpretation of 1951 Refugee Convention obligations but not binding on member states: Haggard & Noland, *supra* note 52 at 37. See Deborah E. Anker, “Refugee Law, Gender, and the Human Rights Paradigm” (2002) 15 Harv. Hum. Rts J. 133 at 137 (pointing out “examples of inconsistencies and incomplete implementations” among States Parties of the 1951 *Refugee Convention*, and that the UNHCR provides non-binding norms on the legalized and non-legalized assessments of refugee claims).

⁷⁰ [22 November 1985] Standing Committee of the Sixth National People’s Congress, Thirteenth Session (entered into effect 1 February 1986), Art. 15, online: <<http://www.chinatoday.com/law/IMMLAW.HTM>>.

⁷¹ Haggard & Noland, *supra* note 52 at 37.

many rights given to Chinese citizens.⁷² Of course, the fact that these Vietnamese refugees are ethnically Chinese is significant, and China might conceivably be less willing to extend the same generosity to non-ethnic Chinese refugees.

China's treatment of North Korean refugees is a stark departure from its general willingness to cooperate with the UNHCR, given that UNHCR reports from northeastern China in the late 1990s characterized some of the newly arrived North Koreans as refugees.⁷³ According to the Congressional Report Service, China has insisted that North Koreans who have crossed the border into China are illegal economic migrants in search of food rather than political refugees.⁷⁴ Suspicious of UNHCR's intentions, China has denied aid agencies access to the border region despite UNHCR's offer of assistance and South Korea's willingness to resettle North Korean refugees.⁷⁵ The legal basis for this policy lies in a 1986 bilateral border protocol that China signed with North Korea, the full official text has never been made public.⁷⁶ The 1986 protocol obligates China to prevent "the illegal border crossing of (North Korean) residents" and "cooperate on the issue of handling criminals."⁷⁷ China's forcible repatriation of North Koreans under the 1986 border security protocol is in direct conflict with China's obligations toward refugees under the 1951 *Refugee Convention* and 1967 *Protocol*.⁷⁸

⁷² U.S., Congressional-Executive Commission on China, *The Rising Stakes of Refugee Issues in China: Roundtable Before the Congressional-Executive Commission on China*, 111th Cong. (Washington, D.C.: United States Government Printing Office, 2009) at 3 (Joel Charny). See also UN, "2005 UNHCR Statistical Yearbook Country Data Sheet - China" in *Statistical Yearbook 2005: Trends in Displacement, Protection and Solutions* (Geneva: United Nations High Commissioner for Refugees, 2007) at 291. The UNHCR has remained involved with the assistance of Vietnamese refugees in China long after 1979. A draft handover agreement between UNHCR and China was finalized in 2007. Under the agreement, \$7 million was handed to China's Ministry of Civil Affairs in order to implement micro-credit schemes for the benefit of Indo-Chinese refugees in China: UNHCR, "East Asia and the Pacific: Operation Highlights" (2007) at 372.

⁷³ 2007 CRS Report, *supra* note 2 at 11.

⁷⁴ *Ibid.* at 10-11.

⁷⁵ *Ibid.* at 11.

⁷⁶ Michael Dillon, *Contemporary China – An Introduction* (New York: Routledge, 2009) at 227.

⁷⁷ *Mutual Cooperation Protocol for the Work of Maintaining National Security and Social Order in the Border Areas*, 12 August 1986 (Democratic People's Republic of Korea, Ministry of State Security, and People's Republic of China, Ministry of Public Security) [1986 China-North Korea Border Protocol]. The document was obtained in December 2002 by the Rescue the North Korean People Urgent Action Network (RENK), and the unauthenticated English translation is available online: <http://www.nkfreedom.org/UploadedDocuments/NK-China-bilateral_treaty.pdf>. See also James D. Seymour, "China: Background Paper on the Situation of North Koreans in China" (WRITENET: 1 January 2005), online: <<http://www.unhcr.org/refworld/docid/4231d11d4.html>>.

⁷⁸ Seymour, *ibid.* at 5. This analysis assumes that the text of the 1986 China-North Korea Border Protocol is accurately reflected in the only English translation available, which is unauthenticated.

2. National Interests That Shape China's Current Policy of Denying Refugee Status to North Koreans

China is keenly aware of the consequences to its international relations and to its security, particularly on the Korean peninsula, that could follow from the acceptance of North Korean refugees. It is well known that Hungary's willingness to allow the entry of East German asylum seekers contributed to East Germany's collapse in the late 1980s.⁷⁹ This lesson is not lost upon China: granting refugee status to North Korean defectors would encourage more North Koreans to flee, which in turn could destabilize the North Korean regime.⁸⁰

China's interests in avoiding such a collapse stem from both economic and domestic security concerns. John S. Park suggests that the fall of North Korea would interfere with South Korean foreign direct investment in China, since part of the investment would likely be redirected toward the reconstruction of North Korea.⁸¹ China also has a domestic security interest in maintaining good relations with its neighbour on the northeast border—a neighbour that serves as a buffer between China and the American troops stationed in South Korea.⁸² The Chinese tradition of providing political and economic aid to North Korea dates back to the Korean War in 1953, and China's customary attitude toward North Korea is one that prefers carrots over sticks. However, when China does feel the need to resort to punishment, such punishment tends to be minimal. For example, when UN Security Council Resolution 1718⁸³ imposed economic sanctions on North Korea following the October 2006 nuclear testing in Pyongyang, Beijing only signed onto the Resolution after economic sanctions on non-luxury goods were removed through revisions.⁸⁴

Recognizing North Koreans as refugees also entails additional obligations for China. For example, China would have to come to terms with both the "loss of sovereignty" in allowing an international aid organization to set up and administer refugee camps on Chinese soil, and with the financial costs in complying with international standards for refugee treatment. Currently the North Koreans in China do not have legal status

⁷⁹ See Andrei Lankov, "North Korean Refugees in Northeast China" (2004) 44 *Asian Survey* 855 at 868.

⁸⁰ See *ibid.*; David Shambaugh, "China and the Korean Peninsula: Playing for the Long Term" (Spring 2003) 26:2 *Wash. Q.* 43.

⁸¹ John S. Park, "Inside Multilateralism: The Six-Party Talks" 28:4 *Wash. Q.* 75.

⁸² See Lankov, *supra* note 79 at 873. But see Anne Wu, "What China Whispers to North Korea" (Spring 2005) 28:2 *Wash. Q.* 35 (pointing out that in the context of recent improvements in U.S.-China relations, "the traditional 'lips and teeth' relationship between China and the DPRK, in which Beijing envisioned using North Korea as a buffer against the United States, appears both obsolete and self-destructive"). For a discussion of the US-South Korea alliance and the Mutual Defense Treaty since 1953, see Bruce E. Bechtol, "The ROK-US Alliance During the Bush and Roh Administrations: Differing Perspectives and their Implications for a Changing Strategic Environment" (2005) 9 *Int'l J. Korean Stud.* 87 at 88-89.

⁸³ SC Res. 1718, U.N. Doc. S/RES/1718 (14 October 2006), online: <http://www.un.org/Docs/sc/unsc_resolutions06.htm>.

⁸⁴ Jayshree Bajoria, "Backgrounder: The China-North Korea Relationship" (Council on Foreign Relations, updated 7 October 2010), online: <<http://www.cfr.org/publication/11097/>>.

and are not entitled to any assistance from the Chinese government. If anything, the cheap labor they provide is a boost to the Chinese economy.⁸⁵ However, if recognized as refugees, the standard of living for North Koreans—as a result of UNHCR aid and other venues of international intervention—could conceivably be superior to what local citizens in Northeast China are accustomed to, and therefore a source of domestic tension.⁸⁶

3. China's Negotiating Power over North Korea

It should be qualified that China's "big brother" patronage of North Korea is not unconditional. Chinese foreign policy has changed considerably since the Korean War more than 50 years ago, and is no longer ideologically dedicated to supporting socialist states and "exporting revolution."⁸⁷ For example, in August 2003, Chinese President Hu Jintao called for North Korea to make progress toward economic self-sufficiency, reform, and improvement of relations with neighbouring countries by putting an end to its nuclear program.⁸⁸ It is becoming increasingly apparent that, due to international interest over the nuclear issue, Beijing's ability and willingness in continuing aid to North Korea is contingent on Pyongyang's progress on nuclear disarmament. President Hu has indicated that even though Beijing values its historical alliance with Pyongyang, it is perfectly willing to collaborate with the international community on issues important to China's national interests such as the denuclearization of the Korean peninsula. This pressure was allegedly a major factor in North Korea's decision to return to six-party talks in 2003.⁸⁹

As North Korea's primary ally and trading partner, China is in a unique position to exert negotiating power over Pyongyang. North Korea is highly dependent on foreign aid, which has essentially replaced the commercial importation of food.⁹⁰ The collapse of the Soviet Union resulted in the dissolution of economic benefits for North Korea, and, as a result, the effects of food shortages in North Korea became increasingly severe. Floods in 1995 catalyzed a nationwide famine that, based on some estimates, killed between five to ten percent of the population. This compelled North Korea to seek international food assistance despite its national ideology of self-reliance.⁹¹

⁸⁵ Lankov, *supra* note 79 at 868.

⁸⁶ Park, *supra* note 81 at 83. For an analogy of this problem during the Indochinese refugee crisis, see disparities in standards of living between Indo-Chinese refugees, who lived under UNHCR's auspice in poor rural areas near Thailand's border, and the local villagers: Sutter, *supra* note 27 at 124.

⁸⁷ See Wu, *supra* note 82 at 41-42.

⁸⁸ Willy Wo-Lap Lam, "Time to act, China tells N Korea" *CNN International* (25 August 2003) online: <<http://edition.cnn.com/2003/WORLD/asiapcf/east/08/24/willy.column>>. See also David Kerr, "The Sino-Russian Partnership and U.S. Policy Toward North Korea: From Hegemony to Concert in Northeast Asia" (2005) 49 *Int'l Stud. Q.* 411 at 426 (citing examples of assertive Chinese diplomacy on the nuclear disarmament issue, such as reportedly disrupting the North Korean oil supply and convening several multilateral negotiations).

⁸⁹ See Lam, *ibid.*

⁹⁰ 2005 NKHRA Joint Hearing, *supra* note 67 at 46.

⁹¹ 2007 CRS Report, *supra* note 2 at 6.

The World Food Programme (WFP) set up operations in North Korea soon after and the United States had been the largest donor in this effort until 2005.⁹²

In August 2005, the North Korean government announced that it would no longer accept humanitarian assistance from the WFP. Later in the same year, it rejected aid from the European Union (EU) after the EU proposed a United Nations resolution on the human rights situation in North Korea. The WFP significantly reduced its operations in North Korea as a result, and no food or energy aid has gone to Pyongyang from the United States since 2006.⁹³

As a result of this progressive isolationism, North Korea has become increasingly reliant on aid from China and South Korea. Those two countries continue to bypass the WFP, sending bilateral aid directly to Pyongyang out of fear that North Korea's collapse would trigger a mass influx of unwanted refugees into their territories.⁹⁴ North Korea's economic survival is becoming increasingly dependent on China, which, according to estimates, has since the early 1990s provided almost 90 percent of energy imports, 80 percent of consumer goods, and 45 percent of food.⁹⁵ Analysts and aid workers within and external to the WFP agree that bilateral aid from China and South Korea weakens the WFP's efforts to promote better internal access, monitoring, and transparency in North Korea.⁹⁶ South Korea gives concessional food assistance with little monitoring of the distribution and no effort to target the most vulnerable groups.⁹⁷ China, which has likely provided even more food than the United States has, does not appear to predicate its aid on any conditions, and certainly not on either policy reform or monitoring within North Korea.⁹⁸

⁹² *Ibid.* See also Mark E. Manyin, Specialist in Asian Affairs, Foreign Affairs, Defense, and Trade Division, "CRS Report for Congress: U.S. Assistance to North Korea: Fact Sheet 1" (updated 3 January 2007), online: <<http://www.nationalaglawcenter.org/assets/crs/RS21834.pdf>> [2007 CRS Fact Sheet] (U.S. aid to North Korea has totalled over \$1.1 billion since 1995—roughly 60% in the form of food aid and 40% in energy assistance processed through the Korean Peninsula Energy Development Organization).

⁹³ 2007 CRS Fact Sheet, *ibid.* at 1-3.

⁹⁴ James T. Laney & Jason T. Shaplen, "How to Deal with North Korea" (March/April 2003) Foreign Affairs 16 at 27.

⁹⁵ Bajoria, *supra* note 84. But see Wu, *supra* note 82 at 35, 42.

⁹⁶ Mark E. Manyin, Specialist in Asian Affairs, Foreign Affairs, Defense, and Trade Division, "CRS Report for Congress: Foreign Assistance to North Korea" (26 May 2005) at 10.

⁹⁷ 2007 CRS Fact Sheet, *supra* note 92 at CRS-4 (In 2005, South Korea conducted 20 monitoring trips to food distribution centers in North Korea. The WFP, in contrast, had a much more intrusive presence in North Korea. Before it reduced its operations in North Korea, the WFP conducted thousands of monitoring trips every year with over 40 expatriate staff and six offices in the country).

⁹⁸ *Ibid.*; Stephan Haggard & Marcus Noland, "Hunger and Human Rights: The Politics of Famine in North Korea" (US Committee for Human Rights in North Korea, January 2006) at 31-32, online: <http://works.bepress.com/marcus_noland/5> (noting that China provides concessional sales or grants of food to North Korea outside of the World Food Program, and that there is no evidence that China has conditioned its aid "on overall policy reform or more particular principles of programmatic design, implementation, or monitoring").

4. China-South Korea Partnership

China's strong relationship with South Korea—the country that has resettled the largest number of North Korean refugees⁹⁹—adds to China's influence in coordinating any international resettlement solution. In 2002, China replaced the United States as South Korea's biggest trading partner, and two-way trade between the two countries had increased by roughly 20 percent over the preceding year, approaching US\$100 billion.¹⁰⁰ As of 2003, South Korea was China's third largest trading partner and fifth largest foreign investor. Its expected investment in China that year was estimated at US\$1 billion—half of South Korea's total overseas investment.¹⁰¹ South Korea also has an active economic development presence in northeast China, the “rust belt” region that has the largest concentration of ethnic Koreans and is most vulnerable to the impact of a refugee influx from North Korea.¹⁰²

In addition to economic considerations, China has a strategic interest in maintaining close ties with South Korea: there is a delicate and continually contested balance between Chinese and American influences over South Korea. If South Korea, the United States, and other countries set up a reassuring multilateral resettlement solution for North Korean refugees and jointly persuade China to provide first asylum, China would be unlikely to flatly refuse solely for the sake of appeasing Pyongyang. Its relations with Seoul are too important. As evidenced by its position on the North Korean nuclear disarmament issue, China is willing to support certain initiatives against North Korea to further its own national interests.¹⁰³

IV. Policy Proposals for A Multilateral Solution

The remainder of the article will analyze the shortcomings of the NKHRA, highlight the Eurocentric nature and imperfections of current international refugee law, and address the burdens that China would take on by providing temporary first asylum. American diplomacy that is sensitive to these three issues can make a significant contribution to the resolution of the North Korean refugee crisis. Rather than criticizing China's international

⁹⁹ Emma Chanlett-Avery, “Congress and U.S. Policy on North Korean Human Rights and Refugees: Recent Legislation and Implementation” (CRS Report for Congress, 30 January 2009) at 5, online: <<http://opencrs.com/document/RS22973/>> [2009 CRS Report]. South Korea's Unification Ministry record shows that in November 2010, there are approximately 20,000 North Korean defectors living in South Korea: “Kim Is Free! Defector No. 20,000” *The Wall Street Journal* (15 November 2010), online: <<http://blogs.wsj.com/korearealtime/2010/11/15/ms-kim-is-free-defector-20000/>>.

¹⁰⁰ James Brooke, “China ‘Looming Large’ in South Korea As Biggest Player, Replacing the U.S.” *The New York Times* (3 January 2003), online: <<http://www.nytimes.com/2003/01/03/world/threats-responses-northeast-asia-china-loomng-large-south-korea-biggest-player.html>>.

¹⁰¹ *Ibid.*

¹⁰² David Shambaugh, “China and the Korean Peninsula: Playing for the Long Term?” (2003) 26:2 Wash. Q. 43 at 49. As of 2003, northeastern China had “an annual per capita income of \$1,154, about one-half that of the greater Beijing area and one-third that of Shanghai”: Brooke, *ibid.*

¹⁰³ See *supra* notes 49–51 and accompanying text for a more detailed account of China's leadership in facilitating multilateral negotiations over the nuclear non-proliferation issue.

treaty violations outright, the United States might make more progress by seeking solutions within the Chinese legal system, and by pledging aid to the unique burdens that China would take on as a provider of first-asylum.

The repeated attention paid to North Korea's human rights record and China's violations of its international obligations toward North Korean refugees brings unwanted spotlight to the refugee issue and only puts China in a more defensive position. Despite the 1986 China-North Korea Border Protocol, Chinese officials have been willing to look the other way as long as refugee inflows and activities of foreign NGOs are carried out quietly.¹⁰⁴ The exception is with respect to North Koreans who, in trying to enter foreign diplomatic compounds, have made their way into the international spotlight as well. But even for such high-profile cases, China still tends to relent to external pressure eventually and allow the refugees subsequent passage to other countries.¹⁰⁵

Reputational concerns may have led China to relent on its policy toward North Korean refugees in these cases,¹⁰⁶ but the high-profile embassy-stormings are outright embarrassments to the Chinese government, and have led to more heavily guarded embassy gates by Chinese security. North Koreans seeking passage to South Korea have attempted entry into the embassies and consulates of many countries, including Spain, United States, Canada, Japan, Germany, and South Korea.¹⁰⁷ The NGOs facilitating these undertakings made sure to alert foreign reporters beforehand in order to maximize the international community's attention and exert pressure on the Chinese government.¹⁰⁸ Chinese Foreign Ministry spokesman Kong Quang's statement regarding these efforts was not without a sense of irony: "I'm really surprised some of the correspondents knew the timing of the cases about a half-hour" before they occurred.¹⁰⁹ In December 2002, the Chinese government, not at all happy with the practice and wanting its end, renewed efforts of forced repatriation of North Koreans in collaboration with North Korean security forces.¹¹⁰

1. *Shortcomings of the 2004 North Korean Human Rights Act*

The United States government is now in a position to start a new chapter in US-China relations by recognizing the *NKHRA*'s shortcomings and taking a conciliatory approach on the North Korean refugee problem. An awareness

¹⁰⁴ 2007 CRS Report, *supra* note 2 at 11.

¹⁰⁵ In an embarrassing 2002 episode, an asylum seeker was dragged away from the South Korean Consulate after a scuffle between the Chinese police and South Korean diplomats. China finally relented after weeks of diplomatic gridlock and allowed 26 North Korean asylum seekers to leave the country: Elisabeth Rosenthal, "North Korea Asylum Seekers Leave China" *The New York Times* (24 June 2002) A6.

¹⁰⁶ See *supra* notes 104-105 and accompanying text.

¹⁰⁷ Benjamin Neaderland, "Quandary on the Yalu: International Law, Politics, and China's North Korean Refugee Crisis" (2004) 40 Stan. J. Int'l L. 143 at 144.

¹⁰⁸ *Ibid.* at 169.

¹⁰⁹ Michael B. Lev, "Hectic day for imagemakers in Beijing" *Chicago Tribune* (4 September 2002).

¹¹⁰ See Doctors Without Borders, "Urgent Appeal for Protection of North Korean Refugees in China" (Press Release, 19 January 2003), online: <<http://doctorswithoutborders.org/press/release.cfm?id=374&cat=press-release>>.

of the *NKHRA*'s shortcomings will enable American foreign policy to better engage China's leadership in resettling North Korean refugees. The *NKHRA* was an American effort to coordinate a multilateral solution to the North Korean refugee situation and to take leadership in the permanent resettlement process. Under Title III of the *NKHRA*, North Koreans are allowed to apply for refugee status and asylum regardless of whether they have any claim to South Korean citizenship.¹¹¹ Furthermore, the *NKHRA* encourages North Korea's neighbours to adopt similar humanitarian measures, the international community more generally to grant safe haven to North Korea refugees, and China to uphold its international obligations toward refugees under the 1951 *Refugee Convention* as well as the 1967 *Protocol*.¹¹²

In passing the *NKHRA*, part of Congress' intention was that "the human rights of North Koreans should remain a key element in future negotiations between the United States, North Korea, and other concerned parties in Northeast Asia."¹¹³ However, China has not altered its treatment of North Korea refugees since the passage of the *NKHRA*, and only 81 North Korean defectors have been granted refugee status in the United States since May 2006.¹¹⁴ Critics of the *NKHRA* have voiced concerns that the legislation not only worsens the plight of the refugees, but also damages North Korea-South Korea relations and weakens the six-party talks' progress on North Korean nuclear disarmament.¹¹⁵

The *NKHRA* has made little progress in garnering China's collaboration for four reasons. The *NKHRA* appears to i) endorse and encourage the collapse of the North Korean regime, an event that the Chinese government is willing to go to great costs to avoid;¹¹⁶ ii) hinder six-party negotiations on North Korean nuclear nonproliferation; iii) impose economic sanctions on North Korea that are unlikely to effect real improvements of human rights within the country; and iv) lack sufficient mechanisms that enable the

¹¹¹ *NKHRA*, *supra* note 7, Title I, s. 302(a). The *NKHRA* provision regarding South Korea citizenship responds to a provision in the South Korean constitution that grants *de facto* citizenship to North Koreans. See Nicole Hallett, "Politicizing U.S. Refugee Policy toward North Korea" (Winter/Spring 2006) 1 Yale J. Int'l Affairs 72 at 76 ("Because North Korean refugees technically could claim citizenship in a safe third country, requests for asylum in the United States were categorically denied. Consequently, very few North Koreans were admitted into the United States prior to the passage of the *North Korean Human Rights Act of 2004*. The State Department notes that only five North Koreans were granted asylum in 2002, three in 2003, and one in 2004.").

¹¹² *NKHRA*, *ibid.*, ss. 304-308.

¹¹³ *Ibid.*, Title I, s. 101.

¹¹⁴ "No. of N.Korean Refugees in U.S. 'Reaches 81'" *Chosun Ilbo* (7 May 2009), online: <http://english.chosun.com/site/data/html_dir/2009/05/07/2009050700644.html>.

¹¹⁵ 2007 CRS Report, *supra* note 2 at 17. See Wu, *supra* note 82 at 35; Balbina Hwang, "Spotlight on the North Korean Human Rights Act: Correcting Misperceptions" (Heritage Foundation, February 2005) at 1, online: <<http://www.heritage.org/Research/Reports/2005/02/Spotlight-on-the-North-Korean-Human-Rights-Act-Correcting-Misperceptions>>.

¹¹⁶ One of the ways that the *NKHRA* is distinguished from its predecessor, the *North Korean Freedom Act* of 2003, is "the supposed de-linkage of refugee 'exodus' with regime change": Jaeho Hwang & Jasper Kim, "Defining the Limits of the North Korean Human Rights Act: A Security and Legal Perspective" (2006) 23 E. Asia 45 at 47.

executive branch to collaborate with South Korea. Support and implementation from the executive branch have been tenuous at best. The Bush administration's emphasis on North Korea's human right record decreased as nuclear negotiations evolved, and the Obama administration has so far not taken a stance on the issue.¹¹⁷

While sponsors of the legislation have stated that the *NKHRA* was a purely humanitarian gesture without political motives,¹¹⁸ it is naïve to believe that any post-War American immigration and refugee policy is implemented without foreign policy goals in mind.¹¹⁹ This point was also illustrated by the United States' response to the Indochinese crisis. However, starting in the 1990s, Congress has increasingly shown a trend of implementing human rights legislations targeting specific "rogue states" with the goal of catalyzing political change.¹²⁰ Stephen Linton, who has visited North Korea 60 times since 1979 and serves as Chairman of the Eugene Bell Foundation that provides medical care to North Koreans, has expressed concerns that a 2005 conference on North Korean human rights, funded by the *NKHRA*, "might hurt those it is trying to help by painting non-governmental groups seeking to work in North Korea as 'agents of regime change.'"¹²¹

The second shortcoming of the *NKHRA* is that it hinders the six-party negotiations over North Korea's nuclear program without making substantial human rights improvements. Tempting as it may be, linking human rights to the international community's efforts toward North Korean nonproliferation is not a realistic way to help North Korean refugees. Section 101 of the *NKHRA* states that "[i]t is the sense of Congress that the human rights of North Koreans should remain a key element in future negotiations between the United States, North Korea, and other concerned parties in Northeast Asia." This implies that humanitarian concerns should be linked to future multi-party negotiations on the nuclear disarmament issue. In practice, however, the *NKHRA* does not appear to have a significant impact on how much emphasis the executive branch chooses to place on human rights issues during nuclear disarmament negotiations.¹²² Perhaps using the *NKHRA* as a straw man, Pyongyang has cited the legislation as "evidence" of America's "hostile policy" of encouraging further defections from North Korean citizens and endorsing regime change in North Korea. In the past, Pyongyang has used this legislation as a justification for North Korea's

¹¹⁷ 2009 CRS Report, *supra* note 99 at 1.

¹¹⁸ 2005 *NKHRA Joint Hearing*, *supra* note 67 (as evidenced by the language of Rep. James Leach).

¹¹⁹ See Newland, *supra* note 32 at 190 ("Throughout the period of the Cold War, U.S. refugee policy [has served as]... a handmaiden of foreign policy. It was meant to contribute to the overarching objective of damaging and ultimately defeating Communist countries, particularly the Soviet Union.").

¹²⁰ Hallett, *supra* note 111 at 72, 76.

¹²¹ Barbara Slavin, "Rights conference may be pitfall for N. Korea talks" *USA Today* (15 July 2005), online: <http://findarticles.com/p/articles/mi_kmusa/is_200507/ai_n14777034/>. The conference opposed economic aid solely in exchange for the North Korean regime's nuclear disarmament without addressing its human rights abuses.

¹²² See *supra* note 117 and accompanying text.

withdrawal of participation in the six-party talks, which results in no net benefit for North Korean refugees.¹²³

The Bush administration's confrontational attitude toward North Korea was a departure from that of the Clinton administration, which always treated security issues with North Korea separately from human rights discussions. The 1994 *Agreed Framework between the United States and North Korea*, which gave Pyongyang economic incentives in exchange for freezing its nuclear program, made no mention of human rights concerns.¹²⁴ In contrast, the Bush administration repeatedly criticized Pyongyang's human rights record and supported UN resolutions in condemnation of it. During six-party talks, the United States has insisted on a hard-line multilateral approach similar to the treatment of Libya, whose nuclear dismantlement was demanded in return for economic benefits following the Libyan-sponsored bombing of a Pan Am flight in 1988.¹²⁵ Observers have noted a correlation between an increased focus on human rights issues and stalled progress in nuclear weapons negotiations.¹²⁶ The Obama administration has stated a willingness to participate in nuclear negotiations but has not taken a clear stance on the human rights issue.¹²⁷

Third, the economic sanctions that the *NKHRA* imposes on North Korea are unlikely to effect real improvements in the country's human rights policies. The *NKHRA* promises "significant increases above current levels of United States support for humanitarian assistance provided inside North Korea ... conditioned upon substantial improvements in transparency, monitoring, and access to vulnerable populations throughout North Korea." The *NKHRA* further states that American non-humanitarian assistance to North Korea is contingent on North Korea's "substantial progress toward ... basic human rights."¹²⁸ However, Steve Pape suggests that authoritarian governments subjected to economic sanctions tend to become more oppressive.¹²⁹ Economic sanctions are often not successful in effecting change in the target country's policies and likely to adversely impact the poorest segment of its population.¹³⁰ The correlation between economic deprivation and political willingness to change is weak, since factors other than the economic impact of sanctions, such as the military potential of the target country, play a primary role in determining political income.¹³¹ None

¹²³ Wu, *supra* note 82 at 35.

¹²⁴ See 2007 CRS Report, *supra* note 2 at 15; "U.S. 'North Korean Human Rights Act' Flailed" *Korean Central News Agency* (4 October 2004), online: <<http://www.kcna.co.jp/item/2004/200410/news10/05.htm>>.

¹²⁵ Park, *supra* note 81 at 79-80.

¹²⁶ See 2007 CRS Report, *supra* note 2 at 16.

¹²⁷ 2009 CRS Report, *supra* note 99 at 1. See "Obama urges North Korea to change" *BBC News* (19 November 2009), online: <<http://news.bbc.co.uk/2/hi/8367585.stm>>.

¹²⁸ *NKHRA*, *supra* note 7, ss. 202(b)(2)(A), 202(a)(2).

¹²⁹ See Steve A. Pape, "Why Economic Sanctions Do Not Work" (1997) 22:2 Int'l Sec. 90 at 91-93 (challenging the effectiveness of economic sanctions but acknowledging existing literature which takes the position that economic sanctions can achieve ambitious foreign policy goals).

¹³⁰ Semoon Chang, "The North Korean Human Rights Act of 2004" (2006) 2 N. Korean Rev. 80 at 87.

¹³¹ Gary Clyde Hufbauer, Jeffrey J. Schott & Kimberly Ann Elliott, *Economic Sanctions*

of the economic sanctions imposed for political reasons by the United States on countries such as Afghanistan, Cuba, and Iraq accomplished their intended purposes, and this will most likely be the outcome for any American sanctions against North Korea.¹³²

Lastly, the *NKHRA* is conspicuously silent with respect to collaboration with South Korea on the North Korean refugee issue. This is despite Congressional acknowledgement that the “principal responsibility for North Korean refugee resettlement naturally falls to the Government of South Korea.”¹³³ One of the challenges to effective *NKHRA* implementation is that the vetting process of North Korean asylum seekers is complex. The United States has no official relations with North Korea and little information of the applicants’ backgrounds, making close coordination with South Korea all the more essential to developing effective vetting mechanisms.¹³⁴

South Korea, a party to both the 1951 *Refugee Convention* and 1967 *Protocol*, is currently the primary destination for North Korea refugees. The number of North Korean defectors arriving in South Korea since the end of the Korean War in 1953 has totaled more than 14,000.¹³⁵ South Korea grants *de facto* citizenship¹³⁶ to North Koreans, and under a 1962 law administers a generous resettlement program for all North Koreans who defect to the South.¹³⁷ What began as a single-digit annual flow of North Korean defectors in the early 1990s ballooned in the late 1990s as a result of the North Korean famine.¹³⁸

Reconsidered: History and Current Policy, 2d ed. (Washington, D.C.: Institute for International Economics, 1990) at 94 (Of the 30 cases examined that involve high policy goals, only seven were successful as a result of implementing economic sanctions, and only three after discounting four cases that ended in world wars and civil wars.).

¹³² See Michael Whitty, Suk Kim & Trevor Crick, “The Effectiveness of Economic Sanctions: The Case of North Korea” (2006) 2 N. Korean Rev. 50.

¹³³ *NKHRA*, *supra* note 7, s. 3(24). Rep. Leach has also stated that “South Korean cooperation will be important to our own efforts to assist North Korean refugees”: 2005 *NKHRA Joint Hearing*, *supra* note 67 at 2.

¹³⁴ See Emma Chanlett-Avery, “Congress and U.S. Policy on North Korean Human Rights and Refugees: Recent Legislation and Implementation” (CRS Report for Congress, 22 October 2008) at 5-6, online: <<http://fpc.state.gov/documents/organization/112040.pdf>> [2008 CRS Report].

¹³⁵ See “Burma frees North Korean refugees” *BBC News* (1 January 2009), online: <<http://news.bbc.co.uk/2/hi/7806925.stm>>; 2008 CRS Report, *ibid.* at 6.

¹³⁶ *Constitution of the Republic of Korea* (1987), Art. 3. online: <www.asianlii.org/kr/legis/const/1987/1.html> (“The territory of the Republic of Korea shall consist of the Korean peninsula and its adjacent islands.”).

¹³⁷ Prior to 1997, the aid payments were fixed in gold rather than South Korean won to assuage the defectors’ distrust of paper currency: Haggard & Noland, *supra* note 52 at 55. The 1962 law was revised in 1978 and remained effective until 1993, when a new law was enacted and shifted to treating North Korean defectors more as economic refugees than as heroes: Byung-Ho Chung, “Between Defector and Migrant: Identities and Strategies of North Koreans in South Korea” (2008) 32 Korean S. 1 at 7-9.

¹³⁸ 2007 CRS Report, *supra* note 2 at 14. The latest estimate is that 2,809 North Koreans defected to the South during 2008: “North Korean Defectors Up 10% Last Year” *Chosun Ilbo* (6 January 2009), online: <http://english.chosun.com/site/data/html_dir/2009/01/06/2009010661029.html>.

2. Imperfections of Current International Refugee Law

Before making outright criticisms of China's noncompliance with its international treaty obligations toward North Korean refugees, it bears keeping in mind that many Asian countries are not signatories to the 1951 *Refugee Convention* and 1967 *Protocol*. These two instruments have been criticized as Eurocentric responses to displaced populations in Europe following World War II and inadequate solutions to Asian refugee problems.¹³⁹ The concept of human rights is, arguably, "legally international" but "historically Western"; and it has been argued that Asian states' viewpoints and interests were not sufficiently incorporated during the drafting process of international refugee law.¹⁴⁰ The scope of current international refugee law may not be comprehensive enough to cover all individuals in need of protection, regardless of China's compliance with its international treaty obligations toward North Korean refugees.

The drafting history of the 1951 *Refugee Convention* is dominated by three themes. First, the scope of the *Convention's* protection was driven by a delegation of predominantly Western states, whose partisan interests were divided along Eastern and Western ideologies. As a result, the *Convention's* protection applied only to refugees as defined primarily by Western ideologies rather than to all similarly situated persons.¹⁴¹ Its refugee definition included only persons seeking civil and political rights and excluded those seeking basic socioeconomic rights like food, healthcare, and education.¹⁴² Second, instead of embracing refugee populations originating from all parts of the world, the burden-sharing regime of refugee resettlement created by the *Convention* was Eurocentric in its focus on European refugees displaced by World War II. Third, the determination of refugee status is largely implemented at the state rather than at the international level, allowing the states considerable discretion in setting their own procedures, screening refugees with domestic interests in mind, and granting asylum to individuals who have been validated as refugees.¹⁴³ The cumulative product of these themes is a Eurocentric protection regime that neither recognizes socioeconomic rights nor obligates Western states to accept asylum seekers from most developing countries.

To this end, the current mechanism for refugee protection under international law has been criticized as too narrow to adequately cover all people in need of international protection.¹⁴⁴ The 1951 *Refugee Convention*

¹³⁹ Sara E. Davies, "The Asian Rejection?: International Refugee Law in Asia" (2006) 52 Aust. J. Pol. & Hist. 562 at 563.

¹⁴⁰ *Ibid.* at 575.

¹⁴¹ James C. Hathaway, "A Reconsideration of the Underlying Premise of Refugee Law" (1990) 31 Harv. Int'l L.J. 129 at 144-46 (The Soviet Union and its allies condemned the Western states' grounding of refugee status in social and ideological incompatibility as politically motivated. Stateless persons, whose interests were sought after by the Soviet Union, were excluded by the 1951 *Refugee Convention* despite the United Kingdom's plea to include all unprotected persons.)

¹⁴² *Ibid.* at 150.

¹⁴³ See *ibid.* at 166-74.

¹⁴⁴ Jose Alvin C. Gonzaga, "The Role of the United Nations High Commissioner for Refugees and the Refugee Definition" in Susan Kneebone, ed., *The Refugees Convention 50 Years On:*

and 1967 *Protocol* protect rights of an individual rather than of a collective nature: civil and political freedoms from persecution because of race, religion, nationality, and political affiliation are protected, while economic, social, and cultural freedoms are not.¹⁴⁵ Individual liberties are emphasized in Western democracies, but collective liberties such as the freedom from starvation are more relevant in socialist and communist states like North Korea.¹⁴⁶ A second imperfection of current refugee law is that it obligates member states to protect only those within, rather than those seeking entry into, their borders. This puts asylum seekers in the vulnerable position of risking dangerous escape routes and paying smugglers large sums of money along the way.¹⁴⁷ In short, even if China is compliant with its international treaty obligations, international refugee law in its current form is not well-suited to Asian refugee problems. As long as international refugee law continues to prioritize civil and political freedoms over socioeconomic freedoms, and to predicate protection upon the asylum seeker's entry into a member state, it will not offer sufficient protection for North Korean refugees.

3. Addressing China's Burdens of Providing Temporary First Asylum

Given the weaknesses of the NKHRA and the current international refugee law regime, this article proposes that convincing China to be what Thailand was to the Indochinese refugee resettlement process is essential to shaping an international solution to help North Korean refugees. During the Indochinese refugee crisis, the lofty humanitarian stance adopted by Western nations did not always match up with their actual practices of refugee resettlement. John Gunther Dean, upon becoming the American Ambassador to Thailand in 1981, announced that he "would be ambassador to Thailand, not to refugees" and set out to repair US-Thai relations that had become frayed as a result of focusing too much attention on the human rights of refugees over the adverse impact on Thailand.¹⁴⁸ Thailand agreed to provide

Globalization and International Law (Burlington, VT: Ashgate, 2003) 233.

¹⁴⁵ Cara D. Cutler, "China's Provision of Temporary Visas to North Koreans" (2006) 6 *Stan. J. E. Asian Aff.* 63 at 65. See Michael J. Dennis & David P. Stewart, "Justifiability of Economic, Social, and Cultural Rights: Should There Be an International Complaints Mechanism to Adjudicate the Rights to Food, Water, Housing, and Health?" (2004) 98 *Am. J. Int'l L.* 462 ("The content of economic, social, and cultural rights is generally said to comprise the following: an adequate standard of living, including food, clothing, housing, health, and medical care; education; work; fair conditions of employment; the opportunity to form and join trade unions; social security; and participation in cultural life.").

¹⁴⁶ See Costas Douzinas, *The End of Human Rights* (Portland, OR: Hart, 2000) at 122-24; Cornelius F. Murphy, Jr., "Objections to Western Conceptions of Human Rights" (1980) 9 *Hofstra L. Rev.* 433 at 439.

¹⁴⁷ Haggard & Noland, *supra* note 52 at 59 ("The typical total cost of an average 'arranged defection' in 2005-2006 was approximately \$3,000 to \$4,000, but in cases of a direct air flight from China the fees are likely to be \$10,000, since this scenario requires a forged passport."). In response to the criticism that the two-thirds reduction in lump sum resettlement packages discourages defections, South Korean officials have defended the policy change as "necessary to discourage exploitative brokers who charge the defectors for facilitating passage from North Korea"; 2007 CRS Report, *supra* note 2 at 14.

¹⁴⁸ Sutter, *supra* note 27 at 128.

temporary first asylum without selectivity but conditional on the commitment to permanent resettlement by other countries. When selective admissions criteria in resettlement countries rejected refugees, they remained Thailand's burden.¹⁴⁹ When the United States curtailed its resettlement rate and adopted more stringent INS screenings, Thailand reacted by adopting humane deterrence policies.

Effective implementation of the *NKHRA* requires Congressional recognition of the unique burdens that China would take on by serving as the primary first asylum base for North Koreans. This can be accomplished partially by pledging part of the annual \$26 million *NKHRA* budget to the development of an effective screening program so that the resettlement rate in the United States does not lag behind the admission rate of North Koreans into China.¹⁵⁰ American diplomatic dialogue with China should also recognize that refugee status comes with its own benefits from the UNHCR and from countries such as the United States and South Korea. The UNHCR, for example, was financially responsible for the refugee camps in ASEAN countries and helped Thailand to implement a screening program that separated refugees from economic migrants.¹⁵¹

The United States also needs to take leadership in pledging financial support to the local population in northeastern China, the region whose economy and stability would bear the brunt of adverse impact from an inflow of North Korean asylum seekers. Some Indochinese refugees brought diseases like malaria, malnutrition, cholera, and leprosy to Thailand, which obligated the Thai government to not only send medical assistance to the refugee camps but also prevent the diseases from spreading into nearby villages. The negative impact of prostitution and narcotics smuggling stemming from the refugee camps spilled over into Thai society, and the significant inflow of refugees in the early 1980s necessitated the Thai government to purchase expensive land in order to expand the capacity of refugee holding centers.¹⁵²

Indochinese refugees also brought problems to the local population of first asylum countries like slash-and-burn farming, deforestation, inflation, and corruption by politicians. In response, the Affected Thai Program was implemented in 1980 with international support in order to provide Thai villages located near refugee camps with emergency relocation services, agricultural development, water sources, education, public health, and road construction.¹⁵³ Indochinese refugee centers in Thailand were often located in rural border areas with low standards of living. The refugees received free food and services from the UNHCR and lived better than the local population, which were obvious sources of resentment and unrest for the Thai villagers. The UNHCR guidelines in Thailand reflected sensitivity to

¹⁴⁹ *Ibid.* at 130.

¹⁵⁰ See House Committee, 2008 *Reauthorization Act Report*, *supra* note 1 at 9.

¹⁵¹ Sutter, *supra* note 27 at 114.

¹⁵² Songprasert, *supra* note 30 at 20-23.

¹⁵³ Sutter, *supra* note 27 at 125.

this issue by specifying that illegal aliens must not receive better treatment than that provided to Thai citizens in the same area.¹⁵⁴

Lastly, fear of the North Korean regime's collapse—a primary driver behind China's unwillingness to recognize North Koreans as refugees—is not fear of an inconceivable scenario. Even though China is unlikely to engage in any multilateral dialogue about the prospect of regime collapse in North Korea, it is nonetheless aware of the possibility and has reportedly developed contingency plans for "possible humanitarian, peacekeeping, and 'environmental control' missions."¹⁵⁵ The United States and South Korea, most likely the top two destinations for North Korean refugees in any multilateral resettlement program, have recently made progress in negotiating the terms of Operations Plan (OPLAN) 5029, a contingency plan that prepares for the North Korean government's collapse and has been in development since at least 2004. OPLAN 5029 in its concept format plan reportedly outlines the ways in which South Korean and American forces would manage an inflow of North Korean refugees and other instabilities in the event of the North Korean regime's disintegration.¹⁵⁶

V. Challenges in Implementation

Past American leadership in the resettlement of Indochinese refugees is not indicative of future success with North Korean refugees, and there are several crucial differences between the two events. The Indochinese refugee crisis, to begin with, was seen as America's responsibility largely because of its involvement in the Vietnam War and failed foreign policy.¹⁵⁷ There is no analogous source of guilt and obligation in the present North Korean situation. Some first asylum countries and particularly Thailand happened to be key American allies, but their relationships with the United States still felt strain when American refugee admissions declined.¹⁵⁸ US-China leadership in resettling North Korean refugees requires trust and collaboration in an area that has been the source of much tension between the two countries in the past.

Secondly, American policies regarding Indochinese refugees were responses to an emergency. The outflow from Indochina escalated to a crisis in 1979 when the Vietnamese government gave official encouragement to the exodus due to deteriorating Sino-Vietnamese relations and the wish to transform the commercially oriented South Vietnam into a socialist state.¹⁵⁹

¹⁵⁴ *Ibid.* at 124.

¹⁵⁵ Paul B. Stares & Joel S. Wit, "Preparing for Sudden Change in North Korea", Council Special Report No. 42 (Council on Foreign Relations Press, January 2009) at 6, online: <http://i.cfr.org/content/publications/attachments/North_Korea_CSR42.pdf>.

¹⁵⁶ GlobalSecurity.org, "OPLAN 5029 – Collapse of North Korea", online: <<http://www.globalsecurity.org/military/ops/oplan-5029.htm>>. See "Korea, U.S. Agree to Compromise N. Korea Concept Plan" *Chosun Ilbo* (5 June 2005), online: <http://english.chosun.com/site/data/html_dir/2005/06/05/2005060561013.html>.

¹⁵⁷ Hein, *supra* note 39 at 29-30.

¹⁵⁸ *Ibid.* at 30.

¹⁵⁹ Suhrke, "Law and Politics of First Asylum", *supra* note 28 at 102-105.

At the request of receiving countries attending the 1979 UN Conference in Geneva, Vietnam resumed its earlier policy of not permitting illegal departures and, as a result, the outflow stabilized. Increased compliance with the Orderly Departure Program in 1981 also demonstrated Vietnam's willingness to cooperate with receiving countries.¹⁶⁰ Unlike Vietnam, North Korea is not likely to facilitate any departure, let alone mass exodus, for its citizens; consequently there is much more inertia in coordinating a multilateral solution in the absence of an outflow emergency.

The ASEAN countries only gave first asylum conditional on the commitment to permanent resettlement by other countries. The United States imposed a ceiling of 100,000 Indochinese admissions for fiscal year 1982 and reduced it further to 72,000 for fiscal year 1983. Meanwhile, other permanent resettlement countries were showing signs of fatigue as well by citing economic depressions and the need to accommodate refugees from other countries. Selective resettlement policy meant that uneducated, unskilled, and handicapped refugees were least likely to be picked and continued to remain ASEAN's burdens.¹⁶¹ To this end, enforcement of no local settlement in first asylum countries will be equally important in designing a resettlement process for North Koreans.

VI. Conclusion

The *NKHRA*, although passed with good intentions by Congress, must engage China's leadership to offer an effective humanitarian solution to the resettlement of North Korean refugees. An international burden-sharing scheme that permanently resettles refugees in recipient states after temporary stays in first asylum countries is a realistic solution, as illustrated by the successful multilateral resettlement of Indochinese refugees following the end of the Vietnam War in 1975. China's historical patronage of North Korea, alliance with South Korea, and status as first-stop destination for most North Korean asylum seekers make it a crucial player in any multilateral resettlement solution. If the United States, along with other key players such as South Korea, takes leadership in setting up a reassuring multilateral resettlement solution for North Korean refugees and jointly persuade China to provide first asylum, China likely would not flatly refuse to cooperate solely for the sake of appeasing the North Korean regime.

The resettlement of Indochinese refugees roughly three decades ago demonstrates that while underlying national interests usually shape humanitarian gestures, a multilateral solution does not require a complete overlap of interests among participating states. There are significant differences, to be sure, between the Indochinese refugee crisis and the North Korean refugee problem at present. The flow of refugees out of Southeast Asia was the result of war and political repression. It was largely seen as America's responsibility because of America's failed foreign policy and

¹⁶⁰ *Ibid.*

¹⁶¹ *Ibid.* at 109.

involvement in the Vietnam War. Without an analogous sense of responsibility, the United States' interests in the successful resettlement of North Korean refugees are arguably less compelling. Nonetheless, Congress has shown commitment to the issue by passing the *NKHRA* in 2004 and renewing it in 2008 for four more fiscal years. To the extent that effective implementation of the *NKHRA* is complementary to the American tradition of humanitarianism and "voting with your feet" foreign policy, the Indochinese refugee crisis offers valuable lessons for the North Korean refugee problem.

The *NKHRA*, as it currently stands, has significant shortcomings. It has been criticized as an encouragement of the North Korean regime's collapse, an obstacle to the six-party nonproliferation talks without substantial improvement of the refugee situation, and a funnel of negative attention that could worsen rather than improve the plight of the very North Korean refugees it seeks to help. Additionally, even though the problem is outside the focus of this article, the *NKHRA* does not provide for collaboration with South Korea, a key player in any multilateral resettlement solution. Rather than confrontational criticisms of China's noncompliance with international refugee law, which is limited in its protection of North Korean asylum seekers, quiet American diplomacy that acknowledges and pledges aid to the adverse first asylum impacts on China would likely be more effective.

China's Energy Investments and the Corporate Social Responsibility Imperative

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I. Introduction

The China National Petroleum Company (CNPC) is technically a private corporation. However, CNPC is a state oil company of the People's Republic of China, a central state-owned enterprise that is the direct successor to the Ministry of Petroleum Industry.¹ Although there is an official split between the Chinese Communist Party (CCP) and the Chinese national oil companies, observers such as Erica Downs recognize that they do maintain a symbiotic relationship: many of the key company executives also hold positions in the Central Committee of the CCP.²

The views expressed in this article are those of the authors, and do not reflect the views of their respective employers.

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¹ China National Petroleum Corporation, "History", online: <www.cnpc.com.cn/en/aboutcnpc/companyprofile/history/default.htm> [CNPC, "History"].

² Erica S. Downs, "China's 'New' Energy Administration" (2008) *The China Business Review*

There is some degree of independence, however. CNPC is administered by the Chinese government through the State-owned Assets Supervision and Administration Commission of the State Council (SASAC).³ SASAC describes itself as acting similarly to a private shareholder or investor under *The Company Law of the People's Republic of China*,⁴ therefore representing the interests of the state only indirectly through SASAC's influence over management, corporate governance, and performance of a subject company.⁵ It is intended to separate the ownership interests of the Chinese state from management of state-owned enterprises.⁶ More specifically, SASAC's role is to safeguard the role of economic interests in management decisions, providing an institutional buffer from the Chinese government's regulatory, political policy-making functions.⁷ Ultimately, the ruling Communist Party envisions privatization of most state-owned enterprises, explicitly including the infrastructure and utility sectors.⁸

Therefore, while CNPC policy reflects policies of the Chinese government because of its status as a state-owned enterprise, it must remain mindful of private sector concerns such as economic returns because of the mission of SASAC and CNPC's potential privatization. CNPC therefore has a multifaceted nature that makes it a unique case study for the role of corporate social responsibility (CSR) norms and public international law in shaping the practices of multinational corporations.

How the management of CNPC navigates these tensions will have consequences that extend beyond direct CNPC corporate practices. Following a corporate reorganization in 1998 and the creation of PetroChina as a private Joint Stock Limited Company under Chinese law, CNPC became the majority shareholder of PetroChina.⁹ PetroChina is currently the largest public company in China by market value and the third largest public oil and gas operations sector company in the world.¹⁰ While PetroChina is careful to publicly distance itself from the control that can be exerted by

(November-December 2008) 42.

³ State-owned Assets Supervision and Administration Commission of the State Council, People's Republic of China, "Central SOEs" (19 June 2008), online: <www.sasac.gov.cn/n2963340/n2971121/n4956567/4956583.html>.

⁴ [27 October 2005] Order of the President of the People's Republic of China, No. 42 (entered into effect 1 January 2006), online: <www.fdi.gov.cn/pub/FDI_EN/Laws/law_en_info.jsp?docid=50878> [Company Law].

⁵ State-owned Assets Supervision and Administration Commission of the State Council, People's Republic of China, "Main Functions and Responsibilities of SASAC", online: <www.sasac.gov.cn/n2963340/n2963393/2965120.html>.

⁶ Li Rongrong, "Welcome Remarks", online: <<http://www.sasac.gov.cn/n2963340/n2963363/2965107.html>>.

⁷ Jiangyu Wang, "Dancing with Wolves: Regulation and Deregulation of Foreign Investment in China's Stock Market" (2004) 5 Asian-Pacific L. & Pol'y J. 1 at 59.

⁸ *Ibid.*

⁹ CNPC, "History", *supra* note 1.

¹⁰ Forbes, "The Global 2000" (20 April 2011), online: <www.forbes.com/global2000/list?industry>All&state>All&country>All> (PetroChina is sixth on Forbes' global list of the largest publicly listed companies, the highest of any Chinese company. Within the oil and gas operations sector, it is behind only ExxonMobil and Royal Dutch Shell.).

CNPC due to its controlling interest,¹¹ shareholders in Chinese joint stock limited companies have power over the company's operational guidelines and investment plans, as well as approval rights over annual financial budgets.¹² Even without day-to-day influence regarding PetroChina operations, CNPC can still have an effect on the ultimate direction of its operational policies. Therefore, it is useful to examine CNPC's own internal policies as an indication of the kinds of policies that might be encouraged at the PetroChina subsidiary level.

Evidence shows that private corporate groupings are gaining strength in China,¹³ and these corporate groupings are attracting increasingly significant public exposure. This article will argue that these two shifts may lead to increased following of CSR norms by China's multinational corporations. As a state-owned enterprise, CNPC faces a unique set of pressures with regards to the implementation (or non-implementation) of CSR norms. This article will explore these pressures, and discuss how CNPC can respond to them. CSR is a broad concept that addresses a company's responsibility to engage in social issues beyond purely economic, legal and technical operational requirements.¹⁴ It requires attention to the social, environmental, ethical and local economic implications of the company's policies and actions.¹⁵ CSR defines how a company should serve the interests of societal stakeholders, rather than the business-oriented interest of maximization of economic investment returns for traditional shareholders.¹⁶ The societal stakeholders who are the target of CSR include individuals and groups, local to or with an interest in where a company operates, as well as end-user customers of a company. In recent years, CSR has moved beyond an exhortation to act in an ethical manner into a call for participation in international development initiatives.¹⁷ Even while the actual positive impact of CSR activities on development is under debate, corporations' perceived need to engage in such activities is less controversial.¹⁸ As a state-owned enterprise, CNPC faces an especially difficult task in balancing global public and political support for CSR norms with the policies of the Chinese government.

The trend towards CSR is part of a larger evolution in the treatment of corporations in public international law. This article will use the example of

¹¹ PetroChina Company Limited, "The Relationship Between CNPC and the Company" (2008), online: <www.petrochina.com.cn/Ptr/Investor_Relations/Corporate_Governance_Structure/gszljg_6.htm>.

¹² *Company Law*, *supra* note 4, Arts. 38, 100.

¹³ Barry Naughton, "SASAC and Rising Corporate Power in China" (12 March 2008) 24 *China Leadership Monitor*, online: <www.hoover.org/publications/china-leadership-monitor/article/5668>.

¹⁴ Krista Bondy, Dirk Matten & Jeremy Moon, "Multinational Corporation Codes of Conduct: Governance Tools for Corporate Social Responsibility?" (2008) 16 Corp. Governance 294 at 295.

¹⁵ *Ibid.*

¹⁶ Jennifer Oetzel, Kathleen A. Getz & Stephen Ladek, "The Role of Multinational Enterprises in Responding to Violent Conflict: A Conceptual Model and Framework for Research" (2007) 44 Am. Bus. L.J. 331 at 335.

¹⁷ Jędrzej G. Frynas, "Corporate Social Responsibility and International Development: Critical Assessment" (2008) 16 Corp. Governance 274.

¹⁸ *Ibid.* at 279.

CNPC—as a state-owned enterprise, neither a purely public nor a purely private multinational corporation—to touch on broader changes in the way corporations govern and are governed. The traditional subjects of public international law have been states; only relatively recently have entities such as international organizations begun to attain incidents of international legal personality.¹⁹

Understanding the unique pressures facing CNPC's management with respect to CSR and its potential obligations in public international law—and therefore gaining insight into CNPC's possible response to these pressures—is important for a number of reasons. The activities of CNPC and of PetroChina affect many in China and in the (often developing) areas in which these corporations undertake resource extraction and transportation. One example of this impact is particularly pressing. CNPC's first major foreign oil and gas exploration project was in Sudan,²⁰ in which it continues to operate more projects than in any other African country.²¹ Sudan is also the largest single foreign state in China's oil investment portfolio,²² and Chinese investment accounts for 40% of Sudanese oil production, much of which is sold on the world market.²³ Since China's domestic crude oil reserves are limited, CNPC has little choice but to increase its international oil supply exploration and investments. At the present time, Africa provides the largest influx of CNPC's business along with energy deals in the Middle East and Central Asia. In an effort to secure these investments, the Chinese government has become a significant supplier of arms to the Sudanese government in its long-standing civil war in Darfur, and may even be the largest supplier.²⁴ The humanitarian crisis in Sudan is severe and continuing,²⁵ and has been characterized as "a massive campaign of ethnic violence," involving war crimes and crimes against humanity, and arguably extending to the commission of genocide.²⁶

On the one hand, the Chinese government has been criticized for its practical and diplomatic support of the Sudanese government's most controversial activities,²⁷ including the way it has influenced UN Security

¹⁹ Allison D. Garrett, "The Corporation as Sovereign" (2008) 60 Me. L. Rev. 129 at 130.

²⁰ China National Petroleum Corporation, 2007 Annual Report, at 46, online: <<http://www.cnpc.com.cn/Resource/english/images1/pdf/07AnnualReport/2007PDF.pdf>> [CNPC, 2007 Annual Report].

²¹ *Ibid.* at 49.

²² Peter S. Goodman, "China Invests Heavily in Sudan's Oil Industry-Beijing Supplies Arms Used on Villagers" *Washington Post* (23 December 2004) A1.

²³ International Crisis Group, "China's Thirst for Oil" (Asia Report No. 153, 9 June 2008) at 24, online: <www.crisisgroup.org/~/media/Files/asia/north-east-asia/153_china_s_thirst_for_oil.ashx>.

²⁴ *Ibid.* at 29; Goodman, *supra* note 22; Amnesty International, "Sudan: Arms Continuing to Fuel Serious Human Rights Violations in Darfur" (8 May 2007), online: <www.amnesty.org/en/library/info/AFR54/019/2007>.

²⁵ For a listing of recent UN documents regarding the situation in Sudan, see United Nations Sudan Information Gateway, "Document Database: Latest Documents", online:

<<http://www.unsudanig.org/library/index.php?fid=documents>>.

²⁶ Leilani F. Battiste, "The Case for Intervention in the Humanitarian Crisis in the Sudan" (2005) 11 Ann. Surv. Int'l & Comp. L. 49 at 49-50.

²⁷ Goodman, *supra* note 22.

Council sanctions and resolutions in response to early reports of the Darfur conflict.²⁸ SASAC, on the other hand, claims a commitment to sustainable economic development and the pursuit of international development goals, through its promulgation of the *World Economic Development Declaration (Zhuhai Declaration)*.²⁹ The *Zhuhai Declaration* expresses a series of sustainable development principles intended to achieve international development in accordance with the Millennium Development Goals.³⁰ The question therefore is how to reconcile these competing positions: against the backdrop of accusations of human rights abuses by the Chinese government, how can—and why should—the state-owned CNPC act in a manner reflecting CSR obligations?

This article examines the adequacy of CNPC's CSR policies. This article does not attempt to critically review particular international norms with respect to CNPC, or even argue that they are binding in law on CNPC; rather, it explores the potential applicability of existing norms to CNPC's specific situation. However, it will be argued that CNPC should amend its CSR policies to incorporate international law guidelines generally, including but not limited to the existing set of CSR norms. Part II will discuss the various motivations for compliance with CSR regimes: market-based, domestic regulatory/civil liability, and international regulatory and quasi-regulatory. The third part will examine the particular set of incentives for CNPC to comply with various global CSR standards, while the next part will discuss the concrete steps that CNPC should take in implementing these standards. Finally, the paper will conclude by reflecting on the future of CNPC with respect to CSR.

II. CNPC's Motivations for Compliance

There are a variety of norms that CNPC can draw upon in order to build its corporate social responsibility policies. However, this does not answer the question of why CNPC should be concerned with compliance with those standards in the first place.

Ralph Steinhardt posits four potential regimes that motivate multinational corporations to comply with human rights standards: (1) market-based regimes, where conforming to standards provide a competitive advantage; (2) domestic regulatory regimes, where local law requires compliance with standards; (3) civil liability regimes, where the threat of civil

²⁸ International Crisis Group, *supra* note 23 at 25.

²⁹ Zhuhai, China, 7 November 2003, online: <www.cicpmc.org/en/detail.asp?id=3114&Channel=4&ClassID=25>; Li Rongrong, "Aggressively Advance SOE Reform and Development, Enhance China's Sustainable Economic Development and Overall Social Progress" (Address delivered to the World Economic Development Conference, Zhuhai, China, 7 November 2003), online: <<http://www.sasac.gov.cn/n2963340/n2964712/3049653.html>> (Mr. Li spoke in his capacity as the Chairman of SASAC).

³⁰ Jemal-ud-din Kassum, "Growth With Equity in an Integrated World" (Address delivered to the World Economic Development Conference, Zhuhai, China, 6 November 2003), online: <<http://go.worldbank.org/YA5SYF1YL0>> (Mr. Kassum spoke for the World Bank in his capacity as the Vice-President, East Asia and Pacific).

litigation incentivizes compliance; and (4) international regulatory and quasi-regulatory regimes, where international non-governmental and inter-governmental organizations use formal and informal tools to reduce human rights violations by corporations.³¹ Each of these regimes is capable of incentivizing compliance not only with the core set of international human rights conventions, but also with standards under international law such as CSR norms, as well as the general pursuit of development goals. CNPC has suffered, or may suffer, specific consequences that align with each of these broad motivational regimes.

1. The Market-based Regime

The market-based regime relies on the assumption that CSR can provide a competitive advantage among market competitors. The consumers that drive market-based regimes now include sophisticated investors interested in “sustainable” business, a concept that encompasses attention to human rights³² and environmental responsibility.³³ Consumers may also directly affect a business by refusing to purchase products produced by companies that do not comply with human rights standards.³⁴ The effects of the market-based regime on CNPC’s CSR compliance are limited, however, due to CNPC’s long-standing (albeit declining) insulation from relevant market forces.

This mechanism for regulation is faced with obvious difficulties when applied to CNPC. First, state ownership insulates CNPC from the effect of purely competitive markets. In addition, CNPC sells its products with a domestic focus and acts as a direct seller to individual consumers primarily in China.³⁵ Meanwhile, international trading activities are carried out as an indirect operation through the PetroChina subsidiary.³⁶ CNPC, then, benefits from a captive and controlled market that may be less responsive to CSR efforts and other corporate activities than a company that sells to a broader consumer base that is potentially more concerned with such considerations.

³¹ Ralph G. Steinhardt, “Soft Law, Hard Markets: Competitive Self-Interest and the Emergence of Human Rights Responsibilities for Multinational Corporations” (2008) 33 Brooklyn J. Int’l L. 933 at 934-35.

³² *Ibid.* at 941-42.

³³ World Bank, Environment and Social Development Unit (EASES) of the East Asia and Pacific Region and Environment Department (ENV), *Corporate Environmental and Social Responsibility in the East Asia and Pacific Region: Review of Emerging Practice* (May 2006) at iv, online: <www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2008/02/04/000020953_20080204141244/Rendered/PDF/423030PAPER0EA1ponsibility01PUBLIC1.pdf>.

³⁴ David Weissbrodt & Muria Kruger, “Current Developments: Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights” (2003) 97 Am. J. Int’l L. 901 at 902.

³⁵ One example is CNPC’s network of over 17 000 service stations throughout China: China National Petroleum Corporation, “Marketing & Trading”, online: <www.cnpc.com.cn/en/aboutcnpc/ourbusinesses/marketingtrading/Marketing_and_Trading.htm>.

³⁶ *Ibid.*, International Crisis Group, *supra* note 23 at 25 (“to make it more difficult for activists to target the company with divestment measures or other forms of sanctions”, CNPC ensured that “its listing on the New York Stock Exchange–PetroChina–excludes overseas investments from its portfolio, making it difficult for international shareholders to affect those operations.”).

Furthermore, CNPC is largely insulated from international consumer boycotts of its goods. Like other national oil companies, CNPC is in a less precarious position than other multinational corporations producing consumer goods. Boycotting a single national oil company is nearly impossible within the confines of the global energy market. In the United States, for instance, gasoline from different importers is combined at the pipeline and bulk terminal level, meaning that different consumer outlets often purchase their petroleum products from the same source.³⁷ Furthermore, local consumer outlets are unlikely to be owned directly by a national oil company, so that boycotting or protesting a local gas station will not affect the parent company whose brand the gas station carries.³⁸ Therefore, as a practical matter, boycotting a particular oil company from a consumer point of view is unlikely to be effective and unlikely to be a sought-after consumer impact strategy.

But this market insulation from consumer-based CSR pressures may be deteriorating. As Chinese consumers become increasingly media-savvy, CNPC cannot continue to rely on its status as a state oil company for its direct-to-consumer success. For CNPC, the example of Russia's Lukoil Oil Company is instructive because it shows a way to promote future economic success through (a) the recognition that CSR norms can be expected in the future to create stronger consumer-based market incentives for compliance; and (b) careful planning of CSR initiatives, to ensure that one's corporation is prepared to capitalize on these market incentives. The policies of Lukoil suggest that in addition to the consumer market benefits of taking on a similar stance as Lukoil and following a CSR scheme, CNPC may also find similar positive effects in its labor and operating market.

Much like the creation of CNPC, Lukoil was created as a state-owned oil company, in the USSR in 1991.³⁹ While Lukoil acquired a United States retail oil company in Getty Petroleum Marketing, Inc. in 2000,⁴⁰ it did not enter the US consumer market under the Lukoil name until three years later.⁴¹ In the intervening time period, Lukoil recognized the role of CSR norms in the American consumer marketplace by creating a CSR code and program, which included attaining certifications and undertaking audits.⁴² It released

³⁷ U.S. Energy Information Administration, "Oil: Crude and Petroleum Products Explained" (19 February 2010), online: <http://www.eia.doe.gov/energyexplained/index.cfm?page=oil_home>.

³⁸ See e.g. Derrick Ho, "BP Boycotts Hurt Local Stations; Gas Giant Offers Help" CNN.com (12 June 2010), online: <http://articles.cnn.com/2010-06-12/us/bp.protest.atlanta_1_gas-station-retail-gasoline-storage-terminals?_s=PM:US> (describes ineffective protests against British Petroleum in the wake of the Gulf of Mexico oil disaster).

³⁹ Lukoil Oil Company, "Company History: 2000-1991", online: <www.lukoil.com/static_6_5id_2132_.html>.

⁴⁰ *Ibid.*; Lukoil Oil Company, "Lukoil to Acquire Getty in First Acquisition of Publicly Held US Company by a Russian Corporation" (3 November 2000), online: <www.lukoil.com/press.asp?div_id=1&id=399&year=2000>.

⁴¹ Lukoil Oil Company, "President Vladimir Putin of Russia Visits Lukoil Gas Station in NYC" (26 September 2003), online: <http://www.lukoil.com/press.asp?div_id=1&id=2143&year=2003>.

⁴² Lukoil Oil Company, "Lukoil Sustainability Report for Operations in the Russian Federation:

its first formal CSR report in 2005 and upon publication of its second report, explicitly stated that the program was intended to "ensure more efficient performance and social protection of employees."⁴³ Lukoil has also acknowledged the role of environmental responsibility and the importance of protecting individuals from harm, both elements of CSR, and the close relationship in economic terms between these elements and its attainment of broader strategic development goals.⁴⁴

Regardless of whether CNPC's future desire to change is driven by moral standards or higher profit margins, there are two market-based factors that are currently pulling China and CNPC toward CSR compliance. The first has already been observed: out of a need for improved logistical capabilities in sub-Saharan Africa, China's national oil companies have increased their local infrastructure finance investments. CNPC needs to be able to transport its product in countries that do not always have basic infrastructure capabilities.⁴⁵ The resulting investments, while responding to market pressures, also have the effect of promoting sustainable development.

The second market-based factor currently driving CSR compliance underlines CNPC's complex role as a private corporation that, through its state ownership, is nonetheless subject to a significant level of state influence. After China's experience leading up to the 2008 Summer Olympics, there are signs that China is beginning to take notice of how its foreign direct investment activities impact public perception. The country's public image was internationally tarnished by anti-China protests carried out against the country's Olympic torchbearers.⁴⁶ The protests grew and eventually armed security was required. China's "Journey of Harmony" turned into an international spectacle, drawing attention to issues such as Tibetan independence, tensions with ethnic minorities, Taiwanese independence and the genocide in Sudan.⁴⁷ These activities have increased the sensitivity of China's leadership to the perception of their foreign policies abroad, and perhaps resulted in increased efforts to communicate China's perspective on these issues.⁴⁸

2003-2004" (1 September 2005), online: <www.lukoil.com/materials/doc/reports/Social_Report-eng.pdf>.

⁴³ Lukoil Oil Company, "Lukoil Published Its Second Social Report" (3 September 2007), online: <www.lukoil.com/press.asp?div_id=1&id=2763&year=2007>.

⁴⁴ Lukoil Oil Company, "Lukoil Presents Main Principles of Strategic Development up to 2016, Including Increase of Daily Hydrocarbon Production to 4 MLN BOE" (18 October 2006), online: <www.lukoil.com/press.asp?div_id=1&id=2587&year=2006>.

⁴⁵ Vivien Foster *et al.*, "Building Bridges: China's Growing Role as Infrastructure Financier for Sub-Saharan Africa" (2009) 5 *Trends and Policy Options*.

⁴⁶ John Burns, "Protests of China Make Olympic Torch Relay an Obstacle Course" *The New York Times* (7 April 2008).

⁴⁷ See e.g. International Crisis Group, *supra* note 23 at 27; Nicholas Kristof, "China's Genocide Olympics" *The New York Times* (24 January 2008); Human Rights Watch, "China: Lhasa Torch Relay Tarnishes Olympic Movement" (17 June 2008), online: <www.hrw.org/en/news/2008/06/16/china-lhasa-torch-relay-tarnishes-olympic-movement>; Human Rights Watch, "China: Police Detain Would-Be Olympic Protesters" (13 August 2008), online: <http://china.hrw.org/press/news_release/china_police_detain_would_be_olympic_protesters>.

⁴⁸ International Crisis Group, *ibid.*, fn. 216 ("The Darfur outcry" associated with the 2008 Beijing Olympics "has heightened China's awareness of the complexity of influences on U.S. policy. It

It is significant that the response from China's political leadership coincided with changes by CNPC to its CSR policies. Politically and militarily, China stepped up its campaign to improve the country's image on foreign direct investments in Sudan;⁴⁹ CNPC followed in step by increasing the reporting of its social and corporate responsibility efforts. CNPC's homepage now explicitly includes such efforts in its corporate philosophy: "While providing energy, we strive for harmonious relationships between operation and the environment, and corporate and community interests."⁵⁰ Furthermore, CNPC now offers an "Environment & Society" section highlighting their contributions to the environment, health, safety and public welfare. Of particular interest is the section "Support for Education in Sudan," highlighting its efforts at improving children's education through the building of new schools and the supplementary funding of local educational programs.⁵¹

The fact that CNPC is willing to invest in the sustainable development of Sudan may seem to stand in tension with the "race to the bottom" hypothesis, which states that multinational corporations will simply seek the lowest labour market costs. However, this must be viewed in light of the gains that arise from improvements in local living standards. Although it may appear counter-intuitive, the race to the bottom approach has shown to ultimately increase costs, through the consequences of poor quality control and inefficient labour.⁵² Indeed, Nike's recent approach to CSR shows benefits beyond simply going through the CSR motions; it now actively promotes CSR norms.⁵³ Multinational corporations have increasingly been interested in improving living standards in developing countries where their workforces are located.⁵⁴ Initial steps taken by multinational corporations

has learned that the government cannot temper the positions of advocacy and lobbying groups and that the best way to deal with them is to reach out to them directly. Chinese diplomats in Washington are trying public diplomacy with a wide variety of NGOs, activist groups, lawmakers and journalists to highlight the steps Beijing has taken to end the conflict."); "China's Xinhua Launches 24-hour Global News Channel in English, Cnc" *Mercopress South Atlantic News Agency* (2 July 2010), online: <<http://en.mercopress.com/2010/07/02/china-s-xinhua-launches-24-hour-global-news-channel-in-english-cnc>>.

⁴⁹ International Crisis Group, *ibid.* at 27-29.

⁵⁰ China National Petroleum Company, "Environment & Society", online: <www.cnpc.com.cn/en/environmentssociety/>.

⁵¹ Online: <www.cnpc.com.cn/en/environmentssociety/public/case/Support+for+education+in+Sudan.htm> [CNPC, "Support for Education in Sudan"].

⁵² The "race to the bottom" hypothesis was intuitively pleasing to many analysts and rings true for states experiencing early stages of globalization. However, overwhelming evidence suggests that manufacturing and production costs actually increase, due to poor quality control. Multinational corporations learned this the hard way in the early 1990's. Most evidence supports the idea that increased CSR adoption leads to greater profitability. For a brief overview and literature list see Daniel W. Drezner, "The Race to the Bottom Hypothesis: An Empirical and Theoretical Review" (Tufts University, The Fletcher School, December 2006), online: <www.danieldrezner.com/policy/RTBreview.doc>.

⁵³ "Nike, Inc. Corporate Responsibility Report FY07-09" (30 May 2007), online: <www.nikebiz.com/crreport/pdf>.

⁵⁴ John Micklewright & Anna Wright, "Private Donations for International Development", UNU-WIDER Discussion Paper No. 2003/82 (December 2003) at 16, online: <www.wider.unu.edu/stc/repec/pdfs/rp2003/dp2003-82.pdf>; William B. Werther, Jr. & David Chandler, *Strategic*

such as Walmart and Proctor & Gamble indicate that more corporations now recognize that investing in the domestic infrastructure and improving local quality of life improves their bottom line in the long-term.⁵⁵ Western oil companies have also recognized the benefits of following CSR norms.⁵⁶

In contemporary times, consumers have become increasingly concerned with whether companies operating in developing countries are exploiting their workers.⁵⁷ Together, these two forces have led to a rise in the CSR movement that encourages support for international development aid.⁵⁸ Participating in CSR is not only consumer-friendly, but also supportive of economic growth of the company. In encouraging the growth of stable society in the countries where they are located, multinational corporations also benefit by being able to attract better local employees.⁵⁹ CSR and human rights obligations can positively affect a company's employee recruitment and retention efforts, its reputation among various stakeholders and its legitimacy within a local community.⁶⁰ As a result, the company may "reduce employee turnover rates, increase the willingness of good employees to relocate, help avoid loss of assets or interruption of cash flow, reduce insurance risk premiums, or improve relations with the community or host government,"⁶¹ thereby decreasing spending and increasing profits. The reputational gains from participating in CSR activities within a host country can also result in increased business access and opportunities for expansion.⁶²

In summary, then, a number of factors limit the current market-based incentives for CSR compliance by CNPC. As a state-owned corporation, its exposure to market pressures is limited. CNPC's direct-to-consumer operations are limited to the Chinese domestic market, where CSR currently plays a relatively minimal role in consumer choices. Meanwhile, international consumer boycotts of national oil companies are practically difficult. However, there are signs that the market pressures on CNPC for CSR compliance will increase in the future: Chinese consumers are becoming increasingly concerned with such matters; there are some signs that the Chinese government may be increasingly sensitive to global public perceptions; and CNPC's increasing investments in developing areas such as Sudan present an inherent market incentive for initiatives consistent with CSR norms and development.

Corporate Social Responsibility: Stakeholders in a Global Environment, 2nd ed. (Thousand Oaks, CA: SAGE Publications, 2011) at 92.

⁵⁵ The Corporate Council on Africa, "Walmart Joins CCA: U.S. Corporate Giant Expanding into Africa" (16 December 2010), online: <[www.africacncl.org/\(4cqzhhm55ovjlq55azbjuhio\)/reader.aspx?viewmode=pressrelease&content_id=930bd7ad-875a-4a4c-a99e-4d5d27f213ba](http://www.africacncl.org/(4cqzhhm55ovjlq55azbjuhio)/reader.aspx?viewmode=pressrelease&content_id=930bd7ad-875a-4a4c-a99e-4d5d27f213ba)>.

⁵⁶ Peter Hulm, International Trade Centre "CSR: A Must for Big Firms in Africa" *International Trade Forum* (2007, Issue 1), online: <www.tradeforum.org/news/fullstory.php/aid/1132> (Interview with Ann Pickard, Shell Exploration and Production Africa).

⁵⁷ *Ibid.*

⁵⁸ Micklewright & Wright, *supra* note 54 at 17.

⁵⁹ Weissbrodt & Kruger, *supra* note 34 at 902.

⁶⁰ Oetzel, Getz & Ladek, *supra* note 16 at 336-337.

⁶¹ *Ibid.*

⁶² *Ibid.*

2. Domestic Regulatory and Civil Liability Regimes

Under Steinhardt's model, domestic regulatory and civil liability regimes can also motivate compliance with international standards.⁶³ These include not only regulatory and civil liabilities imposed by the law of the state of incorporation, but also liabilities that may arise in the law of the various jurisdictions in which a multinational corporation operates or invests. These regimes can only be effective if the relevant government enforces the rule of law, both enforcing regulatory requirements itself, and ensuring a functional civil litigation process. Otherwise, there is no reason why a company would be concerned about complying with unenforced local statutes and court judgments. Further, a civil liability regime is not possible unless the host government permits standing, whether statutory or otherwise, for third parties to enforce public policy, perhaps as simply as by adding a right for private parties to sue corporations for noncompliance with existing regulatory regimes, instead of relying solely on government initiative to investigate and impose penalties for noncompliance.

Similar to the market-based regimes, the current pressures for CSR compliance placed on CNPC by domestic regulatory and civil liability regimes are weak. There is little realistic chance of enforcement in China, in the jurisdictions where CNPC operates, from third party states, or by private parties. But the inherent incentive for CNPC to develop the rule of law in the places where it operates suggests that domestic regulatory and civil liability regimes could become stronger in the future.

In China, the 2006 *Company Law* requires at Art. 5 that "[w]hen undertaking business operations, a company shall comply with the laws and administrative regulations, social morality and business morality. It shall act in good faith, accept the supervision of the government and the general public, and bear social responsibilities."⁶⁴ The extent to which this imposes an enforceable obligation is contested, however: "Some scholars understand it as an exhortatory rather than mandatory provision," and in practice this is currently its effect, due to a lack of access to legal remedies.⁶⁵ Publicly traded companies in China are also subject to a *Code of Corporate Governance* that requires such companies to consider stakeholder interests including those of the community, as well as to pursue sustainable development.⁶⁶ However, given that "the Chinese legal system is notorious for the gap between the law on the books and the law in practice,"⁶⁷ and the complicity of the Chinese government in exporting weapons to Sudan in violation of United Nations

⁶³ Steinhardt, *supra* note 31 at 934-935.

⁶⁴ *Supra* note 4. See also Li-Wen Lin, "Corporate Social Responsibility in China: Window Dressing or Structural Change?" (2010) 28 (1) Berkeley J. Int'l L. 64 at 71 [Lin, "Window Dressing"]; Li-Wen Lin, "Corporate Social Accountability Standards in the Global Supply Chain: Resistance, Reconsideration, and Resolution in China" (2007) Cardozo J. Int'l & Comp. L. 321 at 359 [Lin, "Resistance"].

⁶⁵ Lin, "Window Dressing", *ibid.* at 96.

⁶⁶ Lin, "Resistance", *supra* note 64 at 359-60.

⁶⁷ Lin, "Window Dressing", *supra* note 64 at 96.

arms sanctions during the Darfur genocide,⁶⁸ relying on Chinese domestic enforcement as a route to compliance with international CSR norms is problematic. However, CSR norms are gaining a steadily more prominent place in Chinese business. Although they have not been completely implemented, the various CSR initiatives are leading to increasing levels of awareness.⁶⁹

Third party states do not offer much promise of enforcement, either. Reliance on enforcement by third party states is particularly unrealistic in the CNPC case, given the past history of the international response to genocide allegations in Sudan. Despite findings that Talisman Energy (a transnational oil company 40% owned by CNPC, traded in the United States and headquartered in Canada) was likely complicit in the 1998-1999 Darfur events, the United States and Canada declined to impose sanctions on the company and most of its equity owners, including CNPC.⁷⁰ It seems unlikely that domestic regulation of CNPC in accordance with CSR norms could arise from states other than China.

Regulatory regimes in the various jurisdictions in which a multinational corporation operates or invests are also a potential source of regulatory incentives for CSR compliance. While many of the jurisdictions in which CNPC operates—such as Sudan—may have weak regulatory regimes, particularly for complex multinational corporations such as CNPC, it is in the multinational company's interest to encourage the development of the rule of law in regions where it conducts business. The rule of law increases predictability and efficiency with respect to enforceability of contracts and protection of private property rights, including those relating to intellectual property.⁷¹ A corporation can promote rule of law by, for example, refusing to pay bribes to local government officials,⁷² complying with "well-considered" local laws,⁷³ or providing funding and training in support of rule of law efforts.⁷⁴ Once codified statutes and a consistent judicial process

⁶⁸ See the discussion on this topic above. See also Hannibal Travis, "Genocide in Sudan: The Role of Oil Exploration and the Entitlement of the Victims to Reparations" (2008) 25 Ariz. J. Int'l & Comp. L. 1 at 50-51.

⁶⁹ Lin, "Window Dressing", *supra* note 64 at 100.

⁷⁰ Travis, *supra* note 68 at 44-45.

⁷¹ Robert McCorquodale, "Business, the International Rule of Law and Human Rights" in McCorquodale, ed., *The Rule of Law in International and Comparative Context* (London: British Institute of International and Comparative Law, 2010) 27 at 35-36, citing among others Allan Gerson, "Peace Building: The Private Sector's Role" (2001) 95 Am. J. Int'l L. 101 at 111 (the rule of law is critical for "securing investment, defining property rights, forming contracts, and preventing default on debts, and otherwise to aid in reducing the avoidable risks of investment."). See also "How the Private Sector Can Promote the Rule of Law - The General Counsel Perspective" *Metropolitan Corporate Counsel* (May 2006) 38, online: <www.metrocorpounsel.com/pdf/2006/May/38.pdf> ["Private Sector Can Promote the Rule of Law"].

⁷² Timothy L. Fort & Cindy A. Schipani, "An Action Plan for the Role of Business in Fostering Peace" (2007) 44 Am. Bus. L.J. 359 at 366.

⁷³ Donald O. Mayer, "Corporate Governance in the Cause of Peace: An Environmental Perspective" (2002) 35 Vand. J. Transnat'l L. 585 at 603.

⁷⁴ "CEELI, the Rule of Law and The Corporate Role" *Metropolitan Corporate Counsel* (May 2006) 50, online: <<http://www.metrocorpounsel.com/pdf/2006/May/25.pdf>>.

exist, a company is then obliged to abide by the local legal system when doing business in a host country.⁷⁵ Additionally, supporting rule of law is part of many existing CSR instruments, such as the *Voluntary Principles on Security and Human Rights* (VPs),⁷⁶ and is implicit in the anti-corruption principle of the United Nations *Global Compact*.⁷⁷

3. International Regulatory and Quasi-Regulatory Regimes

Finally, through processes of acculturation in the international CSR community, participation in international regulatory and quasi-regulatory schemes can also directly motivate compliance with CSR norms. These include the *Social Accountability 8000* protocol (SA8000),⁷⁸ the VPs, the UN *Global Compact*, the *Sustainability Reporting Guidelines* (SRG),⁷⁹ and the *Oil and Gas Industry Guidance on Voluntary Sustainability Reporting* (GVSR).⁸⁰ Although none of these instruments are legally binding in an enforceable way, by providing voluntary and public standards, they help to build a normative community among multinational corporations. They also enable increased market pressures for CSR compliance, by making it possible for a company's CSR policies to be evaluated objectively with a standards-based qualification that consumers and investors can rely on—a consistent reporting mechanism allowing for an “apples to apples” comparison between companies. In addition, compliance with reporting standards built into the *Global Compact* and similar regimes provides additional information to the market about a company's commitment to sustainable business. With the third-party confirmation available through regulatory and quasi-regulatory schemes, consumers and investors can reward compliant companies through market investment.

CNPC learned this lesson during its attempted public stock offering, which could not be completed because of allegations of noncompliance with human rights standards.⁸¹ Instead, CNPC was forced to restructure the offering through the creation of PetroChina, which was offered with promises that funds raised would not be used in Sudan.⁸² Going forward,

⁷⁵ “Private Sector Can Promote the Rule of Law”, *supra* note 71 at 38.

⁷⁶ (December 2000), online: <www.voluntaryprinciples.org/files/voluntary_principles_english.pdf> (One section of the principles speaks to “Interactions Between Companies and Public Security”).

⁷⁷ (26 July 2000), online: <www.unglobalcompact.org/AboutTheGC/TheTenPrinciples/index.html> (Principle 10 is that “Businesses should work against corruption in all its forms, including extortion and bribery.”).

⁷⁸ Social Accountability International, *Social Accountability 8000* (2008), online: <www.sa-intl.org/_data/n_0001/resources/live/2008StdEnglishFinal.pdf>.

⁷⁹ Global Reporting Initiative, *Sustainability Reporting Guidelines* (2006), online: <www.globalreporting.org/NR/rdonlyres/A1FB5501-B0DE-4B69-A900-27DD8A4C2839/0/G3_GuidelinesENG.pdf>.

⁸⁰ International Petroleum Industry Environmental Conservation Association (IPIECA), American Petroleum Institute (API) & International Association of Oil and Gas Producers (OGP), *Oil and Gas Industry Guidance on Voluntary Sustainability Reporting*, 2nd ed. (December 2010), online: <www.api.org/ehs/performance/upload/voluntary_sustainability_reporting_guidance_2010.pdf>.

⁸¹ Goodman, *supra* note 22.

⁸² *Ibid.*

CNPC could be well served in the global marketplace by adhering to externally-created CSR standards. These international regulatory and quasi-regulatory regimes can impose strong incentives for compliance. Given its controversial past, a commitment to internationally-recognized norms could reform CNPC's image to that of a socially responsible company. The Sudan issue remains significant enough for China's leaders and CNPC that they have a strong incentive from international regulatory regimes to show themselves as being increasingly responsible in their investment and development projects in Sudan. While it is possible that international public backlash against China's initial activities in Sudan may simply be a detour, it is more likely that the continued longevity of the issue provides the necessary stimulus for greater CSR. Furthermore, with the increased focus on Sudan's bid for WTO membership, CNPC will find it difficult to decrease its CSR efforts without significant political capital loss to the CCP.

The review of Steinhardt's four potential regimes for motivating compliance with human rights and CSR standards has demonstrated that these regimes do not exert equal pressure in CNPC's case. While the market argument will clearly be an issue of increasing significance for CNPC in the future, particularly as seen in the PetroChina stock offering concerns, at the current time neither the market-based regime nor the pressures exerted by regulatory and liability regimes are a significant force for CSR compliance. Moving forward, it may be more useful to consider CNPC's motivations for CSR compliance within the framework of CNPC's concern regarding public perception: a concern that can perhaps be addressed via voluntary participation in international quasi-regulatory compliance regimes. The external market pressures that encourage CSR compliance—which will only grow more salient in the future as Sudan continues to seek accession to the World Trade Organization and further recognition on the world stage—coincide with internal pressures within the CNPC to subject it to the sanctioning effects of international norms.⁸³

III. Available CSR Norms that Can be Implemented by CNPC

CNPC can draw on a number of private and semi-public initiatives to guide its CSR programs. Purely private initiatives have grown out of broad efforts between a large number of diverse commercial enterprises, or cooperation within specific industries. International organizations like the UN have also weighed in with multilateral suggestions that partially reflect input from non-governmental interests, such as the UN *Global Compact* described below. Private corporations can also take their CSR cues from international development programs created by the public and non-governmental organization sectors, particularly in the form of the Millennium Development Goals which, as discussed below, were promulgated with the idea that private industry can and should be involved

⁸³ Victor Mosoti, "The Legal Implications of Sudan's Accession to the World Trade Organization" (2004) 103 *African Affairs* 269.

in pursuing development activities. The availability of *SA8000*, the *VPs*, and the *Global Compact* provides a framework for CNPC's CSR efforts by concretely defining the principles CNPC can adopt in order to demonstrate its commitment to the idea of sustainable business. These are existing norms that can potentially provide guidance to CNPC's CSR implementations, but each must be evaluated to their applicability and practicality for CNPC.

The *SA8000* protocol is a private initiative that uses international human rights norms and labour laws to create an auditable international standard for companies. The standard was created by Social Accountability International, a non-governmental organization advised by a broad range of stakeholders from trade unions, other non-governmental organizations, government representatives and business members.⁸⁴ Participation in *SA8000* is voluntary and can take the form of certification via independent auditing against the protocol, or participation in the "Corporate Program," which is intended to assist companies with implementation of *SA8000* principles in company operations.⁸⁵ Certification in accordance with *SA8000* is a distinguishing characteristic that allows consumers and others to easily identify human rights compliance by a subject company.⁸⁶ The Corporate Program gives member companies access to resources that can enable it to better understand and more effectively integrate *SA8000* into corporate policies.⁸⁷ In addition, Social Accountability International offers relevant training programs to support CSR programs in compliance with *SA8000*.⁸⁸

A company that chooses to comply with *SA8000* has the ability to show third parties that its concern for workers' rights and workplace conditions meets certain minimum standards drawn from such sources as the *Universal Declaration of Human Rights* and the various conventions of the International Labour Organization.⁸⁹ *SA8000* is applicable to companies of all sizes, locations and industries,⁹⁰ and addresses issues relating to child labour, forced and compulsory labour, health and safety, freedom of association, discrimination, disciplinary practices, working hours, remuneration, and management systems.⁹¹ While there are only 18 member companies at this time, and no member companies from the energy sector,⁹² over 2400 facilities

⁸⁴ Social Accountability International, "About Us", online: <<http://www.sa-intl.org/index.cfm?fuseaction=Page.viewPage&pageId=472>>; Social Accountability International, "Who We Are: SAI Advisory Board", online: <<http://www.sa-intl.org/index.cfm?fuseaction=Page.viewPage&pageId=494&grandparentID=472&parentID=490>>.

⁸⁵ Social Accountability International, "SA80000 Certification", online: <<http://www.sa-intl.org/index.cfm?fuseaction=Page.viewPage&pageId=617&parentID=473>> [SAI, "SA8000 Certification"].

⁸⁶ Steinhardt, *supra* note 31 at 941.

⁸⁷ SAI, "SA8000 Certification", *supra* note 85.

⁸⁸ See Social Accountability International, "SAI Training Programs", online: <<http://www.sa-intl.org/index.cfm?fuseaction=Page.viewPage&pageId=553&parentID=473&nodeID=1>>.

⁸⁹ *SA8000*, *supra* note 78 at 4.

⁹⁰ *Ibid.*

⁹¹ *Ibid.* at 3.

⁹² Social Accountability International, "Member Companies", online: <<http://www.sa-intl.org/index.cfm?fuseaction=Page.viewPage&pageId=906&parentID=478&nodeID=1>>.

have been certified in compliance with *SA8000* as of the end of 2010, including 37 facilities classified as part of the energy industry.⁹³

While the lack of participation from companies in CNPC's sector suggests that the *SA8000* principles may not be adequately tailored to CNPC's needs, there would be great reputational gains from "getting in on the ground floor" with this initiative. Even though oil companies have not embraced the *SA8000* initiative, CNPC may find the *SA8000* protocol useful because there are available resources for implementation, because it is a compilation of multiple workers' rights standards, and because it is objectively auditable for compliance.

On the other hand, there are CSR initiatives more specifically tailored to CNPC's needs. The *VPs* are a CSR standard specific to the extractive and energy sector.⁹⁴ Created by a consortium of governments, extractive/energy sector corporations and non-governmental organizations, the *VPs* are intended to address human rights specifically and CSR generally, and provide guidelines for discussing, promoting and protecting human rights interests through the activities of a range of stakeholders.⁹⁵ The *VPs* acknowledge the varying roles and responsibilities of government and corporate stakeholders with respect to human rights, as well as the potential impact of non-governmental organizations and other, less formal interest groups.⁹⁶ Corporate adherents of the *VPs* are expected to work in conjunction with host governments to ensure law and order, as well as security for government, corporations and private citizens.⁹⁷

Primary responsibility belongs to governments, which are responsible under the *VPs* to maintain rule of law in accordance with international human rights standards.⁹⁸ However, companies that adopt the *VPs* are expected to support local authorities in complying with the standards, and to work to mitigate potential human rights abuses. As an example, adopting companies are meant to promote three principles in their use of private security:

- (a) not employ individuals credibly implicated in human rights abuses to provide security services; (b) use force only when strictly necessary and to an extent proportional to the threat; and (c) not violate the rights of individuals while exercising the right to exercise freedom of association and peaceful assembly, to engage in collective bargaining, or other related rights of Company employees as recognized by the *Universal Declaration of Human Rights* and the *ILO Declaration on Fundamental Principles and Rights at Work*.⁹⁹

In addition to encouraging policies that further compliance with relevant international norms, the *VPs* also require companies to actively monitor and

⁹³ Social Accountability International, "SA8000 Certified Facilities: As of December 31st, 2010", online: <http://www.saasaccreditation.org/certfaclists/2010_Q4/Q4%20Certs%20List/%20Public%20List.xls>.

⁹⁴ *VPs*, *supra* note 76, "Introduction".

⁹⁵ *Ibid.*

⁹⁶ *Ibid.*

⁹⁷ *Ibid.*

⁹⁸ *Ibid.*

⁹⁹ *Ibid.*, "Interactions between Companies and Private Security".

report human rights abuses to government authorities, to proactively prevent future human rights abuses by pressuring local government to investigate and take action when violations do occur, and to ensure that company-provided equipment is not used in the violation of human rights.¹⁰⁰ Equipment in this context refers to the tools provided to security forces, including lethal and non-lethal weapons.¹⁰¹ Companies providing equipment are required under the VPs to comply with relevant law with respect to the equipment and to mitigate any potential human rights abuses that may occur if the equipment is misappropriated or diverted in transport.¹⁰² When a host country is unable to satisfactorily protect human rights, the VPs call on companies to engage private security forces to act as local police, subject to the same principles that apply to official government forces.¹⁰³

The VPs are especially important because they reflect a broad consensus of industrialized countries, influential non-governmental organizations, and leading multinational corporations participating in the extractive and energy sectors (including such companies as BP, Chevron, ConocoPhillips, ExxonMobil, Hess Corporation, Marathon Oil, Occidental Petroleum Corporation, Shell and Statoil).¹⁰⁴ The two-pronged approach of the VPs, addressing both the needs of private industry in protecting their operations and the "human rights and fundamental freedoms" of local communities, speaks to commercial and individual interests.¹⁰⁵ For a company to be recognized as a participant, it must implement the VPs in a transparent manner and engage in dialogue to further the goals of the VPs with other governmental, non-governmental and corporate participants.¹⁰⁶ Therefore, a participant of the VPs not only maintains the ability to protect its interests in a host country, but it can do so within an internationally recognized framework and community dedicated to furthering both security concerns and human rights within the context of the energy sector.

The special tailoring of the VPs to the energy sector's specific operations could be especially useful to CNPC. But for CNPC, compliance with the VPs may be problematic given the allegations of its participation in the Sudanese government abuses described above. The focus on providing and supporting security services in compliance with human rights standards is a particular concern because true fulfillment of the VPs by CNPC would require it to proactively address the ongoing human rights violations in Darfur. CNPC could no longer hide behind a division between its actions and the actions of the Chinese government directly, nor could it claim compliance with the VPs merely through examination of its internal policies: the VPs implore

¹⁰⁰ *Ibid.*

¹⁰¹ *Ibid.*, "Risk Assessment".

¹⁰² *Ibid.*

¹⁰³ *Ibid.*, "Interactions between Companies and Private Security".

¹⁰⁴ International Business Leaders Forum & Business for Social Responsibility, "Participants", online: Voluntary Principles <www.voluntaryprinciples.org/participants/>.

¹⁰⁵ International Business Leaders Forum & Business for Social Responsibility, "Amendments Approved at VPs 2009 Oslo Plenary" (May 2009), online: <www.voluntaryprinciples.org/files/vp_amendments_200905.pdf>.

¹⁰⁶ *Ibid.* at 1-2.

companies to influence the activities of external actors. However, given that the VPs have been adopted by a range of leaders in the energy industry, CNPC should strongly consider compliance with the standards in order to gain increased legitimacy in global markets.

Beyond generally private international initiatives like *SA8000* and the VPs, the UN has spearheaded the *Global Compact*, which collects “universally accepted principles” for the sustainable conduct of business in an increasingly globalized world.¹⁰⁷ The principles speak to support of human rights, compliance with labour standards, environmental responsibility and anti-corruption efforts.¹⁰⁸ The human rights principles, like *SA8000* and the VPs described above, draw from the *Universal Declaration of Human Rights* to guarantee individual rights to equality, life, and security, as well as personal, economic, social and cultural freedom.¹⁰⁹ The labour standards follow the ILO *Declaration of Fundamental Principles and Rights at Work*, which addresses worker rights to unionize, as well as the elimination of forced labour, child labour, and discriminatory employment practices.¹¹⁰ The environmental responsibility standards are intended to promote public-private cooperation through the types of partnerships encouraged by the UN Environment Programme’s existing environmental law initiatives, and in compliance with the goals set forth in the multiple existing treaties for environmental protection.¹¹¹ Finally, the anti-corruption principle speaks to the rule of law issues that can undermine sustainable development, with a focus on why controlling corruption is beneficial from both an ethical and a business stance.¹¹²

Corporate participation in the *Global Compact* is voluntary. It requires only a written letter of commitment from a company’s Chief Executive Officer and an annual financial contribution in support of *Global Compact* initiatives, with a suggested amount based on the company’s annual sales/revenues.¹¹³ Participating companies are expected to incorporate the guiding principles of the *Global Compact* into all levels of their regular business processes, provide aid towards fulfillment of development goals including the Millennium Development Goals, and publicize and advocate compliance with the *Global Compact*.¹¹⁴ In return, the company receives the benefit of an established, recognized CSR framework, the ability to participate in a community of like-minded stakeholders engaged in pursuing similar objectives, and access to resources to support sustainable development efforts.¹¹⁵

¹⁰⁷ United Nations, “Overview of the UN Global Compact” (30 April 2011), online: <<http://www.unglobalcompact.org/AboutTheGC/>>.

¹⁰⁸ *Global Compact*, *supra* note 77.

¹⁰⁹ *Ibid.*, “Human Rights”.

¹¹⁰ *Ibid.*, “Labour”.

¹¹¹ *Ibid.*, “Environment”.

¹¹² *Ibid.*, “Transparency and Anti-corruption”.

¹¹³ United Nations *Global Compact*, “Business Participation”, online:

<http://www.unglobalcompact.org/HowToParticipate/Business_Participation/index.html>.

¹¹⁴ *Ibid.*

¹¹⁵ *Ibid.*

The Communication on Progress produced by each participating company on an annual basis is a continuing assertion of intent to comply with the *Global Compact*, a description of activities in support of the *Global Compact* principles, and an assessment of the success of these activities.¹¹⁶ As of 23 May 2011, there were 114 global oil producers participating in the *Global Compact* and filing Communications on Progress.¹¹⁷ While the *Global Compact* claims that it is the world's largest corporate citizenship and sustainability initiative,¹¹⁸ CNPC is not included on the participant list. However, according to the UN, over 100 business participants in China are currently compliant with *Global Compact* requirements in terms of filing Communications on Progress, including China Power Investment Corporation, China Petroleum & Chemical Corporation (Sinopec), and PetroChina Company Limited.¹¹⁹

Since PetroChina participates in the *Global Compact*, CNPC, as controlling shareholder of PetroChina, apparently does not have any objection to participation.¹²⁰ There are few limitations on the types of entities that can participate in the *Global Compact*: the UN does not specify that only certain types of businesses may commit¹²¹ and also permits public sector organizations¹²² and cities¹²³ as stakeholders. CNPC cannot use its state-owned enterprise status as an excuse for not committing to the *Global Compact*. Indeed, SASAC itself could potentially become a participant, bound by the *Global Compact* principles for all of the state-owned enterprises that it operates. There appears to be little reason for CNPC to not join the *Global Compact*.

¹¹⁶ United Nations *Global Compact*, "Progress and Disclosure" (25 February 2011), online: <www.unglobalcompact.org/COP/index.html>.

¹¹⁷ See United Nations *Global Compact*, "Participant Search", online: <www.unglobalcompact.org/participants/search>.

¹¹⁸ United Nations *Global Compact*, "Participants and Stakeholders: UN Global Compact Participants" (30 June 2009), online: <www.unglobalcompact.org/ParticipantsAndStakeholders/index.html>.

¹¹⁹ See United Nations *Global Compact*, "Participant Search", *supra* note 117.

¹²⁰ It is important to note while CNPC originally excluded overseas investments from PetroChina, the latter now participates in international oil and energy investments. See, for example, its recent investment in a large-scale Canadian natural gas project: PetroChina, "PetroChina to Acquire 50 Percent Interest in Encana's Cutbank Ridge Business Assets for C\$5.4 Billion" (10 February 2011), online: <[www.petrochina.com.cn/Ptr/News_and_Bulletin/News_Release/PetroChina_to_Acquire_50_Percent_Interest_in_Encana_s_Cutbank_Ridge_Business_Assets_for_C\\$5.4_Billio.htm](http://www.petrochina.com.cn/Ptr/News_and_Bulletin/News_Release/PetroChina_to_Acquire_50_Percent_Interest_in_Encana_s_Cutbank_Ridge_Business_Assets_for_C$5.4_Billio.htm)>.

¹²¹ See United Nations *Global Compact*, "Business Participation", *supra* note 113.

¹²² United Nations *Global Compact*, "Participants and Stakeholders: Public Sector Organizations", online: <http://www.unglobalcompact.org/ParticipantsAndStakeholders/public_sector.html>.

¹²³ *Ibid.*, "Participants and Stakeholders: Cities", online: <www.unglobalcompact.org/ParticipantsAndStakeholders/cities.html>.

IV. How CNPC Could Comply with International CSR Norms

CNPC can benefit from the ongoing evolution of CSR norms that seek to expand the relationship between states and corporations in promoting human rights. As these norms grow, CNPC does not need to take a one-size-fits-all approach but can look at specific areas of relevance in the host states.

The principles contained in the *VPs* and the *Global Compact* are general, so CNPC may find it useful to look to international development regimes for practical guidance on implementation of business operations in a socially responsible manner. The connection between development and human rights is supported by the World Bank's role as a development financing institution¹²⁴ with a primary goal of carrying out the Millennium Development Goals (MDGs).¹²⁵ As described above, CSR initiatives such as the *Global Compact* are also concerned with the fulfillment of the MDGs. The MDGs are

...the world's time-bound and quantified targets for addressing extreme poverty in its many dimensions—income poverty, hunger, disease, lack of adequate shelter, and exclusion—while promoting gender equality, education, and environmental sustainability. They are also basic human rights—the rights of each person on the planet to health, education, shelter, and security as pledged in the *Universal Declaration of Human Rights* and the *UN Millennium Declaration*.¹²⁶

Implementing the MDGs is not merely a task for governments; the private sector is explicitly expected to provide resources in support of the goals.¹²⁷ Jeffrey Sachs, who directed the UN Millennium Project that promulgated the MDGs,¹²⁸ has argued that the private sector should contribute to business development, as well as invest in health, education and nutrition as a complement to public development efforts.¹²⁹

To this end, the various guidelines associated with the MDGs provide private sector organizations with a rich source of practical steps toward the implementation of the kind of goals that provide the basis for CSR principles. In order to meet the MDGs, the UN has called on the private sector to partner with other international organizations to form development strategies.¹³⁰ The UN also has requested the private sector to provide funding

¹²⁴ World Bank Group, "About Us" (4 October 2010), online:

<<http://go.worldbank.org/3QT2P1GNH0>>.

¹²⁵ *Ibid.*, "About Us: The Challenge", online: <<http://go.worldbank.org/DM4A38OWJ0>>.

¹²⁶ UN Millennium Project, *Investing in Development: A Practical Plan to Achieve the Millennium Development Goals* (New York: United Nations Development Programme, 2005), online: <<http://www.unmillenniumproject.org/documents/MainReportComplete-lowres.pdf>>.

¹²⁷ See *ibid.* at xix (Target 18 of the MDGs is to, "in cooperation with the private sector, make available the benefits of new technologies, especially information and communications technologies." This Target is part of Goal 8, "Develop a global partnership for development").

¹²⁸ *Ibid.* at inside cover.

¹²⁹ Jeffrey D. Sachs, *The End of Poverty: Economic Possibilities of Our Time* (New York: Penguin, 2006) at 252.

¹³⁰ *Supra* note 127; UN Department of Public Information, "Goal 8: Develop a Global Partnership

to meet shortfalls in official development assistance from current donor countries.¹³¹ Therefore, partnerships encouraged for the purposes of pursuing the MDGs are not limited to those between developed and developing states or between developing states and non-governmental organizations.¹³² Corporations can participate in providing access to health and education and developing infrastructure and services.¹³³ Their expertise is also invaluable for facilitating technology transfer, research and development, as well as research and development addressed at prevention and treatment of infectious disease.¹³⁴

Private actors should participate in the pursuit of the MDGs for both moral reasons¹³⁵ and business reasons, as discussed above. Like CSR's intended results, development offers market-oriented incentives—it increases the wealth of potential customers,¹³⁶ stabilizes the health and social environment of potential workers, and promotes a transparent, functional, and less corrupt government marked by rule of law.

There are a variety of ways in which the private sector can use efforts to advance the MDGs to provide an overarching framework for CSR initiatives. Four areas of corporate activity have been suggested by the World Economic Forum's Global Governance Initiatives: core business activity, public-private partnerships, philanthropy, and advocacy.¹³⁷ Even without actively participating in development, a company can further the MDGs simply by doing business in a sustainable manner, such as by following the practices described in the Global Compact outlined above.¹³⁸ Second, the partnerships between private actors and governmental or non-governmental entities that the UN encourages as part of fulfilling the MDGs permit development initiatives to take advantage of business resources and skills for goods and services development, as well as business funds to apply towards facilities

for Development" DPI/2517 N (September 2008), online: <<http://www.un.org/millenniumgoals/2008highlevel/pdf/newsroom/Goal%208%20FINAL.pdf>>.

¹³¹ UN Department of Public Information, *ibid.* at 1-2.

¹³² *Ibid.* at 2.

¹³³ *Ibid.*

¹³⁴ *Ibid.*

¹³⁵ Although private actors may also note the difficulty of defining morality, particularly when attempting to determine moral standards across cultural divides. See Norman Bowie, "New Directions in Corporate Social Responsibility; Moral Pluralism and Social Responsibility" (1991) 34 Bus. Horizons 56 at 63 (describing moral pluralism as the disagreement among people regarding what is right and wrong); Lawrence E. Mitchell & Theresa A. Gabaldon, "What Are the Ways of Achieving Corporate Social Responsibility?: If I Only Had a Heart: Or, How We Can Identify a Corporate Morality" (2002) 76 Tul. L. Rev. 1645 (acknowledging the problems with defining morality and arguing for a definition of "basic goodness" that can be found among people of similar cultural background).

¹³⁶ The first MDG is to eradicate extreme poverty and hunger, including by decreasing by half the number of people living under \$1 per day and achieving full and productive employment for all people. United Nations, "Goal 1: Eradicate Extreme Poverty & Hunger", online: <<http://www.un.org/millenniumgoals/poverty.shtml>>. Increased income will permit potential customers to spend beyond subsistence needs.

¹³⁷ Lisa Dreier, "Case Study: World Economic Forum – Business Partnerships for the MDGs" *Alliance* (1 September 2005) 31-32.

¹³⁸ *Ibid* at 31.

construction.¹³⁹ Third, philanthropy is not limited to individual donations, but can include corporate activity. As suggested by the UN, corporate grants can fill funding gaps to support both public-private partnership activity and infrastructure and capacity-building.¹⁴⁰ Finally, corporate advocacy plays an important role by raising awareness and support for policies that further the MDGs.¹⁴¹

For practical guidance on how to comply with international obligations under the SA8000 standard, the VPs, the *Global Compact* and various reporting guidelines described above, CNPC can adopt the MDGs as a set of concrete targets for its sustainable business goals. It can then consider how other entities pursue MDGs and similar development initiatives. By adjusting its core business policies in accordance with the *Global Compact*, as well as the VPs, CNPC would be able to conduct sustainable business simply in the course of its everyday operations. The *Global Compact* principles do not speak to specifics in implementation, but their integration into policy is still important because they can control the direction of decision-making within a company by changing its core business culture.

CNPC claims that its Sudan programs already include partnerships with local hospitals, orphanages and schools, as well as financial support for governmental projects.¹⁴² If that is the case, then CNPC should extend these programs by continuing to engage in public-private partnerships. Public-private partnerships in general present opportunities for development initiatives to meet local priorities, increased accountability to stakeholders, and the potential to create sustained development continuing after the partnership ends. Further, public-private partnerships are a useful tool to align private efforts with public objectives. In light of general uncertainty that corporate programs are successful in meeting development goals,¹⁴³ CNPC should also consider expanding its development programs to formal partnerships with non-governmental agencies present in Sudan and focusing on addressing poverty and other aspects of the MDGs. Funneling CSR funding through such agencies and through public entities on the ground, instead of duplicating efforts, can enable CNPC to take advantage of their existing expertise and to support current programs that are already successful. Such partnerships are closely connected to the philanthropic activities suggested in the Global Governance Initiative. Rather than participating in specific development and CSR activities, CNPC can simply adjust its core business practices and provide funds to other entities providing on the ground development and human rights support. However, CNPC needs to manage the risk that the Sudanese government may disapprove of the activities of those non-governmental agencies and, if CNPC affiliates itself with those agencies, the Sudanese government may

¹³⁹ *Ibid.*

¹⁴⁰ *Ibid.* at 31-32.

¹⁴¹ *Ibid.* at 32.

¹⁴² CNPC, "Support for Education in Sudan", *supra* note 51.

¹⁴³ Frynas, *supra* note 17 at 279.

remove or restrict CNPC's rights to conduct its oil business within the country. If it seeks to remain involved in Sudan, which surely it does, CNPC must walk a tightrope between cooperating with local government demands and upholding CSR principles.

Finally, CNPC needs to increase its corporate advocacy efforts if it is to meet the Global Governance Initiatives. Participating in advocacy for pursuit of the MDGs aligns with the VPs and their requirements that companies promote human rights and workers' rights.¹⁴⁴ This prong is an especially important commitment for CNPC to make because of the existing allegations with respect to its activities in Sudan. By restructuring its planned public stock offering, CNPC was able to sidestep direct protests regarding its involvement in human rights abuses,¹⁴⁵ but it will continue to face market resistance until it publicly speaks out in favor of socially responsible practices. That is, CNPC could benefit from being more openly verbal in its diplomatic efforts to promote socially responsible practices and rule of law by host country governments. Participation in CSR programs that meet the standards of international organizations and the most responsible multinational corporations, including their commitments to influence host government attitudes, can be an effective way for CNPC to show its commitment to sustainable business practices.

CNPC should implement similar policies, both for the development projects it funds, and for those it participates in directly as part of its CSR program. Its initiatives should not be used as an opportunity to support related or favored businesses, but rather should be open to a transparent, competitive bidding process. In addition, CNPC might consider using its development-related projects as a way to encourage local business development, a strategy that can ultimately benefit the broader local community beyond the discrete goals of a project. The bidding process for these projects should be designed to combat fraud and corruption; at the same time, CNPC needs to be careful not to permit suppliers with a reputation for or history of fraud and corruption to participate in its projects. It should perform due diligence on all potential suppliers—examining their operational policies, and management and ownership structures, to ensure that they are not engaged in fraudulent or corrupt activities. CNPC should also ensure that suppliers comply with the standards of responsible business that CNPC adopts for itself. It needs to be especially mindful in its dealings with the Sudanese government, and may find it wise to use SASAC to put operational distance between itself and the official actions of the Chinese government with respect to Sudan.

In addition to adopting relevant norms, CNPC needs to be transparent about its progress towards compliance. It is not enough to adopt CSR policies; CNPC must also show what it is (and is not) doing in pursuit of those goals. Otherwise, CNPC's claimed efforts will not be visible to investors and consumers for their independent examination and critique. To

¹⁴⁴ VPs, *supra* note 76, "Interactions between Companies and Public Security".

¹⁴⁵ Goodman, *supra* note 22.

this end, CNPC has released Corporate Social Responsibility Reports since 2006.¹⁴⁶ The 2008 report includes a stated mission of pursuing sustainable development,¹⁴⁷ and addresses environmental protection, employee rights, poverty alleviation and education support among its topics.¹⁴⁸

CNPC's Reports are putatively produced in compliance with the guidelines set out in the SRG and the GVSR.¹⁴⁹ However, neither the SRG nor the GVSR provide specific, substantive rules or principles that a company should adhere to; instead they are reporting guidelines, intended to assist companies with being transparent about their sustainability efforts. Therefore, it is difficult to determine the usefulness of CNPC's self-reporting.

The SRG are issued by the Global Reporting Initiative as part of a reporting framework for economic, environmental and social performance. They provide a comprehensive outline of the types of information that a company should disclose with respect to sustainability initiatives, including background information about the company and an assessment of its success in meeting economic, environmental, labor, human rights, society and product responsibility performance indicators.¹⁵⁰

The GVSR is issued by three trade associations: the International Petroleum Industry Environmental Conservation Association, the American Petroleum Institute, and the International Association of Oil and Gas Producers. It is an industry-specific guideline for reporting on environmental, health and safety, social and economic performance,¹⁵¹ but it is explicitly voluntary and disclaims status as an industry standard for compliance with any reporting requirements.¹⁵²

By using the SRG and the GVSR, CNPC therefore is not avoiding reporting on its sustainability initiatives and compliance with various human rights, labor, and environmental norms. However, self-reporting alone only reflects a company's self-analysis of its current programs. It does not provide an independent source of analysis, and it does not provide a standard to which the company should aspire in its future activities. In order to show its commitment to international norms, CNPC should consider opening itself to third party auditing under SA8000, or explicitly adopting the external obligations created by the VPs and the *Global Compact*.

¹⁴⁶ China National Petroleum Corporation, "Corporate Social Responsibility Report 2008", inside cover, online: <www.cnpc.com.cn/Resource/english/images1/pdf/08%20CSR%20Report/CSR%20Report%202008.pdf>.

¹⁴⁷ *Ibid.* at 6.

¹⁴⁸ *Ibid.* at 1.

¹⁴⁹ *Ibid.*, inside cover. See *Sustainability Reporting Guidelines*, *supra* note 79; *Oil and Gas Industry Guidance on Voluntary Sustainability Reporting*, *supra* note 80.

¹⁵⁰ SRG, *ibid.* at 19-36.

¹⁵¹ GVSR, *supra* note 80 at para. 1.1.

¹⁵² *Ibid.* at para. 1.5.

V. Conclusion: The Next Steps for CNPC

CSR is an area of global governance that is rapidly evolving. Developments occurring shortly before this article went to press include the UN Guiding Principles on Business and Human Rights, which articulate an integrated system of government and corporate efforts to assure implementation and enforcement of human rights regimes.¹⁵³ The Guiding Principles are intended to collect existing practices and norms and place them into a single context so that they can be analyzed as a whole, thereby offering guidance for implementation in individual, fact-specific situations. CNPC can use a similar approach in evaluating its CSR approach and determining how it should proceed.¹⁵⁴ CNPC must take into account its own unique pressures, including internal corporate goals and state influence, in order to decide the extent to which a CSR regime would be beneficial to its organization and in what way that sort of regime could be implemented.

CNPC should not merely look to international legal norms for guidelines on what to do and how to do it; it should also engage in partnerships that can take advantage of expertise and experience of organizations already on the ground. The communities of like-minded corporations and other entities that exist as part of the VPs, the *Global Compact* and the MDGs can be a resource for CNPC to locate opportunities for public-private partnerships and relationships with other private or non-governmental organizations engaged in human rights compliance and development aid. Participating in communities of interest surrounding CSR will provide CNPC with practical support as well as enhance its reputation as a counterpart to leading multinational corporations.

While CNPC is technically a state-owned enterprise, if the Chinese government and SASAC intend to show that they are capable of operating the company as a private enterprise responding to economic and not political drivers, then CNPC should be operated in compliance with international legal norms with respect to CSR and related concepts. Ultimately, CNPC needs to frame its activity in foreign countries in terms of compliance with international rules and norms even if it is not formally bound to those obligations. Even if all it does is "talk the talk" of a responsible, globalized corporation observing human rights and development best practices, it will eventually begin to "walk the talk." By making statements about acting or planning to act in a certain way, CNPC creates a social expectation that it will actually follow through on its claims—and such expectations can eventually become, effectively, obligations for corporations. If CNPC wants to compete

¹⁵³ Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and other Business Enterprises, John Ruggie, "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework" (21 March 2011) UN Doc. No. A/HRC/17/31, online: <www.ohchr.org/Documents/Issues/Business/A-HRC-17-31_AEV.pdf>.

¹⁵⁴ *Ibid.* at 5.

on the world stage, then it must comply with its assertions regarding how it will act in the future or risk being dismissed as merely parroting the language of CSR without taking on the work such policies require. Participation in existing international compliance regimes will require CNPC to increase transparency levels to allow the public to assess CNPC's progress towards meeting international rules and norms. In addition, schemes such as the *VPs* and the *Global Compact* will give CNPC a support structure and community within which it can increase compliance with relevant norms.

Even if CNPC does not voluntarily assume membership in these non-binding international normative communities, there is an argument that international legal norms may have an influence over CNPC's operations: through China's accession to treaties, through industry/commercial norms that become *de facto* standards required for doing business in the oil and gas industry, or even through specific contractual obligations. As long as CNPC remains owned by the Chinese government, it will be subject to more scrutiny under traditional international "hard" law than purely private multinationals, because at least in the sphere of public perception (if not clearly in the legal sphere) its actions can be considered the actions of the Chinese state. Further, merely by being present in developing countries, CNPC will necessarily face the inter-related problems of governance, under-development, and poverty currently present in such countries, and may be forced to become involved in order to support and protect its business activities. It cannot do business in a vacuum and must acknowledge the role its presence can and should play. In the end, CNPC benefits by voluntarily conducting itself to the level of states' obligations under international law—particularly international human rights law—because doing so increases the legitimacy of the company as a member of the international business community and increases certainty in its business operations, both as an employer and as a contractual party.