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Prita Amalia
Padjajaran University

M. Lazuardy Thariq Makmun
Padjajaran University

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MULTINATIONAL CORPORATIONS' INVESTMENTS MADE THROUGH ITS SUBSIDIARIES UNDER THE LATEST GENERATION OF INVESTMENT TREATIES

Prita Amalia & Muhammad Lazuardy Thariq Makmun

Faculty of Law, Padjajaran University, Indonesia
Correspondence: lazuardythariq@gmail.com

Abstract

Multinational corporations (MNC) influence and contribution to the world's economic development, particularly in the realm of international investment, is vast and inevitable. The way MNC utilizes its subsidiaries, however, has posed an issue for host States specifically in relation to the series of ISDS claims faced by host States, when the structure of the MNC's investment enables them to go treaty shopping. It is understood that there is a causality between the broad definition of investment and investor contained in the older generation of BITs toward these series of claims. It is also more often than not, in the case of an investment made through a subsidiary company, arbitral tribunals will accept such investment as an investment protected under the relevant BIT due to how investment and investor are defined. Consequently, it has put a considerable amount of concern on host States. In response, States are now starting to move forward with a new generation of BITs hoping that it could give more clarity and certainty than the previous generation of BITs, particularly regarding the definition of investment and investor. Questions arise on whether it brings more clarity and certainty in terms of an investment made through a subsidiary. This article will analyze the impact of the newly tailored definition clause under the latest generation of BITs toward an investment conducted through a subsidiary, including the legal standing of the investor therein.

Keywords *: Investment Treaties, Definition clause, Multinational Corporation, Indirect Investment.*

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I. INTRODUCTION

The perks of Multinational Corporations (hereinafter "MNC") existence as an investor within a Host State is, it could substantially develop the economy of the Host State through transfer of technology, know-how, or other kind of expertise brought by the MNC, and open a new horizon of the host State's market and ultimately expand the market within it.[1] In the realm of the international economy, the role of an MNC as a subject that conducts its businesses that transcends national boundaries has become essential for

[1] An An Chandrawulan, *Hukum Perusahaan Multinasional* [The Law of Multinational Corporation] (Bandung: CV. Keni Media, 2014), 80.

States.[2] The absence of an MNC in a State could even make the State lag in developing the world economy. This is because MNCs and subsidiaries mainly drive the present world economy's development due to its significant role in considerably increasing international trade and international investment.[3]

According to David E. Lilienthal, MNC is a corporation seated in one State. However, in operating its businesses, it is subjugated to the laws and customs of another State, hence making it not bound to any nationality.[4] Moreover, the parent company of the MNC is the one who has the control and the task to oversee while carrying out its business.[5] The parent company is the central power, establishes subsidiaries in another State and is the decision maker in determining the goal and direction of the MNC, including the selection of host States to be targeted for its investment.[6]

The parent company of an MNC could also delegate its decision on investment to its subsidiary that has a closer geographical location to the targeted host State. [7] The parent company employs this kind of corporate strategy in order to benefit from its subsidiary's know-how in doing business within the area.[8] Besides geographical reasons, another reason would be a favorable taxation regime.[9] Such a method is known as an indirect foreign direct investment, where the parent company will become the ultimate beneficiary of the investment. This method of structuring outbound investments and its impact on investment protection clauses will be the main topic of this article.

In conducting its investment, MNC as an investor may receive protections under international law that comes in an investment treaty, whether it be a bilateral investment treaty (BIT) or multilateral investment treaty (MIT).[10] The investment treaty is intended to provide protection for investors from the risks of investment that may arise from the political or economic interest of

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[2] Jessica Leonard, Prita Amalia, and An An Chandrawulan, "Indonesian Perspective on the Investor-State Dispute Settlement Mechanism for Foreign Investment Dispute Settlement in the Field of Intellectual Property Rights," *Indonesian Law Review* 10, no. 1 (2020): 18, doi:10.15742/ilrev.v10n1.615

[3] Andreas F. Lowenfeld, *International Economic Law*, Second Edition (Oxford: Oxford University Press, 2008), 8.

[4] Opinion of David E. Lilienthal in Peter Muchlinski, *Multinational Enterprises and the Law,* Second Edition (Oxford: Oxford University Press, 2007), 5.

[5] An An Chandrawulan*, Hukum Perusahaan Multinasional*, 39.

[6] *Ibid.*

[7] Kalman Kalotay, "Indirect FDI," *The Journal of World Investment & Trade* 13, (2012): 546, doi: 10.1163/221190012X649841.

[8] Kalotay, "Indirect FBI," 546.

[9] Jean-Francois Herbert, "Abuse of Corporate Nationality and the Jurisdiction of International Investment Tribunals," *Journal of Arbitration and Mediation* 1, no. 1 (2010): 121.

[10] Prita Amalia and Garry Gumelar Pratama, "Indonesia and ICSID: Exclusion of ICSID Jurisdiction by Presidential Decision," *Majalah Hukum Nasional* 48*,* no. 1 (2018): 7, doi: 10.33331/mhn.v48i1.110.

the host state through the imposition of a certain measure.[11] In order to ensure protection from these risks, investment treaties also provide legal avenues for investors to resolve disputes that arise from an investment covered by it, which usually refers to arbitration in a neutral forum.[12]

Within investment treaties, some provisions limit the scope of application. This limitation can be found in the definition clause, where investment treaties define what would constitute an investment and who would qualify as an investor. The definition clause is a cornerstone to what kind of investment and who is entitled to benefit from the protection through the investment treaty.[13]

Under the older generation of BITs, an investment, whether conducted indirectly or through a subsidiary. This condition depends on the ambit of the definition clause, investment and investor definitions, which will be elaborated further in the following chapter. This issue has become a concern for host States since there is a possibility that a parent company of an MNC receives protection from the relevant BIT despite little to no involvement in the investment. Moreover, there is a possibility of "treaty shopping", where the MNC could choose the available relevant treaty favorable to them.[14]

To further elaborate on the above issues, this article consists of as follows: Section II will mainly discuss the evolution of investment treaties in defining investment and investor over time and the developments of arbitral tribunal's decision in interpreting it by comparatively analyzing various BITs. Further, Section III will discuss the implications of the definition clause within the latest generation of investment treaties toward investment that is made indirectly or through a subsidiary, specifically on how it affected the method of indirect investment that MNCs use.

II. THE EVOLUTION OF THE DEFINITION CLAUSE IN INVESTMENT TREATIES

Within an investment treaty, there is a limitation to its applicability based upon the object and subject protected by the said treaty.[15] This limitation can be seen in the definition provision, specifically on how an investment treaty defines 'investment' and 'investor'. These two definitions are paramount to

[11] Pandu Rizky Pratama and Prita Amalia, "The ISDS Mechanism and Standard of Protection in the Investment Treaty," *Lentera Hukum* 7, no. 2 (2020): 154, doi: 10.19184/ejlh.v7i2.17348.

[12] Sornarajah, *The International Law on Foreign Investment*, Third Edition (Cambridge: Cambridge University Press, 2010): 216.

[13] Sornarajah, *The International Law on Foreign Investment*, 194.

[14] Martin J. Valasek and Patrick Dumberry, "Developments in the Legal Standing of Shareholders and Holding Corporations in Investor-State Disputes," *Foreign Investment Law Journal* 26, no. 1 (2011): 59.

[15] Sornarajah, *The International Law on Foreign Investment*, 197.

determining the scope of application of the relevant investment treaty, where it shall only apply to an investor's investment covered by the definitions.[16] These definitions also serve as a basis for the arbitral tribunal to provide cases arising from the investment treaty, whether the investment is protected under the relevant investment treaty (*ratione materiae*) and the investor is as defined in the investment treaty (*ratione personae*). Those will be decisive in determining an arbitral tribunal's jurisdiction over the case.[17] Specifically, for cases on the investment made indirectly or through a subsidiary, such cases need to be scrutinized from both *ratione materiae* and *ratione personae* standpoint.[18] Therefore, this chapter will discuss how investment treaties, particularly BITs, define investment and investors from time to time and whether such a definition covers the investment of an investor made through a subsidiary.

A. THE OLD GENERATION OF INVESTMENT TREATIES

1. Definition of Investment

Generally, investment treaties provide a broad definition of what would constitute an 'investment'[19] and defines an investor as a person seated in the contracting States.[20] These definitions directly affect the application of protection within the investment treaty to the investors.[21] The broad nature of investment definition can be *prima facie* identified by its wording, where most investment treaties define investment as 'any/every kind of asset' and is followed by a non-exhaustive list of forms that would amount to an investment, which usually includes shares or other kinds of participation in companies. In that regard, it has been established that the investment treaty shall be interpreted broadly and could possibly cover any economic activity. This is evident in various case laws, where tribunals decided the same manner as the notion above.[22]

The reason behind providing this broad phrase in defining 'investment' is that States have recognized that the forms of investment are constantly evolving.[23] Hence, such a broad wording is an attempt to cover any

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[16] Organization for Economic Cooperation and Development (OECD), *International Investment Law: Understanding Concepts and Tracking Innovations* (OECD, 2008), 9.
[17] Jean Ho, "Passive Investments," *ICSID Review – Foreign Investment Law Journal* 35, no. 4 (2020), 3.
[18] Ho, "Passive Investments," 4.
[19] Sornarajah, *The International Law on Foreign Investment,* 190.
[20] *Ibid.*, 197.
[21] *Ibid.,*194.
[22] *Fedax N.V. v Republic of Venezuela* (Decision on Jurisdiction, 2005) ICSID Case No. ARB/96/3, para. 32; *Mera Investment Fund Limited v Republic of Serbia* (Decision on Jurisdiction, 2018) ICSID Case No. ARB/17/2, para. 122.
[23] OECD, *International Investment Law: Understanding Concepts and Tracking Innovations*, 49.

possibilities. However, in a certain way, the use of such broad phrasing in defining 'investment' has backfired on host states, especially when dealing with the cases of an investment through a subsidiary company.

In most cases, the tribunal will declare its jurisdiction under the basis of the broad wording of the investment, which indicates that such a way of defining 'investment' does not exclude investment conducted through an intermediary or a subsidiary company.[24] The only instances when tribunals denied their jurisdiction in such a case were when they interpreted the definition of investment as requiring an active action or contribution from the claimant or shareholder in question. Such interpretation can be found in the case of Standard Chartered Bank v. Tanzania and the latest in Clorox v. Venezuela,[25] where the former will be discussed in the next section.

Furthermore, the kind of broad asset-based definition, followed by a non-exhaustive list of investment forms in defining investment, is commonly found in the older generation of BITs. We will look at some of the existing model BITs and their evolution over time, particularly how it defines investment. Since the emergence and exploding popularity of BITs in the 1950s,[26] the US, as one of the leading actors in the global economy, has continuously developed a model BIT (hereinafter "US Model BIT") to serve as modern protection of investment in international law, where it first models BIT was developed in 1982[27] and was issued in 1984. Since then, it has gone through a notable evolution, through the development of the 1994 US Model BIT, the 1998 US Model BIT, the revolutionary 2004 US Model BIT and the latest model being the 2012 US Model BIT.[28]

In terms of defining an investment, just like the other kind of early generation BITs, the earlier US Model BITs provide a broad definition using "every kind of investment" followed by a non-exhaustive list of investment forms. Another example can also be seen in the 1996 Australia-Chile BIT,[29]

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[24] Martin J. Valasek and Patrick Dumberry, "Developments in the Legal Standing of Shareholders and Holding Corporations in Investor-State Disputes,"45.

[25] *Standard Chartered Bank v. The Republic of Tanzania* (Award, 2012) ICSID Case No. ARB/10/12, para. 225; *Clorox Spain. S.L. v. Bolivarian Republic of Venezuela* (Award, 2019) PCA Case No. 2015-30, para. 833.

[26] Genevieve Fox, "A Future for International Investment? Modifying BITs to Drive Economic Development," *Georgetown Journal of International Law* 46, (2014): 229.

[27] Jeongho Nam, "Model BIT: An Ideal Prototype or a Tool for Efficient Breach?" *Georgetown Journal of International Law* 48, (2017):1277, 1282.

[28] "Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment", available at https://www.state.gov/investment-affairs/bilateral-investment-treaties-and-related-agreements/

[29] Agreement between the Government of Australia and the Government of the Republic of Chile, on the Reciprocal Promotion and Protection of Investments (opened for signature 9 July 1996, entered into force 18 November 1999), art. 1(1b).

where it defines investment as follows:

> *"Any kind of asset admitted by one or the other Contracting Party, in accordance with its respective laws, regulations and investment policies, and includes in particular, though not exclusively…."*

The above definition is followed by a non-exhaustive list of the investment forms protected by it, including shares or other participation in companies.[30] A similar yet not identical provision can also be seen in the 2005 Indonesia-Singapore BIT.[31] The 1999 Australia-Chile BIT and The 2005 Indonesia-Singapore BIT have been terminated and replaced by a newer version of the investment agreement.

However, this kind of definition has caused concern as it lacks clarity and legal certainty due to its broad nature. In correlation with that, within the early years of the 2010s, such concern also occurred in Indonesia, which became one reason Indonesia decided to terminate its existing BITs to be reviewed and revised. Indonesia views its older generation BITs are too one-sided in protecting investors[32]. The emergence of serial Investor-State Dispute Settlement (hereinafter "ISDS") claims from its investor based on its older generation BITs also took part in this reformation.[33] Such a decision from Indonesia attempts to strike a balance between the protection given to the investor and its right to regulate without making itself prone to ISDS claims. It is not too far-fetched that the ISDS claims faced by Indonesia have causality with the broad definition of investment within its BITs. An example of the case related to it is IMFA v. Indonesia, which used the 1999 India-Indonesia. Consequently, one of the avenues that Indonesia pursued involves revising the formulation of its definition clause, in particular on how it defines investment.[34]

2. Definition of Investor

How investment agreements define investors as both natural and legal persons may vary in each agreement. In general, BITs will provide an objective

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[30] Australia and Chile Agreement 1996, art. 1(1b).

[31] Agreement Between the Government of the Republic of Indonesia and the Government of the Republic of Singapore on The Promotion and Protection of Investments, opened for signature 16 February 2005 (entered into force 21 June 2006), art. 1 (1).

[32] Hamzah, "Bilateral Investment Treaties (BITs) in Indonesia: A Paradigm Shift, Issues and Challenges," *Journal of Legal, Ethical, and Regulatory Issues* 21, no. 1 (2018): 2.

[33] David Price, "Indonesia's bold strategy on bilateral investment treaties," *Asian Journal of International Law* 7, no. 1 (2016): 126, doi:10.1017/S2044251315000247. See also Caslav Pejovic and Juliartha Nugrahaeny Pardede, "Revising Bilateral Investment Treaties as a New Tendency in Foreign Investment Law: India and Indonesia in the Focus," *Indonesian Journal of International Law* 17, no. 2 (2020): 263, doi: 10.17304/ijil.vol17.2.786.

[34] Interview with Deden, Officer of Indonesian Ministry of Foreign Affairs, Directorate of Legal Affairs and International Treaties, 24 July 2021.

criterion on the qualifications of a legal person to be considered as an investor to determine the nationality of the investor in question.[35] The objective criteria may include the place of the corporation's constitution, or incorporation shall be made under the home State's laws. The corporation's seat shall be located in the home State, and the corporation should be controlled by the entity of the home State. Some BITs apply a combination of the aforementioned criteria to ultimately determine the investor's entailment to the protection within the BIT.

Under the place of incorporation criterion, any legal person constituted or incorporated under the laws of a contracting State will be deemed an investor of that State. Definition of investor which requires the place of incorporation test can be found mostly in the older generation of BITs *inter alia* 2005 Indonesia-Singapore BIT, 1989 Hungary-Cyprus BIT, 1999 Indonesia-India BIT. To illustrate the definition of investor under the place of incorporation test, the latter defines an investor as "legal person constituted or incorporated according to its (Contracting Party) laws and regulations".

This definition is considered broad and provides much flexibility for investors to structure their investment[36] since it only concerns the place of incorporation of the immediate investor and disregards any kind of control. The treaty practices pertaining to the definition, which use place of incorporation in defining investor, further affirmed the former notion. As evident in the ADC v. Hungary, where the tribunal interpreted the definition of investor within the 1989 Hungary-Cyprus BIT as not requiring looking further beyond the company's incorporation: control from another entity,[37] despite Hungary's contention that the claimants are merely shell companies controlled by a Canadian entity.[38]

Furthermore, although the older generation of BITs mostly defines investors by using the place of incorporation criterion, some BITs also use the test of effective management or the corporate's seat in determining the investor's nationality.[39] Under this criterion, investors are required to be incorporated in the home State, but they must also have their effective management or seat in

[35] OECD, *International Investment Law: Understanding Concepts and Tracking Innovations* ,18.

[36] Mark Feldman, "Setting Limits on Corporate Nationality Planning in Investment Arbitration," *ICSID Review* 27, no. 2 (2012): 284.

[37] *ADC Affiliate Limited and ADC & AMDC Management Limited v. The Republic of Hungary* (Award, 2006) ICSID Case No. ARB/03/16, para 357.

[38] *ADC Affiliate Limited and ADC & AMDC Management Limited v. The Republic of Hungary* (Award, 2006), para. 335.

[39] Japan and Turkey Agreement Concerning the Reciprocal Promotion and Protection of Investment, opened for signature 12 February 1992 (entered into force 12 March 1993); Agreement Between the People's Republic of China and the Federal Republic of Germany on the Encouragement and Reciprocal Protection of Investments, opened for signature 1 December 2003 (entered into force 11 January 2005).

the home State.[40] The determination of the corporation's seat can be identified by looking at the center of the corporation's business location.[41] By virtue of the application of this criterion, a subsidiary to an MNC will not be able to make a claim against the host State to receive a favorable outcome from the treaty in question, or the so-called "treaty shopping", as it lacks effective management and hence, cannot be construed as an investor. Had this criterion been used in the 1989 Hungary-Cyprus BIT, the tribunal's decision in the ADC v. Hungary case might be different due to the ADC being a shell company controlled by a Canadian entity and lacking effective management.

Regarding the criterion of control, it is usually combined with the other criteria justifying the coverage of an investor under the treaty.[42] The example can be found in The 1992 Indonesia-Australia BIT, which has been terminated and replaced with the latest Indonesia-Australia Comprehensive Economic Partnership Agreement. In respect to Australia, The 1992 Indonesia-Australia BIT defines an investor as a corporation incorporated under Australian law or a third state's law owned or controlled by Australian legal person.[43] Under the 1992 Indonesia-Australia BIT, a corporation incorporated outside of Australia and Indonesia will still have legal standing in the BIT, provided that it is owned or controlled by an Australian legal person.[44]

B. THE DEVELOPMENT OF CASE LAWS IN INTERPRETING THE DEFINITION CLAUSE

Previously, it has been established that there is a causality between the older generation of BITs' way of governing the definition clause towards the serial ISDS claims faced by host States. This section will specifically discuss those cases and how the arbitral tribunal scrutinized the implications of the definition clause within the older generation of BITs, which has subsequently triggered the dawn of the new generation of BITs.

1. The Consistent Jurisprudence in Interpreting the Asset-Based Definition of Investment

As explained above, there is a general view that when BITs define investment using the asset-based definition, it shall be interpreted broadly and is inclusive to investment conducted through a subsidiary or indirectly. This

[40] OECD, *International Investment Law: Understanding Concepts and Tracking Innovations*, 22.
[41] An An Chandrawulan, *Hukum Perusahaan Multinasional* 41.
[42] OECD, *International Investment Law: Understanding Concepts and Tracking Innovations*, 25.
[43] Agreement between the Government of Australia and the Government of the Republic of Indonesia concerning the Promotion and Protection of Investments, opened for signature 17 November 1992 (entered into force 29 July 1993), art. 1 (b) (ii).
[44] Robert Wisner and Nick Gallus, "Nationality Requirements in Investor-State Arbitration," *The Journal of World and Investment Trade* 5, no. 6 (2004): 934.

notion originated from the practices of how arbitral tribunals interpreted such definitions within investment treaties.

The first example where the tribunal deemed the asset-based definition to be interpreted broadly can be seen in the ICSID tribunal's decision in the *Fedax N.V. v. Venezuela* case. The tribunal held that the adoption of asset-based definition as provided in Art. 1(a) Netherlands-Venezuela BIT shows that the Netherlands and Venezuela intended to define investment in a very broad meaning.[45]

The ICSID tribunal in *Mera v. Serbia* also reached the same conclusion regarding the broad nature of an investment under the asset-based definition. In assessing the definition of investment in Article 1(1) Serbia-Cyprus BIT which adopts the asset-based definition, the tribunal considered the object and purpose of Serbia-Cyprus BIT by looking at its preamble. As enshrined in the preamble, the tribunal found that the Serbia-Cyprus BIT wished to create favorable conditions for investments between the two States. By virtue of this, the tribunal concluded that the two contracting States intended to provide broad investment protection.[46] Moreover, the tribunal opined that the silence on whether indirect investments are protected or not indicates that it shall also protect such an investment.[47] The tribunal further compares the Serbia-Cyprus BIT to the Serbia-Azerbaijan BIT. The latter explicitly excludes indirect investments by incorporating the phrase "every kind of assets established or acquired directly by an investor of a Contracting Party…". The tribunal held that if Serbia wished to exclude indirect investments in the Serbia-Cyprus BIT, they would have provided the requirement of investment to only be acquired directly, likewise the Serbia-Azerbaijan BIT.[48]

The next example is from one of the most recent cases. The Permanent Court of Arbitration (hereinafter "PCA") tribunal in the *IMFA v. Indonesia* case addressed the concern of indirect investments under the 1999 Indonesia-India BIT. In that case, the tribunal accepted the legal standing of the IMFA's investment, under the 1999 Indonesia-India BIT, despite the investment being made through a subsidiary company located in Mauritius.[49] The PCA tribunal reached the same conclusion as the tribunal in *Mera v. Serbia* regarding the inclusivity of such definition towards indirect investment in assessing the definition of "investment" within the 1999 Indonesia-India BIT and added as

[45] ICSID, *Fedax N.V. v Republic of Venezuela*, para. 32.
[46] *Ibid.*, para. 122.
[47] *Mera Investment Fund Limited v Republic of Serbia* (Decision on Jurisdiction, 2018) ICSID Case No. ARB/17/2 para. 126-127.
[48] *Ibid.*, 128.
[49] *Indian Metals and Ferro Alloys Limited (IMFA) v Republic of Indonesia* (Award, 2019) PCA Case No. 2015-40, para. 180.

follows:

> *"... the tribunal believes that if the Contracting Parties wanted to exclude indirect investments, in light of the BIT's broad definition of investments, the Contracting Parties needed to say it clearly in the Treaty."*[50]

The decision, however, is not unanimous since Professor Sornarajah, as one of the members of the tribunal, did not share the same view. In his view, indirect investments are protected when the BIT expressly says so.[51] Despite this, it is clear that tribunals largely share the same view regarding the broad nature of an asset-based definition and its coverage towards investments made through a subsidiary or indirect investments.

2. The Distinctive Application of Active Contribution Test to the Definition of Investment

The active contribution test is a test that the International Centre uses for the Settlement of Investment Disputes (hereinafter "ICSID") tribunal to determine the existence of investment in the case of *Standard Chartered Bank v. Tanzania*. This case has attracted much attention from scholars and practitioners alike due to the different approach that the tribunal took in interpreting the term investment in the United Kingdom-Tanzania BIT *vis-à-vis* investment made through a subsidiary. The tribunal decided to deny its jurisdiction over the case due to the lack of active contribution from the claimant in its alleged investment.

The claimant, in this case, was Standard Chartered Bank United Kingdom (hereinafter "SCB UK"), which owns equity in Standard Chartered Bank Hong Kong (hereinafter "SCB HK"), in which the latter holds loans to a Tanzanian borrower in a project financing scheme to finance a power plant, by the purchase of credit from a consortium of Malaysian banks. Notably, the said purchase was financed by the SCB HK themselves.[52] The merits of the dispute concern Tanzania's acts and measures are considered an expropriation and a breach of the fair and equitable treatment under the UK-Tanzania BIT. Having equity ownership in SCB HK, the claimant attempted to avail themselves of the protection within the UK-Tanzania BIT.

The claimant argued that their ownership in SCB HK, even without day-to-day control, is already following the term investment. The notion of investment is naturally understood as having ownership rather than control.[53]

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[50] *Ibid.*
[51] *Ibid.*
[52] *Standard Chartered Bank v. The Republic of Tanzania* (Award, 2012) ICSID Case No. ARB/10/12, para 196.
[53] *Ibid.*, para. 209.

The tribunal admitted that an investment might be made through a subsidiary or indirectly. However, it noted that there must be an investing activity where the actual investor channeled its contribution to a subsidiary. [54]

The tribunal looked at the treaty's language in construing its decision, specifically how the UK-Tanzania BIT uses the word "made" throughout the BIT and uses the rule of ordinary meaning interpretation under Article 31 VCLT. The tribunal concluded that when it comes to describing an investment of an investor, the UK-Tanzania BIT uses the word "made" instead of "own" or "hold," which indicates that some action in carrying out the investment is required. Mere passive ownership would not suffice to be considered an investment under the UK-Tanzania BIT.[55] Accordingly, the tribunal held that for the claimant's alleged investment to be considered an investment within the meaning of the UK-Tanzania BIT, the claimant must have a degree of contribution, either by directing the investment or funded investment.[56]

Some may consider this a "landmark" decision since it took a different direction than tribunals' previous decisions without deviating from it. However, one thing that remains is that the asset-based definition is still considered to cover the investment made through a subsidiary, despite the distinctive approach the tribunal took: the investor has to have an active contribution to its investment.

C.THE LATEST GENERATION OF INVESTMENT TREATIES

As mentioned previously, the asset-based definition in defining investment and place of incorporation criterion in defining investor has caused concern for States due to its broad and unpredictable nature. Particularly for Indonesia, it plays a role in Indonesia's termination of its existing BITs in order for them to be replaced with a newer version. Currently, Indonesia has started to conclude its new generation of BITs, as shown in the conclusion of the IA-CEPA and the latest 2018 Indonesia-Singapore BIT, as a manifestation of its foreign policy priorities, which is to enhance economic diplomacy.[57] In constructing its latest generation of BITs, there is no per se new generation of Indonesia Model BIT on the official record. However, in negotiating new BITs, Indonesia has a specific concern on various issues which serve as a

[54] *Ibid.*, para. 199.
[55] *Ibid.*, para. 222-223.
[56] *Ibid.*, para. 230.
[57] Resha Roshana Putri, An An Chandrawulan, and Prita Amalia, "Peringkat Arus Investasi Indonesia dalam Kerangka ASEAN-China Free Trade Agreement (Perbandingan dengan Singapura, Malaysia, Thailand, dan Vietnam) Ditinjau dari Prinsip Fair and Equitable Treatment [Indonesia's Investment Flow Rate within the Framework of the ASEAN-China Free Trade Agreement (A Comparison with Singapore, Malaysia, Thailand, and Vietnam) Analyzed through the Principle of Fair and Equitable Treatment]," *Jurnal Hukum dan Pembangunan* 48, no. 2 (2018): 276, doi: 10.21143/jhp.vol48.no2.1664.

basis in the negotiation process, this includes the definition of investment and investor.[58] Specifically, Indonesia has made substantial changes in defining investment by applying a narrower definition through the incorporation of "the characteristic of an investment requirement" and an enterprise-based definition instead of the asset-based definition. In terms of defining investors, it has applied a combination of the objective criteria with the hope that it could create more certainty. This section will specifically discuss what is to be expected from those changes in the future by scrutinizing each of its elements.

1. From Asset-Based to Enterprise-Based Definition of Investment

The incorporation of a requirement for an investment to have the characteristic of an investment in the new generation of Indonesia's BIT is not the first time that we have seen such a requirement incorporated in a BIT. Under the 2004 US Model BIT, it introduced a new way of defining investment. Although the broad asset-based definition remains unchanged,[59] it provides additions to the definition in a revolutionary manner *vis-à-vis* its predecessors' model by providing a tighter definition through the incorporation of a requirement for an investment to have "the characteristics of an investment".[60] It further stipulates that the said characteristics shall include the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk.[61]

Akin to the 2004 US Model BIT, the latest Australia-Chile Free Trade Agreement (FTA),[62] which contains the Investment Chapter and replaces the previous Australia-Chile BIT, also an apparent substantial changes in formulating the definition of "investment" *vis-à-vis* the previous version, where the latest version formulated the definition of "investment" in a more precise and detailed manner.[63] The Investment Chapter on the Australia-Chile FTA defines investment as every asset owned or controlled by an investor, regardless of how it is conducted, whether directly or indirectly, provided it has the characteristics of an investment.[64] The requirement for investment to

[58] Interview with Deden Officer of Indonesian Ministry of Foreign Affairs, Directorate of Legal Affairs and International Treaties, 24 July 2021. Provide name of the Officer.

[59] Amokhura Khawaru & Luke Nottage, "Models for Investment Treaties in the Asia-Pacific Region: An Underview," *Arizona Journal of International & Comparative Law* 34, no. 3 (2017): 502.

[60] Luke Nottage, "The TPP Investment Chapter and Investor-State Arbitration in Asia and Oceania: Assessing Prospects for Ratification," *Melbourne Journal of International Law* 17, no. 2 (2016):19.

[61] United States Trade Representative, United States Model Bilateral Investment Treaty, 2004.

[62] Free Trade Agreement between Chile and Australia, opened for signature 30 July 2008 (entered into force 6 March 2009), art. 10.1.

[63] United Nations Conference on Trade and Development, "IIA Issues Note: Recent Developments in the International Investment Regime," May 2018, Issue 1, 7.

[64] The characteristics of an investment means commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk. See Free Trade Agreement between Chile and Australia, opened for signature 30 July 2008 (entered into force 6 March 2009), art. 10.1.

have "the characteristics of an investment" can also be seen in the latest 2018 Indonesia-Singapore BIT,[65] which was replaced with the 2005 Indonesia-Singapore BIT. The latest Indonesia-Singapore BIT seems to narrow down the meaning of investment along with its implications, as it required the investment to have the objective criteria of investment,[66] irrespective of how it is conducted; by way of controlling another company, likewise the definition of investment within the Investment Chapter of Australia-Chile FTA. To a certain extent, the inclusion of the requirement for investment in the investment characteristic founded on these treaties is influenced by the 2004 US Model BIT. [67]

Furthermore, the inclusion of "the characteristics of an investment" as a requirement originated from the notorious *Salini* test in identifying what constitutes an investment. This matter is due to the concern about the overly inclusive nature of the "every kind of asset" definition of investment.[68] This requirement, however, does not limit the forms of investment as it only requires to have the characteristic of an investment.[69]

Prior to incorporating such requirements, some investment tribunals have opined that those requirements are not formal prerequisites[70] or even tribunal may determine the existence of investment solely based on the definition provided in the relevant BIT, without taking into account the requirement in the *Salini* test.[71] Also, the non-fulfillment of one of those elements does not necessarily mean that there was no investment.[72] Incorporating the aforementioned requirements has become a formal prerequisite in determining the existence of an investment. Hence, it necessitates the tribunal to analyze the investment in question-based on such criterion[73] in order to protect . This

[65] Agreement Between the Government of the Republic of Indonesia and the Government of the Republic of Singapore on The Promotion and Protection of Investments, opened for signature 11 October 2018 (entered into force 9 March 2021), Article 1.

[66] David Price, "Indonesia's bold strategy on bilateral investment treaties," 143.

[67] Amokhura Khawaru & Luke Nottage, "Models for Investment Treaties in the Asia-Pacific Region: An Underview," 501; Interview with Deden Officer of Indonesian Ministry of Foreign Affairs, Directorate of Legal Affairs and International Treaties, 24 July 2021.

[68] Michael Hwang and Jennifer Fong, "Definition of "Investment" – A Voice from the Eye of the Storm," *Asian Journal of International Law* 1, (2011): 127-128, doi:10.1017/S2044251310000378.

[69] *Ibid*, 128.

[70] CSOB v The Slovak Republic, (Decisions on Objection to Jurisdiction, 1999) ICSID Case No. ARB/97/4, para. 90.

[71] Joshua Fellenbaum, "GEA v. Ukraine and the Battle of Treaty Interpretation Principles Over the Salini Test," *Arbitration International* 27, no. 2 (2011): 262.

[72] Berk Demirkoel, "The Notion of 'Investment' in International Investment Law," *Turkish Commercial Law Review* 1, no. 1 (2015) 42; Bhagirath Ashiya, "The Shift Towards an Enterprise Based Definition of Investment: The Quagmire of the Salini Test and India's Model BIT," *Jindal Global Law Review* 7, no. 2 (2016): 270, doi: 10.1007/s41020-016-0035-6.

[73] Julian Davis Mortenson, "The Meaning of "Investment": ICSID *Travaux* and the Domain of International Investment Law," *Harvard International Law Journal* 51, no. 1 (2010): 308.

kind of alteration is intended to limit the qualification of parties entitled to make an arbitration claim under the ISDS within the relevant investment agreement,[74] which consequently could prevent any kind of frivolous claims from the shareholder, or the parent company of an MNC in its capacity as the shareholder of its subsidiary.

2. A Combination of Objective Criteria in Defining Investor

Reformation on definition of investor is paramount when the definition of investor within a BIT has the reputation of being able to be interpreted broadly. This is since a broad definition of investor may result in an unanticipated coverage of legal persons.[75] Accordingly, it is of the essence for States to tailor the definition of investor that could enhance the legal predictability compared to the previous generation of BITs.[76]

In an attempt to provide clarity and legal certainty, States have now used all three objective criteria to determine the nationality of an investor. The place of incorporation, the corporate's seat, and the control requirement are now apparent in the latest generation of BITs or other kind of investment treaties *inter alia* the IA-CEPA, 2020 India-Brazil BIT, 2018 Indonesia-Singapore BIT. The implications of such incorporation will be thoroughly discussed in the next chapter.

III. THE PARENT COMPANY OF AN MNC'S PROTECTION IN THE CASE OF INVESTMENT THROUGH A SUBSIDIARY UNDER THE LATEST GENERATION OF INVESTMENT TREATIES

It is clear from the above explanation that States are now starting to move forward to a new generation of BITs with a hope that it could give more clarity and certainty *vis-à-vis* the previous generation of BITs, particularly in regard with the definition of investment and investor. Questions arise on whether it really brings more clarity and certainty in terms of an investment that was made through a subsidiary? This chapter will specifically discuss how the latest generation of BITs may or may not protect the aforementioned kind of investment by analyzing each criterion of investment and the newly tailored definition of investor toward an investment conducted through a subsidiary.

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[74] Resha Putri, "Indonesia's New Model of Bilateral Investment Treaty: Comparison with Brazil," *Padjadjaran Journal of International Law* 3, no. 2 (2019): 249.

[75] United Nations Conference on Trade and Development (UNCTAD), *International Investment Agreements Reform Accelerator,* (UNCTAD, 2018), 13.

[76] *Ibid.*

A. INVESTMENT OUGHT TO HAVE THE CHARACTERISTIC OF AN INVESTMENT: BACK TO THE FUTURE?

Some views said that the objective criteria of *Salini* are not mandatory to be followed, and the definition of investment under the relevant BIT can be considered sufficient in determining the existence of investment. The latest generation of BITs explicitly incorporated some of the criteria in the *Salini* test as a requirement to determine the existence of an investment. As explained previously, one of the hallmarks in the latest generation of BITs is the inclusion of "the characteristic of an investment" as a requirement for an investment to be covered by the relevant BIT, which stemmed from the *Salini* test. Moreover, the latest generation of BITs usually elaborates further on what is meant by the characteristic of investment which includes, commitment of capital or other resources, expectation of gain or profit, and assumption of risk or certain duration.[77]

In regard with the first criterion, which is the commitment of capital or other resources, or in some cases is referred as contribution to the investment, this criterion has been constantly used in identifying the existence of an investment,[78] whatever the form may be.[79] Although the form of the contribution is not something that becomes an issue as the non-exhaustive list of investment forms remain unchanged in the latest generation of BITs, there are views where the extent of contribution should also be taken into account,[80] especially when the investment was made indirectly through a subsidiary. This is because contrary to an investment that was made indirectly, in an investment that was made directly without using a subsidiary, the contribution can be identified simply by looking at the transfer of capital or resources. As can be seen in the *Standard Chartered Bank v. Tanzania*, where the ICSID tribunal in that case highlighted the importance of the relationship between investor and its alleged investment by gauging the extent of contribution in order to determine the existence of investment. It is clear that a capital contribution is paramount to indicate the existence of contribution as it may reveal the true beneficiary of the investment,[81] however the tribunal in *Standard Chartered Bank v.*

[77] Agreement Between the Government of the Republic of Indonesia and the Government of the Republic of Singapore on The Promotion and Protection of Investments, opened for signature 11 October 2018 (entered into force 9 March 2021), art. 1. See also Free Trade Agreement between the Government of Australia and the Government of the Republic of Chile, opened for signature 30 July 2008 (entered into force 6 March 2009), art. 10.1.

[78] Ho, "Passive Investments," 4.

[79] Emmanuel Gaillard, "Identify or Define? Reflection on the Evolution of the Concept of Investment in ICSID Practice" in *International Investment Law for the 21st Century: Essays in Honour of Christoph Schreuer*, Christina Binder, Ursula Kriebaum, August Reinisch and Stephan Wittich, eds. (Oxford: Oxford University Press, 2009), 405.

[80] Michael Waibel, "Subject Matter Jurisdiction: The Notion of Investment," in *19 ICSID Rep*, Jorge Vinuales and Michael Waibel, eds. (Cambridge: Cambridge University Press, 2021), 27.

[81] Ho, "Passive Investments," 15.

Tanzania case went beyond such an indication by also taking into account the control from the shareholder that is manifested through the direction that was given prior to the commencement of the investment.[82] These indications are decisive in determining the actual investor and hence, determine the party actually entitled to receive protection from the relevant BIT.

Also, it is important to note that despite the conclusion in *Standard Chartered Bank v. Tanzania* which requires an active contribution from the investor was a result of a treaty interpretation under the rules of VCLT towards the relevant BIT and does not specifically refer to the objective criterion of investment in determining the existence of investment. However, this just goes to show that irrespective of what the determination of an investment was based, an investment ought to have a 'tangible' contribution from the investor in order to signify the relationship between the investor and its investment.

Furthermore, besides the contribution criterion an expectation of gain or profit has been understood as the objective meaning of the term investment by virtue of the interpretation of ordinary meaning under Article 31 VCLT toward the term investment in Article 25 ICSID Convention. [83] Expectation of gain is considered as a part of the process in acquiring an asset and hoping to receive something in return.[84] In the context of investment made through a subsidiary, naturally this criterion would not pose much of an issue compared to the other criteria as it is something that is supposed to follow the contribution criterion.

Regarding the next requirement, the assumption of risk, this refers to a situation where there is no certainty for the investor of a return on the investment and the amount that will be spent in the end.[85] There are various factors where an investor is exposed to a risk of investment. Generally, the factors can be classified as internal factors and external factors. The former means a risk that is derived from the duration of investment and the capital of investment, whereas the latter means a risk that came from political, economic, legislative and cultural investment of the host State.[86] The form of risk itself shall be looked at on a case-by-case basis depending on the surrounding circumstances. The tribunal in the *GEA v. Ukraine* case held that there exist risks within the investment since the claimant undertook a market risk, credit

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[82] ICSID, *Standard Chartered Bank v. The Republic of Tanzania,* para. 230.

[83] Mavluda Sattorova, "Defining Investment Under the ICSID Convention and BITs: Of Ordinary Meaning, Telos, and Beyond," *Asian Journal of International Law* 2, no. 2 (2012), 275, doi: 10.1017/S2044251312000112.

[84] Satoro.

[85] Antoine Martin, "Definition of Investment: Could a Persistent Objector to the Salini Test Be Found in ICSID Arbitral Practice?" *Global Jurist* 11, no. 2 (2011), 13.

[86] Julien Burda, "A New Step Towards a Single and Common Definition of an Investment? – Comments on the Romak versus Uzbekistan Decision," *The Journal of World Investment & Trade* 11, no. 6 (2010), 1100.

risk, and political risk.[87]

In some cases of an investment through an intermediary, an MNC could utilize a Special Purpose Vehicle (hereinafter "SPV") to finance its investment, where the parent company established a company located in a third State (other than the home and host State) in order to minimize the risk of the investment by allocating it to the SPV.[88] In the context of an SPV in being a tool for MNCs' investment, the establishment of an SPV is based upon the initiative of an MNC's parent company, and has its own distinct legal personality.[89] The shares within an SPV are majorly owned if not wholly-owned by the parent company of an MNC, and therefore it is to be regarded as a subsidiary of the MNC.[90]

In this instance, it might not be that straightforward to distinguish who is the actual investor. Although an SPV is generally established solely for the purpose of achieving a specific and temporary objective of an MNC, however when an SPV is used as an intermediary to conduct an investment, it could seem like the SPV as the immediate investor is seen as the investor of the investment since the flow of capital may *prima facie* look like it came from the SPV and also not to mention that the SPV is the one who assumed the risk of the investment.

As elaborated above, capital contribution and assumption of risk are of the characteristics of an investment and is paramount in determining the existence of investment under the latest generation of BITs. Accordingly, it may be the case that under the latest generation of BITs, an SPV could be the one who will be considered as the investor of an investment under the definition of investment, and not its parent company. If the parent company were to be protected by the relevant BIT, it bears the burden of proof in proving that they have substantially contributed to the investment in question and is the one who assumed the risk of it. The latter might be more difficult to prove as the purpose of establishing an SPV is to allocate the risk of the investment to it. Therefore, in conducting investment through the transshipment method, MNC has to be more careful considering in that event, MNC would be the beneficiary owner of the investment, and might not be able to avail themselves from the protection given from the relevant BIT if its investment does not satisfy the characteristics of an investment.

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87 *GEA Group Aktiengesellschaft v. Ukraine* (Award, 2011) ICSID Case No. ARB/08/16, para. 151.
88 Such a method is known as Transhipment, see Kalotay, "Indirect FDI," 546.
89 Kalman Kalotay, "Indirect FDI," 546.
90 An An Chandrawulan, *Hukum Perusahaan Multinasional*, 42.

B. DEFINITION OF INVESTOR: A NEW LOCK COMBINATION

As mentioned above, in the latest generation of BITs the definition of investor uses a combination of the objective criteria in determining the nationality of an investor: place of incorporation, corporate seat, and control requirement. For instance, the latest 2018 Indonesia-Singapore BIT defines an investor as "Enterprise of a Party", and further defines enterprise of a Party as "… enterprise constituted or organized under the law of a Party and carrying out business activities there". The term "enterprise" also has its own definition and is defined as follows:

> *"Enterprise means any entity, with or without legal personality, constituted or organized under applicable law, whether or not for profit, and whether privately or governmentally owned or controlled, including a corporation, trust, partnership, sole partnership, joint venture, association, or similar organization, and a branch of an enterprise."*

Furthermore, in defining investment it uses the enterprise-based definition where it reads "investment means any kind of asset owned or controlled, directly or indirectly, by an investor…".

From the provided definitions above, it is apparent that the Indonesia-Singapore BIT incorporates all three objective criteria in determining the nationality of an investor. Firstly, it uses the place of incorporation criterion where it requires an enterprise to be constituted in accordance with the laws of the contracting States. Secondly, the corporation's seat criterion can be seen when it requires an enterprise to carry out its business activities within the State where it is constituted. Lastly, the control criterion can be seen by reading the definition of enterprise and enterprise of a party in conjunction with the definition of investment. The definition of investment clearly allows for an investment to be conducted indirectly, notwithstanding the requirement of having been incorporated in the contracting States and has its effective management there.

Therefore, the BIT limits its application only to an enterprise that is located and has its business within the contracting States and does not extend to also cover an enterprise located outside the contracting States that is controlled by an enterprise in a contracting State. If there is a claim from the latter, the odds will be against it as the combination of three objective criteria will most likely eliminate any possibility of such a claim. This definition clearly has provided more clarity and legal certainty compared to the 2005 Indonesia-Singapore BIT, which determines the nationality of an investor solely on the place of incorporation criterion.

IV. CONCLUSION

All of the above explanation shows that under the latest generation of BITs, MNCs that would like to conduct its investment through a subsidiary without having the intention to have major involvement in the investment making process, might not be able to avail themselves of the protection within it. The provided definition clause within the latest generation of BITs might just provide more clarity and certainty in terms of covering investment that is made through a subsidiary by requiring an investment to have "the characteristics of an investment" and by combining the objective criteria of an investor in order to narrow down on the specific investor that would be protected.

In terms of the definition of investment, the latest requirement for an investment to have "the characteristics of an investment" has now restricted a parent company to capitalizing on its passive role as the shareholder of its subsidiary, through requiring it to make a substantial contribution to the investment and to also assumed the risk of the investment. The incorporation of such a requirement, to a certain extent, has shed a light on the issue of claims by a parent company with minor involvement. Pertaining the definition of investor, the use of the three objective criteria of an investor has clarified on the kinds of investor that the contracting States would like to protect under the BIT, hence increasing the predictability of the covered investor. Conclusively, it is still remained to be seen through the practices of this latest generation of BITs regarding the extent of clarity and certainty of the newly tailored definitions, however in terms of investment made through subsidiaries, these definitions have eliminated the chance of a speculative claim from a parent company who has minimum correlation to the investment in question.

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