

IN THE ARBITRATION UNDER CHAPTER TEN OF THE  
DOMINICAN REPUBLIC—CENTRAL AMERICA—UNITED STATES FREE TRADE AGREEMENT  
AND THE ICSID ARBITRATION RULES  
BETWEEN

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PAC RIM CAYMAN LLC,

*Claimant/Investor*

- and -

THE REPUBLIC OF EL SALVADOR,

*Respondent/Party.*

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**SUBMISSION OF THE UNITED STATES OF AMERICA**

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1. Pursuant to Article 10.20.2 of the Dominican Republic—Central America—United States Free Trade Agreement (“CAFTA-DR”) (the “Agreement”), the United States of America makes this submission on a question of interpretation of the Agreement. The United States does not take a position, in this submission, regarding how the interpretation it offers below applies to the facts of this case, and no inference should be drawn from the absence of comment on any issue not addressed below.

Background

2. Chapter Ten of the CAFTA-DR provides that a Party shall provide protection for “investors” from another Party, which are defined to include a broad class of “enterprise[s],” namely those that are “constituted or organized under the law of a Party.”<sup>1</sup> At the same time, however, CAFTA-DR Article 10.12.2 provides that a Party “may deny the benefits” of Chapter Ten to an enterprise of another Party that has “no substantial business activity in the territory” of any other Party and is owned or controlled by a person from the denying Party or from a non-Party:

Subject to Article 18.3 (Notification and Provision of Information) and 20.4 (Consultations), a Party may deny the benefits of this Chapter to an

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<sup>1</sup> A “claimant” under the dispute resolution provisions of Chapter Ten of the CAFTA-DR is defined as “an investor of a Party that is a party to an investment dispute with another Party.” CAFTA-DR, art. 10.28. The term “investor of a Party” is defined under Article 10.28 to include an “enterprise of a Party.” “[E]nterprise of a Party” is defined as “an enterprise constituted or organized under the law of a Party . . . .” CAFTA-DR, art. 10.28.

investor of another Party that is an enterprise of such other Party and to investments of that investor if the enterprise has no substantial business activities in the territory of any Party, other than the denying Party, and persons of a non-Party, or of the denying Party, own or control the enterprise.<sup>2</sup>

Thus, CAFTA-DR Parties may deny Chapter Ten benefits to claimants under these specified circumstances.

3. This treaty right is consistent with a long-standing U.S. policy to include a denial of benefits provision in investment agreements to safeguard against the potential problem of “free rider” investors, i.e., third-party entities that may only as a matter of formality be entitled to the benefits of a particular agreement.<sup>3</sup> In testimony before the U.S. House of Representatives, Ambassador Peter Allgeier, one of the U.S. negotiators of CAFTA-DR, explained that the denial of benefits provision of CAFTA-DR was intended “to protect against . . . establish[ment of] an affiliate that is merely a ‘shell.’”<sup>4</sup> A similar provision, included in Article 1113 of the North American Free Trade Agreement, has been described by commentators as permitting a Party “to deny benefits to an enterprise if it is merely a ‘sham company’ having no ‘substantial business activities’ in the . . . country in which it is established.”<sup>5</sup>

4. The United States hereby addresses two issues of treaty interpretation related to CAFTA-DR Article 10.12.2: first, whether a CAFTA-DR Party is required to invoke the denial of benefits provision under Article 10.12.2 before arbitration commences; and second, whether the notice provision under CAFTA-DR Article 18.3, which is referenced in Article 10.12.2, requires the Party to give notice to the claimant as well as to the Party under the law of which the claimant is constituted or organized.

#### A CAFTA-DR Party Is Not Required To Invoke The Denial Of Benefits Provision Under Article 10.12.2 Before Arbitration Commences

5. Article 10.12.2 imposes two substantive requirements that must be met before the provision can be invoked by a CAFTA-DR Party; specifically, an enterprise must (1) have no substantial business activities in the territory of any Party other than the denying Party, and (2) be owned or controlled by persons of a non-Party or of the denying Party. Article 10.12.2 does not impose any requirement, however, with respect to *when* a

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<sup>2</sup> CAFTA-DR, art. 10.12.2.

<sup>3</sup> See, e.g., Herman Walker, Jr., *Provisions on Companies in United States Commercial Treaties*, 50 Am. J. Int’l L. 373, 388 (1956) (noting that “recent treaties signed by the United States, . . . , indicate that this possibility of a ‘free ride’ by third-country interests is one to be guarded against . . .”).

<sup>4</sup> See *Implementation of the Dominican Republic – Central America Free Trade Agreement (DR-CAFTA): Hearing Before the Committee on Ways and Means, U.S. House of Representatives*, 109th Cong. 193 (April 21, 2005) (questions submitted from the Honorable Lloyd Doggett to Ambassador Peter F. Allgeier, and his responses).

<sup>5</sup> Meg N. Kinnear et al., *Article 1113 – Denial of Benefits*, in INVESTMENT DISPUTES UNDER NAFTA, AN ANNOTATED GUIDE TO CHAPTER 11 1113-5 (2006).

respondent may invoke the denial of benefits provision. Neither this Article nor any other provision of CAFTA-DR precludes a Party from invoking the denial of benefits provision at an appropriate time, including as part of a jurisdictional defense after a claim has been submitted to arbitration, to deny a claimant enterprise benefits under the Agreement.<sup>6</sup> There is no basis to read into the plain language of Article 10.12.2 a requirement that a Party assert its right to deny benefits before the commencement of arbitration.

6. Requiring the respondent to invoke the denial of benefits provision before a claim is filed would place an untenable burden on that Party. It would require the respondent, in effect, to monitor the ever-changing business activities of all enterprises in the territories of each of the other six CAFTA-DR Parties that attempt to make, are making, or have made investments in the territory of the respondent.<sup>7</sup> This would include conducting, on a continuing basis, factual research, for all such enterprises, on their respective corporate structures and the extent of their business activities in those countries. To be effective, such monitoring would in many cases require foreign investors to provide business confidential and other types of non-public information for review. Requiring CAFTA-DR Parties to conduct this kind of continuous oversight in order to be able to invoke the denial of benefits provision under Article 10.12.2 before a claim is submitted to arbitration would undermine the purpose of the provision.

7. Similarly, there is no basis in the plain language of CAFTA-DR to suggest that a respondent is required to invoke Article 10.12.2 between the submission of a claimant's notice of intent and notice of arbitration. Article 10.16.2, for example, requires that a notice of intent include a claimant's "name and address," but Article 10.16.2 does not require a claimant to disclose the extent of the claimant's business activities in the territory of any CAFTA-DR Party or the names of any persons or entities that own or control the claimant enterprise.

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<sup>6</sup> See CAFTA-DR, art. 10.12.2. Under Article 10.12.2, "a Party may deny the benefits of this Chapter." As such, a CAFTA-DR Party may invoke Article 10.12.2 to deny the benefits of both the substantive provisions and the dispute settlement provisions of Chapter Ten.

<sup>7</sup> See Meg N. Kinnear et al., *Article 1113 – Denial of Benefits*, in INVESTMENT DISPUTES UNDER NAFTA, AN ANNOTATED GUIDE TO CHAPTER 11 1113-6 (2006) (discussing the denial of benefits provision under NAFTA Article 1113.2, which has language similar to the denial of benefits provision under CAFTA-DR Article 10.12.2).

Given that a Party cannot know which enterprises in another Party may some day attempt to file a NAFTA Chapter 11 claim, and given the rapidity with which ownership and control of a corporation may change, [the prior notification requirement under NAFTA Article 1113.2] *cannot mean that a Party needs to notify the other Party before a claim is submitted to arbitration* under Chapter 11.

*Id.* (emphasis added).

8. For the above reasons, there is no reasonable basis under any applicable rule of treaty construction to read into the text of Article 10.12.2 a requirement to invoke the denial of benefits provision before arbitration commences.<sup>8</sup>

Neither Article 10.12.2 nor Article 18.3 Requires Notice To Claimants

9. Under Article 10.12.2, a CAFTA-DR Party's denial of benefits is "subject to" Article 18.3, the provision that delineates notification requirements for CAFTA-DR Parties. Paragraph 1 of Article 18.3 provides:

To the maximum extent possible, each Party shall notify any other Party with an interest in the matter of any proposed or actual measure that the Party considers might materially affect the operation of this Agreement or otherwise substantially affect that other Party's interests under this Agreement.

10. On its face, Article 18.3 requires a CAFTA-DR Party, to the maximum extent possible, to provide notice to one or more other CAFTA-DR Parties of certain "proposed or actual" measures as described in the provision.<sup>9</sup> There is no mention of notice to claimants in Article 18.3, and none is required.<sup>10</sup>

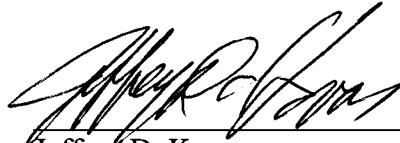
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<sup>8</sup> See Vienna Convention on the Law of Treaties ("VCLT"), May 23, 1969, 1155 U.N.T.S. 331, 8 I.L.M. 679 (1969), art. 31 ("[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.") While the United States is not a party to the VCLT, it has recognized since at least 1971 that the Convention is the "authoritative guide" to treaty law and practice. See Letter from Secretary of State Rogers to President Nixon Transmitting the Vienna Convention on the Law of Treaties, Oct. 18, 1971, reprinted in 65 DEPT OF ST. BULL. 684, 685 (1971). The International Court of Justice has determined that VCLT Article 31 is reflective of customary international law. See, e.g., *Kasikili/Sedudu Island (Bots. v. Namib.)*, 1999 I.C.J. 1045, 1059 (Judgment of Dec. 13, 1999).

<sup>9</sup> Just as a CAFTA-DR Party is not required to invoke the denial of benefits provision before arbitration commences, a CAFTA-DR Party is not required to provide notice to another CAFTA-DR Party of its intent to invoke the provision before arbitration commences. See *supra*, ¶¶ 5-8.

<sup>10</sup> A host State's denial of benefits is also "subject to" Article 20.4, which provides for consultations among Parties in certain circumstances. Article 20.4.1 states that "[a]ny Party may request in writing consultations with any other Party with respect to any actual or proposed measure or any other matter that it considers might affect the operation of this Agreement." Given that a request for consultations pursuant to Article 20.4.1 is discretionary ("[a]ny Party may request"), there is no basis in the Agreement to draw any inference from a Party's decision not to request consultations.

*Respectfully submitted,*



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May 20, 2011