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The Compatibility of the Substance over Form Doctrine with Tax and Investment Treaties: A Case Study of Lone Star v the Republic of Korea[1]

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Abstract: In late August 2022, the Lone Star tribunal concluded one of the latest awards in tax-related investment treaty disputes (the tax-related claims account for almost USD 1.5 billion of the total of almost USD 4.7 billion claimed in compensation). It also is the first award in which the tribunal dealt with the application of the substance over form doctrine (SOFD) by tax authorities and courts of the host state to prevent the abuse of a double tax treaty (DTT), and the impact of the refusal to accord the claimants the benefits under the DTT via a domestic (Korean) SOFD on the investment protection standards under the bilateral investment treaty (BIT). The Lone Star tribunal implicitly considered the Korean SOFD to be a suitable rule to prevent abuses of the Korea-Belgium DTT and thus compatible with the BLEU-Korea BIT. This article critically analyses the tribunal's methodology and reasoning in reaching that conclusion. Notably, the article highlights the need to consider the principle of an abuse of rights while examining the compatibility of a SOFD with a BIT and a DTT. Such an approach could enhance the rule of law in the interpretation of tax and investment treaties in other similar cases. It is also in accordance with the principle of systemic integration. The article argues that it is increasingly more important to properly understand the concept of economic substance insofar as denial of benefits (DoB) clauses in investment treaties and principal purposes test (PPT) in tax treaties appear to specifically prevent abuses of those treaties by arrangements with no or insufficient economic substance. Global and regional tax developments, including the implementation of anti-base erosion and profit shifting (BEPS) rules, as well as Pillar Two rules (global minimum tax of 15%), strengthen the need for a comparative research on economic substance under tax and investment treaties. Such research may reveal that a convergence in denying benefits under DTTs and BITs will enhance the rule of law and increase legal certainty in tax and investment domains.

I. INTRODUCTION

The Lone Star v Korea (Lone Star) Award is one of the latest investment awards in tax-related investment treaty disputes and the first in which the Tribunal dealt with the application of the substance over form doctrine[3] (SOFD) by tax authorities and courts of the host State to prevent the abuse of a double tax treaty (DTT). Previously, tribunals examined the SOFD in the tax domain predominantly in relation to alleged abuses of domestic tax law. It was done either while examining the Respondent's tax avoidance defence and the justification for retroactive

[1] LSF-KEB Holdings SCA and others v Republic of Korea (ICSID Case No ARB/12/37) Award (30 August 2022) (Ian Binnie, President; Charles N Brower; Brigitte Stern). All the Claimants were affiliated with a Texas investment fund, sometimes collectively referred to as 'Lone Star', ie the abbreviation LSF means Lone Star Funds. Hence, the Award analysed is referred to as Lone Star.

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[3] Or principle. The Lone Star Tribunal used the phrase 'substance over form doctrine' (11 times) and 'substance over form principle' (13 times) interchangeably. In this article, the former phrase will be used for consistency purposes. However, it also encompasses the latter phrase. Internationally, substance over form in tax law is linked with judicial doctrines rather than principles codified in tax law statutes. Frederik Zimmer, 'General Report: Form and Substance in Tax Law' (2002) 87a IFA Cah 24–48, 31, 43.

taxation in light of fair and equitable treatment (FET),[4] or as part of the analysis regarding the indirect expropriation of an investment via mala fide taxation measures.[5]

In the strict context of the Lone Star case, SOFD refers to a general domestic anti-tax avoidance doctrine, as it emerged from Korean case law already in 1967 and has been developed in subsequent case law,[6] partly codified in domestic statutory tax law.[7] It is based on a broad and vague anti-tax avoidance concept of economic substance,[8] which, according to the Korean case law, consists of the non-tax avoidance business purpose, the non-tax economic benefit and the engagement in non-tax avoidance related business activities.[9]

Generally, all SOFDs appear to have the same purpose: to prevent tax avoidance via broad, vague and far-reaching interpretative approaches.[10] For instance, local tax authorities and courts may apply SOFDs to prevent an abuse

[4] eg the Indian tax avoidance doctrine, which could hypothetically be applied to prevent the alleged avoidance of taxation of capital gains from offshore indirect transfers of shares in companies with underlying assets in India (crude petroleum and natural gas fields). Cairn Energy plc Cairn UK Holdings Limited v Republic of India, PCA Case No 2016–7, Award (21 December 2020) paras 1261–1591, 1807–17. For an in-depth analysis, see Błażej Kuźniacki and Stef van Weeghel, 'Cairn Energy: When Retroactive Taxation Not Justified by Prevention of Tax Avoidance Is Unfair and Inequitable' (2023) 39(1) Arb Intl 125–54 <https://doi.org/10.1093/arbint/aiad003>. See also the analysis of that case from the perspective of the reparation (compensation and restitution) Prabhash Ranjan, 'Cairn Energy v India: Continuity in the Use of ILC Articles on State Responsibility' (2022) 37(1–2) ICSID Rev—FILJ 4–9.

[5] eg the application of the Russian version of the substance over form doctrine (the jurisprudential 'good faith taxpayer' doctrine) to levy enormous amounts of domestic profit tax and value added tax (VAT) by examining not only the form but also the substance of a particular transaction while determining its tax aspects, including the reattribution of the trading companies' revenue to the taxpayer (Yukos). See a series of Yukos v Russia cases—Yukos Universal Ltd (Isle of Man) v Russian Federation, PCA AA 227, Final Award (18 July 2014); Veteran Petroleum Ltd (Cyprus) v Russian Federation, PCA AA 228, Final Award (18 July 2014); Hulley Enterprises Ltd (Cyprus) v Russian Federation, PCA AA 226, Final Award (18 July 2014) paras 294, 301–02, 316, 394, 494, 613–14, 618, 624, 1558. Although the abuse of the Russia–Cyprus DTT was considered and found in that case, it was not done under the substance over form analysis, but due to the finding of blatant abusive tax avoidance in the form of round tripping, involving sham entities and transactions (existing only on paper). ibid paras 204–10, 244–46, 1549, 1615–21. See also Stef van Weeghel, 'Tax and Investment Treaties: A few Observations' in Georg Kofler, Ruth Mason and Alexander Rust (eds), Thinker, Teacher, Traveler: Reimagining International Tax (IBFD 2021) s 49.3. For more on Yukos v Russia in relation to analysis of international arbitration and taxation, see Ali Lazem and Ilias Bantekas, 'The Treatment of Tax as Expropriation in International Investor-State Arbitration' (2022) 38(1–2) Arb Intl 119–23; Sebastian G Martinez, 'Taxation Measures under the Energy Charter Treaty after the Yukos Awards Articles 21(1) and 21(5) Revisited' (2019) 34(1) ICSID Rev—FILJ 85–106; Ruth Teitelbaum, 'What's Tax Got to Do with It? The Yukos Tribunal's Approach to Motive and Treaty Interpretation' (2015) 12(5) Transnational Dispute Management.

[6] See the following judgments of the Supreme Court of Korea: Case No 65Nu91 (7 February 1967); Case No 90Nu1663 (12 October 1990); Case No 91Nu7170 (13 December 1991); Case No 90Nu10384 (27 July 1993); Case No 92Nu18603 (22 February 1994); Case No 99Do2165 (9 April 2002); Case No 2008Du8499 (19 January 2012); Case No 2010Du15179 (26 April 2012); Case No 2010Du25466 (25 October 2012); Case No 2011Du4411 (11 July 2013); Case No 2010Du11836 (24 June 2014); Case No 2010Du11836 (24 June 2014); Case No 2013Du7711 (26 Mar. 2015); Case No 2015Du2611 (15 December 2016); Case No 2013Du53084 (26 October 2017); Case No 2017Du59253 (28 December 2017). For a discussion on some of these cases, see Lone Star (n 1) paras 392–479. In the literature, see Hun Park and Sun Young Kim, 'International Tax Cases Involving Substance over Form Rules in Korea' (2018) 72(6) Bull Int Tax 398–400.

[7] The codified version of the Korean SOFD is called substance over form principle. It refers to the general principle of Korean tax law that embodies the substance over form doctrine and has been codified by the Korean legislature, with various modifications and updates (1967–2007). This principle aims to achieve the constitutional principle of equality in the area of tax law and taxation according to the ability to pay. In this article, the phrase SOFD will be used for consistency purposes. However, it also encompasses the phrase substance over form principle. See eg the following judgments of the Constitutional Court of Korea: Case No 89HeonMa38 (21 July 1989); Case No 92HeonBa49 (29 July 1992); Case No 2000HeonBa59 (26 April 2001). In Korea, the Supreme Court and the Constitutional Court exist separately, and the Constitutional Court has the authority to review the unconstitutionality of statutes, including tax laws. The Constitutional Court's decision that a statute is unconstitutional has binding effect on the Korean courts, including the Supreme Court. For the origin and evolution of the Korean substance over form principle, see Kyeong-Bong Ahn, 'Korean Report: Form and Substance in Tax Law' (2002) 87A IFA Cashiers 391–404; Kyung Geun Lee, 'Korean Report: Tax Treaties and Tax Avoidance—Application of Anti-Avoidance Provision' (2010) 95A IFA Cashiers 469–72, 475–80; Beomjune Kim and Hun Park, 'Korean Report: Anti-Avoidance Measures of General Nature and Scope—GAAR and Other Rules' (2018) 103 IFA Cashiers 5–24.

[8] Kim and Park (n 7) 11–12; Ji-Hyun Yoon, 'A Giant Leap for Fairer Tax or Blind Compromise with Public Opinion?—A Review of the New Case Law on "Substance-over-Form" by the Supreme Court of Korea' (2013) 13(1) J Korean Law 152.

[9] Lone Star (n 1) paras 396, 403 with references to the Supreme Court of Korea's Judgment, Case No 2010Du15179 (26 April 2012) and the Seoul Administrative Court's Judgment, Case No 2007Guhap37650 (16 February 2009).

[10] According to the OECD, SOFDs include rules and principles of interpretation which are not precluded by the rule and principles of interpretation of treaties of the Vienna Convention on the Law of Treaties (adopted 23 May 1969, entered into force 27 January 1980) 1155 UNTS 331 (VCLT) while interpreting and applying DTTs. See OECD, 'Commentary on Article 1, in Model Tax Convention on Income and on Capital: Condensed Version 2017' (18 December 2017) <https://www-oecd-org.libproxy.smu.edu.sg/ctp/treaties/model-tax-convention-on-income-and-on-capital-condensed-version-20745419.htm> accessed 6 December 2023 (the 2017 OECD Model)

of DTTs by denying their benefits stemming from abusive tax avoidance arrangements. The way this is done in practice, however, is often inconsistent and unpredictable, even in similar cases, because the key concept for SOFD—economic substance—is problematic and differs among legal systems.[11] For example, in the USA, a transaction is considered to have economic substance if it changes the taxpayer's economic position in a meaningful way, apart from federal income tax effects. It applies together with the business purpose test, according to which the taxpayer has to have a substantial non-tax purpose for entering into a transaction in order to be deemed to have a business purpose for entering into the transaction.[12] This is largely similar to the way in which Korean SOFDs operate. By comparison, in the European Union (EU), the Court of Justice of the European Union (CJEU) ultimately looks for a 'genuine' connection between companies and EU Member States, looking at the extent to which the companies physically exist there, in terms of premises, staff and equipment needed to carry out genuine economic activities on its own.[13] In the absence of such a genuine connection, tax benefits under EU treaties and EU secondary law will be denied.

The CJEU's approach towards identifying the economic substance resembles the criteria for benefiting from international investment agreements (IIAs) under denial of benefits (DoB) clauses. They aim to 'exclude from the protection afforded by applicable IIAs, investors and their investments who, although formally satisfying the definition of an investor, do not have a real (economic) connection with the home State'.[14] Although, in essence, DoB clauses and the principle of an abuse of rights converge to the same result and are grounded in similar

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paras 78–80. This OECD view, however, should be subject to a careful consideration on a case-by-case basis. The result of interpretation of DTTs in accordance with the rule and principles of interpretation under the VCLT will always trump a diverging result of interpretation under SOFDs since the former constitutes a codification of customary international law (CIL) legally binding all States and their authorities and courts while SOFDs are only 'views expressed by courts as to how tax legislation should be interpreted', to use the OECD's words cited above. See in respect to CIL: the International Court of Justice (ICJ), Kasikili/Sedudu/Island (Judgment) (13 December 1999) ICJ Rep 1059; the European Court of Human Rights (ECtHR), Golder v the United Kingdom (Judgement) (21 February 1975) 57 ILR 213–14; the Court of Justice of the European Union (CJEU), Firma Brita GmbH v Hauptzollamt Hamburg-Hafen (C-386/08), Judgment, ECLI:EU:C:2010:91 (25 February 2009) paras 42–43. cf Luc de Broe, International Tax Planning and Prevention of Abuse: A Study under Domestic Tax Law, Tax Treaties and EC Law in Relation to Conduit and Base Companies (IBFD 2008) 235; David A Ward, The Interpretation of Income Tax Treaties with Particular Reference to the Commentaries on the OECD Model (IBFD 2005) 15–16; Klaus Vogel and Rainer G Prokisch, 'General Report: Interpretation of Double Taxation Conventions' (1993) 78a IFA 66. However, SOFDs are more precise and focused on prevention of tax avoidance in comparison to the rule and principles of interpretation under the VCLT. Accordingly, tax authorities and courts are usually tempted to rely on SOFDs rather than on the VCLT's provisions in DTT-related tax avoidance cases. cf Briand J Arnold, 'The Interpretation of Tax Treaties: Myth and Reality' (2010) 1 Bull Int Tax 8. In the present article, the abbreviation 'cf' (compare) does not indicate that the views expressed here are directly supported by the text referred to. It means that the topic is discussed in such a way that it is relevant for the understanding of the issue discussed in the text.

[11] In 2007, Philip Baker warned against using an economic substance approach to determine the status of a beneficial owner, which inherently applies only in cross-border payments, not least because cross-border arrangements and transactions are usually accompanied by a detailed legal analysis. Thus, an application of a vague and broad concept of economic substance is not appropriate to determine beneficial owner status and may lead to far-reaching uncertainty in the application of tax treaties. Philip Baker, 'Beneficial Ownership: After Indofood' (2007) 6 Gray's Inn Tax Chambers 24. The concept of beneficial owner was also discussed by the Tribunal in relation to the application of the Korean SOFD. See Lone Star (n 1) para 395.

[12] The economic substance doctrine is a common law creation that has been part of the US tax law for over 85 years. Its origin can be traced to the US Supreme Court, Gregory v Helvering, Judgment (7 January 1935) 293 US 465, 469 (1935). Due to uncertainty and lack of uniformity it ensues, the US legislator decided for the codification of the economic substance doctrine in 2010. See Neha Rastogi, Fanny Karaman and Stanley C Ruchelman, 'The Economic Substance Doctrine: A US Anti-Abuse Rule' (2017) 4(9) Insights 1 <http://publications.ruchelaw.com/news/2017-09/Economic-Substance-Doctrine.pdf>. See also Peter C Canellos, 'Tax Practitioner's Perspective on Substance, Form and Business Purpose in Structuring Business Transactions and in Tax Shelters' (2001) 54(1) SMU L Rev 47–72; Lawrence Zelenak, 'Codifying Anti-Avoidance Doctrines and Controlling Corporate Tax Shelters' (2001) 54(1) SMU L Rev 177–94.

[13] See eg Cadbury Schweppes plc, Cadbury Schweppes Overseas Ltd, v Commissioners of Inland Revenue (C-196/04) ECLI:EU:C:2006:544, Judgment (12 September 2006) paras 67–68; X-GmbH v Finanzamt Stuttgart—Körperschaften (C-135/17) ECLI:EU:C:2019:136, Judgment (26 February 2019) paras 80–84; N Luxembourg 1, X Denmark A/S, C Danmark I, Z Denmark ApS (C-115/16, C-118/16, C-119/16, C-299/16) ECLI:EU:C:2019:134, Judgment (26 February 2019) para 131; T Danmark and Y Denmark Aps (C-116/16 and C-117/16) ECLI:EU:C:2019:135, Judgment (26 February 2019) para 104. See also Adolfo Martín Jiménez, 'International Investment Agreements and Anti-Tax Avoidance Measures: Incoherencies in the International Law System, "Systemic Interpretation" and Taxpayers' Rights' in Pasquale Pistone (ed), Building Global International Tax Law, Essays in Honour of Guglielmo Maisto (IBFD 2022) ss 4–5. For the evolutionary approach of the CJEU to the concept of abuse of rights under EU law and the economic substance, see Błażej Kuźniacki, 'X-GmbH v Finanzamt Stuttgart—Körperschaften: Abuse of Tax Law and Exchange of Tax Information in EU law' (2022) 85(2) MLR 488–506.

[14] See Loukas Mistelis and Crina Baltag, 'Denial of Benefits Clause' (July 2019) Max Planck Encyclopedias of International Law, para 3. The Caratube Tribunal explained that DoB clauses 'allows each of the parties to deny the benefits of the BIT's protection to a company that is controlled by nationals of a third State and does not have any substantial activities in the other State-party to the BIT'. See Caratube International Oil Company LLP v Republic of Kazakhstan, ICSID Case No ARB/08/12, Award (5 June 2012) para 354.

motives, authors argue that DoB clauses should be preferred to deny benefits under IIAs because only such clauses, as opposed to said principle, represent explicit (included in the text of the IIAs) views of the parties to the IIAs regarding the circumstances in which treaty benefits can be denied.[15]

Additionally, although some authors take the view that definitions of investors under IIAs should be interpreted to require the substance of a genuine link between the corporate investor and its home State, especially where the investor is deemed the intermediary company,[16] investor-State dispute settlement (ISDS) case law shies away from reading non-existing requirements of economic substance from definitions of investors under IIAs. The tribunals conferred the protection under IIAs to foreign investors even for round-tripping structures designed predominantly or solely to benefit from IIAs.[17] Only in a few cases did the tribunals deny access to IIAs to entirely or almost entirely sham or empty structures and companies while decoding the meaning of 'the real economic activities' in the definition of 'investor'[18] and during the examination of the application of DoB clauses with substantial business activity criteria under BITs.[19] In cases regarding a DoB clause under an ECT, the tribunals appeared to require very little substance to be considered as adequate under the substantial business activity criteria, accepting anything more than sham or zero substance at the level of the tested company.[20] Such an interpretative approach forges strong armour that protects all formally compliant treaty-shopping structures and heavily burdens States to manoeuvre around it by proving the investors' abusive behaviour.[21]

This introduction to the notion of economic substance shows that it is a problematic legal tool to deny benefits under treaties. Its broad scope and unclear contours appears to shift the burden of its application from a precise legal analysis to broad economic–factual determinations. This is very fact-sensitive and, if detached from the principle of abuse of rights and a strict application of the VCLT's rule and principles of treaty interpretation, could lead to the improper interpretation and application of tax and investment treaties.[22]

In Lone Star, the Tribunal considered whether the Respondent's refusal to accord the Claimants the benefits under the 1979 Korea–Belgium DTT[23] via a domestic (Korean) SOFD was arbitrary and discriminatory, thereby violating FET and other standards of investment protection under the 2011 Belgium–Luxembourg Economic Union (BLEU)–Korea bilateral investment treaty (BIT).[24] This implies that the violation of a DTT by a host State may trigger the violation of a BIT, in particular its FET.[25] In Lone Star, it mainly regarded the two components

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[15] Mark Feldman, 'Setting Limits on Corporate Nationality Planning in Investment Treaty Arbitration' (2012) 27(2) ICSID Rev—FILJ 283.

[16] See eg Olukunle Davis Oke, Towards Limiting Treaty Shopping in International Investment Law and Arbitration: A Critical Analysis of the Effectiveness of the Denial of Benefits Clause (University of Birmingham 2019) ProQuest Dissertations Publishing 41. See more broadly A Yilmaz Vastardis, The Nationality of Corporate Investors under International Investment Law (Bloomsbury 2021) 179–251.

[17] eg Tokios Tokelės v Ukraine, ICSID Case No ARB/02/18, Majority Decision on Jurisdiction (29 April 2004) para 36 (Dissenting: Prosper Weil, Presiding); Yukos v Russia cases (n 5) paras 1368–70.

[18] Alps Finance and Trade AG v The Slovak Republic, UNCITRAL, Award (5 March 2011) paras 217–18, 222–26; Pac Rim Cayman LLC v Republic of El Salvador, ICSID Rules, ICSID Case No ARB/09/12, Decision on the Respondent's Jurisdictional Objections (1 June 2012) paras 4.63–4.78.

[19] Guaracachi America, Inc and Rurelec plc v Plurinational State of Bolivia, PCA Case No 2011–17, Award (31 January 2014) paras 370–84.

[20] See eg Limited Liability Company Amto v Ukraine, SCC Rules, SCC Case No 080/2005, Award (26 March 2008) para 69; Masdar Solar & Wind Cooperatief UA v Kingdom of Spain, ICSID Rules, ICSID Case No ARB/14/1, Award (16 May 2018) paras 206, 224–25, 254.

[21] See Błażej Kuźniacki, 'European Union Law and Global Investment Regime: Unshell Proposal as a Next (Mis)step of the EU Against Investment Treaty Arbitration?' (2023) 50(11) Intertax 799–800.

[22] This observation will be examined in the present article, in particular in Sections IV–V.

[23] Convention between the Republic of Korea and the Kingdom of Belgium for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (signed 29 August 1977, entered into force 19 September 1979).

[24] Agreement between the Government of the Republic of Korea and the Belgium–Luxembourg Economic Union for the Reciprocal Promotion and Protection of Investments (signed 12 December 2006, entered into force 27 March 2011) (BLEU).

[25] This observation cannot be overstated because it shows that investors may have the only chance to directly enforce DTT commitments of a host State via ISDS mechanisms under a BIT. Neither mutual agreement procedure (MAP) nor arbitration under DTTs are comparable to the ISDS under BITs since they have a purely administrative nature thereby 'operating within an entirely non-transparent framework that seems like a relic of the past in which tax authorities exercised absolute power and taxpayers hardly had any rights'. In respect of MAPs, see Pasquale Pistone, 'General Report' in Michael Lang and others (eds), The Impact of Bilateral Investment Treaties on Taxation (IBFD 2017) s 1.8.2. Moreover, MAPs are often criticised by tax experts for 'being inefficient and non-transparent and because they may lead to decisions that are not based on legal principles'. A similar evaluation concerns arbitration clauses under DTTs insofar as they 'are based on the inter-administrative logic of mutual agreement procedures and give no comprehensive procedural rights

of FET of relevance in respect of an application of the 1979 Korea–Belgium DTT: (i) protection of the reasonable legitimate expectations of foreign investors that they are entitled to benefits under the DTT and (ii) conduct of a host State in good faith while interpreting and applying of the DTT.[26] Given that the Korean SOFD aims to prevent abusive tax practices, the Tribunal could have undertaken its analysis from the perspective of the principle of an abuse of rights[27] in order to have an interpretation of broadly formulated FET under the 2011 BLEU–Korea BIT in the Lone Star tax litigation.[28] In Lone Star, the principle of an abuse of rights could guide the Tribunal not only to test whether the Respondent denied the DTT's benefits by applying the SOFD in good faith, but also whether the Claimants intended to obtain those benefits in good faith by establishing their tax scheme. Although the Tribunal did not appear to explicitly rely on the principle of an abuse of rights in its reasoning, this article will underscore the relevance and importance of that principle in tax-related investment-treaty arbitration cases.[29]

Beyond the relations between the Korean SOFD and the DTT and the BIT, the Lone Star Tribunal addressed other key issues.[30] These included: (i) the allegation of wrongful interference by Korea's financial regulator—the Financial Services Commission (FSC), in the sale of shares in Korean Exchange Bank (KEB) to Hana Financial Group, Inc and its subsidiary Hana Bank (Hana), leading to a share price reduction; (ii) the supposed contributory fault of the Claimants to the reduced share price; and (iii) the request to gross up the Award's compensation with income taxes that the Claimants would be obliged to pay in Belgium. For the first issue, the majority of the Tribunal observed that the Respondent had violated the FET under the 2011 BLEU–Korea BIT through its arbitrary and unreasonable acts of the FSC with regard to Lone Star's sale of shares in KEB to Hana, contributing to its price reduction of US$433 million.[31] The analysis of the second issue, intertwined with the first one, led the majority of the Tribunal to the conclusion that Lone Star had contributed to its loss equally with the Respondent in respect of the price reduction due to stock manipulation, constituting a financial crime under Korean law.[32] As

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to the taxpayer concerned'. Arno E Gildemeister, 'Chapter 12: Germany' in Michael Lang and others (eds), The Impact of Bilateral Investment Treaties on Taxation (IBFD 2017) s 12.8. It is therefore no surprise that the Tribunal in the Cairn v India case explicitly dismissed the comparability of the MAP under Article 27(2) of the UK–India DTT with the ISDS clause under Article 9 of the UK–India BIT. Cairn (n 4) para 806.

[26] cf Lone Star (n 1) para 714. In respect to the mentioned components of FET, see Técnicas Medioambientales TECMED SA v United Mexican States, ICSID Case No ARB(AF)/00/2, Award, 29 May 2003 (Tecmed v Mexico) para 154.

[27] The principle of abuse of rights has been recognised as a general principle of law (GPL) under Article 38(1)(c) of the Statute of the ICJ (signed 26 June 1945, entered into effect 24 October 1945)—one of many manifestations of the principle of good faith—by several investment tribunals. For the relevant case law and analysis, see Patrick Dumberry, A Guide to General Principles of Law in International Investment Arbitration (OUP 2020) 61.

[28] cf Stephan W Schill, 'General Principles of International Law and International Investment Law' in Tarcisio Gazzini and Eric De Brabandere (eds), International Investment Law: The Sources of Rights and Obligations (Brill 2012) 157. In similar vein, see M Hirsh, 'Sources of International Law' in Andrea K Bjorklund and August Reinisch (eds), International Investment Law and Soft Law (Elgar Edward 2012) 27.

[29] See Section V.

[30] Not discussed in detail in this article.

[31] In particular, the majority of the Tribunal noted that 'the FSC misconduct was not directed to a "legitimate policy aim" but to its own self-interest'. Moreover, 'the successful efforts of the FSC to secure a price reduction despite its acknowledgment to the National Assembly that the terms of a private agreement, including price, was not within the FSC mandate, and delaying approval until a price reduction was achieved, the FSC exercised its regulatory role arbitrarily and in bad faith' (Lone Star (n 1) paras 781–82, 791, 948(a)).

[32] ibid paras 796, 948(c). Criminal judgments in stock price manipulation cases confirming relevant facts played a crucial role in the Tribunal's analysis. See Supreme Court of Korea, Case No 2008Do6335, Judgment, 10 March 2011; Seoul High Court, Case No 2011No806, Judgment, 6 October 2011. In arriving at its conclusion, the Tribunal examined ISDS case law and literature of relevance for the doctrine of 'contributory fault'. For the ISDS case law referenced by the Lone Star Tribunal, see Yukos v Russia (n 5) paras 1600, 1608, 1633–37; Occidental Petroleum Corporation and Occidental Exploration and Production Company v Republic of Ecuador, ICSID, ARB/06/11, Award (5 October 2012) paras 422, 661, 674–87; MTD Equity Sdn. Bhd and MTD Chile SA v Republic of Chile, ICSID Case No ARB/01/7, Award (25 May 2004) paras 242–43; Iurii Bogdanov, Agurdino-Invest Ltd and Agurdino-Chimia JSC v Republic of Moldova, SCC, Award (22 September 2005) ss 4.1 and 4.2.4; Alex Genin, Eastern Credit Limited, Inc and AS Baltoil v Republic of Estonia, ICSID Case No ARB/99/2, Award (25 June 2001) para 345. See also reference to Case Concerning the Factory at Chorzów (Germany v Poland), PCIJ, Judgment No 13 (13 September 1928) 47 and to Articles 35–36 of the International Law Commission (ILC), Responsibility of States for Internationally Wrongful Acts (Yearbook of the International Law Commission 2001) vol II (Part Two). For the literature cited by the Tribunal, see Brigitte Bollecker-Stern, Le préjudice dans la théorie de la responsabilité internationale (Pedone 1973) 328; Sergey Ripinsky and Kevin Williams, <https://www.biicl.org/books/damages-in-international-investment-law> Damages in International Investment Law (British Institute of International and Comparative Law 2008) 314–19; Martin Jarett, Contributory Fault and Investor Misconduct in Investment Arbitration (CUP 2019) 54; Mark Kantor, Valuation for Arbitration: Compensation Standards, Valuation Methods and Expert Evidence (Kluwer Law International 2008) 110–11. In the view of the facts of the case, as supported by the analysed case law and literature, the majority of the Tribunal stated that 'there was a single

for the tax gross-up of the amount of the Award's compensation, despite undecided ISDS case law in that regard,[33] the Tribunal did not reject that claim as inadmissible per se. Nevertheless, the Tribunal concluded that a tax gross-up must be rejected because the Claimants did not provide essential evidence about the quantum of their tax liability to which they might, even potentially, become liable.[34]

The discussion here is limited to the compatibility of the SOFD with tax and investment treaties, notably the principles of good faith and the FET. While the Award was issued with concurring (Charles N Brower) and dissenting (Brigitte Stern) opinions, this article focuses solely on the issue decided by the Full Tribunal.[35] There are several reasons why the article focuses exclusively on the compatibility of the Korean SOFD's application to the 2011 BLEU–Korea BIT in the context of the Lone Star tax scheme. First, the impact of interplay between domestic anti-tax avoidance measures and tax treaties on IIAs has never been discussed by tribunals or (according to this author's research) scholars in depth. Thus, the chosen topic is novel. Second, this topic is good to shed light on a converging interpretation of tax and investment treaties, especially in difficult borderline cases between abusive and legitimate tax and investment practices. In that regard, the article highlights the need to consider the principle of an abuse of rights while examining the compatibility of the Korean SOFD with the BIT and the DTT. Such an approach could enhance the rule of law in the interpretation of tax and investment treaties in other similar cases. Third, it is increasingly more important to properly understand the concept of economic substance insofar as DoB clauses in investment treaties and ISDS case law and principal purposes test (PPT) in tax treaties appear to specifically prevent abuses of those treaties by arrangements with no or insufficient economic substance.[36]

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indivisible loss to which both the Claimants and the Respondent made a material contribution. The loss cannot be broken down into individually distinct elements that could be assigned exclusively to Lone Star or the FSC. Lacking any such logical division, the entire amount must simply be apportioned.' Since 'it would be unreasonable to attribute a greater share of the fault to one party than to the other', '[i]t is appropriate in the circumstances that the loss be shared equally'. Lone Star (n 1) paras 839 and 895. The doctrine of 'contributory fault' concerns the doctrine of 'clean hands'. However, the latter doctrine is, much broader and concerns, for example, the admissibility of the claim. See Alyosius Llamzon, 'Yukos Universal Limited (Isle of Man) v The Russian Federation: The State of the "Unclean Hands" Doctrine in International Investment Law: Yukos as Both Omega and Alfa' (2015) 30(2) ICSID Rev—FILJ 316; Alyosius Llamzon and Anthony Sinclair, 'Investor Wrongdoing in Investment Arbitration: Standards Governing Issues of Corruption, Fraud, Misrepresentation and Other Investor Misconduct' in Albert Jan van den Berg (ed), Legitimacy: Myths, Realities, Challenges (18 ICCA Congress Kluwer 2015) 451, 509; Patrick Dumberry and Gabrielle Dumas-Aubin, 'The Doctrine of "Clean Hands" and the Inadmissibility of Claims by Investors Breaching International Human Rights Law' in Ursula Kriebaum (ed), Transnational Dispute Management Special Issue: Aligning Human Rights and Investment Protection (TDM 2013) 3.

[33] Ioan Micula, Viorel Micula and others v Romania, ICSID Case No ARB/05/20, Award (11 December 2013) paras 1180–81; Mobil Investments Canada Inc and Murphy Oil Corporation v Canada, ICSID Case No ARB(AF)/07/4, Decision on Liability and on Principles of Quantum (22 May 2012) para 485; Les Laboratoires Servier, SAS, Biofarma, SAS and Arts et Techniques du Progrès SAS v Republic of Poland, UNICTRAL, Final Award (14 February 2012) para 666; Československá Obchodní Banka, AS v Slovak Republic, ICSID Case No ARB/97/4, Award (29 December 2004) para 367. As noted by Stefano Castagna, in some cases, tribunals have decided how the compensation will be provided (net instead of gross of local taxes), eg Tenaris SA & Talta—Trading e Marketing Sociedade Unipessoal Lda v Bolivarian Republic of Venezuela, ICSID Case No ARB/12/23, Award (12 November 2016) para 790, or to whom, eg PSEG Global, Inc, The North American Coal Corporation, and Konya Ingin Electrik Üretim ve Ticaret Ltd Sirketi v Republic of Turkey, ICSID Case No ARB/02/5, Award (19 January 2007) para 338: "with the view of impeding abuses of the respondent state (such as taxing the award with a 99 per cent tax rate on 100 per cent of the amount awarded). If a tribunal found to have the power to ensure the amount of net compensation owed versus the respondent and through the aid of applicable DTTs determined whether and how the amounts will be taxed in other jurisdictions, this would already constitute a step forward in ensuring full compensation with a greater certainty." (Stefano Castagna, 'Essential Elements of Taxation—Investment Protection and Dispute Settlement' in José Rafael Mata Dona and Nikos Lavranos (eds), International Arbitration and EU Law (Edward Elgar 2021) 436).

[34] Interestingly, it seems that 'the sophisticated tax planning' of Lone Star worked against its claim for grossing up of the Award's quantum with a hypothetical income tax: "Given the sophistication of Lone Star's tax planning, the Tribunal is unable to predict with confidence the amount required to 'gross up' the award, even if the Tribunal were inclined to do so. The Tribunal has not been made privy to the Claimants' actual tax situation. The lack of evidence from an independent tax expert on Lone Star's alleged tax exposure further weakens the claim." (Lone Star (n 1) 906).

[35] However, it is worth noting that para 365 of Lone Star (n 1) only refers to the view of the majority of the Tribunal: 'In the view of the Tribunal majority, the Respondent's objection to standing is not fatal to the tax claims for two reasons'. Still, the entire Tribunal undertook the examination of the compatibility of the application of Korean SOFD with the BIT and the DTT. See eg Lone Star (n 1) para 410: 'The Tribunal concludes that Korea's application of the Substance Over Form doctrine did not violate the BIT because, as referenced by Dr. - the doctrine forms "part of the basic rules for determining the facts that give rise to tax liability"'. Neither the concurring nor the dissenting opinion focused on the questions analysed in this article.

[36] On DoBs, see Loukas Mistelis and Crina Baltag, 'Denial of Benefits Clause' (July 2019) Max Planck Encyclopedias of International Law, paras 1–11; Yas Banifatemi, 'Taking into Account Control in Denial of Benefits Clauses' in Yas Banifatemi (ed), Jurisdiction in Investment Treaty Arbitration (IAI Series 8/2018) 235; Davis Oke (n 16) 38, 41, 120, 140; Anthony Sinclair, 'The Substance of Nationality Requirements in Investment Treaty Arbitration' (2005) 20(2) ICSID Rev—FILJ 357–85. For PPT, see Wolfgang Schön, 'The Role of "Commercial Reasons" and "Economic Reality" in the Principal Purpose Test under Article 29(9) of the 2017 OECD Model' in Pistone (n 13) ss 12.4.2.4 and 12.6; Stef van Weeghel, 'A Deconstruction of the Principal Purposes Test' (2019) 11 World Tax J 10, 44;

Fourth, global and regional tax developments, including the implementation of anti-BEPS (base erosion and profit shifting) rules,[37] as well as Pillar Two rules (global minimum tax of 15 per cent),[38] seem to have influenced the wording of modern IIAs. The Lone Star Award also appears to have had an important impact on Korean IIAs. For example, free trade agreements (FTAs) concluded by Korea with New Zealand[39] and Australia[40] and other IIAs[41] indicate that 'a taxation measure that is consistent within internationally recognised tax policies, principles and practices should not constitute an expropriation; [i]n particular a taxation measure aimed at preventing the avoidance or evasion of taxation measures generally does not constitute an expropriation'. In light of these developments, the question is whether SOFDs or other domestic measures based on an economic substance approach always constitute relevant taxation measures aimed at preventing the tax avoidance consistently with internationally recognised tax policies, principles and practices, or whether they should be examined on a case-by-case basis.

The hypothesis of this article is that examining the compatibility of application of domestic anti-tax avoidance measures with IIAs, such as SOFDs, should require tribunals to undertake a standalone legal analysis in accordance with the rule and principles of interpretation under the VCLT[42] and the principle of an abuse of rights, rather than relying only or predominantly on the documentation of the Organisation for Economic Co-operation and Development (OECD), as interpreted by tax expert witnesses. The Tribunal in Lone Star failed to do so, presumably because of the treatment of the Korean SOFD and the 1979 Belgium–Korea DTT as fact, rather than law, and denying that it had jurisdiction under the 1979 Belgium–Korea DTT.[43] As a result, the Tribunal relied on evidence from tax expert witnesses heavily influenced by the OECD documentation, instead of interpreting the 1979 Belgium–Korea DTT for the purposes of determining the impact of the Korean SOFD on that DTT and indirectly also on the 2011 BLEU–Korea BIT.

De lege lata the Tribunal was not incorrect in determining the compatibility of Korea's application of the SOFD with the 2011 BLEU–Korea BIT, due to the fact that local tax litigation did not constitute a denial of justice and the Claimants had failed to prove any other violations of standards of investment protection.[44] However, de lege ferenda it could have significantly increased the quality of the Award by appropriately interpreting the DTT and its relations with the Korean SOFD in accordance with the VCLT's rule and principles of interpretation, including the reliance on the principle of an abuse of rights and other relevant principles of law.[45]

Błażej Kuźniacki, 'The Principal Purpose Test (PPT) in BEPS Action 6 and the MLI: Exploring Challenges Arising from Its Legal Implementation and Practical Application' (2018) 10 World Tax J 267–72.

[37] According to the OECD, BEPS 'refers to tax planning strategies used by multinational enterprises that exploit gaps and mismatches in tax rules to avoid paying tax'. Working together within OECD/G20 Inclusive Framework on BEPS, 142 countries and jurisdictions (as of today, ie 9 May 2023) 'are collaborating on the implementation of 15 measures to tackle tax avoidance, improve the coherence of international tax rules and ensure a more transparent tax environment' OECD, What Is BEPS? <https://www.oecd.org/tax/beps/about/> accessed 6 December 2023.

[38] For the relevant sources released in 2021–23, see OECD, 'Tax Challenges Arising from the Digitalisation of the Economy—Global Anti-Base Erosion Model Rules (Pillar Two)' <https://www.oecd.org/tax/beps/tax-challenges-arising-from-the-digitalisation-of-the-economy-global-anti-base-erosion-model-rules-pillar-two.htm> accessed 6 December 2023.

[39] Taxation and Expropriation of the Free Trade Agreement between New Zealand and the Republic of Korea (signed 8 April 2014, entered into force 12 December 2014) Annex 10-E, para (b).

[40] Taxation and Expropriation of the Free Trade Agreement between the Government of Australia and the Government of the Republic of Korea (signed 8 April 2014, entered into force 12 December 2014) Annex 11-I, para (b).

[41] eg Taxation and Expropriation in the Agreement between the Government of the State of Israel and the Government of the United Arab Emirates on Promotion and Protection of Investments (signed 20 October 2020, entered into force 27 December 2021) Annex C, para 2; Agreement between the Government of the Republic of Kazakhstan and the Government of the Republic of Singapore on the Promotion and Mutual Protection of Investments (signed 21 November 2018, not yet in force) art 21(3)(b).

[42] The 1979 Belgium–Korea DTT is a treaty according to the very definition of 'a treaty' under Article 2(1)(a) of the VCLT. Thus, the VCLT's rule and principles of interpretation apply to the interpretation of the 1979 Belgium–Korea DTT. From a purely domestic perspective, however, the 1979 Belgium–Korea DTT can be seen as domestic law. This follows from Article 6(1) of the Korean Constitution, which provides that the treaties promulgated by the Constitution and the generally approved international laws have the same effect as the domestic laws of the Republic of Korea. See Myung-Hyun Chung, 'Korea's Judicial Interpretation and Application of International Law' (2020) 10(1) KLRI J Law Legislation. In any case, the 1979 Belgium–Korea DTT remains 'a treaty' under the VCLT.

[43] Lone Star (n 1) paras 296 and 372(b).

[44] Lone Star (n 1) paras 443, 465, 469, 479.

[45] For example, Article 31(3)(c) of the VCLT includes the principle of systemic integration according to which the 'relevant rules of international law applicable in the relations between the parties' must be taken into account when identifying the context of the terms of

This methodological approach was justified irrespective of whether the Korean SOFD and the 1979 Belgium–Korea DTT were treated as law or fact, because even if they were treated as fact only, an appropriate interpretation was still necessary in order to understand the material consequences of their application on the 2011 BLEU–Korea BIT for the actors in question.[46] This would lead the Tribunal to enhance the rule of law and benefit the entire ISDS and international tax community. Choosing a different methodology directed the Tribunal to observations that could lead to a misinterpretation of IIAs and DTTs in cases concerning tax avoidance.[47]

After briefly setting out the background of the dispute (Section II), the article presents the Tribunal's assessment of the Korean SOFD's application in the Lone Star tax litigation (Section III); and answers questions about what the Tribunal overlooked in respect of the Korean SOFD's relations with DTTs, and what consequences this may lead to (Section IV). This article ultimately evaluates the importance and relevance of the Lone Star Award in determining the compatibility of SOFDs with DTTs and IIAs and emphasises the need for further comparative research on the role of the substance over form approach in applying the principle of abuse of rights under DTTs and IIAs (Section V).

II. FACTUAL BACKGROUND

The Lone Star case can be traced back to 1997–98. At that time, Korea was among the economies most severely impacted by the Asian Debt Crisis. Lone Star, a private equity fund from Texas, seeking assets it considered undervalued, was one of the foreign investors starting to invest in Korea around then.[48] Foreign investments in Korea at that time were typically concluded via special purpose entities (SPEs)[49] established in Ireland, Belgium, Luxembourg and Labuan (Malaysia), in order to eliminate or limit Korean taxes on the returns from the

a treaty. In that respect, the 1979 Belgium–Korea DTT could be deemed as a treaty containing rules of international law applicable between the parties of the 2011 BLEU–Korea BIT. cf Cairn (n 4) para 808(b): 'Article 31(3)(c) of the VCLT mandates that the "relevant rules of international law applicable in the relations between the parties" must be taken into account when identifying the context of the terms of a treaty. The UK–India DTAA indisputably contains rules of international law applicable between the Parties to the BIT.' The abbreviation DTAA stands for double tax avoidance agreement, ie DTT.

[46] There are conflicting views in respect of treating domestic law either as fact or law for purposes by international courts and tribunals. For the proponents of treating domestic law as fact, see Ian Brownlie, Principles of Public International Law (OUP 2008) 38. In international case law, see PCIJ, Certain German Interests in Polish Upper Silesia (Germany v Poland) Judgment (25 May 1926), Series A No 7 (1926) 19; Bayindir Insaat Turizm Ticaret ve Sanayi AŞ v Pakistan, ICSID Case No ARB/03/29, Award (27 August 2009) para 135; International Thunderbird Gaming Corporation v Mexico, UNCITRAL, Award (26 January 2006) para 127; Vincent Ryan v Poland, ICSID Case No ARB(AF)/11/3, Award (24 November 2015) para 347. For the proponents of treating domestic law as law, see Clarence Wilfred Jenks, 'The Interpretation and Application of Municipal Law by the Permanent Court of International Justice' (1938) 19 BYIL 67, 68; Michel Virally, 'The Sources of International Law' in Max Sorensen (ed), Manual of Public International Law (Macmillan 1968) 171; Sharif Bhuiyan, National Law in WTO Law (CUP 2007) 216; Jarrod Hepburn, Domestic Law in International Investment Arbitration (OUP 2017) 105–08. cf Martin Jarett, 'The International Validity of Domestic Law in Investment-Treaty Arbitration' (2023) 39(1) Arb Intl 2 (advance access online publication 4 February 2023). In international case law, see Elettronica Sicula SpA (ELSI) (US v Italy), Judgment (20 July 1989) [1989] ICJ Rep 15, para 99; Trail Smelter Case (US v Canada) RIAA vol III (1941), Award (16 April 1938 and 11 March 1941) 1905, 1949; Bayview Irrigation District v Mexico, ICSID Case No ARB(AF)/05/1), Award (19 June 2007) paras 109–18; Bernhard von Pezold v Zimbabwe, ICSID Case No ARB/10/15, Award (28 July 2015) para 736; Perenco Ecuador Ltd v Ecuador, ICSID Case No ARB/08/6, Decision on Remaining Issues of Jurisdiction and on Liability (12 September 2014)) para 522. The present author is inclined to agree with the proponents of treating domestic law as law.

[47] cf Brigitte Stern (dissenting opinion) paras 3–4: "I cannot refrain from expressing my profound concern regarding the form of the Award, i.e., the structure and developments of the Tribunal's analysis, which mixes the Parties' positions with the Tribunal's statements and 'Tribunal's Ruling[s]', in a manner that does not appear orderly and could lead to misinterpretations, thus making it often difficult to follow the Tribunal's reasonings in the Award from point A to point B. This being said, my main concern is that I consider that the majority has not applied the proper international law on State responsibility to the facts of the case, neither relating to attribution, nor to causation."

[48] Lone Star (n 1) paras 114, 118, 146.

[49] According to the nomenclature of the OECD, an enterprise is usually considered an SPE if it meets the following criteria: (i) the enterprise is a legal entity, (a) formally registered with a national authority; and (b) subject to fiscal and other legal obligations of the economy in which it is resident; (ii) the enterprise is ultimately controlled by a non-resident parent, directly or indirectly; (iii) the enterprise has no or few employees, little or no production in the host economy and little or no physical presence; (iv) almost all the assets and liabilities of the enterprise represent investments in or from other countries; and (v) the core business of the enterprise consists of group financing or holding activities, that is—viewed from the perspective of the compiler in a given country—the channelling of funds from non-residents to other non-residents. However, in its daily activities, managing and directing local operations plays only a minor role. An entity (company) that meets those five criteria can be considered an SPE. OECD, Benchmark Definition of Foreign Direct Investment. Fourth Edition (2008) para 558. An SPE, in the OECD's nomenclature, can therefore be equated with an intermediary entity most often used for treaty or directive shopping. See de Broe (n 10) 5–40.

investments by a combination of preferable domestic tax laws of the resident States of SPEs and benefits under their DTTs ratified with Korea.[50] Officials from the Korean Ministry of Finance and Economy acknowledged that these DTTs were ‘a necessary evil’ in the 1970s, as Korea sought additional foreign capital to spur economic growth.[51] Lone Star followed this tax route, by investing from the level of ‘upper tier’ limited partnerships from Delaware via various intermediate entities in jurisdictions such as Bermuda, and then via SPEs from Belgium, which become the direct owners of the assets (shares and real estate) located in Korea.[52] One such SPE was LSF-KEB Holdings SCA (LSF-KEB), a Belgian corporation that made a major investment in 2003 by acquiring a controlling interest in Korea’s third largest commercial bank at that time (and sixth largest bank overall)—KEB. Three other important investments made by Lone Star, including through another Belgian SPE—Star Holdings SCA—concerned the acquisition of shares in Star Tower Corporation (Star Tower, a Korean company that owned a large office building in the business district of Seoul), Kukdong Engineering and Construction Co., Ltd (Kukdong, a Korean construction company) and Star Leasing and Finance Co. (Star Lease).[53]

In 2012, LSF-KEB, Star Holdings SCA and other claimants initiated arbitration proceedings against the Republic of Korea under the 2011 Belgium–Luxembourg Economic Union (BLEU)–Korea BIT[54] and the ICSID Convention.[55] The Claimants arbitrated mainly against two measures taken by the Respondent:[56] (I) the arbitrary and unreasonable acts of the FSC pertaining to the sale of shares in KEB to Hana, contributing to their price reduction; and (II) the taxation of income achieved from the four Korean investments,[57] which took place by denying LSF-KEB and Star Holdings SCA benefits under the 1979 Korea–Belgium DTT via the application of the Korean SOFD in an arbitrary and discriminatory way by the Korean National Tax Service (NTS) and Korean courts, thereby violating the FET under the 2011 BLEU–Korea BIT.[58] This article focuses only on the latter allegation, which concerned a very big amount of the tax-related claims.[59]

Although the Tribunal made it very clear that it had no jurisdiction under the 1979 Belgium–Korea DTT,[60] it admitted that the application of the Korean SOFD by the NTS and Korean courts to deny benefits under that DTT was the central tax-related issue to be examined for its conformity with the 2011 BLEU–Korea BIT:

> A central issue in the tax litigation brought by Lone Star is whether Korea’s ‘Substance Over Form’ doctrine is compliant with the Korea–Belgium Tax Treaty or, if it is, whether it has been applied in conformity with the BIT.[61]

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[50] Lone Star (n 1) para 119.

[51] ‘S. Korea Wants to Rewrite its Tax Treaties’ Hankyoreh Daily (10 July 2007) <https://www.hani.co.kr/arti/english_edition/e_business/221456.html> accessed 10 April 2023.

[52] Lone Star (n 1) paras 115–16, 119.

[53] ibid paras 147–49.

[54] BLEU (n 24). In fact, the Claimants also tried to initiate arbitration under the 1976 BIT (as renewed via the 2011 BIT), ie Agreement between the Republic of Korea, on the one hand, and the Belgo-Luxemburg Economic Union, on the other hand, on the Encouragement and Reciprocal Protection of Investments (signed 20 December 1974, entered into force 3 September 1976). However, the Tribunal found that the Claimants’ investments do not qualify for treaty protection under the earlier BIT (ie, it did not cover investments in banking, finance, real estate or construction) and, thus, the Tribunal does not have jurisdiction under that BIT. Lone Star (n 1) paras 17(a), 280.

[55] Convention on the Settlement of Investment Disputes between States and Nationals of Other States (18 March 1965, entered into force 14 October 1966).

[56] Lone Star (n 1) paras 1–11.

[57] ie (i) the sale of shares in Star Tower in 2004; (ii) the sale of shares in Kukdong and Star Lease and the sale of a 13.6 per cent block of shares in KEB in 2007, along with the dividends paid by KEB, Kukdong and Star Lease between 2004 and 2007; (iii) the dividends paid by KEB between 2008 and 2011; and (iv) the sale of the remaining 51 per cent of shares in KEB to Hana in 2012. ibid 430.

[58] Allegations were also made with respect to a breach of Respondent’s obligation to provide full protection and security by withholding benefits that should have been afforded by the 1979 Korea–Belgium DTT, the breach of the national treatment (NT) and most-favoured nation (MFN) treatment obligations by treating Lone Star less favourably than Korean investors and investors of third countries, a violation of the Respondent’s obligation under the umbrella clause by disrespecting its written obligations under the 1979 Korea–Belgium DTT, all this amounting to expropriation and preventing the Claimants’ free transfer of the full amount of their returns. ibid paras 382–86. All of these claims were rejected by the Tribunal as lacking any persuasive factual or legal foundation. ibid paras 469–89.

[59] Lone Star (1) para 361: ‘The tax-related claims account for almost USD 1.5 billion of the total of almost USD 4.7 billion claimed in compensation.’

[60] ibid paras 296 and 372(b).

[61] ibid para 390.

This implies that the Tribunal analysed the compatibility between the application of Korean SOFD and the 1979 Korea–Belgium DTT for the purposes of deciding about the compatibility the fiscal conduct of the Respondent based on the Korean SOFD with the 2011 BLEU–Korea BIT.[62] Thus, the obvious lack of the Tribunal's jurisdiction under the 1979 Belgium–Korea DTT did not remove its analysis of the interplay between the Korean SOFD and the 1979 Belgium–Korea DTT from the ambit of the investment treaty arbitration.[63]

This is in conformity with the Cairn Tribunal's dichotomy between a tax-related investment dispute—a dispute concerning 'alleged violations of an investment treaty resulting from certain sovereign measures taken by the Respondent in the field of taxation', and a tax dispute proper—a dispute 'concerning the taxability (including the tax-amount) of a specific transaction'.[64] In Lone Star, a tax (treaty) related investment dispute concerned the interplay between the application of Korean SOFD and the 1979 Korea–Belgium DTT only to determine whether the application was compatible with the 2011 BLEU–Korea BIT. A tax dispute proper under the 1979 Korea–Belgium DTT was decided on earlier by the Korean tax authorities and courts.

The Tribunal relied significantly on the OECD Commentaries on the Model Tax Convention,[65] as presented to the Tribunal by expert witnesses on tax matters. It found that Korea's SOFD had not been applied in an arbitrary and discriminatory way by the NTS and Korean courts, because its application was grounded on evidence and was 'well within the legal boundaries of internationally accepted tax policy' in accordance with the OECD's commentaries.[66]

This Award represents the first acceptance of SOFD in an ISDS tax-related case, ie it was implicitly considered by the Tribunal suitable to prevent an abuse of the DTT, and thus explicitly not violating the BIT. The article will now look more closely at that matter and the reasoning of the Tribunal.

III. THE TRIBUNAL'S ASSESSMENT OF THE KOREAN SOFD'S APPLICATION IN THE LONE STAR TAX LITIGATION TO DECIDE ON ITS COMPATIBILITY WITH THE BIT

The Tribunal decided that it only had jurisdiction over tax issues allegedly violating the 2011 BLEU–Korea BIT concerning the taxation of dividends paid by KEB between 2008 and 2011 and the sale of the remaining 51 per cent of shares in KEB to Hana in 2012.[67] Pursuant to the relevant provisions of the 1979 Belgium–Korea DTT, this taxation was reduced (Article 10(2))—dividend payments) and exempted (Article 13(3)—capital gains) from taxation in Korea, respectively. The central issue in the Lone Star tax litigation was whether a denial of benefits under those provisions by the NTS and Korean courts through applying the Korean SOFD was compatible with the 1979 Belgium–Korea DTT. The central question for the Tribunal in respect of the main tax-related allegations of the Claimants was whether this taxation measure was applied in conformity with the 2011 BLEU–Korea BIT.

[62] Lone Star (1) paras 390–489.
[63] Robert Danon, 'Relation between Dispute Resolution under Double Taxation Conventions and Investment Treaties' in Werner Haslehner and others (eds), Alternative Dispute Resolution and Tax Disputes (Edward Elgar 2023) 229.
[64] Cairn (n 4) para 793. By the same token, ie that tax measures are arbitrable under IIAs and they may violate their standards of investment protection, such as the FET or indirect expropriation, see EnCana Corporation v Republic of Ecuador, LCIA Case No UN3481, Award (3 February 2006) para 177; Burlington Resources, Inc v Republic of Ecuador, ICSID Case No ARB/08/5, Decision on Liability (14 December 2014) para 395; Occidental Exploration & Production Co v Republic of Ecuador, LCIA Case No UN3467, Final Award (1 July 2004) para 85. In a similar vein, see Thomas W Wälde and Abba Kolo, 'Investor-State Disputes: The Interface between Treaty-Based International Investment Protection and Fiscal Sovereignty' (2007) 35 Intertax 427, 432, 434; Arno E Gildemeister, L'arbitrage des différends fiscaux (LGDJ 2013) 170; Julien Chaisse, 'Investor-State Arbitration in International Tax Dispute Resolution: A Cut above Dedicated Tax Dispute Resolution' (2016) 41 Va Tax Rev 158–65; Pasquale Pistone, 'General Report' in Michael Lang and others (eds), The Impact of Bilateral Investment Treaties on Taxation (IBFD 2017) s 1.2.2.
[65] Danon (n 63) 231.
[66] Lone Star (1) paras 390, 410, 470–71.
[67] Two other tax incidents were not analysed by the Tribunal because they took place before the 2011 BLEU–Korea BIT entered into force and the Claimants' investments do not qualify for treaty protection under the earlier 1976 BIT. Lone Star (1) paras 17(c), 280, 430–31.

A. Establishment and Developments of the Korean SOFD Prior to the Lone Star Tax Litigation

The Tribunal noted that the Korean SOFD was adopted and applied long before Lone Star's tax problems began, ie back in 1967 via the Supreme Court of Korea's case law, and later on codified by the Korean legislature.[68] The Tribunal first recalled the SOFD developments through the Supreme Court of Korea case law between 1990 and 2002 in the following ways: (i) the parties to an agreement 'should be determined not simply in reliance upon names on paper, but in full consideration of the substance of the agreement'; (ii) the 'transaction which is deemed as a "disguised act" intended by the seller to avoid tax shall be ignored'; (iii) 'facts based on which the applicable tax law is chosen should be determined on the basis of the substance of the relevant transaction, notwithstanding records and accounts kept by the relevant company or names used in such transaction'; (iv) 'sham transactions are an exception to the interpretive principle of strict construction, which is normally used when interpreting tax provisions'; (v) the provisions of Korean tax law incorporating the SOFD 'are intended to impose the tax obligation not on the nominal owner of income but on the substantive owner of income, which means that ownership of income should not be determined based on names used in operation or legal relationship, but on the ownership of profits arising out of substantial business activities'.[69]

The Tribunal also noted the update in the Korean tax law reflecting the developments in the case law of the Supreme Court of Korea, according to which tax authorities are authorised to 're-attribute income where an indirect transaction using a third party was used to avoid taxes'.[70] This highlights an emerging anti-tax avoidance function of the Korean SOFD. The case law of the Supreme Court of Korea, further cited by the Tribunal, underscores that function. For example, the Tribunal observed that, in 2012, the Supreme Court of Korea stated that 'even if transactions in [a] tax dispute are effective in terms of contract law, they may nevertheless be ignored or reconstructed for tax purpose[s] if they were designed to unfairly avoid taxes'.[71] The Tribunal also cited the case law of the Supreme Court of Korea, which explicitly relied on the tax avoidance intention test while applying the SOFD to prevent abuses of Korean tax treaties, including the 1979 Korea–Belgium DTT, in cases decided in 2012 and unrelated to Lone Star.[72] In particular, the Tribunal reiterated the two-part test, as established by the Supreme Court of Korea, in order to prevent tax-treaty-facilitated tax avoidance by applying the SOFD. To that effect, a legal entity is disregarded for tax treaty purposes if the answers to the following questions 1 and 2 are positive and negative respectively: '(1) whether the interposed intermediary was established for tax avoidance without economic benefit, and (2) whether the interposed intermediary had [a] business purpose and engaged in business activities'.[73]

The Tribunal's references to Korean tax law and the case law of the Supreme Court of Korea pre-dating the Lone Star tax litigation reveal that the Korean SOFD is much more than merely a general principle of Korean tax law of evidentiary nature aimed at achieving the constitutional principle of equality in the area of tax law and taxation according to the ability to pay.[74] The Korean SOFD is mainly a far-reaching general and vague domestic anti-tax avoidance rule allowing for a redetermination of various types of facts[75] and anti-tax avoidance interpretations of domestic and tax treaty law by Korean tax authorities and courts. It was applied in the Lone Star tax litigation exactly in that way.

B. Application of the Korean SOFD in the Lone Star Tax Litigation

When applying the SOFD, the NTS considered that LSF-KEB and Star Holdings SCA were conduit companies,[76] rather than the substantive owners of shares in KEB and Star Tower, respectively. Therefore, LSF-KEB and Star

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[68] Lone Star (1) paras 391–94. For the relevant case law and literature discussing the emergence and the developments of the Korean SOFD, see above nn 6–7.
[69] Lone Star (1) 392.
[70] ibid para 393.
[71] ibid para 304 with a citation of the Supreme Court of Korea's Judgment, Case No 2008Du8499 (19 January 2012).
[72] ibid 396–97.
[73] See the following Judgments of the Supreme Court of Korea: Case No 2010Du15179 (26 April 2012) and Case No 2010Du11948 (26 April 2012).
[74] cf above n 7.
[75] See further, Section III.C.
[76] According to the OECD's Committee on Fiscal Affairs (CFA), conduits are most often companies with legal personality, but they may also be partnerships, trusts or other forms, with tax resident status in the resident country for the purposes of applying a tax treaty with

Holdings SCA were not entitled to benefits under the 1979 Korea–Belgium DTT in respect of payments of profits nominally made to them from Korea.[77] That is to say, LSF-KEB and Star Holdings SCA were companies interposed between their subsidiaries in Korea and their parents in Bermuda and the USA solely, or at least mainly, to benefit from the 1979 Korea–Belgium DTT. As a result, the NTS disregarded LSF-KEB and Star Holdings SCA for purposes of applying the 1979 Korea–Belgium DTT and reattributed income from profits sourced in Korea (dividends and capital gains) to the US and Bermudan investment entities as the purported correct taxpayers for this income. The lack of any DTT between Korea and Bermuda led to taxation of the investment proceeds attributable to the Bermudan investment entities at the full Korean domestic tax rate. Despite the existence of the DTT between Korea and the USA,[78] the same tax consequences applied to the proceeds attributable to the US capital-pooling partnership. This followed from the assumption that an agreement between Korea and the USA existed according to which the NTS was authorised to tax the capital gains in question, arising out of a Korean company whose assets are comprised primarily of real property, in accordance with the Korean domestic tax rate.[79]

The Korean lower courts, and ultimately also the Supreme Court of Korea, supported the way the SOFD had been applied by the NTS to deny benefits under the 1979 Korea–Belgium DTT.

The Seoul Administrative Court observed that Lone Star had created the corporate structure to avoid paying taxes by interposing conduit companies in Belgium (in particular: LSF-KEB and Star Holdings SCA) solely for the purpose of obtaining benefits (reduced WHT tax rate on dividend payments and exemption from the taxation of capital gains from the disposal of shares) under the 1979 Korea–Belgium DTT. In such circumstances, this court agreed with the NTS that it was appropriate to apply the SOFD to deny benefits under the DTT:[80] (i) Star Tower Corporation did not perform any other business activities, nor did Star Holdings SCA other than transferring Star Tower Corporation shares, (ii) Star Holdings SCA only had a single employee in 2003, although it received hundreds of billions of US$, (iii) one day after the sale of the Star Tower Building closed, Star Holdings SCA's board of directors met and agreed to liquidate the company and (iv) there was no specific material supporting that Star Holdings SCA and its upper-level holding companies conducted substantive business activities in their resident country other than investing in the Star Tower Building.[81] Similar-fact patterns were decided on the conduit status of LSF-KEB.[82]

In three judgments regarding several Lone Star tax litigation proceedings, the Supreme Court of Korea upheld the lower courts' decisions that the SOFD was applied appropriately by NTS to deny benefits under the 1979

the source country established solely or mainly in order to obtain tax treaty benefits on an account of an entity that is not entitled to obtain such benefits directly. In that regard, the CFA indicates that the most important situations of the improper use of tax treaties are those in which a company established in a tax treaty country is acting as a conduit for channelling income economically accruing to a person in another State, who is thereby able to take advantage improperly of the benefits provided by a tax treaty. The CFA also points out that such a situation is often referred to as treaty shopping, a phenomenon that is a disadvantage for the source country, since it leads to no or lower withholding taxation (WHT) in that country in comparison to its domestic taxation. OECD, Double Taxation Conventions and the Use of Conduit Companies (27 November 1986) (Conduits Report) 2. Although it was not clearly stated by the CFA, the context and purpose of the Conduits Report shows that the term 'improper use of tax treaties' can be used interchangeably with 'abuse of tax treaties', including 'abusive treaty shopping'. cf Stef van Weeghel 'The Improper Use of Tax Treaties: With Particular Reference to the Netherlands and the United States' (1998) Kluwer Law Int 120–4.

[77] Lone Star (n 1) paras 432, 447.

[78] Convention between the United States of America and the Republic of Korea for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and the Encouragement of International Trade and Investment (signed 4 June 1976, entered into force 20 October 1979) (the 1979 Korea–US DTT).

[79] Lone Star (n 1) paras 447, 452. As noted by the Tribunal, although the legality of non-application of the Korea–US (1979) and the existence of the mentioned agreement were disputable, the Supreme Court of Korea ultimately rejected Lone Star's argument with respect to the applicability of that DTT. Supreme Court of Korea's Judgment, Case No 2015Du2611 (15 December 2016). It is worth noting that the 2017 OECD Model includes a specific 'real estate' clause in Article 13(4) in order to allocate taxation right to a source State in similar circumstances as said agreement between the US and Korean governments.

[80] Lone Star (n 1) paras 448–49 with a reference to the Seoul Administrative Court's Judgment, Case No 2007Guhap37520 (16 February 2009).

[81] ibid para 449.

[82] ibid para 460 with a reference to the evidence discussed by the Korean Tax tribunal's Judgment, Case No Gukshim2007Seo5223 (21 July 2010): 'LSF-KEB Holdings SCA was a conduit company established for the purpose of tax avoidance, and, as a conduit company, it was not entitled to the benefits of the Korea–Belgium Tax Treaty.'

Korea–Belgium DTT.[83] In particular, this case law confirmed that the Korean SOFD 'can serve as a standard in interpreting and applying a provision of a tax treaty'.[84] Therefore, no benefits under the 1979 Korea–Belgium DTT should be granted to LSF-KEB and Star Holdings SCA, since they were (i) mere conduits established for the sole purpose of avoiding WHT in Korea, rather than for the efficient management and operation of the fund's investment capital and investment assets, and were (ii) deprived of any substance or purpose other than those related to avoiding WHT in Korea. As a result, they could not be considered as the substantive owners of income from dividends and capital gains sourced in Korean and thus benefit from the 1979 Korea–Belgium DTT.[85]

C. The Tribunal's Assessment of the Korean SOFD and Its Application in the Lone Star Tax Litigation to Determine Its Compatibility with the 2011 BLEU–Korea BIT and Indirectly with International Tax Treaty Standards Mainly Set by the OECD

The Tribunal's reasoning and conclusion about the compatibility of the Korean SOFD with the 2011 BLEU–Korea BIT was essentially driven by the opinions from expert witnesses called by the Respondent (Professor Stef van Weeghel) and the Claimants (Professor Luc de Broe).[86] They converged as to the observation that the OECD Commentaries, although not legally binding, 'carry significant weight in the interpretation of existing tax treaties',[87] and are products of 'broad consultation within the international tax community'.[88] Likewise, both expert witnesses cited the passages from the OECD documentation[89] according to which SOFD is not affected by DTTs, and thus generally cannot conflict with them, because it is a rule in domestic tax law 'for determining which facts give rise to a tax liability'.[90] Although the Tribunal acknowledged that the Claimants' expert witness disagrees with the OECD view that SOFD need not be specifically addressed in tax treaties to be compatible with them, it did not present and analyse the arguments of Professor De Broe.[91] By contrast, the Tribunal focused on emphasising the further arguments of the Respondent's expert witness that neither Belgium nor Korea made any observations about the position of the OECD and that 'the Belgian position on the application of domestic law anti-abuse rules to tax treaties matches Korean law and policy … Belgium endorses applying domestic law rules to prevent abuse of Belgian tax treaties'.[92]

Even before the presentation and the analysis of the application of the Korean SOFD by the NTS and Korean courts, the Tribunal concluded that the situation 'did not violate the BIT because, as referenced by Dr De Broe, the doctrine forms "part of the basic rules for determining the facts that give rise to tax liability"'.[93] It was somewhat puzzling for the Tribunal to cite the Claimants' expert witness observation (in fact, his citation of the 2003 OECD commentary on art 1), rather than the Respondent's one, in the conclusion on the compatibility of the Korean SOFD with the 2011 BLEU–Korea BIT, while omitting the arguments of the former in the text of the Award as to his disagreement with the pivotal OECD view. In fact, the Tribunal almost entirely based its conclusion on the OECD view that any SOFD is nothing more than a rule of evidence in tax proceedings.[94]

[83] See the following Judgments of the Supreme Court of Korea: Case No 2015Du2611 (15 December 2016); Case Nos 2014Du3044 and 2014Du3051 (Consolidated) (12 October 2017); and Case No 2017Du59253 (28 December 2017).
[84] Lone Star (n 1) para 452, citing in fn 583 the Supreme Court of Korea's Judgment in Case No 2015Du2611 (15 December 2016).
[85] See references made by the Tribunal to the case law of the Supreme Court of Korea in paras 452, 461–68.
[86] Although the names of the expert witnesses were removed from the text of the Award, they are still publicly available in the earlier document submitted to the Tribunal. See Lone Star v Korea, ICSID Case No ARB/12/37, the Respondent's Counter-Memorial on Jurisdiction and Merits (21 March 2014) eg para 50 <https://www.italaw.com/sites/default/files/case-documents/italaw11847.pdf> accessed 6 December 2023.
[87] Citation of S van Weeghel's First Expert Report para 60 by the Tribunal, Lone Star (1) para 405.
[88] A reference by the Tribunal to L de Broe's First Expert Report para 99, Lone Star (1) para 408.
[89] The phrase 'OECD documentation' refers to all documents produced by the OECD, including its commentaries, reports and guidelines of relevance for interpretation and application of DTTs.
[90] Lone Star (n 1) paras 406–10.
[91] ibid para 408.
[92] Citation of S van Weeghel's First Expert Report paras 46, 109–11 by the Tribunal, Lone Star (1) para 409.
[93] Citation of L de Broe's First Expert Report paras 20, 999 by the Tribunal, Lone Star (1) para 410.
[94] Ie it: "forms 'part of the basic rules for determining the facts that give rise to tax liability'. It is only after the facts have been determined that the tax consequences are assessed, and it is only at the tax consequence stage, not the earlier fact-determination stage, that the treaty provisions come into play. Here the judicial proceedings initiated by the Lone Star companies resulted in a rejection in the relevant cases of Lone Star's version of facts. The Korean courts adequately explained why the application of Substance Over Form was not arbitrary but grounded in the evidence. Nor, in the opinion of the tribunal, as will be discussed, was the application discriminatory. (Lone Star (1) para 410, emphases added, fns omitted).

At a later stage of the analysis, the Tribunal further observed that 'the tax treatment violated neither national nor international standards' and that '[t]he Respondent acted well within the legal boundaries of internationally-accepted tax policy' while applying the Korean SOFD in the Lone Star tax litigation, thereby it was neither arbitrary nor discriminatory.[95] As a result, it did not violate the FET standard or any other standards of investment protection under the 2011 BLEU–Korea BIT, as alleged by the Claimants. In the Tribunal's view, the application of the Korean SOFD was based on 'a rational public policy and on the facts found by the Korean Courts'.[96] More specifically, and again by underscoring the importance of the OECD documentation, the Tribunal concluded that 'the tax treatment of the KEB dividends and the withholding tax on the sale to Hana and the tax on the sale to Hana of the KEB shares did not amount to harassment but was a routine application of a tax system whose relevant provisions were quite consistent with international standards including the OECD Guidelines'.[97]

IV. WHAT DID THE TRIBUNAL OVERLOOK IN RESPECT OF RELATIONS BETWEEN THE KOREAN SOFD AND THE DTT?

This section critically analyses the Tribunal's methodology and reasoning in respect of determining relations between the application of the Korean SOFD and the 1979 Belgium–Korea DTT for the purposes of concluding whether or not the application violated the 2011 BLEU–Korea BIT. The Tribunal's analysis not only required it to determine and assess facts related to the application of the Korean SOFD, but also to interpret the 1979 Belgium–Korea DTT. In the absence of such an interpretation, it would be impossible to decide whether the application of the Korean SOFD was discriminatory and arbitrary and, thus, violated standards of investment protection under the 2011 BLEU–Korea BIT. This inquiry demands a close examination of tax treaty interpretation and an impact of domestic anti-tax avoidance measures on tax and investment treaties. However, this section does not explore the tribunal's assessment of the Claimants' allegation according to which the application of the Korean SOFD violated the 'umbrella clause' in Article 10(3) of the 2011 BLEU–Korea BIT by the failure of the Respondent to comply with its obligations under the 1979 Belgium–Korea DTT. In any event, the Tribunal entirely rejected that allegation.[98]

A. DTT Detrimental Oversimplification of the OECD on the SOFD:Lack of Distinction among Different Levels of Facts Relevant for Tax Purposes

[95] ibid 469–70.

[96] ibid para 471.

[97] ibid 480.

[98] The Tribunal concluded that the 1979 Belgium–Korea DTT 'has its own enforcement mechanisms and neither Party to the Treaty agreed to bring enforcement within the scope of investor-State arbitration' and that 'even if the Claimants could bring their tax claim within the Umbrella Clause, it would fail on the facts'. *Lone Star* (1) paras 486–87. Thus, the right of investors to get protection under umbrella clauses against violation of DTTs by States was not tested yet in the ISDS tax-related cases. It remains to be seen whether said argument will gain traction in ISDS case law. In that regard, the overarching question is whether 'any other written obligation' means any obligation of contracting States expressed in their DTTs, for example the reduced taxation or the exemption from withholding taxation of dividends or capital gains, respectively. Additionally, said argument presupposes that the respondent State violated a DTT, which requires an analysis similar to that carried out by the *Lone Star* Tribunal and examined in this section. For valuable points on the functioning of umbrella clauses in general, see Lee Carroll, 'What Place Does an Umbrella Clause Have in the New Generation of Bilateral Investment Treaties?' (2023) 40(2) J Int Arb 126; Katia Yannaca-Small, 'Interpretation of the Umbrella Clause in Investment Agreements' (2003) OECD Working Papers on International Investment 15–21; Jarrod Wong, 'Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and the Divide between Developing and Developed Countries in Foreign Investment Disputes' (2006) 14 Geo Mason L Rev 164. For valuable points on the functioning of umbrella clauses in ISDS tax-related cases, see Stef van Weeghel, 'Tax and Investment Treaties: Further Thoughts' in Pistone (n 13) s 26.2.5; Paul HM Simonis, 'BITs and Taxes' (2014) 42(4) Intertax 275. For ISDS case law, see eg *Compañía de Aguas del Aconquija SA and Vivendi Universal (formerly Compagnie Générale des Eaux) v Argentine Republic*, ICSID Case No ARB/97/3, Decision on Annulment (3 July 2002) paras 95, 96; *Compañía de Aguas del Aconquija SA and Vivendi Universal (formerly Compagnie Générale des Eaux) v Argentine Republic*, ICSID Case No ARB/97/3, Decision on Annulment (3 July 2002) paras 95, 96; *Eureko BV v Republic of Poland*, Partial Award (19 August 2005) para 246; *Consutel Group SpA in liquidazione v People's Democratic Republic of Algeria*, PCA No 2017–33, Award (3 February 2020) para 325.

Looking closely at the determination of different types of facts for tax purposes is of the utmost importance when determining interrelations between domestic anti-tax avoidance rules such as the Korean SOFD and DTTs.[99] However, neither the Tribunal nor the OECD discussed that issue. This led the Tribunal to the debatable observation that the Korean SOFD is exclusively or at least essentially a fact-determination rule not affected by DTTs,[100] including the 1979 Korea-Belgium DTT, without any need for further scrutiny of that doctrine.

As Professor Zimmer observed, there are at least three levels of facts in tax law.[101] Level 1 pertains to real facts, eg a person's date of birth, the registration of a legal entity in a country's relevant registry of companies, or what senior employees in the group of affiliated companies stated in their interoffice memos and emails.[102] Level 2 pertains to legal facts, eg facts established by the rules of private law or other non-tax fields of law, for instance, how a contract regarding the disposal of shares should be interpreted, whether a payment from a company to a shareholder should be considered as a salary, loan, dividend or capital gain, or who is a legal owner of profits distributed (dividends) or shares disposed (capital gains) by a company. Level 3 is that of tax statutes in which tax facts to a large extent depend on legal facts and are heavily interpretative in nature, eg 'the question of whether a certain tax rule applies in a certain case can depend on the interpretation of the tax rule or on the establishing of the "legal facts", or on both'. At that level, legal facts may often be subject to recharacterisation solely for tax purposes.[103]

Few anti-avoidance doctrines and rules attach legal consequences to real facts (level 1). Instead, the determination of such facts is typically governed by the rules of evidence, not the rules of tax avoidance.[104] Legal facts (level 2) are not established by evidence, but by a legal process. The legal process is also needed to determine tax facts (level 3). Indeed, the Korean SOFD is only slightly interested in real facts (level 1) insofar as it requires legal (tax) consequences to be drawn from real facts instead of sham (simulated, disguised) actions of taxpayers contrary to their genuine intentions.[105] To that extent, it relies on legal rather than economic substance. The legal substance 'most often refers to the characterisation that emerges from a close study of the rights and obligations in a legal relation', its main function being 'to point out that sham or simulation transactions and wrong legal characterizations by the taxpayer will be disregarded for tax purposes'.[106]

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[99] Brian J Arnold and Stef van Weeghel, 'Chapter 5: The Relationship between Tax Treaties and Domestic Anti-Abuse Measures' in Guglielmo Maisto (ed), *Tax Treaties and Domestic Law* (IBFD 2006) 5.4.2; Zimmer (n 3) 28–33. cf Giuseppe Marino, 'The Burden of Proof in Cross-Border Situations (International Tax Law)' s 2.1.2 and Klaus-Dieter Drüen and Daniel Drissen, 'Burden of Proof and Anti-Abuse Provisions' s 4.1, in Gerard Meussen (ed), *The Burden of Proof in Tax Law* (IBFD 2013).

[100] cf Arnold and Weeghel (n 99) 5.4.2; Zimmer (n 3) 28–29.

[101] Frederik Zimmer, 'Domestic Anti-Avoidance Rules and Tax Treaties—Comment on Brian Arnold's Article' (2005) 59 Bulletin—Tax Treaty Monitor 25. By comparison, Professor John Tiley distinguished between nine levels of facts in light of an interpretation and application of tax law, including anti-tax avoidance rules such as an SOFD: "In summary, levels 1 to 4 are concerned with determining the facts to which the tax rules are to be applied, levels 6 to 8 with the ways in which the rules are to be laid down so that they can be applied to the facts at level 5, while level 9 sets the social and intellectual constraints within which the rules are to evolve. Rules evolved from levels 6 to 8 should not conflict; the principles apparent at level 9 almost inevitably do. ('Judicial Anti-Avoidance Doctrines: The US Alternatives—Part 1' (1987) 5 British Tax Rev 195)."

[102] eg interoffice memos dated 26 November 2002 and 17 January 2002 discuss Star Holdings' status as an SA (ie *société anonyme*—public limited company): 'it is possible to avoid capital gains tax if the corporate structure of SH [Star Holdings] is changed to an SCA from an SA while maintaining the Belgian company in Belgium as it is'. See also an internal email of 16 July 2004 from a senior executive of one company to a senior advisory employee of another company in the Lone Star group: 'By the way, it is my personal opinion that we will sell the building north of 900 billion won and probably closer to 940 billion won. The key will be to force the buyer to buy the shares in Star Tower Corp so that we don't have significant tax leakage.' See the Tribunal's references in para 449, fn 78 to the Seoul Administrative Court's Judgment, Case No 2007Guhap37650 (16 February 2009).

[103] Zimmer (n 3) 25.

[104] Ibid.

[105] The case law of the Supreme Court of Korea between 1990 and 2002 confirms that the Korean SOFD focuses on sham transactions only to a little extent. See points (i)–(iii) above in Section III.A. In his nine-level classification of facts, John Tiley classified sham doctrine to level two which is strictly related to real facts and thus level 1 of facts in Zimmer's classification presented above. As put by Tiley, '[i]t is at this level that one can see the application of the doctrine of the sham, at least in its narrow United Kingdom sense, of determining whether what the parties represent as having happened is entitled to the legal classification they claim for it or whether this classification should be withheld on the ground that it does not represent the true intentions of the parties'. Another formulation of sham doctrine worth referencing is that of Lord Devlin in the HL judgment in Campbell Discount Ltd v Bridge (25 January 1962) 1 All ER 385, 402: 'Where a court of law finds that the words which the parties have used in a written agreement are not genuine and are not designed to express the real nature of the transaction but for some ulterior purpose to disguise it, the court will go behind the sham front to get at the reality' (Tiley (n 101) 191, 194).

[106] Zimmer (n 3) 24–25.

The more recent case law to which the Tribunal referred, and which regarded the application of the Korean SOFD to deny benefits under DTTs, indicates that it aims to prevent tax avoidance predominantly by disregarding the interposed entities and recharacterising the transactions based on their economic substance.[107] One of the challenges to applying the Korean SOFD is that its key component—economic substance—is not defined. There is only an approximation to its understanding in imprecise and sometimes circular references of Korean courts to circumstances in which economic substance occurs. For example, the SOFD applies to impose the tax obligation not on the nominal owner of income, but on the substantive owner of income and the substantive ownership of income is determined based on 'ownership of profits arising out of substantial business activities',[108] but it is not defined what substantial business activities mean.[109] Korean case law allows economic substance to be identified with the non-tax avoidance business purpose, the non-tax economic benefit and the engagement in non-tax avoidance related business activities.[110] How much weight is given to each element and whether they need to occur cumulatively to determine the existence of economic substance under the Korean SOFD remains unclear. The Tribunal left that issue outside the scope of the Award.

Accordingly, the Korean SOFD is a general domestic anti-tax avoidance doctrine, partly codified in domestic statutory tax law. It predominantly deals with determining tax facts that are based on an interpretation of tax law, including DTTs, and disregarding or redetermining real and legal facts for tax purposes. It means that the Korean SOFD is not as grounded in evidence, as the Tribunal observed following the OECD view.[111] Instead, it allows the Korean tax authorities and courts to ignore or redetermine evidence (levels 1 and 2 facts) solely for tax purposes based on a broad and vague anti-tax avoidance concept of economic substance. This is an ambiguous and challenging process that requires a thorough legal consideration. The Korean SOFD does, therefore, seem to be affected by DTTs. It also affects how DTTs are interpreted and applied, which is subject to the rule and principles of the interpretation of treaties of VCLT, insofar as it influences the interpretation and application of DTTs.[112] The reason why the Tribunal did not recognise it seems to lie with its overreliance on the OECD documentation, which did not follow the above distinction of facts. Instead, the OECD presented oversimplified remarks on the nature of domestic anti-avoidance rules, including SOFD, and their relation to DTTs.[113]

The OECD view, as followed by the Tribunal, could lead to effects contradicting the object and purpose of DTTs, not least by leading to diverging interpretations of the same provisions of a DTT in the same circumstances in two contracting States.[114] This follows from the diverging scopes and ways in which various States apply SOFDs,[115] following factual or interpretative approaches to a different degree.[116] In a similar vein, tax scholars have warned about an unrestricted use of SOFDs for an interpretation and application of DTTs, not least because

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[107] This observation also follows from the publications of Korean tax scholars, eg Kim and Park (n 7) 11–12; Ji-Hyun Yoon, 'A Giant Leap for Fairer Tax or Blind Compromise with Public Opinion?—A Review of the New Case Law on "Substance-over-Form" by the Supreme Court of Korea' (2013) 13(1) J Korean Law 152.

[108] *Lone Star* (n 1) para 392(e) with a reference to the Supreme Court of Korea's Judgment, Case No 99Do2165 (9 April 2002). See also *Lone Star* (n 1) para 395 with a reference to the National Tax Tribunal's Judgment, Case No Kuksim2004Seo4421 (13 July 2005).

[109] Although beyond the scope of this article, it is worth noting that the rule for determining the substantive owner of income as the only one to which an income is attributed for taxation purposes is problematic in light of the DTT's concept of beneficial ownership (BO). That is to say, this concept must not be 'stretched' to cover abusive treaty-shopping cases that are targeted by 'specific anti-abuse provisions in treaties, general anti-abuse rules and substance-over-form or economic substance approaches', as this practice could restrict the application of such measures. In respect to 'a guiding principle' and the PPT, cf Weeghel (n 36) 44. In this author's view, an SOFD and the economic substance analysis are not part of the examination under the concept of BO. They rather belong to two distinct group of legal measures that should be applied separately and sequentially (the concept of BO before the SOFD). Błażej Kuźniacki, *Beneficial Ownership in International Taxation* (Elgar Edward 2022) 158–59 citing paras 12.5, 10.3 and 4.4 of commentary to arts 10–12 of the 2017 OECD Model, respectively.

[110] *Lone Star* (n 1) paras 396, 403 with references to the Supreme Court of Korea's Judgment, Case No 2010Du15179 (26 April 2012) and the Seoul Administrative Court's Judgment, Case No 2007Guhap37650 (16 February 2009).

[111] Lone Star (n 1) para 410.

[112] Arnold and Weeghel (n 99) 5.4.1–5.4.2; Brian J Arnold, 'Tax Treaties and Tax Avoidance: The 2003 Revisions to the Commentary to the OECD Model' (2004) (6) Bulletin—Tax Treaty Monitor 249–51.

[113] Zimmer (n 3) 26. Admittedly, the reason why the OECD presented an oversimplistic view was most likely purely political, ie to avoid complications during the negotiations for the new text of the 2003 Commentary regarding relations between domestic anti-tax avoidance rules and DTTs and thus more smoothly reaching the agreement in that regard by the majority of the OECD's Member States. cf Arnold (n 112) 252.

[114] Arnold and Weeghel (n 3) 5.4.2.

[115] cf Arnold (n 112) 251–52.

[116] For different approaches to an application of SOFD in general and in respect of determination and redetermination of facts, see Zimmer (n 3) 25–29.

great care is taken on the technical and legal aspects to establish cross-border arrangements and transactions, while 'a broad brush, substance approach' is 'bound to lead to uncertainty'.[117]

This all demonstrates that the Tribunal could have been more alert and sceptical in following the OECD view on relations between SOFD and DTTs. The Tribunal could at least have subjected the OECD view to examination in accordance with the VCLT, especially in light of the pervasive doctrinal criticism of the OECD view.[118] In particular, the OECD view seems to ignore important legal considerations. This also shows that, even if the OECD Commentaries could in certain circumstances be relevant for tribunals in determining the compatibility of a State's fiscal conduct with DTTs and standards of investment protection under IIAs,[119] tribunals must meticulously examine the views of the OECD through an independent analysis of the subject matter in accordance with VCLT and the true nature, purpose and effect of the questioned tax measures towards DTTs and IIAs. While referring to the OECD Commentaries, it should also be borne in mind that this documentation constitutes interpretative materials of the utmost importance primarily for tax authorities, and does not necessarily reflect an appropriate and impartial interpretation of DTTs and their interactions with domestic tax laws of contracting States.[120]

Alternatively, the approach of the Tribunal to render the Award by following the oversimplified view of the OECD on relations between SOFDs and DTTs could be seen as a way to protect the Award. It decided to simplify its explanation on the issue in order to not overcomplicate the way to the conclusion. In this author's opinion, although one of the duties of investment treaty arbitrators is to protect the Award,[121] the very core duty, following from the object and purpose of IIAs, is to promote a foreign investment by protecting it against unfair, unpredictable and discriminatory treatment.[122] It has to be done by adopting 'the interpretation that most fosters a fair, predictable, and non-discriminatory (not necessarily profitable) regulatory environment for foreign investment'.[123] Such an approach also ensures that arbitrators can be recognised as contributors to the rule of law.[124] In that regard, there are at least three good reasons why said assumption does not seem to justify the Tribunal's methodology relying on the OECD's oversimplified view, as presented by the tax expert witnesses, even if it served the protection of the Award.

First, it does not appear to follow the interpretation of the 1979 Korea–Belgium DTT in accordance with the VCLT's rule and principles of treaty interpretation. Despite the lack of any formal hierarchy between these

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[117] In respect of the substance-based approach to the concept of BO, see Baker (n 11) 24. Such doctrines as SOFDs are also considered as unpredictable, taking the form of rather potential than actual rules, thereby resembling 'comets rather than stars or planets'. Tiley (n 101) 195.

[118] Zimmer (n 101) 25; Arnold and Weeghel (n 99) 5.4.2; Arnold (n 112) 251–52.

[119] Looking at this issue from the perspective of the principle of systemic integration under Article 31(3)(c) of the VCLT, Robert Danon claims that: "the Model Commentaries would be 'relevant' where the guidance conveyed by these materials is based on principles which are also at the core of the FET Standard. A good example are cases in which the Model Commentaries reiterate the obligation of the Contracting States to act in good faith not only between themselves but also towards the taxpayer. ((n 63) 237)."

[120] This follows directly from the Recommendation of the OECD Council, according to which the tax authorities of OECD MSs should 'follow the Commentaries on the Articles of the Model Tax Convention, as modified from time to time, when applying and interpreting the provisions of their bilateral tax conventions that are based on these Articles'. OECD, *Recommendation of the OECD Council concerning the Model Tax Convention on Income and on Capital*, adopted by the Council on 23 October 1997 under the written procedure [C/M(97)21/PROV]) point I.3 <https://one.oecd.org/document/C(97)195/FINAL/en/pdf>. It is worth remembering that the OECD is an organisation consisting, among other things, of senior tax administration officials delegated by the governments of the OECD MSs, and therefore this organisation tends to have a pro-fiscal understanding of concepts related to the application of DTTs.

[121] This duty appears to primarily follow from a duty of efficiency, which requires a balance between speed and providing an award that is accurate and acceptable by the parties. See Philipp Habegger, 'The Arbitrator's Duty of Efficiency: A Call for Increased Utilization of Arbitral Powers' in Patricia Shaughnessy and Sherlin Tung (eds), *The Powers and Duties of an Arbitrator: Liber Amicorum Pierre A. Karrer* (Kluwer Law International 2017) 123–36; Nadia Darwazeh, 'Is Efficiency an Arbitrator's Duty or Simply a Character Trait?' in Patricia Shaughnessy and Sherlin Tung (eds), *The Powers and Duties of an Arbitrator: Liber Amicorum Pierre A. Karrer* (Kluwer Law International 2017) 57–64. In general, the duties of an arbitrator are defined as the arbitrator's obligations to the parties of the arbitration in relation to the arbitral proceedings. See Gary B Born, *International Commercial Arbitration* (2nd edn, Kluwer Law International 2014) 1963.

[122] cf Joshua Karton, 'The International Investment Arbitrator's Duty to Apply the Law' (2018) 17(1) LPICT 175. cf also *Suez, Sociedad General de Aguas de Barcelona, SA and Vivendi Universal, SA v Argentine Republic II*, ICSID Case No ARB/03/19, Decision on Liability (30 July 2010) para 189: 'a recognized goal of international investment law is to establish a predictable, stable legal framework for investments'. See more broadly on key duties of investment treaty arbitrators: Katia Fach Gómez, *Key Duties of International Investment Arbitrators: A Transnational Study of Legal and Ethical Dilemmas* (Springer 2019).

[123] Karton (n 122) 175.

[124] Ibid 161.

principles in international practice, also reflected in the jurisprudence of the ICJ, a dominant role is attributed to linguistic interpretation, in the sense that contextual and purposive interpretation cannot alter a clear understanding of the text resulting from linguistic interpretation.[125] In the process of interpreting international treaties, the aim is to achieve the common intention of the State parties to the international treaty as fully as possible. According to the jurisprudence of the ICJ, the intentions of the parties to international treaties are reflected in the text of the treaty and should be determined on the basis of all the factors relevant to the interpretation (de jure indicated in Articles 31–32 of the VCLT).[126] Articles 1, 4(1), 10(2) and 13(3) of the 1979 Korea–Belgium DTT[127] do not include any substance requirement to apply a reduced WHT rate or exempt a resident of a contracting State from the WHT on capital gains from the sale of shares. Accordingly, one may ask whether the Lone Star Tribunal's reliance on the 2003 OECD commentary led to an appropriate conclusion in light of international law (the VCLT), directly in respect of the compatibility of the Korean SOFD's application to the 1979 Korea–Belgium DTT and indirectly the 2011 BLEU–Korea BIT. Although the Korean SOFD requires economic substance to benefit from Korean DTTs, it is not a part of the wording of such treaties. This can, at most, constitute the context of Korean DTTs, which cannot rewrite their provisions by including in them the economic substance requirement. This follows from the principle articulated by the Permanent Court of International Justice (PCIJ) 100 years ago in its advisory opinion of 15 September 1923 on the Acquisition of Polish Nationality case:

To impose an additional condition for the acquisition of Polish nationality, a condition not provided for in the Treaty of 28 June 1919, would be tantamount; not to an interpretation of that Treaty, but to a reconstruction of it.[128]

Such a requirement could be interpreted from the provisions of the 1979 Korea–Belgium DTT in their context and purpose in order to prevent their abuse in accordance with the VCLT's rule and principles of treaty interpretation and the principle of abuse rights. However, the Tribunal never did this. Instead, it relied on the OECD's oversimplified view regarding the relations between SOFDs and DTTs. The very conclusions that the interpretative approach of the Tribunal is doubtful is confirmed by the recent case law concerning the prevention of abusive treaty-shopping under DTTs.[129]

Second, Article 3(2) of the 1979 Korea–Belgium DTT says:

As regards the application of the Convention by a Contracting State any term not otherwise defined shall, unless the context otherwise requires, have the meaning which it has under the laws of that Contracting State relating to the taxes which are the subject of this Convention.

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[125] Richard Gardiner, *Treaty Interpretation* (OUP 2008) 190; Romesh Weeramantry, *Treaty Interpretation in Investment Arbitration* (OUP 2012) paras 3.70–3.71.

[126] *Dispute regarding Navigational and Related Rights (Costa Rica v Nicaragua*), Judgment (13 July 2009) ICJ Rep 2009, paras 213, 237, 46.

[127] Article 1: 'This Convention shall apply to persons who are residents of one or both of the Contracting States'. Article 4(1): "For the purposes of this Convention, the term 'resident of a Contracting State' means any person whose income under the law of that State, is subject to tax therein by reason of his domicile, residence, place of management, place of head or main office or any other criterion of a similar nature. But this term does not include any person who is liable to tax in that Contracting State in respect only of income from sources therein.
Article 10(2): However, such dividends may be taxed in the Contracting State of which the company paying the dividends is a resident, and according to the law of that State, but if the recipient is the beneficial owner of the dividends the tax so charged shall not exceed 15 per cent of the gross amounts of the dividends. This paragraph shall not affect the taxation of the company in respect of the profits out of which the dividends are paid."
Article 13(3): 'Gains from the alienation of any property other than those mentioned in paragraphs 1 and 2, shall be taxable only in the Contracting State of which the alienator is a resident.'

[128] *Acquisition of Polish Nationality*, 1923 PCIJ (Ser B) No 7, Advisory Opinion (15 September 1923) 21.

[129] By contextual and purposive interpretative references to the Articles 1, 4 and 13(4) of Convention between the Government of Canada and the Government of the Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital (as amended through 2012) (signed 10 September 1999, entered into force 17 October 2000 (the 1999 Canada–Luxembourg DTT), the majority of judges (6:3 decision) of the Supreme Court of Canada (SCC), *Canada v Alta Energy Luxembourg SARL*, 2021 SCC 49, judgement (26 November 2021), observed in para 67 that 'the spirit of arts. 1 and 4(1) was not to limit access to the benefits of the Treaty to corporations with "sufficient substantive economic connections" to their country of residence'. Such requirement followed only from the Canadian GAAR (general anti-avoidance rule), which plays the same role as the Korean SOFD in tax cases.

This provision reflects the general rule of interpretation of tax treaties based on Article 3(2) of the OECD Model.[130] It aims to fulfil the purpose of the provision of the tax treaty in which the term is embedded as fully as possible, in accordance with the common intention of the parties to the treaty.[131] Article 3(2) of the OECD Model, and thus its equivalent in the 1979 Korea–Belgium DTT, has a very narrow application, since it only covers treaty terms or concepts and, therefore, cannot be applicable to the interpretation of entire provisions (Article 31 of the VCLT has this competence) or to fill gaps in the provisions of tax treaties via domestic meanings.[132] Given that Articles 1, 4(1), 10(2) and 13(3) of the 1979 Korea–Belgium DTT do not include the term or concept of 'economic substance', it is questionable whether the Korean SOFD could be used via Article 3(2) of the 1979 Korea–Belgium DTT to include in those provisions the economic substance requirement.

Even if it is assumed that the concept of economic substance is used but not defined under Articles 1, 4(1), 10(2) and 13(3) of the 1979 Korea–Belgium DTT, the context of that DTT will require that the domestic Korean meaning of that concept should be abandoned in favour of the treaty's autonomous meaning if the application of the domestic meaning at the time of the application of that DTT renders it partially inoperative.[133] This is mainly the case where the introduction or modification of a particular term in domestic tax law is made after the tax treaty has been concluded solely or mainly in order to change the scope of a treaty distributive norm for the acquisition or enhancement of the right of that State to tax the income under that norm.[134] Such a change may include the introduction or modification of the concept of economic substance by a source State (eg Korea in Lone Star) to its domestic tax law in a way that it significantly narrows the scope of entities that may be considered as tax residents entitled to tax treaty benefits, for example under Articles 1, 4(1), 10(2) and 13(3) of the 1979 Korea–Belgium DTT. This would consequently extend the Korean right to collect WHT on the basis of tax treaties if the domestic meaning of the economic substance were to be applied. For this reason, the context of tax treaties of Korea will require the rejection of the domestic meaning of the concept of economic substance.

Third, as pointed out above (Sections I. and III.A.–B.), SOFDs in general, and in Korea in particular, are problematic legal tools. This mainly follows from their broad and unclear scope of application, shifting the burden of treaty application from a precise legal analysis to broad economic–factual determinations. Accordingly, the reliance of the Tribunal on the oversimplified OECD view appears to be at odds with one of its key duties: to promote foreign investment by protecting it against unpredictable treatment. This arises from the interpretative approach of the Tribunal, which enhanced the compatibility of the Korean SOFD with the 1979 Korea–Belgium DTT without adopting the interpretation that most fosters a predictable regulatory environment for foreign investment.

The Tribunal did not reflect at all on the above three reasons in the text of the Award. Thus the mentioned hypothetical justification (the protection of the Award) for the Tribunal's methodology to rely on the OECD oversimplified view, as presented by tax expert witnesses, does not seem to be valid. In any case, the presence of expert witnesses should not remove the legal character of the Tribunal's determination on the key points to render the Award, especially if those points required interpretation of international treaty, ie the 1979 Korea–Belgium DTT.[135]

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[130] In fact, its wording is closest to art 3(2) of the OECD Models released in 1977, 1995, 2003, 2010 and 2014. The 2017 OECD Model indicates that: "any term not defined therein shall, unless the context otherwise requires or the competent authorities agree to a different meaning pursuant to the provisions of Article 25, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State."

[131] Alexander Rust, 'Article 3' in Alexander Rust and Ekkehart Reimer (eds), *Klaus Vogel on Double Taxation Conventions* (4th edn, Wolters Kluwer Law & Business 2015) para 110; John Avery Jones, 'Treaty Interpretation' in Richard Vann (ed), *Global Tax Treaty Commentaries* (IBFD 2017) s 4.1.

[132] Rust (n 131) para 111 at 207. cf High Court of Australia, *Thiel v FCT*, Judgment (22 August 1990) 21 ATR 531, 532.

[133] cf commentary to Article 3(2) of the 2017 OECD MTC, para 13.

[134] Supreme Court of the Netherlands (*Hoge Raad*), Case Nos 43.978, 07/13267, 08/02288, Judgment (19 June 2009); Supreme Court of Belgium (*Hof van Cassatie*), Case No FJF 2004.63, Judgment (5 December 2003); UK Divisional Court, *IRC v Exxon Corporation* [1982], Judgment (1 March 1982) STC 356.

[135] Although investment tribunals have been known to hear expert witness evidence on questions of international law, the presence of expert witnesses did not remove the legal character of the Tribunal's determination on those points. See Hepburn (n 46) 105 with references to *Pezold* (n 46) 736 and *Chevron Corporation v Ecuador*, PCA Case No 2009-23, Opinion of Jan Paulsson (12 March 2012). It is worth noting that DTTs are specialised kind of treaties, on which there is significant expertise available that may be beyond a

Nevertheless, as will be seen from Section V, the Tribunal appropriately rooted its observation on the compatibility of the application of Korean SOFD with the 1979 Korea–Belgium DTT on the facts that implied the abuse of that DTT. Still, the major methodological imperfection of the Award is that the Tribunal appeared to do so without an application of the VCLT's rule and principles of treaty interpretation and the principle of the abuse of rights. At least, it was not reflected in the text of the Lone Star Award.

B. The Tribunal Did Not Notice that the OECD View on the SOFD's Compatibility with DTTs Is Subject to a Guiding Principle and to the PPT

Although the Tribunal relied heavily on the OECD view on relations between SOFDs and DTTs, as reported by tax expert witnesses,[136] it never referred or even acknowledged the full view of the OECD in that regard.

A key part of the Tribunal's reasoning regarded the consideration of SOFDs and other domestic anti-tax avoidance rules by the OECD as 'part of the basic rules for determining the facts that give rise to tax liability, that they are not addressed in tax treaties and that therefore they are not affected by them'.[137] This consideration was reflected in paras 9.2 and 22.1 of the 2003 OECD commentary on Article 1. The Tribunal, however, in the Award, did not refer to the following sentence in para 22.1: 'Thus, as a general rule and having regard to paragraph 9.5, there will be no conflict' (emphasis added). It clearly means that the compatibility of domestic rules such as SOFDs with DTTs is not absolute and universal but subject to 'a guiding principle', then included in Article 1, para 9.5.[138] It reads as follows:

> It is important to note, however, that it should not be lightly assumed that a taxpayer is entering into the type of abusive transactions referred to above. A guiding principle is that the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions. [emphasis added]

This reveals that domestic anti-avoidance rules that do not meet the cited two-pronged test (1—main purpose to benefit from DTT; 2—contrary to DTT's provisions) of a guiding principle[139] cannot lead to a denial of benefits under the relevant provisions of DTTs in compatibility with them.[140] In other words, such rules are not compatible with DTTs and thus their application is precluded by DTTs, unless the provisions of the DTT state otherwise.[141] Because the 1979 Korea–Belgium DTT did not include any provision permitting the application of SOFDs by

tribunal's own field of practice. Hence, it was fully justifiable to rely on the tax expert witness reports and the OECD documentation by the *Lone Star* Tribunal for addressing the key points related to the interplay between the Korean SOFD and the 1979 Korea–Belgium DTT. However, that does not mean that the Tribunal was justified in not undertaking its own interpretation of the 1979 Korea–Belgium DTT in accordance with the VCLT. That is to say, it is not commendable to decide by a tribunal purely on the basis of the submissions of the parties of the ISDS proceedings. cf a taxonomy of errors of tribunals in appreciating the role of domestic law in determining the question before them in Hepburn (n 46) 163–81.

[136] See Section III.C.

[137] The citation comes from the L De Broe First Expert Report para 99, as cited by the Tribunal in para 407. See also *Lone Star* (n 1) para 410.

[138] Arnold (n 112) 260.

[139] International tax law scholarship clearly identifies that a guiding principle (ie para 9.5 (now: para 61) of the commentary on Article 1) consists of two elements (ie is based on the two-pronged test). See, eg Eivind Furuseth, The Interpretation of Tax Treaties in Relation to Domestic GAARs (IBFD 2018) s 11.1: "The guiding principle consists of two components. First, the main purpose for entering into a transaction or an arrangement must be to secure a favourable tax position which would not have been possible without the transaction or arrangement. Second, obtaining the reduced taxation on the transaction or arrangement must be contrary to the object and purpose of the tax treaty, both in general and under the specific treaty provision." This also follows from the further analysis in this section regarding the PPT and the relevant references to the scholarship and case law insofar as the OECD claims that the PPT is merely a codification of the 2003 guiding principle. See Commentary on Article 29(9) of the 2017 OECD Model, para 169. cf Guglielmo Maisto, 'Counteracting Tax Treaty Abuses from a European Perspective: Frictions and Interactions between the OECD PPT and the ATAD GAAR' in Kofler, Mason and Rust (n 5) ss 344ff.

[140] As put Arnold: 'Not all transactions that result in a reduction of tax are abusive. Tax planning is legitimate, and taxpayers are not expected to arrange their affairs so as to pay the maximum amount of tax. The tax authorities and courts of a country are admonished by the Commentary not to be too quick to deny treaty benefits with respect to transactions'. ((n 112) 247).

[141] Arnold and Weeghel (n 99) s 5.4.3.

Belgium and Korea, the Korean SOFD could be applied in a compatible way with that DTT only if, according to the OECD, it could lead to a denial of benefits under that DTT in accordance with the guiding principle. The very fact-determining nature of the Korean SOFD (however doubtful under closer examination)[142] was therefore not a sufficient factor for determining its compatibility with the 1979 Korea–Belgium DTT.

This observation is even stronger in light of the 2017 OECD commentary, which completely abandoned the reasoning whereby SOFDs and other domestic anti-tax avoidance rules are not affected by DTTs because they merely determine facts giving rise to tax liability, and thus they are generally not in conflict with DTTs. Instead, the 2017 OECD commentary is more careful and nuanced in assuming compatibility of domestic anti-tax avoidance rules with DTTs than its 2003 version. Given that a dynamic interpretation is better suited than a static interpretation to properly interpret DTTs,[143] and that the Award was rendered almost five years after the publication of the 2017 OECD commentary, it would have been feasible and highly recommended that the Tribunal follow that commentary.

In short, the 2017 OECD commentary underscores the principle of pacta sunt servanda in the VCLT in respect of DTTs, meaning that DTTs prevail whenever domestic anti-tax avoidance rules conflict with them, and explains that although such conflicts will often be avoided, it must be analysed in each case based on its own circumstances.[144] There will be no conflict if domestic anti-tax avoidance rules deny DTT's benefits in the same circumstances in which they would be denied under the PPT or a guiding principle (if the DTT does not include the PPT).[145] This commentary applies also to SOFDs,[146] such as the Korean SOFD. Moreover, the OECD appears to acknowledge that the main rule and principles of interpretation relevant for DTTs are those included in Articles 31–33 of the VCLT.[147] Although the application of SOFDs and other judicial doctrines to interpret DTT are not precluded by the VCLT per se,[148] this observation is subject to an important caveat. If the result of an interpretation of a DTT in accordance with Articles 31–33 of the VCLT conflicts with the result of an interpretation stemming from SOFDs or other judicial doctrines, the former result shall prevail.[149] This means that the compatibility of SOFDs with DTTs will always be determined on a case-by-case basis. A relevant conclusion must come from a comparison of the result of the interpretation of the DTT under SOFDs with that arising out of Articles 31–33 of the VCLT and the application of the PPT or a guiding principle.

These observations are further strengthened by a global tax policy consensus of more than 140 members (countries and jurisdictions) of the G20/OECD's Inclusive Framework (IF) on BEPS.[150] They decided that the minimum standard to prevent an abuse of tax treaties is the PPT as the primary (default) option, rather than a

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[142] See Section IV.A.
[143] The terms used in tax treaties, as well as in other international agreements, deliberately use capacious (flexible) formulations in order to allow their dynamic interpretation, preferably achieving the common intention of the parties at the moment of they apply the provisions in accordance with the legal, social and economic reality at the time. Commentary to art 3 of the 2017 OECD Model para 11. See more broadly in respect of interpretation of treaties, Eirik Bjorge, *The Evolutionary Interpretation of Treaties* (OUP 2014) 9–12; Gerald Fitzmaurice, 'The Law and Procedure of the International Court of Justice: Treaty Interpretation and Certain other Treaty Points' (1951) 28 Br YB Int Law 8; Max Sørensen, 'Do the Rights Set forth in the European Convention on Human Rights Have the Same Significance in 1975?' in *Max Sørensen: A Bibliography*, Report presented by Max Sørensen to the Fourth International Colloquy about the European Convention of Human Rights, Rome 5–8.11.1975 (Aarhus University Press 1988) 54–55. In this way, international agreements, including tax treaties, are living instruments that, as a rule, are subject to interpretation in light of present-day conditions. See, in relation to the European Convention on Human Rights, the ECHR, *Tyrer v United Kingdom* (1978) 58 ILR, Judgment (25 April 1978) 339, 353.
[144] Commentary to Art 1 of the 2017 OECD Model paras 70–71.
[145] ibid paras 74, 77.
[146] ibid para 79.
[147] These doctrines and principles of interpretation, which vary from country to country and evolve over time based on refinements or changes resulting from subsequent court decisions, are essentially views expressed by courts as to how tax legislation should be interpreted. Whilst the interpretation of tax treaties is governed by general rule and principles that have been codified in Articles 31 to 33 of the Vienna Convention on the Law of Treaties, these general rule and principles do not prevent the application of similar judicial doctrines and principles to the interpretation of the provisions of tax treaties. (ibid 78)
[148] Ibid.
[149] See (n 10) for relevant references.
[150] According to the OECD, BEPS 'refers to tax planning strategies used by multinational enterprises that exploit gaps and mismatches in tax rules to avoid paying tax'. Working together within OECD/G20 Inclusive Framework on BEPS, 143 countries and jurisdictions (as of today, ie 2 October 2023) 'are collaborating on the implementation of 15 measures to tackle tax avoidance, improve the coherence of international tax rules and ensure a more transparent tax environment'. OECD (n 37). For an updated composition of the IF, see <https://www.oecd.org/tax/beps/inclusive-framework-on-beps-composition.pdf>.

SOFD.[151] In that regard, it is noteworthy that the PPT does not include in its wording any reference to an economic substance or a substance over form approach, but in the OECD's view it merely mirrors a guiding principle.[152] Even though an examination of economic substance seems to implicitly be of relevance to the application of the PPT,[153] the point to be made is that an SOFD-like solution is not a policy choice of the IF to prevent abuses of DTTs.

Although some authors have spotted similarities between the Korean SOFD and the PPT, mainly the orientation of those rules on tax avoidance intention,[154] they did not seem to observe a pivotal difference between them. In short, only the PPT relies on the contradiction test (the second prong of the PPT); the PPT contains an explicit legal premise to deny a DTT's benefit, only if granting this benefit would be contrary to the relevant provisions of that DTT, while the Korean SOFD does not. The mere determination of the sole or a principal purpose of a taxpayer's arrangement or transaction to obtain such benefit is not enough to deny it under the PPT.

It is also doubtful whether the economic substance test can replace the contradiction test, especially as the latter test is considered by tax scholars as by far the most important element of the identification of abusive tax avoidance.[155] It is equally unclear what significance the economic substance has while determining the contradiction test. Additionally, tax literature reveals that the absence of a contradiction test in anti-tax avoidance measures evidently works in favour of the tax authorities.[156] Even if the contradiction test could be ipso facto decoded from the economic substance test,[157] it is not legally guaranteed. Legally, they will not be required to establish that a tax benefit was obtained contrary to the relevant tax provisions. As a result, the taxpayers will lose a guarantee that they can effectively obtain a tax benefit as long as this is in line with the language, object and purpose of relevant tax provisions.[158] This applies equally to domestic and tax treaty law, but seems to trigger more serious tensions with the latter because DTTs are subject to interpretation in accordance with Articles 31–33 of the VCLT and relevant commentaries and models of the OECD. These sources of interpretation of DTTs require a rigorous application of the contradiction test to deny benefits under DTTs, ie the VCLT does so mainly under its purposive part of the integrated linguistic, contextual and purposive interpretation in good faith[159] while

[151] OECD, *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6—Final Report* (BEPS Action 6) (2015) paras 19–24.
[152] Although the OECD claims a far-reaching material identity of the 2003 guiding principle and the PPT (ie the PPT is merely a codification of this guiding principle), due to the differences between the PPT and the guiding principle, it is not correct to treat them as the same rules in terms of the scope, mechanism and effect of their application. Van Weeghel (n 36) 18. cf Kuźniacki (n 36) 249–50; Andrés Báez Moreno, 'GAARs and Treaties: From the Guiding Principle to the Principal Purpose Test –What Have We Gained from BEPS Action 6?' 46(6–7) (2017) Intertax 435. For the wording of the PPT, see Article 29(9) of the 2017 OECD Model: "Notwithstanding the other provisions of this Convention, a benefit under this Convention will not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention."
[153] Schön (n 36) ss 12.4.2.4 and 12.6; Kuźniacki (n 36) 267–71.
[154] Kim and Park (n 7) 13–15 and Beomjune Kim, 'Past, Present, Future of Principal Purpose Test' (2017) 33–3(11) J IFA Korea 61–67.
[155] With regard to the second prong of the PPT, see Schön (n 36) ss 12.1 and 12.2.1. With regard to the second prong of the Canadian general anti-avoidance rule (GAAR) and the PPT, see Michael N Kandev and John J Lennard, 'Treaty Shopping in Canada after Alta Energy Luxembourg (2021): A Closed Door without a Lock' (2022) 76(3) Bull Int Tax s 5.3 *in fine*.
[156] Indeed, the tax scholarship analysing case law on domestic GAARs in an international tax context—judicial and administrative decisions in 2021 in several countries on 'treaty shopping cases', ie Canada: *Alta*; Trinidad and Tobago: *Methanex*; Argentina: *Molinos*; and Spain: a decision of the GAAR committee—reveals a common risk for taxpayers in anti-tax avoidance measures based on 'economic substance' without the contradiction test (ie essentially focusing on 'artificiality' exclusively). Adolfo Martín Jiménez, 'Is There an International Minimum Standard on Tax Treaty Shopping after BEPS Action 6? Some Recent Divergent Trends' (2022) 14(3) World Tax J s 3.4.3.
[157] ie it may be argued that these tests are intertwined in a factual way so that the more artificial an arrangement or transaction is, the more likely that an obtainment of tax benefit from them is contrary to relevant tax provisions. Błażej Kuźniacki, 'The GAAR (Article 6 ATAD)' in Werner Haslehner and others (eds), *A Guide to the Anti-Tax Avoidance Directive* (Edward Elgar 2020) 171.
[158] Kuźniacki and van Weeghel (n 4) 143.
[159] This integrated (holistic) approach to interpretation reflected (and still reflects) the methodology of the ICJ for the interpretation of international treaties. Santiago Torres Bernardez, 'Interpretation of Treaties by the International Court of Justice Following the Adoption of the 1969 Vienna Convention on the Law of Treaties' in Gerhard Hafner and others (eds), *Liber Amicorum: Professor I. Seidl-Hohenveldern in Honour of his 80th birthday* (Kluwer Law International 1998) 744, 747–48; Bjorge (n 90) 63. Such a holistic interpretation is also applied when determining the intention of the parties by courts in cases concerning tax treaties. See in particular the Federal Court of Australia, *Lamesa Holding BV v Commissioner of Taxation*, 1997 (ATR) 589, Judgment (20 August 1997) 97 ATC 4752. This court used the phrase 'a holistic approach to the interpretation of a tax treaty'. For a presentation and analysis of this

the OECD requires that in line with the second prong of the PPT or a guiding principle. This is, however, not to say that the VCLT, the PPT and a guiding principle apply the same standard for the contradiction test. Rather they apply independently of one another and may lead to different results.[160] Indeed, if one sketches a spectrum of difficulties to deny benefits under DTTs, the most difficult would be to do so via the VCLT exclusively,[161] easier via a guiding principle,[162] and easiest of all three via the PPT.[163] If we add the Korean SOFD to that spectrum, it will be the easiest tool for tax authorities and courts to deny benefits under DTTs (if the VCLT is ignored), even easier than via the PPT, due to the lack of an explicit requirement to apply the contradiction test.

This shows that the Tribunal's omissions in the text of the Award might lead to distortions in perception of the internationally agreed standards for denying benefits under DTTs, since the Tribunal implicitly considered the Korean SOFD to be compatible with such standards, without analysing the limits imposed on the denial of the DTT's benefits by the VCLT, a guiding principle and the PPT. Apparently, no such analysis was necessary in the Tribunal's opinion to determine the compatibility of the Korean SOFD's application to the 2011 BLEU–Korea BIT under the facts and circumstances of the Lone Star tax scheme. Nevertheless, had the Tribunal performed that analysis,[164] it would have significantly contributed to a systemic interpretation of DTTs and IIAs in respect of the application of the substance over form approach to deny benefits under those treaties.[165]

V. CONCLUSIONS AND THE NEED FOR FURTHER RESEARCH

The Lone Star Tribunal implicitly considered the Korean SOFD to be a suitable rule to prevent abuses of the 1979 Korea–Belgium DTT. Its application was, in the Tribunal's view, an example of rational public policy, grounded in evidence and consistent with international standards, including the OECD Commentaries, so it did

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judgment, see Richard Vann, 'Interpretation of Tax Treaties in New Holland' in Henk van Arendonk and others (eds), *A Tax Globalist: Essays in Honour of Maarten J. Ellis* (IBFD 2005) 144ff.

[160] As aptly observed by Professor van Weeghel: "The words 'object and purpose' as used in paragraph 61 of the Commentary on and in article 29(9) of the 2017 OECD Model nudge one in the direction of article 31(1) of the VCLT. It is unlikely that article 29(9) and its reference to the object and purpose of the relevant provisions of the Convention was merely included in the OECD Model to confirm the guiding principle and the general rule of interpretation of article 31 of the VCLT. If that were the case, the inclusion of the new preamble, perhaps in combination with the expression of the guiding principle in the Commentary on Article 1 of the 2017 OECD Model, would have been enough to accomplish the desired result […]. [A]rticle 29(9) does not merely confirm the guiding principle, but adds a dimension to it, and one could argue that article 29(9) reduces the weight of the principal purpose of the tax treaty (the avoidance of double taxation) in favour of an ancillary purpose (the prevention of tax avoidance). ((n 36) 15, 18)." Contra: Michael Lang, 'The Signalling Function of Article 29(9) of the OECD Model—The "Principal Purpose Test"' (2020) 74(4/5) Bull Int Tax 264, 266, who argues that the introduction of the PPT to the OECD Model is both superfluous and unhelpful and can, at best, be attributed a 'signalling function'.

[161] The VCTL attributes a dominant role to linguistic interpretation, in the sense that it is a starting point of every interpretation of a treaty and that contextual and purposive interpretation cannot alter a clear understanding of the text resulting from linguistic interpretation. Gardiner (n 125) 190; Weeramantry (n 125) paras 3.70–3.71. Accordingly, if a DTT, like the 1979 Korea–Belgium DTT, does not ensure an application of domestic anti-tax avoidance rules, it may be very difficult to deny a benefit under that DTT. In that regard, it is worth remembering that while some authoritative commentators argue in favour of the presence or applicability of a general anti-abuse principle in the interpretation of DTTs—Klaus Vogel and others, *Klaus Vogel on Double Taxation Conventions: A Commentary to the OECD-, UN- and US Model Conventions for the Avoidance of Double Taxation of Income and Capital, Introduction* (1991 Kluwer) para 121, others do question such arguments—David A Ward, 'Abuse of Tax Treaties' in Herbert H Alpert and Kees van Raad (eds), *Essays in International Taxation in Honor of Sydney I. Roberts* (Kluwer Law and Taxation 1993) 403.

[162] Clearly, this principle more precisely and more smoothly guides tax authorities and courts to deny benefits under DTTs than the VCLT.

[163] In comparison to a guiding principle, the PPT (at least linguistically and grammatically) lowers the threshold to pass the tax intention test from a main to one of the principal purposes and appears to shift the burden of proof under the contradiction test from tax authorities to taxpayers. Michael Lang, 'BEPS Action 6: Introducing an Antiabuse Rule in Tax Treaties' (14 May 2014) Tax Notes Int 661. cf a more nuanced approach to the perception of the PPT in that regard: Kuźniacki (n 36) 246–51; Schön (n 36) s 12.5.

[164] One may wonder if, in such a case, the Tribunal would conclude that the Korean SOFD led to a denial of benefits under the 1979 Korea–Belgium DTT in accordance with the VCLT and a guiding principle. Although this requires an in-depth analysis going beyond the scope of this article, it seems that the Tribunal might find it difficult to conclude this affirmatively due to the contradiction test.

[165] cf Martín Jiménez (n 13) s 25.5: "Maybe, rather than extending IIAs to cover tax rules, the ideal solution would be to identify offensive tax provisions and amend them within the tax world. However, until this happens, it appears that the systemic interpretation and application of (domestic and international) tax law in light of some IIA standards, as a second-best solution, may contribute to mitigating the most troublesome rule of law and taxpayer rights issues that may arise with the aggressive application of (vague) tax rules (such as PPTs, GAARs or similar clauses), especially in countries in which these issues are not controlled effectively in their domestic systems. This is a field in which taxpayers can probably benefit from IIAs, even if the threshold to apply them is high, in a post-BEPS or post-Pillars era where PPTs and GAARs are spreading out all over a world dominated by tax uncertainty."

not violate the 2011 BLEU–Korea BIT in any way.[166] However, the way the Tribunal reached that conclusion could lead to a more thorough and self-standing analysis of the relations between the Korean SOFD with the 1979 Korea–Belgium DTT. It could have led the Tribunal to determine the role of the substance over form approach in an application of an abuse of rights principle under DTTs and IIAs in a similar way, thereby contributing to the convergence and predictability of determination of abuse of those treaties.

It seems that the highly sophisticated technical 'battle' between tax expert witnesses prompted the Tribunal to pragmatically draw on their reports and include in the text of the Award only oversimplified observations of the OECD. According to those observations, SOFDs are compatible with DTTs, and thus the application of one of them (the Korean SOFD) did not violate the 2011 BLEU–Korea BIT. No in-depth or careful consideration of the Korean SOFD in respect of the 1979 Korea–Belgium DTT took place.[167] It starkly contrasts the Lone Star Award with the Cairn Award in which the Tribunal's exploration of the Indian SOFD constitutes the most comprehensive analysis of domestic anti-tax avoidance rule in international arbitration case law so far.[168]

Nevertheless, in ISDS case law in tax-related cases,[169] the Lone Star Award demonstrates that taxation by a State hosting an investment is deemed a breach of an IIA only in extreme circumstances.[170] Accordingly, although there were certain issues with the Tribunal's reasoning regarding a denial of benefits under the 1979 Korea–Belgium DTT by the NTS and Korean courts via the Korean SOFD,[171] the fact was that the denial did not violate that DTT by an extreme deviation from the OECD's view and a guiding principle. The same can be said in relation to the rule and principles of interpretation of the VCLT. Neither the NTS nor the Korean courts violated the 1979 Korea–Belgium DTT (if at all) enough to breach the 2011 BLEU–Korea BIT.[172]

Similarly, tax authorities can err in the interpretation of tax law, including DTTs, but that in itself does not violate an IIA's FET or other standards of investment protection. While the domestic court's examination of a decision of the tax authorities is not immune to scrutiny by a tribunal, the bar to considering their case law violating an IIA is high: there must be a denial of justice or a manifest failure of justice before a violation of the FET or other standards of investment protection are evident.[173] In Lone Star, the Tribunal highlighted many times that the 'Claimants have not alleged that there has been a denial of justice in the resulting tax litigation', and they have

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[166] *Lone Star* (n 1) paras, 410, 469–71, 480.

[167] In that sense, the approach of the Lone Star Tribunal resembles that of the CJEU in the Danish BO cases. In those cases, the CJEU appeared to omit many of the non-trivial legal and factual threads that had emerged in the course of years of proceedings in front of the tax authorities and courts in Denmark. The CJEU (C-115/16, C-118/16, C-119/16 and C-299/16) and (C-116/16 and C-117/16) (n 12). The cases were also heavily anonymised and, on many levels, simplified and generalised by the Danish courts for the purpose of asking preliminary questions to the CJEU. All this made it extremely difficult for the CJEU to prioritise the facts and legal issues that should be properly analysed. cf Susi Baerentzen, 'Danish Cases on the Use of Holding Companies for Cross-Border Dividends and Interest—A New Test to Disentangle Abuse from Real Economic Activity?' (2020) 12(1) World Tax J 12. This most likely prompted the CJEU to cut the Gordian knot (the complexity of the cases) by using the general principle of a prohibition on the abuse of rights under EU law as a one-fits-all solution, while the concept of BO was highly marginalised. Still, the CJEU further developed and relied on the principle of abuse of rights, while the Lone Star Tribunal did not do so.

[168] Although it was not articulated by the *Cairn* Tribunal explicitly, the proper decoding of the Indian SOFD was pivotal not only to (i) assess the major defence of the Respondent, but also (at least partly) to (ii) examine the main justification for the violation of the principles of legal certainty and predictability by the retroactive taxation. *Cairn* (n 4) paras 931–1591, 1794–97, 1809–17. Kuźniacki and van Weeghel (n 4) 126, 138.

[169] For a thorough analysis of international arbitration case law in tax-related cases, see William W Park, 'Tax and Arbitration' (2020) 36(2) Arb Intl 166–97.

[170] 'This is also why foreign investors will search for possibilities to include specific provisions in investment agreements (stability provisions, set-off clauses/adjustment clauses) in order to be better protected against unforeseen taxation' (Simonis (n 98) 275).

[171] See Section IV.

[172] Interestingly, a commentator made a point before an award was rendered in *Lone Star* case that the fact that Brigitte Stern is one of the arbitrators in *Lone Star*, and she was previously in the *Burlington* case, in which even 99 per cent taxation on windfall profits was not considered by the Tribunal as an indirect expropriation: "might indicate a significant obstacle in Lone Star's attempts to raise these claims under anything other than an expropriation standard because Lone Star is not a party to the BTT [DTT] and is therefore not guaranteed by any specific tax-based investment rights. As expropriation claims, however, are difficult to prove, Lone Star faces a daunting task in proving its tax-related damages. The fact that the alleged damages fall far below the 50–99 per cent tax rates deemed legitimate in Burlington also bodes poorly for Lone Star's chances. (Joel K Browning, 'Investor-State Dispute between Lone Star and Korea: Legal and Policy Analysis' (2016) 9(1) J East Asia Int Law 203)." *Burlington Resources, Inc v Republic of Ecuador*, ICSID Case No ARB/08/5, Decision on Liability (14 December 2014) para 220: 'Windfall taxes of between 50% and [99%] were not expropriatory as they did not render the claimant's investment totally unprofitable'.

[173] In respect of the FET, see eg *Sergei Paushok, CJSC Golden East Company and CJSC Vostokneftegaz Company v The Government of Mongolia, Award on Jurisdiction and Liability*, *ad hoc* Tribunal (UNCITRAL) IIC 490 (2011) (28 April 2011) paras 625–26. For an analysis, see van Weeghel (98) s 26.2.3.

not evidenced any other violations of standards of investment protection, therefore there was no violation of the 2011 BLEU–Korea BIT or the 1979 Korea–Belgium DTT.[174] It implies that, when determining the lack of violation of the BIT, the Tribunal placed a lot of emphasis on the fact that the claims had been litigated locally and that the litigation did not constitute a denial of justice. This in conjunction with the quite blatant treaty-shopping scheme of Lone Star strongly influenced the Tribunal's reasoning against tax-related claims. In that regard, the Tribunal's analysis of the application of the Korean SOFD was clearly in conformity with Korean domestic jurisprudence and the prevailing interpretations given by the State's judicial authorities. Such methodological approach to the examination of domestic law is widely appreciated in international case law.[175]

Might the Tribunal have concluded differently if Lone Star had not litigated in the Korean courts, but decided to arbitrate straight away against the NTS? This question underscores the importance of having an upfront strategy in terms of where claims are going to be advanced, ie in administrative tribunals, national courts or international arbitration courts. In the author's view, however, Lone Star Belgium SPEs: (i) were too deprived of any other reason than benefiting from the 1979 Korea–Belgium DTT; (ii) had so little economic substance; (iii) had so little control over the received income; and (iv) were liquidated so quickly once they had served their purpose as the facilitators of obtaining benefits under the DTT that the Tribunal's conclusion would be the same. That is to say, the Claimants in Lone Star did not appear to have legitimate expectations to benefit from the 1979 Korea–Belgium DTT due to their own wrongdoing, ie establishing a tax avoidance scheme that was evaluated by the domestic courts as an abuse of the DTT. In addition, the Lone Star Award leaves the impression that it was not only the view of the Korean courts but also the Tribunal.[176] In that regard, a parallel can be made to the Yukos Award: in Yukos, the Tribunal's observation of an abuse of the DTT by the Claimants had an impact on the quantum of damage (reduction by 25 per cent) while the Lone Star Tribunal considered it earlier on at the merits phase to dismiss the Claimants' tax claims regarding benefits under the DTT altogether. Also, while the doctrine of 'contributory fault' was instructive for the Yukos Tribunal,[177] the Lone Star Tribunal seemed to implicitly rely on the principle of abuse of rights.

Still, the Lone Star Award could have increased its quality, furthered the rule of law[178] and would have otherwise benefited significantly the entire ISDS and international tax community if the Tribunal had relied explicitly on the principle of abuse of rights while examining the compatibility of the Korean SOFD with the BIT and the DTT and referred to other relevant principles of law, as the Cairn Tribunal did.[179] As Stephan Schill aptly observed,

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[174] *Lone Star* (n 1) paras 443, 465, 469, 479.
[175] PCIJ, *Payment in Gold of Brazilian Federal Loans Contracted in France (France v Brazil)*, Judgment (12 July 1929) Series A No 21 (1929) 124; *ELSI* (n 47) para 47; *Hussein Nuaman Soufraki v UAE*, ICSID Case No ARB/02/7, Decision of the *ad hoc* Committee on the Application for Annulment of Mr Soufraki (5 June 2007) para 96; *Fraport AG Frankfurt Airport Services Worldwide v Philippines*, ICSID Case No ARB/03/25, Decision on the Application for Annulment of Fraport AG Frankfurt Airport Services Worldwide (23 December 2010) para 236; *Emmis International Holding BV v Hungary*, ICSID Case No ARB/12/2, Award (16 April 2014) para 175. In literature, see Ole Spiermann, 'Applicable Law' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (OUP 2008) 114. When an allegation of a denial of justice is made, it is less justifiable to rely on domestic jurisprudence. See Hepburn (46) 177. However, no such allegation was made by the Claimants in *Lone Star* (1).
[176] Ibid.
[177] For relevant references on that doctrine, see n 12.
[178] For a recent scientific contribution on the rule of law in standards of investment protection, see August Reinisch and Stephan W Schill (eds), *Investment Protection Standards and the Rule of Law* (OUP 2023).
[179] eg the *Lone Star* Tribunal could have referred to the *Cairn* Award by pointing out that domestic anti-tax avoidance rules, such as the Korean SOFD, are 'less intrusive on taxpayers' interests of legal certainty and predictability, since taxpayers that actively engage in abusive practices can hardly have a legitimate interest to benefit from their conduct'. *Cairn* (n 4) para 1796. This could be a powerful way to bridge the understanding of dynamics between the prevention of abuse of DTTs and IIAs insofar as tax scholars rightly recognise that the principle of legal certainty and predictability does not seem to equally protect the taxpayers actively seeking to abusively avoid taxation and the taxpayers who in the course of ordinary day-to-day business or investment practices benefit from tax advantages in a full compliance with the letter and the purpose of tax law. Judith Freedman, 'Defining Taxpayer Responsibility: In Support of a General Anti-Avoidance Principle' (2004) 4 Br Tax Rev 356: 'There will be no deficit in the rule of law if the area of uncertainty is one that does not affect day-to-day transactions and is governed not by arbitrariness but rather by procedures that attract the support of the compliant members of the tax community.' However, it is worth bearing in mind that the borderline between abusive tax avoidance and acceptable tax planning is very thin and context-sensitive. Therefore '[t]hose who deliberately and with open eyes try to balance on the borderline of acceptable tax planning should not be surprised if they have to realize that they fall down on the wrong side'. Frederik Zimmer, 'In Defence of General Anti-Avoidance Rules' (2019) 73(4) Bull Int Tax s 5. One could even argue, as Brian Arnold did, that taxpayers are exclusively responsible for tax uncertainty whenever they attempt to avoid taxation by artificial structures and thus they may not deserve to be protected by the principle of legal certainty. Brian Arnold, 'Some Thoughts on Tax Certainty' (2021) 2(1) Belt Road Initiative Tax J 93, 98. cf Stef van Weeghel and Błażej Kuźniacki, 'Raising Tax Certainty in Cross-Border Tax Disputes through a Body of Experts' (2022) 3(2) Belt Road Initiative Tax J 65.

'one of the most important areas where general principles of public law can impact and transform international law is in elucidating the interpretation of broadly formulated substantive standards of treatment'.[180] His point is apt per analogiam to clarify and sharpen the understanding of an SOFD for the purposes of DTTs and IIAs. However, the role of the substance over form approach in applying the principle of an abuse of rights under DTTs and IIAs requires further research, which could pave the way to a convergence in their interpretation, especially in difficult borderline cases between abusive and legitimate tax and investment practices. Global and regional tax developments, including the implementation of anti-BEPS rules and Pillar Two rules, strengthen the need for interdisciplinary research. Such research might reveal that a convergence in denying benefits under DTTs and IIAs will enhance the rule of law and increase legal certainty in tax and investment domains.

[180] Stephan Schill, 'General Principles of International Law and International Investment Law' in Gazzini and De Brabandere (n 28) 157. In a similar vein, see M Hirsh, 'Sources of International Law' in Bjorklund and Reinisch (n 28) 27.