

Briefing paper on conceptual topics related to the Informal Working Group on Institutional Matters in the ISA's Exploitation Regulations

Effective Control

Facilitated by Ambassador Georgina Guillén-Grillo (Costa Rica) and Mr. Salvador Vega (Chile),

I. Background

1. It appears from the Indicative Programme of Work for the first part of the twenty-ninth session, that one conceptual topic of 'Effective Control' may be discussed within the Informal Working Group on Institutional Matters, scheduled for three hours on the morning of Monday 25th March 2024.
2. The following briefing paper sets out proposed focus areas and objectives for this session.
3. Delegates are also invited to review the materials previously shared for a webinar on the same topic, in September 2023, which are accessible here: <https://www.isa.org.jm/events/webinar-informal-working-group-on-institutional-matters-effective-control/>

II. Summary of Issue

4. Since the beginning of the Council's discussions on the Draft Exploitation Regulations, a growing number of delegations have noted the need to discuss the issue of "effective control" within the framework of the Informal Working Group on Institutional Matters. "Effective control" is shorthand for the relationship between a sponsoring State and a non-State ISA contractor.
5. According to UNCLOS (Article 139), ISA contracts can be held by the Enterprise, by State Parties, or by non-State entities with the nationality or sponsorship of a State Party.
6. The rationale for State sponsorship was expressed succinctly by the Seabed Disputes Chamber of the International Tribunal for the Law of the Sea in its 2011 Advisory Opinion, as follows, "*The purpose of requiring the sponsorship of applicants for contracts for the exploration and exploitation of the resources of the Area is to achieve the result that the obligations set out in the Convention, a treaty under international law which binds only States Parties thereto, are complied with by entities that are subjects of domestic legal systems.*"¹
7. The ISA "State sponsorship" system ensures there is always a State (which is subject to UNCLOS and ISA rules, regulations and procedures) accountable to the rest of the international community for any ISA contractor's conduct. The individual State can hold its sponsored contractor to the relevant rules, by way of national law and administrative measures.
8. For that mechanism to work in practice, there needs to be a real link between the State and the contractor: a relationship of "effective control". UNCLOS stipulates that any non-State contractor must be "effectively controlled" by a sponsoring State or by nationals of the sponsoring State. ² This is both a pre-condition to ISA contract award, and a continuing

¹ ITLOS, *Responsibilities and obligations of States sponsoring persons and entities with respect to activities in the Area*, Advisory Opinion, 1 February 2011, ITLOS Reports 2011.

² UNCLOS, Articles 139(1) and Article 153(2)(b), and Annex III, Articles 4(3) and 9(4).

requirement throughout contract term. UNCLOS does not however expressly define “effective control” or say much more about how it should work.

9. According to the travaux préparatoires for UNCLOS, there were some concerns expressed about the “effective control” provisions, which were resolved by a compromise that requirements for “effective control” were to be set forth in rules, regulations and procedures of the ISA.³

10. This is reflected in Annex III to UNCLOS (Article 4(3)) which states:

*“Each applicant shall be sponsored by the State Party of which it is a national unless the applicant has more than one nationality, as in the case of a partnership or consortium of entities from several States, in which event all States Parties involved shall sponsor the application, or unless the applicant is effectively controlled by another State Party or its nationals, in which event both States Parties shall sponsor the application. **The criteria and procedures for implementation of the sponsorship requirements shall be set forth in the rules, regulations and procedures of the Authority.**”*

11. This Article also indicates that nationality and “effective control” are separate criterion, and that multiple sponsoring States are envisaged where the State of effective control differs from the State of nationality.

12. To date, none of the ISA’s rules have provided a clear definition of “effective control”.

13. A paper published by an ISA working group of experts, focused on liability questions, noted two different possible approaches to the “effective control” question⁴, which can be summarised as follows:

- i. The **regulatory control** approach, which examines which State has the (*de jure*) ability to exercise regulatory jurisdiction over the entity. In this regard, the country of registration or incorporation of that company is the primary factor.
- ii. The **economic control** approach, which examines which State has the (*de facto*) ability to exercise economic and management control over the entity. In this regard relevant factors may include: the wider company structure (e.g. holding and parent companies); owners of majority shares and voting rights; source of the capital and ongoing resources invested into the ISA project; who has the rights to elect the company’s Board; who has influence over company decisions; who represents the entity in its dealings.

14. It is noted that these are two quite different approaches, which may lead to different outcomes, if applied by the Council to the definition of “effective control”.

15. The ITLOS Advisory Opinion cautioned against an interpretation that would allow ‘sponsoring States of convenience’.

“Equality of treatment between developing and developed sponsoring States is consistent with the need to prevent commercial enterprises based in developed States from setting up companies in developing States, acquiring their nationality and obtaining their sponsorship in

³ Report of the coordinators of the working group of 21 to the First Committee during the ninth session of the conference.

⁴ Rojas and Phillips (2019), ‘Effective Control and Deep Seabed Mining: Towards a Definition,’ Liability Issues for Deep Seabed Mining Series: <https://www.cigionline.org/publications/effective-control-and-deep-seabed-mining-toward-definition-1/>

*the hope of being subjected to less burdensome regulations and controls. The spread of sponsoring States “of convenience” would jeopardize uniform application of the highest standards of protection of the marine environment, the safe development of activities in the Area and the protection of the common heritage of mankind”.*⁵

16. In considering interpretation, Council may find the following sources informative:

- i. Use of the same term ‘effective control’ in a different context in Part XI to UNCLOS, but with further elaboration, whereby Article 5(3)(c) of Annex III to UNCLOS⁶ provided that:

“...In cases where there is a substantial corporate relationship between the contractor and the owner of the technology, the closeness of this relationship and the degree of control or influence shall be relevant to the determination whether all feasible measures have been taken to acquire such a right. In cases where the contractor exercises effective control over the owner, failure to acquire from the owner the legal right shall be considered relevant to the contractor's qualification for any subsequent application for approval of a plan of work;”

- ii. The International Law Commission (ILC) Draft Articles from 2006 which, in considering a different matter (the purposes of the diplomatic protection of a corporation), noted that the relevant State would be the State under whose law the corporation was incorporated unless *“the corporation is controlled by nationals of another State or States and has no substantial business activities in the State of incorporation, and the seat of management and the financial control of the corporation are both located in another State”*. In which case the other State or States would be the relevant State(s).⁷

17. We also wish to bring Council’s attention to the fact that the discussion of “effective control” inter-relates to other aspects of the Draft Exploitation Regulations, and the ISA’s overall regime to control and supervise activities in the Area, including:

- i. Identifying beneficial owners of a contract, which may be relevant to ensure ISA rules regarding monopolisation, and access to reserved areas, are respected.
- ii. The ability in practice for the sponsoring State to meet its responsibilities including:
 - a) to ensure that activities in the Area under its sponsorship shall be carried out in conformity with UNCLOS and the rules, regulations and procedures of the ISA [Article 139 UNCLOS],
 - b) to assist the ISA exercise compliance control over activities in the Area [Article 153(4) UNCLOS], and
 - c) to ensure that recourse is available in accordance with their legal systems for prompt and adequate compensation or other relief in respect of damage caused by pollution of the marine environment by natural or juridical persons under their jurisdiction [Article 235 UNCLOS].

⁵ Ibid. paragraph 159.

⁶ Subsequently disappplied by the Agreement relating to the Implementation of Part XI of the United Nations Convention on the Law of the Sea of 10 December 1982 (1994), Annex, Section 5, para 2

⁷ International Law Commission, Diplomatic Protection: text of the draft articles with commentaries (2006) UN Doc A/61/10, draft article (9):

https://legal.un.org/ilc/texts/instruments/english/commentaries/9_8_2006.pdf

- iii. Promotion of the effective participation of developing States in activities in the Area [Article 148 UNCLOS].
 - iv. Joint sponsorship possibilities envisaged under UNCLOS [e.g. Article 139 UNCLOS].
 - v. Liability of and benefits to sponsoring States [Articles 139 and 153 UNCLOS], also recalling the ‘Equalization’ discussions under the Informal Open-Ended Working Group which raised examples of tax exemptions given to private sector contractors by sponsoring States.
 - vi. Risks and liabilities that may arise to the ISA and the implementation of UNCLOS, if there are loopholes in the overall regulatory regime, or if Council due diligence at contract award stage is flawed. [Article 22 of Annex III UNCLOS]
18. In the context of these discussions, it may also be helpful to note that the majority of ISA contractors currently in operation are either States Parties themselves, which do not require sponsorship, or State-owned enterprises, where questions of effective control do not arise. There are however also a number of existing exploration contracts held by private sector entities, with State sponsorship, for whom this question is highly pertinent.
19. Finally, we refer Council members to another useful commentary from the ITLOS 2011 Advisory Opinion, which clarified that no State can be compelled unwillingly to become a sponsoring State:

“No provision of the Convention imposes an obligation on a State Party to sponsor an entity that holds its nationality or is controlled by it or by its nationals. As the Convention does not consider the links of nationality and effective control sufficient to obtain the result that the contractor conforms with the Convention and related instruments, it requires a specific act emanating from the will of the State or States of nationality and of effective control. Such act consists in the decision to sponsor.”⁸

III. Relevant Regulations

20. The definition that the ISA will apply to “Effective Control” will be relevant for a number of the draft Exploitation Regulations, and in particular we note the following:
- i. Draft Regulation 6: Certificate of Sponsorship;
 - ii. Draft Regulation 13 (or 13 Alt): Assessment of applications (or Assessment of applicants and application);
 - iii. Annex I: Application for approval of a Plan of Work to obtain an Exploitation Contract;
 - iv. Schedule of defined terms.

IV. Questions for Consideration

21. We propose the following questions to structure the conceptual discussion around “effective control” scheduled for the March 2024 session of Council:
- 1) Can Council agree on the overall purpose and rationale for “effective control”?
 - 2) Does Council agree that our responsibility to develop “*the criteria and procedures for implementation of the sponsorship requirements [...] in the rules, regulations and*

⁸ Supra footnote 4, paragraph 78.

procedures of the Authority.” includes a need to provide a clear definition of “effective control” in the Exploitation Regulations?

- 3) Do Council members prefer the ‘regulatory control’ or ‘economic control’ approach to “effective control” (or a mixture, or another option), and for what reason?