INTERNATIONAL COURT OF JUSTICE

REPORTS OF JUDGMENTS,
ADVISORY OPINIONS AND ORDERS

CASE CONCERNING ELETTRONICA SICULA S.p.A. (ELSI)

(UNITED STATES OF AMERICA *v.* ITALY)

JUDGMENT OF 20 JULY 1989

1989

COUR INTERNATIONALE DE JUSTICE

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(ÉTATS-UNIS D'AMÉRIQUE c. ITALIE)

ARRÊT DU 20 JUILLET 1989

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CASE CONCERNING ELETTRONICA SICULA S.p.A. (ELSI)

(UNITED STATES OF AMERICA *v.* ITALY)

Diplomatic protection — Rule of exhaustion of local remedies — Applicability to claim under treaty which does not mention the rule — Applicability to claim for declaratory judgment — Allegation that objection barred by estoppel — Conditions required for the satisfaction of the rule.

Alleged breaches of 1948 Treaty of Friendship, Commerce and Navigation between Italy and United States, the Protocol and the 1951 Supplementary Agreement thereto.

Article III of FCN Treaty — Alleged interference with shareholders' right to "control and manage" company, by requisition of its plant and equipment — Meaning of qualifying phrase "in conformity with the applicable laws and regulations" of Party — Relevance of municipal law — Possibility of disturbance of normal exercise of rights during public emergencies and the like.

Article V, paragraphs 1 and 3, of FCN Treaty — "Constant protection and security" of nationals of each Party "for their persons and property" — Standard of protection required — Identification of "property" to be protected — Complaint of occupation of property — Treaty provision not equivalent to a warranty that property shall never in any circumstances be occupied or disturbed — Complaint of delay in ruling an appeal against requisition.

Article V, paragraph 2, of FCN Treaty — Paragraph 1 of Protocol to FCN Treaty — "The property of nationals . . . of either . . . Party shall not be taken . . ." — Difference between English text ("taken") and Italian text ("espropriati") *— Disguised expropriation — Relevance of company's financial situation.*

Article I of Supplementary Agreement to FCN Treaty — Prohibition of "arbitrary or discriminatory measures . . . resulting particularly in" preventing effective control and management of enterprises or impairing legally acquired rights — Effect of word "particularly" — Definition of arbitrariness in international law — Relevance of finding of municipal court to question whether act was to be classed

as arbitrary in international law — Whether order made in context of operating system of law and remedies may be arbitrary measure.

Article VII of FCN Treaty — Right "to acquire, own and dispose of immovable property or interests therein" — Difference between English text ("interests") and Italian text ("diritti reali") *— Standards of protection laid down by treaty.*

JUDGMENT

Present: President RUDA; *Judges* ODA, AGO, SCHWEBEL, Sir Robert JENNINGS; *Registrar* VALENCIA-OSPINA.

In the case concerning Elettronica Sicula S.p.A. (ELSI),

between

the United States of America,

represented by

The Honorable Abraham D. Sofaer, Legal Adviser, Department of State,
Mr. Michael J. Matheson, Deputy Legal Adviser, Department of State,

as Co-Agents;

Mr. Timothy E. Ramish,

as Deputy Agent;

Ms Melinda P. Chandler, Attorney/Adviser, Department of State,
Mr. Sean D. Murphy, Attorney/Adviser, Department of State,
The Honorable Richard N. Gardner, Ambassador to Italy (1977-1981); Henry L. Moses Professor of Law and International Diplomacy, Columbia University; Counsel to the Law Firm of Coudert Brothers,

as Counsel and Advocates;

Mr. Giuseppe Bisconti, Studio Legale Bisconti, Rome,
Mr. Franco Bonelli, Professor of Law, Genoa University; Partner, Studio Legale Bonelli,
Mr. Elio Fazzalari, Professor of Civil Procedure, Rome University; Partner, Studio Legale Fazzalari,
Mr. Shabtai Rosenne, Member of the Israel Bar; Member of the Institute of International Law; Honorary Member of the American Society of International Law,

as Advisers,

and

the Republic of Italy

represented by

Mr. Luigi Ferrari Bravo, Professor of International Law at the University of Rome; Head of the Legal Service of the Ministry of Foreign Affairs,

as Agent and Counsel;

Mr. Riccardo Monaco, Professor Emeritus at the University of Rome,

as Co-Agent and Counsel;

Mr. Ignazio Caramazza, State Advocate; Secretary-General of the Avvocatura Generale dello Stato,

as Co-Agent and Advocate;

Mr. Michael Joachim Bonell, Professor of Comparative Law at the University of Rome,
Mr. Francesco Capotorti, Professor of International Law at the University of Rome,
Mr. Giorgio Gaja, Professor of International Law at the University of Florence,
Mr. Keith Highet, Member of the Bars of New York and the District of Columbia,
Mr. Berardino Libonati, Professor of Commercial Law at the University of Rome,

as Counsel and Advocates;

assisted by

Mr. David Clark, Ll.B. (Hons), Member of the Law Society of Scotland,
Mr. Alberto Colella, Assistant Legal Adviser to the Ministry of Foreign Affairs,
Mr. Alan Derek Hayward, Fellow of the Institute of Chartered Accountants in England and Wales,
Mr. Pier Giusto Jaeger, Professor of Commercial Law at the University of Milan,
Mr. Attila Tanzi, Assistant Legal Adviser to the Ministry of Foreign Affairs,

Mr. Eric Wyler, Maître assistant of Public International Law at the Faculty of Law of the University of Lausanne,

as Advisers,

THE CHAMBER OF THE INTERNATIONAL COURT OF JUSTICE formed to deal with the case above mentioned,

composed as above,

after deliberation,

delivers the following Judgment:

1. By a letter dated 6 February 1987, filed in the Registry of the Court the same day, the Secretary of State of the United States of America transmitted to the Court an Application instituting proceedings against the Republic of Italy in respect of a dispute arising out of the requisition by the Government of Italy of the plant and related assets of Raytheon-Elsi S.p.A., previously known as Elettronica Sicula S.p.A. (ELSI), an Italian company which was stated to have been 100 per cent owned by two United States corporations. By the same letter, the Secretary of State informed the Court that the Government of the United States requested, pursuant to Article 26 of the Statute of the Court, that the dispute be resolved by a Chamber of the Court.

2. Pursuant to Article 40, paragraph 2, of the Statute, the Application was at once communicated to the Government of the Republic of Italy. In accordance with paragraph 3 of that Article, all other States entitled to appear before the Court were notified of the Application.

3. By a telegram dated 13 February 1987 the Minister for Foreign Affairs of Italy informed the Court that his Government accepted the proposal put forward by the Government of the United States that the case be heard by a Chamber composed in accordance with Article 26 of the Statute; this acceptance was confirmed by a letter dated 13 February 1987 from the Agent of Italy.

4. By an Order dated 2 March 1987, the Court, after recalling the request for a Chamber and reciting that the Parties had been duly consulted as to the composition of the proposed Chamber in accordance with Article 26, paragraph 2, of the Statute and Article 17, paragraph 2, of the Rules of Court, decided to accede to the request of the Governments of the United States of America and Italy to form a special Chamber of five judges to deal with the case, declared that at an election held on that day President Nagendra Singh and Judges Oda, Ago, Schwebel and Sir Robert Jennings had been elected to the Chamber, and declared a Chamber to deal with the case to have been duly constituted by the Order, with the composition indicated.

5. The Court further fixed time-limits, by the said Order, for the filing of a Memorial by the United States of America and a Counter-Memorial by Italy, which were duly filed within the time-limits. In its Counter-Memorial, Italy presented an objection to the admissibility of the Application; by letters addressed to the Registrar on 16 November 1987, the Parties agreed, with reference to Article 79, paragraph 8, of the Rules of Court, that the objection should "be heard and determined within the framework of the merits". By an Order dated 17 November 1987, the Chamber took note of that agreement, found that the filing of further pleadings by the Parties was necessary, authorized the filing of a Reply by the United States of America and a Rejoinder by Italy, and fixed time-limits for these; the Reply and Rejoinder were duly filed within those time-limits.

6. On 11 December 1988 Judge Nagendra Singh, President of the Chamber, died. Following further consultations with the Parties with regard to the composition of the Chamber in accordance with Article 17, paragraph 2, of the Rules of Court, the Court, by Order dated 20 December 1988, declared that Judge Ruda, President of the Court, had that day been elected a Member of the Chamber to fill the vacancy left by the death of Judge Nagendra Singh. In accordance with Article 18, paragraph 2, of the Rules of Court, President Ruda became President of the Chamber.

7. At 12 public sittings held between 13 February and 2 March 1989, the Chamber was addressed by the following representatives of the Parties:

For the United States of America: The Honorable A. D. Sofaer
Mr. M. J. Matheson
Mr. T. E. Ramish
Ms M. P. Chandler
Mr. S. D. Murphy
The Honorable R. N. Gardner
Mr. G. Bisconti
Professor F. Bonelli
Professor E. Fazzalari

For Italy:

Professor L. Ferrari Bravo
Professor R. Monaco
Mr. I. Caramazza
Professor M. J. Bonell
Professor F. Capotorti
Professor G. Gaja
Mr. K. Highet
Professor B. Libonati

8. The United States called as witnesses Mr. Charles Francis Adams (who was examined by Mr. Sofaer and cross-examined by Mr. Highet) and Mr. John Dickens Clare (who was examined by Ms Chandler and cross-examined by Mr. Highet). The United States called as expert Mr. Timothy Lawrence (who was cross-examined by Professor Bonell). Mr. Giuseppe Bisconti also addressed the Court on behalf of the United States; since he had occasion to refer to matters of fact within his knowledge as a lawyer acting for Raytheon Company, the President of the Chamber acceded to a request by the Agent of Italy that Mr. Bisconti be treated *pro tanto* as a witness. Mr. Bisconti, who informed the Chamber that both Raytheon Company and Mr. Bisconti himself waived any relevant privilege, was cross-examined by Mr. Highet. Italy called as expert Mr. Alan Derek Hayward.

9. During the hearings questions were put to the Parties, and to the witnesses and experts, by the President and Members of the Chamber; replies were given orally or in writing prior to the close of the oral proceedings, with documents in support. The Chamber decided further that each Party might comment in writing on the replies of the other Party to a series of questions, put at a late stage of the oral proceedings, and a time-limit was fixed for that purpose; written comments were duly filed within that time-limit. A further question was put to one Party after the close of the hearings and answered in writing; the other Party was given an opportunity to comment on the answer.

10. In the course of the written proceedings the following submissions were presented by the Parties:

On behalf of the United States of America,

in the Application:

> "while reserving the right to supplement and amend this submission as appropriate in the course of further proceedings, the United States requests the Court to adjudge and declare as follows:
>
> *(a)* that the Government of Italy has violated the Treaty of Friendship, Commerce and Navigation between the United States of America and the Italian Republic of 1948, in particular, Articles II, III, V and VII of the Treaty, and Articles I and V of the 1951 Supplement; and
> *(b)* that the Government of Italy is responsible to pay compensation to the United States, in an amount to be determined by the Court, as measured by the injuries suffered by United States nationals as a result of these violations, including the additional financial losses which Raytheon suffered in repaying the guaranteed loans and in not

recovering amounts due on open accounts, as well as expenses incurred in defending against Italian bank lawsuits, in mitigating the damage to its reputation and credit, and in pursuing its claim for redress";

in the Memorial:

"the United States submits to the Court that it is entitled to a declaration and judgment that:

(a) Italy — by engaging in the acts and omissions described above, which prevented Raytheon and Machlett, United States corporations, from liquidating the assets of their wholly-owned Italian corporation ELSI and caused the latter's bankruptcy, and by its subsequent actions and omissions — violated the international legal obligations which it undertook by the Treaty of Friendship, Commerce and Navigation between the two countries, and the Supplement thereto, and in particular, violated:

- Article III (2), in that Italy's actions and omissions prevented Raytheon and Machlett from exercising their right to manage and control an Italian corporation;
- Article V (1) and (3), in that Italy's actions and omissions constituted a failure to provide the full protection and security as required by the Treaty and by international law;
- Article V (2), in that Italy's actions and omissions constituted a taking of Raytheon's and Machlett's interests in property without just compensation and due process of law;
- Article VII, in that these actions and omissions denied Raytheon and Machlett the right to dispose of their interests in immovable property on terms no less favorable than an Italian corporation would enjoy on a reciprocal basis;
- Article I of the Supplement, in that the treatment afforded Raytheon and Machlett was both arbitrary and discriminatory, prevented their effective control and management of ELSI, and also impaired their other legally acquired rights and interests;

(b) that, owing to these violations of the Treaty and Supplement, singly and in combination, the United States is entitled to compensation in an amount equal to the full amount of the damage suffered by Raytheon and Machlett as a consequence, including their losses on investment, guaranteed loans, and open accounts, the legal expenses incurred by Raytheon in connection with the bankruptcy, in defending against related litigation and in pursuing its claim, and interest on such amounts computed at the United States prime rate from the date of loss to the date of payment of the award, compounded on an annual basis; and

(c) that Italy accordingly should pay to the United States the amount of US$12,679,000, plus interest, computed as described above";

in the Reply:

"the United States submits to the Court that it is entitled to a declaration and judgment that:

(a) the claims brought by the United States are admissible before the Court since all reasonable local remedies have been exhausted;

(b) Italy — by engaging in the acts and omissions described above and in the Memorial, which prevented Raytheon and Machlett, United States corporations, from liquidating the assets of their wholly-owned Italian corporation ELSI and caused the latter's bankruptcy, and by its subsequent actions and omissions — violated the international legal obligations which it undertook by the Treaty of Friendship, Commerce and Navigation between the two countries, and the Supplement thereto, and in particular, violated:

- Article III (2), in that Italy's actions and omissions prevented Raytheon and Machlett from exercising their right to manage and control an Italian corporation;
- Article V (1) and (3), in that Italy's actions and omissions constituted a failure to provide the full protection and security as required by the Treaty and by international law;
- Article V (2), in that Italy's actions and omissions constituted a taking of Raytheon's and Machlett's interests in property without just compensation and due process of law;
- Article VII, in that these actions and omissions denied Raytheon and Machlett the right to dispose of their interests in immovable property on terms no less favorable than an Italian corporation would enjoy on a reciprocal basis;
- Article I of the Supplement, in that the treatment afforded Raytheon and Machlett was both arbitrary and discriminatory, prevented their effective control and management of ELSI, and also impaired their other legally acquired rights and interests;

(c) that, owing to these violations of the Treaty and Supplement, singly and in combination, the United States is entitled to compensation in an amount equal to the full amount of the damage suffered by Raytheon and Machlett as a consequence, including their losses on investment, guaranteed loans, and open accounts, the legal expenses incurred by Raytheon in connection with the bankruptcy, in defending against related litigation and in pursuing its claim, and interest on such amounts computed at the United States prime rate from the date of loss to the date of payment of the award, compounded on an annual basis; and

(d) that Italy accordingly should pay to the United States the amount of US$12,679,000, plus interest, computed as described above and in the Memorial."

On behalf of the Republic of Italy,

in the Counter-Memorial and in the Rejoinder:

"May it please the Court,

To adjudge and declare that the Application filed on 6 February 1987 by the United States Government is inadmissible because local remedies have not been exhausted.

If not, to adjudge and declare:

(1) that Article III (2) of the Treaty of Friendship, Commerce and Navigation of 2 February 1948 has not been violated;
(2) that Article V (l) and (3) of the Treaty has not been violated;
(3) that Article V (2) of the Treaty has not been violated;
(4) that Article VII of the Treaty has not been violated;
(5) that Article I of the Supplementary Agreement of 26 September 1951 has not been violated;

and, accordingly, to dismiss the claim."

11. In the course of the oral proceedings the following submissions were presented by the Parties:

On behalf of the United States of America,

at the hearing of 16 February 1989:

"The United States requests that the objection of the Respondent be dismissed and submits to the Court that it is entitled to a declaration and judgment that:

(1) the Respondent violated the international legal obligations which it undertook by the Treaty of Friendship, Commerce and Navigation between the two countries, and the Supplement thereto, and in particular, violated Articles III, V, and VII of the Treaty and Article I of the Supplement; and
(2) that, owing to these violations of the Treaty and Supplement, singly and in combination, the United States is entitled to reparation in an amount equal to the full amount of the damage suffered by Raytheon and Machlett as a consequence, including their losses on investment, guaranteed loans, and open accounts, the legal expenses incurred by Raytheon in connection with the bankruptcy, in defending against related litigation and in pursuing its claim, and interest on such amounts computed at the United States prime rate from the date of loss to the date of payment of the award, compounded on an annual basis; and

(3) that Italy accordingly should pay to the United States the amount of $12,679,000 plus interest."

At the hearing of 27 February 1989 (afternoon) the Agent of the United States confirmed that these were the final submissions of the United States.

On behalf of the Republic of Italy,

at the hearing of 23 February 1989, repeated as final submissions at the hearing of 2 March 1989 (afternoon):

"May it please the Court,

A. To adjudge and declare that the Application filed on 6 February

1987 by the United States Government is inadmissible because local remedies have not been exhausted.

B. If not, to adjudge and declare:

(1) that Article III of the Treaty of Friendship, Commerce and Navigation of 2 February 1948 has not been violated;
(2) that Article V, paragraphs 1 and 3, of the Treaty has not been violated;
(3) that Article V, paragraph 2, of the Treaty, and the related provisions of the Protocol to the Treaty, have not been violated;
(4) that Article VII of the Treaty has not been violated;
(5) that Article I of the Supplementary Agreement of 26 September 1951 has not been violated; and
(6) that no other Article of the Treaty or the Supplementary Agreement has been violated.

C. On a subsidiary and alternative basis only: to adjudge and declare that, even if there had been a violation of obligations under the Treaty or the Supplementary Agreement, such violation caused no injury for which the payment of any indemnity would be justified.

And, accordingly, to dismiss the claim."

* *

12. The claim of the United States in the present case is that Italy has violated the international legal obligations which it undertook by the Treaty of Friendship, Commerce and Navigation between the two countries concluded on 2 February 1948 ("the FCN Treaty") and the Supplementary Agreement thereto concluded on 26 September 1951, by reason of its acts and omissions in relation to, and its treatment of, two United States corporations, the Raytheon Company ("Raytheon") and The Machlett Laboratories Incorporated ("Machlett"), in relation to the Italian corporation Raytheon-Elsi S.p.A. (previously Elettronica Sicula S.p.A. (ELSI)), which was wholly owned by the two United States corporations. Italy contests certain of the facts alleged by the United States, denies that there has been any violation of the FCN Treaty, and contends, on a subsidiary and alternative basis, that if there was any such violation, no injury was caused for which payment of any indemnity would be justified.

13. In 1955, Raytheon (then known as Raytheon Manufacturing Company) agreed to subscribe for 14 per cent of the shares in Elettronica Sicula S.p.A. Over the period 1956-1967, Raytheon successively increased its holding of ELSI shares (as well as investing capital in the company in other ways) to a total holding of 99.16 per cent of its shares. In April 1963 the name of the company was changed from Elettronica Sicula S.p.A. to "Raytheon-Elsi S.p.A."; it will however be referred to hereafter as "ELSI". The remaining shares (0.84 per cent) in ELSI were acquired in April 1967 by Machlett, which was a wholly-owned subsidiary of Raytheon. ELSI was established in Palermo, Sicily, where it had a plant for the production of electronic components; in 1967 it had a workforce of

slightly under 900 employees. Its five major product lines were microwave tubes, cathode-ray tubes, semiconductor rectifiers, X-ray tubes and surge arresters.

14. During the fiscal years 1964 to 1966 inclusive, ELSI made an operating profit, but this profit was insufficient to offset its debt expense or accumulated losses, and no dividends were ever paid to its shareholders. In June 1964, the accumulated losses exceeded one-third of the company's share capital, and ELSI was thus required by Article 2446 of the Italian Civil Code to reduce its equity from 4,300 million lire to 2,000 million lire. The capital stock was therefore devalued by 2,300 million lire and recapitalized by an equal amount subscribed by Raytheon. A similar operation was necessary in March 1967. In February 1967, according to the United States, Raytheon began taking steps to endeavour to make ELSI self-sufficient. Raytheon and Machlett designated a number of highly-qualified personnel to provide financial, managerial and technical expertise, and Raytheon provided a total of over 4,000 million lire in recapitalization and guaranteed credit. By December 1967, according to the United States, major steps had been taken to upgrade plant facilities and operations.

15. At the same time, however, the Chairman of ELSI, and other senior Raytheon officials, held numerous meetings, between February 1967 and March 1968, with cabinet-level officials of the Italian Government and of the Sicilian region, as well as representatives of the Istituto per la Ricostruzione Industriale ("IRI"), the Ente Siciliano per la Produzione Industriale ("ESPI"), and the private sector. IRI was a holding company controlled by Italy with extensive commercial interests, and dominated at this time the telecommunications, electronics and engineering markets. ESPI was the Sicilian Government industrial organization responsible for the promotion of local development. The purpose of these meetings was stated to be to find for ELSI an Italian partner with economic power and influence and to explore the possibilities of other governmental support. The management of Raytheon had formed the view that, "without a partnership with IRI or other equivalent Italian Governmental entity, ELSI would continue to be an outsider to the Italian industrial community"; such a partnership would, it was thought, "positively influence government decision-making in economic planning", and enable ELSI also to secure benefits and incentives under Italian legislation designed to favour industrial development in the southern region, the Mezzogiorno. Evidence has been given that the management of ELSI was advised that the company was entitled to such Mezzogiorno benefits, but the Chamber has been told by Italy that it was not so entitled. The support of the national and regional governments was regarded as particularly important because in numerous markets crucial to ELSI's operations and success

the Italian Government, through IRI or otherwise, played a dominant role as a customer. A detailed "Project for the Financing and Reorganization of the Company" was prepared and submitted to ESPI in May 1967.

16. The management of ELSI took the view that one of the reasons for its lack of success was that it had trained and was employing an excessively large labour force. In June 1967 it was decided to dismiss some 300 employees; under an Italian union agreement this involved a procedure of notifications and negotiations. On the intervention of ESPI, an alternative plan was agreed to whereby 168 workers would be suspended from 10 July 1967, with limited pay by ELSI for a period not exceeding six weeks. After a training programme during which the workers were paid by the Sicilian Government, it was contemplated that ELSI would endeavour to re-employ the suspended employees. The necessary additional business to make this possible was not forthcoming, and the suspended employees were dismissed early in March 1968. A number of random strikes had occurred in early 1968, and as a result of the dismissals a complete strike of the plant occurred on 4 March 1968. According to the Government of Italy, this strike also involved an occupation of the plant by the workforce, which occupation was still continuing when the plant was requisitioned on 1 April 1968 (paragraph 30 below). The United States claims however that strikes and "sit-ins" prior to the requisition were only sporadic and that only after the filing of a petition in bankruptcy on 26 April 1968 (paragraph 36 below) did the workers actually occupy the plant for a sustained period.

17. When it became apparent that the discussions with Italian officials and companies were unlikely to lead to a mutually satisfactory arrangement to resolve ELSI's difficulties, Raytheon and Machlett, as shareholders in ELSI, began seriously to plan to close and liquidate ELSI to minimize their losses. General planning for the potential liquidation of ELSI began in the latter part of 1967, and in early 1968 detailed plans were made for a shut-down and liquidation at any time after 16 March 1968. On 2 March 1968, the company's books and accounting records, and, according to a witness at the hearings, "quite a lot of inventory", were transferred from its offices in Palermo to a regional office in Milan. On 7 March 1968, Raytheon formally notified ELSI that, notwithstanding ELSI's need for further capital, Raytheon would not "subscribe to any further stock which might be issued by Raytheon-Elsi or to guarantee any additional loans which might be made by others to Raytheon-Elsi".

18. This decision was stated to have been taken, *inter alia*, on review of the proposed balance sheet showing the position on 30 September 1967; that balance sheet showed the book value of the assets of ELSI as 17,956.3 million lire, its total debt as 13,123.9 million lire; the accumulated losses of 2,681.3 million lire had reduced the value of the equity (capital stock and capital subscription account) from 4,000 million lire to 1,318.7 million lire. The total debt included a number of liabilities to one United States bank and several Italian banks, some (but not all) of which were guaranteed by Raytheon. For the purposes of a possible liquidation, an asset analysis was prepared by the Chief Financial Officer of Raytheon showing the expected position on 31 March 1968. This showed the book value of ELSI's assets as 18,640 million lire; as explained in his affidavit filed in these proceedings, it also showed "the minimum prospects of recovery of values which we could be sure of, in order to ensure an orderly liquidation process", and the total realizable value of the assets on this basis (the "quick-sale value") was calculated to be 10,838.8 million lire. A balance sheet subsequently prepared to show the position at 31 March 1968, extrapolated from the balance sheet at 30 September 1967, showed the book value of total assets as 17,053.5 million lire and total debt of 12,970.6 million lire.

19. During the hearings, at the request of the Agent of Italy, the Chamber asked the Government of the United States to produce the financial report showing ELSI's financial position at 30 September 1967, from which the figures for the book value of its assets had been derived. The report, prepared by Raytheon's Italian auditors, and dated 22 March 1968, was produced in evidence. The balance sheet attached thereto showed two sets of figures; the first of these, corresponding to the figures for assets and liabilities set out in paragraph 18 above, gave the figures as recorded in the company's books of account. The second set of figures was based on the first set, but a number of adjustments had been made in accordance with the financial accounting policy of Raytheon "In order to assure comparability of the financial information reported from abroad" by its subsidiary companies. According to the Co-Agent of the United States, the major difference between the accounts on the Italian basis and the Raytheon basis was

> "the item of Deferred Charges, which for the most part represented the cost of developing new lines and improving product quality. This asset is carried on the Italian books but is routinely written off by Raytheon Company."

The adjustment of the item for "Deferred Charges" reduced the total assets figure by 1,653 million lire. Taking all adjustments into account,

the second set of figures gave a value of 14,893.9 million lire for the assets, and 15,775.2 million lire for the liabilities. The auditors stated in their covering letter to Raytheon accountants that

> "The adjustments made by the company in preparing the above mentioned balance sheet and statement of income and accumulated losses have not, at the date of this report, been recorded in the books, essentially for tax reasons. Accordingly, the accompanying financial statements are not in agreement with the company's books of account."

Among the "Notes on Financial Statements" attached to the accounts by the auditors was the following:

> "10. The adjusted accumulated losses at September 30, 1967 exceeded the total of the paid up capital stock, capital reserve and Stockholders subscription account by an amount of 881.3 million lire. Should this become 'officially' the case (e.g. should the adjustments made in arriving at this total of accumulated losses be entered in the company's books of account), under Articles 2447 and 2448 of the Italian Civil Code the directors would be obliged to convene a Stockholders' Meeting forthwith to take measures either to cover the losses by providing new capital or to put the company into liquidation."

The auditors also expressed reservations on two other items totalling 1,168.5 million lire.

20. The officials of Raytheon and ELSI were nevertheless advised by their Italian counsel in March 1968 that "ELSI's capital, after taking into account losses to date at that time, was well in excess of the minimum statutory requirement" (1 million lire) under Articles 2447 and 2448 of the Italian Civil Code, which provide that if action is not taken to restore the capital to the required minimum, the company is dissolved as a matter of law. In the view of ELSI's counsel, "it was therefore possible under Italian law for ELSI's shareholders to plan an orderly liquidation of the company".

21. Throughout this Judgment this phrase "orderly liquidation" is used solely in the sense in which it was employed by the officers of ELSI and by the representatives of the United States, i.e., to denote the operation planned in 1967-1968 by ELSI's management for the sale of the business or of its assets, en bloc or separately, and the discharge of ELSI's debts, fully or otherwise, out of the proceeds, the whole operation being under the control of ELSI's own management.

22. According to the United States, the chief objectives in the planned orderly liquidation were to conserve the assets and preserve as many of the

characteristics of a going concern as possible in order to attract and interest prospective buyers; it was planned to advertise ELSI's assets widely, offering them both as a total package and as separate items — the distinct manufacturing lines of the plant. The intention was, if the sums realized by the sale of the assets were sufficient, to pay all creditors in full. Planning had however also proceeded on the basis of the "quick-sale" valuation of the assets (paragraph 18 above), which, it was recognized, was less than the total liabilities of the company. It was not considered possible to continue normal production; the personnel was to be dismissed, with the exception of some 120 key employees needed for the wind-up operation and for continuing limited production for a time to meet (in particular) military contracts and maintain customer contact.

23. The intended treatment of creditors in the planned liquidation, in the event of only the "quick-sale" value being realized, was stated by the Financial Controller of Raytheon to have been as follows:

> "Ideally, we would settle first with the small creditors, subject, of course, to the agreement of the major creditors, in order to minimize the administrative effort during liquidation. Secured and preferred creditors would take priority and would be paid when the assets used for collateral were sold. Major unsecured creditors were to be paid on a pro rata basis from within the funds realized from the sale of assets. Then Raytheon would be called upon to satisfy any guaranteed creditor to the extent not already paid from asset sale proceeds. We calculated that the secured and preferred creditors would receive 100 per cent of their outstanding claims, while the unsecured major creditors who were not covered by Raytheon guarantees would realize about 50 per cent of their claims. The latter creditors were certain banks and Raytheon and its subsidiaries. We were confident that an orderly liquidation of this type would be acceptable to the creditors as it was much more favorable than could be expected through bankruptcy."

According to the United States, settlement with all the smaller creditors was regarded as a priority

> "to reduce the creditors to a manageable number and also to eliminate the risk that a small irresponsible creditor would take precipitous action which would raise formidable obstacles in the way of orderly liquidation".

Appended to one of the affidavits by officers of Raytheon and ELSI annexed to the United States Memorial were detailed calculations showing *(inter alia)* various valuations of ELSI's assets, analysis of the company's

liabilities and their priority in liquidation, and estimated distribution of the proceeds of disposal of assets calculated both on book value and alternatively on a "minimum liquidation value".

24. It is contended by the United States that notwithstanding Raytheon's formal notification on 7 March 1968 that it would not subscribe to any further stock or guarantee any additional loans (paragraph 17 above, *in fine*), Raytheon was ready to give certain financial support and guarantees to enable the orderly liquidation to proceed, as distinct from making more funds available to ELSI for continued operations. According to officials of ELSI, if Raytheon had handled the liquidation as planned, it would have guaranteed the settlements outlined in the previous paragraph; they stated that

> "Demonstrating its support of the liquidation plan, Raytheon organized to provide funds to ELSI in advance of the sale of its assets so that disbursements could easily be made to the small creditors and, as a first step, transferred 150 million lire to the First National City Bank branch in Milan specifically for that purpose."

Evidence was given at the hearing that payment of small creditors out of these funds was begun, but then stopped by the creditor banks because this was "showing preference". It was contemplated that Raytheon would take over ELSI's accounts receivable (subsequently valued at some 2,879 million lire) at face value, thus supplying immediate cash resources.

25. In the view of ELSI's legal counsel at the time (paragraph 20 above) and of Italian lawyers consulted by the United States, ELSI was in March 1968 entitled to engage in orderly liquidation of its assets, was under no obligation to file a petition in bankruptcy, and was never in jeopardy of compulsory dissolution under Article 2447 of the Italian Civil Code, and was at all times in compliance with Article 2446 of the Code. It has however been contended by Italy that ELSI was in March 1968 unable to pay its debts, and its capital of 4,000 million lire was completely lost; accordingly, an orderly liquidation was not available to it, but as an insolvent debtor it was under an obligation to file a petition in bankruptcy. The disagreement turns on the value of ELSI's assets for this purpose at 31 March 1968: the Parties have made conflicting statements of what is correct accounting practice for the purposes of compliance with the relevant requirements of Italian law. It has also been observed by Italy that, whether or not ELSI was insolvent, the procedure contemplated did not correspond to a voluntary liquidation as provided for in Article 2450 of the Italian Civil Code; under that procedure a liquidator has to be appointed by the shareholders, or if they fail to do so, by the Tribunal. According to one expert appearing on behalf of Italy, ELSI being insolvent the only

course open to it in order to avoid the duty of filing a petition in bankruptcy was to request to the tribunal to be admitted to the procedure of judicial settlement *("concordato preventivo")* under Articles 160 *et seq.* of the Italian Bankruptcy Act; this would have required proof that at least 40 per cent of the unsecured claims would be met. The expert appearing on behalf of the United States however stated that apparent inability to pay all creditors at 100 per cent is not fatal to voluntary and orderly liquidation. In this context he mentioned in particular the practice of "private settlement" *("concordato stragiudiziale").*

26. The management of ELSI was conscious that a financial crisis was imminent, and during the period from September 1967, the responsible officers of the company were keeping a close watch on the declining funds to ensure that the company did not reach a point where continued operation would be contrary to Italian law. At a meeting held on 21 February 1968 between representatives of Raytheon and ELSI and the President of the Sicilian region, the Chairman of ELSI "drew a precise time chart showing: *(a)* February 23 — Board Meeting; *(b)* February 26 to 29 — inevitable bank crisis; *(c)* March 8 — we run out of money and shut the plant"; the hand-written minutes of that meeting record also that "the date of March 8 was stressed repeatedly as the absolute limit for the shut-down due to a total financial crisis".

27. On 16 March 1968, the Board of Directors of ELSI met to consider a report on the financial situation, and concluded "that there is no alternative to the discontinuation of the company's activities"; the Board

> "decided the cessation of the company's operations, to be carried out as follows:
> (1) production will be discontinued immediately;
> (2) commercial activities and employment contracts will be terminated on March 29, 1968".

This decision was notified to the employees of ELSI by a letter of 16 March 1968. On 28 March 1968, a meeting of shareholders of ELSI was held, at which it was decided *(inter alia)* "to ratify the resolutions adopted by the Board of Directors at the meeting of March 16, 1968, and hence to agree that the Company cease operations". Meetings with Italian officials however continued up to 29 March 1968; the Italian authorities continued to give broad assurances of an intervention by ESPI, and vigorously pressed ELSI not to close the plant and not to dismiss the workforce, but the officials of the company insisted that this was inevitable unless more capital was forthcoming. On 29 March 1968 letters of dismissal were mailed to the employees of ELSI.

28. The Managing Director of ELSI had a meeting early on the morning of 31 March 1968 with the President of the Sicilian region, Mr. Carollo, at which the latter stated that the Italian Prime Minister had said that a company would be formed by ESPI and IMI (Istituto Mobiliare Italiano) to deal with the acquisition of ELSI's assets, and that a holding company would be formed which would eventually own ELSI. Mr. Carollo continued by saying that "to keep the people in Palermo and avoid an exodus to other jobs, and to protect the plant and machinery, the plant would be requisitioned . . .". On 1 April 1968 representatives of the company met representatives of the bank creditors of ELSI to discuss the company's plans for an orderly liquidation. According to the United States, ELSI's representatives stated that Raytheon was not prepared to provide any further financial support to ELSI either by way of capital, loans, advances, or guarantees, but also informed the banks of the arrangement (referred to in paragraph 24 above) which would provide for ELSI's immediate cash needs in such an orderly liquidation through the sale to Raytheon of ELSI's accounts receivable at 100 per cent of face value, the proceeds being used to pay off the small creditors and to meet payroll and severance pay claims as well as other pressing priority obligations.

29. No agreement was reached at that meeting; certain of the banks requested more information, and another meeting was to be held later with an agreed agenda. Subsequently ELSI's representatives learnt that the plant had been requisitioned. According to the United States, and in the view of the officers of Raytheon and ELSI, there was reason to believe that in a liquidation the creditor banks would have accepted a settlement of their claims on payment of 40 to 50 per cent of each, but no independent evidence is available that such was the banks' attitude at that time. It does not appear from the evidence that the banks were asked specifically at the meeting of 1 April 1968 whether they would co-operate on the basis of a guaranteed 50 per cent of their claims; on the contrary, it was contended on behalf of the United States by ELSI's then legal adviser that

> "There is no evidence of bank negotiations at the time of the requisition because at the time the stockholders were fully confident that ELSI's assets would have recovered book value, and there was no need at the time to start any such negotiations. What the stockholders and ELSI's Board were seeking at the time was an understanding with the banks on the manner and timing of an orderly liquidation."

According to the same legal adviser, the banks were ready, during negotiations in September-October 1968, after ELSI had been declared bankrupt, to accept settlement on the basis of 40 per cent or 50 per cent payment (see paragraph 37 below).

30. On 1 April 1968 the Mayor of Palermo issued an order, effective immediately, requisitioning ELSI's plant and related assets for a period of six months. The text of this order, in the translation supplied by the United States, was as follows:

"The Mayor of the Municipality of Palermo,

Taking into consideration that Raytheon-Elsi of Palermo has decided to close its plant located in this city at Via Villagrazia, 79, because of market difficulties and lack of orders;

That the company has furthermore decided to send dismissal letters to the personnel consisting of about 1,000 persons;

Taking notice that ELSI's actions, beside provoking the reaction of the workers and of the unions giving rise to strikes (both general and sectional) has caused a wide and general movement of solidarity of all public opinion which has strongly stigmatized the action taken considering that about 1,000 families are suddenly destituted;

That, considering the fact that ELSI is the second firm in order of importance in the District, because of the shutdown of the plant a serious damage will be caused to the District, which has been so severely tried by the earthquakes had during the month of January 1968;

Considering also that the local press is taking a great interest in the situation and that the press is being very critical toward the authorities and is accusing them of indifference to this serious civic problem;

That, furthermore, the present situation is particularly touchy and unforeseeable disturbances of public order could take place;

Taking into consideration that in this particular instance there is sufficient ground for holding that there is a grave public necessity and urgency to protect the general economic public interest (already seriously compromised) and public order, and that these reasons justify requisitioning the plant and all equipment owned by Raytheon-Elsi located here at Via Villagrazia 79;

Having noted Article 7 of the law of 20 March 1865 No. 2248 enclosure *e*;

Having noted Article 69 of the Basic Regional Law EE.LL.,

the requisition, with immediate effect and for the duration of six months, except as may be necessary to extend such period, and without prejudice for the rights of the parties and of third parties, of the plant and relative equipment owned by Raytheon-Elsi of Palermo.

With a subsequent decree, the indemnification to be paid to said company for the requisition will be established."

The order was served on the company on 2 April 1968.

31. On 6 April 1968 the Mayor issued an order entrusting the management of the requisitioned plant to Mr. Aldo Profumo, the Managing Director of ELSI, for the purpose, *inter alia*, of "avoiding any damage to the equipment and machinery due to the abandoning of all activity, including maintenance". Mr. Profumo declined to accept this appointment, and on 16 April 1968 the Mayor wrote to Mr. Silvio Laurin, the senior director, appointing him temporarily to replace Mr. Profumo "in the same capacity, with the same powers, functions and limitations", and Mr. Laurin accepted this appointment. The company management requested another of its directors, Mr. Rico Merluzzo, to stay at the plant night and day "to preclude local authorities from somehow asserting that the plant had been 'abandoned' by ELSI".

32. On 9 April 1968 ELSI addressed a telegram to the Mayor of Palermo, with copies to other Government authorities, claiming *(inter alia)* that the requisition was illegal and expressing the company's intention to take all legal steps to have it revoked and to claim damages. On 12 April 1968 the company served on the Mayor a formal document dated 11 April 1968 inviting him to revoke the requisition order. The Mayor did not respond and the order was not revoked, and on 19 April 1968 ELSI brought an administrative appeal against it to the Prefect of Palermo, who was empowered to hear appeals against decisions by local governmental officials. The decision on that appeal was not given until 22 August 1969 (paragraph 41 below); in the meantime however the requisition was not formally prolonged, and therefore ceased to have legal effect after six months, more than four months after the bankruptcy of ELSI had been declared (paragraph 36 below).

33. As noted above (paragraph 16) the Parties disagree over whether, immediately prior to the requisition order, there had been any occupation of ELSI's plant by the employees, but it is common ground that the plant was so occupied during the period immediately following the requisition. On 19 April 1968 the representatives of the company stated, in an appeal against the requisition addressed to the Prefect of Palermo, that there had at that time been no occupation of the plant as a consequence of the dismissal of the employees on 29 March 1968, but that on 30 March 1968 a group of representatives of the personnel went to the plant to talk to the

company executives and "peacefully remained thereafter all day on the premises", and on subsequent days a small group of employees wandered about on the premises. The Mayor of Palermo, in an affidavit, has stated that

> "The occupation of the plant by the employees (which started well before the requisition) turned out to be of a 'cooperative' nature after the requisition and was no obstacle to the continuation of those activities which were possible under the circumstances",

and an official of the Municipality of Palermo has stated, in an affidavit, that "there were no problems such as 'hard' picketing" and that one of the production lines was re-activated and "we proceeded regularly with the contracts in hand". According to an affidavit filed by the United States "the plant sat idle for the remainder of 1968", but Italy has produced evidence showing that some work in progress was continued and completed in the months following the requisition, in particular for the Nato Hawk programme.

34. On 19 and 20 April 1968 meetings were held between officials of Raytheon and the President of the Sicilian region, Mr. Carollo, who stated that "the Regional and Central Governments had reached agreement to form a management company with IRI participation to operate ELSI" and invited Raytheon to join the management company. The proposal would have entailed the contribution by ELSI of new capital and its assuming complete responsibility for past debts; in the discussion Mr. Carollo stated that "the Region now has a single goal, to keep the workers employed". At the request of Raytheon, Mr. Carollo, on 20 April 1968 supplied Raytheon with a memorandum to provide the company with "some fundamental elements of judgment". In that memorandum he explained that it was impossible for the time being for Raytheon to liquidate ELSI, for the following reasons:

> "1. Nobody in Italy will purchase *[Nessuno in Italia comprerà]*, that is to say IRI will not purchase, neither for a low nor for a high price, the Region will not purchase, private enterprise will not purchase. Let me add that the Region and IRI and anybody else who has any possibility to influence the market will refuse in the most absolute manner to favor any sale while the plant is closed.
>
> 2. The Banks, which have outstanding credits for approximately 16 billion Lire, cannot and will not accept any settlement even at the cost of dragging the Company into litigation on an international level. I mean to refer to Raytheon and not to ELSI because the distinction between ELSI and Raytheon is not found to be admissible, since any and all financing was granted to ELSI based on the moral

guarantee of Raytheon, whose executives have always negotiated said financing.

3. Anyway, it is known in Italy that one can enforce the claims directly against Raytheon because it has interests and revenues in our country also outside ELSI.

It is obvious that every attempt will be made (even at the cost of long litigation) to obtain from Raytheon what is owed by ELSI.

4. In the event that the plant will be kept closed, waiting for Italian buyers who will never materialize, the requisition will be maintained at least until the courts will have resolved the case. Months will go by . . ."

35. On 26 April 1968 the Chairman of the Board of ELSI wrote to Mr. Carollo formally rejecting the proposal for participation in the new management company; in his view the proposal "was a temporary caretaker measure which would not solve the fundamental problem, namely keeping ELSI in Sicily and making it a viable and vital industry", and that it "would only aggravate ELSI's critical financial condition". The letter continued: "We are therefore forced to file [a] voluntary petition for bankruptcy, as required by Italian law."

36. In view of what had been said by Mr. Carollo that the requisition of the plant would be maintained for months, "at least until the courts will have resolved the case", ELSI's Italian counsel advised as follows:

"The disposability of ELSI's assets was a fundamental prerequisite to ELSI's shareholders' ability to take ELSI through an orderly liquidation; they were relying on the proceeds of these sales in large part to pay ELSI's creditors in an orderly manner. Without the ability to dispose of its assets, ELSI would not have the liquidity needed to pay its debts as they came due and therefore would soon become technically insolvent under Italian law.

. . . . . .

I advised ELSI's directors that they had an obligation to file a petition for a declaration of bankruptcy, failing which they could be held personally liable pursuant to Article 217 of the Bankruptcy Law, Royal Decree of March 16, 1942, No. 267."

On 25 April 1968 the Board of Directors voted to file a voluntary petition in bankruptcy, and the bankruptcy petition was filed on 26 April 1968. The petition referred to the requisition order of 1 April 1968 and stated *(inter alia)*:

"Because of the order of requisition, against which the Company

has in due time filed an appeal, the Company has lost the control of the plant and cannot avail itself of an immediate source of liquid funds; in the meanwhile payments have become due (as for instance instalments of long-term loans; an instalment of Lit. 800,000,000 to Banca Nazionale del Lavoro became due on April 18, 1968 and the note therefor has been or will be protested, etc.); it is acknowledged that it is impossible for the Company to pay such sums with the funds existing or available such impossibility being due to the events of these last weeks . . ."

A decree of bankruptcy was issued by the *Tribunale di Palermo* on 16 May 1968, and a Palermo lawyer was appointed *curatore* (trustee in bankruptcy). A creditors' committee of five members was appointed, composed of two representatives of ELSI's employees, two representatives of bank creditors, and a representative of Raytheon Europe International Company ("Raytheon Europe") (the European management subsidiary of, and wholly owned by, Raytheon), which had submitted a claim as creditor in the bankruptcy. Raytheon itself and another of its subsidiaries, Raytheon Service Company, had unsecured claims against ELSI of some 1,140 million lire for goods and services they had advanced to ELSI on unsecured open accounts. On advice of Italian counsel, however, Raytheon and Raytheon Service Company did not file claims in the bankruptcy proceedings because it was clear that they would not receive enough in the bankruptcy to justify their filing costs.

37. From April 1968 onwards discussions were held between Raytheon's Italian counsel, representatives of the creditor banks and officials of the Italian Government, with a view to the takeover of ELSI by a company owned by the Italian Government and a settlement with the ELSI creditors. This proposed settlement involved the grant to the new company by Raytheon of a technical license (to use Raytheon patents and know-how) of the same scope as ELSI had; the payment by Raytheon of the debts of ELSI which it had guaranteed, but no others, and a formal release and indemnity of Raytheon in this latter respect; and a waiver by Raytheon of its rights of subrogation resulting from payment of the guaranteed debts. According to Raytheon's Italian counsel, he was told by Italian Government officials in October 1968 that the majority of the Italian creditor banks were agreeable to a settlement on payment of 40 per cent of their claims, and that only one bank was holding out for 50 per cent. In July, a statement had been made in the Italian Parliament by the Minister of Industry, Commerce and Crafts, which has been subject to differing interpretations, but which put forward as a fact the establishment by the Sicilian region and other public agencies of a management company, which would allow productive activities to be resumed until such time as the financial problems of ELSI could be

finally resolved, if possible through settlement out of court. On 13 November 1968 the Italian Government issued a press communiqué which stated that

> "while the STET Group [Società finanziaria telefonica, an affiliate or subsidiary of IRI] remains committed to build a new plant in Palermo for the production of telecommunication products, the IRI-STET Group, urged by the Government, after the examination of alternative solutions which proved unfeasible, stated its willingness to intervene in the take-over of the [ELSI] plant in the organization of new lines of production".

According to the communiqué, the conditions of STET's intervention were to be agreed between the STET Group and the authorities of the Sicilian region.

38. The court dealing with the bankruptcy ordered an auction of ELSI's premises, plant and equipment to be held on 18 January 1969, and set a minimum bid of 5,000 million lire. This auction, and the subsequent auctions mentioned below, were advertised in leading newspapers both in Italy and in Belgium, Japan, the Netherlands, the United Kingdom and the United States. No bids were received at this auction, and a second auction was set for 22 March 1969, this time with the inclusion also of the entire inventory at the plant and elsewhere, the minimum bid being set at 6,223,293,258 lire. In the meantime negotiations were being carried on for a takeover of the plant by an IRI subsidiary and the re-employment of most of ELSI's former staff. It was reported in the Sicilian press, first that on 18 March 1969 it had been agreed that IRI would acquire ELSI's assets, beginning with a lease of the plant for 150 million lire, and secondly that the former President of Sicily, Mr. Carollo, had stated at a public meeting on 5 April 1969 that there had been a written agreement with IRI in October 1968 that

> "entailed the acquisition of the [ELSI] factory by IRI for the sum of four billion lire. It was even agreed that IRI would be absent from the first auction, participating instead in the second one, where the basic price was precisely four billion lire".

39. No bids were received at the second auction. A week later a proposal to lease and re-open the plant was made to the trustee in bankruptcy by ELTEL (Industria Elettronica Telecommunicazioni S.p.A.), a subsidiary of IRI set up in December 1968. The terms proposed for the lease were not acceptable as such to the creditors' committee, which did however recom-

mend *(inter alia)* that it should be granted if ELTEL agreed to purchase all ELSI's inventorial raw material for 1,800 million lire; the representative of Raytheon Europe on the committee vigorously opposed the lease. The trustee in bankruptcy however recommended that the lease be granted on the terms requested, and on 8 April 1969 the bankruptcy judge so directed. Raytheon Europe appealed against this decision but without success. A third auction was scheduled for May 1969; in April ELTEL proposed to buy the work in progress — the material left on ELSI's production lines when the plant was requisitioned — for 105 million lire; this had been valued in the course of the bankruptcy proceedings at 217 million lire. Raytheon Europe's representative on the creditors' committee opposed this sale, but was outvoted.

40. The third auction of ELSI's premises, plant and equipment and inventory was held on 3 May 1969, the minimum bid being set at 5,000 million lire, but again no bids were received. ELTEL had informed the bankruptcy court on 16 April 1969 that it was willing to offer 3,205 million lire for the premises, plant and equipment, excluding the supplies — "merchandise, raw materials and semifinished goods" — which it did not regard as indispensable. On 3 May 1969, the trustee in bankruptcy requested the bankruptcy court to approve a sale of the work in progress to ELTEL on the terms proposed by ELTEL and approved by the creditors' committee. On 9 May 1969, Raytheon Europe's appeal against the decision authorizing the lease of the premises and plant to ELTEL was rejected. On 27 May 1969 ELTEL made an offer to the bankruptcy court to buy the remaining plant, equipment and supplies for 4,000 million lire. The trustee in bankruptcy proposed acceptance (subject to minor changes in the terms), and the creditors' committee decided on 6 June 1969 to approve the proposal, the Raytheon Europe representative voting against. On 7 June 1969 the bankruptcy judge set 12 July 1969 as date for an auction on the terms approved by the creditors' committee. On 9 June 1969 Raytheon Europe appealed against this decision, but the appeal was rejected on 20 June 1969. The auction was held on 12 July 1969, and ELTEL purchased the auctioned property at the total price of 4,006 million lire.

41. The appeal filed by ELSI on 19 April 1968 (paragraph 32 above) against the requisition order of 1 April 1968 was determined by the Prefect of Palermo by a decision given on 22 August 1969. The Parties are at issue on the question whether this period of time was or was not normal for an appeal of this character. The decision on the appeal was given following a request to that effect by the trustee in bankruptcy made on 9 July 1969, in exercise of a right to request a decision conferred by an Italian Law of 3 March 1934. That Law provides that if the appeal has not been heard 120 days after it has been filed (i.e., in this case by 17 August 1968), a request

may be served on the Prefect requiring him to render a decision within 60 days thereafter; if he fails to do so, this is treated as a dismissal of the appeal. The decision of the Prefect was to uphold the appeal and thus to annul the requisition order made by the Mayor of Palermo; the precise terms of the decision will be considered later in this Judgment (paragraphs 75, 96, 125 and 126). The Mayor of Palermo appealed against the Prefect's decision to the President of Italy who, having been advised by the Council of State that the Mayor's appeal was inadmissible, so ruled on 22 April 1972.

42. In the meantime, on 16 June 1970 the trustee in bankruptcy had brought proceedings in the *Tribunale di Palermo* ("the Court of Palermo") against the Minister of the Interior of Italy and the Mayor of Palermo for damages resulting from the requisition. The damages claimed were identified as

> "the considerable decrease in value of the plant and the electronic equipment existing in Palermo at 79 Via Villagrazia, which results from the difference between the book value at the date of the bankruptcy of Raytheon-Elsi, of Lire 6,623,000,000 and the evaluation made on October 11, 1968 (that is, immediately after the six-month period of requisition had elapsed) by the Court Appraiser, Prof. Mario Puglisi, appointed by the Judge by Decree of September 19, 1968, of Lire 4,560,588,400, with a real loss of value of Lire 2,062,411,600 and as the lack of disposability of the plant and relative equipment for six months which, on the basis of the amortization rate for the industrial plants, equal to 10% per year, can be determined in Lire 33,150,000, and, therefore, in the aggregate amount of Lire 2,395,561,600, plus the interests at the legal rate from October 1, 1968 to the payment."

43. On 2 February 1973, the Court of Palermo, in a decision to be examined more fully below (paragraphs 57, 58, 97 and 127), ruled that the trustee was not entitled to compensation for the requisition, either in respect of the alleged decrease in value of the plant and equipment, or of the alleged lack of disposability thereof. On appeal, the *Corte di Appello di Palermo* ("the Court of Appeal of Palermo"), in its decision of 24 January 1974, upheld the conclusion of the lower court as regards the damages claimed for the alleged decrease in value of the plant and equipment. It however reversed the finding of the lower court on the second head of damage, and found that the trustee was entitled to compensation from the Minister of the Interior for loss of use and possession of ELSI's plant and assets during the six-month requisition period. It therefore awarded, in effect, a "rental" payment of some 114 million lire, computed as half the annual rate of 5 per cent of the total value of the assets. This decision, which will be examined in more detail below (paragraphs 97, 98 and 127), was upheld by the Court of Cassation on 26 April 1975. The amount of

the judgment was ultimately received by the trustee and, less costs and expenses, distributed to ELSI's creditors.

44. In the bankruptcy proceedings, creditors presented claims against ELSI totalling some 13,000 million lire; these did not include amounts due to Raytheon and Raytheon Service Company (see paragraph 36 above). The bankruptcy proceedings closed in November 1985. According to the bankruptcy reports, the bankruptcy realized only some 6,370 million lire for ELSI's assets, as compared with the minimum liquidation value estimated by ELSI's management in March 1968 at 10,840 million lire. Of the amount realized, some 6,080 million lire went to pay banks, employees, and other creditors. The remainder went to pay bankruptcy administration, tax, registry, and customs charges. All of the secured and preferred creditors who filed claims in the bankruptcy were paid in full. The unsecured creditors received less than one per cent of their claims; accordingly no surplus remained for distribution to the shareholders, Raytheon and Machlett.

45. Raytheon had guaranteed the indebtedness of ELSI to a number of banks, and on the bankruptcy of ELSI it was accordingly liable for, and paid, the sum of 5,787.6 million lire to the banks in accordance with the terms of the guarantees. Five of the seven banks which had also made unguaranteed loans to ELSI brought proceedings in the Italian courts seeking payment of these loans by Raytheon, on the basis primarily of Article 2362 of the Italian Civil Code, which renders a sole shareholder liable for the debts of the company. It was argued that Raytheon was in effect sole shareholder, since Machlett was its wholly-owned subsidiary. Three of these cases were ultimately resolved by the Italian Court of Cassation in favour of Raytheon, and two were discontinued by the plaintiffs.

* *

46. On 7 February 1974, the Embassy in Rome of the United States transmitted to the Italian Ministry of Foreign Affairs a note enclosing the "claim of the Government of the United States of America on behalf of Raytheon Company and Machlett Laboratories, Incorporated". That claim, which was based not only on the FCN Treaty but also on customary international law, incorporated a Memorandum of Law, Chapter VI of which was devoted to "Exhaustion of Local Remedies". It was there noted that it was "generally recognized that local remedies must be exhausted before a claim may be formally espoused under principles of international law"; an account was given of the relevant litigation in Italy (some of which was at the time still pending) and, in the light of annexed opinions

of two Italian legal experts, it was concluded that "Raytheon and Machlett have exhausted every meaningful legal remedy available to them in Italy". At the time this claim was submitted, the Court of Appeal of Palermo had ruled on the action by the trustee in bankruptcy, but the case was thereafter brought before the Court of Cassation (paragraph 43 above); it is recognized by both Parties that any other action arising out of the requisition would by then have been barred by limitation of time. It appears that the United States received no formal response from Italy to the claim until 13 June 1978, when Italy denied the claim in a written aide-mémoire, the text of which has been supplied to the Chamber. The aide-mémoire contained no suggestion that local remedies had not been exhausted, and indeed stated that "the claim is juridically groundless, both from the international and domestic point of view". During the oral proceedings in the present case, counsel for Italy asserted that at an unspecified date prior to the institution of the present proceedings the Italian Government "had made it clear to the United States Government that as a Respondent it would raise the objection of non-exhaustion of local remedies in judicial proceedings". No evidence to that effect has however been supplied to the Chamber.

* *

47. Many of the documents constituting evidence submitted to the Chamber are in the Italian language. Where the Chamber relies in the present Judgment on passages in these documents, it will, for the sake of clarity, set out the original Italian together with an English translation, which is not always the translation supplied by one of the Parties pursuant to Article 51, paragraph 3, of the Rules of Court.

* * *

48. It is common ground between the Parties that the Court has jurisdiction in the present case, under Article 36, paragraph 1, of its Statute, and Article XXVI of the Treaty of Friendship, Commerce and Navigation, of 2 June 1948 ("the FCN Treaty"), between Italy and the United States; which Article reads:

> "Any dispute between the High Contracting Parties as to the interpretation or the application of this Treaty, which the High Contracting Parties shall not satisfactorily adjust by diplomacy, shall be submitted to the International Court of Justice, unless the High Contracting Parties shall agree to settlement by some other pacific means."

The jurisdiction is thus confined to questions of "the interpretation or the application" of the FCN Treaty and Protocols and of the Agreement Supplementing the Treaty between the United States of America and the Italian Republic, of 26 September 1951 (which Agreement is hereinafter called "the Supplementary Agreement"), Article IX of which provides that it is to "constitute an integral part" of the FCN Treaty. This same jurisdiction may accordingly be exercised by this Chamber, created by the Court to deal with this case by virtue of Article 26, paragraph 2, of its Statute, and Articles 17 and 18 of its Rules, at the request of and after consultation with the Parties.

49. While the jurisdiction of the Chamber is not in doubt, an objection to the admissibility of the present case was entered by Italy in its Counter-Memorial, on the ground of an alleged failure of the two United States corporations, Raytheon and Machlett, on whose behalf the United States claim is brought, to exhaust the local remedies available to them in Italy. This objection, which the Parties agreed should be heard and determined in the framework of the merits, must, therefore, be considered at the outset.

50. The United States questioned whether the rule of the exhaustion of local remedies could apply at all to a case brought under Article XXVI of the FCN Treaty. That Article, it was pointed out, is categorical in its terms, and unqualified by any reference to the local remedies rule; and it seemed right, therefore, to conclude that the parties to the FCN Treaty, had they intended the jurisdiction conferred upon the Court to be qualified by the local remedies rule in cases of diplomatic protection, would have used express words to that effect; as was done in an Economic Co-operation Agreement between Italy and the United States of America also concluded in 1948. The Chamber has no doubt that the parties to a treaty can therein either agree that the local remedies rule shall not apply to claims based on alleged breaches of that treaty; or confirm that it shall apply. Yet the Chamber finds itself unable to accept that an important principle of customary international law should be held to have been tacitly dispensed with, in the absence of any words making clear an intention to do so. This part of the United States response to the Italian objection must therefore be rejected.

51. The United States further argued that the local remedies rule would not apply in any event to the part of the United States claim which requested a declaratory judgment finding that the FCN Treaty had been violated. The argument of the United States is that such a judgment would declare that the United States own rights under the FCN Treaty had been infringed; and that to such a direct injury the local remedies rule, which is a rule of customary international law developed in the context of the espousal by a State of the claim of one of its nationals, would not apply. The Chamber, however, has not found it possible in the present case to

find a dispute over alleged violation of the FCN Treaty resulting in direct injury to the United States, that is both distinct from, and independent of, the dispute over the alleged violation in respect of Raytheon and Machlett. The case arises from a dispute which the Parties did not "satisfactorily adjust by diplomacy"; and that dispute was described in the 1974 United States claim made at the diplomatic level as a "claim of the Government of the United States of America on behalf of Raytheon Company and Machlett Laboratories, Incorporated". The Agent of the United States told the Chamber in the oral proceedings that "the United States seeks reparation for injuries suffered by Raytheon and Machlett". And indeed, as will appear later, the question whether there has been a breach of the FCN Treaty is itself much involved with the financial position of the Italian company, ELSI, which was controlled by Raytheon and Machlett.

52. Moreover, when the Court was, in the *Interhandel* case, faced with a not dissimilar argument by Switzerland that in that case its "principal submission" was in respect of a "direct breach of international law" and therefore not subject to the local remedies rule, the Court, having analysed that "principal submission", found that it was bound up with the diplomatic protection claim, and that the Applicant's arguments "do not deprive the dispute ... of the character of a dispute in which the Swiss Government appears as having adopted the cause of its national ..." (*Interhandel, Judgment, I.C.J. Reports 1959,* p. 28). In the present case, likewise, the Chamber has no doubt that the matter which colours and pervades the United States claim as a whole, is the alleged damage to Raytheon and Machlett, said to have resulted from the actions of the Respondent. Accordingly, the Chamber rejects the argument that in the present case there is a part of the Applicant's claim which can be severed so as to render the local remedies rule inapplicable to that part.

53. There was a further argument of the Applicant, based on estoppel in relation to the application of the local remedies rule, which should be examined. In the "Memorandum of Law" elaborating the United States claim on the diplomatic plane, transmitted to the Italian Government by Note Verbale of 7 February 1974, one finds that the whole of Part VI (pp. 53 *et seq.*) deals generally and at some length with the "Exhaustion of Local Remedies". There were also annexed the opinions of the lawyers advising the Applicant, which dealt directly with the position of Raytheon and Machlett in relation to the local remedies rule. The Memorandum concluded that Raytheon and Machlett had indeed exhausted "every meaningful legal remedy available to them in Italy" (paragraph 46 above). In view of this evidence that the United States was very much aware that it must satisfy the local remedies rule, that it evidently believed that the rule had been satisfied, and that it had been advised that the shareholders of

ELSI had no direct action against the Italian Government under Italian law, it was argued by the Applicant that Italy, if it was indeed at that time of the opinion that the local remedies had not been exhausted, should have apprised the United States of its opinion. According to the United States, however, at no time until the filing of the Respondent's Counter-Memorial in the present proceedings did Italy suggest that Raytheon and Machlett should sue in the Italian courts on the basis of the Treaty. The written aide-mémoire of 13 June 1978, by which Italy rejected the 1974 claim, had contained no suggestion that the local remedies had not been exhausted, nor indeed any mention of the matter.

54. It was argued by the Applicant that this absence of riposte from Italy amounts to an estoppel. There are however difficulties about drawing any such conclusion from the exchanges of correspondence when the matter was still being pursued on the diplomatic level. In the *Interhandel* case, when Switzerland argued that the United States had at one time actually "admitted that Interhandel had exhausted the remedies available in the United States courts", the Court, far from seeing in this admission an estoppel, dismissed the argument by merely observing that "This opinion was based upon a view which has proved unfounded" (*Interhandel, Judgment, I.C.J. Reports 1959,* p. 27). Furthermore, although it cannot be excluded that an estoppel could in certain circumstances arise from a silence when something ought to have been said, there are obvious difficulties in constructing an estoppel from a mere failure to mention a matter at a particular point in somewhat desultory diplomatic exchanges.

55. On the basis that the local remedies rule does apply in this case, this Judgment may now turn to the question whether local remedies were, or were not, exhausted by Raytheon and Machlett.

* *

56. The damage claimed in this case to have been caused to Raytheon and Machlett is said to have resulted from the "losses incurred by ELSI's owners as a result of the involuntary change in the manner of disposing of ELSI's assets": and it is the requisition order that is said to have caused this change, and which is therefore at the core of the United States complaint. It was, therefore, right that any local remedy against the Italian authorities, calling in question the validity of the requisition of ELSI's plant and related assets, and raising the matter of the losses said to result from it, should be pursued by ELSI itself. In any event, both in order to attempt to recover control of ELSI's plant and assets, and to mitigate any damage flowing from the alleged frustration of the liquidation plan, the first step was for ELSI — and only ELSI could do this — to appeal to

the Prefect against the requisition order. After the bankruptcy, however, the pursuit of local remedies was no longer a matter for ELSI's management but for the trustee in bankruptcy (Raytheon could, even after the bankruptcy, have influenced decisions of the committee of creditors, had it not decided against claiming in bankruptcy in respect of sums due to it as creditor; it did exercise some influence however through its subsidiary company, Raytheon Europe, which did claim as a creditor).

57. After the trustee in bankruptcy was appointed, he, acting for ELSI, by no means left the Italian authorities and courts unoccupied with ELSI's affairs. It was he who, under an Italian law of 1934, formally requested the Prefect to make his decision within 60 days of that request; which decision was itself the subject of an unsuccessful appeal by the Mayor to the President of Italy. On 16 June 1970, the trustee, acting for the bankrupt ELSI, brought a suit against the Acting Minister of the Interior and the Acting Mayor of Palermo, asking the court to adjudge that the defendants should

> "pay to the bankrupt estate of Raytheon-Elsi ... damages for the illegal requisition of the plant machinery and equipment ... for the period from April 1 to September 30, 1968, in the aggregate amount of Lire 2,395,561,600 plus interests ..."

On 2 February 1973, the Court of Palermo, as indicated above (paragraph 43), rejected the claim. The trustee in bankruptcy then appealed to the Court of Appeal of Palermo; which Court gave a judgment on 24 January 1974 which "partly revising the judgment of the Court of Palermo" ordered payment by the Ministry of the Interior of damages of 114,014,711 lire with interest. Appeal was taken finally to the Court of Cassation which upheld the decision of the Court of Appeal, by a decision of 26 April 1975.

58. It is pertinent to note that this claim for damages (paragraph 42 above), as it came before the Court of Palermo in the action brought by the trustee, was described by that Court as being based *(inter alia)* upon the argument of the trustee in bankruptcy

> "that the requisition order caused an economic situation of such gravity that it immediately and directly triggered the bankruptcy of the company"
>
> *("il provvedimento di requisizione avrebbe determinato una situazione economica di tale pesantezza da farne scaturire immediatamente e direttamente il fallimento della società").*

Similarly the Court of Appeal of Palermo had to consider whether there was a "causal link between the requisition order and the company's bankruptcy". It is thus apparent that the substance of the claim brought to the

adjudication of the Italian courts is essentially the claim which the United States now brings before this Chamber. The arguments were different, because the municipal court was applying Italian law, whereas this Chamber applies international law; and, of course, the parties were different. Yet it would seem that the municipal courts had been fully seized of the matter which is the substance of the Applicant's claim before the Chamber. For both claims turn on the allegation that the requisition, by frustrating the orderly liquidation, triggered the bankruptcy, and so caused the alleged losses.

59. With such a deal of litigation in the municipal courts about what is in substance the claim now before the Chamber, it was for Italy to demonstrate that there was nevertheless some local remedy that had not been tried; or at least, not exhausted. This burden Italy never sought to deny. It contended that it was possible for the matter to have been brought before the municipal courts, citing the provisions of the treaties themselves, and alleging their violation. This was never done. In the actions brought before the Court of Palermo, and subsequently the Court of Appeal of Palermo, and the Court of Cassation, the FCN Treaty and its Supplementary Agreement were never mentioned. This is not surprising, for, as Italy recognizes, the way in which the matter was pleaded before the courts of Palermo was not for Raytheon and Machlett to decide but for the trustee. Furthermore, the local remedies rule does not, indeed cannot, require that a claim be presented to the municipal courts in a form, and with arguments, suited to an international tribunal, applying different law to different parties: for an international claim to be admissible, it is sufficient if the essence of the claim has been brought before the competent tribunals and pursued as far as permitted by local law and procedures, and without success.

60. The question, therefore, reduces itself to this: ought Raytheon and Machlett, suing in their own right, as United States corporations allegedly injured by the requisition of property of an Italian company whose shares they held, have brought an action in the Italian courts, within the general limitation-period (five years), alleging violation of certain provisions of the FCN Treaty between Italy and the United States; this mindful of the fact that the very question of the consequences of the requisition was already in issue in the action brought by its trustee in bankruptcy, and that any damages that might there be awarded would pass into the pool of realized assets, for an appropriate part of which Raytheon and Machlett had the right to claim as creditors?

61. Italy contends that Raytheon and Machlett could have based such an action before the Italian courts on Article 2043 of the Italian Civil Code, which provides that "Any act committed either wilfully or through fault which causes wrongful damages to another person implies that the wrongdoer is under an obligation to pay compensation for those dam-

ages." According to Italy, this provision is frequently invoked by individuals against the Italian State, and substantial sums have been awarded to claimants where appropriate. If Raytheon and Machlett suffered damage caused by violations by Italian public authorities of the FCN Treaty and the Supplementary Agreement, an Italian court would, it was contended, have been bound to conclude that the relevant acts of the public authorities were wrongful acts for the purposes of Article 2043. It is common ground between the Parties that implementing legislation *("ordini di esecuzione")* was enacted (Law No. 385 of 15 June 1949 and Law No. 910 of 1 August 1960), to give effect in Italy to the FCN Treaty and Supplementary Agreement, but that their provisions cannot be invoked in protection of individual rights before the Italian courts unless those provisions are regarded by the courts as self-executing. In order to show that the relevant provisions would be so regarded, decisions of the Court of Cassation have been cited by Italy in which provisions of the FCN Treaty (not the provisions relied on in the present case) have been applied for the benefit of United States nationals who have invoked them before Italian courts, and a provision of a treaty between Italy and the Federal Republic of Germany, said to be comparable with Article V of the FCN Treaty, was given effect.

62. However, those decisions were not based on Article 2043 of the Italian Civil Code; and the treaty provisions applied were given effect in conjunction with municipal legislation or the provisions of other treaties, through the mechanism of a most-favoured-nation provision. In none of the cases cited was the FCN Treaty provision relied on to establish the wrongfulness of conduct of Italian public officials. When in 1971 Raytheon consulted two Italian jurists on the question of local remedies for the purposes of a diplomatic claim, it apparently did not occur to either of them to refer even as a possibility to action under Article 2043 in conjunction with the FCN Treaty. It thus appears to the Chamber to be impossible to deduce, from the recent jurisprudence cited, what the attitude of the Italian courts would have been had Raytheon and Machlett brought an action, some 20 years ago, in reliance on Article 2043 of the Civil Code in conjunction with the provisions of the FCN Treaty and the Supplementary Agreement. Where the determination of a question of municipal law is essential to the Court's decision in a case, the Court will have to weigh the jurisprudence of the municipal courts, and "If this is uncertain or divided, it will rest with the Court to select the interpretation which it considers most in conformity with the law" (*Brazilian Loans, P.C.I.J., Series A, Nos. 20/21,* p. 124). In the present case, however, it was for Italy to show, as a matter of fact, the existence of a remedy which was open to the United States stockholders and which they failed to employ. The Chamber does not consider that Italy has discharged that burden.

63. It is never easy to decide, in a case where there has in fact been much resort to the municipal courts, whether local remedies have truly been "exhausted". But in this case Italy has not been able to satisfy the

Chamber that there clearly remained some remedy which Raytheon and Machlett, independently of ELSI, and of ELSI's trustee in bankruptcy, ought to have pursued and exhausted. Accordingly, the Chamber will now proceed to consider the merits of the case.

* * *

64. Paragraph 1 of the United States final submissions claims that:

> "(1) the Respondent violated the international legal obligations which it undertook by the Treaty of Friendship, Commerce and Navigation between the two countries, and the Supplement thereto, and in particular, violated Articles III, V, and VII of the Treaty and Article I of the Supplement".

It is necessary therefore to examine these Articles of the FCN Treaty and the Supplementary Agreement, against the conduct which is said to have been a violation of the obligations set out in these Articles. In doing so, it will be kept in mind that although the stated purposes of the FCN Treaty were those normally to be found in treaties of that kind, nevertheless a purpose of the Supplementary Agreement, which is to "constitute an integral part" of the FCN Treaty, was to give "added encouragement to investments of the one country in useful undertakings in the other country".

65. The acts of the Respondent which are thus alleged to violate its treaty obligations were described by the Applicant's counsel in terms which it is convenient to cite here:

> "First, the Respondent violated its legal obligations when it unlawfully requisitioned the ELSI plant on 1 April 1968 which denied the ELSI stockholders their direct right to liquidate the ELSI assets in an orderly fashion. Second, the Respondent violated its obligations when it allowed ELSI workers to occupy the plant. Third, the Respondent violated its obligations when it unreasonably delayed ruling on the lawfulness of the requisition for 16 months until immediately after the ELSI plant, equipment and work-in-process had all been acquired by ELTEL. Fourth and finally, the Respondent violated its obligations when it interfered with the ELSI bankruptcy proceedings, which allowed the Respondent to realize its previously expressed intention of acquiring ELSI for a price far less than its fair market value."

66. The most important of these acts of the Respondent which the Applicant claims to have been in violation of the FCN Treaty is the requisition of the ELSI plant by the Mayor of Palermo on 1 April 1968, which is claimed to have frustrated the plan for what the Applicant terms an "orderly liquidation" of the company as set out in paragraphs 22-25

above. It is fair to describe the other impugned acts of the Respondent, to be explained more fully below (paragraph 115), as ancillary to this core claim based on the requisition and its effects.

67. The Chamber is faced with a situation of mixed fact and law of considerable complexity, wherein several different strands of fact and law have to be examined both separately and for their effect on each other: the meaning and effect of the relevant Articles of the FCN Treaty and Supplementary Agreement; the legal status of the Mayor's requisition of ELSI's plant and assets; and the legal and practical significance of the financial position of ELSI at material times, and its effect, if any, upon ELSI's plan for orderly liquidation of the company. It will be convenient to begin by examining these considerations in relation to the Applicant's claim that the requisition order was a violation of Article III of the FCN Treaty.

* *

68. Article III of the FCN Treaty is in two paragraphs. Paragraph 1 provides for rights of participation of nationals of one High Contracting Party, in corporations and associations of the other High Contracting Party, and for the exercise by such corporations and associations of their functions. Since there is no allegation of treatment less favourable than is required according to the standards set by this paragraph, it need not detain the Chamber. Paragraph 2 of Article III is however important for the Applicant's claim; it provides:

> "The nationals, corporations and associations of either High Contracting Party shall be permitted, in conformity with the applicable laws and regulations within the territories of the other High Contracting Party, to organize, control and manage corporations and associations of such other High Contracting Party for engaging in commercial, manufacturing, processing, mining, educational, philanthropic, religious and scientific activities. Corporations and associations, controlled by nationals, corporations and associations of either High Contracting Party and created or organized under the applicable laws and regulations within the territories of the other High Contracting Party, shall be permitted to engage in the aforementioned activities therein, in conformity with the applicable laws and regulations, upon terms no less favorable than those now or hereafter accorded to corporations and associations of such other High Contracting Party controlled by its own nationals, corporations and associations."

Again there is no allegation of treatment of ELSI according to standards less favourable than those laid down in the second sentence of the para-

graph: the allegation by the United States of a violation of this paragraph by Italy relates to the first sentence.

69. In terms of the present case, the effect of the first sentence of this paragraph is that Raytheon and Machlett are to be permitted, in conformity with the applicable laws and regulations within the territory of Italy, to organize, control and manage ELSI. The claim of the United States focuses on the right to "control and manage"; the right to "organize", apparently in the sense of the creation of a corporation, is not in question in this case. Is there, then, a violation of this Article if, as the United States alleges, the requisition had the effect of depriving ELSI of both the right and practical possibility of selling off its plant and assets for satisfaction of its liabilities to its creditors and satisfaction of its shareholders?

70. It is undeniable that the requisition of a firm's "plant and relative equipment" must normally amount to a deprivation, at least in important part, of the right to control and manage. It was objected by Italy that the requisition in no way affected "control by the shareholders over the company", but merely concerned the management by the company of property belonging to the company. It is true that the direct impact of the requisition was only on control of the property requisitioned. It is however also undeniable that this requisition, which remained in effect until 30 September 1968, was issued to avoid the closure of ELSI's plant, the dismissal of its workforce, and as a consequence the probable dispersal of the assets, all of which were integral to ELSI's plan for orderly liquidation. Since the requisition thus had the design of preventing Raytheon from exercising, for six critical months, what was at that time a most important part of its right to control and manage ELSI, there exists a question whether the requisition was in conformity with the requirements of Article III, paragraph 2, of the FCN Treaty. Before coming to a conclusion on that question it is necessary now to take into consideration certain other matters.

71. Article III of the FCN Treaty, both in paragraph 1 concerning rights to be enjoyed by the nationals of one party in the territory of the other, and in paragraph 2, concerning rights of nationals of one party to "organize, control and manage" corporations of the other party, contains the qualifying phrase, "in conformity with the applicable laws and regulations" of the latter party. It was argued by Italy that this clause confirms that the correct interpretation of that paragraph is that it was not intended to confer upon United States nationals any rights of control and management more extensive, or more extensively protected, than those enjoyed by other stockholders, of whatever nationality, in Italian companies. Therefore, it was said, the requisition was no breach of the rights conferred by the FCN Treaty, because its "invalidity . . . as ascertained by the decision of the Prefect of Palermo, does not alter the fact that it was issued by the competent authority on a regular legal basis". But, in the Chamber's view, the reference to conformity with "the applicable laws and regu-

lations" cannot mean that, if an act is in conformity with the municipal law and regulations, that would of itself exclude any possibility that it was an act in breach of the FCN Treaty.

72. The reference to conformity with "the applicable laws and regulations" surely means no more than that Italian corporations and associations controlled by United States nationals must conform to the local applicable laws and regulations; moreover, they must do so even if they believe a law or regulation to be in breach of the FCN Treaty, and, indeed, even if it were in breach of the FCN Treaty. This the Applicant has never denied. Raytheon and Machlett did conform to the terms of the requisition. Indeed they had no other choice.

73. The question still remains, therefore, whether the requisition was or was not a violation of Article III, paragraph 2. This question arises irrespective of the position in municipal law. Compliance with municipal law and compliance with the provisions of a treaty are different questions. What is a breach of treaty may be lawful in the municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision. Even had the Prefect held the requisition to be entirely justified in Italian law, this would not exclude the possibility that it was a violation of the FCN Treaty.

74. This question whether or not certain acts could constitute a breach of the treaty right to be permitted to control and manage is one which must be appreciated in each case having regard to the meaning and purpose of the FCN Treaty. Clearly the right cannot be interpreted as a sort of warranty that the normal exercise of control and management shall never be disturbed. Every system of law must provide, for example, for interferences with the normal exercise of rights during public emergencies and the like. In this respect considerable interest must attach to the reasons given by the Prefect in his decision, and to the legal analysis of that decision by the Court of Appeal of Palermo.

75. The Prefect took note in his decision of the fact that the Mayor had relied on legislative authority empowering him to act in cases of "grave public necessity and unforeseen urgency". He did not find that those conditions were absent; he however annulled the requisition on the basis primarily of the following considerations:

> *"Non v'ha dubbio che anche se possono considerarsi, in linea del tutto teorica, sussistenti, nella fattispecie, gli estremi della grave necessità pubblica e della contingibilità ed urgenza che determinarono l'adozione del provvedimento, il fine cui tendeva la requisizione non poteva trovare pratica realizzazione con il provvedimento stesso, tanto è vero che nessuna ripresa di attività dell'azienda vi è stata a seguito della requisizione, nè avrebbe potuto esserci. Manca, pertanto, nel provvedimento, genericamente, la causa giuridica che possa giustificarlo e renderlo operante."*

There has been some controversy between the Parties as to the translation

of this passage (see paragraph 123 below); in the view of the Chamber it may be translated as follows:

> "There is no doubt that, even though, from the purely theoretical standpoint, the conditions of grave public necessity and of unforeseen urgency warranting adoption of the measure may be considered to exist in the case in point, the intended purpose of the requisition could not in practice be achieved by the order itself, since in fact there was no resumption of the company's activity following the requisition, nor could there have been such resumption. The order therefore lacks, generically, the juridical cause which might justify it and make it operative."

The Court of Appeal of Palermo, for reasons to be examined more fully below (paragraph 127), considered that the Prefect's finding had been one of

> *"un tipico caso di eccesso di potere, che è, come è noto, un vizio di legittimità dell'atto amministrativo"*
>
> ("a typical case of excess of power, which is of course a defect of lawfulness of an administrative act").

The requisition was thus found not to have been justified in the applicable local law; if therefore, as seems to be the case, it deprived Raytheon and Machlett of what were at the moment their most crucial rights to control and manage, it might appear prima facie a violation of Article III, paragraph 2.

76. There remains however a crucial question to be considered. According to the Respondent, Raytheon and Machlett were, because of ELSI's financial position, already naked of those very rights of control and management of which they claim to have been deprived. It is necessary now, therefore, to consider what effect, if any, the financial position of ELSI may have had in that respect, first as a practical matter, and then also as a question of Italian law.

*

77. The essence of the Applicant's claim has been throughout that Raytheon and Machlett, which controlled ELSI, were by the requisition deprived of the right, and of the practical possibility, of conducting an orderly liquidation of ELSI's assets. This plan for an orderly liquidation was however very much bound up with the financial state of ELSI, and the two need to be considered together.

78. ELSI's lack of success was attributed by its management at least in part to the fact that it was over-manned in relation to its order book; it had needed repeated injections of fresh capital, and was never able to produce an operating profit sufficient to offset its debt expense and its accumulat-

ing losses. No dividends were ever paid to its shareholders. The 30 September 1966 balance sheet already showed accumulated losses of some 2,000 million lire.

79. The position was worsening, moreover, as the balance sheet for 30 September 1967 (above at paragraphs 18-19) showed. Raytheon's Italian auditors pointed out that the balance sheet, when "adjusted" to Raytheon's own accounting requirements for internal purposes (the unadjusted statement, however, appears to have satisfied Italian legal requirements), then showed adjusted accumulated losses, actually exceeding "the total of the paid up capital stock, capital reserve and Stockholders' subscription account" by 881.3 million lire; and warned that if these adjustments to the total of accumulated losses were entered in the company's books of account,

> "under Articles 2447 and 2448 of the Italian Civil Code, the directors would be obliged to convene a Stockholders' meeting forthwith to take measures either to cover the losses by providing new capital or to put the company into liquidation".

80. On 7 March 1968, Raytheon formally notified ELSI of its decision that Raytheon would not provide any further capital, whether in the form of subscribing to new stock or guaranteeing additional loans. At a board meeting of ELSI held in Rome on 16 March 1968, it was decided on the "cessation of the company's operations"; that production would be "discontinued immediately"; that "commercial activities and employment contracts" would be terminated on 29 March 1968; and that "a shareholders' meeting be called for 28 March 1968, to adopt the necessary resolutions". This was not, however, in ELSI's plans, to involve a liquidation under Article 2450 of the Italian Civil Code, which requires a liquidator to be appointed. The plan for an orderly liquidation, as conceived by the ELSI management, was to be managed by them. At a special meeting of shareholders, held on 28 March 1968, in Palermo, it was resolved to ratify the resolutions adopted by the Board of Directors at the meeting of 16 March 1968; and

> "to empower the Board of Directors to make contacts with the banks and principal creditors of the company to reach an agreement on procedures to be followed in the interest of all the creditors for the orderly disposal of the company's assets at their highest realizable value . . ."
>
> *("di dare mandato al Consiglio di Amministrazione di prendere contatti con gli istituti di credito e con i maggiori creditori della Società per concordare procedure che consentano nell'interesse di tutti i creditori una ordinata alienazione delle attività sociali al massimo valore di realizzazione").*

81. This policy of the ELSI management during the months prior to the requisition had, however, a Janus-like character. Although the orderly liquidation contemplated closure of the plant, and dismissal of the workforce, an alternative aim of the management and of Raytheon was to keep the place going, the hope being that the threat of closure and dismissal of the workforce might bring such pressures to bear on the Italian authorities as to persuade them to provide what Raytheon had long hoped for: an influential Italian partner, new capital, and Mezzogiorno benefits. The "Project for the Financing and Reorganization of the Company" prepared in May 1967 spelled out the need for additional capital, new products from Italian Government sources, and financial help for transport costs, capital investment and training; the Project made it clear that the alternative was that Raytheon would decline to invest more funds, over 300 people would become redundant forthwith, and dwindling markets would reduce the employment level still further; as stated in that Project, "The alternative is really the actual destruction of the existing asset with the undesirable social effects which must follow."

82. Right up to the eve of the requisition the company's representatives went on talking to Italian officials; but at the same time the company's management, according to an affidavit by one of its officials,

> "were aware of the need to have back-up plans in case these efforts were not successful. In the latter part of 1967, we reluctantly began to plan in general for the potential liquidation of ELSI."

In the words of the affidavit of another company official, Raytheon had

> "developed a plan for the orderly disposal of ELSI over about six months during 1968. While this plan was being developed, Raytheon and ELSI representatives continued to meet with Italian Government representatives in an ongoing attempt to find a way for the company to continue to operate."

The company no doubt wished to postpone liquidation as long as possible, both in the hope of avoiding it, and because the threat of closure of the plant would be a means of pressure on the Italian authorities so long as it remained only a threat. The risk, of which the company was well aware, was that to carry on too long might topple the company into insolvency under Italian law. In the event the Italian authorities did not come to the rescue, at least not with terms acceptable to ELSI's management; and the management was left at the last minute with the orderly liquidation plan to be put into effect as seemingly the only way of avoiding bankruptcy or liquidation under the supervision of the Italian court; and the

bankruptcy of its subsidiary was undoubtedly a most unwelcome prospect for Raytheon.

83. The crucial question is whether Raytheon, on the eve of the requisition, and after the closure of the plant and the dismissal, on 29 March 1968, of the majority of the employees, was in a position to carry out its orderly liquidation plan, even apart from its alleged frustration by the requisition. That plan, as originally conceived, contemplated that the disposal of plant and assets might produce enough to pay all creditors 100 per cent of their dues, with a modest residue for the shareholders. In one of the affidavits quoted above it is stated: "If the assets had been disposed of at book value all liabilities, including the payables to Raytheon Company, would have been paid in full." And, indeed, the trustee in bankruptcy, in his report of 28 October 1968 to the bankruptcy judge, explained that in March 1968:

> "the management of Raytheon-Elsi decided, and publicly stated their intention (which was later adopted by the Board of Directors), to suggest to the shareholders the liquidation of the company. The intention was to proceed with an orderly liquidation of all assets in order to pay all the Company's creditors 100 per cent."

This must have seemed a reasonable aim, for the "book value" may well have been a conservative figure. It has not been demonstrated that ELSI was, until shortly before the bankruptcy petition, ever actually in default. Moreover, Raytheon had opened an account in Milan for the payment at 100 per cent of small creditors.

84. Nevertheless since no new investment capital was forthcoming, the possibility of paying creditors in full depended upon putting the orderly liquidation plan into operation in good time. Time was running out because money was running out. As the position worsened daily, the moment might at any time arrive when liabilities exceeded assets, or default resulted from lack of liquidity. ELSI's management had prepared the assessment of the "quick-sale value" (see paragraph 18 above), which was markedly less than book value, being aware that the sale of the company's assets might fail to provide sums approximating to book value. There were plans also to approach the large bank creditors in the hope of securing their agreement to settlements of 50 per cent.

85. Did ELSI, in this precarious position at the end of March 1968, still have the practical possibility to proceed with an orderly liquidation plan? The successful implementation of a plan of orderly liquidation would have depended upon a number of factors not under the control of ELSI's management. Since the company's coffers were dangerously low, funds had to be forthcoming to maintain the cash flow necessary while the plan

was being carried out. Evidence has been produced by the Applicant that Raytheon was prepared to supply cash flow and other assistance necessary to effect the orderly liquidation, and the Chamber sees no reason to question that Raytheon had entered or was ready to enter into such a commitment. Other factors governing the matter however give rise to some doubt.

86. First, for the success of the plan it was necessary that the major creditors (i.e., the banks) would be willing to wait for payment of their claims until the sale of the assets released funds to settle them: and this applied not only to the capital sums outstanding, which may not at the time have yet been legally due for repayment, but also the agreed payments of interest or instalments of capital. Though the Chamber has been given no specific information on the point, this is of the essence of such a liquidation plan: the creditors had to be asked to give the company time. If ELSI had been confident of continuing to meet all its obligations promptly and regularly while seeking a buyer for its assets, no negotiations with creditors, and no elaborate calculations of division of the proceeds, on different hypotheses, such as have been produced to the Chamber, would have been needed.

87. Secondly, the management were by no means certain that the sale of the assets would realize enough to pay all creditors in full; in fact, the existence of the calculation of a "quick-sale value" suggests perhaps more than uncertainty. Thus the creditors had to be asked to give time in return for an assurance, not that 100 per cent would be paid, but that a minimum of 50 per cent would be paid. While in general it might be in the creditors' interest to agree to such a proposal, this does not mean in this case that ELSI could count on such agreement. At the date of the requisition, it seems apparent that the banks, while informed of the financial position, had not yet even been consulted on whether they would accept a guaranteed 50 per cent (see paragraphs 28-29 above), so their reaction remains a matter of speculation.

88. Nor should it be overlooked that the dismissed employees of ELSI ranked as preferential creditors for such sums as might be due to them for severance pay or arrears. In this respect Italy has drawn attention to the Sicilian regional law of 13 May 1968, providing for the payment

> "for the months of March, April and May 1968, to the dismissed employees of Raytheon-Elsi of Palermo of a special monthly indemnity equal to the actual monthly pay received until the month of February 1968".

From this it could be inferred, said Italy, that ELSI did not pay its employees for the month of March 1968. Further it was conceded by the former

Chairman of ELSI, when he appeared as a witness and was cross-examined, that the cash available at 31 March 1968 ("22 million in the kitty"), would have been insufficient to meet the payroll of the full staff even for the first week of April ("at least 25 million"). The suggestion that ELSI did not meet its March 1968 payroll was not put to the witness; and counsel for the United States later stated that the assertion that "ELSI could not make its March payroll", was "simply wrong". It is in any event certain that when the company ceased activity there were still severance payments due to the dismissed staff; those, the Applicant suggested, would have been covered by funds to be provided by Raytheon (paragraph 28 above). They could not have been met from the money still remaining in ELSI's coffers at the time.

89. Thirdly, the plan as formulated by ELSI's management involved a potential inequality among creditors: unless enough was realized to cover the liabilities fully, the major creditors were to be content with some 50 per cent of their claims; but the smaller creditors were still to be paid in full. Whether or not this would have been legally objectionable as a breach of the rule of *par condicio creditorum* (it appears that Raytheon contemplated accepting a smaller share in the eventual distribution so that the small creditors could receive 100 per cent without affecting the share attributed to the banks), it was an additional factor which might have caused a major creditor to hesitate to agree. According to the evidence, when in late March 1968 ELSI started using funds made available by Raytheon to pay off the small creditors in full, "the banks intervened and said that they did not want that to happen as that was showing preference". Once the banks adopted this attitude, the whole orderly liquidation plan was jeopardized, because a purpose of the settlement with small creditors was, according to the 1974 diplomatic claim, "to eliminate the risk that a small irresponsible creditor would take precipitous action which would raise formidable obstacles in the way of orderly liquidation".

90. Fourthly, the assets of the company had to be sold with the minimum delay and at the best price obtainable — desiderata which are often in practice irreconcilable. The United States has emphasized the damaging effect of the requisition on attempts to realize the assets; after the requisition it was no longer possible for prospective buyers to view the plant, nor to assure them that if they bought they would obtain immediate possession. It is however not at all certain that the company could have counted on unfettered access to its premises and plant, and the opportunity of showing it to buyers without disturbance, even if the requisition had not been made. There has been argument between the Parties on the question whether and to what extent the plant was occupied by employees of ELSI both before and after the requisition; but what is clear is that the company was expecting trouble at the plant when its closure plans became

known: the books had been removed to Milan, according to the evidence given at the hearings, "so that if we did have problems we could at least control the books" and "we had moved quite a lot of inventory [to Milan] so that we could sell it from there if we had to".

91. Fifthly, there was the attitude of the Sicilian administration: the company was well aware that the administration was strongly opposed to a closure of the plant, or more specifically, to a dismissal of the workers. True, the measure used to try to prevent this — the requisition order — was found by the Prefect to have lacked the "juridical cause which might justify it and make it operative" (paragraph 75 above). But ELSI's management in March 1968 could not have been certain that the hostility of the local authorities to their plan of closure and dismissals would not take practical form in a legal manner. The company's management had been told before the staff dismissal letters were sent out that such dismissals would lead to a requisition of the plant.

92. All these factors point towards a conclusion that the feasibility at 31 March 1968 of a plan of orderly liquidation, an essential link in the chain of reasoning upon which the United States claim rests, has not been sufficiently established.

93. Finally there was, beside the practicalities, the position in Italian bankruptcy law. Article 5 of the Italian Bankruptcy Act of 1942 provides that

> "An entrepreneur who is in a state of insolvency shall be declared bankrupt.
>
> The state of insolvency, moreover, becomes apparent not only by default but also by other external acts which show that the debtor is no longer in a position regularly to discharge his obligations."
>
> *("L'imprenditore che si trova in stato d'insolvenza è dichiarato fallito.*
>
> *Lo stato d'insolvenza si manifesta con inadempimenti od altri fatti esteriori, i quali dimostrino che il debitore non è più in grado di soddisfare regolarmente le proprie obbligazioni.")*

This formula excludes a merely momentary or temporary disability, and refers to one which shows every sign of going on. "Regular" payment *("regolarmente")* apparently refers to payment in full at the due time. Given this definition it is apparent that ELSI could have been "insolvent" in the sense of Italian bankruptcy law, at the end of March, even though not actually in default. The Chamber has been given conflicting evidence on the question whether a debtor in such a position is bound under Italian law to go into bankruptcy, or whether he may still enter into voluntary composition with his creditors outside the supervision of the bankruptcy court (paragraph 25 above).

94. If however ELSI was in a state of legal insolvency at 31 March 1968, and if, as contended by Italy, a state of insolvency entailed an obligation on the company to petition for its own bankruptcy, then the relevant rights of control and management would not have existed to be protected by the FCN Treaty. While not essential to the Chamber's conclusion, already stated in paragraph 92 above, an assessment of ELSI's solvency as a matter of Italian law is thus highly material.

95. Italy has argued that even before the requisition, ELSI was insolvent in the sense that its liabilities exceeded the value of its assets, and in support of this has pointed to, first, the "quick-sale value" calculated for the purposes of the liquidation plan, and secondly the observations of the auditors on the September 1967 balance sheet. The Chamber does not however consider that it has to conclude from this that ELSI was insolvent as early as 1967. The value of assets of this kind, until they are actually sold, must be a matter for assessment by informed opinion, and different views, and the use of different accounting conventions, may lead to different results. The company's management was clearly of the view that it could legally continue trading up to the end of March 1968, since its former Chairman has told the Chamber that the company's legal and financial advisers were keeping a close and continuous watch on the position to ensure that Italian legal requirements were respected. But there is no doubt that ELSI was indeed in a state of insolvency when on 25 April 1968 its Board of Directors voted to file a petition in bankruptcy. The conclusion then made that "The company's financial situation has worsened and has now reached a state of insolvency" was based, according to the minutes of the board meeting, on the fact that "There are payments on long-term loans that fell due a few days ago, and other payments which the company cannot make as a result of lack of liquidity . . ." In the bankruptcy petition, it was specified that "an instalment of Lit. 800,000,000 to Banca Nazionale del Lavoro became due on 18 April 1968 and the note therefor has been or will be protested, etc." In other words, the company had by then committed a default *("inadempimento")*, by failing to meet its debts as they became due.

96. On this matter of insolvency in Italian law, consideration must also be given to the reasons employed by the Prefect of Palermo for his decision to annul the requisition order, and the findings of the Court of Palermo and the Court of Appeal of Palermo on the action brought by ELSI's trustee in bankruptcy, for damages following the decision of the Prefect annulling the requisition order. As indicated above (paragraph 75), the Prefect considered that the purpose of the requisition could not be achieved, since the company's activity could not be resumed. He explained that

> *"lo stato dell'azienda era tale, per circostanze di carattere economico-funzionale e di mercato, da non consentire la prosecuzione dell'atti-*

vità . . . La requisizione, quindi, nulla ha mutato nella situazione aziendale . . . La situazione di dissesto ha, anzi, determinato la dichiarazione di fallimento dell'azienda . . ."

("the situation of the company, due to functional-economic and market factors, was such as not to permit of the pursuance of its activity . . . The requisition consequently changed nothing in the situation of the company . . . On the contrary, the situation of insolvency determined the declaration of bankruptcy of the company . . .")

97. The Court of Palermo was faced with the argument, mentioned in paragraph 58 above, that "the requisition order caused an economic situation of such gravity that it immediately and directly triggered the bankruptcy of the company". It dealt with this by pointing to the situation of the company on the eve of the requisition:

"A 31 marzo 1968, in sostanza, lo stabilimento dell'Elsi non era più in fase produttiva, fermata per deliberazione dell'organo sociale competente che . . . aveva . . . opinato, non potendo trovare altro rimedio, per la soluzione più drastica, evidentemente reputandola più confacente agli interessi della società e che aveva come oggetto preciso l'arresto totale della produzione . . . Devesi a ciò aggiungere . . . che proprio dai primi dell'anno 1968 vi era stato un notevole peggioramento della situazione generale dell'azienda, che via via si andava aggravando per le sfavorevoli condizioni del mercato, avversata, altresì, dai fatti sismici del gennaio e da una serie di scioperi che, per l'appunto, nel mese di marzo ebbero a carattere ora di continuità ora di intermittenza, con la conseguenza della perdita di un considerevole numero di ore lavorative . . ."

("On March 31, 1968, the Elsi plant was for all practical purposes no longer in operation, stopped in accordance with a decision of the competent organ of the company which . . . had decided, in the absence of any other solution, to go for the most drastic solution, evidently considering it most conducive to the interests of the company, a solution which meant the total shutdown of production . . . To this must be added . . . that in the early part of 1968, there was a notable deterioration of the general situation of the company, which was further aggravated by unfavourable market conditions as well as the January earthquakes and a series of strikes which in March were sometimes continuous and sometimes intermittent, causing the loss of a considerable amount of production hours . . .")

From this the Court was able to conclude that

"Dalle condizioni premesse discende che l'aggancio del fallimento della società all'intervenuta requisizione non ha fondamento, siccome, esattamente, è stato sostenuto coll'amministrazione convenuta, essendo la situazione economica della Raytheon-Elsi già gravemente compromessa da anni per esplicito riconoscimento dei suoi stessi dirigenti."

("It is clear from these conditions that the connection between the company's bankruptcy and the requisition is unfounded, as the defendant administration correctly maintained, since Raytheon-Elsi's economic situation had for years already been seriously compromised, as its own management explicitly admitted.")

The Court of Palermo did not however go so far as to state that ELSI was legally insolvent prior to the requisition.

98. However the Court of Appeal of Palermo, in its judgment, states that ELSI was insolvent before the requisition order was made. The salient passage on this point in the Court of Appeal's judgment states:

"per quanto riguarda i danni che si fanno consistere nell'avere la requisizione provocato il fallimento della società, la conclusione negativa del tribunale è ampiamente e convincentemente motivata e . . . le considerazioni critiche dell'appellante non valgono a provocare un convincimento diverso; . . . La circostanza certa della insolvenza della società in tempo immediatamente anteriore allo intervento del Sindaco . . . è sufficiente per escludere il collegamento causale fra il successivo provvedimento di requisizione e il fallimento della società, per il quale ultimo quello stato di insolvenza è causa determinante e sufficiente (Art. 5 legge fallim.)."

("as regards the damages consisting in the fact that the order triggered the company's bankruptcy, the negative conclusion arrived at by the court below is amply and convincingly motivated and the critical considerations of the appellant are not sufficient to lead to a different determination . . . The certain circumstance that the company was insolvent during the time immediately prior to the Mayor's intervention . . . is sufficient to rule out any causal link between the subsequent requisition order and the company's bankruptcy of which the company's state of insolvency was the decisive and sufficient cause (Art. 5, Bankruptcy Law).")

The Court of Appeal also refers to the "prior insolvency" *("precedente insolvenza")* of the company, and to "the decisive effect of the state of insolvency" *("la efficacia determinante dello stato di insolvenza").*

99. Whether these findings by the municipal courts are to be regarded as determinations as a matter of Italian law that ELSI had been insolvent, within the meaning of the relevant legislative provisions, on 31 March 1968, or whether they are no more than findings that the financial position of ELSI on that date was so desperate that it was past saving, so that it was not the requisition which "caused an economic situation of such gravity that it immediately and directly triggered the bankruptcy of the company" makes no difference to the conclusion to be drawn. If ELSI was legally insolvent, then even if the liquidation plan could in fact have been implemented with co-operation from the creditors, the stockholders no longer had rights of control and management to be protected by the FCN Treaty. If, as the Prefect of Palermo stated, and the courts of Palermo certainly thought, the factual situation at least was such that the requisition

changed nothing, then the United States has failed to prove that there was any interference with control and management in any real sense. The Chamber has no need to go into the question of the extent to which it could or should question the validity of a finding of Italian law, the law governing the matter, by the appropriate Italian courts. It is sufficient to note that the conclusion above, that the feasibility of an orderly liquidation plan is not sufficiently established, is reinforced by reference to the decision of the courts of Palermo on the claim by the trustee in bankruptcy for damages for the injury caused by the requisition. Whether regarded as findings of Italian law or as findings of fact, the decisions of the courts of Palermo simply constitute additional evidence of the situation which the Chamber has to assess.

100. It is important, in the consideration of so much detail, not to get the matter out of perspective: given an under-capitalized, consistently loss-making company, crippled by the need to service large loans, which company its stockholders had themselves decided not to finance further but to close and sell off because, as they were anxious to make clear to everybody concerned, the money was running out fast, it cannot be a matter of surprise if, several days after the date at which the management itself had predicted that the money would run out, the company should be considered to have been actually or virtually in a state of insolvency for the purposes of Italian bankruptcy law.

101. If, therefore, the management of ELSI, at the material time, had no practical possibility of carrying out successfully a scheme of orderly liquidation under its own management, and may indeed already have forfeited any right to do so under Italian law, it cannot be said that it was the requisition that deprived it of this faculty of control and management. Furthermore, one feature of ELSI's position stands out: the uncertain and speculative character of the causal connection, on which the Applicant's case relies, between the requisition and the results attributed to it by the Applicant. There were several causes acting together that led to the disaster to ELSI. No doubt the effects of the requisition might have been one of the factors involved. But the underlying cause was ELSI's headlong course towards insolvency; which state of affairs it seems to have attained even prior to the requisition. There was the warning loudly proclaimed about its precarious position; there was the socially damaging decision to terminate the business, close the plant, and dismiss the workforce; there was the position of the banks as major creditors. In short, the possibility of that solution of orderly liquidation, which Raytheon and Machlett claim to have been deprived of as a result of the requisition, is purely a matter of speculation. The Chamber is therefore unable to see here anything which can be said to amount to a violation by Italy of Article III, paragraph 2, of the FCN Treaty.

* *

102. There are two claims of the Applicant that are based upon the provisions of Article V of the FCN Treaty: one relates to paragraphs 1 and 3, and is concerned with protection and security of nationals and their property; another relates to paragraph 2, and is concerned with the taking or expropriation of property. No claim is based upon paragraph 4 of Article V. The Applicant's claim under paragraphs 1 and 3 will be dealt with first.

103. Paragraph 1 of Article V provides as follows:

> "1. The nationals of each High Contracting Party shall receive, within the territories of the other High Contracting Party, the most constant protection and security for their persons and property, and shall enjoy in this respect the full protection and security required by international law. To these ends, persons accused of crime shall be brought to trial promptly, and shall enjoy all the rights and privileges which are or may hereafter be accorded by the applicable laws and regulations; and nationals of either High Contracting Party, while within the custody of the authorities of the other High Contracting Party, shall receive reasonable and humane treatment. In so far as the term 'nationals' where used in this paragraph is applicable in relation to property it shall be construed to include corporations and associations."

Paragraph 2 of this Article is not relevant here, but is set out in paragraph 113 of this Judgment. Paragraph 3 provides as follows:

> "3. The nationals, corporations and associations of either High Contracting Party shall within the territories of the other High Contracting Party receive protection and security with respect to the matters enumerated in paragraphs 1 and 2 of this Article, upon compliance with the applicable laws and regulations, no less than the protection and security which is or may hereafter be accorded to the nationals, corporations and associations of such other High Contracting Party and no less than that which is or may hereafter be accorded to the nationals, corporations and associations of any third country. Moreover, in all matters relating to the taking of privately owned enterprises into public ownership and the placing of such enterprises under public control, enterprises in which nationals, corporations and associations of either High Contracting Party have a substantial interest shall be accorded, within the territories of the other High Contracting Party, treatment no less favorable than that which is or may hereafter be accorded to similar enterprises in which nationals, corporations and associations of such other High Contracting Party have a substantial interest, and no less favorable than that which is or may hereafter be accorded to similar enterprises in which nationals, corporations and associations of any third country have a substantial interest."

104. Paragraph 1 thus provides for "the most constant protection and security" for nationals of each High Contracting Party, both "for their persons and property"; and also that, in relation to property, the term "nationals" shall be construed to "include corporations and associations"; and in defining the nature of the protection, the required standard is established by a reference to "the full protection and security required by international law". Paragraph 3 elaborates this notion of protection and security further, by requiring no less than the standard accorded to the nationals, corporations and associations of the other High Contracting Party; and no less than that accorded to the nationals, corporations and associations of any third country. There are, accordingly, three different standards of protection, all of which have to be satisfied.

105. A breach of these provisions is seen by the Applicant to have been committed when the Respondent "allowed ELSI workers to occupy the plant" (see paragraph 65 above). It is the contention of the United States that once the plant had been requisitioned, ELSI's employees began an occupation of the premises which continued, so far as the United States was aware, up to the re-opening of the plant by ELTEL; and that this occupation had the tacit approval of local authorities, who made no effort to prevent or to end it, or otherwise to protect the premises. To this occupation the United States attributes as injurious consequences, first a deterioration of the plant and related material and equipment, and secondly that it impeded the efforts of the trustee in bankruptcy to dispose of the plant.

106. Italy has objected that Article V, paragraphs 1 and 3, guarantees the protection and security of property belonging to United States companies in Italy, but the plant in Palermo which, according to the United States, should have been protected under the FCN Treaty belonged to the Italian company ELSI. The United States replies that the "property of Raytheon and Machlett in Italy" was ELSI itself, and Italy was obligated to protect the entire entity of ELSI from the deleterious effects of the requisition. While there may be doubts whether the word "property" in Article V, paragraph 1, extends, in the case of shareholders, beyond the shares themselves, to the company or its assets, the Chamber will nevertheless examine the matter on the basis argued by the United States that the "property" to be protected under this provision of the FCN Treaty was not the plant and equipment the subject of the requisition, but the entity of ELSI itself.

107. That there was some occupation of the plant by the workers after the requisition is something that Italy has not sought to deny, and the Court of Appeal of Palermo referred in passing to the circumstance of the requisitioning authority having tolerated the "unlawful" act of occupation of the plant by the workers *("la autorità requirente avesse tollerato l'illecito penale di una occupazione dei reparti di lavorazione da parte delle maestranze").* It appears, nevertheless, to have been a peaceful occupation, as may be learned from ELSI's own administrative appeal of 19 April 1968 to

the Prefect against the requisition, and the affidavits of the Mayor of Palermo and one of his officials (see paragraph 33 above). It is difficult to accept that the occupation seriously harmed the interests of ELSI in view of the evidence produced by Italy that measures taken by the Mayor of Palermo for the temporary management of the plant permitted the continuation and completion of work in progress in the months following the requisition. The United States has asserted that the continued production was very limited, and cannot be equated with resumption of full production in the plant, and continues to contend that the plant and machinery fell into disuse following the requisition and deteriorated rapidly in value. The Court of Palermo however found itself unable to establish that any damage to the plant had been caused by the occupying workers.

108. The reference in Article V to the provision of "constant protection and security" cannot be construed as the giving of a warranty that property shall never in any circumstances be occupied or disturbed. The dismissal of some 800 workers could not reasonably be expected to pass without some protest. Indeed, the management of ELSI seems to have been very much aware that the closure of the plant and dismissal of the workforce could not be expected to pass without disturbance; as is apparent from the removal of the company's books and "quite a lot of inventory" to Milan (paragraph 17 above). In any event, considering that it is not established that any deterioration in the plant and machinery was due to the presence of the workers, and that the authorities were able not merely to protect the plant but even in some measure to continue production, the protection provided by the authorities could not be regarded as falling below "the full protection and security required by international law"; or indeed as less than the national or third-State standards. The mere fact that the occupation was referred to by the Court of Appeal of Palermo as unlawful does not, in the Chamber's view, necessarily mean that the protection afforded fell short of the national standard to which the FCN Treaty refers. The essential question is whether the local law, either in its terms or its application, has treated United States nationals less well than Italian nationals. This, in the opinion of the Chamber, has not been shown. The Chamber must, therefore, reject the charge of any violation of Article V, paragraphs 1 and 3.

*

109. The Applicant sees a further breach of Article V, paragraphs 1 and 3, of the FCN Treaty, in the time taken — 16 months — before the Prefect ruled on ELSI's administrative appeal against the Mayor's requi-

sition order, or, to cite the words of counsel for the Applicant (paragraph 65 above),

> "the Respondent violated its obligations when it unreasonably delayed ruling on the lawfulness of the requisition for 16 months until immediately after the ELSI plant, equipment and work-in-process had all been acquired by ELTEL".

The time taken by the Prefect was undoubtedly long; and the Chamber was not entirely convinced by the Respondent's suggestion that such lengthy delays by Prefects were quite usual. Yet it must be remembered that the requisition in fact lapsed after six months and that Italian law did provide a safeguard against delays by the Prefect. It was possible after 120 days from the filing of the appeal to serve on the Prefect a request requiring him to render a decision within 60 days (paragraph 41 above). Raytheon and Machlett were never in a position to take advantage of this procedure, because by the time the 120 days had elapsed the trustee in bankruptcy was in control of the company; on the other hand, the trustee in bankruptcy did employ this procedure, and the Prefect shortly afterwards gave his decision on the appeal.

110. Counsel for the Applicant has referred to this delay as "a denial of the level of procedural justice accorded by international law". Its claim in this respect is however not founded on the rules of customary international law concerning denial of justice, nor on the text of the FCN Treaty (Article V, paragraph 4) which provides for access to justice. The relevance of the delay of the Prefect's ruling has been expressed in two ways. First, it is said, had there been a speedy decision by the Prefect, the bankruptcy of ELSI could have been avoided; the Chamber is unable to accept this argument, for the reasons already explained in connection with the claim under Article III, paragraph 2, of the FCN Treaty. Secondly, it is contended that once the requisition occurred, the Respondent had an obligation to protect ELSI from its deleterious effects, and one of the ways in which it fell short of this obligation was by failing to provide an adequate method of overturning the requisition.

111. The primary standard laid down by Article V is "the full protection and security required by international law", in short the "protection and security" must conform to the minimum international standard. As noted above, this is supplemented by the criteria of national treatment and most-favoured-nation treatment. The Chamber is here called upon to apply the provisions of a treaty which sets standards — in addition to the reference to general international law — which may go further in protecting nationals of the High Contracting Parties than general international law requires; but the United States has not — save in one respect — suggested that these requirements do in this respect set higher standards than the international standard. It must be doubted whether in all the circumstances, the delay in the Prefect's ruling in this case can be regarded as falling below that standard. Certainly, the Applicant's use

of so serious a charge as to call it a "denial of procedural justice" might be thought exaggerated.

112. The United States has also alleged that the delay in ELSI's case was far in excess of the delay experienced in prior suits involving companies owned by Italian nationals, and that it therefore constituted a failure to accord a national standard of protection. As already stated, the Chamber was not entirely convinced by the contention that such a lengthy delay was quite usual (paragraph 109 above); nevertheless, it is not satisfied that a "national standard" of more rapid determination of administrative appeals has been shown to have existed. The Chamber is therefore unable to see in this delay a violation of paragraphs 1 and 3 of Article V of the FCN Treaty.

* *

113. The Chamber now turns to the United States claim based on Article V, paragraph 2, of the FCN Treaty, which provides as follows:

> "2. The property of nationals, corporations and associations of either High Contracting Party shall not be taken within the territories of the other High Contracting Party without due process of law and without the prompt payment of just and effective compensation. The recipient of such compensation shall, in conformity with such applicable laws and regulations as are not inconsistent with paragraph 3 of Article XVII of this Treaty, be permitted without interference to withdraw the compensation by obtaining foreign exchange, in the currency of the High Contracting Party of which such recipient is a national, corporation or association, upon the most favorable terms applicable to such currency at the time of the taking of the property, and exempt from any transfer or remittance tax, provided application for such exchange is made within one year after receipt of the compensation to which it relates."

This is a most important paragraph, of a kind that is central to many investment treaties. Where the English version begins by providing that

> "The property of nationals, corporations and associations of either High Contracting Party shall not be taken within the territories of the other High Contracting Party without due process of law and without the prompt payment of just and effective compensation",

the corresponding Italian text reads as follows:

> *"I beni dei cittadini e delle persone giuridiche ed associazioni di ciascuna Alta Parte Contraente non saranno espropriati entro i territori dell'altra Alta Parte Contraente, senza una debita procedura legale e senza il pronto pagamento di giusto ed effettivo indennizzo."*

There was considerable argument before the Chamber over the difference between the English version of the provision, which uses the word "taken", and the Italian, which uses the word *"espropriati"*. Both versions are authentic. Obviously there is some difference between the two versions. The word "taking" is wider and looser than *"espropriazione"*.

114. The United States argued that, however the provision is read, the result is the same in this case; which is not the same as arguing that the two versions mean the same thing; and if one looks at the acts and conduct which the Applicant claims to constitute a violation of Article V, paragraph 2, one finds this claim expressed in the following terms. In the contention of the United States, both the Respondent's act of requisitioning the ELSI plant and its subsequent acts in acquiring the plant, assets, and work in progress, singly and in combination, constitute takings of property without due process of law and just compensation. The requisition in itself is, in the view of the United States, such a taking, because Italy physically seized ELSI's property with the object and effect of ending Raytheon and Machlett's control and management, in order to prevent them from conducting the planned liquidation; and according to the United States, in international law a "taking" is generally recognized as including not merely outright expropriation of property, but also unreasonable interference with its use, enjoyment or disposal. Secondly, the United States claims that the Respondent, after the requisition and before the Prefect ruled on the administrative appeal, proceeded through ELTEL to acquire the ELSI plant and assets for less than fair market value. The matter was summed up by counsel at the hearings as follows:

> "The requisition and the delay in overturning the requisition not only interfered with Raytheon and Machlett's management and control of ELSI, not only impaired Raytheon and Machlett's legally acquired interests in ELSI, but also resulted in what can only be described as the taking of the property."

115. The specific United States allegations of interference by the Italian Government with the ELSI bankruptcy proceedings may be summarized as follows. The object in view is said to have been to secure ELSI's facilities for IRI, on the terms and at the below-market price which IRI desired, while responding to the political pressure brought by ELSI's former workers. Having requisitioned the plant and caused ELSI's bank-

ruptcy, the Government of Italy discouraged private bidders at the auctions held to dispose of ELSI's assets, by informing the public at large that the Government would be taking over ELSI's facilities. While proceeding with plans to take over ELSI, for example by negotiating agreements for rehiring the staff, IRI is said to have "boycotted" the first three auctions of the assets, at which the terms set by the bankruptcy judge were not to its liking. ELTEL proposed to the trustee in bankruptcy that it be permitted to lease the plant, and to purchase the work in progress, and this was agreed to by the bankruptcy authorities on terms which, it is claimed, were adverse to ELSI's interests, both because the sums involved were too low and because ELTEL was placed in a position to dictate the terms of the final sale. At the final auction, ELTEL, already in possession under the lease, acquired the plant and related equipment for 4,000 million lire, the figure reported in the press to have been previously agreed on between IRI and the Italian authorities. As a result of the arrangements made with the bankruptcy authorities for a piecemeal take-over, the total amount received for ELSI's assets was slightly over 4,000 million lire, as compared with the company's book valuation of over 12,000 million lire.

116. Thus, the charge based on the combination of the requisition and subsequent acts is really that the requisition was the beginning of a process that led to the acquisition of the bulk of the assets of ELSI (which was wholly owned by Raytheon and Machlett) for far less than market value. That is a charge, not of mere temporary taking — though the United States also contended that a temporary requisition can constitute an indirect taking — but of a process by which title to ELSI's assets itself was in the end transferred. So far as the requisition is concerned, counsel put the United States argument this way:

> "the fact that the requisition was for an extendable six-month period does not make this any less of an expropriation of interests in property, given the fact that the requisition drove ELSI into bankruptcy".

What is thus alleged by the Applicant, if not an overt expropriation, might be regarded as a disguised expropriation; because, at the end of the process, it is indeed title to property itself that is at stake. The argument is that if a series of acts or omissions of the Italian authorities had the end result, whether intended or not and whether the result of collusion or not, of causing United States property in Italy to be ultimately transferred into the ownership of Italy, without proper compensation, there would be a violation of Article V, paragraph 2, of the FCN Treaty.

117. It must immediately be added that the United States, in the course of the oral proceedings, in response to an Italian assertion that it was attempting to establish a conspiracy to bring about the change of ownership, made it very clear that this part of its case did not depend upon, or in any way involve, any allegation that the Italian authorities were parties to such a conspiracy. The United States stated formally that it "has never argued and does not now argue that the acts and omissions of the Respondent that violated the Treaty amount to a 'conspiracy'". Moreover, it was added that whilst the relief sought was "based on the acts and omissions of the Respondent's agents and officials at the federal and local levels (including IRI), without any allegation that these officials were working in conspiracy", the United States did not "speculate as to why these agents and officials of the Respondent acted in the manner they did"; or, as the United States Agent put it in his argument:

> "These acts and omissions constituted Treaty violations ... whether or not the Italian Government entities involved knew of each other's actions, and whether or not they were acting in concert or at cross purposes."

118. The argument that there was a "taking" involving transfer of title gives rise to a number of difficulties. Even assuming, though without deciding, that *"espropriazione"* might be wide enough to include not only formal and open expropriation, but also a disguised expropriation, there would still be a question whether the paragraph can be extended to include even a "taking" of an Italian corporation in Italy, of which, strictly speaking, Raytheon and Machlett only held the shares. This, however, is where account must also be taken of the first paragraph of the Protocol appended to the FCN Treaty, which provides:

> "1. The provisions of paragraph 2 of Article V, providing for the payment of compensation, shall extend to interests held directly or indirectly *[si estenderanno ai diritti spettanti direttamente od indirettamente ai cittadini . . .]* by nationals, corporations and associations of either High Contracting Party in property which is taken within the territories of the other High Contracting Party."

The English text of this provision suggests that it was designed precisely to resolve the doubts just described. The interests of shareholders in the assets of a company, and in their residuary value on liquidation, would appear to fall in the category of the "interests" to be protected by Article V, paragraph 2, and the Protocol. Italy has however drawn attention to the use in the Italian text — which is equally authentic — of the narrower term

"diritti" (rights), and has argued that, on the basis of the principle expressed in Article 33, paragraph 4, of the Vienna Convention on the Law of Treaties, the correct interpretation of the Protocol must be in the more restrictive sense of the Italian text.

119. In the view of the Chamber, however, neither this question of interpretation of the two texts of the Protocol, nor the questions raised as to the possibilities of disguised expropriation or of a "taking" amounting ultimately to expropriation, have to be resolved in the present case, because it is simply not possible to say that the ultimate result was the consequence of the acts or omissions of the Italian authorities, yet at the same time to ignore the most important factor, namely ELSI's financial situation, and the consequent decision of its shareholders to close the plant and put an end to the company's activities. As explained above (paragraphs 96-98), the municipal courts considered that ELSI, if not already insolvent in Italian law before the requisition, was in so precarious a state that bankruptcy was inevitable. The Chamber cannot regard any of the acts complained of which occurred subsequent to the bankruptcy as breaches of Article V, paragraph 2, in the absence of any evidence of collusion, which is now no longer even alleged. Even if it were possible to see the requisition as having been designed to bring about bankruptcy, as a step towards disguised expropriation, then, if ELSI was already under an obligation to file a petition of bankruptcy, or in such a financial state that such a petition could not be long delayed, the requisition was an act of supererogation. Furthermore this requisition, independently of the motives which allegedly inspired it, being by its terms for a limited period, and liable to be overturned by administrative appeal, could not, in the Chamber's view, amount to a "taking" contrary to Article V unless it constituted a significant deprivation of Raytheon and Machlett's interest in ELSI's plant; as might have been the case if, while ELSI remained solvent, the requisition had been extended and the hearing of the administrative appeal delayed. In fact the bankruptcy of ELSI transformed the situation less than a month after the requisition. The requisition could therefore only be regarded as significant for this purpose if it caused or triggered the bankruptcy. This is precisely the proposition which is irreconcilable with the findings of the municipal courts, and with the Chamber's conclusions in paragraphs 99-100 above.

* *

120. Article I of the Supplementary Agreement to the FCN Treaty, which confers rights not qualified by national or most-favoured-nation standards, provides as follows:

"The nationals, corporations and associations of either High Contracting Party shall not be subjected to arbitrary or discriminatory measures within the territories of the other High Contracting Party resulting particularly in: *(a)* preventing their effective control and management of enterprises which they have been permitted to establish or acquire therein; or, *(b)* impairing their other legally acquired rights and interests in such enterprises or in the investments which they have made, whether in the form of funds (loans, shares or otherwise), materials, equipment, services, processes, patents, techniques or otherwise. Each High Contracting Party undertakes not to discriminate against nationals, corporations and associations of the other High Contracting Party as to their obtaining under normal terms the capital, manufacturing processes, skills and technology which may be needed for economic development."

The United States bases its claims upon allegations that measures were taken which were both "arbitrary" and "discriminatory" in the sense of this text.

121. The Applicant pressed strongly the claim that the requisition was an arbitrary or discriminatory act which violated both the *"(a)"* and the *"(b)"* clauses of the Article. The requisition, it is said, clearly prevented Raytheon and Machlett from exercising their control and management of ELSI and also resulted in an impairment of their legally acquired rights and interests in ELSI, inasmuch as it prevented the voluntary liquidation of ELSI and caused it to file for bankruptcy. To the claim as it is presented in those terms, however, the Chamber has already given its answer: the absence of a sufficiently palpable connection between the effects of the requisition and the failure of ELSI to carry out its planned orderly liquidation (paragraph 101 above). Accordingly, it cannot be said that it was the requisition *per se* which either prevented Raytheon's effective control and management of ELSI, or which resulted in impairing legally acquired rights, in the sense of the clauses called *"(a)"* and *"(b)"* in Article I of the Supplementary Agreement. Yet, although this is an answer to the claim as it is presented in terms of those clauses of Article I, it is not the end of the matter. The effect of the word "particularly", introducing the clauses *"(a)"* and *"(b)"*, suggests that the prohibition of arbitrary (and discriminatory) acts is not confined to those resulting in the situations described in *"(a)"* and *"(b)"*, but is in effect a prohibition of such acts whether or not they produce such results. It is necessary, therefore, to examine whether the requisition was, or was not, an arbitrary or discriminatory act of itself.

122. The allegation of the United States that Raytheon and Machlett were subjected to "discriminatory" measures can be dealt with shortly. It is common ground that the requisition order was not made because of the nationality of the shareholders; there have been many cases of requisition

orders made in similar circumstances against wholly Italian-owned companies. But the United States claims that there was "discrimination" in favour of IRI, an entity controlled by Italy; and this was, in the view of the United States, contrary to the FCN Treaty and Supplementary Agreement. It is contended that the interests of IRI were directly contrary to those of Raytheon and Machlett, and the Italian Government intervened to advance its own commercial interests at the latter's expense. However, the requisition order in itself did not serve any interest of IRI; it is only if the requisition is regarded as a step in a process destined to transfer ELSI's assets to IRI that the factual situation would afford any basis for the argument now under examination. As indicated above, the United States stated formally during the oral proceedings that it was not arguing that the acts and omissions complained of amount to a "conspiracy", and did not speculate as to why the relevant agents and officials of the Respondent acted as they did (see paragraph 117 above). There is no sufficient evidence before the Chamber to support the suggestion that there was a plan to favour IRI at the expense of ELSI, and the claim of "discriminatory measures" in the sense of Article I of the Supplementary Agreement must therefore be rejected.

123. In order to show that the requisition order was an "arbitrary" act in the sense of the Supplementary Agreement to the FCN Treaty, the Applicant has relied *(inter alia)* upon the status of that order in Italian law. It contends that the requisition "was precisely the sort of arbitrary action which was prohibited" by Article I of the Supplementary Agreement, in that "under both the Treaty and Italian law, the requisition was unreasonable and improperly motivated"; it was "found to be illegal under Italian domestic law for precisely this reason". Relying on its own English translation of the decision of the Prefect of Palermo of 22 August 1969, the Applicant concludes that the Prefect found that the order was "destitute of any juridical cause which may justify it or make it enforceable". Italy first contended that the word "or" in the translation of this passage should be replaced by "and", and subsequently put forward the alternative translation that "the order, generically speaking, lacks the proper motivation that could justify it and make it effective". It may be noted in passing that when ELSI, immediately after the making of the requisition order, formally invited the Mayor of Palermo to revoke the order, it referred to it throughout as "the said illegal and arbitrary order" *("detto illegale ed arbitrario provvedimento")*; but the appeal submitted to the Prefect, while citing numerous legal grounds for annulment, including *"eccesso di potere per sviamento del fine"* ("excess of power by deviation from the purpose"), contained no claim that the order had been "arbitrary". It is therefore appropriate for the Chamber to examine the legal grounds given by the Prefect of Palermo for his decision, as well as what was said by the Court of Appeal of Palermo on the legal impact of the Prefect's decision on the requisition order, and consider whether the findings of the

Prefect or of the Court of Appeal are equivalent to, or suggest, a conclusion that the requisition was an "arbitrary" action.

124. Yet it must be borne in mind that the fact that an act of a public authority may have been unlawful in municipal law does not necessarily mean that that act was unlawful in international law, as a breach of treaty or otherwise. A finding of the local courts that an act was unlawful may well be relevant to an argument that it was also arbitrary; but by itself, and without more, unlawfulness cannot be said to amount to arbitrariness. It would be absurd if measures later quashed by higher authority or a superior court could, for that reason, be said to have been arbitrary in the sense of international law. To identify arbitrariness with mere unlawfulness would be to deprive it of any useful meaning in its own right. Nor does it follow from a finding by a municipal court that an act was unjustified, or unreasonable, or arbitrary, that that act is necessarily to be classed as arbitrary in international law, though the qualification given to the impugned act by a municipal authority may be a valuable indication.

125. The principal passage from the decision of the Prefect which is relevant here has already been quoted (paragraph 75 above), but it is convenient to set it out again here:

> *"Non v'ha dubbio che anche se possono considerarsi, in linea del tutto teorica, sussistenti, nella fattispecie, gli estremi della grave necessità pubblica e della contingibilità ed urgenza che determinarono l'adozione del provvedimento, il fine cui tendeva la requisizione non poteva trovare pratica realizzazione con il provvedimento stesso, tanto è vero che nessuna ripresa di attività dell'azienda vi è stata a seguito della requisizione, nè avrebbe potuto esserci. Manca, pertanto, nel provvedimento, genericamente, la causa giuridica che possa giustificarlo e renderlo operante."*

The differing translations offered by the Parties of the sentence upon which the Applicant places considerable reliance are set out in paragraph 123 above. In the Chamber's translation, the passage reads:

> "There is no doubt that, even though, from the purely theoretical standpoint, the conditions of grave public necessity and of unforeseen urgency warranting adoption of the measure may be considered to exist in the case in point, the intended purpose of the requisition could not in practice be achieved by the order itself, since in fact there was no resumption of the company's activity following the requisition, nor could there have been such resumption. The order therefore

lacks, generically, the juridical cause which might justify it and make it operative."

126. In support of this conclusion, the Prefect explained that the Mayor had believed that he could deal with the situation by means of a requisition, without appreciating that

> "the state of the company as a result of circumstances of a functional-economic and market nature, was such as not to permit of the continuation of its activity".

He also emphasized the shutdown of the plant and the protest actions of the staff, and the fact that the requisition had not succeeded in preserving public order. Finally the Prefect also observed that the order had been adopted

> *"anche sotto l'influsso delle pressioni e dei rilievi formulati dalla stampa cittadina, per cui è da ritenere che il Sindaco, anche per sottrarvisi e dimostrare l'intendimento della Pubblica Amministrazione di intervenire in qualche modo, addivenne alla requisizione quale provvedimento diretto più che altro a porre in evidenza la sua intenzione di affrontare comunque il problema".*

In the translation of the Prefect's decision supplied by the Applicant:

> "also under the influence of the pressure created by, and of the remarks made by the local press; therefore we have to hold that the Mayor, also in order to get out of the above and to show the intent of the Public Administration to intervene in one way or another, issued the order of requisition as a measure mainly directed to emphasize his intent to face the problem in some way [or, as quoted in the judgment of the Court of Appeal of Palermo, in the translation supplied by the Applicant: 'his intention to tackle the problem just the same']".

It was of course understandable that the Mayor, as a public official, should have made his order, in some measure, as a response to local public pressures; and the Chamber does not see, in this passage of the Prefect's decision, any ground on which it might be suggested that the order was therefore arbitrary.

127. In the action brought by the trustee in bankruptcy for damages on account of the requisition, the Court of Palermo and subsequently the Court of Appeal of Palermo had to consider the legal significance of the decision of the Prefect. The Court of Palermo accepted the argument of the respondent administration that *"il provvedimento prefettizio è sostanzialmente di revoca dell'atto richiamato essendo stati ritenuti irrealizzabili gli scopi cui lo stesso miravano"*, i.e., that "the Prefect's order is in substance a revocation of the act in question, the objectives which were contemplated by it having been adjudged to have been impossible to achieve". When the matter came before the Court of Appeal, it observed that this argument was contrary to the argument of the trustee in bankruptcy *"che ravvisa in*

detto decreto una dichiarazione di illegittimità del provvedimento di requisizione", i.e., "who regarded the [Prefect's] decree as a declaration of the unlawfulness of the requisition order". The Court of Appeal understood the lower court as meaning simply that *"i vizi del provvedimento di requisizione, rilevati dal Prefetto, sono vizi di merito e non vizi di legittimità"*, i.e., "the defects found by the Prefect in the requisition order were defects in respect of the merits and not defects in respect of lawfulness"; it found that this finding was incorrect because the reasoning of the Prefect was, in its view, a clear finding of *"un tipico caso di eccesso di potere, che è, come è noto, un vizio di legittimità dell'atto amministrativo"*, i.e., "a typical case of excess of power, which is of course a defect in respect of lawfulness of an administrative act". Having reached this conclusion, the Court of Appeal refers later in its judgment to the requisition as having been "unlawful" *("illecito")*. The analysis of the Prefect's decision as a finding of excess of power, with the result that the order was subject to a defect of lawfulness does not, in the Chamber's view, necessarily and in itself signify any view by the Prefect, or by the Court of Appeal of Palermo, that the Mayor's act was unreasonable or arbitrary.

128. Arbitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law. This idea was expressed by the Court in the *Asylum* case, when it spoke of "arbitrary action" being "substituted for the rule of law" (*Asylum, Judgment, I.C.J. Reports 1950*, p. 284). It is a wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety. Nothing in the decision of the Prefect, or in the judgment of the Court of Appeal of Palermo, conveys any indication that the requisition order of the Mayor was to be regarded in that light.

129. The United States argument is not of course based solely on the findings of the Prefect or of the local courts. United States counsel felt able to describe the requisition generally as being an "unreasonable or capricious exercise of authority". Yet one must remember the situation in Palermo at the moment of the requisition, with the threatened sudden unemployment of some 800 workers at one factory. It cannot be said to have been unreasonable or merely capricious for the Mayor to seek to use the powers conferred on him by the law in an attempt to do something about a difficult and distressing situation. Moreover, if one looks at the requisition order itself, one finds an instrument which in its terms recites not only the reasons for its being made but also the provisions of the law on which it is based: one finds that, although later annulled by the Prefect because "the intended purpose of the requisition could not in practice be achieved by the order itself" (paragraph 125 above), it was nonetheless within the competence of the Mayor of Palermo, according to the very provisions of the law cited in it; one finds the Court of Appeal of Palermo, which did not differ from the conclusion that the requisition was *intra vires*, ruling that it was unlawful as falling into the recognized category of administrative law of acts of *"eccesso di potere"*. Furthermore, here was an act belong-

ing to a category of public acts from which appeal on juridical grounds was provided in law (and indeed in the event used, not without success). Thus, the Mayor's order was consciously made in the context of an operating system of law and of appropriate remedies of appeal, and treated as such by the superior administrative authority and the local courts. These are not at all the marks of an "arbitrary" act.

130. The Chamber does not, therefore, see in the requisition a measure which could reasonably be said to earn the qualification "arbitrary", as it is employed in Article I of the Supplementary Agreement. Accordingly, there was no violation of that Article.

* *

131. Finally, the United States claims that there has been a violation by Italy of Article VII of the FCN Treaty. This long and elaborately drafted Article, in four paragraphs, is principally concerned with ensuring the right "to acquire, own and dispose of immovable property or interests therein within the territories of the other High Contracting Party". The full text is as follows:

> "1. The nationals, corporations and associations of either High Contracting Party shall be permitted to acquire, own and dispose of immovable property or interests therein within the territories of the other High Contracting Party upon the following terms:
>
> *(a)* in the case of nationals, corporations and associations of the Italian Republic, the right to acquire, own and dispose of such property and interests shall be dependent upon the laws and regulations which are or may hereafter be in force within the state, territory or possession of the United States of America wherein such property or interests are situated; and
>
> *(b)* in the case of nationals, corporations and associations of the United States of America, the right to acquire, own and dispose of such property and interests shall be upon terms no less favorable than those which are or may hereafter be accorded by the state, territory or possession of the United States of America in which such national is domiciled, or under the laws of which such corporation or association is created or organized, to nationals, corporations and associations of the Italian Republic; provided that the Italian Republic shall not be obligated to accord to nationals, corporations and associations of the United States of America rights in this connection more extensive than those which are or may hereafter be accorded within the territories of such Republic to nationals, corporations and associations of such Republic.

2. If a national, corporation or association of either High Contracting Party, whether or not resident and whether or not engaged in business or other activities within the territories of the other High Contracting Party, is on account of alienage prevented by the applicable laws and regulations within such territories from succeeding as devisee, or as heir in the case of a national, to immovable property situated therein, or to interests in such property, then such national, corporation or association shall be allowed a term of three years in which to sell or otherwise dispose of such property or interests, this term to be reasonably prolonged if circumstances render it necessary. The transmission or receipt of such property or interests shall be exempt from the payment of any estate, succession, probate or administrative taxes or charges higher than those now or hereafter imposed in like cases of nationals, corporations or associations of the High Contracting Party in whose territory the property is or the interests therein are situated.

3. The nationals of either High Contracting Party shall have full power to dispose of personal property of every kind within the territories of the other High Contracting Party, by testament, donation or otherwise and their heirs, legatees or donees, being persons of whatever nationality or corporations or associations wherever created or organized, whether resident or non-resident and whether or not engaged in business within the territories of the High Contracting Party where such property is situated, shall succeed to such property, and shall themselves or by their agents be permitted to take possession thereof, and to retain or dispose of it at their pleasure. Such disposition, succession and retention shall be subject to the provisions of Article IX and exempt from any other charges higher, and from any restrictions more burdensome, than those applicable in like cases of nationals, corporations and associations of such other High Contracting Party. The nationals, corporations and associations of either High Contracting Party, shall be permitted to succeed, as heirs, legatees and donees, to personal property of every kind within the territories of the other High Contracting Party, left or given to them by nationals of either High Contracting Party or by nationals of any third country, and shall themselves or by their agents be permitted to take possession thereof, and to retain or dispose of it at their pleasure. Such disposition, succession and retention shall be subject to the provisions of Article IX and exempt from any other charges, and from any restrictions, other or higher than those applicable in like cases of nationals, corporations and associations of such other High Contracting Party. Nothing in this paragraph shall be construed to affect the laws and regulations of either High Contracting Party prohibiting or restricting the direct or indirect ownership by

aliens or foreign corporations and associations of the shares in, or instruments of indebtedness of, corporations and associations of such High Contracting Party carrying on particular types of activities.

4. The nationals, corporations and associations of either High Contracting Party shall, subject to the exceptions in paragraph 3 of Article IX, receive treatment in respect of all matters which relate to the acquisition, ownership, lease, possession or disposition of personal property, no less favorable than the treatment which is or may hereafter be accorded to nationals, corporations and associations of any third country."

The Italian text of the opening sentence of paragraph 1 is as follows:

"I cittadini e le persone giuridiche ed associazioni di ciascuna Alta Parte Contraente avranno facoltà di acquistare, possedere e disporre di beni immobili o di altri diritti reali nei territori dell'altra Alta Parte Contraente alle seguenti condizioni . . ."

132. It was objected by Italy that this Article does not apply at all to Raytheon and Machlett because their own property rights *("diritti reali")* were limited to shares in ELSI, and the immovable property in question (the plant in Palermo) was owned by ELSI, an Italian company. The United States contended that "immovable property or interests therein" is a phrase sufficiently broad to include indirect ownership of property rights held through a subsidiary that is not a United States corporation. The argument turned to a considerable extent on the difference in meaning between the English, "interests" and the Italian, *"diritti reali"*. "Interest" in English no doubt has several possible meanings. But since it is in English usage a term commonly used to denote different kinds of rights in land (for example rights such as charges, or easements, and many kinds of "future interests"), it is possible to interpret the English and Italian versions of Article VII as meaning much the same thing; especially as the clause in question is in any event limited to immovable property. The Chamber however has some sympathy with the contention of the United States, as being more in accord with the general purpose of the FCN Treaty. The United States argument is further that Raytheon and Machlett, being the owners of all the shares, were in practice the persons who alone could decide (before the bankruptcy), whether to dispose of the immovable property of the company; accordingly, if the requisition

did, by triggering the bankruptcy, deprive ELSI of the possibility of disposing of its immovable property, it was really Raytheon and Machlett who were deprived; and allegedly in violation of Article VII.

133. There are however problems in any attempt to apply the provisions of Article VII to the actual facts of this case. First, the protection which paragraph 1 of Article VII affords to this group of rights is not unqualified. The qualification designated *"(a)"* refers to the rights enjoyed by Italian nationals in the territory of the United States of America, which in effect simply subjects Italian nationals to the municipal laws in the United States, and does not concern us. Qualification *"(b)"* does, for this applies to the rights enjoyed by United States nationals in the territory of the Republic of Italy. It is a convoluted qualification because it lays down alternative standards, which standards are themselves then both qualified by the same proviso. The terms governing the rights are to be no less favourable than those which are or may hereafter be accorded by the "state, territory or possession of the United States of America in which such national is domiciled, or under the laws of which such corporation or association is created or organized" — which in the case of Raytheon is the State of Delaware and in the case of Machlett the State of Connecticut — "to nationals, corporations and associations of the Italian Republic". The proviso is:

> "that the Italian Republic shall not be obligated to accord to nationals, corporations and associations of the United States of America rights in this connection more extensive than those which are or may hereafter be accorded within the territories of such Republic to nationals, corporations and associations of such Republic".

134. The Chamber has thus to make the somewhat elaborate juridical calculus which this provision in the FCN Treaty appears to demand for its application. No very cogent evidence was put before the Chamber to show that the application of Italian law in this matter was less favourable than the treatment accorded by Italy to its own nationals, corporations and associations, in Italy. Indeed it appeared that, particularly during the troubled times of 1968, requisitions of Italian companies by the local Mayors had happened rather frequently. The claim must therefore be taken to be that ELSI was given less favourable treatment than might have been enjoyed by an Italian company under the laws of Delaware and Connecticut in similar circumstances. The United States drew attention to texts showing that

> "Under the laws of both Delaware and Connecticut, corporations may be dissolved and their assets sold pursuant to determinations by their boards of directors and shareholders",

and that if those States were to take the immovable property of a corporation for a lawful public use, they would have to make compensation; Italy has not disputed these legislative provisions.

135. Secondly, however, even so there remains precisely the same difficulty as in trying to apply Article III, paragraph 2, of the FCN Treaty: what really deprived Raytheon and Machlett, as shareholders, of their right to dispose of ELSI's real property, was not the requisition but the precarious financial state of ELSI, ultimately leading inescapably to bankruptcy. In bankruptcy the right to dispose of the property of a corporation no longer belongs even to the company, but to the trustee acting for it; and the Chamber has already decided that ELSI was on a course to bankruptcy even before the requisition. The Chamber therefore does not find that Article VII of the FCN Treaty has been violated.

* *

136. Having found that the Respondent has not violated the FCN Treaty in the manner asserted by the Applicant, it follows that the Chamber rejects also the claim for reparation made in the submissions of the Applicant.

* * *

137. For these reasons,

THE CHAMBER,

(1) Unanimously,

Rejects the objection presented by the Italian Republic to the admissibility of the Application filed in this case by the United States of America on 6 February 1987;

(2) By four votes to one,

Finds that the Italian Republic has not committed any of the breaches, alleged in the said Application, of the Treaty of Friendship, Commerce and Navigation between the Parties signed at Rome on 2 February 1948, or of the Agreement Supplementing that Treaty signed by the Parties at Washington on 26 September 1951.

IN FAVOUR: *President* Ruda; *Judges* Oda, Ago and Sir Robert Jennings;
AGAINST: *Judge* Schwebel.

(3) By four votes to one,

Rejects, accordingly, the claim for reparation made against the Republic of Italy by the United States of America.

IN FAVOUR: *President* Ruda; *Judges* Oda, Ago and Sir Robert Jennings;
AGAINST: *Judge* Schwebel.

Done in English and in French, the English text being authoritative, at the Peace Palace, The Hague, this twentieth day of July, one thousand nine hundred and eighty-nine, in three copies, one of which will be placed in the archives of the Court and the others transmitted to the Government of the United States of America and the Government of the Republic of Italy, respectively.

(Signed) José María RUDA,
President.

(Signed) Eduardo VALENCIA-OSPINA,
Registrar.

Judge ODA appends a separate opinion to the Judgment of the Chamber.

Judge SCHWEBEL appends a dissenting opinion to the Judgment of the Chamber.

(Initialled) J.M.R.
(Initialled) E.V.O.