

Standard on Effective Control of an applicant or Contractor: Determination and Evidence

1. This Standard shall be applied by the Authority when interpreting and applying Regulations 5, 6, 13, 21, 24, and 24.bis.

Effective Control

2. Effective Control is defined in the Exploitation Regulations as follows:

“**Effective Control**” of an applicant or Contractor means the ability to secure that the operational conduct, compliance, and procedures of the applicant or Contractor pertaining to activities under an Exploitation Contract in the Area are conducted in accordance with the instructions or directions of one of the following:

- (a) a State Party of which an applicant or Contractor is a national (“State of Nationality”);
- (b) a State Party which is not the State of Nationality (“Another State”); or
- (c) nationals of a State Party which is not the State of Nationality (“Nationals”).

3. The Legal and Technical Commission (LTC) is the organ responsible for determining Effective Control.

4. For the purposes of this Standard:

- i. “effective controller” refers to the entity determined to have Effective Control over an applicant or Contractor by the LTC;
- ii. “potential effective controllers” refers to the entities in paragraph 2(a), 2(b), and 2(c), prior to the LTC’s determination of Effective Control;
- iii. “instructions or directions” refer to those regarding the operational conduct, compliance, and procedures of the Applicant or Contractor pertaining to activities in the Area under an Exploitation Contract.

5. An applicant or Contractor can only be effectively controlled by one effective controller at the same point in time.

Instructions or directions

6. “Instructions or directions” may be exercised differently by the potential effective controllers.

7. For a State of Nationality, instructions or directions can be effected through

- i. a legally binding instrument (for example under a contract, license, undertaking, assignment or cessation deed) between itself and another potential effective controller, that grants it the legal ability to issue instructions or directions over and above those of another potential effective controller; or
- ii. measures provided for in its domestic laws, regulations or administrative measures that grant it the legal ability to issue instructions or directions over and above those of another potential effective controller, provided that those measures go beyond ensuring, within the State of Nationality’s legal system, that an applicant or Contractor so sponsored shall carry out activities in the Area in conformity with the terms of its contract and its obligations under the

Convention, as referred to in Article 4(4) of Annex III to the Convention.

8. In order to be considered to have Effective Control, a State of Nationality must have state organs (such as administrative bodies) in operation with the factual ability to effect instructions or directions.

9. For Another State or Nationals, “instructions or directions” can be effected through direct or indirect legal rights in the applicant or Contractor, provided that these legal rights result in the factual ability to direct or determine the applicant’s or Contractor’s operational conduct, compliance, and procedures pertaining to activities under an Exploitation Contract in the Area, without a State of Nationality being able to issue instructions or directions over and above those instructions or directions.

10. For the avoidance of doubt, no potential effective controller requires the ability to issue instructions or directions beyond those regarding the operational conduct, compliance, and procedures of the Applicant or Contractor pertaining to activities in the Area under an Exploitation Contract to be considered to have Effective Control. In particular, they are not required to have the ability to issue instructions or directions in relation to all corporate decisions (i.e. those that are exclusively financial in nature)

11. The following information shall, as applicable, be provided by applicants and Contractors to the LTC for its assessment in accordance with this Standard:

- a. legal instruments between a potential effective controller and an applicant or Contractor, for example under a contract, license, undertaking, assignment or cessation deed;
- b. legal instruments between a potential effective controller and another potential effective controller pertaining to an applicant or Contractor, for example under a contract, license, undertaking, assignment or cessation deed;
- c. measures provided for in domestic laws, regulations or administrative measures of a State;
- d. information relating to relevant State organs;
- e. constitutional documents of the applicant or Contractor, such as articles of association or articles of incorporation and partnership agreements;
- f. information on legal ownership (shares or otherwise) of the applicant or Contractor, by providing the shareholder registry and the percentage ownership;
- g. information on any juridical persons or States involved in the chain of ownership of the applicant or Contractor;
- h. information on voting rights, economic rights, convertible stock or outstanding debt that is convertible into voting equity which any person or State holds in respect of the applicant or Contractor; and
- i. any other information the Commission deems relevant to an assessment of Effective Control in respect of an applicant or Contractor.

12. The LTC shall review the information received under paragraph 12 in the following order, and take all of the following steps:

- a. assess whether a State of Nationality is party to a legal instrument described under paragraph 11(a) or (b);
- b. assess whether a State of Nationality has any measures described in paragraph 11(c) in place;
- c. assess the documents listed at paragraph 11(e) through 11(i) to determine whether a potential

effective controller has the ability to secure that the operational conduct, compliance, and procedures of the applicant or Contractor pertaining to activities under an Exploitation Contract in the Area are conducted in accordance with its instructions or directions;

- d. assess whether any legal instruments described under 11(a) or 11(b), or any measures described in paragraph 11(c), mean that the State of Nationality's instructions or directions, by operation of law, should be adhered to by the applicant or Contractor over and above any instructions or directions that any other potential effective controller could issue pursuant to a right originating from any documents listed at 11(e) through 11(i); and
- e. in the event of either (a) or (b) above, assess whether the State of Nationality has state organs described in paragraph 11(d) in operation with the factual ability to effect instructions or directions.

13. In assessing whether Another State or its Nationals has direct or indirect legal rights in the applicant or Contractor, consideration shall be given to ownership interests elaborated below and ways to exercise control over a juridical person that exist within the jurisdiction where such applicant or Contractor is incorporated, pursuant to commercial and administrative law (other than through measures taken in the ordinary course of regulating a natural or juridical person).

- i. In assessing juridical persons with shares, only the following shall be considered to constitute legal rights in the applicant or Contractor for the purposes of paragraph [9] of this Standard:

Voting rights: Rights of shareholders to participate in the decision-making of the company. Different classes of shares may give certain shareholders more control than others, for example through differential voting rights. Thus, even a shareholder that falls well below a specified threshold may in fact give that minority shareholder control over the company.

Rights to appoint and / or remove the majority of directors and / or senior management: The legal right to appoint and / or remove the majority of the board of directors and / or senior management.

The right of minority shareholders or certain shareholders to appoint one representative to senior management does not by itself confer control over a juridical person.

Control through debt instruments: Control can also be exercised through debt instruments or other financing arrangements, for example where a lender or creditor can control a juridical person via the provisions of the lending agreement (such as debt that is convertible into voting equity), or by a third party that can otherwise influence a shareholder by means of a financial or other relationship.

However, a bank providing financing to a juridical person will rarely be considered as exercising control over the juridical person by the act *per se*.

Control through positions held within a juridical person: Natural persons who exercise substantial control over a juridical person and are responsible for strategic decisions that fundamentally affect the business practices or general direction of the juridical person may be considered to control the legal entity under certain limited circumstances, depending on the juridical person and the laws of the jurisdiction of which the juridical person is a national.

Control through informal means: These shall only be considered where an actor possesses, in substance, rights equivalent to legal rights even if those rights are not expressed formally in written instruments.

Such informal means shall not include:

- personal, family or professional relationships absent specific legal rights;
- customary commercial interactions;
- economic dependence absent specific rights to direct activities in the Area, or;
- mere use, enjoyment, or benefit from corporate assets.

- ii. Attention shall also be paid to the type and form of juridical persons. For an applicant or Contractor in any of the following forms, the factors in paragraph 14(i) of this Standard may, if applicable, be considered to constitute legal rights in the applicant or Contractor, but so too may other factors as follows:

Companies without shares: Juridical persons that do not issue shares, including non-stock companies and companies limited by guarantee, will not be captured by any ownership threshold expressed in share ownership. These entities would require an alternative approach to determination of ownership interests.

Partnerships: Limited and unlimited liability partnerships have legal personality distinct from their partners, but in some jurisdictions, they do not have shares and are thus not captured by any share threshold.

In the absence of a share threshold, an individual can have control over a partnership if they have the right to exercise significant influence over the running of the activities of the partnership. This could include, for example, the right to appoint or remove any partner, to direct or veto the investment decisions, profit share or capital returns of the partnership's funds or assets, to direct amendments to the partnership's constitutional documents (e.g., the partnership agreement) or to dissolve or convert the partnership.

Foundations: A variety of other juridical persons have legal personality but are not juridical persons and do not have shares, so will not be captured by any share threshold. This requires an alternative approach to determination of control. For example, foundations have no owners and are controlled by a board.

Where foundations are similar to trusts, individuals holding the positions of founders, beneficiaries and members of the management may be considered to exercise control over the foundation.

Furthermore, an individual can have control if they exercise significant influence over the running of the activities of the foundation. This could include, for example, the right to appoint or remove any of the board members, to direct or veto the distribution of the foundation funds or assets or its investment decisions, to wind up or convert the foundation.

[Note to draft: Council would need to have a conceptual discussion about the question as to the extent to which (i) parent companies or (ii) natural persons with control over a national which, in turn, Effectively Controls an applicant or Contractor should be taken into account in the overall assessment of Effective Control.]