1. INTRODUCTION

Although generally regarded as being the most critical element in international arbitration and claims practice relating to the nationalization of foreign-owned assets, the question of reparation for loss arising from either 'direct' or 'indirect takings' by a host State remains shrouded in controversy.[1] The requirement for a State to pay compensation or damages for economic loss sustained by

[1]- M. SORNARAJAH, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT, (2010), at 412; for a discussion of the international law on nationalization generally, Jeménez de Aréchaga, International Responsibility, in MAX SØRENSON (ED), MANUAL OF PUBLIC INTERNATIONAL LAW 533 (1968); Edwin Bourchard, "The Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreign Nationals", 20 AM. J. INT'L L 738 (1926); IAN BROWNLIE, SYSTEM OF THE LAW OF NATIONS: STATE RESPONSIBILITY, PART 1 (1983); L. Goldie, "International Responsibility and the Expropriation of Property", 12 INT'L LAWYER 63 (1978); F.A. Mann, "State Contracts and State Responsibility", 54 AM. J. INT'L L 572 (1960). See, with regard to indirect nationalization, Rudolf Dolzer, "Indirect Expropriation of Alien Property", 1 ICSID REV.: FOREIGN INV. L.J. 41 (1986); Burns Weston, "Constructive Takings under International Law: A Modest Foray into the Problem of 'Creeping Expropriation'", 16 VA.J. INT'L L. 103 (1975); Catherine Yannaca-Small, "Indirect Expropriation" and the "Right to Regulate" in International Investment Law, WORKING PAPERS ON INTERNATIONAL INVESTMENT, OECD (2004), available at http://www.oecd.org/dataoecd/22/54/33776546.

foreign nationals or enterprises as a consequence of an act of nationalization or expropriation is now a generally accepted principle of international law. The right of a host State to lawfully take foreign-owned property or interference with foreign contractual interests (i.e. nationalization) is itself recognized by international law. Expropriation, on the other hand, denotes an unlawful interference by a host State with the contractual or proprietary interests of foreign nationals – i.e. a direct or indirect taking by the State which does not comply with the requirements and conditions prescribed by international law.[1] One of the key customary international law prescriptions in this area is the payment of compensation (for lawful nationalization) or damages (for unlawful takings or expropriation).[2]

[1]- See I. FOIGHEL, NATIONALIZATION: A STUDY IN THE PROTECTION OF ALIEN PROPERTY IN INTERNATIONAL LAW (1974); ZOUHAIR KRONFOL, PROTECTION OF FOREIGN INVESTMENT: A STUDY IN INTERNATIONAL LAW (1972).

[2]- C, GRAY, JUDICIAL REMEDIES IN INTERNATIONAL LAW (1990);see also S. RIPINSKY and K. WILLIAMS, DMAGES IN INTERNATIONAL LAW (2009).

It is worth noting that this distinction between compensation for lawful nationalization and damages for expropriation has not always been drawn in doctrinal writings or even in the judicial renderings of international claims tribunals on the subject of reparations for injury caused by a host State to foreign economic interests. The distinction is important not only from a conceptual or theoretical perspective, but more importantly from the practical implications which it could have on the measure and quantum of an arbitration award. We believe that the absence of this critical distinction has in the past contributed to the general uncertainty and lack of clarity regarding the international law on reparations for injury to foreign economic interests. Only of recent have academic writers started to expound on the theoretical and practical importance of the distinction.[1] The present article, by employing rigorous conceptual analysis, will seek to enquire

[1]- Marboe, "Compensation and Damages in International Law", J. WORLD INVEST. & TRADE, 723 (2006); see also John Y. Gotanda, "Assessing Damages in International Commercial Arbitration: A Comparison with Investment Treaty Disputes", TRANS. DISPUTE MANAGEMENT, 1 (2007).

into the normative significance of the distinction between compensation and damages in international investment law. It will further explore the potential theoretical and practical contribution of the distinction towards the finding of solutions to the contemporary legal problems of international economic law.

Our discourse in this article regarding reparations for loss or injury caused by a host State to foreign economic interests will be conducted on two premises: the first is from the viewpoint that the requirement of compensation or damages constitutes as a basic condition for nationalization is now a well established principle of international law; secondly, from the premise that international law on the subject as it currently stands offers little clarity or certainty as to the precise scope, content , legal status or normative value of some of the underlying principles governing compensation for nationalization. In stating the second premise we especially take note of the conflicting standards posited by opposing schools of thought on the subject to this day. We also take cognizance of the political controversy, intellectual cleavage of opinion and normative uncertainty which have been the defining characteristics and historical

hallmarks of this area of international law.[1] We equally take into account the fact that long term solutions to the contemporary problems of international law in the area of international economic relations are not to be found in the advancement of one ideology over an opposing one. A sustainable solution lies rather in the articulation and conception of a legal regime which accords equal importance and significance to the interest of all stakeholders - capital exporting and capital importing nation alike.

To be sustainable the international investment regime has to be founded on principles which attract universal recognition amongst the community of nations and have a reasonable degree of permanence. A sustainable regime cannot be one which is in a constant state of flux as with the current international investment regime. As recently as 2010, for instance, a prominent scholar on the subject noted that

[1]- F.V. García-Amador, A Basic Dispute: Conflicting Views on Expropriation, in J. NORTON (ED), PUBLIC INTERNATIONAL LAW AND THE FUTURE WORLD ORDER (1987): Chapter 7; S. Asante, "Traditional Concepts versus the Developmental Imperatives in Transnational Investment Law, in R. DUPUY (ED), COLLOQUIUM ON THE RIGHTS TO DEVELOPMENT AT THE INTERNATIONAL LEVEL, 352 (1979).

"*there is no clear principle as to compensation for nationalisation in international law at the present time.*"[1] One of the ultimate conclusions we draw from our current study is that the contemporary problems of international law as highlighted herein are not necessarily as intractable, elusive or unsolvable as they seem. The differences of opinion, and the sometimes discordant strands underlying the debate on compensation for nationalization, all point towards the exigency for a reformed international investment regime. This reformed system has to be based on normative certainty and much greater clarity. In this article the authors will be focusing not so much on the technical computation or calculation of damages in foreign nationalization cases, but on the question of the approach to the measurement of damages.[2]

The accepted fact of some form of recompense in international law for loss arising from nationalization, expropriation or some other form of host State interference

[1]- M. SORNARAJAH (2010), at 412.

[2]- For a comprehensive review and analysis of the various methods of quantifying damages in international arbitration, see the special issue of TRANSNATIONAL DISPUTE MANAGEMENT (No. 2), 2007.

with foreign economic interests is well established in international law (as seen above). This in part explains the prominence of principle of compensation as a fundamental component of international arbitration and claims practice on questions concerning the international responsibility of States. The principle has been given further prominence in analytical jurisprudence (by which we mean the doctrinal writings of academic writers) through the various and often conflicting theoretical postulations attributable to the two schools of thought on the subject (the two schools roughly represent the West/ South divide - i.e. the Western capitalist states versus the capital importing natural resources producing nations). The rationale for reparations is itself broadly based on concepts such as the protection of human rights;[1] a more specific legal justification has been that of '*acquired rights'*.[2] The human rights aspect is sometimes expressed under the traditional legal theory of foreign

[1]- For an articulation of the human rights aspect of FDI, see R. Higgins, "The Taking of Property by the State: Recent Developments in International Law", 176 RECUEIL DES COURS (1982-III), at 355.

[2]- P. Lalive, "The Doctrine of Acquired Rights", in RIGHTS AND DUTIES OF PRIVATE INVESTORS ABROAD 145 (1965).

investment law as the *international minimum standard* of protection for FDI.[1]

Some writers have approached the subject of recompense for nationalization from a more pragmatic perspective by identifying policy considerations based on the potential benefits of FDI projects to the host economy. These writers see in the requirement for compensation a pre-requisite or guarantee for the continuous flow of FDI subsequent to any act of nationalization.[2] Viewed from this perspective, it would seem that that the contractual prescription compensation in the event of nationalization could serve as a specific country risk management device. In other words, the very concept of recompense can in itself serve as a magnate for inward foreign investment; the offer of potential compensation could thus be deemed a persuasive (if perhaps a not very innovative) tool for investment promotion and protection. The guarantee of compensation

[1]- See further SORNARAJAH (2010), at 122-130; see also R.B. LILICH, THE HUMAN RIGHTS OF ALIENS IN CONTEMPORARY INTERNATIONAL LAW (1984); and A. ROTH, THE MINIMUM STANDARD OF INTERNATIONAL LAW APPLIED TO ALIENS (1949).

[2]- J. DUNNING, INTERNATIONAL INVESTMENT (1972), p.44;

(and consequently of due process of law) could be thus seen to constitute a useful device in the tool-set which a country could deploy as part of its overall political risk management strategy in its quest to attract much needed long term investment. This partly explains the prominence of the principle of compensation in natural resources development contracts and in bilateral investment treaties.

However, in keeping with the controversy which surrounds this area of international law, it is not surprising to find that not everyone subscribes to or agrees with these justifications. As expected the need for compensation in the event of nationalization has been very strongly contested and disputed by scholars whom one would associate with the Southern (capital-importing) school of thought.[1] These critics of the traditional view of compensation tend to accord

[1]- See, for example, N. Girvan, "Expropriating the Expropriators: Compensation Criteria from a Third World Viewpoint", in 3 VALUATION OF NATIONALIZED PROPERTY IN INTERNATIONAL LAW (R. LILICH (ED)), 49 (1975); O. Kamanu, "Compensation for Expropriation in the Third World" , 10 STUDIES IN COMPARATIVE INT'L DEV'T, 3 (1979); and M. Sornarajah, "Compensation for Expropriation: The Emergence of New Standards", 13 J. WORLD TRDADE L. 108 (1979).

greater prominence to the sovereign prerogatives and national regulatory competences of host States – thus recognizing in municipal law rather than international law the competence to adjudicate on matters relating to nationalization.[1]

The real difficulty on the question of recompense for nationalization reside not so much in the principle of compensation itself given the fact that both schools of thought recognize the basic requirement for some form of recompense for the deprivation of foreign economic rights or entitlements. The debate has centred rather on the applicable measure of compensation and the applicable choice of law in deciding the measure of compensation. At the heart of the controversy has thus been the question of 'compensation standards': full compensation versus appropriate compensation; national legal standard against the minimum international standard. The unequivocal view of the traditional (Western) school of thought is that the requirement of a nationalizing State to compensate the

[1]- An Tang, "The Law Applicable to Transnational Development Contracts", 21 J. WORLD TRADE L. 95 (1987).

affected FDI investor amounts to an obligation under customary international law to provide 'full' compensation. 'Full' compensation in this context is interpreted to mean recompense which is "*prompt, adequate and effective*". For adherents of the traditional school of thought the requirement of 'full' compensation thus constitutes a basic and necessary precondition for the legality of any nationalization or expropriation of foreign economic interests under international law.[1] Revisionist (Southern) scholars have not only contested the claims of the traditional school of thought but have postulated alternative concepts which they deem more suitable to the post-colonial economic, political and social context of the international investment regime. This in turn led to the advent of the proposed new standard of appropriate compensation. The new approach postulated the setting aside of the full compensation standard if it was seen to be inconsistent the newly found economic goals and

[1]- F. DUNN, THE PROTECTION OF NATIONALS (1932); H. Schemers, "Judicial Protection of International Rights", 23 GERM.Y.B.INT'L L 181 (1980); Stephen Schwebel, "International Protection of Contractual Arrangements", 53 A.S.I.L PROCS. 266 (1959); Georg Schwarzenberger, "The Protection of British Property Abroad", 5 CURRENT LEGAL PROBS. 295 (1952).

aspirations of the nationalizing State, or with the exigencies and new developmental ethos of the international community as a whole.[1]

While the customary international law 'full' compensation standard had frequently been contested by capital-importing countries, State practice in the form of 'full' compensation provisions in natural resources agreements and in bilateral investment treaties has introduced into the debate an inconsistency which has further accentuated the confusion in this area. It may well be the case that some nations, especially resource rich but capital poor developing countries, are left with little option but to accept the stipulation of 'full' compensation as a precondition for attracting much needed inward investment. Whatever may be the reason for this inconsistency of approach, the fact remains that the provision of full compensation in the event of nationalization is clearly at odds with the underlying philosophy of appropriate compensation to which these countries subscribed through

[1]- See further F.V. GARCÍA-AMADOR, THE CHANGING LAW OF INTERNATIONAL CLAIMS (1984), at 301.

the various United Nations General Assembly resolutions on the question. The findings of our research would also seem to suggest that international arbitration and claims tribunals continue to favour the full compensation standard.

One of the key objectives of this article is to review the current state of State practice and as well as the judicial renderings of international arbitration and claims tribunals. Rather than seeking to assert the superiority of one of the opposing points of view over the other, our discussion will attempt an objective analysis which will enquire into the evolution of the concept of compensation with a view to assessing the current state of international law on this key question. Our discourse will extend to an examination of the non-negligible role played by economic concepts (as well as the usually political context of international investments disputes) in influencing the outcomes of investment litigation. In the course of our analysis the question will be posed whether considerations other than the customary international law of 'full' compensation form part of legal considerations in the settlement of international investments disputes. In our view this question is warranted in view of the alternative legal developments and other significant departures from the 'full' compensation standard which has

attended the historical evolution as well as the theoretical development of relevant principles.[1] In attempting a balanced perspective to our analysis, we shall also be posing the question whether the appropriate compensation standard (now seemingly obsolete) has been fatally undermined by the increasing prevalence of the 'full' compensation standard in State practice as the proposed or acceptable measure of potential compensation for nationalization. These developments, coupled with concurrent trends in modern arbitration and claims practice, would appear at the very least to have stifled the normative development of the appropriate compensation standard. This does not necessarily imply that dissatisfaction with the procedural and substantive aspects of the present investment regime has been satisfactorily addressed. Such dissatisfaction may indeed have subsided from its peak in the 1970s-80s. But it rumbles on, most particular amongst Latin American countries.[2]

[1]- See further P. Norton, "A Law of the Future or a Law of the Past: Modern Tribunals and the International Law of Expropriation", 85 AM. J. INT'L L., (1991), at 85.

[2]- Asha Kaushal, "Revisiting History: How the Past Matters for the Present Backlash Against the Foreign Investment Regime", 50 HARV. INT'L L.J. 491 (2009).

In Part 2 we shall be examining the historical background to the debate over the required standard of compensation for nationalization in international law. As part of the discussion in the section we shall also be explain the continuing relevance of the debate to the contemporary legal problems on nationalization. A critical review and appraisal of traditional legal theory and its promotion of the orthodox view of compensation as equating to full compensation will be undertaken in Part 3. In Part 4 we shall identify and explain the nature of the challenge posed to classical international law by new principles aimed at the normative reform of the international investment regime - most notably the principles of permanent sovereignty over natural resources and the claims to a founding of a new international economic and legal order. Part 5 will then examine the compensation requirement from a perspective of the modern context of international arbitration and claims practice on the question of compensation for nationalization. A comparative approach is adopted in Part 6 through a review of national law requirements on the question of compensation for nationalization in selected number of countries. Our aim in this part is to ascertain if the selected sample of national legal systems is reflective of either of the two opposing standards of compensation for nationalization

– i.e. full compensation and appropriate compensation. In Part 7 we propose to analyze the compensation requirement from a functional and applied by examining the underlying economic concepts used for the computation of compensation or damages awards. Our chief aim in this part is to establish what link there is between particular economic concepts (which are employed for the valuation of nationalized assets) and the opposing standards of appropriate and full compensation. The article will then conclude with a summary of our specific findings and recommendations.

As part of our study we will seek to develop a number of hypotheses. In the first of these hypotheses we attempt to identify the key economic drivers and social undercurrents which have informed the philosophical foundations of each of the two schools of thought. Behind the traditional school of thought clearly resides the capitalistic (or market) economic model with the 'full' or 'market value' compensation serving as the defining pillar of classical international law on nationalization. The 'revisionist' school of thought advocates for a reform of the current international investment regime with a view to according greater emphasis to emergent principles of international law and giving priority to the national regulatory competencies of the host

State. This school would thus seem to be informed by an opposing model based not on the 'economic' but on the social function of property.

Empirical evidence based on the evolution of international investment relations in the past half century, particularly in the petroleum and mineral development sectors, also point to the political context in which the debate on compensation for nationalization has been conducted. The strident calls advocating a reform of the current international investment regime (together with its customary international law foundations) have been and continue to be informed by the distant political background of colonialism, post-independence aspirations towards genuine self-determination and sovereignty over domestic natural resources. These, therefore, are some of the underlying historical themes which have informed our research.

It is in view of this academic controversy which has surrounded the question of compensation for nationalized property that international law on the question remains in an acknowledged state of uncertainty and flux to this day. This has in turn given rise to a situation where competing standards continue to vie for supremacy within the international investment regime - with each one laying a

superior claim to the prioritization of norms to govern international investment relations. Even though the traditional view of 'full' compensation appears to have made considerable headway and to have established itself as the preferred standard in contractual practice, bilateral investments treaties and in claims practice, we cannot ignore the fact that there is still an ongoing challenge to the basic precepts of the current international investment regime. The present challenge, emanating mainly from Latin American countries such as Bolivia and Venezuela[1], centres on two contentious points: firstly, the admissibility of international claims involving sovereign states and private investors - with the countries involved questioning both the amenability of sovereign parties to such litigation and the conferring of international *locus standi* to private investors on the public international law plane.[2] In other words, they contest the

[1]- See George Joffe, Paul Stevens, Tony George, Jonathan Lux & Carl Searle, "Expropriation of Oil and Gas Investments: Historical, Legal and Economic Perspectives in an Age of Resource Nationalism", 2 J. WORLD ENERGY L. & BUS. 3-23 (2009); Brian Alperstein & Marco Kirby, What is Really Behind the Nationalizations in Latin America? The Cases of Venezuela and Bolivia, available at http://www.Imvlaw.com/archivos/117966530.pdf.

[2]- See Susan Franck, "Development and Outcomes of Investment Treaty Arbitration", 50 HARV. INT'L L. J. 435 (2009)' at 436.

justiciability of such disputes in any forum other than in relevant national courts of the host States.[1] Secondly, these countries continue to question the applicability of the substantive principles of customary international law (including the international norms governing nationalization and compensation) to investment disputes involving private corporations who are themselves not subjects of public international law. At the heart of this second question has been the debate as to whether or not the 'full' compensation requirement as espoused by the orthodox or traditional school of thought is indeed an obligatory norm of international law.[2] The question thus to be asked is whether the full compensation requirement is a reflection of an international custom providing evidence of a general practice accepted as law. It is now proposed to undertake a critical overview of the theoretical debate on this question in the section which follows.

[1]- Kate Supnik, Making Amends: Amending the ICSID Convention to Reconcile Competing Interests in International Investment Law, 59 DUKE L.J. 343 (2009).

[2]- See further P. Gann, "Compensation Standard for Expropriation", 23 C.J.T.L. 615 (1985).

2. HISTORICAL BACKGROUND AND CONTINUING RELEVANCE OF THE THEORETICAL DEBATE ON COMPENSATION FOR NATIONALIZATION.

The advent of the debate concerning the acceptable standard of compensation for the nationalization of foreign economic interests dates back to the immediate post-colonial period. This was an era in which the newly independent countries of Africa, Asia, the Middle East and Latin America sought to exercise greater sovereign control over the exploitation of domestic natural resources. The upstream petroleum and mineral sectors in particular – perceived by the new governments to be the "commanding heights" of the economy - attracted the increasing attention and regulatory impulses of the governments of the newly independent States. Complete control over the development of domestic petroleum and mineral deposits quickly became the chief indicator of progress on the new concepts of permanent sovereignty over natural resources and the new international economic order. Aspirations towards national self-determination in turn led to the advent of new contractual

arrangements such as production sharing contracts, or in extreme cases nationalization.[1] State petroleum and mining enterprises became the norm and proliferated in petroleum and mineral producing countries, thus serving as the vanguard for the new policies.

Politically the exercise of national sovereign control over key sectors of the economy became the chief measure of the call to nationhood. But standing in the way of these aspirations were the principles of customary international law which sought to offer some measure of protection to the foreign enterprises adversely affected by the new measures.[2] While recognizing in principle the right of host States to 'regulate' foreign owned property within their territorial jurisdiction, customary international law nonetheless prescribed stringent pre-conditions for such regulation where

[1]- SORNARAJAH (2010), at 118; O. Lando, "Renegotiation and Revision of International Contracts: An Issue of North-South Dialogue", 23 GERM. Y.B. INT'L L., 37 (1980).

[2]- See generally D. BENNET and K. SHARPE, TRANSNATIONAL CORPORATIONS VERSUS THE STATE (1985); Peters, P., Schrijver, N., and de wart, P, "Responsibility of States in Respect of permanent Sovereignty over Natural Resources", 36 NETHER. J. INT'L L., 285 (1989).

foreign economic interests were concerned. Amongst these pre-conditions were the prescriptions that where regulation culminates in a direct or indirect taking of foreign owned property by the regulating State the taking must be for a public purpose, must be non-discriminatory as to the nationality of the investors affected by the measures, and must be subject to the payment of full compensation.[1]

Taken at face value these prescriptions seem reasonable enough. But on closer examination their stringent application in practice could pose an insurmountable obstacle to the sovereign aspirations of a developing nation in its quest to exercise domestic control over the exploitation of its natural resources by foreign enterprises. In fact it could be argued that the requirement of 'market value' compensation for nationalized assets amounts in effect to the '*marketisation*' of regulation. This approach would, in effect, shut out those poor nations who could not afford the market price of nationalization or regulation through their inability to pay for the foreign enterprise as a 'going market concern'. This in

[1]- See further I. BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW, 7th Edition (2008), p.533.

turn would render the right of the host State to regulate (a right recognized by customary international law as an expression of sovereignty) somewhat meaningless. Those advocating the reform of customary international law and the establishment of a new international order saw in the international investment regime based on the principles of classical international law a system which was over-indulgent in its quest to protect the interests of foreign enterprises to the detriment of the national interests.[1] In place of the minimum international minimum standard of protection prescribed by classical international law for the foreign investor[2], those who advocated reform posited equality of treatment between national and foreign investors. They perceived in international a discrepancy which requires such equality of treatment but only makes provision for compensation to foreign investors in the event of nationalization. Genuine equality, they argued, can only be

[1]- R. VERNON, SOVEREIGNTY AT BAY (1971); S. Hymer, "The Multinational Corporation and the Law of Uneven Development", in H. RADICE (ed), INTERNATIONAL FIRMS AND MODERN IMPERIALSM, 1 (1975)

[2]- For a discussion on this see SORNARAJAH (2010), at 120-124.

achieved through the application of the same national standard of treatment for both domestic and foreign investors under domestic law - with investment disputes such to the jurisdiction of municipal courts and tribunals.[1]

Where, on the other hand, such disputes are subject to the jurisdiction of international claims tribunals, the standard of compensation to apply should be that of 'appropriate' compensation as opposed to full compensation. Finally, those advocating the reform of customary international law were quick to highlight not only the inconsistency of State practice with regard to negotiated settlements and lump sum payments which both seem to be at variance with the 'full' compensation requirement, but also the fact that the newly independent nations had played no part in the development of customary international law on those vital questions.[2] The

[1]- A. Giardina, "State Contracts: National Versus International Law?", 5 ITAL. Y.B. INT'L L., 147 (1980-81); see further Rudolf Dolzer, "New Foundations of the Law of Expropriation of Alien Property" 75 AM. J. INT'L L., 55 (1981); Ahmed El Kosheri and Tarek Riad, "The Law Governing a New Generation of Petroleum Agreements: Changes in the Arbitration Process", 1 ICSID REV.– F.I.L.J.257 (1986).

[2]- See further F.V. García-Amador, "A Basic Dispute: Conflicting Views on Expropriation", in J.J. NORTON (ed), PUBLIC

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most that could be said of the new nations was that they had inherited, through the international law principles of state succession and of the continuity of states, customary international law prescriptions from the previous colonial administrations. The contested principles of classical international law on the standard of compensation, with their market driven ethos, was clearly at odds with the social programmes and development goals and aspirations of the newly independent nations.[1] The governments of the new nations perceived in nationalized petroleum and mining projects not the profit driven market model promoted by the capital exporting nations, but the social function of such project vis-à-vis their potential contribution to national economic development goals and political aspirations towards economic self-determination.[2]

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INTERNATIONAL LAW AND THE FUTURE WORLD ORDER, Chapter 7 (1987); also see by the same author, "Current Attempts to Revise International Law: A Comparative Analysis", 77 AM. I. INT'L L., 286 (1983).

[1]- A. ANGIE, IMPERIALISM, SOVEREIGNTY AND THE MAKING OF INTERNATIONAL LAW (2005).

[2]- For more on the perceived social function of property within the context f the nationalization debate, see Seidl-Hohenveldern, "The Social Function of Property and Property Protection in Present Day

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The theoretical debate concerning the traditional norms of classical international law which prescribe 'full' compensation for nationalization and the proposed new norms with their preference for an 'appropriate' standard of compensation thus revolve around the question of the status of each of these standards as a law-creating norm. Critics of the proposed new norms have disputed their normative significance on the grounds that they did not receive the support of capital exporting nations in the relevant United Nations General Assembly resolutions.[1] But critics of the old order have countered such views by pointing out that these arguments hold equally true for the customary international law norm of 'full' compensation. In their view the latter could be perceived not to be a valid rule of international law given that relevant UNGA resolutions adopting the 'appropriate' compensation standard for nationalization could be construed as evidence of the fact that capital-

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International Law", in ESAYSO N THE DEVELOPMENT OF THE NTERNATIONAL LEGAL ORDER IN HONOUR OF KARO F. VAN PANHUYS, 77 (1980).

[1]- This view have found support in a number of international arbitration cases including Texaco-Calasiatic Oil Company v Government of the Libyan Arab Republic, 53 I.L.R 420 (1979).

importing nations do not accept the 'full' compensation standard.[1] In the words of one author, the UNGA resolutions serve as an indication of international community expectations which require a norm different from the classical international law norm of full compensation.[2]

It is still apparent from a theoretical understanding of the present international law framework governing compensation for nationalization that two currents of thought continue to drive the conceptual and normative development and evolution of the international investment regime. While it is true that the orthodox view which favours 'full' compensation currently holds sway, it would be nonetheless be disingenuous of anyone to believe that this is the universally (or even the generally accepted) standard. Indeed the very presence of UNGA resolutions on *Permanent Sovereignty over Natural Resources* and on the *New International Economic Order*, dormant though they may lie at the moment, serves as a pertinent reminder of the absence

[1]- M. Sornarajah (1979), at 129.
[2]- J. Fawcett, "UNCTAD IV: A Bill of Rights?", 32 WORLD TODAY, 152 (1979).

of unanimity on the question of the acceptable standard to govern the measure of compensation for nationalized property.

From a purely conceptual viewpoint each of the two standards ('full' compensation and 'appropriate' compensation) would appear to offer a viable remedial option for international arbitration and claims practice on the question of recompense for the deprivation of foreign economic interests through a sovereign act of nationalization. But such optimism is subject to caution. In our view, the continuing challenges being posed to the current international investment regime - coupled with the historic uncertainty over the precise normative status of relevant principles - precludes us from reaching an unequivocal judgment as to the exclusive normative appeal of one particular standard as being the exclusive source of international law obligations. Nor can we be certain that one particular standard of compensation will find political acceptance in the long term with the opposing school of thought and with the international community as a whole.

The cleavage in academic and political opinion on the subject[1], coupled with the sometimes confused and conflicting renderings of international arbitration tribunals, serve to reinforce this caution and also highlights the absence of consistency in the evolution of relevant international norms. In the Libyan oil nationalization disputes in which most of the cases shared a similar factual background, for instance, the opinions of the arbitrators in some of the cases appear to conflict with each other - thus underlining the uncertain state of international law on the question of compensation. [2] In the *TOPCO Arbitration*[1], for

[1]- Se further A. CASSESE, INTERNATIONAL LAW IN A DIVIDED WORLD (1986); Rosalyn Higgins, "The Taking of Property by the State: Recent Developments in International Law", 176 RECUEIL DES COURS 263 (1982-III); C.G. Fenwick, "International Law: The Old and the New", 60 AM. J. INT'L L. 475 (1966); and A. Grahl-Madsen, "International Law at the Crossroads", in SCAND. STUDIES IN LAW (1980), at 177-86.

[2]- Robin White, "Expropriation of the Libyan Oil Concessions: Two Conflicting International Arbitrations", 30 INT'L & COMP. L.Q. 1-19 (1981); see also Brigitte Stern, "Trois Arbitrages, Un Même Problème, Trois Solutions: Les Nationalisations Pètrolières Libyennes devant l'Arbitrage International", in REV. DE L'ARBITRAGE 1-43 (1980), at 3. On the question of general lack of clarity in the decisions of international arbitration tribunals on FDI disputes: see Richard Lillich and David Bederman, "Jurisprudence of the Foreign Claims Settlement Commission: Iran Claims", 91 AM. J. INT'L L. 436-65 (1997).

example the principle of restitution was upheld by the arbitration tribunal in its compensation award; whereas the same principle was rejected in the *LIAMCO*[2] and *BP Exploration v Libya*[3] cases notwithstanding the factual similarities between them. We do not contest the fact that the full compensation standard will always continue to retain a certain attraction amongst its adherents or a continuing judicial and contractual appeal. At the same time it would be injudicious of anyone to dismiss the fact that the appropriate compensation formula will always present itself as a real and viable alternative to 'full' compensation.[4] Indeed a review of previous arbitration awards and claims settlements is instructive in that arbitration tribunals do not seem to consider themselves bound or wedded to 'full' (market value) compensation. Rather, it is the case that such tribunals do sometimes adopt a flexible approach which takes into consideration the influence of other factors which could have

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[1]- 53 I.L.R. 389 (1979).

[2]- Libyan American Company (LIAMCO) v Government of the Libyan Arab Republic, 20 I.L.M 1 (1981).

[3]- BP Exploration (Libya) v Government of the Libyan Arab Republic, 53 I.L.R 300 (1979).

[4]- See further O. Schachter, "Compensation for Expropriation", 78 AM. J. INT'L L., 121 (1984), at 126.

a bearing or impact on the potential award. An overview of the practice of international arbitration and claims tribunals reveals no evidence of a dogmatic adherence or an unyielding attachment by tribunals to the orthodox expression of the classical international law requirement for 'full' compensation.[1]

It is thus clearly the case that each of the opposing standard continues to have some judicial appeal (with varying degrees of persuasiveness) in the history of international arbitration and claims practice on the question of compensation for nationalized property. Each of the two standards also continues to attract a substantial body of adherents, advocates and supporters. Our submission in this regard would thus be that it is far too premature to hold that the 'full' compensation standard has succeeded in laying down a compelling claim to unrivalled or uncontested supremacy in the prioritization of norms to govern the question of compensation for nationalization within the legal framework of the current international investment regime.

[1]- Ibid

2.1. A Question of Form versus Substance?

Our discussion so far has centred on the theoretical or seemingly ideological basis for the postulation of alternative norms to govern the question of compensation for nationalization. But are there any practical implications underlying each of the competing claims? The political symbolism associated with each of the two standards of compensation is readily apparent. This can be explained on three grounds: first, the politicization of the process can be ascribed in part to the political overtones which have tended to accompany discussions on the regulation of FDI in international arena and negotiating forums such as the United Nations General Assembly; secondly, the political complexion of the law in this area can be readily deduced from the political sub-text which is implicit in the various UNGA resolutions on the question of compensation for nationalized property; and thirdly, the "North-South" (or more appropriately West-South) ideological loyalties which have often infused and will continue to shape scholarly opinions on the subject.

It is thus obviously the case that the question of compensation for nationalized property and the applicable

standard for recompense is informed on each side as much by political attitudes to these questions as by purely legal arguments. But what role do considerations relating to the probable scope, extent and magnitude of potential compensation awards play in the formulation of the respective concepts? Do the postulated standards have any quantum significance in relation to the actual size of compensation awards in the event of nationalization? It could possibly be argued that to some extent the theoretical debate on the subject has revolved mainly around a question of semantics - i.e. the perceived meaning and possible legal implications of specific words and phrases vis-à-vis the probable scope of international responsibility which the use of such words could entail; and concomitantly the extent of the protection which the use of particular words or phrases could afford to the foreign investor or the nationalizing host State. It is perhaps for these reasons that the debate regarding the normative content of the international law on compensation for nationalization has tended to focus more on the permissible limits of regulatory State actions affecting foreign economic interests and far less on the practical implications or remedial aspects of each of the postulated

standards. In other words, not much attention seems to have been paid to the quantum aspect in terms of the possible amount of compensation payable under each standard. This can be further seen in the prominence given to the political aspects of sovereignty and national control over domestic natural resources in relevant UNGA resolutions.[1] As part of our research we will endeavour to fill this gap in academic analyses with a critical commentary on the quantum aspects and implications of each of the opposing schools of thought in terms of the correlation (if any) of their respective postulations to the probable size of potential compensation awards under each of the competing standards.

[1]- R. Dolzer (1981), at 556.

2.2 A Critical Commentary on the Historical Evolution of the International Law Governing Compensation for Nationalization.

A number of successive historical episodes are clearly identifiable in the development of international law governing compensation for nationalization. From a theoretical and conceptual point of view we believe that four key stages are discernible in the evolution of norms purporting to govern both the wider question of nationalization and the more specific question of compensation in general international law. We may outline these stages as follows:

(a) The first of these stages constitutes the colonial period from the early part of the twentieth century right up to the second World War; this period saw the advent of the conceptual development of the requirement of compulsory compensation for State deprivation of foreign owned property in traditional legal theory based on classical international law. Founded on neo-classical economic liberalism it drew its authority from the perceived norms of customary international law.[1]

[1]- See further Schachter (1984), at 294.

(b) The second stage saw the parallel and concurrent development in the post-World War 1 period of socialist legal theory. In keeping with the underlying philosophical principles of socialism the international law requirement of compensation for acts of expropriation and nationalization lost its compulsory legal character. Pre-eminence in socialist legal theory was given to the social function of property while the requirement for compensation acquired a discretionary character which thus became dependent on the sovereign will of the expropriating State.[1]

(c) The third stage constitutes the post-colonial era which followed the aftermath of the Second World War. Increasing self-assertion on the part of the newly independent in their quest for sovereign control over domestic natural resources led to the postulation of the new norms of international law advocating a greater role for national regulatory competences and less emphasis on international regulation. It was during

[1]-See also S, FRIEDMANN, EXPROPRIATION IN NTERNATIONAL LAW (1953), pp.9-12.

this period that the new standard of 'appropriate' compensation for nationalized property was postulated as an alternative to the 'full' compensation standard.[1]

(d) In the fourth stage, we perceive the advent of the twenty-first century concept of globalization with the increasing projection human rights and democratic governance as global values with international legal implications.[2] With particular reference to international arbitration and claims practice there appears to be an increasing tendency the fusion of private law and public law[3], and the continuous

[1]- M. MUGHRABY, PERMANENT SOVEREIGNTY OVER OIL RESOURCES: A STUDY OF MIDDLE EAST OIL CONCESSIONS AND LEGAL CHANGE (1965); See also C. BROWER, THE FUTURE OF FOREIGN INVESTMENT: RECENT DEVELOPMENTS IN THE INTERNATIONAL LAW OF EXPROPRIATION AND CONFISCATION (1975).

[2]- M. Sornarajah, "The Impact of Globalisation on the International Law of Investment", 12 CANADIAN FOREIGN POLICY 1 (2002), see also D. SCHNEIDERMAN, CONSTITUTIONALISING ECONOMIC GLOBALISATION: INVESTMENT RULES AND DEMOCRACY'S PROMISE (2008); G. FOX and A, ROTH (eds), DEMOCRATIC GOVERNANCE AND INTERNATIONAL LAW (2000)

[3]- For a discussion of this trend in claims practice, see G. VAN HARTEN, INVESTMENT TREATY ARBITRATION AND PUBLIC LAW (2007).

blurring of the boundaries between national and international legal standards in international economic law.

The cumulative impact of the various political, economic, social and legal developments since World War 1 has thus been to pose a very serious challenge to the classical international law foundations of the international investment regime. Nowhere has this challenge been more seriously felt than in the area of nationalization. Here, the orthodox view which advocates full compensation as a basic requirement for the legality of the nationalization of foreign owned property - and then equates 'full' compensation with 'market value' recompense - has been very severely put to the test by the new developments which have sought to inform the evolution of international law on these questions in the post-war years.

Faced with these challenges, the orthodox view which asserts the 'fullness' of compensation as an international law requirement for nationalization involving foreign economic interests has itself undergone some measure of transformation since the early part of the twentieth century. Rather than yield to the new challenges, we find that the

orthodox expression of the traditional international law requirement of recompense for nationalized property has progressively acquired a more rigid character over time. Our review of early cases, particularly those precedents on which the traditional theory of compensation for nationalization is founded, indicate that prior to the *Hull formula*[1] international law required not 'full' but "just" or "fair" compensation. In one of these cases, the *Chorzow Factory Case*[2], the court referred to a duty to pay *fair compensation* while recognizing the possibility of restitution in kind.[3] Similarly in the *Norwegian Shipowners' Claim*[4] the judgment of the tribunal was founded on the requirement for *just compensation* in view of all "the surrounding circumstances".[5] In neither of these cases was there any reference to a national or international law requirement for "full" compensation. It thus seems surprising that adherents of the 'full' compensation standard appear to rely on these

[1]- The "Hull formula" denotes the orthodox expression of the international law requirement as amounting to 'full' compensation – i.e. "prompt, adequate an effective" compensation.
[2]- Factory at Chorzow (Germany v Poland) (Indemnity) P.C.I.J. 14 (1928).
[3]- Id, at 146.
[4]- Norway v U.S.A 1 R.I.A.A. 307 (1922).
[5]- Id, at 309.

two for judicial authority in support of the orthodox view. Many of the other early cases relied on by adherents of the 'full' compensation principle do not offer any categorical or specific support for the standard.[1] It could indeed even be argued in the *Norwegian Shipowners Claim* [2]the tribunal's readiness to take into account all the surrounding circumstances when assessing the compensation seems to have adopted, in so doing, a position much closer to the philosophy of what subsequently became known as "appropriate" compensation.

Our submission on his point is that the conceptual underpinning of the traditional legal theory vis-à-vis its articulation of the 'full' compensation requirement as a rule of international law can thus be traced not to early claims practice but to the postulation of the Hull formula in 1938. Through a critical analysis of the evolution of international law on the question of compensation for nationalized property two main conclusions may be drawn from the absence of the 'full' compensation requirement in judicial

[1]- See, for example, the Spanish Zone in Morocco Case (Great Britain v Spain), 2 R.I.A.A 615 at 617 in which the tribunal's award was for "juste indemnité".
[2]- Supra, 309-341.

precedents and early claims practice. The first of these is that the *Hull formula* lacks judicial foundation in view of the fact that there is little support for the *full* compensation standard in early cases.[1] The second conclusion which is to be drawn is that under traditional legal theory the principle appears to have evolved first from *just* or *fair* compensation to *full* compensation, and then came the assimilation of *full* compensation to *"prompt, adequate and effective"* compensation[2] - supported by the economic prescription of *full market value*. It is interesting to note that a reflection of this defining traits in international commercial practice which mirror a parallel evolution from early mercantile traditions to the advent of an international market economy based on foreign investment - and consequently the need to protect fully the private property rights of foreign nationals through the medium of international law.

[1]-Among the authors who share this view are the following: Schachter, (1984), at 123; and Sornarajah, (1979), p.116 et seq., according to whom some of the claims settlements relied on by traditional legal theory arose out of political coercion, and hence lack both legitimacy and a judicial basis as precedent.

[-2]- Se further B. Clagett, "The Expropriation Issue Before the Iran-United States Claims Tribunal;: Is 'Just Compensation' Required by International Law or Not?", 16 LAW & POLICY IN INTERNATIONAL BUSINESS (1984), 813.

3. OVERVIEW AND CRITICAL ANALYSIS OF TRADITIONAL LEGAL THEORY ON THE QUESTION OF 'FULL' COMPENSATION AS AN INTERNATIONAL LAW REQUIREMENT.

As seen in the preceding section the precise origin of the concept of '*full'* compensation as posited by traditional legal theory is very much unclear. However, the reliance of classical international law on the principle of '*restitution in kind' (*which the Permanent Court of International Justice identified as a possible remedy for unlawful expropriation) appears to suggest that the requirement for '*full'* compensation in traditional legal theory may have emanated from the judgment in the *Chorzow factory (Indemnity)* case.[1] In its quest to identify a suitable remedy for the nationalization of foreign owned assets the court stated as follows:

> "The essential principle contained in the actual notion of an illegal act - a principle which seems to be established by international practice and in particular by the decisions of arbitral tribunals - is

[1]- Factory at Chorzow, (Germany v. Poland) (Indemnity), 1928 P.C.I.J., (Ser. A), No.17, (Judgment of Sept. 13).

> that reparation must, as far as possible, wipe out all the consequences of the illegal act and reestablish the situation which would, in all probability, have existed if that act had not been committed. Restitution in kind, or, if that is not possible, payment of a sum corresponding to the value which a restitution in kind would bear [should be made]."[1]

Much reliance has since been placed by traditional legal theorists on this passage from the court's judgment to promote the view that 'full' compensation equals restitution. These theorists hold the view that the judgment in this case remains of paramount importance to the founding of the principle of *full* compensation in international law. Classical international law scholars have thus been eager to highlight the fact that the PCIJ's judgment is significant in view of its continuing vitality as a starting point for subsequent arbitration tribunal decisions supporting the 'full' standard of

[1]- Id. at 47.

compensation as an international law requirement.[1] It has further been argued that none of the tribunals in earlier cases granted compensation less than the full market value of the nationalized assets, and that many of the early judgments specifically affirmed the need for 'full' compensation.[2]

But these scholars seem to ignore the fact that judicial reasoning in earlier cases on the question of compensation tended to lack clarity and are for the most part obscure. In very few of the early cases do we find an unequivocal requirement for full compensation or its explicit expression as a normative requirement. Thus whereas the requirement for *restitution in kind* as the prescribed remedy in the *Chorzow Factory* case could be seen as equating to full compensation, the judgments in other notable cases were not as categorical in requiring 'full' compensation. In the *Affaire Goldenberg (Germany v Roumania)*[3], for instance, the court in its judgment pointed

[1]- See for example Norton, (1991), at 476. See also, Arbitrator Dupuy, in the TOPCO Arbitration (supra, at 498), in whose view the principle of restitution was expressed in the Chorzow Factory Case in such general terms that it would be "difficult not to view it as a principle of reasoning having the value of a precedent."

[2]- Ibid, at 476-477

[3]- 2 R.I.A.A. 901.

out that payment of less than the full value of the property was an act contrary to the law of nations; it then went on to prescribe equitable payment in the quickest possible time.[1] And in the *Norwegian Shipowners' Claim* (which if often cited in support of the '*full'* compensation requirement) the judgment of the tribunal explicitly required "*just compensation in due time*".[2]

As seen above the orthodox view which stipulates 'full' market value' compensation for nationalization as a requirement of customary international law is rooted in the so-called "Hull formula". This orthodox view of recompense for the deprivation of foreign owned property or contractual rights can clearly be traced to the prescription of "*prompt, adequate and effective*" compensation. This requirement was first put forward by the U.S. Secretary of State Cordell Hull in 1938 as a necessary pre-condition for the legality of Mexican expropriation of assets (including oilfields) belong to American nationals.[3] Under its better known rubric of the *Hull*

[1]- Ibid at 909
[2]- Supra, at 332.
[3]- A copy of the full diplomatic correspondence containing the US demands as put for forward by Secretary Hull can be found in G. =

formula, this American prescription is now claimed to constitute the normative basis and legal foundation of the international law on the question of compensation for nationalized property. The effect of the three attributes which form the constitutive elements of the *Hull formula* (i.e. prompt, adequate and effective) was thus to substantially modify the requirement of *just* or *fair* compensation laid down in early cases such as the *Affaire Goldenberg* and the *Norwegian Shipowners' Claim* vis-à-vis the form, character and timing of international compensation settlements.

For it to be considered "*adequate*", compensation had to equate to the full market value of the expropriated property.[1] In theory at least (perhaps less so in practice[2]) partial compensation, or compensation which does not correspond to the full market value of the nationalized property, will be

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HACKWORTH, 3 DIGEST OF INTERNATIONAL LAW, (1942), at 655-665. See also N. HYDE, INTERNATIONAL LAW, (1945), pp.710-711.

[1]- See A. FATOUROS, GOVERNMENT GUARANTEES TO FOREIGN INVESTORS (1962), at 325.

[2]- But it has been pointed out by Fatouros (id at p.326), amongst others, that in State practice compensation has seldom been "adequate" - i.e., commensurate with the full value of the nationalized assets.

considered inadmissible under the formula and therefore a breach of international law.[1] This in turn will render the nationalization exercise an internationally unlawful act. The second attribute for lawful nationalization under the *Hull formula*, the criteria of "*effectiveness*", refers to the specific form of the indemnity and the possibility of its immediate redemption or utilization by the affected party.[2] This requires compensation in the form of a cash payment or in kind – but with the *proviso* that the payment is subject to "effective realization".[3] An orthodox interpretation of 'effective realization' would imply that the compensation is in the form

[1]- Doctrinal support for full market value compensation in keeping with the Hull formula can be found in the following sources: K. Carlston, "Concession Agreements and Nationalization", 52 AM. J. INT'L L., 274-276 (1958); Brandon, "Legal Aspects of Foreign Private Investment", 18 Fed. Bar J., 318 (1958); L. Kissam and e. Leach, "Sovereign Expropriation of Property and Abrogation of Concession Contracts", 28 FORDHAM L. REV. 188-189 (1959); and Note, "Foreign Seizure of Investments: Remedies and Protection", 12 STANFORD L. REV., 609-611 (1960).

[2]-I. FOIGHEL, NATIONALIZATION: A STUDY IN THE PROTECTION OF ALIEN PROPERTY IN INTERNATIONAL LAW, 122-126 (1982); and Bindschedler, "La protection de la proprieté priveé en droit international public", 90 RECUEIL DES COURS, 268 (1956).

[3]- Bindschedler (1956), p.251 points out, for instance, that for compensation to be considered effective it must be practically realizable as otherwise its idea of reparation could become an illusion.

of hard or convertible currency, or under fiscal conditions which allows the beneficiary access to either foreign exchange or foreign remittance.[1] The requirement for 'effective realization' is clearly intended to reinforce the basic principle of restitution as expounded through traditional legal theory given that the Hull formula itself is founded on financial recompense rather than restitution in kind. In so far as the attribute of "*promptness*" is concerned, compensation ought to be offered either before the final act of deprivation (in view of the customary international law pre-conditions for the legality of nationalizations) or soon thereafter. But how soon afterwards is a matter for conjecture. The determination of the permissible time lapse following the act of deprivation will always thus remain a matter of fine judgment. What seems apparent is that under the prescriptions of the *Hull formula* a deferred payment is only acceptable where appropriate

[1]- The Hickenlooper Amendment United States Constitution, for example, asserts that under international law there is a requirement for "speedy compensation in convertible foreign exchange equivalent to the full value" of the nationalized assets.

arrangements have been for the interest payments on the amount of compensation which is due to the claimant.[1]

It is undeniably the fact that the *Hull formula* descriptors, even if they are not always adhered to in State practice, have impacted significantly on the conceptual development and theoretical evolution of the international law principle of compensation for nationalized assets. Where early precedents required *just* compensation "*in due time*"[2], "*equitable payment as quickly as possible*"[3], or *fair payment* made "*as quickly as possible*[4], the *Hull formula* prescribed in their place *prompt, adequate, and effective* or full market value compensation. And although it relies on the *Chorzow Factory Case* as judicial precedent for the *Hull formula*, the traditional legal theory appears to accord little (if any) consideration at all to the tribunal's reference in that case to "a duty to pay *fair compensation*".[5] Equally, the equitable aspect of the principle of restitution on which traditional legal theory appears to found its premise of the *full* compensation requirement seems

[1]- FATOUROS (1962), at 331.
[2]- Norwegian Shipowners' Claim, (1922), supra, at 332.
[3]- Affaire Goldenberg, (1928), supra, at 901.
[4]- Ibid, at 909.
[5]- (Merits), 1928, supra, at 146.

to have played an insignificant role in the conceptual development of classical international law on the subject.

The prescriptions for compensation laid down by the *Hull formula* have been consistently amplified in official statements issued by the capital-exporting nations as representative of their position on the international law governing the legality of foreign expropriations.[1] However, the emergence of the Hull formula as a perceived norm of customary international law owes its vitality not to the political declarations of Western nations but to its articulation and amplification through traditional legal theory and its subsequent endorsement in a significant number of international arbitration awards. These two sources (traditional legal theory and international arbitration awards) have without doubt played an important role in the conceptual development of the orthodox view of compensation. It is now proposed to embark on a further examination of their precise role in the evolution of the international law on compensation for nationalization.

[1]- See further R. Smith, "The United States Government Perspective on Expropriation and Investment in Developing Countries", 9 VAND. J. TRANS. L., 517 (1976).

3.1 The Development of Traditional Legal Theory on the Basis of the 'Hull Formula' in Doctrinal Analysis.

As explained in the preceding sections, the principle of *restitutio in integrum* (or restoration to the *status quo ante*) provides the starting point for the theoretical development of the concept of *full* compensation under traditional legal theory. The latter perceived the obligation of a nationalizing State to pay compensation from two perspectives. First, in cases of lawful nationalization where the State's actions are non-discriminatory and the deprivation is for a public purpose: in such cases traditional legal theory perceived the duty to compensate the victim of the deprivation as being in conformity with the requirements of customary international law. Secondly, where the expropriating measures are deemed to be in violation of treaty provisions or customary international law (or in cases in which a subsequent denial of justice renders an otherwise lawful nationalization unlawful), thus creating an obligation to compensate.[1] It is thus evident

[1]- For an analysis of the distinction between the lawful and unlawful measures and their implication for compensation awards in =

that traditional legal theory, from a conceptual point of view, saw in the principle of restitution a suitable mechanism for the prompt and effective restoration of a dispossessed investor to the *status quo ante* following an unlawful act of nationalization. Viewed from this perspective, restitution therefore has a theoretical attraction as the preferred mode of redress - with financial or monetary compensation acquiring the character of a secondary, subsidiary or alternative mode of recompense. Pecuniary compensation thus becomes an applicable remedy only when *restitutio in integrum* is not practically possible or feasible; monetary compensation also applies in situations where the nationalization measures, deemed to be lawful *per se* in international law, require financial recompense on the basis of unjust enrichment or the protection of acquired rights.[1]

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expropriation cases, see FATOUROS (1962), at 307; and GARCÍA-AMADOR, (1984), at 289.

[1]- Scholars who have posited this orthodox view of compensation as an international law requirement for nationalization include the following: ANZILOTTI, 1 COURS DE DROIT INTERNATIONAL (Gidel trans. 1929), pp.526-527; SIBERT, 1 TRAITÉ DE DROIT INTERNATIONAL PUBLIC, (1951), at 320-325; CAVARÉ, 2 DROIT INTERNATIONAL PUBLIC POSITIF, (1951), at 394; PERSONNAZ, LA RÉPARATION DU PRÉJUDICE EN DROIT

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From an analytical and theoretical perspective it this becomes evident that the tacit premise on which traditional legal theory based its backing for the *Hull formula* as the accepted rule of international law has always been that the concept of restoration to the *status quo ante*. The Hull formula has thus been promoted by traditional legal theory as representing a rule of law in favour of restitution which has not been negated or undermined by any widespread and consistent support for a contrary or opposing rule.[1] Among the scholars who share this view is Alvarez de Eulate, who, in arguing this point, has posited the following:

> "In fact one finds a fair number of cases of *restitutio in integrum* and those cases have a fairly varied content: restitution of persons, vessels, documents, money, rights and properties

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INTERNATIONAL PUBLIC, (1938), at 78 et seq.; L. REITZER, LA RÉPARATION COMME CONSÉQUENCE DE L'ACTE ILLICITE EN DROIT INTERNATIONAL, (1938), pat 171-174; B. WORTLEY, EXPROPRIATION IN PUBLIC INTERNATIONAL LAW, (1959), at 78 et seq.; and G. SCHWARZENBERGER, INTERNATIONAL LAW, (1957), at 656-660.

[1]- D. Robinson, "Expropriation in the Restatement (Revised)", 78 A.J.I.L.,176 (1984). In this article the author criticizes the draft Restatement for being defective in view of its treatment of the Hull formula as a position of the United States as opposed to being a rule of law.

> of various types, cancellations of measures taken, etc ... It is therefore inaccurate to say that *restitutio in integrum* would be a form of reparation practically unknown in international law."[1]

Other scholars who have sought to promote the principle of 'full' compensation and of restitution within the framework of traditional legal theory include Mann, in whose view restitution is the primary remedy in international law.[2] Reuter, on his part, argues that compensation in essence consists mainly of re-establishing the status quo ante through restitution and to ensure in the best way possible the discharging of the original obligations.[3] An orthodox

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[1]- B. Alvarez de Eulate, "La 'restitutio in integrum' en la pràctica y en la jurisprudencia internacionales", TEMPS, REV. CIENCIA & TÉCHNICA JURÍDICA, Nos.29-31, (1971-1975), at 11; see also 12-32.

[2]- F. A. Mann, "The Consequences of an International Wrong in International and National Law", XLVIII BRIT.Y.B.I.L., (1976-77), at 2-3.

[3]- P. Reuter, "Principes de droit international public", 103 RECUEIL DES COURS, (1961-II), at 595. See also R. von Mehren and N. Kourides (1981), at 534; L. Reitzer, (1938), at 173; G. SCHWARZENBERGER, 1 INTERNATIONAL LAW AS APPLIED BY INTERNATIONAL COURTS AND TRIBUNALS (1945), at 233; ibid, "The Protection of British Property Abroad", 5 CURRENT LEGAL PROBLEMS (1952), at 316-317; SCHWARZENBERGER and E. D. BROWN, A MANUAL OF INTERNATIONAL LAW, =

understanding of these opinions clearly leads to a postulation of the necessity for restitution in kind in foreign expropriation cases.[1] The obvious impossibility of restoration to the status quo ante as a remedy in most cases of nationalization, on the other hand, serves both as an illustration and a pertinent reminder of the practical limitations of traditional legal theory in responding to the problems of nationalizations involving the

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(1976), at 147; P. GUGGENHEIM, TRAITÉ DE DROIT INTERNATIONAL PUBLIC, (1956), pp.68-69; A. FREEMAN, THE INTERNATIONAL RESPONSIBILITY OF STATES FOR DENIAL OF JUSTICE (1938), at 573; L. DELBEZ, LE PRINCIPES GÉNÉRAUX DU DROIT INTERNATIONAL PUBLIC (1964), at 384-385; D. O'CONNELL, 2 INTERNATIONAL LAW, (1970), pp.780-790; B. WORTLEY, EXPROPRIATION IN INTERNATIONAL LAW, (1959), at 129-133; G. WHITE, NATIONALISATION OF FOREIGN PROPERTY (1961), at 15; and M. Whiteman, 2 DAMAGES IN INTERNATIONAL LAW, (1937), at 857. See also C. Amerasinghe, "State Breaches of Contracts with Aliens and International Law", 58 AM. J. INT'L L., (1964), at 882.

[1]- S. Schwebel, "Speculations on Specific Performance of a Contract Between a State and a Foreign National" in THE RIGHTS AND DUTIES OF PRIVATE INVESTORS ABROAD (1965), at 209-210, has suggested that restitution might also be an appropriate remedy where the expropriating State cannot pay the pecuniary compensation required - i.e., as an alternative or secondary remedy to "damages". This view only serves to highlight further the argument that traditional theory is inherently circumscriptive of the State's right to nationalize property under international law as restitution under these circumstances would simply amount to a denial of that right. This, in effect, could amount to a possible derogation from the principle of national sovereignty.

deprivation of foreign economic interests.[1] Even after making due allowance for possibility of the conceptual appeal of traditional legal theory on point of principle, a much more practical, pragmatic and workable approach would counsel the putting in place of arrangements partly involving restitution in kind (e.g., of returnable items such as documents, money, and other non-productive assets), and partly monetary compensation. It is thus to be submitted that in the absence of such a compromise, the practical appeal of the orthodox view of compensation as articulated through traditional legal theory would be very limited indeed within the modern context of international claims practice on the question of compensation for nationalization.

But to what extent can it be said that the practical problems associated with restitution imply an erosion of judicial support for the orthodox view in international claims practice? In the section we propose to examine the response of post-*NIEO*[2] international claims practice to the prescriptions of traditional legal theory and its promotion of the principles of restitution and 'full' compensation.

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[1]- For a discussion of factors which may hinder restitution in kind as a potential remedy, see R. HIGGINS (1982-III), at 315-316.

[2]- New International Economic Order as encapsulated in United Nations general Assembly (UNGA) Resolution 3201 of 1 May 1974.

3.2 Traditional Legal Theory in the Jurisprudence of International Arbitration and Claims Practice.

A critical review of the history of the jurisprudence emanating from international arbitration and claims tribunals leads us to the view there is some degree of support for the orthodox view of compensation in the form of either restitution or full compensation present in various awards.[1] In the majority of such cases, however, notwithstanding a tribunal's identification of the principle of restitution as the most appropriate remedy for an unlawful act of nationalization, pragmatism seems to have dictated an alternative award of financial recompense to the magnitude of

[1]- Even so the actual restitution of property has been ordered only in exceptional cases, examples of which include The Case of Religious Properties (France v. Poland), 1 R.I.A.A., (1920), at 7-11; and Chorzow Factory Case, Germany v. Poland), (Judgment No.7, May 25, 1926), P.C.I.J., Ser. A, No.7. (Following Poland's refusal to restore the factory and subsequent agreement with its owners to accept compensation, the Court ordered a financial settlement in the Judgment of September 13, 1926; supra, at 47). Other cases which have been cited as supporting the principle of restitutio in integrum include the Mavrommatis Jerusalem Concessions Case, (1925), P.C.I.J., Ser. A, No.5, at 51; the Martini Case, 25 A.J.I.L, 554 (1931), at 585; and the Temple of Preah Vihear Case, (1962), I.C.J. Reports, 6 at 36-37.

the loss incurred.[1] It is also evident that apart from some of the pre-*NIEO* cases which have already been discussed, judicial support for the concept restitution as an expression of the *full* compensation standard can also be found in some relatively modern cases. This fact led one commentator to take the view that with very few exceptions, every modern arbitral tribunal which has considered the issue of compensation has affirmed that customary international law requires an expropriating State to pay for the full value of the property in question to any foreign nationals or enterprises adversely affected by the measure in question.[2] This view further asserts that although no tribunal has expressly invoked the *Hull formula*, the ultimate conclusion to be drawn from post-*NIEO* cases remains the same – to wit, the requirement to pay for the full value of nationalized assets, measured (where possible) by market price. The stated intention of this approach, it has been further argued, is to achieve the ultimate remedy of restitution of any economic loss sustained through the act of

[1]- FATOUROS (1962), at 311; see also Chorzow Factory Case (Judgment of Sept. 13), supra, at 27-28, and at 47.
[2] P. Norton, (1991), at 488.

nationalization.[1] The viewpoint has obviously not gone undisputed, as will be seen latter in our analyses.

The *Texaco-Calasiatic*[2] dispute concerning the nationalization of foreign petroleum interests in Libya marks the starting point for post-*NIEO* judicial precedents which appear to support the traditional legal theory of reparation as equating to 'full' compensation in international law. The arbitration tribunal in this case recognized restitution as the best possible remedy (amongst all other remedies) because in the tribunal's view it expressed the basic principle of reparation.[3] In rendering its judgment the tribunal stated as follows:

> "The tribunal must hold that *restitutio in integrum* is ... under international law the normal sanction for non-performance of contractual obligations and that it is inapplicable only to the

[1]- Mendelson, "Compensation for Expropriation: The Case Law", 79 A.J.I.L., 414 (1985).
[2]- P. Norton (1991), pp.487-488.
[3]- Ibid, (Merits), supra, para 102.

extent that restoration of the *status quo ante* is impossible."[1]

Notwithstanding the criticisms of various scholars of the tribunal's judgment in the *Texaco-Calasiatic* arbitration, it has to be conceded that the case clearly lends judicial support to the underlying philosophy of traditional legal theory which is based on restitution (or, if restitution is impossible, then *full* compensation). The prefix of "normal sanction" which the tribunal attached to *restitutio in integrum* as a legal remedy for non-performance further emphasizes the secondary role assigned to alternative methods of settlement such as monetary

[1]- Ibid, paragraph 109; see further Jessup, Expert Opinion to Texaco/ Calasiatic Memorial on Merits, 18-46. At p.72, the Opinion states as follows: "It is a principle of international law that reparation must be made for an internationally illegal act and that restitutio in integrum is the primary or preferred form of reparation." For further support of this view, see J-F. Lalive, "Un grand arbitrage pétrolier entre un gouvernement et deux société privées étrangères", 104 J. DROIT INT'L, (1977), at 345-347. Criticisms of the judgment in this case have come from, among others, R. HIGGINS (1982-III), at 320, who, in criticizing the tribunal's reliance on the legal convictions of the claimants as evidence of the fact that restitution was a norm of customary international law, notes that such convictions hardly in themselves constitute evidence of international law. She also points out that the defendant government of Libya would undoubtedly have held equally strong convictions that restitution was inappropriate.

recompense under the orthodox conception of remedies for nationalized property in classical international law.

There are other relatively modern arbitration cases which have been cited as offering judicial support for the *full* compensation requirement in international claims practice. These include *ICSID* awards and majority opinions from the *Iran-U.S Claims Tribunal*. With regard to *ICSID* awards, it has been posited that the case of *Benvenuti & Bonfant v. People's Republic of Congo*[1], supports the "*full*" compensation requirement. This proposition seems, however, to be founded on shaky grounds given that the tribunal based its *dicta* on the premise that the "principle of compensation in the event of nationalization is in accordance with the Congolese Constitution and is one of the generally recognized principles of international law as well as of *equity*."[2] The proposition from advocates of full compensation (in support of their reliance on the *Benvenuti* case as persuasive precedent) appears to be based on the following argument - that the principles of restitution could be used in conjunction with the

[1]- 67 I.L.R 345 (1984).
[2]- Id, at 758.

tribunal's subsequent reference to "full compensation"[1], to imply that full or adequate compensation means at the very least the payment of the market value of the property expropriated.[2] It could, however, be equally argued that the principle of *equity*, (which the tribunal expressly stated played a role in its deliberations), qualifies to some degree the concept of *full* compensation as equating to market value recompense which has to be prompt and effective. Our understanding of the way equity operates is that it does not and would not support a *prima facie* claim to full compensation in all cases of foreign nationalizations; much will depend on the surrounding circumstances and other factors will surely be taken into account (including the history of the project and its past contribution to national development goals and objectives). Equity by its very nature is a flexible instrument and a discretionary remedy; it is inconceivable that it would lend its support to a rigid proposition founded on restitution; nor will it countenance an orthodox interpretation of restitution as equating to an iron cast formula which

[1]- Id, at 758-761.
[2]- F. Francioni, "Compensation for Nationalisation of Foreign Property: Borderline Between Law and Equity", 24 I.C.L.Q., 255 (1975).

uncompromisingly mandates the payment of *prompt, adequate and effective* compensation.

With regard to the Iran-U.S claims process, it has been argued that judicial support for the orthodox view of compensation in the ensuing claims settlement can be identified from majority opinions in cases such as the *AIG* claim, in which two out of three of the arbitrators found that "*it is a principle of public international law that even in a case of lawful nationalization the former owner of the nationalized property is normally entitled to compensation for the value of the property taken*", and that "*the appropriate method is to value the company as a going concern*."[1] In the *TAMS* case two of the arbitrators (Riphagen and Aldrich) in a much more forthright manner ruled that the claimant was "*entitled under international law and general principles of law to compensation for the full value of the property of which it was deprived.*"[2] However, it could be argued that the arbitrators' reliance on past precedents such as the *Chorzow Factory* and

[1]- Arbitrators Mangård and Mosk in American International Group v. Islamic Republic of Iran, 4 Iran-U.S. C.T.R. 96 (1983-III), at 109.
[2]- 6 Iran-U.S C.T.R, 219 (1984-II), at 225.

Norwegian Shipowners' cases in reaching these conclusions renders the judicial basis of their *dicta* somewhat suspect – if not unsound - in view of the fact that both of these early cases (as discussed above) do not appear to offer categorical or unequivocal support for the full compensation requirement.

Still with reference to the Iran-US Claims process, it is also argued that further support for the orthodox view of reparation for nationalization as amounting to an international law requirement for full compensation can be found in the case of *Sola Tiles* case[1]. In this case a majority of the arbitrators (Böckstiegel and Holtzmann) held that the "full" compensation standard laid down in the *Treaty of Amity*[2] between Iran and the United States - notwithstanding that it was founded in this instance on '*lex specialis'* or particular international law in the form of bilateral treaty relations - equated to the standard required by general international law.[3]

[1]- Sola Tiles Inc., v. Iran, 14 Iran-U.S C.T.R., 223 (1987-I).

[2]- U.S-Iran Treaty of Amity, Economic Relations and Consular Rights, Article IV, in paragraph 2 referred variously to "prompt payment of just compensation" and compensation in an "effectively realizable form" representing the full equivalent of the property taken.

[3]- 14 Iran-US C.T.R (1987-I) at 234.

In Sedco Inc., v. Iran,[1] Arbitrators Mangård and Brower also ruled that customary international law required the payment of full compensation for the deprivation of foreign economic interests. It is worth noting, however, that the potential orthodoxy of this ruling was in effect tempered by the restriction of the requirement for full compensation to discrete, selective or discriminate expropriations of alien property - as opposed to large scale nationalizations involving the restructuring of whole economic sectors.[2] Other cases cited[3] as offering support for the *full* compensation requirement include the partial award in *Amoco International Finance Corp.*[4], and the *Phillips Petroleum Case*.[1]

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[1]- 10 Iran-US C.T.R 180 (1986).

[2]- 25 I.L.M. (1986) at 634-635. See also INA Corp., v. Iran, 8 Iran-U.S C.T.R., 373 (1985-I), at 388 where it was held that expropriation involving investments of "a rather small amount" would attract full compensation - and that restitution and full compensation were available remedies in cases of unlawful expropriations (at 385). For large-scale nationalizations which are lawfully executed and involve commercial enterprises of fundamental importance to the nation's economy, it was suggested that appropriate compensation would be the proper remedy.

[3]- See P. Norton, (1991), at 483-485.

[4]- 15 Iran-U.S C.T.R., 189 (1987-II), at 253 in which the tribunal (Arbitrators Virally and Brower) held that international law requires restitutio in integrum in all cases of unlawful expropriation and "just compensation" in cases of lawful expropriation - "just compensation"

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So to what extent does international arbitration and claims practice process offer support for the *full* compensation standard? Before we can turn our attention to this question, we intend first of all to undertake a critical appraisal of orthodox view of the requirement for compensation in international law as promoted through traditional legal theory.

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being "compensation equal to the full value of the expropriated assets" measured as "going concern value" (at 289 et seq.). The tribunal nonetheless made reference to the uncertainty surrounding the principle of compensation in customary international law. This uncertainty is vividly brought to light by the arbitrators' inability in this case to reach agreement on the question whether 'full value' in cases of lawful compensation should include lost profits (with Arbitrator Virally dissenting on the question of lucrum cessans).

[1]- 21 Iran-US C.T.R 9 (1989), in which the tribunal endorsed the relevance of lost profits to the assessment of full compensation both in cases of lawful and unlawful expropriation. See further Payne v. Iran, 12 Iran-U.S. C.T.R., 3 (1986-III); and the Phelps Dodge Case, 25 I.L.M. (1986) at 626-627, both of which have been cited by Norton (1991) at 485, as "containing language supportive of a full compensation standard under international law", although the ratio decidendi of each resting on the application of the Treaty of Amity.

3.2 A Critical Appraisal of Traditional Legal Theory on the International Law on Compensation for Nationalized Property.

Traditional legal theory vis-à-vis the international law requirement for compensation in foreign expropriation cases has evidently made a sustained effort aimed at the advancement the orthodox view that compensation in international law equates to restitution. Viewed from a purely theoretical perspective, it has to be conceded that this orthodoxy seems sound enough in so far as the most effective legal remedy for an unlawful deprivation of foreign property or contractual rights would be restitution in kind or restoration to the *status quo ante*. In principle this much is obvious regardless of the impracticality of *restitutio in integrum.* It is for this reason that some of the problems associated with restitution does not in principle detract from the basic appeal of the restitution as a probable remedy. It is, therefore, as a remedial concept of law which requires practical implementation on the ground that the real weaknesses of the principle as a norm of international law begin to emerge.

Other inferences of conceptual weakness which militate against an orthodox insistence on the need for *full*

compensation may be drawn from the rigid nature of the conditions laid down in the *Hull formula*. We would argue that these prescriptions, if applied to the letter and in an indiscriminate manner, could in practice translate into the circumscription of the sovereign right of State to regulate economic activities within its territorial boundaries, including the right to nationalize.[1] In other words, the Hull formula has the potential to impose a disabling burden on the regulatory capacity of poorer nations thus stifling their ability to undertake large-scale economic restructuring through nationalization. Viewed from this perspective, we would further submit that the requirement of *full* compensation appears to be a conceptually flawed approach. Viewed from both a theoretical and a practical perspective, its chief flaw resides in the fact that by its very nature it implies an inbuilt tension and conflict with the doctrine of state sovereignty. This is in view of its innate or natural incompatibility with the exercise by poor nations of the sovereign right to regulate.

[1]- The right of sovereign States to regulate economic activities within their territories is recognized by international law albeit subject to conditions.

Whilst we acknowledge that the right to regulate or to nationalize property is itself subject to conditions imposed by international law, we nonetheless hold that the nature of the conditions imposed ultimately determines the feasibility or practicability of exercising the right thus granted. In our view this in turn determines the authenticity, as well as the practical and functional value, of the right in question. The ultimate effect, if not the aim, of any pre-conditions must not be to stifle the possible exercise of the rights granted in law. In the absence of a genuine opportunity to exercise the right to regulate (especially for poor nations) we hold that this in effect amounts to an attempt to foreclose any genuine opportunity of exercising such rights. It seems to us that the ultimate effect of traditional legal theory through the principle of restitution and the *Hull* formula is to circumscribe (or to otherwise severely restrict) the right of sovereign states to regulate. It is equally our submission that such as an outcome is legally unsustainable within the context of most national legal systems and also possibly in public international law.

Theoretical expositions of the orthodox view of compensation as an international law requirement for nationalization habitually rely on explicit linkages to State practice and customary international law for authority.

Customary international law in particular has frequently been identified in academic literature as the conceptual cradle of the *full* compensation requirement.[1] It is indeed the case that long-established custom and judicial precedents are presumed to confer legitimacy and certainty on legal norms. However, in the case of the full compensation requirement, the inference could equally be one of a conceptual paralysis - most notably evidenced in the failure of the principle to evolve in line with historical developments and adjust to modern realities particularly in the new geo-political context of the post-independence era. This perception of conceptual paralysis is accorded further credence by the widely acknowledged absence of consistency of practice or general acceptance within the community of nations of the full compensation requirement. This in turn seems to have undermined the principle and to deprive it of certainty in practice and hence, arguably, of its legitimacy as a generally recognized rule of law.

[1]- George Ray, "Some Reasons for the Binding Force of Development Contracts Between States and foreign Nationals", 16 BUS. LAW 942 (1961); and F.A. Mann, "A Theoretical Approach to the Law Governing Contracts Between States and Private Parties", in 11 REV. BELGE DU DROIT INT'L 562 (1975).

When viewed from a political perspective, a further distortion to the legal foundations of the concepts of restitution and *full* compensation as rules of customary international law may be perceived. This distortion derives from the association of both principles with past claims settlements which were often preceded by military force or some other form of political coercion. It could thus be argued that the effect of such extra-judicial methods and practices has been to compromise the normative value of the requirement and hence to deprive traditional legal theory of its legitimacy in the modern era. This in turn raises serious questions over the sustainability of the concepts of restitution and full compensation as current norms of international law. In the modern era the political and legal fallout from this historical shadow of coerced settlements has been to render arbitration and claims practice based on the full compensation requirement widely suspect - thus exposing the international investment regime itself to often critical and uncomplimentary commentaries.[1]

[1]- GARCÍA-AMADOR (1984), at 17 where the author identifies three key areas of international law where is there an absence of =

In our view the impracticality of applying the orthodox view of compensation in every given instance clearly seems to counsel a more flexible and practical approach in favour of the relaxation of what appear to be the unintended strictures of the Hull formula. We believe this view to be persuasive - even compelling – on account of the historical, political and legal controversy which has been a perennial feature of this area of international law.

In concluding this section, one further development calls for observation. It is not unusual to find arguments to the effect that the *appropriate* compensation standard adopted in various UNGA resolutions on Permanent Sovereignty over Natural Resources (*PSNR),* New International Economic Order *(NIEO) and* Charter of Economic Rights and Duties of States (*CERDS)* equate - or can otherwise be understood as

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universally recognized authority for the governing norms - to wit, the principle of State responsibility (including compensation for nationalized assets); the doctrine of State succession; and maritime jurisdiction; see also Phillip Jessup, Modernization of the Law of International Contractual Agreements, 41 AM. J. INT'L L. 378 (1947); S. SINHA, NEW NATIONS AND THE LAW OF NATIONS (1967); R. ANAND, NEW STATES AND INTERNATIONAL LAW (1972), at 57; N. REMBE, AFRICA AND THE LAW OF THE SEA (1980), at 8.

upholding - the *full* compensation requirement postulated by traditional legal theory. In the *INA Corporation v. Iran*[1] claims settlement, for instance, Arbitrator Holtzmann observed that the meaning of *full* compensation has frequently been ascribed to the term *appropriate* compensation by some scholars. These scholar seem to have adopted the view that relevant *UNGA* resolutions "recognized and reinforced the strict duty to compensate"[2] - and that *appropriate* compensation can indeed be understood as being the equivalent of the customary international law *full* or *adequate* compensation requirement.[3]

We believe that such an attempt at the assimilation of the two standards is ill-conceived both on conceptual and theoretical grounds. Even if it were to be assumed that the *full* and *appropriate* compensation standards were not mutually exclusive, it will still be apparent that the underlying philosophy and ethos - as well as the substantive principles – associated with each standard is fundamentally different. It can also be argued that suggestions of an inherent affinity or

[1]- 8 Iran-US C.T.R 373 (1985), at 395.

[2]- Olmstead, Krauland and Orentlicher, "Expropriation in the Energy Industry: Canada's Crown Share Provision as a Violation of International Law", 29 McGill L.J. 439 (1984),at 458.

[3]- S. Schwebel, "The Story of the U.N.'s Declaration on Permanent Sovereignty over Natural Resources", 49 A.B.A.J. 463 (1963), at 465-466.

similarity between the two standards were effectively dismissed by the *UN* General Assembly's rejection of a US sponsored amendment which would have had the effect of assimilating the appropriate compensation to the full compensation standard.[1] It is indeed the case that subsequent to the UNGA resolutions the *World Bank Investment Guidelines* of 1992 appears to have moved closer towards this assimilation in view of its provision in *Guideline IV (2)* which stipulates that "compensation for a specific investment taken by the State will ... be deemed to be 'appropriate' if it is adequate, effective and prompt." These guidelines, however, do not constitute a source of international law on the question of compensation for nationalization. No normative significance or value can thus be attached to this particular provision. In the section which follows, we shall now turn our attention to the normative challenges posed to the orthodox view of compensation as expressed through traditional legal theory.

[1]- Schachter (1984), at 127 et seq.; Norton (1991), at 478, n.27 also wonders why the various resolutions, even if they were the normal product of a political impasse, did not use the terms full and adequate if that had been the intention. See further HIGGINS, (1982-II), at 289; and M. AKEHURST, A MODERN INTRODUCTION TO INTERNATIONAL LAW, (1987), at 94.

4. TRADITIONAL LEGAL THEORY UNDER THREAT: THE EMERGENCE OF NEW NORMS ON COMPENSATION FOR NATIONALIZATION.

The profound transformation in the geo-political landscape following the immediate aftermath of the decolonization process witnessed the first attempts at a concerted challenge to the established foundations of traditional legal theory on the question of compensation for nationalization in international law. Viewed from the perspective of the newly independent capital-importing nations, the orthodox view of recompense for nationalized assets as equating to full compensation signified a somewhat dogmatic attachment to colonial era principles. Critics perceived in the restitutionary foundations of traditional legal theory an incompatibility with the increasing diversity of value systems away from Eurocentric market driven hegemony. Emerging political and legal opinion in the newly-independent capital-importing nations also posited that whereas *adequate* compensation may have afforded the best possible protection to the investor in the past[1], the retention of the principle in the

[1]- See, for instance, F. Dunn, "International Law and Private Property Rights", 28 COLUMB. L. REV. 166 (1928).

modern era could have the undesired effect of hindering the restructuring of inherited pre-independence investment agreements (particular in the petroleum and mineral development sectors). This in turn would hinder the pursuit of much desired socio-economic goals and development objectives of the new States.[1] Against this historical backdrop, various theoretical expositions began to emerge and to challenge the conceptual and legal basis of the orthodox 'full' compensation requirement. The ensuing doctrinal debate brought to light questions relating to the interaction (and conflict) between State or community objectives and private economic interests; it also highlighted the fraught relationship between private property rights and the sovereign rights of States, and between national law or domestic public policy and international law.[2] Most of the new arguments claimed as their philosophical foundation the social function of property in

[1]- See M. Sornarajah (1979), at 118.

[2]- See S. Asante, "Traditional Concepts versus Development Imperatives in Transnational Investment Law", in R-J. DUPUY, (ED), COLLOQUIUM ON THE RIGHT TO DEVELOPMENT, 352 (1979); O. Schachter, "The Evolving International Law of Development", 15 COLUMB. JN. TRANS. L., 1 (1976); Muller, "Compensation for Nationalization: A North-South Dialogue", 19 COLUMB. L. REV., 35 (1981).

international law - a concept within which the protection of private property rights had to cede way to the supremacy of the community interests. [1]

Within the emerging framework of doctrinal expositions, the magnitude of confusion and uncertainty attending the issue of compensation for nationalization in international law was interpreted by some critics to be symptomatic of the absence of consensus and lack of general acceptance of the orthodox principles of customary international law. The practical problems of restitution associated with the orthodox view were also seen to symbolize the inherent limitations of traditional legal theory on issues relating to the international regulation of the FDI regime.[2] The

[1]- Seidl-Hohenveldern, "The Social Function of Property and Property Protection in Present-Day International Law", in ESSAYS ON THE DEVELOPMENT OF THE INTERNATIONAL LEGAL ORDER, 47 (1980).

[2]- See, for example, White's criticisms of the Hull formula on account of the imprecise nature of the requirement of adequacy in compensation settlements, in NATIONALIZATION OF FOREIGN PROPERTY (1961), at 160 where, in the author's view, "... possibly due to the vagueness of the international law standard of adequacy, States have not acted consistently but have paid or accepted respectively amounts of compensation in accordance with economic, political and other non-legal motives."

perceived shortcomings of traditional legal theory have also been identified by a modern international arbitration tribunal as follows:

> "The rules of customary international law relating to the determination of the nature and amount of compensation to be paid, as well as the conditions for its payment, are [not] well settled. They were, and still are, the object of heated controversies, the outcome of which is rather confused. Terms such as 'prompt, adequate and effective', 'just', 'adequate', 'adequate taking into account all pertinent circumstances', 'equitable', and so on, are currently used in order to qualify the compensation due, and are construed with broadly divergent meanings."[1]

Set against this background of confusion, uncertainty and controversy on the international law question of compensation for nationalization was a clearly discernible trend in the post-colonial era which symbolized the decline in the universal

[1]- Amoco International Finance Corporation v. Iran, supra, at 223.

appeal of traditional legal theory and its advocacy of the payment of full compensation for nationalization. This decline became the more visible in the decade of the 1960s-70s with the advent of various *UNGA* resolutions on *PSNR, NIEO and CERDS* whose explicit intentions were to establish a new foundation of international law for the international investment regime. The particular focus of the new proposals was on nationalization of foreign assets in the upstream petroleum and natural resources development sectors. Emerging from these reformist endeavours was the proposed new standard of compensation for nationalization - to wit, the "*appropriate"* compensation standard. The tribunal's critique of customary international law governing compensation in the *Amoco Case* (above) clearly echoes the criticisms by scholars and commentators. A combination of these factors ultimately contributed to the decline of traditional theory in the post-colonial era.

4.1 Continuity versus Change: Doctrinal Critique of Traditional Legal Theory and its Aftermath

In the post-independence era doctrinal challenges to the orthodox view of compensation was mounted on two fronts: first, at perceived conceptual weaknesses which tended to undermine the theoretical articulation of the orthodox view; and secondly, at the manifest inconsistency of State practice *vis-à-vis* the question of *full* compensation. From a theoretical perspective, doctrinal criticisms - some of which pre-date the *UNGA Resolutions* on *PSNR, NIEO, and CERDS* - was directed at the blanket articulation of the principle of *full* compensation as represented in the requirements of "prompt, adequate and effective". It was, for example, suggested that an important qualification to the duty to compensate is necessary in situations where fundamental changes in the political system and economic structure of the state or far-reaching social reforms rendered interference on a large scale with private property interests inevitable. It was also forcefully argued that in such cases a solution must be sought an found in the grant of partial compensation.[1] And it was further

[1]- L. OPPENHEIM, INTERNATIONAL LAW (8th Edn, H. Lauterpacht, ed, 1955), at 352-354; and García-Amador, 4TH =

suggested that an exception to the Hull formula should be possible in situations in which an overwhelming and debilitating financial burden will be imposed on the expropriating State if full compensation was required.[1]

The principal thrust of the argument for the reform of the international law in this area, however, focused mainly on the perceived new role of international law in a post-colonial context. According to these arguments, since national economic development objectives form part and parcel of the accepted aspirations and agenda of the new international community, rules which facilitate development must be preferred over those of a circumscriptive disposition.[2] The

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REPORT ON INTERNATIONAL RESPONSIBILITY TO INTERNATIONAL LAW COMMISSION, (1959), 2 Y.B.Int'l L. Comm. at 1-36.

[1]- Louis Sohn & R. Baxter, Convention on the International Responsibility of States for Injuries to Aliens, 55 AM. J. INT'L L. 545 (1961).

[2]- Sornarajah (1979), at 109-113; and R. Dolzer, (1981) at 562. Doctrinal criticism of the orthodox view has sometimes tended to be laced with North-South ideological undertones. It is has been claimed, for example, that the "adequate" compensation standard reflects Western free-market notions of property rights which are alien to peoples of non-European origins, and that the conflict between views on compensation in its larger context reflects the unwillingness on the part of new States to accept norms developed during a period of

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contention thus seems to be that the conceptual basis of traditional legal theory had been undermined and eroded by modern trends in the political economy of international economic relations - a process most vividly exemplified by the then global efforts to establish a new international economic order. These claims, although fiercely disputed, nonetheless gained currency as time progressed.

At the sharp end of various criticisms leveled against the *Hull formula*, from a purely normative point of view, has thus been its perceived status as a norm of general or customary international law. Sustained emphasis has been placed on the fact, for example, that early cases contain no expression or reference to the *Hull formula* or any indication to the effect that in the event of lawful nationalization, *full* compensation will be required.[1] The weakness of judicial backing for the formula as a recognized rule of customary

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European hegemony. See further Guha-Roy, (1961), at 863; and R. P. Anand, ASIAN STATES AND INTERNATIONAL LAW, (1973).

[1]- See further Wengler, Völkerrecht, (1964), at 1008, n.3, (cited in O. Schachter, (1984), at 123) at which the author also points out that early cases relied mainly on just or fair compensation in accordance with the terms of relevant agreements.

international law is clearly underlined by the sketchy character of judicial precedents of importance which offer explicit and unequivocal support for the *full* compensation requirement. This view is further emphasized by Rousseau's statement to the effect that the "prompt, adequate and effective" formula has not won general acceptance either in case law or in State practice.[1]

The uncertain state of the international law on compensation for the nationalization of foreign economic interests in the period leading up to the adoption of the *UNGA Resolutions* is thus clearly manifested through the absence of general acceptance of the orthodox view of compensation in scholarly writings. This turn points to the fact that traditional legal theory was already in a state of decline in terms of its conceptual appeal prior to the adoption of the various *UNGA* resolutions. The increased intensity of doctrinal critique in the immediate aftermath of the *UNGA* debates likewise point to the absence of clear and consistent political and legal support for full compensation requirement in State practice. What was

[1]- C. ROUSSEAU, DROIT INTERNATIONAL PUBLIC, (1983), at 250.

to be by far the most incisive and sustained criticism of traditional legal theory in the post-*PSNR* period came from Professor Schachter, in whose view the requirement lacked consistency in practice. He was of the view that European state practice frequently showed substantial deviations from what would normally be understood as *full* compensation, or as *prompt* and *effective*.[1] In articulating this view, he further argued that a critical examination of State practice in cases of post-war nationalization show that compensation was often *less than full value* (or fair market value), and that payments were routinely *deferred* and often made in *inconvertible currency*.[2] In no way can the recompense emanating from such practices be regarded as being prompt, adequate or effective.

[1]- O. Schachter (1984), at 124.

[2]- See also H. Baade, "Indonesian Nationalization Measures Before Foreign Courts", 54 A.J.I.L., (1960), 801; Dawson and Weston, "'Prompt, Adequate, Effective': A Universal Standard of Compensation?", 30 FORDHAM L. REV., 727 (1961-62); Doman, "Post-War Nationalization of Foreign Property in Europe", 48 COLUMBIA L. REV., 1125 (1948), at 1128; and S. Rubin, PRIVATE FOREIGN INVESTMENT: LEGAL AND ECONOMIC REALITIES, (1956), at 11-23.

In his critique of traditional legal theory, Sornarajah lends support to Schachter's views through his observation that capital-exporting countries in many instances (including in claims practice[1]) have accepted or permitted their citizens to accept compensation amounting to less than the market value of nationalized property.[2] These practices, he argues, could be seen to have depreciated to a great extent the normative value of the full compensation requirement. This line of argument, which has also been pursued by Higgins, holds that there is little evidence to show that restitution is perceived as a required remedy in international law or that it is anticipated as being likely to be granted by tribunals involved in international arbitration and claims practice.[3]

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[1]- In the Marcona Settlement, for example, in which the USA was the claimant, compensation of less than the full monetary value of the assets expropriated was accepted. For a detailed discussion of the dispute and its settlement, see D. A. Gantz, "The Marcona Settlement: New Forms of Negotiation and Compensation for Foreign Property", 71 A.J.I.L., 474 (1977).

[2]- Schachter (1979), at 109.

[3]- HIGGINS (1982-III), at 321. The author cites cases such as Lena Goldfields, Losinger et Cie v. Government of Yugoslavia, (P.C.I.J. Ser. C., No.78 at 32); Sapphire Petroleum v. NIOC, 35 I.L.R., 136; and some of the Libyan oil nationalization cases as evidence of the fact that in practice, restitution is not often sought. She further points out, as an example of the inconsistency in State practice on the question, the fact that in the Anglo-Iranian Oil Company Case, supra, the UK as

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Additionally, when viewed from the perspective of State practice, the frequency of lump sum agreements in claims practice in the post-war years could be seen to provide further evidence of a deviation from the *Hull formula*. This, it could be argued, signaled the decline of traditional theory within the context of the increasing necessity for political or economic expediency in international claims settlement. Recompense for nationalization through lump sum and partial settlements thus provide clear evidence of the inconclusive nature of State practice on the question of compensation for foreign expropriations in the post-war period.[1]

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the claimant State insisted on the fact that the abrogation of the oil concession agreement was unlawful and that full restitution was required, but in the BP v. Libya, monetary compensation was considered as a possibility in the Note of Protest from the UK Government to Libya, which read as follows: "Her Majesty's Government must, therefore, call upon the Libyan Government to act in accordance with the established rules of international law and make reparation to British Petroleum Exploration (Libya) Ltd either by restoring the company to its original position in accordance with the Concession No. 65 or by payment of full damages for the wrong = = done to the company"; cited in Higgins (1982-III), at 320. In the Higgins' view, both the Anglo-Iranian Company Case and the Barcelona Traction Case can be considered as being neutral on the question of restitution as a requirement of customary international law.

[1]- See further R. LILLICH AND B. WESTON, INTERNATIONAL CLAIMS: THEIR SETTLEMENT BY LUMP SUM AGREEMENTS,

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Other deviations from the requirements of the *Hull formula* in claims practice have included, for example, the offer of oil in place of a monetary settlement in the Libyan oil nationalizations.[1] And, to further emphasize the demonstrable inconsistency of State practice *vis-à-vis* the *Hull formula*, one commentator has observed that in most instances of expropriation in a North-South context, some abstract formula such as "book value". It is further posited that such "book value" settlements have been used to justify amounts of compensation that were in fact below those required under the Hull rule and its prescription of adequate compensation in the sense of full market value.[2] These practices clearly provide ample evidence of the fact that modern settlements have not

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(1975), at 207-256; and B. WESTON, INTERNATIONAL CLAIMS: POST-WAR FRENCH PRACTICE, (1971). See, however, R. Dolzer, (1981), at 559, in whose view the significance of wartime lump sum agreements for the development of customary international law is not easy to discern. According to the author, "... lump sum agreements tend to have an 'exceptional character' inasmuch as they relate to a variety of damages that occurred during war or warlike situations", and that "they also reflect the specifically political factors that characterize the necessity of resuming diplomatic or political ties under certain conditions." In his judgment, "the premise formula reached in any such agreement thus has no particular value for the determination of customary international law."

[1]- See Introductory Note, 17 I.L.M. (1978), at 2.

[2]- Dolzer, (1981), at.560.

always conformed to the orthodox view of compensation in as much as the formula has not been observed with consistency in practice. It could thus be argued that evidence of the *Hull rule*'s continuing validity, from the point of view of the mode and amount of compensation due, "*falls short of the mark that an international court would require to be convinced that state practice confirms the existence of the old rule*."[1]

The unavoidable conclusion to be drawn from these theoretical and conceptual criticisms of traditional legal theory is thus that State practice regarding compensation for nationalization has substantially qualified the requirement of restitution (or of *full* and prompt indemnification) either as a judicial remedy, or as an international law pre-requisite for the legality of foreign expropriations.[2] There has been incremental evidence over time that the principle requiring the payment of the full market value of nationalized property, if it was ever an accepted part of international law, has clearly undergone

[1]- Id at 561-562.

[2]- See C. DE VISSCHER, THEORY AND REALITY IN INTERNATIONAL LAW, (Corbett transl. of 3rd French Edn., 1968), at 203. In the author's view, nationalization hardly ever permits more than partial compensation calculated less by the extent of the loss suffered than by the capacity to pay and the goodwill of the nationalizing State.

substantial change in the course of time.[1] As a consequence of this, Friedmann posits that "... it would be nothing short of absurd to pretend that the protestation of the rule of full, prompt and adequate compensation ... in all circumstances is representative of contemporary international law."[2] Indeed, we find no categorical evidence to support the view that the full compensation requirement was ever an international custom recognized by States as evidence of a general practice accepted as law.

In the above passages, we attempted a critical examination of the shortcomings of traditional legal theory as seen from the perspective of analytical doctrine. Drawing the various strands of these arguments together, Sornarajah sums up as follows:

> "In *classical* international law, it is the State of the alien whose property is expropriated without

[1]- Sornarajah, (1979), at 109, n.12. See also D. A. Gantz, (1977).

[2]- W. Friedmann, "National Courts and the International Legal Order", in GEO. WASH. L. REV., (1966), at 454. See also O. Schachter, (1984), at 125-126; S. Rubin, (1956), at 23-28; Weston, "The CERDS and the Deprivation of Foreign-Owned Wealth", 75 A.J.I.L., at 455 et seq.; T. Farer, "The United States and the Third World", 54 FOREIGN AFFAIRS (1975), p.84; and Sornarajah, (1979), at 116-119.

> compensation which suffers the injury. Given this principle, a State's tacit consent to settlements on principles other than market value as compensation could give rise to inferences of the State's acquiescence in other standards of compensation."[1]

Sustained arguments and propositions to the effect that the *Hull formula* is not a requirement of international law which applies to all cases of nationalization is can be said to mark the onset of the decline of traditional theory in the post war period after 1945. This decline was to culminate in the *UNGA* debates in search of an alternative standard of compensation. Following these debates, the advent of relevant *UNGA* resolutions proposing the replacement of the traditional standard with the "*appropriate"* compensation standard clearly signaled the lowest point in the decline of traditional theory.

[1]- Sornarajah (1979), at 109.

5. COMPENSATION FOR NATIONALIZATION IN INTERNATIONAL LAW: THE MODERN CONTEXT

The declining appeal of traditional legal theory created the capacity and impetus for the articulation of new norms of international law governing compensation for nationalization. At the same time it was argued that in view of the opposition of newly-independent States to the orthodox view of compensation, the prescriptions of traditional legal theory could no longer continue to be regarded as a valid basis for the establishment of a viable normative system for the international investment regime.[1] It was thus largely due to this combination of factors – i.e. sustained doctrinal critique, the inconsistency in the practice of States vis-à-vis the full compensation requirement, and changing complexion of the international political landscape - that the standard of *appropriate* compensation emerged as a possible alternative to the Hull formula.

[1]- See further Sornarajah (1979), at 109-113; and Dolzer, (1981), at 564-565.

The proposed new norms quickly won support from the majority of States within the *UN* system. However, the persistent opposition of the capital-exporting States effectively precluded the reaching of any categorical conclusion in favour of the displacement of the orthodox standard of full compensation by the postulated new principles. To forestall the normative development of the new principles it was argued that the development of customary international law requires the consent of all significant interest groups of States.[1] The end result typifies the confusion and uncertainty which has for so long been an indelible feature of the international legal framework governing the international investment regime, most notably on questions of State responsibility and the acceptable standard of compensation for nationalization. Given the opposition of capital-importing nations to the old principles governing State responsibility compensation on the one hand, and the inability of the proposed new norms to acquire a normative value due to lack of support from the capital-exporting States on the other, the predictable result was political deadlock. From a normative perspective this meant international law as it applied in this area was in a state of flux.

[1]- Norton, (1991), at 505.

The legal impasse borne out of this stalemate clearly implied that whereas the old law was no longer supportable, a new legal framework could not emerge in its place.

Our view is that irrespective of this uncertain background, a modern understanding of the requirement for compensation for nationalization in international law qualifies to a considerable extent the orthodox view which prevailed under traditional legal theory. As seen above, the practice of lump sum agreements between States could be interpreted as indicating the possible existence of an international law standard other than (and falling short of) the orthodox *full* compensation requirement.[1] In a similar vein, the post-nationalization claims of many countries to exclusive national competence in determining the measure of compensation due for nationalized property (and the insistence in such cases on the exclusive application of a national standard of compensation) may be construed as contributing to a further erosion of the international appeal of the full compensation standard. It could further be argued that the normative claims of the alternative concept of *appropriate* compensation, if

[1]- See Sornarajah (1986), at 214.

nothing else, served to further weaken the foundations of traditional legal theory in terms of its exclusive and singular appeal in international arbitration and claims practice. The cumulative effect of these developments, we would submit, has been to alienate to a certain degree the norm of full compensation which in any event has always rested on insufficient conceptual foundations.[1]

Viewed from another perspective, however, a critical analysis of modern contractual practice and treaty relations between States equally reveals a lack of consistency in the practice of natural resources producing countries vis-à-vis their stated political preference for the alternative standard of "*appropriate* compensation. A review of FDI agreements concluded with foreign investors reveals frequent references to the full compensation standard. In view of this inconsistency, our perception of the compensation provisions contained in modern natural resource development agreements leads us to belief that such compensation provisions aspire more towards the transactional management of the sovereign risk of expropriation than towards the promotion of the norms of

[1]- Id

international law within the contractual framework. In other words, their chief aim is to inspire confidence in the FDI investor as a way of promoting and attracting inward investment and not to serve as a normative standard for the measurement of potential compensation in the event of nationalization.

It is now proposed to examine a number of what could be perceived to be modern developments in international claims practice whose net effect have arguably been an erosion the normative value of the full compensation as the required standard of recompense for the nationalization of foreign owned assets.

5.1 The Corrosive Impact of the Practice of Lump Sum Settlements on the Orthodox Interpretation of Recompense for Nationalization.

In the *Barcelona Traction Case* the International Court of Justice was of the view that lump sum agreements do not contribute to the creation of international law rules because of their *sui generis* character.[1] We would nonetheless submit

[1]- (1970), I.C.J. Reps., 3. In the Court's view, such agreements in normative terms constituted lex specialis.

(and there is considerable academic opinion which appears to be supportive of our viewpoint) that the significant increase in the number of such agreements in the post war years - and the magnitude and relevance of their contribution to international claims practice[1] - is indicative of a conspicuous departure from the orthodoxy of the full compensation requirement.[2] It is thus noteworthy that whereas the Court in the *Barcelona Traction Case* was disinclined to accept the contention that lump sum agreements could be regarded as a norm creating practice, some eminent commentators have nonetheless taken exception to such a view. Amongst these scholars are Lillich and Weston, in whose opinion the "*truly extraordinary consistency in these agreements*" could be interpreted as amounting to customary State practice.[3] We would thus summit that lump sum settlements - in view of their

[1]- It has, for example, been estimated by R. LILLICH and B. WESTON, INTERNATIONAL CLAIMS: THEIR SETTLEMENT BY LUMP SUM AGREEMENTS (1975), at 43, that such agreements contributed to 95 per cent of total claims settlements in the immediate post-war period. See also R. Lillich, "Lump Sum Agreements", 8 ENCYCLOPEDIA OF PUBLIC INT'L LAW 367 (1985).

[2]- Schachter (1984), at 124.

[3]- LILLICH and WESTON (1975), at 36. The rigid approach taken by the Court has been criticized by, amongst others, Dolzer (1981), at 560, in whose view the Court did not explain why "such a large mass of state practice should not reveal, in a general way, any opinion prevailing in state practice."

magnitude, regularity and consistence - have possibly acquired the character of an international custom derived from a general practice deserving of the status of a norm of international law. Assuming that our hypothesis is correct (or at the very least sustainable) then there is no obvious reason why lump sum agreements should not be accorded a normative significance derived from the crystallization of State practice into a rule of customary international law. It is indeed the case that the practice of lump sum settlements is based on special agreements (*lex specialis*); but given the fact that 95% of international claims in the post war period have been resolved on the basis of lump sum payments[1], it is nonetheless arguably that the generality of such settlements amounts to a practice universally accepted as the international norm. Whatever be the case, the popularity and generality of lump sum payments cannot be denied nor can their potential appeal as a norm of customary international law. Viewed from this perspective, its corrosive effect on the normative function of the full compensation standard becomes apparent.

Our review of relevant literature on the subject shows that some doctrinal writers have equally been emphatic in

[1]- R. LILLICH and B. WESTON (1975), p. 43.

emphasizing the normative significance of lump sum agreements. Fatouros (1962), for example, is of the view that although there can be little doubt that lump sum agreements have tended to be based mostly on political compromise and the economic necessity of resuming international economic relations, this does not mean that such agreements represent nothing more than temporary political expediency.[1] He further points out that the considerable uniformity of practice involved in such settlements could indeed be considered as having established a precedent, "*at least insofar as [the settlements] indicate the locus of possible agreement between states with different political and economic tendencies.*"[2]

Pursuing a similar line of argument, Sornarajah (1986) is of the following opinion:

> "The practice of lump sum settlements certainly cannot be ignored. Though the lump sum agreements made in connection with war time expropriations must be distinguished from lump sum agreements following nationalizations of

[1]- At 330-331.
[2]- Id.

> property [footnoted omitted], the agreements following nationalizations are of value in the formulation of an acceptable compromise in this area of the law as they most often were agreements between socialist states and capital-exporting states. Indications are that the practice will continue."[1]

Notwithstanding his reservations as to the normative value of lump sum agreements as a source of international law, Dolzer has nonetheless acknowledged the possibly erosive impact or derogatory effect of this post-war practice on the normative appeal of traditional legal theory in postulating full compensation as an international law requirement for nationalization. In his view it is deductible from post-war practice, vis-à-vis the mode and amount of compensation in foreign expropriation cases, that the normative appeal of the Hull formula falls well short of the mark that an international tribunal would require as compelling evidence that State

[1]- At 215. For the relevance of the distinction between lump sum settlements arising out of post-war claims and those relating to peace time nationalizations, see W. Bishop, INTERNATIONAL LAW, (1970), at 960; and Dolzer, (1981), at 559-560.

practice conforms to the existence of a *full* compensation requirement.[1]

Significant to the persuasive appeal of these theoretical arguments is the existence of a number of important lump sum agreements which have been concluded since the 1970s. In 1979, for instance, lump sum agreements were reached concerning the settling of claims between China and the United States.[2] Also noteworthy is the agreement reached in 1981 between the former Czechoslovakia and the United States[3] - as well as other lump sum settlements relating to the Cuban nationalization programmes.[4]

The relevance of lump sum agreements to arguments concerning the diminished value of traditional legal theory and its *full* compensation requirement lies in the fact that in

[1]- (1981), at 561-562.

[2]- See 18 I.L.M. 551 (1979). See also Shanghai Power Company v. United States, 78 A.J.I.L., 678 (1984).

[3]- See V. Pechota, "The 1981 U.S-Czechoslovak Claims Settlement Agreement: An Epilogue to Post War Nationalization and Expropriation Disputes", 76 A.J.I.L., 639 (1982).

[4]- For a discussion of some of these settlements, see M. Gordon, "The Settlement of Claims of Expropriated Foreign Property Between Cuba and Foreign Nations Other than the United States", 5 LAWYER OF THE AMERICAS, (1973), 457.

practice, these settlements have often tended to involve acceptance by the claimant State of partial compensation - i.e. either compensation of less than full market value for the nationalized assets or of less than the amount of compensation initially sought by the claimant. Analysis of lump sum settlements agreed in the immediate post-war period clearly offer support for this assertion.[1] Pertinent examples include the following:

- In 1948 United States agreed a settlement with Yugoslavia, in which the final settlement sum amounted to 42.5% of the original claim;
- The United Kingdom on its part has agreed partial settlements with the following countries: Argentina in 1948 (for 60% of the initial claim); the former Czechoslovakia in 1948 (33.3%); France in 1951 (70%); Mexico in 1947 (30%); Poland in 1948 (33.3%); Uruguay in 1949 (60%); and the former Yugoslavia in 1949 (50%).[2]

[1]- See further Z. KRONFOL, PROTECTION OF FOREIGN INVESTMENT (1972), at 111-112.
[2]- Id.

- Settlements involving American post-war claims have typically amounted to 40% of the initial compensation claimed.[1]

The practice of lump sum agreements, in our view, indicates at the very least a qualification of the requirement f *full* compensation. And we are not alone n holding this view. Sornarajah (1986) for instance, is of the opinion that if only for the reason that the continuing trend in lump sum agreements indicates an understanding on the issue of compensation between States with opposing ideologies - and even if it would be too optimistic to regard such settlements as given rise to any rule of law - their significance to international law is nonetheless assured. In elaborating this view the author further opines:

> *"Though in the making of these agreements, capital exporting countries disavow any intention to deviate from the norm of full compensation, nevertheless, the consistent theme of the agreements involves the acceptance of partial compensation [footnote omitted]."*[2]

[1]- See V. Pechota, (1982) at 640, n.6.
[2]- Sornarajah (1986), at 215.

The acceptance of partial compensation by capital-exporting States in lump sum agreements - even if this could not be construed as constituting an implicit rejection of the traditional international law prescription for *full* compensation - clearly amounts to the recognition of alternative methods of settlement. In terms of their normative influence and relevance to international claims practice, Pechota (1986) posits the following opinion:

> "It is maintained that the global settlements following the post-war nationalizations in European countries are 'negotiated compromises and as such do not constitute a departure from the traditional international law principle'*[footnote omitted];* yet while they have created no new law common to the West and the East, their prevalence in the settlement practice cannot fail to undermine each side's case concerning the content of relevant international rules. Several scores of such global settlements have been reached through negotiation and compromise. It would surely be wrong to dismiss them as diplomatic decisions that are addressed to private

pecuniary claims and have no legal effect beyond the unique circumstances giving rise to them."[1]

In our analysis of lump sum claims we take cognizance of the fact that lump sum settlements representing a fraction of the initial amount claimed in compensation to a certain extent reflects the tendency on the part of claimants to exaggerate the original claim. But even after making due allowance for such tactical and negotiating strategies, the magnitude of the difference in the amount initially claimed and that which is finally accepted in settlement (illustrated in the examples given above) provides in each case a clear evidence of a substantial deviation from the *full* compensation requirement. This submission applies, *à fortiori,* to cases where the final settlement clearly falls short of the full market value of the nationalized assets.

It is our view that the practice of lump sum agreements is neither negligible nor inconsequential to the assessment of the continuing normative appeal of traditional legal theory on the key international law question of compensation for

[1]- At 642-643.

nationalization. The important attributes of uniformity and consistency of practice which has been characteristic of lump sum agreements in the post-war years clearly stand as a sharp contrast to the uncertainty and inconsistency of practice which have been the undeniable features of the orthodox *full* compensation requirement. It is in view of his contrast that a prominent commentator has suggested that for anyone to maintain (against the background of post-war State practice) that the *Hull formula* is the supreme law would be a view which seems far removed from reality.[1]

5.2 The Normative Challenge to Classical international Law on the Question of Compensation for Nationalization

In the post-independence period the postulation of new norms supporting a standard other than the customary international law *full* compensation requirement constituted the principal basis of the normative challenge posed by new geo-political landscape to the foundations of traditional legal theory. The specific nature of this challenge rested on the

[1]- Schachter (1984), at 124.

following claims made by what was then known as emergent principles of international law:

> (a) that whereas some measure of compensation should be due for the economic loss sustained by a foreign national or enterprise following an exercise of the sovereign prerogative of regulation or nationalization, the acceptable standard to apply for the measurement of compensation in such cases should be that of *appropriate* compensation, not full compensation as prescribed by classical legal theory;
>
> (b) the claims of a significant segment of political and legal opinion to the effect that in view of the perceived inadequacies of classical international law the proposed new standard of *appropriate* compensation is warranted as part of the reform of the legal framework governing the international investment regime.[1]
>
> (c) the proposition in *Article 2 (2c)* of *CERDS* that questions of compensation in nationalization cases

[1]- See, for similarly held viewpoints, GARCÍA-AMADOR (1984), at 295 et seq; Sornarajah, (1986) at 222-225.

should be decided by domestic tribunals and in accordance with relevant national laws except otherwise agreed by the parties; this is a radical proposition in as much as it attempts to remove compensation claims arising from nationalization disputes from the aegis of international law and to place such disputes (from a procedural point of view at the very least) within the context of exclusive municipal legal or domestic jurisdictional competence.[1]

[1]- In the view of some commentators, the attempted transfer of exclusive competence over the determination of compensation awards to the domestic jurisdiction of the expropriating State signifies the universalization of the Calvo doctrine. Emanating from Latin America, this doctrine constitutes one of the normative challenges to classical international law. See further Sornarajah, (1986), at 223 where the author makes the following observation: "... national tribunals are best suited for applying the emerging doctrines on nationalization and compensation. They can readily assess whether the foreign investor had conformed to the conditions on which his entry was permitted and whether his investment had been beneficial to the economy. They can assess the extent to which any malpractices ... affected the host economy and take into account 'all the [relevant] circumstances' of the investment. The assertion of national competence is but an extension of the local remedies rule. That rule has a greater role to play in the area of nationalizations for, unlike in traditional international law, more factors internal to the State have been made relevant in assessing the compensation for nationalized property. It is therefore logical that the primacy of national tribunals must be recognized and extended in modern international law".

With reference to the substantive content of emergent international law and it challenge to classical legal theory on the question of compensation, the relevant provisions of *Resolution 1803 on Permanent Sovereignty over Natural Resources* are contained in *Paragraph 4*. This provides that in the event of nationalization,

> "... the owner shall be paid *appropriate* compensation [in accordance] with the rules in force in the State taking such measures in the exercise of its sovereignty and in accordance with international law. In any case where the question of compensation gives rise to controversy, the national jurisdiction of the State taking such measures shall be exhausted. However, upon agreement by sovereign States and other parties concerned, settlement of disputes shall be made through arbitration or international adjudication."

This claim to the founding of a new legal order based on the payment of *appropriate* compensation for nationalization has been favourably interpreted by advocates of the proposed new norms to put forward arguments in support of their normative

significance and value. Critics, on the ot6her hand, have sought to highlight the perceived shortcomings of the proposed new principles while postulating the continuing vitality of traditional principles of international law.[1] In articulating his support of the new norms Professor Friedmann, for example, was of the opinion that the *appropriate* compensation standard, "*while capable of the most diverse interpretations and probably deliberately imprecise, may [nonetheless] indicate an evolution from the formerly predominant Western sponsored principle of 'full, prompt and adequate' compensation to a more flexible principle that takes into account the circumstances under which the interests in question were acquired and is more likely to achieve a balance of equities in the various situations*."[2]

[1]- See, for a discussion of the controversy surrounding the legal status of the proposed new principles, T.O. ELIAS, NEW HORIZONS IN INTERNATIONAL LAW (1992), at 208-214.

[2]- W. Friedmann, "Half a Century of International Law", 50 VIRGINIA L. R. (1964), at 1352; see also, by the same author, THE CHANGING STRUCTURE OF INTERNATIONAL LAW, (1964), at 206-210, and at 358-361.

Advocates of the proposed new standard of appropriate compensation have often adopted these twin attributes (of flexibility and relevance to new international conditions and circumstances) as the main platform for arguments advancing the normative value and function of the proposed new principles within the framework of the international investment regime. J. de Aréchaga (1978-I), for instance, has argued that the proposed *appropriate* compensation standard better conveys the complex circumstances which may be present in each individual instance of nationalization and the resulting claims settlement.[1] Schachter (1984) has equally pointed to the pragmatism of the *appropriate* compensation approach; he argues that the new formula has a practical advantage in that capital-importing States will be more willing to subscribe to international law obligations and submit to international procedures for dispute settlement if the applicable norms were seen to offer greater flexibility.[2] With reference to the continuing evolution of international law, García-Amador (1984) is of the opinion that there is a case for

[1]- At 302.
[2]- At 129.

modifying or setting aside the classical international law *full* compensation requirement if it is shown to have ceased to be consistent with the needs and interests of the international community as a whole.[1] He further argues that the advent of new concepts such as the 'right to development' through the emergence of an international law of development provides ample justification for such modification. Sornarajah (1986), on the other hand, has advocated the transfer of exclusive competence over the adjudication of compensation claims to municipal legal jurisdiction.[2]

Despite these arguments the acknowledged imprecision and vagueness attending the articulation of the new norms - and the possibility of diverse and conflicting interpretations which this implied – have led some critics to take a rather dim view of the the normative significance of the alternative new principles of international law. Foremost amongst this perception of vagueness and imprecision were the often ambiguous references in relevant *UNGA Resolutions* requiring conformity by States with the "principles of international law"

[1]-At 290 et seq.
[2]- At 223.

as part of the new norms. But which international law? The very classical international law for which reform has been advocated? Such ambiguity appeared to confer on the new principles the character of an enigma. This led advocates of traditional legal theory to go as far as to argue that by requiring *appropriate* compensation "in accordance with international law", *Resolution 1803* was in fact representative of the views of capital-exporting States. Such commentators also highlighted the explicit rejection of an amendment put forward by the government of what was then the Soviet Union proposing the exclusive use of national legal standards in assessing the level of compensation due in nationalization cases.[1] Critics of the new norms have thus on the basis of these arguments postulated that that *Resolution 1803*'s acceptance that international law standards remain relevant to the assessment of compensation claims for nationalization upheld

[1]- See, for example Schwebel, "The Story of the U.N.'s Declaration on Permanent Sovereignty over Natural Resources", 49 A.B.A.J., (1963), at 463. The validity of these arguments appear to have been weakened by subsequent developments including the content of latter resolutions, more on which, see ELIAS (1992), at 206-207.

the continued vitality and validity of classical international law on these questions.[1]

As seen above that the normative challenge posed by *Resolution 1803* (among others) to classical international law resided both in the postulation of the alternative new standard of appropriate compensation and in the assertion of exclusive municipal judicial competence in the adjudication and assessment of compensation claims in foreign expropriation cases. Both these postulations were subsequently reinforced and made explicit in later resolutions. With regard to compensation, for example, *UNGA Resolution 3171 (XXVII) on Permanent Sovereignty over Natural Resources* of 1973 provides as follows:

> "*... each State is entitled to determine the amount of possible compensation and the mode of payment, and ... any disputes which might arise should be settled in accordance with the national legislation of each state carrying out such measures.*"

[1]- Id

In a similar vein UNCTAD Resolution 88 (XII) of 1972 provides that "*such measures of nationalization as States may adopt in order to recover their natural resources are the expression of a sovereign power in virtue of which it is for each State to fix the amount of compensation and the procedure for these measures, and any dispute which may arise in that connection falls within the sole jurisdiction of its courts*."

In our view the replacement of "appropriate" with "possible" compensation in *Resolution 3171* clearly proposes a radical new challenge to classical international law. This normative challenge, far from being limited to the orthodox *full* compensation requirement, appeared to go as far as questioning the very existence and function of the principle of compensation as an accepted rule of international law.

5.2 An Assessment of International Arbitration and Claims Practice with Regard to the Proposed Alternative New Norms.

Our review of modern international claims practice has led to an identification of a number of awards in which recognition has been accorded to the normative significance of the proposed new principles governing compensation for foreign expropriations. Such recognition emanates from a number of cases involving nationalization in the upstream petroleum development sector. Admittedly, these decisions could equally be interpreted as implying or limited to judicial recognition of the "principle" of compensation and therefore of no relevance to the legality of the type or standard of compensation in question. We are however struck by the explicit acknowledgment of the importance attached by claims tribunals in each instance to the proposed new principles – a fact which in our view seems indicative of the normative influence of these principles on the international jurisprudence on these questions.

The first of these cases is that of *Anglo-Iranian Oil Company v. Idemitsu Kosa*[1] in which the district court in Tokyo (a domestic tribunal) - in its decision upholding the validity of an Iranian nationalization decree – took judicial notice of the fact that the Iranian action taken against the Anglo-Iranian Oil Company had been consistent with the provisions of the *UNGA Resolution* of 1952 on *Permanent Sovereignty over Natural Resources*.

Also noteworthy in this respect is the *Sabbatino Case*, in which a US court was as stated:

> "It may well be the consensus of nations that full compensation need not be paid 'in all circumstances', ... and that requiring an expropriating to pay 'appropriate compensation' - even considering the lack of [a] precise definition of that term - would come closest to reflecting what international law requires."[2]

[1]-20 I.L.R. 305 (1953). See also Anglo-Iranian Oil Company v. S.U.P.O.R, 22 I.L.R. 23 (1953), in which an Italian court, in reaching a similar decision, upheld the legality of an expropriation which had clearly not been accompanied by the payment of "adequate" compensation.

[2]- 658 F.2d at 892, paragraphs 14-15; in elaborating further on its judgment, the court did however state that the adoption of the appropriate compensation requirement would "not exclude the

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In the case of *Aminoil* v. *Kuwait,* an international arbitration tribunal held that the *appropriate* compensation standard had had the effect of codifying positive principles of international law.[1] It was the view of the tribunal's that "the determination what amounted to appropriate compensation was better carried out by means of an enquiry into all the circumstances relevant to the particular case, as opposed to resorting to abstract theoretical analyses.[2] Also, in citing *Resolution 1803* in support of its ruling, an international arbitration tribunal similarly held in the *TOPCO* arbitration that the appropriate compensation requirement could be said to amount to "*opinio juris communis"* in as much as it reflected the state of customary international law on the question of recompense for nationalized foreign-owned assets.[3] In a parallel development in *AMCO Asia Corp.* v. *Indonesia* the principle of *restitutio in integrum* was on the other hand rejected as a possible remedy. In the tribunal's view, it was obvious that it could not

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possibility that in some cases full compensation would be appropriate".

[1]- 21 I.L.M. 976 (1982), at 1032, paragraph 143.

[2]- Id at 1033, paragraph 144.

[3]- Supra, at 29.

substitute itself for the Indonesian government in order to cancel the revocation and restore the licence, for it was more than doubtful that restitution could be ordered against a sovereign State.[1]

The tribunals' departure in the cases reviewed above from the strict prescriptions of classical international law on the question of compensation for nationalization leads us to an unavoidable conclusion; and it is this: that since the well-considered judicial opinions in such cases did not refer to the

[1]- 24 I.L.M. (1985) at 1022. In Letco v. Government of Liberia, 26 I.L.M. (1987) at 668 a claim for restitution was also rejected. See also Arbitrator Lagergren in BP(Exploration) Libya v. Libya, supra; and Arbitrator Mahmassani in the Liamco Arbitration, supra. For a review of other cases in which claims for restitution have been rejected, see GRAY, JUDICIAL REMEDIES IN INTERNATIONAL LAW, (1987), at 12-16. Among academic writers, HIGGINS, (1982-III), at 320-321, is of the view that whereas an interpretation of case law would suggest that restitution is in general terms a recognized remedy, it is nonetheless not an established remedy in the field of concession agreements. In her opinion therefore, there is little practical evidence to suggest any real expectation that restitution can be granted in nationalization. D.W. Bowett, "State Contracts with Aliens: Contemporary Developments for Termination or Breach" 59 BRIT. Y.B. INT'L L., 49 (1988), at 60-61, in pointing to the impracticality of restitution has, however, also suggested the possibility of partial restitution - e.g. of items such aircraft, ships or other chattel, or the withdrawal of forces in cases involving the unlawful occupation of territory.

Hull formula as an authoritative standard or a rule of international law, a case could indeed be made in favour of the normative significance of the proposed new principle of appropriate compensation.[1] It is in light of this possibility that Sornarajah (1986) postulated the following view:

> "In the context of ... recent developments, the norm requiring payment of full compensation upon nationalization of alien property must be rejected. It is doubtful whether the norm was ever based on sound legal foundations. Even if it was, it has now been severely undermined by the development of contrary norms. The practice of lump sum agreements may indicate that the capital exporting States have tacitly accepted this change. The role of developing States has resulted in the requirement that the whole process of the foreign investment, the nature of the profits made by the investor, the malpractices, if any, committed by him and similar factors are relevant to the assessment of compensation."[2]

[1]- See further Schachter (1984), at 128.

[2]-At 225. See generally Kaj Hobér, "Fair and Equitable Treatment - Determining Compensation", in 6(4) TDM (Special Issue: 2007)

In assessing the precise nature and substantive content of the alternative norms, it could thus be argued that in its use of the word "appropriate compensation" relevant *UNGA* resolutions promoting the new law on nationalization in the natural resources development sector implied the possible relevance of the following factors to the assessment of compensation:

- Excess profits made by the foreign investor which must be taken into account on grounds of equity. As such, even the principle of *restitutio in integrum* will not support a *full* compensation requirement as equitable considerations would require that account be taken of past performance under the agreement on the basis of a cost-benefit analysis.[1] It has thus been argued that claims or counter-

[1]- Sornarajah (1986) at 121-123. It has also been argued that if the concept of unjust enrichment provides a basis for full compensation, then "... the idea of excess profits contains an embryonic notion of fairness that commends itself to the unjust enrichment doctrine": Rohwer, "Nationalization - Chilean Excess Profits Deduction", 14 HARV. INT'L L. JN., (1973), at 378; see alsoHeiben, "The Chilean Copper Nationalization: The Foundation for the Standard of Appropriate Compensation", 23 BUFFALO L. REV., 765 (1974). See also Falk, "The New States and the International Legal Order", 118 RECUEIL DES COURS, (1966-II), at 29, where the author holds that appropriate compensation encompasses the principle of unjust enrichment. Such arguments seem to imply that the assessment of

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claims "relating to excess profits must be looked upon with favour in situations where the investment had an exploitative character."[1]

- Where the nationalization relates to the public interest or is vital to a general economic restructuring exercise or to the national interest as opposed to one which is politically motivated, then the financial and economic capacity of the nationalizing State to pay for the measures should constitute a key consideration. Hence, it is feasible that that compensation could even equal zero where the purpose is clearly to promote the public good and the

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compensation depend not just on legal criteria, but also on moral and political judgments which easily come into play.

[1]- Sornarajah (1986), at 271-218. The author cites in support of this contention the Aminoil Arbitration (supra, at 1033) which, he argues, contains indications that unreasonable profits made by the investor could be the subject of counter-claims by the nationalizing State. In the author's view, the termination of agreements operating under exploitative conditions would be consistent with international community objectives in that such nationalizations remove a continuing source of friction between the parties, and the ending of such friction would facilitate the free flow of investment and raw materials.

State is not in a position to afford the required payment.[1] Far more controversial is the claim sometimes made by States that the nationalization is a revindication for perceived injustices or past malpractices on the part of the deprived investor for which no compensation is due.[2]

- Other factors which are likely to affect the determination of appropriate compensation are listed in relevant *UNGA* resolutions as including relevant national laws and regulations, equitable principles and all other circumstances considered to be pertinent both to the past functioning of the natural resources agreement and to the nationalization.

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[1]- See ACKERMAN, PRIVATE PROPERTY AND THE CONSTITUTION, (1977), at 2-5. As already noted above, Schwebel (1965), at 201, and at 209-210, holds a contrary opinion to the effect that in situations where the expropriating State has no means to pay full compensation, then restitution offers the only hope for the investor in foreign expropriation cases. See also MIKESELL, FOREIGN INVESTMENT IN COPPER MINING IN PAPUA NEW GUINEA AND PERU, (1979), in whose view nationalization without full compensation would be inconsistent with international law in a situation where an investor has been invited to prospect for minerals and having found and set up operations, is subjected to expropriation. In the author's opinion, the mineral developer under these circumstances is denied profits consistent with the risks he had taken in undertaking the venture.

[2]- See Sornarajah (1986), at 219-221 for a discussion on this particular aspect of foreign expropriations.

In our summing up in this section we would submit that the conclusion to be drawn from the foregoing analysis is that in view of the normative challenges which classical international law has come under through the postulation of alternative legal standards, traditional legal theory promoting the *full* compensation prescription no longer enjoys its unrivalled supremacy within the legal framework governing the international investment regime. Even if we make due allowance for the controversy which surrounds the precise legal status of the proposed new norms to this day, it would still be difficult - or even unsustainable from a practical point of view - to maintain that there remains an unqualified requirement for *full* compensation. Such an orthodox view of the international law requirement for compensation would clearly fly in the face of the obvious fact that at least 104 countries voted in favour of relevant UNGA resolutions proposing a reform of the international law on nationalization and compensation.[1]

[1]- See also White, "The New International Economic Order", 24 I.C.L.Q., (1975), at 547.

Even so we still need to pose the question as to whether relevant State practice on compensation for nationalization has been consistent with political aspirations towards the founding of a new law on nationalization based on the proposed new principles. What is the current position of national laws on this key question? And do the various opposing theories and arguments hold any potential implications in terms of the approach to the actual computation of compensation or damages for nationalization? In the next section we will attempt to answer these and other questions.

6. A COMPARATIVE PERSPECTIVE: THE QUESTION OF COMPENSATION FOR NATIONALIZATION IN NATIONAL LAW

It is remarkable that given the aspirations for the founding of a new international economic and legal order on the part capital-importing nations – an aspiration encapsulated as we have seen in relevant UNGA resolutions – State practice subsequent to these resolutions on the question of compensation for nationalization does not appear to reflect the these aspirations. This is in view of the fact that the requirement for compensation in the event of nationalization as expressed within the framework of contractual and investment treaty continue to bear a close affinity to the classical international law prescription of full compensation as a pre-condition for the legality of foreign expropriations.

Our objective in this part of the article is to attempt to shed light on the dynamics which inform the investment process and to explore the synergies between investment policy and law, between State practice and their normative implications and between national law and international law vis-à-vis the regulatory aspects of the FDI process. We

therefore propose to go beyond the traditionally narrow perception of State practice with regard to compensation clauses as a contractual risk-management mechanism solely at the disposal of the foreign investor party; part of our objective is to posit a hypothesis to the effect that compensation clauses in natural resources development agreements and investment treaties which prescribe the full compensation standard serve a 'country-risk management' device aimed at attracting inward foreign investment. The novelty in this approach to the conception of political risk management strategies clearly lies in its departure from customary investment promotion devices such as tax incentives and other fiscal benefits offered to the foreign investor. The adoption of 'full' compensation clauses by governments as a mechanism for managing the political or sovereign risk of expropriation involves increased reliance on contractual and other legal forms as mechanisms for promoting and consolidating foreign investor confidence. Our research offers some pertinent examples of the existence of such provisions within the framework of the national policy initiatives aimed at promoting the inward flow of FDI into the natural resources development sectors.

An objective and critical perception of the stipulations providing for compensation, when viewed outside the confines of traditional legal theory and in the specific context of modern resource development agreements, would clearly ascribe to such provisions a risk-management function. In other words it would be ill-conceived to assign to such provisions a strictly normative function in the sense of restitution. Such provisions have as their purpose the following rationale: the first is to serve in a preventive role – in as much as the requirement to compensate fully for nationalized assets can be interpreted as a possible deterrent to future expropriatory measures; and the second, a remedial (rather than a restitutionary) function with regard to the possibility of any future nationalization. A good example of a clause with a preventive function can be found in the terms and conditions governing petroleum exploration in Mali. Of particular relevance here is the so-called "*No Nationalization*" clause which provides as follows:

> *The Government assures the company that it has no intention of nationalising it; however, if circumstances imperatively call for such measures, a*

just and equitable indemnity in transferable currency shall be paid.[1]

An illustrative example of provisions in the remedial category is the 1982 *Model Agreement for Offshore Petroleum Development* in Guinea Bissau. Although not a clause relating to nationalization *per se*, it is nonetheless intended to provide for compensation in the event of ensuing State intervention in the normal functioning of the agreement. The relevant provision stipulates the following:

"Right of Requisition by the State:

In the case of national emergency, the State may requisition all or a part of the production and shall indemnify the company in full for all damages and for the production requisitioned."[2]

Such guarantees of compensation in the event of regulatory State intervention are not confined to the sphere of contractual practice. They are also present in national legislative instruments - i.e. in investment legislation, and sometimes in

[1]- WORLD PETROLEUM LAWS (1987), at 451.
[2]- Id at 334. For similar guarantees extended under the terms of exploration permits in Burundi, see page 147.

petroleum and mining laws. In Albania, for example, Article 4 and 5 of *Decree 7764* dated 2 November 1993 on *Foreign Investments* provides that foreign investment projects in Albania will not be subject to expropriation or nationalization except for specific reasons and always against the payment (without delay) of damages equating to the real market value of the nationalized investment or assets.[1] Similarly, in Namibia, Article 11 (2) of the *Foreign Investment Act of 1990* provides for "just" compensation to be paid in the event of a nationalization of foreign investments.[2] In Tanzania, the *National Investment (Promotion and Protection) Act* of 1990 provides for the payment of "full and fair" compensation for

[1]- http://www.slas.info/legislazione_albanese/law%207764_1993foreign_investments.php#top_contenuto also A. Parra, "Principles Governing Foreign Investment as Reflected in National Investment Codes", 7 ICSID REV.-F.I.L.J., 428 (1992), at 442-444; M. S. Mahmassani, "The Legal Framework for Investment in Czechoslovakia", 6 ICSID REV.-F.I.L.J. 65 (1991); and I. Pogany, "Recent Developments in the Law Relating to Foreign Investment in Hungary", id, at 114. With regard to developments in Eastern Europe and Russia, see generally T. WÄLDE/ G. NDI (EDS), INTERNATIONAL OIL & GAS INVESTMENT: MOVING EASTWARD?, GRAHAM & TROTMAN, LONDON, (1994).

[2]- See 31 I.L.M. (1992), at 211.

the taking of foreign-owned property.[1] A new investment code enacted in 1997 contains similar provisions. Kuwaiti law which governs the expropriation of real estate and lands, on the other hand, makes no explicit reference to any particular standard for the measurement of compensation. Decree Law No. 131 of 1986, however, contains detailed procedures for both permanent and temporary seizures of land or real estate; the expropriation must be for the public interest and the land owner has the right to submit a formal objection to any aspects of the expropriation which they find disagreeable..

These statutory guarantees of 'no nationalization' and of 'full', 'fair' or 'just' indemnification in the event of a requisitioning by the host State, while illustrative of their risk-management function, can also be said to be conceptually enigmatic. This in view of the fact that these very nations had voted in favour of the reforming the substantive rules of classical international law on these questions. The problematic in this instance derives both from the interpretation which may

[1]- Article 24 (2), in accordance with Article 24 of the national constitution, of which see 30 I.L.M. (1991), at 905. See also Maina Peter, "Promotion and Protection of Foreign Investments in Tanzania: A New Investment Code", 6 ICSID Rev.- F.I.L.J., 42 (1991).

be given to such State sponsored guarantees. Clauses of the 'no-nationalization' category could be said, for instance, to be suffer from a conceptual flaw as a political risk-management model if they were to be perceived as an attempt to circumscribe or fetter the regulatory competences and impulses of the State. As such these guarantees could in turn be perceived as sanctioning a derogation from the principle of national sovereignty in view of the fact that international law recognizes in the latter principle the right to regulate. The exercise of the right to regulate includes within it acts of nationalization.

The potential for controversy does not end here; provisions in the second category are equally subject to controversy. To what extent, for example, is the close affinity which exists between such provisions and the *full* compensation requirement an expression of legal opinion on the part of the developing nations involved as to the normative value of the classical international law principles which these same nations sought to reject? Or can the orthodox leanings of some of these guarantees be explained or attributed simply to the policy exigency of investment promotion? In other words, can a perception which equates the increased tendency to

embrace the spirit of traditional legal theory with a willingness on the part of these countries to accept the traditional norm of *full* compensation be justified? Before examining these questions we proposed to first of all examine the compensation requirement from an economic and functional perspective.

7. AN APPLIED AND ECONOMIC PERSPECTIVE TO THE QUESTION OF COMPENSATION FOR NATIONALIZATION.

It has been posited that the general notion of compensation, no matter how expressed or qualified (i.e. either as 'full', 'just', 'reasonable', or 'appropriate') is itself inadequate; it is further argued that what is more important in claims practice is to break down the different heads of claim pursued by the claimant and to undertake a computation of these as opposed to dealing with "compensation" in the abstract.[1] If this is indeed the case, does it imply for the legal semantics of "standards" a less prominent role in the actual

[1] See further Bowett, (1988), at 61.

practice of international arbitration and claims tribunals? A purely applied and practical approach to the assessment of compensation (or damages a the case may be) in international claims settlement would appear to suggest that such is the case. Viewed from this perspective - i.e. as the legal arguments and submissions of counsel shifts to the practical questions of valuation and away from the legal semantics of standards - economic and accounting concepts tend to assume a more significant and important role in claims settlement. Thus when the heads of claim are broken down and categorized the following main categories emerge[1]:

- Assets: i.e., tangible, physical or "book" value assets; intrinsic value unrelated to the earning capacity of the assets - in legal parlance this is known as *damnum emergens*;[2]

[1]- Id. See also HIGGINS, (1991-V), at 190-194.

[2]- It should be pointed out that modern methods of valuation sometimes tend to focus exclusively on the capacity of an asset to generate future profits. This, however, does not negate the essential function of this classification exercise - i.e. a systematic approach to the assessment and computation of compensation and damages.

- Interest on the value of assets (usually covering the period between the date of the taking and the date of the award or its payment);[1]
- Loss of future profits or expectation loss: i.e. *lucrum cessans*.[2]

To varying degrees, both traditional legal theory and the proposed new principles of international law are agreed on the question that some form of compensation is due for the nationalization of foreign owned assets.[3] The point of separation comes where the former prescribes full compensation whereas the latter advocates the concept of *appropriate* compensation taking into account all relevant

[1]- Interests awarded in the recent Iran-U.S claims have generally been in the range of 10-12%, with the tribunal in some cases awarding a lump sum as interest damages. See further Stewart and Sherman, "Developments at the Iran-United States Claims Tribunal: 1981-1983", 24 VIRGINIA J. INT'L L., (1984), at 35-36; and Bowett, (1988), at 62.

[2]- For more on claims based on lucrum cessans, see generally HIGGINS, (1991-V), at 193-194.

[3]- In the LIAMCO Arbitration (supra at 201), for example, Arbitrator Mahmassani noted that "... there is no difficulty [in concluding] that the indemnity shall include as a minimum the damnum emergens, e.g. the value of nationalised corporeal property, including all assets, installations and various expenses incurred." See also Sedco v. Iran, supra.

circumstances. Needless to say, the two other heads of claim relating to the payment of interests and lost profits have provided even further grounds for more contentious debate. This debate has seen traditional legal theory upholding, and postulated new principles contesting, the relevance of lost profits and interest payments to the assessment of recompense for nationalized property.[1]

[1]- On the question of lost profits, Bowett, (1988), at 74 is of the view that whereas "full compensation" will be required for nationalized assets, there is no right to any expectation of profits from the moment in time when the State takes over the actual exploitation of the resources or means of production. In asserting this view, the author points out that profits produced subsequent to the take-over "are the fruit of the State's own efforts." On the other hand, one could equally argue that an asset's true value lies in its ability to generate income, and that as such lost profits should be due to the investor right up to the moment when compensation is assessed and an agreeable arrangement reached as to the modalities for its payment. In both the LIAMCO and Amoco International Finance cases, however, claims for lost profits were seemingly rejected. The view of one commentator on the question of lucrum cessans is that without advocating a punitive role or criminal jurisdiction for international arbitral and claims tribunals, a solution would seem to lie not in excluding lucrum cessans from the valuation of property in lawful nationalizations but in including a penal element in the valuation of unlawful takings: HIGGINS (1991-V), at.194. In any event where the valuation method adopted involves a factoring of future expected profits into an asset's value, then there would be no additional value to compensate, and the whole question of damnum emergens/ lucrum cessans in effect becomes a non-issue; see further Stauffer, "Political Risk and Overseas

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Even assuming that agreement is reached on the question of which heads of claim ought to be included in the award, there still lingers the problem of putting a value on the assets involved. In discussing this problem, Bowett (1988) has highlighted the following pertinent issues:

> "Assets will normally have a 'book value', which may be 'net', or 'updated' or 'depreciated', and according to the nature of the asset, its value may have increased or decreased with time *[footnote omitted]*. Thus land and building may well increase in value; machinery and plant will tend to decrease. 'Replacement cost' may be yet another standard of value, if assets will have to be replaced by the owner. Yet these are largely technical problems which accountants or valuers are used to handling, and courts will frequently seek technical advice of this kind in arriving at an appropriate figure."[1]

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Oil Investment", SOCIETY OF PETROLEUM ENGINEERS (SPE 18514), Sept. 1988.

[1]- Bowett (1988), at 62. An example of the employment of the 'net book value' method of valuation in the petroleum sector is the 1979 Bapco Agreement for 100% Nationalization of Bahrain Petroleum Co. Ltd.,

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It is indeed the case that the technicalities involved in property valuation in nationalization disputes have often shifted the emphasis in modern international claims practice to economic concepts of valuation and away from the purely juristic question of which standard of compensation to apply. In *Kuwait v. Aminoil*, for example, the tribunal appears to have attached a great deal of significance to the 'replacement cost' method of valuation (which it regarded as appropriate in the case of a recent investment in which the original cost is likely to reflect more closely the replacement cost).[1] It ultimately preferred "depreciated replacement value" - a term which the tribunal unfortunately did not explain - in assessing compensation for fixed assets.[2] Less prominent in the tribunal's deliberations was the role of the competing legal standards of compensation in the calculation of the final amount of the award.

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which provided that the government will pay the company compensation equating to the net book value of the latter's interests in the venture: PETROLEUM LEGISLATION, Suppl. 109, (1992), p.27.

[1]- Supra at 1042. The tribunal did however point out that differences between the two can be accommodated through the technique of 'updating'.

[2]- Id.

Other economic concepts which have been employed by tribunals include "reasonable rate of return"[1], discounted cash flow (DCF)[2], 'going concern value', 'net present value' (NPV), etc.[3]

[1]- Id.

[2]- Starrett Housing v. Iran (supra); and the Phillips Petroleum Case (supra). See further W. Knull, S. Jones, T. Tyler and R. Deutsch, "Accounting for Uncertainty in Discounted Cash Flow Valuation of Upstream Oil and Gas Investments" in 6(4) TDM (Special Issue 2007).

[3]- For a discussion of the various methods of valuation and specific case studies of their application to various cases, see Friedland and Wong, "Measuring Damages for the Deprivation of Income-Producing Assets: ICSID Case Studies", 6 ICSID REV.- F.I.L.J., (1991), in particular at 403 et seq.; see also World Bank Investment Guidelines, Introductory Note, paragraphs 39-46, and Guideline IV, Sections 4-6, at 1376-1377. The novel approach adopted in a dispute concerning the expropriation of land from the United Fruit Company by the Government of Guatemala provides an interesting departure from the methods commonly employed by international claims tribunals. The government in this case insisted on using the company's own valuation of its assets for taxation purposes as the basis for the measurement of any compensation payments. In so doing, it was argued that the tax value was the proper method of assessment as "it would neither be just nor lawful for the State to give such properties a valuation higher than that which the company itself had given to them and which served as the basis for [taxation]": cited in Sornarajah (1979), at 116. In the event, insistence on this particular method of valuation appeared to have transpired to be a somewhat hazardous and avoidable precedent not since used in by governments in foreign expropriation cases, as the government in this particular instance was shortly thereafter overthrown. The new government subsequently agreed to a more conventional valuation.

Despite what seems to be the prevalence of these economic concepts in compensation awards, we would nonetheless counsel that the continuing relevance of the distinction between *full* and *appropriate* compensation in claims practice cannot and should not altogether be discounted. Analysis of the *dicta* in these claims tends to reveal that the various methods listed above relate in varying but indeterminate degrees to each of the two legal standards. Hence, whereas a 'reasonable rate of return' approach may relate more closely to a valuation for the purposes of determining *appropriate* compensation, the adoption of methods such as 'net present value' and 'going concern value' clearly foreshadows a correlation of the final settlement to market value; these latter methods of valuation thus bear a closer affinity to the orthodox standard which requires full compensation. Our research clearly identifies an underlying relationship between these economic approaches to the valuation of compensation for nationalized assets and each of the two 'legal' standards of compensation.

There is also the question concerning the payment of interests which may have accrued on the claimant's outstanding monetary claim.[1] This can sometimes be quite substantial, as can be seen from the dispute in *Santa Elena v Costa Rica*, in which the interest due to the claimants amounted to US$4.15 million based on an expropriated asset value of US$11.85 million.[2] It is arguably that interest awards can be interpreted to be an essential component of the full compensation requirement. If this proposition is correct, and we believe it is, the award of interest can ultimately be traced and sourced through the full compensation requirement to customary international law. But if customary international law is said to be based on evidence of a general practice accepted as law, this in turn begs the question as to validity of the practice of such interest payment in an international community of nations which includes a significant number of

[1]- See further Gotanda, 1(2007) at 6-11; see also J. Gotanda, "Awarding Interest in ICSID Arbitration", 90 Am. J. Int'l L. 50 (1996); J Colón and M. Knoll, "Prejudgment Interest in International Arbitration", 6(4) TDM (Special Issue: 2007).

[2]- Compañía des Desarrollo de Santa Elena S.A v Costa Rica, ICSID Case No ARB/96/1 (2000), available at http://www.worldbank.org/icsid/cases/awards.htm (cited in Gotanda (2007), at 7).

countries where the charging of interest is prohibited on religious grounds. What then would be the position where the two parties involved in a nationalization dispute are both bound by the same religious law which prohibits the payment of interest on the outstanding monetary claim? While this question remains to be tested in law, we would submit that under such circumstances the appropriate compensation standard would present a more suitable remedy than that of full compensation. We reach this conclusion on the premise that of the two standards the full compensation requirement is more amenable and accommodating of an award of interest on the principal amount claimed.

7.1 The Relevance of the Distinction Between Lawful Nationalization and Expropriation to Compensation Awards.

A significant factor which could exert an influence on the assessment of compensation awards is the customary international law distinction between lawful and unlawful nationalization. A lawful nationalization which is the term used to describes measures which comply with the international law pre-conditions for legality: to wit, that the asset deprivation should be for a public purpose, be non-

discriminatory and be subject to the payment of compensation. Unlawful, also known as expropriation, signifies a failure to comply with the said pre-conditions for legality. Compensation, in principle, applies to lawful nationalization; technically, expropriation or unlawful nationalization attracts the award of damages.[1] In academic writings and in practice, however, only the term compensation is used with little or hardly any reference to the award of damages. A possible reason for the rarity of its use could derive from the fact that damages is a concept more associated with contract law and private commercial transactions whereas the term compensation has traditionally been associated by publicists with the international responsibility of States arising from the deprivation of foreign owned property or contractual rights.

The distinction between lawful and unlawful nationalization will be of little obvious value if it did not have practical implications for the potential amount of compensation to be awarded.[2] By the logic of this distinction,

[1]- See further 4(6) TRANSNATIONAL DISPUTE SETTLEMENT (2007): Special issue on Compensation, Damages and Valuation in International Investment Law.

[2]- Bowett (1988), at 59.

a much higher level of compensation should in practice be due for an unlawful nationalization (also known as expropriation) and lawful nationalization (i.e. measures which comply with the international law pre-conditions that the asset deprivation should be for a public purpose, be non-discriminatory and be subject to the payment of compensation). The much higher level of compensation for expropriation could perhaps be justified on basis of lost profit or *lucrum cessans* accruing between the date of the taking and that on which the award is made.[1] Viewed from the perspective of traditional legal theory, the distinction between lawful and unlawful acts of nationalization seems to be somewhat blurred by the insistence classical international law on the principle of *restitutio in integrum* - which it has consistently posited as the most appropriate remedy in cases of unlawful nationalization.[2] For

[1]- See, however, HIGGINS, (1991-V), at 194, in whose view the inclusion of a penal element in such cases would appear to be the most suitable approach. See also, at 190-194, the author's identification of the elements to be included in the valuation of property relating to a lawful nationalization.

[2]- See, for example, comments in the Chorzow Factory Case (supra), at 47; the Topco Arbitration, (supra) at 497-508; and the Amoco International Finance Claim (supra), paragraphs 192-197 where the following propositions were stated: (i) That a clear distinction must be made between lawful and unlawful expropriations; (ii) That for

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lawful nationalization it prescribes full compensation as the equivalent of restitution. But we would argue that if full compensation equates to restitution, the ultimate consequence would be a blurring (in theory at least) of the distinction between lawful nationalization and expropriation.

Our review of international arbitration and claims practice in the modern era also reveals that a distinction often drawn between *ad hoc* measures on the one hand and general or whole-scale expropriatory measures on the other, for the purposes of ascertaining the amount of compensation due in each instance. In a number of cases including the *Sola Tiles case , the INA Claim, and Sedco Claims* – all previously referred to in this paper as emanating from the Iran-U.S claims process - the tribunal in each case sought to establish a distinction between 'a discrete expropriation' and a formal large-scale nationalization.

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unlawful expropriations, international law requires restitutio in integrum, or (if not possible), its financial equivalent; and (iii) That for a lawful expropriation, the obligation is to pay 'fair compensation' or the 'just price' of the property that has been taken.

In view of the underlying philosophy and logic of the essential distinction between lawful and unlawful nationalization - and between ad hoc takings and general expropriation measures - the following propositions or hypotheses would seem to emerge from our analysis of international arbitration and claims practice concerning the correlation between unlawful takings and the required measure of compensation[1]:

(a) Claims for loss of profits or *lucrum cessans* would be awarded for unlawful nationalization but applies only to lost profits suffered between the time of the expropriation and the date of the award – but not for the potential whole duration of the project;

(b) An award may be made for the 'full value' of the expropriated assets in an *ad hoc* or discrete taking, but would exclude loss of future profits beyond the date of the award;

[1]- Bowett (1988), at 69.

(c) A lower value (i.e. less than full value) of the nationalized assets- may be awarded in case of a formal, systematic large-scale nationalization.

It may be thus concluded from our analysis in this section that economic and practical considerations are equally relevant to the international law measurement and award of compensation for nationalized assets, as are purely legal or normative formulations. It is also submitted that the legal distinction between lawful nationalization and expropriation (unlawful deprivation of assets) also has practical implications for the measurement of compensation (or damages as the case may be). Finally it may be concluded that despite the ongoing uncertainty in this area of international law, the various methods of valuation so far adopted for the purpose of a formal determination of awards in the majority of international arbitration and claims practice appear to lean in favour to the "market value" method of valuation.

8. CONCLUSION

Our study has revealed that the question of compensation has been and remains one of the most problematic areas in international arbitration and claims practice. It has generated, and will most likely continue to generate, a great deal of interest amongst scholars and practitioners alike – if not controversy and contentious debate amongst the chief protagonists of the two main standards for the measurement of compensation for nationalization. The future course of international arbitration and claims practice on the question appears uncertain given the competing claims and multiple approaches open to tribunals for the assessment of compensation and damages. As such, any attempt at predicting possible future developments on these questions is bound to be subject to a considerable element of conjecture. We believe, however, that the existence and validity of the principle of compensation for nationalized assets as a norm of international law is well assured. Even the advocates for reform have in the past acknowledged that there is good reason to believe that the international law obligation to pay

some form of compensation for nationalized property will continue to be widely accepted in the future.[1] Far less reassuring is the prospect of finding future solutions to these problems which will appeal to every shade of political and legal opinion in the international community. Our view is that the normative problems in this area of international law derive as much from political as from jurisprudential factors.[2]

We believe that before an effective resolution of the normative problems in this area of international law can be attained an adequate balance between community interests and individual rights, between the community gains and private loss arising out of foreign expropriations, will need to be found. In seeking the required balance, the primary focus

[1]- See, for example, Schachter (1984), at 130. In the author's view, however, "It would be unfortunate if the expression of this rule as international law were to be rendered unacceptable to many States by the inclusion of a standard that was little more than a [provocative] symbol derived from old controversies. Foreign investment will not be helped by that ..."

[2]- See further Z. MIKDASHI, THE INTERNATIONAL POLITICS OF NATURAL RESOURCES (1979); KAPLAN and KATZENBACH; THE PLITICAL FOUNDATIONS OF INTERNATIONAL LAW; and R. HIGGINS, CONFLICT OF INTERESTS: INTERNATIONAL LAW IN A DIVIDED WORLD (1965).

should be on providing a reasonable degree of protection to the foreign investor, though not in such a manner as to fetter or otherwise circumscribe the right of the State under international law to regulate domestic economic activity - a right which includes the sovereign prerogative of nationalization. The imposition of international law restraints on this right would clearly be inconsistent with community expectations and national aspirations to full and permanent sovereignty over natural resources. Hence, what is required above all is that each case should be treated on its merits – i.e. a pragmatic approach which takes account of all the relevant circumstances surrounding the nationalization.

Based on our analysis and findings from the research, we would recommend the following criteria for possible application to the assessment of compensation for the nationalization of foreign owned assets, particular in the upstream petroleum and natural resources development sectors. Starting from the premise that restitution is not always a practically feasible remedy, we would propose that the standard and amount of monetary compensation take into consideration the following questions and factors:

(a) Is the nationalization or expropriation in breach of specific prior contractual or treaty commitment? If the answer is yes, then the standard of compensation prescribed in the relevant compensation provision in the agreement or treaty should *prima facie* apply except where other overriding considerations superimpose themselves;

(b) Is the nationalization in pursuit of a public purpose or in the public interests of the expropriating State? If yes, the full compensation standard can only warrants consideration alongside alternative standards of compensation in determining the measurement of compensation.

(c) The ability of the expropriating State to pay the amount claimed is undoubtedly of a practical relevance to the assessment of compensation. Considerations relating to the effectiveness of compliance with (and the enforcement of) compensation awards clearly hinges on the paying ability or solvency of the State against which the award is made. From this point of view the

appropriate compensation standard would seem to provide a much more flexible, pragmatic and effective in view of its less rigid character as compared to the *full* compensation standard.

(d) In the final analysis, we would submit, the theory and practice of compensation claims must not in effect lead to a negation of the sovereign prerogative of States to regulate domestic economic activity either through nationalization or similar measures which the may be deemed a necessity by the State in question.

In conclusion, we would also counsel that judicial interpretation of the compensation clauses contained in agreements and bilateral or multilateral investment treaties should take into account not just the express provisions as stipulated, but also the possible influence of extraneous factors which may impact the measurement of the compensation award.

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