PROTECTION OF FOREIGN INVESTMENT:
A STUDY IN INTERNATIONAL LAW

BY

ZOUHAIR A KRONFOL

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ZOUHAIR A. KRONFOL

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Zouhair A. Kronfol

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INTRODUCTION

The importance attributed to economic development is certainly one of the important phenomena of our days. The term itself refers to a process of economic change, as manifested in the increase of a country's national income, a high degree of productivity, and a general increase in the welfare of its inhabitants. In international relations, economic development, as a relative term, denotes the existence of two categories of states. One consists of the so-called "developed" countries, which are industrially advanced and have a high degree of technology and productivity, and a high national income per capita; the other is composed of the "underdeveloped" countries, which are primarily agricultural and in which productivity, per capita national income and technical achievement are low. Of the people living in the world, more than two thirds are inhabitants of countries to the second category.

The existence of these two categories on the international scale, is not new. Rich and poor countries have always existed in the world. But what is new is that the peoples of the under-developed countries of today have become conscious of their condition and are trying to improve it.

No nation can today develop political or economic security in isolation. Some argue that the United States would not be what it is today had it not been for the investments of British

exporters of capital and know-how. Therefore, economic assistance to underdeveloped countries is one of the dominating problems of today. The disproportionate share of the world's hunger and disease carried by the underdeveloped nations can be eliminated not only by public foreign aid, but also through private investments abroad. Therefore, the economic development of these nations depends to a large extent on private foreign capital. The private investor in helping himself, can help these countries. By making his talents and capital available, he encourages the growth of these nations. However, foreign capital may not move to these areas, where they are most needed, unless favorable conditions of security exist. The protection of foreign investment is, therefore, one of the means to increase the flow of private capital to the less developed countries. Because of this great need for security and foreign capital in these areas, it has become increasingly important for states to adopt measures necessary to assure the degree of certainty and stability which are essential for a high degree of development.

The present thesis deals with one set of measures which tend to promote stability and which relate to the need for an increase of private capital in the less developed countries of the world. The measures in question are guarantees given by states to foreign investors, insofar as the latter is affected by state action. Such guarantees relate only to a few of the

factors affecting the internal flow of private capital, namely, the factors generally included under the heading of "investment climate". Moreover, the problem of foreign investment itself is but one of the problems related to economic development of the underdeveloped countries.

In addition, the present study deals with the problems which such guarantees raise in international law; it is therefore the international law aspects which are chiefly discussed and which receive the main emphasis. Since this is a legal study, it cannot be expected to deal with matters from an economic or sociological point of view. However, this does not mean the non-legal factors should be ignored. The problem of the legal security of private foreign investment is closely related to the political, economic, and social questions so that any "isolated" legal study is impossible and meaningless.

Therefore, one should constantly be aware of the non-legal factors involved. For this reason, it is necessary to give a brief account on the economic considerations involved in the grant of guarantees to foreign investors, and this is covered in chapter I. Chapter II is concerned with the international law rules governing the treatment of aliens and their property.

The main body of the thesis, chapters III and IV are devoted to the analysis of the forms and contents, as well as the legal effects of the various legal guarantees given to foreign investors. Chapter V is devoted to the settlement of investment disputes and the remedies available to the investor against foreign states. The closing chapter contains conclusions and evaluations of the study.

TABLE OF CONTENTS

CHAPTER I

Economic Development and Private Foreign Investment

Since the end of the last world war there has been a growing recognition in the world community of the urgent need to accelerate the pace of development in the underdeveloped countries. A rapid rate of growth in these countries is considered essential for the humanitarian purpose of raising the standard of living of the world population as well as for the active promotion of international peace and stability.

A. Economic Development and Foreign Capital

Among the factors affecting economic growth, the availability of capital is one of extreme importance. Economic development is achieved through the productive employment of labor and the full utilization of natural resources. Capital is needed for the accomplishment of both these objectives.

The productive employment of labor presupposes a raising of the general level of education and the acquisition of technical skills, the formation of a body of administrators and entrepreneurs, and provision of adequate tools and machinery. For the exploitation of natural resources, on the other hand, a number of basic facilities are needed, such as roads, railways and other means of transportation, and electrical power. In most underdeveloped countries today, emphasis is laid on industrialization as the key to economic development and

the improvement of the standard of living.[1] However, industrialization must not result in total neglect of other economic sectors, particularly agriculture.

The Scarcity of Domestic Capital

It is obvious that none of the objectives just mentioned can be achieved without the supply of capital. In order to educate the masses, to build roads, or to import machinery, one has to invest a sizable amount of capital. However, capital by itself is necessary, but not a sufficient condition to progress.[2] Economic development has much to do with endowments, social attitudes, political conditions and historical accidents.

At present, capital is scarce in the underdeveloped countries whether domestic or foreign. Domestic financing in underdeveloped areas is very restricted. Economists have spoken in this connection of the "vicious circle of poverty", of a "circular constellation of forces tending to act and react upon one another in such a way as to keep a country in a state of poverty".[3] According to this view, a backward economy remains backward because its total output is low and savings are small, so that after consumption needs are fulfilled, little remains for

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1. P.T. Bauer and B.S. Yamey, The Economics of Under-developed Countries (Cambridge: James Nisbet and Company Limited, 1960), p. 237.

2. Ibid., p. 127.

3. Ragnar Nurkse, Problems of Capital Formation in Under developed Countries (New York: Oxford University Press, 1960), p. 4.

the accumulation of capital. Consequently, there can be no marked increase in output. In the extreme form, such an economy remains on the subsistence level. To break the circle therefore, capital outflow to less developed countries is necessary, but not sufficient to guarantee development.

B. The Present Situation of Foreign Investment

Importation of foreign capital is then necessary for a country's economic development. This is not a novel phenomenon. In the past as well, especially during the nineteenth century, foreign capital contributed greatly to the economic development of several countries. The United States is a good example. Foreign investment in the nineteenth century and the beginning of the twentieth came from private sources.[4]

In the years since the second world war, certain new trends have appeared in the international investment scene. A new factor of major importance is the extraordinary part played by public investment. Public capital in the form of inter-government lending as well as in other forms, has dominated the international financial scene.[5]

The chief creditor government is the United States, either directly or through a number of special agencies, such as the Export-Import Bank of Washington. In recent years, other states, including

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4. A.A. Fatouros, Government Guarantees to Foreign Investors (New York: Columbia University Press, 1962), p. 16.

5. Ibid., p. 19.

the Soviet Union, have begun to offer long-term loans. Public capital was also provided by international financial agencies, such as the International Bank for Reconstruction and Development (IBRD or World Bank), the International Finance Corporation (IFC), and the International Development Association (IDA).

Another form of public financing which at present plays an important role, is economic aid, i.e. capital in any form granted to a foreign state without obligation of repayment or payment of interest. Most funds of this type are provided by individual states, especially the United States.

With regard to private capital, the average annual outflow of private long-term capital in the period 1955-58 is about $ 4 billion.[6] The chief creditor country is the United States. The second most important creditor is the United Kingdom. Then comes France, Switzerland and recently the Federal Republic of Germany.

Even at its present level, private foreign investment falls short of the need of underdeveloped countries, not only because of its inadequate amount, but also because of its form and direction. Paul Hoffman,[7] Managing Director of United Nations Special Fund has said that the present combination of both public and private capital is only just enough to keep the underdeveloped nations from slipping backwards. Today, direct investment prevails over

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6. For these and the following figures, see United Nations, Department of Economic and Social Affairs, The International Flow of Private Capital 1956-1958 (E/3249) (New York, 1959), p. 9-20.

7. Earl Snyder, "Protection of Private Foreign Investment: Examination and Appraisal", The International and Comparative Law Quarterly, Vol. X (July 1961), p. 471.

indirect. According to an estimate, during the period 1953-57, United States direct investment abroad have been ten times as great on the average, as the net outflow of United States portfolio investment.[8]

Direct foreign investment is heavily concentrated in industries producing primary goods for export. Petroleum industry being the most important single industry. Investment in the petroleum industry and related activities has accounted for over 45% of the capital outflow of United States direct foreign investment in the years 1946-51.[9] The form of private foreign investment and its geographical distribution among industries is a matter of importance. The bulk of foreign capital continues to flow to the now highly developed countries, and goes only in relatively low proportion to the underdeveloped countries.[10] At the end of 1959, investments in Canada and Western Europe constituted more than 50% of total United States private foreign investments.[11]

The unequal distribution of private foreign investments with respect both to geographical areas and to industries, is to a certain extent counterbalanced by effects of public capital. A high proportion of public capital is directed today to less developed areas. The United States and the World Bank are the main sources of supply.

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8. United Nations, Op. cit., p. 25.

9. United Nations, Department of Economic Affairs, The International Flow of Private Capital 1946-1952 (E/2531, ST/E CA/22, January 18, 1954) (New York, 1954), p. 12.

10. United Nations, Op. cit., p. 20.

11. A.A. Fatouros, Op. cit., p. 25.

C. Obstacles to Private Foreign Investment

The present situation of foreign investment conditions leads to the conclusion that the underdeveloped countries receive less private foreign capital than they need. It is difficult to provide a comprehensive classification of the causes for this shortage. The factors limiting private foreign investment in these countries are of diverse character, economic, legal, social and psychological. Some or all are in force in varying degree in one capital importing country or another. They all serve to discourage the potential investor or drive out the existing ones.

Here it is important to note that only a few of the obstacles in question, namely, those that can be removed through legal form, or, more particularly, by legal guarantees that are dealt with. The avoidance and removal of these deterrents will no doubt encourage the flow of private foreign capital.

1. Investment Climate

One of the many causes usually cited as responsible for the shortage of private foreign investment in the underdeveloped countries is the unfavorable investment climate existing im a great number of them. The term "investment climate" is to be understood as referring to the general attitude in a given country toward foreign investment, particularly as expressed in the relevant legal regulations.[12]

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12. Ibid., p. 34.

Many elements of diverse character, contribute to the formation of a country's investment climate. There are political, sociological, psychological, and other elements involved. The following quotation is representative: "Economic progress will not occur unless the atmosphere is favorable to it. The people of a country must desire progress, and their social, economic, legal and political institutions must be favorable to it."[13]

A country's investment climate depends closely on positive or negative action on the part of its government. In underdeveloped countries, government interference in the country's economy during its initial stages of economic development is essential to make such progress possible. The conditions prevailing in the under-developed countries make it necessary for their governments to undertake a wide range of functions. State measures affecting foreign investment may be divided into two general categories based on the relation of their objectives to foreign investment.[14] The first consists of measures relating specifically to foreign investors' activities, they are intended to control or regulate-screening requirements. The second category is composed of measures whose objectives are general in the sense that they relate to both foreign and domestic investors, but which either affect foreign investors more than domestic ones (for example, exchange restrictions), or affect both to the same extent but are of vital importance to all investors (for example, expropriation or taxation measures).

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13. United Nations, Department of Economic Affairs, Measures for the Economic Development of Underdeveloped Countries (E/1986,ST/ECA/10 May 3, 1951) (New York, 1961), p. 13.

14. A.A. Fatouros, Op. cit., p. 36.

The "Screening" of Foreign Investment

One of the situations sometimes cited as an obstacle to private foreign investment in underdeveloped countries, is the imposition by the state of restrictions or conditions on the entry of foreing capital. Typically, such restrictions take the form of "screening": in order to import his capital, the prospective investor needs prior approval of the competent government authority to which he submits his plans and which reaches its decision on the basis of considerations of general economic policy. The requirement of approval, in whatever form, is based on a number of economic considerations. Some of these considerations are made to avoid any balance of payment difficulties arising from unessential investments, others to protect established local industries, or in order to control inflationary tendencies, resulting from unrestricted investments.[15] This control over the entry and direction of capital is an indispensable condition for the operation of national economic planning.

From a legal point of view, the process of screening is within a state's sovereign rights under international law, but it acts as a deterrent to private foreign investment.[16]

2. Restriction on the Entry of Foreign Capital

The practice of screening is closely related to the imposition of restrictions on the entry of foreign capital, either into certain

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15. Michael Brandon, "Legal Deterrents and Incentives to Private Foreign Investments," The Grotius Society: Transaction For the Year 1957 (London: Wildly and Sons Limited, 1962) Vol. XLIII, p. 51.

16. Ibid.

specific fields of the economy or into the country as a whole. Such restrictions are usually derived either from investment laws or from exchange control legislation. These restrictions most commonly take the form of outright exclusion of foreign investments from the development of natural resources, notably petroleum which are reserved for government enterprise. Many of these restrictions express the deep distrust of foreign investors. The control over a country's key industries entails a significant measure of influence over the operation of its whole economy. Such countries feel insecure about foreign investment and try to equate it with "economic imperialism" and political dependency.

Such restrictions, often seek to achieve not the total exclusion of aliens but the increased participation of local capital in foreign-owned enterprises. In most instances, the ownership of a minority share by local nationals is accepted as sufficient to permit the establishment of a foreign owned enterprise. However, most countries place restrictions on the entry of aliens and foreign capital in a number of fields, mainly, in mining, petroleum extraction, transportation, and public utilities. In Colombia, for example, aliens may have only a minority share in the ownership of enterprises engaged in air transport or coastal shipping.[17] Provisions of this sort may affect unfavorably the interests of foreign investors when they require majority participation or effective control of the enterprise by local nationals.

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17. George Kalmanof and Rafael Benal Salamenca, "Colombia", Legal Aspects of Foreign Investment, ed. Wolfgang G. Friedman and Richard C. Pugh (Boston: Little, Brown and Company, 1959), pp. 174-175.

3. Restrictions on the Employment of Aliens

Similar problems arise with regard to the requirements found in the labor legislation of some states concerning the obligatory employment of their nationals by all enterprises operating in them. Under such legislation, a certain proportion of the personnel of all enterprises must be nationals of the state in which they are operating. Sometimes an additional requirement is required, by providing a minimum percentage of the payroll of an enterprise must be paid to local nationals. These limitations on the employment of aliens are a direct consequence of the labor situation in underdeveloped countries. They are calculated to contribute to the raísing of the general level of employment and to increase the existing native skilled labor. Actually the problem rises with regard to the limitation on the employment of skilled personnel in technical or managerial capacities. Foreign investors complain about and emphasize the inefficiency created because of the inexperienced and unqualified persons present among the higher-level personnel. In Pakistan, for example 50% of skilled personnel must be Pakistani nationals.[18] Other requirements sometimes impose restrictions with respect to the members of the boards of directors or equivalent bodies of local corporations. In the United Arab Republic, for example, the majority of the members of any company's board of directors must be nationals of the Republic.[19]

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18. United Nations, Department of Economic Affairs, Foreign Investment Laws and Regulations of the Countries of Asia and the Far East (ST/ECAFE/1, January, 1951) (New York, 1951), p. 57.

19. S. Habachy, "United Arab Republic", ed. Wolfgang G. Friedman and Richard C. Pugh, Op. cit., 572.

4. Exchange Control and Restrictions

Exchange Control, which is invoked because a country's supply of foreign exchange is not equal to the demand, operates to establish a rationing system. In its typical form, it involves a monopoly of all foreign exchange by a central agency which handles all imports and exports of foreign currencies and allocates the available foreign exchange. It may also involve restrictions on the outward movement of capital in times of financial crises.

The practice of exchange control is of great importance to underdeveloped countries, because of the fluctuations in the prices of their primary products, which constitute a constant source
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of balance of payment instability.

The existence, or the future imposition of exchange control is an obstacle to private foreign investment. The foreign investors have to submit to various requirements formalities and delays, whenever they wish to transfer their earnings or their capital outside the country of investments. They may not be allowed to take such funds out of the country, or they may be permitted to take out only a fraction. Moreover, exchange control affects foreign enterprises in that the employment of technical or managerial personnel in a foreign enterprise becomes difficult due to the limitations on the transfer of their salaries abroad.

5. Problems of Taxation

Compared to other elements which have been discussed, taxation presents certain peculiarities of its own. In the first place, the

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20. A.A. Fatouros, Op. cit., p. 48.

capital-exporting countries' policies are in this connection as important as those of the capital-importing ones. In the second place, it is usually considered as a normal business risk. In the third place, taxation is the sole element of the investment climate which affects directly a basic economic factor, namely, the investment rate of return. From the investor's point of view, any increase or decrease in the taxes which he would normally have to pay corresponds to a change in the profit rate of his investment. From this we can conclude that taxation may be a possible deterrent as well as a possible incentive to private foreign investment.

Taxation is considered as an obstacle to foreign investment in two ways. On the one hand, the foreign investor's income may be taxed both in his state of residence as well as in the country of investment. This "double taxation" is resented by the investors and seems undesirable for the development of international investment. On the other hand, taxation is related to the possible discrimination against foreigners by imposing excessive taxation on them. This discrimination and excessive taxation have adverse effect on the prospective foreign investor.

6. . <u>The Fear of Expropriation</u>

Expropriation, in its widest sense includes all forms of taking of private property by a state for public use in time of

peace,war, or national emergency.[21] It is considered as the strongest possible obstacle to foreign investment in underdeveloped countries.

The right of a state to expropriate the property of its subjects has been well established for a long time both in positive law and in legal theory.[22] However, the manner in which this right is exercised and, ultimately, the whole conception of expropriation, have changed in our days. The "social function" of property and the consequent duties of property owners are now stressed. There is a wide disagreement today, among states as well as among scholars as to the extent to which modern conceptions of private property have been adopted in international law.

During the nineteenth century, expropriations were generally rare and their legality depended on certain strict conditions: private property was not to be taken except for a public purpose and against payment of adequate compensation. But since the end of the second World War, the principle of the inviolability of private property has been disregarded by the expropriation measures that occurred in a great number of states. Today, expropriations are generally associated with social reform, political and economic reforms. They are large-scale operations and they assume a variety of forms, the most important of which is "nationalization." Nationalization is defined as the process whereby property, and rights and interests in property are transferred from private to public ownership by agents of the state on the

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21. Bin Cheng, "The Rationale of Compensation for Expropriation", The Grotius Society: Transactions for the Year (London: Wildly and Sons Limited, 1959), Vol. XLIV, p. 268.

22. A.A. Fatouros, Op. cit., p. 51.

authority of a legislative or executive measure.[23] Nationalization is said to have an adverse effect on the flow of private foreign investment in three ways.

Firstly, there is the relative uncertainty of the international law rules concerning the nationalization of foreign property, particularly, the requirement of compensation. Reference is made to the divergence of the standards of treatment between those states who uphold the standard of national treatment and those who support the international minimum standard. The fact that, if a dispute arose as a result of a measure of nationalization, and the investor had an opportunity to resort to an international tribunal, which will probably apply the international minimum standard and award him just compensation is not sufficient in the eyes of the foreign investor because compensation will seldom be equivalent to the profits to be expected of the normal continuation of the enterprise. Moreover, the possibility of an international tribunal to deal with an issue involving nationalization is not probable. No state within the Soviet block has signed the optional clause of the Statute of the International Court of Justice, and the argument put forward, by Iran in refusing the Anglo-Iranian Oil Company's request to submit their dispute to arbitration is a good example.

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23. Gillian White, Nationalization of Foreign Property (London: Stevens and Sons Limited, 1961), p. 41.

Secondly, there is the fact that nationalization measures are often a manifestation of one of the opposing concepts to private property. Its consequence is the weakening of the principle of the inviolability of private property. This lack of respect for private property was first shown in the Soviet confiscation of 1917 and subsequent years. Since then, the spread of socialist doctrine has caused an increasing number of nationalizations, principally in the Eastern European States, and the rise of nationalism has had similar results in the countries of Asia, the Middle East, and Latin America. The foreign investor, therefore, is aware that private property rights are no longer respected in many states and he is accordingly cautious and hesitant in investing his money.

Thirdly, there is the continual breach of the international law rule requiring the payment of prompt adequate and effective compensation for the nationalized property of aliens. States have flouted the rule time and again in the post-war period with the result that foreign investors feel that they can no longer rely on international law to protect their interests.

D. Necessity for State Guarantees

As has been shown, in many underdeveloped countries, domestic capital formation is so small that foreign capital, when available, is of considerable importance in starting economic development.

The task of developing the economies of these countries is especially urgent in view of the spreading national consciousness among the peoples concerned, and in some cases, e.g. India, of the rapid growth of the population, it will have to be accomplished within a short time.

The Role of Private Foreign Investment

The necessity of foreign investment is evident for a country's economic development. This is true for both public and private investment. Public capital, has certain definite advantages to the underdeveloped countries. It can be used to provide the basic facilities which are scarce or lacking and which cannot be provided by private investors. Moreover, it is strictly controlled by the country's government and may be used in accordance with an overall plan to cover in a balanced manner the various needs of the country. Such capital may be provided in the form of loans or grant, by individual states or through international financial organizations such as the IBRD. In public capital, political consideration plays an important role in determining the choice of form and the allocation of capital between recipient states.

Private capital, in general, and private foreign investment, in particular has an important part to play in the economic

growth of less developed countries. Private investment can assist chiefly by establishing new industries in certain fields. Its contribution is twofold. In the first place, it provides the capital necessary for the establishment of the various industries. In the second place, private foreign investment brings with it the technical and managerial experience which is scarce and needed in underdeveloped countries; thus making possible both the operation of the enterprise and the training of local nationals. Such experience is at least as important to underdeveloped areas as capital itself.

In America, it has been calculated that every dollar invested privately has the same success as three dollars invested from public funds and under public administration.[24] This proves that the private investor examines the market prospects more closely, and that profitability plays an important part for him in investing his capital. Thus misdirected investment is more easily avoided in case of private investment.

The Need for State Guarantee

If there is to be any increase in the amount of private

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24. Fritz Berg, "Investment Problems of the European Economy", International Convention for the Mutual Protection of Private Property Rights in Foreign Countries, comp. Society to Advance the Protection of Foreign Investments (Bergisch Gladbach: Joh Heider Druckerei und Verlag GmbH, n.d. [1959]), p. 18.

foreign capital in underdeveloped countries, some or all of the obstacles to its investment must be eliminated. Government action can affect most of these obstacles to various extents, especially those related to the investment climate. A country's investment climate must be understood as referring not only to the present but also to the future.

To the prospective investor, the existing legal situation regarding foreign investment is important enough, but it is even more important as an indication of the situation which will probably exist in the future. Since by investing his capital in a foreign country, he is subjecting it to the future changes in local conditions. In other words, the investor, must be reasonably certain of the future, he must be made to believe that there is little or no possibility of the creation of an unfavorable legal situation, at a later date, which will be harmful to his investment. The investor usually gains such assurance when a favorable legal situation existed for a long time, or when the country's economic and political structure is so stable that there is little probability of any major change in the immediate future. Thus, arises the need for legal guarantees to be given by the state or states concerned to foreign investors.

The guaranteeing states have to commit themselves as to the future, to promise that certain measures are not to be taken, or

that the investor will be compensated for any loss due to changes in such measures. The foreign investors have to be assured that they will receive, in the future as well as today, certain definite legal treatment as specified in the guarantees. Consequently, they need not fear of any major change unfavorable to their interests in the domestic legal or political conditions.

Legal guarantees to foreign investors are in all cases issued by states, but the party to whom the guarantees are directly addressed is not always the same.[25] It may be a single state, several states, a category of private persons or a single private person.

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25. A.A. Fatouros, Op. cit., p. 64.

CHAPTER II

Treatment of Aliens and their Property

With the progressive development of international society by increased facilities for travel and communication, the number of persons going abroad for purpose of business or of pleasure has steadily increased. Consequently, an increasing amount of capital, has been seeking investment in foreign countries, and the growth of international commerce and intercourse has resulted in the creation of vast commercial and other interests abroad. These movements of men, money and commodities, while of economic advantage both to the importing and to the exporting countries and establishing relations of mutual dependency between them, also create occasional friction.

The individual abroad finds himself in legal relation to two states, the state of which he is a national, and the state in which he resides or establishes his business. Nations, by common consent have established a certain standard of conduct by which a state must be guided in its treatment of aliens.

A. Legal Status of Persons Abroad

The alien in law occupies a position between two extremes - the one a barbaric exclusion of all aliens, the other, a complete

equality of nationals and aliens.[1] The first extreme, complete exclusion, is no longer compatible with the existence of the state as a member of international society. The first point of contact between a state and an alien is at the frontier or port where he presents himself for admission. Therefore, the first thing to inquire about, is the right of states to admit, exclude, and expel aliens.

With regard to admittance of aliens, every state has the right to admit aliens into its territory, or forbid them only in such cases as command themselves to its judgment. This is a well established principle of international law, which is best represented in the following quotation: "A state is under no duty in the absence of treaty obligations, to admit aliens to its territory. If it does admit them, it may do so on such terms and conditions as may be deemed by it to be consonant with its national interests. Likewise, a state may deport from its territory aliens whose presence therein may be regarded as undesirable. These are incidents of sovereignty."[2]

However, in practice the right of admission is freely accorded, subject to specific exceptions fully announced in advance and recognized as reasonable by world public opinion. The grounds for exclusion of undesirable aliens are fixed by the public interests of each state, which determines for itself what aliens or class of

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1. Edwin M. Borchard, The Diplomatic Protection of Citizens Abroad (New York: The Banks Law Publishing Company, 1927), p. 36.

2. Herbert W. Briggs, The Law of Nations: Cases, Documents, and Notes (New York: Appleton-Century Crofts, Inc., 1952), p. 535.

aliens are considered undesirable or dangerous. For political, social and economic reasons various classes of aliens are excluded. The following classes of aliens e.g. the physically, morally, or socially unfit have generally been excluded.

The right to expel aliens rests upon the same foundation and is justified by the same reasons as the power to exclude, namely, the sovereignty of the state and its public interests. The United States Supreme Court has said: "The right to exclude or expel aliens, or any class of aliens, absolutely or upon certain conditions, in war or in peace (is) an inherent and inalienable right of every sovereign and independent nation, essential to its safety, its independence and its welfare."[3] In recent times, collective expulsion has been resorted to only in very exceptional cases, while individual expulsion is still practiced and has been limited by statute and treaty, both to the justifying causes and the manner of exercise.

As has been mentioned, the general justification for expulsion is usually based on the public welfare of the state. Therefore, it would appear that the foreign government has a right to inquire into the reason for the expulsion of its citizens. On the other hand, the government exercising the right of expulsion must on demand provide evidence that the action was based on a

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3. Edwin M. Borchard, Op. cit., p. 49.

legitimate fear that the public interests were in danger. An expulsion without cause or based on insufficient evidence has been held to afford a good title to indemnity. Thus, in the Baffolo Case,[4] (1903) Baffolo, an Italian subject was expelled from Venzuela on the grounds of writing articles derogating to the Venzuelan government. On demand, Venzuela failed to furnish evidence that his action was detrimental to the welfare of the state and therefore, the umpire demanded that the injured alien be compensated.

The Alien is Subject to the Local Law

A foreigner within a state owes it a considerable measure of obedience in return for the local protection of person and property he receives while residing. The general principle is that a foreigner who voluntarily settles in a state, accepts the conditions and liabilities of a national of that state. His rights, opportunities and risks are subject to the local law. The state of residence is not expected to relinquish its right of jurisdiction over all such persons within its territory.

These alien rights are not derived directly from international law, but from the municipal law of the state of residence, although international law imposes upon it certain obligations which is compelled to fulfill. The establishment of the limit of rights which the state

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4. Milton Katz and Kingman Brewster, Jr., The Law of International Transactions and Relations: Cases and Materials (Brooklyn: The Foundation Press, Inc., 1960), pp. 62-65.

must grant to the alien is fixed along certain broad lines by treaties and international practice. It has secured to the alien a certain minimum of rights necessary to the enjoyment of life, liberty, and property, and has so controlled the arbitrary action of the state. When the local state violates these minimum rights, the right of diplomatic protection is invoked by the state of the injured alien. By a universally recognized customary rule of international law, every state holds the right to protection over its citizens abroad, to which corresponds the duty of every state to treat foreigners on its territory with a certain consideration.[5]

B. Standard of Treatment

The legal status of aliens is fixed by municipal law, but international law and the obligations of states towards each other, have imposed certain restrictions upon the freedom of action of the territorial sovereign. National legislation granting rights to aliens is usually based upon one or more of the following standards.

1. The Standard of Identical Treatment

According to this standard, states will promise to grant each other identical treatment in certain matters. Thus, a state in order to obtain for itself a favorable legal position in certain matters, is compelled to accord to other states a corresponding

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5. Alexander P. Fachiri, "Expropriation and International Law," The British Year Book of International Law, Vol. VI (1925), p. 161.

legal position. For example, Article II of the French Civil Code provides that "Aliens shall enjoy in France the same civil rights which are or shall be accorded to Frenchmen by the treaties of the nation to which that alien belongs."[6]

2. The Standard of National Treatment

This standard provides for inland parity, that is to say, equality of treatment between nationals and aliens. For example, Article II (2) of the Treaty Establishing the Benelux Economic Union (February 3, 1958) provides that the nationals of each High Contracting Party "shall enjoy the same treatment as nationals of that state as regards:[7]

(a) Freedom of movement, sojourn and settlement;

(b) Freedom to carry on a trade or occupation, including the rendering of services;

(c) Exercise of civil rights as well as legal and juridical protection of their person, individual rights and interests."

3. The Most-Favored Nation Treatment

In accordance with this standard, states undertake to grant each other the same rights or favors as they have granted or may grant, to any third state. For example, Article II (2) of the GATT

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6. Edwin M. Borchard, Op. cit., p. 71

7. Milton, Katz and Kingman Brewster, Jr., Op. cit., p. 82.

Agreement provides that the most-favored nation standard shall apply to custom duties, charges imposed in connection with the importation and exportation of goods, and to methods and formalities in connection with the importation and exportation.[8] This standard of treatment permits discrimination by each country in favor of its nationals but prohibits treating the nationals of any other country more favorably than those of the contracting parties.

It is important to note that these standards are not operating in isolation from one another. If, for instance, the most-favored treatment is coupled in a treaty with that of national treatment, it may well secure treatment to foreigners, which is privileged as compared with that of the nationals of one of the contracting parties. Thus, a treaty of commerce may provide for national and most-favored nation treatment, such as most of the United States FCN treaties.

The Equality Doctrine and the International Standard

International law is concerned with the specific provision of municipal legislations of states related to aliens, as well as

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8. Georg Schwarzenberger, The Frontiers of International Law (London: Stevens and Sons Limited, 1962), p. 225.

with the establishment of a standard which the state cannot violate without incurring international responsibility. International law demands - without regard to the status of nationals - that the treatment of aliens should not fall below the standard of international civilization as the objective goal. The State's liberty of action, therefore, is limited by the right of other states to be assured that a certain minimum in this respect will not be overstepped. This was clearly illustrated in the Neer Case[9] (1926) as follows: "that the treatment of an alien in order to constitute an international delinquency, should amount to an outrage, to bad faith, to willful neglect of duty, or to an insufficiency of governmental action so far short of international standards that every reasonable and impartial man would recognize its insufficiency. Whether the insufficiency proceeds from deficient execution of an intelligent law or from the fact that the laws of the country do not empower the authorities to measure up to international standards is immaterial."

The recognition of the international standard in the treatment of aliens frequently finds treaty expression, as in Article V of the United States - Italian Treaty of Friendship, Commerce and Navigation signed in February 2, 1948, which provides that the nationals of each High Contracting Party shall receive within the territory of the other "the full protection and Security; required

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9. Herbert W. Briggs, Op. cit., p. 614.

by international law."[10] The international standard deserves first place among the standards of treatment of aliens because it is the only standard which has grown into a rule of international customary law and because its applicability was widened so as to apply to all foreign nationals.[11]

Much controversy occurred on the question whether customary international law has actually established an international obligation requiring the state of residence to grant to aliens more than equality of treatment with its nationals, when the local standard falls below the international standard.

Certain governments and jurists hold that the alien, coming into the state of his own free will, is entitled to no better treatment that that which is accorded to the citizens of the state itself. This is based on the ground that each state, in the exercise of its sovereign rights, is privileged to maintain its own methods of procedure. If they are observed, the alien can have no complaint, and the state of which he is a national can have no ground of intervention on his behalf. In other words, if a state grants equality of treatment to nationals and non-nationals it fulfills its international obligations. This view has been advocated by Latin American States, jurists and by other states which have suffered most from diplomatic intervention. This is due to the unsettled social and economic conditions in the Latin American countries, which often placed the lives and property

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10. Ibid., p.

11. Georg Schwarzenberger, Op. cit., p. 219.

of aliens in danger. Therefore, these countries, knowing the advantages under which diplomatic protection has placed aliens, have in their municipal laws emphasized and insisted upon the application of the doctrine of equality of treatment of nationals and aliens.

But as has been mentioned, international law requires that the state of residence should treat aliens in a manner not to fall below the international standard of civilization. Hence, the doctrine of equality of treatment of nationals and aliens, while prima facie a fair defence, is not always internationally sufficient. As in the case of any international obligation, a state cannot set up its own municipal laws as the final test of its international rights and obligations, unless they are in harmony with the international standard.

One reason why the alien is not bound to submit to unjust treatment equally with nationals, against which the national has no judicial redress, is because the latter is presumed to have a political remedy, whereas the alien's inability to exercise political rights deprives him of one of the principal safeguards of the rights of the citizen.[12] For this reason diplomatic intervention may be invoked for the enforcement of his rights. Another powerful reason is the fact that international practice and arbitral decisions while admitting that the equality of treatment is a fair defence, yet it is not conclusively the final test for an international delinquency. Thus in the Robert Claim Case[13] (1926), the Commission

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12. Edwin M. Borchard, Op. cit., p. 106.

maintained: "Robert was accorded the same treatment as that given to all other persons . . . Facts with respect to equality of treatment of aliens and nationals may be important in determining the merits of a complaint of mistreatment of an alien. But such equality is not the ultimate test of the propriety of acts of authorities in the light of international law. That test is, broadly speaking, whether aliens are treated in accordance with ordinary standards of civilization." It follows from the above case that a state cannot justify its conduct merely by referring to the fact that its own nationals are not better off than the aliens. Therefore, the equality doctrine of nationals and aliens is not internationally sufficient, if it falls below the international standard of civilization.

C. Property Rights of Aliens

It is a well established principle of international law that every state has the right to regulate the conditions upon which property within its territory, shall be based. Therefore, any question in relation to property rights, should be found in the territorial legal system. Thus, the Permanent Court of International Justice held in the Panevezys - Saldutiskis Railway Case[14] (1939) that "In principle, the property and the contractual rights of individuals depend in every state on the municipal law and fall therefore more particularly within the jurisdiction of municipal tribunals."

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14. S. Friedman, Expropriation in International Law (London: Stevens and Sons Limited, 1953), p. 126.

Generally speaking, the power to acquire personal property is usually granted to aliens. However, a state may exclude foreigners from the acquisition of certain classes of immovables such as airplanes and ships, as well as impose other restrictions for public welfare. This should be limited to the effect that the alien should be granted certain rights pertaining to his legal personality (e.g. right of contract, marriage and family rights) and other prerequisites necessary for the enjoyment of a normal private life.

The Universal Declaration of Human Rights[15] (December 1948) in Article 17 (1) explicitly recognizes that "Everyone has the right to own property . . ." The object of that wording was undeniably to invest every person, at least in principle, with the capacity to acquire property rights any place whatever. But the primary purpose, seems to be rather to protect private property, against arbitrary action of the state.

This brings us to the question whether international law requires a state to respect the validly acquired rights of aliens. The United Nations International Law Commission[16] (1959), has studied this question and came to the conclusion that the respect for acquired rights "constitutes one of the principles of international law governing the treatment of aliens." This view is well supported by

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15. Milton Katz and Kingman Brewster, Jr., Op. cit., p. 850.

16. United Nations, Yearbook of the International Law Commission 1959 , Vol. II (A/CN.4.SER.A/1959/ADD. 1) (New York, 1960), p. 3.

writers and international judicial decisions. The Permanent Court of International Justice in its Advisory Opinion on the German Settlers in Poland[17] (1923), a case involving a question of succession, said that "private rights acquired under existing law do not cease on a change of sovereignty." This statement clearly shows that, in the event of a territorial change, there exists an international obligation to respect the rights of private individuals acquired under the legislation previously in force.

Another express statement of the principle of acquired rights was made by the Permanent Court of International Justice in its judgment in the case of German Interests in Polish Upper Silesia[18] (1926), where it declared that ". . . the principle of respect for vested rights forms part of generally accepted international law."

Lord McNair considers the principle of respect for acquired rights as "one of the general principles of law recognized by civilized nations."[19] Recently, however, some writers have on occasions voiced their objections and criticisms against the principle of respect of acquired rights. One of the most severe critics is Friedman,[20] in whose view the concept of acquired rights is not only "obscure, ambiguous and indefinable", but also "finds

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17. United Nations, Op. cit., p. 4.

18. Lord McNair, "The General Principles of Law Recognized by Civilized Nations," The British Yearbook of International Law, Vol. XXXIII (1957), p. 18.

19. Ibid., p. 16.

20. S. Friedman, Op. cit.,

no support in international judicial decisions and was repudiated by states during the preparatory work for the Codification Conference and cannot, therefore, be raised to the dignity of a principle of international law."[21] Similarly, Kaeckenbeeck has said that, as a means of solving major social reforms (nationalizations), "the theory of acquired rights has had to be admitted to be totally inadequate and powerless."

Nevertheless, despite these various criticisms and objections, the principle of respect for acquired rights, as a principle of general character, is undoubtedly of value from the technical and practical points of view.[22]

D. Nationalization Under International Law

Since World War I, the principle of the inviolability of private property until then generally accepted by civilized nations, has been disregarded by nationalization measures in a great number of states. These nationalizations relate not only to nationals of the nationalizing state, but in many cases also affect aliens. Many states have espoused the claims of their nationals for compensation against the nationalization of their property abroad, and many writers have been concerned with the effect of such measures on both the municipal and the international levels. Present-day international law concerning the protection of the private property of aliens is uncertain. In examining its content, it is essential

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21. B.A. Wortley, "Expropriation in Public International Law (Cambridge: The University Press, 1959), p. 125.

22. United Nations, Op. cit., p. 7

to keep in mind the disagreement as to the extene to which it adapted itself to modern conceptions of private property.

1. The States Right to Nationalize Foreign Property

The right of a state to nationalize foreign property is an attribute of the sovereignty of the state, in the sense of the supreme power which the state possesses in relation to all persons and things within its territorial jurisdiction. Some evidence of the recognition of this right by states is afforded by the United Nations General Assembly Resolution 626 (VII) of 21 December 1952 relating to the underdeveloped countries, in which the General Assembly has stated that "the right of peoples freely to use and exploit their natural wealth and resources is inherent in their sovereignty and is in accordance with the purposes and principles of the Charter of the United Nations."[23] A more recent illustration of this recognition may be found in the statement issued on August 2, 1956 by the Governments of France, the United Kingdom and the United States of America regarding the Egyptian Decree of July 26, 1956 nationalizing the Suez Canal Company. Paragraph 2 of the statement reads: "They (the three Governments) do not question the right of Egypt to enjoy and exercise all the powers of a fully sovereign and independent nation, including the generally recognized right, under appropriate conditions, to

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23. United Nations, Op. cit., p. 11.

nationalize assets, . . . which are subject to its political authority."[24]

At the present time, sovereign states claim the right to treat their nationals according to their discretion, and international law upholds this claim, but as soon as the property rights of aliens are affected, nationalization ceases to be a purely internal affair of the state. It produces external effects and accordingly comes within the domain of international law. That law recognizes the existence of a state's right to nationalize property within its boundaries, but at the same time it protects property rights of other states by insisting on a certain standard of treatment for the property of aliens.

2. The Territorial Limitation

Since the right of a state to nationalize the property of aliens flows from its territorial sovereignty, a state is not entitled to nationalize effectively the property of a foreigner which is located outside its territory at the time of nationalization. This territorial limitation on the right of nationalization is one of the principles of international law which has found uniform recognition in many countries of the world, both in case law and in legal writings.[25]

Nationalization laws sometimes expressly confine their

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24. Gillian White, Nationalization of Foreign Property (London: Stevens and Sons Limited, 1961), p. 36.

25. Martin Domke, "Foreign Nationalization," The American Journal of International Law, Vol. LV (July, 1961), p. 600.

application to assets located inside the territory of the nationalizing state. For example, the Iranian Law nationalizing oil industry in Iran provides that "the oil industry throughout all parts of the country, without exception, be nationalized."[26] On the other hand, the Egyptian Decree on the Nationalization of the Suez Canal Company specifically provided for the taking of the Company's property outside of Egypt "All its assets, rights and obligations",[27] thereby indicating the intention of the government to nationalize the foreign funds of the nationalized company as well. However, the extraterritorial effect of the Egyptian nationalization decree was not recognized in the Suez Canal Settlement Agreement[28] of July 14, 1958, which provided that the Government of the United Arab Republic "shall leave the assets outside Egypt" to the Company.

It is important here to note that the question of the legality or otherwise of the extraterritorial nationalization of foreign property does not arise unless the nationalizing state manifests an intention that its measure should extend to such property. If the nationalizing state showed such an intention, then the legal validity of an extraterritorial nationalization of foreign property can arise. In such a case, the rule of inter-

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26. Alan W. Ford, The Anglo-Iranian Oil Dispute of 1951-1952 (Berkeley: University of California Press, 1954), p. 268.

27. Martin Domke, Op. cit., p. 599.

28. E. Lanlerpacht (ed.) The Suez Canal Settlement (London: Stevens and Sons Limited, 1960), p. 11.

national law is clear; it is contrary to international law for a state to commit an act of sovereignty within the territory of another state, unless that other state should consent to such commission. The illegality lies in the violation of the territorial sovereignty of this latter state. However, if this latter state consent to the nationalization of property within its territory by a foreign state, then the internationally illegal act will be transformed into a legitimate exercise of the sovereign right to nationalize.

3. The Rule of Non-Discrimination

Nationalization of foreign property often involves discrimination by the manner and circumstances in which the measures are taken. Under international law, the nationalization measures must apply to all properties in a similar situation and must not discriminate against aliens or any particular group of aliens. Thus, if the property of aliens is nationalized and the property of nationals remains unaffected by the nationalization law, the measure is discriminatory and involves the responsibility of the nationalizing state towards the state whose nationals have been affected . Similarly, a state is internationally responsible if its measure affects the property rights of aliens of nationality A and not those of nationalities B and C who also own property rights of the kind specified in the measure. Therefore, in order to prevent nationalization from being discriminatory, it must at least provide equal treatment for all concerned.

An interesting question to be considered here is whether or not a measure which is expressly aimed at, or which in practice affects, a single undertaking possessing alien nationality constitutes illegal discrimination. The answer to this question is that there is as yet no rule of international law which provides that a state is guilty of illegal discrimination if it nationalizes alien property in a field where there are no national interests capable of being affected.[29]

A recent example of discrimination against aliens is to be found in the Cuban Nationalization Law[30] No. 851, of July 6, 1960, which was directed exclusively against American-owned interests, as expressed in Article 1 which reads as follows: "the nationalization, through expropriation, of the properties or concerns belonging to natural or juridical persons nationals of the United States of America or the concerns in which the said persons have a majority interest or participation even though they be organized under the laws of Cuba." In protesting against the Nationalization Law, the United States emphasized its discriminatory character by saying that "this law to be manifestly in violation of these principles of international law which have long been accepted by the free countries of the West. It is in its essence discriminatory, arbitrary and confiscatory."[31]

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29. Gillian White, Op. cit., p. 144.

30. Martin Domke, Op. cit., p. 602.

31. Ibid.

4. The Public Utility Principle

The right of a state to nationalize foreign property located within its territory, is sometimes qualified to the extent that the property has to be taken for a public purpose. This concept of public purpose or public utility is embodied in the nationalization laws of many countries, as a justification of taking private property. For example, the Cuban Resolution No. 1 of August 8, 1960, implementing the Nationalization Law No. 851 of July 6, 1960, states: "It is hereby declared that these expropriations are effected for reasons of public necessity and use and national interest."[32]

The position of international law with regard to the principle of public utility is not well settled. The majority of writers on the subject have supported the proposition that the nationalization of the property of an alien had to be for the public benefit of the nationalizing state. If the taking was not for public utility purposes, but for example was intended to benefit a private person, then the taking is a breach of international law.[33] Thus, Kunz, in his comment on the Mexican expropriations, regarded the principle of public utility as one of the conditions of expropriation laid down by a fully recognized international law. In the Walter Fletcher Smith Case[34] (1929) the Arbitrator regarded the taking of foreign

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32. Ibid.,p. 590.

33. Gillian White, Op. cit., p. 5

34. Bin Cheng, "The Rationale of Compensation For Expropriation," The Grotius Society: Transactions For the Year 1957 (London: Wildly and Sons Limited, 1962),(Vol. XLIV), p. 289.

property not for public purpose as illegal. The decision was based on the ground that "The expropriation proceedings were not, in good faith, for purpose of public utility . . . While the proceedings were municipal in form, the properties seized were turned over immediately to the defendant company, ostensibly for public purposes, but, in fact, to be used by the defendant for purposes of amusement and private profit, without any reference to public utility."

The Harvard Draft Convention[35] No. 12, in Article 10, paragraph 1 (a), considers the taking of foreign property as wrongful "if it is not for a public purpose clearly recognized as such by a law of general application in effect at the time of general application in effect at the time of the taking." Recently, the United Nations General Assembly[36] in its resolution 1803 XVII of December 1962 entitled "Permanent Sovereignty over Natural Resources" stated in paragraph 4 that "Nationalization, expropriation, or requisitioning shall be based on grounds of reasons of public utility, security or the national interest which are recognized as overriding purely individual or private interests, both domestic and foreign."

On the other hand, Metzger[37] seems to deny the existence

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35. Louis B. Sohn and R.R. Baxter, "Responsibility of States for Injuries to the Economic Interests of Aliens," The American Journal of International Law, Vol. LV (July, 1961), p. 553.

36. The American Society of International Law, International Legal Materials, Vol. II (January, 1963), p. 224.

37. Stanley D. Metzger, "Multilateral Convention for the Protection of Private Foreign Investment," Journal of Public Law, Vol. IX (Spring, 1960),

of the public utility limitation by saying that it is not "an international law requirement."[38] Similarly, Freidman considers that the motives of expropriation are a matter of indifference to international law, since the latter does not contain its own definition of public utility.

Admittedly any absence of public purpose will be normally difficult to prove, since it is hardly conceivable that a country will expropriate unless it considers that a public purpose, as it sees it, is involved. However, both state practice and international juridical practice know of cases in which the complete absence of a public purpose in purported acts of expropriation has been established. Moreover, the presence of the public utility principle is still useful and advisable since it can be of assistance in defining the concept of nationalization and distinguishing it from other forms of state interference with private property such as penal confiscation.

5. Compensation

From the international point of view, compensation is undoubtedly the crucial question in the matter of nationalization of foreign property. The important question to raise here is to examine whether international law imposes an obligation upon States to pay compensation to aliens whose property has been nationalized. In the opinion of some authors, the answer is in the negative. Thus,

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38. S. Friedman, Op. cit., p. 141.

Friedman[39] states that in the case of a general expropriation, no legally binding rule can be deduced from the practice of states requiring compensation to the owners, whether national or foreign, of property expropriated as a result of such reforms. This view appears to be shared, at any rate as regards nationalization by Charles De Visscher, Freeman and Delson.[40]

On the other hand, the view that a state is under an obligation to compensate to aliens in case of nationalization, is well supported by numerous authorities and international practice. Thus, it was pointed out by Domke[41] that the duty to compensate for nationalized alien property is "almost universally recognized." Similarly, Foighel[42] concludes that recent developments in international law seem to tend toward a rule that nationalization entails a "liability to pay compensation to foreigners affected by nationalization." The United Nations International Law Commission,[43] while examining the duty to pay compensation against nationalized alien property, has stated that "This obligation although it may have originated as one of the 'general principles of law recognized by civilized nations,' has now become a principle of customary

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39. S. Friedman, Op. cit., p. 206.

40. B.A. Wortley, Op. cit., p. 35.

41. Martin Domke, Op. cit., p. 603.

42. Isi Foighel, Nationalization: A Study in the Protection of Alien Property in International Law (Copenhagen: Nut Mordisk Forlag Arnold Busck, 1957), p. 85.

43. United Nations, Op. cit., p. 18.

international law." The International Law Association[44] has also recognized that the duty to pay compensation against foreign nationalization as "one of the basic principles of international law governing the treatment of aliens." Similarly, the Harvard Draft Convention No. 12, in Article 10, paragraph 2, considers the taking of foreign property as wrongful "if it is not accompanied by prompt payment of compensation . . ."[45]

Traditional case-law on the matter; offers ample precedents in support of this view. Thus, in the Upton Case[46] (1903), the Mixed Claims Commission held that "the right of the state . . . to appropriate private property for public use is unquestioned, but always with the corresponding obligation to make just compensation to the owner thereof." Similarly, in the de Sabla Case[47] (1933), the Commission examined the problem directly from the standpoint of international responsibility: "It is axiomatic that acts of a government in depriving an alien of his property without compensation impose international responsibility."

The classic formula which evolved during the nineteenth century and which has comparatively recently acquired some currency in legal writings, is that international law not only imposes an

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44. International Law Association, A Response by the Committee on the Study of Nationalization of the American Branch to the Questionnaire of the International Committee on Nationalization. A Report prepared by the Committee on The Study of Nationalization of the American Branch (International Law Association, February 20, 1958), p. 7.

45. Louis B. Sohn and R.R. Baxter, Op. cit.

46. United Nations, Op. cit.

47. Ibid.

obligation to pay compensation but also requires that compensation must, in order to be internationally valid, be prompt, adequate, and effective.[48]

The element "prompt", usually refers to the time at which payment should be made, not to the time at which the amount of compensation should be assessed. In order to be prompt, compensation must be paid either before the taking or within a reasonable time thereafter. This requirement is certainly not satisfied by a mere provision in the nationalization decree which leaves compensation to a future determination by the state's own legislation, adaptable to the wishes of the government. Thus, in Cuba, for example, the Agrarian Reform Law[49] of June 3, 1959, provided that compensation should be paid in twenty-year Agrarian Reform Bonds, with interest not exceeding four and one-half percent, and that their terms and conditions should be fixed in "due time". This provision that later legislation will provide, for the payment of compensation, does not comply with the requirement of prompt payment. On the international level, tribunals have used various expressions to indicate the proper moment for the payment of compensation. Thus, according to an important award in an arbitration between Germany and Roumania (Goldenberg Case 1928), compensation must be paid "as quickly as possible", while the decision in another case between Portugal and Germany (1930),[50] speaks of a "reasonable period."

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48. Ibid., p. 19.
49. Martin Domke, Op. cit., p. 605.
50. S. Friedman, Op. cit., p. 218.

The element "adequate" is a vague term capable of varying interpretations when it has to be expressed in terms of money. To be adequate, compensation must correspond fully to the value of the alien's interests affected by the nationalization measure. Usually, the alien's actual loss will correspond to the State's gain, so that by calculating the former, the latter is determined. However, in state practice and possibly due to the vagueness of the international 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.

The last element "effective", means that the compensation, when paid, should be of real economic value to the alien recipient. The question of "effectiveness" turns over on the currency in which compensation should be paid. In its final judgment in the S.S. Wimbledon Case[52] (1923), the Permanent Court of International Justice considered this question when particularising the compensation to be paid by Germany to the French Government. The court said: "Payment shall be effected in French francs. This is the currency of the applicant in which his financial operations and accounts are conducted, and it may therefore be said that this currency gives the exact measure of the loss be made good."

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51. Gillian White, Op. cit., p. 14.

52. Ibid., p. 16.

CHAPTER III

Form and Content of State Guarantees

A. Form of State Guarantees

Legal guarantees to foreign investors may assume several forms. States may offer protection to foreign investors by concluding international agreements concerning foreign investment. Capital-exporting and capital-importing states may come together and conclude several bilateral agreements, all states concerned may conclude a multilateral convention, embodying a "code" regarding the treatment of foreign investment. On the other hand, each state by itself may guarantee the security of investments of foreigners in the state or of investments by the state's nationals abroad by means of general promises.

1. Multilateral Conventions and Investment Codes

Since the Second World War, the adoption of a code of state practice regarding foreign investment in the form of a multilateral treaty has been strongly advocated. The increased consciousness of international economic problems together with the rise of international organization led to the formation of a strong movement for the general adoption of such a code. This movement was supported by writers, businessmen and was discussed by governments and international agencies, but with limited results.

The first chief general multilateral treaty to embody a code of foreign investment has been the Charter of the International Trade Organization (ITO)[1], signed at Havana, Cuba on March 24, 1948. Chapter III of the Charter (Arts. 8-15) dealt with economic development and laid down certain general rules regarding the treatment and position of foreign investment in the Contracting Parties. The Charter recognized the value of international investment, private as well as public, and the need for allowing opportunities for private investors and for assuring their security (Art. 12 (1) (a) and (b)). Capital-importing countries undertook in the Charter to avoid "unreasonable or unjustifiable action" injurious to the rights or interests of foreign investors (Art. 11 (1) (b); to "provide reasonable opportunities for investments acceptable to them and adequate security for existing and future investments (Art. 12 (2) (a) (i); to "give due regard to the desirability of avoiding discrimination as between foreign investments" (Art. 12 (2) (a) (ii), and to enter into consultation or negotiation with other governments with the aim of concluding bilateral or multilateral agreement relating to such matters (Art. 12 (2) (b).

The Charter provisions on foreign investments are limited. The provisions maintain that foreign investment should be protected, but with several qualifications and exceptions. The obligations

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1. Clair Wilcox, A Charter For World Trade (New York: The MacMillan Company, 1949), pp. 231-327.

of the capital-importing countries depend on a large extent on such vague terms as "just", "appropriate", and "reasonable". The Charter provisions did more to affirm the right of underdeveloped countries to interfere with investments than the rights of investors themselves.[2] The unsatisfactory investment provisions were a principal reason for the failure of the Charter to receive the endorsement of American business circles or the approval of the United States Congress.[3]

Another multilateral international instrument dealing in part with the protection of foreign investment is the Economic Agreement of Bogota, signed at the Ninth International Conference of American States on May 2, 1948.[4] The relevant provisions, which constitute Chapter IV of the Agreement (Arts. 22-27) are similar to the ITO Charter though more elaborate and somehow clearer.[5] The importance of foreign investments is emphasized and a general guarantee of "equitable treatment" and especially of non-discrimination, is given. The Contracting States undertake to reduce excessive taxes and to "impose no unjustifiable restrictions" on the transfer of earnings and capital. Expropriation of property is permitted, when non-discriminatory, but it is

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2. Richard N. Gardner, "International Measures for the Promotion and Protection of Foreign Investment", Journal of Public Law, Vol. IX (1960), p. 182.

3. Ibid.

4. Raymond Donnet and Robert K. Turner (ed.) Documents On American Foreign Relations (Princeton: Princeton University Press, 1950), Vol. X, p. 516.

5. Ibid., p. 523.

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2. Richard N. Gardner, "International Measures for the Promotion and Protection of Foreign Investment", Journal of Public Law, Vol. IX (1960), p. 182.

3. Ibid.

4. Raymond Donnet and Robert K. Turner (ed.) Documents On American Foreign Relations (Princeton: Princeton University Press, 1950), Vol. X, p. 516.

5. Ibid., p. 523.

clearly stated that "any expropriation shall be accompanied by payment of fair compensation in a prompt, adequate and effective manner." However, the provisions of the agreement, somewhat, inadequate from the private investor's point of view, were rendered meaningless by reservations attached to the agreement by various Latin American countries, subordinating the provisions of the treaty to their national laws.[6] The Bogota Agreement, like the ITO Charter, has never become a legally effective instrument.

The Organization for European Economic Cooperation (OEEC) has been studying in recent years the problems involved in the proposals for an international investment code.[7] Two draft conventions were submitted to it in 1959, one by the German and one by the Swiss government, and they have been under consideration by the Organization's Committee for Invisible Transactions. The Swiss proposal is a draft international convention concerning guarantees for the investment of foreign capital. It is relatively brief, consisting of seven articles, and it places special emphasis on repatriation of capital and earnings, compensation payments and currency inconvertability. The German proposal was the product of a joint revision of two earlier draft conventions, one prepared by a group of English and Continental lawyers under the Chairmanship of Lord Shawcross, the other drawn up by the German

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6. Richard N. Gardner, Op. cit.

7. Michael Brandon, "Survey of Current Approaches to the Problem," The Encouragement and Protection of Investment in Developing Countries (London: The British Institute of International and Comparative Law, 1962), p. 10.

Society to Advance the Protection of Foreign Investments, under the chairmanship of Dr. Abs.

When the Organization for Economic Cooperation and Development (OECD) came into being on September 30, 1961, one of the items carried forward from the predecessor organization (OEEC) was the project for drafting of an international convention for the protection of foreign investments, which had been referred by the OEEC Council to the Committee for Invisible Transactions.

In July 1962, a draft Convention was agreed by the Committee for Invisible Transactions and was submitted to the OECD Council. The OECD Draft Convention[8] consists of fourteen articles, and it places special emphasis on the obligations arising from taking of private property, the general standards of treatment, and the performance of undertakings.

In 1949, the International Chamber of Commerce (ICC) published a draft International Code of Fair Treatment for Foreign Investments,[9] to be embodied in a multilateral investment convention. The code prohibits discrimination against foreign investors and prevents restrictions on the ownership and personnel of private enterprises, allowing an exception only in case of "enterprises,directly concerned

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8. The American Society of International Law, International Legal Materials, Vol. II (March, 1963),pp. 241-267.

9. International Chamber of Commerce, International Code of Fair Treatment for Foreign Investments (Paris: Legram Press, 1949), pp. 13-17.

with national defence" (Arts. 3,4,5,6 and 7). It provides full freedom for the repatriation of capital and earnings outside the capital-importing country (Arts. 9 and 10); and full compensation in case of nationalization of foreign property (Art. 11).

In December 1960, an international businessmen's conference was held in Karachi by the ICC and dealt with the Code of Fair Treatment and finally agreed that it should be reviewed by the ICC in the light of the opinions expressed at the Karachi Conference.[10] However, despite this recent effort the Code of Fair Treatment has not received official recognition as yet.

In December 1958, the International Association for the Promotion and Protection of Private Foreign Investments (known as the APPI) was set up in Geneva as a non-political, non-profit-making organization with the aim of coordinating non-governmental efforts in the field of foreign investment and of promoting solutions safeguarding the interests of both investors and developing countries. It is composed of a number of industrial, banking and other concerns having international relations and interests in the development of foreign trade and investment. The APPI is convinced that any effort to promote the flow of foreign investments should be based on a multilateral Convention embodying

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10. Earl Snyder, "Protection of Private Foreign Investment: Examination and Appraisal," The International and Comparative Law Quarterly, Vol. X (July 1961), p. 481.

the following four principles:[11]

(1) Specific engagement by states must be carried out by application of the rule "Pacta Sunt Servanda."

(2) Prompt, adequate and effective compensation in the case of nationalization.

(3) Aliens and their property must be treated without discrimination.

(4) Settlement of disputes by means of neutral arbitrators.

In 1957, the German Society to Advance the Protection of Foreign Investments was established in Cologne, by a group of businessmen in Western Germany. The first major move of this society was its proposal for the adoption of a "Magna Charta" for the protection of foreign investments. A draft code entitled "International Convention for the Mutual Protection of Private Property Rights in Foreign Countries"[12] was published by the Society in November 1957.

The Draft Convention's chief objective is to provide to foreign investors the most extensive protection possible. Aliens are guaranteed "national treatment" and freedom from any restriction on the acquisition and utilization of property rights with some few

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11. International Association for the Promotion and Protection of Private Foreign Investments, APPI (Genève: International Association for the Promotion and Protection of Private Foreign Investments, n.d. (1964), p. 7.

12. Society to Advance the Protection of Foreign Investments, International Convention for the Mutual Protection of Private Property Rights in Foreign Countries (Bergisch Gladbach: John Heider Druckerei und Verlag n.d. (1959)),pp. 44-51.

exceptions in special fields. (Arts. IV and V). The Convention limits the capital-importing states' right to expropriate the property of Aliens and describes the form and extent of the compensation to be awarded (Arts. VI and VII). When, and if, expropriation occurs, it should be compensated for adequately and promptly (Art. VII). Not only the state party to the Convention but their nationals as well are entitled to rights under the Convention. In other words, an individual would be permitted to assert "rights before all courts and government authorities" (Art. IX). The Convention gives a list of possible sanctions against states violating its provisions (Art. XI (5) and (3)) and provides for the creation of an International Court of Claims. (Arts. X and XI). The proposal had a favorable reception in business circles and received considerable publicity.

In 1959, what appears to be an important effort to negotiate a multilateral treaty to protect foreign investment, is the effort brought forth by groups of European businessmen and lawyers, under the leadership of Dr. Abs of the Deutche Bank and Lord Shawcross, former Attorney General of Great Britain. The initial impetus came in 1957 when the German Society to Advance the Protection of Foreign Investments published its Draft Convention. This version was subsequently revised, and in April 1959, a "Draft Convention on Investments Abroad"[13] was issued. Sometimes known as the (Abs/ Shawcross Draft Convention on Investments Abroad).

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13. Society to Advance the Protection of Foreign Investments, Convention on Investments Abroad with Comments, Speeches and New Literature (Bergisch Gladbach: John Heider Druckerei und Verlag n.d. (1959)), pp. 9-12.

The proposed Convention provides for the fair and equitable treatment of the property of Aliens (Art. 1) and for the obligation of states to observe strictly "any undertakings which (they) may have given in relation to investments made by nationals of any other party" (Art. II). Expropriation of foreign property is to be allowed only under certain conditions (Art. III). Disputes relating to the Convention are to be submitted to an Arbitrational Tribunal (Art. VII (1)), to which nationals of the states party to it may also have access (Art. VII (2)).

In the United Kingdom, the Parliamentary Group for World Government established a Commission on a World Investment Convention which issued in July 1959, a report proposing a multilateral investment code.[14] The report was entitled "A World Investment Convention" and lays particular emphasis on the necessity of a wide membership and the participation of underdeveloped countries. It envisages the establishment of a special international agency, possibly the World Bank to deal with international investments. The possibility of the conclusion of special agreements between foreign investors and the governments of capital-importing states is generally favored. Such agreements should be respected or "fair compensation should be paid if they are revoked." The report further provides for the establishment of an Arbitration Tribunal (in case of dispute) and permits individuals and companies to have access. Sanctions should not be applied in case of non-compliance with the award.

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14. Parliamentary Group for World Government, A World Investment Code, A Report Prepared by the Commission on a World Investment Code (London: A.J. Crisp and Son Limited, 1959), pp. 5-21.

Recently, a number of international private groups have expressed in general terms their support for the adoption of an international investment code, stating on occasion, certain general principles whose inclusion in a code they favor. Such support is expressed in a resolution of the International Bar Association at its Conference in Cologne in 1958 and in Salzburg in 1960; the European League for Economic Cooperation, in 1958, and the Inter Parliamentary Union, at its Conference in Rio de Janeiro in 1958.[15] The studies on the international law of state responsibility by the Harvard Law School[16] may be mentioned here, although they are not directly related to an international investment code.

The subject of private foreign investments was brought up within the activities of international organization and usually the related discussions resulted in general recommendations on the policies of states to improve the investment climate in the capital importing countries. The United Nations General Asseembly adopted in its 1954 session, a resolution (Resolution 824 (IX))[17] concerning the encouragement and protection of private foreign investment. It recognized the important role of private foreign investment in the economic development of underdeveloped countries and made various recommendations to

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15. Earl Snyder, Op. cit., p. 486.

16. Louis B. Sohn and R.R. Baxter, "Responsibility of States for Injuries to the Economic Interests of Aliens", The American Journal of International Law, Vol. IV (July, 1961), p. 548.

17. United Nations, Department of Public Information, Yearbook of the United Nations 1954 (New York, 1955), pp. 135-136.

both capital-importing and capital-exporting states. To the former, it recommended the avoidance of discrimination and the facilitation of importation of capital goods and the repatriation of capital and earnings abroad. It also recommended both countries to conclude agreements for the promotion of private foreign investments. In this connection, one may compare the resolution favoring private investment mentioned above to the 1952 resolution on "sovereignty over natural resources", which emphasized the "right of peoples freely to use and exploit their natural wealth and resources."[18]

At the United Nations Economic Commission for Asia and the Far East (ECAFE), the Prime Minister of Malaya called for an international charter to safeguard the legitimate rights of foreign investors in the countries of Asia, a proposal which stirred some hopes especially because it was made by a representative of an underdeveloped country.[19]

In December 1958, the General Assembly adopted a resolution (Resolution 1318 XIII)[20] concerning the need for the improvement of investment climate in underdeveloped countries. It requested the Secretary-General to prepare a report concerning the promotion of international investments. The Secretary-General, in response to

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18. Oscar Schachter, "Private Foreign Investment and International Organization", Cornell Law Quarterly, Vol. XL (Spring, 1960), p. 419

19. Ibid., p. 422

20. United Nations, Economic and Social Council, The Promotion of the International Flow of Private Capital, A Progress Report by the Secretary-General (E/3325) (New York, 1960), Annex I, p. 1.

the above resolution adopted a report entitled "The Promotion of the International Flow of Private Capital".[21] This report dealt in detail with incentive measures taken by capital-importing as well as capital-exporting countries to increase the outflow of private capital. Moreover, the report dealt with measures for the protection of foreign investment and briefly examined the different forms which they may take. The attempt for an international investment code and other related proposals were discussed. Finally, the report, on the whole, was informative and seems to favor an international investment code.

2. Bilateral Investment Treaties

The recognition of the difficulties involved in the creation of an investment code is one of the important reasons toward the conclusion of bilateral agreements on the protection of foreign investments. This seems to be a new phenomenon since the commercial treaties concluded before the end of the Second World War were primarily concerned with the protection of the trader and merchant rather than the industrial investor.[22]

After the Second World War, treaty provisions dealing with investments and investors began to increase in number and relative importance. The United States first inaugurated a series of treaties dealing chiefly with investment problems. This is due to the

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21. Ibid., pp. 5-81.

22. Herman Walker, "Modern Treaties of Friendship, Commerce and Navigation," Minnesota Law Review, Vol. XXXXII (April, 1958), p. 807.

important position of the United States as the chief capital-exporting country and because "economic development of the under-developed countries is the hard core of the United States foreign policy."[23]

The main instrument used to serve this aim has been the United States Friendship, Commerce and Navigation (FCN) treaties. The general feature of the FCN treaties can be better understood in the "synoptical outline of normal content" provided by Herman Walker.[24] The typical modern FCN treaty contains provisions covering the following subjects: (1) entry, travel, and residence; (2) basic personal freedoms; (3) guarantees respecting property rights; (4) the conduct and control of business enterprises; (5) taxation; (6) exchange restrictions on currency conversion; (7) exchange of goods; (8) navigation and (9) exceptions and miscellaneous provisions such as the settlement of disputes arising under the treaty.

Since 1945 a considerable number of such treaties have been concluded by the United States though less than half of them with countries which may be considered economically underdeveloped.[25]

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23. George W. Ray, "Economic Development as the Hard Core of Foreign Policy: An American View," The Encouragement and Protection of Investment in Developing Countries (London: The British Institute of International and Comparative Law, 1962), p. 50.

24. Herman Walker, Op. cit., p. 808.

25. United States Council of the International Chamber of Commerce, Rights of Businessmen Abroad under Trade Agreements and Commercial Treaties, (New York: United States Council of the International Chamber of Commerce, 1960), pp. 53-54.

These bilateral treaties in the words of the United States Government - contain assurances against "rigid exchange controls, inequitable tax statutes, drastic expropriation laws and any other laws or juridical conditions that do not afford investors a proper measure of security against risks over and above those to which venture capital is normally subject."[26]

In recent years other countries also entered into bilateral investment treaties. The first such agreement concluded by United Kingdom, with Iran in March 1959. Article 8 (2) of the agreement maintains that "Each High Contracting Party shall at all times accord fair and equitable treatment to nationals and companies of the High Contracting Party, and to their property and enterprises; shall refrain from applying unreasonable or discriminatory measures that would impair their rights and interests; and shall ensure that their contractual rights are afforded effective means of enforcement in conformity with the applicable law."[27] Article 15 of this agreement provides that in case of expropriation, "prompt, adequate and effective compensation" should be paid "for any such measure". The Federal Republic of Germany have concluded a similar agreement with the Dominican Republic in 1957.[28] More recently, Switzerland

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26. United Nations, Economic and Social Council, Op. cit., p. 70.

27. Ibid.

28. Ibid., p. 71.

concluded commercial agreements with Sengal, Niger, Ginea, and the Ivory Coast, containing provisions for the protection of foreign investments.[29]

3. Guarantees by Capital-Exporting Countries.

In view of the difficulties and limitations of international arrangement, bilateral or multilateral, the need for legal guarantees to foreign investors can be met through municipal state action. Since it is the capital-importing states that are in need of foreign capital, it is usually they that offer legal guarantees to prospective investors. However, in accordance with their general policy of encouraging foreign investment, certain capital-exporting states, as well, offer guarantees to those of their nationals who invest abroad. At present, investment guarantee programs operate in at least three major capital-exporting countries. In recent years, both West Germany and Japan have expanded their guarantee programs, to include guarantees to foreign investments.

The United States investment guarantee program came into being in 1948 as a part of the Economic Cooperation Act "to promote world peace and the general welfare, national interest and foreign policy through economic, financial and other measures necessary to the maintenance of conditions abroad in which free institutions may survive and consistent with the maintenance of the strength and stability of the United States."[30] This program

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29. The American Society of International Law, International Legal Materials, Vol. II (January, 1963), pp. 144-150.

30. Marina von Newman Whitman, The United States Investment Guaranty Program and Private Foreign Investment: (Princeton: Princeton University

was broadened in 1950 to permit protection against loss from expropriation and confiscation. In 1951, the guarantees were further made available in all countries receiving foreign assistance from the United States. In 1959, the geographical area covered by the program was restricted to underdeveloped countries. The investment guarantee program then was enacted into law in 1961, as a part of the Foreign Assistance Act of 1961. The program is administered by the Agency for International Development (AID), on a fee basis, as a part of the United States Government effort to encourage private investment in friendly, less developed countries.

The American investment guarantee program[31] provides to the American Investors insurance, upon payment of a premium, against inconvertability of currency, expropriation of property, and war risks. In order that they may be insured, the investment must be approved both by the United States agency administering the program and by the government of the capital-importing state concerned. Only investments in countries which have concluded special agreements with the United States may be guaranteed. Under these agreements, the United States Government is subrogated to the rights of the investors who have invoked the insurance contract. In cases of expropriation, the matter would be submitted immediately to international arbitration, without following the usual procedure under international law which requires the exhaustion of local remedies.

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31. International Bank for Reconstruction and Development, Multilateral Investment Insurance, A Staff Report (Washington, D.C.: International Bank for Reconstruction and Development, 1962), Annex A-1, pp. 24-26.

The American investment program has been in operation for more than ten years and the total guarantees issued up to the end of June 30, 1959 amounted to about $ 448.2 million.[32]

A similar system of investment guarantees has been established in Japan in 1956, as an extension of its Export Insurance Law of March 1950.[33] The Japanese investment guarantee program was originally limited to the principal of overseas investments, then it was extended to profits in 1957. Under this program, eligible investment projects must be approved by the Japanese Government; the countries where the investment is operative may develop as well as underdeveloped; and there is no necessity for a related specific inter-governmental agreement. The program covers risks of expropriation, war, and non-convertability of investment earnings. Only 75% of the amount of loss is compensable, and upon payment of compensation, the Government of Japan is subrogated to the rights of the insured investor.

By the end of December 1961, 40 principal insurance policies amounting to about $ 12 million had been issued.[34]

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32. Marina von Newman Whitman, Op. cit., p. 51.

33. International Bank for Reconstruction and Development Op. cit., p. 27.

34. American Bar Association, The Protection of Private Property Invested Abroad, A Report by the Committee on International Trade and Investment, Section of International and Comparative Law (Chicago: American Bar Association, January, 1963), p. 34.

The most recent investment guarantee program is that established by the Federal Republic of Germany in 1959.[35] The guarantees are available to all firms established in Germany, which invest abroad, and especially in those investing in less developed countries. The investment in question must "merit encouragement, particularly those which strengthen Germany's relations with the less developed countries." There is no formal requirement for the specific approval by the government of the country of investment, as in the case of the American guarantees. Guarantees are available only to investments made in countries which have concluded investment protection agreements with Germany. The guarantees cover the risk of nationalization, war, and non-convertability. Capital investments may be guaranteed for a maximum of 15 years normally, but in exceptional cases, the term may be for 20 years.

By the end of December 1961, 87 applications for capital investment guarantees totalling D.M. 466.6 million had been approved.[36] Of the approved applications, 37 totalling D.M. 108.5 million, related to investment in Central and Latin America; 21, for D.M. 36.2 million, related to investment in Asia; and 4, for D.M. 1.8 million related to investments in Europe.

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35. International Bank for Reconstruction and Development, Op. cit., Annex A-3, pp. 28-29.

36. American Bar Association, Op. cit., p. 38.

Within the past few years, a number of private individuals and organizations have proposed that investment insurance should be placed on a multilateral basis. The object of these attempts was to increase the effectiveness of the insurance mechanism and to make insurance protection more widely available. The Development Association Group (now the Development Assistance Committee (DAC) of the Organization for Economic Cooperation and Development), meeting in Tokyo in July 1961, asked the International Bank for Reconstruction and Development to prepare a study of possible multilateral investment guarantee systems. The management of the Bank accordingly, undertook a study of multilateral investment insurance.[37]

While the principal proposals for multilateral investment insurance, differ from one another in detail, almost all of them envision a format: a group of both capital-importing and capital-exporting countries would establish an international agency (often suggested as an affiliate of the IBRD), which would insure private foreign investments in the less developed countries against certain risks. The "insured risks" vary, but usually include expropriation, currency inconvertability and wars. The investor would have to pay a premium for the insurance coverage, which might vary for the type of risk or investment involved, but which would be uniform for comparable investments in each participating host nation. Under

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37. International Bank for Reconstruction and Development, Op. cit., Annex B, pp. 30-37.

some proposals the host nation in which the investment is made would also pay a part of the insurance premium. If an "insured-against event" occurred, the international agency would pay to the investor from a capital fund consisting of accumulated premiums and capital contributions made by all the member nations. It would be a condition of participation under some proposals that countries accept certain rules of good conduct vis-à-vis foreign investment made in their territories, e.g., non-discriminatory treatment, no expropriation except for a public purpose and against full compensation, promptly paid and freely transferable.

4. Guarantees Offered by the Capital-Importing Countries

The most widely found type of state guarantee today consists of guarantees given to foreign investors by the government of capital-importing countries.[38] The manner in which such guarantees are offered varies in several respects. In recent years, the use of "investment laws", that is, statutes specifically designed to provide protection and encouragement to foreign investors has been increasingly favored, such as the "Law for Encouragement of Foreign Capital Investment"[39] of Jordan and the "Law for the Protection of Foreign Capital Investment"[40] of Turkey. In several cases, the governments of underdeveloped countries have issued formal statements of policy, indicating their general attitude towards foreign investments. For example, the Indian Minister of Finance, made a statement in November 1959, in which he said "that he had made it

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38. A.A. Fatouros, Government Guarantees to Foreign Investors (New York: Columbia University Press, 1962), p. 120.

39. United Nations, Economic and Social Council, Op. cit., p. 65.

clear to foreign private investors that India did not believe in nationalization as a creed, and had therefore no programme of nationalization as such. This did not mean, however, that particular industries will not be nationalized if public interest demanded it. In such an event, compensation would be paid. There was no scope for apprehension on the part of the foreign investors in regard to the security of their investment in India."[41]

The basic investment laws or other instruments often provide for special procedures through which specific guarantees, which refer to each individual investor, may be granted. A wide variety of provisions determine the procedures through which such guarantees are granted. In the typical procedure, the prospective investor must apply to the competent state agency, designated and created by the basic investment law, in order to have his investment approved or "registered". The agency investigates the nature and the qualities of the proposed investment in accordance with general rules usually set out in the original investment law. On the basis of this investigation, it approves or rejects the investors' application. It may also ask him to modify the application in accordance with its own suggestions; and the final instrument of approval is usually the product of extensive negotiations. By that instrument, the state grants to the investor some or all the assurances and privileges provided for in the original investment law, while the investor

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41. United Nations, Economic and Social Council, Op. cit.

undertakes certain obligations with regard to the form, amount and other elements of the investment. In short, we may find that such instruments are nothing more than that the investor has complied with the procedure provided by law. An example of an instrument of approval is the one issued in May 1956, [42] by the Greek Government concerning the importation of capital for the exploitation of Greek asbestos by an American corporation. It is in the form of a Royal Decree and starts with a statement of the importation of capital up to the sum of $ 8,350,000 to be used by the investing company for exploration, research and mining for asbestos, and for its production and sale. The validity of the instrument is conditioned upon the use of the capital for the purposes specified in this initial statement. The investing corporation is allowed to transfer abroad, without limitation, the capital imported and its profits. Its products may be exported abroad without restrictions, except for a proportion of 10% yearly, which must be disposed of in the local market. The investing corporation is granted exemptions from import duties and other charges on the machinery imported by it during the initial period of ten years. The employment of foreign personnel up to the number of twenty-five persons is permitted, and such personnel are allowed to export part of their salaries.

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42. A.A. Fatouros, Op. cit., p. 124.

There exist, however, two other types of instrument, which serve similar function although they are different in form and sometimes in content, than instrument of approval. These other forms are concession agreements and special contracts of guarantee.

A "concession agreement" is an instrument between a state and a private person and providing for the granting by the state to the individuals of certain rights or powers which normally would belong to and would be exercised by the state.[43] The subject matter of concessions falls into two principal categories, that is, public utilities and the exploitation of natural resources.

By "guarantee contract" on the other hand, is understood the instrument by which a state grants to an investor , under certain conditions, certain guarantees or privileges, in the absence of a special statute regulating the granting of such guarantees.[44]

Despite their similarities, the three types of instruments are not identical. They often differ in form: the instrument of approval usually takes the form of administrative acts, while concessions and guarantee contracts often assume the form of legislation. They also differ in content: the content of instrument of approval is generally predetermined by the investment laws by virtue of which they are issued. It follows certain

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43. Ibid., p. 125.

44. Ibid., p. 126.

predetermined formulae. Whereas concession agreements and guarantee contracts are more individual in character; they are designated to fit the specific investment involved. The differences in scope between these legal instruments can be better understood when concrete examples are examined.

An important concession agreement is the one between the National Oil Consortium (consisting of eight foreign oil companies) and the Government of Iran.[45] The agreement generally provides for the exploitation of the Iranian Oil through the cooperation of the two parties. Two operating companies are set up, one for the exploitation and production and the other for the refining of petroleum. The agreement describes in great detail the organization of the operating companies, their duties and rights and their relations with the government of Iran. The companies undertake, inter alia, to train Iranian personnel and "to be always mindful in the conduct of their operations of the rights and interests of Iran". An important section of the agreement is devoted to the financial arrangement between Iran and the Consortium. In short, the agreement is basically a 50-50 arrangement in a complicated form. The agreement was to extend for a minimum period of twenty-five years, subject to extension.

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45. J.C. Hurewitz, Diplomacy in the Near and Middle East (Princeton: D. Van Nostrand Company, Inc., 1956), Vol. II, p. 348.

An agreement of a different sort is the one between the Indian Government and the Standard Vacuum Oil Company concerning the establishment of oil refineries in India.[46] This may be a typical guarantee contract, a common enough form of agreement, in use in several Middle Eastern and Latin American States. This agreement was concluded in the form of an "exchange of notes"; that is, the investing company set forth in a letter all its proposals to the Indian Government, and the latter replied accepting them en bloc. After stating its proposals concerning the formation of an Indian corporation to construct and operate a refinery, the company asked the Government certain "assurances" which the Government by its letter of acceptance agreed to give. These assurances provide that the Government will not expropriate the refinery for at least twenty-five years, and to pay "reasonable compensation" for any expropriation thereafter. It also agreed that foreign exchange would be made available to the company for all expenses abroad, for the purchase of construction materials and equipment and of crude oil. It also assured that it would use its "good offices" to secure for the company any necessary lands and harbor facilities and supply of water and electricity. The investing company on the other hand, assured the prompt construction of the refinery, arrangement for the "training of an adequate number of Indian personnel", expenditures of certain sums to provide housing facilities for its employees.

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46. A.A. Fatouros, Op. cit., p. 127.

B. Content of State Guarantees

Despite the variety of the forms of state guarantees, there are close similarities between them from the point of view of content. They all refer to the same elements of a country's investment climate and they have largely common objectives. However, there exist some variations in content of these guarantees.

1. Standard of Treatment of Foreign Investors

In order to provide for the treatment of foreign investors, state guarantees have to determine certain legal standards by reference to which the lawfulness of a particular state measure is to be judged. Such standards have been classified under the two general headings of contingent and non-contingent standards.[47] A contingent standard is one that defines the treatment provided in relative terms. The specific content of this standard, at any time and in connection with any subject, is determined not by reading the treaty itself, but by reference to an exterior state of law and fact. The objective is to secure a non-discrimination or equality of treatment. The non-contingent standards, are "absolute" independent legal rules, which are to be applied whenever the need arises, without reference to the treatment given to others. Of the contingent standards, two are the most common, in the international and municipal practice of states. The standard of "national" treatment and that of "most-favored nation" treatment.

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47. Herman Walker, Op. cit., pp. 810-812.

In applicable situations nowadays, the first-class treatment tends to be that of national treatment.[48]

The definitions contained in the United States FCN treaties reflect the general usage of these terms. National treatment is defined in the FCN treaty of 1954 with Germany, (Art. XXV) reads as follows: "The term 'National treatment' means the treatment accorded within the territories of a party upon terms no less favorable than the treatment accorded therein, in like situations, to nationals, products, vessels, or other objects, as the case may be, of such party."[49]

The most-favored-nation treatment, on the other hand, is defined in the same treaty (Art. XXV), as the "treatment accorded within the territories of a party upon terms no less favorable than the treatment accorded, in like situations, to nationals, companies, products, vessels or other objects, as the case may be, of any third country."[50]

The non-contingent standards are illustrated in some of the FCN treaties. Thus the legal rules to be applied may refer to the standard of international law. For example, (Art. III (1)) of the FCN treaty of 1956 with Netherlands, provides that "the nationals of either Party, within the territories of the other Party shall be free from molestations of every kind, and shall receive the most constant protection and security. They

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48. Ibid.

49. United States Council of the International Chamber of Commerce, Op. cit., p. 60.

50. Ibid., p. 58.

shall be accorded in like circumstances treatment no less favorable than that accorded to nationals of such other Party for the protection and security of their persons and their rights . The treatment accorded in this respect shall in no case be less favorable than that accorded to nationals of any third country or that required by international law."[51]

Reference to the same standard of international law may also be found in the ICC Code of Fair Treatment (Art. 5 and 11 (a)).

The 1959 Draft Convention on Investment Abroad seems to follow the non-contingent standards. This is illustrated in the Comment on the Draft Convention by its authors, where they explained that the principles mentioned in the Convention, "are believed to be fundamental principles of international law."[52] The national treatment of foreign investors is found in the ICC Code of Fair Treatment (Art. 3). This standard was also used in the 1957 Draft Convention for the Mutual Protection of Private Property rights in Foreign Countries, which also provided for the application of the most-favored nation standard whenever, it was more favorable to Aliens (Art. IV (4)). Similar provisions are somehow found in the proposal of the Parliamentary Group of World Government (Para. 33 and Para. 39).

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51. U.S. Treaties and Other International Agreements, Vol. VIII, Part 11, p. 2047.

52. Society to Advance the Protection of Foreign Investments, Convention on Investments Abroad with Comments, Speeches and new Literature (Bergisch Gladbach: John-Heider Druckerei und Verlag, n.d. (1959)) p. 13.

In some investment laws, we find that the grant of national treatment to foreign investors is not expressly stated, but may be inferred from various provisions. For example, Article 10 of the Turkish Investment Law No. 6224, January 18, 1954 reads as follows: "All rights, immunities, and facilities granted to domestic capital and enterprises shall be available, on equal terms, to foreign capital and enterprises operating in the same fields."[53]

2. Restrictions on Business Activities of Foreign Investors

Most of the United States FCN treaties contain provisions allowing states to impose restrictions on ownership of property by aliens, either on grounds of public safety or with respect to ownership of enterprises not granted national treatment. This is to be done "without impairing the rights and privileges" accorded to aliens by other provisions of the treaty (Art. IX (2)).[54]

The ICC Code, in addition of granting national treatment to all foreign investments (Art. 3) provides in Article 6, that the parties to it, "Shall not introduce any legislative or administrative provisions on: The nationality of the shareholders; the composition of the board of directors and the choice of the directors". Exceptions are permitted only in case of enterprises "directly concerned with national defence".

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53. Rasim Cenani, Op. cit., pp. 29-30.

54. Robert Renbert Wilson, United States Commercial Treaties and International Law (New Orleans: The Hanser Press, 1960), p. 340.

The 1957 Draft Convention for the Mutual Protection of Private Property Rights goes further in this respect and recognizes the right of each state "to limit the acquisition, utilization and administration of property, rights and interests by non-nationals, and their right to dispose thereof, whenever such non-nationals intended to become active in the field of public utilities, public transport, the utilization of nuclear energy and the production of arms and war material". (Art. V (1)).

The OECD Draft Convention provides that the Convention "shall not affect the rights of any party to allow or prohibit the acquisition of property or the investment of capital within its territory by nationals of another." (Art. 1 (b)).

With regard to investment laws, foreign investors are not granted national treatment with respects to all fields of the capital-importing country's economy. Several fields are restricted to local nationals; aliens are either not admitted in them at all, or they are admitted only under strict conditions. For example, the Mexican legislation, limits foreign participation in the ownership of enterprises engaged in a number of specific activities to a minority shares.[55]

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55. Edward Hidalgo, "Mexico", Legal Aspects of Foreign Investment, ed. Wolfgang G. Friedman and Richard C. Pugh (Boston: Little, Brown and Company, 1959),pp. 356-358.

The United States FCN treaties regarding the employment of skilled personnel in alien-controlled enterprises are not forceful. Article VIII (1), of the treaty with Netherlands provides that the nationals and companies of either party, "shall be permitted to engage within the territories of the other party, accountants and other technical experts, executive personnel, attorneys, agents and other specialists of their choice." Of the different investment codes, the ICC Code seems to go into some detail concerning this question of employment of foreign personnel. According to Article 6 of the Code, no restriction should be placed on "the selection or introduction into their territories of such administration, executive and technical officers and staff, not nationals of those territories, as shall be deemed by the enterprises to be requisite for their efficient operation."

Investment laws are often more elaborate on this question. For example, the Greek Law[56] of 1953 provides that: "Enterprises established or assisted financially by foreign capital shall be permitted to employ foreign nationals in higher positions of their technical and administrative personnel to pay them in foreign exchange transferable abroad as provided in the instrument of approval to be executed in each case." Similar provisions are found in the Turkish investment Law of 1954 (Art. 7 (a) and (b)).

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56. A.A. Fatouros, Op. cit., p. 152.

The problems of foreign exchange control in most capital-importing countries have received particular attention in the various proposals to encourage private foreign investments. Most of the recent proposals provide for freedom of transfer of capital and earnings. The ICC Code of Fair Treatment provides that capital-importing countries should allow freedom of transfer of current payments arising of the alien's investment including dividends and profits (Art. 9 (a)). No restrictions or limitations on the investor's freedom of transfer are recognized except those which "may be authorized under the Agreement of the International Monetary Fund." (Art. 9).

The British Parliamentary Groups' proposal, provides for the free transfer of capital and earnings, "subject to the possibility of exchange control on reasonable balance of payments grounds as well as to any agreement regarding the rate of withdrawal of capital or limitation of dividends (Para. 45).

Most of the United States FCN treaties contain a general prohibition of exchange restrictions, while at the same time they allow several exceptions to it. Sometimes restrictions specifically approved by the International Monetary Fund (IMF) are permitted under the terms of the treaty. For example, Article VII (a) of the treaty with Netherlands provides that "Neither party shall impose exchange restrictions . . . except to the extent necessary to maintain or restore adequacy in its monetary reserves . . . . It is understood that the provisions of the present article do not

alter the obligations of either party which may have to the IMF." Under the American Investment Guarantee Program, the investor is protected against the convertibility of foreign currency investment into dollars. If a protected risk should materialize, the investor should surrender his inconvertible currency to the Government and would receive dollars in exchange in accordance with an agreed rate-of-exchange formula fixed by the guarantee contract. However, it is important to keep in mind that under the American Program, protection is not available against loss by virtue of normal commercial risks.

Investment laws also contain provisions concerning the repatriation of capital and earnings of foreign investors. However, the withdrawal is not always the same. Sometimes withdrawal of all profits is allowed. Thus, the Turkish Law of 1954 provides that "such net amounts (of profits) as accrue to the owners of the foreign capital base are entitled, subject to the permission of the Ministry of Finance, to transfer abroad in the currency of the country which the foreign capital base originated and at the prevailing official rate of exchange." (Art. 4 (a) (1) and (c)). In most investment laws, withdrawal of profits is allowed within certain limits, usually in proportion to the amount of initial investment. Thus, the Bolivian Law[57] of 1954 provides that the profits which may be

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57. A.A. Fatouros, Op. cit., p. 160.

withdrawn and transferred abroad each year cannot exceed 15% of the original capital invested.

3. Protection Against Expropriation

Investment codes and bilateral treaties place particular emphasis on the problems arising out of possible measures of expropriation of foreign property. Investment laws, generally, do not attach importance to this matter, though relevant provisions are found in several of them.

The ITO Charter provisions on expropriation are of limited effects. Each member state promises to take no "unreasonable or unjustificable action within its territory injurious to the rights or interests of nationals of other members in the enterprise, skills, capital, arts on technology which they have supplied" (Art. II (1) (b)). Each member state should provide "reasonable opportunities for investments acceptable to them and adequate security for existing and future investments." (Art. 12 (a) (i)).

The Bogota Economic Agreement was more explicit, by stating that national treatment must be accorded in matters of expropriation as well as some absolute standards, by stating the need for "fair compensation in a prompt, adequate and effective manner." (Art. 25).

Some of the proposed codes provide strict conditions for the expropriation of foreign property. According to the ICC Code of Fair Treatment, expropriation of foreign property are to be effected in accordance with certain "principles". The expropriating

state "shall state explicitly the purpose and conditions of such expropriation or dispossession." (Art. 11 (b)). The expropriating law, "should be in accordance with the appropriate legal procedures and with fair compensation according to international law" (Art. 11 (a)). The compensation to be paid to the alien, should be determined prior to the expropriation and should be paid in cash or in "readily marketable securities," freely transferable to the Alien's currency. (Art. 11 (d)).

Similar strict conditions for the expropriation of foreign property are found in the OECD Draft Convention. Article 3, provides that no party shall take any expropriation measures against a national of another party, except under certain specific situations. The measures should be taken in "the public interest and under due process of law" and are "not discriminatory or contrary" to previous undertakings" (Art. 3 (i) (ii)). The measures should be accompanied by the payment of just compensation, "representing the actual value of the property affected and shall be paid without undue delay, and shall be transferable" in an effective form (Art. 3 (iii)).

The 1957 Draft Convention of the German Society to Advance the Protection of Foreign Investments dealt in great detail on the problem of expropriation. The property of foreign investors must not be expropriated for a period of at least thirty years after investment. (Art. VI (1)). Only one exception is allowed, that of national emergency. The property of other aliens could be expropriated only when the "predominance of public interests demands such action". (Art. VI (A)). With regard to compensation, the alien would be

granted "substitution and/or compensation equivalent to the value of the expropriated property", at his own choice. (Art. VII (1)). The amount and form of compensation would be determined prior to the taking and final payment should be made "as soon as practicable" (Art. VII (3)).

The British Parliamentary groups' study seems to ignore the conditions for expropriation and concentrates on the need for fair compensation. "Fair compensation should be paid in the event of nationalization. (Para. 46). This compensation "should be adequate effective and prompt." (Para. 47). However, compensation should "depend on the amount required in relation to the capacity of the country to pay." (Para. 47). This is an interesting point and seems to be a great departure from the other proposals.

The 1959 Draft Convention on Investment Abroad lays down the conditions for the lawfulness of expropriation. Measures depriving aliens of their property had to be taken under the "due process of law," without discrimination, with no violation of undertakings given to the alien, and should be accompanied by "just and effective compensation," representing the genuine value of the expropriated property and paid in transferable form, without undue delay. (Art. III). Provisions for the determination and payment of such compensation would have to be made at or prior to the time of taking. (Art. III).

Probably the most important purpose of the United States FCN treaties is the protection of persons, property and other acquired interests from ill usage and expropriation.[58] The provisions on expropriation of the FCN treaties are similar to those of the investment codes. The treaties assure that the property of nationals and companies of either party will receive within the territories of the other "fair and equitable treatment" (Art. 1 of the treaty with Netherlands), as well as "the most constant protection and security (Art. III). Aliens are accorded national and most-favored treatment with regard to such matters. No party to the treaty shall take "unreasonable or discriminatory measures" that would impair the "legally acquired rights on interests of aliens in the enterprises which they have established, in their capital, or in the skills, arts or technology which they have supplied" (Art. V (3) of the treaty with Germany of 1954.)

The inviolability of private property is particularly reflected in the following quotation: "Property of nationals and companies of either party shall not be taken". . . except. . . . (Art. V (4) of the treaty with Germany). The exception to the rule refer both to the motive of the expropriating state and to the payment of just compensation. The justifiable reason for expropriation is "public benefit and in accordance with due process of law" (Art. V (4) of the treaty with Germany) or "public interest" (Art. VI (4) of the treaty with Netherlands). The provisions on

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58. Herman Walker, Op. cit., p. 822.

compensation are qualified. The alien-property is not to be taken without "just" compensation, representing the "equivalent of the property taken" in an effectively realizable form and adequately provided for at the time of the taking. (Art. V (E) of the treaty with Germany).

Under the American Investment Guarantee Program, the investor is protected against expropriation and confiscation. Expropriation may be broadly defined for guarantee purposes as any form of governmental action which prevents a foreign enterprise from controlling its property. In the case of loan investment, however, governmental action will be considered expropriatory only if it presents payment of principal or interest. Prior to the 1961 Act, a few cases arose in which breaches of concession agreements by the host government materially interfered with business operations.[59] There was some doubts whether to consider such acts as falling within the scope of expropriation. But the 1961 Act made it clear that "the term 'expropriation' includes but is not limited to any abrogation, repudation, or impairment is not caused by the investors' own fault or misconduct, and materially adversely affects the continued operation of the project."[60] The measure of loss for expropriation cases is the amount of the original investment not previously repatriated plus or minus the profit or loss thereon since the investment was made. Reinvested profit up to an amount equal to the original investment

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59. American Bar Association, Op. cit., p. 25.

60. Ibid., p. 26.

are generally covered. The investor whose claim is paid is required to turn over to the United States Government all right, title and interest in the expropriated investment.

Certain investment laws provide relevant provisions for the protection of foreign investors against expropriation. In Thailand, approved industrial undertakings are guaranteed that "the state will not transfer private industrial establishment to state ownership;" while in Oraguay, new investments in coffee cultivation may be granted exemption from expropriation proceedings.[61] Several other governments, on the other hand have expressed their readiness to grant to foreign investors' exemption from expropriation for a limited period of time. Thus, the Cambodian investment statute of May 1956 provides that the instrument of approval of the investment may guarantee against nationalization for a period of ten to twenty years after the importation of the capital.[62]

The 1954 Agreement between Iran and the Consortium of oil companies, contains an express provision against expropriation by providing that no act whatsoever of Iran or any governmental authority in Iran "shall annul this Agreement, amend or modify its provisions or prevent or hinder the due and effective performance of its terms. Such annulment, amendment or modification shall not take place except by agreement of the parties to this Agreement. (Art. 41 (B)).

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61. A.A. Fatouros, Op. cit., p. 172.

62. Ibid.

CHAPTER IV

Legal Effects of State Guarantees Given to Foreign Investors

A. The Legal Character of State Guarantees

Before examining the concrete effects of the promises of states to foreign investors, it would be useful to mention briefly the theoretical question of their legal character.

Not all forms of state guarantees present difficult problems in this connection. Guarantees made by treaty, either bilateral or multilateral, raise no special problems. FCN treaties and multilateral conventions are evidently instruments of public international law. They are agreements between states under public international law, basically contractual in nature, which impose certain obligations on and accord certain rights to the participating states. If the treatment promised by treaty to nationals of the other party to it is not accorded, this constitutes a breach of an international agreement and entails states' responsibility. Therefore, the legal character of international treaties cannot be doubted.

Neither does there arise any problem as to the legal character of the contracts of guarantees by virtue of which a capital-exporting country insures the foreign investments of its nationals against certain non-business risks. Two of the investment guarantee programs require inter-governmental agreements as a prerequisite for the eligibility of investments. Thus, the investment guarantee program

acquires an international character, since its continuous operation depends on the continuing operation between the governments involved. However, despite this international element found in investment guarantee program as a whole, the particular contracts belong entirely to the municipal law of the guaranteeing state. The performance by this state of its contracts with its own nationals is a matter governed by municipal law. Therefore, if the capital-exporting country refuses to perform its contracts with its nationals, its international responsibility will not arise.

It is when we study the guarantees given by capital-importing countries to individual foreign investors by means of special instruments that several complicated questions arise.

B. Legal Effects of Investment Treaties

The legal effects of state guarantees made by instruments of public international law, that is, the manner and extent of their implementation and the consequences of a possible violation of their provisions, are not difficult to determine. There is a vast body of legal literature, based on the case-law of international and municipal tribunals and on the practice of states, which deals with the effect of treaties, their binding character and other related problems. Treaties concerning matters of investment are not exceptional in their form. The difficulty, in such treaties, is to examine in each particular case, whether the violation of the treaty

has occurred. Therefore, a study of their legal effects, should drive us into an examination of the treaties' contents and the possible concrete instances of implementation or violation of the treaties.

1. The Standards of Treatment to Foreign Investors

The problem is how to apply the provisions of the treaties to any given factual situation and thus determine whether the treaty has been implemented or whether a violation has occurred. In this connection, the question of the choice between contingent and non-contingent standards of reference in the treaties is of special importance. Contingent standards, and in particular the standard of national treatment, have definite advantages from this point of view: since they refer to a body of precise and detailed legal rules, it is easier to determine in any concrete instance whether the treatment given to the foreign investors is in accordance with these rules.

However, the application of the standard of national treatment presents certain problems of its own. The first difficulty, involves the application of normally general measures which affect, only or chiefly, aliens and not nationals. When the oil industry is national-ized in a country where the only existing petroleum-exploiting company is foreign-owned, it is problematical whether this can be called a "general" act in accordance with the rule of national

treatment. The second difficulty, relates to the content rather than to the application of the rules in question. The rules applicable in the case of nationals may be unsatisfactory to the foreign investor. It may be that the political regime in the host state is corrupt and inefficient and that the existing laws offer little protection against arbitrary government action. It may be that, with respect to the particular industry in which the foreign investor is engaged, no definite legal or administrative policy has developed in the host state. In such cases, as in several other situations, the standard of national treatment might prove to be insufficient to protect the legitimate interests of the foreign investor.

With regard to this last feature of contingent standards, the non-contingent standards present certain advantages in that the treatment they prescribe is determined beforehand thus, presumably, does not fall below the international standard of civilization. However, the generality and abstraction of these standards, remains an important drawback. It is generally difficult whether a certain measure is in accordance with them, that is to say whether, in the usual treaty terms, it is "just", "reasonable", or "equitable".

2. Restrictions on Economic Activities of Aliens

The problems arising over the application and interpretation of treaties to foreign investors are quite evident in the case of United States FCN treaties. Under international law, the legality

of the limitations on the employment of aliens in underdeveloped countries, is unquestionable, since it rests on the sovereign right of every state to control the entry of aliens into its territory and to regulate economic activities therein. The FCN treaties place few real limitations on the powers of the host state to employ alien personnel. However, their legal value is more than doubtful, since they are phrased in such a manner as to leave to the governments concerned full freedom of action in the employment of foreigners. Even the permission to employ skilled personnel "regardless of nationality" is subordinated to the immigration and other laws of the host state. Therefore, it is possible for the capital-importing state to regulate the employment of aliens in foreign-owned enterprises as it wishes with very few limitations due to the FCN treaties.

As regards exchange control restrictions, customary international law seems to have evolved no special rules regarding this matter. However, the general principles applicable is that a state has exclusive competence to regulate its monetary matters. Consequently, the imposition of exchange control restrictions is not unlawful under international law. The FCN treaties establish as a general rule that exchange restrictions are not going to be imposed except in case of exceptional situations. This rule, it should be noted, replaces a pre-existing rule of customary international law according to which states as a rule are free to impose whatever restrictions they consider necessary to matters of money and foreign exchange.

One general exception to the said rule, under which the imposition of exchange restrictions is permitted is when they are specifically authorized or requested by the International Monetary Fund (IMF). The existence of the specific conditions is easy to determine, and the Fund's authorization is an indication of the necessity for exchange restrictions at the particular time.

The treaties further provide that foreign investors shall be accorded certain facilities for the transfer abroad of their earnings and capital when exchange restrictions are in force. Here, it cannot be contested that the provisions relating to the transfer abroad of the investors' funds are not very definite or certain. The states concerned do not undertake to make such transfer possible, but to "make reasonable provision" for it. Such provision may well consist in making possible the partial transfer of the sums involved. The proportion to be transferred cannot be determined with any precision in the abstract. It has to be judged according to the concrete conditions prevailing at the particular time. A proportion which might be "reasonable" under certain conditions might not be considered such when the conditions are different.

The treaties regarding taxation are similar to those on exchange restrictions chiefly in one respect. They reverse the customary rules of international law in the matter. While the imposition of taxes is a matter of exclusive domestic concern and there is no international law rule condemning discrimination against

aliens in matters of taxation, the FCN treaties provide for the national treatment of foreign investors, once certain conditions are fulfilled.[1] The standard they employ is in this case a very appropriate one which can safeguard better than any other investors' interests. The alien may thus refer, before or after investing his capital, to the relevant laws, administrative regulations, and court decisions in the capital-importing state and determine with some degree of precision the tax burden he will have to bear. However, the treaties do not protect the investor from the effects of any future change in the host state's tax legislation.

3. Expropriation in Violation of Treaties

The general rule with respect to the violation of state guarantees of non-expropriation made by means of public international law is clear and well settled. Expropriation in violation of such guarantees is in itself unlawful and constitutes an internationally tortious act, for which the expropriating state is fully responsible. This statement holds true regardless of the validity of the act of expropriation in municipal law, the existence or absence of public purpose and even the payment or not of adequate compensation.

The rule of law on the matter has been clearly stated by the Permanent Court of International Justice in its Judgment No. 13

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1. 1. A.A. Fatouros, Government Guarantees to Foreign Investors (New York: Columbia University Press, 1962), p. 222.

(1928) on the case concerning the factory at Chorzov.[2] In its judgment on the merits of the German claim for indemnity, the Court held that expropriation in violation of a treaty was to be distinguished from expropriation of foreign property under normal circumstances (that is, in the absence of a treaty provision). The Court said: "The action of Poland which the Court has judged to be contrary to the Geneva Convention is not an expropriation - to render which lawful only the payment of fair compensation would have been wanting; it is a seizure of property, rights and interests which could not be expropriated even against compensation, save under the exceptional conditions fixed by article 7 of the said Convention . . ."

The distinction, with some variations, is by now generally accepted in international law theory and practice.

However, this general rule, is of limited usefulness in considering the legal effects of the provisions on expropriation of the various treaties under consideration. It would be directly applicable in the case of expropriation in violation of the particular provision which is found in the 1957 Draft Convention for the Mutual Protection of Private Property Rights and which guarantees the non-expropriation of the property of foreign investors before the lapse of a certain period of time after the date of their original investment (Art. VI (1)). If expropriation occurred

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2. Gillian White, Nationalization of Foreign Property (London: Stevens and Sons Limited, 1961), p. 10.

before the lapse of the specific period of time, such an expropriation would have been unlawful, in accordance with the rule just stated.

The provisions in the other proposed investment codes, however, as well as those in the United States FCN treaties are of a different character. They provide that an expropriation is lawful under certain conditions. In these provisions, there is no attempt to create a new rule in international law concerning the expropriation of foreign-owned property, but to give conventional validity to a customary rule whose validity has been questioned.[3] With regard to this conventional rule, therefore, all the problems which exist with respect to the content of the customary rule will again arise. What cannot be disputed any more between parties to an FCN treaty is the validity of the rule itself, within the limits of the validity of conventional rules of international law.

Accordingly, if a state party to an FCN treaty expropriates the property of a United States citizen protected by it and refuses to grant compensation (on the ground, for example, that no compensation is being paid for the expropriated property of its own nationals), its action is internationally unlawful, because it violates the rule established by the treaty. If, however, the state agrees to pay compensation but not the amount demanded by the alien, then the treaty provisions would be of little help. The state might maintain that the compensation offered is "just" while the investor might be claiming the contrary; a deadlock might

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3. Robert Renbert Wilson, United States Commercial Treaties and International Law (New Orleans: The Hanser Press, 1960), p. 323.

well arise and the solution would depend on the negotiations of the parties concerned, or on the judgment of an international tribunal. Similarly, with regard to the requirement of "public purpose" which is found in many FCN treaties.

The main usefulness of investment treaties regarding expropriation lies in establishing a clear conventional rule in the place of an uncertain and contested customary rule. According to the official view of most capital-exporting states, the content of these two rules does not differ substantially. Therefore, the conventional rule is useful only insofar as it clarifies the customary one and makes impossible any contestation of its validity. In fact, since the content as well as the validity of the customary rule is a center of controversy, the treaty rule assumes great importance and usefulness.

The treaties provide an international law standard for judging the lawfulness or unlawfulness of an expropriation. The state whose nationals' property has been expropriated may well intervene diplomatically even before the exhaustion of local remedies, when the municipal law to be applied by the local courts falls below the standard established by the treaty. Moreover, the question of national treatment versus minimum standards of international law arises in a new form under such treaties. If the treatment accorded to a state's national is better than the minimum standards laid down in the treaties, then the expropriating

state has to extend such treatment to aliens as well by virtue of its promise to grant national treatment regarding such matters. If the treatment of its nationals falls below the treatment prescribed in the treaty, then by virtue of the non-contingent treaty rule, it has to accord to aliens the treatment which the treaty prescribes. In other words, the state has now a conventional obligation toward aliens which is quite distinct from its general obligation not to discriminate against them.

Generally speaking, there can be no doubt that, from the investor's point of view, the situation in the presence of investment treaties constitutes a distinct improvement over the situation in their absence. The diplomatic intervention of the state of the investor's nationality is now legally admissible being founded on the provisions of the FCN treaties. If the diplomatic methods of intervention prove not to be effective in any particular instance, there exists now a possibility of bringing the matter before an international juridical body, chiefly the International Court of Justice or an arbitration tribunal.

Investment codes as well as FCN treaties include provisions making recourse to juridical settlement of disputes and provides for the procedure to be followed in such cases. Under international law, such recourse would have been more difficult with respect to disputes involving expropriation and it would have been somehow impossible in most cases with regard to matters of taxation,

exchange restrictions, and the like. Similarly, under such treaty provisions, a final decision favorable to the investor's interests is more probable. An investor is far better protected when he can invoke treaty provisions applicable in his particular case. Regardless, of their interpretation of customary international law or the general principles of law, international tribunals have never rejected the rule of pacta sunt servanda, or even thrown doubt on it.[4]

In case of investment codes, it is suggested, by some of them that the enforcement of their provisions should be assumed by the threat of sanctions. Article XI of the 1957 Draft Convention for the Mutual Protection of Private Property Rights in Foreign Countries provided for the procedure to be followed and the means to be taken against a state acting in violation of its obligations under the convention. Once the unlawfulness of the state measures involved was established by a court decision, the state at fault would be asked to revoke them within a fixed period of time. If it failed to comply, its conduct would be publicly condemned by the court. The other states party to the convention would refuse to recognize within their territories the measures in question and would make available for the satisfaction of the judgment among property of the state at fault which they might have in their power (Art. XI (2) and (4)). A list of possible additional

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4. Hans Wehberg, "Pacta Sunt Servanda", The American Journal of International Law, Vol. LIII (October, 1959), p. 784.

economic sanctions is provided in the Appendix. Their application, nature, and extent would depend on the character and degree of unlawfulness of the states' measures involved. Such sanctions would include refusal of public or private loans to the state at fault, denial of investment guarantees to foreign investors operating in it, and recommendations to private or public banks in the capital-exporting states to refuse credits to enterprises intending to invest in the state at fault.

The 1959 Draft Convention on Investments Abroad, on the other hand, contains no such elaborate provisions. It only includes a general clause to the effect that when a state fails to comply with an award against it, the other states party to the convention "shall be entitled, individually or collectively to take such measures as are strictly required to give effect to that judgment or award" (Art. VIII).

No specific provisions on sanctions are included in the other proposed codes. In some of them, the advisability of such provisions is explicitly denied. For example, the report of the British Parliamentary Groups for World Government provides "no sanction in any normal sense of the word, are likely to be generally acceptable at the present time" (Para. 78). The only possible measure would be the publication of Arbitration Tribunal's award, and consequently exposing the states at fault before the world public opinion.

C. Legal Effects of Concession Agreements

It has already been noted that there are three main types of instruments by which states give specific guarantees to foreign investors, namely, concession agreements, guarantee contracts and instrument of approval issued by virtue of investment laws. These types of instruments have certain important common elements. They all involve two parties, one of which is a state or a public authority, the other, a private person, individual or corporation. These instruments are similar in their general contents. Through them, the state grants to private persons certain rights and powers which normally belong to the state. For example, private persons are permitted to exploit state-owned mineral resources. In several cases, the state may not actually grant its powers to the private persons, but it may undertake to refrain from exercising some of its powers with respect to such persons. A state may, for instance, grant to private persons exemptions from general taxation, or it may undertake not to expropriate their property.

These instruments have contractual elements and may be discussed under the heading of economic concessions.

1. The Nature of Economic Concessions

The nature, character and legal status of concession agreements have never been clearly determined. They are not in

fact treaties, since one of the parties is a private individual or corporation. Nor are they simply private contractual agreements, since the other party is a sovereign state. The state of the individual or corporation is also frequently involved directly or indirectly.

However, it seems to be generally accepted that one of the elements in the definition of an economic concession is that it involves an agreement by a state to grant a privilege to conduct an enterprise of some sort for a definite period.

A recent study on concession agreements stated that "an economic concession is a contract between a public authority and the concessionaire . . . Whatever be its form, a concession always involves a more or less complicated system of rights and duties between the concessionaire on the one hand and the state on the other. This relationship is one of mixed public and private law."[5]

Sometimes concession agreements are called economic development agreements so as to stress their economic importance. These are contracts made between states which have natural resources or other phases of the economy awaiting development but not enough capital or skill available for that purpose and corporations belonging to states which have capital and skill to spare.

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5. Kenneth S. Carlston, "International Role of Concession Agreements", Selected Readings On Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Mathew Bender and Company, 1964), p. 242.

G. Schwarzenberger classifies such agreements as quasi-international agreements, because they are concluded between a state and a foreign corporation inter pares.[6] They are neither contracts, governed by municipal law of some states, nor are they international treaties, since they are not concluded between subjects of international law.

These economic concessions are considered to be international by nature, not in the sense of being agreements between states but in the sense that their performance will require action in more than one state. Usually, a state's purpose in making a concession agreement is to have the natural resources of the state developed and revenue obtained by the state therefore under an agreement whereby the foreign national is granted rights and powers respecting the business involved. Therefore, a concession agreement is more than a mere sovereign grant. It is an organic instrument for the organization of international economic relations embracing many states of diverse economic interests. It becomes the means whereby much of the world's mineral resources are exploited and internationally distributed.

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6. Alfred Verdross, "The Status of Foreign Private Interests Stemming from Economic Development Agreements With Arbitration Clauses," Selected Readings On Protection By Law Of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Mathew Bender and Company, 1964), p. 121.

Its continued functioning becomes a basic expectation of producing, consuming and investing nations. Moreover, the concession agreement itself, of necessity generates economic movement both to and from the state. Frequently no phase of any operation under the agreement however local could be performed without materials, facilities and men brought into the local area from beyond the boundaries of the state.

The nature of economic concessions touches on the fundamental aspect of the question, namely, the law which governs the contractual relations which a state may establish with an alien private individual.

2. Law Governing Economic Concessions

The question of what law governs an economic concession has been answered in various ways.

Some argue that concessions are governed strictly by municipal law. They contend that there are only two kinds of law, international law and municipal law. International law governing relationships between sovereign states only and municipal law governing all other relationships. Since a concession agreement is not an agreement between two sovereign states, under this theory it can only be a private contract and hence can only be governed by municipal law.

In the Serbian Loans Case[7] (1929) the Permanent Court of

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7. F.A. Mann, "The Proper Law of Contracts Concluded by International Persons," The British Yearbook of International Law, Vol. XXXV (1959), p. 74.

International Justice asserted that "Any contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country."

Basing itself on judicial precedents and on diplomatic practice, the Committee established by the League of Nations for the study of international loan contracts stated that "Every contract which is not an international agreement - i.e., a treaty between States - is subject to municipal law . . ."[8]

It has been said that, unless a contrary intention appears, a concession is prima facie subject to the municipal law, and the presumption "is in favor of the municipal law of the granter."[9]

The United Nations International Law Commission in its Second Report on International Responsibility states that "Learned opinion and practice are agreed that contracts made between the Government of a State and an alien are governed, so far as their conclusions and performance are concerned, by the municipal law of the State and not by (public) international law, for a private person who enters into a contract with a foreign government ipso facto agrees to be bound by the local law with respect to the legal consequences which may flow from that contract."[10]

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8. United Nations, Yearbook of the International Law Commission, 1959, VOL. II (A/CN.4.SER. A/1959/ADD.1) (New York, 1960), p. 26.

9. Leo T. Kissam and Edmond K. Leach, "Sovereign Expropriation of Property and Abrogation of Concession Contracts," Fordham Law Review, Vol. XXVIII (1959), p. 195.

10. Leo T. Kissam and Edmond K. Leach, Op. cit.

Friedman[11] also stated that contracts cannot be the subject of international disputes since international law contains no rules respecting their form and legal effect.

Others, however, take the position that concession agreements in all essential respects are analogous to treaties and, therefore, like treaties, are governed primarily by international law. Even though a dispute arising under a concession agreement may begin as a dispute between a private person and a state, when the individual's government takes up his case, it then becomes a dispute between two states and thus enters the domain of international law. The Permanent Court of International Justice, in one of its judgments asserted that "By taking up a case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on its behalf, a State is in reality asserting its own rights - its right to ensure, in the person of its subjects, respect for the rules of international law. ... Once a State has taken a case on behalf of one of its subjects before an international tribunal, in the eyes of the latter, the State is sole claimant."[12]

There is a third view to the effect that concession contracts fall neither completely under the rules of international law nor under the rules of municipal law but somewhere in between, being governed in part by both and exclusively by neither.

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11. S. Friedman, Expropriation in International Law (London: Stevens and Sons Limited, 1953), p. 156.

12. Leo T. Kissam and Edmond K. Leach, Op. cit., p. 196.

Thus, O'Connel[13] states that the rights of the concessionaire are neither exclusively public nor private in character, but a mixture of both. Since a concession is not a treaty, it cannot be confined within the scope of international law. On the other hand, since one of the parties to the contract is the state, it cannot be exclusively a matter of private law.

Lord McNair[14] also maintains that concession contracts are governed in part by public and in part by private law. The system of law governing such contracts cannot be international law stricto sensu since these contracts are not interstate contracts and do not deal with interstate relations. He suggests that the system of law most likely suitable for the regulation of these contracts and the adjudication of disputes arising under them is "the general principles of law recognized by civilized nations."

Frequently, concession agreements contain provisions of a very general nature as to the law which shall govern their operation, such as the "principles of mutual goodwill and good faith as well as on a reasonable interpretation of this Agreement,"[15] or "goodwill and sincerity of belief and on the interpretation of this agreement in a fashion consistent with reason."[16]

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13. Ibid.

14. Lord McNair, "The General Principles of Law Recognized by Civilized Nations," The British Yearbook of International Law, Vol. XXXIII(1957), p. 19.

15. Alan W. Ford, The Anglo-Iranian Oil Dispute of 1951-1952 (Berkeley: University of California Press, 1954), p. 244.

16. Lord McNair, Op. cit., p. 12.

Still others provide that they shall be governed by the law of the granting state and "such principles and rules [17] of international law as may be relevant," or by such law and by the principles of law recognized by civilized nations."[18]

Both the Anglo-Iranian Concession Agreement of 1933 and the Consortium Agreement of 1954, which arose out of the settlement of the Anglo-Iranian dispute contained typical provisions illustrating the customary intent of the parties to this type of agreement to be governed other than only the law of the granting state.

Thus, Article 22 (F) of the Anglo-Iranian Concession Agreement[19] of 1933, stipulated that all differences between the parties were to be settled by an arbitral tribunal provided for in the agreement and further stated: "The award shall be based on the principles contained in Article 38 of the Statute of the Permanent Court of International Justice."

Article 46 of the Consortium Agreement[20] of 1954 between Iran, the National Iranian Company and certain other American, British, French and Dutch companies, provided as follows: "In view of the diverse nationalities of the parties to this Agreement, it shall be governed by and interpreted and applied in accordance

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17. The American Society of International Law, Proceedings of the Fifty-Third Annual Meeting (Washington, D.C., 1959), p. 268.

18. Lord McNair, Op. cit., p. 11.

19. Alan W. Ford, Op. cit., p. 245.

20. J.C. Hurewitz, Diplomacy in the Near and Middle East (D. Van Nostrand Company, Inc., 1956), Vol. II., p. 377.

with principles of law common to Iran and the several nations in which the other parties to this Agreement are incorporated, and in the absence of such common principles, then by and in accordance with principles of law recognized by civilized nations in general, including such of those principles as may have been applied by international tribunals." The elaborate methods and procedures of settlement envisaged by this Agreement shows the markedly international character of the Agreement.

Some important arbitration awards concerning concession agreements, refer to such principles in considering the question of law which governs them. An example can be found in the Lena Goldfidds Arbitration[21] (1930). So far as thequestion of the applicable law was concerned, the Court of Arbitration accepted the distinction formulated by the plaintiff company, namely, that on all domestic matters not excluded by the contract, including its performance by both parties inside the U.S.S.R., Russian law was "the proper law of the contract." But for other purposes, the "proper law" was contained in the general principles of law such as those recognized by Article 38 of the Statute of the Permanent Court of International Justice, because many of the terms of the contract contemplated the application of international rather than merely national principles of law. In

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21. Lord McNair, Op. cit.,

dealing with the question of compensation for damage caused, the Court of Arbitration stated that it preferred to base its award on the principle of unjust enrichment, as a general principle of law recognized by civilized nations.

In a concession agreement made between the Ruler of Abu Dhabi and a foreign Company, the parties declared that "they base their work in this Agreement on goodwill and sincerity of belief and on the interpretation of this Agreement in a fashion consistent with reason." (Clause 17) Of this clause, Lord Asquith of Bishopstone[22] as Sole Arbitrator between the Petroleum Development (Trucial Coast) Limited and the Ruler of Abu Dhabi (1951) declared in connection of the "proper law" of the Agreement that: "What is the 'Proper Law' applicable in construing this contract? This is a contract made in Abu Dhabi and wholly to be performed in that country. If any municipal system of law were applicable, it would prima facie be that of Abu Dhabi. But no such law can reasonably be said to exist. The Sheikh administers a purely discretionary justice with the assistance of the Koran; and it would be fanciful to suggest that in this very primitive region there is any settled body of legal principles applicable to the construction of modern commercial instruments. Nor can I see any basis on which the municipal law of England could apply. On the contrary, Clause 17 of the Agreement, cited above, repels the

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22. Ibid., p. 12.

notion that the municipal law of any country, as such, could be appropriate. The terms of the clause invite, indeed prescribes, the application of principles rooted in the good sense and common practice of the generality of civilized nations - a sort of 'modern law of nature'."

This was an important arbitral award and it was worth quoting, since in a later arbitration between the Ruler of Qatar and International Marine Oil Company Limited, relating to a contract which contained no provision on the applicable law, the arbitrator set forth similar opinions and conclusions.[23]

Most of these concession agreements, made more than a quarter of a century ago, clearly indicate that the parties were looking beyond the local law of either party for a settlement of their disputes. It seems safe to say that these are typical examples of the usual intent of the parties to such agreements not to rely upon the municipal law of either party as the only standard by which disputes arising under these agreements are to be judged.

Moreover, the fact that many of these agreements often contain provisions for the arbitration of disputes on an international level is further evidence of the fact that the parties are not thinking exclusively in terms of municipal law, Therefore,

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23. United Nations, Op. cit., p. 28.

at least on so far as any major alteration or modification of the mutual rights and obligations under the agreement is concerned, the parties are relying on something more universal and impartial than the local municipal law of either party, which is subject to unilateral change without notice.

Finally, it appears that the proposition that agreements between a state and a foreign national should be governed by international law is both logical and desirable and the adoption by international law of certain general principles of law recognized by civilized nations, is adequate evidence of their validity as legal principles and of their wide acceptance by civilized nations.

3. Expropriation in Breach of Economic Concessions

It has been established before that expropriation in violation of a treaty is in itself unlawful and constitutes an internationally illegal act, for which the expropriating state is fully responsible. The crucial question now, is whether the same principles that govern the legality of the expropriation of property by a state in violation of a treaty also govern the legality of its abrogation of a concession agreement.

A preliminary question to be settled first, is whether a state has the power to limit by contract its future action. It may be argued, in defense of the alleged right of a state to abrogate its contractual obligations at will, that a state is sovereign, and that as a sovereign, and as a lawmaker, it may lawfully alter the law it makes. Also one may contend that,

since the state is concerned with the economic welfare of its citizens, it cannot bind itself to relationships with individuals that might derogate from that welfare. Whenever the state considers that the general interest requires the breaking of a contract with an individual, it may lawfully do so. Furthermore, the alien who voluntarily contracts with a foreign state, subjects himself to the local law, and takes into account the probabilities of performance by the foreign state and the available local remedies, if any.

Frank Hindryx, in a recent paper delivered to the Arab Oil Congress held in Cairo in April 1959, presented the argument cited above, namely, the right of a state to abrogate a concession, despite its promise not to do so. He said : "Thus it seems clear that the sovereign state may by the accepted law of civilized nations, act through legislative or administrative decree, at its will, in ways which directly or in effect alter or nullify part or all of one of its existing concession agreements, so long as these actions are taken in good faith, that is on behalf of a substantial public interest and not merely because it repents of a former bargain."

There are some who argue that nationalization in defiance of contractual obligation is not contrary to international law, since the same rules that apply to the nationalization of foreign

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24. George W. Ray, "Law Governing Contracts Between States and Foreign Nationals," Selected Readings On Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Mathew Bender and Company, 1964), pp. 501-502.

property should apply to contracts.

Thus, Foighel,[25] stated that "The fact that nationalization is not a breach of international law cannot be altered by the fact that nationalization destroys contract rights, for example, a concession which the nationalizing state granted to a foreign company . . . There is no rule in international law that gives a greater degree of protection to rights secured by contract than to other right of property."

On the other hand, it may be argued with a greater force and conviction that there is the possibility of a government to commit its successor to abide by the terms of a concessionary contract. The advocates of this view, point out that in principles it is no different from the unlimited treaty-making power of a sovereign state in international law, whereby it can limit its future action and therefore becomes liable for the violation of the agreement made therein.

It was held that such a limitation in the exercise of sovereignty is an affirmation rather than a negation, of national sovereignty. Thus in a recent arbitral award between Saudi Arabia and Aramco[26] (1958), it was held: "By reason of its very sovereignty within its territorial domain, the State possesses

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25. Isi Foighel, Nationalization: A Study in the Protection of Alien Property in International Law (Copenhagen: Nut Nordisk Forlag Arnold Busck, 1957), p. 74.

26. George W. Ray, Op. cit., p. 493.

the legal power to grant rights which it forbids itself to withdraw before the end of the Concession . . . Nothing can prevent a State, in the exercise of its sovereignty, from binding itself irrevocably by the provisions of a concession and from granting to the concessionaire irretractable rights."

The arguments against the right of a state to abrogate a concession agreement have been put on several grounds. One such argument is based on the principle of acquired rights. Thus, a concession which has properly come into force, and has become a vested private right is considered to be under the protection of international law against the unlawful siezure on the part of the grantor.[27] Lord McNair, for example, maintains, that concessions should be governed by the general principles of law recognized by civilized nations, and that one of these is the principles of respect for acquired rights.

Other principles which have been advanced in support of the international responsibility of a state for the abrogation of a concession include: the principle of unjust enrichment, the principle of good faith, and the principle of respect for private property and the sanctity of contracts.

The most important and persuasive argument for holding states internationally responsible for nationalization in breach of a concession contract, is that based on the principle of pacta

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27. Lord McNair, Op. cit., p. 15.

sunt servanda. In accordance with this principle, it is universally agreed that under international law states are bound to perform their treaties with other states and to carry out in good faith the obligations assumed thereunder. It has been pointed out that the maxim pacta sunt servanda is a part of customary international law as well as one of the general principles of law recognized by civilized nations, and that no arbitral tribunal has ever rejected its rule or even thrown doubt on it.[28]

There is a strong support for the proposition that the principle pacta sunt servanda as a principle of international law also applies to contracts between states and foreign nationals.[29] Thus, Professor Wehberg, lending his weighty authority, concludes that "The principle of sanctity of contracts is an essential condition to the life of any social community. The life of the international community is based not only on relations between States but to an ever-increasing degree, on relations between States and foreign corporations or foreign individuals. No economic relations between States and foreign corporations can exist without the principle pacta sunt servanda. This has never been disputed in practice."

In its memorandum to the Permanent Court of International Justice in the Losinger and Company Case[30] (1936), the Swiss

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28. Hans Wehberg, Op. cit.

29. Ibid., p. 786.

30. Lowell C. Wadmond, "The Sanctity of Contract Between a Sovereign and a Foreign National," Selected Readings On Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal

Government contended that "The principle pacta sunt servanda . . . applies not only to agreements directly concluded between states but also to those between a state and foreigners."

The Swiss position received some support in the studies recently made by a non-governmental organizations of state measures affecting the contractual rights of aliens. The Committee on Protection of Foreign Property in Time of Peace of the International Bar Association[31] at its 1959 meeting in Cologne proposed the following resolution:

"International law recognizes that the principle pacta sunt servanda applies to specific engagements of States towards other States or the nationals of other States and that in consequence a taking of private property in violation of a specific State contract is contrary to international law."

The same position is taken by the International Law Association[32] in its 1958 meeting, where it asserted as a basic principle that states must perform their contracts with aliens (just as they must perform their treaties) in good faith and that nationalization is not a valid excuse for breach of such contractual obligations.

At its session in 1950 and in 1952, the Institute of International Law[33] submitted a draft proposal by its rapporteur, Professor de La

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31. George W. Ray, Op. cit., p. 500.

32. International Law Association, A Response by the Committee on the Study of Nationalization of the American Branch to the Questionnaire of the International Committee on Nationalization, A Report Prepared by the Committee on the Study of Nationalization of the American Branch (International Law Association, February 20, 1958), p. 15.

33. Lowell C. Washmond, Op. cit., p. 166.

Pradella which provided that "Nationalization . . . must respect agreements validly concluded, whether by treaty, or by contract."[34]

The United Nations International Law Commission, in its recent report on state responsibility, distinguishes between two categories of state contracts, namely, those of the "traditional type" where municipal law is applicable, and "internationalized" contracts, that is, which either refer, expressly or by implication, to international law, the general principles of law or contain arbitration clauses. The non-performance of such a contract in the first category will constitute a violation of international law only when it is "arbitrary" in character. The breach of a contract in the second category will constitute in itself a violation of international law and thus gives rise to international responsibility.

It has been said that the maxim pacta sunt servanda is linked with the principle of good faith. Thus, Bin Cheng asserts that "pacta sunt servanda,. . . is but an expression of the principle of good faith which above all signifies the keeping of faith, the pledged faith of nations as well as that of individuals. Without this rule, international law as well as civil law would be a mere mockery."[35]

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34. United Nations, Op. cit., pp. 31-32.

35. R.Y. Jennings, "State Contracts in International Law," The British Yearbook of International Law, Vol. XXXVII (1961), p. 175.

The principle pacta sunt servanda should apply irrespective of what the agreement provides as to what law is to govern. In case where the agreement specifically provides that international law or the general principles of law recognized by civilized nations,is to govern, then abrogation would clearly be a violation of the basic principles, namely: the principles of respect for acquired rights, unjust enrichment, pacta sunt servanda and the principles of respect for private property and sanctity of contracts. Even if the agreement provides that the law of a particular state, either alone or in conjunction with more universal principles, is to govern, or contains no provisions as to the governing law, the result would be no different. The unilateral and unjustified abrogation of such an agreement would be a violation of international law regardless of the provisions of the contract because it would deprive the concessionaire of that international standard of justice to which all aliens are entitled. The violation of this international standard occurs when a state enters voluntarily into a contract with a foreign national and then subsequently enacts legislation which abrogates the contract and permits the government unilaterally to repudiate its obligations. Since there is as a rule no local juridical remedy against the legislative action of a state, then its action in violation of a contract with a foreigner, constitutes a denial of justice which in tern, is a breach of international law.

Moreover, when the local municipal law is the proper law of the contract, just as in other situations, it must conform to the requirements laid down by international law. Thus, a termination or abrogation of the contract by a change made in the proper law, though it cannot amount to a breach of contract in the proper law, may nevertheless amount to a breach of international law.

Furthermore, it is to be noted that most of the concession agreements under consideration, provide for the arbitration of their disputes under the agreement and the refusal of the state to abide by the arbitration clause, has been held to constitute a denial of justice and consequently violates international law.

This short review on concession agreements, confirms the impression that the foreign investor, rather than submitting by his contract to the changing laws and likes of the host state, contracts on an equal plane, on the bilateral assumption that neither party can alter the agreement unilaterally. Parties normally contract in the expectation of performance. This expectation is a fundamental one and is a cornerstone in international relations. Therefore, there is no legal or moral justification for a state after committing itself to a contract with a foreign national to avoid its responsibilities on the theory that sovereignty embraces rights without correlative duties. Rightly, it was stated that nothing inherent in sovereignty prevents the performance of contracts and the granting of

irrevocable rights.[36]

D. Compensation

An important element in international law rules concerning the effects of state measures affecting the rights of aliens is its requirement that states' responsible for such measures should compensate to the aliens for the damage to their interests. The existence of such a requirement under international law is well settled. It is supported by the existing case law of international tribunals, by state practice and by the consensus of competent legal opinion.

1. Compensation for Lawful and Unlawful Expropriations

A state's obligation to compensation to aliens may arise either out of an unlawful interference with alien rights or out of interference which in itself is lawful under international law, but still creates a duty to compensate. The conditions governing lawful expropriation as laid down by international law are three. First, the measure should be calculated to promote the public welfare of the expropriating state. Second, the measure should be taken without discrimination against foreigners as such. Thirdly, there must be just compensation for the expropriated alien property.

Therefore, measures taken in accordance with these three conditions, are lawful under international law. If one or more of these conditions is not fulfilled, the act is internationally

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36. Leo T. Kissam and Edmond K. Leach, Op. cit., p. 393.

illegal. Moreover, it has already been noted, that measures taken in violation of treaty commitments, or measures followed by a denial of justice, are unlawful under international law. This distinction between lawful and unlawful measures, which now appears to be well established is of considerable practical importance because it corresponds to a difference in the manner in which compensation is to be assessed.

The reason for this difference lies in different legal foundations of the duty to compensate in the two cases. With respect to unlawful measures, compensation constitutes reparation for an international tort and has therefore a mixed punitive and compensatory character. Such compensation aims at restoring the exact status quo ante, at least in financial terms. It has to cover the alien's loss, as promptly and effectively as possible.

Different considerations apply in the case of lawful measures. The chief ground on which compensation is founded in this case is the general principles of law condemning unjust enrichment. This principle holds that a person who has been unjustly enriched at the expense of another is required to make restitution to that other. Friedmann[37] has expressed the view that "the principle of unjustified enrichment should now be held to be a general principle of law recognized among civilized nations."

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37. B.A. Wortley, Expropriation in Public International Law (Cambridge: The University Press, 1959), p. 96.

He cites the Lena Goldfields Case[38] (1930), as an example of an investment by a foreign company in the U.S.S.R., where the Arbitrators awarded damages to the company for its expropriation without compensation, holding that the company was entitled "to be compensated in money for the value of the benefits of which it had been wrongfully deprived. On ordinary legal principles this constitutes the right of action for damages, but the Court prefers to base its award on the principle of 'unjust enrichment', although, in its opinion, the money result is the same." The application of this principle means that the compensation to be awarded will have to be assessed on the basis of the state's profit from the measure involved, not on the basis of the aliens' loss.

Such a difference in the measure of compensation in each case is then a necessary consequence of the distinction between lawful and unlawful measures of expropriations. The Permanent Court of International Justice in the Chorzow Factory Case[39] (Merits) (1928) made it clear that it would be both erroneous and unjust if the financial results of lawful expropriation and unlawful dispossession were indistinguishable.

In connection with this distinction two important problems arise, the question of restitution and that of pecuniary compensation, each of which is closely related to one of these two kinds of measures. It has been widely held in the theory of international

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38. Ibid.

39. Bin Cheng, "The Rationale of Compensation for Expropriation," The Grotius Society: Transactions for the Year 1957 (London: Wildly and Sons Limited, 1962) Vol. XLIV, p. 290.

law that integral reparation (restitutio in integrum) is the principle mode of reparation for an internationally illegal act, pecuniary compensation being subsidiary in character, applicable when restitutio is not possible or not claimed.

The fullest exposition of the principle of integral reparation is to be found in the judgment of the Permanent Court of International Justice in the Chorzow Factory Case[40] (Merits) (1928):

"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 that reparation must, as far as possible, wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed. Restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear; the award, if need be, of damages for loss sustained which would not be covered by restitution in kind or payment in place of it - such are the principles which should serve to determine the amount of compensation due for an act contrary to international law."

Therefore, in case of unlawful expropriation, the first duty is not compensation, but "restitution in kind," whereas, in case of lawful expropriation, a state is not under a duty to

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40. Ibid., p. 291.

restitute the property expropriated. No problem of restitution arises in case of lawful exporpriation and pecuniary compensation should correspond to the value of the property exporpriated.

However, it is generally admitted that in practice restitutio in integnum is possible only in exceptional cases and that in the overwhelming majority of cases the responsibility of the state is discharged by the payment of pecuniary compensation.[41] This view is supported by the case law of international tribunals as well as by the prevailing diplomatic practice. The Permanent Court of International Justice in one of its judgments, has stated that "an indemnity corresponding to the damage which the nationals of the injured state have suffered . . . is . . . the most usual form of reparation."[42]

Therefore, there exists a contradiction between theory and practice. In reality, practice follows a pattern which is exactly the opposite of the one accepted in theory. In practice, compensation constitutes the principal remedy, restitution being clearly an exceptional one.

It is true that if this view is accepted, then a strong similarity appears to exist between the legal effects of lawful and unlawful measures of expropriations. In both cases, there arises on the part of the expropriating state an obligation to compensate the aliens involved. However, the difference in the

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41. A.A. Fatouros, Op. cit., p. 310.

42. Ibid., p. 311.

character of the measures in each case is reflected in the applicable measure of compensation. In practical, oversimplified terms, a state which unlawfully interferes with aliens' interests will probably have to pay more than otherwise.

2. Assessment of Compensation

The first step in the determination of the amount of compensation in any particular case is logically the assessment of the damages for which the compensation is to be paid. The difficulty in assessing damages here, is that international claims are usually presented in greatly exaggerated amounts. This is not strange, since it is a well known fact even in municipal law that a claimant seldom underestimates his claim. In the recent case of claims for compensation for properties of United States citizens nationalized in Yugoslavia, the claims originally submitted to the Foreign Claims Settlement Commission (a United States Government Agency) amounted to $ 148,472,773, out of which the Commission allowed only $18,817,904.89.[43] This is not an extreme or exceptional case. Therefore, some caution is needed when dealing with any particular claims.

Damages to property rights are usually classified in international law under the two broad headings of direct and

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43. Ibid., p. 316.

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indirect damages. Direct damages include all capital already invested by the alien, e.g., in factory plants, offices or machinery. They will also include any stocks of raw materials or goods taken along with the enterprise as well as other possible actual damages. Indirect damages include the intangible assets of the enterprise involved (such as goodwill) and the prospective profits of the investor had there been no interference with his interest. Which of these elements will be included in the compensation in any particular case depends on several factors, the most important of which is the lawful or unlawful character of the measures involved.

In case of losses resulting from lawful measures, compensation will probably include only direct damages, while, if the measures are unlawful, it may include prospective profits or other indirect damages.

In the municipal law of most states, the compensation to be paid in case of lawful taking of property is assessed on the basis of the market value of such property. This standard is also used in international law, when the property involved is such as to make the determination of its market value possible. But in many cases where a concession agreement is involved, this standard seems to be inappropriate. Since enterprises functioning by virtue of concession agreements, may often have no market value

because of their relative position and size within the host state's economy. The Anglo-Iranian Oil Company in Iran and the Suez Canal Company in Egypt are the most obvious examples of such enterprises.

A related method of assessment is that which bases the amount of compensation on the valuation of the properties involved by the investors themselves in their latest tax declaration. This method has been applied in the Mexican land expropriations and, most recently, it forms the proposed basis of assessment of compensation for the landholdings expropriated under the 1959 Cuban Agrarian Reform Law.[44] There is a strong support in favor of the proposed method. Since it prevents property owners who had managed or permitted under previous regimes, to declare a false value for their properties in order to pay lower taxes. They argue that foreign investors should be held to the same standards of good faith to which the host government is held .

Another possible method, particularly appropriate to enterprises of great size operating under concessions, is the assessment of the enterprise's value on the basis of the price of its shares of capital stock. This method has been adopted in many recent nationalizations, especially those effected within the Western World. Under appropriate conditions, this method is

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44. Ibid., pp. 318-319.

fair and practical, since shares of stock are of relatively small value and are numerous enough; they have a market, namely the Stock Exchange, and a market price, their quotation in it.

Since there is no single permanent price of shares but rather a series of successive prices, the question is which price will be selected as the one on which the calculation of the corporation's value will be based. The situation in the stock exchange at various times before the taking of the measures in question constitutes one of the variables which have to be taken into account. Such choice involves ideological and political rather than legal considerations. The Egyptian Law No. 235 of 1956 nationalizing the Suez Canal Company provided for compensation "in accordance with the value of the shares shown in the closing quotations of the Paris Stock Exchange" on the day preceding the nationalization.[45]

There exists in international law a dispute of long standing regarding the existence of an obligation to compensate for indirect damages. In one instance, the Permanent Court of International Justice in the Oscar Chinn Case[46] (1934) held that "the possession of customers and the possibility of making a profit" cannot be considered in the nature of a vested right of the owner of an enterprise.

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45. Martin Domke, "Foreign Nationalizations," The American Journal of International Law, Vol. LV. (July, 1961), p. 608.

46. Lord McNair, Op. cit., p. 17.

Wortley,[47] on the other hand, maintains that goodwill may be regarded as an acquired right and the direct abolition of which calls for compensation, like any other claim of property.

Admittedly, whatever the position one takes, the determination of the market value of an enterprise is influenced by so many elements that the question of goodwill will be of little practical significance for the calculation of compensation.

Another category of indirect damages which presents problems is that of prospective profits (lucrum cessans). When expropriation is lawful, compensation aims at the elimination of the alien's loss and not the restoration of the status quo ante. Accordingly, inclusion in it of payment for future profits is not indicated. The state, in such cases, pays to the extent of its own enrichment. Payment for profits lost, would be an addition to the alien's loss or the state's enrichment.

Furthermore, acceptance of the view that there exists an obligation to compensate for future profits would certainly lead to severe practical difficulties. For example, in the Anglo-Iranian Oil Company Case, the lost profits would amount to large sums, many times higher than the value of the original investments, the factory plants and any other concrete assets of the enterprise in question. In fact, allowance for future profits in all cases of general measures of radical character would render the cost of

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47. B.A. Wortley, Op. cit., p. 112.

such measures prohibitive to most states. Olmstead[48] maintains that the inclusion of lucrum cessans in the compensation for expropriated property "would serve as a useful deterrent to nationalization as there would be no financial gain to the state, and therefore less incentive to nationalize."

It is important to note here that the question of lucrum cessans should not arise except in the case of unlawful expropriation, since the state in such a case is bound to restore the exact status quo ante. However, recent practice tends to support the rule that, generally speaking, compensation for expropriation affected by general measures of a state should cover actual losses (damnum emergens) and not prospective profits.[49] Thus, in the course of negotiations leading to the agreement on compensation for the nationalization by Egypt of the Suez Canal Company, the representatives of the latter's shareholders abandoned their claim to compensation for the loss of revenue expected during the remaining years of the concession.[50]

3. Elements of "Just" Compensation

The qualities usually required for a just compensation are

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48. Cecil J. Olmstead, "Nationalization of Foreign Property Interests Particularly Those Subject to Agreements with the State," Selected Readings On Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Mathew Bender and Company, 1964), p. 232.

49. A.A. Fatouros, Op. cit., p. 324.

50. Ibid.

its adequacy, promptness, and effectiveness.

To be adequate, compensation should correspond fully to the value of the alien's interests affected by the state measure. Ordinary, the alien's actual loss will correspond to the state's gain, so that by calculating the former, the latter is also determined. In recent state practice compensation has seldom been adequate, that is, proportional with the full value of the expropriated assets. In most instances of nationalization, the compensation paid has been partial. This is mostly evident in the agreements between the states of Eastern and Central Europe and the Western countries. In the agreement concluded between the United States and Yugoslavia in July 1948, in pursuance of which 17 million dollars were paid in compensation for nationalized property, it was announced in the House Committee on Foreign Affairs that the settlement arrived at represented about 42.5% of the amount originally claimed.[51]

According to G. Schwarzenberger, the settlement arrived at in respect of British claims for compensation were as follows:[52]

Argentina (1948)	60%
Czechoslovakia (1949)	33 1/3%
	(official figures)

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51. Isi Foighel, Op. cit., p. 117.

52. Bin Cheng, Op. cit., p. 304.

France (1951)	70%
Mexico (1947)	30%
Poland (1948)	33 1/3%
Uruguay (1949)	60%
Yugoslavia (1949)	50%

(official figures)

The practice of partial compensation has found theoretical support in the writing of several jurists, though the majority of writers on the subject condemn it unreservedly. The main argument in support of this view is economic necessity, that is, the fact that, if full compensation had to be paid, the nationalization would have been impossible since the nationalizing state would have been led into bankruptcy.[53] Thus, Sir Hersch Lanterpacht, maintains that the financial capacity of the expropriating state limits the obligation to pay full compensation in the case of fundamental reforms. He argues pragmatically that full compensation could in effect mullify the proposed reform and sees justification for payment of less than full compensation. Similarly, Professor de La Pradelle[54] in 1951 proposed a project to the same effect, in support for partial compensation to be considered by the Institute of International Law.

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53. Loftus Becker, "Just Compensation in Expropriation Cases: Decline and Partial Recovery," U.S. Department of State Bulletin, Vol. XL (June 1, 1959), p. 786.

54. Ibid.

Opponents of partial compensation, on the other hand, point out that if a state cannot afford to nationalize, it should not do so. If a state is unable to pay for what it takes, then it has no legal or moral right to take from those who are not nationals of the state. Thus, Kissam and Leach in considering the question of full compensation, conclude that "poverty is no more an excuse for unjust enrichment in the case of a state than it is in the case of an individual."[55]

Similarly, Becker,[56] in condemning the practice of partial compensation, asserts that "partial compensation is a compromise with principle."

It has been said once that nationalization of foreign property against inadequate compnesation may be regarded as a "type of imperialism in reverse."[57]

Finally, Lord McNair,[58] puts it rather as a statement of fact "I am aware of no juridical or arbitral authority whatever for the view that a State is entitled to nationalize the property of foreigners on the condition of paying only partial compensation."

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55. Leo T. Kissam and Edmond K. Leach, Op. cit., p. 189.

56. Loftus Becker, Op. cit., p. 791.

57. Kenneth S. Carlston, "Concession Agreements and Nationalization," The American Journal of International Law, Vol. LIII (April, 1959), p. 275.

58. Lord McNair, Op. cit., p. 297.

Lamp-sum agreements are the characterstics of the national-ization measures taken after the Second World War by various countries of Eastern and Western Europe. Under these agreements the nationalizing state and the state of the nationality of the aliens affected by the measure agree on a lump-sum compensation as indemnification for all the property nationalized, without regard to its real value.[59] Foighel, in his survey of forms of compensation, shows that by far the great majority of recent compensation agreements have provided for global compensation. This form of compensation despite the fact that the compensation paid seldom amounts to 100% of the amount claimed, has several advantages. First, the fixing of the amount of compensation at an amount of the sum claimed is less complicated for all parties. Secondly, because of the simpler procedure, the amount of the compensation can be decided relatively quickly, which is nearly always an advantage to the claimants. Thirdly, the problem of individual doubtful claims can be solved by regulating the lump-sum compensation upward or downward, without the legal problems involved by the doubtful claims needing to be investigated in detail and perhaps cause conflict as between the two parties. Finally, these agreements have the effect of discharging claims.[60] Thus, the Danish-Polish Protocol of 26 February 1953, contains the following provision: "On completion of the payment of the sum of 5,700,00 Danish Kroner, the Danish Government will consider

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59. Isi Foighel, Op. cit., p. 133.

60. Ibid., p. 99.

all the Danish claims, enumerated in Article 1, as definitively settled. This settlement has the effect of discharging the Polish Government, in respect of Danish interested parties and their claims, from all liability."

There is indeed a recognition that agreements in which less than full compensation has been accepted, are based on political and economic reasons. Typical examples are the World-War-II Peace Treaties of February 10, 1947, which provided for a rate of compensation for loss, suffered as a result of war, of Allied property in the amount of two thirds of the sum necessary to make good the loss: "The delegates of the Great Powers at the Peace Conference all insisted most emphatically that, as a matter of legal principle, full compensation ought to be paid and that their departure from that principle was due to political and economic considerations only."[61] The Great Powers, therefore, exercised a liberty of accepting a lump-sum settlement of less than 100%; they were not legally bound to do so.

The United Kingdom in the Economic Commission for Italy declared: "Insofar as the United Kingdom Delegation took part in the voting of any of the proposals of partial compensation, this was without prejudice to the United Kingdom's own principle of full compensation, to which she still adheres, and to which she attaches the greatest importance."[62]

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61. Martin Domke, Op. cit., p. 609.

62. Ibid.

Therefore, the international political settlement for less than full compensation were not legal precedents that prejudice the international law rule requiring payment of full compensation. They were primarily a product of the political rather than the legal process.

Beneficial as nationalization may ultimately prove to a state and its citizens, there is little to justify placing the burden of a state's economic experimentation upon the shoulders of the foreign investor, who has neither any voice in the decision to indulge in such experimentation nor any status to enjoy whatever benefits may ultimately derived therefrom. Rightly, it was once stated by Justice Holmes: "In general, it is not plain that a man's misfortune or necessities will justify shifting the damages to his neighbor's shoulders."[63] Financial difficulties offer no justification for the repudiation of obligations, either by individuals or by nations.

The two other attributes of just compensation need not be considered at a great length as the first one. In order to be prompt, compensation must be paid either before the taking or within a short time thereafter. Payments may be further delayed if an appropriate rate of interest is determined, so that the claimant will not suffer any additional loss through delay. In most recent instances of general measures affecting alien's rights, the payment

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63. Kenneth S. Carlston, Op. cit.

of the compensation provided was spread over a number of years. Thus, the 1948 agreement between France and Poland provided for payment by the latter, in compensation for the nationalized properties of French nationals, over a period of fifteen years, while the agreement between Switzerland and Poland provided for thirteen years.[64] In some of the compensation agreements, it has been agreed that the compensation shall be paid in a fairly large amount cash and the remainder spread over a number of years. This is the case in the agreement between Switzerland and Roumania of Agust 1951, Switzerland and Bulgaria of November 1954 and Norway and Bulgaria of December 1955.[65]

This principle of payment by instalments seems to be generally accepted, with respect of lawful nationalization.

The term effectiveness usually refers to the precise form of the indemnity, and especially to the possibility of its immediate utilization by the alien. Although a wide variety of forms of payment are contemplated in the compensation agreements, payment is generally affected through the use of frozen assets of expropriating state in the other state or through the delivery of specified raw materials or other goods. An example of payment in kind is furnished by the agreement between Poland and France of May 1948, which provided for the delivery of specified quantities of coal over a number of years.[66] An example of the first form of

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64. A.A. Fatouros, Op. cit., p. 331.

65. Isi Foighel, Op. cit., p. 121.

66. Gillian White, Op. cit., p. 205.

payment is offered by the agreement between Switzerland and Roumania of 1951, under which about 50% of the agreed compensation was to be paid from Roumanian funds frozen in Swiss banks.[67]

In the Swiss-Hungarian agreement of 1950, on the other hand, it was stipulated that part of the compensation would be paid in the legal currency of the expropriating state.[68]

In the very recent compensation agreement between the United Arab Republic and the Republic of Lebanon of November 1964,[69] it was held that 30% of the annual instalment due to the Lebanese nationals, should be paid in cash; 50% for tourism and other services to be spent in the United Arab Republic (excluding the taxes and charges due for using the Suez Canal); and 20% for exportation of Egyptian products and goods (excluding the exportation of oil, cotton and rice).

There is a very close relationship between the three requirements here discussed. In most cases, the states and aliens involved have to choose between alternative forms and amount of compensation. The value of each one of them depends on the surrounding conditions and circumstances. Thus, for example, when the debtor state is under a socialist regime, effectiveness becomes the ruling consideration, since there are no other investment opportunities in that state to absorb the capital to the alien. Prospects of government instability may increase the value of promptness, while in a capitalist regime of relative economic stability, it is the amount of compensation that becomes all important.

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67. Ibid., p. 215.

68. Isi Foighel, Op. cit., p. 126.

69. Al-Yom (Beirut), December 1, 1964.

CHAPTER V

Settlement of Investment Disputes

A. Remedies Available to Investors Against Foreign States

In this section, we are concerned with remedies, not with the substantive question of what constitutes a wrong by a government to a foreign private investor. The crucial question here, is when the investor asks himself or his lawyer, "Now that the government has taken over my waxworks, what will I do?"

The sovereign character of a state does not in principle relieve it from responsibility to other states or to the international community for actions affecting other states or their nationals. Its sovereign character may raise certain obstacles to the redress of a wrong. But a wrong is not made right by the single fact that it was done in the exercise of a sovereign power. Whenever there is a wrong, there should be a remedy.

1. Remedies Under the Municipal Law

It is a recognized rule of international law that a state may not take up or claim on behalf of its national against a foreign state, unless he has exhausted the local remedies available to him under the municipal law of the foreign state. The chief reason for this rule is the public interest of the state in avoiding international friction over any issue that can be disposed of

otherwise. In most cases of nationalization, however, this rule will not come into operation since the injury to the alien is caused by the application of the local law which is binding on the local courts. These courts are unable to give a remedy for an act which is not wrongful according to the law which they administer. Thus, when addressing the Council of the League of Nations in connection with the cancellation by the Persian Government of the Anglo-Persian Company's 1901 Concession, the United Kingdom representative said that since the cancellation had been ratified by the Persian Parliament resort to the local courts would have been in vain, as they had no jurisdiction to grant a remedy to the Company.[1]

A course of action, which is not strictly a remedy for the private claimant but which on occasion has been resorted to in order to bring pressure on the foreign state, is the freezing by executive action of the foreign state's assets in the home state. This was done, for example by Britain, France and the United States with respect to Egyptian funds within their jursidiction after the Egyptian nationalization of the Suez Canal Company in 1956.[2]

Frequently, a private investor and a foreign state agree on a particular means of settling any dispute that may arise between

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1. Gillian White, Nationalization of Foreign Property (London: Stevens and Sons Limited, 1961), p. 258.

2. Richard Young, "Remedies of Private Claimants Against Foreign States," Selected Readings on Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Matthew Bender & [illegible] 1964), p. 915.

them, usually by way of an ad hoc arbitration proceeding. Provisions to that end are often incorporated in the principal agreement between the parties. For example, Article 22 (A) of the Concession Agreement of April 29, 1933 between the Persian government and the Anglo-Persian Oil Company Ltd., stipulates that "Any difference between the parties of any nature whatever and in particular any differences arising out of the interpretation of this Agreement and of the rights and obligation therein contained as well as any differences of opinion which may arise relative to questions for the settlement of which, by the terms of this Agreement, the agreement of both parties is necessary, shall be settled by arbitration."

When such provisions exist, they replace the ordinary requirement of resort to local remedies unless the agreement itself affirms otherwise. Thus, if a private investor complaining about an alleged wrong seeks and fails to obtain the arbitration proceeding called for in his agreement, he is under no obligation to exhaust the local remedies. He is free, rather, to pursue the recourses open to him under international law. This was the position of the United Kingdom government in the Anglo-Iranian Oil Company Case before the International Court of Justice in 1951-1952.

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3. Alan W. Ford, The Anglo-Iranian Oil Dispute of 1951-1952 (Berkeley: University of California Press, 1954), p. 244.

2. Remedies on the International Level

Let us assume that none of the above remedies is available and that there is nothing more for the private investor to pursue or to arrange for himself. He, then, seeks the aid of his own government, asking it to take up his claim against the foreign state, through diplomatic channels. Here he finds his first task is to persuade his own government to undertake the job.

In order to pursuade his own government, the private investor finds himself in a difficulty. It is not enough for the foreign office of the private investor to be satisfied that the claim of wrong is prima facie sound, that local remedies are exhausted or non-existent, or that efforts at arbitration or other settlement have failed - although all of these points are essential. The foreign office also has the right and duty, before officially taking up a claim to consider what its impact might be on the relation between the two states or on foreign policy generally. If the relations with a foreign state are good, the foreign office is reluctant to press an unpleasant claim for fear of spoiling them; while if the relations are bad, it is reluctant to spend time and effort on a futile mission. Therefore, the determination to espouse a claim against a foreign state becomes an act of national policy. The private investor may thus lose his best chance for redress.

But let us assume that the home state of the private investor agrees to espouse his claim officially. Henceforth, the issue lies between two sovereign and equal states, whose relations with each other are governed by international law. The private claim, therefore, is transformed into a public claim - the claim of the home state of the private investor: "By taking up the case of one of its subjects and by resorting to diplomatic action or international judicial proceedings on his behalf, a State is in reality asserting its own rights - its right to ensure, in the person of its subjects, respect for the rules of international law."[4]

Important consequences flow from this transfer of a claim to the interstate level, some advantageous to the private investor and some disadvantageous. On the advantageous side, the espousal by the home state opens possible remedies under international law, which the private investor could not pursue directly. Moreover, the foreign state may find that the home state has arguments, legal and extra-legal, which were not available to the private investor and which the foreign state can not afford to ignore.

On the disadvantageous side, the major disadvantage to the private investor is that he loses control when his claim is transformed into a state claim. The home state will have exclusive control over the claim. The method of settlement, the arguments

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4. Richard Young, Op. cit., p. 920.

to be used, the relief to be sought, are for the state to determine. At its discretion the home state may abandon or compromise the claim, while the private investor must accept any settlement obtained by it.

Despite all the home state's persuations, diplomatic intervention may fail to produce either a settlement or an agreed recourse to judicial or arbitral proceedings. In such cases, one possibility may be recourse to the United Nations Security Council or General Assembly. Other possibilities are to seek the good offices or mediation of a third state or of an international official or organization.

International Judicial Recourses

The judicial or quasi-judicial institutions of public international law fall into four general classes: International Court of Justice, Permanent Court of Arbitration, ad hoc arbitral tribunals, and international claims commissions. Generally, two prerequisites should be satisfied if these bodies are to assume jurisdiction over a claim of private origin. First, the claim should be raised to the interstate level through espousal by the home state, since under existing rules of international law only states (or public international organizations) can be parties in such proceedings. Second, the foreign state which is the potential defendant, should in some way consent to the jurisdiction;

for without some such consent it cannot be sued as a sovereign state. This consequence of the doctrine of sovereignty places a procedural obstacle in the way of international judicial settlement.

By far the most important international judicial institution is the International Court of Justice at the Hague, established under the United Nations Charter as the principal judicial organ of the United Nations. Disputes are referred to the Court by the parties concerned in three different ways: (1) if the parties agree to submit a dispute to the Court; (2) if both parties have agreed to the "compulsory jurisdiction" provision of the Court's Statute and one of them refers the dispute to the Court; (3) if both parties have concluded a treaty which makes provision for utilizing the Court to resolve different interpretations of a treaty and one party submits the problem to the Court.

The Permanent Court of Arbitration established under the Hague Conventions of 1899 and 1907, is in fact neither a court nor a permanent institution. It is actually a panel of arbitrators who may be called to act as an arbitral tribunal. It has no regular sessions, and it meets only when a dispute arises and some of its members are selected to adjudicate it.

A tribunal of the Permanent Court of Arbitration stricto sensu should be constituted from the panel. But under the

Conventions the Bureau is authorized to place its services at the disposal of "special boards of arbitrators," which may have been constituted outside the panel. There is nothing in the Hague Conventions which says that these boards should be concerned only with interstate disputes.[5]

In February 1962, the Bureau of the Permanent Court of Arbitration established new rules for organizing in the future arbitration proceedings between states and public international bodies on the one hand, and companies or individuals on the other.[6] The prospect thus opened, offers possibilities which may be worth considering when questions of arbitration proceedings between a state and a private investor arise. The use of the Permanent Court's facilities would make available suitable premises, an excellent library, a suitable atmosphere for peaceful settlement and a trained administrative staff to handle details of an arbitration - details which are often difficult to provide on an ad hoc basis.

Recourse to the Permanent Court of Arbitration is one means of organizing an international arbitration. In general, states may arrange any arbitration they see fit. For the many states

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5. Ibid., p. 932.

6. "The 1962 Rules of Arbitration and Conciliation for the Settlement of International Disputes Between Two Parties of which Only One is a State," Arbitrale Rechtspraak, No. 497 (May, 1962), pp. 135-143.

not parties to the Hague Conventions, the establishment of ad hoc tribunals outside the framework of the Permanent Court would be the normal approach to arbitration, not the exception. In some cases, a treaty may exist between the foreign state and the home state, which provides for submission to arbitration of disputes arising between them.

Whatever the arrangement under which an arbitral proceeding is instituted, its methods of procedure are likely to conform in broad outline to practice previously worked out. For a long period the chief influence on such practice was the rules of procedures laid down in the 1907 Hague Convention. Recently, however, the United Nations International Law Commission has studied the subject, which resulted in 1958 in a set of model rules of arbitral procedure.[7]

A special form of arbitral tribunal is the international claims commission, to which resort is sometimes had when a substantial number of unsettled claims accumulate between states. These international claims commissions should be distinguished from domestic claims commissions set up under municipal legislation. In the latter situation, the international liability of the foreign state to the home state has already been settled by agreement or other means, often in the form of a lump-sum payment.

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7. United Nations, Yearbook of the International Law Commission 1958, Vol. II (A/CN.4/SER.A/1958/ADD.1) (New York, 1958), p. 83.

The home state may then establish a purely domestic commission, as one of its own agencies, to receive and pass upon claims against that foreign state. The claims allowed are then paid from the lump-sum received by the home state.

The merits and demerits of international claims commissions were briefly evaluated by Judge Hudson in these terms: "The jurisprudence of claims tribunals holds an important place in history of international law. It has supplied many precedents to serve as guides for the future, but it has not developed a consistent body of case-law. Instruments creating the tribunals have varied widely in their provisions, and even tribunals created on parallel lines have not followed a uniform procedure. Difficulties have often arisen in their functioning, extraordinary delays have been frequent, and the personnel of tribunals has sometimes proved to be unsatisfactory. Recriminations have resulted in some instances, and they have tended to jeopardize confidence in the method."[8]

From this statement it can be seen that practical drawbacks have resulted from these claims commissions. Yet a claims commission is far better than no means of redress and many private claimants have welcomed their establishment.

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8. Richard Young, Op. cit., p. 934.

The Problem of Enforcement

Compliance with the judgment or award by the tribunal is the last great problem in the achievement of justice in an international proceeding. In the absence of voluntary acceptance, the means afforded by international law to secure obedience by a state to an international judicial or arbitral decision are limited. International tribunals have no police to call and no process to issue. Undoubtedly, this is a great weakness of international law, and unless states give up some of their sovereignty, one cannot be optimistic about an early improvement.

Regarding judgments rendered by the International Court of Justice, Article 94 of the United Nations Charter provides that each member shall comply with the decision of the Court in any case which the member is a party. It further provides that, if any party to a case fails to perform the obligations incumbent upon it under a judgment of the Court, the other party may have recourse to the Security Council. The Council, then may, if it deems necessary, make recommendations or decide measures for giving effect to the judgment. Just what the Security Council could do in such an event is not clear. In any case, viewing the problem as a whole, the action or non-action of the Council under Article 94 will be governed largely by political considerations. However, it seems unlikely that a state will refuse to abide by a decision of the Court, if the past practice of states is any

indication for the future. In reality, the crucial question is not one of a state abiding by a judgment, but of getting states to submit cases to an international court.

B. State Guarantees and Settlement of Disputes

An important problem arising in connection with state guarantees to foreign investors is that of the machinery for the settlement of related disputes. Provisions concerning such machinery are highly important because they determine in part the concrete effect of such guarantees. The importance of this factor has been recognized by the drafters of the recently proposed investment codes as well as by the states which have concluded bilateral treaties dealing with investment.

Both the ITO Charter and the Bogota Economic Agreement stressed the role of diplomatic rather than strictly judicial methods. The former instrument provided for consultation between governments within or outside the Organization, for discussions of the issues in various organs of the Organization and for eventual arbitration, provided the states concerned agreed to it (Arts. 92-97). The Bogota Agreement, in addition to provisions on consultation between governments concerned, also referred to the possibility of submission of the dispute to the Council of the Organization of American States (Art. 38).

Some of the other proposals go so far as to suggest the creation of a special judicial body, which would have jurisdiction to deal with any dispute arising in connection with foreign investments. The ICC Code of Fair Treatment provided for the creation of an International Court of Arbitration to which any differences which might arise between the states party to the proposed code and which were not settled "within a short and reasonable period by direct negotiations or by any other form of conciliation" were to be referred (Art. 13). The determination of the details of the working and composition of this court were left to the negotiating governments (Art. 14).

Some of the arguments for the creation of a special judicial body are stated in the report of the British Parliamentary Group for World Government (Paras. 68-77). The report admits that it would be simpler to refer all related disputes to one of the already existing bodies, such as the International Court of Justice. It points out, however, that in such a case and in view of the statutes of these bodies, no individual investor would be allowed to bring his case before the court. The report considers this limitation inadvisable insofar as investment disputes are concerned. The creation of a new judicial body is therefore proposed, which would specialize in the problems of international investment. Its permanent seat would be in one of the under-developed countries, and it might even hold sessions in several countries.

The 1957 Draft Convention of the German Society to Advance the Protection of Foreign Investments provided for the creation of an International Court to deal with the legal disputes arising over the application of the convention (Art. X(1)). The court was to be a permanent one, composed of members appointed by the states party to the convention for a specific period of time. The court was to determine the unlawful character of measures in contravention of the convention and could apply a number of sanctions (Art. XI). The convention also provided for the creation of Arbitration Committees to decide problems of compensation arising under the terms of the convention (Art. X(2)). These Committees would be a special ad hoc bodies competent to deal with the economic matters arising in connection with expropriations and other measures.

The 1959 Draft Convention on Investments Abroad provides for the establishment of an Arbitral Tribunal for the settlement of disputes arising from the interpretation or application of the Convention. In an Annex to the Convention a detailed procedure is set out for the formation of a special arbitral tribunal to deal with each particular dispute. If the parties to a dispute do not agree to submit it to arbitration, the dispute may be brought to the International Court of Justice (Art. VII(1)).

It is to be noted that most of the recent proposals provide for the possibility of recourse of private parties to the court

or arbitration tribunal to be established. This need was emphasized in the 1957 Draft Convention, which provided that private individuals as well as states would be entitled to the rights under the Convention (Art. IX(2)). In the accompanying commentary, it was stated that "this individualization of rights under the Convention will do much to strengthen private responsibility." It would also eliminate the individual's dependence upon the espousal of his claim by the state of his nationality which might refuse to do so for political reasons. These provisions were included in a modified form in the 1959 Draft Convention (Art. VII (2)). The right of individuals to have recourse to the arbitral tribunals to be instituted under the convention, were made contingent upon an "optional clause." Any state party to the convention may file a declaration to the effect that it accepts the tribunal's jurisdiction in respect of claims made by nationals of one or more of the parties.

The bilateral investment treaties did not contain any provision regarding the access of private persons to international jurisdictions. However, some of them dealt with the enforcement of arbitration agreements between private parties. Enforcement cannot be denied merely because the award was rendered in a country other than where the execution is being sought, or that the nationality of the arbitrator was not that of the party concerned.

For example, Article V of the United States FCN treaty with Netherlands provides that "Contracts entered into between nationals or companies of either Party and nationals or companies of the other Party, that provides for the settlement by arbitration of controversies, shall not be deemed unenforceable within the territories of such other Party merely on the grounds that the place designated for the arbitration proceedings is outside such territories or that the nationality of one or more of the arbitrators is not that of such other Party.[9]

Most of the investment treaties provide for the settlement of disputes which may arise between the parties concerning the treaties' application or interpretation. The United States FCN treaties give precedence to consultation between governments, as the first step toward any settlement. Recourse may be to the International Court of Justice, if all other means of settlement are unsuccessful. Thus, Article 15 of the FCN treaty with Netherlands provides that "Any dispute between the Parties as to the interpretation or application of the present Treaty, not satisfactory adjusted by diplomacy shall be submitted to the International Court of Justice, unless the Parties agree to settlement by other pacific means."[10]

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9. U.S., Treaties and Other International Agreements, Vol. VIII, Part 2, p. 2049.

10. Ibid., p. 2083.

The relevant provision of the treaty between Switzerland and Senegal of August 1962,[11] follows almost identical lines.

Similarly the recent agreement between Algeria and France of June 1963,[12] provides for the settlement of disputes by means of arbitration in all matters concerning the exploitation of the saharan subsoil. The agreement provides in detail for the constitution and procedure of the arbitration tribunal.

The agreements concluded by the United States concerning the application of the investment guarantee program also provide for a procedure for the settlement of disputes which might arise after the subrogation of the United States to an investor's rights. If direct negotiations between the two governments fail to bring about a settlement, the dispute is to be brought to arbitration before a single arbitrator named by agreement of the parties. If such agreement is not reached within three months, the arbitrator "shall be one who may be designated by the President of the Permanent Court of Justice at the request of either Government."[13]

Most investment laws do not contain detailed provisions on the settlement of disputes. But there are some exceptions.

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11. The American Society of International Law, International Legal Materials, Vol. II (January, 1963), p. 148.

12. The American Society of International Law, Op. cit., Vol. II (November, 1963), p. 1025.

13. Richard Young, Op. cit., p. 948.

For example, the Greek investment law[14] of October 22, 1953, provides for the settlement by arbitration of disputes arising between the Greek government and the foreign investors over the interpretation and application of the instrument of approval issued by virtue of this law. Provisions on arbitration are also found in some countries in their legislation concerning the development of petroleum resources. In India, for instance, under the Petroleum Concession Rules,[15] disputes between the Government and the licencee regarding the licence, the royalties, any alleged breaches or the amount of compensation to be paid upon acquisition of the concession, are to be submitted to arbitration.

Although not very common in investment laws, provisions on arbitration are frequently included in agreements between states and foreign individuals or companies. For example, the concession agreement between Qatar and the Shell Overseas Exploration Company, Ltd.[16] of November 29, 1952, provides that "If any doubt or dispute shall arise between the Sheikh and the Company concerning the rights or liabilities of either party, and if the two parties fail to settle it in any other way, the matter shall be referred to two arbitrators."

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14. A.A. Fatouros, Government Guarantees to Foreign Investors (New York: Columbia University Press, 1962), p. 186.

15. Ibid.

16. Alfred Verdross, "The Status of Foreign Private Interests Stemming from Economic Development Agreements with Arbitration Clauses," Selected Readings on Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Matthew Bender and Company, 1964), p. 126.

Some concession agreements describe in detail the procedure to be followed in case of dispute. The 1954 Agreement between Iran and the Consortium[17] of oil companies, contains detailed procedures to be followed in case of dispute (Art. 44). This agreement provides for initial attempts at conciliation through consultation between the parties or other friendly methods of settlement. When such methods fail, a Mixed Conciliation Commission is to be established. Procedures of arbitration are also provided. In this connection, the agreement distinguishes the disputes which relate to technical matters from those of more importance. In the former case, the parties may request the help of the two Swiss institutions in appointing experts to decide the issues. In the case of disputes of a general character, a more elaborate procedure is to be followed. The parties will first appoint an equal number of arbitrators each. If one of the parties fails to appoint its arbitrators, or if the arbitrators cannot agree on the appointment of an umpire, the arbitrators or the umpire will be appointed by the President of the International Court of Justice. If the President refuses, or is unable to make the appointment, the request should be addressed successively to the International Court's Vice-President, the President of the

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17. J.C. Hurewitz, Diplomacy in the Near and Middle East (Princeton: D. Van Nostrand Company, Inc., 1956), Vol. II, pp. 374-377.

Swiss Federal Tribunal, and the Presidents of the highest courts of Denmark, Sweden, and Brazil, in that order.

C. International Commercial Arbitration

With the expansion of international trade and investment in recent years, the business world has been increasingly reluctant to litigate in courts of law differences arising from international commercial transactions. Businessmen are evidently reaching the conclusion that the present legal procedures are unsuited to the solution of commercial disputes. It is not surprising, therefore, that they have been turning with increasing frequency to arbitration as a quicker and simpler means of settling international commercial disputes. Among the factors which have contributed most to the attraction of arbitration for international business circles, the first is certainly the speed and relatively low cost of its proceedings. Another factor, is the care which arbitrators take to avoid any kind of publicity for the disputes which have led the parties to have recourse to it, or for the discussions which precede and pave the way for arbitral awards. Moreover, arbitration provides a satisfactory means for parties domiciled in different countries, and therefore subject to different systems of law, to find an equitable way of settling differences which may arise between them. Reference of disputes to national courts as has

been shown, is possible, but traders and companies are not willing to carry on litigation before foreign courts whose procedure is entirely strange. In addition, each branch of international trade has its own particular usages, on the interpretation of which an arbitrator expert in the field is often better fitted to decide than a judge who, however, widely qualified, may lack the necessary specialized knowledge.

Therefore, businessmen have recognized that reliable facilities for arbitration are essential elements in the organization of international commerce. It is for this reason that a noticeable movement in favor of arbitration has occurred and arbitration facilities and institutions have increased. Parties to a commercial dispute, no longer give their exclusive confidence to arbitrators chosen by themselves, but to permanent and well-equipped arbitration centers, offering arbitration tribunals whose rules of procedures, composition, qualification and objectivity provide the guarantee wished by their users.

1. Arbitration Centers

Arbitration facilities for any commercial disputes are provided in about 40 countries by chambers of commerce and national and international arbitral bodies.[18] Some private organizations, such as the International Chamber of Commerce, the American Arbitration

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18. Paolo Contini, "International Commercial Arbitration," The American Journal of Comparative Law, Vol.VIII, (Summer, 1959), p. 284.

Association, the Inter-American Commercial Arbitration Commission the Comité Français de L'Arbitrage, and the Netherlands Arbitration Institute, have actively promoted the advancement of arbitration. Moreover, the literature on the subject of arbitration, has significantly become quite extensive. Two current periodicals, the Arbitration Journal published by the American Arbitration Association, and the Revue de L'Arbitrage published by the Comité Français de L'Arbitrage, are devoted exclusively to arbitration.

These private arbitration centers, comprise a body of independent experts, not under the control of any government or any private interests, their function being to appoint neutral arbitrators where the parties fail to do so themselves and to review awards impartially in order to correct obvious errors.

In order to understand and assess the effectiveness of such arbitration centers, it is essential to give a brief survey on one of them.

The International Chamber of Commerce (ICC) is one of these centers which are active in the field of international commercial arbitration. It was founded in 1923 with headquarters in Paris, for the purpose of improving international economic relations. It has a Court of Arbitration, which exists to arrange for the settling by an arbitrator or arbitrators of disputes submitted

to it - usually a result of the parties to an international contract stipulating the settlement under ICC rules of any disputes which may arise between them. The Court of Arbitration offers its facilities both to disputes between private firms and between states and private firms.

The general and universal nature of the ICC arbitration gives it certain important aspects which become evident from a brief description of its activities resulting from an analysis of a series of 300 recent cases. The following are some of the important results:[19]

A breakdown of the parties to a dispute according to nationality will show:

- 22 European countries have produced 253 plaintiffs and 246 defendants.

- The American continent has produced 26 plaintiffs and 33 defendants.

- The participation of Asia and Africa is identical, being 18 plaintiffs and 13 defendatns on the one hand, and 15 plaintiffs and 12 defendants, on the other.

- Finally, Australia has produced 2 plaintiffs and 2 defendants.

Besides being universal in the geographical sense, the ICC arbitration also covers a wide range of professions and occupations

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19. International Chamber of Commerce, Guide to ICC Arbitration (Paris: L'Edition Artistique, February 1963), pp. 9-14.

not only among the parties who use it but also among the arbitrators and conciliators. The following is a breakdown according to their nationality:

Europe has supplied 113 conciliators and 146 arbitrators; America, 6 conciliators and 6 arbitrators; Asia and Africa have supplied 2 conciliators and 3 arbitrators.

With regard to the professions of the arbitrators, the legal nature of international arbitration leads to a predominance of personalities drawn from the legal professions.

The nature of the disputes submitted to ICC arbitration covers a wide variety of every branch of international trade and investment. Of the 300 cases submitted to the ICC arbitration, about 4% are disputes between state and individuals, involving differences of varied nature.

Finally, with regard to the costs of proceedings, the ICC has a schedule in which the cost of conciliation and arbitration may be assessed in each individual case by the parties concerned. The following are two examples:

- With regard to conciliation, for a sum in dispute of approximately US$ 100,000 the schedule provides for a minimum of 0.3% and a maximum of 0.7%.

- With regard to arbitration, for the same sum in dispute the minimum and maximum rates in the schedule are 0.8% and 2% respectively.

2. The United Nations Conference on International Commercial Arbitration

The subject of international commercial arbitration, has reached the various United Nations bodies and several measures have been taken to encourage its use in international commercial transactions. The Economic and Social Council and the Regional Economic Commissions for Europe and for Asia and the Far East, have adopted resolutions for the encouragement of arbitration in international transactions.

On April 17, 1959, the Economic and Social Council[20] adopted resolution 708 (XXVII) which proposed ways in which interested governments and organizations might make practical contributions toward the more effective use of arbitration in the settlement of international commercial disputes. Emphasis was placed upon the importance of educational activities, particularly in promoting among members of the business community knowledge about arbitration facilities, and encouraging the inclusion of arbitration clauses in contracts. Governments were asked to consider improving their arbitral legislation and institutions and, where appropriate to develop new arbitration facilities. The Secretariat of the United Nations was requested to assist governments and private organizations in their efforts to improve arbitral legislation, practice and institutions, principally by helping them to obtain technical advice and by providing guidance in coordinating their progress

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20. United Nations, Secretary-General, Annual Report on the Work of the Organization for 1958-1959, p. 97.

and promoting arbitration in international trade and investment.

One aspect of international arbitration - the enforcement of arbitral awards rendered in a country other than that of the debtor's state, has always presented a great problem in the practice of international commercial arbitration. A foreign party which does not voluntarily comply with the arbitrator's determination may oppose or delay enforcement procedures and challenge the binding effect of the arbitration agreement, the arbitrability of issues submitted to the arbitrator, or the compliance of the award with the law applicable to the arbitration. It is for that reason that a uniform basis for enforcement of awards has been sought, a movement of decisive importance to the development of international commercial arbitration.

The Geneva Protocol on Arbitration Clauses of September 23, 1923 and the Geneva Convention on the Execution of Foreign Arbitral Awards of 1927 adopted under the auspices of the League of Nations, were the outstanding pre-war multilateral conventions on international commercial arbitration.[21]

This movement for the uniformity for the enforcement of foreign awards, has been revived by the "Convention on the Recognition and Enforcement of Foreign Arbitral Awards,"[22] which

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21. Paolo Contini, Op. cit., p. 286.

22. United Nations, Economic and Social Council, Convention on the Recognition and Enforcement of Foreign Arbitral Awards (E/CONF.26/8/Rev.1) (New York, 1958), p. 1.

was adopted by the United Nations Conference on International Commercial Arbitration in New York on June 10, 1958. The Conference resulted from a proposal by the International Chamber of Commerce to the Economic and Social Council to conclude a convention on enforcement of foreign arbitral awards, and was represented by 45 states and many inter-governmental and non-governmental organizations.

The Convention was designated to facilitate the carrying out of arbitral awards made in the territory or under the laws of a state other than the state in which recognition and enforcement of such awards are sought. It provides for the recognition of the validity of arbitral agreements and for simplification of the conditions for obtaining recognition and enforcement of an award in a foreign country.

Under the Convention, the enforcement of an arbitral award is made simply by filing in court the arbitration agreement and the award, whereupon enforcement follows unless the defendant establishes any one of five specified challenges, i.e, absence of a valid arbitration agreement, lack of a fair opportunity to be heard, an award in excess of the submission, improper arbitral procedure, or lack of finality of the award in the rendering state (Arts. IV and V). Therefore, if it can be shown that the award has not become "binding" in the country in which it was rendered,

then enforcement may be refused. But the burden of proof that it has not become binding, is thrown into the party seeking to resist enforcement, so that his chances to delay enforcement are reduced to a minimum. However, the court may on its own motion deny enforcement on only two specified grounds, i.e., that the subject matter is not arbitrable under the local law of the country in question, or that enforcement would violate the public policy of the state involved (Art. V(2)).

A significant feature of the new Convention, is that it may be applicable to the enforcement of foreign arbitral awards arising out of contracts between an individual and a foreign government. It contains no express provision on this point, but its scope extends to awards arising out of differences "between persons, whether physical or legal." (Art. 1)

Finally, there is no doubt that the acceptance of the new Convention by many states will facilitate the task of international commercial arbitration, by providing businessmen with an assurance of prompt enforcement of their contractual rights, an essential element of all business transactions. Rightly, it was once stated that "the encouragement of foreign trade and investment must involve the encouragement of enforcement measures. Law may not depend for its existence upon remedy, but a system without means of enforcing awards is basically deficient."[23]

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23. George W. Haight, "American Foreign Trade and Investment Disputes," Selected Readings on Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Matthew Bender and Company, 1964), p. 900.

D. <u>The Draft Convention on the Settlement of Investment Disputes of the World Bank</u>

The question of private foreign investments and the various state guarantees have attracted the attention of the World Bank. This is not only because some of them contemplated that any program established would in some way be associated with the Bank, but also because their primary purpose, the encouragement of an increased flow of private capital to less developed countries, is one of the Bank's own basic objectives. Moreover, the position of the Bank, its reputation for integrity and impartiality, are trusted to a considerable extent by the governments of both the capital-exporting as well as the capital-importing countries. These led many governments and foreign investors to appeal to the Bank to assist them in settling investment disputes that had arisen between them, or wanted to assure themselves that the Bank's assistance would be available in the event that differences between them should arise in the future. The function assigned to the World Bank in the agreement concerning compensation for the nationalization of the Suez Canal Company is an illustration of such possibilities. The World Bank gave considerable assistance during the negotiations leading to the agreement in question and it was itself a party to the agreement, though for limited purposes. It was stipulated that the Bank would act "as fiscal agent for

the purpose of the payments to be made," pursuant to the Agreement. It was further provided that "In case of any disagreement between the Parties concerning the interpretation or implementation of this Agreement, the Parties will request I.B.R.D. to use its good offices to assist them in composing their differences."

More recently, Ghana have enacted a legislation concerning foreign investment which contemplated the settlement of certain investment disputes "through the agency of" the World Bank.[25]

On the basis of the above mentioned proposals, the Bank have reached the conclusion that the most promising approach would be to attack the question of unfavorable investment climate from the procedural angle, by creating an international machinery which would be available on a voluntary basis for the conciliation and arbitration of investment disputes.

In September 1963, the Bank prepared a preliminary draft entitled "Convention on the Settlement of Investment Disputes Between States and Nationals of Other States."[26] The Draft Convention was considered at four regional consultative meetings of legal experts held in Addis Ababa on December 16-20, 1963;

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24. E. Lanterpacht (ed.), The Suez Canal Settlement (London: Stevens and Sons Limited, 1960), p. 15.

25. International Bank for Reconstruction and Development, Settlement of Investment Disputes, An Address by A. Broches, the General Council (Washington D.C.: International Bank for Reconstruction and Development, 1963), p. 5.

26. International Bank for Reconstruction and Development, Legal Department, Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (Washington D.C., 1963), pp. 1-52.

Santiago on February 3-7, 1964; Geneva on February 17-22, 1964; and Bangkok on April 27-May 1, 1964, and attended by experts designated by 86 governments in all. The Executive Directors of the World Bank are now examining the results of the regional meeting in order to determine what further steps should be taken toward preparing a final text of a convention for consideration by governments.

The Draft Convention consists of a preamble and eleven articles on the establishment of an International Conciliation and Arbitration Center, its organization, jurisdiction, the constitution of the Conciliation Commission and Arbitration Tribunal etc...

The Preamble contains a general statement of the aims and purposes of the Convention, and is, in addition, intended to be declatory of the fundamental norms upon which the specific rules of the Convention are based. Paragraph 1, places the Convention in the context of the need for promoting economic development while paragraph 2, assures respect, for the proper exercise of national sovereignty under international law. The purpose for which conciliation and arbitration machinery is set up is limited in paragraph 2, to the settlement of investment dispute between Contracting States and the nationals of other Contracting States. Paragraphs 4 and 6 emphasize that recourse

to the Center is purely optional. Paragraph 5 recognizes the binding character of arbitration, representing the generally accepted principle of international arbitration to the effect that "recourse to arbitration implies an engagement to submit in good faith to the award."

Article 1, deals with the establishment of the International Conciliation and Arbitration Center by the World Bank. The Bank would provide the Center with purely administrative facilities and staff. The seat of the Center would be at the headquarters of the Bank, and shall have "full judicial personality." Its structure is conceived on the simplest lines and shall consist of an Administrative Council, a Secretariat, and the Panels.

The Administrative Council would be composed of one representative and one alternate representative of each Contracting State. The president of the World Bank shall be ex officio Chairman of the Council. The Council meets annually, and each member of the Council shall have one vote and except as otherwise provided, all matters before it shall be decided by majority vote. As its name implies, the Council shall have purely administrative functions, such as approving the annual budget of the Center, the terms of service of the Secretary-General, and the adoption of the rules for conciliation and arbitration.

The Secretariat consists of a Secretary-General, one or more Deputy Secretaries-General and staff. The Secretary-General

and Deputy Secretaries-General shall be appointed by the Administrative Council upon the nomination of the Chairman. The Secretary-General would be the principal administrative officer of the Center and shall be responsible for its administration. His office requires him to be one of complete independence.

The Panels consist of qualified conciliators and arbitrators designated by the Contracting Parties and the Chairman for a four years term. The Chairman, in exercising his right of designation of the panels, shall "pay due regard to the importance of assuring representation on the panels of the principal legal systems of the world and of the main forms of economic activity."

Article 11, deals with the jurisdiction of the Center and limits the proceedings to "conciliation and arbitration with respect to any existing or future investment dispute of a legal character," and shall bebased on the consent of the parties concerned. Consent of the parties to have recourse to the Center may be given either by a prior undertaking in writing or by ad hoc acceptance of jurisdiction. The facilities of the Center would be available only in disputes between a Contracting State on the one hand and a national of another Contracting State on the other, or between governments when subrogated to the rights of its national, as for example under a scheme of investment insurance.

Thus the facilities of the Center would not be available in a dispute involving a non-contracting state or a national of such state, as well as in a dispute between private individuals.

The Convention leaves the determination of the law to be applied in a particular case to the parties, and if they cannot agree thereon to the Tribunal. The parties, however, may also give the Tribunal the power to decide ex aequo et bono.

In the absence of agreement, consent to have recourse to arbitration, is considered consent to have recourse to such proceedings in lieu of any other remedy. Thus, in such a case, the exhaustion of local remedies is no more required.

The Arbitral Award is final and binding on the parties; each party is required to enforce it within its territory as if it were a final judgment of the courts of that state.

Articles III and IV deal respectively with conciliation and arbitration, the mechanism for the selection of the Conciliation Commission, the Arbitral Tribunal, their powers, functions and the conduct of proceedings. The request for conciliation as well as for arbitration may be made by either party to the dispute, and shall be addressed to the Secretary-General in writing, stating that the other party has consented to the jurisdiction of the Center.

The composition of the Conciliation Commission as well as the Arbitral Tribunal, their terms of reference, and the

procedures applicable in proceedings before them, are matters left for agreement between the parties concerned. However, in the absence of such agreement, the provisions of Articles III and IV would become operative. Therefore, in the absence of agreement, the Conciliation Commission would consist of three conciliators,one appointed by each party, and the third appointed by the agreement of the parties, and all appointees are to be selected from the Panel of Conciliators. Similar procedure is provided for the constitution of the Arbitral Tribunal. However, in distinguishing between the conciliation and the arbitration process, the proposed Convention provides that "none of the arbitrators shall be a national of a State Party to the dispute or of a State whose national is a Party to the dispute," whereas the Conciliation Commission on the other hand, does not prevent appointment of a conciliation on the ground that he is a national of a state party to the dispute, or of the state whose national is a party to the dispute. Moreover, it is important to note, in the recognition between the difference between conciliation and arbitration, and in the absence of agreement, that the recommendations of the Commission "shall not be binding upon" the parties, whereas the award of the Tribunal "shall be final and binding on the parties."

Article V is concerned with the replacement and disqualification of conciliators and arbitrators; while Articles VI and VII are devoted to the place of proceedings and the apportionment of the

costs of the proceedings. The place of proceedings shall be held either at the seat of the Center, or at the seat of the Permanent Court of Arbitration, or other public international institutions, as the parties may agree.

Article VIII is concerned with the question of interpretation and application of the Convention. Such interpretation would be referred to the International Court of Justice, unless the parties concerned agree to another mode of settlement.

Finally, Articles IX, X and XI deal respectively with amendment, definitions, and final provisions regarding the Convention, such as its entry into force, its territorial application, and its registration.

The important features of the Convention appears to be firstly, the recognition of the principle that a non-state party, an investor, might have direct access, in his own name and without requiring the espousal of his claim by his national government, to a state party before an international forum. Therefore, in signing the Convention, the party states have recognized that principle, and thus have emphasized the growing recognition of the individual as a subject of international law. However, the use of the facilities of the Center would be entirely voluntary. No state by the mere fact of accepting the Convention would be bound to resort to the facilities of the Center, and no foreign investor could initiate proceedings against a signatory state

unless both have agreed to do so. But once having consented, they would be bound to carry out their undertaking and, in the case of arbitration, to abide by the award.

Secondly, it is important to note that once the consent of the host government has been given, the investor would have direct access to the facilities of the Center, without the intervention of his national government. In such a case, the investor is considered to have waived the diplomatic protection of his national government, and thus his government is not entitled to take up his case. This development of existing international law would have the great merit of helping to remove investment disputes from the intergovernmental political sphere.

Thirdly, the proposed Convention, in considering the rule of local remedies, leaves it open to a state to stipulate that local remedies must first be exhausted before the dispute could be submitted for arbitration under the Convention. If the parties to a dispute had not made such a stipulation then and only then the Convention provides that arbitration would be regarded as excluding any other remedy.

Finally an award of an arbitral tribunal rendered pursuant to the Convention would be recognized and enforced by the parties on the same footing as a final judgment of the national courts.

Thus, if such judgment could be enforced under the domestic law in question, so could the award; if that judgment could not be so enforced, neither could the award.

These are some of the highlights of the proposed Convention, which are presently being studied in the World Bank. On the whole, the Convention is modest in the sense of being limited to procedures which are optional in nature. However, its importance, is the assurance which it provides by the fact that if the parties agreed to have recourse to the facilities available under it, their agreement would be given full effect. This would, undoubtedly, create an element of mutual confidence which would, in turn contribute to a healthier investment climate. In addressing the Economic and Social Council of the United Nations in April 1963, the President of the World Bank said that this Convention in his opinion "deserves the support of both capital-exporting nations and capital-importing nations and seems sufficiently promising to justify further constructive study and investigation in an attempt to reach a workable agreement."[27]

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27. International Bank for Reconstruction and Development, Op. cit., p. 7.

CHAPTER VI

Conclusions and Evaluations

One of the important and urgent problems of today is to create a more satisfactory and stable climate for the flow of private capital. This is because the economic development of the underdeveloped countries depends to a large degree upon private foreign investments and because these may not move to the areas where they are most needed unless reasonable conditions for security exist. Various state measures have been taken during the past years to deal with the protection of private foreign investment.

Each form of the guarantees given to foreign investors has its own advantages and limitations. As regards multilateral treaties, the advocates of an investment code, point out that it is the simplest as well as the most effective means to assure the protection of private foreign investment. They generally admit the difficulties involved in assuring that states will comply with the provisions of the code, but they tend to assume that the existence of such a code, in the form of a multilateral international convention, will in most cases be sufficient to prevent any breach of its provisions. However, the general adoption of an effective investment code, under present conditions, appears to be difficult for several reasons. Firstly, the multilateral

convention is a difficult kind of instrument when one is dealing with matters where particular situations and exceptional cases are matters of importance. An international convention would have to be made in general terms, since many states with various political and economic structures would be involved. Qualifications and exceptions would have to be added, each one of them quite necessary to the state or states concerned. The end result will tend to make the instrument meaningless. The precedents of the ITO Charter and the Economic Agreement of Bogota, are good examples in this connection.

Secondly, the provisions in a code, if they are to afford some protection to foreign investors, would have to limit the sovereignty of all states participating in it. It seems certain that many states would not be prepared to undertake far reaching commitments in this connection. Their reluctance should in part be attributed to a desire not to commit themselves on matters of domestic economic policy. Moreover, most of the underdeveloped countries have recently achieved nationhood after a lengthy struggle for independence - believe that the newly won political independence could be jeopardized by foreign investment protected by far reaching international commitments. If these commitments are not lived up to, the fear is that the private investor will be able to invoke the political and economic assistance of his government

in order to exert pressure upon the underdeveloped country in a manner that make them remember the old state of affairs, from which the host country hoped it had departed permanently. Therefore, these countries tend to favor specific, limited commitments rather than general and extensive undertakings.

Thirdly, certain additional considerations obtain in the case of capital-importing countries. The capital-exporting states can not give any assurance that substantial amounts of new foreign private capital will be invested, since their governments have limited control over the disposition of the funds of private citizens.[1] Even if legal obstacles are eliminated, economic reasons may prevent foreign investments in some underdeveloped countries. Thus, the capital-importing countries would have to accept certain definite obligations without any corresponding obligation on the part of the capital-exporting countries.

Finally, most of the proposed codes, are said to be one-sided in the sense of providing protection to the investor's interests without attempting to safeguard the capital-importing state's interests.[2] A convention on international investment is obviously meaningless unless it is agreed to by the host country as well as the investing country. It is therefore difficult to understand

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1. A.A. Fatouros, Government Guarantees to Foreign Investors (New York: Columbia University Press, 1962), p. 90.

2. Arthur Larson, "Recipients' Rights Under an International Investment Code," Journal of Public Law, Vol. IX (Spring, 1960), p. 172.

why so little attention has been given to the desires and attitudes of the host countries. The need, therefore, is for investors and investing companies to take a greater interest in the social, economic and human needs of the people of the host country, in order to obtain an investment code which is both workable and acceptable.

The bilateral investment treaties present definite advantages over the multilateral arrangements, such as the proposed investment code. Generally speaking, multilateral conventions are more difficult to conclude than bilateral ones, if only because of the need to reconcile a greater number of points of view and special interests. Moreover, bilateral treaties are more flexible. They can be adjusted to an important extent to the particular conditions prevailing in each country.

The bilateral approach, however, also has its limitations. Most of the difficulties mentioned in connection with the investment code, apply to various extents in the case of bilateral treaties. The fundamental problem is again the differences in the interests of the capital-importing and capital-exporting countries. Also the protection of the particular foreign investor depends on the willingness of his state of nationality to espouse his claim. The requirement of espousal of the claim may bring in a number of considerations, political or other, which have no relevance to the investment.

The investment guarantees provided by the capital-exporting countries have great usefulness. They, too, have limitations. They have been criticized by the capital-exporting states as being limited to new investments only and that they are conditioned on specific advance agreements between the host state and the investing state. They, also have been criticized on several grounds by the capital-importing states. Several of these states were reluctant to conclude a guarantee agreement because they regarded the provisions on immediate direct negotiations and the consequent by-passing of the requirements of local redress as a possible infringement of their sovereignty. Moreover, the guarantee program implies, as in the case of the United States, that the grantor state will be the judge of the fair or unfair character of the government policies in the capital-importing countries, determining by itself whether certain measures constitute expropriation and whether they render a currency non-convertible. Such implications, will no doubt be resented in the capital-importing country.

The content of the guarantees given by virtue of investment laws is well determined; the guarantee refers in each case to a particular investment. Several difficulties of interpretation are thus eliminated. On the other hand, the effectiveness of these guarantees are limited, despite their precision, to an important extent to action on the part of the capital-importing state.

Within their limitations, state guarantees can play a useful role in promoting international investments in underdeveloped countries. They are important in the sense of providing an indication that a favorable attitude toward foreign investment prevails in the particular capital-importing country. The offer of guarantees shows that the state concerned is conscious of its own need for foreign investment and of the foreign investor's desire for security. Such an attitude is itself reassuring to the investors. As has been shown, each form of guarantees has its own advantages and limitations. The latter are perhaps more prominent in the case of the proposed investment code; they seem to outweigh the advantages of certainty and universality that a code would presumably possess. The two forms of guarantees which are most widely used are the investment treaties and guarantees given by the capital-importing states. Bilateral investment treaties are perhaps the most effective. The step-by-step approach, seems to be feasible under present conditions in building international rules of law for the protection of private property invested abroad. Moreover, bilateral treaties are international instruments, binding upon the parties under international law. The protection they guarantee is backed by the existing machinery of international law.

The general need is felt more and more in the field of international economic relations, to favor the development of arbitration as a means in the settlement of investment disputes. Experienced international lawyers, such as Lord Shawcross, G.W. Haight,

and G.W. Ray have persuasively agreed that arbitration clauses in investment agreements would be of considerable mutual advantage to both capital-importing countries and to the investors. While it is difficult to prove that the absence of arbitration procedures constitutes an important obstacle to the flow of foreign investment generally, there is reason to believe that many enterprises, especially, those operating on a large scale, will be concerned about the risk resulting from a government relying on its"sovereign" power to cancel or modify contractual arrangements. For such firms, the willingness to contract for neutral arbitration in case of dispute is itself a significant symptom that the investment climate is favorable, and may be an important element in deciding to proceed with the investment.

However, the mere existence of an obligation to arbitrate does not always solve the problem. For even if the proceeding is carried through to a final award, it may be difficult to secure compliance from an unwilling government. Fortunately, such dangers do not always materialize, and many governments have been willing to honor their obligations. It is notable to mention in this connection, the correct attitude of the Saudi Arabian government toward an arbitration decided in 1958, with the Arabian American Oil Company.[3] In this particular arbitration, both the sovereign state and the foreign company, affirmatively insisted that the arbitration process go forward, and that both parties would abide by the arbitral award. This is the

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3. George W. Ray, "Law Governing Contracts Between States and Foreign Nationals," Selected Readings on Protection by Law of Private Foreign Investments, International and Comparative Law Center, The Southwestern Legal Foundation (Texas: Matthew Bender and Company, 1964), p. 507.

correct relationship that should exist between sovereigns and foreign investors in their settlement of disputes.

The attitude of the parties to an agreement is important. Where the parties willingly perform their obligations, there is no problem. Law and its enforcement become important in the extreme when one or the other party refuses to perform its obligations. The problem generated by the violation by a state of an international obligation is difficult, especially because of the lack of an appropriate enforcement machinery. The law is sufficient to answer questions raised by the violation. But the problem is to get the matter before an international tribunal empowered to declare it, and then to put it before an executive, armed with the power to enforce the tribunal's award, or to apply appropriate sanctions. In short, the need is for an impartial court with compulsory jurisdiction and enforcement procedures to carry out its judgments.

Our international society has not yet established a forum where states as well as foreign nationals can be required to submit their disputes to arbitration. However, several remedial suggestions have been made to facilitate the process of arbitration.

One such effort was to facilitate the arbitral process by providing standard rules for arbitral tribunals. The first rules of procedures on arbitration were those laid down in the Hague Convention of 1907. More recently, however, the United Nations International Law

Commission have prepared in 1958 a Model Draft on Arbitral Procedure. The relevant question to be asked here, is whether there should be a general international convention to embody a code of procedure for arbitrations between a private party and a foreign state. Such a code of procedure could be incorporated by reference in the agreements made between such parties, similar to the rules of the ICC, which are used in ordinary commercial transactions. It would apply insofar as the parties did not otherwise provide. Failure to comply with the terms of the convention would become a breach of obligation on the international level, for which the remedies of international law would be available. Such a code of arbitral procedure, established by a convention, would have certain definite advantages: (1) would reduce friction and delay over purely procedural matters; (2) would reinforce the obligation to arbitrate as specified in the individual agreements; and (3) through well-defined rules, would aid the growth of uniform jurisprudence on the subject.

The establishment of an international arbitral machinery by the World Bank for the settlement of investment disputes between states and foreign nationals is highly significant. For once such a Center (International Conciliation and Arbitration Center of the World Bank) has been founded, then in contracts between states and foreign investors, agreements can be made to

the effect that all disputes arising out of such contracts are to be referred to the Center. Moreover, the enforcement of the arbitral award should be assured; otherwise these awards may become totally ineffective. The adoption of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958, is important in this connection.

These instruments mentioned above suggest an approach valuable in the search to improve the remedies of the private claimant against foreign states. The proposed code for arbitral procedures would not necessary entail the establishment of a permanent arbitral machinery to handle disputes between private parties and foreign states. Nor would the establishment of such machinery necessarily call for the existence of a code of procedure, for procedure may be settled on an ad hoc basis each time. But the two undertakings together, incorporating the United Nations convention on the enforcement of foreign arbitral awards, would undoubtedly provide a complete and effective system of arbitration facilities in the settlement of investment disputes.

Many factors in addition to purely legal considerations will influence the private investor contemplating investment abroad. At the outset, he should feel assured of the probability of realizing a profit proportional to the evaluation of the risk involved. In all types of investments, economic factors, such as the availability of adequate labor, power resources and transportation facilities, may have an important bearing on the analysis of

probable profits. The foreign investor should also be satisfied that the political climate is not unfavorable. Such factors as nationalistic or socialistic sentiment which might result in exercise of government control or even expropriation, and government instability, which might result in important legislative changes, should carefully be weighed by the prospective investor.

In many cases, economic, or political or other non-legal factors will tip the scales in favor of or against the venture. When legal factors are favorable, they are not by themselves sufficient as investment incentives and they cannot attract foreign capital; other factors as well will have to favor investment in the country concerned.[4] It is therefore, no paradox that some countries offer guarantees of all forms without attracting foreign investors, while foreign capital is invested in others which do not offer such guarantees. In Egypt, for instance, although nationalization of commerce and industry occurred, there are still some foreign investments. The agreement between Fiat and the Egyptian government to manufacture Fiat cars in Egypt is one example.

The problem of international investment is basically an economic problem as well as a political one, to the extent that no

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4. A.A. Fatouros, Op. cit., p. 361.

serious world problem can avoid being political. Application of legal rules and concepts is necessary, but cannot be isolated from economic and political realities. This can be illustrated by the fact that most compensation agreements were settled by political rather than by legal means. This shows that the legal relationships between the parties, were dominated by the political and economic realities behind them. The latter, not the former, were found controlling in arriving at a settlement.

Finally, no guarantee can today provide complete security even from non-business risk only. The lack of security for investments in the underdeveloped countries is due to, and is a manifestation of, the general lack of stability in today's economic and political situation. It is not possible to provide complete security for investment where the underlying economic and political conditions are unstable. Legal means are useful, since they provide some degree of security, but there are definite limits to their effectiveness.

APPENDIX I

THE 1959 DRAFT CONVENTION ON INVESTMENTS ABROAD

The High Contracting Parties:

believing that peace, security, and progress in the world can only be attained and ensured by fruitful co-operation between all peoples on a basis of international law and mutual confidence; appreciating also the importance of encouraging commercial relations and promoting the flow of capital for economic activity and development; and considering the contribution which may be made towards these ends by a restatement of principles of conduct relating to foreign investments; have resolved for this purpose to conclude the present Convention.

Article I

Each Party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties. Such property shall be accorded the most constant protection and security within the territories of the other Parties and the management, use, and enjoyment thereof shall not in any way be impaired by unreasonable or discriminatory measure.

Article II

Each Party shall at all times ensure the observance of any undertakings which it may have given in relation to investments made by nationals of any other Party.

Article III

No Party shall take any measures against nationals of another Party to deprive them directly or indirectly of their property except under due process of law and provided that such measures are not discriminatory or contrary to undertakings given by that Party and are accompanied by the payment of just and effective compensation. Adequate provision shall have been made at or prior to the time of deprivation for the prompt determination and payment of such compensation, which shall represent the genuine value of the property affected, be made in transferable form, and be paid without undue delay.

Article IV

Any breach of this Convention shall entail the obligation to make full reparation. The Parties shall not recognise or enforce within their territories any measures conflicting with the principles of this Convention and affecting the property of nationals of any of the Parties until reparation is made or secured.

Article V

No Party may take measures derogating from the present Convention unless it is involved in war, hostilities, or other public emergency which threatens its life; and such measures shall be limited in extent and duration to those strictly required

by the exigencies of the situation. Nothing in this Article shall be construed as superseding the generally accepted laws of war.

Article VI

The provisions of this Convention shall not prejudice the application of any present or future treaty or municipal law under which more favourable treatment is accorded to nationals of any of the Parties.

Article VII

1. Any dispute as to the interpretation or application of the present Convention may, with the consent of the interested Parties, be submitted to an Arbitral Tribunal set up in accordance with the provisions of the Annex to this Convention. Such consent may take the form of specific agreements or of unilateral declarations. In the absence of such consent or of agreement for settlement by other specific means, the dispute may be submitted by either Party to the International Court of Justice.

2. A national of one of the Parties claiming that he has been injured by measures in breach of this Convention may institute proceedings against the Party responsible for such measures before the Arbitral Tribunal referred to in paragraph 1 of this Article, provided that the Party against which the claim is made has declared

that it accepts the jurisdiction of the said Arbitral Tribunal in respect of claims by nationals of one or more Parties, including the Party concerned.

Article VIII

If a Party against which a judgment or award is given fails to comply with the terms thereof, the other Parties shall be entitled, individually or collectively, to take such measures as are strictly required to give effect to that judgment or award.

Article IX

For the purposes of this Convention,

a. "nationals" in relation to a Party includes (i) companies which under the municipal law of that Party are considered national companies of that Party and (ii) companies in which nationals of that Party have directly or indirectly a controlling interest. "Companies" includes both juridical persons recognised as such by the law of a Party and associations even if they do not possess legal personality.

b. "property" includes all property, rights, and interests, whether held directly or indirectly. A member of a company shall be deemed to have an interest in the property of the company.

Article X

Final clauses relating to ratification, entry into force, accession, deposit, etc.

ANNEX RELATING TO THE ARBITRAL TRIBUNAL

1. The Arbitral Tribunal referred to in Article VII of the Convention shall consist of three persons appointed as follows: one arbitrator shall be appointed by each of the parties to the arbitration proceedings; a third arbitrator (hereinafter sometimes called "the Umpire") shall be appointed by agreement of the parties or, if they shall not agree by the President of the International Court of Justice, or failing appointment by him, by the Secretary-General of the United Nations. If either of the parties shall fail to appoint an arbitrator, such arbitrator shall be appointed by the Umpire. In case any arbitrator appointed in accordance with this Article shall resign, die, or become unable to act, a successor arbitrator shall be appointed in the same manner as herein prescribed for the appointment of the original arbitrator and such successor shall have all the powers and duties of such original arbitrator.

2. Arbitration proceedings may be instituted upon notice by the party instituting such proceedings (whether a Party to the Convention or a national of a Party to the Convention, as the case may be) to the other party. Such notice shall contain a statement setting forth the nature of the relief sought, and the name of the arbitrator appointed by the party instituting such proceedings. Within 30 days after the giving of such notice, the adverse party shall notify the party instituting proceedings of the name of the arbitrator appointed by such adverse party.

3. If, within 60 days after the giving of such notice instituting the arbitration proceedings, the parties shall not have agreed upon an Umpire, either party may request the appointment of an Umpire as provided in Article 1 of this Annex.

4. The Arbitral Tribunal shall convene at such time and place as shall be fixed by the Umpire. Thereafter, the Arbitral Tribunal shall determine where and when it shall sit.

5. Subject to the provisions of this Annex and except as the parties shall otherwise agree, the Arbitral Tribunal shall decide all questions relating to its competence and shall determine its procedure and all questions relating to costs. All decisions of the Arbitral Tribunal shall be by majority vote.

6. The Arbitral Tribunal shall afford to all parties a fair hearing and shall render its award in writing. Such award may be rendered by default. An award signed by the majority of the Arbitral Tribunal shall constitute the award of such Tribunal. A signed counterpart of the award shall be transmitted to each party. Any such award rendered in accordance with the provisions of this Annex shall be final and binding upon the parties and shall be published. Each party shall abide by and comply with any such award rendered by the Arbitral Tribunal.

APPENDIX II

INVESTMENT GUARANTEE PROGRAM OF THE FEDERAL REPUBLIC OF GERMANY

1. The investment guarantee program of the Federal Republic of Germany has been in operation since the latter part of 1959.

Geographic Scope of Program

2. Guarantees may be granted for capital investments to be made in countries which have entered into bilateral investment protection agreements with Germany or, on a transitional basis, in countries which adequately protect foreign investments through general legislation or other means (e.g.,assurances applicable to the particular investment). As of the end of 1961, investment protection agreements had been entered into with Pakistan, Malaya, Greece, Togo, Morocco, Liberia and Thailand. Negotiations are in progress with a number of other countries; some of these are close to completion.

Investment Protection Agreements

3. By the terms of the investment protection agreements, the parties bind themselves not to discriminate against the investments of each other's nationals or of the nationals of third countries. Investments and earnings may be expropriated only if required in the public interest and upon payment of compensation equal to the value of the investment, promptly paid, actually collectible and

freely transferable. Expropriation includes nationalization and action tantamount to expropriation. Prompt transfer of capital, earnings and the proceeds of liquidation of an investment is guaranteed, normally at the rate for current transactions. The mutual guarantees of the agreements may be retroactive, having application to investments made prior to the date of the agreement (although subsequent to a stated date). Each party agrees to recognize the succession of the other to the rights of an insured investor whose claim has been paid. In the event of a dispute concerning the meaning of the agreement which cannot be settled by consultation between the parties, the dispute may be referred to arbitration at the request of either party. The agreements are of stated duration and normally continue to be operative, for a specified period after their termination, to investments made before the termination date.

Eligible Investors

4. Guarantees may be purchased by German nationals and by companies having their domicile or place of business in the Federal Republic.

Eligible Investments

5. Guarantees are granted for future (new) investments which are deemed (to merit encouragement, particularly those which strengthen Germany's relations with the less developed countries).

Guarantees are intended primarily for enterprises engaged in production, extraction or marketing of goods or in transport.

6. Investments may be in the form of equity, a long-term loan (a loan of an investment type) or capital provided to an overseas branch, and may be made in cash or in some non-monetary form. Earnings from equity investments or long-term loans are eligible for guarantee if their coverage is sought when application is first made for the guarantee; protection extends to dividends declared but not paid and earnings in process of transfer.

Scope of Protection

7. A guarantee covers the risk of loss by reason of the following action by the government of the country of investment (guarantee contingency):

(a) nationalization, confiscation or measures equal to confiscation in their effect (confiscation contingency);

(b) war or other armed conflict, revolution or insurrection (war contingency);

(c) blockage of payment or moratoria (moratorium contingency); and

(d) impossibility of conversion or transfer (CT contingency).

8. The coverage offered is blanket coverage; the investor cannot purchase protection against a single risk or combination of risks.

Duration of Guarantee

9. A capital investment may be guaranteed for a maximum of 15 years normally; in exceptional cases the term may be 20 years. Renewal or further extension is not permitted. The guarantee becomes effective and the term begins to run when a "notice of guarantee" is delivered to the investor; coverage does not begin, however, until the investor has made the investment which is the subject of the guarantee. Earnings are protected for a term of years which may, in specified circumstances, be extended as long as the term, so extended, does not run beyond the term of the capital guarantee.

Amount of Coverage

10. The maximum amount of coverage for capital is the original book value of the investment. Any increment in value is thus not protected, although an expansion of the original undertaking by the investment of additional capital may be covered as a new investment. Normally, beginning with the fourth year of the guarantee, the maximum amount of coverage is automatically reduced at the end of each year by an amount stated in the notice of coverage, determined after taking account of the expected return on investment and duration of the guarantee. Coverage is also proportionately reduced by a reduction in the original investment, as by a repatriation of capital. The maximum earnings coverage is an aggregate, over the term of the earnings guarantee, of 24% of the original book value of the investment, and no more than 8% in any one year. There is

no automatic and progressive reduction of the maximum coverage for earnings.

Cost of Guarantee

11. In the case of a capital guarantee the premium, payable annually in advance, is a percentage of the maximum amount of coverage applicable at the beginning of the contract year. For an earnings guarantee, it is the same percentage of an amount arrived at by applying the annual rate of earnings coverage in force at the beginning of the contract year to the book value of the investment then applicable. For a guarantee term up to 5 years, the premium will be .75% per annum on the foregoing amount; for a term up to 10 years, the premium will be 1% per annum; for a term up to 15 years, the premium will be 1¼% per annum; for a term up to 20 years, 1½% per annum. A lower premium (.10%; .15%; .20%; and .25% respectively) is charged where the guarantee period begins to run before coverage becomes effective (where the investor has received a notice of guarantee but has not yet made the investment which is the subject of the guarantee); it applies until the investment is actually made.

12. A processing fee is payable upon application for a guarantee. The fee is 1 DM per thousand for the first DM 10 million of the amount of the guarantee, and ½ DM per thousand of the amount by which the guarantee exceeds DM 10 million; there is a ceiling of DM 20,000 upon the fee.

Operation of Guarantee

13. The guarantee becomes operative when a capital investment is wholly or partially lost by reason of a confiscation or moratorium contingency, or where the assets of the enterprise in which the guaranteed investment was made have been confiscated or destroyed totally or substantially.

Amount of Loss

14. When the guarantee becomes operative, the amount of loss will be fixed at the DM value of the investment at the time of the guarantee contingency. In the case of partial loss of an equity interest or a long-term loan, the amount of loss will be the difference between the value of the investment immediately prior to the guarantee contingency (subject to the ceiling of original book value) and its value following that event. In the case of an earnings guarantee, the amount of loss will be the unpaid amount of earnings distributed during the term of the guarantee.

Compensation

15. If the amount of loss does not exceed the maximum coverage applicable when the guarantee contingency occurred, the loss figure will serve as the basis for compensation; otherwise the maximum coverage is determinative. Any payments or benefits received by the insured investor from the host government,

the enterprise or other sources subsequent to the guarantee contingency will be deducted. The investor is required to be a self-insurer for 20% of any loss sustained, and may not insure this portion elsewhere. Compensation will be paid for the balance remaining after application of these ceilings and deductions, unless by the notice of guarantee the government has exempted itself from liability for claims of less than a specified amount and the claim in question falls below that amount.

16. Upon payment of compensation, the Federal Republic is subrogated to the investor's rights.

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