Reducing The Political Risk Of Investing In Russia And Other C.I.S. Republics: International Arbitration And Stabilization Clauses

Paul E. Comeaux *Jackson & Walker, L.L.P.* Houston
N. Stephan Kinsella *Jackson & Walker, L.L.P.* Houston

Political risks[1] may be a minor concern to a businessman investing in a stable liberal democracy with an independent judiciary and a track record of protecting property rights.

For example, a Belgian national investing in oil and gas properties in the U.S. is reasonably confident that in the unlikely event that the government nationalizes his property, the government would have to account for this action before a neutral U.S. court, which would not allow such an action to be taken arbitrarily, and which would order that just compensation be awarded.[2]

However, a foreign investor investing in an unstable regime or a regime hostile to property rights has no such assurances, and thus faces greater political risk.

The laws of a politically unstable country may unexpectedly change to an investor's detriment rendering his investment of time and capital worthless. The investor's options may be very limited, especially if the country does not have an independent judiciary to serve as a check on its powers of legislation. Furthermore, in most circumstances, the investor has no standing under international law to appeal this type of matter to an international tribunal. International law traditionally considers such matters purely within the jurisdiction and discretion of the country involved.[3]

Investors with greater bargaining power—those with large amounts of capital and expertise which are needed by the government to develop its economy and exploit its resources—can often reduce these uncertainties by asking the host state to grant the investor specific assurances and promises which can be enforced under international law. The state might provide assurance, for example, that will agree to settle disputes in a neutral forum (that is, not in the state's own courts), and promise that the state will not later pass internal legislation which may alter detrimentally the rights of the investor.

This article focuses on two important assurances for which a prudent investor in Russia or any other C.I.S. republic should ask before committing his resources.

This discussion of the relevant international law principles centers around asking for these assurances in a specific type of investor-state contract called a concession agreement, because much of the significant international law to date concerning agreements between a private investor and a host state focusses on concession agreements.

The international law principles discussed here concerning concession agreements are, however, equally applicable to other investor-state contracts which also contain these assurances.[4] Therefore, whenever an investor negotiates an agreement directly with a state or state agency, whether the agreement is called a concession, license, or joint venture, the investor should attempt to negotiate the clauses discussed here.

The nature of concessions

A concession is one type of contract between one state and a national of another state. It differs from a standard contract in that one of the parties to it is a sovereign state, which can make the relationship subject to international law.

This has important ramifications for

the investor.

The most important consequence is that the concession agreement is given international status. If the concession includes the clauses discussed in this article, then the state may not unilaterally change its terms without consequence in international law, despite the fact that the obligations must be performed on the territory of that country.[5]

This is of vital importance to the investor who wishes to invest in a country which might be tempted to change its laws in order to expropriate the investor's profits and assets.

For example, if a well-drafted concession contract were to state that the investing oil company has a right to choose which shipping fleet to use to transport the produced oil, then the country may not later impose unilaterally on the company a requirement that only government-favored tankers can export oil.[6]

Two provisions are often inserted in concession agreements in order to invoke these principles and to prevent the state from unilaterally changing the terms of the concession.

First, an international arbitration clause contemplates that any disputes arising in relation to the concession shall be settled before an international tribunal. This clause ensures the investor of a neutral forum to protect its rights in the concession, including its rights under the stabilization clause.[7]

Second, a stabilization clause, which states that the law in force in the country at the time the concession takes effect is the law that will apply to supplement the terms of the contract, is often included. A stablization clause prevents the state from imposing new laws on the investor that would change the terms of the concession or affect detrimentally the rights guaranteed thereunder.

The following focuses on the structure and validity of international stabilization clauses and arbitration clauses in international contracts, and the suitability for using these clauses in Russia and other C.I.S. republics.[8]

International arbitration clauses

Certain types of disputes seem to recur in international oil and gas concessions.

For example, the state will often raise dramatically the investor's taxes after promising not to do so, or will nationalize the investor's property without providing adequate compensation. A prudent investor will negotiate an arbitration clause into the concession agreement so that if a dispute cannot be resolved by negotiation, these and other problems can be settled in a neutral forum.

The investor should insist that the contract contain an international arbitration clause which provides that international arbitration shall be the method to settle any disputes arising in connection with the contract.

The presence of an arbitration clause serves a dual function. First, it defines the scope of an arbitration and procedures and details by which the arbitration shall be conducted. Second, and perhaps more important, it helps to establish the jurisdiction of an arbitrator to hear the matter.

Structure

A typical ad hoc international arbitration clause will provide detailed provisions concerning the scope of the arbitration clause, the method by which a party can invoke arbitration, the method for choosing the arbitrators, the procedural and substantive laws that will apply, the procedure if one party refuses to participate, the method by which the arbitrators render a decision, and the time period within which the parties must comply with the results of the arbitration.

In addition, the clause usually states that the decision of the arbitrators is binding.

To illustrate, a portion of the international arbitration clause found in the concession agreement that was the subject of the B.P. v Libyan Arab Republic arbitration is set forth below. The first paragraph of the arbitration clause establishes the consent of the parties to arbitration, the scope of any arbitration, and the method for choosing an arbitrator, and reads as follows:

"If at any time during or after the currency of this Concession any difference or dispute shall arise between the Government and the Company concerning the interpretation or performance hereof, or anything herein contained or in connection herewith, or the rights and liabilities of either of such parties hereunder and if such parties should fail to settle such difference or dispute by agreement, the same shall, failing any agreement to settle it any other way, be referred to two Arbitrators, one of whom shall be appointed by each such party, and an Umpire who shall be appointed by the Arbitrators immediately after they are themselves appointed.

In the event of the Arbitrators failing to agree upon an Umpire within 60 days from the date of the appointment of the second Arbitrator, either of such parties may request the President or, if the President is a national of Libya or of the Country where the Company was incorporated, the Vice-President, of the International Court of Justice to appoint the Umpire."[9]

The remainder of the arbitration clause concerns the matters referred to in the paragraph immediately above.

As an alternative to ad hoc arbitration, which sets out the procedures and administrative details of a possible arbitration in full detail, parties may choose to have their arbitration managed by an international arbitration system.

The International Center for the Settlement of Investment Disputes is one of several organizations that provide, for a fee, a detailed arbitration system, a list of experienced arbitrators, and administrative amenities.[10]

Validity and effect

The international arbitration clause, in addition to defining the scope, procedure, and administrative details of an arbitration, also serves as authority for an arbitrator to claim jurisdiction over a dispute. This is important, as often a state will object to the jurisdiction of the arbitrator and will refuse to recognize the validity of the proceedings. A firm basis in international law for the validity of the tribunal's authority will assist the investor in later efforts to enforce any award in its favor.

International case law confirms that an arbitrator has discretion to decide whether or not he has authority to

hear a matter presented to him.[11] One of the factors which is often cited in the arbitrator's "jurisdiction to decide jurisdiction" is the express consent of the parties. This consent should be found in the arbitration clause. As an example, the arbitration clause in the Texaco concession contains the following phrase:

"The Arbitrators . . . shall determine the applicability of this Clause and the procedure to be followed in the Arbitration."[12]

The arbitrator in the Texaco case cited this phrase as one of the justifications for his assuming jurisdiction.

If the arbitrator decides that he has jurisdiction, then jurisdiction cannot be revoked unilaterally by the state. International law dictates that a government bound by an arbitration clause cannot free itself of this obligation by unilateral action, such as by changing its internal law or by unilaterally rescinding the contract.[13]

"It is well-established in case law that the unilateral cancellation of a contract can have no effect on the arbitration clause which continues to be operative . . . ."[14] An arbitration clause is severable from the remainder of the concession and thus cannot be nationalized by the state even where the state nationalizes other rights contemplated by the concession agreement.

Stabilization clauses

A stabilization clause states that the law in force in the state at a given date—typically, the time the concession takes effect—is the law that will apply to supplement the terms of the contract, regardless of future legislation, decrees, or regulations issued by the government.[15]

Its purpose is to "preclude the application to an agreement of any subsequent legislative (statutory) or administrative (regulatory) act issued by the government . . . that modifies the legal situation of the investor."[16]

In other words, the state alienates its right to unilaterally change the regime and rights relied upon by, and promised to, the investor.

Structure

The concession contract between the parties in Liamco v. Libya provides a good example of a stabilization clause, which states:

"(1) The Government of Libya, the Commission and the appropriate provincial authorities will take all steps necessary to ensure that the Company enjoys all the rights conferred by this Concession. The contractual rights expressly created by this Concession shall not be altered except by mutual consent of the parties.

(2) This Concession shall throughout the period of its validity be construed in accordance with the Petroleum Law and the Regulations in force on the date of execution of the Agreement of Amendment by which this paragrph [sic] (2) was incorporated into this Concession Agreement. Any amendment to or repeal of such Regulations shall not affect the contractual rights of the Company without its consent."[17]

A stabilization clause states that the law in force in the state at a given date—typically, the time the concession takes effect—is the law that will apply to supplement the terms of the contract, regardless of future legislation, decrees, or regulations issued by the government.

The first paragraph makes it clear that mutual consent of the parties is needed to alter the contractual rights secured by the concession. The second establishes that the municipal law by which the concession is to be interpreted is fixed as of a certain date, so that no later government legislation or action can unilaterally infringe upon the company's contractual rights.

The key element of the stabilization clause is the removal of the government's right to unilaterally alter the investor's rights by changing its municipal law; this is made more explicit by the requirement that the investor's consent is necessary before any such change in law will affect the investor.[18]

Validity and effect

International law upholds both the validity of stabilization clauses and the right of a sovereign nation to bind itself through the use of such clauses.[19]

The tribunal in Texaco v. Libyan Arab Republic[20] stated that "[n]othing 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 concessionnaire irretractable rights." The tribunal in Texaco held that, "in entering into concession contracts with the plaintiffs, the Libyan State did not *alienate* but *exercised* its sovereignty."[21]

Some nations protest, however, that it is an infringement on their sovereignty for a tribunal to rule that they may not legislate in a way that would violate the terms of a concession agreement.

A stabilization clause is valid in principle under international law, although arbitrators differ as to the consequences of the violation of such a clause.[22] Generally, arbitrators will not order specific performance of a concession agreement, even if it contains a stabilization clause, due to respect for state sovereignty and an inability to enforce such an award (Texaco, discussed below, is an exception to this rule).

Instead, violation of a stabilization clause is more likely to have an effect on the amount of damages awarded or on the certainty that damages will be awarded.[23]

The decisions in several major international arbitrations are discussed in the following to examine the current state of international law concerning stabilization clauses:

- Texaco—In Texaco, Libya nationalized the property and rights of sev-

eral oil companies in violation of a concession agreement.[24] The concession contained a stabilization clause very similar to the Liamco clause discussed above.

The tribunal recognized the validity of a stabilization clause in a concession agreement. The clause was one factor in the tribunal's decision to declare the taking illegal and to render an award of restitution (ie., a return of the property the government nationalized).[25] The tribunal stated that this was "the normal sanction for non-performance of contractual obligations,"[26] although the award was in fact atypical.

Nevertheless, the tribunal held that where the contract was stabilized on a certain date by specific clauses, "the decision of a State to take nationalizing measures . . . carries international consequences . . . ."[27] This holding demonstrates the potential significance of a stabilization clause to help convince an arbitrator to grant a remedy to an aggrieved investor.

- Liamco—In Liamco v. Libya, Libya had awarded concessions to Liamco in 1955, and then nationalized the concession rights in 1973.[28] The tribunal held this to be a breach of the concession and awarded approximately $80 million as damages.[29] The concession's stabilization clause was discussed earlier in this article.

The tribunal held that, partially because of the stabilization clause's provision that "contractual rights expressly created by this Concession shall not be altered except by mutual consent of the parties,"[30] a "nationalization of concession rights . . . constitutes . . . a source of liability to compensate the concessionnaire for said premature termination of the concession agreement."[31] The court did not award lucrum cessans (i.e., lost profits) to the investor, which means that the investor did not receive compensation for the full value of what was taken.

However, the fact that a stabilization clause was present was one of the factors considered in the award of "equitable compensation"[32] by the tribunal.

- Aminoil—A recent international arbitration that contains a significant discussion of stabilization clauses is the Aminoil arbitration.[33] In 1948 Aminoil was granted a concession by Kuwait "for the exploration and exploitation of petroleum and natural gas in what was then called the Kuwait 'Neutral Zone'."[34] In 1961, Kuwait became fully independent, and the concession was modified by a supplemental agreement. In December 1974, OPEC countries adopted the "Abu Dhabi formula," which effectively raised taxes on the oil produced by Aminoil, to which Aminoil objected.[35]

Negotiations between the parties were unsuccessful and Kuwait expropriated Aminoil's assets in 1977.[36] In the ensuing arbitration, Aminoil claimed that this action was a breach of the stabilization clause contained in the concession agreement. The stabilization clause reads:

"The Shaikh shall not by general or special legislation or by administrative measures or by any other act whatever annul this Agreement except as provided in Article 11. No alteration shall be made in the terms of this Agreement by either the Shaikh or the Company except in the event of the Shaikh and the Company jointly agreeing that it is desirable in the interest of both parties to make certain alterations, deletions or additions to this Agreement."[37]

The tribunal stated that stabilization clauses were valid in principle, although it reasoned that this particular clause did not accomplish what it clearly contemplates on its face.

First, the tribunal held that the stabilization clause did not prohibit nationalization because it contained no *express* prohibition.[38] The arbitrator stated that a "contractual limitation on the state's right to nationalise . . . would be a particularly serious undertaking which would have to be expressly stipulated for . . . ."[39] He stated further that "[t]he case of nationalisation is certainly not expressly provided against by the stabilisation clauses of the Concession."[40]

Thus, this particular clause did not prevent nationalization despite its apparently clear and express wording.

Second, the tribunal held that the fact that Aminoil agreed during protracted negotiations to allow changes to the concession "brought about a metamorphosis in the whole character of the Concession."[41] The tribunal's position, in essence, was that since the investor had been willing to compromise during negotiations, it had in effect implicitly agreed to a weakening of the stabilization clause. Therefore, under this diluted or weakened stabilization clause, nationalization was permissible under the concession agreement as long as compensation was paid.[42]

The tribunal held that the existence of the clause merely warranted an award of damages despite the wording of the stabilization clause which seemed to clearly prohibit unilateral changes in law. Nevertheless, the existence of the stabilization clause—even weakened—was an important element in the tribunal's justification of the award of damages. The standard used to determine the amount of damages was that of "appropriate compensation".[43]

The investor negotiating a stabilization clause should learn two valuable lessons from this case. The first is that a stabilization clause should be very explicit in what it is meant to prohibit. The clause should provide that the State expressly waives its right to nationalize.

The second lesson is that a stabilization clause should provide that its terms are binding regardless of subsequent compromise, negotiation, or amendment of the contract unless both parties provide expressly, in writing, to change the meaning or binding effect of the stabilization clause.

This will allow the investor to negotiate changes in the contract with the state if circumstances change, without fear that a tribunal may later declare that the investor had agreed to these negotiations and somehow weakened or changed the nature of the stabilization clause.[44]

Enforceability of awards of damages

The relevance of a stabilization clause in international law is not that it will be, or even can be, specifically enforced,[45] but rather that it makes damages awarded by an international

tribunal either more certain to be awarded or likely to be higher than if a stabilization clause were not present. An award of damages, besides helping to bring international opinion and pressure to bear upon the nationalizing state and thereby aiding in settlement negotiations between the parties, may sometimes be recognized and enforced in national courts against property of the defendant state within the court's jurisdiction.

Various international agreements and treaties are currently in force which are designed to assist in the enforcement of foreign arbitral awards. Perhaps the most important is the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, first signed in New York in 1958, which provides for enforcement of foreign arbitral awards.

This is useful "where the assets of parties may be situated in different countries and transnational enforcement is desired."[46]

Obtaining an award of damages is desirable, despite problems in enforcement, as it increases the chances an investor has of obtaining compensation from the offending state. Furthermore, the mere prospect of having an award granted to an expropriated investor will help to dissuade a state from taking the investor's property in the first place.

Damages clause

One of the benefits of having a stabilization clause is the likelihood of a higher damages award than would otherwise be expected.

An additional method to help guarantee the award of the full value of the rights taken is for the investor to negotiate a damages clause. The damages clause should provide, although the state has no right under the contract to violate its terms, that if the state expropriates the investor's property or other rights, the state is obliged to compensate the investor for the full value, including lost profits (i.e., both damnum emergens and lucrum cessans).

An example of this type of clause is found in a recent Ghanaian concession contract, which contained an arbitration clause with the following paragraph:

"If any Contractor's rights, interests or property provided for herein are expropriated, nationalized or otherwise taken by reason of any act of the State or any central or local governmental authority of Ghana, then the arbitrators shall apply the principle of full and fair compensation for loss of profits determined on the basis of a going concern."[47]

The term "full and fair," and even the term "lost profits," may be subject to conflicting interpretations. The damages clause should therefore provide for a specific method to determine valuation, in order to avoid disputes over which accounting method is proper. This clause, if well drafted, would also make a state more reluctant to expropriate in the first place, since much of the temptation to take property is removed if the expropriating party must pay for the expropriated property.

Several decisions and authorities indicate that the amount of damages awarded may be higher if the expropriation is considered illegal under international law.[48]

The concept of international "illegality" is, however, a vague and uncertain one. Therefore, it would be advantageous for the investor to have the stabilization clause provide further that any nationalization or expropriation contrary to the terms of the agreement is, and is deemed to be by both parties, illegal and unlawful under international law. This should help to further ensure an award of damages which compensates the investor for the full value of the property and other contractual rights taken.

Investor-state contracts in Russia, other C.I.S. republics

The various clauses recommended in this article should be of particular importance to an investor in Russia or one of the other C.I.S. republics, as these states do not have impressive track records of protecting private property.

An investor should attempt to have these clauses included in any contracts negotiated with any of these states, whether or not the particular state has in place its own laws purporting to protect foreign investment, since the state's own internal laws are less likely to give the investor protection under international law.

Russian law provides a good example, for it has in place both laws purporting to protect a foreign investor and laws which seem to allow the investor to negotiate contractual clauses discussed in this article. Foreign private investors were given specific guarantees in Part II of the Law of the Russian Soviet Federative Socialist Republic ("RSFSR") on Foreign Investment ("Foreign Investment Law").[49]

Article 7 purports to be a protection against uncompensated nationalization. It provides that "[f]oreign investments of the RSFSR are not subject to nationalization . . . other than in exceptional cases . . . when these measures are undertaken in the public interest. . . . In [such] cases . . . the foreign investor shall immediately be paid adequate and effective compensation." As noted above, however, the worth of such guarantees is uncertain because the law that embodies the guarantees can be changed by the state itself and will be interpreted by the state's courts.

Furthermore, because of the holdings of the international arbitrations discussed above,[50] an investor should not depend upon an arbitral tribunal interpretation that an internal law of the state is an undertaking by the government not to nationalize the investor's property. An international tribunal would likely decline to assume jurisdiction absent a concession or other agreement with an international arbitration clause to provide the tribunal with jurisdiction.[51]

Laws in Russia also contemplate direct negotiation between the state and an investor and do not seem to exclude the right of an investor to negotiate the clauses discussed in this article. Article 40 of Russia's Foreign Investment Law authorizes "[t]he assignment to foreign investors of rights to develop . . . natural resources" through a "concession agreement concluded with foreign investors by the RSFSR Council of Ministers or other state organs so authorized . . . ."

Article 9 states that "[d]isputes of foreign investors and enterprises with foreign investments . . . are subject to review by RSFSR courts, or, pursuant to an agreement of the parties, by arbitration courts." Thus, the Foreign Investment Law of Russia contemplates that concession agreements, with arbitration provisions, may be entered into with foreign companies.[52]

Besides the Foreign Investment Law, a "law of particular importance to the petroleum industry is the Law of the Russian Federation Concerning Subsurface Resources enacted in February 1992"[53] ("Resources Law"). This law allows underground resources to be authorized through licenses. The Resources Law also "envisions the enactment of more detailed legislation,"[54] which was enacted in July 1992 as the Statute on Licensing of the Use of Subsoil Resources ("Licensing Statute").

The Licensing Statute adopts, unfortunately, an approach "in which the license takes the form of a mere permit to carry out authorized administrative acts. Such acts are treated as regulations subject to unilateral change by the government."[55]

This would appear to leave no room for stabilization clauses, which aim to remove the state's discretion to unilaterally change the investment environment. The Licensing Statute instead appears to contemplate that the investor will be subject to the state's regulatory framework.

However, an initial draft of the Law of the Russian Federation on Oil and Gas ("Draft Law on Oil and Gas") has been submitted to Parliament for consideration[56] and it appears to allow direct negotiation between the investor and the state. The Draft Law on Oil and Gas is intended to supplement the Resources Law. "It is designed to be largely consistent with this law but of equal weight so that it can supply . . . protections common to international practice that are necessary to attract the substantial long term investments needed in petroleum operations."[57]

This proposed law requires an investor to obtain the right to explore and exploit petroleum under a license from the state. "Unlike the Licensing Statute, [however,] the Draft Law on Oil and Gas defines the license as a contractual arrangement,"[58] a format which is more suitable for inclusion of international arbitration and stabilization clauses.

The Draft Law on Oil and Gas "permit[s] the licensing authority and the licensee to negotiate an agreement on private arbitration for disputes arising under the license."[59] If this bill were to be enacted into law, then the authority of the state and its relevant entities to negotiate international arbitration and stabilization clauses would be clearer.

Although it is clear from the above discussion that the legal framework in Russia is uncertain and still developing, certain laws currently in place, such as the Foreign Investment Law, and certain laws currently before the Russian Parliament, such as the Draft Law on Oil and Gas, indicate that direct negotiation between a foreign investor and the state will probably continue to be one way of doing business in Russia.

International arbitration and stabilization clauses are a good tool with which the investor can better protect his investment.

The laws of the other C.I.S. republics are also developing and it is uncertain whether these republics will be willing to agree to include stabilization and international arbitration clauses in contracts entered into with foreign investors.[60] These states will likely need to be willing to agree to such clauses in order to attract much-needed western skills, capital, and technology.

This is made more likely by the fact that international arbitration between states and investors has been growing in importance recently.[61] Therefore, investors may be successful in having these clauses inserted in contracts in at least some of the C.I.S. republics, if they insist upon them in negotiations.

Conclusion

Russia and other republics of the C.I.S. need the finances and knowledge of western investors. These investors will be attracted by reasonably stable opportunities for making profits.

An anti-property communist history and an unpredictable future will need to be overcome before the republics earn the trust of investors who are wary, yet eager, to help the republics and themselves create new wealth. A state's willingness to agree to international arbitration and stabilization clauses is a way to earn that trust.

Investors should push hard for these clauses and Russia and other C.I.S. republics would be wise to agree to them.

References

1. Political risk is the risk of government intervention faced by a foreign investor. Examples are the risk that the government will raise import or export duties, increase taxes, impose further regulations, or nationalize or expropriate the assets of the investor. Political risks do not include typical business risks such as changes in consumer demand or increases in the cost of production.
2. It should be noted, however, that many governmental actions in the U.S. which are takings of property rights—such as regulations and taxes—are not always considered to be takings by U.S. courts. *See generally* RICHARD EPSTEIN, TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN (1985).
3. Recent trends in international law indicate that this principle may not apply if human rights violations against the investor are involved. Such matters are beyond the scope of this article. *See generally* Rosalyn Higgins, *The Taking of Property by the State: Recent Developments in International Law*, 3 RECUEIL DES COURS DE L'ACADÉMIE DE FROIT INTERNATIONAL (Collected Courses of the Hague Academy of International Law), 259, at Chapter V, p. 355 *et seq.* (1982).
4. For a discussion of four basic arrangements between host countries and multinational oil companies, see Ernest E. Smith & John S. Dzienkowski, *A Fifty-Year Perspective on World Petroleum Arrangements*, 24 TEX. INT'L L.J. 13, 35 (1989). The authors also state that "[i]t is important to note, however, that some existing agreements have borrowed clauses and concepts from two or more types of arrangements. Thus, precise categorization of a particular country's arrangements is not always possible." *Id.* at 35-36.
5. Laws which affect the investor only incidentally or which are of general importance to the country as a whole, such as health and safety regulations, are generally upheld by international tribunals on the theory that their necessity justifies such a taking. For a further discussion of this topic, see Higgins, *supra* note 3, and Leo J. Bouchez, *The Prospects for International Arbitration: Disputes Between States and Private Enterprises*, 8 J. INT'L ARB. 81, 87 (1991).
6. Saudi Arabia v. Arabian American Oil Company (Aramco), Award of August 23, 1958, 27 I.L.R. 117, 227-38 (1963).
7. In addition, international law is often chosen as one of the laws to be applied by the arbitrator, as a further guarantee of neutrality. *See generally* Branson & Wallace, *Choos-*

ing the Substantive Law to Apply in International Commercial Arbitration, 27 VA. J. INT'L L. 39 (1986); A. Z. El Chiati, *Protection of Investment in the Context of Petroleum Agreements*, 4 RECUEIL DES COURS DE L'ACADÉMIE DE DROIT INTERNATIONAL (Collected Courses of the Hague Acadmey of International Law), 9, 121 *et seq.* (1987); and Bouchez, *supra* note 5, at 100 *et seq.*

8. There are many other considerations which must be taken into account when negotiating agreements with states. They are beyond the scope of this article. *See generally* Detlev F. Vagts, *Dispute-Resolution Mechanisms in International Business*, 3 RECUEIL DES COURS DE L'ACADÉMIE DE DROIT INTERNATIONAL (Collected Courses of the Hague Academy of International Law), p. 9 (1987) and the bibliography contained therein; Chiati, *supra* note 7 and the bibliography contained therein; ERNEST E. SMITH & JOHN S. DZIENKOWSKI, INTERNATIONAL PETROLEUM TRANSACTIONS INSTITUTE (November 20, 1992, Houston, Texas, sponsored by The University of Texas School of Law, forthcoming as a coursebook on International Energy Transactions); K. BLINN, C. DUVAL, H. LE LEUCH & A. PERTUZIO, INTERNATIONAL PETROLEUM EXPLORATION AGREEMENTS: LEGAL, ECONOMIC, AND POLICY ASPECTS (1986); GEORGES R. DELAUME, TRANSNATIONAL CONTRACTS: APPLICABLE LAW AND SETTLEMENT OF DISPUTES (1982); R. FOLSOM, M. GORDON & J. SPANOGLE, INTERNATIONAL BUSINESS TRANSACTIONS (1992); A.F. LOWENFELD, INTERNATIONAL PRIVATE INVESTMENT (2d ed. 1982); REDFERN & HUNTER, LAW AND PRACTICE OF INTERNATIONAL COMMERCIAL ARBITRATION (1986); Note, *Unilateral Action by Oil Producing Countries: Possible Contractual Remedies of Foreign Petroleum Companies*, 9 FORDHAM INT'L L.J. 63 (1985-1986); R. MIKESELL, PETROLUM COMPANY OPERATIONS AND AGREEMENTS IN THE DEVELOPING COUNTRIES (1984); and Barrows, *International Trends and Latest Changes in Oil Laws, Concession, and Production-Sharing Agreements Worldwide*, 1983 INST. ON INT'L OIL & GAS L. at A-1.

In addition, besides concession agreements and other contractual relations, other methods are commonly used to help sucure investments. Examples include government-sponsored insurance schemes and bilateral treaties. *See generally* KENNETH J. VANDEVELDE, UNITED STATES INVESTMENT TREATIES (1992); Chiati, at chapter III; Akinsanya, *International Protection of Direct Foreign Investment in the Third World*, 36 INT'L & COMP. L.Q. 58 (1987); Chatterjee, *The Convention Establishing the Multilateral Guarantee Agency*, 36 INT'L & COMP. L.Q. 76 (1987); Denza & Brooks, *International Protection of Investment Treaties*, 36 INT'L & COMP. L.Q. 909 (1987); Zakariye, *Insurance Against Political Risks in Oil Development*, 4 J. ENERGY NAT. RESOURCES & ENVTL. L. 217 (1986); WILLIAM F. FOX, JR., INTERNATIONAL COMMERCIAL AGREEMENTS (1988); Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Role of ICSID and MIGA*, ICSID REV. (1986); and Gallins, *Bilateral Investment Protection Treaties*, 2 J. ENERGY NAT. RESOURCES & ENVTL. L. 77 (1984).

9. BP Exploration Company (Libya) Limited v. Government of the Libyan Arab Republic (1973/74), 53 I.K.R. 297, 302 (1979).
10. For further discussion of international arbitration mechanisms, including a comparison of *ad hoc* and institutionalized arbitration, see Vagts, *supra* note 8; Bouchez, *supra* note 5, at 93 *et passim;* and Park, *Arbitration of International Contract Disputes*, 39 BUS. LAW. 1783 (1984).
11. *See* the Nottebohm Case (Liechtenstein v. Guatemala), [1953] I.C.J. 111, 20 I.L.R. 567 (1953); and the Case Concerning the Arbitral Award Made by The King of Spain on December 23, 1906 (Honduras v. Nicaragua), [1960] I.G.J. 192, 30 I.L.R. 457 (1966).
12. Texaco Overseas Petroleum Company and California Asiatic Oil Company v. The Government of the Libyan Arab Republic, Award on the Merits of January 19, 1977, 53 I.L.R. 389, 403-04 (1979), 17 I.L.M. 1 (1978).
13. Jiméniz de Aréchega, "L'Arbitrage entre les Etats et les Sociétés Privées Etrangères," in Mélanges en l'Honneur de Gilbert Gidel 367, 375 (1961), cited in *Texaco*, 53 I.L.R. at 410.
14. *Texaco*, 53, I.L.R. at 409, citing the *Losinger* case.
15. Principles of international law may also apply. The state's municipal law, as it stands on a given date, is often chosen as the law to govern certain local matters. *See generally* Chiati, *supra* note 7, at 121 *et seq.*
16. Chiati, *id.*, at 115. For examples of various stabilization clauses, see *id.*, at 115-21.
17. Libyan American Oil Company (LIAMCO) v. Government of the Libyan Arab Republic, Award of 12 April 1977, 62 I.L.R. 140, 170 (1980); 20 I.L.M. 1 (1981).
18. The first paragraph, in requiring mutual consent to change the concession contract, is sometimes referred to as an "intangibility clause" to distinguish it from a stabilization clause, which freezes the law as of a certain date. *See, e.g.*, Bouchez, *supra* note 5, at 86 *et seq.* Most such clauses, however, combine both complementary aspects. Chiati, *supra* note 7, at 115-116. Therefore, the term "stabilization clause" in this article will refer to both intangibility and stabilization provisions, as set out in the two paragraphs of the Liamco stabilization clause.
19. *See, e.g.*, Chiati, *supra* note 7, at 161, stating that "[s]tabilization clauses, validly entered into, are valid and binding."
20. *Texaco*, *supra* note 12, 53 I.L.R. at 474, quoting *Aramco*, *supra* note 6, 27 I.L.R. at 168.
21. *Texaco*, 53 I.L.R. at 4872 (emphasis added). *See also*, Bouchez, *supra* note 5, at 86, discussing a similar holding by the Permanent Court of International Justice in the *Wimbeldon* case, P.C.I.J. (1928) Ser. A, No. 1, p. 25.
22. As stated in *Liamco*, 62 I.L.R. at 205, international law is unclear on the question of damages. *See also* M.N. SHAW, INTERNATIONAL LAW 521 (3d ed. 1991).
23. *See* Chiati, *supra* note 7, at 165, stating that "the extent of the indemnity due to the investor . . . may vary from compensation for the value of the property taken to the financial equivalent of restitution and may even include, at least theoretically, punitive damages." (Footnote omitted.) *See also* SHAW, *supra*, at 523-24.
24. Texaco, *supra* at note 12, 53 I.L.R. at 422 *et seq.*
25. *Texaco*, 53 I.L.R. at 507. The award of restitution against a state is rare in concession cases; usually any award given is for damages only. For a discussion of the remedy of *restitutio in integrum*, see Higgins, supra note 3, at Chapter III, p. 298 *et seq.*
26. *Texaco*, 53 I.L.R. at 507.
27. *Id.* at 471.
28. *Liamco*, *supra* note 17, 62 I.L.R. at 160 *et seq.*
29. *Id.* at 218.
30. *Id.* at 191.
31. *Id.* at 217.
32. *Id.* at 217-218.
33. Government of Kuwait v. American Independent Oil Company (Aminoil), 21 I.L.M. 976 (1982), 66 I.L.R. 518 (1984).
34. *Id.*, 21 I.L.M. at 989.
35. *Id.* at 995 *et seq.*
36. *Id.* at 996-98. *See also* the discussion of the *Aminoil* case in Fernando R. Tesón, *State Contracts and Oil Expropriations: The Aminoil-Kuwait Arbitration*, 24 VA. J. INT'L L. 323 (1984); and Geoffrey Marston, *The Aminoil-Kuwait Arbitration*, 17 J. WORLD TRADE L. 177 (1983).
37. *Aminoil*, 21 I.L.M. at 990-991.
38. *Id.* at 1023.
39. *Id.*
40. *Id.*
41. *Id.*
42. *Id.* at 1024.
43. *Id.* at 1032. The international law principle of requiring "appropriate compensation" in such cases was codified in U.N. General Assembly Resolution no. 1803 (XVII) of 14 December, 1962, on Permanent Sovereignty over Natural Resources, Article 4. *Aminoil*, *supra* note 33, 21 I.L.M. at 1032. See also *Texaco*, *supra* note 12, 53 I.L.R. at 489, citing the standard "appropriate compensation" with approval as a rule of customary law.
44. The separate opinion of Sir. G. Fitzmaurice, *Aminoil*, 21 I.L.M. at 1043 *et seq.*, which is better reasoned than the main opinion, concurs in the judgment. Fitzmaurice reasons differently, and states that stabilization clauses do not need to be express to be effective; that this clause was express anyway; and that the character of the concession or of the stabilization clause had not changed due to subsequent negotiations and amendments. *Id.* at 1051-53.
45. Although the tribunal in *Texaco* awarded restitution, such an award will not, in practice, be enforceable against the offending state, not will an award of damages be enforceable against property within the territory of the state. "The problems . . . of enforcing such restitution awards against a recalcitrant state by be imagined." SHAW, *supra* note 22, 521-24. *See also* Chiati, at 158. "The futility of claiming a *restitutio in integrum* has become so apparent that some litigants do not even bother to claim it." *Id.* at 161.
46. Ian F. G. Baxter, *International Business Disputes*, 39 INT'L & COMP. L.Q. 288, 294 (1990). For further information concerning enforcement of foreign arbitral awards, see Bouhez, *supra* note 5, at 111 *et passim;* Peter M. McGowan, *Arbitration Clauses as Waivers of Immunity from Jurisdiction and Execution under the Foreign Soverign Immunities Act of 1976*, 5 N.Y.L. SCH. J. INT'L & COMP. L. 409, 417-19 (1984); Note, *Enforcing International Commercial Arbitration Agreements and Awards Not Subject to the New York Convention*, 23 VA. J. INT'L L. 75 (1982); Georges R. Delaume, *State Contracts and Transnational Arbitration*, 75 AM. J. INT'L L. 784 (1981); and J. Stewart McClendon, *Enforcement of Foreign Arbitral Awards in the United States*, 4 NW. J. INT'L L. & BUS. 58 (1982).
47. Chiati, *supra* note 7, at 166.
48. *See* SHAW, *supra* note 22, 523-24. For a recent discussion of compensation issues, see Amerasinghe, *Issues of Compensation for the Takings of Alien Property in the Light of Recent Cases and practice*, 41 INT'L & COMP. L.Q. 1 (1992).

49. Coudert Brothers translation, *Law of the RSFSR on Foreign Investments in the RSFSR*, in LEGAL AND PRACTICAL ASPECTS OF DOING BUSINESS IN THE SOVIET REPUBLICS (PRACTICING LAW INSTITUTE, RICHARD N. DEAN AND EUGENE THEROUX, CO-CHAIRMEN) 307-10 (1992). *See also* Gary B. Conine & J. Lanier Yeates, *Russian Petroleum Legislation: Assessing The New Legal Framework*, RUSSIAN OIL & GAS GUIDE, Jan. 1993, p. 3 at 4-5.
50. *Aminoil, supra* note 33, 21 I.L.M. at 1023.
51. *See supra* test accompanying notes 11-14.
52. Sarah C. Carey, *Five Years Later: Evaluating Foreign Investment Experience in the 'Former USSR'*, in *id.*, at p. 66. *See also* Gary B. Conine & J. Lanier Yeates, *supra* note 49, at 4 *et passim*. Additionally, it should be noted that "[e]nforcement of an international arbitration apparently still requires approval of the award by a Soviet court." *Id.* at note 20.
53. Gary B. Conine & J. Lanier Yeates, *supra* note 49, at 5 (footnote omitted).
54. *Id.*
55. *Id.*
56. *Id.* at 6. "Concepts embodied in the Draft Law on Oil and Gas were the product of joint efforts by Russian experts assembled by the Ministry of Fuel and Energy and western specialists assembled under the oversight of the University of Houston under a 1991 protocol." *Id.* at note 47.
57. *Id.* at 6.
58. *Id.*
59. *Id.* at 9. *See also id.*, at 7, stating that "[t]he Draft Law on Oil and Gas does not prescribe private arbitration as a method for resolving license disputes, but does recognize that the licensee and the licensing authority can bind themselves to private arbitration by agreement [Draft Law, art. 70], as permitted under the Foreign Investment Law. Russian law is of course the choice of law but a stability clause requires modification of license terms if a new law diminishes the licensee's economic advantages [Draft Law, art. 33]."
60. For the text of the foreign investment laws of several C.I.S. republics, see the appendices in PRACTICING LAW INSTITUTE (RICHARD N. DEAN AND EUGENE THEROUX, CO-CHAIRMEN), LEGAL AND PRACTICAL ASPECTS OF DOING BUSINESS IN THE SOVIET REPUBLICS (1992).
61. "In recent years there has been an increase in the activity and promotion of international arbitration." Baxter, *supra* note 46, at 299. "[T]aking into account the growing importance of international commercial arbitration arbitration with respect to international dealings between private parties—including international transactions between private parties and State enterprises . . . it is to be expected that international arbitration will continue to play an important role between States and State enterprises on the one hand and foreign private parties on the other." Bouchez, *supra* note 5, at 115.

Comeaux

Kinsella

The authors...

Paul E. Comeaux is an associate in the finance and real estate sections and in the international law practice group of the law firm Jackson & Walker. He received his B.A. degree (1988) from Louisiana State University, his J.D. degree (1991) from the Paul M. Hebert Law Center, Louisiana State University, and his LL.M. degree (1992) in International Business Law from King's College London, University of London. He is licensed to practice in the States of Texas and Louisiana.

Mr. Comeaux may be contacted at Jackson & Walker, 1100 Louisiana, Suite 4200, Houston, TX 77210-4771. Phone: (713) 752-4386. Fax: (713) 752-4221.

N. Stephan Kinsella is an associate in the energy section and in the international law practice group of the law firm Jackson & Walker. He received his B.S. (1987) and M.S. (1990) degrees in electrical engineering from Louisiana State University, his J.D. degree (1991) from the Paul M. Hebert Law Center, Louisiana State University, and his LL.M. degree (1992) in International Business Law from King's College London, University of London. He is licensed to practice in the States of Texas and Louisiana.

Mr. Kinsella may be contacted at Jackson & Walker, 1100 Louisiana, Suite 4200, Houston, TX 77210-4771. Phone: (713) 752-4360. Fax: (713) 752-4221.

Russian Oil & Gas Guide

April 1993 Vol. 2, No. 2

Editor and Publisher
JOHN L. KENNEDY

Managing Editor
ROBERT G. LAIR

Art Director
JO JEANNE LONDON

Circulation Manager
LARRY LOFTON

Vice President Energy Group
TOM T. TERRELL

Atlantis International
BRYAN W. ALDRIDGE

The Cover
This crude gathering and processing facility is near Tarko Sale in northern central Siberia. Photo by Grant Lichtman, Jebco Seismic, Inc., Houston.

The Russian Oil & Gas Guide [ISSN 1064-9697] *is published by PennWell Publishing Co., 1421 S. Sheridan Rd., Tulsa, Okla., Box 1260, 74101. Editorial office is located at 3050 Post Oak Blvd., Suite 200, Houston, Tex. 77056; mailing address, P.O. Box 1941, Houston, Tex. 77251. Phone: (713) 621-9720.*

Subscription rates: *1 year (four issues), US $800.*

Address changes, *letters about subscription service, or subscription orders should be sent to Circulation Manager, Russian Oil & Gas Guide, P.O. Box 2002, Tulsa, Okla. 74101.*

Contents