REducing political risk in developing countries: bilateral investment treaties, stabilization clauses, and MIGA & OPIC investment insurance

Paul E. Comeaux* & N. Stephan Kinsella**

* LL.M. (International Business Law) (1992), University of London—King's College London; J.D. (1991), Paul M. Hebert Law Center, Louisiana State University; B.A. English Literature (1988), Louisiana State University. The author is an associate in the finance and real estate sections and in the international law practice group in the Houston office of Jackson & Walker, L.L.P.

** LL.M. (International Business Law) (1992), University of London—King's College London; J.D. (1991), Paul M. Hebert Law Center, Louisiana State University; M.S. Electrical Engineering (1990), B.S.E.E. (1987), Louisiana State University. The author is an associate in the intellectual property department of Schmehl, Harrison, Segal & Lewis in Philadelphia. Internet: mkinzel@ware.com.
I. INTRODUCTION

The emergence of relatively free-market economic policies in the
developing nations of the world has created immense opportunities for
Western investors. However, along with these opportunities comes
substantial risk. In addition to ordinary business risk, which is faced by
every businessman or investor whether investing at home or abroad,
investors in developing countries face political risk that is much greater
than that experienced when investing in liberal Western democracies.

Political risk is the risk that the laws of a country will unexpectedly
change to the investor’s detriment after the investor has invested capital in
the country, thereby reducing the value of the individual’s investment. Put
simply, political risk is the risk of government intervention.1 Examples of
debt and equity risks may be substantial if a treaty to protect private
risk are the risks that a government will raise import or export
duties, increase taxes, impose further regulations, or nationalize or
expropriate the assets of the investor.

Political risk may be a minor concern to a business person investing
in a stable liberal democracy with an independent judiciary and a track
record of protecting property rights; 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. For example, a Belgian
national investing in oil and gas properties in the United States can be
reasonably confident that, in the unlikely event that the government were
to nationalize his property, it would have to account for this action before
a neutral U.S. court that would not allow such an action to be taken
arbitrarily and would award just compensation.2 The investor’s options in
the face of such intervention may be very limited, especially if the country

---

1. One type of political risk that is not often recognized as such is the very ability of
legislatures to enact legislation, to change the rules from day to day. As pointed out by
the late Italian legal theorist Bruno Leoni in his Freedom and the Law, even if a given
statute is written clearly, “we are never sure that tomorrow we shall still have the rules
we have today.” Bruno Leoni, Freedom and the Law 75 (3d ed. 1991) (emphasis in
original). For a detailed discussion of these issues, see Peter H. Aranson, Bruno Leoni
in Retrospect, 11 HARV. J. L. & PUB. POL’Y 661 (1988); Leonard P. Liggio & Tom G.
Palmer, Freedom and the Law: A Comment on Professor Aranson’s Article, 11 HARV.
J. L. & PUB. POL’Y 713 (1988); and N. Stephan Kinseala, The Irrationalism of the Civil
Law (forthcoming).

2. It should be noted, however, that many governmental actions in the U.S. which are
in fact takings of property rights, such as zoning regulations and taxes, are not always
considered to be takings by U.S. courts. See generally Richard A. Epstein, Takings:

---

1994] REDUCING POLITICAL RISK 5

does not have an independent judiciary to serve as a check on its
legislature.

The investor can take some comfort, however, in the recently signed
bilateral investment treaties between the U.S. and several developing
countries. These treaties contain promises by these countries guaranteeing
certain standards of treatment of U.S. investors and investments.

In addition, an investor with enough clout may be able to negotiate
directly with a host state to receive “internationalized” contractual
assurances containing “stabilization clauses” and international arbitration
clauses. These clauses provide that the law in place when the investor
initially invests will continue to apply to the investor and that disputes
between the investor and the government will be settled in a neutral
forum.

An investor can also purchase political risk insurance. This insurance
typically provides coverage against risks such as currency inconvertibility,
repatriation, and war and is available from a number of sources,
including nationally-sponsored insurance agencies, private insurers, and
the World Bank’s Multilateral Investment Guarantee Agency (“MIGA”).

Each of these ways of controlling political risk is discussed in turn in
this Article.3

II. BILATERAL INVESTMENT TREATIES

Political risk may be substantially reduced if a treaty to protect private
investment is in place between the foreign state and the investor’s home
state. Treaties aimed specifically at protecting private foreign direct
investment are called bilateral investment treaties (“BITs”). BITs set forth
standards for treatment of foreign investors in areas such as expropriation
of property, repatriation of funds, and settlement of disputes.

While investors can, and should, use other methods to reduce political
risks—such as concession agreements4 and government-sponsored
insurance programs—the presence of a treaty provides a strong incentive for a host state to honor its obligations under international law and its agreements with the investor. When a host state violates the rights guaranteed to the investor by the treaty, that state has not only violated norms of customary international law (such as the requirement to expropriate only for a public purpose, in a nondiscriminatory fashion, and upon the payment of prompt, adequate, and effective compensation), but has also breached a treaty with the investor's home state.

While European countries have been successfully negotiating BITs since the late 1950s, the United States did not begin to do so until the early 1980s. In 1982, the United States announced the formulation of a model BIT, which was updated in 1983, 1984, and again in 1987. The model BIT is used as a starting point in all BIT negotiations conducted by the United States.

It is likely that BITs will soon be in place between the United States and several developing countries, including many of the C.I.S. republics. As part of its ongoing program of negotiating BITs with its trading partners, especially less developed countries, the United States has signed BITs with the Russian Federation and several other states. The U.S.-Russia BIT received the advice and consent of the U.S. Senate and requires similar domestic approval from the Russian government before it enters into force.

5. See infra Part IV.
8. Previously, issues of private foreign investment were addressed collaterally in treaties known as Friendship, Commerce, and Navigation Treaties ("FCNs"). Although the first FCN was negotiated with France by Benjamin Franklin, Arthur Lee, and Silas Deane shortly after the signing of the Declaration of Independence, BITs were the first treaties focused solely on these issues. Kenneth J. Vandevelde, The Bilateral Investment Treaty Program of the United States, 21 CORNELL INT'L. L.J. 201, 203-13 (1988). For further discussion of FCNs, see id. at 204. See also Valerie H. Rottenberg, The United States Bilateral Investment Treaty Program: Variations on the Model, 9 U. PA. J. INT'L. BUS. L. 121 (1987).
9. Vandevelde, supra note 8, at 210-11.
10. The treaty power is granted to the President, by and with the advice and consent of the Senate, providing two-thirds of the Senators present concur. U.S. Const. art. II, § 2, cl. 2.
11. Telephone Interview between Paul E. Comeaux and the Office of Treaty Information, United States Department of State (Nov. 30, 1994).

This section discusses the major provisions of the U.S.-Russia BIT, as an example of a typical U.S. BIT, and examines how these provisions will affect investors.12

A. The U.S.-Russia BIT

The BIT between America and Russia (the "U.S.-Russia BIT") was signed in Washington, D.C. on June 17, 1992.13 It is the first BIT with a C.I.S. Republic to be submitted for Senate consideration14 and has since been approved by the United States Senate.15 Although the U.S.-Russia BIT imposes obligations on both Russia and the United States with respect to foreign investment, we focus here on Russia's obligations to American investors under the BIT.

The issues addressed by the U.S.-Russia BIT include: the standard of treatment of U.S. investment by Russia; the legality of and remedies for expropriation of U.S. investments; the transfer of currency into and out of Russia; certain provisions for the settlement of investment disputes; the duration of the U.S.-Russia BIT; and the status of the U.S.-Russia BIT in the event that the Russian Federation splits apart.

1. Treatment of Investment

Article II concerns the standard of treatment which Russia must provide to U.S. investors and their investments.16 These standards fall into two broad categories: relative treatment, which means that Russia must treat U.S. investment as well as it treats investment from any other

14. Letter of Submittal from Secretary of State Lawrence S. Eagleburger to President George Bush (July 21, 1992) (included with the U.S.-Russia BIT).
15. Id.
country; and absolute treatment, which states that Russia must treat U.S. investment fairly and equitably, and in accordance with international law, regardless of how it treats non-U.S. investment.

- Relative Standards. Paragraph 1 of Article II provides for "relative" standards of treatment, by requiring Russia to treat U.S. investment "on a nondiscriminatory basis" with non-U.S. investment, subject to exceptions in certain sectors of the economy which are listed in an Annex to the BIT. 17

These relative standards are sometimes known as "national treatment" and "most-favored-nation" ("MFN") treatment. National treatment generally requires the host state to treat the foreign investment no less favorably than the investment of its own nationals; MFN treatment requires the host state to treat the investment no less favorably than it treats the investment of any third country's investors. 18 Paragraph 4(a) of the Protocol to the U.S.-Russia BIT specifically refers to the requirement to accord national treatment with respect to the entry of investments. 19

The exceptions listed in the Annex generally relate to matters such as land, power production, state loans, banking, and mass media. 20 One significant sector in which Russia reserves the right to make exceptions is "ownership of land and use of subsoil and natural resources." 21 Attached to the U.S.-Russia BIT is a letter between the U.S. and Russia containing an understanding of the BIT shared by both countries. The letter states that

[b]ased on the Law of the Russian Federation on Subsoil and legislation relating to natural resources, the Russian Federation

17. Id.
20. Id.
21. It is noteworthy that in the U.S.-Russian treaty the United States has accepted, for a period of five years, the requirement of a special investment permission by the Russian Government for "large-scale investments that exceed the threshold amount set forth in the Russian Federation Law on Foreign Investments of July 4, 1991." It should be recalled that Article 16 of the Law requires that "enterprises into which foreign investors contributed in excess of the total of 100 million Rubles" be subject to an approval process by the Russian Government.


23. Id.
24. See Shaw, supra note 6, at 516-521.
25. Paragraph 2(c) refers to "obligations [Russia] may have entered into with regard to investments . . . ." This type of agreement is known as a concession. See id. at art. I, ¶ 1 (defining "investment agreement" as "an agreement between a Party (or its agencies or instrumentalities) and a national or company of the other Party concerning an investment"). Although it is useful to have this obligation embodied in a treaty, this
terminate in the future even after it does come into force (discussed below), and because of Russia's power to make exceptions with respect to natural resources, an investor would be wise to consider the use of a concession to protect his investment, as discussed in Part III, below.

- **Other protections.** Other provisions of Article II guarantee the right of U.S. investors to bring U.S. nationals to Russia to establish the investment (Paragraph 3) and to hire top managerial personnel of their choice, regardless of nationality (Paragraph 4). Russia is barred from imposing on the investor requirements to export goods produced, or to purchase goods and services locally, or other similar requirements (Paragraph 5). Russia is to provide effective means of asserting claims and enforcing rights related to investments and investment agreements (Paragraph 6) and must publish all laws or regulations affecting investments (Paragraph 7).

2. Expropriation

Provisions protecting an individual's investment from the consequences of an expropriation or nationalization are of particular importance—especially in an unstable regime such as Russia, which also has a history of hostility towards private property rights.

Article III of the U.S.-Russia BIT limits Russia's right to expropriate U.S. investments in Russia and provides for compensation when expropriation does occur. The Article provides that investments shall not be expropriated, directly or indirectly, unless performed: (1) for a public purpose; (2) in a nondiscriminatory manner; (3) upon payment of prompt, adequate, and effective compensation; and (4) in accordance with due process of law and the "absolute" standards of treatment discussed above.

Realistically, although Russia would be technically in breach of a treaty obligation, as well as customary international law, if it were to take property in a discriminatory manner or not for a public purpose, merely finding Russia to have violated international law will be of little economic benefit to an injured investor, who may well have lost millions, or even billions, of dollars' worth of assets and other rights.

Therefore, one of the most important guarantees an investor can have is a guarantee of compensation if an expropriation occurs. Practically speaking, it is impossible to prevent a nation from expropriating assets it is determined to confiscate because other states would not be willing to prevent the expropriation by force. This is especially true in the context of the modern movement towards "permanent sovereignty over natural resources," in which many states (typically, third-world, developing economies) have declared that a state always retains the right to expropriate certain assets, such as natural resources, if the "public interest" demands it—even if the state has promised not to do so, e.g. in a concession agreement or in a BIT.

It is, however, more acceptable under current international law and practice for a state to bind itself to pay compensation in the event that it does nationalize or expropriate an investor's property. Based upon an obligation to compensate, the courts of other nations, in certain circumstances, are willing to enforce a damages award, against the assets of the offending state which are located within the court's jurisdiction. It is seen as less of an infringement on the sovereignty of the confiscating state to simply enforce a commitment to pay compensation than to declare that the confiscating state may not perform expropriating acts within its own sovereign territory.

---


29. It is not realistic to expect an award of specific performance, or of restitution, to either be awarded or enforced against a sovereign state. Although the tribunal in Texaco Overseas Petroleum Company v. The Government of the Libyan Arab Republic, Award on the Merits of January 19, 1977, 53 Ill. L.R. 339 (1970), 17 L.L.M. 1 (1978), awarded restitution, such an award will not, in practice, be enforceable against the offending state, nor will an award of damages be enforceable against property within the territory of the
Thus the provision of Article III requiring "payment of prompt, adequate and effective compensation" is one of the most potentially useful to an investor. Such a requirement is likely to be one of the most effective in terms of protecting the value of the investment because other nations are more willing to enforce a damages award based on this obligation and because Russia would be less willing to expropriate in the first place if it would have to pay for the property it confiscates.

Of further benefit to the investor is the adoption of the "prompt, adequate and effective compensation" standard and the further requirement that compensation should be the "fair market value of the expropriated investment immediately before the expropriatory action was taken or became known." 30 This compensation standard is the "Hull Formula," which is promoted by the United States but is not universally accepted as customary international law. This standard better protects the investor by insisting that the aggressor nation pay the true economic value of the investment which is taken, rather than "appropriate" compensation—an inadequate standard which is often favored by less developed countries. 11

This provision also requires that compensation be paid without delay, include interest from the date of the expropriation, be fully realizable, and be freely transferable at a market rate of exchange. 32 Additionally, the

state: "The problems . . . of enforcing such restitution awards against a recalcitrant state may be imagined." Shaw, supra note 6, at 321-24. See also Z. El Chanti, Protection d'Investissement en Contexte de Petrole, 4 RECUEIL DES COURS D'ACADEMIE DE DROIT INTERNATIONAL [R.C.A.D.I.] (Collected Courses of the Hague Academy of International Law) 9, 158 et seq. (1987). "The feasibility of claiming a restitution in integral has become so apparent that some litigants do not even bother to claim it." Id. at 161.


32. Since the time of signature of the BIT there was no single market rate of exchange in Russia, the U.S.-Russia BIT carries with it a side letter stating that in the absence of a unified rate of exchange in the Russian Federation at the time of ratification, the provision in question has to be renegotiated at the request of the United States. The same applies to a market rate for all other transfers, referred to in Article IV (2) of the Russian BIT.

1994]

REDUCING POLITICAL RISK

Article prohibits indirect, as well as direct, expropriation. This provision helps to ensure that Russia may not avoid the prohibition against expropriation by indirectly or gradually imposing regulations 33 that have the same economic effect as a direct expropriation.

Other provisions in Article III concern the right of an investor complaining of an expropriation to review of the complaint by the appropriate judicial or administrative authorities in Russia and the right of an investor to be accorded nondiscriminatory treatment by Russia as regards restitution, compensation or other measures following losses due to war or revolution in Russia.

3. Currency Transfers

Although highly onerous exchange control regulations may constitute an expropriation, exchange control regulations which do not rise to this level can still be very costly to investors. 34 Article IV of the U.S.-Russia BIT addresses this concern by providing for free transfer of currency into and out of the Host State. 35 The treaty states that each country shall allow "all transfers related to an investment to be made freely and without delay into and out of its territory." Investors are allowed to convert currency "into the freely convertible currency of their choice."

The treaty gives examples of what is meant by "transfers related to an investment." Such transfers fall into two broad categories. First, a transfer may occur in the normal course of the investor's business. Examples include returns and proceeds from the sale or liquidation of all or part of an investment. Second, a transfer may occur as a payment from Russia to the investor as compensation for a transgression. If Russia compensates the investor for a violation of an agreement between them, Russia may not pay the money and then refuse to allow the money to be expatriated.

Article IV does, however, list several qualifications. Russia is allowed to require reports of currency transfers by the investor and to impose withholding taxes on expatriated currency. Finally, Russia is

Golsong, supra note 21, at 795.

33. Gradually increasing regulations which amount to a taking are sometimes known as "creeping expropriation."

34. Vandeveld, supra note 8, at 244.

35. U.S.-Russia BIT, supra note 13, art. IV, S. TREATY DOC. No. 102-33 at 11-12.
allowed to pass laws protecting the rights of creditors, which may interfere with an investor’s right to freely transfer currency.

4. Arbitration and Settlement of Investment Disputes

Article VI of the U.S.-Russia BIT concerns the settlement of disputes between the investor and the Host State.\(^{36}\) This Article covers “investment disputes,” which are defined as disputes arising over: (a) an investment agreement between the investor and the host state; (b) the authority given to the investor by the Host State; or (c) a breach of the U.S.-Russia BIT itself. If any such dispute arises, the U.S.-Russia BIT mandates that the parties first attempt to settle the dispute between themselves, with or without the help of third-party, non-binding mediation. This rule overrides contractual provisions between the investor and the Host State to the contrary. Thus, even if the investor and the Host State are parties to a concession which provides that, upon violation of the concession, either party may immediately invoke binding arbitration, the U.S.-Russia BIT mandates that the parties must nevertheless first attempt to settle their differences by negotiation. An investor that negotiates to resolve an investment dispute in accordance with this provision of the U.S.-Russia BIT should keep records of such negotiations to prevent later claims by the Host State that no such negotiations were undertaken.

If the investment dispute cannot be resolved by negotiation between the parties, the parties are then allowed to settle their dispute “in accordance with previously agreed, applicable dispute-settlement provisions.”\(^{37}\) This provision contemplates and allows dispute settlement provisions, such as international arbitration provisions, in agreements between a Host State and an investor.\(^{38}\) The U.S.-Russia BIT states that these dispute-settlement procedures are enforceable in accordance with “the terms of the agreement, relevant provisions of domestic law, and applicable international agreements regarding enforcement of arbitral awards.”\(^{39}\)

---

36. Such disputes are differentiated from disputes between the U.S. and Russia themselves, which are governed by Articles V and VII. Id. arts. V, VI, VII at 12-16.
37. Id. art. VI at 13.
38. See infra part III.
39. This provision may be interpreted to mean that dispute settlement provisions can be invalidated by domestic law. This interpretation would allow the Host State to invalidate an international arbitration provision that it had previously agreed to in a concession by legislating against it. The investor can best protect itself from this contingency by including a stabilization clause in any contract negotiated with a state. For further discussion of stabilization clauses, see infra Part III.
40. The ICSID is an international arbitral institution with both a standing secretariat and rules for arbitration between states and nationals of other states. It was formed by the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, which was signed in Washington D.C. in March of 1965. Currently, over 100 countries are parties to the ICSID Convention. As of this writing, Russia has signed but not ratified the convention. See generally The Convention on the Settlement of Investment Disputes, 136 R.C.A.D.L. 330 (1972).
41. The ICSID Additional Facility is a part of the ICSID and is designed to handle arbitration between States which are not a part of the ICSID convention and nationals of other States.
42. For further discussion of stabilization clauses, see infra Part III.
5. Termination of the U.S.-Russia BIT

Article XIII provides that the BIT enters into force thirty days after it has been ratified by both the U.S. and Russia and remains in force for at least ten years.\(^{43}\) Of particular importance to investors with already-existing investments in Russia, this Article also provides that the BIT “shall apply to investments existing at the time of entry into force as well as to investments made thereafter.”\(^{44}\) This provision helps reduce any incentive an investor might have to wait until the BIT is in force before investing, and also, as a bonus, protects current investments on an equal footing with post-BIT investments.

After the initial ten-year period, either Russia or the U.S. may, by giving at least one year’s written notice, terminate the BIT. Thereafter, any prospective investor would be aware that the BIT was no longer in force and could decide not to invest in Russia if the risk was felt to be too high. For investors who had already invested in Russia, the Article provides that the provisions of the BIT continue to be effective for a period of ten years from the date of termination of the treaty. Therefore, any investor relying upon the protections afforded by the U.S.-Russia BIT should be aware that Russia could, at any time after the initial ten-year period, announce termination of the BIT, giving the investor benefits under the BIT for only eleven more years (one year’s notice to terminate plus ten years after termination).

To the extent that investors require protection lasting longer than this, other options, such as investment insurance programs or concession agreements negotiated directly with the government that contain a longer term than that of the BIT, should be considered.

6. Dissolution of the Russian Republic

Given recent unrest and instability in Russia, investors may understandably be concerned that republics or parts of Russia could separate from Russia to form one or more independent states. For example, three of the most restless of the republics are Chechnya, Tatarstan, and the oil-rich Bashkortostan; it is not inconceivable that these republics could break away from Russia entirely.\(^{45}\)

---

43. U.S.-Russia BIT, supra note 13, S. TREATY DOC. No. 102-33 at 19-20.
44. Id. at 19.
III. STABILIZATION AND INTERNATIONAL ARBITRATION CLAUSES

After an individual has made a foreign investment, the political regime may become unstable, thus rendering the investment of time and capital worthless. As discussed in the introduction above, 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.

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 specific assurances and promises which can be enforced under international law. The state might provide assurance, for example, that it will agree to settle disputes in a neutral forum (not in the state's own courts), and a promise that the state will not later pass internal legislation which may alter detrimentally the rights of the investor.

This section of this Article focuses on two important assurances for which a prudent investor in any developing country should ask for 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 focuses on concession agreements.

51. 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, Problems and Process: International Law and How We Use It (1994) and a book review of Higgins's book, N. Stephan Kinella, REASON PAPERS No. 20 (Fall 1995, forthcoming); Rosalyn Higgins, The Taking of Property by the State: Recent Developments in International Law, 3 R.C.A.D.L. 259, 355 at seq. (1982) (hereinafter Higgins, The Taking of Property by the State).

52. 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 "[t]he 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.
Reducing Political Risk

I. Introduction

The decision to invest in a foreign country involves understanding the political risks associated with the country in question. It is important to consider the potential for political instability, changes in government policy, and the impact of political events on business operations. Countries where the political landscape is uncertain or where there have been recent political upheavals may present a higher risk for international investment. Understanding these risks is crucial in order to make informed decisions and prepare for potential challenges.

A. Political Instability

Political instability can arise from a variety of factors, including coups, revolutions, and civil wars. Such events can disrupt normal business operations, lead to changes in regulations, and affect the security of investments. It is important to assess the level of political instability in a country and consider how it might impact the business venture.

B. Changes in Government Policy

Government policies can change rapidly, leading to shifts in the regulatory environment and market conditions. For example, changes in taxation laws or regulations governing foreign investment can significantly impact the profitability of a business. It is essential to monitor the political climate and stay informed about potential policy changes in order to make strategic decisions.

C. Economic Sanctions

Economic sanctions imposed by international organizations or governments can have a profound impact on a business's operations. Sanctions can restrict access to resources, limit export opportunities, and create additional costs, such as increased security measures. Understanding the risk of being targeted by sanctions is crucial for businesses operating in countries under scrutiny.

D. Diplomatic Relations

Diplomatic relations between nations can influence trade and investment opportunities. A change in the relationship between two countries, such as the establishment of diplomatic ties or the severance of existing relations, can impact market access and business opportunities. It is important to consider the political climate and diplomatic relations when deciding to invest in a foreign country.

E. Labor and Employment

Labor relations and employment laws can significantly impact business operations. Countries with labor unrest or high unemployment rates may pose challenges for businesses seeking to establish or expand operations. Understanding the labor market and its dynamics is crucial for successful international investment.

II. Mitigation Strategies

It is important to develop strategies to mitigate the risks associated with political instability and other political factors. This may include diversifying investments, maintaining strong relationships with local partners, and staying informed about political developments.

A. Diversification

Diversifying investments across multiple countries can help mitigate the risks associated with political instability. By spreading investments, businesses can reduce exposure to individual political risks and maintain a more stable revenue stream.

B. Local Partnerships

Building strong partnerships with local companies and government officials can help navigate the complexities of doing business in a foreign country. Local partners can provide valuable insights into the political climate and help mitigate potential risks.

C. Monitoring and Communication

Staying informed about political developments and communicating effectively with the local government and other stakeholders is crucial. Regular updates and open lines of communication can help businesses better understand and respond to political changes.

D. Legal and Regulatory Compliance

Ensuring compliance with local laws and regulations is essential for maintaining a good relationship with the government and minimizing the risk of legal challenges. Regularly reviewing and updating business practices to align with local regulations is important.

E. Risk Assessment and Management

Developing a comprehensive risk assessment strategy can help identify potential political risks and develop strategies to mitigate them. This may include conducting regular risk assessments and implementing contingency plans to address potential challenges.

III. Conclusion

Investing in foreign countries poses unique challenges due to the potential for political risks. By understanding these risks and implementing strategies to mitigate them, businesses can increase their chances of success in international markets. Staying informed, building strong relationships, and adapting to changing circumstances are key to navigating the complexities of international investment.
President of the International Court of Justice to appoint the Umpire.  

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 can choose to have their arbitration managed by an international arbitration system. The ICSID is one of several organizations that provide a detailed arbitration system, a list of experienced arbitrators, and administrative amenities.

2. Validity and Effect

An international arbitration clause, in addition to defining the scope, procedure, and administrative details of an arbitration, also grants authority to an arbitrator to claim jurisdiction over a dispute. This authority is important, as often a state will object to the jurisdiction of the arbitrator and will refuse to recognize the validity of the proceedings. Establishing 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.

International case law confirms that an arbitrator has jurisdiction to decide whether he has authority to hear a matter presented to him. 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 is 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.” The arbitrator in the Texaco case cited this phrase as one of the justifications for 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.

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... 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.

C. 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. 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.” In other words, by agreeing to a stabilization clause, a state alienates its right to unilaterally change the regime and rights relied upon by, and promised to, the investor.

64. Id.
67. 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 Chisiti, supra note 29.
68. Id. at 115. For examples of various stabilization clauses, see id. at 115-21.
The decisions in several major international arbitrations are discussed below to examine the current state of international law concerning stabilization clauses. In Texaco, Libya nationalized the property and rights of several oil companies in violation of a concession agreement.77 The concession contained a stabilization clause very similar to the LAMCO 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 award of restitution invalid, on returned to the company a source of its property and rights.78

The tribunal stated that this award was the normal sanction for non-performance of contractual obligations,79 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..."80 This holding demonstrates the potential significance of a stabilization clause to help convince an arbitrator to grant a remedy to an aggrieved investor.

In LAMCO v. Libya, Libya had awarded concessions to LAMCO in 1955 and then nationalized the concession rights in 1973.81 The tribunal held that the nationalization to be a breach of the concession and awarded approximately $80 million as damages.82 The concession's stabilization clause was discussed earlier in this article. The tribunal held83 that a stabilization clause constitutes a source of liability to compensate the concessionaire for said premature termination of the concession agreement.84 The court did not award luxrum cessans (i.e., lost profits) to the investor; consequently, the investor did not receive compensation for the full value of what was taken. However, the

77. Texaco, 53 I.L.R. at 422.
78. Id. 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 restitution in international law, see Higgins, The Taking of Property by the State, supra at 51, at 298-355.
79. Texaco, 53 I.L.R. at 507.
80. Id. at 471.
82. Id. at 218.
83. Id. at 218.
84. Id. at 217.
85. Id. at 217-18.
87. Id.
88. Id.
91. Id.
arbitrator stated that a "contractual limitation on the state's right to nationalize . . . would be a particularly serious undertaking which would have to be expressly stipulated for . . . ." 92 He stated further that "[i]n the case of nationalisation is certainly not expressly provided against by the stabilisation clauses of the Concession." 93 Thus, this particular clause did not prevent nationalization despite its apparently clear wording.

Second, the tribunal held that the fact that Aminoli agreed during protracted negotiations to allow changes to the concession "brought about a metamorphosis in the whole character of the Concession." 94 The tribunal's position, in essence, was that since the investor had been willing to compromise during negotiations, the investor had in effect implicitly agreed to a weakening of the stabilization clause. Therefore, under this diluted or weakened stabilization clause, a nationalization was permissible under the concession agreement as long as compensation was paid. 95

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." 96

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 compromises, negotiations, or amendments to the contract unless both parties provide expressly, in writing, to change the meaning or binding effect of the stabilization clause. This flexibility 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 fact that the investor had agreed to these negotiations and somehow weakened or changed the nature of the stabilization clause. 97

3. 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, 98 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. 99 This provision is useful where the assets of parties may be situated in different countries and transnational enforcement is desired. 100 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.

92. Id.
93. Id.
94. Id.
95. Id.
96. Id. at 527. For the international law principle of requiring "appropriate compensation" in such cases, see Permanent Sovereignty over Natural Resources, para. 4, G.A. Res. 1803, U.N. GAOR, reprinted in DURAN J. DICINOSKI, 9 UNITED NATIONS RESOLUTIONS, SERIES I. RESOLUTIONS ADOPTED BY THE GENERAL ASSEMBLY, 1962-1963, at 107 (1974). See also Texaco Overseas Petroleum Company v. Libyan Arab Republic, 53 I.L.R. at 489 (citing the standard "appropriate compensation" with approval as a rule of customary law).
97. The separate opinion of Sir G. Fitzmaurice in Aminoli, 66 I.L.R. at 524-31, 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.
98. Although the tribunal in Texaco awarded restitution, such an award will not, in practice, be enforceable against the offending state, nor 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 may be imagined." SHAW, supra note 6, at 221-24. See also Chisli, supra note 29, at 158. "The futility of claiming a restitution in integrum has become so apparent that some litigants do not even bother to claim it." Id. at 161.
100. Id.
4. 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 that if the state nevertheless 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.

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. The concept of international "illegality" is 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 provision 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.

D. INVESTOR-STATE CONTRACTS IN DEVELOPING COUNTRIES

The various clauses recommended in this Article should be of particular importance to an individual investing in developing countries that do not have impressive track records of protecting private property. Since the states' own internal laws are less likely to give the investor protection under international law, an investor should attempt to have these clauses included in any contracts negotiated with these states, whether or not a particular state has in place its own laws purporting to protect foreign investment. It is likely that many states will be willing to enter into such concessions, since international arbitration between states and investors has been growing in importance recently. Therefore, investors

---

101. Chiari, supra note 29, at 166.
may be successful in having these clauses inserted in contracts with at least some of the developing countries, if they insist upon them in negotiations.

IV. MIGA, OPIC, & PRIVATE INVESTMENT INSURANCE

Individuals investing in developing countries face risks, such as the risk of currency inconvertibility and expropriation, which are much greater than the risks experienced by investors who invest in Western liberal democracies. Other than relying upon the existence of BITs and negotiating contractual assurances such as stabilization and international arbitration clauses, an investor can also reduce political risk by purchasing political risk insurance. This insurance typically provides coverage against risks such as currency inconvertibility, expropriation, and war and is available from a number of sources, including nationally-sponsored insurance agencies, private insurers, and the World Bank's Multilateral Investment Guarantee Agency ("MIGA"). This Article focuses on MIGA and on the U.S.-government-sponsored investment agency, the Overseas Private Investment Corporation ("OPIC").


104 See discussion supra Part II.

105. See discussion supra Part III.

106. The largest government-sponsored insurance agencies, which are the U.S. Overseas Private Investment Corporation, Germany's Treuhand, and the Japanese Export Insurance Division, Ministry of International Trade and Industry, together represent over 80 percent of all outstanding national insurance coverage. Malcolm D. Rowat, Multilateral Approaches to Improving the Investment Climate of Developing Countries: The Cases of ICSID and MIGA, 33 HARV. INT'L L.J. 103, 119, 122 (1992).


are the insurance providers of the most interest to U.S. investors. In addition, this Article briefly discusses several private insurers that offer political risk insurance.

A. OPIC

1. Background

OPIC, established under the Foreign Assistance Act in 1969, is a self-sustaining U.S. government agency that provides political risk insurance, as well as project financing through direct loans and loan guarantees and a variety of investor services, to U.S. investors. OPIC's insurance is "backed by the full faith and credit of the United States, as well as by OPIC's own substantial reserves." OPIC services are available for U.S. investments in more than 139 developing nations. Its goal is to encourage American overseas private investment in sound business projects, thereby improving U.S. global competitiveness, creating American jobs, and increasing U.S. exports. OPIC's political risk insurance is discussed in detail below.

were used.


108. Much of the following discussion on OPIC draws on information obtained directly from OPIC. See e.g., the "Investment Insurance" pamphlet and related information supplied by OPIC. OVERSEAS PRIVATE INVESTMENT CORPORATION, INVESTMENT INSURANCE (n.d.).


110. OVERSEAS PRIVATE INVESTMENT CORPORATION, supra note 108, at 1.
2. Risks Covered by OPIC Insurance

OPIC will insure both new ventures and expansions of existing enterprises and can cover equity investments, loans, technical assistance agreements, leases, and other investment structures which subject the investor to long-term exposure. The investor may purchase insurance coverage for one or more of the following three types of risks: (1) currency inconvertibility, which is the inability to convert profits and other remittances into U.S. dollars; (2) expropriation, which is the confiscation of the investor's property by the host state; and (3) political violence, which includes war, revolution, insurrection, and civil strife. In addition, OPIC offers specialized insurance coverage for certain specific types of investments, including specialized insurance for oil and gas-related investments.

a. Currency Inconvertibility

Currency inconvertibility insurance coverage compensates investors if they cannot convert remittances from the local currency into U.S. dollars and transfer those remittances outside of the host country. It includes earnings, returns of capital, principal and interest payments, technical assistance fees, and other remittances related to investment projects. This coverage also extends to losses to the investor caused by discriminatory exchange rates. Currency inconvertibility coverage does not extend to the devaluation of a country's currency. In addition, the investor may only collect on currency inconvertibility insurance if the currency was convertible into "U.S. dollars at the time the insurance was issued." 111

b. Expropriation

Expropriation insurance protects against the nationalization, confiscation, or expropriation of an enterprise as well as creeping expropriation, which is defined as a series of illegal government actions that cumulatively deprive an investor of the financial interests in his investment. Expropriation coverage excludes losses due to lawful regulatory or revenue actions by host governments and actions provoked or instigated by the investor or foreign enterprise. For equity investments, the amount of compensation is based on the book value of the investment as of the date of expropriation. For loans, payment is based on outstanding principal and accrued interest.

c. Political Violence

Political violence insurance compensates for property and income losses caused by violence undertaken for political purposes. Examples of the types of violence covered are declared war, undeclared war, hostile actions by national or international forces, civil war, revolution, insurrection, and civil strife. Civil strife may be included or excluded from coverage, at the investor's option. Actions undertaken primarily to achieve labor or student objectives are not covered. The insurance may cover one or both of two types of losses—business income losses and damage to property. An investor may purchase one or both coverages.

Business income loss coverage includes income losses resulting from damage to the investor's property caused by political violence. With an "off-site" rider, OPIC will provide compensation for income losses resulting from damage to specific sites outside the investor's facility. Compensation is based on expected net income plus continuing, normal operating expenses. OPIC also will pay for expenses that reduce the business income loss, such as renting a temporary facility. Compensation is paid until productive capacity is restored, for a time period not to exceed one year.

"Damage to property" compensation is based on the adjusted cost of the property or replacement cost. Adjusted cost is defined as the least of the original cost of the item, the fair market value at the time of loss, or the cost to repair the item. OPIC will pay replacement costs or twice the equipment's original cost, provided the item is actually replaced in the host country.

d. Special Oil and Gas Insurance

OPIC offers specialized insurance coverage to encourage petroleum exploration, development, and production in developing countries. In addition to insurance coverage for the risks discussed above, an investor may purchase "exploration" coverage and "interference with operations" coverage.

Exploration coverage expands expropriation coverage to insure against losses due to material changes unilaterally imposed by a host government on project agreements. These changes include an abrogation, impairment, repudiation, or breach of concession agreements, production sharing

111. Diasconis, supra note 109, at 274.
112. Id.
agreements, service contracts, risk contracts, and other agreements between the U.S. company and the host state. Such actions must last for at least six months and prevent the insured from effectively exercising its fundamental rights with respect to the project agreement, such as rights to take and export petroleum or to be paid for it. The coverage also compensates for tangible assets and bank accounts that are confiscated.

Interference with operations coverage expands political violence coverage to insure against cessation of operations for six months or more caused by political violence. Compensation for such cessation is based on the amount of investment, less returns of capital. Compensation must be repaid to OPIC, without interest, if within five years the political violence has abated and the insured can resume operations.

3. Eligibility for OPIC Insurance

OPIC political risk insurance may only be issued if the investor, the foreign country, and the investment itself meet OPIC's requirements. In addition, OPIC will take certain political requirements into account. These eligibility requirements are discussed in more detail below.

a. Eligible Investors

To be eligible for OPIC insurance, an investor must be: a U.S. citizen; a corporation, partnership, or other association created under the laws of the U.S., its states, or territories beneficially owned by U.S. citizens; or a foreign business at least 95% owned by U.S. citizens or by associations owned by U.S. citizens.

b. Eligible Projects

An investment project qualifies for OPIC insurance coverage if the investment is a new investments, a privatization, or an expansion or modernization of an existing plant or investment. Acquisitions of existing operations are eligible if the investor contributes additional capital for modernization and/or expansion. There is no requirement that the foreign enterprise be owned or controlled by U.S. investors. However, in the case of a project with foreign ownership, only the portion of the investment made by the U.S. investor is insured by OPIC. Insurance is normally not available for investments in enterprises which are majority-owned and controlled by a foreign government.

Investments may take many forms: conventional equity investments and loans; construction and service contracts; production sharing agreements; leases; and various contractual arrangements, such as consigned inventory, licensing, franchising, and technical assistance agreements.

Finally, the investor must submit a Request for Registration for Political Risk Investment Insurance before the investment is made or irrevocably committed.

c. Eligible Countries

OPIC may not offer insurance for a project in a country with which the U.S. does not have an investment agreement. Currently, OPIC programs are available in 140 developing countries. Investors should contact OPIC to determine the status of OPIC assistance in a particular country.

Under agreements with the host countries, the host government must approve the issuance of OPIC insurance for a project. The approval procedures vary from country to country and are available from OPIC.


114. OPIC's "Country and Area List" lists countries in which OPIC programs are generally available: Albania, Algeria, Anguilla, Antigua & Barbuda, Argentina, Armenia, Aruba, Azerbaijan, Bahamas, Bahrain, Bangladesh, Barbados, Belarus, Belize, Benin, Bolivia, Botswana, Bosnia & Herzegovina, Brazil, Bulgaria, Burkina Faso, Burundi, Cameroon, Cape Verde, Central African Republic, Chad, Chile, Colombia, Congo, Cook Islands, Costa Rica, Côte d'Ivoire, Croatia, Cyprus, Czech Republic, Djibouti, Dominica, Dominican Republic, Ecuador, Egypt, El Salvador, Equatorial Guinea, Estonia, Ethiopia, Fiji, French Guiana, Gabon, Gambia, Georgia, Germany (eastern), Ghana, Greece, Grenada, Guatemala, Guinea, Guinea-Bissau, Guyana, Honduras, Hungary, India, Indonesia, Ireland, Israel, Jamaica, Kazakhstan, Kenya, Kiribati, Kuwait, Kyrgyzstan, Laos, Latvia, Lebanon, Lesotho, Lithuania, Madagascar, Malawi, Malaysia, Mali, Malta, Marshall Islands, Mauritania, Mauritius, Federated States of Micronesia, Moldova, Mongolia, Morocco, Mozambique, Namibia, Nepal, Netherlands Antilles, Nicaragua, Niger, Nigeria, Northern Ireland, Oman, Panama, Papua New Guinea, Paraguay, Peru, Philippines, Poland, Portugal, Qatar, Romania, Russia, Rwanda, St. Kitts & Nevis, St. Lucia, St. Vincent & the Grenadines, Sao Tome & Principe, Saudi Arabia, Senegal, Sierra Leone, Singapore, Slovakia, Slovenia, Somalia, Sri Lanka, Swaziland, Taiwan, Tajikistan, Tanzania, Thailand, Togo, Tonga, Trinidad & Tobago, Tunisia, Turkey, Turkmenistan, Uganda, Ukraine, United Arab Emirates, Uruguay, Uzbekistan, Venezuela, Western Samoa, Yemen, Zambia, Zimbabwe. OPIC'S PRIVATE INVESTMENT CORPORATION, COUNTRY AND AREA LIST (January 12, 1993).
d. Political Considerations

OPIC has a legislative mandate to support projects which are responsive to the development needs and the environment of the host country and which foster private initiative and competition. In particular, OPIC must give preferential treatment to investments in countries with a per capita annual income of less than $984 in 1986 U.S. dollars.115 If a project is given monopoly rights or other competitive advantages for more than five years, special justification for OPIC involvement is required.

The effect of a proposed investment on the U.S. economy also is closely examined. Coverage is denied to projects which are likely to have a negative impact on U.S. employment and where the host country imposes requirements that substantially reduce the potential U.S. trade benefits of the investment.

OPIC also may decline coverage to projects which are likely to have a significant adverse effect on the U.S. balance of payments. OPIC also requires that countries respect certain individual rights and internationally-recognized workers' "rights."116

4. Terms

a. Duration

The term of an insurance policy may extend a maximum of twenty years. For loans, leases, and transactions covered by the contractors and exporters program, the term is generally equal to the duration of the underlying contract.

b. Cost

OPIC insurance premiums are based on fixed rate schedules, which are determined by reference to the type of investment and the types of coverage sought.117 As an example, OPIC's current base rates for coverage on oil and gas investments are as follows: for expropriation, 0.4% for development/exploration, and 1.5% for production; for political violence, 0.75%; for interference with operations, 0.4%; and for currency inconvertibility, 0.3%.118

---

115. Diacosia, supra note 109, at 275.
117. Orloff, supra note 107, at 7.
118. OVERSEAS PRIVATE INVESTMENT CORPORATION, INSURANCE RATES (ARGUM
B. MIGA

1. Background

The World Bank, a multilateral lending agency and MIGA’s parent company, was formed over forty years ago. It consists of the International Bank for Reconstruction and Development, the International Development Association, and the International Finance Corporation, as well as MIGA. MIGA entered the political risk insurance market in 1988.121 “One of its basic objectives is to increase the flow of capital and technology to developing countries . . . by complementing government-sponsored and private investment guarantee programs.”122

Many national insurance programs, due to their respective national objectives, contain strict eligibility requirements that exclude many investors and investments. In addition, national insurance programs have limited financial resources. MIGA’s insurance program overcomes some of these shortcomings and helps to fill the gaps.123 Also, because MIGA is a multilateral agency, it can insure projects for both U.S. and non-U.S. investors.

2. Risks Covered by MIGA Insurance

Like OPIC, MIGA insurance covers risks of currency inconvertibility, expropriation, and political violence. MIGA also covers breach of contract loss as a separate class of risk coverage.124 These coverages, which may be purchased individually or in combination, are discussed below.

a. Currency Inconvertibility

Currency inconvertibility insurance covers restrictions of currency transfers outside of the country that prevent the investor from transferring profits or liquidation proceeds out of the host country. Excessive delays in acquiring foreign exchange caused by host government action or inaction, by adverse changes in exchange control laws or regulations, and by deterioration in conditions governing the conversion and transfer of local currency are insured as well. On receipt of the blocked local currency from the investor, MIGA pays compensation in the currency of its guarantee. Like OPIC, currency devaluation is not covered.

b. Expropriation

Expropriation coverage protects against acts that deprive the investor of ownership or control of its investments. “Creeping” expropriation, a series of acts which, over time, have an expropriatory effect, is also covered. However, an important difference is that MIGA, unlike OPIC, excludes from this coverage non-discriminatory measures of general application which governments normally take for the purpose of regulating economic activity in their territories. Unfortunately, this exclusion can allow governments to enact “general” regulations that amount to an expropriation from the investor’s viewpoint, without the regulation being covered under the expropriation insurance.

For total expropriation of equity investments, MIGA pays the net book value of the insured investment. For partial expropriation of funds or assets, MIGA pays the insured portion of the funds or the net book value of the expropriated assets. For loans and loan guarantees, MIGA insures the outstanding principal and any accrued and unpaid interest.

c. Political Violence

War and Civil Disturbance coverage insures against losses arising from politically-motivated acts of war or civil disturbance, including revolution, insurrection, coup d’etat, sabotage, and terrorism. Compensation paid is similar to that paid in the event of expropriation. This coverage also extends to such events that, for a period of one year, result in an interruption of project operations essential to overall financial viability. This feature is effective when the investment is considered a total loss.

120. Much of the following discussion of MIGA draws on information obtained directly from MIGA, e.g. the MIGA Investment Guarantee Guide and related information supplied by MIGA. MULTILATERAL INVESTMENT GUARANTEE AGENCY, INVESTMENT GUARANTEE GUIDE (n.d.). See also Rowat, supra note 106, at 128-30, 140-44 passim; Berger, supra note 107, at 13 passim.


122. MULTILATERAL INVESTMENT GUARANTEE AGENCY, supra note 120; Rowat, supra note 106, at 127 (citing the Preamble to the MIGA Convention).

123. Shiibata, Factors, supra note 107, at 690.

124. See generally Rowat, supra note 106, at 128-29 and 141-42.
d. Breach of Contract

Breach of Contract coverage compensates investors for any breach or repudiation of a contract by the host government with the holder of a guarantee when the holder does not have recourse to another forum, or where a decision of the other forum is not available within a reasonable period of time, or where such a decision cannot be enforced.

3. Eligibility for MIGA Insurance

a. Eligible Investors

MIGA requires that the investor seeking insurance be a national of a member country other than the host country. A corporation is eligible for coverage if it is either incorporated in and has its principal place of business in a member country or if it is majority-owned by nationals of member countries.

b. Eligible Projects

Insurance may be obtained for new investments that are “economically sound,” originate in any member country, and are destined for any developing member country. New investments also include expansion, modernization, and refinancing of existing projects, reinvestment of earnings, and acquisitions that involve privatization of state enterprises. Environmental impact must also be considered. Eligible investments must be new and medium- or long-term in nature. They encompass equity investments, shareholder loans, and loan guarantees issued by equity holders, provided that the loans have a minimum average maturity of three years. Loans to unrelated borrowers can be insured, provided that equity in the project is being insured concurrently.

Other forms of investment are also eligible, including technical assistance and management contracts and franchising and licensing agreements, provided they have terms of at least three years and the investor’s remuneration is tied to the project’s operating results.

126. Eligible MIGA Member Countries. MIGA News (Multilateral Investment Guarantee Agency, Washington, D.C.), Summer 1993, at 1, 4. The newsletter states that “as of August 30, 1993, the MIGA Convention had been signed by 139 countries (20 industrialized countries and 119 category two developing countries), whose subscriptions total 97 percent of the Agency’s authorized capital. Countries listed below in italics have signed the Convention but have not yet completed all of the membership requirements.”

INDUSTRIALIZED COUNTRIES: Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, Netherlands, Norway, Portugal, South Africa, Spain, Sweden, Switzerland, United Kingdom, United States.

DEVELOPING COUNTRIES: Latin America/Caribbean: Argentina, Bahamas, Barbados, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominica, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Nicaragua, Paraguay, Peru, St. Kitts-Nevis, St. Lucia, St. Vincent, Trinidad and Tobago, Uruguay, Venezuela.

Europe/Central Asia: Albania, Armenia, Azerbaijan, Belarus, Republic of Bosnia Herzegovina, Bulgaria, Czech Republic, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Kazakhstan, Kyrgyzstan, Lithuania, Former Yugoslav Republic of Macedonia, Malta, Moldova, Poland, Romania, Russian Federation, Slovak Republic, Republic of Slovenia, Tajikistan, Turkey, Turkmenistan, Uzbekistan, Federal Republic of Yugoslavia.

Middle East/North Africa: Bahrain, Arab Republic of Egypt, Israel, Jordan, Kuwait, Libya, Morocco, Oman, Saudi Arabia, Syrian Arab Republic, Tunisia, United Arab Emirates, Republic of Yemen.

Asia/Pacific: Bangladesh, China, Fiji, India, Indonesia, Republic of Korea, Malaysia, Micronesia, Mongolia, Nepal, Pakistan, Papua New Guinea, Philippines, Sri Lanka, Vanuatu, Western Samoa.


125. See Rowat, supra note 106, at 128-30 and 140-44; Berger, supra note 107, at 29-37.
Political Considerations

Political considerations are not as important under MIGA as under OPIC. For example, there is no "human rights" standard that must be met by the host country, as is required by OPIC.

4. Terms

a. Amount of Insurance

MIGA's guarantee authority is limited to 150% of its unimpaired subscribed capital and reserves. Underwriting authority for individual investment projects is limited to 5% of MIGA's total capacity to issue guarantees. This portion amounts to a maximum coverage of approximately $50 million per project.

Insurance can be obtained for 90% of the amount invested plus up to an additional 180% for earnings attributable to the investment; an additional 90% can be obtained for interest accruing to increased principal for loans and loan guarantees.

For technical assistance and similar contracts, MIGA insures up to 90% of the total value of payments under the agreement. Regardless of the nature of the project, the investor is required to remain at risk for at least 10% of any loss.

b. Duration

The duration of insurance is from three to fifteen years. The standard term of coverage is fifteen years, and typically follows the term of the insured agreement for investments other than equity, such as a ten-year loan agreement. The term can be extended to twenty years if MIGA finds that the nature of the project "justifies" an extended term. MIGA may not terminate its coverage unless the insured investor defaults on its contractual obligations, but the insured may terminate coverage after three years or any anniversary thereafter.

c. Cost

MIGA is supposed to be self-sustaining, and its premiums are similar to OPIC's. Typical base rates for oil and gas coverage for currency inconvertibility, expropriation, breach of contract, and war risks are 0.50%, 1.25%, 1.25%, and 0.60%, respectively (as percentages of the total insured amount). Stand-by coverage is available for an additional 0.25%, 0.50%, 0.50%, and 0.25%, respectively.

d. Co-Insurance

MIGA will cooperate with both public and private political risk insurers by entering into coinsurance and reinsurance arrangements for joint coverage of eligible investment projects.

e. Application

A Preliminary Application for Guarantee should be submitted before the investment is made or irrevocably committed. Applications are treated confidentially. If MIGA determines that the investment and investor are eligible, a Notice of Registration and a Definitive Application for Guarantee are sent to the investor. There is no fee for filing either a Preliminary Application or a Definitive Application, and there is no obligation to accept a Contract of Guarantee if one is offered.

C. Private Insurance

1. Background

In the last fifteen years, private insurers have begun to offer political risk insurance that both complements and competes with government-subsidized insurance programs. This rapidly growing market is concentrated mainly in the U.S. and U.K. and has been estimated to amount to $200 to $350 million in annual premiums. The most versatile and experienced private insurer offering political risk insurance is Lloyd's

127. See e.g., Shiha, Factors, supra note 107, at 690.

128. MULTILATERAL INVESTMENT GUARANTEE AGENCY, supra note 120, at 9.

129. For further information contact:
Multilateral Investment Guarantee Agency
1818 H Street, N.W.
Washington, D.C. 20433
Telephone: (202) 473-0179 or (202) 473-6168.
Fax: (202) 477-9886.

130. Orloff, supra note 107, at 1.

131. Rowat, supra note 106, at 125 n.84.
of London. Other insurers include American International Group (AIG), Citicorp International Trade Indemnity (CITD), Professional Indemnity Association (PIA, New York), Pan Financial (London and New York), Chubb Group (New Jersey), and Poole d’Assurance des Risques Internationaux et Spéciaux (P.A.R.I.S.).

2. Risks Covered by Private Insurance

Private political risk insurance is generally divided into two categories: asset coverage and contract coverage. Asset coverage may include risks such as confiscation, nationalization, expropriation (including creeping expropriation), and repossessing of equipment. Contract coverage may include loss from contract repudiation, currency inconvertibility, and contract cancellation due to political violence. Thus, the risks covered are similar to the risks covered by government-sponsored insurance.

Of the types of risk insured against by private insurers, confiscation, nationalization, and expropriation insurance are of the most interest to energy investors. As with government-sponsored insurance, compensation is usually based upon book value. Confiscation/nationalization/expropriation insurance policies can usually be expanded to cover license cancellations, trade embargoes, strikes, riots, loss of income following expropriation, and other types of political risk. In addition, each insurer will have additional limitations and qualifications as to the amounts and types of insurance it can offer.

3. Terms

The terms offered by the private insurers are between one and three years, which are significantly shorter than those offered by OPIC and MIGA. Underwriting limits range from $5 million to $300 million per risk, depending on the insurer and the country in which the investment is located. These limits are in the same range as those of OPIC ($100 million) and MIGA ($50 million per project).

Private market fees are substantially higher than those of government insurance programs and "in some cases can be as much as seven percent for coverage in high risk countries." Lloyd’s current rate for insuring investments in the former Soviet republics is between two and three percent of the value of the investment. Premiums are based on a number of factors, including the size of the investment, nationality of the investor, risks associated with the host country, risks covered by the insurance, and the structure of the investment. Despite relatively higher rates, however, private insurance remains attractive to certain investors, such as those who fall outside the eligibility requirements of programs such as OPIC and MIGA.

Whether OPIC, MIGA, or private insurance is best suited for any particular investment can only be determined on a case-by-case basis. On the one hand, private insurance is more flexible, can be customized to meet the needs of a particular investment, can be kept in strict confidence, and can be negotiated in days rather than months. Private insurance is also not constrained by political considerations to the same degree as government-subsidized insurance. On the other hand, because OPIC and MIGA policies are government subsidized, they are generally less expensive; they can also be issued for terms of up to twenty years. Finally, OPIC and MIGA also have better facilities for covering currency risk.
inconvertibility risks than do private insurers. As between OPIC and MIGA, a decision as to which policy is best will often be based upon price and eligibility requirements.

V. CONCLUSION

Western investors seek to benefit themselves and the populace of developing countries by investing needed capital to finance production and economic growth. But unless political risks are minimized, investors will not be willing to invest their precious time and capital. Fortunately, as the world begins to gain a greater appreciation for the importance of property rights, methods are becoming available to lower political risks to allow investment to proceed.

Concessions, directly negotiated between the investor and the host state, containing stabilization and international arbitration clauses, are one method of reducing political risks; purchasing government-sponsored or even private insurance is still another. The protections won by BITs also serve to reduce the political risks inherent in foreign investment. BITs create a regime anchored in international law which is favorable, not hostile, to investment—a regime which attempts to prevent expropriation, direct or indirect, and to provide for full compensation when expropriation does occur.

Hopefully, for the sake of both investors and the developing countries, the trend towards greater protection of the property rights of investors will continue in this direction.

142. Orloff, supra note 107, at 7.