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Revitalizing the International Law Governing Concession Agreements

by
Michael E. Dickstein†

INTRODUCTION

The international law governing disputes over concession agreements¹ has been inflexible and unresponsive to the needs of the developed and developing nations. Consequently, there has not been a viable framework for resolving such disputes, and parties to concession agreements have, therefore, chosen informal mechanisms such as negotiation to settle their differences. A more flexible and responsive law of internationalized contracts would reestablish international law as an attractive means of resolving concession disputes.

Traditionally, international law left most disputes relating to concession agreements to be resolved under the domestic law of the nation granting the concession. Nonetheless, international law has become “increasingly concerned with the development and regulation of international collaboration in spheres formerly outside the field of international law.”² With these changes in the coverage of international law has come a change in the perception of what constitutes an international agreement. Originally, it was thought that such agreements could only be concluded between two sovereign states. Presently, there is a movement towards considering agreements between a sovereign state and a nonsovereign actor (generally a corporation) from another state to be international agreements. These agreements have been labeled “internationalized contracts.” The impetus for the internationalization of contracts has come from the increasing frequency with which such contracts are breached. It has also stemmed from the fact that the municipal law of the contracting state tends to serve the interests of the contracting state and to ignore the interests of the foreign contracting party.

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1. In a concession agreement, a state grants the right to exploit one of its resources. This article examines concession agreements between a sovereign state, usually a developing nation, and a nonsovereign foreign entity, usually a corporation. These concession agreements are half contract and half legislation, half treaty and half ordinary municipal contract. It is this schizophrenic nature, the result of an agreement between a state and a foreign corporation or individual, that has led to controversy about these agreements' international status. Typical of such agreements are the oil agreements between oil producing nations and multinational oil companies.

2. Friedmann, *Some Impacts of Social Organization on International Law*, 50 AM. J. INT'L. L. 475, 476 (1956).

There has been a serious rift, however, between the positions of the developed and developing nations. At one extreme, the developing nations, who are usually the states granting concessions, have advocated that disputes over such agreements are within their national jurisdiction, that international law does not apply because they have signed contracts with private parties and not other states, and that the cancellation of such contracts is a prerogative implicit in the notion of a nation retaining permanent sovereignty. At the other extreme, the developed nations, whose corporations tend to be the private contracting parties, have insisted that sovereign states must abide by their undertakings, that they must recognize that international law governs such disputes, and that they must either specifically perform their obligations or pay monetary compensation equal to the full prospective value of the contracts.

To understand the divergence in the positions of the developed and developing nations, one must examine the evolution of disputes over concessions, changes in the world economic system, and present practice in resolving concession disputes. This article briefly examines the role of multinational corporations in diminishing the sovereignty of developing nations and the response of First and Third World nations to that role. The developing nations' concept of "permanent sovereignty" is then contrasted with the developed nations' concept of alienable sovereignty. This contrast in the arguments of the developed and developing nations provides a basis for understanding the fundamental dispute as to whether concession contracts should be considered "internationalized contracts."

Using this approach, it is concluded that such contracts should be considered internationalized in order to protect best the interests of both developed and developing nations. However, the present legal doctrines applied in the area of internationalized contracts are rigid and inadequately protect the interests that justify their internationalization. Consequently, balanced and flexible international rules will have to be developed to assure the fair treatment of both contracting parties. The advantage of developing such a set of international doctrines is that it would encourage disputants to resolve their conflicts within a generally recognized framework. The existence of such a framework would also "serve a stabilizing role in the negotiation process,"³ even for those who avoid "judicial" dispute resolution mechanisms entirely.

I.

THE POSITION OF MULTINATIONAL CORPORATIONS IN THIRD WORLD COUNTRIES

Although multinational corporations are not the only foreign investors, they tend to be the most powerful ones and the only ones with sufficient assets

3. Vicuna, *The International Regulation of Valuation Standards and Processes: a Reexamination of Third World Perspectives*, in 3 THE VALUATION OF NATIONALIZED PROPERTY IN INTERNATIONAL LAW 141 (Lillich ed. & contrib. 1975) [hereinafter 3 LILLICH].

to conclude long-term concession agreements. As a result of the size and international power of multinational corporations, Third World scholars have often described them as exercising pernicious influences upon the countries in which they function.⁴ Even scholars from developed nations agree that "the extent of private economic power in the world economy is vast; many private corporations holding concession contracts are multinational enterprises that are more powerful, in fact, than the sovereign with whom they contract."⁵

Examples of the economic power of multinational corporations abound. In 1971, General Motors' annual sales exceeded the gross national products of about 130 countries.⁶ In the same year, the sales revenue of each of the big four aluminum producers exceeded the gross national income of any one of the three leading Caribbean bauxite producing nations.⁷ While these figures give some sense of the relative power of the nations and the multinational corporations with whom they deal, an examination of the multinational corporations' control over the economies of particular developing nations is even more revealing.

In examining the economy of Peru prior to its nationalization program in the 1970s, J. Huerta found that "Peru was completely dominated by foreign (primarily United States) corporations in several nationally vital industries."⁸ An Exxon subsidiary accounted for two-thirds of Peru's oil production, IT&T owned over two-thirds of Peru's utilities, Goodyear sold four-fifths of Peru's tires, and one foreign corporation alone accounted for over two-thirds of the production of zinc, lead and silver. The latter corporation was also the country's largest employer.⁹ Peru's situation was typical of that of most developing countries.¹⁰

Although it could be argued that foreign corporations were expanding Peru's economy, the Peruvian government undertook a substantial program of nationalization because it perceived Peru to be excessively dependent on those corporations. Raymond Vernon observed that developing nations will continue to feel dependent as long as they need to market their products in foreign countries and that, despite an improvement in their bargaining position vis-à-vis multinational corporations, they do not feel more secure.¹¹ He

4. *Id.* at 147.

5. Murphy, *Limitations Upon the Power of a State to Determine the Amount of Compensation Payable to an Alien Upon Nationalization*, in 3 LILLICH, *supra* note 3, at 57.

6. R. VERNON, *SOVEREIGNTY AT BAY* 7 (1971).

7. Girvan, *Making the Rules of the Game: Company-Country Agreements in the Bauxite Industry*, 20 SOC. & ECON. STUD. 378, 383 (1971).

8. Huerta, *Peruvian Nationalization & the Peruvian-American Compensation Agreements*, 10 N.Y.U. J. INT'L LAW & POL. 1, 5-6 (1977).

9. In addition, 98.3 percent of iron production was accounted for by one U.S. corporation, and two corporations were responsible for 83.7 percent of copper production. *Id.* at 6 *et seq.*

10. R. VERNON, *supra* note 6, at 24.

11. *Id.* at 9.

also found that "the basic asymmetry [of power] between multinational enterprises and national governments may be tolerable up to a point, but beyond that point there is a need to reestablish balance."¹²

However, one must keep some perspective on the connection between the penetration of the Third World nations by multinational corporations and the arguments advanced by the developing nations. To begin with, the penetration may not debilitate the host nation as seriously as one might at first assume. Vernon discovered that "there are only a few countries in the world where the subsidiaries of U.S. parents represent a dominant proportion of all enterprises in that country, whether dominance be measured by sales or assets or employment Canada is the outstanding case."¹³ To say that the Canadian government cannot deal equally with foreign corporations, or that any contract it concludes with them is concluded under duress, would be to say that even the most advanced nations cannot conclude fair contracts with multinational corporations. Hence, one cannot automatically assume that multinational corporations dominate developing nations on the basis of their penetration of Third World markets and production facilities. Figures demonstrating penetration¹⁴ are inconclusive: they may indicate dependence of the host country, vulnerability on the part of the multinational corporation, or nothing at all. The case of Canada would suggest that there are factors other than total foreign ownership or relative income of the nation and the corporation that are more important in gauging whether a contract could have been fairly formed.

Furthermore, however strong the initial position of a corporation concluding a concession agreement in a foreign country, that position usually erodes over time.¹⁵ While this phenomenon suggests that the general power of corporations in a nation's economy is somewhat overstated, it also supports the view that the original contract was obtained through duress.¹⁶

Nevertheless, in order to understand the debates occurring over concession agreements, one must constantly reconsider the perspective of the developing nations on the penetration of their economies by multinational corporations. Thus, arguments that do not seem legally rigorous or fair in a particular instance become more comprehensible in view of the general picture. For example, in the dispute between Kennecott Copper and Chile, the

12. *Id.* at 284.

13. *Id.* at 20. Vernon also points out that in the 1960s, sixty percent of Canadian manufactures were created by U.S. companies. The penetration of the Canadian market by U.S. enterprises and investment has led to much concern on Canada's part, and the figures on foreign ownership of her resources and production are in many ways as startling as those of Peru. *Id.*

14. See *supra* note 9 and accompanying text.

15. R. VERNON, *supra* note 6, at 27.

16. The strength of a corporation's position at the time of the initial negotiation of the contract, often amounting to the corporation's holding a *de facto* monopoly over that which the state requires, can be considered sufficient to amount to duress. The fact that a corporation's position deteriorates over time after the conclusion of a contract is arguably proof that the corporation could not have obtained as favorable an arrangement without duress.

success of Chile's argument that the "excessive profits" garnered by Kennecott Copper had to be subtracted from Kennecott's compensation for its expropriation in Chile would have resulted in Kennecott's receiving no compensation.¹⁷ This argument seems absurd standing on its own. But, Third World countries like Chile believe that their present situation results from the developed nations having despoiled developing nations. Hence, although a particular contract might seem equitable if one accepts the status quo, developing nations question the equity of the situation that developed nations take as a given. Chile's insistence that "excessive" profits must be subtracted from compensation is based upon its belief that international law should assess the fairness of a contract *in view of* the fairness of the status quo, rather than assess the fairness of a contract *given* the status quo.

II.

THE THIRD WORLD REACTION AND FIRST WORLD RESPONSE TO THE ROLE OF MULTINATIONAL CORPORATIONS

The Third World has rejected the current international economic order, and the laws which support it, because it serves the needs of multinational corporations and their countries of origin.¹⁸ A typical formulation of this view states that "as the international community was confined, during by far the longest period of its growth, to the Western Christian Powers, the bulk of international law, if not the whole of it, represents their common customs and traditions . . ." ¹⁹ Thus, "many developing countries . . . [are] committed to redistribution of the world's wealth" and feel that the standards applied in disputes should depend on the identity of the parties involved.²⁰ The position of the developing nations is summarized by the statement that one should "judge the actions of the Third World states on the basis of a legal standard that takes into account the presence of a continuing emergency."²¹

The Third World has acted aggressively upon its perception that there are inequities in the international legal order. Its actions have shifted the balance of interests in concession agreements in favor of host countries so that:

modern arrangements tend to support much more strongly than the old ones the developmental aims of the developing countries[;] . . . [n]ew concepts of profit sharing, technology clauses, local personnel involvement, and various

17. Seidl-Hohenveldern, *Chilean Copper Nationalization Before the German Courts*, 69 AM. J. INT'L L. 110, 111-12 (1975).

18. Girvan, *Expropriating the Expropriators: Compensation Criteria From a Third World Viewpoint*, in 3 LILLICH, *supra* note 3, at 149.

19. Roy, *Is the Law of Responsibility of States for Injuries to Aliens a Part of Universal International Law?*, 55 AM. J. INT'L L. 863, 867 (1961).

20. Neville, *The Present Status of Compensation by Foreign States for the Taking of Alien Owned Property*, 13 VAND. J. TRANSNAT'L L. 51, 60 (1980).

21. Fatouros, *International Law and the Third World*, 50 VA. L. REV. 783, 813 (1964).

other aspects of these agreements are supported by general efforts to promote the interests of developing nations on the international level.²²

Nevertheless, the Third World continues to find the situation unsatisfactory, since "what at first sight appear to be generous sacrifices of acquired rights and interests of considerable value . . . are really in most cases no more than either belated justice or overdue rectifications of past wrongs . . ." ²³ The wrongs which much of the Third World wishes to remedy through the breach of concessions extend far beyond those wrongs committed by the particular companies or countries with whom they have concession agreements.²⁴ Thus, Norman Girvan emphasized that any compensation due to multinational corporations should be "merely entered as a credit against the historic debts owed to the peoples of the Third World."²⁵ This statement amounts to a claim by the Third World of entitlement to affirmative action, since it seeks to force the corporations to pay reparations for all inequities suffered in the past by Third World nations at the hands of First World nations.²⁶

22. Dolzer, *New Foundations of the Law of Expropriation of Alien Property*, 75 AM. J. INT'L L. 553, 585 (1981).

23. Roy, *supra* note 19, at 891.

24. At the extreme, Norman Girvan complained that the "demoralizing economic impotence of the Third World peoples today in most cases can be traced back to the destructive effects of the European impact." Responding to the demands that multinational corporations be compensated, he asked "who has compensated the African peoples for the millions seized and killed in the service of the European slave trade, or for the land, cattle, and minerals expropriated by European colonization and the millions who died in the process?" Girvan, *supra* note 18, at 150.

25. *Id.* at 157. While Girvan's position is extreme, it is echoed in less severe forms by many commentators and representatives of developing nations. See, e.g., Neville, *supra* note 20, at 74; Garcia-Amador, *The Proposed New International Economic Order: A New Approach to the Law Governing Nationalization and Compensation*, 12 LAWYER OF THE AMERICAS 1, 19 (1980).

26. The problems with this form of affirmative action are even greater than those with most affirmative action programs. While, superficially, this situation seems similar to that complained of by Bakke in *Regents of University of California v. Bakke*, 438 U.S. 265 (1978) (white medical school applicant rejected in favor of minority students who, according to standardized criteria, were less qualified), where an innocent party was forced to pay for the transgressions of his predecessors, it can be distinguished.

Like the defendant in *Bakke*, a new corporation is not culpable for the past inequities for which it is often forced to pay. But, unlike *Bakke*, a new corporation has a lesser duty to ameliorate those problems. Whereas *Bakke* was a white member of, and a participant in, an organized society in which whites had discriminated, and continued to discriminate, against blacks, the new company may have had no connection with the companies that previously exploited the host country. The company is not a member of an organized international society; often the concession agreement is its only link to the developing nation.

Even if the company were considered to be a member of an organized society, the international community is far looser than American society, in terms of the responsibilities of one member to another. In addition, since the concession agreement can be the company's only link to the developing nation, using the concession agreement to derive a duty on the company's part to ameliorate a country's previous victimization would often mean that the concession agreement would be a losing proposition for the company from the day it was concluded. This would mean either that the company was engaged in a charitable venture or that the country had defrauded the company. Thus, the company should have, and does have a lesser duty than *Bakke* to ameliorate the position of the exploited party.

The Third World's demand for affirmative action explains why its position collides with that of American jurists.²⁷ The American judicial system is predicated upon the notion that particular cases will be tried upon the merits of their particular facts. Thus, previous misapplications of the law would have no effect upon its proper application to a present set of facts. In applying this principle to the termination of concession agreements, Justice Jessup wrote that, "just because practices were abused in earlier times, the rules should not be swept away as if they were 'mere cobwebs of the attics of legal history.'"²⁸ Jessup thereby reaffirmed his belief in the international legal system's ability to handle breaches in a fair manner. He did so by focusing upon the particular instance, without attempting to examine the cumulative effect of previous abuses in defining the status quo within which the present rules are applied.

In contrast, the broader Third World view encompasses action by judicial bodies which American jurists would view as more appropriately undertaken by a legislature. The Third World seeks to right old injustices and achieve a New International Economic Order by resolving individual disputes on broad policy grounds, rather than solely on the particular facts of those disputes.

Outside of the legal context, the developed nations have countered the demands of the developing nations by arguing that "a new international economic order may be a valid aspiration and a relevant goal for the future, but in economic relationships, rhetoric should not replace reality."²⁹ Economic "reality" means that "property and contractual rights have to be maintained in order to further the development of stable economic relations between the countries of the world."³⁰ Therefore, if developing nations continually breach contracts that are beneficial to corporations and nationalize effective industries, they will be harmed by curtailed investment flows.

It is unclear to what degree this theory is correct. So long as companies are convinced that there is still money to be made and that they will be allowed to make it, it does not follow that nationalization will curtail investments. Developing nations can certainly renegotiate contracts without major fears, but if they demand too much they will have problems finding investors. Whether or not companies would actually invest in countries that breached

27. The Third World approach looks to global and historical instances of oppression and dependence in evaluating any particular investment situation. Even concession agreements that are "modern and well balanced," may be breached by Third World governments. R. VERNON, *supra* note 6, at 53.

28. Jessup, *Non-Universal International Law*, 12 COLUMB. J. TRANSNAT'L L. 415, 421 (1973).

29. Von Mehren & Kourides, *International Arbitrations Between States and Foreign Private Parties: The Libyan Nationalization Cases*, 75 AM. J. INT'L L. 476, 551 (1981).

30. Domke, *Foreign Nationalizations*, 55 AM. J. INT'L L. 585, 616 (1961).

their agreements, developing nations have adjusted their behavior in response to their fear that investment might otherwise be curtailed.³¹

In summary, there are two main points of view underlying the debate over cancellation of concession agreements. The developed nations argue that one must examine the particular circumstances of each controversy within the framework of international law. The position of the developed nations is intended to bolster the present system. In contrast, the Third World contends that a New International Economic Order is required to remedy the injustices they claim to have suffered. At the extreme, the Third World position ignores the entire existing international economic order and the laws which support it. However, the Third World's need for future investment tempers this extreme position. The more moderate Third World position resembles a claim for affirmative action. This position uses traditional legal concepts in novel ways to inject arguments concerning the Third World's disadvantaged position into specific controversies with companies that are not directly responsible for their predicament. As a result, the general philosophical battle between these two viewpoints is replicated in each of the doctrinal arguments affecting concession disputes.

III.

SOVEREIGNTY TO LIMIT ONE'S OWN SOVEREIGNTY VERSUS PERMANENT SOVEREIGNTY

Both the creation and the termination of a concession agreement by a state involve exercises of sovereignty. There is, therefore, a lively debate as to which exercise of sovereign power takes precedence when they come into conflict. One of the two exercises must be preferred since the commitment to limit sovereignty, by binding oneself to abide by the terms of a contract, and the decision to terminate the contract unilaterally are contradictory. For obvious reasons, the developed nations argue that, when a sovereign commits itself not to breach an agreement, it is not alienating its sovereignty, but rather limiting its future options through the exercise of its sovereignty. The developing nations reply that sovereignty, particularly over natural resources, cannot be limited or alienated by an agreement with a corporation. They argue that a concession agreement merely expresses a present intention which the state may alter at will.

The positions of both the developing and developed nations suffer from internal flaws. The developing nations argue that a state may limit its sovereignty in an agreement with another sovereign, thus begging an inquiry as to

31. For instance, with regard to the period since nationalization, Huerta states that "in order to get economic development assistance from the capitalist world Peru has had to compromise its goal of economic independence." Huerta, *supra* note 8, at 58-9. Nonetheless, Peru nationalized a significant proportion of foreign investments and breached contracts with foreign investors without destroying its future economic prospects.

why it cannot do so with a nonsovereign entity. What appears to be a categorical position becomes more open to question. For their part, the developed nations admit that a state cannot permanently and totally alienate its sovereignty. This position leaves in question how much sovereignty can actually be alienated and why the reasons forbidding a total alienation of sovereignty³² do not apply with equal force to the case of a partial alienation of sovereignty.

A. *Alienable Sovereignty*

There are both theoretical and practical arguments in favor of the view that a sovereign has power to bind itself in a concession agreement. The theoretical argument is based upon the idea that "a basic attribute of sovereignty is that a state may make international commitments."³³ The proponents of this argument assert that "there is no legal or moral justification for a State . . . seeking to avoid its responsibilities . . . on some outworn theory that sovereignty embraces privileges only, without correlative obligations."³⁴ The practical argument was advanced in the *Revere Copper* case in which it was stated that:

under international law the commitments made in favor of foreign nationals are binding notwithstanding the power of Parliament and other governmental organs under the domestic Constitution to override or nullify such commitments. Any other position would mean in this case Jamaica could not in the exercise of its sovereign powers obtain foreign private capital to develop its resources or attract foreign industries.³⁵

Without the ability to contract, developing nations will find that they cannot achieve many of their developmental goals.³⁶ Hence, sovereignty which cannot be alienated would have little meaning, since it could not be effectively exercised.

B. *Permanent Sovereignty*

In opposition to arguments that uphold a nation's right to alienate its sovereignty stand the views of several formidable commentators and the somewhat vague pronouncements of the U.N. General Assembly supporting

32. The problems implicit in totally alienating sovereignty are similar to those of selling oneself into slavery. One cannot totally alienate sovereignty without destroying the concept of independent statehood. To exercise sovereignty in such a manner directly contradicts the very purposes for which a state's sovereign authority is intended to exercise a nation's sovereignty.

33. Von Mehren & Kourides, *supra* note 29, at 516-17.

34. Kissam & Leach, *Sovereign Expropriation of Property and Abrogation of Concession Contracts*, 28 *FORDHAM L. REV.* 177, 204 (1959-60).

35. *Revere Copper & Brass, Inc. v. Overseas Private Investment Corporation (OPIC)* (Amer. Arb. Assn. 1978) [hereinafter *Revere Copper*], reprinted in 17 *I.L.M.* 1321, 1342 (1978).

36. Garcia-Amador, *supra* note 25, at 56.

the notion of permanent sovereignty.³⁷ An example of such a pronouncement is article 2 of the Charter of Economic Rights and Duties of States. It provides that “[e]very State has and shall freely exercise full and permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities.”³⁸ The former Chief Justice of the International Court of Justice, Mr. Eduardo Jimenez de Arechaga, has asserted that the U.N. General Assembly resolutions proclaiming permanent sovereignty embody international law. He has further stated that the characterization of sovereignty as permanent “signifies that the Territorial State never loses its legal capacity to change the status or the method of exploitation of [its] resources regardless of any arrangements that may have been made.”³⁹ Thus, he concludes that “the acquired right to private property . . . is no longer protected by contemporary international law.”⁴⁰ Since the state is the sole and absolute owner of the resources within its territory, “no one person or leader of a country can contractually bind its citizens in perpetuity.”⁴¹

The immediate response of the developed nations is that this position is ridiculous and that no sophisticated economy could run on the basis of such a system. It is, however, worth remembering that the states of the United States cannot alienate their power of eminent domain in private contracts.⁴² Given this fact, it is somewhat harder to believe an argument based upon the notion that such a policy would lead to economic chaos. One should, however, consider that American expropriations tend to be far less extensive than foreign nationalizations and that the United States Constitution requires payment of “just compensation.” For these reasons, investors require less assurance in the case of United States investments than in the case of Third World investments. Thus, it may be that a developing nation’s commitments must be binding in order to give investors similar levels of assurance. Nevertheless, the American example should give some pause to those vehemently opposed to permanent sovereignty.

37. *Permanent Sovereignty Over Natural Resources*, G.A. Res. 1803, 17 U.N. GAOR Supp. (No.17) at 15, U.N. Doc. A/5217 (1962); G.A. Res. 2158, 21 U.N. GAOR Supp. (No.16) at 29, U.N. Doc. A/6316 (1966); G.A. Res. 2386, 23 U.N. GAOR Supp. (No.18), at 24, U.N. Doc. A/7218 (1968); G.A. Res. 2692, 25 U.N. GAOR Supp. (No.28) at 63, U.N. Doc. A/8028 (1970); G.A. Res. 3016, 27 U.N. GAOR Supp. (No.30) at 48, U.N. Doc. A/8730 (1972); G.A. Res. 3171, 28 U.N. GAOR Supp. (No.30) at 52, U.N. Doc. A/9030 (1973).

38. General Assembly Resolution 3281, *Charter of Economic Rights & Duties of States*, G.A. Res. 3281, 29 U.N. GAOR Supp. (No.31) at 49, U.N. Doc. A/9631 (1974), *reprinted in* 14 I.L.M. 251 (1975) (Six nations voted against, ten abstained. These sixteen nations included the seven leading trading nations.)

39. Arechaga, *State Responsibility for the Nationalization of Foreign Owned Property*, 11 N.Y.U. J. INT'L L. & POL. 179 (1978).

40. *Id.* at 181.

41. Huerta, *supra* note 8, at 10.

42. Murphy, *supra* note 5, at 57.

C. Tribunals' Decisions on Sovereignty

Despite the support for permanent sovereignty, few arbitrations or cases have taken any notice of it, except to disparage it. In 1930, the *Shufeldt Claim* found that sovereignty cannot be interposed to work unfairness to an alien,⁴³ thus gainsaying defenses based upon concepts such as permanent sovereignty. Furthermore, once the concept of permanent sovereignty had come explicitly to the fore of international discussion, it was soundly rejected in arbitrations. For example, in the 1982 arbitration between Kuwait and the American Independent Oil Co. [hereinafter *Aminoil*], it was stated that:

it has been claimed that permanent sovereignty over natural resources has become an imperative rule of *jus cogens* prohibiting states affording, by contract or by treaty, guarantees of any kind against the exercise of the public authority in regard to all matters relating to natural riches. This contention lacks all foundation.⁴⁴

In contrast, there has been a long history of arbitrations that accept the position that a sovereign may limit its sovereignty by entering into an agreement with a foreign corporation. In a submission to the arbitrators in the *Delagoa Bay Railway Case*, the United States argued that, "though the Portuguese Government had in granting the concession exercised acts of sovereignty, it had at the same time entered into an actual contract by the provisions of which it was bound."⁴⁵ The arbitrators accepted this position in finding for the United States. The case most frequently cited for this view of sovereignty is *Radio Corporation of America v. Republic of China*, which declared that "[t]he Chinese Government can certainly sign away a part of its liberty of action It will, as any other party, be bound by law and by any obligations legally accepted."⁴⁶

This view has also been supported in several more recent arbitrations involving the cancellation of concession agreements.⁴⁷ In *AGIP v. Popular Republic of Congo*, the arbitration panel held that the Congo was bound to

43. *Shufeldt Claim (Guatemala v. USA)*, 2 R. Int'l Arb. Awards 1079, 1098 (1930).

44. *Government of Kuwait v. American Independent Oil Co.* [hereinafter *Aminoil*], 21 I.L.M. 976, 1021 (1982). See also *Texaco Overseas Petroleum Co. & California Asiatic Oil Co. v. Government of the Libyan Arab Republic* [hereinafter *Topco*], 17 I.L.M. 1 (1978). The arbitrator in the *Topco* case stated:

as regards the question of permanent sovereignty, a well-known distinction should be made as to enjoyment and exercise. The State granting the concession retains the permanent enjoyment of its sovereign rights . . . the contract which it entered into with a private company cannot be viewed as an alienation of such sovereignty but as a limitation, partial and limited in time, of the exercise of sovereignty.

Id. at 26. In short, the binding of the sovereign merely meant that the enjoyment of the sovereignty was transferred from a potential to an actual form.

45. *Delagoa Bay Railway Case (U.S. v. Portugal)*, 2 J. MOORE, INTERNATIONAL ARBITRATIONS HISTORY 1865 (1898).

46. *Radio Corporation of America v. Republic of China*, reprinted in 30 AM. J. INT'L L. 535, 540 (1936).

47. In *Saudi Arabia v. Arabian American Oil Co.* [hereinafter *Aramco*], 27 I.L.R. 117 (1963), it was found that "by reason of its very sovereignty within its territorial domain, the state

follow the provisions of its contract with AGIP.⁴⁸ The arbitrators stated that, despite the right to nationalize, international law "recognizes that in concluding an international agreement with a private individual the state exercises its sovereign powers from the moment that consent is freely given."⁴⁹ The arbitrators went on to allow for a very broad alienation of sovereignty, even one lasting for an infinite amount of time, since they focused upon the sovereignty remaining to the state rather than the sovereignty given away.

Thus, international practice supports the notion that sovereigns can bind themselves in agreements with foreign private actors and denies the concept of permanent sovereignty. This is not unreasonable because international law must balance the needs of developing nations with the needs of developed nations. To accept permanent sovereignty would entirely deny the needs of the developed nations and, thereby, result in an ineffective international economic system. Instead, the developing nations have used their extreme claim that they retain permanent sovereignty as a bargaining position from which to obtain compromises from the developed nations in the evolution of other legal doctrines affecting concessions.⁵⁰

IV. THE INTERNATIONALIZED CONTRACT

Once international law recognized that a sovereign could limit its own sovereignty in a concession agreement, the next issue became the consequences of the breach of such an agreement. This issue in turn depended on the agreement's international status. The developing nations argued that such agreements were the product of a sovereign nation's municipal law and that any concessions disputes should, therefore, be governed by that law. The developed nations countered that such contracts were similar to treaties and that their breach should, therefore, be considered a breach of international law.

This disagreement was accentuated by confusion as to the relationship between the law governing concession agreements and any choice of law made in the concession agreement. The parties' choice of law cannot itself

possesses the legal power to grant concessions which it forbids itself to withdraw before the end of the concession." *Id.* at 168.

In the 1978 *Topco* arbitration, the arbitrator insisted that "a state cannot invoke its sovereignty to disregard commitments freely undertaken through the exercise of this same sovereignty." *Topco*, 17 I.L.M. at 24. The arbitrator also found that "the right to nationalize is not sufficient ground to empower a state to disregard its commitments, because the same law also recognizes the power of a state to commit itself internationally . . . with a foreign private party." *Id.*

48. AGIP v. Popular Republic of the Congo [hereinafter *AGIP*], 21 I.L.M. 726 (1982).

49. *Id.* at 735.

50. These doctrines include many affecting internationalized contracts, such as changed circumstances, duress, estoppel, and prompt, adequate, and effective compensation. As shown in the body of this article, the developing nations can moderate the effects of being bound to concession agreements through adjustments in these doctrines.

create an internationalized contract, since the "human will can only create a contractual relationship if the applicable system of law has first recognized its power to do so."⁵¹ Thus, one must decide what source of law creates the power to contract before determining the effect of the parties' choice of law. It is this question of background law, and not the subsequent question of what laws will be used in the interpretation of contractual clauses, that is examined in determining whether a contract is internationalized. Thus, the controversy as to internationalization of contracts is actually a controversy as to governing law.⁵²

A. *The Evolution of Internationalization*

It is only recently that international law has been considered to govern concession agreements. In 1929, in the *Serbian Loans* case, the Permanent Court of International Justice [hereinafter PCIJ] found that "[a]ny contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country."⁵³ Commentators also concluded as late as 1974 that contracts, "as a general rule, will be governed by the internal law of the host state"⁵⁴ and that it is "unquestionable in light of traditional international law" that concession agreements are governed by the domestic law of the host state.⁵⁵

While historically it has been found that many concession contracts are governed by the municipal law of the host state and this approach continues to be approved by some commentators, an increasing body of contracts are being found by tribunals to be internationalized. Many of these cases find their roots in the *Lena Goldfields, Ltd.* arbitration.⁵⁶ In 1925, the Soviet Union granted a mining and transportation concession to Lena Goldfields, Ltd. The Soviet Union interfered with the contract such that performance by Lena Goldfields, Ltd. became impossible. The arbitrator took the view that,

51. *Aramco*, 27 I.L.R. at 165.

52. Nonetheless, some arbitrations have relied upon an agreement's choice-of-law clause in which the parties have chosen either the "general principles of law" or "international law" as an indication of the internationalization of the contract. *Topco*, 17 I.L.M. at 15. While this approach appeals to common sense, it is open to misinterpretation. If the parties' choice determines the law governing, see Geiger, *The Unilateral Change of Economic Development Agreements*, 23 INT'L & COMP. L.Q. 73, 80 (1974), then what system gives the parties the power to make that choice? If the choice-of-law provision is considered to be merely one of many indicators of internationalization, important because of its reference to the international world, but not because of its command that international law be used, one arrives at a more cogent system. In this view, it is the reference to non-municipal concerns, a reference that would be equally important in any clause of the contract, which helps in the determination of whether a contract has been internationalized.

53. *Case of Serbian Loans (France v. Serbs)*, 1929 P.C.I.J. (ser. A) No. 20/21, at 41 (Judgment of July 12).

54. Geiger, *supra* note 52, at 80.

55. Garcia-Amador, *supra* note 25, at 55.

56. *Lena Goldfields Ltd.*, 5 Ann. Dig. 3 (Special Arbitral Tribunal 1930).

while Soviet law governed the day to day performance of the contract, "general principles of law" must be used to decide more fundamental issues.⁵⁷ The 1963 *Aramco* arbitration followed the example set in the *Lena Goldfields, Ltd.* arbitration, declaring that "[t]he Concession Agreement is thus the fundamental law of the Parties" and "[i]n so far as doubts may remain . . . it is necessary to resort to the general principles of law."⁵⁸

The 1967 *Sapphire* arbitration found that "[t]hese concessions give the contract a particular character, which lies partly in public law and partly in private law" and "[t]his contract has therefore a quasi-international character which releases it from the sovereignty of a particular legal system."⁵⁹ The 1978 *Topco* case went further still, explicitly rejecting the position of the PCIJ in *Serbian Loans* as outdated⁶⁰ and insisting that "the legal order from which the binding nature of the contract derives is international law itself."⁶¹ Thus, a line of cases is developing which embraces the concept of an internationalized contract and rejects the position declared in *Serbian Loans*. Recently, the *Revere Copper* decision followed this line of cases. It relied heavily on the *Topco* decision to reach the conclusion that the concession agreement in the case was internationalized and that international law principles were thus applicable.⁶²

57. *Id.* One commentator strongly opposed this view, insisting that "[t]here can be little doubt that the legal consequences of a contract establishing a concession in Soviet territory and under control of the Soviet Government are determined by Soviet law." Nussbaum, *The Arbitration between the Lena Goldfields, Ltd. and the Soviet Government*, 36 CORNELL L.Q. 31, 36 (1950-51). This view, however, appears to have had little effect on the development of international law in this area.

58. *Aramco*, 27 I.L.R. at 168. The arbitrator in *Aramco* rejected international law as the governing law, *id.* at 165, and chose instead the "general principles of law." Although the reasoning of the case is somewhat confused, it has been used in several subsequent decisions as a strong precedent for rejecting municipal law.

59. *Sapphire International Petroleum Ltd. v. National Iranian Oil Co.* [hereinafter *Sapphire*], 35 I.L.R. 136, 171, 173 (Cevin, Sole Arbitrator 1963).

60. *Topco*, 17 I.L.M. at 12.

61. *Id.*

62. *Revere Copper*, 17 I.L.M. at 1338; see also *Sapphire*, 35 I.L.R. at 175-76. The *Topco* and *Revere Copper* cases depended upon similar examinations of the contracts to discover whether they should be internationalized. In *Topco*, the choice-of-law and arbitration clauses were examined in order to discern whether they had a non-municipal character. *Topco*, 17 I.L.M. at 15-16. In addition, the contract was found to be an "Economic Development Agreement" because it invoked a broad subject matter, the bringing of techniques and investments to the host country, a long duration, and the necessity of a cooperative relationship between the parties. *Id.* at 16-17. Finally, the arbitrator found that there is a presumption that Economic Development Agreements are internationalized. *Id.*

In *Revere Copper* these criteria were explicitly followed, 17 I.L.M. at 1335, and the arbitrator reiterated that there is a presumption that Economic Development Agreements should be internationalized. *Revere Copper* also pointed to the different nationalities of the parties and the enticement of the host country as further support for a finding that the concession agreement was an Economic Development Agreement. *Id.* These definitions are sufficiently broad to cover most concession agreements concluded by developing nations.

Given an increasing trend towards internationalizing concession contracts, there remains the question as to whether or not this is a reasonable development.

B. *The Reasonableness of Internationalization*

The first objection to the internationalization of concession agreements involves the inequality of the contracting parties. Third World scholars have claimed that the two parties are not equal and that considering a contract internationalized would mean that "corporations would receive nothing more or less than the treatment which should be reserved solely for States."⁶³ Furthermore,

if international law governed a contract between a State and an alien, it could only govern the obligations of the State and not the obligations of the alien, for international law does not operate on the individual directly It would clearly be inequitable to subject the State to the regime of international law in the performance of its obligation under a contract, while leaving the obligation of the alien to the domain of municipal law. . . .⁶⁴

Yet, since the power of multinational corporations puts them on a par with many nations,⁶⁵ "[t]he transnational corporation must be regarded as a political, and not just an economic, actor in international politics."⁶⁶ Hence, the two parties are often no less equal in their relative strengths than any two states. The notion that, since corporations and individuals are not bound by international law, applying international law to concession agreements would be unfair, is circular: it assumes individuals and corporations are not bound by international law as a first step in attempting to prove that international law should not be applied to them. The very point of internationalizing a contract is to see that both parties are bound by a legal system they do not control. This led the arbitrator in the *Topco* case to avoid the circularity by stating that the individual may "invoke in the field of international law, the rights which he derives from the contract" and, therefore, is a party with "specific international capacities."⁶⁷ The notion that, for the purposes of concession agreements, states and individuals are equal is also bolstered by U.N. General Assembly Resolution 1803, which states that "investment agreements freely entered into by or between sovereign States shall be observed."⁶⁸ By stating "by or between," the Resolution makes it clear that it considers contracts with individuals equally binding as those with states.

63. Garcia-Amador, *supra* note 25, at 42; see also Arechaga, *supra* note 39, at 189.

64. C. AMERASINGHE, STATE RESPONSIBILITY FOR INJURIES TO ALIENS 69 (1967).

65. See *supra* section I.

66. Bock & Fuccillo, *Transnational Corporations as International Political Actors*, 10 *STUD. COMP. INT'L DEV.* 51, 74 (1975).

67. *Topco*, 17 *I.L.M.* at 17.

68. General Assembly Resolution 1803, *supra* note 37.

A second objection, similar to the first, is that a concession agreement "is not a treaty and cannot involve state responsibility as an international obligation."⁶⁹ The International Court of Justice [hereinafter ICJ] decision in the *Anglo-Iranian Oil* case⁷⁰ is most often cited to support this proposition, and many consider it fatal to the arguments in favor of the internationalization of contracts. This view is mistaken. It is true that the ICJ decided that a concession agreement was not a "treaty." It is not true, however, that the ICJ concluded that, as a result, there could be no international responsibility on the part of a nation which signs a concession agreement or that concession agreements were therefore governed by municipal law. The ICJ was not required to decide the international status of concession agreements because Iran had submitted to the ICJ's jurisdiction under a very limited set of circumstances. The court had jurisdiction to resolve controversies arising from "the application of a treaty or convention accepted by Iran."⁷¹ Since the ICJ decided the concession agreement was neither a "treaty" nor a "convention," it declared itself lacking jurisdiction. Thus, the *Anglo-Iranian Oil* case does not support the proposition that concession agreements are not governed by international law.

While concession agreements are not treaties, they do have an international character, and their breach arguably leads to a violation of international law.⁷² Their similarity to treaties is far greater than their similarity to municipal contracts. In both treaties and concession agreements, "promises with an international scope, or of an international flavor, are made; in both cases, reliance is placed on those promises; in both cases, the obligation to perform those promises should be the same."⁷³ In addition, distinguishing between treaties and concession agreements favors state trading nations,⁷⁴ whose concession agreements are concluded by the state and are, therefore, considered treaties.⁷⁵ Finally, the corporation's state often takes an active part in the negotiation and execution of foreign contracts,⁷⁶ and the contract itself may be the most important document governing the relationship between the corporation's state and the host state. A document with such important international repercussions should be recognized as having an international status.

A third objection to internationalizing contracts is that municipal law should govern a concession because the concession is an act of government.

69. I. BROWNLIE, *PRINCIPLES OF PUBLIC INTERNATIONAL LAW* 551 (3d ed. 1979).

70. *Anglo-Iranian Oil Case* (U.K. v. Iran), 1952 I.C.J. 93 (July 22, 1952).

71. *Id.* at 103.

72. Schwebel, *International Protection of Contract Arrangements*, 53 AM. SOC'Y INT'L L. PROC. 266 (1959).

73. Kissam & Leach, *supra* note 34, at 209.

74. Those nations whose governments own and control substantially all of the nation's companies.

75. Schwebel, *supra* note 72, at 268.

76. *Id.* at 267.

This position, principally supported by the USSR,⁷⁷ ignores the fact that the concession agreement is also half private contract. In addition, a treaty, like a concession agreement, results from an act of government. Since the domestic legislation which implements a treaty does not render its breach a question for municipal law, the Soviet analysis does not resolve the question of whether municipal or international law should govern a concession contract.

Several factors favor internationalizing contracts. One such factor is that a foreign subject cannot be sure of impartial treatment when it is suing the sovereign of the country in which its case is being tried—particularly when its suit opposes a major initiative of the sovereign. The reason for this is that the decision to breach, as well as related pronouncements, is usually a part of the municipal law applicable to the case. Also, “a municipal court will comply with an order embodied in municipal law, either on account of the pressure exerted on it by the power of the state or out of respect for the national law, which at the present juncture is often greater than that for international law.”⁷⁸ Therefore, it is generally agreed that no state should be the judge in its own case.⁷⁹ While internationalizing a contract under international law does not by itself keep a case from being heard by a municipal court, it does mean that the court should apply the rules of international law. If the court does not apply international law, this failure will be redressable at the international level.⁸⁰

A second factor favoring internationalizing concession agreements is that doing so enhances the uniformity of the international economic system.⁸¹ This is particularly true given that many countries “have not yet embodied in their systems of municipal law features that are pertinent to legal arrangements for modern economic development.”⁸² In the *Aminoil* arbitration, the finding went so far as to say that it is on the unification and internationalization of the laws governing concessions “that the future of a truly international economic order in the investment field will depend.”⁸³

77. Sapozhnikov, *Neocolonialistic Doctrines of International Protection of Foreign Concessions*, 1966-7 SOVIET Y.B. INT'L L. 90, 98 (1968); Vilkov, *Nationalization and Internationalization Law*, 1960 SOVIET Y.B. INT'L L. 58, 77 (1961).

78. Kollwijn, “Nationalisation” *Without Compensation and the Transfer of Property*, 6 NEDERLANDS TIJDSCHRIFT VOOR INTERNATIONAL RECHT 140, 149 (1959).

79. Von Mehren & Kourides, *supra* note 29, at 533.

80. While a sovereign can never be forced to follow international law and a sovereign can always pass legislation contrary to international law, both these actions can be redressed internationally. See *supra* note 35 and accompanying text.

81. “Agreements between States and individuals of other States should also be performed under the only rules that can insure predictability of result — and those are the rules of international law.” Kissam & Leach, *supra* note 34, at 209. Nonetheless, while such unification and internationalization favor stability and overall growth, they do not address the concerns of the Third World. The developing nations are dissatisfied with the present economic situation and the legal order that protects it. Consequently, they would be glad if the system were less stable and entrenched, particularly if that would give them a greater degree of self-determination.

82. Domke, *supra* note 30, at 596.

83. Government of Kuwait v. American Independent Oil Co., 21 I.L.M. at 1001.

These arguments favoring internationalization would be more attractive to all states if each state was as likely to conclude a contract with a foreign corporation as one of its corporations was to conclude a contract with another state. Internationalization would bolster the consistency of the international economic system, would focus upon the international character of concession agreements, and would avoid the unfairness of having the injured party judged by the party against whom its complaint lay. Nonetheless, developing nations tend to oppose internationalizing contracts because they know that they will be the states directly involved in concession agreements and that applying their own municipal law will benefit them.

Despite the objections of the Third World, the doctrine of the internationalized contract has gained acceptance in recent arbitrations. This reflects the fact that the interests of the developed nations were being badly injured under the laws of host states and that developing nations are not hurt by the internationalization of contracts, rather they are hurt by the doctrines applied to internationalized contracts. Although developed nations have gained some ground through greater acceptance of the doctrine of internationalized contracts, if they wish to maintain a system acceptable to the developing nations, they will be forced to compromise on the content of the international doctrines applied to those contracts.

V.

THE INTERNATIONAL LIABILITY DOCTRINES TO WHICH INTERNATIONALIZED CONTRACTS COULD BE SUBJECT

A. *Pacta Sunt Servanda*

1. *General Application of the Doctrine*

Pacta Sunt Servanda means that obligations undertaken shall be fulfilled. The Vienna Convention of Treaties expresses it as “[e]very treaty in force is binding upon the parties to it and must be performed by them”⁸⁴ There has been a good deal of argument as to whether this rule should be applied to concession agreements as well as treaties.

The 1958 resolutions of the International Bar Association stated that “the principle of *Pacta Sunt Servanda* applies to the specific engagements of States towards . . . the nationals of other States” while the resolutions of the International Law Association affirmed that the “parties to a contract between a State and an alien are bound to perform their undertakings in good faith.”⁸⁵ In 1962, the U.N. General Assembly passed Resolution 1803 which restated the rule of *Pacta Sunt Servanda* and applied it to agreements between states and individuals. The Resolution stated that “[f]oreign investment

84. Vienna Convention on the Law of Treaties, May 22, 1969, art. 26, 1155 U.N.T.S. 331, reprinted in 8 I.L.M. 679, 690 (1969).

85. Domke, *supra* note 30, at 598.

agreements freely entered into by or between sovereign States shall be observed in good faith"⁸⁶ Commentators have supported this position with categorical statements such as "international contracts are as binding as treaties between states"⁸⁷

Not surprisingly, many of the arbitrations which favored internationalizing contracts also favored applying *Pacta Sunt Servanda*. The *Sapphire* arbitration found that "[t]he rule *Pacta Sunt Servanda* is the basis of every contractual relationship."⁸⁸ Each of the arbitrations stemming from the Libyan oil nationalizations confirmed "the basic tenet that states cannot disregard duties to foreign private persons."⁸⁹ In particular, the arbitrator in the *Libyan American Oil Company* [hereinafter *Liamco*] arbitration⁹⁰ found that the "principle of the respect for agreements is thus applicable to ordinary contracts and concession agreements. It is binding on individuals as well as governments."⁹¹ The arbitrator in *Topco* wrote that the "*maxim pacta sunt servanda* should be viewed as a fundamental principle of international law,"⁹² hence "where the state has concluded an international contract with a foreign contracting party, the state is bound by the international legal order to recognize the terms and conditions of that agreement."⁹³

However, the cases and commentators are far from unanimous in their support of applying *Pacta Sunt Servanda* to concession agreements.⁹⁴ In cases that opposed internationalizing contracts, the tribunal did not reach the *Pacta Sunt Servanda* question. Also, arbitrators who held that a contract should be internationalized would usually support *Pacta Sunt Servanda*. Consequently, it is hard to find cases directly opposing the application of *Pacta Sunt Servanda*. In *The Unilateral Change of Economic Development Agreements*, Geiger finds that "[t]o insist on the absolute sanctity of concession agreements . . . seems to be nothing else than a more subtle form of colonialism."⁹⁵ There are also criticisms that *Pacta Sunt Servanda* interferes intolerably with sovereignty.⁹⁶

86. General Assembly Resolution 1803, *supra* note 37.

87. Schwebel, *supra* note 72, at 273.

88. *Sapphire*, 35 I.L.R. at 181.

89. Von Mehren & Kourides, *supra* note 29, at 513.

90. *Libyan American Oil Company v. Government of the Libyan Arab Republic* [hereinafter *Liamco*], 62 I.L.R. 140 (Mahmassoni, Sole Arbitrator 1977).

91. Von Mehren & Kourides, *supra* note 29, at 519.

92. *Topco*, 17 I.L.M. at 19.

93. Von Mehren & Kourides, *supra* note 29, at 516.

94. Even the Restatement of the Foreign Relations Law of the United States, which tends to represent the position of the developed nations, has decreased its support for strict adherence to concession agreements (*Pacta Sunt Servanda*). Compare RESTATEMENT (SECOND) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 and comment h, at 119-25 (Tent. Draft No. 7, 1987) with Tentative Draft No. 3, at 193 (1982).

95. Geiger, *supra* note 52, at 102. Geiger proposes that concessions be made subject to a state's prerogative of unilateral modification in the public interest.

96. Sapozhnikov, *supra* note 77, at 98-99.

Whatever the significance of *Pacta Sunt Servanda* in legal theory, the state practice of renegotiating concession agreements calls into question the doctrine's practical importance. Although corporations may once have anticipated that their contracts with foreign governments would be observed, they can no longer have the same expectation.⁹⁷ This is largely because "[e]conomic development agreements cannot be understood as a rigid scheme of rights and duties, but rather as a frame of reference for future relations. They are of prospective character and therefore must provide a certain degree of flexibility."⁹⁸ The foreign corporation is at the height of its power vis-à-vis the host state when it first signs the concession agreement. Over the course of time, however, as the corporation invests more in the host state, and as the host state develops the independent capacity to perform the work done by the corporation, the position of the corporation deteriorates.⁹⁹ In addition, as failing projects disappear and as only successful ventures remain, "[t]he returns to the foreign company no longer seem appropriate to the risk, and the government feels justified in demanding more out of the project."¹⁰⁰ As a result of these changes and the long duration of concession agreements,¹⁰¹ they tend to be renegotiated several times over their lifespan.

The Kuwait/Aminoil agreement was renegotiated twice during the twenty-nine years it was in force, the first time after thirteen years and the second time after twenty-five years.¹⁰² The agreement was then terminated thirty-one years before it was due to expire. During the eighteen years it was in force, the Libya/Topco agreement was renegotiated after seven, ten, fourteen, and fifteen years.¹⁰³ It was terminated thirty-two years prior to its expiration date. What these figures indicate is that a corporation would be foolish to expect its concession agreements to be strictly followed. Assuming that corporations are aware of this when they contract, and that they take full advantage of the strength of their positions while negotiating contracts to create very one-sided agreements, it does not seem unreasonable that concession agreements should be open to periodic renegotiation. This is particularly true given their long duration.

97. R. VERNON, *supra* note 6, at 46.

98. Geiger, *supra* note 52, at 104.

99. *Id.* at 76.

100. R. VERNON, *supra* note 6, at 48.

101. The Lena Goldfields Ltd. concessions (signed 1925) were to last thirty and fifty years. Nussbaum, *supra* note 57, at 45. The Aminoil concession (1948) was to last sixty years. *Aminoil*, 21 I.L.M. at 990. The Revere Copper agreement (1967) was to last twenty-five years. *Revere Copper*, 17 I.L.M. at 1323. The Aramco concession (1933) was to last sixty years. *Aramco*, 27 I.L.R. at 118. The Topco concession (1956) was to last fifty years. *Topco*, 17 I.L.M. at 24. Finally, for bauxite concessions, Girvan found the average concession to cover between twenty-five and seventy-five years, with an average duration of forty-one years. Girvan, *supra* note 7, at 413. Despite the long duration, Girvan claims that it rarely takes longer than ten years for the company to recover its capital. *Id.* Thus, the renegotiations serve to redistribute a surplus of profit over cost between the corporation and the state.

102. *Aminoil*, 21 I.L.M. at 1021.

103. *Topco*, 17 I.L.M. at 4.

This leaves the problem of how to match the international standard of *Pacta Sunt Servanda* to the reality that these agreements are constantly renegotiated. If international law is to be applied to concession agreements, it must be practical in its application. One way to bridge the gap between law and practice is demonstrated by the *Aminoil* arbitration which found that the constant renegotiation of the concession agreement belied the application of *Pacta Sunt Servanda*.¹⁰⁴ The arbitrator based this finding on two grounds. First, it would not make sense to start suddenly enforcing the letter of the contract. Second, one would have difficulty deciding which form of the contract should be absolutely enforced. Another way of bridging the gap between law and practice would be to develop a more flexible body of international law intended to deal with concession disputes.¹⁰⁵ The final way to bridge the gap between law and practice would be to temper the strictures of *Pacta Sunt Servanda* with the doctrine of *Rebus Sic Stantibus*.¹⁰⁶

Barring a change in the nature of concession agreements that causes them to be of shorter duration and more equitable in their original distribution of profits, the gap between law and practice will not be closed by attempting to apply *Pacta Sunt Servanda* strictly. In addition, even if the original distribution of profits is equitable, the developing nations will continue to feel a sense of dependence. Consequently, a developing nation might not accept the original profit distribution, regardless of its fairness, as the developing nation's relative power increased with the progression of the contractual relationship. In short, *Pacta Sunt Servanda* is not a doctrine flexible enough to be useful in resolving concession disputes.

2. *The Effect of Stabilization Clauses*

In response to the developing nations' challenge to *Pacta Sunt Servanda*, developed nations began to insist that stabilization clauses be inserted in agreements. Stabilization clauses are intended to bind a sovereign to abstain from cancelling or interfering with an agreement.¹⁰⁷ The effect of such clauses has been disputed. Some commentators have argued that "[w]here a state . . . by special contractual arrangements . . . with foreign individuals or companies, has undertaken to protect them against expropriation or other

104. *Aminoil*, 21 I.L.M. at 1024.

105. See *infra* section V(C)(3) on estoppel.

106. See *infra* section V(B) on *Rebus Sic Stantibus*.

107. An example of a stabilization clause can be found in the agreement that was the subject of the *Sapphire* arbitration. It stated that "no general or special statutory enactment, no administrative measure or decree of any kind . . . can cancel the agreement or affect or change its provisions, or prevent or hinder its performance. No cancellation, amendment or modification can take place except with the agreement of the two parties." *Sapphire*, 35 I.L.R. at 140. Similar clauses are included in most modern concession agreements, see, e.g., *Topco*, 17 I.L.M. at 4; *Revere Copper*, 17 I.L.M. at 1323, and in some bilateral investment treaties; see, e.g., *Reciprocal Encouragement and Protection of Investments*, September 29, 1982, United States-Egypt, art. III(e), reprinted in 21 I.L.M. 927, 935 (1982).

forms of interference with property, a breach of such undertaking will be clearly an international delinquency."¹⁰⁸ Others have argued that:

in international law the express exemption from the effects of future legislation is redundant. Such exemption cannot and ought not to preclude the genuine exercise of the state's police power. On the other hand, where, in substance, the state takes property without compensation, its international liability is engaged even in the absence of the [stabilization] clause.¹⁰⁹

Although arbitral tribunals have found that stabilization clauses either render concession agreements binding¹¹⁰ or require full compensation for their breach,¹¹¹ there is little theoretical support for these positions. There is no reason that stabilization clauses should be any more binding than any of the surrounding clauses. If states have the power to bind themselves in concession agreements, then stabilization clauses are unnecessary to bind them. If states retain permanent sovereignty and cannot bind themselves in concession agreements, then, for the same reasons, they cannot bind themselves to stabilization clauses.

The only response to these objections is that a stabilization clause provides the contracting parties with notice of their obligations, and thereby further binds them. This is not a sound response. States are assumed to be knowledgeable and competent contracting parties,¹¹² and implicit in the notion of a contract is the fact that it is binding upon both parties. Finally, the view that stabilization clauses are binding is as inflexible as the doctrine of *Pacta Sunt Servanda*.

B. *Rebus Sic Stantibus*

Many commentators have suggested that applying the treaty doctrine of *Rebus Sic Stantibus* to concession disputes would soften the harsh effect of employing *Pacta Sunt Servanda*. *Rebus Sic Stantibus* is the doctrine which

108. Friedmann, *supra* note 2, at 505; see also Weil, *Les Clauses de Stabilisation ou D'Intangibilité Inserées Dans les Accords de Développement Economique*, in *MÉLANGES OFFERTS A CHARLES ROUSSEAU* 301 (1974).

109. Mann, *State Contracts and State Responsibility*, 54 *AM. J. INT'L L.* 572, 587-88 (1960); see also Sornarajah, *Compensation for Expropriation: The Emergence of New Standards*, 13 *J. WORLD TRADE L.* 108, 122 (1979).

110. In the *Liamco* and *Topco* arbitrations, it was found that stabilization clauses "have been considered as legally binding under international law." Von Mehren & Kourides, *supra* note 29, at 520. The *AGIP* arbitration followed this position finding that "changes in the legislative and regulatory arrangements stipulated in the agreement simply cannot be invoked against the other contracting party" where the two parties have included a stabilization clause in their contract. *AGIP*, 21 *I.L.M.* at 736.

111. In the *Aminoil* arbitration it was found that:

[t]he effect of the stabilisation clause is not to fetter the ability of the host State to expropriate, but it does mean that any expropriation being a breach of 'the international law of contracts' will cost the host State more. The measure of compensation will be the full measure of the investor's loss

White, *Expropriation of the Libyan Oil Concessions - Two Conflicting International Arbitrations*, 30 *INT'L & COMP. L.Q.* 1, 16 (1981); see also Arechaga, *supra* note 39, at 192; Geiger, *supra* note 52, at 103.

112. See *infra* section V(C)(1) on duress.

allows for the termination of a treaty when there has been a fundamental change in the circumstances underlying the treaty.¹¹³ An important aspect of the doctrine is that it focuses upon changes that would contradict the "parties' shared expectations" and thereby "defeat their apparent objectives."¹¹⁴ This means that arguments dependent upon a change in the world's view of the exploitation of the developing nations, or upon the shift of power from the corporation to the host nation during the life of a concession, do not fit within *Rebus Sic Stantibus* since these changes do not affect the parties' original expectations or objectives.

The developing nations strongly disagree with this traditional definition of *Rebus Sic Stantibus*. They would define it much more broadly. They mock the piousness with which the developed nations insist upon the fulfillment of obligations¹¹⁵ and believe that changes in the understanding and power of the developing nations alone justify the abrogation of concession agreements.

However, neither loss of expected profit nor profound economic hardship has been considered sufficient to constitute an exception to *Pacta Sunt Servanda*.¹¹⁶ Even the Soviets, whose political philosophy is based upon overturning entrenched property rights, do not consider a change in economic circumstances sufficient excuse for breach. The Soviet tribunal in charge of trade disputes "applies the principle of strict observance by the parties of the contractual obligations which they have assumed, independent of the economic hardship of performance resulting as a consequence of change of circumstances"¹¹⁷

Another common event which is not considered sufficient to warrant the application of *Rebus Sic Stantibus* is a change of government or government policy.¹¹⁸ In fact, tribunals have even held that "the rights which a private company derives from a deed of concession cannot be nullified or affected by

113. See, e.g., article 62 of the Vienna Convention on the Law of Treaties which mandates that "a fundamental change" 1) "not foreseen by the parties"; 2) in circumstances which "constituted an essential basis of the consent of the parties"; and 3) the effect of which was "radically to transform the extent of obligations" must have occurred in order to implicate the doctrine of *Rebus Sic Stantibus*. Vienna Convention on the Law of Treaties, *supra* note 84, at 702.

114. Lissitzyn, *Treaties and Changed Circumstances*, 61 AM. J. INT'L L. 895, 896 (1967).

115. S. Roy, a former judge of the High Court of Calcutta, writes:

the history of the establishment and consolidation of empires overseas by some of the members of the old international community and of the acquisition therein of vast economic interests by their nationals teems with instances of a total disregard of all ethical considerations. A strange irony of fate now compels those very members of the community of nations on the ebb tide of their imperial power to hold up principles of morality as shields against the liquidation of interests acquired and held by an abuse of international intercourse.

Roy, *supra* note 19, at 866.

116. Kissam & Leach, *supra* note 34, at 204.

117. Armstrong, *Soviet Contract Law*, 31 AM. J. COMP. L. 63, 94 (1983).

118. A. McNAIR, *THE LAW OF TREATIES* Ch. 41 (1961); 1 OPPENHEIM, *INTERNATIONAL LAW* 925 (H. Lauterpacht 8th ed. 1955); Geiger, *supra* note 52, at 86.

the mere fact of a change in the nationality of the territory."¹¹⁹ Given that a change in the nationality of a territory is insufficient to justify the application of *Rebus Sic Stantibus*, it is not surprising that a change in the party in power, or even a revolutionary change in the form of a state's government, is also considered insufficient by most commentators.

Nonetheless, there is a growing movement that holds the belief that a change in government should allow a change in policies and commitments, in conjunction with the belief in permanent sovereignty over resources. Former ICJ Chief Justice Arechaga typified this position in stating that "contemporary international law recognizes the right of every state to nationalize foreign-owned property, even if a predecessor state or a previous government engaged itself . . . by contract not to do so."¹²⁰

Several commentators have specifically considered the effect on a concession agreement of a host state's change in government from colonial to non-colonial status. Most have examined the change in terms of its effect upon compensation after a breach by the independent state. It has been argued that "since the host State was not a free and independent agent at the time the contract or concession was entered into, it should not be subject to the payment of full compensation."¹²¹ The argument that fundamental changes should diminish compensation to be paid is the same as that which says changes should mitigate breach. As a corollary to allowing the change from colonial status to mitigate the breach of colonial agreements, it has been proposed that a greater degree of protection should be afforded post-colonial agreements and that this should be done to encourage investment without validating the acts of colonial regimes.¹²²

An increasing number of commentators have accepted the developing nations' view that changes in the general circumstances and understanding of developed and developing nations fit under the doctrine of *Rebus Sic Stantibus*. However, this inclusion has not been accepted, or even widely considered, by tribunals. Tribunals have narrowly interpreted *Rebus Sic Stantibus* to require a fundamental change in the circumstances surrounding a particular contract. *Rebus Sic Stantibus* has been examined both as an argument to

119. Sopron Kozseg Local Railway Co. Case, 5 Ann. Dig. 57 (Trib. of the League of Nations 1929); see also *German Settlers in Poland*, (Adv. Op.) 1923 P.C.I.J. (ser. B) No. 6, at 35-36 (Sept. 10).

120. Arechaga, *supra* note 39, at 179.

121. C. AMERASINGHE, *supra* note 64, at 119; Muller, *Compensation for Nationalization: A North-South Dialogue*, 19 COLUM. J. TRANSNAT'L L. 35, 45 (1981).

122. Lillich, *The Valuation of Nationalized Property in International Law: Towards a Consensus or More "Rich Chaos"?*, in 3 LILlich, *supra* note 3, at 199. A dissenting viewpoint holds that since the expectations of the parties should govern the contract, and the expectations of multinationals were higher under colonial regimes, it is colonial contracts that should be given the most protection and yield the most compensation upon breach. See Dolzer, *supra* note 22, at 580. On its face, this position seems less acceptable, since it does not grant any recognition to the viewpoint of the developing nations. In addition, it does not recognize the coerced position of a nation under colonial rule nor the major alteration in structure that occurs upon the independence of the developing nation.

insure a fair return on a company's investment,¹²³ and as an argument to insure a state not be held by the commitments of a previous government.¹²⁴ In neither case did the tribunal accept it.

In fact, no international tribunal up through 1981 had ever relied on *Rebus Sic Stantibus*, either in cases involving treaties or concession agreements.¹²⁵ R. von Mehren, in his article on arbitrations between states and foreign private parties, wrote "*Rebus Sic Stantibus* is now generally accepted as a very limited rule applicable to the international law of treaties. If it applies to international contracts at all, its application would be even more limited."¹²⁶

Part of the reason that change of circumstances has been ineffectual on the international level as a defense to breach has been the fact that a state is one of the contracting parties. In general, "[a]lthough parties operating in a domestic setting often conclude contracts casually . . . international contracts are generally drafted quite carefully and with attention to the variety of risks."¹²⁷ The state, in particular, has the resources and expertise to ensure a careful and well-reasoned decision.¹²⁸ While this care cannot eliminate all unforeseeable events, it can lessen the number of events considered to be unforeseeable. The other reason that international tribunals do not accept change of circumstances as a defense is that to do so would disturb the international trading system by introducing uncertainty into investments.¹²⁹

The application of *Rebus Sic Stantibus* suffers from the same problems as the application of *Pacta Sunt Servanda*. Both are all-or-nothing doctrines which yield results that are absolute. Consequently, tribunals have attempted to avoid the inflexibility of such doctrines by declaring them inapposite. As an example, one arbitration found that the renegotiation of a concession agreement had reaffirmed it. Thus, the tribunal was freed from the need to consider whether *Rebus Sic Stantibus* applies to concessions.¹³⁰ The parallel between this decision and the decision that *Pacta Sunt Servanda* cannot be applied to contracts that have been renegotiated is striking. In both cases, the tribunals used renegotiation, a commonplace occurrence in concessions, to avoid the application of inflexible doctrines.

123. *Real Property Tax Exemption Case* (1961) and *Tunnel Indemnity Case* (1933), both stemming from Greek expropriations described in Wetter & Schwebel, *Some Little-Known Cases on Concessions*, 40 BRIT. Y.B. INT'L L. 183, 210 (1964).

124. *Aminoil*, 21 I.L.M. at 1021.

125. Von Mehren & Kourides, *supra* note 29, at 532; Geiger, *supra* note 52, at 85.

126. Von Mehren & Kourides, *supra* note 29, at 531.

127. Armstrong, *supra* note 117, at 95.

128. Domke, *supra* note 30, at 594.

129. It is for this reason that the Soviet trade tribunal has rejected the defense, despite the general Soviet position on private property. Armstrong, *supra* note 117, at 94-96. In this rejection, one can see the impact of the philosophical position of the developed Western nations. Nonetheless, one must remain aware of the fact that the Western insistence upon rigid observation of contractual arrangements counters not only *Rebus Sic Stantibus*, but also any flexible international doctrine involving contracts.

130. *Aminoil*, 21 I.L.M. at 1024-26.

This inflexibility also explains why tribunals are more comfortable applying the doctrine of changed circumstances to mitigate damages than to excuse breach. The damage suffered as a result of changed circumstances can be distributed between the parties rather than absorbed by one party. Consequently, considering changed circumstances in assessing compensation is a more precise and effective approach than either enforcing *Pacta Sunt Servanda* or *Rebus Sic Stantibus*.

C. Less Commonly Applied Contractual Doctrines

1. Duress

Given the position of the developing nations on the historical unfairness of their contractual relationships, it is surprising that they so seldom raise duress as a defense to their termination of concessions. One reason duress is not used by the developing nations may be its lack of acceptance in international law. Resolution 1803 of the U.N. General Assembly emphasizes that investment agreements "freely entered into" shall be followed.¹³¹ This provision implies that agreements which are not freely entered into need not be followed. It does not, however, define what impairment of free choice is, and so gives little practical guidance.

The developing nations attempted to have economic coercion included as a form of force outlawed by article 52 of the Vienna Convention on Treaties.¹³² This position was rejected and has, therefore, not been applied to concession agreements. A partial reason for this outcome may be that "the traditional notion of consent in treaty law has stated that any form of coercion on the state does not invalidate a treaty; freely given consent is not required."¹³³ This is true despite, or perhaps as a result of, the fact that great coercion is necessary to the conclusion of some treaties (e.g. peace treaties). Thus, the defense of duress as it has developed in treaty law will not prove useful in concession law unless its contours are significantly altered.¹³⁴

Practice has borne this position out. In the *Aminoil* arbitration, the corporation claimed it had been subject to duress because it was forced to renegotiate its concession. The tribunal responded that "the company made a choice; disagreeable as certain demands might be, it considered that it was better to accede to them because it was still possible to live with them."¹³⁵

131. General Assembly Resolution 1803, *supra* note 37. See *supra* note 86 and accompanying text.

132. Malawer, *A New Concept of Consent and World Public Order*, 4 VAND. J. INT'L L. 1, 28 *et seq.* (1970).

133. *Id.* at 2.

134. Schwebel has attempted to argue, in addition, that concession agreements "are not characterized by the legalized duress treaties may have embodied." Schwebel, *supra* note 72, at 273. This estimation does not recognize the previously discussed power of multinational corporations, nor the great monetary and technological needs of the developing nations.

135. *Aminoil*, 21 I.L.M. at 1008.

The tribunal concluded that there had been no duress. The same line of argument can also be applied to the claim that states are subject to duress when they negotiate concessions. As in treaty law, the position of international concession law on duress results from the law's recognition that parties to concession agreements are generally sophisticated.

The likelihood of creating an acceptable body of law based upon economic duress is very low. Given the shifting nature of power in a concession relationship, it could be said that duress is exercised by the corporation when the contract is concluded, and later by the state when it demands that the contract be renegotiated. Deciding whether either use of power constitutes duress depends upon differentiating bargaining power from duress. This inquiry focuses upon the relative power of parties concluding concession agreements, rather than upon the agreements themselves. As such, it mandates one outcome in any dispute between the same two parties. To accommodate the interests of both developed and developing nations, international doctrine must instead focus upon both the parties and upon the agreement they conclude.

The argument for an international doctrine of duress is more interesting when examined in light of the world in which developing nations function than in light of a particular contractual relationship. The Third World position that it has been forced into unconscionable arrangements, especially by colonial powers, seems to fit well under the doctrine of duress. While tribunals do not tend to take cognizance of this sort of global complaint, the historical realities which underlie the position of the developing nations render it sympathetic.

2. *Unjust Enrichment*

Unjust enrichment has been much discussed as a theory of compensation in concession disputes. It has been applied in favor of a corporation whose contract was terminated to the benefit of a host state.¹³⁶ Recently, states have argued unjust enrichment theories against corporations that repatriate "excess profits,"¹³⁷ while corporations have claimed that the deduction of "excess profits" from the compensation paid to them amounts to unjust enrichment of the host state.¹³⁸

136. *Lena Goldfields, Ltd.*, 5 Ann. Dig. 3 (Special Arbitral Tribunal 1930); Friedmann, *supra* note 2, at 505-06.

137. Kamanu, *Compensation for Expropriation in the Third World*, 10 *STUD. COMP. INT'L DEV.* 3, 11 (1975); Sornarajah, *supra* note 109, at 124 *et seq.*

138. In Chile, "excess profits" were found to be greater than the total compensation due. Lillich, *International Law and the Chilean Nationalizations*, in 2 *THE VALUATION OF NATIONALIZED PROPERTY IN INTERNATIONAL LAW* 125 (Lillich ed. & contrib. 1973) [hereinafter 2 LILLICH]. This will usually be the case because it is the host state which calculates what profits are "excess."

The problem with unjust enrichment as a doctrine is that it is a conclusion rather than a legal tool. Both parties to a concession are generally enriched. The only inquiry, therefore, is which party has been "unjustly" enriched. While *Pacta Sunt Servanda* examines the agreement concluded by the parties, and estoppel examines the nature of encouragements by the host state,¹³⁹ unjust enrichment offers no insight into the interpretation of an agreement. Focusing upon unjust enrichment merely highlights the disagreement between the developed and developing nations as to what constitutes a "just" situation, without providing any insight into a solution to the disagreement.¹⁴⁰

3. Estoppel

The theory of estoppel has been more widely discussed and accepted than that of duress, although less than that of unjust enrichment. Estoppel is the contractual theory that justifiable reliance by one party, upon the encouragement of the other party, should bind the second party to perform its apparent promises. The ICJ has found estoppel to be "among the general principles of law accepted by international law."¹⁴¹ Nonetheless, tribunals have tended to rely only implicitly on estoppel to resolve concession disputes. Commentators have, however, been more explicit in their application of estoppel.

In 1925, the British submitted in their memorial for the *Portuguese Religious Properties* case that "foreigners are entitled to count upon the legal protections and guarantees under the cover of which they came into the country and acquired their rights."¹⁴² More recently Dolzer has written that "[i]f an alien investor imports his property lawfully one day and is expropriated the next day without compensation, it would hardly be proper to deny . . . that the investor's 'legitimate reliance' on the host state has been unfairly frustrated."¹⁴³

Other commentators have argued that a corporation's reasonable reliance creates obligations not only in the realm of expropriation but also within the context of concession agreements themselves.¹⁴⁴ Some have even claimed that those obligations mean that a country which terminates a concession agreement, when the other party reasonably relied upon the country's

139. See *infra* section V(C)(3) on estoppel.

140. While in *Lena Goldfields, Ltd.*, it was found that taking away a company's rights under its contract with a sovereign amounted to "unjust enrichment," this constitutes only one interpretation of the word "just." See *Lena Goldfields, Ltd.*, 5 Ann. Dig. 3 (Special Arbitral Tribunal 1930).

141. North Sea Continental Shelf Cases (Germany v. Denmark and the Netherlands), 1969 I.C.J. 1, 120 (sep. op. J. Ammoun); see also 1969 I.C.J. at 27 (majority opinion).

142. McNair, *The Seizure of Property and Enterprises in Indonesia*, 6 NEDERLANDS TIJDSCHRIFT VOOR INTERNATIONAAL RECHT 218, 225 (1959).

143. Dolzer, *supra* note 22, at 580.

144. Friedmann, *supra* note 2, at 506; Domke, *supra* note 30, at 595; Weil, *supra* note 108, at 306.

promises, has violated international law.¹⁴⁵ In addition, at least one court has used estoppel to resolve an international concession dispute.¹⁴⁶

The advantage of applying the doctrine of estoppel to concession agreements is that estoppel focuses upon an important component of international investment agreements: the encouragements and representations of host states. It is unfair for states to exhort companies to invest, by promising them benefits that the state does not intend to confer. Estoppel forces states to accept the obligations that come with concession agreements as well as the benefits. In addition, it circumvents the superficial problem of equating corporations to states. Estoppel merely recognizes that states should be held to commitments reasonably implied from their actions, and that if a state does not honor dealings with the nationals of other states, it debases all states.

Initially, the difference between the effect of estoppel and that of *Pacta Sunt Servanda* does not appear to be pronounced. Yet, a closer examination reveals that estoppel allows for the very flexibility lacking in *Pacta Sunt Servanda*. While both doctrines can require that contractual obligations be fulfilled, estoppel focuses upon "reasonable" reliance. Therefore, a theory of concession enforcement dependent upon estoppel could reject contractual clauses or whole contracts that were not "reasonable." This would allow some compromise between the positions of the developed and developing nations which could be incorporated into the definition of "reasonable."

The inquiry as to what is "reasonable" could start with the original agreement and subsequent renegotiations. One could then analyze the benefits derived and costs incurred by the host nation and the corporation prior to termination, the benefits gained by the host nation through termination, and the loss to the corporation as a result of termination. The net positions of the two parties could then be compared with the positions of parties to similar contracts. This would ensure consideration of a premium to be paid to corporations engaged in industries (particularly extractive industries) where a high proportion of concessions fail to make a profit. It would also ensure that neither party treated the other party unconscionably, relative to industry norms. Further inquiries could be made into whether the investment was a colonial investment, and whether it was non-developmental.¹⁴⁷ If either was found to be the case, then the ratio of the company's profit to the state's profit should be decreased. Finally, any other factors which seemed particularly

145. Friedmann, *supra* note 2, at 505; I. BROWNIE, *supra* note 69, at 539.

146. In considering the Chilean nationalizations, the German courts found that Kennecott Copper "had to be able to rely on the fact that a few years later it would not be expropriated at short notice by the Chilean government," Seidl-Hohenveldern, *supra* note 17, at 114, since the government had led Kennecott to believe that it would not be expropriated if Chile were granted a majority participation in the corporation. Kamanu, *supra* note 137, at 11; Sornarajah, *supra* note 109, at 124 *et seq.* Hence, Chile was estopped from expropriating Kennecott without paying sufficient compensation.

147. Dolzer suggests that an investor who concludes a "manifestly non-developmental investment" (i.e., one not in the developmental interest of the host nation) cannot be considered to have justifiably relied upon the agreement with the host state. Dolzer, *supra* note 22, at 586.

appropriate in the specific instance could be considered, and damages could be assessed.

While this process fails to assign an exact weight to each factor, it is precisely this flexibility which is beneficial in evaluating unique investments and which is conducive to the careful balancing of particular interests. In addition, experience in applying the doctrine of estoppel will, over time, yield a framework within which to consider the weighing of various factors.

VI.

THE INTERNATIONAL REMEDY DOCTRINES TO WHICH INTERNATIONALIZED CONTRACTS COULD BE SUBJECT

The disagreement between the developed and developing nations over liability doctrines also appears in the area of international remedies. Some authorities, mainly those from the developed nations, argue that specific performance should be the primary remedy for concession breaches. Others, for the most part from the developing nations, argue that damages should be the primary remedy. Even among those who accept damages as the primary remedy for concession disputes, there is a split between those who favor forcing the breaching party to pay the full prospective value of the contract rights lost, and those who believe the needs of developing nations require that they be allowed to pay less than the full future value.

A. *Specific Performance*

Those who support specific performance as a remedy for the breach of a concession agreement point to the *Chorzow Factory* case¹⁴⁸ as primary authority for their position. In that case, Poland breached a treaty by nationalizing a factory in territory ceded to it by Germany. The court held:

reparation must, as far as possible, wipe out all the consequences of the illegal act and reestablish the situation which would, in all probability, have existed Restitution in kind [specific performance], or if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear . . . such are the principles which should serve to determine the amount of compensation due for an act contrary to international law.¹⁴⁹

Authorities who favor the application of this formula to concession agreements state that the breach of a concession agreement is an international wrong. They add that the language in *Chorzow Factory* specifies that restitution in kind is the primary remedy for such a wrong.

One of the reasons advanced as to why specific performance should be the norm is that it fulfills expectations. Von Mehren argues that:

148. Concerning the Factory at Chorzow (Germany v. Poland), 1928 P.C.I.J. (ser. A) No. 17 (Judgment of Sept. 13).

149. *Id.* at 47.

[t]he expectation that one will carry out one's obligations and receive the benefits for which one had bargained is a cornerstone of commercial relations among civilized nations. Consequently, there is an important interest in establishing that performance is the natural and preferred remedy for breach of an international contract from the point of view both of host countries and of foreign private investors.¹⁵⁰

While this has swayed several commentators,¹⁵¹ many others remain unimpressed. One commentator has said that "[n]o one seriously can argue in the present times for specific performance in international law."¹⁵² This is partly because tribunals lack the authority to order specific performance¹⁵³ and, partly because it is difficult to force a sovereign nation to behave in a certain way.¹⁵⁴

Whatever the position of the commentators, few tribunals have attempted to force a state to specifically perform its commitments. Among recent cases, specific performance has only been strongly supported by the *Topco* arbitration. That case stated that "*Restitutio in integrum* [specific performance] is, . . . under the principles of international law, the normal sanction for non-performance of contractual obligations and that it is inapplicable only to the extent that restoration of the *status quo ante* is impossible."¹⁵⁵ It has been argued that the reasons so few tribunals have ordered specific performance are that the parties tend to settle the sort of cases that would give rise to it, the claimants often fail to request it, and it is sometimes physically impossible to specifically perform obligations.¹⁵⁶ Even these reasons, however, do not fully explain the dearth of cases ordering that concession agreements be specifically performed.

One possible explanation for the lack of support for specific performance is that it entirely neglects the position of the developing nations and, in so doing, casts international law into disrepute.¹⁵⁷ To accept specific performance would deny any merit to the Third World's claims of permanent sovereignty, and would ignore the factors that make renegotiation of concessions

150. Von Mehren & Kourides, *supra* note 29, at 552.

151. Kissam & Leach, *supra* note 34, at 214; Rolin, *Avis de Monsieur le Professeur H. Rolin*, 6 NETH. INT'L L. REV. 260, 271 (1959).

152. Sornarajah, *supra* note 109, at 121.

153. Geiger, *supra* note 52, at 102. In addition, just as specific performance is almost never applied to contracts for personal services in the United States because to do so would be offensive to individual liberty, E. FARNSWORTH, CONTRACTS § 12.7, at 835-36 (1982), Fitzpatrick v. Michael, 177 Md. 248, 254, 9 A.2d 639, 641 (1939), it should not be applied to states that are parties to concession agreements because to do so would be offensive to the concept of national autonomy.

154. A tribunal encounters nearly insurmountable obstacles in ordering a sovereign nation to specifically perform its contractual obligations, despite the nation's objection. While a damage award can be enforced against the assets of a nation in other countries, specific performance would often entail ordering a sovereign to act in a designated manner within its own borders, a virtually unenforceable order.

155. *Topco*, 17 I.L.M. at 36.

156. Von Mehren & Kourides, *supra* note 29, at 534.

157. This is particularly true because a tribunal's inability to enforce an order of specific performance would undermine the credibility of international law.

essential.¹⁵⁸ Thus, while the value of a going concern which possesses an agreement with the sovereign should be greater than that of a going concern that does not, the presence of the concession agreement should not serve as a sixty year straight jacket upon the parties to it.¹⁵⁹ It is not surprising, therefore, to discover that in the one arbitration which favored specific performance (*Topco*), the developing nation defendant did not even present its side of the case to the arbitrator. Just as permanent sovereignty should not be accepted since it ignores the interests of the developed nations, specific performance should not be accepted since it ignores the interests of the developing nations.

B. Compensation

Faced with the international community's rejection of specific performance, some developed nations fell back on the alternative position suggested by the *Chorzow Factory* case, that the breaching party should pay damages equal to the full value of specific performance.¹⁶⁰ While investors have usually had to settle for less than this amount, developed nations have insisted that the value of damages should be measured by the profits expected had the concession not been breached.¹⁶¹

The developing nations make three arguments to counter those favoring full damages for breach. First, relying on their claims of permanent sovereignty,¹⁶² they argue that a concession agreement merely expresses a nation's present intention, which can be changed at will.¹⁶³ The contract, therefore, has no future value. Second, they argue that concession agreements are simply another form of property,¹⁶⁴ and that they can be nationalized¹⁶⁵ at a far

158. See *supra* section III(B).

159. Cf. O.W. HOLMES, *The Path of Law*, in COLLECTED LEGAL PAPERS 168-78 (1920).

160. See *supra* note 149.

161. *Delagoa Bay Railway Case (U.S. v. Portugal)*, 2 J. MOORE, INTERNATIONAL ARBITRATIONS HISTORY 1865 (1898); *Norwegian Shipowners' Claims (Norway v. U.S.)*, 1 R. Int'l Arb. Awards 307 (1922); *Goldenberg Claim (Germany v. Rumania)*, 2 R. Int'l Arb. Awards 901 (1928); *Lena Goldfields, Ltd.*, 5 Ann. Dig. 3 (Special Arbitral Tribunal 1930); *Sapphire*, 35 I.L.R. 136; *AGIP*, 21 I.L.M. 726; *Aminoil*, 21 I.L.M. 976.

162. See *supra* section III(B).

163. *Id.*

164. While the *Norwegian Shipowners' Claims* case does support viewing concession agreements as property, *Norwegian Shipowners' Claims*, 1 R. Int'l Arb. Awards at 334, it has also been said that "the principal of respect [for acquired property rights] is not confined to rights in land but extends to 'all things and rights considered as having a money value . . . such as trademarks and copyrights, patents and rights *in personam* capable of transfer or transmission as debts.'" *McNair*, *supra* note 142, at 238. Nonetheless, the developing nations rely only on the first proposition.

165. "There is no rule in international law that gives a greater degree of protection to rights secured by contract than to other rights of property." *Kissam & Leach*, *supra* note 34, at 205. For this reason, it is argued that the characterization of property rights acquired through a concession agreement as contractual should not change the amount of damages awarded for a "nationalization" of a concession agreement.

lower cost than would be required under concession law.¹⁶⁶ Finally, the developing nations argue that to prevent them from breaching concession agreements, by forcing them to pay the full value of prospective profits, would prevent them from controlling their own destinies.¹⁶⁷

Most arbitrations that have considered the question of compensation for breached concession agreements have found the host states to be liable for the value of future profits.¹⁶⁸ The theoretical arguments of developing nations have generally been rejected, except as levers to lower the total amount of compensation owed under the compensation theories of developed nations.

If one accepts compensation as the preferred remedy, both the positions of the developing and developed nations must be rejected as flawed. The position of the developing nations must be rejected because a theory of compensation based on permanent sovereignty, or upon the valuelessness of contracts, ignores the legitimate interests of developed nations. Similarly, the demand of the developed nations for compensation equal to the full amount of specific performance must be rejected. While paying compensation equal to the value of specific performance does not directly interfere with a nation's sovereignty as does specific performance, it does not mesh with the flexible liability doctrines outlined in this article. The various considerations used in determining the "reasonableness" of reliance must also be used in calculating "reasonable" damages. In this way, the penalty for breach will be carefully calibrated to the dictates of flexible and just laws of liability.

VII. THE RELATIONSHIP BETWEEN NATIONALIZATION AND BREACH

The international law governing breaches of concession agreements is closely intertwined with the law governing nationalizations of industries. This is so because some tribunals have considered contracts to be property,¹⁶⁹ because breaches of concession agreements often occur as part of larger nationalization programs, and because tribunals have failed to separate their analyses of nationalization from their analyses of breach of concession agreements. Thus, a breach of a concession agreement can be described by a developing nation as nationalization of the enterprise underlying a concession agreement, or even of the agreement itself. Developing nations have often taken this position because the law governing breaches of concession agreements requires greater compensation than does that governing nationalizations.

166. See *infra* section VII.

167. See Goldman & Paxman, *Real Property Valuations in Argentina, Chile and Mexico*, in 2 LILLICH, *supra* note 138, at 165; Dawson & Weston, *Prompt, Adequate and Effective: A Universal Standard of Compensation?*, 30 *FORDHAM L. REV.* 727, 735 (1961-62); Dolzer, *supra* note 22, at 582; Friedmann, *supra* note 2, at 513.

168. See *supra* note 161.

169. See *supra* note 164.

Historically, the developing nations have argued that they have no duty to compensate for nationalizations beyond a duty imposed by their own laws.¹⁷⁰ Not unexpectedly, this position has been rejected by developed nations.¹⁷¹ Practice has confirmed the position, or perhaps the power, of the developed nations. The modern practice of most states which make pervasive expropriations of alien property has been to pay some compensation.¹⁷²

However, the position of the developed nations on the amount of compensation required to be paid has not been upheld. Traditionally, the developed nations have insisted upon "prompt, adequate, and effective" compensation.¹⁷³ This standard has been entrenched both in bilateral investment treaties¹⁷⁴ and in national constitutions of developing nations,¹⁷⁵ and was the traditionally accepted international legal standard of compensation.¹⁷⁶ Recently, the Third World developed the concept of a New International Economic Order which was described in several U.N. General Assembly resolutions, including resolutions leaving the appropriate amount of compensation to be decided by the nationalizing state.¹⁷⁷ Even where developing nations agree that compensation must be paid, they argue that no more than discounted book value, a very meager historical measure of the worth of a company's assets, should be paid.¹⁷⁸ Commentators from developed nations have rejected the book value standard¹⁷⁹ and both commentators¹⁸⁰ and tribunals¹⁸¹ have rejected the claim that the U.N. resolutions declaring a New International Economic Order have legal force. The net result of the disagreements over the amount of compensation that must be

170. Note, *Expropriation of Alien Property*, 109 U. PA. L. REV. 245, 250 (1960).

171. See Garcia-Amador, *supra* note 25, at 36; Neville, *supra* note 20, at 63; von Mehren & Kourides, *supra* note 29, at 522.

172. See Note, *supra* note 170, at 253.

173. I. BROWNLIE, *supra* note 69, at 533.

174. See Treaty Concerning the Treatment and Protection of Investments, Oct. 27, 1982, Panama-United States, art. IV, reprinted in 21 I.L.M. 1227, 1231 (1982); Reciprocal Encouragement and Protection of Investments, Sept. 29, 1982, Egypt-United States, art. III, reprinted in 21 I.L.M. 927, 935 (1982); Agreement on the Mutual Protection of Investments, March 29, 1982, People's Republic of China-Sweden, art. 3, reprinted in 21 I.L.M. 477, 477 (1982); Agreement Concerning the Promotion and Protection of Investment, March 1, 1982, Japan-Sri Lanka, art. 5, reprinted in 21 I.L.M. 963, 966 (1982); see also *The Compensation Requirement in the Taking of Alien Property*, 22 RECORD OF THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK 195 (1967).

175. Botswana Const. § 8(1), W. Samoa Const. art. 14(1), Kenya Const. § 75(1), Senegal Const. art. 12, in CONSTITUTIONS OF THE COUNTRIES IN THE WORLD (A. Blaustein & G. Flanz eds. 1984).

176. Domke, *supra* note 30, at 609.

177. See *supra* note 37.

178. See Wesley, *A Compensation Framework for Expropriated Property in Developing Countries*, in 3 LILLICH, *supra* note 3, at 15; Kennecott Copper Corporation, *An Analysis of the Expropriation of the Properties of Sociedad Minera El Teniente*, in 2 LILLICH, *supra* note 138, at 36; Girvan, *supra* note 18, at 167 *et seq.*

179. McCosker, *Book Values in Nationalization Settlements*, in 2 LILLICH, *supra* note 138, at 48, 51; Lillich, in 2 LILLICH, *supra* note 138, at 121.

180. White, *A New International Economic Order?*, 16 VA. J. INT'L L. 323, 330 (1975-76); von Mehren & Kourides, *supra* note 29, at 523.

paid is that "the principle of 'prompt, adequate, and effective' compensation has failed entirely."¹⁸²

The practical effect of the failure of the prompt, adequate, and effective standard of compensation has been that, while compensation is generally paid, it is paid "in an amount substantially less than the fair market value."¹⁸³ Thus, an expropriated corporation can expect to receive compensation, but as the Kennecott Copper dispute demonstrated,¹⁸⁴ the corporation cannot expect very much compensation.

There appear to be two possible reasons why the international law governing concession agreements requires greater compensation for those individuals whose concessions have been lost, than does the international law of nationalizations. First, as the *Norwegian Shipowners' Claims* case found, the contract itself has some value.¹⁸⁵ This value could result from the reliance a party places upon a sovereign's commitments, or from the explicit guidelines that a concession agreement provides as to what the future value of a corporation's investment will be. Second, the developing nations may have chosen to ignore concession law in favor of nationalization law, and may, therefore, have viewed the breach of concessions as a subset of nationalizations.

Whatever the reasons for the disparity between concession law and nationalization law, the result of the alternative ways in which a concession dispute can be characterized is that the international law governing concessions cannot develop entirely independently of the international law governing nationalizations. Otherwise, nationalization law will be applied by developing nations when they have the power to do so and concession law will be applied in disputes in which multinational corporations have the upper hand. This would eliminate the possibility of ordered investment and would instead allow disputes in the international investment community to disintegrate into an unpredictable power struggle.

CONCLUSION

The international law governing concession disputes has been relatively inflexible in its approach, and therefore has been insufficient to resolve many

181. *Topco*, 17 I.L.M. at 30; *Aminoil*, 21 I.L.M. at 979. "The tribunals based their conclusions upon the fact that major industrialized nations voted against or abstained from the operative portions of the resolutions." Von Mehren & Kourides, *supra* note 29, at 523; *Topco*, 17 I.L.M. at 29.

182. Vicuna, *supra* note 3, at 132. Even the Restatement of the Foreign Relations Law of the United States, traditionally a spokesman for developed nations' views of international law, has retreated from its previous position that prompt, adequate, and effective compensation is necessary in all circumstances. See RESTATEMENT (SECOND) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 (Tent. Draft No. 7, 1987).

183. See Note, *supra* note 170, at 253.

184. See *supra* note 17 and accompanying text.

185. See *supra* note 164.

disputes between parties to concession agreements. As a result, many disagreements are resolved outside of the legal context, usually through negotiations between the two parties involved. An effort should be made to bring the inflexible international laws on concession agreements in line with international practices, by looking towards more flexible legal doctrines.

Flexibility is necessary to allow for compromise between the conflicting interests of developed and developing nations. Underlying any dispute is the power of developing host nations to terminate concession agreements and the power of the developed nations' corporations to cease to invest. The balance between these two powers prevents any international law which protects only the interests of one side from being effective.

The inadequacies of contemporary international concession law result largely from its failure to keep up with changes in the world economy. In the early 1900s, cases such as the *Serbian Loans* case left to municipal law problems associated with an agreement between a sovereign and a nonsovereign actor. As the 1900s progressed, the presence of multinational corporations in the Third World expanded. But, as the power of multinationals increased, the growing feelings of dependence among Third World nations led them to terminate concessions and nationalize foreign assets. While the Third World took the view that this was their right, and developed the concept of permanent sovereignty, the developed nations insisted that the power implicit in a state's sovereignty, which allowed it to bind itself, dictated that the developing nations abide by concessions to which they had agreed. International law has sided with the developed nations on the question of sovereignty. Recognition of the Third World's position would have totally ignored the needs of developed nations, since permanent sovereignty would allow the developing nations to do as they pleased. In addition, transactions with developing nations would have been limited, since no commitment by a state would have been binding. The inflexibility of this position was its downfall.

For the same reason that a state's sovereignty to bind itself must be recognized, international law must also recognize that concession agreements can be internationalized. To consider concession agreements as municipal contracts would give host nations absolute authority and leave the corporations of developed nations unprotected. This explains the growing acceptance of the doctrine of the internationalized contract in international law.

The doctrines that have been applied to govern internationalized contracts, however, have not been sufficiently flexible to accommodate the interests of both parties. Since the concept of the internationalized contract was derived from the comparison of concession agreements to treaties, it was thought that treaty law should govern disputes over internationalized contracts. *Pacta Sunt Servanda* and its corollary, that specific performance should be the remedy of first recourse, prevent the developing nations from escaping the one-sided constraints originally negotiated in concession agreements. Thus, just as permanent sovereignty is unacceptable since it ignores

the needs of developed nations, *Pacta Sunt Servanda* is unacceptable because it ignores the needs of developing nations. In each case, it would be in the interests of one of the parties to bypass international law entirely.

While some argue that *Rebus Sic Stantibus* adds flexibility to the doctrine of *Pacta Sunt Servanda*, it merely leads to an equally extreme opposite result. When *Rebus Sic Stantibus* is successfully invoked, it leaves no room for consideration of the needs of the developed nations. This is particularly true given the developing nations' global notion of what constitutes changed circumstances. Unless the doctrine of *Rebus Sic Stantibus* were considerably revised, it could not function effectively as an internationalized contract doctrine.

Thus, an effective and flexible international law of concession agreements should not be fashioned from revamped inflexible doctrines such as *Pacta Sunt Servanda* modified by *Rebus Sic Stantibus*. It should include new doctrines that respond to both the varied situations under which concession agreements are formed and to each agreement's unique characteristics. To that end, this article suggests that the application of a variant of estoppel would be an effective approach. Estoppel's requirement that a company's reliance be "reasonable," would give the leeway necessary to fashion a solution responsive to the needs of all parties and to the particular circumstances of a dispute. In addition, the doctrine's arrival in the international forum would not be encumbered by previous doctrinal pronouncements, such as those associated with treaty law for *Rebus Sic Stantibus*.

It can, however, be argued that estoppel is an inappropriate doctrine exactly because it is not accompanied by settled precedent. Additionally, it can be claimed that determining the existence of "reasonable" reliance involves an unstructured decision as to the fairness of a particular investment. Therefore, it can be argued that estoppel is unworkable and that the parties are left no better off than under the present system. These arguments fail to recognize the very real benefits achieved, and structure imposed, by the proposed system. To begin with, no system of doctrines in the field of concession law should be highly structured. The flexibility of the proposed system is exactly its benefit over the previous system. At the same time, it would structure the decisions that could be made.

Implicit in accepting a variant of estoppel as a rule governing international concession law, is accepting a sovereign's ability to bind itself in an agreement with a non-state, and accepting the newly developed concept of the internationalization of concessions. Further, because reliance focuses upon a particular relationship, the facts of a particular controversy are examined rather than the global situation of developed and developing actors. Accordingly, the notion of "affirmative action" for the Third World is rejected as unworkable in this context. While the question of the subordinate position of the Third World can be considered as it affects the negotiation of the particular contract, the inquiry focuses upon the relationship between the two parties

involved. Thus, even before one reaches the question as to what is "reasonable," a significant framework has been generated within which that inquiry can be made.

The inquiry as to what is "reasonable" will involve an examination of the situations and expectations of both parties.¹⁸⁶ When coupled with growing experience derived from similar disputes, a flexible and yet predictable system will evolve. Once a flexible approach to liability has been adopted, an equally flexible approach to remedies should also be accepted. In this respect, compensation is far superior to specific performance. Compensation respects the decision of a sovereign, while still requiring that the sovereign be responsible for its earlier exercises of sovereignty. Compensation also allows for consideration of the balance of equities in arriving at a solution. While specific performance requires a decision as to which party was "right," compensation allows an allocation of blame whereby the breaching party only pays as much compensation as is necessary to alleviate any wrong done to the other party. Compensation thereby allows an arbitrator to factor the "reasonableness" considerations into any award.

This overall approach should lessen the dissatisfaction of the developing nations by considering the historic relationship between the contracting parties, and the costs and benefits of the relationship to each party, in arriving at a settlement. At the same time, the concerns of developed nations should be appeased, since disputes would not be resolved under the law of the breaching party, and corporations would be compensated for any opportunities lost as a result of the breach. Once these needs have been satisfied, developed and developing nations would hopefully abandon their present extreme positions and reduce their levels of confrontational rhetoric. If this approach is not taken, then most concession disputes will continue to be resolved through negotiations outside of international law. This will provide a less predictable climate for international investment, since viable international legal doctrines provide a framework for dispute resolution and a backdrop against which negotiations can take place. Failing to adjust the international doctrines will mean that a salutary experiment with internationalizing contracts has gone to waste and that the resolution of contract disputes will continue to be subject to the vagaries of unstructured negotiations.

186. See *supra* section V(C)(3) on estoppel.