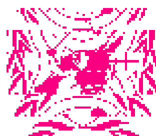
UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

TAKING OF PROPERTY

UNCTAD Series
on issues in international investment agreements



UNITED NATIONS
New York and Geneva, 2000

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Two dots (..) indicate that data are not available or are not separately reported. Rows in tables have been omitted in those cases where no data are available for any of the elements in the row;

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A slash (/) between dates representing years, e.g. 1994/95, indicates a financial year;

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The main purpose of the UNCTAD Series on issues in international investment agreements is to address key concepts and issues relevant to international investment agreements and to present them in a manner that is easily accessible to end-users. The series covers the following topics:

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Preface

The United Nations Conference on Trade and Development (UNCTAD) is implementing a work programme on a possible multilateral framework on investment, with a view towards assisting developing countries to participate as effectively as possible in international investment rule-making at the bilateral, regional, plurilateral and multilateral levels. The programme embraces capacity-building seminars, regional symposia, training courses, dialogues between negotiators and groups of civil society and the preparation of a series of issues papers.

This paper is part of that series. It is addressed to government officials, corporate executives, representatives of non-governmental organizations, officials of international agencies and researchers. The series seeks to provide balanced analyses of issues that may arise in discussions about international investment agreements. Each study may be read by itself, independently of the others. Since, however, the issues treated closely interact with one another, the studies pay particular attention to such interactions.

The series is produced by a team led by Karl P. Sauvant and Pedro Roffe. The principal officer responsible for its production is John Gara who oversees the development of the papers at various stages. The members of the team include S.M. Bushehri, Obiajulu Ihonor and Jörg Weber. The series' principal advisors are Arghyrios A. Fatouros, Sanjaya Lall and Peter T. Muchlinski. The present paper is based on a manuscript prepared by M. Sornarajah. The final version reflects comments received from Joachim Karl, Nick Mabey and Marinus Sikkel. The paper was desktop-published by Teresita Sabico.

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Secretary-General of UNCTAD

Geneva, January 2000

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UNCTAD has carried out a number of activities related to the work programme in cooperation with other intergovernmental organizations, including the Secretariat of the Andean Community, La Francophonie, the Inter-Arab Investment Guarantee Corporation, the League of Arab States, the Organization of American States, and the World Trade Organization. UNCTAD has also cooperated with non-governmental organizations, including the Centro de Estudios Interdisciplinarios de Derecho Industrial y Económico - Universidad de Buenos Aires, the Consumer Unity and Trust Society - India, the Economic Research Forum - Cairo, the European Roundtable of Industrialists, the Friedrich Ebert Foundation, the International Confederation of Free Trade Unions, Oxfam, SOMO - Centre for Research on Multinational Corporations, the Third World Network, Universidad del Pacifico, University of the West Indies, and World Wildlife Fund International.

Funds for the work programme have so far been received from Australia, Brazil, Canada, France, the Netherlands, Norway, Switzerland, the United Kingdom and the European Commission. Countries such as China, Egypt, Guatemala, India, Jamaica, Morocco, Peru, Sri Lanka and Venezuela have also contributed to the work programme by hosting regional symposia. All of these contributions are gratefully acknowledged.

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Executive summary

The taking of private assets by public authorities raises significant issues of international law, where such takings involve the assets of foreign private investors. This paper examines the concept of "takings" in the context of international law and international investment agreements. The focus of the analysis is twofold. First, different categories of takings are distinguished, addressing in particular the problem of the distinction between governmental measures that involve interference with the assets of foreign investors, yet do not require compensation, and those that do require compensation. Second, the requirements for a taking to be lawful are discussed, in particular the issue of the standard for compensation. The paper highlights the challenges that remain when considering the takings clause in international investment agreements, and discusses policy options relative to defining a "taking" when drafting the clause. It also illustrates some drafting models.

The takings clause aims at protecting foreign investors by establishing standards for the manner in which host States might take or otherwise interfere with their property rights. That is to say, it limits the right of States to take property by imposing certain requirements. Under customary international law and typical international investment agreements, three principal requirements need to be satisfied before a taking can be considered to be lawful: it should be for a public purpose; it should not be discriminatory; and compensation should be paid. The first two requirements are generally accepted. As regards the third, it too is widely accepted in principle, but there is no universal agreement relating to the manner of assessment of the compensation due. The more recent bilateral investment treaties (BITs) use the formula that the compensation must be prompt, adequate and effective, but, alternative formulas, such as just compensation, are also used. An emerging trend in international investment agreements (IIAs) that deserves attention is the development of a fourth requirement, due process.

The issue of the formula for compensation aside, a threshold problem is how to provide for clear guidance on the type of governmental measures and their effects that would trigger the

takings clause in an IIA. The measures that fit the classical category of takings are nationalizations (outright takings of all foreign property in all economic sectors, or on an industry-specific basis) and expropriations (takings that are property- or enterprise-specific).

Certain governmental measures may not involve an actual physical taking of property, but may still result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor. Such measures pose the problem of distinguishing between measures that trigger the takings clause and its requirement of payment of compensation, and those that involve interference with the property rights of foreign investors but would nevertheless be considered as not falling within the ambit of the takings clause. Typically, a measure that is a consequence of the violation of a regulation has been regarded as non-compensatory in many legal systems. A penal measure following the violation of a criminal statute cannot give rise to a compensatory taking. There is authority that a tax measure, if not excessive, also cannot amount to a taking. The same is true of violations of antitrust laws. In some jurisdictions, even interference with property rights in order to further environmental or planning decisions could be considered non-compensatory.

Drafting a provision that adequately addresses the issues of the protection of the foreign investor and the ability of a host State to govern its economy can pose a challenge. Although some IIAs have sought to list the regulatory measures the exercise of which will not amount to takings, the compilation of an exhaustive list is a difficult if not impossible task. Instead, the takings clause could be drafted to reflect the formulation of a certain relationship that can accommodate both the concerns of foreign investors and national policy makers. This paper provides policy makers with a blend of policy options that could strike a balance between the level of investment protection, on the one hand, and the level of discretion retained by the host State in adopting measures that affect foreign investments, on the other hand.

INTRODUCTION

The taking of foreign property by a host country has constituted, at least in the past, one of the most important risks to foreign investment. As a foreign investor operates within the territory of a host country, the investor and its property are subject to the legislative and administrative control of the host country. The risk assessments that a foreign investor makes at the time of entry may not be accurate since internal policies relating to foreign investment are subject to change, as are the political and economic conditions in a host country. Changes could be brought about by several factors, such as a new Government, shifts in ideology, economic nationalism or monetary crises. Where these changes adversely affect foreign investment or require in the view of a host country a rearrangement of its economic structure, they may lead to the taking of the property of a foreign investor.

An understanding of the types of takings that could be effected and the legal and business precautions that could be taken against them are factors to be considered in making a foreign investment as well as in the shaping of international norms to regulate such interferences by host countries. So, too, a policy maker in a State that seeks to attract foreign investment must understand the implications of governmental interferences in foreign investment that amount to a taking and the extent of the international legal controls or restraints that exist in respect of them.

This paper is an analysis of the law relating to takings of foreign property by host countries and of the clauses in IIAs seeking to provide protection against such takings. The paper deals with the development of the law and considers both what possible protection against governmental interference can be given by international instruments and under what conditions and in which manner a State retains, under international law, the freedom to take action that may affect foreign property in the interests of its economic development.

The taking of property by Governments can result from legislative or administrative acts that transfer title and physical

possession. Takings can also result from official acts that effectuate the loss of management, use or control, or a significant depreciation in the value, of assets. Generally speaking, the former can be classified as "direct takings" and the latter as "indirect takings". Direct takings are associated with measures that have given rise to the classical category of takings under international law. They include the outright takings of all foreign property in all economic sectors, takings on an industry-specific basis, or takings that are firm-specific. Usually, outright takings in all economic sectors or on an industry-specific basis have been labeled "nationalizations". Firm specific takings on the other hand have often been called "expropriations". Both nationalizations and expropriations involve the physical taking of property. In contrast, some measures short of physical takings may amount to takings in that they result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor (Christie, 1962; Weston, 1975; Dolzer, 1986). Some particular types of such takings have been called"creeping expropriations",[1] while others may be termed "regulatory takings". All such takings may be considered "indirect takings".

The classifications of takings outlined above give an indication of how the terminology on takings is used in this paper. But it needs to be pointed out that, despite the extensive legal and other literature on the topic in the past few decades, the terminology and to some extent the classification of takings of property is not fully clear, consistent or established. There are many reasons for this. To begin with, the terms (and concepts) in question have their origin in national law and practice and their "translation" in international law is sometimes problematic. In the second place, the actual practice of States evolves, partly in response to developments in the economy and in the forms that "property" takes, and partly because the ideologies and policies in effect change. Thirdly, the topic has a long history and has gone through several phases, during which the importance of the particular facets of the relevant problems varied considerably. What follows is a brief summary of some of the major phases.

In the twentieth century, the first major phase of taking of property of aliens by States which can be classified as "nationalizations" and had an impact on shaping international law on the subject of takings, began with the Russian and Mexican revolutions.[2] These takings were not accompanied by the payment of compensation and resulted in conflicts between the host countries and the home countries of the aliens whose property was taken. In response to the taking of United States property by Mexico, the Government of the United States did not contest Mexico's right to nationalize but argued that it was subject to certain international law standards, including the payment of "prompt, adequate and effective compensation" ("Hull formula").[3] The formula encapsulates the view that takings by a host country should conform to an external standard mandated by international law which would fully protect the investor's interests. This stance on takings has been maintained by the Government of the United States ever since as representing international law and has been generally espoused by other capital exporting countries. Developing countries, however, generally resisted this stance on the ground that such a high standard of compensation may deter national action in pursuance of objectives of restructuring their economies especially in cases of large-scale takings or where host countries are short of foreign exchange.

Another phase of takings followed the period of decolonization. Here, the newly independent States, seeking to wrest economic control from the nationals of the erstwhile colonial States, embarked on across-the-board nationalizations of foreign affiliates and their assets.[4] Their position was that only "appropriate compensation" needed to be paid for these takings of foreign property. This position came to be associated with the formulation of a series of resolutions in the General Assembly of the United Nations spelling out the doctrine of permanent sovereignty over natural resources[5] and the campaign for a New International Economic Order.[6] In this period, the discussion on takings was coloured by the objective of ending the economic control of former colonial powers. The General Assembly resolutions were intended to facilitate this objective.

Though outright nationalizations are still possible in situations of regime changes, this phase has generally passed. Likewise, nationalizations on an industry-wide basis are also a rare

phenomenon.[7] This is not to say that such instances of takings may not reoccur.[8] In any event, interferences in specific industries that a State may want to reorganize for different reasons will continue to result in the direct takings of alien property. The United Kingdom and Canada have renegotiated contracts relating to natural resources investments when they turned out to be disadvantageous to them, indicating that governmental power will be utilized, both by developed and developing countries, in order to redraw disadvantageous contracts in important industries (Cameron, 1983; Mendes, 1981). Closely related to nationalization are large-scale take-overs of land by the State to distribute to the landless. This differs from nationalization proper in that the State does not retain the properties. Again, this is no longer a very important category in most countries but the issue has resurfaced in the recent past.

In the more usual situation, at least in recent times, direct takings are likely to be expropriations, that is, takings targeted at individual properties or enterprises. But — perhaps even more importantly — the focus on takings is increasingly turning to indirect takings. However, almost any governmental measure could be construed as an act of interference in the business of a foreign investor. The difficulty lies in distinguishing between regulatory measures that have to be compensated and measures that do not carry with them, under international law, the obligation to pay compensation.

This has become an increasingly grey area. The law will have to be developed to provide sufficient criteria for distinguishing between "tolerable"[9] regulatory takings that are not compensable and unjustified takings that are. Already, the issue has been raised that changes in ministerial and other policy having an effect of diminishing the profitability of investment should be considered as takings since the value of the investment is diminished as a result of these policy changes. An important case in point was that of a dispute between Canada and Ethyl Corporation of Virginia, United States (box 1).[10] To a large extent, the debate here will track the constitutional debates within domestic legal systems on what amounts to a compensable taking and what amounts to a truly regulatory non-compensable taking.

Box 1. Regulatory measures and depreciation in value: the Ethyl case

Canada's Manganese-based Fuels Additives Act came into force on 24 June 1997. Under the Act, the gasoline additive MMT was placed on a schedule which resulted in banning interprovincial trade and importation into Canada of MMT. Three legal challenges to the legislation were launched against the Government of Canada: an investor-State challenge under the North American Free Trade Agreement (NAFTA) Chapter Eleven by Ethyl Corporation; a constitutional challenge in the Ontario Court by Ethyl's Canadian affiliate (Ethyl Canada); and a dispute settlement panel was established under the Agreement on Internal Trade (AIT) at the request of Alberta (joined by three other provinces).

On 20 July 1998, the Government announced its decision to lift the trade restrictions on MMT by removing MMT from the schedule to the Act. This decision responded to the AIT Panel recommendations announced 19 July 1998, concerning the inconsistency of the Act with obligations under the AIT. The Government also dealt with the investor-State challenge launched by Ethyl Corporation and the constitutional challenge in the Ontario Court. Under the terms of settlement, the Government paid $13 million to Ethyl, representing reasonable and independently verified costs and lost profits in Canada. Ethyl dropped both claims.

At the time of settlement, the NAFTA case had not moved beyond a preliminary jurisdictional challenge initiated by the Government, and the merits of the claim had not yet been heard.

Studies in Canada and the United States are proceeding on the impact of MMT and other fuel additives on health and automotive tailpipe emissions. If subsequent federal government action is warranted, the Government would use the Canada Environmental Protection Act, based on further scientific analysis and full disclosure of data.

/...

(Box 1, concluded)

The case has raised concerns as to whether regulatory measures in the field of environment, public health and similar areas will be regarded as takings and that compensation could be claimed under the takings provision in treaties. The issue raised is whether acts such as Government interferences in areas like land use planning, health and zoning matters and similar areas could be construed as takings which are compensable under the takings provisions of IIAs.

Source: UNCTAD.

Notes

1 Much of the arbitral jurisprudence on creeping expropriations was produced by the Iran-United States Claims Tribunal, where the issue of creeping expropriation has been considered in several cases. They are surveyed in Aldrich, 1996.

2 There were State interferences in alien property before. But, the history of large-scale takings begins only with the socialist takings and takings in pursuance of social reform. For analyses of takings that have occurred, see Burton and Inoue, 1984. The authors found 1,857 cases of takings between 1960 and 1977.

3 The standard is referred to as the "Hull standard" or formula as it was contained in a letter of the then Secretary of State, Cordell Hull to the Government of Mexico (Kunz, 1940).

4 One of the most discussed in the literature is the Indonesian nationalization of Dutch property. It attracted much litigation in Europe. See for example McNair, 1959; Domke, 1960; Sornarajah, 1986b.

5 The doctrine began life in the form of economic self-determination in a General Assembly resolution in 1952 (res. 626 (VII) 21, December 1952); see Hyde, 1956, p. 854. The early resolutions linked self-determination with permanent sovereignty over natural resources (see res. 1314 (XIII) 1958). The resolution that had unanimous support was resolution 1803 (XVII) of 14 December 1962. It had no negative votes as it represented a compromise between the different views of States. While the doctrine was recognized and appropriate compensation was to be paid in the event of nationalization, thus representing

a victory for the position of the developing countries, the resolution required that "foreign investment agreements freely entered into by or between sovereign States shall be observed in good faith", thereby securing the interests of the developed countries (Schwebel, 1963, pp. 463-469).

6 The resolution on a New International Economic Order was passed by the Sixth Special Session of the General Assembly; res. 3201 (S-VI) 1974. The Charter of Economic Rights and Duties of States which is contained in General Assembly res. 3281 (XXIX) 1974 had, in its article 2(2)(c), the controversial proposition that issues of compensation should be settled by national courts only. This was in fact an assertion of the Calvo doctrine. (The "Calvo doctrine" denotes the idea that foreign investors are, or ought to be, required to settle their foreign investment disputes exclusively in the courts of the host State.) France, Germany, Japan, United Kingdom and the United States refused to accept this provision. Later resolutions retreated from this position.

7 The Libyan nationalizations of United States oil companies in 1973 are the last major example. They resulted in leading arbitral decisions on the subject: BP v. Libya, 1973; Texaco v. Libya, 1973; and Liamco v. Libya, 1977.

8 The possibility of large-scale nationalizations recurring is contemplated in the literature; see Penrose, et al., 1992.

9 On "tolerable" takings, see Higgins, 1982.

10 For further discussion of the dispute, see Zedalis, 1996; Graham, 1998; and Soloway, 1999.

Section I
EXPLANATION OF THE ISSUE

A. Categories of takings

From the discussion in the Introduction, a number of categories of takings can be identified. They include:

- **Outright nationalizations in all economic sectors.** These measures result in the termination of all foreign investment in a host country. They are usually motivated by policy considerations; the measures are intended to achieve complete State control of the economy and involve the takeover of all privately-owned means of production. [1]

- **Outright nationalizations on an industry-wide basis.** Here, a host country seeks to reorganize a particular industry, by taking over the private enterprises in the industry and creating a State monopoly. [2]

- **Large-scale taking of land by the State.** Usually the purpose for such takings is to redistribute land to the landless.

- **Specific takings.** In such cases, a foreign firm (such as a firm dominating a market or industry) or a specific lot of land (such as that necessary to build a road) is the target of the taking. The issue of legal significance is that no discrimination can usually be alleged in such a case (Amco v. Indonesia, 1992).

- **Creeping expropriation.** This may be defined as the slow and incremental encroachment on one or more of the ownership rights of a foreign investor that diminishes the value of its investment. The legal title to the property remains vested in the foreign investor but the investor's rights of use of the property are diminished as a result of the interference

by the State (box 2). There is an accumulation of authority that assimilates creeping expropriation with the first three categories of takings (Zedalis, 1996; Paasivirta, 1990).

Box 2. Examples of creeping expropriation

- Forced divestment of shares of a company;
- interference in the right of management;
- appointment of managers;
- refusal of access to labour or raw materials;
- excessive or arbitrary taxation.

Source: UNCTAD.

- **Regulatory takings.** Regulatory takings are those takings of property that fall within the police powers of a State, or otherwise arise from State measures like those pertaining to the regulation of the environment, health, morals, culture or economy of a host country.

A taking by a host country destroys the ownership rights of an investor in its tangible or intangible assets. The first four categories of takings identified above clearly accomplish this, and the rules of international law apply to them, although there is still controversy as to the precise consequences. It is the last two categories of takings that present new and difficult legal issues.

B. Requirements for a lawful taking

A taking is lawful provided it satisfies certain conditions. To begin with, special limitations on a State's right to take property may be imposed by treaty. In customary international law, there is authority for a number of limitations or conditions that relate to:

- the requirement of a public purpose for the taking;
- the requirement that there should be no discrimination;

- the requirement that the taking should be accompanied by payment of compensation; and,
- the requirement of due process.

1. Public purpose

This requirement is not complicated. Usually, a host country's determination of what is in its public interest is accepted.[3] There is some indication that, where a taking is by way of reprisal against the act of a home State of a foreign national, it is considered illegal on the ground that it lacks public interest.[4]

2. Non-discrimination

Traditionally, the requirement relating to the absence of discrimination was directed particularly at the singling-out of aliens on the basis of national or ethnic origin. Where the taking, specific or general, is racially motivated, it is clearly violative of the *ius cogens* norm against racial discrimination and hence illegal (Sornarajah, 1994). In fact, the non-discrimination requirement would imply that measures that can be construed as expropriations be across-the-board. Progressively however, as the issue of regulatory takings becomes prominent, any taking that is pursuant to discriminatory or arbitrary action, or any action that is without legitimate justification, is considered to be contrary to the non-discrimination requirement, even absent any singling-out on the basis of nationality. This includes prohibition of discrimination with regard to due process and payment of compensation requirements. Moreover, the non-discrimination requirement demands that governmental measures, procedures and practices be non-discriminatory even in the treatment of members of the same group of aliens.

3. Compensation

The issue that is most likely to raise a dispute in the taking of alien property is the standard of compensation that is payable to a foreign investor. Historically, communist States, in keeping with the principle that there cannot be private ownership of property,

took the view that no compensation is payable. This is not the current view taken by some communist States.[5] Capital exporting States have usually taken the position that the Hull standard of prompt, adequate and effective compensation should be met. This requires the payment of full market value as compensation, speedily and in convertible currency.[6] Some developing countries have taken the position that the payment of "appropriate compensation" would be sufficient. This is a vague standard, but the idea is that inability to pay immediate and full compensation should not deter a State which decides that it is necessary to take foreign property in the interest of economic development, from doing so. The standard of appropriate compensation contemplates that equitable principles should be the guide in the matter of assessing compensation rather than a hard and fast rule relating to market value. It implies a variable standard that permits consideration of past practices, the depletion of natural resources, possible lack of foreign exchange and other factors such as environmental damage.[7] Another variation used in investment agreements that do not adopt the Hull formula is an explicit reference to the book-value method of valuation. This may consist of either the net book value (depreciated assets value) or the updated book value, also referred to as the adjusted book value, taking inflation into account. Alternatively, the tax value of the assets could be referred to.[8] More generally, each of the competing formulas of compensation have acquired a certain symbolic value: the "Hull formula" suggests a fuller, more satisfactory to the investor type compensation, while the "appropriate compensation" formula suggests that additional concrete (historical or other) considerations may be taken into account which will result in a lower final payment.

The distinction between regulatory and other types of takings will cause concern in the future with regard to compensation.[9] The novel problem that has to be worked out is the extent to which regulatory actions by a State could be regarded as compensable takings. Clearly, a taking in response to criminal conduct by a foreign investor or in response to a violation of penal or other laws of a host country is legitimate and is not compensable as compensation will negate the punitive purpose behind such takings. This issue has been addressed in some international instruments.

For example, the first protocol of the European Convention on Human Rights specially states that punitive and tax measures are not to be regarded as violations of the right of property (Brownlie, 1992).[10] Perhaps, such punitive takings should be regarded as a separate category of takings. Punitive takings could be defined as responses to violations of laws by a foreign investor. In fact, they can be simply regarded as typical confiscations under criminal law.

But, the issue arises as to which non-punitive regulatory measures are to be treated like takings for which compensation is due. In many States, regulatory structures have been built up to harness the foreign investment to the economic objectives of a host country or to prevent harm to the economy, environment, health, morals or culture of the host country. An issue that could frequently arise in the future with regard to the response of international law to these non-punitive regulatory measures is the basis of assessment of compensation, if any.[11]

This can be an important issue if, for example, regulatory measures to protect the environment were to be included in the scope of treaty protection provisions against regulatory takings. Such provisions, it has been argued, would insure a foreign investor from the consequences of the environmental harm the foreign investment causes and hence remove all deterrence against the causing of such environmental harm. There is, also, the likelihood that Governments may be wary of challenges to the underlying scientific validity of their measures in case investors assert that there is no conclusive proof that there is danger from their production processes. Another objection is that whilst local business is subject to regulatory interferences in the environmental interest, foreign investment would be protected from such interferences. The argument is also made that, as a result of treaty protection against regulatory harm, a foreign investor may obtain greater protection in the international sphere than it would under the laws of its own home country.[12]

The issue also arises as to the conflict between IIAs containing protection against regulatory takings and conventions asserting environmental standards which form the basis of international

environmental laws. A State effecting a regulatory taking may be conforming to the convention containing the environmental standard but may be contravening the IIA by not paying compensation. In that regard, IIAs have to be drafted taking into account possible conflicts with other international arrangements.

4. The due process requirement

In large-scale nationalizations in the past, countries often expressly denied judicial review of compensation. The requirement that the compensation due to a foreign investor should be assessed by an independent host country tribunal is now found in the takings provisions of many bilateral and some regional agreements. This requirement is usually satisfied by the legislation effecting the taking which will provide for the mechanism for the assessment of the compensation. Thus due process may be met by other kinds of regular administrative procedures other than courts of law. However, there remains some uncertainty as to the interpretation of the term "due process" in international law. [13]

Notes

1 For example, the Russian nationalizations after the October Revolution.

2 For example, the Chilean nationalization of its copper industry; or the Iranian nationalization of its oil industry.

3 The *Restatement of the Law: The Foreign Relations Law of the United States* points out in its commentary that, for these purposes, "...public purpose is broad and not subject to effective reexamination by other states" (American Law Institute, 1987, p. 200). The European Court of Human Rights, considering the issue of taking in violation of the right to property under the first protocol of the European Convention on Human Rights, has held that it will "respect a national legislature's judgement as to what is in the public interest ... unless that judgement is manifestly without reasonable foundation" (James v. United Kingdom, 1986, p. 123).

4 The consequence of an illegal taking is that reparation will not be confined to the making good of the loss alone but additional factors such as loss of future earnings could be taken into account in calculating the damages owed to a foreign investor (BP v. Libya, 1973).

5 For example, an earlier Chinese position of an absence of a requirement to compensate has changed; China has recognized an obligation to compensate in several bilateral investment treaties, and its present position is to accept that compensation should follow takings of foreign property, though the exact standard of compensation is left in doubt (Chew, 1994).

6 The last part of the requirement creates a significant interaction with the issue of funds transfer. See further section III below.

7 There is no standard definition of "appropriate compensation"; see Sornarajah, 1994.

8 For an overview of the issue of compensation, see UNCTAD, 1998, pp. 67-71.

9 A study of takings in the context of domestic law that adverts to the difficulty of distinguishing between different types of takings is contained in Epstein, 1985; a recent survey of the law on takings in the United States is contained in Alexander, 1996. Because of the increasing prevalence of regulatory takings in the international sphere, there would be a tendency to transfer arguments in the domestic sphere into the international sphere.

10 There is further authority for this category of non-compensable regulatory takings. The *Restatement of the Law: The Foreign Relations Law of the United States* recognizes this category: "A state is not responsible for loss of property or for other economic disadvantage resulting from bona fide general taxation, regulation, forfeiture for crime, or other action of the kind that is commonly accepted as within the police power of states..." (American Law Institute, 1987, p. 201).

11 There is rich case law on whether regulatory takings are compensable and the basis on which such compensation, if any, should be assessed. See Mellacher v. Austria, 1990; Fredin v. Sweden, 1991; further see Jacobs and White, 1996. For a problem concerning regulatory takings, see Mobil Oil v. New Zealand, 1989.

12 For these arguments, see Graham, 1998.

13 There is reference to the due process requirement in the judgment of the International Court of Justice in the ELSI Case, 1989, at para. 128, where the Court said that "...a wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety" will amount to a denial of justice. There is also reference to a pre-taking due process requirement in Amco v. Indonesia, 1992. This requirement was based on the view that due process is a general principle of international law. A contrary view expressed is that the authority for such a proposition was not adequately canvassed in the award (Sornarajah, 1995).

Section II
STOCKTAKING AND ANALYSIS

This section of the paper takes stock of the manner in which existing investment instruments have dealt with the main issues identified in section I. It first deals with what amounts to a taking. It then focuses on requirements for a taking to be lawful.

A. What amounts to a taking?

In the early instruments on foreign investment, the terms mostly used to describe takings were "nationalization" or "expropriation". Though the distinction between the two terms was not clearly made, they basically applied to the taking of property by the State through legislative or administrative measures. Modern BITs[1] started to widen the types of takings to include indirect takings so that any diminution in the value of property due to Government action would be caught up in the definition of takings. The treaty practice, however, still refers to "nationalization" or "expropriation" as the benchmark of takings and refers to indirect takings as "measures tantamount to nationalizations" or "measures having effect equivalent to nationalization or expropriation".[2] It indicates a reluctance to move away from the paradigm of the law that was developed in the context of direct takings, despite the fact that the legal form of takings has now undergone a change.

But, with the emphasis shifting to regulatory and other erosions of the rights of a foreign investor, a definition of takings that was not tied to the idea of nationalizations or expropriation had to be found. To be able to deal with the problem of indirect takings, BITs, while retaining the old notion of "nationalization" or "expropriation" increasingly sought to give a wider definition to those terms. For example, the Germany-Bangladesh BIT (1981) includes in its protocol, section 3, "the taking away or restricting of any property right which in itself or in conjunction with other rights constitutes an investment" (ICSID, 1981, p. 7). In some treaties, the prevention of "dispossession" was one primary aim

of the treaty. Thus, the Belgium-Cyprus BIT (1991) in article 4 states :

> "Each Contracting Party undertakes not to adopt any measure of expropriation or nationalization or any other measure having the effect of directly or indirectly dispossessing the investors of the other Contracting Party of their investments..."(ICSID, 1991, p. 5).

The formulation in the Argentina-Sweden BIT (1991) provides an example of a technique that calls for the viewing of ownership of property as involving a bundle of rights so that the infringement of any one of the rights will amount to a taking.[3] Article 4 reads:

> "Neither of the Contracting Parties shall take any direct or indirect measure of nationalization or expropriation or any other measure having the same nature or the same effect..." (ICSID, 1991, p. 4).

It is not the physical invasion of property that characterizes nationalizations or expropriations that has assumed importance, but the erosion of rights associated with ownership by State interferences. So, methods have been developed to address this issue. The tendency in some cases has been to analogize the infringement of any right of ownership with nationalization or expropriation. This is the position adopted by the World Bank Guidelines on the Treatment of Foreign Direct Investment (1992) and the Energy Charter Treaty (1994), both of which seek to widen the definition of nationalizations or expropriations to include any measures producing effects akin to those of nationalization or expropriation. Article IV(1) of the World Bank Guidelines ties indirect takings to nationalizations or expropriations by referring to nationalizations or expropriations and then stating "or take measures which have similar effects". Similarly, article 13 (1) of the Energy Charter Treaty, reads:

> "Investments of Investors of a Contracting Party in the Area of any other Contracting Party shall not be nationalized, expropriated or subjected to a measure

> or measures having effect equivalent to nationalization or expropriation (hereinafter referred to as "Expropriation") except where ..." (UNCTAD, 1996, vol. II, p. 558).

The alternative strategy is to give examples of the type of measures that could amount to takings so as to illustrate the width of the concept. Thus, for example, article 3 of the United States model BIT (1982)[4] refers to "any other measure or series of measures, direct or indirect, tantamount to expropriation (including the levying of taxation, the compulsory sale of all or part of an investment, or the impairment or deprivation of its management, control or economic value) ...". Canadian treaties have adopted yet another strategy to deal with specific regulatory interferences by addressing the issues as to circumstances in which these interferences could be regarded as takings (box 3).

Box 3. Examples of takings in Canadian IIAs

Tax measures. Tax measures could amount to a taking, particularly in circumstances where they are raised to siphon off profits that a foreign investor is seen as making. Canadian BITs specifically provide for situations regarding tax measures. They state that tax measures will not be affected by the provisions of the treaties; but that where there is a claim of excessive taxation, then the parties to the treaty will jointly determine whether the measure of taxation amounts to an expropriation. This is an innovative method of dealing with this situation. It is, however, unlikely that the State imposing the measure would accept that the measure amounts to an expropriation. In this case, a dispute would arise that under the terms of the treaty could be submitted to arbitral decision.

Compulsory licensing of technology. Canada has another innovation in its treaties relating to compulsory licensing of technology protected by patents and other forms of industrial property. Compulsory licensing is a regulatory measure that prevents a company from keeping unutilized patents. Potentially, where such licensing of technology

/...

(Box 3, concluded)

belonging to a foreigner is ordered by a host country, there would be a taking of the intellectual property. The treaties state that such compulsory licensing requirements should be imposed only by courts or other competent tribunals, acknowledging that such infringements will not amount to takings protected by the treaty, provided some due process requirements have been satisfied.

Management control. Some Canadian treaties also specifically provide for the situation in which managers and directors are appointed by the State to impair the control of the company set up by a foreign investor.

Interferences in financial sectors. The Canadian treaties also exempt interferences in the financial services sector from the scope of the protection given in the treaties. Here again, there is a consciousness shown that regulatory interferences in certain areas should not be regarded as amounting to takings.

Source: UNCTAD, based on Canada-Barbados BIT, 1996; Canada-Venezuela BIT, 1996; Canada-Ecuador BIT, 1996.

The Organisation for Economic Co-operation and Development (OECD) Draft Multilateral Agreement on Investment (MAI) also addresses the issue of indirect expropriation. Interestingly, it does so in two ways. First article IV(2) on expropriation states that " A Contracting Party shall not expropriate or nationalise directly or indirectly an investment ... of an investor of another Contracting Party...". It then continues "or take any measure or measures having equivalent effect..." (UNCTAD, forthcoming). The reason for this double reference may well be the difference in BIT tradition between the OECD countries. Whereas some of them prefer the "directly or indirectly" approach, others are used to the "equivalent effect" approach. Since yet others are using the double reference, this may have resulted in a compromise combining both approaches.

At a much later stage during the MAI negotiations non-governmental organizations and others, who first saw this text, feared that the double reference was meant to imply a broader definition of indirect expropriation than was used in most BITs so far. They specifically feared that this article, combined with the investor-State dispute settlement article, would have a negative effect on the ability of Governments to enact and implement new legislation in environmental and other fields.[5] The Ethyl case was used as an example to demonstrate this possibility.

In a reaction to these concerns, the MAI negotiators discussed several options to address the issue. They agreed on the objective of protecting Government regulators and their normal non-discriminatory work. They also agreed that this was a broader issue, not just relevant to environmental regulations. The solutions discussed included a general exception such as that of the General Agreement on Tariffs and Trade (GATT), article XX[6] and a clarification approach such as that of NAFTA, article 1114 (1).[7] This debate was not concluded before the negotiations came to a stop. However, in the Ministerial statement on the MAI of 28 April 1998, the ministers confirmed "that the MAI must be consistent with the sovereign responsibility of governments to conduct domestic policies. The MAI would establish mutually beneficial international rules which would not inhibit the normal non-discriminatory exercise of regulatory powers by governments and such exercise of regulatory powers will not amount to expropriation" (OECD, 1998, p. 1).[8]

This text clearly covers not only environmental measures, but also all other sorts of regulatory measures taken by Governments. It does not contain a "carte blanche" for Government regulators, since it refers to "normal" exercise of regulatory powers. This is in line with the references to "arbitrary or unjustifiable discrimination or a disguised restriction on investment" in GATT, article XX and "otherwise consistent with this Chapter" in NAFTA, article 1114(1). Presumably, "normal" should be compared with words like "bona fide" and "commonly accepted". In the context of expropriation it refers to jurisprudence on what constitutes a compensable taking and what amounts to a truly regulatory non-compensable taking. Thus in the MAI context, while discussions on possible additions

to the text were never finalized, it was felt necessary to issue a political declaration on the relation between regulation and expropriation.

The extent to which States will accept that regulatory measures could be covered by a takings provision remains uncertain. This is a concern that affects not only developing but also developed countries, some of which are among the largest recipients of foreign investment flows. Since developed countries have considerably more regulatory legislation in areas such as antitrust, corporate securities, environment and planning, they may show a greater reluctance in participating in treaties that transfer review of these matters to international tribunals.[9] The idea that State policies could be litigated or arbitrated before foreign courts or arbitration tribunals will cause unease to any State. It is for this reason that States may seek a narrower definition of taking or require that there are limiting criteria that would not make all regulatory interferences subject to the treaty provisions.[10]

B. Provisions on requirements for the legality of takings

IIAs recognize that it is lawful for a host country to take alien property provided four requirements are met. These four requirements (outlined below) are stated in almost all investment agreements, though terminology varies. There is considerable similarity among IIAs as to the provisions on public purpose and non-discrimination. It is as to the requirement relating to the standard of compensation that there is variation. As for due process there remains, as indicated before, some uncertainty about the meaning of the term.

1. Public purpose

Almost all IIAs contain the requirement, in varying terminology, that there must be a public purpose for the taking. For example, NAFTA states, in article 1110 (1) (a):

> "No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:
>
> (a) for a public purpose ..." (UNCTAD, 1996, vol. III, p. 79).

The BIT between the Netherlands and Sudan (1970) provides in article XI that:

> "The investments of nationals of either Contracting Party in the territory of the other Contracting Party shall not be expropriated except for the public benefit and against compensation" (UNCTAD, 1998, p. 68).

The public purpose requirement is usually included in IIAs, despite the fact that, as already noted, a host country's determination that its taking was for a public purpose is seldom challenged. Yet, this requirement continues to be stated either because it is time hallowed or because of the still remaining view that a taking by way of a reprisal lacks a public purpose (BP v. Libya, 1973). Sometimes, this limitation is made clear, as in the United Kingdom-Costa Rica BIT (1982) which states that "the public purpose must be related to the internal needs" of the country (UNCTAD, 1998, p. 68). The formulation clearly applies to takings by way of reprisals which are acts of external policy. But, this rule relating to takings by way of reprisals can be derived from customary law, without the aid of treaty provisions.

2. Non-discrimination

The non-discrimination requirement continues to have relevance with regard to takings, as it affects the legality of a taking, and therefore the quantum of compensation. Examples of the formulation of this requirement in IIAs are article 5 of the United Kingdom model BIT (1991) and article 1110(1)(b) of the NAFTA. Similarly, the Chinese model BIT (1994), article 4 states:

> "Neither Contracting Party shall expropriate, nationalize or take similar measures (hereinafter referred to as "expropriation") against investments of investors of the other Contracting Party in its territory, unless the following conditions are met:
>
> (a) for the public interests;
> (b) under domestic legal procedure;
> (c) without discrimination" (UNCTAD, 1996, vol. III, p. 153).

In the Japan-China BIT (1988), article 5 (2) states:

> "Investments and returns of nationals and companies of either Contracting Party shall not be subjected to expropriation, nationalization or any other measures the effects of which would be similar to expropriation or nationalization, within the territory of the other Contracting Party unless such measures are taken for a public purpose, ... are not discriminatory, and ..." (UNCTAD, 1998, p. 68).

Another similar formulation can be found in the Energy Charter Treaty, article 13 (1):

> "Investments of Investors of a Contracting Party in the Area of any Contracting Party shall not be nationalized, expropriated or subjected to a measure or measures having effect equivalent to nationalization or expropriation (hereinafter referred to as "Expropriation") except where such Expropriation is...... (b) not discriminatory ..." (UNCTAD, 1996, vol. II, p. 558).

3. The standard of compensation

There is no uniformity in IIAs as to the standard of compensation that should apply upon a taking. A multiplicity of methods is employed in dealing with the matter, and much has depended on the bargaining

strengths of the parties in the type of protection that is secured. Moreover, whatever the formulation of the standard of compensation, attention must be paid to the method of valuation of property that had been subject to a taking, which might be decisive on the issue.

The terminology preferred by some countries particularly developing ones is "appropriate compensation". The genesis of the term can be traced to a series of General Assembly resolutions associated with a New International Economic Order and Permanent Sovereignty over Natural Resources. In some cases, this standard has been construed to reflect the view that full compensation need not always follow upon expropriation, to provide the host country more flexibility in determining the compensation to be paid. There are treaties and other instruments that incorporate this view. For example, Model "B" of the Model Agreements on Promotion and Protection of Investments of the Asian-African Legal Consultative Committee (AALCC) provides in its first alternative formulation of article 7(i) that:

> "A Contracting Party may exercise its sovereign rights in the matter of nationalization or expropriation in respect of investments made... upon payment of appropriate compensation..." (UNCTAD, 1998, p. 231).

The provision, in its first alternative in part (ii), defines appropriate compensation as "compensation calculated on the basis of recognized principles of valuation"(ibid., p. 232). Thus, there exists some flexibility for the host State to choose amongst different recognized principles of valuation.

The BIT between China and Thailand (1985) provides a variant of this formulation. Article 5 (1)(a) provides:

> "Only for the public interest and against compensation may either Contracting Party expropriate, nationalize or take similar measures.... Such compensation shall be equivalent to the appropriate value of expropriated investments ..." (United Nations, 1986, p. 56).

Again, the provision provides for a certain flexibility on the issue of the determination of the amount of compensation.

The alternative view which involves the use of the Hull formula has received recently increasing support. In particular, developing countries are prepared to deviate from standards that they have espoused collectively in the past as shown in the BITs they now conclude not only with developed countries but also with other developing countries (Guzman, 1998).[11] Of the treaties made in 1995, only one, the Netherlands-Oman treaty, uses the formula "just compensation" but it is followed by the requirement of market value being paid. Another formula refers to compensation without qualification but uses a method of valuation which will result in the payment of market value of the property taken. The Chinese model BIT, article 4(2), for example, states that "the compensation.....shall be equivalent to the value of the expropriated investments at the time when expropriation is proclaimed..." (UNCTAD, 1996, vol. III, p. 153). The German model BIT in article 4 refers to compensation "equivalent to the value of the expropriated investment immediately before the date on which the actual or threatened expropriation, nationalization or comparable measure has become publicly known" (UNCTAD, 1996 vol. III, p. 169). The China-Japan BIT (1988) does not refer to market value but to restitution, that is restoration to the status quo ante. A further variation encountered in some BITs is a reference to the book-value method of valuation. This may involve either the net book value, also referred to as the depreciated assets value, or the updated book value, also referred to as the adjusted book value. One example of this approach can be found in the BIT between the Netherlands and Sudan (1970) where, by article XI, compensation shall represent the equivalent to the depreciated value of the investment (UNCTAD, 1998, p. 68).

It should be pointed out that the BITs practice of some individual countries does not show a uniform pattern. Thus, China, a prolific maker of such treaties, has used a variety of standards on compensation. Its treaty with Australia (1988) refers to the Hull standard but its treaty with France (1984) refers to appropriate compensation. Its treaties with Singapore (1985) and New Zealand

(1988) simply mention compensation without any qualification. Negotiations with the United States on an investment treaty appeared to have failed because there could be no agreement, among other things, on the standard of compensation (Lin and Allison, 1994). Even Singapore, a State traditionally hospitable to foreign investment, lacks uniformity in this area. There are treaties that Singapore has made that refer to the Hull standard and those that refer to the alternative standard of "appropriate compensation" (Sornarajah, 1986a).

The regional instruments also seem to favour the payment of full compensation upon a taking. Thus, NAFTA and the Energy Charter Treaty both use the Hull formula. The NAFTA provisions are elaborate, refer to fair market value but are essentially a paraphrasing of the Hull standard (Levy, 1995) (box 4).

Box 4. The NAFTA provision on taking

Article 1110: Expropriation and Compensation

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:

   (a) for a public purpose;
   (b) on a non-discriminatory basis;
   (c) in accordance with due process of law and Article 1105(1); and
   (d) on payment of compensation in accordance with paragraphs 2 through 6.

2. Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation"), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.

/...

(Box 4, concluded)

3. Compensation shall be paid without delay and be fully realizable.

4. If payment is made in a G7 currency, compensation shall include interest at a commercially reasonable rate for that currency from the date of expropriation until the date of actual payment.

5. If a Party elects to pay in a currency other than a G7 currency, the amount paid on the date of payment, if converted into a G7 currency at the market rate of exchange prevailing on that date, shall be no less than if the amount of compensation owed on the date of expropriation had been converted into the G7 currency at the market rate of exchange prevailing on that date, and interest had accrued at a commercially reasonable rate for that G7 currency from the date of expropriation until the date of payment.

6. On payment, compensation shall be freely transferable as provided in Article 1109.

7. This Article does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights, or to the revocation, limitation or creation of intellectual property rights, to the extent that such issuance, revocation, limitation or creation is consistent with Chapter Seventeen (Intellectual Property).

8. For purposes of this Article and for greater certainty, a non-discriminatory measure of general application shall not be considered a measure tantamount to an expropriation of a debt security or loan covered by this Chapter solely on the ground that the measure imposes costs on the debtor that cause it to default on the debt.

Source: UNCTAD, 1996, vol. III, pp. 79-80.

The Energy Charter Treaty uses the Hull standard directly.[12] Likewise, the APEC Non-Binding Investment Principles (1994) also adopted the Hull standard. The World Bank Guidelines specify "appropriate compensation", but go on to redefine the standard as no different from prompt, adequate and effective compensation. They state, in article IV (2):

> "Compensation for a specific investment taken by the State will, according to the details provided below, be deemed "appropriate" if it is adequate, effective and prompt" (UNCTAD, 1996, vol. I, p. 252).

In line with the traditional position of capital exporting States, the MAI (chapter IV(2)) uses the Hull standard.

Overall, there is a trend in modern BITs towards the Hull standard of compensation. Though the traditional formula of "prompt, adequate and effective" compensation may not always be used, the treaties spell out the meaning of the formula in different, yet roughly equivalent ways. Thus, the Singapore-Mongolia BIT (1995) uses the words "effectively realizable" and "without unreasonable delay" and require that compensation shall be "the value immediately before the expropriation". The reference is to a standard no different from the Hull standard. The Hull standard is employed in BITs between developed and developing countries as well as in BITs between developing countries. While there are still modern BITs that use other formula such as "just compensation", even in such cases the treaties may spell out that the assets taken should be given a market value.[13]

4. Due process

The due process requirement is found in a variety of treaties, particularly those that the United States has concluded. The term "due process" itself is terminology that distinctly relates to United States law. In fact, it has no definite content except in United States law. Yet, it is employed in treaties entered into by other countries (for example, the Chile-Sweden BIT (1993)). However, the view that a taking must be reviewed by appropriate, usually judicial, bodies (especially in relation to the assessment of compensation) finds expression in the practice of a large number of States and is indeed found in many national constitutional provisions. For example, the United Kingdom model BIT (1991) states in article 5 (1):

"... The national or company affected shall have a right, under the law of the Contracting Party making the expropriation, to prompt review, by a judicial or other independent authority of that Party, of his or its case and of the valuation of his or its investment in accordance with the principles set out in this paragraph" (UNCTAD, 1996, vol. III, p. 188).

Another example is the Chilean model agreement which in article 6 (3) provides that:

"The investor affected shall have a right to access, under the law of the Contracting Party making the expropriation, to the judicial authority of that Party, in order to review the amount of compensation and the legality of any such expropriation or comparable measure" (ibid., p. 146).

While bilateral investment dispute provisions do mention due process requirements, they usually seem to allude to the requirement only after a taking so that there could be a review of whether proper compensation standards were used in assessing the compensation. They do not face the issue of whether or not a foreign investor should be given an opportunity to show the regulatory authority the reason why measures proposed by it should not be taken against the investor. Indeed, this is a matter of the internal public law of the host State. Should proper procedural standards not be followed in such a case, then a different set of questions arises from those relating to the issue of expropriation, in particular, whether an investor has suffered a denial of justice for which no effective domestic remedy exists. That is an issue of State responsibility in general and not an issue related to expropriation as such.

Notes

1 For a comprehensive study on modern BITs, see UNCTAD, 1998.

2 For example, article 5 of the United Kingdom model BIT (1991) reads : "Investments of nationals or companies of either Contracting Party shall not be nationalised, expropriated or subjected to measures having effect equivalent to nationalisation or expropriation...." (UNCTAD, 1996, vol. III, p. 188). (Unless otherwise noted, the texts of the BITs mentioned in this study may be found in the United Nations Treaty Series or in the collection of BITs maintained by the International Centre for Settlement of Investment Disputes (ICSID) (ICSID, 1970—). Similarly, unless otherwise noted, all instruments cited herein may be found in UNCTAD, 1996 or forthcoming.)

3 In developed systems, ownership is regarded as a bundle of rights a person has against others. These ideas have been developed more fully in the context of United States constitutional law on taking of private property (Michelman, 1967; Epstein, 1985).

4 See Vandevelde, 1992, appendix A-1 for the full text of the model BIT; the United States-Zaire BIT (1984) also contains this provision.

5 See for example, Council of Canadians, "Under the MAI it would be considered a form of expropriation if the federal government or a province moves to enact new laws to protect the enviornment, wilderness, species or natural resource prodution" (Council of Canadians, 1998, p. 1).

6 "Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any contracting party of measures: ... (b) necessary to protect human, animal or plant life or health ... (g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption." ... (United Nations, 1950, p. 262).

7 "Nothing in this Chapter shall be construed to prevent a Contracting Party from adopting, maintaining or enforcing any measure otherwise consistent with this Chapter that it considers appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental concerns" (UNCTAD, 1996, vol. III, p. 81).

8 In the broader context of an Expert Group Meeting of the UNCTAD Commission on Investment, Technology and Related Financial Issues, dealing with international investment agreements, the Agreed Conclusions noted similarly: "that flexibility, including with regard to a Government's normal

ability to regulate, can be reflected, *inter alia,* in the objectives, content, implementation and structure of IIAs" (UNCTAD, 1999a, p.2).

9 The possibility of such a review is raised in Mobil Oil v. New Zealand, 1989.

10 NAFTA specifically excludes environmental measures from the scope of the taking provisions. But, the issue arises as to whether environmental regulation is the only sphere of regulation that should be excluded.

11 In a few cases (Brazil-Venezuela (1995), Ecuador-Paraguay (1994), Peru-Paraguay (1994) BITs) the more general expression "just compensation" is used. In most cases however, in relation to the value of the expropriated investment, the terms "market value", "fair market value", or "genuine value" immediately before the expropriatory action was taken or became known, is stipulated.

12 For an interpretation of the provision in the Energy Charter Treaty, see Norton, 1996 and Sornarajah, 1996.

13 The increasing usage of the Hull standard may not be conclusive for, despite such use in many other instruments, some arbitral tribunals have regarded the standard in treaties covering disputes before them as indicating a mere starting point for the calculation of the compensation that is finally to be awarded. In the Shahin Shane Ebrahimi Claim, a dispute covered by a Friendship, Commerce and Navigation treaty using the Hull standard, Judge Gaetano Arangio-Ruiz concluded that considering the scholarly opinions, arbitral practice and tribunal precedents, once full value of the property has been properly evaluated, the compensation to be awarded must be appropriate to reflect the pertinent facts and the circumstances of each case (Shahin Shane Ebrahimi v. Iran, 1995).

Section III
INTERACTION WITH OTHER ISSUES AND CONCEPTS

The issue of taking of foreign property is central to the risk perceptions in foreign investment. Hence, the issue has relevance to a wide variety of other issues and concepts in the area of foreign investment.

Table 1. Interaction across issues and concepts

Concepts in other papers	Taking of property
Scope and definition	+ +
Admission and establishment	+
Incentives	0
Investment-related trade measures	+
National treatment	
Most-favoured-nation treatment	+ +
Fair and equitable treatment	+ +
Taxation	+
Transfer pricing	+
Competition	+
Transfer of technology	+
Employment	+
Social responsibility	+
Environment	+ +
Home country measures	+
Host country operational measures	0
Illicit payments	+
State contracts	+ +
Funds transfer	+ +
Transparency	+
Dispute settlement (investor-State)	+ +
Dispute settlement (State-State)	+ +
Modalities and implementation	+

Source: UNCTAD.

Key: 0 = negligible or no interaction.
+ = moderate interaction.
++ = extensive interaction.

- **Scope and definition** (UNCTAD, 1999d). Firstly, the issue of taking concerns the definition of foreign investment because the protected investment is defined in the scope and definitions provisions of IIAs. In the past, the concern was only with the physical property of a foreign investor. In modern times, the concern is not so much with the physical property but with the antecedent rights that are necessary for the enjoyment of these property rights as well as with incorporeal property such as patents, copyright and other rights connected with intellectual property and shares in companies which play a crucial role in international business. Most recent BITs include intellectual property within the definition of investment so that, if there are infringements of intellectual property rights by State interference, there would be a taking. So too, contractual rights and regulatory rights associated with the making of an investment are included within the definition of foreign investment in treaties. For example, a progressive enlargement of the categories of protected assets is reflected in the newer IIAs, a number of which have included within the definition of investment descriptions like "any right conferred by law or contract, and any licenses and permits pursuant to law" (United States-Sri Lanka 1991 BIT, article 1) (ICSID, 1991, p. 2). This partly indicates concern on the part of developed countries with the newer problem of regulatory takings resulting from controls on foreign investment instituted by developing States.

  But many developing countries continue to preserve their regulatory structures. Thus, the Australia-Indonesian BIT (1992) applies only to investments made "in conformity with the laws, regulations and investment policies ... applicable from time to time" (ICSID, 1992, p. 2). This formula ensures that full play is given to the regulatory laws of a host country despite the treaty so that only foreign investment which conforms with legislation is entitled to the protection. In South-East Asian treaty practice, only "approved" investment is given treaty protection. This formula ensures that a State decides on an *ad hoc* basis whether a foreign investment is so desirable that it be given treaty protection.

- **Most-favoured-nation treatment** (UNCTAD, 1999c). The existence of a most-favoured-nation (MFN) treatment clause ensures that better standards of protection against taking flow through to the State that had negotiated a lower standard. Thus, a State which had agreed to appropriate compensation with another State may argue that it is entitled to the higher Hull standard, if the latter State had concluded a treaty agreeing to the Hull standard with a third State, provided there was an MFN clause in its treaty.

- **Fair and equitable treatment** (UNCTAD, 1999b). It has been suggested that the fair and equitable standard of treatment referred to in an IIA creates an obligation to pay full compensation upon a taking (Dolzer and Stevens, 1986). This is on the basis that fairness and equity require that a foreign investor be returned to its original position prior to the taking at least in monetary terms.

- **Environment.** The issue of takings also has relevance to environmental issues. Termination or lesser forms of interference may be necessary to ensure that a foreign investor does not do harm to the environment. Thus some IIAs like NAFTA have provisions that exclude environmental measures from the scope of treaty protection.[1] On the other hand, some IIAs may seem to include such measures and this may deter a State from intervening to protect the environment.[2]

- **State contracts.** Contracts are sometimes the basis on which firms enter a host country. The local partner may be the State or a State corporation. In the natural resources sphere, in particular, the making of agreements often involves a State corporation. Large projects in areas like telecommunications, transport, power-supply and other similar fields also often involve the making of contracts with the State or State agencies.

  The issue arises as to whether a breach of these contracts would amount to a taking. There are two opposing views on this question. One is that these contracts are, by their very nature, internationalized contracts. Quite apart from

their nature, the inclusion of arbitration, choice of law and stabilization clauses in these contracts would indicate that the parties desired these contracts to be treated as internationalized contracts so that, when a State breaches these contracts, international responsibility would arise. The breach of a foreign investment agreement by State-induced measures (such as legislation or some regulatory action) would therefore be a taking that is compensable. This view finds support in several arbitral awards.[3] The other view is that a foreign investment contract of whatever kind is subject to the laws of a host country. The notion of permanent sovereignty over natural resources assures this result in the case of contracts in the resources sphere but the argument is equally applicable in the case of all other foreign investment contracts so that the breaches of these contracts can be remedied only in accordance with the laws of a host country. So where it is claimed that a breach of a contract amounts to a taking, the claim must be settled in accordance with local laws by local courts or tribunals.

However, in BITs as well as in regional investment treaties, there is an increasing trend to include contracts, especially in the form of concessions, in the definition of investments so that, where there is a breach of such contracts, such a breach would fall within the definition of an expropriation or other measure similar to it and would become compensable in terms of the treaty. The dispute resolution provisions of these treaties would require the submission of these claims to arbitration by an international tribunal. There is a considerable body of arbitral jurisprudence that accepts this position.

- **Funds transfer.** A significant interaction occurs between the issue of taking of property and that of the free and unhindered transfer of funds. Where an investment has been expropriated and compensation is paid to an investor by the host country, such a remedy would be worthless unless the investor was able to transfer the sum of compensation out of the host country. Hence, the right of free transfer of funds may often include the free transfer of amounts paid

by way of compensation for expropriated assets belonging to the foreign investor. An example of a typical provision dealing with this issue can be found in the BIT between Chile and Norway (1993). By article 5 (1) (e): "Each Contracting Party shall allow without delay the transfer of payments ... in a freely convertible currency, particularly of compensation for dispossession or loss described in Article 6 of this Agreement" (UNCTAD, 1998, p. 77). In other agreements, this issue is dealt with by the expropriation provision itself.

- **Dispute settlement (investor-State and State-State).** Because disputes are caused by State interference with foreign investment, the interaction between takings and dispute settlement becomes very relevant in IIAs. A number of issues are particularly important:

  - **Takings provisions.** The article on takings usually contains a provision that the taking and the assessment of compensation must be reviewed by a national tribunal. This is sometimes included in the form of a due process requirement. The provision is inserted as a protection for a foreign investor. Its genesis may also be in the "local remedies" rule which requires a foreign investor to exhaust all local remedies.[4] Unless this is done, no State responsibility can arise and therefore a home country cannot espouse the claim of the foreign investor. This gives the host country an opportunity of settling a dispute through its own tribunals.[5]

  - **Diplomatic protection.** Almost all IIAs facilitate diplomatic protection by providing for subrogation so that home country insurance agencies may pay out the claims of a foreign investor and the home country could stand in the investor's place to pursue its claims. Once the claim is espoused, the normal procedures of inter-State dispute settlement are used to settle the dispute.

- **Arbitration.** Whereas reference in the IIAs to the first two procedures is confirmatory of existing customary international law, IIAs adopt novel solutions in devising arbitration as a method of dispute settlement. The now widely used method of creating standing in the foreign investor itself was a novelty when first employed. But provisions in modern regional and bilateral treaties have gone even further by vesting a virtual right to compulsory arbitration in a foreign investor. The early IIAs (usually BITs) that adopted this strategy confined this right to arbitration to the International Centre for Settlement of Investment Disputes (ICSID). But more recent treaties, including regional treaties like NAFTA, permit a choice to a foreign investor of using either ICSID or *ad hoc* arbitration. Expansive interpretations have been placed by ICSID tribunals on these treaty provisions in claiming jurisdiction not only in respect of takings but also in respect of acts resulting in State responsibility.[6] These trends resulting from IIAs and developments in arbitration mean that regulatory policies and interferences with foreign investment resulting from their application can be reviewed by international tribunals. Control by a host country on foreign investment through implementation of policy may, as a result is curtailed.

Notes

1 The use of regulatory measures on environmental grounds is subject to review as the Ethyl case shows.

2 This was an objection raised against the MAI by environmental groups.

3 The authority supporting this view is canvassed in Sornarajah, 1994.

4 See for example, the CARICOM Guidelines for use in the Negotiation of Bilateral Treaties.

5 The International Court of Justice, considering a Friendship, Commerce and Navigation treaty, held in the ELSI case that the rule on the exhaustion of local remedies must be deemed as incorporated in the treaty even in the absence of any specific reference to it in the treaty.

6 AAPL v. Sri Lanka, 1990.

CONCLUSION: ECONOMIC AND DEVELOPMENT IMPLICATIONS AND POLICY OPTIONS

The classical instances of takings — nationalizations or expropriations — have greatly influenced the development, interpretation and application of the takings clauses in IIAs. Progressively however, the ambit of takings provisions has moved beyond the classical cases, and now attempts to include all direct and indirect takings that, from the investor's point of view, are tantamount to nationalization or expropriation, that is, result in substantial loss of control or value of a foreign investment.

Given the broad scope of the typical takings clause, and looking beyond the classical category of takings, there is growing concern and controversy that the potential expanse of the takings clause might encroach on too large a category of regulatory measures that can potentially interfere or otherwise affect the property rights of a foreign investor, or diminish the value of the foreign investment (regulatory takings). Clearly, those takings that can be characterized as criminal law penalties, resulting from the violation of laws of a host State, are not compensable under customary international law. The problem remains, how to address other measures, not clearly covered under existing customary law, given the difficulty of making precise classifications of measures and takings and clear distinctions among the various types of measures. The challenge of adequately protecting the investor from takings may conflict with the concerns of national regulators in discharging their duties, and promoting economic development or serving other objectives. IIAs are also becoming instruments that reflect national and global interests in a variety of social issues. Thus, the issue also concerns non-governmental organizations, some of which are involved with issues that transcend national boundaries such as the environment and human rights. They are particularly concerned that an open-ended international legal requirement of compensation could have a chilling effect on national regulatory activity.

Whether in the case of the classical category of takings or concerning more recent issues related to regulatory takings, there is substantial accord about some fundamental issues. Takings need to be for a public purpose, on a non-discriminatory basis, under due process of law, and accompanied by payment of compensation. As illustrated in section II, there remains, however, some diversity with respect to the standard of compensation that should be applicable. Increasingly, the general trend reflects the use of a standard that requires the payment of "prompt, adequate and effective" compensation. Nevertheless, there remains abundant practice of employing provisions that provide for some flexibility on the issue of determining the amount of compensation. Such provisions are generally based on standards like "just" or "appropriate" compensation. Thus while the requirement for payment of compensation is now generally regarded as a settled issue, its application illustrates that a variety of policy options still need to be considered today.

The following discussion first examines policy options that have recently been thrown into the national and international arena as the issue of regulatory takings continues to take increasing prominence. It then illustrates a number of other policy considerations relevant to some still rather controversial issues relating to the standard of compensation in case of a taking. Finally, and based on the above, an illustration of drafting models is provided.

A. Defining a taking: policy options

The task of negotiating and drafting a clause on takings requires from a negotiator to engage in the concomitant attempt to address, among others, the important issue of what constitutes a taking. There are a number of policy options that may be considered. The main ones are identified below.

1. A comprehensive definition

As already noted, it is today likely that countries would agree that the coverage of the takings clause should be broad enough

to maximize the protective effect of the IIA. It would thus typically include in its scope both direct and indirect expropriations, or use similar formulations intended to include all measures having effects equivalent to expropriations of the "classical" kind. However, the effect of an all encompassing formulation, without more, could be interpreted to include within the ambit of the takings clause all governmental acts (and omissions) that interfere with a foreign investment. It may be desirable, therefore, to examine other possible options, so as to exclude certain regulatory takings from the reach of the takings clause.

2. A narrow definition

One option is to tailor narrowly the takings clause so that it only covers the classical instances of direct takings, that is, nationalizations or expropriations. This would provide limited protection for the investor, and maximum regulatory discretion for Governments.

Theoretically, the scope of such a clause could be broadened to include any taking, under whatever name or in whatever form, that is intended to deprive investors of their property. Intent is not, however, a useful or workable test, the motivation behind governmental action being by definition complex and difficult to determine with precision. In fact, intent is relevant only in highly exceptional cases, where it is possible to show that a Government had abused its powers, by acting for a purpose other than the one it had invoked.

3. Interpretative provisions

Under this option, IIAs could include an interpretative provision, either within the takings clause or separately, that seeks to clarify whether or not a regulatory measure triggers the takings clause and, thus, its requirement of compensation. This clarification could, for example, address the regulatory activity in question, or the effects of the measures on property rights. A variation of the former approach was discussed in the MAI negotiations, where the Ministerial statement on the MAI sought to clarify that the intention of the

parties was not to include, in the scope of the expropriation and compensation draft provisions, "the normal, non-discriminatory exercise of regulatory powers by governments" (OECD, 1998, p. 1). Thus, while the broad scope of the takings provision could remain, it would be understood that it is not intended to cover some types of regulatory activity or effects.

Since there are no express exclusionary provisions as to specific regulatory activities or effects under this option, there would necessarily be reliance on some appropriate mechanism to determine whether or not a particular measure is intended to be covered by the interpretative provision. Therefore, areas of uncertainty would exist on the part of both national regulators and investors, until a number of cases were considered under the appropriate mechanism.

4. Carve-out provisions

This approach would include the identification and carving-out of certain areas of regulatory activity from the ambit of the takings clause. Here, for example, a provision could expressly address measures taken to protect the environment and exclude them from the coverage of the takings clause. The issue would then arise on safeguarding against regulatory abuses. A right to an international review of the regulatory measures could be provided and, depending on the type of review mechanism and access, agreement may be desirable upon standards of review of governmental measures.

A related issue would be considered here. When countries enter into international obligations, they typically provide for their implementation within their national legal systems. This might pose a potential problem of conflicts between different international obligations, where, for example, under an environmental treaty, a State is obligated to take certain measures that amount to a regulatory taking, and thus be required to pay compensation therefore. A variation under this option could provide for the consideration of other potentially conflicting international obligations in the IIA, and the establishment of a hierarchy to determine whether and

how the takings clause would be applicable as to these obligations in the case of a conflict.

5. International reviews

This approach would essentially leave the determination on whether or not a particular taking is compensable to a case-by-case review. Thus, the compensability of all regulatory takings would be subject to review. Here, there is no need to make any *a priori* classification between types of measures or takings. However, an international review mechanism would be provided for to decide whether or not a particular taking triggers the takings clause. Access to this mechanism could be made available only to States. The rationale is that States would be prudent in assessing the compensability of regulatory takings, as each State has an interest in exercising its own right to regulate.

B. Standard of compensation: policy options

The discussions on the issue of compensation in the earlier sections of this paper reveal three factors.

- In case of a compensable taking, there exists a tension between the host country's need to infringe upon the property rights of a foreign investor, and the need to ensure that the investor is adequately compensated in the event of such infringement. On the one hand, a host country should not be put in a position to forego or delay the development of its national objectives or the restructuring of its economic sectors that might entail takings. On the other hand, investors who would suffer loss of their property rights should not further suffer inadequate or delayed compensation.

- There is no unanimity when it comes to the determination of compensation and the calculation of the value of affected property. As previously illustrated in section I, none of the various terms currently in use have become generally accepted definitions in this regard under international law. The use of terminology incorporating the Hull formula, for example,

implies that the compensation would only include market value whereas terms like "just" or "appropriate" compensation tend to imply a certain flexibility in reaching the value of compensation due.

- Terms such as "just" or "appropriate" are often employed in a context silent on other critical considerations such as the time frame within which payment is to be made, the type of currency in which payment is made, and the transferability of the compensation paid. Even the Hull formula variations may sometimes be ambiguous in this regard, though, by contrast, they usually imply that since compensation would be promptly paid it would be freely transferable from the host country, thus further implying that the currency in which payment is made is freely convertible.

Therefore, irrespective of the compensation formula employed, some of these foregoing factors need individual consideration and raise a number of policy options with regard to the standard of compensation in IIAs.

1. Determination of the value of compensation

The typical starting point is the calculation of the value of the affected property using market value based methods. Such methods include the going concern value, asset value (including declared tax value) and book value. At the same time, it is important that the selected method addresses issues such as depreciation and damage to property.

It is also important to know that once a specific method is indicated in an IIA, it might be difficult to use other legitimate methods. Therefore, to retain flexibility, the provision of an IIA could simply require that the value of property could in any case be calculated in accordance with generally recognized principles of valuation.

The value of the affected property, once calculated, could be the sole consideration in determining the amount of compensation.

However, other equitable principles might have to be reflected in the IIA takings provisions. For example, market value based methods might not leave scope for recoupment of funds necessary to rehabilitate property, such as expenditures to clean hazardous wastes dumped on the property. Other considerations that might be taken into account include past practices, the depletion of natural resources and environmental damages (either recoupment costs or damages to the wider environment). On the other hand, including equitable principles within the provisions on the standard of compensation might raise controversy. Firstly, equitable principles are not universally accepted; they are creations of specific jurisprudence. Secondly, their introduction would necessitate a clarification of whether or not they only would be used to reduce the amount of compensation (as in the case of environmental damages) or if, for example, they could also be used to increase the amount of compensation (as in the case of attaching a value to the training of the labour force or diffusion of technology effected by the investor to the benefit of the host country).

2. Limitation on the time frame within which payment is made

An IIA may provide that budgetary or foreign exchange severe limitations might be justification for delaying payment, subject to payment of reasonable interest. As previously indicated, these limitations should not deter or delay the host country's pursuance of its development objectives or the restructuring or of its economic sectors. The flexibility that is required could be attained by IIA provisions that provide for delaying payment under conditions of adequate guarantees that the investor would receive the compensation in the near future.

3. Type of currency in which payment is made

The range of options available are from the requirement of payment in a specific hard currency (e.g. United States dollars) to payment in the local currency of the host country. A requirement of payment in a specific hard currency is often regarded by host countries as unduly restrictive. Firstly, it does not allow the host

country to use other freely convertible currency in its foreign exchange reserves, or places transaction costs on the host country by requiring it to exchange to the indicated hard currency. Secondly, the host country could not use advantageous arbitrage rates in foreign exchange markets to reduce its exposure with regard to the payment of compensation to a given investor.

It could also be argued that, where there exists a private banking system including a foreign exchange market in the host country, together with no transfer restrictions, there is no reason why the host country should pay in any other currency than its own. This is so, even if the local currency is not fully convertible, so long as private foreign exchange enterprises in fact operate in the host country.

Amongst the range of options in this regard are, therefore, IIA provisions that guarantee the requirement that compensation be paid in a freely convertible currency, without specifying the currency and leaving room for the possibility that the compensation could be in the local currency.

4. Transferability of compensation paid

The same factors mentioned above as in relation to the time frame within which payment is made are relevant here. Flexibility could be attained by allowing exceptions to the general "freely transferable" requirement for budgetary or foreign exchange limitations, subject to adequate protection of the investor for loss of interest and currency rate fluctuations that the delay in repatriation of funds might entail.

C. Drafting models

Besides the important issues of determining what constitutes a compensable taking in the first place, and then the standard of compensation, the other issues relating to requirements for a taking to be lawful — including the need for a public purpose, non-discrimination and the due process of law of course — remain relevant to the drafting of a clause on taking. In that regard, three main models of takings clauses that attempt to cover the principal

relevant issues can be identified. Clearly there will be variations of these three models, depending on the particular circumstances of the States negotiating an IIA.

1. High protection for investment model

If a host country believes that foreign investment is important to fuel its economic development it will provide wide guarantees against takings in the hope that such guarantees will result in greater flows of foreign investment. States adopting such a view would subscribe to a model of IIA that will provide wide protection against takings. The typical clause on takings in the high protection for investment model includes the generally accepted requirements for a taking to be lawful:

- public purpose;
- non-discrimination;
- due process of law; and
- payment of compensation.

In addition, such a model has the following features:

- a taking is broadly defined, so as to cover all kinds of assets, as well as direct and indirect takings;
- it includes stringent requirements for payment of compensation. The payment should be prompt, adequate and effective, that is to say, compensation which must be:
  - (a) paid without delay;
  - (b) equivalent to the fair market value immediately before the expropriation; and
  - (c) fully realizable and freely transferable.

The protective effect of this model is enhanced if, in the other provisions of the IIA:

- the initial definition of investment is very wide, covering not only physical property but intangible property like patents and know-how, shares in stocks of companies, contracts like concession agreements in the natural resources sector and

the new type of "property" brought about by regulatory controls — licences and permits necessary for a foreign investor to operate;

- dispute resolution provisions giving standing to a foreign investor to invoke arbitration against a host country at its option.

Such a model restricts sovereign control over foreign investment to the extent that a host State not only is not free to take at will property belonging to foreign investors but must conform to severe limitations on its ability to regulate foreign investments. As such this model forms the basis of IIAs that seek primarily to further the goal of protection of investments. The dispute resolution provision in this model might be of concern to the host country as it could transfer issues relating to the legitimacy of regulatory measures to a non-national tribunal. Home countries may prefer this model to the extent that it provides increased protection to their foreign investors, although they may be concerned that their own regulatory measures may be contested before international tribunals and their courts are bypassed. From the point of view of developing countries following this model, the limitation of sovereign powers is balanced by the conviction that a liberal regime would result in economic development.

2. High host country discretion model

The typical clause in this model would also include certain general requirements for a taking to be lawful:

- public purpose;
- non-discrimination;
- due process of law; and
- payment of compensation.

At the same time, in this model, such requirements would be accompanied by the following features of the takings clause:

- a narrow definition of the assets to which the takings clause applies;

- a narrow definition of takings, limiting them to the classical cases of expropriation or nationalization, not including measures of equivalent effect;

- provision for fair and just (or appropriate) compensation, as provided for in national law, with the host country having the right to determine the quantum of compensation and the terms of payment;

Here the host country provides the basic minimum protection against a taking. This will also mean that in the other provisions of the IIA:

- the definition of investment is relatively narrow, referring to specific physical assets and other interests in the IIA; and

- the dispute settlement provision provides for arbitration but permits it only if there is a specific arbitration provision in the contract; inter-State arbitration on investment issues is possible only after exhaustion of local remedies by the investor.

The high host country discretion model least restricts sovereign control over foreign investment. The model does not give any more protection than is given by existing customary international law. Some may even argue that customary international law gives a higher standard of protection than this model. This model presupposes that the regulatory authorities charged with screening and approving of investments function in an effective manner and avoid excessive interference with the operation of the enterprises involved.

3. Intermediate model

This model contains the basic features found in both the other models, that is to say:

- public purpose;
- non-discrimination;

- due process of law; and
- payment of compensation.

In addition, this model may contain some or a combination of the other features that distinguish "high protection" and "high host country discretion" models. A major difference could be that the definition of "investment" is qualified by a clause to the effect that only "approved investments" or investments made "in conformity with the laws and regulations of the host country" are covered by the agreement's protection provisions. The former formulation implies that a screening mechanism is in operation, while the latter formulation gives full scope for regulatory intervention in foreign investments and makes it clear that regulatory takings are not to be protected by the expropriation provisions of the treaty. Thus, the expropriation provision could be as extensive as that in the high protection for investment model, but the provision protects only approved investments or investments made according to a host country's laws and regulations. Compulsory arbitration between host State and investor, at the instance of the investor, may also be permitted, since this possibility would only apply to investments that have been specifically approved or made consistently with host country laws.

The important characteristic of such a model is that it is a dynamic one. It allows for a type of governance that would permit foreign investment to meet the desired development goals of a host country. At the same time, it provides safeguards to a foreign investor against unjustified takings. The model leaves the State with the power to legislate in order to protect the environment, human rights or other desirable public policy goals. At the same time, it ensures that a foreign investor, being desirous of protection against State interference, keeps to the goals behind the regulatory legislation of the host country. It may be relevant in this model to strengthen further the exclusion of regulatory takings by making specific exclusionary provisions relating to the environment and other areas such as tax, exchange controls and punitive measures.

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The issue of taking of property has historically been a contentious one. At present, however, the prospect of mass nationalizations or expropriations, characteristic of many investment disputes during the twentieth century, has greatly diminished. As knowledge of the benefits of foreign direct investment has increased, and fear of exploitation by foreign investors has declined, the need for the extreme sanction of nationalization or expropriation has lessened. However, the function of IIAs is to protect investors and investments against the economic neutralization of their assets. Provisions on takings will therefore continue to be included, even if the need for them seems, at times, remote; and a number of policy options remain particularly relevant to the issue of the standard of compensation.

At the same time, the paper also emphasizes that, within this changed situation, the major issues surrounding takings have also shifted. In particular, the need remains, in cases that fall short of outright takings, to reconcile the preservation of assets belonging to foreign investors and the role of the State as a regulator of the economy, even in a more liberal economic environment. In this context the paper has also outlined options for effecting a balancing of such interests.

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