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Sovereignty Over Natural Resources Versus Rights Under Investment Contracts: Which One Prevails?

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SOVEREIGNTY OVER NATURAL RESOURCES VERSUS RIGHTS UNDER INVESTMENT CONTRACTS: WHICH ONE PREVAILS?

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I. Introduction

In the area of natural resources, the relationship between foreign investors and host States today – and indeed the relationship between members of the international community more broadly – must be viewed within the prism of three important events commencing with the end of the Second World War. First, the creation of the United Nations system enabled States to gather in a more democratic global environment. Within that nascent United Nations structure, States that were traditionally isolated or recently independent were allowed to influence – at least to a greater extent than before – the world around them. Second, the independence from colonial control of a massive number of new nations allowed these young States to become fully-fledged members of the broad community of peoples and to assert themselves as such. Third, the increase in the prices and strategic importance of raw materials such as oil, gas, and other minerals led to an uneasy interdependence between foreign investors and host States. As many of these resources were located in developing countries, multinational companies struggled to gain access to products at the same time that those States realized their newly-acquired economic influence and sought control over their natural resources. The State's ability to actually enjoy its natural resources, however, was limited by its lack of technology, which remained in the control of multinational companies. Thus, a fragile community was established between developing nations and transnational corporations.

Even a cursory look at the relationship between foreign investors and host States over the 20th century exposes the uncertainties of this interdependence. The first half of the 20th century saw the creation and then rapid growth of the international energy industry. Many governments granted generous concessions in the early years to multinational oil corporations in which title to the oil in place was conveyed to the companies, the concession covered large areas, the terms of the concessions were very long (*e.g.*, 60 years or more) and the royalties payable to the government were low. Not surprisingly, developing nations soon decided to reverse course.

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Accordingly, the second half of the 20th century was characterized by the nationalization of the oil industry, the termination of those same concession agreements and the expropriation of the assets connected to the concessions.

By the end of the 20th century, the pendulum had swung once again. The 1980s and 1990s were characterized by the growing interest of developing nations in receiving foreign investment by means of new projects or privatizations of already existing state-owned enterprises. Added to this, many nations agreed to enter into bilateral investment treaties and multilateral agreements to promote themselves as investment-friendly countries.[3]

Predictably, the pendulum has now swung once again back in the direction of the host State. For instance, on December 31, 2005, Venezuela announced that it was taking over thirty-two (32) private oil fields in the first stage of an ongoing "statization"[4]. This process of taking control over the oil fields was completed during the next year; in some cases, through the creation of "mixed companies" under Venezuelan control. In 2007, Venezuela radicalized the oil nationalization by forcing six western major oil companies to renegotiate their agreements with respect to four heavy oil projects located in the Orinoco basin. In these negotiations, the Venezuelan government demanded a minimum of 60 percent control of the four Orinoco projects. Some of the oil companies decided to accept the Government-imposed terms while others - including Exxon-Mobil - have initiated arbitration proceedings against Venezuela and several PDVSA-owned subsidiaries.

Each of the three developments mentioned above and the constant pendulum swings they created provoked – indeed necessitated – a new approach to international law, especially in the field of expropriation and compensation. This was particularly so as these newly-formed or independent nations were repudiating the principles of international responsibility developed by

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[3] This trend now appears to have moved towards more comprehensive free trade agreements like those promoted by the United States, such as the NAFTA and DR-CAFTA.

[4] Statization can be distinguished from nationalization in that the former covers situations where the State takes direct control or ownership of specific enterprises, while the latter implies measures directed to taking over an entire industry or sector (*e.g.*, oil, iron).

the traditional western nations,[5] arguing that they were not bound by the existing principles and rules of international law.[6]

Among the existing principles of international law that these countries attempted to diminish was the principle of *pacta sunt servanda* underlying contractual commitments. Developing states argued that their sovereignty over natural resources superseded any contractual promise, including express commitments by the State not to impair those contractual rights. Furthermore, they proposed that any agreement with a foreign investor was subject to modification or termination based on national interest motives alone. In the face of these stark positions, industrialized nations and developing nations were forced to come together to espouse positions that would meet the needs of both developing nations and international investors.

It is these positions that have today created a tension between investment protections available to foreign investors outside of international treaties – in the form of contractual protections, stabilization clauses and legal stability agreements (discussed in Section III below) – and a State's sovereign right to the resources within its borders.

II. <u>The New International Economic Order</u>

A. Development of the New International Economic Order: The UN Resolutions

The attempt to create a new structure of economic relations between industrialized nations and developing countries has been one of the most important global events of the 20th century. It was the first time that an important majority of the States forming part of the international community actually raised, in a single voice, the call for a fairer distribution of the wealth and advancement that had been achieved by humanity up to that moment. However, at the same time, the negotiation, discussion and voting of the documents adopted within the United Nations system between 1950 and 1980 demonstrated the deep differences in philosophies and expectations between two very defined group of nations.

On December 21, 1952, for instance, the United Nations General Assembly issued Resolution No. 626 (VII), providing for the right of peoples to exploit their natural resources *as*

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5 García-Amador, *The Proposed New International Economic Order: A New Approach to the Law Governing Nationalization and Compensation*, 13 LAW. AM ps. 1, 2 (1980).

6 *See* Abi-Saab, *The Newly Independent States and the Rules of International Law*, 8 HOW. L.J. p. 99 (1962); R.P. Anand, NEW STATES AND INTERNATIONAL LAW (1972).

part of their sovereignty. Resolution No. 626 was the first General Assembly text in using the notion of the term "permanent sovereignty over natural resources".[7]

Ten years later, however, on December 14, 1962, the General Assembly adopted Resolution No. 1803 (XVII). It provided that nationalization measures could *only* be implemented for public purposes, security or national interest, subject to the investor receiving "appropriate compensation" in accordance to domestic and international law.[8] Although Resolution No. 1803 recognized the right to nationalize property for a public purpose, Paragraph 8 of the Resolution stated that investment agreements entered into by States "shall be observed in good faith."

In 1974, however, developing nations attempted to introduce radical changes into the legal principles of nationalization. United Nations Resolution No. 3201 (S-VI) of May 1, 1974,[9] entitled "Declaration on the Establishment of a New International Economic Order" stated in Article 4(e) that a State had the right to nationalize its resources and could not be subject to economic, political or other coercion to prevent the exercise of that right. Further to the principles of equality, self-determination, prohibition of the use of force and non-interference, the Resolution called for an effective participation of all countries in confronting economic issues. As with the previous resolutions, the General Assembly confirmed the "full permanent sovereignty" of the State over its natural resources and went on to provide for a list of social, trade, economic, environmental and technology aims directed at closing the gap between countries.

Most significant of all is Resolution No. 3281 (XXIX), dated July 26, 1974.[10] Through this Resolution, the General Assembly adopted the Charter of Economic Rights and Duties of

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[7] Significantly, the International Covenant on Economic, Social and Cultural Rights and the International Covenant on Civil and Political Rights, both opened for signature in 1966, also incorporated the principle of sovereignty over natural resources. The Covenants entered into force on January 3 and March 23, 1976, respectively.

[8] The use of the term "appropriate compensation" was developed as response to the use of the standard of "prompt, adequate and effective" compensation, or "Hull formula", first articulated by United States Secretary of State Cordell Hull in response to Mexico's nationalization of American petroleum companies in 1936. The main difference between "appropriate compensation" and the "Hull formula" is that the former involves a flexible approach that would take into account all circumstances underlying the investment, instead of the static nature of the latter, which requires "full payment" as compensation. *See* Sornarajah, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT p. 479 (2004).

[9] G.A. Res. 3201, 6th Special Session, GAOR, Supp. (No. 1), U.N. Doc. A/9559 (1974).

[10] G.A. Res. 3281, 29 GAOR, Supp. (No. 31), UN Doc. A/9361 (1974).

States. This text reaffirmed that the right to nationalize foreign-owned property required "appropriate compensation," and admitted that, if compensation was not paid, the nationalizing State's international obligation would not have been fulfilled in "good faith."[11] Nevertheless, the General Assembly also adopted that any dispute as to compensation for nationalization was subject *only* to the State's *domestic* law and circumstances that the *State* deemed relevant for the specific case. Resolution No. 3281 also provided that any dispute shall be settled under the *domestic* law of the expropriating State and within its judicial system, unless there was an agreement calling for other peaceful means.[12]

B. The Legal Effect of the New International Economic Order UN Resolutions

Soon after Resolution Nos. 3201 and 3281 were adopted, Professor Oscar Schachter explained that the purpose of this "New International Economic Order" was to "delegitimate" certain principles and practices which were against the interests of developing nations, such as most-favored-nation clauses and the international standard for compensation.[13] Likewise, the

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[11] *Id.* Chapter I(j).

[12] Resolution No. 3281, Article 2.2(c).

[13] Schachter, *The Evolving International Law of Development*, 15 COLUM. J. TRANSNAT'L L. ps. 1, 7 (1976). It is unclear, however, whether there has ever been an "accepted international standard for compensation." For example, Sir Hersch Lauterpacht, in his edition of OPPENHEIM'S INTERNATIONAL LAW, suggested that the standard of "full" compensation was not applicable to nationalizations occurred as consequence of a state's economic reorganization. *See* OPPENHEIM'S INTERNATIONAL LAW p. 352 (1952). In any event, the current status of this issue under international law appears to be that an important number of states consider that expropriation can only take place on payment of "adequate and effective" compensation or "just compensation." *See* Brownlie, PRINCIPLES OF PUBLIC INTERNATIONAL LAW at p. 519-520 (2003). A review of bilateral treaties for the protection of investments shows a tendency to incorporate different standards of compensation. Some bilateral investment treaties, like those entered into by Japan or Canada, have adopted the concept of "prompt, adequate and effective" compensation. *See, for example*, Agreement between Japan and The Socialist Republic of Vietnam for the Liberalization, Promotion and Protection of Investment, signed on November 14, 2003; available at http://www.bilaterals.org/IMG/pdf/Japan-Vietnam_BIT_2003.pdf; Agreement between the Government of Canada and the Government of the Republic of Venezuela for the Promotion and Protection of Investments, signed on July 1, 1996, available at http://www.sice.oas.org/BITS/caven1_e.asp. Other bilateral investment treaties, like those executed by the United States, include a provision by which "compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriatory action was taken or became known." *See, for example*, the Treaty between the United States of America and the Argentine Republic concerning the Reciprocal Encouragement and Protection of Investment, with Protocol, signed on November 14, 1991, published at http://tcc.export.gov/Trade_Agreements/All_Trade_Agreements/exp_000897.asp. *See also* the 2004 United States Model Bilateral Investment Treaty, available at http://www.ustr.gov/assets/Trade_Sectors/Investment/Model_BIT/asset_upload_file847_6897.pdf. Other bilateral investment treaties only include a reference to "effective and adequate" compensation. *See, for example*, Accord entre la Confédération Suisse et la République du Péru concernant la promotion et la protection réciproque des investissements, conclu le 22 novembre 1991, available at http://www.admin.ch/ch/f/rs/i9/0.975.264.1.fr.pdf. Finally, some bilateral investment treaties, such as those ordinarily executed by the Netherlands, contain the

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former judge of the International Court of Justice, Eduardo Jiménez de Aréchaga, also attempted to rationalize the effects of the New International Economic Order.[14] In his opinion, the proposed New Order provided for nationalization and expropriation as lawful exercises of a sovereign right of the State, and modified the application of the rules of State responsibility, particularly with respect to the duty to compensate foreign investors whose property has been nationalized.[15]

Conversely, some authors have tried to pull back from the significance of these UN Resolutions. F.V. Garcia-Amador, for instance, has suggested that one of the most relevant features of both the Declaration on the Establishment of a New International Economic Order and the Charter of Economic Rights and Duties of States is the use of the term "should" instead of "shall" in relation to the principles underlying the New International Economic Order.[16] As a result, he suggests that these features must be construed as not creating true legal obligations for the international community with respect to the New International Economic Order, but rather only mere aims.[17]

Each of these positions, however, appears to be too narrow. Many of the protections granted to foreign investors in bilateral and multilateral investment treaties – including those originally rejected by developing nations – are now widely recognized as limits to and the boundaries of a State's sovereignty over its natural resources. Conversely, several of the provisions contained in the United Nations Resolutions, such as sovereignty and protection of the environment, have become accepted principles of the international order.[18]

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standard of "just" compensation. *See*, *for example*, Agreement on encouragement and reciprocal protection of investments between the Kingdom of the Netherlands and the Republic of Peru, signed on December 27, 1994, available at http://www.sice.oas.org/ctyindex/PER/PERBits_e.asp.

14 Jiménez de Aréchaga, *State Responsibility for the Nationalization of Foreign –owned Property,* N.Y.U. J. INT'L AND POL. ps. 179, 180 (1978).

15 *See also* Brownlie, PRINCIPLES at p. 518 (2003). Brownlie states that the resolutions must be weighed according to their respective merits. On this basis, he concludes that the provisions on nationalization contained in the Charter of Economic Rights and Duties of States must be considered as an emerging principle of international law. In his opinion, takings for public purposes are lawful and that a majority of states does not accept the "prompt, adequate, and effective" formula with respect to compensation. He also considers that the local courts' failure to provide compensation would be contrary to international law, through devices such as denial of justice. Brownlie, however, recognizes that these principles would not be binding on those States that rejected the Charter.

16 Garcia-Amador at p. 54.

17 Garcia-Amador at p. 18.

18 *See* Brownlie, PRINCIPLES at p. 519-520. For example,

Further, and perhaps more remarkably, international tribunals have, over the last few decades, recognized that *contracts* between the host State *and the investor itself* (*i.e.*, outside of any treaty regime), may place a limitation on the State's sovereignty over its natural resources.[19] It is this recognition that the State can, with the stroke of pen, waive its sovereign rights to the resources within its control that has become the most remarkable feature of the New International Economic Order.[20]

III. The Limitation of Sovereignty by Contract

A. Sovereign Rights and Contracts

First, it is a fundamental principle of law that contractual undertakings must be respected. The rule of *pacta sunt servanda*, therefore, has application to all types of agreements, including those between investors and the host State.[21] It is only logical that a party entering into an agreement expects that the other party will fulfill its promises. Furthermore, the respect for

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[19] Starting in the second part of the 20th century, a group of scholars developed a monist approach to State contracts in international law. Under this approach international law supersedes domestic law as the overriding governing law. The origin of this school of thought can be found in Judge Lauterpacht's separate opinion in the *Norwegian Loans* cases. *See Case of Certain Norwegian Loans*, ICJ REPORTS p. 9 (1957). The internationalization of State contracts would assist in applying international general principles of law such as *pacta sunt servanda* and acquired rights in the context of State contracts. A consequence of this approach would be that a State cannot invoke its own municipal law to justify the impairment of contractual obligations. The primacy of international law over domestic law is simply an extension of the general principle that a state which has broken a rule of international law cannot justify itself by referring to its municipal law; otherwise international law would be evaded by passing appropriate domestic legislation. *See* Article 27 of the Vienna Convention on the Law Treaties (1969). Subsequent arbitral awards, such as the *Libyan* arbitrations and the well-known *Pyramids* case, *SPP (Middle East) Ltd. and Southern Pacific Projects v. Egypt and EGOTH*, [1998] LAR 309, 330, also adopted this view of the supremacy of international law over municipal law. Currently, there is a strong debate as to whether the view that State contracts are subject to a supranational system of law is acceptable. *See* A.F.M. Maniruzzaman, *State Contracts in Contemporary International law: Monist versus Dualist Controversies*, 12 EJIL p. 309 (2001); Sornarajah, THE INTERNATIONAL LAW at p. 416.

[20] The internationalization of State contracts may also imply that a contractual obligation in violation of the State's constitutional norms could nonetheless create a valid obligation under international law. This principle has been adopted with respect to international relationship between States. *See* Bin Cheng, GENERAL PRINCIPLES OF LAW APPLIED BY INTERNATIONAL COURTS AND TRIBUNALS at p. 171 (1953), *citing* the Advisory Opinion of the Permanent Court of International Justice in the *Polish Nationals in Danzig* case, (1931) P.C.I.J. series A/B, No. 44, p. 24 ("… a State cannot adduce as against another State its own Constitution with a view to evading obligations incumbent upon it under international law or treaties in force.") However, it is not clear whether the same principles could be applied to contractual obligations between an investor and the State, including the validity of obligation deemed void *ad initio* under the State's own constitution.

[21] *But see* Sornarajah, THE INTERNATIONAL LAW at p. 426 (arguing that *pacta sunt servanda* cannot be accepted as a general principle of law with respect to State contracts because of the public interest involved in their performance.)

acquired rights is another principle of law accepted by international tribunals.[22] As reflected in United Nations Resolution No. 1803, the principle of *pacta sunt servanda* was considered applicable to investment agreements executed within the context of the New International Economic Order.

The principle of good faith has also been universally applied as a general legal principle, both in civil and international law, to prohibit, *inter alia*, a State from taking actions or making representations which are contrary to or inconsistent with actions or representations it has taken previously to the detriment of another.[23] It is also well-established that good faith is a key principle of international law, just as it is in domestic law.[24] As stated by the Permanent Court of International Justice in 1934, "contracting parties are always assumed to be acting honestly and in good faith. That is a legal principle, which is recognized in private law and cannot be ignored in international law."[25] Moreover, even the controversial United Nations Resolution No. 3281 also expressly stated that international obligations had to be performed in good faith.

This principle has also been recognized in the specific context of foreign investment agreements.[26] Today, it is widely held that the international minimum standard of protection to be afforded by a host State to a foreign investor and its investments in the territory of the host State encompasses the requirement of good faith. In light of the good faith principle, the international minimum standard has evolved to embody a duty of governments to treat foreign investors with transparency and to protect their legitimate expectations – both based on specific

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22 *See Sapphire International Petroleum Ltd. V. National Iranian Oil Co.*, 35 ILR at p. 136 (1967).

23 *See, e.g., Amco v. Indonesia*, ICSID Case No. ARB/81/8, Decision on Jurisdiction of September 25, 1983, 1 ICSID REPORTS at ps. 407/8, Resubmitted Case: Award of June 5, 1990, 1 ICSID REPORTS at p. 606; *Klöckner v. Cameroon*, ICSID Case No. ARB/81/2, Decision on Annulment of May 3, 1985, 2 ICSID REPORTS at ps. 140/1; *SPP v. Egypt*, ICSID Case No. ARB/84/3, Decision on Jurisdiction of November 27, 1985, 3 ICSID REPORTS at p. 123.

24 Bin Cheng, GENERAL PRINCIPLES at p. 123; Joerg Mueller, VERTRAUENSSSCHUTZ IM VOELKERRRECHT (1971); E. Zoller, LA BONNE FOI EN DROIT INTERNATIONAL PUBLIC (1977); F. Orrego Vicuña, *Regulatory Authority and Legitimate Expectations*, 5 INTL LAW FORUM at ps. 188, 193 (2003); *Nuclear Test Case*, ICJ REPORTS p. 268 (1974).

25 Permanent Court of International Justice: *Lighthouse Case (1934)*, cited in Bin Cheng, GENERAL PRINCIPLES p. 106 (1987). *See also* Bin Cheng, GENERAL PRINCIPLES at p. 118 ("It may be said that in such cases good faith consists in a sincere and honest desire, as evidenced by a genuine effort, to fulfill the substance of the mutual agreement. It is essentially a moral quality or perhaps what Judge Moore has described as the "ordinary conception of fair dealing as between man and man." The enforcement of the principle of good faith may be considered as the enforcement of that degree of morality which is necessary for the functioning of the legal system.")

26 "Foreign investment agreements freely entered into by or between sovereign States shall be observed in good faith….", U.N.G.A. Res. 1803, XVII, 1962, *para.* 8.

assurances and with respect to the image foreign investors reasonably and legitimately form about the country's legal, institutional and fiscal regime when they enter the country. This is confirmed by the *jurisprudence constante* that has developed in recent NAFTA and ICSID awards.[27]

Indeed, many international projects, particularly those in the oil and gas industry, involve the commitment of substantial capital and resources. Therefore, it is natural that the agreement underlying the relationship between the State and the investor provides for a very long duration. During the course of the Middle East oil nationalizations, some governments invoked their domestic law to allege that concessions were administrative contracts. In countries inspired by French administrative law, a contract may include exorbitant clauses allowing the government to amend or modify the service provider's obligations. Accordingly, States argued that concession agreements, as administrative contracts, were subject to the changes and modifications within the State's policy powers. In *Saudi Arabia v. Aramco*,[28] however, the arbitral tribunal rejected the

[27] Examples of the relevant jurisprudence include: *Tecmed v. Mexico*, ICSID Case No. ARB(AF)/00/2, Final Award of May 29, 2003, *para.* 154: The Arbitral Tribunal considers that [Article 4(1) of the Mexico-Spain BIT], in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments a treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, *i.e.* without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation….
Cited with approval in *MTD Equity Sdn. Bhd. and MTD Chile S.A. v. Republic of Chile*, ICSID Case No. ARB/01/7 (2003), para. 114; *Occidental Exploration and Production Company (OEPC) v. The Republic of Ecuador*, Final *Award*, LCIA Case No. UN 3467 (2004), para. 185; *CMS Gas Transmission Company v. Republic of Argentina*, ICSID Case No. ARB/01/8 (May 12, 2005), para. 268; *Eureko v. Poland*, *Ad Hoc* UNCITRAL Arbitration, Partial Award of August 19, 2005, para. 235; *Saluka v. Czech Republic*, *Ad Hoc* UNCITRAL Arbitration, Partial Award of March 17, 2006, para. 302; *see also OEPC v. Ecuador*, para. 190 ("The Tribunal is of the opinion that in the instant case the Treaty standard [of fair and equitable treatment] is not different from that required under international law concerning both the stability and predictability of the legal and business framework of the investment. To this extent the Treaty standard can be equated with that under international law as evidenced by the opinions of the various tribunals cited above."); *CMS v. Argentina*, para. 284 ("In fact, the Treaty standard of fair and equitable treatment and its connection with the required stability and predictability of the business environment, founded on solemn legal and contractual commitments, is not different from the international law minimum standard and its evolution under customary law.").

[28] 27 ILR at p. 171 (1958).

State's argument that it could modify an oil concession through regulation. The tribunal reasoned that an oil concession did not involve a public service, an element of any administrative contract, but was an ordinary contract of private nature. Some years later, in *Texaco v. Libya*,[29] Libya raised the same argument as Saudi Arabia did in *Saudi Arabia v. Aramco*. The arbitrator, after reviewing the content of Libyan administrative law, rejected the notion that the oil concession was an administrative contract.[30]

Nevertheless, despite the foregoing, it is generally accepted that concessions for the exploitation of natural resources are contracts that can be breached under international law.[31] Furthermore, it has also been held that the contractual rights contained in the concession can be expropriated.[32] This same principle applies to product sharing agreements, exploratory agreement or other contracts.[33] Thus, with respect to the effect of the New International Economic Order resolution on contractual obligations, the arbitrator in the *LIAMCO v. Libya*[34] arbitration concluded that although the 1974 resolutions reflected a more current trend of State opinion concerning their rights over natural resources, these rights are always subject to the respect of contractual obligations validly agreed upon by the State.[35] The arbitrator went on to argue that while Libya was legally obliged to observe the terms of the concessions agreement, the nationalization measure was not necessarily unlawful. In the arbitrator's opinion, any

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29 *Texaco Overseas Petroleum Co./California Asiatic Oil Co. v. Government of the Libyan Arab Republic*, 17 ILM 1 (1978).

30 17 ILM at p. 20. The arbitrations concerning the nationalizations in the Middle east and Libya were pervaded by the notion of the internationalization of State contracts. Thus, it was a necessary consequence that administrative law would be excluded in the construction of those concessions. There is developing strong sentiment that administrative law should be considered when analyzing the contractual relationship between the investor and the State. *See* Sornarajah, THE INTERNATIONAL LAW at p. 422.

31 *British Petroleum Co. (Libya) Ltd (BP) v. Government of the Libyan Arab Republic*, Award of 10 October 1973, 53 ILR (1979) p. 297, Yearbook V (1980) p. 143. The arbitrator, accepting the claimant's expert testimony, declared that the concession underlying the dispute had the nature of a contract and thus could be breached. At any event, the issue of the legal nature of concession agreements is subject to substantial debate. *See* Sornarajah, THE INTERNATIONAL LAW at p. 422-423 ("There is a more credible basis now than before to argue that contracts made by states with private parties are universally recognized as defeasible in the public interest and that no illegality can be attached to its breach by the state provided it can demonstrate a public purpose for the breach.")

32 *Amoco International Finance v. Islamic Republic of Iran*, Award No. 310-56-3 (14 July 1987), 15 Iran –US CTR p. 189 at pp. 219-221; *Phillips Petroleum Co. v. Islamic Republic of Iran*, Award No. 425-39-2 (29 June 1989), 21 Iran-US CTR p. 79 at ps. 118-119.

33 Bishop, *International Arbitration of Petroleum Disputes: The Development of a Lex Petrolea, Yearbook of Commercial Arbitration*, YEARBOOK OF COMMERCIAL ARBITRATION, A.J. van den Berg (ed.), Vol. XXIII (1998), p.1155.

34 *Libyan American Oil Co. v. The Government of the Libyan Arab Republic*, VI YEARBOOK OF COMMERCIAL ARBITRATION 89 (1981).

35 *Id.* at p. 107.

wrongful act had to be considered in light of Libya's offer to compensate the claimant and not from the nationalization itself.[36]

There is no question, therefore, that under international law, States have the right to nationalize their own natural resources but that the right is subject to the corresponding obligation to compensate the investor whose property is expropriated. It can be gleaned from the arbitral awards referred to above that there is a theoretical discussion as to whether nationalization constitutes a breach of contract *per se*.[37] The respect for contractual obligations, however, does not imply that a State cannot exercise its sovereignty to adopt laws or regulations. As a general principle, a State is authorized to adopt *bona fide* regulation within its accepted police powers even if such measures may cause economic damage to those subject to its powers. In these cases, the injured party may not have the right to compensation.[38]

B. Stabilization Clauses

In light of the perceived weakening of the commitment principles underlying contract – *i.e.*, a "get out" clause for States - most foreign investors today demand the inclusion of contractual guaranties aimed at maintaining the legal status in force at the time the investor made its investment. Stabilization clauses in investment agreements serve the purpose of freezing the effects of changes adopted by a State in its national system of law as of the date of the contract.[39]

In *AGIP Co. SpA v. Government of the Popular Republic of Congo*,[40] the arbitral tribunal held that the nationalization that was the subject-matter of the dispute violated both domestic and

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[36] *Id.* at 103. A different approach was followed, however, in the *Texaco v. Libya* arbitration. In analyzing the meaning of Resolution No. 3281, the arbitrator referred to the principle of good faith. The arbitrator held that good faith prevented the State from creating an imbalance in the parties' obligations as consequence of a release of the State and not the investor. Thus, the arbitrator took the view that the State, by agreeing to subject the agreement to international law, accepted the international consequences of such measures (nationalization) affecting its international responsibility. *See* ILM at pp. 22, 31.

[37] *Compare Texaco v. Libya*, 17 ILM at p. 22 (holding that an expropriation imports the breach of contractual obligations) with *LIAMCO v. Libya*, VI YEARBOOK at p. 186 (concluding that nationalization did not imply a breach of contract but that the State anyway had to compensate the investor).

[38] *See Lauder (U.S.) v. Czech Republic* (Final Award), (September 3, 2002) available at www.mfcr.cz/scripts.hpe/default.asp; *Técnicas Medioambientales Tecmed S.A. v. The United Mexican States*, ICSID Award Case No. ARB(AF)/00/2. In *Feldman v. United Mexican States*, ICSID Case No. ARB(AF)/99/1, Award of December 16, 2003, the arbitral tribunal stated that governments are entitled to change their laws and regulations to adapt to changing economic, political, or social circumstances even if these measures affect commercial activities.

[39] *Amoco International Finance v. Islamic Republic of Iran*, 15 Iran – US CTR at p. 239.

[40] Award of 30 November 1979, 21 ILM at p. 726 (1982).

international law because it breached the stabilization clause contained in the agreement. The arbitral tribunal stated:

> These stabilization clauses, freely accepted by the Government, do not affect the principle of its sovereign legislative and regulatory powers, since it retains both in relation to those, whether national or foreigners, with whom it has not entered into such obligations, and that, in the present case, changes in the legislative and regulatory agreements stipulated in the agreement simply cannot be invoked against the other contracting party.[41]

In *Texaco v. Libya*, the sole arbitrator also dealt with a stabilization clause included in the concession agreement.[42] The clause provided that the concession would be construed according to the regulatory framework in effect at the time it was granted and no changes in the legal system would apply without the parties' agreement. In the arbitrator's opinion, although Libya could nationalize other investors' property according to its sovereign powers, it could not nationalize contractual rights protected by a stabilization clause.[43]

Government of the State of Kuwait v. American Independent Oil Co. (AMINOIL)[44] is another important arbitral decision regarding the effect of a stabilization clause. In that case, the tribunal rejected Kuwait's arguments that the clause was contrary to domestic and international law. The tribunal held that a State could agree not to nationalize specific foreign-owned property within a limited period of time.[45] The tribunal, however, also implied that the stabilization clause would only apply in cases of a confiscatory measure taken by the State. Any lesser damage, the panel reasoned, would be payable as consequence of the legitimate expectations of the investor arising out of the parties' relationship and not the breach of the stabilization clause.[46] One of the arbitrators, Sir Gerald Fitzmaurice, disagreed with the majority opinion.[47] Fitzmaurice's dissenting opinion stated that any nationalization has a confiscatory nature but that

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[41] 21 ILM at p. 736.

[42] The clause provided that Libya "shall take all steps that are necessary to ensure that the Company enjoys all the rights conferred upon it by this concession, and the contractual rights expressly provided for in this concession shall not be infringed except by agreement of both parties."

[43] 17 ILM at p. 22. Significantly, the arbitrator held that by entering into the stabilization clause the State had placed itself within the international legal order at the same level that the foreign investor to secure certain legal status during a certain period of time.

[44] Award of 24 May 1982, IX YEARBOOK OF COMMERCIAL ARBITRATION at p. 71 (1982).

[45] *Id.* at p. 81.

[46] To calculate the amount compensation payable to the claim, the tribunal engaged in an analysis of the circumstances applicable to the specific case. *Id.* at p. 85.

[47] *Id.* at p. 91.

the important aspect was whether the nationalization was lawful or not. According to the dissenting arbitrator, Kuwait's actions were unlawful as they clearly contradicted the stabilization clause.[48] Unlawful expropriations in breach of a stabilization clause are relevant because they may affect the scope of the compensation payable by the State. An unlawful taking may provide additional remedies that are not available to the investor in case of a lawful expropriation: (1) restitution of the property; and (2) damages for the increase of the value of the property between the date of the expropriation and the date of the award.[49]

In summary, and notwithstanding some divergent views as to the State conduct prohibited by a stabilization clause,[50] arbitration practice demonstrates that in the presence of an express commitment not to alter the parties' legal relationship, a State cannot invoke its sovereignty to disregard obligations acquired with respect to foreign investors. In addition, it cannot, through measures based on its domestic law, terminate or substantially affect the contractual rights of the investor.[51]

C. Legal Stability Agreements: The Latin American Model

Commencing in the 1990s, several Latin American countries sought to attract foreign investment to their territories.[52] To accomplish this goal, these States enacted legislation authorizing the government to use special agreements by which the State guaranteed legal stability to a particular investor. At least six Latin American nations including Colombia,[53]

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48 *Id.* at 93.

49 *See Phillips Petroleum v. Iran.*, 21 Iran-US CTR p. 79 at 122.

50 *See, for example*, Sornarajah, THE INTERNATIONAL LAW at p. 408 (arguing that, at most, a stabilization clause imposes an obligation on the investor and the State to renegotiate the terms of the agreement and bring back a balance to their contractual obligations.)

51 *See* Faruque, *Validity and Efficacy of Stabilization Clauses – Legal Protection vs Functional Value*, 23 JOURNAL OF INT'L ARB. ps. 317, 322 (2003) ("The prevailing view suggests that stabilization clauses are valid despite the invocation of the principle of permanent sovereignty over natural resources, because the state's freedom of contract remains intact (irrespective of whether the principle has assumed the status of *jus cogens.*)")

52 As background, it is worth noticing that the member countries of the Cartagena Agreement (Bolivia, Colombia, Ecuador, Perú, and Venezuela), in 1970, adopted Decision 24, whereby they declared void any stipulation providing that controversies involving investments could be subject to the courts of origin of the investment or to international arbitration. *See* Decision 24, Article 21, available at http://intranet.comunidadandina.org. In 1991, the Cartagena Commission adopted a friendlier regime toward foreign investments. The settlement of disputes between foreign investors and Member States, however, remained subject to each Member's domestic law. *See* Decision 291, Article 10, available at http://intranet.comunidadandina.org ("In settling disagreements or disputes arising from direct foreign investments or investments by Subregional investors or transfers of foreign technology, the Member Countries shall abide by the provisions of their domestic legislation.")

53 Law 963 of 2005, Article 1.

Chile,[54] Ecuador,[55] Panamá,[56] Perú,[57] and Venezuela[58] have adopted this foreign investment mechanism. Legal Stability Agreements ("LSAs") reinforce rights and protections available to investors under domestic law. The rights granted to foreign investors under domestic law are standalone protections guaranteed by the State to all foreign investors and do not require a special agreement in order for them to be valid. These governments, however, as an added protection, may contractually guarantee the stability of certain of these rights and protections, both express and implied, by executing LSAs[59] which these States have accepted "are internationally recognized as instruments which promote investments."[60]

LSAs are essentially investment incentives in that they serve as additional measures on the whole and not substitutes for the basic rights and protections available to all investors in the State. Simply put, LSAs do not displace the basic rights established by the investment laws and domestic law in general but rather reinforce them. Significantly, because the authorization to enter into LSAs and, in some the cases, the approval process applicable to a specific LSA arise from legislative acts, LSAs enjoy a stronger legal platform than stabilization clauses.

The most developed and extended use of LSAs is found in Perú. Perú was the first nation to use LSAs in Latin America. It also provides useful guidance as to the legal consequences of LSAs for other countries where this mechanism has been adopted. The Preamble to the Foreign

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54 Foreign Investment Statute, Decree-Law No. 600 of December 16, 1993, Article 8.

55 Law on Promotion and Guaranty of Investment, Law No. 46. R/O219 of December 19, 1997, Article 30

56 Law No. 54 of July 22, 1998. Panama's regime differs from that used in other countries in that the investor is not required to enter into an agreement to enjoy the stabilization guaranties. The stabilization status with respect to a foreign investor automatically arises out of the completion of the investment registration process. Pursuant to Article 8 of Law No. 54, the foreign investor shall prepare and make the required minimum investment and register with the entity in charge foreseeing the investment. This public entity certifies the specific investment to the Ministry of Commerce and Industry, which shall decide whether to register the investment. This registration triggers the enjoyment of stabilization rights in favor of the investor.

57 Framework Law for the Development of the Private Investment, Legislative Decree No. 757 of November 8, 1991, Articles 38-45; Foreign Investment Law, Legislative Decree No. 662 of August 29, 1991, Article 10; Regulation of the Guaranty Regimes for Private Investment, Supreme Decree 162-92 of October 9, 1992 ("Private Investment Regulations"), Article 24-28.

58 Law on Promotion and Protection of Investments, Decree No. 356 of October 3, 1999, Article 17. The Decree was published in Official Publication No. 5.390 Extraordinary, dated October 22, 1999.

59 *See* UNCTAD Investment Policy Review, Peru, United Nations Conference on Trade and Development (UNCTAD/ITE/IPP/Misc. 19), dated 2000, at p. 20, *Cl. Exh. C-001.* Almost all foreign companies that have acquired Peruvian state–owned assets have executed Legal Stability Agreements with the Government. A recent study shows that more than 600 Legal Stability Agreements were executed between 1992 and 2003, 29 percent of which involved privatized companies. The same study indicates that Legal Stability Agreements represent at least US$14 billion in investment commitments in Peru and at least US$9.9 billion has been collected by Peru's treasury in connection with investments made pursuant to such agreements.

60 *See, for example,* Private Investment Regulations, Supreme Decree 162-92, Preamble.

Investment Law, Legislative Decree No. 662 of 1991, which authorized the execution of LSAs with foreign investors in Peru, states in relevant part:

> [….]
>
> Whereas, the Congress of the Republic, by means of [legislative decree], has ratified the Convention Establishing the Multilateral Guarantee Agency (MIGA), in order to create favorable conditions for foreign investments to contribute to the expansion of a free market economy;
>
> Whereas, foreign investment … [is] vital for the economic dynamism intended to be implemented in Peru, as provided for in Article 137° of the Political Constitution of Peru;
>
> Whereas, the Government's objective is to remove obstacles and restrictions to foreign investment in order to guarantee equal rights and obligations to foreign and domestic investors;
>
> Whereas, the Government must provide Legal Stability to foreign investors by recognizing guarantees to assure them of the continuity of the existing rules;
>
> [….]

LSAs, therefore, cement the key protections within the investment legislation for a certain period of time by ensuring that Perú will not introduce changes in its practices or its fiscal, legislative and administrative framework that might adversely affect the economic return on the underlying investment originally forecasted by the investor. Indeed, LSAs grant a continuation of the validity of the legal regime – including the regulatory texts and the way the law and texts are interpreted and applied – in force at the time of the agreement's execution. This means that a party protected by an LSA "will continue to be subject to the same legislation in force at the time of the agreement's execution, without being affected by the amendments thereto on the matters and during the term foreseen in such agreements, including the derogation of legal rules, even in the case of more or less favorable provisions."[61]

[61] Private Investment Regulations, Article 24.

LSAs typically incorporate, by express or implied reference, relevant provisions of Peruvian law.[62] The standard text for the LSAs executed by Perú is incorporated as an Annex to the Private Investment Regulations. Such text refers in general terms to the stabilization of legal regimes applicable to several of the basic rights guaranteed to foreign investors, as follows:

- **Stability of the Tax Regime**. A foreign investor cannot be subject to a higher tax effect than that contemplated by the various LSAs relating to the investment in connection with: (i) the income tax payable by the target company that is the recipient of the investment; (ii) the taxes imposed on the profits attributed to the target company; or (iii) the dividends distributed by the target company. If the income tax payable by the target company is increased by the government of Peru's actions, the foreign investor is entitled to receive compensation in an equal amount. In this way the foreign investor's net return on its investment is protected for the term of stabilization granted by the government.[63]

- **Stability of the Right to Non-Discrimination**. Perú guarantees it will treat the foreign investor and the enterprise in which it invests on an equal basis with Peruvian nationals, subject only to limited exceptions explicitly set out in the Peruvian investment laws. As such, foreign and national investors are granted identical rights and obligations regardless of nationality, geographic location, or the type or sector of economic activity they are engaged in.[64]

- **Stability of the Right to Use the Most Favorable Exchange Rate**. Foreign investors are granted the right to use the most favorable rate of exchange when converting currency.[65]

- **Stability of the Free Availability of Foreign Currency**. Foreign investors are granted the right to access foreign currency at the most favorable rate of exchange that is available.[66]

- **Stability of the Right of Free Remittance**. Foreign investors are guaranteed the right to transfer profits, capitals, and dividends abroad without any restraints. The investor may do so in freely convertible currency without having to obtain prior authorization from governmental entities.[67]

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[62] *See Duke Energy Int'l Peru Investments No. 1, Ltd. v. Republic of Peru*, Case No. ARB/03/28, Decision on Jurisdiction of February 1, 2006, at *para.* 26.

[63] *See, e.g.*, Foreign Investment Law, Article 10(a); Private Investment Regulations, Articles 19(a) and 23(a).

[64] *See, e.g.*, Foreign Investment Law, Article 10(c); Private Investment Regulations, Article 19(e).

[65] *See, e.g.*, Foreign Investment Law, Article 10(b); Private Investment Regulations, Article 19(d).

[66] *See, e.g.*, Foreign Investment Law, Article 10(b); Private Investment Regulations, Article 19(b).

[67] *See, e.g.*, Foreign Investment Law, Article 10(b); Private Investment Regulations, Article 19(c).

Not all countries have provided the same stability rights as Perú. Ecuador, for example, only provides for the stability of its tax regime.[68] Panama expressly includes any legal provision affecting acquired rights to the extent the measure is taken for a public purpose.[69] Furthermore, Panamá also provides the stability of its custom and labor regimes. Venezuela provides for a two-prong stability regime. First, LSAs may include stability clauses with respect to taxes or exports.[70] Second, the government may adopt special benefit or incentive regimes applicable to specific industries and the stability of these special regimes can be included within the respective LSA.[71] Finally, the Colombian model includes a general provision establishing the stability of those regulations identified in the respective LSA as *essential* to the agreement formalizing the investment.[72]

The legal nature of LSAs is perhaps best summarized by the arbitral tribunal in the Decision on Jurisdiction rendered in *Duke Energy Int'l Peru Investments No. 1, Ltd. v. Republic of Peru*:[73]

> [P]ursuant to the investment laws of Peru, the main features of LSAs are that (i) the stabilized legal regimes cannot be changed unilaterally by the State, and (ii) the agreements are subject to private or civil law and not administrative law. As private-law contracts, the negotiation, execution, interpretation and enforcement of the provisions set forth in LSAs are subject to the general principles applicable to contracts between private parties under the Peruvian *Civil Code.* As such, the fundamental rights granted by Perú pursuant to an LSA are private contractual rights that are enforceable against the State as if it were a private party.

Indeed, the relevant provisions in the Peruvian legislation governing private contracts in general apply to LSAs. In particular, these agreements are subject to the principle of *Contrato-Ley*, as set forth in Article 1357 of the Peruvian Civil Code. That Article states as follows:

> By law, supported by reasons of social, national or public interest, the State may establish guarantees and assurances by means of a contract.

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68 Law on Promotion and Guaranty of Investment, Article 22.

69 Law No. 54, Article 10.

70 Investment Law, Article 17.

71 *Id.* Article 15.

72 Law 963, Article 1.

73 Case No. ARB/03/28, Decision on Jurisdiction of February 1, 2006, at *para.* 31.

Article 39 of the Peruvian Investment Law confirms the foregoing:

> Legal stability investment agreements shall be concluded subject to Article 1357 of the Civil Code and shall have the [legal] effect of contracts enforceable as law, such that they may not be modified or terminated unilaterally by the State. Such contracts shall have a private rather than administrative character, and shall only be modified or terminated by agreement between the parties.

Moreover, Article 26 of the Peruvian Private Investment Regulations reinforces these principles regarding the legal nature of LSAs. Pursuant to these regulations, LSAs (a) are civil law contracts, governed by the Peruvian Civil Code; and (b) they have force of law between the parties, so the agreements may not be unilaterally amended for any reason while they are in force.

The investment protections provided for by LSAs are guaranteed by the Peruvian Constitution, as set forth in the last paragraph of Article 62:

> Liberty to contract guarantees that parties may validly agree according to the legal norms in force at the time of the contract. Contract terms may not be modified by law or other dispositions of any type. Conflicts that arise from contractual relations may only be resolved by arbitration or judicial decree, according to the mechanisms of protection set forth in the contract or contemplated by law.
>
> Through contracts-law [special investment-related private contracts of an obligatory character], the State may establish guaranties and grant securities. These may not be modified by legislation, without prejudice to the protection referred to in the preceding paragraph.

A critical feature, therefore, of the Peruvian legal stability regime is that the State contractually reinforces a set of constitutional and legal guarantees to protect private investment, which it cannot unilaterally modify, thereby ensuring that the investor's legitimate and investment-backed expectations regarding the return on its investment are protected. By virtue of the special status constitutionally accorded to such contracts, they are not subject to the State's sovereign prerogative to terminate or modify unilaterally its agreements with a private party. LSAs, by their very nature, are instruments reflecting the State's voluntary limitation of its sovereignty, at least *inter partes*. They therefore operate in a legal relationship – one of civil law – that is fundamentally distinct from, though certainly cognizant of, the administrative relationship between the local company and public authority.

Finally, as private law contracts, LSAs are subject to the principle of good faith set forth in the State's domestic law. The principle of good faith confirms that LSAs have to be interpreted in light of the meaning and purposes both parties shared when concluding the agreements. Conduct contrary to these mutually shared and, in the text, formalized expectations will breach the LSAs.

By contrast, the case of Venezuela is very interesting. After the current Government enacted the Law on Promotion and Protection of Investments, which provides for the use of LSAs, certain individuals sought a declaration of unconstitutionality from the Venezuelan Supreme Tribunal with respect to the Law's (i) provisions on LSAs,[74] and (ii) Venezuela's consent to international arbitration for investment disputes.[75] In 2001, the Supreme Tribunal rendered its opinion affirming the constitutionality of the legal norms regulating LSAs in Venezuela and the State's consent to international arbitration.[76] The Court's opinion and the arguments advanced by both the National Council for the Promotion of Investments (CONAPRI)[77] and Venezuela's Attorney-General, are relevant to understand Venezuela's commitments with respect to LSAs and international dispute resolution.

In its memorandum defending the constitutionality of the Investment Law, CONAPRI argued that the importance of LSAs arises out of the need to provide guaranties to foreign investors deciding whether to invest in the country. The constitutionality of the LSAs was supported by the requirement that these agreements be approved by the National Assembly, after the favorable opinion of the Venezuelan tax authority. Furthermore, CONAPRI alleged that the congressional approval for LSAs transformed these agreements into true legislative acts and not mere contracts. With respect to the submission of investment disputes to international arbitration, CONAPRI stated that the Venezuelan Constitution expressly provides for alternative dispute resolution mechanisms as part of the national judicial system.[78] It added that this

74 Law on Promotion and Protection of Investments, Articles 17 and 18.

75 Law on Promotion and Protection of Investments, Article 22.

76 Supreme Tribunal of Justice, Constitutional Chamber, Judgment No. 186, dated February 14, 2001. The opinion is published at the Tribunal's official website, www.tsj.gov.ve.

77 Not-for-profit organization that promotes business opportunities in Venezuela.

78 *See* Venezuelan Constitution, Article 253 ("The power to administer justice emanates from the citizens and is exercised in the name of the Republic by authority of law. The organs comprising the Judicial Power are charged with dealing with all cases and matters within their competence, through such procedures as may be determined by the laws, and with carrying out or causing the execution of their judgments. The justice system consists of the Supreme Tribunal of Justice, such other courts as may be determined by law, the Office of Public Prosecutions, the

(continued...)

constitutional mandate in favor of arbitration also applies to disputes between a foreign investor, whose country has a bilateral investment treaty with Venezuela or has ratified the ICSID Convention. Finally, CONAPRI cited Article 151 of the Venezuelan Constitution to state that there is a special regime based on the public interest to allow the use of arbitration with respect to investment agreements "when the nature of the agreement so requires".[79]

Likewise, the Venezuelan Attorney-General stated that the Investment Law was adopted to fulfill the aims of the Venezuelan Constitution of establishing a viable legal framework that it could provide legal protection to the economic activity, thus inviting foreign investment subject to the same treatment granted to nationals. The Attorney-General further stated that LSAs do not cover tax measures alone but also technologic and environmental developments and so these agreements are not directed to provide unreasonable tax advantages to foreign investors. Finally, the Attorney-General also affirmed the principle that international arbitration is accepted by the Venezuelan Constitution.

The Supreme Tribunal adopted the arguments presented by the Attorney-General. It stated that the legal authorization to subscribe LSAs did not militate against the constitutional legal reserve applicable to taxes. Venezuela's highest court explained that the government is entitled to extend guaranties to investors in areas as taxes, real estate, exports, *etc.*, as it deems fit to promote its economic goals. According to the Supreme Tribunal, the purposes of the LSAs are to provide legal protection by means of a specific regulatory framework agreed up to a certain time.

Moreover, the Supreme Tribunal rejected the notion that international arbitration was unconstitutional in Venezuela. The Tribunal reasoned that the Investment Law promotes and develops the constitutional mandate in favor of arbitration by establishing arbitration as a valid mechanism to resolve disputes between foreign investors and Venezuela.

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Public Defender's Office, criminal investigation organs, judicial assistants and officials, the penitentiary system, *alternative means of justice*, citizens participating in the administration of justice in accordance with law and attorneys at law admitted to practice.")

79 Article 151 of the Venezuelan Constitution of 1999 states: "In the public interest contracts, unless inapplicable by reason of the nature of such contracts, a clause shall be deemed included even if not expressed, whereby any doubts and controversies which may raise concerning such contracts and which cannot be resolved amicably by the contracting parties, shall be decided by the competent courts of the Republic, in accordance with its laws and shall not on any grounds or for any reason give rise to foreign claims."

Significantly, both the Supreme Tribunal and the Government have stated the constitutionality and importance of LSAs in Venezuela.[80] Furthermore, both branches of the government have also affirmed the validity of arbitration agreements as a mechanism to attract foreign investment. In light of the recent measures taken or announced by the Venezuelan government against foreign interests, these representations should play an important role in ascertaining the preeminence of freely acquired contractual obligations over unilateral actions or modifications imposed by the State's will over foreign investors.

IV. <u>Conclusion</u>

As the foregoing demonstrates, the New International Economic Order gave heretofore voiceless States, including Venezuela, the courage and ability to assert their rights over natural resources in their territory. Those rights, however, have been given shape over time. They have been limited by bilateral and multilateral investment treaties, free trade agreements and customary international law. But they have also been constrained by simple contractual principles and provisions – good faith, stabilization clauses and legal stability agreements. Even in those cases, such as Venezuela, where the government agrees to pay compensation for the breach of concessions and other State contracts, the amount offered as compensation, or the measure of damages in a potential dispute, is affected by the State's prior contractual promises. While some States continue to ignore limits to their sovereignty and the consequences of adopting unilateral measures in contravention of the acquired obligations and some investors ignore the adverse actions of the State while economic profit is still to be made, the fact remains that the New International Economic Order of today is a finely tuned balance between the rights of developing nations, the desires of developed nations and the protections granted to individual investors from around the globe.

[80] As of the date of this article, however, the Venezuelan government has yet to enter into any LSA. Accordingly, the use, scope, and effect of LSAs in Venezuela are limited to theoretical and doctrinal exercises.