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The Ponderosa Claim:

OPIC Concludes that Argentina Violated International Law

by

Perry S. Bechky*

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On 2 August 2005, the U.S. Overseas Private Investment Corporation ("OPIC") issued a determination that the Government of Argentina (the "GOA") violated international law by abrogating key provisions of the license that it had granted to operate the major natural gas pipeline in southern Argentina.[1] As a result, OPIC decided to pay a $50 million political-risk-insurance claim filed by Ponderosa Assets L.P. ("Ponderosa"), which owned 35% of the licensee.[2] This appears to be the second-largest cash payment ever made by OPIC.[3]

This article will introduce the major actors in the *Ponderosa Claim*, describe in turn Ponderosa's request for compensation and OPIC's decision, and offer preliminary observations about the analysis and significance of the *Ponderosa Claim*. As discussed further below, OPIC's

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* Perry S. Bechky is an international lawyer with Shearman & Sterling LLP, which prosecuted the *Ponderosa Claim*. The views expressed here are personal and do not represent the views of his law firm or any of its clients.

[1] OPIC, "Memorandum of Determinations – Expropriation Claim of Ponderosa Assets L.P.: Argentina – Contract of Insurance No. D733," 2 Aug. 2005 (hereinafter, "MOD"), available at http://www.opic.gov/foia/ClaimsDeterminations/2005%20Determinations/Ponderosa_Assets_L.P._202005.pdf (last checked 5 Nov. 2005).

[2] MOD at 1, 2.

[3] In 1999, OPIC paid $217,500,000 for the expropriation of two power projects in Indonesia. OPIC, "Memorandum of Determinations – Expropriation Claim of MidAmerican Energy Holdings Co.," available at http://www.opic.gov/foia/ClaimsDeterminations/1999Determinations/MidAmericanEnergy.htm (last checked 28 Oct. 2005). The $47,504,034 paid to Anaconda Company in fiscal 1977, for the expropriation of its copper mine in Chile, is nominally smaller but exceeds the *Ponderosa Claim* in real terms. See Anaconda Co. v. OPIC (AAA 1975), 14 I.L.M. 1210 (1976) (finding liability and allowing the parties to negotiate damages).

The Dabhol matter should also be noted. In 2003 and 2004, OPIC paid a total of about $111,000,000 to four separate policy-holders in connection with the expropriation of the Dabhol Power Plant in Maharashtra, India, but no individual payment exceeded about $32,000,000. See United States, Request for Arbitration under the Investment Incentive Agreement between the Government of the United States of America and the Government of India ¶35 (4 Nov. 2004), available at http://www.opic.gov/foia/Awards/GOI110804.pdf (last checked 5 Nov. 2005). The U.S. request for arbitration mentions a $20,390,000 payment to Enron for its insured losses in Dabhol. The author can find no other public acknowledgment of this payment, raising the question whether there are any other OPIC cash payments larger than the *Ponderosa Claim* that are not on the public record.

determination on the *Ponderosa Claim* is just the second public decision on the merits of the many parallel claims brought against the GOA or insurers. Its analysis differs in important respects from the other decision (*CMS (Merits)*), and may influence the developing jurisprudence. In addition, the *Ponderosa Claim* points to areas of congruence and divergence between political-risk-insurance and investor-state arbitration of expropriation claims.

The Cast

OPIC

OPIC, an agency of the U.S. Government, provides financing and insurance to U.S. businesses investing abroad. It sells insurance protecting against three political risks: expropriation, inconvertibility, and political violence.[4]

OPIC "helps U.S. businesses invest overseas, fosters economic development in new and emerging markets, complements the private sector in managing risks associated with foreign direct investment, and supports U.S. foreign policy."[5] OPIC describes its mission as "[m]obilizing America's private sector to advance U.S. foreign policy and development initiatives" and thereby "expanding economic development, which can encourage political stability and free market reforms."[6]

As part of the foreign policy apparatus of the United States, OPIC operates somewhat differently than a commercial insurer. It cannot insure any investments contrary to the environmental, labor, and other policies of the United States.[7] It only insures investments in nations that have agreed to welcome OPIC involvement, a rule that both furthers OPIC's foreign policy mission and establishes the terms under which OPIC may pursue salvage from host governments.[8] And, it generally justifies its decision whether to pay a claim in a "memorandum of determinations" available to the public. Such a memorandum should provide a reasoned explanation of a claimant's entitlement to compensation under the terms of its insurance policy.[9] Accordingly, while a

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[4] For a good introduction to OPIC, see Pablo Zylberglait, Note, OPIC's Investment Insurance: The Platypus of Governmental Programs and Its Jurisprudence, 25 Law & Pol. Int'l Bus. 359 (1993).

[5] OPIC, Program Handbook at 1 (2004), available at http://www.opic.gov/pdf/publications/04_ProgramHandbook.pdf (last checked 5 Nov. 2005).

[6] *Id.*

[7] 22 U.S.C. § 2191. Also, in OPIC's so-called "model policy," policy-holders must expressly commit to respect worker rights and, more generally, acknowledge that "OPIC has issued this contract based on statutory policy goals ... as well as underwriting considerations." Form 234 KGT 12-85 (Revised 12/03) NS, "OPIC Contract of Insurance No. __" (on file with author); an earlier edition is reprinted in R. Doak Bishop, et al., Foreign Investment Disputes at 517 (2005) (hereinafter "Bishop").

[8] Agreements entered by OPIC since 1996 are available at http://www.opic.gov/foia/Bilaterals/bilaterals_05.htm (last checked 6 Nov. 2005). OPIC's "model agreement" and an accompanying article by Robert O'Sullivan of OPIC are reprinted in Bishop, supra note 7, at 534.

[9] For a thorough review of OPIC's early determinations, see Vance Koven, Expropriation and the "Jurisprudence" of OPIC, 22 Harv. Int'l. L. J. 269 (1981).

commercial party will routinely negotiate settlements to avoid the costs and risks of litigation, OPIC generally decides claims on the merits. Through fiscal 2001, OPIC had only negotiated three small settlements of expropriation claims – totaling about $250,000 – "without determining that expropriatory action had occurred."[10]

Policy-holders generally have recourse to American Arbitration Association ("AAA") arbitration in the event OPIC denies a claim. The *Ponderosa Claim* determination is an example of OPIC explaining its reasons for paying a claim – unlike, for example, the 2003 decision on Dabhol in which an AAA tribunal obligated OPIC to pay claims by General Electric and Bechtel that OPIC had constructively rejected.[11]

Argentina

In the early 1990's, the GOA adopted policies intended to attract foreign capital needed to revitalize the Argentine economy. These policies included privatizing many state-owned businesses, signing a network of investment-protection treaties, and tying the Argentine peso to the U.S. dollar at an exchange rate of one-to-one.

In late 2001, Argentina suffered a severe financial crisis. By the end of the year, violence erupted in the streets, the GOA defaulted on its national debt, and four Presidents resigned. The resulting economic policies gave rise to the *Ponderosa Claim* (and a host of arbitral claims, discussed below).

Ponderosa

When privatizing its natural gas company, Gas del Estado, the GOA created two transportation companies to operate the southern and northern halves of the major gas pipeline: Transportadora de Gas del Sur, S.A. ("TGS") and Transportadora de Gas del Norte, S.A. ("TGN"). The GOA sold a majority of each company to a consortium of international investors. Enron Corp. ("Enron") was one of the investors in TGS, while (as we will see below) CMS Gas Transmission Company ("CMS") was one of the investors in TGN.

Enron initially held 17.5% of TGS, and later increased its stake to 35%. In December 1998, Enron assigned its interest in TGS (including the OPIC policy) to Ponderosa, an affiliated partnership. Ponderosa was therefore the policy-holder and claimant before OPIC, and its investment in TGS was the "insured investment" under the OPIC policy.

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[10] OPIC, Insurance Claims Experience to Date n.3 (30 Sept. 2001) (on file with author). Subsequently, as mentioned supra note 3, OPIC paid approximately $20 million to settle Enron's Dabhol claim without publishing any memorandum of determinations. However, since the payment to Enron followed a ruling of expropriation in an arbitration brought by Enron's co-investors, the determination of "expropriatory action" was effectively taken out of OPIC's hands. See Bechtel Enterprises Int'l (Bermuda) Ltd. v. OPIC (AAA 2005), available at http://www.opic.gov/foia/Awards/2294171_1.pdf (last checked 5 Nov. 2005).

[11] Bechtel, supra note 10.

TGS holds a gas-transportation license issued by the GOA, dated 18 December 1992 (the "License"). The License authorizes TGS to operate the southern pipeline for 35 years. TGS derives "approximately 80%" of its revenues from gas-transport fees, called "tariffs," paid by its customers.[12] Tariffs are set by the GOA, but the License requires the GOA to calculate tariffs in accordance with certain rules, including:

(i) *Devaluation Adjustments*. Tariffs are calculated in U.S. dollars and expressed in Argentine pesos. Thus, a tariff fixed at $1 would be expressed as 1 peso for so long as the peso remained pegged to the dollar at 1:1. But, if the peso were to depreciate to 2:1 against the dollar, the $1 tariff would be expressed as 2 pesos. The Devaluation Adjustments ensured TGS a constant tariff in dollar terms regardless of the peso-dollar exchange rate.

(ii) *Inflation Adjustments*. Tariffs are adjustable every six months in accordance with changes in the U.S. Producer Price Index. The Inflation Adjustments ensured TGS a constant tariff in real dollars regardless of inflation.[13]

The Ponderosa Claim

On 6 January 2002, the GOA enacted Law 25,561, the Public Emergency and Exchange Regime Reform Act (the "Act"). The Act ended the 1:1 peg of pesos to dollars. It also provided for the conversion of many dollar-denominated obligations into pesos, a policy known as "pesification."

Article 8 of the Act expressly declared Devaluation and Inflation Adjustments to be "no longer ... effective." It also pesified dollar-denominated tariffs at 1:1. As a result, a $1 tariff became a flat 1 peso tariff without any right to automatic increases for devaluation and inflation.[14]

The peso rapidly devalued to nearly 4:1, before recovering partially and stabilizing around 3:1.[15] In dollar terms, the tariffs had lost two-thirds of their value. While TGS suffered this loss of dollar value of its principal revenue stream, its international debt obligations remained constant in dollars. As TGS disclosed in its annual report, the change in the "fundamental parameters" of its

[12] MOD at 9.

[13] MOD at 3, 8-9.

[14] Article 8 reads in full, "As from the enactment of this law, in contracts entered into by the public administration and subject to public law, including contracts for works and public services, dollar (or other foreign currency) adjustment clauses indexation clauses based on the price indexes of other countries, as well as any other indexation mechanism, shall no longer be effective. The prices and rates resulting from such clauses shall be fixed in pesos at a ONE PESO (Ps. 1) = ONE U.S. DOLLAR (U.S.$1) exchange rate."

[15] See www.oanda.com/convert/fxhistory (last checked 5 Nov. 2005).

business forced it into "technical default" on its debt obligations and (unless it reached agreement with its creditors) "could jeopardize the Company's ability to remain a going concern."[16]

On 12 August 2002, Ponderosa filed an insurance claim with OPIC for the "total expropriation" of Ponderosa's investment in TGS.[17] Subject to certain exceptions and limitations, the insurance policy obliged OPIC to pay such a claim where an act or acts "constituted a violation of international law or a material breach of local law" and "directly" "deprived" Ponderosa "of fundamental rights in the insured investment."[18] In brief, Ponderosa claimed that the Act deprived Ponderosa's investment in TGS of its economic value and led to the complete write-off of that investment.[19]

The Memorandum of Determinations

On 2 August 2005, OPIC determined that the Act violated international law, deprived Ponderosa of fundamental rights in TGS, and caused a complete write-off of Ponderosa's investment in TGS.

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[16] TGS Annual Report (Form 20-F) for the fiscal year ended December 31, 2001 (filed June 20, 2002), at F-29 - F-30, stating:

> In view of the substantial and significant adverse conditions prevailing in Argentina and the alteration of fundamental parameters of the Company's License, TGS has not been able to maintain the financial ratios required by its outstanding debt instruments. As a result, and because the Company has not complied with certain related covenants contained in its debt agreements, the Company is in technical default under those agreements, meaning that the Company's creditors may declare the debt immediately due and payable. If that were to happen, the Company would not have the funds necessary to repay its indebtedness, unless it were able to obtain alternate financing or implement another strategy such as selling certain assets, restructuring or refinancing its indebtedness or seeking additional equity capital.
>
> ...
>
> TGS currently is negotiating with its creditors for waivers of the relevant covenants, due to the uncertainty regarding the outcome of the renegotiation of the Company's tariffs no assurance can be given that these negotiations will be successful or that any agreed-upon solution will not have additional adverse consequences for the Company. If negotiations fail, the Company's creditors may accelerate the Company's debt which could jeopardize the Company's ability to remain a going concern.

[17] "OPIC does not insure against partial expropriation as such. An expropriation of a portion of the insured investment, or an action which partially impairs the investor's rights in the investment, is covered only if it meets the requirements for 'total expropriation.'" Notice of Adoption of Form Contract, 51 Fed. Reg. 3438, 3440 (27 Jan. 1986).

[18] MOD at 4 (citing Section 4.01 of the policy). The OPIC policy also required that the acts be attributable to an actual or *de facto* governing authority and that their "expropriatory effect" continues for at least six months. Neither of these requirements, however, is of much interest where a statute clearly attributable to the legislature of a sovereign state clearly remains in effect for several years (to date).

[19] MOD at 13-14.

OPIC applied customary international law as articulated in the American Law Institute's *Restatement (Third) of Foreign Relations Law of the United States* (1987) (the "Restatement"). According to the Restatement, a state is responsible under international law for economic injury to an alien in two cases: for certain expropriations of the alien's property and for certain breaches of a public contract with the alien. OPIC focused on the latter, because "the second grounds for an international law violation are much more clearly demonstrated in the present circumstance."[20]

In relevant part, the Restatement provides that international law is violated where (a) a state (b) breaches or repudiates (c) a contract (d) with a national of another state, provided (e) the breach or repudiation is "motivated by noncommercial considerations" and (f) compensation is not paid.[21] OPIC determined that each criterion was satisfied in the *Ponderosa Claim*:

- The License is a contract between the GOA (a state, of course) and TGS.[22]
- TGS should be treated as an alien for relevant purposes. OPIC looked to TGS's foreign ownership, regardless of the fact that TGS itself is organized under Argentine law.[23]
- The "GOA has materially changed the terms of the [License] unilaterally," which "constitutes a repudiation by the GOA of its obligations under the License."[24] OPIC considered the tariff-calculation formula – including the Devaluation and Inflation Adjustments – to constitute the GOA's "main," "primary," and "fundamental" obligation under the License. The License expressly constrained GOA's right to modify tariffs, but the Act "purportedly supersedes any previous laws to the contrary by a sweeping provision" that expressly "abrogate[s]" any contrary provision of law.[25]

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[20] MOD at 6-7.

[21] Restatement, § 712. International responsibility also arises where the breach or repudiation is discriminatory, and where the investor is denied either an "adequate forum" to hear a contractual claim or any compensation awarded as a result of such a claim. *Id.*; see discussion infra under "Commentary."

[22] MOD at 7.

[23] MOD at 7-8; see discussion infra under "Commentary."

[24] MOD at 8. OPIC appears to wrestle with the question whether this holding goes beyond its earlier interpretation of "repudiation" in *Revere Copper*, infra note 41, before concluding in essence that there is a difference in wording but not in substance.

[25] The MOD quotes Article 19 of the Act, which provides, "This law deals with matters concerning the overriding public interest. No person may assert irrevocably acquired rights against it. Any other provision to the contrary is hereby abrogated." This Article appears to reinforce Article 8, supra note 14, which pronounced that Devaluation and Inflation Adjustments "shall no longer be effective."

- The repudiation of the GOA's main obligation under the License was "motivated by noncommercial considerations."[26] OPIC noted that the GOA's interest in the License and its repudiation was that of a regulator and a sovereign, because the GOA did not have "a commercial interest in the License.[27] Adding suspenders to this belt, OPIC further considered the "actual motive of the GOA" and concluded that the purposes stated in Article 1 of the Act were regulatory and not commercial.[28]

- Compensation was not paid. OPIC highlighted the role of lack of compensation in completing the international delict: "While the contractual obligation [to allow Devaluation and Inflation Adjustments] could not prevent the government from carrying out sovereign acts, it does require that the government answer in damages for its conduct.... [Repudiation] gave rise to a right to compensation. The GOA's decision not to compensate TGS thereby constitutes a violation of international law."[29]

Having found that the Act violated international law, OPIC considered whether it also "directly" "deprived" Ponderosa of "fundamental rights" in the insured investment.[30] OPIC concluded that, even though the Act had no impact on the shareholders' control over "the assets of TGS, including the License," the Act reduced "the revenue stream of Ponderosa ... so drastically ... that it resulted in the total write-off of the investment under the equity method of accounting.... [T]he right to recover [an investment's] economic value in accordance with the terms governing that investment is a fundamental right of the investor."[31]

Finally, OPIC considered whether any exceptions or limitations applied. Notably, OPIC put on the record that its independent expert in forensic accounting had verified that Ponderosa's claim was "substantially correct," notwithstanding "deficiencies" found in Enron's accounting.[32] Given Enron's well-publicized collapse, it is understandable that OPIC would want to demonstrate the

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[26] MOD at 10-11.

[27] In this regard, the License allowed TGS to transport gas in exchange for tariffs to be paid by its customers, not by the GOA. Contrast this with a case where a government more clearly has both commercial and regulatory interests. For example, when the Indian State of Maharashtra terminated its purchases of energy produced by the Dabhol Power Plant, there was a dispute whether an act apparently commercial on its face was in fact motivated by commercial or political considerations. See Bechtel, supra note 10, at 17, 26.

[28] MOD at 11 (noting that Article 1 of the Act declared a state of national emergency and specified that the purposes were "to rearrange the financial, banking and exchange market system" and "to relaunch the economy").

[29] MOD at 11-12.

[30] MOD at 4 (citing Section 4.01 of the policy).

[31] MOD at 13-14; see also OPIC Model Policy, supra note 7, § 4.01(a) ("rights are 'fundamental' if without them the Investor is substantially deprived of the benefits of the investment").

[32] MOD at 2 & n.3, 14-17.

lengths to which it had scrutinized the claim.[33] This approach points the way forward in this age of heightened attention to accounting.

Commentary

CMS (Merits) and the Coming Arbitral Awards

The *Ponderosa Claim* is best understood in light of the dozens of parallel claims brought against the GOA. The International Centre for Settlement of Investment Disputes ("ICSID") has registered nearly forty claims against the GOA; most were filed by utilities hurt by the Act's effects on tariff-calculation mechanisms in their contracts.[34]

The *Ponderosa Claim* is only the second public decision examining the merits of the Act's consistency with international law. Ten weeks earlier, an ICSID tribunal had rendered the first such decision; it concerned the injury to CMS's investment in TGN.[35] The *Ponderosa Claim* does not cite the *CMS (Merits)* award. The two decisions may be regarded as independent analyses of the same situation, which follow separate paths to a common conclusion: the Act violated international law.

The *CMS* Tribunal found that the Act violated two provisions of the Bilateral Investment Treaty ("BIT") between the United States and the GOA. First, the Act denied CMS "fair and equitable treatment" by removing the "crucial" tariff-calculation adjustments and thereby "entirely transform[ing] and alter[ing] the legal and business environment."[36] Second, the removal of the tariff provisions also violated the BIT's so-called "umbrella clause," which obliges GOA to "observe

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[33] Indeed, OPIC went so far as to consider expressly whether Enron "provo[ked]" the GOA to enact the Act, before concluding unsurprisingly that the allegations of Enron's "unorthodox accounting practices ... are unrelated to the expropriation and to [Ponderosa's] loss in Argentina...." MOD at 14.

[34] See www.worldbank.org/icsid/cases/pending.htm (last checked 5 Nov. 2005). In addition, the press has reported other claims filed with ad hoc tribunals, albeit with less transparency.

[35] CMS Gas Transmission Company v. Argentine Republic, ICSID Case No. ARB/01/8 (12 May 2005), 44 I.L.M. 1205 (2005). The *CMS* award is subject to a pending annulment proceeding registered by the ICSID Secretariat on 27 September 2005. The GOA argues that (i) the *CMS* Tribunal "manifestly exceeded its powers" by rejecting the GOA's defense that the national economic emergency justified its actions and excused any obligation to pay compensation, and (ii) the award "failed to state the reasons on which it is based." The GOA's application for annulment is available at http://www.iisd.org/pdf/2005/investsd_cms_annulment_petition.pdf (last checked 4 Nov. 2005).

OPIC also had occasion to consider an aspect of the TGN situation. A creditor of TGN claimed that other measures taken by the GOA in the weeks before and after the Act had prevented TGN from converting payments on a note. OPIC rejected this claim on the ground that the GOA had not significantly interfered with TGN's ability to convert currency for a sufficiently long period to satisfy the requirements of the policy for "inconvertibility" coverage. OPIC did not examine whether these measures were expropriatory or otherwise violated international law. OPIC, "Memorandum of Determinations – Inconvertibility Claim of First Trust of New York, National Association: Argentina – OPIC Contract of Insurance No. F181" (11 Feb. 2002), available at http://www.opic.gov/foia/ClaimsDeterminations/2002Determinations/TGNclaim2002.pdf (last checked 28 Oct. 2005).

[36] CMS (Merits) Award. at ¶ 275.

any obligation it may have entered into with regard to investments."[37] By contrast, the Tribunal held that the Act was not expropriatory, on the ground that it did not affect CMS's control over TGN.[38]

There are obvious parallels between the *Ponderosa Claim's* repudiation-of-contract analysis and the *CMS* Tribunal's analysis of the umbrella and "fair and equitable" clauses. In broad strokes, both center on the fact that the GOA ended tariff-calculation commitments in gas-transport licenses with devastating effects on the licensee. The *CMS* Tribunal even considered the noncommercial character of the Act to be highly relevant to the umbrella clause,[39] thus highlighting the convergence between the Tribunal's conventional and OPIC's customary analyses.

On expropriation, the paths diverge and OPIC took the higher road. This difference might be overlooked, because OPIC expressed no ultimate conclusion on expropriation.[40] Yet, OPIC in fact made several points about expropriation that implicitly contradict the *CMS* Tribunal's cramped view that a finding of expropriation is contingent on deprivation of the investor's control.[41]

First, OPIC surveyed customary support for the "theory of indirect expropriation."[42] This survey demonstrated that an expropriation may occur even where an investor retains both title to and possession of its property. It did not expressly address control. But its very focus on other criteria, especially loss of economic benefit, implicitly denies the central role the *CMS* Tribunal claimed for control.

Second, OPIC stated that "there is reason to believe that the [Act] went beyond the commonly accepted principles of a state's power," and therefore crossed the line between "a valid exercise of regulatory power" and expropriation.[43] Although OPIC judged it unnecessary to resolve the issue definitively, the "belie[f]" telegraphed here is supported elsewhere in the opinion.

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[37] CMS (Merits) Award. at ¶¶ 296-303.

[38] *Id.* at ¶¶ 263-64 ("the investor is in control of the investment; the Government does not manage the day-to-day operations of the company; and the investor has full ownership and control of the investment.").

[39] *Id.* at ¶¶ 301-01.

[40] MOD at 5 ("We take no position as to whether the GOA's enactment of the [Act] constitutes a 'taking' by the state of [Ponderosa's] property."), 6-7 ("we need not decide this question").

[41] The *CMS* Tribunal's view evokes the position taken by OPIC – and rejected by the arbitral tribunal – in *Revere Copper*. In that case, the Government of Jamaica raised taxes on Revere Copper's investment notwithstanding a contractual promise not to do so. Revere Copper asserted that the taxes forced it to close the investment, and filed an expropriation claim under its OPIC policy. OPIC denied the claim on the ground that Jamaica did not deprive Revere Copper of possession or the ability to operate. OPIC derided Revere Copper's contract abrogation argument as "nonsense." But the tribunal disagreed. It held that international law applied to the contract, that international law required "good faith" compliance with "[f]oreign investment agreements freely entered into," and that Jamaica breached the contract in violation of international law. "We do not regard [the investment company's] 'control' of the use and operation of its properties as any longer 'effective' in view of the destruction by Government actions of its contract rights." Revere Copper & Brass, Inc. v. OPIC (AAA 1978), 56 I.L.R. 258, 270, 279-90 (1980).

[42] MOD at 5-6.

[43] MOD at 1, 6-7.

Specifically, OPIC concluded that the Act deprived Ponderosa of "fundamental rights" even when it had no impact on control. Reading this conclusion together with OPIC's survey on indirect expropriation strongly suggests that the Act constituted an indirect expropriation.

Finally, although OPIC splits its analysis between expropriation and contract repudiation, it also bridges this divide with the suggestion that repudiation is essentially equivalent to expropriation. Immediately after concluding that the GOA repudiated the License, OPIC stated:

> The theory that certain contractual breaches may constitute expropriation has other bases in law. International arbitral tribunals have recognized that rights under contracts are property subject to expropriation.[44] Furthermore, in its definition of expropriation in the United States Code, Congress has explicitly included impairment by a government of a contract with a foreign investor.[45]

The Restatement also lends support to this bridge, explaining that international responsibility arises for contract repudiation that is "akin to an expropriation."[46]

OPIC Relationship with Investor-State Arbitration

Political-risk-insurance is planted in the same soil as ICSID and BITs. Both insurance and ICSID/BITs address concerns impeding foreign direct investment in developing states. Substantively, developing and Communist states had challenged the customary protections for investors. Procedurally, an investor often lacked effective means of enforcing its rights unless it could persuade its own home state to bring a claim against the host state on its behalf ("diplomatic protection"). Both political-risk-insurance and ICSID/BITs are designed to give investors adequate and enforceable alternatives to customary protections.[47]

Both took root and grew. OPIC has signed agreements with "more than 150 countries."[48] Other states and the Multilateral Investment Guarantee Agency of the World Bank also offer

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[44] MOD at 10, citing *Liamco*, *German Interests in Polish Upper Silesia*, and *Norwegian Shipowners*.

[45] *Id.*, citing 22 U.S.C. § 2198(b) (defining "expropriation" to include "any abrogation, repudiation, or impairment by a foreign government of its own contract with an investor with respect to a project, where such abrogation, repudiation, or impairment is not caused by the investor's own fault or misconduct, and materially adversely affects the continued operation of the project"). As a matter of OPIC history, this citation is noteworthy. For decades, OPIC had taken the view that this statutory language was "enabling" and did not actually govern OPIC insurance policies, because OPIC had opted not to offer insurance to the full extent authorized by Congress. See Koven, supra note 9, at 278, 281. The *Ponderosa Claim*'s contract-repudiation analysis, together with this citation, appears to signal the demise of that view.

[46] Restatement § 712 comment h & Rep. Note 8.

[47] On BITs, see, e.g., Kenneth Vandevelde, U.S. Bilateral Investment Treaties: The Second Wave, 14 Mich. J. Int'l L. 621, 625 (1993); Jeswald Salacuse, BIT by BIT: The Growth of Bilateral Investment Treaties and Their Impact on Foreign Investment in Developing Countries, 24 Int'l Law. 655, 660 (1990).

[48] OPIC Program Handbook, supra note 5, at 1, 40-43.

political-risk-insurance, as do some major commercial insurers like AIG and Lloyd's. Meanwhile, ICSID has 102 arbitrations pending on its docket – more than the total number of cases (94) concluded in its 39-year history.[49] And more than 150 states have negotiated a network of more than 2000 BITs, a network characterized as "truly universal in [its] reach and essential provisions."[50] Indeed, the BIT network demonstrates such extensive and widespread state practice as to raise the question whether BITs have resolved, as a matter of custom as well as convention, the very debate that gave them life. In this regard, an arbitral tribunal regarded BITs as establishing custom on the measure of compensation to be paid, while Professor Reisman observes that the broad substantive definition of "expropriation embodied by BITs to some extent has become – and to some extent remains in the process of becoming – customary international law...."[51]

Despite their common history, OPIC and ICSID/BITs represent fundamentally different approaches to the same problem. ICSID/BITs "depoliticize" investment disputes; they remove the investor's home state from the customary role of diplomatic protection.[52] In place, they provide the investor with a set of substantive rights directly enforceable by the investor through "investor-state arbitration" against the host state.[53] The investor's home state has no role in such arbitration. In fact, the Washington Convention expressly bars traditional diplomatic protection in connection with arbitrations submitted to ICSID unless the host state "fail[s] to abide by and comply with the award rendered" by an ICSID tribunal.[54] By contrast, OPIC embodies a political solution – what might be called contractual politicization. The OPIC policy gives the insured investor a contractual right to

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[49] Compare www.worldbank.org/icsid/cases/pending.htm with www.worldbank.org/icsid/cases/conclude.htm (last checked 5 Nov. 2005).

[50] CME Czech Republic B.V. v. The Czech Republic, Final Award ¶ 497 (UNCITRAL 2003). It should be noted that Professor Brownlie both joined the unanimous award and issued a separate opinion. Id. at ¶ 650.

[51] Compare id. ¶¶ 497-99 (discussing, inter alia, Mondev Int'l Ltd. v. United States, Final Award ¶¶ 117, 125 (ICSID Add'l Facility 2002) with W. Michael Reisman & Robert Sloane, Indirect Expropriation and Its Valuation in the BIT Generation, Brit. Y.B.I.L. 2003 at 115, 150 n. 158 (2004) ("Whether and to what extent BITs codify customary international law remains an open question. The nearly 2,200 BITs in existence today ..., and the increasing citation and application of general principles enunciated in arbitral awards rendered on the basis of their standards, suggests that the broader conception of expropriation embodied by BITs to some extent has become – and to some extent remains in the process of becoming – customary international law, insofar as states begin to acknowledge these standards as legally binding in contexts not governed by BITs.").

[52] See Christoph H. Schreuer, The ICSID Convention: A Commentary at 397-414 (2001); see also Vandevelde, supra note 47, at 626.

[53] Cf. The Loewen Group Inc. v. United States, ICSID Case No. ARB(AF)/98/3, Final Award ¶223 (2003) (investor-state arbitration "represents a progressive development in international law whereby the international investor may make a claim on its own behalf and submit the claim to international arbitration"), available at www.state.gov/documents/organization/22094.pdf (last checked 5 Nov. 2005).

[54] Convention on the Settlement of Investment Disputes between States and Nationals of Other States, done at Washington, entered into force 14 Oct. 1966, art. 27(1).

compensation. But payment of compensation inherently politicizes the dispute: the U.S. Government must bring a claim against the host state unless it is prepared to bear the costs itself.[55]

Political-risk-insurance and ICSID/BITs each offer advantages to the investor. The former can be negotiated in advance to clearly cover anticipated risks to particular investments. And it may offer a shorter and surer route to compensation than investor-state arbitration.[56] But it requires advance planning and payment of insurance premiums.

Like neighboring trees, the branches of OPIC and ICSID/BITs can be expected to intertwine. The *Ponderosa Claim* highlights several issues about these relationships.

First, as one would expect, the *Ponderosa Claim* respectfully cited the jurisdictional rulings by the *CMS* and *Ponderosa* Tribunals – without, of course, any suggestion that those rulings are binding upon OPIC. As part of its contract-repudiation analysis, OPIC considered whether to regard TGS as an alien based on its non-Argentine ownership. It looked to the BIT definition of "investment" and the ICSID rulings upholding jurisdiction. OPIC concluded, "Since TGS would be treated as a national of a country other than Argentina for purposes of arbitrating claims under the BIT, it can also be considered a foreign national party to a contract under international law principles."[57] This decision to look past corporate formalities is consistent with the thrust of the

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[55] Cf. Revere Copper, supra note 41, at 277-78 (finding that OPIC insurance for a contract inherently "internationalize[s]" the contract, "particularly as all rights acquired by OPIC upon paying a claim ... become rights of the U.S. Government").

[56] The *Ponderosa Claim* is instructive. Ponderosa's OPIC claim lasted three years, but is now finished. Its ICSID claim will have a merits hearing "late in 2005." MOD at 12. The Tribunal presumably will render an award in 2006. If Ponderosa were to win the award, the GOA would almost certainly file an annulment proceeding (as in *CMS*). Indeed, the GOA has indicated its willingness to further challenge any award in its municipal courts. See, e.g., Michael Casey, "Argentina Justice Minister Seeks to Declaw World Bank Tribunal," Dow Jones Newswires (12 Apr. 2005). And Ponderosa's ICSID claim is more advanced than all but one of the parallel ICSID claims against the GOA.

In addition, the U.S. proposal to replace ICSID annulment proceedings with a fuller appellate mechanism should be noted as well. See, e.g., 19 U.S.C. § 3802(b)(3)(G)(iv). The merits of this proposal are beyond the scope of this article, but it is clear that the availability of appellate review would not shorten ICSID proceedings.

[57] The Restatement sets forth a strict rule that "a corporation has the nationality of the state under the laws of which the corporation is organized." Restatement, § 213. It also, however, repeatedly mentions the practice of states (especially the United States) to afford diplomatic protection to foreign subsidiaries of local corporations with claims against the state where the subsidiary is incorporated. *Id.* § 213, comment d; § 713, comment e. And it appears to endorse this practice, stating that a state with "significant connections" to a corporation other than nationality, including links based on shareholder nationality, "may treat the corporation as its national at least for certain purposes." *Id.* § 213, comment d. Indeed, it expressly states that *Barcelona Traction* "does not preclude representation of the company by a state with significant links against the state of incorporation itself." *Id.* § 213, Rep. Note 3. Thus, the Restatement may be said to imply that state practice was adding flexibility to strict notions of corporate nationality – a trend that may have advanced in the years since 1987.

In any event, the Restatement also acknowledges that "States are free to depart from the rule of this section by international agreement." *Id.* § 213, comment e. Among the examples cited were "friendship, commerce, and navigation treaties," the precursors to modern BITs. *Id.* So, OPIC appropriately relied on the U.S.-Argentina BIT as establishing the governing rule.

modern law of international investments. Through the BIT network, the international community has shifted the locus of inquiry from the nationality of the investment vehicle to that of the investor, the real party in interest.[58]

Second, the divide in OPIC's analysis between expropriation and contract repudiation reveals that OPIC understands a compensable "expropriation" to occur whenever there is "a violation of international law" (provided the other criteria in the insurance policy are satisfied as well). This raises the question whether the key phrase, "a violation of international law," embraces conventional as well as customary law. If so, then compensation would be due for any breach of a BIT with a host state (meeting the other policy criteria), effectively incorporating the BIT into OPIC policies insuring investments in that state.

Finally, in dicta, OPIC considered whether the GOA failed either to provide an adequate forum for resolution of the contractual-repudiation claim or to pay compensation "for any repudiation or breach determined to have occurred."[59] OPIC acknowledged that the GOA agreed to resolve the claim through international arbitration and that the claim was in fact pending before an ICSID tribunal. However, since OPIC "determined" that the GOA had repudiated the License and the GOA had not yet paid compensation, OPIC concluded that – for the time-being – the GOA was in violation of the obligation to pay compensation for any repudiation "determined to have occurred." OPIC stated that the GOA could "remed[y]" this violation by paying the arbitral award – if in fact the tribunal orders the GOA to compensate Ponderosa. This dicta is analytically unsupportable (although harmless practically). The GOA can be said to have violated international law by repudiating its contract with TGS, thus giving rise to the arbitral claim, but it cannot be condemned for declining to pay an arbitral award that has not yet been rendered. The "determin[ation]" of repudiation contemplated by the Restatement is a determination by the "adequate forum" referenced in the first-half of the same clause.[60] It would have been preferable for OPIC to omit this discussion, expressly recognizing (as it had done with the question whether the repudiation was discriminatory in fact) that this issue was irrelevant to its conclusion.■

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[58] For example, the new "model" text developed by the United States for negotiating BITs applies substantive protections to a "covered investment," a term that embraces a foreign shareholder's interest in a local corporation. See "Treaty between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment," arts. 1 (definitions), 2(1)(b) (general application to covered investments), 5(1) (application of minimum standard of treatment to covered investments), 6(1) (expropriation of covered investments), available at http://www.ustr.gov/assets/Trade_Sectors/Investment/Model_BIT/asset_upload_file847_6897.pdf (last checked 6 Nov. 2005). The "2004 Model BIT" also allows an investor to commence investor-state arbitration on its own behalf and on behalf of a local corporation that it owns or controls directly or indirectly. *Id.* at art. 24(1).

[59] MOD at 12 (discussing Restatement, § 712).

[60] See Restatement § 712, comment h & Rep. Note 10 ("[A] state would incur responsibility under international law if it failed to provide access to an adequate forum for dispute resolution or failed to carry out a determination *by a forum thus provided.*") (emphasis added).