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State Responsibility in Case of Stabilization Clauses

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STATE RESPONSIBILITY IN CASE OF "STABILIZATION" CLAUSES

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MODERN concession agreements between States and foreign corporations sometimes contain, in addition to choice-of-law clauses, the specific commitment on the part of the contracting State not to alter the terms of the concession, by legislation or by any other means, without the consent of the other contracting party. These stipulations are usually known as "stabilization" clauses.[1] The commitment embodied in these clauses poses a special situation from the standpoint of State responsibility. Before discussing such a situation, let us first see what is the traditional position as to the international responsibility of States for measures affecting contractual rights, and also, the position as to responsibility in situations where those rights are derived from concession agreements containing choice-of-law clauses.

I. STATE RESPONSIBILITY FOR THE BREACH OF CONTRACTUAL OBLIGATIONS: THE TRADITIONAL POSITION

A. The Law Governing Ordinary State Contracts

Questions concerning State responsibility for measures affecting contractual rights of an alien (individual or corporation) depend primarily on the law governing the particular contractual relationship between the State and the alien. In traditional international law, the problem of determining the governing law did not arise in the way that it does after the type of choice-of-law clauses contained in modern concession agreements came into the picture. It was always assumed that State contracts were governed by municipal law. Such an assumption is reflected in the position taken by the World Court in

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1. A distinction has been made between "stabilization" clauses *stricto sensu* and "intangibility" clauses. Under the former, the State "freezes" its legislation; under the latter, it commits itself not to exercise other sovereign powers to change the terms of the concession agreement. *See* Prosper Weil, *Les Clauses de Stabilisation ou d'Intangibilité Insérées dans les Accords de Développement Economique*, *in* MÉLANGES OFFERTS À CHARLES ROUSSEAU 301, 307-08 (A. Pedone ed., 1974).

the *Serbian*[2] and *Brazilian Loan*[3] cases. In the view of the Permanent Court of International Justice, "[a]ny contract which is not a contract between States in their capacity as subjects of international law is based on the municipal law of some country."[4] Since the will or intention of the parties was the primary factor in determining the applicable law, it was also a logical assumption, in the absence of an express provision to the contrary, that the parties agreed that their contractual relationships be governed by the domestic law of the contracting State. This was only natural given the weight usually attached to the fact that one of the contracting parties in this kind of relationship is a State.[5]

If, in light of the foregoing, it can be assumed that ordinary contracts between States and aliens are governed by the municipal law of the former, when or how do measures affecting the contractual rights of the latter give rise to international responsibility? Those measures, *per se*, certainly do not make the State internationally responsible; there must be a related act or omission constituting a breach of an international obligation, including that prohibiting the abuse of rights. Let us now consider how the traditional position is formulated.

B. How the Traditional Position is Formulated

The late Edwin M. Borchard, one of the first to contribute to the formulation of the traditional position, contended that "diplomatic interposition" in the cases of responsibility under consideration "will not lie for the natural or anticipated consequences of the contractual relation, but only for arbitrary incidents or results, such as a denial of justice or flagrant violation of local or international law."[6] To Miss M. Whiteman, in order to substantiate an international claim of this

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2. Concerning the Payment of Various Serbian Loans Issued in France (Fr. v. Kingdom of Serbs, Croats and Slovenes), 1929 P.C.I.J. (ser. A) No. 20/21 (July 12) [hereinafter *Serbian Loans*].

3. Concerning the Payment in Gold of the Brazilian Federal Loans Issued in France (Fr. v. Braz.), 1929 P.C.I.J. (ser. A) No. 20/21 (July 12) [hereinafter *Brazilian Loans*].

4. *Id.* at 121 (the World Court took the same position in the case of the *Serbian Loans* at 41). The same view is frequently found in the jurisprudence of international claims commissions. *See* A. FELLER, THE MEXICAN CLAIMS COMMISSIONS 1923-1934, at § 157 (1935). Basing itself on these precedents as well as diplomatic practice, a League of Nations committee admitted that "[e]very contract which is not an international agreement — *i.e.*, a treaty between States — is subject (as matters now stand) to municipal law . . . ." *Report of the Committee for the Study of International Loan Contracts*, League of Nations Doc. C.145 M.93 1939 II A, at 21 (1939).

5. *See* F.A. Mann, *The Proper Law of Contracts Concluded by International Persons*, 1959 BRIT. Y.B. INT'L L. 34, 41.

6. EDWIN M. BORCHARD, THE DIPLOMATIC PROTECTION OF CITIZENS ABROAD § 112, at 284 (1915).

kind, it was necessary to prove that the respondent Government has committed a wrong through its duly authorized agents or that the claimant has suffered a denial of justice in attempting to secure redress.[7] Other American writers have expressed themselves in the same or similar terms.[8]

The same view has been taken by European publicists. K. Lipstein, for example, maintains that "the failure of a State to fulfill a contractual obligation [towards an alien], unless such a failure is confiscatory or discriminatory in nature, does not automatically result in a breach of international law."[9] Also, Olof Hoijer had contended earlier that an "unlawful invasion of the [contractual] rights of an alien does not *per se* constitute a violation of international law; the latter is violated only if no reparation is made for the injuries sustained after the remedies established by the laws of the country have been exhausted."[10] In addition, to F.A. Mann, the "crucial case" is whether there is "ground for an allegation of discrimination, *abus de droit*, denial of justice, or any other international tort of the traditional type."[11]

The foregoing formulations of the traditional position find support in arbitral precedents. To illustrate, in *International Fisheries Co. v. United Mexican States*[12] the U.S.-Mexican General Claims Commission was of the opinion that the cancellation of the contract "was not an arbitrary act, a violation of a duty abhorrent to the contract and which in itself might be considered as a violation of some rule or principle of international law."[13] The Commission further stated, "[i]f every non-fulfillment of a contract on the part of a government were to create at once the presumption of an arbitrary act, which should therefore be avoided, governments would be in a worse situation than

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7. 3 MARJORIE M. WHITEMAN, DAMAGES IN INTERNATIONAL LAW 1558 (1943).

8. *See* CLYDE EAGLETON, THE RESPONSIBILITY OF STATES IN INTERNATIONAL LAW §§ 47-48 (1928); FELLER, *supra* note 4, § 154; ALWYN V. FREEMAN, THE INTERNATIONAL RESPONSIBILITY OF STATES FOR DENIAL OF JUSTICE 111-12 (1938). More recently it was stated that "[a] simple breach of contract . . . constitutes a violation of local but not of international law." PHILIP C. JESSUP, A MODERN LAW OF NATIONS 109 (1948).

9. K. Lipstein, *The Place of the Calvo Clause in International Law*, 1945 BRIT. Y.B. INT'L L. 130, 134.

10. OLOF HOIJER, LA REPONSABILITÉ INTERNATIONALE DE ÉTATS [The International Responsibility of States] 118 (1930); *see also* J.C. Witenberg, *La Recevalilite des Reclamations Devant les Jurisdictions Internationales*, 1932-III RECUEIL DES COURS D'ACADEMIE DE DROIT INTERNATIONAL [R.C.A.D.I.] 1, 57-58 (1968).

11. F.A. Mann, *State Contracts and State Responsibility*, 54 AM. J. INT'L L. 572, 577 (1960); *see also* CHARLES DE VISSCHER, THEORY AND REALITY IN PUBLIC INTERNATIONAL LAW 194 (P.E. Corbett trans., 1957); IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 547-51 (3d ed. 1979).

12. (U.S. v. Mex.), 4 R.I.A.A. 691 (1931).

13. *Id.* at 699.

that of any private person, a party to any contract."[14] In the famous *North American Dredging Co. of Texas v. United Mexican States*[15] case, the General Claims Commission indirectly took the same position when it held that the Commission retained jurisdiction over any case in which the "claim is based on an alleged violation of any rule or principle of international law"[16] notwithstanding any "Calvo clause"[17] in the contract. In the *Rudloff*[18] case, the Claims Commission held that "[i]f any consideration of public policy required the abrogation of the Rudloff concession, the proper judicial proceedings should have been taken to that end, and in conformity with the law."[19]

C. *Rationale of the Traditional Position*

The rationale of the traditional position lies upon a principle common to most, if not all, municipal legal systems. As formulated by the United States Supreme Court in *Georgia v. City of Chattanooga*,[20] the right of eminent domain was referred to as:

> [t]he taking of private property for public use upon just compensation is so often necessary for the proper performance of governmental functions that the power is deemed to be essential to the life of the State. It cannot be surrendered, and if attempted to be contracted away, it may be resumed at will.[21]

In the words of Lord Radcriffe, the law of the forum "not merely sustains but, because it sustains, may also modify or dissolve the contractual bond."[22] Thus, like in those situations resulting from measures affecting acquired rights of other kinds, the breach of ordinary contracts between States and aliens, being governed by municipal law, constitutes the exercise of a sovereign power, and therefore, cannot involve, *per se*, international responsibility.

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14. *Id.* at 700.
15. (U.S. v. Mex.), 4 R.I.A.A. 26 (1926).
16. *Id.* at 33.
17. *Id.* A "Calvo clause" in contracts between nations and aliens is a clause that a nation inserts to preclude the alien party from exercising any rights other than those granted by the laws of that nation. The alien party is thereby deprived of any rights as aliens and no intervention by foreign diplomats is permitted. *Id.* at 26-27.
18. JACKSON H. RALSTON, THE VENEZUELAN ARBITRATIONS OF 1903, at 182 (1904).
19. *Id.* at 197.
20. 264 U.S. 472 (1924).
21. *Id.* at 480.
22. Kahler v. Midland Bank, 1950 App. Cas. 24, 56 (H.L. 1949).

D. *The Swiss-French Doctrine: A Challenge to the Traditional Position*

The traditional position as to State responsibility (for measures affecting contractual rights) has been challenged twice in proceedings before the World Court. Notwithstanding the fact that the contractual relationship was wholly governed by the municipal law of the contracting State, in *Losinger and Co.*[23] the Swiss Government contended before the former Permanent Court that *pacta sunt servanda* (as a principle of international law) was applicable.[24] In its view, such principle "must be applied not only to agreements directly concluded between a State and an alien . . . . The principle *pacta sunt servanda* . . . enables a State to resist the nonperformance of conventional obligations assumed by another State in favor of its nationals . . . ."[25]

The French Government approached the question of the breach of the contractual relation in a similar way in the present World Court in the case of *Certain Norwegian Loans.*[26] In its view, the bonds involved were of the nature of "international loans."[27] The Court also contended that "a domestic law cannot modify the substance of *international contracts* agreed to by a State."[28] In neither of the two cases did the Court have to pronounce itself on the merits. Apparently, no other State has endorsed the Swiss-French doctrine.

II. Responsibility in the Case of Modern Concession Agreements

A. *The Law Governing Modern Concession Agreements*

After the above-mentioned dictum of the World Court, the "choice-of-law" principle was no longer confined to municipal legal orders. The practice of inserting in State contracts a new type of choice-of-law (as well as choice-of-forum) clause, which was initiated in the mid-1920s, progressively developed up to the present time. Such practice is reflected in the resolutions adopted by the *Institut de Droit International* at its Athens session.[29] According to pertinent provisions

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23. Mémoire Pour le Gouvernement de la Confédération Suisse (Switz. v. Yugo.), 1936 P.C.I.J. (ser. C) No. 78, at 10 (Jan. 7).

24. *Id.* at 32.

25. *Id.*

26. (Fr. v. Nor.), 1957 I.C.J. 9, 15 (July 6).

27. *Id.*

28. Reply of the Government of the French Republic (Fr. v. Nor.), 1957 I.C.J. Pleadings (Certain Norwegian Loans) 381, 404 (July 6, 1955) (emphasis added).

29. Georges Van Hecke, *Agreements Between a State and a Foreign Private Person*, 57-I Annuaire de l'Institute de Droit International [A.I.D.I.] 192 (1977).

of the resolution, "[t]he parties may in particular choose as the proper law of the contract either one or several domestic legal systems, or the principles common to such systems, or the general principles of law, or the principles applied in international economic relations, or international law, or a combination of these sources."[30] The new type of clauses are not to be found in the traditional, ordinary state contracts, but in the so-called "economic development agreements," that are in the modern concession agreements concluded between states and foreign enterprises.[31]

One of the earliest clauses of the new type is found in the 1933 concession granted to the Anglo-Persian Oil Company by the then Persian government.[32] Under Article 22 of the Agreement, differences between the parties would be settled by arbitration, and the award would "be based on the juridical principles contained in Article 38 of the Statutes of the Permanent Court of International Justice."[33] The clauses later became more explicit. For instance, under the pertinent provisions of the 1954 Consortium Agreement concluded between the Government of Iran and several foreign companies of different nationalities, the agreement was to be governed;

> in accordance with principles of law common to Iran and the several nations in which the other parties to this Agreement are incorporated, and in the absence of such common principles, then by and in accordance with principles of law recognized by civilized nations in general, including such of those principles as may have been applied by international tribunals.[34]

In some concession agreements, "international law" as a whole is included as part of the applicable law. In 1966, the foreign oil companies operating in Libya agreed to amend the concessions in force following approval of new Libyan oil legislation.[35] The standard arbitration clause (Clause 28, paragraph 7, of the Deeds of Conces-

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30. *Id.* at 195.

31. For the salient features of the current modern contractual relationships, see A.O. Adede, *A Profile of Trends in the State Contracts for Natural Resources Development Between African Countries and Foreign Companies*, 12 N.Y.U. J. INT'L L. & POL. 479, 494-517 (1980). For the features of early modern concession agreements, see Lord McNair, *The General Principles of Law Recognized by Civilized Nations*, 1957 BRIT. Y.B. INT'L L. 1.

32. J.C. HUREWITZ, 2 DIPLOMACY IN THE NEAR AND MIDDLE EAST 188 (1956).

33. *Id.* at 195.

34. *Id.* at 377. This clause served as a model for corresponding stipulations in other investment agreements subsequently concluded by the governments of Kuwait, Egypt and Indonesia. *See* JUHA KUUSI, THE HOST STATE AND THE TRANSNATIONAL CORPORATION, AN ANALYSIS OF LEGAL RELATIONSHIPS 68 (1979).

35. KUUSI, *supra* note 34, at 188.

sion) now included applicable law principles common to Libya and international law, and in the absence of such common principles, "the general principles of law, including such of those principles as may have been applied by international tribunals."[36]

A different form of the choice-of-law clauses under consideration is found in Article 42(1) of the 1965 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, concluded under the auspices of the World Bank.[37] The article provides that the arbitral Tribunal shall decide the dispute in accordance with such rules of law as may be agreed to by the parties, and in the absence of such agreement, "the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable."[38] Still another form is that adopted by the clause of the Arbitration Agreement concluded in 1979 between Kuwait and the American Independent Oil Co. (AMINOIL).[39] Under this clause, the arbitral Tribunal shall determine the law governing the substantive issues between the parties, "having regard to the quality of the parties, the transnational character of their relationships and the principles of law and practice prevailing in the modern world."[40]

B. The International Validity of Modern Concession Agreements

By virtue of the choice-of-law clauses contained in modern concession agreements, the contractual relationship entered into by a State and a foreign private person is removed, wholly or in part, from the domestic law of the contracting State, and is subject to a different and

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36. OPEC, *Model Agreement for Amendment of Petroleum Concessions in Libya*, *in* SELECTED DOCUMENTS OF THE INTERNATIONAL PETROLEUM INDUSTRY 1966, at 198. Out of a total of 23 contracts published by OPEC in 1966-68, nine contained choice-of-law or arbitration clauses referring to the general principles of law and to international law. Such clauses, identical or similar to those developed in the post-war period, have appeared in concession agreements concluded with Abu Dhabi, Iran, Iraq, Kuwait, and Libya. *See* KUUSI, *supra* note 34, at 140 and nn.95-99, where full information is offered as to the documentary sources. Stipulations of similar tenor are found in agreements entered into by Tunisia and the former Republic of Vietnam, among other developing countries. *Id.* at 68-69. *See also* G.R. Delaume, *Des Stipulations de Droit Applicables dans les Accords de Pret et de Dévelopement Économique et de Leur Role*, 4 REVUE BELGE DE DROIT INTERNATIONAL [R. BELG. D. INT'L] 336 (1968).

37. Aron Broches, *The Convention on the Settlement of Investment Disputes Between States and Nationals of Other States*, 1972-II R.C.A.D.I. 331, 392 (1973).

38. *Id.* at 391. This article contains a comment on the scope and purpose of the provision.

39. Matter of an Arbitration Between the Government of Kuwait and the American Independent Oil Co. (AMINOIL), 21 I.L.M. 976 (1982).

40. *Id.* at 980.

hierarchically higher legal order which may be either the general principles of law or international law as a whole. This proposition can be sustained in light of arbitral precedents.[41] Hence, the generally accepted view is that these clauses, in contrast to traditional ones, have the effect of "internationalizing" or "delocalizing" the contractual relationship.[42] Being so, the concession agreement has an international validity, which means in turn that obligations stipulated therein also partake the nature of international obligations.

What is the rationale, the basis of the international character and validity of the modern concession agreements and of the obligations stipulated therein? The rationale is the mutual consent of the contracting parties, that is, the universal and well-established principle of the autonomy of the will of the parties to a contract. As Professor Dupuy, the Sole Arbitrator in the *TOPCO* case has observed, contractual practice tends more and more to "de-localize" the contract, or if one prefers, to sever the automatic connections to some municipal law; so much so that today when municipal law governs the contract it is because the parties have agreed to it and no longer by a privilege, but by a mechanical application of the municipal law.[43] Under the pressures of the needs of international trade, the principle of the autonomy of the parties appears today to be so much more significant than at the end of the 1920s, when the *Serbian* and *Brazilian Loans* judgments were rendered.[44] In short, it is with the intention of the contracting parties — the State and the foreign individual or corporation — where

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41. *See* Société Rialet et le Gouvernment éthiopen, 8 Trib. Arb. Mixtes 74 (1929); Petroleum Development Ltd. v. Sheikh of Abu Dhabi, 18 I.L.R. 144 (1951); Ruler of Qatar v. International Marine Oil Co. Ltd., 20 I.L.R. 534 (1953); Saudi Arabia v. Arabian American Oil Co. (ARAMCO), 27 I.L.R. 117 (1963); Sapphire International Petroleum Ltd. v. National Iranian Oil Co., 35 I.L.R. 136 (1963); B.P. Exploration Co. (Libya) Ltd. v. Government of Libyan Arab Republic, 53 I.L.R. 297 (1973-74); Dispute Between Texaco Overseas Petroleum Company/California Asiatic Oil Company and the Government of the Libyan Republic, 17 I.L.M. 3 (1978); Dispute Between Libyan American Oil Co. (LIAMCO) and the Government of the Libyan Arab Republic, 20 I.L.M. 1 (1977); Matter of an Arbitration Between the Government of The State of Kuwait and the American Independent Oil Co. (AMINOIL), 21 I.L.M. 976 (1982). For a list of the 24 arbitrations under Article 42(1) of the World Bank Convention, and basic information thereon, see ICSID (W. Bank) Cases 1972-1987, ICSID/16/Rev.1 (July 1987).

42. *See* F.A. Mann, *The Law Governing State Contracts*, 1944 BRIT. Y.B. INT'L L. 11; Georg Schwarzenberger, *The Protection of British Property Abroad*, 5 CURRENT LEGAL PROBS. 295, 315 (George W. Keeton & Georg Schwarzenberger eds., 1952); Prosper Weil, *Problémes Relatifs aux Contrats Passés Entre un État et un Particulier*, 1969-III R.C.A.D.I. 95, 189-204. As to the inapplicability of *les voluntatius* to State development contracts, see Tang An, *The Law Applicable to a Transnational Economic Development Contract*, 21 No. 4 J. WORLD TRADE L. 95, 112 (1987).

43. Dispute Between Texas Overseas Petroleum Company/California Asiatic Oil Co. and the Government of the Libyan Republic, 17 I.L.M. 3, 12-13, para. 29 (1978).

44. *See id.*

the basis of the "internalization" or "de-localization" of the contractual relation, or aspects thereof, is to be found.[45]

That the "international" character and validity of modern concession agreements stem from the will of the contracting parties is shown in most of the other arbitrations. Where the clause was so explicit as, for example, in Article 46 of the 1954 Iran-Consortium Agreement, the arbitrators just applied the law as defined by the parties.[46] Wherever the stipulation was rather vague and imprecise, they applied the legal system which, in their view, conformed better with the presumed intention of the parties. In the *Petroleum Development Ltd. v. Sheikh of Abu Dhabi*[47] case, for instance, the Arbitrator stated that in applying "a sort of modern law of nature," he did not think that "there is any conflict between the parties."[48] More significant is the role attributed to the intention of the parties when there were no choice-of-law clauses at all, as in the *Société Rialet*, the *Ruler of Qatar* and the *Electricity Companies* cases.[49]

In situations such as those present in the last three cases, however, the intention of the parties cannot be presumed. When a waiver of domestic law is involved, the presence of a choice-of-law clause is required, either expressly making a non-municipal legal system applicable, or allowing to assume, beyond any doubt, that such a choice was the intention of both parties.

The question has been raised as to the legal capacity of the contracting parties, and in particular, the foreign individual or corporation, to "internationalize" the relationship. In this respect, one must first take into consideration that arbitrators are apparently never concerned about the character of the parties and their capacity to "delocalize" the agreement. The question of legal capacity has been raised in some scholarly writings,[50] and also by international forums in developing countries.[51]

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45. Even the World Court admitted in one of the judgments mentioned above that "it may also take into account the expressed or presumed intention of the Parties." *Serbian Loans*, 1929 P.C.I.J. (ser. A) No. 20-21, at 41 (July 12).

46. *See* HUREWITZ, *supra* note 32, at 377.

47. 18 I.L.R. 144 (1951).

48. *Id.* at 149.

49. For the pertinent passages of the three awards, see F.V. GARCIA-AMADOR, 1 THE CHANGING LAW OF INTERNATIONAL CLAIMS 369 (1984).

50. The basic argument is that individuals and private corporations, not being capable of possessing rights and obligations directly under international law, lack the capacity to choose the latter or any other non-municipal system as the law governing their contractual relationship with a sovereign State. *See* KUUSI, *supra* note 34, at 88-92 (discussing the competing views taken with regard to this argument, by A.P. Sereni, Giovanni Kojanec and Georges Abi-Saab).

51. Concerning the Third World position, as taken in international fora, see F.V. GARCIA-AMADOR, THE EMERGING INTERNATIONAL LAW OF DEVELOPMENT, A NEW DIMENSION OF INTERNATIONAL ECONOMIC LAW 172-73 (1990).

Arguments, however, supporting the viability under contemporary international law of both the choice-of-law and choice-of-forum clauses abound and seem far more persuasive. Thus, to Schwarzenberg, "[a] head of State or government has discretionary power to recognize an entity as an international person and to enter into relations with it on the basis of international law. If international law is declared to be the law applicable to a concession, the situation is somewhat similar."[52] In his view, it would appear inappropriate, not to say unrealistic, in light of the emergence of new rules of commercial and administrative international law, to deny the parties the right to select, among the legal systems with which the transaction is connected, that particular one which they consider is most suited to give to the transaction its proper legal setting.[53]

So far as the capacity of the private person is concerned, it cannot be argued, on the basis of the traditional orthodox position, that because private persons are not subjects of international law, their agreements with foreign States may never become internationally valid. In the matter of contractual relations, like in other fields, the international personality and the capacity of individuals to acquire rights or obligations simply cannot be questioned any longer. In the particular area of contractual relations between States and foreigners, the international personality and capacity of the foreigners will depend on the extent the State recognizes such personality and capacity. Agreements providing for the application of a non-municipal legal system, or for the settlement of disputes by international means, differ from those governed exclusively by municipal law in that the contractual relation between the State and the private person is raised to an international level, thus necessarily conferring upon that person a degree of personality and capacity sufficient to make the agreements internationally valid.[54]

C. *Applicability of Clausula Pacta Sunt Servanda*

Given the different character of the contractual relationships between States and foreign individuals or corporations, is the traditional

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52. Schwarzenberger, *supra* note 42, at 315.

53. *Id.*

54. In connection with the debate on the question of whether the individual may be considered as a "subject" of international law, it is worth noting the following remark by I. Seidl-Hohenveldern: "[t]he private partner is recognized as a subject of only those rights and duties, as are embodied in the contracts concerned." Ignaz Seidl-Hohenveldern, *The Theory of Quasi-International and Partly International Agreements*, 11 R. BELG. D. INT'L 567, 570 (1975). In the same sense it has been said that "the mere fact that the parties by agreement make their contract to be governed by international law does not make the private entity concerned a *subject* of international law. It merely subjects the *contract* to that law." CHRIS N. OKEKE, CONTROVERSIAL SUBJECTS OF CONTEMPORARY INTERNATIONAL LAW 214 (1974) (emphasis in original).

position regarding the origin of State responsibility for the breach of contractual obligations still valid? To state it more explicitly, given the stipulations of modern concession agreements concerning the law applicable, is responsibility still not incurred by the mere breach of the obligations contained in an agreement? As one may recall, the rationale of the traditional position is that the State can exercise its sovereign rights to alter or repudiate altogether its contractual obligations since the relationship is governed by the state's municipal law. In the case of modern concession agreements, however, this legal situation no longer exists due to the stipulation removing the contractual relationship from the municipal legal order.

Now, given that different legal situation, can state sovereignty over acquired rights still be invoked? Or rather, given the new situation, is *clausula pacta sunt servanda* not applicable? No doubt that the traditional position must be approached in light of modern juridical developments. It is evident that said position was taken with regard to ordinary State contracts, and having in mind the law governing such contractual relationships. Therefore, given the different character of modern concession agreements, and of the obligations contained therein, it is only natural that the traditional position is no longer the only correct approach to State responsibility in this area. It continues to be the correct one so far as the ordinary contractual relationships are concerned. Being exclusively governed by the municipal law of the contracting State, the mere breach will not engage the latter's international responsibility; the concurrence of a denial of justice, or of any other wrongful or arbitrary state conduct, must still be required.

The situation, however, is altogether different in so far as those contractual relationships which are governed, wholly or in part, by the general principles of law, or international law as a whole, that is, by a non-municipal legal system. The non-municipal legal order governing the modern concession agreements "internationalizes" the contractual relationship, and therefore, the obligations contained therein. There is no need to dwell any further on the rationale of the "international" character and the validity of these agreements. It only remains to be seen why the traditional approach to the question of State responsibility is no longer the only proper one.

The answer is clearly implied in the nature of the obligations contained in the new type of contractual relationship which is agreed to between the State and the foreign private person. Given the "international" character of such a relationship, *clausula pacta sunt servanda*, as a principle of international law, becomes applicable. Accordingly, State responsibility is entailed on account of the mere breach of the

obligation involved. As in the case of treaty obligations, no additional act or omission is required.

The scope of this analogy, however, must not be misunderstood. To say that the "mere" breach of contractual obligations suffices, as in the case of a breach of treaty obligations, to give rise to State responsibility, does not necessarily mean a total assimilation of the two kinds of obligations. It only means that the breach of obligations emanating from an "internationalized" contractual relationship creates a legal situation similar to that created by the breach of any of the international obligations of the State regarding the treatment of aliens, including its treaty obligations in this regard. This view is clearly reflected in international jurisprudence. Actually, a glance at the aforementioned arbitrations involving choice-of-law clauses will show that no denial of justice or any other act or omission contrary to international law was required to hold the State responsible. Thus, the "mere" breach of the contractual obligations was considered the only sufficient ground to establish international responsibility.

As will be noted, in contrast to the Swiss-French doctrine, the above approach to State responsibility for the breach of contractual obligations does not pose a new challenge to the traditional position. While under said doctrine *clausula pacta sunt servanda* would be applicable to the breach of obligations emanating from ordinary State contracts, under the new approach, the applicability of the *clausula* is confined to the case of those modern concession agreements where contractual obligations of an "international" character are involved. There is not a new attempt, therefore, to revise the traditional position, much less to repudiate it. The idea is strictly limited to approaching the traditional position in light of those legal developments that had not yet taken place at the time said position evolved.[55]

III. Responsibility in the Case of Stabilization Clauses

A. Position of Legal Professional Associations and Institutions

Associations of the legal profession were, perhaps, the first to debate systematically the international validity of the stabilization clauses. In accordance with a resolution proposed in committee during

55. This author's proposals to the International Law Commission on State responsibility for the breach of contractual obligations were based on the foregoing considerations. *See* F.V. Garcia-Amador, *International Responsibility: Fourth Report*, [1959] 2 Y.B. Int'l L. Comm'n 1, 29, U.N. Doc. A/CN.4/119. *See also* F.V. Garcia-Amador, *International Responsibility: Sixth Report*, [1961] 2 Y.B. Int'l L. Comm'n 1, 47, art. 10, U.N. Doc. A/CN.4/134/Add.1.

the Cologne Conference of the International Bar Association in 1958, "[i]nternational law recognizes that the principle of *pacta sunt servanda* applies to the specific engagements of States towards other States or the nationals of other States and that, in consequence, a taking of private property in violation of a specific state contract is contrary to international law."[56]

The same position was taken in some of the replies to the questionnaire prepared for the Forty-Eighth Conference of the International Law Association. In its reply, for example, the American Branch stated that "the contractual obligations freely assumed by a State [toward aliens] are no less binding than its treaty obligations."[57] Other replies received by the Association's International Committee on Nationalization drew the same analogy and maintained that the principle *pacta sunt servanda* must be applied without reservations; they therefore deny categorically to the State any right to end a concession or contract before the expiration of its term.[58] In the resolution adopted on the subject, the Conference of the International Law Association declared that:

> [t]he principles of international law establishing the sanctity of a State's undertakings and respect for the acquired rights of aliens require . . . (ii) that the parties to a contract between a State and an alien are bound to perform their undertakings in good faith. Failure of performance by either party will subject the party in default to appropriate remedies.[59]

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56. *Proposed Resolution of the Open Committee Meeting*, International Bar Association Conference, Cologne 1 (1958). The problem has already been considered by the Association in the past. On that occasion, the same view was advanced by Franz M. Joseph, *International Aspects of Nationalization, an Outline*, International Bar Association Conference, Monte Carlo 2 (1954). Concerning other aspects of the breach of contractual obligations it has been said that the presence of an undertaking not to expropriate imposes a "higher obligation," the non-observance of which creates a liability not only to pay compensation for the expropriated property or undertaking but also to indemnify the alien for all the damage and loss which he has sustained. Sir Hartley Shawcross, *Some Problems of Nationalisation in International Law*, International Bar Association Conference, Monte Carlo 14, 17-18 (1954).

57. Report of the Committee on Nationalization, *in* PROCEEDINGS AND COMMITTEE REPORTS OF THE AMERICAN BRANCH OF THE INTERNATIONAL LAW ASSOCIATION 68 (1957-58).

58. The replies of Prof. Gihl and Dr. Weiss-Tessbach can be found in INTERNATIONAL LAW ASSOCIATION, REPORT OF THE FORTY-EIGHTH CONFERENCE HELD AT NEW YORK 192, para. 31 (1959).

59. See the full text of the resolution adopted by the Conference, *in* INTERNATIONAL LAW ASSOCIATION, REPORT OF THE FORTY-EIGHTH CONFERENCE HELD AT NEW YORK XI (1959). In this sense, it has been argued that, "[s]ince states are equally obliged . . . to exercise good faith in their relations with aliens, it follows that they are bound by the contractual agreements they enter into with aliens . . . although such agreements are not *stricto sensu* international agreements." Michael Brandon, *Legal Aspects of Private Foreign Investments*, 18 FED. B.J. 298, 338-39 (1958).

The International Law Association eventually took a new position. Reference is made to the Conference held in Seoul in 1986. This time the subject was dealt with in connection with the legal aspects of the proposed new international economic order. While endorsing the view that "[p]ermanent sovereignty over natural resources, economic activities, and wealth," (as a principle of international law emanating from the principle of self-determination) is "inalienable,"[60] the Conference agreed that "[a] State may, however, accept obligations with regard to the exercise of such sovereignty, by treaty or by contract, freely entered into."[61] Moreover, in connection with the conditions for the exercise of the right of nationalization, expropriation, etc., the Conference expressly mentioned the "legal effects flowing from any contractual undertaking."[62]

The experience of the *Institut de Droit International* is even more interesting for the purpose of this Article. In the draft resolution presented by M.A. de La Pradelle in 1950, there was the following provision declaring "[n]ationalization, a unilateral act of sovereignty, shall respect obligations validly entered into, whether by treaty or by contract."[63] At its Siena session, the Institut rejected the proposal that the State should be bound to respect (express or tacit) commitments not to nationalize entered into either with another State or with alien private individuals.[64] The Institut returned to the topic two decades and a half later in its Oslo session with a report and a draft resolution presented by G. van Hecke.[65] In accordance with one of the whereas of the latter, "in case of a contract between a State and an alien, the rules of private international law allow the parties, if such is their will, to remove the contract from any municipal law and incorporate, by reference, the general principles of law, or to international law."[66] Under one of the operative provisions of the draft, the parties were authorized, by an express stipulation, to "[s]ubject their contract ei-

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60. *Declaration on the Progressive Development of Principles of Public International Law Relating to a New International Economic Order, in* INTERNATIONAL LAW ASSOCIATION, REPORT OF THE SIXTY-SECOND CONFERENCE HELD AT SEOUL 2, 6-7, paras. 5.1, 5.2 (1987).

61. *Id.* at para. 5.2.

62. *Id.* at 7, para. 5.5.

63. M.A. de La Pradelle, *Les Effets Internationaux des Nationalisations*, 43-I A.I.D.I. 42, 68 (1950).

64. The proposal was rejected by 20 votes to 16, with 22 abstentions. 44-I A.I.D.I. 318 (1952). A proposal covering only commitments entered into by a State *vis-a-vis* another was, on the contrary, overwhelmingly adopted. *Id.* at 317.

65. 57-I A.I.D.I. 204 (1977).

66. *Id.* For the full text of van Hecke's report, see *id.* at 192-203. For written observations by members see *id.* at 209.

ther to a municipal law, or to the general principles of law as principles of international law."[67]

The matter was thoroughly debated by the members of the Institut, and a resolution was eventually adopted to the above-mentioned provision in the Athens session.[68] According to Article 6 of the resolution, the law governing the contract should determine "the incidence of contractual liability between the parties, in particular, those raised by the State exercise of its sovereign powers in violation of any of its commitments toward the contracting partner."[69] In light of the discussion that took place at the Institut on this point, it may be safely assumed that this last provision was intended to cover stabilization clauses.[70]

B. Arbitrations Involving Stabilization Clauses: Early Arbitrations

The case of *Lena Goldfields, Ltd. v. U.S.S.R* (1930)[71] is the first arbitration involving both a choice-of-law clause and a stabilization clause. Under the former, "the parties base[d] their relations with regard to this agreement on the principle of goodwill and good faith, as well as on reasonable interpretation of the terms of the Agreement."[72] In addition, the 1925 Concession Agreement between Lena Goldfields and the Soviet Union contained a provision in Article 76, under which the Soviet Government undertook not to make any alteration in the agreement by Order, Decree, or other unilateral act, or at all except with Lena's consent.[73] As construed by the Court of Arbitration, the purpose of this provision was "to protect Lena's legal position — i.e., to prevent the mutual rights and obligations of the parties under the contract being altered by any act of Government, legislative, executive, or fiscal, or by any action of local authorities or trade unions."[74]

With regard to the applicable law, the counsel for *Lena* made the distinction that on all domestic matters not excluded by the contract, including its performance by both parties inside the U.S.S.R., Russian law was the proper law of the contract, but that for other purposes, the proper law was contained in the general principles of law, such as

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67. *Id.* at 205.

68. 58-II A.I.D.I. 42 (1979).

69. *Id.* at 44.

70. For final discussion of those aspects of the draft resolution more directly related with the matter under consideration, see *id.* at 42-44, 72-73, 99-100. The resolution was adopted by the overwhelming majority of 38 votes, 4 against, and 13 abstentions. *Id.* at 103.

71. The full text of the award is reprinted in Arthur Nussbaum, *The Arbitration Between the Lena Goldfields Ltd. and the Soviet Government*, 36 CORNELL L.Q. 31 app. (1950-51).

72. *Id.*

73. *Id.* at 46.

74. *Id.*

those recognized by Article 38 of the Statute of the Permanent Court of International Justice, because, among other reasons, many of the terms of the contract contemplated the application of international, rather than merely national, principles of law.[75] In dealing with the question of compensation, the Court stated that it preferred to base its award on the principle of "unjust enrichment," as a general principle of law recognized by civilized nations.[76] The Court, however, did not elaborate with regard to relevance of the aforementioned Article 76, the stabilization clause of the concession agreement.

The next case involving a stabilization clause is *Sapphire International Petroleum Ltd. v. National Iranian Oil Company*.[77] Apparently, since the 1925 *Lena* concession agreement, none of the subsequent concessions up to 1958 (the year of the agreement between Sapphire and the Iranian Co., an organ of the State of Iran) contained stabilization clauses. The 1958 Iranian concession contained a choice-of-law clause similar to that of *Lena's*: "the parties undertake to carry out the provisions of the contract in accordance with the principles of good faith and goodwill and to respect the spirit as well as the letter of the agreement."[78] The stabilization clause stated:

> [n]o general or special statutory enactment, no administrative measure or decree of any kind, made either by the Government or by any governmental authority in Iran (central or local), including NIOC, can cancel the agreement or affect or change its provisions, or prevent or hinder its performance. No cancellation, amendment or modification can take place except with the agreement of the two parties.[79]

How did the Sole Arbitrator (M. Pierre Cavin, a Swiss Federal Judge) construe the provision of the agreement concerning the applicable law? First, he noted that the agreement contained "no express choice of law."[80] Notwithstanding that it had been concluded in Iran, and that it was to be performed for the most part also in Iran, he considered that these two important connecting factors were "not necessarily decisive."[81] In his view, the dimensions of the concession created rights which were "not merely 'contractual'."[82] Hence, the

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75. *Id.* at 36.
76. *Id.*
77. The full text of the award is reprinted in 35 I.L.R. 136 (1967).
78. *Id.* at 140.
79. *Id.*
80. *Id.* at 171.
81. *Id.*
82. *Id.*

particular character of the agreement laid partly in public law and partly in private law. Also, the legal security that the investments, responsibilities, and considerable risks of the foreign company required, "could not be guaranteed . . . by the outright application of Iranian law, which . . . is within the power of the Iranian State to change."[83] In addition, the Sole Arbitrator viewed the clause contained in the aforementioned paragraph 1 of Article 38 as "scarcely compatible with the strict application of the internal law of a particular country."[84] In this connection he cited the holdings in the *Lena Goldfields Arbitration* and the *Petroleum Development Ltd. v. Ruler of Abu Dhabi* cases.[85]

Unfortunately, the Sole Arbitrator did not consider it necessary to comment on paragraph 3 of Article 38, the stabilization clause of the concession agreement. Most likely, the reason was that the alleged violations of the agreement did not involve any specific violation of the obligations stipulated in said paragraph. In any event, some of the above reasonings of the Arbitrator show a clear bearing upon the provisions of the paragraph. In effect, the very aim of these provisions was to prevent the State of Iran from taking measures that would affect the terms of the agreement or hinder its performance by invoking its sovereign powers.

C. *Awards Concerned with Clause 16 of the Libyan Concessions*

The Libyan nationalization measures of the early 1970s gave rise to three arbitrations, the first of which was *BP Exploration Company (Libya) Ltd. v. Government of the Libyan Arab Republic*.[86] The concession involved in this arbitration, like those involved in the other two, were governed by the legal principles set forth in the above-cited Clause 28, paragraph 7 of the Deeds of Concession. In addition, the latter contained a stabilization clause, Clause 16, the text of which reads as follows:

> 1. The Government of Libya will take all the steps necessary to ensure that the Company enjoys all the rights conferred by this Concession. The contractual rights expressly created by this concession shall not be altered except by mutual consent of the parties.
> 2. This Concession shall throughout the period of its validity be construed in accordance with the Petroleum Law and the

83. *Id.*
84. *Id.* at 173.
85. *Id.* at 171-73.
86. The full text of the award is reprinted in 53 I.L.R. 297 (1973-74).

> Regulations in force on the date of execution of the agreement of amendment by which this paragraph 2 was incorporated into this concession agreement. Any amendment to or repeal of such Regulations shall not affect the contractual rights of the Company without its consent.[87]

Regarding the choice-of-law clause, Judge Gunnar Lagergren, the Sole Arbitrator, held that "[w]hile the provision generates practical difficulties in its implementation, it offers guidance in a negative sense by excluding the relevance of any single municipal legal system as such."[88] In response to the Claimant's argument that "international law alone is applicable,"[89] he further held that the conduct of the contracting State "in the last analysis should be tested by reference to the general principles of law."[90] To him, "[t]he governing system of law is what that clause expressly provides, *viz.*, in the absence of principles common to the law of Libya and international law, the general principles of law, including such of those principles as may have been applied by international tribunals."[91] As will be seen, the arbitrator in the *LIAMCO* case does not seem to have shared this interpretation of Clause 28.

With regard to the "breach of contract," the Sole Arbitrator thought that elaborate reasons were not required. He held, however, that:

> [t]he BP Nationalization Law, and the actions taken thereunder by the Respondent, do constitute a fundamental breach of the BP Concession as they amount to a total repudiation of the agreement and the obligations of the Respondent thereunder, and, on the basis of rules of applicable systems of law too elementary and voluminous to require or permit citation, the Tribunal so holds. Further, the taking by the Respondent of the property, rights and interests of the Claimant clearly violates public international law as it was made for purely extraneous political reasons and was arbitrary and discriminatory in character. Nearly two years have now passed since the nationalization, and the fact that no offer of compensation has been made indicates that the taking was also confiscatory.[92]

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87. *Id.* at 322.
88. *Id.* at 327.
89. *Id.*
90. *Id.* at 328.
91. *Id.* at 329.
92. *Id.* at 329.

Curiously enough, no express reference is made to Clause 16, either in the above passage of the award, or in any of its final decisions.[93] In addition, the assertion that the nationalization acts constituted a fundamental breach of the concession and amounted to a total repudiation of the agreement and the obligations of the Respondent, may have indirectly or impliedly covered the specific obligations under the stabilization clause. The fact is, however, that no separate mention was made to the breach of such specific obligations. Does it mean that in the view of the Sole Arbitrator the presence of such a clause in concession agreements is not particularly relevant? Half of the above quoted paragraph sets forth the different reasons why the taking of the property, rights, and interests of the Claimant were in clear violation of international law. In addition, a surprising fact is that more than two-thirds of the award is concerned with the "effect of the breach," especially with the question of whether specific performance and *restitutio in integrum* were — as the Claimant claimed — the appropriate remedies.[94] As is well known, the Sole Arbitrator rightly decided to recognize only the right to claim damages.[95]

The second arbitration concerned with Clause 16 of the Libyan concessions was the *Texaco Overseas Petroleum Company/California Asiatic Oil Company and the Government of the Libyan Arab Republic (TOPCO)*.[96] In contrast to the arbitrator in the preceding case, Professor R. J. Dupuy, the Sole Arbitrator in *TOPCO*, examined the nature and implications of the stabilization clause. First, in his view the provisions of Clause 16 did not impair, in principle, the sovereignty of the Libyan State, since all its sovereign legislative and regulatory powers are preserved, and can be exercised in the field of oil activities with respect to national or foreign persons with whom the state has not undertaken the obligation contained in the clause.[97] In addition, Libya had undertaken commitments under an international agreement, which is the law common to the parties, through the exercise of its sovereignty.[98] The foregoing reasoning led the Sole Arbitrator to conclude:

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93. The pertinent passage in the decision simply states that "[t]he BP Nationalisation Law and the subsequent implementation thereof were each a breach of the obligations of the [Libyan Government] owed to the Claimant under the [Concession Agreement]." *Id.* at 355.

94. *Id.* at 329-355.

95. *Id.* at 355-57.

96. 17 I.L.M. 3 (1978).

97. *Id.* at 24-25, para. 71.

98. *Id.*

> the recognition by international law of the right to nationalize is not sufficient ground to empower a State to disregard its commitments, because the same law also recognizes the power of a State to commit itself internationally, especially by accepting the inclusion of stabilization clauses in a contract entered into with a foreign private party.[99]

Next, the Arbitrator considered whether the theory of the *contrat administratif* might be invoked to justify nationalization measures.[100] In this respect, he first distinguished between public service concessions and oil concessions. To him, in regard to the former, the State had "prerogatives which go beyond the ambit of ordinary law, which enable the public authority to alter or abrogate unilaterally a given contract."[101] The oil concessions, however, while remaining in the nature of acts governed by public law, have a contractual character which is better designed to afford to operators who assume important economic risks, guarantees of greater stability.[102]

Along this line of thought, the Sole Arbitrator held further that nationalization is a measure falling outside the State's prerogatives recognized by the theory of administrative contracts.[103] This theory recognizes the State's power, under certain conditions and subject to certain limitations, to make some alterations, or even to unilaterally terminate a given contract. In his view, nonetheless, such measures could affect only the contract and cannot, in themselves, include acts of expropriation or confiscations affecting private property.[104] The Sole Arbitrator did not elaborate on this distinction.

The Arbitrator, however, did elaborate on the point we are concerned with in this Article, i.e., the international validity of the stabilization clauses, in the present case, Clause 16. In this respect, he arrived at only the following conclusion:

> Thus, in respect of the international law of contracts, a nationalization cannot prevail over an internationalized contract, containing stabilization clauses, entered into between a State and a

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99. *Id.* The argument that international law recognizes the State's "right to commit itself internationally" in its relations with foreign individuals was used before in Radio Corp. of America v. National Government of China, 3 R.I.A.A. 1623, 1627 (1935) and Saudi Arabia v. Arabian American Oil Co. (ARAMCO), 27 I.L.R. 117, 168 (1957), though not with reference to stabilization clauses.

100. 17 I.L.M. at 25 (1978).

101. *Id.*

102. *Id.*

103. *Id.*

104. *Id.*

> foreign private company. The situation could be different only if one were to conclude that the exercise by a State of its right to nationalize places that State on a level outside of and superior to the contract and also to the international legal order itself, and constitutes an 'act of government' (*'acte de gouvernement'*) which is beyond the scope of any judicial redress or any criticism.[105]

The first sentence of the above paragraph raises an important question: Can a nationalization measure prevail over an internationalized contract, if the latter does not contain a stabilization clause? To state it more explicitly, assuming that "internationalization" of the contractual relationship is obtained through a choice-of-law clause that removes the contractual relationship from the domestic legal order, is not the presence of such a clause sufficient to bar any State act in violation of its contractual obligations? Likewise, the second sentence, in a sense, raises the same question. Here the Sole Arbitrator seems to have envisaged an "international legal order." Now, is it his view that such higher legal order is generated, again, by the presence of the stabilization clause? If so, what would have been the situation in the case of a contractual relationship containing a stabilization clause, but entirely governed by the municipal law of the contracting State?

Dispute Between Libyan American Oil Company (LIAMCO) and the Government of the Libyan Arab Republic[106] was the third arbitration concerned with Clause 16 of the Libyan concessions. Like in the preceding case, the question was raised as to how to interpret paragraph 7 of Clause 28, the choice-of-law clause. In the view of the Arbitrator, the principal and proper law of the contract was Libyan domestic law, but only so far as the principles of this law were common to the principles of international law; hence, any part of the Libyan law which was in conflict with said principles was excluded.[107] To determine the meaning of the principles of international law, he referred to "those of its sources" as set forth in Article 38 of the Statute of the International Court of Justice.[108] Regarding the reference in Clause 28 to the "general principles of law as may have been applied by international tribunals," they "are usually embodied in most legal systems," and "form a compendium of legal precepts and maxims, universally accepted in theory and practice."[109]

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105. *Id.* at 25, para. 73.

106. The full text of the award (which was rendered approximately three months after *TOPCO*) is reprinted in 20 I.L.M. 1 (1977).

107. *Id.* at 35.

108. *Id.*

109. *Id.* at 37.

Turning to the stabilization stipulations contained in Clause 16, the Sole Arbitrator found the clause "justified not only by the said Libyan petroleum legislation, but also by the general principle of the sanctity of contracts recognized also in municipal and international law."[110] He found it "likewise consistent with the principle of non-retroactivity of laws, which denies retrospective effects to a new legislation and asserts the respect of vested rights *droits acquis* acquired under a previous legislation."[111]

The Sole Arbitrator also examined the remedies for premature termination of a contract. In this connection, he was of the view that *LIAMCO*'s concession agreements were "binding." Therefore, they could not validly be terminated except on the ground, *inter alia*, of "[m]utual consent of the contracting parties, in compliance with the said principle of the sanctity of contracts and particularly with the explicit terms of Clause 16 of the Agreements."[112]

Some of the conclusions of the award do not seem to be altogether consistent with the views of the Sole Arbitrator concerning the validity of the stipulations under consideration. Thus, to him, the premature nationalization act, if not discriminatory and not accompanied by a wrongful conduct, was not unlawful as such, and constituted not a tort, but a source of liability to compensate the concessionaire. How is it that the nationalization act was not "unlawful as such," but, rather, an ordinary act of expropriation involving only the duty to pay compensation, considering that the nationalizing State was "bound" by the concession agreements and, in addition, the latter could not be terminated without the consent of the other contracting party? Accordingly, the Arbitrator awarded "indemnification" for the *damnum emergens* sustained by *LIAMCO*, representing the value of the nationalized physical plant and equipment owned by the company. As to the loss of profit (*lucrum cessans*) also claimed by *LIAMCO*, the Arbitrator concluded that it was "just and reasonable to adopt the formula of 'equitable compensation' as a measure for the assessment of damages in the present dispute, with the classical formula of 'prior, adequate and effective compensation' remaining as a maximum and a practical guide for such assessment."[113]

D. AGIP and AMINOIL Awards

The oil products distribution sector in the Congo was nationalized by a law of January 12, 1974. The measure affected all companies

110. *Id.* at 31.
111. *Id.*
112. *Id.* at 62.
113. *Id.* at 86.

involved in the sector, except for AGIP, which, a few days before, had concluded a protocol agreement with the Government for the sale of 50% of the Company's capital.[114] Under the agreement, the Government undertook to "adopt appropriate measures to prevent the application to the Company of future amendments to company law affecting the structure and composition of the Company's bodies."[115] The agreement contained other stabilization clauses in Articles 4 and 11. Besides, Article 15 of the agreement (arbitration clause), provided that the applicable law should be "Congolese law, supplemented . . . by any principle of international law."[116]

The *AGIP Co. v. Popular Republic of the Congo*[117] award was rendered by a tribunal constituted under the World Bank Convention on the Settlement of Investment Disputes Between States and Nationals of other States.[118] With regard to the applicable law, the Government, in its counter-memorial, had proposed that the Tribunal should play the part of a friendly arbitrator.[119] The Tribunal decided that, in light of Article 42 (1) of the Convention, it must make its decision in accordance with the provisions of the applicable law agreed by the parties.[120] In a further passage of the award, the Tribunal interpreted the proviso of the aforementioned Article 15, and noted that "the term 'supplemented' at least means that there can be recourse to the principles of international law either to fill a gap in Congolese law or to supplement it if necessary."[121]

Subsequently, the Tribunal examined the question as to whether the measures taken by the Government affected the "stability of the Company's legal status." On this question, the Tribunal held that "in the light of consistent international practice, positive international law also recognizes that in concluding an international agreement with a private individual the State exercises sovereign powers from the moment that consent is freely given."[122] Then, after citing the commitments entered into by the Government, it declared that the

> unilaterally-decided dissolution which took place under Order No. 6/75 represented a repudiation of these stability clauses [in particular,

114. AGIP Co. v. Popular Republic of the Congo, 21 I.L.M. 726, 727 (1979).
115. *Id.* at 727, para. 18.
116. *Id.*
117. *Id.* at 726.
118. *Id.*
119. *Id.* at 731, para. 44.
120. *Id.* at 731, para. 43.
121. *Id.* at 735, para. 83.
122. *Id.* at 735, para. 81.

> the one contained in the above-mentioned Art. 11], whose applicability results not from the automatic play of the sovereignty of the contracting State but from the common will of the parties expressed at the level of international juridical order.[123]

Like the Sole Arbitrator in *TOPCO*, the Tribunal was of the view that "[t]hese 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 nationals or foreigners, with whom it has not entered into such obligations."[124] It is interesting, also, to note that unlike the Sole Arbitrator in *LIAMCO*, the Tribunal considered that the present case involved "not just an act of nationalization but also a series of repudiations by the Government of its contractual undertakings."[125] Accordingly, it awarded compensation covering both the loss suffered *damnum emergens* and the loss of profits *lucrum cessans*.[126]

In the *Matter of an Arbitration Between the Government of the State of Kuwait and the American Independent Oil Co. (AMINOIL)*,[127] both the applicable law and the stabilization clauses showed different features. As will be recalled, in accordance with Article III (2) of the Arbitration Agreement of June 23, 1979, the applicable law was to be determined by the Tribunal, which would have "regard to the quality of the Parties, the transnational character of their relations and the principles of law and practice prevailing in the modern world."[128] As interpreted by the Tribunal, this choice-of-law clause reserved Kuwait's sovereign rights, "[a]t the same time, by referring to the transnational character of relations with the concessionaire, and to the general principles of law, this Article brings out the wealth and fertility of the set of legal rules that the Tribunal is called upon to apply."[129]

The stabilization clauses were found in Articles 1 and 17 of the 1948 Concession Agreement and in Article 7(g) of the 1961 Supplemental Agreement. The relevant part of Article 1 of 1948 provided for the period of the agreement (60 years), and Article 7(g) of 1961 expressly prohibited termination of the concession before the expiration period.

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123. *Id.* at 735, para. 85.
124. *Id.* at 735-36, para. 86.
125. *Id.* at 737, para. 97.
126. *Id.* at 737, para. 98.
127. The full text of the award rendered by the Arbitration Tribunal is reprinted in 21 I.L.M. 976 (1982). The Tribunal was composed by Professor Paul Reuter (President), Professor Hamed Sultan, and Sir Gerald Fitzmaurice. *Id.*
128. *Id.* at 1000, para. 8.
129. *Id.* at 1001, para. 9.

A more explicit and typical stabilization clause was Article 17 of the original agreement:

> The Shaikh shall not by general or special legislation or by administrative measures or by any other act whatever annul this Agreement except as provided in Article 11. No alteration shall be made in the terms of this Agreement by either the Shaikh or the Company except in the event of the Shaikh and the Company jointly agreeing that it is desirable in the interest of both parties to make certain alterations, deletions or additions to this Agreement.[130]

The crucial issue in the present case was whether the Law Decree No. 124, of September 19, 1977, which declared the 1948 Agreement to be terminated and the property and assets of the Company to be nationalized, constituted a violation of the aforementioned stabilization clauses. In other words, whether these clauses operated to prevent nationalization by a unilateral legislative measure. As it is known, the Tribunal arrived at the conclusion that "the 'take-over' of AMINOIL's enterprise was not, in 1977, inconsistent with the contract of concession, provided always that the nationalization did not possess any confiscatory character."[131]

It is of significance, also, to note that the Tribunal viewed "the stabilization clauses, as being no longer possessed of their former absolute character."[132] In this regard it stressed that the case was not one of a "fundamental change of circumstances *rebus sic stantibus*," but of a change "in the nature of the contract itself, brought about by time, and the acquiescence or conduct of the Parties."[133] Along this line of thought, the Tribunal went as far as to say that

> the Concession had become a contract under the changed régime of which the State had, over the years, acquired a special position that included the right to terminate it, if such a step became necessary for the protection of the public interest, and subject to the payment of adequate compensation."[134]

The soundness of the foregoing propositions is not relevant for our present, specific purposes. It would be, if we were concerned with the question of whether or not the nationalization measures were compat-

130. *Id.* at 1020, para. 88.
131. *Id.* at 1024, para. 102.
132. *Id.* at 1024, para. 100.
133. *Id.* at 1024, para. 101.
134. *Id.* at 1026, para. 113.

ible with the State's obligations of the agreement, including those contained in the stabilization clauses. That is the question Sir G. Fitzmaurice raised in his elaborate separate opinion.[135] We are concerned with only the intrinsic validity of those clauses, and therefore, with the question of whether the Tribunal challenged their validity *in abstracto*. Regarding this point, there is no passage of the award where the Tribunal, either expressly or impliedly, seems to have done it. On the contrary, the very fact that the Tribunal argued, so strongly, the nonapplicability of the clauses, given their changed character, shows that its position would have been different had those circumstances not been present.

In ascertaining the Tribunal's position as to the validity of stabilization clauses *in abstracto*, also worthy of consideration is its holding concerning Kuwait's contention that "permanent sovereignty over natural resources has become an imperative rule of *jus cogens* prohibiting States from affording, by contract or by treaty, guarantees of any kind against the exercise of the public authority in regard to all matters relating to natural riches."[136] In the view of the Tribunal, "[t]his contention lacks all foundation."[137] It held further that the UN General Assembly Resolution 1803 (XVII) did not allow "to deduce the existence of a rule of international law prohibiting a State from undertaking not to proceed to a nationalisation during a limited period of time."[138]

E. Basis of Responsibility for Breach of the Clauses

In light of the above arbitral awards, there is little room for doubts as to the international validity of stabilization clauses. Hence, in case of a breach of such clauses the applicability of *clausula pacta sunt servanda*, as a principle of international law, should not be questioned. Now, what is the rationale of this proposition? The idea is that the validity of the clauses rests on the international character of the concession agreement containing them, either explicitly stated or clearly implied in the awards. The clauses *per se* do not impose international commitments on the contracting State. It is the choice-of-law clause of the agreement which, by "internationalizing" the contractual relationship as a whole, makes those commitments internationally valid.

That is why stabilization clauses inserted in ordinary State contracts lack international validity. The contractual relationship is not re-

135. *Id.* at 1043-53.
136. *Id.* at 1021, para. 90(2).
137. *Id.*
138. *Id.* at 1022, para. 90(2).

moved from the domestic law of the contracting State, thus, these clauses cannot prevent the State from exercising its sovereign powers and affect acquired rights.[139] As stated by the United States Supreme Court, the power of eminent domain cannot be surrendered, but if "contracted away, it may be resumed at will."[140] Therefore, there will be no international responsibility for the mere breach of the clauses under consideration. As in the case of traditional contractual claims, a requirement will be a related act or omission constituting a breach of the State's international obligations, which includes prohibiting the abuse of rights. But if the stabilization clauses are contained in a modern concession agreement governed by a non-municipal legal system, the mere breach of the clauses will give rise to State responsibility. Given the international character and validity of the concession agreement, the sovereign powers which have been "contracted away" now cannot be resumed by the contracting State without the consent of the other party. Hence, what is relevant for the purposes of State responsibility is the nature of the contractual relationship and the law governing it.

The choice-of-law clauses and the modern concession agreements themselves, if compared with the clauses under consideration, are also "stabilization" devices. Actually, both the clauses and the agreements as a whole aim to create a legal situation which precludes changes in the municipal law of the contracting State in violation of the stipulations of the agreement. Hence, the so-called "stabilization" clauses are nothing but express stipulations containing the specific concrete commitment of that State to comply with the terms of the agreement. Such clauses, in the last analysis, are mere expressions of a tacit clause in every contractual relationship.

Stabilization clauses incorporate in concession agreements not only express, but the specific concrete commitment on the part of the contracting State not to change the terms of the contractual relationship without the consent of the other contracting party. This commitment may make a difference from the point of view of international responsibility. The breach of the obligations contained in a stabilization clause may well be viewed as a circumstance aggravating the responsibility of the contracting State. The breach of any of the obligations emanating from the contractual relationship entails responsibility, but when there is a breach of an obligation involving an explicit State's promise to respect the agreement, the breach logically becomes a more

139. *See* Weil, *supra* note 1, at 327-38; Nicolas David, *Les Clauses de Stabilité dans les Contrats Pétroliers. Questions d'un Practicien*, 113 JOURNAL DU DROIT INTERNATIONAL 79, 93 (1986).

140. Georgia v. City of Chattanooga, 264 U.S. 472, 480 (1924).

serious act or omission, entailing a higher degree of responsibility. It is also logical to think that the higher degree of responsibility will affect the measure of reparation.