

in the partnership agreement in certain limited areas.

The Joint Venture practice has up to the present been limited, although negotiations are afoot to expand it considerably. One cannot foresee whether East and West will be brought together through economic cooperation, but if this happens it may prove what some Americans have predicted, namely that from economic cooperation may come a lessening of Soviet suspicion of the West and a willingness to terminate the tensions caused by continuing class struggle attitudes on the Soviet side.

In conclusion, it seems evident that Gorbachev has wielded a new broom in Soviet domestic and foreign policy. Yet, it can be seen that he is a broom wielder and not an architect of a new structure which will not resemble the old. The Communist Party remains; state enterprises and economic planning predominate. Yet, there is an opening to the citizen to blow the whistle on bad management, corruption, and bureaucratic excesses. Further the citizen may indicate choice of representatives in state organs, although not to the point of creating a second political party. Courts are admonished to provide "justice" and not to listen to the dictate of Party Secretaries. The level of international tension is being reduced, and foreign capital is being invited to revitalize production.

In short, there has been change of a startling nature for those who have followed Soviet developments over decades, but the system remains recognizable. As a Soviet law professor told me a short time ago, "You will not have to restructure your books about the Soviet political and legal system. They will only require updating."

## THE NEW MULTILATERAL INVESTMENT GUARANTEE AGENCY GLOBALIZING THE INVESTMENT INSURANCE APPROACH TOWARDS DEVELOPMENT

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The status and protection of investment abroad are central and perennial, but ever-changing themes of International Economic Law.

George Schwarzenberger, *Foreign Investments And International Law VII* (1969)

#### A. INTRODUCTION

On April 12, 1988<sup>1</sup> the United States and the United Kingdom ratified the Convention Establishing the Multilateral Investment Guarantee Agency (MIGA).<sup>2</sup> With these, the last ratifications required,<sup>3</sup> the Convention entered into force, two and a half years after it was opened for signature at the World Bank's Board of Governor's Annual Meeting on October 11, 1985 in Seoul, Korea. This marked the Bank's fortieth anniversary.<sup>4</sup> The Agency's principal purpose and objective is to encourage the flow of investment to and among developing countries by means of guarantees.<sup>5</sup> Toward this end, the drafters set up a new World Bank affiliate which follows the tradition of the International Finance Corporation<sup>6</sup> and the International Center for the Settlement of Investment Disputes.<sup>7</sup> From its inception, the Bank has not only served as a multilateral lending organization, but also as a catalyst for the devel-

1. See Wall St. J., Apr. 13, 1988 at 24, col. 6; Washington Post, Apr. 13, 1988, § F, at 1, col. 1; Financial Times, Apr. 13, 1988, at 4, col. 3; Handelsblatt, Apr. 14, 1988, at 12, col. 1.

2. The text of the Convention is published in 24 I.L.M. 1606 (1986) [hereinafter Convention] together with an official World Bank Commentary in 1 ICSID REV. FOREIGN INVESTMENT L. J. 145 (1986); for an account of one of the co-founders of MIGA see Shihata, *The Multilateral Investment Guarantee Agency*, 20 INT'L L. 485 (1986) [hereinafter Shihata, *The Agency*]; cf. also I. SHIHATA, *MIGA and Foreign Investment-Origins, Operations, Policies and Basic Documents of the MIGA 61-99* (1988) [hereinafter SHIHATA, ORIGINS].

3. Convention, *supra* note 2, art. 61(b) requires ratification of at least five capital exporting and fifteen capital importing countries as listed in Schedule A. Prior to April 12, the Convention had already been ratified by six capital exporting countries. However, their total subscription, together with that of eighteen capital importing countries, did not amount to the necessary one third of the Agency's authorized capital; the U.S. subscription alone amounts to 20.519 percent of MIGA's authorized capital.

4. Resolution No. 406 of the Board of Governors, reprinted in World Bank/IFC/IDA 1985 Annual Meeting of the Board of Governors, Summary Proceedings 244 (1986). cf. also Clausen, Address to the Board of Governors (Oct. 8, 1985) (Seoul, Korea), reprinted in THE DEVELOPMENT CHALLENGE OF THE EIGHTIES, A.W. CLAUSEN AT THE WORLD BANK 391, 415 (World Bank ed. 1986) [hereinafter Clausen, Address to the Board].

5. See Convention, *supra* note 2.

6. Articles of Agreement of the International Finance Corporation, opened for signature May 25, 1955, 7 U.S.T. 2197, T.I.A.S. No. 3620, 264 U.N.T.S. 117.

7. Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, opened for signature Mar. 18, 1965, 17 U.S.T. 1270, T.I.A.S. No. 6090, 575 U.N.T.S. 159.

opment of new ideas, institutions and procedures to facilitate the flow of private investment capital to developing countries. The roots of MIGA can thus be traced back to the Bank's Articles of Agreement which provide that it is the Bank's purpose to both "assist in the reconstruction and development of territories of members by facilitating the investment of capital for productive purposes,"<sup>8</sup> and "[t]o promote foreign investment by means of guarantees."<sup>9</sup> The prospects and principal goals of MIGA have been discussed and researched thoroughly prior to and after the Convention's opening for signature both within the Bank<sup>10</sup> and in the international trade and investment community.<sup>11</sup> The Agency's ultimate success, however, will largely depend upon its ability to benefit from its unique transnational organizational and financial structure in order to achieve a "synergism of cooperation"<sup>12</sup> between developing and developed countries.

The administrative machinery was set in motion with MIGA's Board of Governors inaugural session on June 8, 1988, followed by the directors first meeting on June 22, 1988,<sup>13</sup> and finally with the acquisition of the initial financial endowment.<sup>14</sup> MIGA has thus ar-

8. Articles of Agreement of the International Bank For Reconstruction And Development, opened for signature Dec. 27, 1945, Art. I(i), 60 Stat. 1440, T.I.A.S. No. 1502, 2 U.N.T.S. 134.

9. *Id.* at art. I(ii).

10. See generally WORLD BANK WORKING PAPER, THE PROSPECTS OF A MULTILATERAL INVESTMENT GUARANTEE SCHEME TO ENHANCE THE FLOW OF RESOURCES TO DEVELOPING COUNTRIES (1985) [hereinafter PROSPECTS]; see also WORLD BANK: MULTILATERAL INVESTMENT GUARANTEES, QUESTIONS AND ANSWERS, Staff Working Paper (Mar. 21, 1986) [hereinafter QUESTIONS AND ANSWERS]; J. VOSS, THE MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA): ELIGIBILITY REQUIREMENTS (World Bank Working Paper, Jan. 30, 1987) [hereinafter ELIGIBILITY REQUIREMENTS]; J. VOSS, THE MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA): UNDERWRITING POLICIES (World Bank Working Paper, Feb. 6, 1987) [hereinafter UNDERWRITING POLICIES]; J. VOSS, THE MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA): ADJUSTMENT OF CLAIMS AND RECOVERY OF PAYMENTS FROM HOST COUNTRIES (World Bank Working Paper, Feb. 9, 1987) [hereinafter ADJUSTMENT OF CLAIMS]; J. VOSS, THE MULTILATERAL INVESTMENT GUARANTEE AGENCY (MIGA): OBJECTIVES, FEATURES AND STATUS OF IMPLEMENTATION (World Bank Working Paper, Nov. 1987) [hereinafter OBJECTIVES].

11. See, e.g. Statement of The National Association of Manufacturers on MIGA, Submitted to the Senate Foreign Relations Committee (May 8, 1987); Letter of the International Law Association, Committee on Foreign Investment, American Branch, to House Trade Bill Conferees on MIGA (Sept. 22, 1987). [Both on file with author].

12. A.W. Clausen in his Address to the 1981 Joint Annual Meeting of World Bank and International Monetary Fund, cited in Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA*, 1 ICSID REV. FOREIGN INVESTMENT L.J. 1, 22 (1986) [hereinafter DEPOLITICIZATION].

13. J. VOSS, MIGA'S INVESTMENT GUARANTEE PROGRAM, 2 (World Bank Working Paper, July 1988).

14. The deadline for the pay in of the share capital for the initial member countries was

rived at an important juncture of its work which warrants a comprehensive analysis of its prospects of success. Although there is no generally accepted methodology to predict the impact of an investment guarantee program on the volume of investment to developing countries,<sup>15</sup> this article seeks to evaluate MIGA's general prospects, its acceptability for all partners in the investment process, and its developmental value and impact on the international law of investment protection. To arrive at a comprehensive assessment, the article will also discuss briefly the scope of foreign direct investment and its benefits for host country development. Finally, it will look at the MIGA project in the broader perspective of other national and international investment promotion and protection schemes.

#### B. FOREIGN DIRECT INVESTMENT: A MAJOR FACTOR OF DEVELOPMENT

MIGA's declared primary objective, to enhance and stimulate the flow of foreign direct investment (FDI) to developing countries, cannot be evaluated without a basic understanding of (1) the scope of FDI and (2) its impact on host country development.<sup>16</sup>

##### 1. Definition of Scope

Together with official development assistance (ODA)<sup>17</sup> and private bank lending, FDI constitutes a major external source of investment resources for many developing countries.<sup>18</sup> However, due to the highly complex nature of FDI, with its "generic" charac-

July 11, 1988. See MIGA, INFORMATION ON PAYMENTS OF THE INITIAL SUBSCRIPTION TO THE CAPITAL STOCK OF THE MIGA BY THE ORIGINAL MEMBERS OF THE AGENCY, 1 (World Bank Working Paper, Apr. 1988).

15. PROSPECTS, *supra* note 10, at 5.

16. See Brelsford, *International Investment Insurance - The Convention Establishing the Multilateral Investment Guarantee Agency*, 27 HARV. INT'L L. J. 735, 737 n.10 (1986) (citing Professor Detlev Vagts in an unpublished manuscript prepared for the U.N. Conference on Trade and Development in May 1978 at 2: "Finding a role for a multilateral insurance agency requires an affirmative answer to three preliminary questions: (1) is there a significant role for private foreign direct investment in the development process? (2) does it require guarantees to maintain or stimulate the flow of such investment? (3) is there a role for a multinational agency that will not be preempted by national agencies? (emphasis added)).

17. Development assistance constitutes about one third of all net capital flows to developing countries. Cf., *Development Cooperation: Efforts And Policies of the Members of the Development Assistance Committee*, 1982 REV. 51, 53 (OECD 1982).

18. C. OMAN, NEW FORMS OF INTERNATIONAL INVESTMENT IN DEVELOPING COUNTRIES 9 (OECD 1984).

ter<sup>19</sup> involving aspects of trade, finance, structural adjustment policies, and business behavior of multinational corporations, it is difficult to formulate a comprehensive and generally acceptable definition of FDI.<sup>20</sup>

From the outset, there are two undisputed and obvious distinctions. The concept of investment, as distinguished from a simple sales transaction, involves the acquisition of assets expected to yield revenues in future periods, thus inferring the investors expectations of future, hence uncertain events (time dimension of investment).<sup>21</sup> With respect to foreign direct investment, the foreign investor retains at least part of the ownership and control, unlike ODA and private bank lending where the business is owned and controlled by local companies or entrepreneurs. Given these basic determinants, FDI may best be defined as the creation, acquisition or endowment<sup>22</sup> in the host country, of enterprises either incorporated as branches, subsidiaries or associate companies, or in the form of unincorporated enterprises or joint ventures. The desired result is to acquire a lasting interest, with powers of management and control, where the investor's return depends upon the performance of the enterprise.<sup>23</sup> FDI flows include all funds provided by the direct investor, specifically, equity capital, reinvested earnings and net borrowing. Equity investment that does not meet this standard constitutes portfolio investment which is placed through the capital market without entrepreneurial commitment and merely for the sake of capital yield. All other liabilities that have a predetermined schedule of repayment are classified as external

19. See *Official Commentary on the MIGA Convention*, 1 ICSID REV. FOREIGN INVESTMENT L. J. 195, 200 (1986) [hereinafter *Commentary*].

20. For a brief account on the problems of gaps and differences in coverage and scope of investment data and the resulting problems of comparability of different systems of data collection see Witherell, *OECD Improves Direct Investment Statistics*, 18 CTC REP. 40 (Winter 1982).

21. C. OMAN, *supra* note 18, at 18.

22. Investment flows are by no means limited to monetary forms but encompass contributions of machinery, technology and services. See *Commentary*, *supra* note 19, at 201, para. 19; see also OPERATIONAL REGULATIONS OF THE MIGA (Draft approved by the Board of Directors first session, June 22, 1988), published in SHIHATA, ORIGINS, *supra* note 2, at 435 [hereinafter OPERATIONAL REGULATIONS].

23. For different approaches to a definition of FDI that served as guidelines for the definition in this article see IMF BALANCE OF PAYMENTS MANUAL, PARA. 408 (IMF 4th. ed. 1977); J. VOSS, *The Protection and Promotion of FDI in Developing Countries: Interests, Interdependencies, Intricacies*, 31 INT'L COMP. L.Q. 686 (1982) [hereinafter Voss, *Interdependencies*]; OECD, DETAILED BENCHMARK DEFINITION OF FOREIGN DIRECT INVESTMENT 7 (1983); Oman, *Changing International Investment Strategies in the North-South Context*, 22 CTC REP. 47 (Autumn 1986).

debt.<sup>24</sup> Since the 1970's, however, new subtle forms of FDI have emerged, in which foreign investors do not hold a controlling interest via equity ownership. It is instead, acquired through contractual arrangements which provide the foreign investor with some degree of control and return. Typical examples include licensing, technical assistance, and "product in hand" or "product sharing" contracts.<sup>25</sup> The modern notion of FDI, therefore, includes both the classical and the contractual forms. The MIGA operational framework,<sup>26</sup> as a major innovative feature, takes into account these new developments and incorporates them in its coverage provisions.

## 2. The Role of FDI in the Development Process

While there are some undisputed benefits of FDI for multinationals and their home countries (establishing or securing a monopoly in international trade, exploring new attractive markets and resources), there is some controversy on the question of relative costs and benefits of FDI to developing countries.<sup>27</sup> However, several advantages of FDI are generally accepted and may have a long term beneficial impact on the development process. First and foremost, FDI insulates host countries,<sup>28</sup> to a certain extent, from unanticipated external payment difficulties. Because FDI is not a debt creating instrument requiring regular payments and generating continuous demands on the host countries' balance of payments, only when the investment earns a profit are payments implied, thereby placing part of the risk on the foreign investor.<sup>29</sup> Despite the lack of reliable key information, there appears to be a

24. IMF, FOREIGN PRIVATE INVESTMENT IN DEVELOPING COUNTRIES 28 (Occasional Paper No. 33, 1985) [hereinafter IMF OCCASIONAL PAPER].

25. Oman, *supra* note 23, at 47. The rationale behind these new arrangements is the retention of control by the host country over the rate and pattern of exploitation of its natural resources, inspired by the principle of Permanent Sovereignty Over Natural Resources. See J. C. FERNANDEZ, DIRECT INVESTMENT IN PETROLEUM VENTURES IN DEVELOPING COUNTRIES: A REVIEW OF RISKS AND STRATEGIES 31 (Rand Corp. ed. 1985).

26. OPERATIONAL REGULATIONS, *supra* note 22, §§ 1.05 (i)-(vii) include these forms in the definition of eligible investments.

27. For a recent survey of the pros and cons of FDI in developing countries see GRIECO, FOREIGN INVESTMENT AND DEVELOPMENT: THEORIES AND EVIDENCE IN INVESTING IN DEVELOPMENT: NEW ROLES FOR PRIVATE CAPITAL? 35 (Th. Moran ed. 1986).

28. The term "host country" means the country where the investment takes place, whereas "home country" refers to the origin of the investor.

29. Shihata, *Factors Influencing the Flow of Foreign Investment and the Relevance of a Multilateral Investment Guarantee Scheme*, 21 INT'L L. 671, 673 (1987) [hereinafter Shihata, *Factors*].

positive correlation between the annual rate of return on FDI and the annual growth of the GNP in the host country.<sup>30</sup> FDI, therefore, provides a "countercyclical stabilization" of the host countries' abilities to pay. FDI is also often substantially involved with import substituting and export industries so the foreign trade performance of enterprises based on direct investment can have a significant impact on their host's balance of payments.<sup>31</sup> This is critical in view of the severe debt crisis plaguing these economies. The total debt overhang of these countries rose from \$755 billion in 1981<sup>32</sup> to \$1,190 billion in 1987,<sup>33</sup> and is estimated to reach \$1,245 billion in 1988.<sup>34</sup> These countries need to increase domestic resource mobilization and stimulate export oriented industries to reduce their debt-service ratio,<sup>35</sup> improve their balance of payment and restore their credit worthiness, which has suffered heavily from the debt crisis. Since these economies are too weak to recover on their own, the urgent need for FDI and estimated new inflows of up to \$30 billion a year becomes apparent.<sup>36</sup> However, due to a deteriorating investment climate, the flow of FDI to developing countries other than China,<sup>37</sup> has steadily decreased from \$16.7 billion in 1981 to \$9.5 billion in 1984.<sup>38</sup> FDI can also help these econ-

30. IMF OCCASIONAL PAPER, *supra* note 24, at 23 (chart 3). The study points out that for 28 countries which rescheduled debt during 1983, the stock of FDI accounted for an average of only 14 percent of their total external liabilities, compared to an average of 24 percent for those 24 LDCs that did not reschedule debt, obviously not facing severe payment problems.

31. IMF OCCASIONAL PAPER, *supra* note 24, at 11. However, the paper also hints at the danger of multinational corporations being engaged mainly in intrafirm transactions which makes them less responsive to relative price changes than companies engaged in arms length market transactions which have no reason to be concerned with the effects of their transactions on other affiliates. *Id.* at 12.

32. 1 WORLD DEBT TABLES, VIII (World Bank ed. 1987-88). The data exclude debt of the high income oil exporting countries.

33. *Id.* (data are estimated).

34. *Id.* (data are projected).

35. The debt-service ratio is a primary indicator of creditworthiness of debtor countries and reflects the ratio of external debt payments to exports. Financial authorities regard a ratio of 20 percent as prudent. See Barnett, et. al., *On Third World Debt*, 25 HARV. INT'L L. J. 83, 89 n.18 (Winter 1982).

36. Moran, *Shaping a Future for Foreign Direct Investment in the Third World*, 11 THE WASH. Q. 119, 128 (Winter 1988) [hereinafter Moran, *Shaping a Future*].

37. For this notable exception which is mainly due to China's favorable policy toward foreign investment and the huge domestic market see UNCTC CURRENT STUDIES NO. 7, *Foreign Direct Investment, the Service Sector and International Banking*, at 12-15 (1987).

38. *Id.* at 28 and 189, Table III. Low or negative growth rates in LDCs have also reduced return on existing investment and thus also the funds for new investment, since a large portion, often around two-thirds, of FDI is financed from profits made in earlier periods. *Policy Analysis and Research, Changes in the Pattern of FDI, an Update*. 23 CTC

omies to improve their long term growth prospects, which is generally accompanied by an initial and often permanent input of financial resources, managerial skills, technical know how and marketing connections, which have a high contribution potential to the countries' economic growth.<sup>39</sup> This may increase the real domestic income of the host country by more than the profits repatriated to the investor's home country. As a side effect, FDI also stimulates local entrepreneurship by providing increased competition and opportunities for subcontracting by local suppliers. Consequently, the MIGA project plays an important role in recent growth proposals like the "Secretary of the Treasury Baker's Program for Sustained Growth"<sup>40</sup> or former World Bank President Clausen's "Twin Pillared Strategy of Adjustment Assistance and Resource Mobilization".<sup>41</sup>

The success of FDI, however, depends largely on the favorable economic policy of the host country. Many developing countries have been extremely concerned with the behavior of multinational enterprises and the loss of autonomy caused by investment that is connected with a substantial degree of overseas managerial control by large transnational corporations.<sup>42</sup> This was regarded as perpetuating the economic dependence of the Third World<sup>43</sup> and as being

REF. 3, 6 (Spring 1987).

39. Martin, *Multilateral Investment Insurance: the OECD Proposal*, 8 HARV. INT'L L. J. 281, 282 (1967) [hereinafter Martin, *The OECD Proposal*]. Indira Gandhi in a speech to the New York Economic Club on March 30, 1966, stated: "[India] welcomes private investment not only for the capital it brings with it, but also for the transfer of modern technology and managerial skills private investment facilitates" *Id.* at 281, n.1-6.

40. Farnsworth, *Bankers at IMF Talks Cautious on Baker Plan*, N.Y. Times, Oct. 9, 1985, § 1, at 1, col. 1.

41. Clausen, Address to the Board, *supra* note 4.

42. These concerns ultimately led to a wave of nationalizations and expropriations in the 1970's. See, e.g. the nationalization of British Petrol's and Milton Bunker Hunt's oil interests in Libya in 1973, text of the Libyan decree, 13 I.L.M. 58 (1974); The expropriation of Kennecott's and Anaconda's copper mines in Chile in 1971 with a book value of \$318,801,198.77. Deduction of "excess profits", i.e. alleged amount of injury caused to national interests by these enterprises, led to a denial of compensation and the resulting claims of over \$360 million against OPIC, which exceeded its insurance reserves. See A. LOWENFELD, *INTERNATIONAL PRIVATE INVESTMENT* (2d ed. 1982); the complaint of Chile regarding the practices of ITT ultimately led to the "New International Economic Order", 53 U.N. ESCOR (1822d mtg.) at 19, 22; U.N. Doc. E/SR. 1822 (1972).

43. See IMF OCCASIONAL PAPER, *supra* note 24, at 11; cf. also Rubin, *Transnational Corporations and International Codes of Conduct: A Study Of The Relationship Between International Legal Cooperation and Economic Development* 30 AM. U.L. REV. 903, 912 (1981) (hints at the dilemma that multilateral enterprises may be accused of acting as conduits for the policies of a foreign state - the developed home country - which results in "a feeling of dependency that may or may not have undesirable economic aspects but certainly is psychologically unsettling").

inconsistent with the Principle of Permanent Sovereignty over Natural Resources as developed in several U.N. Resolutions.<sup>44</sup>

From an economic point of view, foreign-controlled firms were accused of adopting overly capital-intensive production techniques, making insufficient transfers of technology at too high a cost and contributing to similar negative economic influences.<sup>45</sup> In the past decade, however; due to an increasing willingness of home countries to accept economic and social objectives of host countries and the fruitful negotiations on the U.N. Code of Conduct on Transnational Corporations,<sup>46</sup> host countries have gained increasing confidence in the role of FDI in development.<sup>47</sup> By now, both partners in the investment process seem to realize that investment protection schemes provide the linkage *par excellence* between dynamic allocation efficiency and developmental interests of the Third World.<sup>48</sup>

#### C. MIGA: GENESIS, STRUCTURE, FUNCTIONS

An analysis of MIGA's institutional and financial structure, within this economic background, and when compared with the characteristics of previous proposals and the reasons for their failure, will assist in a comprehensive assessment of MIGA's prospects of success.

44. Voss, *Interdependencies*, *supra* note 23, at 690; cf. *Declaration on Permanent Sovereignty over Natural Resources*, G.A. Res. 1803, 17 GAOR Supp. (No. 17) U.N. Doc.A/5217 (1962); *Charter of Economic Rights and Duties of States*, G.A. Res. 3281, 29 GAOR Supp. (No. 30) U.N. Doc.A/9030 (1974), stating that each state has the right "to nationalize, expropriate or transfer ownership of foreign property". The Charter is part of the instrumental framework of the "New International Economic Order" adopted at the Sixth Special Session of the General Assembly of the U.N. on raw material and development in 1974, and implies that the territorial state can never lose its legal capacity to change the destination or method of exploitation of resources whatever arrangements have been made for their exploitation or administration. See generally Jimenez de Arechaga, *Application of the Rule of State Responsibility to the Nationalization of Foreign Owned Property*, LEGAL ASPECTS OF THE NEW INTERNATIONAL ECONOMIC ORDER 220 (1980). For the legal quality of the declarations see Horn, *Normative Problems of a New International Economic Order*, 16 J.W. TRADE L. 338, 340 (1982) (no law but a "mixture of ethical values, political norms and claims which look a little bit like law").

45. Shihata, *Factors*, *supra* note 29, at 676.

46. See *Code of Conduct on Transnational Corporations: Outstanding Issues in the Draft Code of Conduct*, U.N. Doc.CE/C.10/1985/S/2; the most recent draft dates June 2, 1983 U.N. ESCOR Doc. E/C.10/1983/S/5.

47. Moran, *Shaping a Future*, *supra* note 36, at 119. "There has been a fundamental shift from the overwhelming criticism of multinational corporations to a pervasive enthusiasm about it" *Id.*

48. Cf. Voss, *Interdependencies*, *supra* note 23, at 699.

### 1. Previous Proposals and Reasons for their Failure

The idea of insuring investment against the uncertainties of non-commercial risks on a multinational basis is not new. One of the first schemes of this kind was proposed by a working group of the Council of Europe's Consultative Assembly in 1957<sup>49</sup> and later reconsidered in a report of the Economic Committee of the Council of Europe in 1959, though limited to investment by Europeans in African Countries.<sup>50</sup>

Apart from considerable discussion in the United States,<sup>51</sup> several proposals were made at the private level by bankers and industrialists in the 1960's. One such proposal was that of the Dutch banker E.H. Van Eeghen, made at meetings of the International Chamber of Commerce in 1960/61.<sup>52</sup> These proposals were regarded as either viable alternatives to the establishment of an international investment code, (which was regarded as having no prospect of success),<sup>53</sup> or a way to arrive at a combined insurance/investment code scheme.<sup>54</sup> Considerations of the issue in the World Bank date back to 1948, and the Bank staff prepared the first major study in 1962.<sup>55</sup> Without taking a position supportive of a mul-

49. *Report of the Study Group for the Development of Africa*, Eur. Consult. Ass., 20th Sess., Doc. No. 701 at 22 (1957).

50. *Report on an Investment Statute and a Guarantee Fund Against Political Risk*, Eur. Consult. Ass., 20th Sess., Doc. No. 1027, at 22 (1959) (designed as one element in a general plan to tackle the problem of economic development in Africa and contemplating that guarantees might well precede and smooth the way for a transnational investment code). See Brewer, *The Proposal for Investment Guarantees by an International Agency*, 58 AM. J. INT'L L. 62, 70-71 [hereinafter Brewer, *The Guarantee Proposal*]. The idea was later revived in a proposal of the European Council for a "Community Guarantee System for Private Investment in Third Countries". See Commission of the European Community, Doc. 290/72.

51. A first proposal was advanced by the Kennedy administration in 1961. In 1976 Henry Kissinger proposed an "International Resource Bank" at the fourth UNCTAD session. See A. BRENNGLASS, *THE OVERSEAS PRIVATE INVESTMENT CORPORATION, A STUDY IN POLITICAL RISK*, 99-120 (1983).

52. See Van Eeghen, *Multilateral Investment Guarantees*, 5 A.B.A. SECT. INT'L COMP. L. BULL. 36 (1961).

53. See COMMITTEE OF INTERNATIONAL TRADE AND INVESTMENT OF THE ABA SECTION OF INTERNATIONAL AND COMPARATIVE LAW PROTECTION OF PRIVATE PROPERTY INVESTED ABROAD 115 (1963).

54. Snyder, *Foreign Investment Protection: A Reasoned Approach*, 61 MICH. L. REV. 1087, 1102 (1963); cf. also Broches, *International Investment Guarantees: Possibilities And Problems*, AM. SOC. INT'L L. 81, 85 (1962). The differing opinions hint at the principal issue of including investment standards in the convention. See *infra* note 207 and accompanying text.

55. INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, *MULTILATERAL INVESTMENT INSURANCE*, (Staff Report, Washington D.C. 1962) [hereinafter WORLD BANK REPORT].

tilateral scheme, the study analyzed the "incentive effect of investment insurance" and concluded that an actual improvement of the investment climate by an international investment guarantee scheme "was not capable of demonstration."<sup>56</sup> In 1965, the Deputy Secretary General of the OECD, supported by the International Chamber of Commerce,<sup>57</sup> submitted to the Bank a "Report on the Establishment of an International Investment Guarantee Corporation" (IIGC).<sup>58</sup> This report served as a basis for the drafting of the "Articles of Agreement of the International Investment Insurance Agency" (IIIA) which was completed in 1966, redrafted in 1968 and 1972, and subsequently discussed in the Bank for several years.<sup>59</sup> Despite slight optimism,<sup>60</sup> few developed and the developing countries expressed interest in promoting the establishment of such an agency. The draft sank into oblivion. Not until the early 1980's was the idea revived by the then President of the Bank, A. W. Clausen<sup>61</sup> and the then General Counsel, Heribert Golsong.<sup>62</sup> The reasons for the failure are complex and reflect the vehement disagreement over the Agency's operational structure more than disagreement over its purpose and goal.<sup>63</sup> The issues of disagreement are of crucial significance for an analysis of the MIGA project since they reflect the principal problems the Seoul Convention had to overcome. Five basic areas of conflict can be delineated in the

56. *Id.* at 6. The paper contains a synopsis of twelve proposals from private and official sources. *Id.* at 30-37.

57. See INTERNATIONAL CHAMBER OF COMMERCE, STATEMENTS AND RESOLUTIONS 1963-65, at 11 (1965).

58. IBRD Doc. No. R 65-97, Annex C.

59. QUESTIONS AND ANSWERS, *supra* note 10, at 2. The 1972 draft is reprinted in Staff of Foreign Affairs Division, Congressional Research Service, Library of Congress for the House Committee on Foreign Affairs, 93d Congress, 1st session, "The Overseas Private Investment Corporation, A Critical Analysis", Committee Print 130 (1973) [hereinafter *The OPIC*]. For a discussion of these drafts see BRENNGLASS, *supra* note 51, at 106-110.

60. Martin, *The OECD Proposal*, *supra* note 39, at 288. "[i]t appears likely that Articles of Agreement will be opened for signature within the coming year."

61. Address to the Board of Governors of the World Bank on September 29, 1981 in Washington, D.C., "I believe that this whole issue now merits fresh attention, and if there is widespread support in principle, we in the Bank are prepared to join in an effort to see if such a mechanism can be established." This came as a total surprise to everybody in the Bank, interview with Professor Heribert Golsong in Washington, D.C., July 20, 1988 [hereinafter Golsong interview].

62. H. Golsong, Office Memorandum on an International Investment Insurance Scheme (Apr. 29, 1982) (on file with the author).

63. However, it was also the discussion of the NIEO and the principle of Permanent Sovereignty over Natural Resources which led many developing countries to object to the idea of a multilateral investment agency. Golsong, *Proceedings, Seventy-Seventh Annual Meeting*, 1983 AM. SOC. INT'L L. 303.

previous proposals: (1) the linkage between the agency and the Bank, (2) the distribution of voting rights between developing and developed countries, (3) the nature of financial participation by developing countries, (4) subrogation as a means of recovery by the agency, and (5) arbitration as a means of dispute settlement.<sup>64</sup>

Apart from these specific host country objections, many developed countries, like Japan and West Germany, had developed their own national investment insurance scheme in the 1960's and were skeptical that an international agency could be as efficient, reliable and cheap as their own national schemes.<sup>65</sup> The following discussion will reveal whether the MIGA Convention has been able to address these issues without impairing its efficiency.

## 2. MIGA's Organizational Structure

MIGA will have a fully juridical personality<sup>66</sup> and be legally and financially independent, with membership being open to all member states of the World Bank and Switzerland. A Council of Governors composed of one representative of each member country will govern the Agency<sup>67</sup> and elect a Board of Directors responsible for the general operation of the Agency and the election of the President, who conducts the ordinary business. A personal link is established with the World Bank by the Bank's President being *ex officio* Chairman of MIGA's Board of Directors.<sup>68</sup> MIGA's voting structure clearly reflects the drafters' attempt to avoid a majority vote for capital exporting (developed) countries. The Convention basically follows the Bretton Woods model of weighted voting, offering each member country 177 membership votes and one additional vote per share subscribed.<sup>69</sup> To ensure parity between capi-

64. INTERNATIONAL INVESTMENT INSURANCE AGENCY, STAFF MEMORANDUM ON PRINCIPAL OUTSTANDING ISSUES, reprinted in The OPIC, *supra* note 59, at 145; Meron, *The World Bank and Insurance*, 47 BRIT. Y.B. INT'L. L. 301, 313 (1974-75) [hereinafter Meron, the World Bank and Insurance]; see also Shihata, *MIGA and the Standards Applicable to Foreign Direct Investment*, 1 ICSID REV. FOREIGN INVESTMENT L. J. 327, 335 (1986) [hereinafter Shihata, *Applicable Standards*] (listing the following as unresolved issues in the last round of drafting negotiations of the MIGA Convention: the voting structure, the settlement of disputes between MIGA acting as subrogee and a host country and the inclusion of investment standards).

65. The OPIC, *supra* note 59, at 32.

66. Convention, *supra* note 2, at art. 1(b).

67. *Id.* at art. 31.

68. *Id.* at art. 32(b).

69. *Id.* at art. 39(a). See also Martin, *The OECD Proposal*, *supra* note 39, at 289. In opposition to the OECD proposal, a voting system similar to that of the World Bank was suggested which placed a majority of the capital exporting countries on the Board, thus

tal exporting and importing countries<sup>70</sup> during the critical period of the first three years, each group is assured a minimum of 40 percent of total voting power by allocation of supplementary voting shares as necessary. Also, all decisions during this initial period require a special majority of at least two-thirds of the total voting power, representing at least 55 percent of total capital subscription.<sup>71</sup> This structure has been criticized for not ensuring that capital importing countries cannot block prompt awarding of claims to investors.<sup>72</sup> Though the Convention provides that final decision on claims will be made "under the direction of the board,"<sup>73</sup> this only refers to general procedure policies<sup>74</sup> and the board will not participate in the President's decision on individual claims, thus ensuring prompt and apolitical decision making by the President and his claims committee. The same organizational structure is used in the recoupment process, for which similar concerns have been raised by the former General Counsel of the Bank.<sup>75</sup>

The North-South conflict within the Agency is unlikely to arise since the Category II list includes developing countries from the OECD like Greece and Turkey and, most importantly, such oil-producing capital exporting countries as Kuwait and Saudi-Arabia, which, in view of their strong interest in investment protection,<sup>76</sup> are likely to vote with the Category I states.<sup>77</sup>

making the proposal almost unacceptable for LDCs. See *id.* at 329-330 (Art. 13 of the OECD Draft).

70. Countries belonging to either group are listed, together with their number of shares and capital subscription in Schedule A of the Convention, *supra* note 2.

71. Convention, *supra* note 2, art. 39(b) and (d); *Commentary*, *supra* note 19, at 212-213, para. 63.

72. Moran, *Shaping a Future*, *supra* note 36, at 126.

73. Convention, *supra* note 2, at art. 17.

74. *Commentary*, *supra* note 19, at para. 28.

75. Golsong, *Eine multilaterale Investitionsversicherungsagentur?* in CAPITAL INVESTMENT ABROAD - CHANCES AND RISKS, 163-169 (1983) [hereinafter CHANCES AND RISKS] (claims against the host country would be removed from the international to the agency-internal plane and host countries could, through their voting, influence the recoupment process).

76. Both countries therefore had a strong interest in establishing MIGA, especially since the Inter Arab Investment Guarantee Corporation covers only investments in Arab member states. Golsong Interview, *supra* note 61. Saudi-Arabia was the third country to ratify the convention only nine months after its opening for signature. See LIST OF SIGNATURES AND RATIFICATIONS OF THE CONVENTION ESTABLISHING THE MIGA (July 6, 1988) (issued and updated regularly by the World Bank).

77. Touscoz, *L'agence multilaterale de garantie des investissements*. 13 DROIT ET PRATIQUE DE COMMERCE INTERNATIONAL 311, 320 (1987).

### 3. MIGA's Financial Structure

In accordance with the American OPIC scheme and unlike other national agencies, MIGA is designed to become financially self-sufficient, namely, able to pay claims and meet other liabilities from premium income and other revenues such as return on investment. To establish the necessary confidence of investors, MIGA's guarantees will be secured by a share capital in the initially authorized amount of one billion Special Drawing Rights, fixed at the equivalent of \$1.082 billion.<sup>78</sup> All member countries<sup>79</sup> subscribe to shares of MIGA's capital, each in proportion to its relative economic strength as measured in accordance with its allocation of shares in the capital of the World Bank as of March 1, 1985.<sup>80</sup> As both groups of countries have a financial stake in the Agency, this structure complements the organizational pattern described above and ensures the necessary financial responsibility of all members. The Convention itself does not provide rules for the determination of premiums.<sup>81</sup> Operational Regulations authorize the Agency to fix the premium between 0.3 percent and 1.5 percent of the guaranteed amount per year for each individual typical risk covered on a case by case basis.<sup>82</sup> In the event all risks listed in Article 11 are

78. Convention, *supra* note 2, at art. 5(a).

79. This structure constitutes an important deviation from previous proposals that provided for financial participation only by those countries which wanted to assume liability for the investment. The structure is based on the assumption that underwriting an investment benefits only, or mainly, the countries directly involved in the investment flow, and that no country will make a commitment based upon the suggestion that it may derive benefits from an investment flow in which it is not directly involved. Martin, *The OECD Proposal*, *supra* note 39, at 323 (strongly approving the financial participation of all countries). See also Brewer, *The Proposal For Investment Guarantees By An International Agency*, 58 A.J.I.L. 62, 72 (1964) [hereinafter Brewer, *The Investment Guarantee Proposal*] (setting forth the Van Eeghen proposal, which required each country to pay in capital equal to one half of the capital it has imported or exported; this formula tends to penalize the successful countries and is hence self-defeating).

80. SHIHATA, *THE AGENCY*, *supra* note 2, at 494. Ten percent of the subscription will be paid in cash, in freely usable currencies. See Convention, *supra* note 2, art. 8. Developing countries may pay up to 25 percent in their own currency. *Id.* An additional 10 percent will be paid in non-negotiable, non-interest bearing promissory notes to be cashed by MIGA in case of need only, art. 7(i). The remaining subscribed capital will be subject to call. *Id.* The specific amount of subscribed capital for each member is listed in Schedule A of the Convention. *Id.*

81. A premium's purpose in this context is not only to provide financial endowment to MIGA, but also to ensure that the Agency's limited resources cover only those investments that are badly needed to overcome politically motivated deterrents, cf. Martin, *The OECD Proposal*, *supra* note 39, at 314-315.

82. OPERATIONAL REGULATIONS, *supra* note 22, § 3.19 - 3.43. These premiums are subject to continuous verification and review, which might lead to a downward or upward adjust-

covered, the regulations provide for a discount of up to 50 percent of the sum of individual payments.<sup>83</sup> The premium is determined by the risk involved.<sup>84</sup> This might be problematic in that the investment most in need of a guarantee will also be exposed to the highest political risk, thus requiring maximum premiums which may render MIGA's guarantees unattractive for those investors.<sup>85</sup> The premium structure remains within the range of other national investment insurance agencies like the American OPIC (from 0.3 percent for inconvertibility up to 1.5 percent for expropriation of production oil and gas projects),<sup>86</sup> the French COFACE (0.4 percent - 0.6 percent) and BFCE (0.7 percent - 1 percent)<sup>87</sup> and the German Treuarbeit (0.5 percent of the full amount of guaranteed investment).<sup>88</sup> The same holds true for private risk insurers who charge annual premiums between 0.1 percent and 9 percent of the insured amount with an average premium of 2.5 percent for confiscation in developing countries.<sup>89</sup>

The aggregate amount of guarantees which MIGA will offer may not exceed 1.5 times the subscribed capital.<sup>90</sup> This does not mean that there is no room for leverage since this risk to asset ratio may later be increased to a maximum of 5 to 1.<sup>91</sup> With respect to individual guarantees, MIGA will limit its exposure to 5 percent of its total underwriting capacity. However, the drafters of the convention expect that MIGA will leverage its capacity through coinsurance and reinsurance arrangements and by induc-

ment within certain margins. *Id.* § 3.41.

83. *Id.* § 3.34.

84. *Id.* § 3.42.

85. Cf. Brelaford, *supra* note 16, at 742.

86. OPIC INVESTMENT INSURANCE HANDBOOK 6-7. OPIC has base rates varying with the industry and flexible within a margin of 33 percent depending on the risk profile of the specific project.

87. Klein, *Le Systeme Francais de Garantie des Investissements a l'etranger*, 13 DROIT ET PRATIQUE DU COMMERCE INTERNATIONAL 63, 76 (1987). France is the only country with two insurance agencies: the COFACE (compagnie francaise d'assurance pour le commerce exterieur) for "commercial" investments, and the BFCE (banque francaise du commerce exterieur) for "industrial" investments.

88. CHANCES AND RISKS, *supra* note 75, at 176.

89. OPERATIONAL REGULATIONS, *supra* note 22, § 3.43, n.60.

90. Convention, *supra* note 2, at art. 22(a).

91. *Id.* Under accepted principles of insurance and banking, the incurring of aggregate liabilities in excess of the insurer's or bank's equity is permissible since it cannot reasonably be expected that under prudent and sound risk diversification all risks will become losses. Art. 25 of the Convention requires the agency to follow sound business and prudent financial management practices. *Commentary*, *supra* note 19, at 206, para. 38. See also QUESTIONS AND ANSWERS, *supra* note 10, at 40.

ing investors to retain a large portion of the risk - at least 10 percent of the guaranteed investment - on their own account.<sup>92</sup> While previous proposals, and even the Golsong Memorandum<sup>93</sup> provided for a "sponsorship arrangement" as the sole underwriting mechanism,<sup>94</sup> thus impairing every guarantee by political considerations and objections of the member states,<sup>95</sup> the MIGA Convention uses sponsorship arrangements only as a *supplemental* device, making its financial structure more flexible and able to increase its guarantee capacity above the allowed leverage to an infinite amount. Under the arrangement, a member country or group of member countries can propose the guarantee of a specific investment but must incur a loss-sharing contingent obligation in the amount of the guarantee sponsored.<sup>96</sup> This obligation will be demanded if a payable insurance amount cannot be paid out of a separate "Sponsorship Trust Fund."<sup>97</sup> Interestingly enough, these sponsored guarantees may even cover investment in developed countries without absorbing scarce underwriting capacity to the detriment of developing countries.<sup>98</sup>

This financial structure, viewed in conjunction with the organizational features outlined above, is unique in the sense that, in contrast to previous proposals,<sup>99</sup> it removes diplomatic and politi-

92. ADJUSTMENT OF CLAIMS, *supra* note 10, at 6.

93. MEMORANDUM, *supra* note 62, at 3 (Professor Golsong suggested a 90 percent sponsorship by the home country that had proposed the investment for sponsorship and 10 percent by the developing host country, with a proportional loss sharing formula for all countries having sponsored investment when the claim occurs).

94. Meron, *The World Bank and Insurance*, *supra* note 64, at 310 (setting forth the previous World Bank Proposal). Cf. art. 34 of the OECD proposal fixing the loss sharing liability of all member countries that have approved the guarantee and excluding any liability of a state only by virtue of its membership. Martin, *The OECD Proposal*, *supra* note 39, at 332.

95. Art. III § 3 of the World Bank proposal prohibited sponsorship if any member state objected on the grounds that the sponsored investor was its national. See Meron, *The World Bank and Insurance*, *supra* note 64, at 311.

96. Convention, *supra* note 2, art. 24 and Annex I to the Convention. This arrangement may serve as a risk diversification device for member countries, allowing them to reallocate their entire contingent liabilities in their national investment schemes to only a pro rata share in the sponsorship arrangement. See *Commentary*, *supra* note 19, at 208, para. 47 (in contrast to MIGA's own guarantees, sponsored guarantees are not limited to nationals of member countries, thus further increasing MIGA's flexibility and possible range of action).

97. Convention, *supra* note, 2, art. 2 of Annex I. The Fund will be kept separate from MIGA's own assets, and the Agency cannot incur any liabilities with respect to its assets under a sponsorship arrangement, art.6. *Id.*

98. Voss, *The Multilateral Investment Guarantee Agency: Status, Mandate, Concept, Features, Implications*, 21 J. WORLD TRADE L. 5, 19 [hereinafter Voss, *The MIGA*].

99. Martin, *The OECD Proposal*, *supra* note 39, at 326 He strictly rejected the sponsorship arrangement of the OECD draft, stressing that "it would lead to continuing political

cal implications from the decision making process prior to issuing a guarantee and secures the cooperation of host and home countries through their financial and equal voting participation.

#### 4. MIGA's Underwriting Function

The most outstanding characteristic of the Agency's guarantee program is flexibility in the design of its risk coverage. The Seoul Convention does not give a precise and rigid description and definition with respect to possible insurable risks. Rather, it provides a general framework which leaves to the Board's discretion defining more precisely the scope of its operations. This enables the Agency to meet the challenges of new forms of investment and changed conditions in the world investment climate.<sup>100</sup>

##### a. Insurable Risks

The Convention provides for three "classical"<sup>101</sup> non-commercial investment risks, namely (1) host government restrictions on currency conversion and transfer, today the most sought after form of coverage producing the most claims,<sup>102</sup> (2) expropriation and (3) risk of war and civil disturbance.<sup>103</sup> In addition to and in contrast with most national insurance schemes, coverage is extended to breach of contract risk.<sup>104</sup> Upon the joint request of the investor and host country, with approval of MIGA's Board by special ma-

fighting within the corporation" although "the investor is seeking insurance . . . to insulate himself from the vagaries of politics." *Id.*

100. For a taxonomy of the new forms of FDI that have emerged in the past decade see Oman, *supra* note 18. Concrete guidelines for coverage of these new contractual forms of FDI have been developed. See OPERATIONAL REGULATIONS, *supra* note 22, § 1.05.

101. Cf. art. 27 § (1) - (3) of the OECD Draft of 1965; Martin, *The OECD Proposal*, *supra* note 39, at 330. For the Council of Europe Proposal see Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 71; cf. also 22 U.S.C. § 2194 (a)(1) (A)-(C)(1982)(for the American OPIC).

102. Shanks, *Insuring Investments and Loans against Currency Inconvertibility, Expropriation and Political Violence*, 9 HASTINGS INT'L. COMP. L. REV. 417, 427 (1986). In total dollar amounts, however, the expropriation claims still exceed the inconvertibility claims. During fiscal year 1986, OPIC resolved eight inconvertibility, but only one expropriation claim. See OPIC Press Release Dec. 31, 1987, at 10-11. The debt crisis forces many countries to decree suspension of payments to foreign creditors, as did the Philippines in 1983 and 1984. See KIMBERLY CLARK CORPORATION MEMORANDUM OF DETERMINATION, OPIC Contract No. A 108, at 1 (on public file at OPIC).

103. Convention, *supra* note 2, art. 11 (a)(i), (ii), (iv).

104. *Id.* at art. 11(a)(iii) which is, however, designed as *ultima ratio*, when the investor cannot obtain a final and binding decision on the breach (denial of justice). See UNDERWRITING POLICIES, *supra* note 10, at 12 (so MIGA does not run the risk of becoming judge in its own affairs).

jury, coverage is also extended to other non-commercial risks, such as acts of terrorists directed at the investor, kidnapping, or politically motivated strikes.<sup>105</sup> With the latter provision, the Convention follows the earlier proposals of World Bank and OECD which, as a somewhat revolutionary approach, allowed the Board to insure other non-commercial risks which discourage international investment.<sup>106</sup>

Article 11 is certainly the most important provision of the Convention, from the investors point of view, because it tries to strike a difficult balance between its appeal to the private investment community and its acceptability to the governments of both capital importing and exporting countries.<sup>107</sup> The "expropriation" definition in Article 11(a)(ii) constitutes a crucial step forward. Historically, the definition of the expropriation risk became a major obstacle to the establishment of a multilateral investment insurance scheme acceptable to parties on both sides of the investment flow.<sup>108</sup> The drafters had to cope not only with the problem of outright expropriation, which has become very infrequent in post-colonial investment, but with the complex issue of what is commonly termed "creeping"<sup>109</sup> or "indirect"<sup>110</sup> expropriation. This concept encompasses a broad range of host country measures and modes of conduct, primarily through apparently lawful means such as administrative harassment, which in their economic consequences constitute an interference with the property rights of the foreign investor, and ultimately render the investment unproductive.<sup>111</sup> The problem in this context lies in the nearly impossible task of drawing a line of delimitation between lawful state regulations in pursuit of legitimate state objectives on the one side, and

105. Convention, *supra* note 2, at art. 11(b). Coverage for the risk of devaluation and depreciation is specifically excluded, mainly because they are considered "normal business risks" and because to offer protection against it, would subject the program to a prohibitively large contingent liability. Martin, *The OECD Proposal*, *supra* note 39, at 296.

106. See art. III § 1 of the World Bank draft, cited with approval in Meron, *The World Bank and Insurance*, *supra* note 64, at 310; cf. art. 27(4) and 31(1) of the OECD draft, Martin, *The OECD Proposal*, *supra* note 39, at 330-331.

107. The World Bank Report, *supra* note 55, at 7 (stressing the crucial significance of a broad and flexible political risk definition, and raising doubts as to the feasibility of such a definition).

108. Brelsford, *supra* note 16, at 783 n.17; Martin, *The OECD Proposal*, *supra* note 39, at 290. For the developing countries view of expropriation in the context of the New Economic Order see *supra* note 44 and accompanying text.

109. Shihata, *The Agency*, *supra* note 2, at 489.

110. Dolzer, *Indirect Expropriation of Alien Property*, 1 ICSID REV. FOREIGN INVESTMENT L. J. 41, 44 (1986).

111. Voss, *Interdependencies*, *supra* note 23, at 702.

unlawful expropriation on the other, an issue that has been neglected in international law but is of crucial importance in the field of investment insurance.<sup>112</sup> Article 11 (a) (ii) attempts to strike this balance by excluding from its definition of expropriation all non-discriminatory measures of general application which governments normally take for the purpose of regulating economic activity in their territory.

This provision resembles the "negative clause" in the standard contract of the U.S. Overseas Private Investment Corporation which precludes payment under certain circumstances.<sup>113</sup> Because it refers to "generally accepted principles of international law" and "constitutionally sanctioned governmental objectives", this clause has been criticized as too broad and vague.<sup>114</sup> MIGA's prospects of success in this respect are much more promising, since the Official Commentary on the Convention<sup>115</sup> and the Operational Regulations<sup>116</sup> provide investors and host countries with concrete and surprisingly detailed guidelines including *bona fide* taxation, labor, environmental legislation and other measures normally taken by host countries to regulate their economic activities as non-coverable by the Agency.<sup>117</sup> In contrast to national insurance agencies, which indemnify the investor only in cases of "total" expropriation,<sup>118</sup> MIGA may, in certain easily discernable cases cover partial

112. H. WHITMAN, THE UNITED STATES INVESTMENT GUARANTEE PROGRAM AND PRIVATE FOREIGN INVESTMENT 15 (1959) ("The question of the point at which legitimate regulations ceases to be that and becomes a "taking" is essentially unanswerable, and in recent years investors have come to fear creeping expropriation . . . more than the outright variety"). See also the unpublished model standard contracts of national insurance schemes cited in Dolzer, *supra* note 110, at 56-57; cf. also Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 83.

113. Dolzer, *supra* note 110, at 57 ("any law, decree, regulation and administrative action of the Government which is not by its express terms for the purpose of nationalization, confiscation or expropriation . . .").

114. *Id.*

115. See *supra* note 19, at 200, para. 14. For the legal quality and binding force of the Commentary, see Shihata, *Applicable Standards*, *supra* note 64, at 332 n.26.

116. See *supra* note 22, §§ 1.29 - 1.41.

117. Commentary, *supra* note 19, at 200, para. 14. The OPERATIONAL REGULATIONS, *supra* note 22, go much farther in their detailed outline of the Agency's underwriting policy with respect to expropriation. A measure may be attributed to the host government not only in case of direct government action, but also where it approves, authorizes, ratifies or directs the action or omission (§ 1.34); discriminatory and confiscatory measures are always covered by MIGA's guarantees (§ 1.36).

118. OPIC Insurance Contract Form 234, KGT 12-85, art. 5.01, 4.01; Shanks, *supra* note 102, at 425; Hence, the investor must be willing to give up all his investment in order to be indemnified.

losses.<sup>119</sup>

b. *Eligibility of Investment*

The criteria for eligibility of both investors and investment are likewise broad and flexible and again reflect the drafters' efforts to balance the need to preserve MIGA's scarce capital resources with maintaining sufficient flexibility in its eligibility determination. The investment to be guaranteed must be made in the territory of a developing member country,<sup>120</sup> and the investor must be a national of a member state other than the host state.<sup>121</sup> An important exception is made to the latter requirement if an investor wants to transfer assets from abroad to his home country.<sup>122</sup> This may induce investors with large off-shore funds to transfer or repatriate them to their respective home countries, forming an important additional investment flow to developing countries and contributing to a reversal of the "capital flight".<sup>123</sup>

Eligible investments have to be new and medium or long term in nature.<sup>124</sup> They encompass equity investments, including equity type loans made by the holder of equity in the project enterprise to this enterprise with repayment periods of not less than three years, and various classical and new forms of non-equity direct investment. The latter form, however, has to meet the typical characteristics of direct investment outlined above,<sup>125</sup> namely terms of at least three years and the return must depend substantially on the production, revenues or profits of the investment project.<sup>126</sup> In accordance with aspired maximum flexibility, the Board may extend coverage to additional forms of investment, as long as the capital flow does not amount to a pure export credit.<sup>127</sup>

119. OPERATIONAL REGULATIONS, *supra* note 22, §§ 5.01, 4.01.

120. Convention, *supra* note 2, at art. 14.

121. *Id.* at art. 13(a)(i). A corporate investor must be incorporated and have its principal place of business in a member country or must have the majority of its stock owned by nationals of a member country, thus encompassing foreign owned subsidiaries.

122. *Id.* at art. 13(c).

123. *Cf. Commentary, supra* note 19, at 202, para. 23. For the detrimental impact of capital flight on development see Shihata, *Factors, supra* note 29, at 672-73.

124. Convention, *supra* note 2, art. 12(c).

125. See *supra* note 21 and accompanying text.

126. *Id.* at art. 12(a); Operational Regulation, *supra* note 22, §§ 1.05-1.06 (for detailed provisions on the determination of eligible non-equity investment). As a general guideline and pursuant to its objective the Regulations direct special attention to investment arrangements of long duration and high developmental potential. See *id.* at § 1.07.

127. *Id.* at art. 12(b); *Commentary, supra* note 19, at 201, para. 20.

c. *Underwriting Policy*

MIGA's underwriting policy can be briefly characterized by three broad terms: Project Assessment, Risk Assessment and Host Country Approval.

With respect to the investment project, the Agency is required to undertake a thorough project appraisal satisfying itself of the economic soundness, contribution to development needs of the host country, compliance with host countries laws and regulations and the consistency of the investment with the declared development objectives and priorities of the host country.<sup>128</sup> This requires a comprehensive assessment of the project's technical feasibility, financial and economic viability and its impact on the respective developing country. This is a highly complex and hence time-consuming process, which may cause intolerable delays in the decision-making process leading to the final underwriting decision, rendering MIGA unattractive for investors who desire speedy underwriting decisions. However, since the Agency will be located in the World Bank Building in Washington D.C. and staff cooperation agreements are envisaged by the drafters,<sup>129</sup> MIGA may benefit from the outset from the unique legal and economic expertise of the World Bank staff. In addition, the Operational Regulations give a time limit of 120 days of receipt by the Agency of an application within which underwriting decisions should be made.<sup>130</sup> This time limit seems realistic, especially since the the Agency is allowed to rely on its project and country assessment, and the written statements of the applicant and the respective countries.<sup>131</sup> Another source of possible delay lies in Article 38 of the Convention, requiring the Agency to issue guarantees only with the prior approval of the host country, thus respecting its sovereignty. This procedure, which was also included in previous proposals,<sup>132</sup> has been strongly criticized for causing significant delays in the application process.<sup>133</sup> In this area, too, the Convention and its accom-

128. Convention, *supra* note 2, art. 12(d)(i)-(iii).

129. See OPERATIONAL REGULATIONS, *supra* note 22, at §§ 5.20-5.23.

130. *Id.* at § 3.26

131. *Id.* at §§ 3.27, 3.28.

132. Martin, *The OECD Proposal, supra* note 39, at 331, art. 30(1); *World Bank Proposal* art. III § 2, *The OPIC, supra* note 59, at 134. For the Council of Europe and Van Eeghen proposals see Brewer, *The Investment Guarantee Proposal, supra* note 79, at 85.

133. See Martin, *The OECD Proposal, supra* note 39, at 309. (stressing that the investor may be confronted with complicated, lengthy forms which neither he nor his lawyer is able to understand; further, lower officials involved in the approval process in the host country may feel pressure from higher ranking officials, who are opposed to the program but did

panying framework turn out to be more sophisticated than previous proposals. The Operational Regulations allow the Agency to obtain from individual host countries *advance* approvals for the coverage of all or certain types of investments or risks.<sup>134</sup> In addition, the Convention provides for approval on a non-objection basis.<sup>135</sup> The host country may even limit its approval to certain types of risks. MIGA will then limit its coverage accordingly, provided that the investor is still interested in a limited guarantee which does not enjoy the full benefits of MIGA's unique coverage program. As to the approval of the home country, which was also required by previous proposals and doubled the administrative obstacles to investment insurance, MIGA provides that the respective home country take the initiative to notify the Agency of a violation of its domestic laws.<sup>136</sup> This system does not eliminate the risk of politically motivated disputes in the underwriting process but it does limit them to a minimum.

#### d. Subrogation and Arbitration

The dispute settlement and recoupment procedures represent another highly sensitive issue in the negotiation of the Convention and were a major reason for the failure of previous proposals.<sup>137</sup> In fact, the very *raison d'être* for the World Bank and OECD proposals was to make subrogation a non-political, technical, non-confrontation issue.<sup>138</sup> Many developing countries opposed compulsory arbitration in principle and the Latin American Calvo Doctrine is

not have a majority in the initial ratification of the Convention). Note that a refusal to approve may not result from economic development factors but from a "temporary disenchantment with the investor's government or from other, essentially irrelevant, domestic policies". *Id.* at 310-311; see also Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 85.

134. OPERATIONAL REGULATIONS, *supra* note 22, § 3.22. This is similar to the proposal of Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 85 with regard to a general consent to investment guarantees covering a particular type of risk.

135. Convention, *supra* note 2, art. 38(b); OPERATIONAL REGULATIONS, *supra* note 22, § 3.25 (fixing the period after which approval is deemed to be given to no less than 30 days from the date of the request for approval and allowing extension at the request of the host country).

136. OPERATIONAL REGULATIONS, *supra* note 22, § 3.10.

137. See Seidl-Hohenveldern, *Subrogation under the MIGA Convention*, 2 ICSID REV. FOREIGN INVESTMENT L. J. 112 (1987); Brelsford, *supra* note 16, at 741; Voss, *Die Multilaterale Investitionsgarantie Agentur*, 33 RECHT DER INTERNATIONALEN WIRTSCHAFT, 90, 93 (1987).

138. Meron, *The World Bank and Insurance*, *supra* note 64, at 312 (stating that the objections against these principles would "seem to go to the essence of a multilateral insurance institution")

particularly hostile towards subrogation and international arbitration with respect to foreign investment.<sup>139</sup> Due to their experience with the abuse of diplomatic protection, these countries tried to avoid the intervention of the home states of investors which would turn any conflict into an intergovernmental one. Therefore, the proposal required these investors to agree to the settlement of disputes exclusively under domestic law and by domestic tribunals and rejected subrogation of a state to the rights of a private foreign national,<sup>140</sup> a proceeding unacceptable for a multinational agency. Right to suit outside national courts would confer a privilege upon the foreign investor, placing the nationals of the host country in a position of inferiority, contrary to the legal equality of states.<sup>141</sup> These traditional reservations notwithstanding, the Convention provides for subrogation of MIGA to the rights which the indemnified investor has acquired against the host country as a result of the event giving rise to his claim<sup>142</sup> and requires disputes which arise between the Agency as subrogee and a host country to be submitted to international arbitration, if prior negotiations and conciliation fail.<sup>143</sup> To benefit from the institutional advantages of the ICSID Dispute Settlement procedures,<sup>144</sup> MIGA, which as a multilateral organization cannot directly participate in ICSID arbitration, can nonetheless benefit from these rules. It can either pur-

139. See C. CALVO, INTERNACIONAL TEORICO Y PRACTICO 22 (1868); Carcia-Amador, *Calvo Doctrine. Calvo Clause* in 8 ENCYCLOPEDIA OF PUBLIC INTERNATIONAL L. 62 (R. Bernhardt ed. 1985); cf. art. 2(2)(c) of the U.N. Charter of Economic Rights and Duties of States, *supra*, note 44 (providing that controversies caused by the question of compensation "shall be settled under the domestic law of the nationalizing state," although this has always been deemed a question of international law).

140. Shihata, *Depoliticization*, *supra* note 12, at 2. Note that the Calvo Doctrine cannot prevent the sovereign home government from diplomatic intervention and preventing a claim for the injury of its own inhabitant. *Id.* at 3.

141. Carcia-Armado, *supra* note 139, at 62.

142. Convention, *supra* note 2, art. 18; Subrogation is an accepted principle of insurance law, see *Commentary*, *supra* note 19, para. 26. As an example, see 12 U.S.C.A. § 182(g) (Subrogation of the FDIC under the U.S. National Banking Act). Every U.S. investment guarantee agreement, even those with Latin American countries, contain a subrogation clause. *But see infra* note 149.

143. Convention, *supra* note 2, art. 57(b) and Annex II for the applicable arbitral procedure. This framework has to be distinguished from the internal procedure of resolving questions of interpretation and application of the Convention (art. 56; dec. of the Board of Directors, appeal to the Board of Governors for final determination) and disputes arising out of contracts of guarantee which may be referred to arbitration according to the rules fixed in the respective contracts (art.58). The Convention does not include rules on the settlement of disputes between a member state and a foreign investor.

144. For a recent account on ICSID see Delaume, *ICSID and the Transnational Financial Community*, 1 ICSID REV. FOREIGN INVESTMENT L. J. 237 (1986).

sue rights under the Convention as an agent of the investor or require the investor to pursue his claim under the Convention even after advance payment through MIGA. This would, of course, be conditioned upon the investor finally obtaining an award on the merits.<sup>145</sup> This framework does not conflict with the aforementioned reservations of the developing countries since MIGA, as an international organization, will be led by strictly non-political, purely pro-investment purposes<sup>146</sup> being in the common interest of the controlling members, i.e. capital exporting and importing countries. Arbitration between such an agency and its members is a generally accepted principle of dispute settlement in international law.<sup>147</sup> In addition, MIGA's highly flexible procedural framework allows for the agreement of alternative methods of dispute settlement,<sup>148</sup> thus enabling adjustment to the particular situation in the respective host country. Many Latin American countries have expressed their willingness to accept subrogation by concluding executive agreements with the U.S. providing for subrogation of the U.S. Overseas Private Investment Corporation to the rights of indemnified U.S. investors.<sup>149</sup> Furthermore, MIGA's right to subrogation will be recognized by all member countries by virtue of their ratification of the Convention.<sup>150</sup> The system employed in the Convention also contributes to legal clarity and predictability since in contrast to national systems, which have discretion in pressing a subrogated claim if this would embarrass a friendly country, MIGA, though having discretion and being able to refrain from

145. Seidl-Hohenveldern, *supra* note 137, at 113-114; ADJUSTMENT OF CLAIMS, *supra* note 10, at 20.

146. Convention, *supra* note 2, art. 34.

147. SHIHATA, APPLICABLE STANDARDS, *supra* note 64, at 338 (pointing out that some domestic laws prohibit resort to arbitration only with respect to disputes with foreign investors and hence, are not applicable to disputes between two international persons).

148. Convention, *supra* note 2, art. 57(b)(ii) (in connection with Annex II of the Convention). The Agency might, for example, first seek remedies available under the domestic laws of the host or ask for an advisory opinion of the ICJ in lieu of arbitration. See *Commentary*, *supra* note 19, at 216, para. 76(c).

149. See, e.g., Agreement Relating to Investment Guarantees, Nov. 26 and 29, 1962, between the U.S. and Venezuela, 474 U.N.T.S. 107 (1963). However, traces of the Calvo Doctrine can still be found in these agreements: the recent 1985 agreement with Bolivia provides for appointment of a fiduciary agent who holds rights or claims for OPIC, instead of OPIC itself (art. 3) and conditions arbitration on exhaustion of appeals and administrative and judicial remedies available in Bolivia (art. 6 b). Exchange of notes on Dec. 19, 1985, unpublished, available at OPIC, Washington, D.C.

150. See Convention, *supra* note 2, art. 18(b); but see Seidl-Hohenveldern, *supra* note 137, at 116-17 (in view of the ambiguous language of the provision "shall be recognized," recommends an authoritative interpretation by the Board under art. 56(a)).

pressing a claim for business reasons,<sup>151</sup> can treat the recoupment problem in the way it should be treated, namely as a purely legal issue.<sup>152</sup> As a practical matter, it seems highly unlikely that MIGA will have to resort to arbitration, given that OPIC never had to resort to arbitration under its investment guarantee agreements.<sup>153</sup>

As with other problematic issues, the drafters of the Convention seem to have found a way to balance the legitimate concerns and interests of the developing capital importing countries with the needs and necessities of an efficient recoupment and dispute settlement scheme, which is reflected by five Latin American countries having signed the MIGA Convention thus far.<sup>154</sup>

##### 5. MIGA's Promotional Capacity

Probably the most striking and outstanding difference between MIGA and previous proposals is that its function is not limited to mere underwriting of investment but goes far beyond that, covering a broad range of promotional activities,<sup>155</sup> such as research, providing technical advice and assistance and serving as a forum for consultations and cooperations among its members. The rather vague notion of investment promotion in this context encompasses such concrete projects as the establishment of a data bank for investment opportunities, the organization of investors, missions to potential host countries, the arrangement of sectoral workshops and the bringing together of joint venture partners.<sup>156</sup> The information disseminated through these services and MIGA's forum function will, in return, benefit MIGA by promoting interest in investment and in the Agency's guarantee program. The whole promotion and information system will especially benefit the inves-

151. SHIHATA, ORIGINS, *supra* note 2, at 260.

152. See the comments to previous proposals by Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 85; see Martin, *The OECD Proposal*, *supra* note 39, at 319. "[T]here will be no political bickering over when it [i.e. the Agency] should and when it should not exercise that discretion." *Id.*

153. Shanks, *supra* note 102, at 431. The mere availability of an international arbitration mechanism has been a decisive factor in encouraging negotiated settlements. *Id.* at 431-32.

154. See List of Signatory States, *supra* note 76. These countries are Bolivia, Colombia, Uruguay, Chile and Ecuador; the latter two have also ratified the Convention. These countries have also signed new investment guarantee agreements with the United States in the past few years, a prerequisite for OPIC covering investment in these countries. See Shanks, *supra* note 102, at 432.

155. See Convention, *supra* note 2, art. 23; see *Commentary*, *supra* note 19, at 207, para. 41.

156. Voss, *The MIGA*, *supra* note 98, at 13.

tors in developing countries who, except for Indian and Korean investors, commonly lack access to a reliable source of information and services. These promotional activities are by no means new. The American OPIC, for example, has sponsored investment missions to LDCs, established a computer data system for investment opportunities and set up an Investor Information Service that provides basic investment data,<sup>157</sup> so that smaller enterprises can share their marketing experience. However, MIGA's transnational character bears a much greater potential for generally accepted and hence fruitful promotional activities.

#### 6. *The Agency's Acceptability for the Investment Community*

Viewed as a whole, MIGA's organizational, financial and operational structure seems to be much more acceptable to the parties of the international investment community than those of previous proposals. Sensitive business information, submitted by the applicant during the registration process, will be kept confidential.<sup>158</sup> The concerns connected with the OECD proposal, that the Agency may not appear as financially safe, since it is not backed by government budgetary resources (OPIC's obligations are entitled to the "full faith and credit" of the U.S. government)<sup>159</sup> and will therefore be less appealing to investors,<sup>160</sup> seems unwarranted in view of MIGA's capital reserve requirements and commitment to prudent management. As of July 6, 1988, MIGA's subscribed capital was approximately \$685 million, which allows a total amount of contingent liabilities of roughly \$1 billion and an exposure in each individual project of \$10 million.<sup>161</sup> In comparison, OPIC had, in fiscal year 1987, a capital of \$50 million and insurance reserves of \$849.9 million, while total liabilities amounted to \$20.6 million.<sup>162</sup>

157. OPIC INFORMATION BOOKLET 8 (OPIC N.D.).

158. OPERATIONAL REGULATIONS, *supra* note 22, §3.30.

159. OPIC ANNUAL REPORT 1987, at 39.

160. Martin, *The OECD Proposal*, *supra* note 39, at 327; Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 76.

161. Theoretically, the exposure could be about \$51 million, but the Operational Regulations require a broad distribution of guarantees among member countries. See Operational Regulations, *supra* note 22, at §3.57. This conservative ceiling is also advisable in view of the slow buildup of MIGA's reserves; a project of \$10 million with an annual premium of 0.6% will only generate \$60,000 annually and the registration fee is \$5,000, 0.05% of the insured amount. See Operational Regulations, *supra* note 22, at §3.46.

162. OPIC Annual Report, *supra* note 159, at 36. The reserves may be increased by transfers from unrestricted retained earnings, which were \$4.2 million in fiscal 1987. *Id.* at 34.

The \$10 million initial ceiling seems realistic, given the fact that the majority of OPIC's insured investment in fiscal 1987 ranged between \$50,000 and \$10 million.<sup>163</sup> Coverage problems may, however, occur in large oil or gas exploitation ventures,<sup>164</sup> but here co-insurance arrangements with national insurance agencies will provide a viable alternative. These figures make it easy to predict that the Agency will find world-wide acceptance not only with respect to the signing and ratification of the Convention,<sup>165</sup> but also in its day-to-day practice.

#### D. MIGA'S RELATION TO EXISTING GUARANTEE SCHEMES

A crucial question for MIGA's success will be its relation to the guarantee schemes that already exist on the national and international level. Will it be cooperation or competition? The MIGA project is doomed to fail if these schemes leave no place for MIGA's insurance program or if MIGA's operations would result in ruinous competition with those schemes.

##### 1. *MIGA and National Investment Guarantee Programs*

To date, most of the investment protection and promotion between North and South takes place on a national or bilateral basis. Apart from bilateral investment treaties,<sup>166</sup> all DAC member countries and Korea and India operate national investment guarantee programs, the most important being (in order of size) the Japanese Export Insurance Division, Ministry of International Trade and Industry (EID/MITI), the U.S. Overseas Private Investment Corporation (OPIC)<sup>167</sup> and the German program<sup>168</sup> administered by

163. *Id.* at 26-29.

164. Two of OPIC's three \$100 million projects in fiscal year 1987 were natural resource exploitations. *Id.* at 28.

165. Martin, *The OECD Proposal*, *supra* note 39, at 310, hints at the inherent conflict between the general approval of a multinational program carried by a broad national and international consensus and the daily work with it that is likely to be jeopardized by narrower, more vigilant interests opposing the program.

166. Worldwide, there are over 210 of those treaties in force today. See Akinsanya, *International Protection of Direct Foreign Investment in the Third World*, 36 INT'L & COMP. L.Q. 58 (1987); see also the list as of October 1, 1982 in 21 I.L.M. 1208 (1982).

167. See 22 U.S.C.A. §§ 2191-2200 (1979 & Supp. 1988) OPIC is an "agency of the United States under the policy guidance of the Secretary of State." *Id.* at §2191. OPIC has its origins in the Marshall plan of 1948. See M. Von Neumann-Whitman, GOVERNMENT RISK-SHARING IN FOREIGN INVESTMENT 69-81 (1965).

168. Federal Budget Law (Bundeshaushaltsgesetz) 1959, art. 18, § 1, Bundesgesetzblatt II, 793 (1959) for the first statutory basis.

the Treuarbeit AG in Hamburg.<sup>169</sup> Like FDI itself, the purpose of these programs is twofold, promotion of development and of domestic industries, why they have sometimes been criticized as hidden export subsidies.<sup>170</sup> Although the figures of investment insured by these national agencies are impressive - the OPIC alone issued a total of \$12.8 billion of insurance coverage for 438 projects between 1981 and 1984<sup>171</sup> - most of these schemes still show important gaps and shortcomings. According to World Bank data, less than twenty percent of investment flows from these countries to the Third World were covered by national programs and the utilization level varied substantially from fifty percent in Japan and Austria to less than five percent in most European schemes.<sup>172</sup> The Swiss agency GERG (Geschäftsstelle für die Exportrisikogarantie, Zurich) has been almost inoperative in the past few years.<sup>173</sup> In addition, most of the national risk portfolios, even of large insurers like the German Treuarbeit, tend to concentrate on a few host countries with which they have close economic ties and on a few major projects, leading to a problematic lack of risk diversification potential.<sup>174</sup> The new, sophisticated investments in contract form sometimes do not qualify for coverage of these agencies<sup>175</sup> and may even remain uninsured if export insurance schemes like the German "Hermes Exportkreditversicherungs AG" require a fixed claim. These deficiencies are mainly caused by constraints inherent in national guarantee schemes, especially different approaches towards nationality<sup>176</sup> of the investor. The American OPIC can insure investment

169. These institutions have to be distinguished from national export insurance agencies which often times cover the same non-commercial, political risks such as the U.S. Commodity Credit Corporation's Export Guarantee Program GSM-102, see 7 C.F.R. §1493 (1988); based on the Commodity Credit Charter Act, 15 U.S.C. §§ 713a(4), 714, 714(m) and the German Hermes Kreditversicherungs AG.

170. Seidl-Hohenveldern, *General Course on Public International Law*, 3 RECUEIL DES COURS 13, 190 (1986).

171. Akinsanya, *supra* note 166, at 68.

172. QUESTIONS AND ANSWERS, *supra* note 10, at 17.

173. Golsong interview, *supra* note 61.

174. Golsong, *International Investment Insurance Against Political Risks-A Need or Fantasy? in INSURING AMERICAN BUSINESS AGAINST POLITICAL RISK ABROAD* 3, 8-9 (NFTC Foundation ed. 1983).

175. Voss, *supra* note 137, at 94.

176. The German and French systems are based on the principle of corporate domicile (Sitzprinzip, Siege Sociale), irrespective of whether the firm is controlled by foreigners, thus following the general principles of international law as elaborated in the Barcelona Traction case. See Evans, *Judicial Decisions Involving Questions of International Law*, 64 AJIL 653, 686 (1970). However, the French system does not insure investment by companies controlled (majority of voting stock or capital in foreign hands) by foreigners whereas Germany refuses

by foreign companies controlled by Americans,<sup>177</sup> which is not feasible under the German program.<sup>178</sup> Other such shortcomings include the exclusive focus on projects deemed to serve particular development policies of the home country and lack of financial capacity or underwriting capacity to cover large investments.<sup>179</sup> The MIGA Convention recognizes these shortcomings and requires the Agency to cooperate with international agencies in order to increase their effectiveness and efficiency.<sup>180</sup> MIGA, freed from any constraints of nationality of investor or political considerations, may thus<sup>181</sup> co-guarantee investments with national agencies through parallel or joint underwriting, provide reinsurance for these agencies, and may guarantee investments which fail eligibility tests of national schemes but are sound and have developmental character<sup>182</sup> and guarantee investment by a multinational investor consortium. Most importantly, MIGA may guarantee investments from capital surplus developing countries or newly industrialized countries which do not operate national insurance programs, thus pursuing its mandate to give particular attention to the flow of investment *between* developing countries.<sup>183</sup> MIGA will not compete with national investment guarantee schemes but rather complement and supplement their activities in terms of di-

indemnification in case of foreign majority only if there is a causal link between the foreign ownership and the loss. See German General Insurance Conditions, §4(2), reprinted in J. Salow, *Bundesgarantien für Kapitalanlagen im Ausland und internationalen Investitionsschutz* 248 (1984) [HEREINAFTER Salow, *Investitionsschutz*]; see also Metzger, *Nationality Of Investment Under Investment Guaranty Schemes - The Relevance Of The Barcelona Traction Case*, 65 AJIL 532 (1971).

177. The nationality test in 22 U.S.C. § 2198 (c) (3) (1982) does not focus on the investors principal place of business but includes foreign entities provided that less than five percent of the total of issued and subscribed share capital is in foreign hands; the Germans are concerned that this might promote flight of investors to tax haven countries, SALOW, *INVESTITIONSSCHUTZ*, *supra* note 176, at 92.

178. *Id.* at 91.

179. See Voss, *The MIGA*, *supra* note 98, at 17; cf. Petersmann, *The World Bank's Contribution to the Law of International Finance and Development (1944-1984)*, 23 ARCHIV FÜR VOLKERRECHT 241, 264 (1985); see Golsong, *supra* note 174, at 9.

180. See Convention, *supra* note 2, art. 19.

181. For a detailed outline of possible fields of cooperation see *Commentary, supra* note 19, at 204, para. 29; QUESTIONS AND ANSWERS, *supra* note 10, at 33-34; OPERATIONAL REGULATIONS *supra* note 22, at §§ 5.03-5.19.

182. MIGA may especially underwrite viable, export-oriented "enclave projects" in highly indebted countries, the balance of payment problems of which force national agencies, like the German Treuarbeit, to refuse coverage, benefit from its focus on the individual project rather than on the economic and political situation in the respective host country at large. See Voss, *supra* note 137, at 94.

183. See Convention, *supra* note 2, art. 23(c).

versification of risk portfolio and expansion of coverage. The same is true for the private risk insurance market that has developed since the early 1970's,<sup>184</sup> although cooperation in this field seems more complicated in view of their traditionally short insurance period of usually not more than three years,<sup>185</sup> as compared to MIGA's coverage of up to 15 years.<sup>186</sup>

## 2. MIGA and International Protection and Promotion Schemes

Closely related, in view of the potential benefits of transnational investment promotion, is MIGA's relation to international investment promotion and protection schemes. As mentioned above,<sup>187</sup> the establishment of MIGA is generally viewed as being in line with the World Bank's previous efforts to institutionalize investment promotion schemes. The International Finance Corporation (IFC), a Bank's affiliate and multilateral development institution, is designed to promote and supplement productive private investment in developing countries by making both equity investment and loans directly in the private sector.<sup>188</sup> However, IFC limits its own investment to 25 percent of the total equity, in June 1987 its portfolio of disbursed loans and equity was only \$1.9 billion.<sup>189</sup> Typically it focuses on raising investor confidence and bringing together and reconciling the diverse interests of commercial, investment and merchant banks as loan participants, joint venture co-investors, partners in corporate restructuring and loan conversions. Taking into account its additional comprehensive advisory services, especially the Foreign Investment Advisory Service

184. See Kobrin, DESCRIPTION AND ANALYSIS OF THE U.S. MARKET FOR POLITICAL RISK INSURANCE FOR OVERSEAS INVESTMENTS IN DEVELOPING COUNTRIES, STUDY FOR OPIC, CONTRACT No. 85-C-015, (1986); Lloyds of London and the American International Group, are the major underwriters in a market with an estimated premium volume between \$150-200 million; American banks are now also entering the market. *Id.* at 6-9.

185. *Id.* at 17; OPERATIONAL REGULATION, *supra* note 22, at §3.50(i) require a reinsurance contract to expire "no sooner than the reinsured contract of guarantee or applicable portion thereof." Apart from that, private insurers usually do not cover the war risk. See Golsong, *supra* note 174, at 9.

186. OPERATIONAL REGULATIONS, *supra* note 22, at §2.04 provides for a range of three to fifteen years, which may be extended to twenty years; MIGA's coverage will focus on long insurance periods which are also used by national agencies. OPIC finds it difficult to co-insure with private insurers; such attempts were relinquished in 1977; interview with Gerald T. West, Vice President for Development at OPIC, Washington, D.C. (June 29, 1988).

187. See *supra* page 2; see generally MIGA Convention, Approved - Already signed by Korea, Turkey, Ecuador, Senegal and Sierra Leone, 3 News From ICSID 6 (Winter 1986).

188. International Finance Corporation, Annual Report 1987, at ii.

189. *Id.* at i.

(FIAS) established in fiscal 1986<sup>190</sup> and the new Guaranteed Recovery of Investment Principal (GRIP), through which IFC shares the risk with foreign investors,<sup>191</sup> the parallel approach of IFC and MIGA as "honest brokers"<sup>192</sup> between capital exporting and importing countries becomes apparent. The GRIP Program in particular, which goes further than MIGA since it covers all risks, not just non-commercial risks,<sup>193</sup> is, like MIGA, expected to increase additionally the development process<sup>194</sup> and promote multilateralization of investment standards.<sup>195</sup> In pursuit of cooperation provisions included in MIGA's operational framework, the FIAS staff and program will be transferred to MIGA and a cooperation agreement will be concluded between the two institutions.<sup>196</sup>

ICSID provides not only a unique dispute settlement scheme for investment conflicts, but is also designed to increase the availability of information, knowledge, and expertise related to investment by processing and carrying out research, and disseminating pertinent information.<sup>197</sup> MIGA will primarily try to avoid investment disputes and contribute a great deal to their "depoliticization" as a necessary by-product of its day to day activities, limiting decision making and problem resolution to wholly legal and economic criteria.<sup>198</sup> MIGA's forum function offers broad room for cooperation in this respect.

The close connection of these three institutions is also under-

190. *Id.* at 34-35. FIAS advises developing member countries at their request on design and implementation of policies and strategies related to FDI. See J. Voss, PRIMARY RESPONSIBILITY OF MIGA FOR TECHNICAL AND ADVISORY SERVICES RELATED TO FDI (DRAFT) 1 (World Bank Working Paper, 1988) [hereinafter PRIMARY RESPONSIBILITY].

191. Shirley, *Promoting the Private Sector*, 25 Fin. & Dev. 40, 42 (March 1988) (providing a good survey of recent endeavors of the Bank to strengthen the private sector in the Third World).

192. See Petersmann, *supra* note 179, at 260 (IFC approach); Voss, MIGA and the Code of Conduct, 22 THE CTC REPORTER 51 (Autumn 1986) [hereinafter Voss, MIGA and the Code] (MIGA approach).

193. In the GRIP Program the IFC invests the funds provided by the investor in its own name. At the end of an agreed period, the investor has the option to become the full legal and beneficial owner of the shares of the company in which the investment has been made or to be paid back its original capital investment. See Silkenat, GRIP: guaranteed recovery of investment principal 7 INT'L FIN. L.R. 39 (March 1988).

194. *Id.* at 40.

195. C-TH. EBENROTH, CODE OF CONDUCT - ANSATZE ZUR VERTRAGLICHEN GESTALTUNG INTERNATIONALEN, INVESTITIONEN 456 (1987) [hereinafter ANSATZE] (he hints at IFC's strong bargaining position in negotiating inclusion of strict protection standards in the investment contract, to which it, and not the private investor, is a party).

196. See PRIMARY RESPONSIBILITY, *supra* note 190, at 2-3.

197. SHIHATA, *Depoliticization*, *supra* note 12, at 4.

198. *Id.* at 25.

scored by the fact that the Bank's President is *ex officio* non-voting chairman of ICSID's Administrative Council,<sup>199</sup> non-voting Chairman of MIGA's Board of Directors,<sup>200</sup> and non-voting Chairman and President of the Board of Directors of IFC.<sup>201</sup> But MIGA's potential for cooperation with international institutions goes far beyond the World Bank Group itself. The Agency will be able to benefit from the special regional expertise of the, to date, only regional investment protection scheme, the Inter-Arab Investment Guarantee Corporation.<sup>202</sup>

It is still an open question whether and how MIGA will affect the EEC plans, fixed in art. 244 of the Lome III Convention,<sup>203</sup> to establish a multinational investment insurance scheme in cooperation with the ACP states. So far, no definite decision seems to have been made in this direction.<sup>204</sup> If the EEC should eventually step forward with this project, perhaps even structuring it according to the MIGA model,<sup>205</sup> it must be careful not to wind up in ruinous competition with MIGA. This project, however, requires extensive coordination with the Bank, a factor that may considerably delay the EEC plans and might ultimately even lead to its relinquishment.<sup>206</sup>

199. ICSID Convention, *supra* note 7.

200. Convention, *supra* note 2, at art. 32(b). MIGA is also expected to share facilities, personnel and services with the World Bank and IFC, which are all located in Washington, D.C., at 1818 H Street. See OPERATIONAL REGULATIONS, *supra* note 22, at §5.22.

201. Articles of Agreement of the International Finance Corporation, at art. IV, *supra* note 6.

202. See Shihata, *Arab Investment Guarantee Corporation- A Regional Investment Insurance Project*, 6 J. WORLD TRADE L. 185 (1972).

203. Lome III Convention, reprinted in 24 I.L.M. 571 (1985). Articles 243 and 244 provide for conclusion of bilateral and multilateral investment promotion and protection agreements and for the study of a joint ACP-EEC investment guarantee program, complementary to existing national schemes; MIGA is not mentioned in this context. *Id.* at 633. The envisaged scheme might take the form of secondary coverage for the portion of the risk not underwritten by national schemes. See Note, *Promises, Promises: A Critical Analysis Of Lome III's Private Investment Provisions* 9 FORDHAM INT'L L.J. 634, 677 (1986). Pooling of assets of national agencies is also discussed in the EEC. See R. ALLISON, *PROTECTING AGAINST THE EXPROPRIATION RISK IN INVESTING ABROAD*, §3.05 (1988).

204. See *International arrangements and agreements related to transnational corporations: Report of the Secretary-General*, U.N. Doc. E/C.10/5 (1988), at 15 [hereinafter *Report of the Secretary General*].

205. Simon, *Le système conjoint de garantie des investissements CEE/ACP de la convention de Lome III*, 13 DROIT, ET PRATIQUE DU COMMERCE INTERNATIONAL 91, 108 (1987): Il n'est pas, exclu que [MIGA] ne fournisse, sinon un "modele", du moins d'utiles indications pour la mise en place du système conjoint de Lome III".

206. *Id.* at 109-110.

#### E. MIGA AND INVESTMENT STANDARDS

As noted above,<sup>207</sup> the question of including investment standards has always been a dominant and highly controversial issue in the discussions on a multilateral insurance scheme. Every proposal necessarily touches upon the question of investment standards,<sup>208</sup> and consequently, article 12(d) of the Convention, spelling out four eligibility requirements for a guaranteed investment, was one of the most debated provisions in the drafting process.<sup>209</sup> Introducing for the first time a reference to the investment conditions in the host country as an element in MIGA's guarantee decision, it was added only after considerable debate in the last stage of the discussions by the Executive Director's Committee of the Whole in September 1985.<sup>210</sup> While the majority<sup>211</sup> did not want to undermine the negotiations on the United Nations Code of Conduct on Transnational Corporations<sup>212</sup> and impair MIGA's acceptability for capital importing countries, Germany, which had since long opposed the creation of a multilateral scheme,<sup>213</sup> insisted on the inclusion of basic standards or at least guidelines similar to those in art. 240 of the Lome III Convention between the European Community and African, Caribbean and Pacific (ACP) countries of December 1984.<sup>214</sup> Art. 241 of the Convention provides for "fair and equitable treatment", "clear and stable" investment conditions

207. See *supra* note 54 and accompanying text; cf. World Bank Report, *supra* note 55, at 22: "it is . . . possible that the inherent difficulties of reaching agreement in this touchy area could prove insurmountable, precluding establishment of any insurance scheme, even one which is not directly linked with an investment protection code." *Id.*

208. Brewer, *The Investment Guarantee Proposal*, *supra* note 79, at 86. "[s]ome minimal agreement about private investment [standards] is of course necessary even to the most rudimentary guarantee plan." *Id.*

209. Shihata, *Applicable Standards*, *supra* note 64, at 328.

210. *Id.*

211. India and France strongly opposed the inclusion of investment standards. See Golsong interview, *supra* note 61.

212. For the most recent draft, see *supra* note 46.

213. E. SHEIKH, *THE LEGAL REGIME OF FOREIGN PRIVATE INVESTMENT IN THE SUDAN AND SAUDI ARABIA* 191 (1984). Germany did not want to deal with underwriting decisions guided by foreign political and economic interests. *Id.* at 191 n.1.

214. See Interview with M. Von Harpe, Alternate Executive Director, the World Bank, in Washington, D.C. (Mar. 18, 1988); see also Voss, *supra* note 137, at 90 n.11. For the text of the Lome III Convention see *supra* note 203; cf. also Legal Protection as Elements of the Draft Convention of MIGA, Proposal submitted by the German Delegation to the Committee of the Whole on June 10, 1985 (unpublished), which wanted to include standards such as "fair and equitable", "national treatment", "most favored nation treatment", "free transfer of payment that is related to investment." See also Shihata, *Applicable Standards*, *supra* note 64, at 334.

and a "secure" investment climate.<sup>215</sup> This language, committing both EEC and ACP countries, constitutes a major breakthrough and would have been inconceivable in the previous Conventions, reflecting a drastic change in the attitude of the ACP countries towards foreign investment.<sup>216</sup> Similarly, the draft convention, still under negotiation, between the EEC and the Arab League on the reciprocal promotion and protection of investment contains particularly strong investment protection provisions, mainly due to the fact that not only the EEC but also several Arab countries are interested in strong protection for their investment.<sup>217</sup> The final compromise reached in art. 12(d)(iv) and art. 23(b) of the MIGA Convention requires the Agency "to satisfy itself" as to "fair and equitable treatment" and "legal protection" by the host country, and, in case no such protection is assured under a bilateral investment treaty or the domestic law of the host country, MIGA will issue its guarantee only if it reaches an agreement with the member host country pursuant to art. 23(b)(ii).<sup>218</sup>

The German concerns have to be seen in the context of the very successful German investment protection treaty program.<sup>219</sup> The crucial question is whether MIGA, through its findings in evaluating host country investment climates and in its investment agreements pursuant to art. 23(b)(ii),<sup>220</sup> might, in trying to achieve a compromise of differing host and home country opinions, undercut the high investment standards contained in the German and

215. Lomé III Convention, *supra* note 203.

216. Huber, *From Lomé II To Lomé III: Improvements And New Features In The Third ACP-Lomé Convention Signed On 8 December 1984*, 1985 *Legal Issues of European Integration* 1, 19. The previous Conventions contained only rudimentary investment provisions without spelling out any standards.

217. *Report of the Secretary General, supra* note 204, at 5; Burkhardt, *Die Verhandlungen über eine Investitionsschutzkonvention im Rahmen des Euro-Arabischen Dialogs*, 29 *RECHT DER INTERNATIONALEN WIRTSCHAFT* 164, 165 (1983); the situation was atypical since it lacked the typical home-host country confrontation like, e.g., the Lomé negotiations.

218. The link between guarantee coverage and a preceding agreement between MIGA and the respective host country is not explicitly stated in the Convention, but is fixed in para. 21 of the *Commentary, supra* note 19, at 201; *OPERATIONAL REGULATIONS, supra* note 22 at 3.17; see also, the Preamble of the Convention, *supra* note 2, at 1605 (stressing MIGA's purpose to enhance the flow of investment "on the basis of fair and equitable standards for the treatment of foreign investment").

219. So far, Germany has concluded over 60 investment promotion treaties, their principal purpose being to create a framework for the free flow of investments between the countries, to fill the gaps left by national investment laws of the host state and to protect against unilateral alteration of these laws. See *ANSATZ, supra* note 195, at 60.

220. These agreements might contain substantive investment protection standards. See *OPERATIONAL REGULATIONS, supra* note 22, §3.33(i).

most European treaties.<sup>221</sup> These treaties contain such standards as "fair and equitable treatment," "most favored nation," and "national treatment."<sup>222</sup> This might eventually lead to a substantial change in the international law of investment protection, which is strongly influenced by those treaties,<sup>223</sup> and might even induce host countries to renegotiate their treaties to adjust them to the new, lower standards.<sup>224</sup> This could ultimately lead to a weakening of national investment insurance agencies, which, to a great extent, derive their efficiency from a strong interaction with the respective investment protection treaties<sup>225</sup> and the high protection standards included therein. These standards lower the risk of expropriation,

221. See *CHANCES AND RISKS, supra* note 75, at 171, 174-175 (Comments of Kramer, Wecker and Golsong). Similar concerns have been raised by European countries in the context of EEC investment protection agreements. See Voss, *The Protection And Promotion Of European Private Investment In Developing Countries: An Approach Towards A Concept For A European Policy On Foreign Investment, A German Contribution*, 18 *COMMON MKT. L. REV.* 363, 367 (1981). For the Euro-Arab Draft Convention see Burkhardt, *supra* note 217, at 167.

222. See *ANSATZ, supra* note 195, at 449. The French treaties also refer to "protection et securite pleines et entieres." See Juillard, *Le reseau francais des conventions bilaterales d'investissement: a la recherche d'un droit oerdu*, 13 *DRIFT ET PRATIQUE DU COMMERCE INTERNATIONAL* 9, 39-41 (1987). A typical clause is contained in art. 2 of the Swiss-Sudan BIT: "treatment shall be at least equal to that granted by each contracting party to its own nationals or companies, or equal to the treatment to nationals or companies of the most favored nation, if the latter is more favorable." cited in *SHIKH, supra* note 213, at 113. The German treaty (art. 8(2)) also includes an "umbrella clause" in which the host state promises to respect contractual arrangements with the investor, thus transferring the contractual obligations into treaty obligations; apart from these protection standards, the treaties also include references to compensation in case of expropriation, most of them referring to the "Hull" formula of "prompt, adequate and effective" or "just" compensation. See Shihata, *Origins, supra* note 2, at 239.

223. Bilateral investment treaties, while frequently referring to international law, (see art. 2(2) of the American model treaty; art. 3 of the French model treaty) are *vice versa* influencing the customary law in this field. See Juillard, *supra* note 222, at 49, (vecteur d'internationalite) (maintaining that such treaties do not actually form customary international law due to their limited geographic distribution); Cf. *ANSATZ, supra* note 195, at 450. "Through the most favored nation treatment, the bilaterally granted protection level is slowly transferred to and stabilized on the multinational plane" *Id.*; Shihata, *Origins, supra* note 2, at 238-239 (limited to the compensation aspect).

224. See *CHANCES AND RISKS, supra* note 75, at 175 (Wecker Comment).

225. See Golsong, *Proceedings, Seventy-Seventh Annual Meeting*, Am. Soc. Int'l L. 306 (1983); see Juillard, *supra* note 222, at 58. Note that the American Investment Guarantee Agreements contain no substantive standards but deal only with procedural aspects of the insurance program, subrogation and arbitration. The American Bilateral Investment Treaty Program, in effect since 1982, has been criticized for the many exceptions to the most favored nation and national treatment contained in the Annex of the treaties even allowing future sectoral exceptions. See Golsong, *Proceedings, Seventy-Seventh Annual Meeting*, Am. Soc. Int'l L. 306 (1983). The program has been halted pending Senate action on the treaties so far negotiated. See Minutes of the NFTC Investment Committee session of January 20, 1988, at 2.

hence ease the burden of investment insurance programs on the home country budget and make it easier to issue guarantees for investments in those host countries.<sup>226</sup> Since host countries are now attracting FDI to help their economies to recover, the national schemes also constitute an important leverage in negotiating a bilateral investment protection treaty.<sup>227</sup>

MIGA's potential to influence the international law in this field is certainly high, especially since the Operational Regulations empower the Agency to ascertain adequate legal protection "in the light of the consistency of the law and practice of the host country with international law"<sup>228</sup> (emphasis added). MIGA's determination of an expropriation action, especially in the controversial field of creeping expropriation, can also have an impact on international law and the bilateral investment protection treaties. However, the drafters of the Convention were well aware of this danger and incorporated adequate safeguards. Assessment of investment conditions will be conducted in strict confidentiality.<sup>229</sup> In defining an expropriation measure, the Agency is to refrain from any measures which might prejudice the rights of any member country or of any investor under "bilateral investment treaties, other treaties and international law."<sup>230</sup> Furthermore, the most favored nation clause in art. 23(b)(ii)<sup>231</sup> requires the Agency to meet the aforementioned high standards in its agreements. In the case of countries that have not signed any investment treaty, home member countries with particularly high investment standards may veto the conclusion of an agreement, because a special majority of the board is required by art. 23(b)(i). In its starting phase, the Agency will adopt a very cautious policy in order not to bypass these built-in safeguards.<sup>232</sup>

226. SALOW, INVESTITIONSSCHUTZ, *supra* note 176, at 55, 58; See also § 2(a) of the German General Conditions for Underwriting Capital Investment Abroad (July 1987) reprinted in *id.* at 248 (expressly refers to a bilateral investment treaty as a precondition for coverage). *Vice versa*, some of these treaties now refer to government guarantees for German investments in the host country. *Id.* at 54.

227. Juillard, *supra* note 222, at 10, 58.

228. OPERATIONAL REGULATIONS, *supra* note 22, at § 3.16.

229. *Id.*

230. *Commentary*, *supra* note 19, at 200, para. 14; OPERATIONAL REGULATIONS, *supra* note 22, at § 1.38.

231. Convention, *supra* note 2. With respect to investment guaranteed by it, the Agency has to have treatment "at least as favorable as that agreed by the member concerned for the most favored investment guarantee agency or State in an agreement relating to investment. . . ." *Id.* at art. 23(b)(ii).

232. Shihata, *Origins*, *supra* note 2, at 235. "MIGA should not be influenced by its self-serving views on what [the] law should be or by its interest in securing maximum protection for the investment to be guaranteed. . . . MIGA is best advised to avoid in its formative

In the field of the new, contractual investment forms, MIGA is not in danger of running counter to German treaty policy since German treaties do not cover these new forms of FDI.<sup>233</sup>

Although the German Delegation had to make concessions with respect to their initial comprehensive proposal, the present text of the standards provision is still viewed as the most important and innovative feature of the operational part of the Convention,<sup>234</sup> since for the first time, a multilateral investment protection convention makes mention of at least some rudimentary<sup>235</sup> standards applicable to foreign investment in host countries. The requirement of adequate legal protection is, for example, also included in the provisions for granting investment guarantees in the German "Bundeshaushaltsgesetz" (Federal Budget Law).<sup>236</sup> It has to be born in mind, however, that contrary to the German proposal, the Convention does not spell out actual obligations for host countries to accord such investments fair and equitable treatment. Rather, it creates an indirect, subtle incentive for capital importing countries to comply with these standards in order to attract investment guaranteed by MIGA. Consent to the inclusion of "hard" investment standards was impossible to obtain in light of the various doctrinal, psychological and philosophical codes involved in the formulation of Codes of Conduct for Multilateral Enterprises. As a consequence, these codes<sup>237</sup> were adopted as "voluntary codes" (soft law) not intended to be legally binding or enforceable upon the parties.<sup>238</sup> The same concerns led to the failure of efforts to

years imposing a codification of customary law in this controversial matter." *Id.* at 245.

233. ANSATZE, *supra* note 195, at 446.

234. Von Harpe Interview, *supra* note 214.

235. Terms such as "equitable" and "fair" are admittedly rather broad, but in view of the controversy around the issue and the need for flexibility, the formula is probably the best suited; the formula constitutes the minimum standard of international law and serves to interpret and correct bilateral treaties as well as to fill their gaps. See ANSATZE, *supra* note 195, at 449.

236. See Kopernick, *Das Instrumentarium des Bundes zur Förderung privater Direktinvestitionen in Entwicklungslandern*, 25 RECHT DER INTERNATIONALEN WIRTSCHAFT 672 (1979).

237. The term, "codes of conduct", came into vogue in the 1970s and is used to denote written sets of rules for transnational business relations set up not only by states and inter-governmental organizations but also by private companies and organizations, irrespective of their legal nature as treaties, declarations or guidelines and whether binding and enforceable or not, see Petersmann, *Codes of Conduct in 7 ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW* 28, 30-32 (R. Bernhardt ed. 1984).

238. See, e.g., 1972 OECD Declaration On International Investment and Multinational Enterprises (as reviewed in 1979 and 1984); *The Guidelines for Multinational Enterprises*, at ¶ 6. Which provide: "observance of the guidelines is voluntary and legally not

conclude international investment protection conventions like the Abs-Shawcross Draft Convention on the Protection of Investment Abroad.<sup>339</sup>

The solution found by the drafters in no way interferes with the negotiations on the United Nations Code of Conduct because MIGA focuses on the specific guaranteed investment, which requires a case by case determination of the investment condition for that particular investment. Whereas the Code spells out *uniform* investment protection rules for all investments worldwide.<sup>340</sup> Furthermore, the standard of "fair and equitable treatment" of transnational corporations is one of the few issues in the negotiations of the treatment part of the Code of Conduct that has been virtually agreed upon.<sup>341</sup> Therefore, friction and conflict with respect to these standards is highly unlikely, and the Code might even help to clarify the applicable standards through the provision of a stable, predictable and transparent frame work.<sup>342</sup>

On the other hand, MIGA may, as was already expected from earlier proposals,<sup>343</sup> promote final agreement on the Code.<sup>344</sup> Through its underwriting practice, which requires the Agency to communicate with the host governments to enable improvement of their investment conditions,<sup>345</sup> the Agency may help reach a general consensus on the investment standards needed to resolve the

enforceable." *Id.*; see also the 1977 ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, ILO Doc. Gn 204 14, U.N. Doc. E/C.10/AC.2/3 (Annex II), reprinted in 17 I.L.M. 422 (1978). The provisions are recommended "to [be] observe[d] on a voluntary basis." *Id.* at ¶ 7. For an overview on these and other codes, see Horn, *International Rules for Multinational Enterprises: The ICC, OECD and ILO Initiatives*, 30 AM. U. L. REV. 923 (1981).

239. Reprinted in J. PUB. L. 116 (1960); cf. SCHWARZENBERGER, PROTECTION OF INVESTMENT IN INTERNATIONAL LAW 109-34 (1969).

240. Voss, *MIGA and The Code*, supra note 192, at 53; Shihata, *Applicable Standards*, supra note 64, at 339.

241. UNCTC CURRENT STUDIES, THE UN CODE OF CONDUCT ON TRANSNATIONAL CORPORATIONS 39 (1986). It is understood that "fair and equitable" excludes unfair discrimination. *Id.* at 18.

242. For the expectations of the World Bank in this respect, see QUESTIONS AND ANSWERS, supra note 10, at 53.

243. Cf. supra note 54; cf. also Brewer, *The Investment Guarantee Proposal*, supra note 79, at 86. "Taken as a whole, the treaty program of an international guarantee agency could make an important contribution to international good behavior towards investment property. It will require delicate guidance by its sponsors so that everything is not lost by too much being sought." Similar expectations were connected with the execution of investment protection treaties and the various already existing "voluntary" codes on multinational enterprises. See Horn, supra note 238, at 938-939.

244. Voss, *MIGA and The Code*, supra note 192, at 54.

245. Operational Regulations, supra note 22, at §3.16.

remaining controversial issues in the Code negotiations. The possible interplay of the Code and MIGA - both offering transnational legal frameworks for the development and implementation of generally accepted investment protection standards - may well lead, as did the Codes negotiated during the GATT Tokyo Round in the field of tariff and non tariff trade barriers, to a further reduction of investment barriers, a process of "generalization and harmonization" of investment protection rules,<sup>246</sup> and ultimately to a "GATT for international investment."<sup>247</sup> This becomes even more important, when one takes into account that inclusion of investment issues in the GATT system seems far from achievable.<sup>248</sup> The development of a separate protection and promotion scheme in the field of international investment through the Code and MIGA might finally close the gap between both fields. It is in this context that the Code and the MIGA Convention may well be expected to be "complementary and mutually supportive."<sup>249</sup>

#### F. MIGA'S INFLUENCE ON INVESTOR BEHAVIOR

Having analyzed MIGA's prospective beneficial impact on the development process, and its acceptability for host and home countries, the question remains, whether an international investment guarantee scheme actually attracts investors to carry out investments that would not otherwise be made, in other words, will MIGA increase "additionality"? Like every business decision, an investment decision is based on a complex basis of commercial, economic and financial factors. Each decision is basically an "exer-

246. Juilliard, supra note 222, at 59 (hinting at MIGA's mandate to promote the conclusion of investment protection treaties among its member states, art. 23(b)(iii) of the Convention, which are likely to contain the same clauses as the already existing treaties).

247. See UN Doc E/CIO/5 (1988), at 19: "Through the complex and confused network of arrangements at different levels, with varying participants and of differing degrees of binding force, a body of principles concerning the conduct and treatment of transnational corporations is beginning to emerge. . . ." Both the U.N. Code and MIGA have been paralleled to the GATT system of free trade promotion and protection. See Ebenroth, Karl, *International Investment Contracts and the Debt Crisis*, 22 INT'L LAW. 179, 188 (1988); see The U.N. Code and Voss, supra note 137, at 91 n.4 (for MIGA); cf. Dolzer, *Ein GATT für internationale Investitionen?*, FRANKFURTER ALLGEMEINE ZEITUNG, June 25, 1986, at 24, col. 2.

248. McCulloch, *Linking Negotiations On Trade And Foreign Direct Investment in THE MULTINATIONAL CORPORATIONS OF THE 1980s*, 348 (Kindleberger, Audretsch eds. 1983). "To extend the GATT fragile achievements in this difficult area [i.e. trade barriers] to a set of issues as sensitive and politically explosive as host country regulation of FDI could be premature and counterproductive." *Id.*

249. Voss, supra note 192, at 55.

cise in prediction, with the strongest pressures upon management to reduce the unknown to acceptable levels, and the unknowns of non business, i.e. political risks, will often exceed the acceptable limits."<sup>250</sup> Risk in financial theory represents the variability of returns in relationship to the degree of risk and any perceived improvement in the risk profile is bound to lower the return required by the investor to undertake the investment. This is commonly referred to as "hurdle rate reduction".<sup>251</sup>

In the past decade, however, host country tactics and investor perspective have changed from outright takeover of foreign owned enterprises to future rebargaining, thus forcing initially favorable investment contracts to be renegotiated to the disadvantage of the investor.<sup>252</sup> This is especially true for the extractive natural resources industry.<sup>253</sup> Developing countries today, independent from their ideological orientation, tend to change the rules of the game, once appreciable sunk costs are involved.<sup>254</sup> The discussion among foreign investors in Chile in early 1988<sup>255</sup> is a typical example of this new viewpoint. Several studies indicate that this perception of political risk constitutes a major deterrent to private foreign investment in developing countries, even though the actual adjustment measures vary from industry to industry. Some industries, especially those that by their nature require large capital investment, long gestation periods, and which are physically tied to a given location, tend to be more susceptible to non-commercial risks than others.<sup>256</sup>

A good measurement for the impact of political risk percep-

250. Spofford, *Social Conflict and the Protection of Foreign Investment*, in SELECTED READINGS ON PROTECTION BY LAW OF PRIVATE FOREIGN INVESTMENT 653, 656 (1964).

251. See QUESTIONS AND ANSWERS, *supra* note 10, at 15.

252. R. VERNON, SOVEREIGNTY AT BAY 47 (1971) ("obsolescing bargaining").

253. FERNANDEZ, *supra* note 25, at 26. The large sunk costs involved constitute an important "hostage" for the host country. *Id.*; Cf. E. SCHANZ, INVESTITIONSVERTRÄGE IM INTERNATIONALEN WIRTSCHAFTSRECHT 46-49 (1986).

254. McCullough, *Linking Negotiations On Trade And Foreign Direct Investment in THE MULTINATIONAL CORPORATIONS OF THE 1980s*, at 334 (Kindleberger, Audretsch eds. 1983).

255. The plebiscite for a new president planned by the Chilean military administration, which has authorized \$1.4 billion of overseas investment in the first three months of 1988, was not deemed to affect the overall economic policy; however, Chile's largest political party, together with some smaller groups, had presented a paper which proposes restricting new investment and reserves the right to review existing contracts; the opposition is highly skeptical of foreign investment both for ideological reasons and on the basis of nationalism. See Spooner, *Overseas Investors in Chile are Hedging Their Political Bets*, *Fin. Times*, Apr. 13, 1988, at 4, col. 2.

256. Shihata, *Factors*, *supra* note 29, at 687.

tion is the ratio of productivity and investment in typical home and host countries. Although the "incremental capital output ratio (ICOR)"<sup>257</sup> over the period of 1970-1982 was roughly 7:1 in developed countries and only 5:1 in developing countries, thus indicating a higher productivity in the latter countries, the FDI share of these countries stagnated in the same period to below 30 percent.<sup>258</sup> Concern about non-commercial political risk is also reflected in the growing market for private political risk forecasting services<sup>259</sup> and in the flourishing new science of political risk study and assessment.<sup>260</sup> In view of MIGA's broad risk coverage, investors provided with a MIGA guarantee can well be expected to reduce their hurdle rates considerably in return for the diminished risk. This is especially true for MIGA's innovative breach of contract coverage which aims at the problem of "obsolescing bargaining."<sup>261</sup> As the premiums would reduce the return from investment, direct additionality will ensue whenever the reduction in the hurdle rate exceeded the premium.<sup>262</sup> In addition to this "project specific" or "direct" additionality MIGA's guarantees will also increase "indirect" additionality, meaning that the improvement of the overall risk portfolio through guarantee coverage will allow investors to invest more capital in developing countries or that guaranteed investment will attract additional investment, domestic or foreign, of suppliers or customer.<sup>263</sup> Qualitatively, MIGA's investment guarantees may encourage investors to change the form of

257. ICOR measures the amount of investment capital needed to produce one additional unit of extra gross domestic product and hence reflects the productivity of capital. See PROSPECTS, *supra* note 10, at 6.

258. QUESTIONS AND ANSWERS, *supra* note 10, at 14.

259. A number of consulting firms provide these services, see e.g., Frost and Sullivan, the WORLD Political Risk Forecast (WPRF) (quantitative and qualitative data on approximately 80 countries worldwide through on-line computer system); see Beri Ltd., Business Environment Risk Index (BERI) (quarterly reports, covering fewer countries); see Data Resources Inc., POLICON (evaluates political risk on a country, group and issue specific basis). Many U.S. companies have institutionalized risk assessment systems like the ASPRO/SPAIR of Shell Oil Company, focusing on risk leading to a unilateral modification of the initial contract, so that return is inadequate and risks constraining the free repatriation of funds. See generally Zimmerman, *Political Risk Assessment and the Expanding Role of the International Practitioner*, 11 SUFFOLK TRANSNAT'L L.J. 29-34 (1987).

260. See Bergner, *Political Risk Analysis: An Asset Now, Soon a Must*, 27 PUB. REL. Q. 28 (1982); see also Vagta, *Foreign Investment Risk Reconsidered: The View from the 1980s*, 2 ICSID REVIEW FOREIGN INVESTMENT L.J. 1 (1987) (ICSID Review).

261. Shihata, *Origins*, *supra* note 2, at 131.

262. See Shihata, *Factors*, *supra* note 29, at 689.

263. PROSPECTS, *supra* note 10, at 5 citing Arthur Young & Co., A Study of Additionality of OPIC Assistance to U.S. Private Direct Investment.

their investment, thus increasing the benefits for the host country, e.g. substituting equity for credit, accepting longer payback periods or generally extending the time of investment.<sup>264</sup> Host countries might hence be in a better position to attract small companies, which can't afford investment at high risk but are oftentimes better able to offer contractual arrangements and technology that suits the needs of developing countries.<sup>265</sup> Finally, one should not underestimate the more psychological, confidence building effect that MIGA's guarantee extension may have on other investors, inducing them to enter the market *without* a guarantee. This will be the indicator par excellence for MIGA's ultimate improvement of the global investment environment and total success.

#### G. MIGA AND U.S. POLICY IMPLICATIONS - A SETBACK ?

Prior to the ratification by the United States on April 12, 1988, the MIGA project had long been in danger of being frustrated by objections of one of its most important member countries. The United States, whose involvement was a key factor in the establishment of the Convention,<sup>266</sup> signed on June 18, 1986, but ratification and ultimate pay in of the U.S. capital contribution of \$44 million met strong opposition from U.S. labor unions. They were concerned that guaranteed investment in Third World subsidiaries of U.S. firms might export jobs and undermine the economic basis of the United States.<sup>267</sup> Moreover, they insisted on internationally recognized worker's rights determination in those subsidiaries.<sup>268</sup> Both aspects are in fact required as part of the evaluation for insurance from OPIC<sup>269</sup> and Workers' Rights deter-

264. See *id.*; see also Shihata, *Factors*, *supra* note 29, at 687.

265. See Shihata, *Factors*, *supra* note 29, at 692; see also Voss, *Interdependencies*, *supra* note 23, at 691.

266. See *L.A. Times*, June 19, 1986, § 4, at 7, col. 1.

267. See Moran, *Shaping a Future*, *supra* note 36, at 123-24; MIGA BACKGROUND 12/14/1987, HOUSE BANKING COMMITTEE PAPER (on file with the author); the same concern is raised in the context, of the Mexican Maquiladora, Program, Tarbox, *An Investor's Introduction to Mexico's Maquiladora Program*, 22 *Tex. Int'l L.J.* 109, 113 (1987).

268. See MIGA Background, *supra* note 267; U.S. labor unions are particularly dissatisfied with the lacking enforcement mechanisms in ILO Charters and feel thus entitled to watch the obedience of international labor standards in the Third World, Speech of Lane Kirkland, President AFL-CIO on "Labor Issues of the Eighties", delivered at the U. Va. Darden Business School (March 28, 1988).

269. See 22 U.S.C.A. §2199(h),(i) (1979 & Supp. 1988); see 22 U.S.C.A. §2191(2)(k)(1) (1979 & Supp. 1988); 22 U.S.C. 2191a(a)(1) (Supp. 1986). OPIC follows the policy of the U.S. Trade Representative; in 1987 OPIC suspended its programs in Romania, Nicaragua, Paraguay and Ethiopia; however, these provisions do not constitute major obstacles to

mination has been, since 1984, also included in the Generalized System of Preferences of the 1974 Trade Act.<sup>270</sup> In addition, the United States were concerned that guaranteed foreign investment would result in exports to the United States, thereby causing further loss of jobs and that MIGA investment would produce competition for U.S. manufacturers in Third World markets.<sup>271</sup> It was obvious that proposals in Congress which wanted to link U.S. accession to MIGA to the above conditions and which even provided for other countries to ratify those conditions so that they would not just apply to the United States<sup>272</sup> made U.S. accession impossible.<sup>273</sup> It would have required renegotiating MIGA's operational framework on issues that seemed to have already been resolved, namely the inclusion of investment-related labor standards in the Convention.<sup>274</sup> The final compromise reached in the International Financial Institutions Act<sup>275</sup> contains no conditions but instructs the U.S. Director on MIGA's Board to seek adoption of policies and procedures which will prevent issuance of guarantees for investments with the negative economic and social impacts outlined above,<sup>276</sup> and to oppose any such guarantee.<sup>277</sup> The Board of Direc-

OPIC's work. Interview with Robert O'Sullivan, Assistant General Counsel for Claims at OPIC (July 22, 1988).

270. 19 U.S.C.A. §2462b (1982).

271. See MIGA BACKGROUND, *supra* note 267.

272. This was the basic content of the "Sanford" Amendment, see Daily Report For Executives, June 5, 1987, at L-10.

273. U.S. Treasury Secretary James A. Baker III expressed this concern in a letter to the President of the U.S. AFL-CIO: "we cannot dictate the policies and operating guidelines of a multilateral organization. . . [this] would result in the U.S. not being able to join MIGA, and thus could effectively prevent MIGA from coming into existence" (emphasis added); see also Talking Points, Paper of the House Banking Committee: "The Senate Version effectively kills U.S. participation."

274. For this issue see *supra* note 207 and accompanying text.

275. Pub. L. 100-202, §101(e), 22 U.S.C.A. §290k (1988).

276. See 22 U.S.C.A. §290k-2 (Supp. 1988). This section refers to "any proposed investment that would:

(1) be in any country which has not taken or is not taking steps to afford internationally recognized workers' rights to workers in that country;

(2) be subject to trade-distorting performance requirements imposed by the host country that are likely to result in a significant net reduction in--

(A) employment in the United States or other member countries; or

(B) other trade benefits likely to accrue to the United States or other member countries from the investment; or

(3) increase a country's productive capacity in an industry already facing excess worldwide capacity for the same similar or competing product, and cause substantial injury to producers of such product in another member country. *Id.*

277. See 22 U.S.C.A. §290k-3. The pay-in of the U.S. capital share was also linked to these conditions.

tors, at its first meeting on June 22, 1988, adopted the Operational Regulations without change but issued a policy statement that in its underwriting, MIGA will adhere to the general World Bank policy.<sup>278</sup> MIGA's President, who is in charge of the day-to-day approval of guarantees, will have to adhere to this policy statement according to § 3.35 of the Operational Regulations.<sup>279</sup>

#### H. CONCLUSION

After almost 40 years of more or less intensive discussions in the World Bank and worldwide investment and business community, during which several promising proposals have been made and rejected, MIGA has good prospects to become the first viable world-wide operating transnational investment insurance scheme.

The new Agency can benefit from the newly developed international consensus on the necessity and benefits of foreign investment in developing countries. The drafters have succeeded in removing the obstacles that prevented agreement on previous proposals. The already widespread acceptance of MIGA among both capital exporting and importing countries shows that the Convention removes investment discussions and decisions from the doctrinal stage where they have been trapped in past decades.

MIGA will make a major contribution to removing the relics of deep rooted antagonism between developed and developing countries and may, at least in this respect, put an end to the New International Economic Order.<sup>280</sup> The perceptions encountered in international trade, where many developing countries still think that GATT, in spite of its one country/one vote structure is a club for the rich nations,<sup>281</sup> can be eliminated through MIGA's unique financial and organizational structure. Its position as an international financial institution, affiliated with the World Bank and sharing the Bank's excellent reputation in the investment community, may induce developing countries to avoid investment disputes and confrontation with an international organization all the

278. Interview with Jurgen Voss at the World Bank (July 19, 1988).

279. Section 3.35 states in pertinent part: "The president shall . . . only approve contracts of guarantees which are consistent with the limitations and priorities approved by the Board in . . . future guidelines which the Board may issue from time to time." OPERATIONAL REGULATIONS, *supra* note 22, at §3.35.

280. See Letter from Professor Detlev Vagts, Harvard Law School, to the author (July 21, 1988).

281. See J. JACKSON & W. DAVEY, LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 1139 (2nd ed. 1986).

more since these countries have a substantial financial stake in MIGA. Even if investment disputes should arise, MIGA has an enormous potential to serve as a depoliticizing factor.

Together with the U.N. Code of Conduct for Multinational Enterprises, which has been under negotiation for more than ten years, MIGA may complement bilateral investment treaties without impairing their effectiveness and may ultimately help to establish a basic framework for worldwide investment standards on the international plane, which would introduce more stability, predictability and certainty into the investment process. Though by no means a panacea for the Third World economic crisis, MIGA is likely to make a major contribution to recovery of that region, a basic prerequisite for restoration of creditworthiness and resumption of commercial lending. Through its screening policy, MIGA will filter out those investments with no substantial developmental benefits for the host country and might hence improve the overall investment pattern in the Third World. Later, MIGA's coverage might even be expanded to cover straight project loans, in response to a Japanese proposal,<sup>282</sup> and debt-equity swap transactions.<sup>283</sup>

The individual investor will greatly benefit from MIGA's flexible underwriting policy and premium structure, enabling the agency to tailor the insurance coverage according to his specific needs. The ratification by the United States and the United Kingdom, with a combined capital share of over 25 percent, sent an important signal to other signatory states, and as of July 6, 1988, thirteen other states have ratified the Convention, China<sup>284</sup> being the most important one. Still, the MIGA project has to overcome major challenges. The principal Latin American debtor countries,

282. See *Statement of World Bank President Barber Conable*, Wash. Post, Apr. 13, 1988, § F, at 1, col. 1. The Agency might administer such a special fund under its ancillary powers of art. 2(c) provided that such loans are related to "a specific investment covered or to be covered by the Agency." Convention, *supra* note 2, at art. 12(b); cf. Shihata, *Origins*, *supra* note 2, at 115, 209.

283. See *Remarks of Ibrahim Shihata before the international group at Arent, Fox, Kintner, Plotkin & Kahn*, Washington, D.C. (June 29, 1988); since 1987, OPIC enures debt-equity swap transactions and has insured four U.S. companies covering over \$118 million of converted debt, OPIC ANNUAL REPORT 1987, at 17; however, such swaps may also have anti-developmental, especially inflationary effects.

284. The People's Republic of China signed on April 28, 1988 and ratified only two days later, see *List*, *supra* note 76; the quick ratification is in line with its progressive pro-investment policy. China has concluded several investment protection treaties, one of the first with West Germany in 1983 (BGBl. 1985 Teil II, 30), the most recent one with Austria in 1985, and also an investment guarantee agreement with the U.S. (32 U.S.T.S. 4010 1979-1980). In 1987, OPIC insured 9 projects in China with a total value of \$21,476,270. See OPIC Annual Report 1987, at 26-29.

Brazil and Argentina, have neither signed nor ratified the Convention. Without them, the aspired-to equilibrium between North and South will be hard to obtain. It also remains to be seen how the World Bank Group and MIGA, in particular, will be influenced or restructured if the Soviet Union, and with it other East Block countries, should join the Bank.<sup>285</sup>

So far, several preliminary applications for insurance have been filed and other investors have already indicated their interest in the MIGA program.<sup>286</sup> If all goes well, MIGA might well make its first underwriting decision before the end of the year. From the present perspective, one might thus state with confidence that MIGA "might well be the most important and most constructive initiative in favor of development in the past years."<sup>287</sup>

285. Experts expect the Soviet Union to join the Bank in the near future. See Golsong interview, *supra* note 61. The U.S.S.R. has since long been trying to build closer ties to the western banking community, the latest example being a \$270 million bond offering to international investors, placed with an international banking consortium. See N.Y. Times, July 27, 1988, § D, at 15, col. 3.

286. Interview with Jurgen Voss at the World Bank (July 19, 1988); these preliminary applications, however, should not be overestimated, since they are not binding upon MIGA or the investor and serve only to secure eligibility if the investment has to be made during the registration process, see Preliminary Application For Guarantee, draft reprinted in Shihata, *Origins*, *supra* note 2, at 498. Interested investors may obtain information from The World Bank, MIGA Executive Vice-President, 1818 H Street, N.W., Washington, D.C. 20433, Telex: ITT 440098.

287. Touscoz, *supra* note 77, at 332.

## NOTES

### IN SEARCH OF A STOLEN MASTERPIECE: THE CAUSES AND REMEDIES OF INTERNATIONAL ART THEFT

A masterpiece of art has in the mind a fixed place in the chain of being . . . .

Ralph Waldo Emerson

#### I. INTRODUCTION

On February 8, 1988, one of New York City's largest art thefts took place at the Colnaghi Gallery on the upper east side of Manhattan.<sup>1</sup> The thieves broke into the gallery through an unalarmed skylight on the roof of the building.<sup>2</sup> During the course of the robbery, the thieves set off alarms within the gallery, but they were able to escape before the police arrived.<sup>3</sup> The thieves escaped with \$6 million worth of small Italian masterpieces that they cut out of the frames.<sup>4</sup>

Art theft is a problem that has been prevalent in society for decades, and the number and magnitude of thefts will continue to increase as long as the demand for art continues to grow.<sup>5</sup> At the present time, art thievery has become the second largest international criminal activity after narcotics.<sup>6</sup> Countries that have not been bothered by art theft in the past find it an increasing problem.<sup>7</sup> The lack of proper security caused by insufficient funds in

1. See Pitt, \$6 million in Art Stolen from Gallery on the Upper East Side, N.Y. Times, Feb. 10, 1988, at B1, col. 2 [hereinafter Pitt].

2. See *id.*

3. See *id.*

4. See *id.*

5. See Greenberg, *Smuggled Treasures*, ART AND ANTIQUES 81, 83 (Summ. 1986). For example, in 1982, there were 2981 reported art thefts and 283 recoveries. Whereas, in 1984, there were 4157 reported art thefts and 160 recoveries. See *id.* The increase in art theft has resulted from the increase in the average price of an artwork which has doubled over the past few months. Paintings selling for several million dollars have become routine. See Cox, *Art Prices Continue Their Trip to the Stars, Belying Predictions About a Market Fall*, Wall St. J., May 19, 1988, at 37, col. 4.

6. See Esterow, *Confessions of an Art Cop*, ARTNEWS 134, 137 (May 1988).

7. For example, Holland reported one of its first major art thefts on May 20, 1988. The theft occurred at the Municipal Museum in Amsterdam. An expert at Christie's has estimated the value of the stolen paintings at \$10 million. See *Dutch Masterpieces Stolen*, N.Y.