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PhD Thesis

The Role and Nature of Export Credit Agencies in Foreign Direct Investment:
Home and Host States' Coordination and the Problem of Political and Com-
mercial Risks Distinguished

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Declaration

I, Wael Saghir, declare that this thesis is my own work. It has not been previously included in a thesis, dissertation or report submitted to this university or to any other institution for a degree, diploma or other academic or non-academic qualification, except where due acknowledgment is made.

Signed WAEL AHAMD SAGHIR

Abstract

Each state in order to promote foreign investment, and to stimulate its economy, offers loans and insurance services against certain risks to investors willing to invest abroad. For that purpose, Export Credit Agencies (ECAs) have been established. Their purpose is to facilitate foreign investment and to cover and insure against certain political and financial risks that a foreign investor may face in the host state.

Since political instability and the fear of expropriation in some developing states pose grave risks to foreign investors, along with the behavior of the financial markets of these states, the need to insure against such risks is something to be considered in order to encourage investments in these regions. ECAs have also been established to assist foreign investors conducting their business in a given market through granting them loans, guarantees and insurance against certain risks encountered by investors. These loans to foreign investors are granted in order to ease their entry into the foreign market so that the recipient market benefits from the expertise and technology that the foreign investor possess.

The study will start with introducing a comprehensive definition for investment in light of the suggested view to what foreign investment stands for. It will highlight the difference between direct and indirect investments as well. Then it will move on to discuss entry of investors to foreign markets and it will discuss the open-door and closed-door approaches in order to identify the various risks associated with such investments. The thesis will emphasize on the need to have a more detailed approach towards investment-risks based on the five-risk distinction rather the classic three-risk approach. This will be of importance especially since the borderline between these risks interlink at times. The thesis emphasizes on the changing role of risks

through giving an example of how new risks are emerging.

The study will examine the harmonization of both host and home states' measures enacted to protect foreign investments. It will examine the freedom and restrictions of entry into foreign markets by investors and the various types of risks, including the political, financial and commercial risks, that such investors may face in order to sort out the role ECAs play in that respect. It will suggest a new approach to foreign investment protection based on a pre-investment and a post-investment protection.

The thesis will study the coordination between the home and host states in the protection of foreign investors through IIAs, BITs, MITs and other forms of cooperation. It will also introduce the role that the home state plays in the protection of its investors through diplomatic protection and through national unilateral and multilateral investment insurance programs such as those of ECAs and the MIGA. It will show how the role of ECAs complements that of IIAs in protecting foreign investors. The study will include an analysis of the nature of such agencies and a comparison of the role that those agencies play, that of MIGA and, that of the private insurance companies in insuring against various investment related risks.

It will compare the various insurance programs offered by ECAs, MIGA and insurance companies and will discuss how ECAs are managed, their corporate governance and how their services may differ from one agency to another (and not necessarily offer a universal set of insurance services).

The thesis will focus on the role of the home state's protection through investment risk insurance provided through ECAs. Basically, it will emphasize on political risk insurance (PRI)

available to investors through ECAs, MIGA and other insurance providers. For this, the thesis will have a comparative approach where it will study different regulations of a number of states in North America, Latin America, Europe, Middle East and in China including any notable regional cooperation's between various states.

It will conclude that even with the existence of the safeguard means presented in this research, these are not enough to eliminate the risks faced by investors rather these are risk-reduction mechanisms and the success of such reduction depends upon a particular investor's due diligence and proper analysis of the foreign market and in knowing the protection limits present in laws and regulations and in international agreements.

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List of Abbreviations

American International Group, Inc.	<i>AIG</i>
Andean Common Market	<i>ANCOM</i>
Andean Community of Nations	<i>CAN</i>
Association of Southeast Asian Nations	<i>ASEAN</i>
Berne Union	<i>BU</i>
Bilateral Investment Treaty	<i>BIT</i>
Board of Directors	<i>BoD</i>
Build-Operate-Transfer	<i>BOT</i>
Casa Depositi e Prestiti S.p.A	<i>CDP</i>
Citicorp International Trade Indemnity	<i>CITI</i>
Compagnie Francaise d'Assurance pour le Commerce Exteriorur	<i>COFACE</i>
Compañía Española de Seguros de Credito a la Exportacion	<i>CESCE</i>
Compañía Española de Financiación del Desarrollo	<i>COFIDES</i>
Commercial Interest Rate Reference	<i>CIRR</i>
Corporación Andina de Fomento (Development Bank of Latin America)	<i>CAF</i>
Empire State Development	<i>ESD</i>
European Community	<i>EC</i>
European Union	<i>EU</i>
Export Credit Agency	<i>ECA</i>
Export Credit Guarantees Department of the UK	<i>ECGD</i>
Export Credit Insurance Corporation	<i>ECIC</i>
Export Finance and Insurance Group	<i>EFIC</i>

Export Development Canada	<i>EDC</i>
Export-Import Bank	<i>Ex-Im Bank</i>
Foreign Direct Investment	<i>FDI</i>
Foreign Indirect Investment	<i>FII</i>
Foreign Investment Promotion and Protection Agreement (Canada)	<i>FIPA</i>
Foreign Sovereign Immunities Act of the United States (1976)	<i>FSA</i>
Free Trade Agreement	<i>FTA</i>
Free Trade Zone	<i>FTZ</i>
Friendship Navigation and Commerce	<i>FNC</i>
General Agreement on Trade in Services	<i>GATS</i>
General Agreement on Tariffs and Trade	<i>GATT</i>
Governor's Office of Business and Economic Development	<i>GO-Biz</i>
Instituto de Crédito Oficial	<i>ICO</i>
International Center for Settlement of Investment Disputes	<i>ICSID</i>
International Chamber of Commerce	<i>ICC</i>
International Institute for the Unification of Private Law	<i>UNIDROIT</i>
International Investment Agreement	<i>IIA</i>
International Monetary Fund	<i>IMF</i>
Istituto per i Servizi Assicurativi del Commercio Estero	<i>SACE</i>
Joint Venture	<i>JV</i>
Letter of Credit	<i>LC</i>
Most Favored Nation Clause	<i>MFN</i>
Multilateral Agreement on Investment	<i>MAI</i>
Multilateral Investment Guarantee Agency	<i>MIGA</i>
Multilateral Investment Treaty	<i>MIT</i>

Multinational Corporation	MNC
Multinational Enterprise	MNE
Non-Precluded Measures	<i>NPM</i>
North American Free Trade Agreement	<i>NAFTA</i>
Organisation for Economic Co-operation and Development	<i>OECD</i>
OECD Export Credit Group	ECG
Overseas Private Investment Corporation	<i>OPIC</i>
Paris Club	<i>PC</i>
Political Risk Insurance	<i>PRI</i>
Pool d'Assurance des Risques Internationaux et Speciaux	<i>P.A.R.I.S.</i>
PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft	<i>PwC</i>
Professional Indemnity Association	<i>PIA</i>
Public Private Partnership	<i>PPP</i>
Saudi Arabian General Investment Authority	<i>SAGIA</i>
Schweizerische Exportrisikoversicherung	<i>SERV</i>
Societa Italiana per le Imprese all'Estero	<i>SIMEST</i>
Société de Promotion et de Participation pour la Coopération Economique	<i>Proparco</i>
Sovereign Wealth Fund	<i>SWF</i>
Southern Common Market	<i>MEROSUR</i>
Transatlantic Trade and Investment Partnership	<i>TTIP</i>
Treaty on Functioning of the European Union	<i>TFEU</i>
Trade Related Aspects of Intellectual Property Rights	<i>TRIPS</i>
Trade Related Investment Measures	<i>TRIMs</i>
Union de Naciones Suramericanas	<i>UNSA</i>
United Kingdom	<i>U.K.</i>

United Kingdom Export Finance	<i>UKEF</i>
United Nations	<i>UN</i>
United Nations Commission on International Trade Law	<i>UNCITRAL</i>
United Nations Conference on Trade and Development	<i>UNCTAD</i>
United States of America	<i>U.S.A</i>
World Bank	<i>IBRD</i>
World Trade Organization	<i>WTO</i>

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Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc v The United Mexican States [2007] ICSID Case No. ARB(AF)04/05., 21 November 2007

Casati Case, Judgment 11 November 1981 ECR 2595 Case No 203/80.

Deutsche Bank AG v Sri Lanka, Awarded, 31 October 2012, ICSID Case No ARB/09/02.

Emilio Agustín Maffezini v The Kingdom of Spain, Award Ratified, 21 January 2001, ICSID Case No. ARB/97/7.

Hochtief AG v The Argentine Republic, ICSID Case No. ARB/07/31.

Loewen Group, Inc and Raymond L Loewen v United States, Awarded, 26 June 2003, ICSID Case No ARB(AF)/98/3.

Luisi and Carbone Case, Judgment 31 January 1984 *Joined case 286/82 and 26/83 Luisi and Carbone*

Salini Costruttori S.p.A. and Italstrade S.p.A. v. Kingdom of Morocco, ICSID Case No. ARB/00/4

United City Merchants (investments) Ltd v Royal Bank of Canada [1983] House of Lords [1983] 1 AC 168.

List of Notable Investment Related Protection

1688	Establishment of Lloyd's Insurance Market
1794	Jay Treaty (Between United States of America and Great Britain)
1795	Pinckeney Treaty (Between United States of America and Spain)
1838	Pastry War
1868	Calvo Doctrine (National Treatment for foreign investors)
1872	Establishment of Zurich Insurance Company
1886	FNC between Greece and the United Kingdom
1893	Establishment of ACI [Now Euler Hermes]
1906	Establishment of the first ECA in the world. (Privately held Federal of Switzerland)
1907	Potter Convention
1919	Establishment of the UK ECGD (First Government ECA)
1919	Establishment of American Asiatic Underwriters (AAU) [Now American Insurance Group (AIG)]
1923	US-Mexican General Claims Commission
1928	Spanish Law regulating Export Credit Insurance
1929	Harvard Draft Convention on the Responsibility of States for Damages Done in their Territory to the Person or Property of Foreigners
1930	Hague Codification Conference
1934	Establishment of the Export Import Bank of the U.S. (U.S. Ex-Im Bank)
1944	Establishment of Export Credit Insurance Corporation Canada (ECIC)
1946	Establishment of Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE)
1948	General Agreement on Tariffs and Trade (GATT)

- 1957 European Coal and Steel Community and TFEU (Rome Treaty)
- 1959 Abs-Shawcross Draft Convention on Investment Abroad
- 1960 Signing of the Convention for Economic Co-operation and Development (OECD)
- 1961 UN Yearbook of the International Law Commission
- 1961 Revised Draft on International Responsibility of the State of Injuries Caused on Its Territory to the Person or Property of the Alien
- 1962 Preeminent Sovereignty Over Natural Resources [Resolution 1803 (XVII) of the UN]
- 1963 OECD Draft Convention on the Protection of Foreign Property
- 1965 Washington Convention (Convention establishing ICSID)
- 1967 OECD Draft Convention on Protection of Foreign Property
- 1967 Establishment Association of Southeast Asian Nations (ASEAN)
- 1969 Establishment of Export Development Canada (EDC)
- 1970 Establishment of La Compañía Española de Seguros de Credito a la Exportacion (CESCE)
- 1971 Establishment of the Overseas Private Investment Corporation (U.S. OPIC)
- 1974 Declaration for Establishment of a New Economic Order [UN Resolution 3201 (S-VI)]
- 1974 Charter of economic rights and Duties of States [UN Resolution 3281 (XXIX)]
- 1975 Lome Convention
- 1976 OECD Declaration on International Investment and Multinational Enterprise
- 1978 Arrangement on Guidelines for Officially Supported Export Credits (Known as the OECD Consensus)
- 1985 Convention Establishing the Multilateral Investment Guarantee Agency (MIGA)
- 1985 Draft of International Code of Conduct on the Transfer of Technology (UN)
- 1985 Canadian Export Development Act
- 1990 First Canadian FIPA concluded with Poland

1991	Establishment of the Mercosur (Treaty of Asunción)
1991	Helsinki Package (Added to the OECD Consensus)
1992	World Bank Guidelines on the Treatment of Foreign Direct Investment
1992	North American Free Trade Agreement (NAFTA)
1994	Trade Related Measures (TRIMs)
1994	Energy Charter Treaty
1994	Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur
1994	Protocolo Sobre Promoción y Protección de Inversiones Provenientes de Estados no Partes del Mercosur
1994	Schaerer Package (Added to the OECD Consensus)
1994	WTO's Agreement on Subsidies and Countervailing Measures
1995	Creation of World Trade Organization
1996	UNCITRAL Notes on Organizing Arbitral Proceedings
1996	Signature of a Bilateral Investment Treaty between the UK and Chile
1997	Knaepen Package (Added to the OECD Consensus)
1998	London Court of International Arbitration Rules (LCIA)
1998	Establishment of Istituto per i Servizi Assicurativi del Commercio Estero (SACE)
1998	International Chamber of Commerce Arbitration Rules (ICC)
1998	Establishment of PricewaterhouseCoopers (PwC)
1999	FIPA between Canada and Argentina
2000	OECD Declaration on International Investment and Multinational Enterprise
2003	OECD's Council Recommendation on Common Approaches on the Environment and Officially Supported Export Credit
2006	International Law Commission's Articles on Diplomatic Protection
2006	Arbitration Rules (Rules of Procedures for Arbitration Proceedings)
2006	Articles on Diplomatic Protection (International Law Commission)

2006	Rules Governing the Additional Facility for the Administration of Proceedings by Secretariat of the International Centre for Settlement of Investment Disputes
2008	Principals and Guidelines to Promote Sustainable Lending Practices in the Provision of Official Export Credits to Low-Income Countries
2010	UNCITRAL Arbitration Rules
2010	UK Anti Bribery Act
2010	Arbitration Institute of the Stockholm Chamber of Commerce's Arbitration Rules
2012	International Chamber of Commerce Arbitration Rules (ICC)
2016	Arrangement on Guidelines for Officially Supported Export Credits (Known as the OECD Consensus)

Chapter One: Introduction and Research Methodology

Many investors are attracted by what foreign states have to offer. Such investors are drawn to the vast markets that some states offer.¹ Others are drawn to the natural resources a foreign territory may possess.² Some are keen on being the first to go into certain markets to enjoy a number of benefits, while others take advantage of attractive tax regimes or friendly profit and capital repatriation laws.³ The process invariably starts with a potential investor investigating whether a specific investment abroad would be justified or not. For example, a risk analysis study is carried out in order to find out the

¹ Blanca Sanchez-Robles and Marta Bengoa-Calvo, 'Foreign Direct Investment, Economic Freedom and Growth: New Evidence from Latin-America' (Social Science Research Network 2003) p 8.

Article can be found:

<<http://papers.ssrn.com/abstract=353940>>

Last accessed on 18th January 2013

And;

Harinder Singh and Kwang W. Jun, 'Some New Evidence on Determinants of Foreign Direct Investment in Developing Countries' (Social Science Research Network 2004) p 7.

Article can be found:

<<http://papers.ssrn.com/abstract=623885>>

Last accessed on 18th January 2013.

And;

Erin Anderson and Hubert Gatignon, 'Modes of Foreign Entry: A Transaction Cost Analysis and Propositions' (1986) 17 Journal of International Business Studies pp 2 & 5.

² Sanchez-Robles and Bengoa-Calvo, (n 1) p 8.

And;

Christian De La Medina Soto and Tania Ghossein, 'Starting a Foreign Investment Across Sectors, Benchmarking the ease of establishing a foreign subsidiary across economies' (November 2013) p 4.

Article can be found at:

<http://iab.worldbank.org/~media/FDPKM/IAB/Documents/FDI-Starting-a-Foreign-Investment.pdf>

Last accessed on 18th February 2016

And;

Elizabeth Asiedu, 'Foreign Direct Investment in Africa: The Role of Natural Resources, Market Size, Government Policy, Institutions and Political Instability' (Social Science Research Network 2005) SSRN Scholarly Paper ID 717361. p 65

Article can be found at:

<<http://papers.ssrn.com/abstract=717361>>

Last accessed 18 January 2013

And;

Marcelo Jose Braga Nonnenberg and Mario Jorge Cardoso Mendonca, 'The Determinants of Direct Foreign Investment in Developing Countries' (Social Science Research Network 2004) SSRN Scholarly Paper ID 525462. p 2

Article can be found at:

<<http://papers.ssrn.com/abstract=525462>>

Last accessed 18 January 2013.

³ De La Medina Soto and Ghossein (n 2) p 4.

comparison merits of investing in a foreign territory. In such studies, laws and regulations governing the entry of foreign investors into a foreign market and the protection granted to such investor play a major role in the decision-making.⁴

These investors are referred to as foreign investors. Foreign investors have the choice, when investing in a foreign state, between investing there directly or indirectly. For the purpose of this research there will be reference to foreign direct investment (FDI) only.

This is true especially since FDI endures a more direct risk than that of indirect investment. For that, a special protection should be provided. This comes in many forms from specific contractual agreements concluded by the foreign investor or as an agreement between home and host states’.

Entry into a new market for the purpose of profit maximization may take the form of international trade which is less risky than directly investing in a given state and in that case the investor is referred to as the exporter who enters in a relationship with a host state importer who imports the goods and services of the foreign exporter.⁵

The foreign investor may go into partnerships with a host state investor through joint ventures (JVs) or mergers and/or the investor may, while investing in the host state, retain 100% of the shares of the investment.⁶

⁴ Braga Nonnenberg and Cardoso Mendonca, (n 2) p 2.

⁵ Anderson and Gatignon, (n 1) pp 2 & 5.

And;

Peter J Buckley, Mark C. Casson, ‘Analyzing Foreign Market Entry Strategies: Extending Internationalization Approach’ (1998) 29 *Journal of International Business Studies*, p 548.

⁶ Anderson and Gatignon, (n 1) pp 2 & 5.

And;

Tracing the trend of foreign investments and trade, in general, can go back to as far as World War I where it has been observed that international trade witnessed its prime expansion before World War I started and later after World War II ended. This was followed by a period of international trade recession in the 1950s where major traders were Western European countries and Japan. This continued until innovation in the information technology sector (IT) and regional agreements helped in facilitating more international trade in the 1990's until 2007. It is worth mentioning that international trade faced a small contraction in 2001.⁷

According to Jeswald W. Salacuse, the earliest modes of international investment came through trade where merchants formed limited partnerships to finance their trade and then subsequently started investing in properties to facilitate their investments abroad.⁸ Hymer believes there is a theoretical association between trade and investment where trade lead to direct investment, which he referred to in his work as international operations, where firms decided to distribution channels.⁹ Some regard the modern theory of foreign direct investment to go back to Hymer.¹⁰

Luis A. Reviera-Batiz, Maria-Angels Oliva, *International Trade: Theory, Strategies, and Evidence*, (Oxford University Press 2003) p 167.

⁷ This information was retrieved from the World Trade Organization in a document published in 2008 on Globalization.

Full reference of the document is as follows:

'World Trade Report 2008' World Trade Organization.

Found at:

< https://www.wto.org/English/res_e/booksp_e/anrep_e/wtr08-2b_e.pdf >

Last accessed on the 5th of August 2015.

⁸ Jeswald W. Salacuse, *The Three Laws of International Investment: National, Contractual and International Frameworks for Foreign Capital* (Oxford University Press 2013) p. 13.

⁹ Stephen Herbert Hymer, *The International Operations of National Firms: A Study of Direct Foreign Investment* (MIT Press 1976) p 75.

¹⁰ This was suggested by Professor Magnus Blomstrom in one of his articles published by the OECD.

See:

Mangus Blomstorm, 'The Economies of international Investment incentives', (2001 OECD) pp 166.

Available at:

It is noted that the location of the desired investment's laws and regulations, play a role in the choice of the type of investment selected by the investor.¹¹ For instance, in some of the Gulf states and due to the presence of laws and regulations, foreign investors, those who are not citizens of a member state of the Gulf Cooperation Council, can only own minority of the shares of an investment whereas in Europe, investors (both foreign and local) are, in principle, free to own 100% of the shares of an investment established in any of the EU member states.¹²

Generally, for an investment to be classified as FDI, according to the International Monetary Fund (IMF), the investor must hold at least 10% of the voting powers of a company which is resident in an economy to which the investor is foreign.¹³ But as it will be examined in the research, the definition of what is considered direct investment and what is considered indirect is not quite a standard one where various legal documents provide different definitions and different legal justifications.

<<http://www.oecd.org/daf/inv/investmentstatisticsandanalysis/incentivesforattractingforeigndirectinvestmentanoverviewofecdwork.htm>>

Last accessed on the 15th of July 2016.

¹¹ Dirk Willem Te Velde, 'Foreign Direct Investment and Development: An Historical Perspective' (2006) World Economic Survey. p 9.

¹² For example, in Qatar, foreign investors cannot own more than 49% of the shares of their investment and the majority shareholding is expected to be made by a Qatari national. And only in some cases the foreign investor may own up to 100%.

This can be found at:

Qatar Investment Law Article 2(1) and Article 2(2)

In the United Arab Emirates, foreign investors may own up to 49% of the shares of their investment.

This can be found at:

UK Trade and Investment, 'Doing Business in the United Arab Emirates: UAE Trade and Export Guide' (21 December 2015)

Information can be found at:

<https://www.gov.uk/government/publications/exporting-to-the-united-arab-emirates/exporting-to-the-united-arab-emirates>

Last accessed on the 26th of February 2016.

More about the EU will be presented throughout the thesis in chapters 3.2, 3.3, 4.1, 4.2, 4.4.

¹³ International Monetary Fund (IMF), *Balance of Payment Manual, Fifth Edition* (International Monetary Fund 1993), para 362. p 86.

Found at the following link:

<<http://www.imf.org/external/pubs/ft/bopman/bopman.pdf>>

Last accessed on the 18th of May 2013

Whatever the reason behind investors' decision to invest beyond their country of citizenship, referred to hereafter as the 'home state', these investors will conduct a risk analysis study in order to find out the comparative attractions of investing in a foreign territory. This analysis includes gathering all needed information about the investment from identification of any risks the investor may face overseas to the allocation of these risks.

In this study, investors intend to find out a number of factors that will help them reach a decision whether or not to invest in a given state. The driving force behind the decision to invest abroad may be an internal or an external one. As this was observed by Yair Aharoni, the internal forces are normally traced to the high ranked executives of the company whereas the external factors could be traced to a proposal submitted by a government or an interested importer, or from the fear of losing the market share or due to the belief that the line of business the investor is involved in has been proven successful in the host state or, finally, due to the growing competition in the home state.¹⁴

Investors, normally, take into account certain types of risks, in the risk analysis study, to find out if these risks outweigh the expected benefit or visa-versa. These risks can be classified into political risk, financial risk and commercial risk. Political risk is any threat faced by foreign investors, in the host state, through any form of political intervention or political instability that would restrict them from benefiting from their proper-

¹⁴ These ideas are presented in the work of Yair Aharoni where he discussed the driving forces behind foreign investment and how the decision to invest abroad is reached.

Found at:

Yair Aharoni, *The Foreign Investment Decision Process* (Division of Research, Graduate School of Business Administration, Harvard University 1966).

This work by Yair Aharoni's can also be found at:

Peter J. Buckley and Pervez N. Ghauri, *The Internationalization of the Firm*, (Cengage Learning EMEA, 1999) pp 1-24.

ty rights in part or in full.¹⁵ Commercial risk is the threat faced by the foreign investor due to the home states market's perception of the service or product offered by the investor or due to any disagreement on the part of the local partner of the foreign investor or due to any other contractual disagreements with other involved parties.¹⁶ Finally, financial risk is the threat faced by the foreign investor due to the economic and financial standings of the host state.¹⁷ It is worth noting that, in his book, *Principals of Project Finance*, E. R. Yescombe argues that financial risk is one directly related to inflation and to interest and exchange rates and he refers to it as the micro-economic risk.¹⁸

For the purpose of this thesis, a narrow analysis of political risk, commercial risk and financial will be adopted. This will be done in order to find out the borderline between these three risks. Defining this borderline between political and financial risk is of importance when it comes to insuring against these risks. As the present research will examine what type of risks insurance companies cover against and how can FDIs be protected against risks that are not covered by insurance companies.

In addition, nowadays, in the age of globalization and technological advancements, investments in the technology sector are growing with the introduction of new advancements such as mobile phone applications. Such types of niche investments come with their own set of risks and novel legal issues. These risks come in the form of Cyber-Risk

¹⁵ Hoffman suggests the presence of financial and political risks in investments related to project finance. More about this will be discussed in chapter 2.4.1

Information on Hoffman's distinction can be found at:

Scott L. Hoffman, *The Law and Business of International Project Finance: A Resource for Governments, Sponsors, Lawyers, and Project Participations* (Cambridge University Press 2007) p 23.

¹⁶ This will be further elaborated in chapter 2.4.2.

¹⁷ This will be further elaborated in chapter 2.4.3.

¹⁸ ER Yescombe, *Principles of Project Finance* (1st edn, Elsevier Science 2002) pp 183-199.

which will be argued to fall either under the Commercial Risk Classification or under the Political Risk.

When talking about FDI the first idea that comes into one's mind is the flow of capital, technology, expertise and know-how, and the flow of skilled labor from developed states into less developed ones. While this may be true in general it is, however, not always the case. According to the latest findings, the top five capital exporting countries were the U.S, Germany, U.K, Switzerland and France. The top five capital importing states were U.S, Hong Kong, U.K, Germany and China accordingly.¹⁹ According to these findings, the majority of the top exporting countries are also the capital importing ones, which suggests that it is not necessarily that the flow of capital originates from a developed state into a less developed one. On the contrary, the flow of capital should be seen from an investors' perspective and not from a developed/less-developed state prospective. In that sense, the flow of capital originates from investors wishing to maximize their profits to a state that would allow them to realize such goal without any threats to their investment.

¹⁹ The data presented were last reviewed and checked on the 10th of August 2015. This data was found at the CIA Factbook. For the full list please visit the following links:

For capital exporting countries list:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2199rank.html#sp>>

Last accessed on the 10th of August 2015.

For capital importing countries list:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last accessed on the 10th of August 2015.

United States of America, according to the Global Opportunity Index on Attracting Foreign Investment ranked 18th internationally while the United Kingdom came in 7th, Hong Kong in the 2nd place and Switzerland came in 21st place.

With Regard to Quality of Regulations, the U.S. ranked 42nd internationally while the United Kingdom came in 14th, Hong Kong in the 8th place and Switzerland came in 10th place.

As for the Rule of Law, the United States ranked 7th internationally while the United Kingdom came in 4th, Hong Kong in the 2nd place and Switzerland came in 30th place.

Finally, as for the Ease of doing business, U.S. ranked 26th internationally while the United Kingdom came in 21st, Hong Kong in the 2nd place and Switzerland came in 30th.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last accessed on the 1st of September 2015

Foreign investors may attempt to invest in certain states that may be suffering from political instability. Therefore, it is essential that foreign investors receive proper protection against such risk. As such investors and multinationals may be protected through the means offered by the home state and by those offered by the host state. They could be protected through public international law through means of diplomacy. This may take the form of BITs, MITs and the general rules of public international law in addition to contractual obligations and the role of arbitration as a protection mechanism multinationals and investors may be protected thorough ECAs, multilateral investment agencies and insurance companies.

It shall be noted that, both states may coordinate and cooperate with one another to further promote, protect and facilitate investments between them. Means of coordination between home and host states offered by the host state could take different forms. One of those can be in the form of International Investment Agreements (IIAs). These are also means of protection of foreign investors offered by the host state. Through these IIAs, especially through Bilateral Investment Treaties (BITs), host states open the door to foreign investors and grant them the same treatment as local investors.²⁰ Not only that, but also these BITs include clauses where the host state takes it upon itself not to expropriate any investment made by a foreigner (or, at least if expropriation occurs, the host state undertakes to pay fair and equitable compensation to the foreign investor). This special treatment, along with others, are some of the components of the BIT.²¹

²⁰ This will be further elaborated in chapter 3.1. and 3.2.

²¹ See Mary Hallward-Driemeier, 'Do Bilateral Investment Treaties Attract Foreign Direct Investment? Only a Bit... And They Could Bite' (Social Science Research Network 16 December 2004) SSRN Scholarly Paper. pp 4-6.

BITs specify the rights of investors' and in that respect, it may grant them the right to freely transfer the proceeds of their investment, the right to resort to dispute settlement centers to settle disputes arising between investors and the host state and grant them protection from expropriation and grant them a minimum standard of treatment.²² It is, therefore, a form of commitment taken by the host state.²³ This form of IIA, i.e. BITs, has become a popular tool to attract foreign investment thus becoming a popular form of policy initiative.²⁴ This is primarily due to the fact the host developing states started viewing FDIs as one of the major sources of funding, economic development and overall growth of the state.²⁵

Prior to the introduction of IIAs as a mean of promotion and protection of FDIs, investors' rights were protected through customary international law, which ensured the application of minimum standard of protection to foreign investors' property rights. Such minimum standard included in what is known as the *Hull Standard*, which is related to compensation granted to an investor due to an act of expropriation carried out by the host state against the investors' property rights.²⁶

And;

Susan Rose-Ackerman and Jennifer Tobin, 'Foreign Direct Investment and the Business Environment in Developing Countries: The Impact of Bilateral Investment Treaties' (Social Science Research Network 11 May 2005), p 7. This will be further elaborated in chapter 4.2.

²² Karl P Sauvart and Lisa E Sachs, *The Effect of Treaties on Foreign Direct Investment: Bilateral Investment Treaties, Double Taxation Treaties, and Investment Flows* (Oxford University Press 2009) p 395.

²³ *ibid* at 398.

²⁴ *ibid* at 421.

²⁵ Te Velde (n 11). p 4.

²⁶ Olivier De Schutter, Johan F.M. Swinnen and Jan Wouters, *Foreign Direct Investment and Human Development: The Law and Economics of International Investment Agreements*, (Routledge 2013) p 28.

Another decisive factor is the amount of freedom granted to foreign investors to conduct their operations in a foreign territory free of any state involvement and protected from any changes in the host state's regulations affecting, directly or indirectly, investors' rights. Latin American states are a good example of that where in 1990's they managed to attract investments in the technology sector.²⁷ It is worth noting that, developing states which were successful in attracting foreign investors have taken steps that liberalizes the investment environment and tend to enjoy political and economic stability.²⁸

For the purpose of promoting FDIs and in order to facilitate investors financing their activities and be protected against defaults of the buyers, or other risks including the political risk, export credit insurance was developed.²⁹ A number of states created their own ECAs to encourage local investors export their services to developing and risky host states.³⁰ The topic of Export Credit Insurance is not the main subject of discussion of the thesis rather it is the role of Export Credit Agencies and for that the thesis will not discuss further the topic of ECI. It will rather discuss only ECA in chapter 5. It will elaborate more, in chapter 5, on the role of ECAs in protection against various types of foreign investment associated risks.

These agencies, as it will be examined in the research, offer a variety of coverage and insure against political and commercial risks related to export and offer export-related loans. ECAs have also been established to assist investors in conducting their business in

²⁷ Te Velde (n 11). p 10.

N.B. Throughout the research, there will be references to the Andean Community of Nations' Decisions which were aimed at attracting foreign investments in the technological sector.

²⁸ *ibid.* pp 9-11.

²⁹ See Jean-Pierre Chauffour, Christian Saborowski, and Ahmet I. Soylemezoglu, 'Trade Finance in Crisis: Should Developing Countries Establish Export Credit Agencies?' (Social Science Research Network 11 January 2010) SSRN Scholarly Paper. p 5.

³⁰ See Malcolm Stephens, *The Changing Role of Export Credit Agencies* (International Monetary Fund 1999) p xi.

a given market through granting them loans alongside the guarantees and insurances products and services it offers against the said risks.³¹ These government-backed loans to investors willing to go abroad are granted in order to ease up their entry into foreign markets so that the recipient market benefits from the expertise and technology that the foreign investor possess and at the same time, to stimulate the home states' economy.³²

Since political instability and the fear of expropriation in some developing states pose grave risks to foreign investors along with the acceptability of these markets to certain products or services offered by the foreign investor, the need for protection against such risks was something to be considered in order to encourage investments in these regions.

The study examines the coordination of both the host state and home state's and the measures enacted to protect and promote foreign investments. It will examine the extent of freedom or restrictions of entry into local markets by foreign investors and the political, financial and commercial risks that such investors may encounter in order to sort out the role that ECAs play in that respect.

The thesis will demonstrate that protection of foreign investments comes in many forms.

³¹ *ibid* at 5.

³² Marcos A. Orellana, 'Export Credit Agencies and The World Trade Organization' p 1.

Article can be found at

<http://www.ciel.org/Intl_Financial_Inst/IFI_Research_Publications.html>

Last accessed on the 14th of June 2013.

And;

Kathryn Gordon, *Investment Guarantees and Political Risk Insurance: Institutions, Incentives and Development* (Organization for Economic Co-operation and Development (OECD) 2008) pp 105-106.

And;

Soh Young In, 'Do Export Credit Agencies Benefit the Economy?' (Sep 24 2014) Stanford International Policy Review, Stanford University Journals of International Policy Studies.

Under Objectives of ECAs.

<<http://www.stanfordpolicyreview.org/essay/do-export-credit-agencies-benefit-the-economy/>>

Last accessed on the 17th of 2016.

It includes the cooperation and coordination between home and host states through negotiating and signing International Investment Agreements. It also includes designing investor-friendly regulations by the host state and lowering any expropriation or nationalization risks. In addition, it includes contractual protection in contracts conducted between investors and host states. It also includes protection through political risk insurance programs and it includes international arbitration as a medium of protection of investors.

The study will include an analysis of the nature of such agencies and a comparison of the role that those agencies play with that of MIGA and that of insurance companies. It will focus on the insurance covers offered by different agencies against risks faced by foreign investors with special focus on the role that ECA play in insuring against such risks and how their insurance and guarantee services are compared to other public or private sector agencies.

Since MIGA and ECAs are playing an important role in the promotion or facilitation of foreign investment in developing countries, the study shall include a thorough analysis of the role that these two organizations play in promoting foreign direct investment in developing host states especially in areas considered risky for foreign investment through the insurance services they offer.

The study examines the nature of ECAs in terms of ownership structure as in some states they are governmental or semi-governmental agencies while in others they are privately-owned organizations. The research examines the structure of such agencies and how corporate governance is applied within these ECAs. This will be done in order to

demonstrate that though ECAs differ from one another, yet their services are similar to one another with just some minor differences as to what risks they cover.

Switzerland is credited with the creation of the first export credit insurance program in the world. The program, which was, and still is, offered privately, started in 1906, though this agency is not delegated by the government to offer Export Credit products and services anymore.³³ The U.K., on the other hand, is home for the first governmentally-supported ECA in the world established in 1919 known then as the Export Credits Guarantee Department, or ECGD.³⁴ Today the ECGD is known as the UK Export Finance or the UKEF.

Some countries, as it will be discussed in chapter 6, had export credit insurance offered through a company formed and owned by the government then later on this company was privatized. This is the case of France where COFACE, or the Compagnie Française d'Assurance pour le Commerce Extérieur, has historically been formed as a governmental institution and became later privatized. While other states found it more effective to involve the private sector in the offering of such service alongside the public sector. This is for example the case with the Spanish ECA la Compañía Española de Seguros de Crédito a la Exportación (CESCE).³⁵

On the other hand, there are states that decided to have the official provider of export credit guarantee a company or an agency that is owned and operated by another compa-

³³ The official Export Credit Agency of Switzerland nowadays is SERV. Please note that the research will not handle the position of SERV and what products and services it offers.

³⁴ Stephens (n 20) p 1

³⁵ This will be further elaborated in chapter 4.

ny whose shares are owned by the public and private sector. This is the case of Italy's Istituto per i Servizi Assicurativi del Commercio Estero (SACE), which is owned by the Casa Depositi e Prestiti S.p.A (CDP).³⁶

The German Export Credit Guarantee known as Hermesdeckung or as the HERMES Cover, is delegated by the Federal Government to and managed by Euler Hermes Deutschland AG and PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft.³⁷

The German model forms an example of an agency that guarantees German ventures abroad against failure of payment on the part of the foreign party. Germany, in its efforts to promote foreign investment by German companies, had also started the German Mittelstand Initiative, which intends to empower the position of German firms around the world. This country is regarded as a leading nation in the automotive sector where a group of German automotive companies are responsible for a number of international investments. The study will examine, as well, the position of investment in countries that have been deemed risky to foreign capital. These countries have also been known for their effort to attract foreign capital. Argentina and the Andean Community, including Venezuela, and Brazil are a good example of that. Argentina was subject to a number of arbitration cases from foreign investors due to its constant instability, politically and financially. Including this state in the research will present an example to the borderline between political and financial risks. The Andean Community with its sets of regulations

³⁶ *ibid.*

³⁷ Information can be found at:
<<http://www.agaportal.de/en/aga/index.html>>
Last accessed on the 29th of February 2016.
This will be further elaborated in chapter 4.

that are said to be foreign friendly is still a region trying to attract foreign investors especially in the areas of technology transfer. Venezuela, a previous member of the said community, was recently in the headlines when talking about political risks facing FDIs and primarily expropriation.³⁸

It is worth noting that the Andean Community along with Argentina and Venezuela are members of a regional organization called the Development Bank of Latin America (CAF) which was created by a number of Latin states alongside Spain and Portugal and the Caribbean and by a number of regional banks to offer services similar to those offered by ECA for the exception of guarantee and insurance services.³⁹ Brazil, finally, has been able to attract foreign investors even though it had not put in force any of the BITs it concluded nor can it be subject to arbitration in ICSID.

The aim of this research is to study the validity of the following hypothesis:

- That the home state plays a role in protecting its investors who are willing to invest in foreign markets and provide them with means that they can undertake to protect themselves from foreign investment associated risks.
- That host state can play a vital role in promoting and protecting foreign investors through IIAs.
- That ECAs and the host state can both help in facilitating and protecting FDI.

³⁸ This will be further elaborated in chapters 3 and 4.

³⁹ 'About CAF - Who We Are' (*CAF Development Bank of Latin America*)

Available at:

<<http://www.caf.com/en/about-caf/who-we-are/>>

Last accessed on the 24th of May 2015

For that, the research formulates recommended improvements to the following issues:

- Clearly defining what an investment is in order to define effectively what direct investment is and what foreign direct investment stands for.
- Redefining investment-related risks and how they are categorized.
- Clearly defining the line between the various types of risks
- Effectively analyzing the role that the home and host states play in protecting local and foreign investments.
- Currently applied investment protection mechanisms in developed and developing states and the various modes of entry into foreign markets.
- Analyzing the role ECAs play in promoting FDIs through its risk coverage schemes and Examining the various means available to protect foreign investors

For that, a Comparative Analysis research methodology will be followed throughout the research comparing various countries and agencies in a number of capital exporting and importing states.

Since we live in an era of globalization of law, it may be beneficial for developing countries to borrow successful models from developed ones after adjusting these models to their national needs. Rather than improving old laws and regulations applied in a given state, it may be advantageous for a state to look into a successful model of law or regulation adopted elsewhere and tailor such laws and regulations to what is suitable for this developing state. This does not only apply to laws and regulations, it extends to the creation of national organizations, such as ECAs.

The research will, basically, be based on literature review of FDI regulations in a number of developing and developed states as well as a number of scholarly work written about the ECAs.

The research will examine a number of BITs to find out the common grounds and defining clauses with respect to FDI protection as well. For that purpose, it will sample a number of BITs signed by Canada, the United States of America, Spain, Chile, Switzerland, Germany, the U.K., Austria and China. These states were chosen to the following factors:

- The United States of America has a model of its own when it comes to BITs. It follows the standard of normal BITs but, as it will be examined in this research, it has certain criteria that are included in the majority of its BITs.
- The U.K., Germany, Spain and Austria were selected to present the similarities in the BITs signed between these states and third states. Since all of these states are members of the E.U., it would be beneficial to examine how these states' BITs are similar to one another. Germany was precisely chosen since it was the first state to sign modern day BITs.
- China was chosen as an example of an Asian nation with an advanced economy that has been able to attract a significant number of foreign investors.
- Brazil was selected to elaborate that though there aren't so many BITs signed with other states, it still managed to attract foreign investors. It was for that reason that an examination of certain aspects of one of Brazil's BITs was presented.

- Chile was chosen in order to show the model that this nation followed and elaborate how Chile have specially designed laws that are aimed at attracting foreign investors.

Additionally, the study will probe MIGA's roles, as well as the UN's initiative in that matter. Along with that, the research will follow the qualitative method based on a series of interviewees with two ECA representatives. One with Mr Christophe Viprey, the Director of Public Guarantees at COFACE together with Mrs. Myriam Crosnier, the Credit Assurance Expert at COFACE. The second interview conducted was with Mrs Rocio Uriarte Chavarri, the Head of International Relations at CESCE Credit Insurance.

The research will discuss the international effort directed at the promotion, protection and facilitation of foreign investment and will also discuss the nature of ownership of ECAs and their corporate governance. It will help in introducing the role of ECAs and it will show how these agencies complement the role of private insurance companies and how they assist in the facilitation of foreign investment.

The study will tackle the different products and services offered by ECAs and compare it with other agencies providing similar services but it will mainly focus on the insurance and guarantee services against risks encountered by foreign investors. It will also discuss the borderline between the three types of risks since, at times, it is more complicated to find out under which kind of risk a certain action falls. Then, after studying this borderline, the study will introduce two new categories of risks faced by foreign investors and will recommend the usage of a five-risk approach rather than the classical three-tier approach.

There were many difficulties finding material related to the ideas presented in thesis and for that there was major reliance on the information found as the basis for ideas the thesis intends to present. The thesis, was based on a number of resources that were chosen to help in elaborating the ideas presented in this research. For example, the research resorted to the CIA Factbook to reflect the inflow and outflow of investments in a given state. It has also used the 'Global Opportunity Index on Attracting Foreign Investment' ranking system which ranks host states on the basis of four matrixes; The Economic Fundamentals Matrix, the Ease of Doing Business Matrix, the Quality of Legislation Matrix and the Rule of Law Matrix. With regard to the Economic Fundamental matrix, they measure how host states macroeconomic policies are helping in attracting and facilitating foreign investments by measuring the labor force of the host state, the oppress to foreign investments and the infrastructure of the host state. As for the Ease of Doing Business matrix, it measures the costs associated with foreign investment including terrorism, taxes, crime and other business associated expenses. With regard to the quality of regulations, the matrix measures the extent to which laws and regulations of the host state prevent the free flow of trade and investment through measuring corruption, transparency, the burden of regulation and the extant of control over capital. As for the Rule of Law, finally, the matrix hopes to reflect the extent of which host state's legal regime helps in protecting investors and their property rights.

The thesis referred to some material published by the OECD and MIGA and to the official websites ECAs along with a couple of interviews made with representatives of the French and Spanish ECAs. The research also referred to some studies prepared by credible financial institutions and big players in the insurance sector like the Corporation of

Lloyd's of London. This, for example, was used to elaborate certain aspects related to investment risks.

Since there was already some literature that covers the various services offered by ECAs, this thesis will not go in details about these services, but will rather discuss the nature of these agencies and the ownership structure. It will also discuss its role, along with other organizations and international movements, in the reduction of foreign investment-associated risks. The focus will fall on studying the political risk insurance (PRI) and other investment risk insurance programs provided by such agencies. By studying these matters, the thesis aims to show how the structure of ECAs and their nature can be different and that there is no one standardized structure of ownership for such agencies. It also aims to study PRI products offered by these agencies all done in order to show that though these agencies are in theory intended to promote investments and almost have similar PRI coverage yet some of them cover more risks than others.

At the end of this thesis, an attachment of some important material related to the thesis will be presented. For that, a list of Appendices that includes members of the Berne Union, the Guidelines on the Treatment of Foreign Direct Investment of the World Bank are inserted, together with the member states of the EU, MIGA, OECD and ICSID. The inclusion of the full list of Berne Union Member States, MIGA and OECD Member States along with the states member at ICSID at the end of the research aims to show the international movement directed towards protection of foreign investors. Since these were referred to regularly within the research, they were added in the Appendices of the thesis.

For the purpose of comparison, and in order to present different points of view and different models adopted with regard to the structure of ECA, and to present different attitudes and approaches towards foreign investors, the study will refer to a number of countries such as China, Argentina, Brazil and Mexico. China being a major player in attracting foreign investors, it is beneficial to study the Chinese attitude towards foreign investors. Argentina, on the other hand, suffered a number of financial and economic instabilities. Therefore, it was included in the research to be a practical example of the financial risk associated with foreign investments. Brazil was chosen due to its ability to attract foreign investors though the 14 BITs it signed haven't been into force yet. Finally, Mexico represents developing economies and was included in the study since it is a member of the NAFTA agreement.

The thesis will also present and emphasize on some models applied within the EU and North America and for that, the research will refer to France, Italy, Spain, Germany, the United Kingdom, the United States of America and Canada. France, Italy, Spain and Germany are all, along with the United Kingdom, E.U. member states that house many multinationals and are the home of some of the biggest players in PRI in the world like COFACE, Lloyds of London and UKEF. These were chosen to show how each member states' own initiative may be different than the other in protecting their respective investors. They were also chosen to elaborate on how a bloc of states, the E.U., was able to promote foreign investment through their multilateral initiatives. On the other hand, Canada was chosen since it is credited for introducing the FIPA, which is one of the forms of BITs and the United States of America was selected due to the number of multinationals and inventors it houses and since it has certain means aimed at protecting

their investors and at insuring that their investors are not engaged in malpractices while they're abroad.

The study will begin by defining what is considered as a foreign investment, in chapter 2, to find out, afterwards, what may be referred to as FDI through suggesting a new approach to distinguish between direct and indirect investments. For that, an analysis of the major components of investment will be presented and later a presentation of the meaning of FDI in various instruments will be highlighted.

The study will move on to discuss the various efforts directed at attracting and protecting FDIs in chapter 3 and for that an analysis of the open-door and closed-door policies will be elaborated in order to find out the role that such policies in the attraction of foreign capital. Knowing a home state's attitude towards foreign investors helps in forming an idea about the amount of red tape and political risk a given investor may face and, in return, will be connected to PRI products offered by ECAs.

The thesis will move on to present the role of international movements directed at the promotion and protection of foreign investment including the role of Bilateral Investment Treaties (BITs) and Multilateral Investment Treaties (MITs) as a mean of coordination and cooperation between home and host states. It will elaborate, as well, on the role of diplomatic protection offered by home state to its investors in chapters 3 and 4.

Later on, the study will look into the means of reduction of risks associated with foreign investment after presenting the various types of risks associated with FDI and, for that, it

will suggest a new category of risks rather than the known standard three-risk approach. This will be elaborated in chapters 2.

Lastly, the thesis will examine the different types of ECA and the PRI services they offer to foreign investors, in chapter 4, in order to find out the role they play in protecting investors and in reducing foreign investment risks. This will be done to show how PRI products may differ from one ECA to another and to show how these products are different from those offered by insurance companies and MIGA.

The thesis will present a number of hypotheses and suggestions. It will suggest a new approach to the various types of risks and rather than following the three-risk approach the thesis suggests a more detailed approach on the basis of the five-risk approach. For that, rather than distinguishing between political, commercial and financial risks the study will suggest adding to the known three-risk approach, i.e., political risk, financial risk and commercial risk, the political financial risk and the political commercial risk.

One of the main hypotheses that the thesis will address is that the home and host states have a role in the reduction of risks associated with foreign investment. This will be elaborated through focusing on the role of International Investment Agreements (IIAs) in the reduction of investment-related risks. It will also discuss on the role that ECAs play in protecting investors and how PRI products and services offered by ECAs and that of MIGA and that of insurance companies compare to one another.

The thesis basically focuses on two main matters. The first being, clearly defining the borderline between the various types of foreign investment risks and distinguishing be-

tween two levels of investment protection, i.e. the pre-investment protection and the post-investment protection. The second matter focuses on, exploring the role of ECA is protecting ECAs as a unilateral initiative that helps in hedging investment risks, specifically political risk.

Chapter Two: FDI, Conditions of Entry and Risks Encountered

Investor wishing to invest overseas may be limited to certain conditions. Given that investors fulfill these conditions, upon their entry into the new market, they may face certain risks that would not allow them to gain the economic benefits which drove them to invest there initially.

It is not only the conditions of entry that matters in that respect, it is what can be considered as an *investment* or who is considered as a *foreign investor*, especially since there is no one unified definition for term *investment*. In addition, it is important to know what types of risks investors may be facing while investing abroad.

In that respect, investors basically face three different types of risks, political risk, commercial risk and financial risk. Though actions falling under each of these risks may seem, at first, straightforward and easy to distinguish it is, however, at times, more complicated and more challenging to do.

Basically, the problem would exist once the host state's government undertakes certain actions where in that case even the commercial or financial risk may be political due to such intervention. For that, it is necessary to highlight the cases where actions falling under commercial or financial risks may integrate with the political risk.

There have been different justifications as to which a host state would either be friendly or hostile towards a foreign investment. Those who were welcoming foreign investors saw an opportunity for economic, labor, financial and technological growth while others thought such investors only seek to exploit their natural resources of the state.¹

These two classic attitudes towards foreign investors sees that realizing the host state's advantage, or a loss, due to hosting a foreign venture, is not a thing that would appear directly, rather requires time to observe the effect such investment had on the host state and for that, and in order to ensure a fair gain for investors and for the host state, it might be better to negotiate the fair distribution of the anticipated benefits from such investments.²

This chapter will discuss what a foreign investor means and what is foreign direct Investment. It will look into the modes of entry of investors into foreign markets and what risks they may encounter. This chapter will also present a thorough analysis of these risks faced by foreign investors and will suggest a proper distinction of the borderline between these risks in order to find out how such risks can be hedged or covered against. It will prove that there is a need to unify the various definitions of investment when talking about qualifying foreign investments. This will take place through examining various definitions available and through suggesting a new way of differentiating be-

¹ See Salacuse (*Chapter 1, n 8*) pp 52-56.

And;

Joze Damijan, Mark S. Knell, Boris Majcen and Matija Rojec, 'Technology Transfer through FDI in Top-10 Transition Countries: How Important Are Direct Effects, Horizontal and Vertical Spillovers?' (Social Science Research Network 2003) p 1.

Article can be found at:

<<http://papers.ssrn.com/abstract=404241>>

Last accessed on the 18th of January 2013.

² Salacuse (*Chapter 1, n 8*) pp 56-58.

tween direct and in-direct investment. This differentiation will be based on the intention of the investor. In addition, this chapter will also look at entry modes available for foreign investors and will attempt to make it clear that there is no absolute open-door or closed-door approach to foreign investors rather there is a friendly and a less-friendly environment. Finally, this chapter will introduce a new approach to looking at investment-related risks and suggest, rather than the classic three-risk approach a more detailed five-risk approach.

2.1. Definition of Investments and Foreign Direct Investment and its Components

Foreign investors can be defined as a natural or legal persons who have commercial interest in a state which they are not a national of with the purpose of profit maximization.³ An example of foreign investors includes the Walt Disney Company. This company established a number of theme parks and other investments in the hospitality sector outside of the United States. Notably the company invested in Japan, China and in France.⁴

³ This was also concluded from:

Feliciano R. Fajardo, *International Economics*, (REX 1977). p 125.

And;

'Foreign Direct Investment Statistics: How Countries Measure FDI'

Article can be found at:

<<http://www.oecd.org/daf/internationalinvestment/investmentstatisticsandanalysis/foreigndirectinvestmentstatisticshowcountriesmeasurefdi.htm>>

Last accessed on the 18th of January 2013.

And;

Charlotte H. Brink, *Measuring Political Risk: Risks to Foreign Investment*, (Ashgate 2004) p 1.

According to Brink, Investment implies an expected return.

⁴ The investment made by Disney in France will be further highlighted in this section and in section 2.4.3.

As it will be elaborated hereafter, and in order to determine if an investment made by a foreigner is a direct one or not, one must look into the following facts:

1- Time of holding of the share:

Holding the share for a medium to long term will indicate the investor's interest in having a direct influence in the decision-making.

2- Interest behind purchase or ownership of the share:

This is closely tied with the previous factor where a short-term investment indicates a more indirect approach in which the investor wishes to maximize profit through trading with the shares of the investment rather than maximizing profit through activities of the investment itself. This condition is based on the intention of the investor which could be concluded from the period of holding shares and from how active the investor is in the decision making of the investment.

3- Location of the investment:

In order for a direct investment to be classified as foreign, the investment should take place in a state of which the investor is not a citizen of. It is worth noting, however, that the IMF adds another condition related to a minimum number of shares held by the investor. It classifies a foreign investor as one who holds at least 10% of the shares of an investment.⁵

This definition was the result of analyzing components of foreign investment and of direct and indirect investments as well. These components include the length of holding

⁵ Balance of Payment Manual (*Chapter 1, n 11*), para 362. p. 86

shares in an investment to determine if an investor is a direct or an indirect one, the interest investors have in the investment as to whether they intend to control and manage the investment or not and, finally, the geographic location of the investment, which requires an investment to be established in a state of which the investor is not a citizen of. The thesis stipulates that the intention should be the main focus along with the mentioned components in order to find out if an investor is a direct or an indirect one.

Taking the Walt Disney's investment in France as an example, this Multinational Corporation (MNC) owns majority of the shares of the company that manages the Disneyland Paris Theme Parks and Hotels. This company is called EuroDisney SAL which is also partially owned by Prince Al-Waleed Bin Talal and by other shareholders. For example, following the IMF's definition of a foreign direct investment, Prince Al-Waleed Bin Talal can be considered a foreign direct investor in Euro Disney SAL in France since he holds 39.8% of the shares this company.⁶

Since *investment* can be defined as commercial interest carried out by a natural or legal person with the purpose of profit maximization, *direct investors*, therefore, should have the intention of profit maximization through actively controlling and participating in the management of the investment. This means that the investment should be made on a long-term basis and not just for the purpose of trading in the shares.⁷ *Indirect foreign*

⁶ For more information about Prince Al-Waleed's investment in Disneyland Paris please see: Maria Khan, Saudi Billionaire Prince Al-Waleed bin Talal to Rescue Paris-Based Euro Disney (International Business Times) 12th of October 2014.
<<http://www.ibtimes.co.uk/saudi-billionaire-prince-al-waleed-bin-talal-rescue-paris-based-euro-disney-1469655>>
Last accessed on the 7th of February 2016.

⁷ Maitena Duce, 'Definitions of Foreign Direct Investment (FDI): A Methodological Note' [2003] Banco de Espana, pp 2-3.
Article can be found at:
<<https://www.bis.org/publ/cgfs22bde3.pdf>>

investors, on the other hand, may be natural or legal person who have commercial interest in a state of which they are not a national of for the purpose of profit maximization through the holding of financial instruments for short or medium term without the intention to control or manage the investment.⁸

The thesis proves that basing the differentiation between direct and indirect investment on the period of holding shares is not sufficient since investors basing their investment on purely financial interests may keep holding such instruments even for a long-term in order to maximize their profit without necessarily having the willingness to control or influence the decision making in the company subject of the investment.

The importance in defining clearly what an investment is and what an FDI is lies in the fact that such definition will create less confusion among investors who maybe investing in more than one host state. This is true whenever there is a difference on what qualifies as an investment among different home states.

In general, the term *investment* refers to “the action or process of investing money for profit.”⁹ Though this may seem straight-forward, defining the term ‘*investment*’, when it

Last accessed on the 18th of January 2013.

And;

Voss Jürgen, ‘The Protection and Promotion of Foreign Direct Investment in Developing Countries: Interests, Interdependencies, Intricacies’ (1982) 31 *International and Comparative Law Quarterly*, p 686.

And;

Shanshan Zou, ‘Foreign Direct Investment Opportunities for Georgia’ p 5.

Article can be found at

<<http://stip.gatech.edu/wp-content/uploads/2010/05/Foreign-Direct-Investment-Opportunities-for-Georgia.pdf>>

Last accessed on the 15th of August 2013.

⁸ Similar approach was suggested in the work of Duce:

Duce (*Chapter 2, n 7*) pp 2-6.

⁹ This definition is according to the Oxford Dictionary.

Found at:

<<https://en.oxforddictionaries.com/definition/investment>>

Last accessed on the 1st of February 2017.

comes to cross-border investments, poses a challenge due to the lack of clarity on what the term encompasses.¹⁰ This is true since the definition of *investment* is a reflection of each state's preferences and policies.¹¹ As such, the term was broadly defined to include any asset owned or controlled by the investor.¹²

Generally speaking, defining '*investment*' was left to be determined by international agreements or treaties. Rather than defining the term, these treaties have introduced a set of actions that constitute an *investment*.¹³ As such, these bilateral agreements described, rather than defined, what an *investment* is.¹⁴ These treaties have broadly described the actions constituting investment.¹⁵ For example, in the BIT between Canada and Argentina and the one between the United States of America and Morocco, they both described what acts constitute a qualifying investment without defining what is an investment.¹⁶ In the Canada and Argentina BIT, *investment* was described as follows:

“For the purpose of this agreement
(a) the term means any kind of asset defined in accordance with the laws and

¹⁰ Christopher Dugan, Don Wallace, Noah Rubins and Burzo Sabahi, *Investor-State Arbitration* (2nd edn, Oxford University Press 2008) p. 247.

¹¹ Scope of Definition, UNCTAD Series on Issues in International Investment Agreements II, UN (2011). p. 13.

¹² Peter Muchlinski, '*Corporations in International Law*', Max Planck Institute for Comparative Public Law and International Law, Heidelberg and Oxford University Press (2012). p. 6.

Available at:

<[http://www.uio.no/studier/emner/jus/jus/JUS5851/v13/undervisningsmateriale/muchlinski-\(2009\)-corporations-in-international-law-max-planck-enc.-of-pil-co-1.pdf](http://www.uio.no/studier/emner/jus/jus/JUS5851/v13/undervisningsmateriale/muchlinski-(2009)-corporations-in-international-law-max-planck-enc.-of-pil-co-1.pdf)>

Last accessed on the 2nd of February 2017.

And;

M. Sornarajah, *The International Law on Foreign Investment*, (3rd Edition), Cambridge University Press 2010. p. 10.

¹³ This was also observed in the work of Muchlinski.

See;

Peter Muchlinski, Federico Ortino, and Christoph Schreuer, *The Oxford Handbook of International Investment Law* (Oxford University Press 2008) Chapter 1, pp 19-20.

¹⁴ Dugan, Wallace, Rubins and Sabahi (n43) pp. 247 - 249.

¹⁵ M. Sornarajah, *The International Law on Foreign Investment*, (3rd Edition), Cambridge University Press 2010. P 16.

¹⁶ For the Canada and Argentina BIT see:

Agreement Between the Government of Canada and the Government of the Republic of Argentina for the Promotion and Protection of Investments, E101514 - CTS 1993 No. 11. Article 1.

And;

For the USA and Morocco BIT see:

Treaty between the United States of America and the Kingdom of Morocco Concerning the Encouragement and Reciprocal Protection of Investments, Signed July 22, 1985; Entered into Force May 29, 199. Article 1.

regulations of the Contracting Parties- in whose territory the investment is made, held or invested either directly, or indirectly through an investor of a third State, by an investor of one Contracting Party in the territory of the other Contracting Party, in Accordance with the latter's laws It includes in particular, though not exclusively

- (i) movable and immovable property and any related property rights, such as mortgages, liens or pledges;
- (ii) shares, stock, bonds and debentures or any other form of participation in a company, business enterprise or joint venture money, claims to contract having a and loans
- (iii) money, claims to performance under financial value, related to a specific investment;
- (iv) intellectual property rights, including rights with respect to copyrights, patents, trademarks as well as trade names, industrial designs, good will, trade secrets and know-how;
- (v) rights, conferred by law or under contract, to undertake any economic and commercial activity, including any rights to search for, cultivate, extract or exploit natural resources.”¹⁷

¹⁷ Agreement Between the Government of Canada and the Government of the Republic of Argentina for the Promotion and Protection of Investments, E101514 - CTS 1993 No. 11. Article 1.

A similar description was also present in the United States of America and the Kingdom of Morocco BIT where an *investment* included:

“4. Investment means every kind of investment owned or controlled directly or indirectly, including equity, debt; and service and investment contracts; and includes;

(i) tangible and intangible property, including rights, such as mortgages, liens and pledges;

(ii) a company or shares, stock, or other interests in a company or interests in the assets thereof;

(iii) a claim to money or a claim to performance having economic value, and associated with an investment;

(iv) intellectual property, including rights with respect copyrights and related patents, trademarks and trade names, industrial designs, trade secrets and know-how, and goodwill.

(v) any right conferred by law or contract, including rights to search for or utilize natural resources, and rights to manufacture, use and sell products; and

(vii) reinvestment of returns and of principal and interest payments arising under load agreements.”¹⁸

There are generally two types of foreign investments: direct and indirect. The U.S. Bureau of Economic Analysis defined *foreign direct investment* as “an investment in which resident of one country obtains a lasting interest in, and a degree of influence over the

¹⁸ Treaty between the United States of America and the Kingdom of Morocco Concerning the Encouragement and Reciprocal Protection of Investments, Signed July 22, 1985; Entered into Force May 29, 199. Article 1.

management of, a business enterprise in another country.”¹⁹ And according to the IMF, a *foreign direct investor* is one who invests in a foreign state through owning at least 10% of the ordinary shares or voting powers of the company.²⁰ It involves the transfer of organizational expertise, management, capital, and technology, access to national market of the host state and includes the transfer of entrepreneurship incentives.²¹ FDI was described as a long-term relationship based on an interest of the investor in the host state.²² It is assumed from the IMF’s definition of direct investment that the threshold for considering an investment as direct or as an indirect one lies within the ownership of ordinary shares.²³ That, nevertheless, is not the case in domestic legislation where there have been different models followed in determining what is considered an indirect investment. For example, there is a US System which considers an ownership of a 10% or more of the shares of a direct investment, such as a branch or a fully owned subsidiary of the investment, or of an indirect investment.²⁴

Following the distinction suggested by the IMF based on a percentage threshold is rather shallow since investors may decide to invest in a given existing legal entity with the intention of being active and practicing their rights as owners, while another investor

¹⁹ This can be found at:

Zou (*Chapter, 2 n7*) p 5.

²⁰ Balance of Payment Manual, Fifth Edition (*Chapter 1, n 11*), paragraph 362, p. 86.

And;

Salacuse (*Chapter 1, n 11*) pp 14-15.

And;

This rationale is also followed by a number of other initiatives.

See;

‘Foreign Direct Investment Statistics: How Countries Measure FDI’ (n 41) p 23.

²¹ John H Dunning and Sarianna M Lundan, *Multinational Enterprises and the Global Economy* (2nd edn, Edward Elgar Publishing 2008) p. 7.

And;

Duce (*Chapter 1, n 7*) pp 2-3.

And;

Jürgen (*Chapter 2, n 7*) p 686.

²² R Barry J Jones (ed), *Routledge Encyclopedia of International Political Economy* (Routledge 2002). p 754.

²³ Balance of Payment Manual, Fifth Edition (*Chapter 1, n 11*), paragraphs 362 and 363, p. 86.

²⁴ European Central Bank, ‘Indirect FDI Relationships’ (Issues Paper Number 3) April 2004, Introduction (3) p 2.

may be interested in trading with the shares or financial instruments of an existing legal entity.²⁵

Basing the definition and the distinction on the mere intention behind the investment may not be an easy thing to start with but like any other legal precedent, intention is the basis of any legal action.

Combining the intention of investors to have continuous interest in the decision making of the investment, with the percentage threshold, i.e. the 10%, should result in achieving a more comprehensive and rather accurate distinction where a *direct investment* is then any long-term investment made with the intention of profit maximization through actively controlling and participating in the legal entity's decision-making process. Moreover, the financial instrument chosen by investors should allow them to control and participate in the decision making of the legal entity. On the other hand, and based on that, an *indirect investment* is one made without the intention of controlling or participating in the decision making of the legal entity and rather made with the intention of trading the financial instrument related to this investment in exchange of profit.

Klaus P. Berger, defined *foreign direct investment* as the endowment, creation or acquisition of an establishment in the host state with the goal of controlling and managing this establishment in a way that shows the dependency of the investors return on their managerial decisions and control of the establishment.²⁶ It involves, according to M. Sornara-

²⁵ 'Foreign Direct Investment Statistics: How Countries Measure FDI' (*Chapter 2, n 3*) p 23.
N.B. This matter will also be highlighted within this chapter.

²⁶ Klaus P. Berger, 'The Multilateral Investment Guarantee Agency Globalizing the Investment Insurance Approach Towards Development', (1988-1989) 15 *Syr. J. Int'l L. & Com.*, p. 17

jah, the transfer of tangible and intangible assets from one state to another for the purpose of generating wealth under partial or total ownership of these assets.²⁷ It is therefore understood that, according to the IMF, *direct investors* are, mainly, keen on having a voice in the management of the company and, through this management, have a say in how the company is controlled.²⁸ This can be clearly observed from the classification of *direct investment* cited by the IMF where it recognized a situation in which the direct investor, i.e., one who owns more than 10% of the voting shares of an investment, owns, through the said investment, voting powers in another investment and referred to such situation as *indirect direct investment*.²⁹

Alternatively, *indirect foreign investment* takes the form of ownership of shares, stocks, bonds, commercial papers, certificate of deposit, country funds, external stock offerings and other financial instruments in one or more host states.³⁰ It is basically the ownership of debt or equity instruments.³¹

Article can be found at:

<<http://0->

www.heinonline.org/catalogue.ulrsls.lon.ac.uk/HOL/Page?handle=hein.journals/sjilc15&id=21&collection=fijournals&index=journals/sjilc>

Last accessed on the 18th of May 2013

And;

According to Duce, the classification of direct investment is based on three merits: direction, investment instrument and on sector breakdown.

This is found at:

Duce (*Chapter 1, n 7*) pp 5-6.

²⁷ Sornarajah, (*Chapter 2, n 12*) p 8.

²⁸ Balance of Payment Manual, Fifth Edition (*Chapter 1, n 11*), paragraphs 361, p. 86.

²⁹ See:

Balance of Payments and International Investment Position Manual, (6th edn, IMF 2009). Chapter 6 (B) I(c), 6.12. p 110.

And;

Marie Montanjees, Indirect Investment: Defining the Scope of the Direct Investment Relationship, Issue Paper (DITEG) #3. (IMF, April 2004) p3

³⁰ Jürgen referred to such investments as portfolio investments.

See;

Jürgen (*Chapter 2, n 7*) p 686.

³¹ Indirect investment is seen as one in less than 25% of the securities of a given venture.

See;

Edwin M Martin, 'Multilateral Investment Insurance: The OECD Proposal' (1967) 8 Harvard International Law Journal, p 303.

Taking the 10% threshold suggested by the IMF alone to determine whether an investment is direct or not might, in theory, present a good distinction yet it is an incomplete one. For that, and in addition to the classic IMF definition of direct investment of having 10% of the voting rights, adding 'with the intention to actively manage and participate in the decision making of the company for the long term and with the intention to make profit primarily from the company's commercial activities' result in a more comprehensive.³²

However, this is not to be confused with the distinction between short-term and long-term investors. Knowing the difference between short-term and long-term investments will help in understanding the distinction between direct and indirect investment.

The distinction between short-term and long-term investments are classically thought to be based on the intention of the investor and the period of which an investor holds the financial instrument of a given legal entity.³³ For that, short-term shareholders invest in a specific legal entity with the intention of reselling their financial instruments in this entity back again once the value of the instrument increases. As it will be elaborated later in this section, indirect investment may not exclusively be in the form of equity rather could include debt instruments. On the other hand, long-term investors are those who invest with the intention of profit maximization through sharing the profits, and losses, of their chosen legal entity and from the increase in the value of the entity.³⁴ These investors normally invest on a long-term basis. This distinction falls between the

³² The matter of long-term relationship was also present in the definition suggested in the work of Duce.

See;

Duce (*Chapter 1, n 7*) pp 2-3.

³³ Jürgen (*Chapter 2, n 7*) p 686.

³⁴ *ibid.*

direct and indirect distinction of an investment. It relies, primarily, on the length of investments to determine the intention of the investor and this, in return, will help in determining the nature of the investment as to whether it is a direct or indirect.

As it can be concluded from the above, the distinction between these two types of foreign investments lies under the presence of a certain percentage of controlling in a given investment, i.e. the willingness of foreign investors to control and manage their investment.³⁵ Some authors regard indirect investment as portfolio investment yet others chose to separate portfolio from indirect investments.³⁶ The IMF, as well, cited the case where an investor may own debt or securities in an investment and referred to it as Portfolio Investment.³⁷

For some, there are more than the direct and indirect forms of foreign investment. These come as follows: direct investment, indirect investment, supplier credit, international loan and bonds.³⁸

In principle, such distinction may be comprehensive but it, nevertheless, does not present any new approach or justification to such distinction. This is true since all the instruments mentioned, other than the direct-indirect investment, are rather debt instru-

³⁵ Dunning and Lundan (*Chapter 2, n 21*) p.7.

And;

Duce (*Chapter 1, n 7*) pp 3.

³⁶ The idea that Portfolio and Indirect Foreign Investment are one or the same was concluded from:

Stephen H Hymer, *The International Operations of National Firms: A Study of Direct Foreign Investment* (MIT Press 1976) pp. 1-2.

The idea that Portfolio and Indirect Foreign Investment are two different categories of investment was concluded from:

Dugan, Wallace, Rubins and Sabahi (*Chapter 2, n 10*) pp. 247 - 249.

³⁷ Balance of Payments, 6th edition (*Chapter 2, n 29*). p 110.

³⁸ See:

Salacuse (*Chapter 1, n 11*) pp 13-17.

ments and loans and as such, they could be considered as Portfolio Investment. Starting with international loans, which are debt instruments, the reason they are considered as portfolio investment is the fact that the loan provider, i.e. banks or financial institutions in that case, does not engage in investment activities, i.e. the loan provider is neither has a certain degree of control over the investment nor is the provider directly or indirectly involved in providing goods or services of the investment. As for international bonds, these are normally financial instruments issued by companies or governments and considered as a loan rather than an ownership instrument and, since they are loans, they are considered portfolio investment exactly for the same justification presented for international loans. Finally, supplier credit is when investors sell their goods to the host state party on credit supported by a financial or governmental institution.³⁹ This is, for example one of the services offered by ECAs. Such service is another form of a loan of which the provider does not wish to exercise any form of control over the commercial activities of the borrower.

Normally, states entering into international investment agreements with other states tend to define actions constituting an investment in general without distinguishing between direct or indirect.⁴⁰ In addition, what is considered as a covered investment in one investment agreement may not be a covered one in another agreement. This is especially true since investment means different things for different states depending on the purpose of such activity.⁴¹

³⁹ *ibid* at p 17.

⁴⁰ This issue will be examined in detail in the next chapter.

⁴¹ *International Investment Law: Understand Concepts and Tracking Innovation*, OECD 2008, Chapter 1, p 46.

Historically and under customary international law when talking about investment, it usually refers to FDI. Nowadays, using the word investment has different meanings depending on how it is defined by the host state or home state. This may differ from the definition found in the IMF for example, or that found in a Bilateral or a Multilateral Agreement or that cited by ICSID. For example, and in comparison, to the examined IMF definition, in the BIT between the United Kingdom and Lebanon, an *investor* means any:

“physical persons deriving their status as United Kingdom nationals from the law in force in the United Kingdom: corporations, firms and associations incorporated or constituted under the law in force in any part of the United Kingdom or in any territory to which this Agreement is extended in accordance with the provisions of Article 12.”⁴²

According to UNCTAD’s ‘Comprehensive Study of the Interrelationship between Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI)’, FDI is normally a long-term investment and it entails a lasting interest in the investment.⁴³ The UNCTAD followed, as well, the same conclusion as that of the IMF with regard to the 10% investment threshold to determine whether it is a direct one or not. Portfolio Investment, on the other hand, is one made in debts or securities of a given enterprise. It also includes investing in bonds and in any financial derivatives.⁴⁴ The study concluded that in order for an investment to be categorized

⁴² Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Lebanese Republic for the Promotion and Protection of Investment (1999), Article 1.

⁴³ Comprehensive Study of the Interrelationship between Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI), UNCTAD [1999], Chapter I (A)a, p 4.

Also see:

Dugan, Wallace, Rubins and Sabahi (*Chapter 2, n 10*) p 1.

Dugan, Wallace, Rubins and Sabahi distinguished between FDI, indirect investment and portfolio investment. They concluded that FDI are normally medium to long-term investments through infusion of cash, expertise, equipment or any other type of assets into the host state. Whereas portfolio investments take place through the purchase of publicly traded securities of foreign companies.

⁴⁴ Comprehensive Study of the Interrelationship between Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI) (n 75) Chapter I (A)b, p5.

as a portfolio investment it should be less than 10% and it shouldn't involve any affiliated enterprises.⁴⁵ This last does not, however, differ from the definition of indirect investment, which may include such types of investment.

Stephen Herbert Hymer also followed this conclusion where he distinguished between direct investments and portfolio investments.⁴⁶ For the purpose of this research there will be no distinction between indirect and portfolio investment and the latter shall be part of the definition of the indirect investment.

There are different types of direct investment that foreign investors may choose from. These depend on the type of risk that investors are may face abroad and the goals that they seek. For that, investors may opt to create a branch in the host state and retain 100% control of the investment or through a subsidiary.⁴⁷ Investors may decide to establish a factory in the host state of which they also retain 100% control over it. This is known as a greenfield investment.⁴⁸ Or investors may decide to acquire an existing investment in the host state. On the other hand, investors may decide to go into partnership with a local host state investor and create a joint venture or they may do so through an affiliate company created with another host state investor. The investor may, also, opt to establish an investment and transfer all the technology and to build the local know-how through the qualifying local labor of the host state and then, after an exchange of a pre-agreed sum,

⁴⁵ *ibid.*

⁴⁶ Hymer (*Chapter 2, n 36*) pp. 1-2.

⁴⁷ Giorgis Barbora Navaretti, Anthony J Venables and Frank Barry, *Multinational Firms in the World Economy* (Princeton University Press 2004) pp 15-16.

And;

Anderson and Gatignon, (*Chapter 1, n 1*) p 5,

And;

Luis A. Riviera-Batiz, Maria-Angels Oliva, *International Trade: Theory, Strategies, and Evidence*, (Oxford University Press 2003) p 167.

⁴⁸ Muzaffer Eroglu, *Multinational Enterprises and Tort Liabilities: An Interdisciplinary and Comparative Examination*, Edward Elgar Publishing (2008) p 30.

transfer this establishment to the host state government. This is similar to the Build-Operate-Transfer concept (BOT), which is common in the infrastructure sector.⁴⁹

Finally, investors may choose to go to a host state through licensing or franchising where investors, in a licensing agreement, transfers the know-how and knowledge to a host state importer in exchange of specific payments and royalties.⁵⁰ Franchising grants the importer the right to use the business model, including the trademarks, of the owner for a specified period in exchange of an agreed percentage and royalties.⁵¹ Normally, the owner in franchise agreements, the Franchisor, retains a considerable amount of control in the franchise agreement and provides training and support to the Franchisee, the importer of Franchise, whereas the licensor, the owner in the license agreement, gives up such control and does not provide training or support to the licensee, the importer in the license agreement.⁵²

As mentioned, BITs describe what constitutes an *investment*. For example, in the Italy and Morocco BIT signed in 1990, the term *investment* in Article 1 of the Treaty defined

⁴⁹ Wenhua Shan, *The Legal Protection of Foreign Investment: A Comparative Study* (Bloomsbury Publishing 2012) p 260.

⁵⁰ Anderson and Gatignon, (*Chapter 1, n 1*) p 5,

And;

Reviera-Batiz, Oliva, (*Chapter 2, n 47*) p 167

⁵¹ *ibid.*

⁵² See;

Mario Glowik, *Market Entry Strategies: Internationalization Theories, Network Concepts and Cases of Asian Firms: LG Electronics, Panasonic, Samsung, Sharp, Sony and TCL China* (Walter de Gruyter & Co 2009) pp 74-88.

And;

Vyuptakesh Sharan, *International Business Concepts, Environment and Strategy* (2nd edn, Pearson Education India 2008) pp 31-41.

And;

Dean McFarlin and Paul D Sweeney, *International Management: Strategic Opportunities & Cultural Challenges* (Routledge 2014) Chapter 9 Part III.

And;

Sidney M Levy, *Build, Operate, Transfer: Paving the Way for Tomorrow's Infrastructure* (1st edn, Wiley, John & Sons 1996) pp. 1-26.

And;

Reviera-Batiz and Oliva (*Chapter 2, n 47*) p 167.

Investment as “each property invested, before or after the entry into force of this Agreement, to natural or legal persons, including the Government of a Contracting Party, in the territory of the other Contracting Party, in accordance with the laws and regulations of the latter.”⁵³ The BIT also stated a number of investments as an example in the same Article.⁵⁴ It specifically included “any economic rights conferred by law or by contract and any license and concession granted in accordance with the current provisions for the exercise of economic activity, including prospecting, cultivation, extraction and exploitation of natural resources.”⁵⁵ This latter was one of the claims brought up by the Salini representatives in the *Salini v. Morocco* case, against Morocco.⁵⁶

Salini and Italstarde, two Italian companies, agreed with a state-controlled company in Morocco called Societe Generale des Autoroutes du Maroc, in 1994, to construct part of a highway connecting two cities in Morocco. Upon completion of the contractual obligation, Salini reached to the state-controlled company seeking compensation only to find this request denied. After the denial of the request, Salini submitted claims to the Minister of Infrastructure of Morocco who did not get back to Salini. For that, Salini sought after arbitration in ICSID and submitted an Arbitration request in 2000 on the basis of the arbitration clause present in the Morocco & Italy BIT.⁵⁷ As a result, this landmark case was the basis of a test, known as the Salini Test, which determines the Nationality of the Investment. The Salini test will be discussed in following chapters.

⁵³ Italy and Morocco Bilateral Investment Treaty (1990), Article 1(1).

⁵⁴ *ibid.*

⁵⁵ *ibid* at 1(1)(e).

⁵⁶ *Salini Costruttori S.p.A And Italstrade S.p.A v Kingdom of Morocco, Decision on Jurisdiction* [2001] International Centre for Settlement of Investment Disputes ICSID Case No. ARB/00/4

⁵⁷ *ibid.*

On the other hand, for example, it can be concluded from NAFTA's definition of *investment* that it refers to both direct and indirect.⁵⁸ NAFTA defined *investment* as follows:

“investment means:

(a) an enterprise;

(b) an equity security of an enterprise;

(c) a debt security of an enterprise

(i) where the enterprise is an affiliate of the investor, or

(ii) where the original maturity of the debt security is at least three years,

but does not include a debt security, regardless of original maturity, of a state enterprise;

(d) a loan to an enterprise

(i) where the enterprise is an affiliate of the investor, or

(ii) where the original maturity of the loan is at least three years,

but does not include a loan, regardless of original maturity, to a state enterprise;

(e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise;

(f) an interest in an enterprise that entitles the owner to share in the assets of that enterprise on dissolution, other than a debt security or a loan excluded from subparagraph (c) or (d);

(g) real estate or other property, tangible or intangible, acquired in the expectation or used for the purpose of economic benefit or other business purposes; and

(h) interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory, such as under

(i) contracts involving the presence of an investor's property in the territory of the Party, including turnkey or construction contracts, or concessions, or

⁵⁸ North American Free Trade Agreement (NAFTA), Art. 1139(a), 1139(d) & 1139 (e-g).

(ii) contracts where remuneration depends substantially on the production, revenues or profits of an enterprise.”⁵⁹

It shall be noted that ICSID, the International Center for Settlement of Investment Disputes, left the door wide open for each contracting state to define *investment* in the most suitable way to each state.

As it will be discussed further in this research, there have been a number of cases presented to ICSID against host states under the claim of infringement of property right. In some of these cases, it has been noted that the claimants, who usually are foreign investors, used different claims. Among these claims, one is related to the definition of *investment*. This is for example what the aforementioned *Salini Case* was about.

The importance of knowing what an *investment* is lies in the fact that such definition would actually be the grounds of protection of investors themselves and the protection of their property. In that respect, an act that may be considered as an investment done by the same investor in a given state may not be considered as such in another state and therefore may not be able to benefit from the same protection he is benefiting from in the other state.

Normally, in IIAs, the scope of an *investment* is defined. Such agreements may introduce a broad understanding of what constitutes an *investment* is while others may limit the scope of its definition. For example, a number of IIAs tend to include contractual con-

⁵⁹ *ibid*, Art. 1139(a)-(g)

cessions along with equity and physical assets in the definition of *investment*.⁶⁰ Other agreements, on the other hand, such as that of Association of Southeast Asian Nations (ASEAN) and China do not include portfolio investments in its definition of *investment*.⁶¹ The reason behind such exclusion is that such investments does not require a higher level of protection as that granted to foreign direct investments since it is less stable than FDIs.⁶²

It shall be noted that the definition of a qualifying *investment* does not only refer to the acts considered an *investment*, it also includes nationality of investors. This is true when talking about protection of foreign investors.

The issue of nationality of investors was present in the aforementioned Salini case where the nationality of the investor played a role in determining whether the investor's investment is qualified under the present BIT between Italy and Morocco and, therefore, whether the investor can make a claim to protect his investment or not.⁶³

Since it is not the subject of this research, the issue of nationality of the investor will not be further elaborated. It is worth mentioning that there is a debate on which nationality should be taken into account; nationality of the investor or that of the legal person investing. This is happening in order to find out the scope of protection offered to foreign direct investors in BITs and in other IIAs.

⁶⁰ Sauvants and Sachs, (*Chapter 1, n 40*) p 39.

⁶¹ *ibid* at 40.

⁶² *ibid*.

⁶³ Italy and Morocco Bilateral Investment Treaty (1990), Article 1(1).

And;
Salini v Morocco (Chapter 2, n 56).

For ECAs, in general, an investor, a natural or a legal person, is a national of the home state where the ECA is based. A qualifying investment differs from one agency to another. There are agencies willing to cover the technology sector while others are willing to cover only the agriculture-related investment for example.⁶⁴ For MIGA, on the other hand, an investor is someone who is a national of one of the member states of the agency, and a qualifying investment is an economically sound investment that will be developed in a member state of the MIGA.⁶⁵

It shall be noted that, the legal nature of the investor, according to the OECD and IMF, may refer to an individual, or an incorporated or unincorporated private or public body. It may also include a government, a group of individuals, or a group of incorporated or unincorporated enterprises that have a direct investment enterprise, operating in the host state. In that sense Sovereign Wealth Funds (SWFs) may fall under this definition.⁶⁶ SWFs are state-created vehicles of investment where the state, through this vehicle, invests in a number of sectors and owns a number of financial instruments and may also invest in hedge funds or private equity funds.

In the EU, there is no definition as to what constitutes foreign direct investment.⁶⁷ Neither in the Lisbon treaty nor in the Rome Convention.⁶⁸ Though there is no definition of FDI within

⁶⁴ This will be elaborated in chapter 4.4.

⁶⁵ Noah Rubins and Stephan N Kinsella, *International Investment, Political Risk, and Dispute Resolution: A Practitioner's Guide* (Oxford University Press, USA 2005) p 104.

List of MIGA member states is available at Appendix II.

⁶⁶ Balance of Payment Manual, Fifth Edition (*Chapter 1, n 11*), para 362. p 86.

⁶⁷ The EU Approach to International Investment after the Lisbon Treaty, (EU Parliament Policy Department 2010). p 6. Available at:

<[http://www.europarl.europa.eu/RegData/etudes/etudes/join/2010/433854/EXPO-INTA_ET\(2010\)433854_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/etudes/join/2010/433854/EXPO-INTA_ET(2010)433854_EN.pdf)>

U.K. legislations, there are, however, some other UK official resources defining FDI. For example, the UK Office for National Statistics defined FDI as an “investment that adds to, deducts from or acquires a lasting interest in an enterprise operating in an economy other than that of the investor where the investor’s purpose is to have an effective voice in the management of the enterprise”.⁶⁹ On the other hand, there are some states that have defined Foreign Investment or Foreign Investor within its laws. For example, Foreign Investor was defined, in the Chilean Law, as an individual or a corporate body that is domiciled outside of Chile and wishes to transfer capital into Chile through a foreign investment contract.⁷⁰ The Qatari Law defines a Foreign Investor as natural or judicial Non-Qatari person who invest their money in any of the legally permitted directed investment projects.⁷¹

The concept of foreign investment, in the E.U., is not related to the nationality within member states rather, it is related more to the crossing of borders.⁷² Indeed, third country investors, i.e. those who do not belong to one of the member states, are considered as foreign investors while EU investors investing in any member state are considered more as national investors in the scope of EU treaties.

There are two major classifications for foreign investment. Inward foreign investment and the outward foreign investment. These classifications are basically linked to the

Last accessed on the 12th of September 2016.

⁶⁸ *ibid.*

⁶⁹ Foreign Direct Investment Involving UK Companies: 2012, UK Office for National Statistics. Section 11: Background Notes.

Available at:

<<https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/bulletins/foreigndirectinvestmentinvolvingukcompanies/2013-12-05>>

Last Accessed on the 1st of May 2017.

⁷⁰ Chilean Foreign Investment Statute Decree Law 600, Title I(1) and (2).

⁷¹ Qatari Law No (13) of the year 2000, Chapter One Article 1

⁷² Angelos Dimopoulos, *EU Foreign Investment Law* (1st edn, Oxford University Press 2011) p 42.

location of the investment where inward foreign investment takes place when the host state becomes recipient of the capital and investment made by a foreigner and the outward foreign investment refers to the home state being the exporter of the capital and investment.

Moreover, it could be, nowadays and after the technological advancement and emergence of new means of investments and trade, more complicated to label an investment as direct or indirect especially since the original definition of direct and indirect investments entails the obvious physical presence of an investment in a given host state. Therefore, the concept of control plays a role in defining whether a certain investment is a direct or an indirect one.

This is especially true when talking about investments based on publicly-accessed networks like the internet. The issue arises when companies like Apple through its online iTunes store, that offer a range of music, movies, books and mobile phone applications offer such products virtually to any iTunes member through a number of international iTunes store which offer products tailored to the market's needs and restrictions and without necessarily having a physical store or presence in such states. In most of these stores, Apple does not have a physical presence in these countries and yet its online products are offered to its clients while retaining full voting powers.⁷³

⁷³ More information about this could be found on the official website of Apple Inc.

<<http://www.apple.com/legal/>>

Last accessed on the 29th of February 2016.

And;

<<http://www.apple.com/about/>>

Last accessed on the 29th of February 2016.

In this case, the criterion of control is fulfilled while the physical presence in the state where services and products are offered is not present. In this case, these investors are considered exporters of their goods and services without having an importer and without establishing an office, a branch or other forms of classical direct investment methods. In this way, these investors aim to avoid a number of risks and, at the same time, minimize their expenses in order to maximize their profit. For that, and after following the criteria of control, such investors may be considered as direct investors.

Perhaps, the varying definitions of *investment* depends on the approach the state is willing to take towards investors.⁷⁴ In that respect, the host state will define what foreign investment stands for through identifying who is a foreign investor and it will define what incentives it is willing to grant to investors, if the it will be impose any control on investors and, finally, it will determine the process of which foreign investors are admitted to the host state to invest, i.e. prior approval or authorization.⁷⁵ This is noticeable, for example, in the Qatari Law where foreign investors require a prior license.⁷⁶ The Law also defines the permitted and prohibited sectors for Foreign Investors, the process of their admittance and investment incentives offered by the state.⁷⁷

But basically in BITs and FTAs they include analytical definitions while ICSID has a more determinative insight with regard to what investment is and MIGA, on the other hand, offers a complementing definition to what qualifies as an *investment* in main pro-

⁷⁴ Scope of Definition, UNCTAD Series on Issues International Investment Agreements II, UN (2011). p. xiii.

⁷⁵ Salacuse (*Chapter 1, n 11*) pp. 91-92.

⁷⁶ Qatari Law No (13) of the year 2000, Chapter Two Article 4.

⁷⁷ *ibid.* Chapter Two & Three.

tection instruments.⁷⁸ Though it may be somewhat challenging to determine what an *investment* is, it is, nevertheless easier to determine what foreign investment is, since this is related to the nationality of the investor yet this also was somewhat challenging since an investor may be a legal person.⁷⁹

Figuring out whether this foreign investment is direct or indirect one, on one hand, or what is considered as a foreign investment in a given host state, on the other, is subject to BITs and international conventions. It is, however, safe to define an *investment* as a commercial interest that a legal or natural person has in order to maximize profits. Therefore, a *foreign investor* is a natural or legal person who is willing to invest in a state of which he is not a citizen of or incorporated in or shares a number of connecting factors with.

Since *direct investment* is a form of investment that involves holding equity of a given entity and requires controlling the investment and having a continuous interest in the investment, *foreign direct investment* can, therefore, be defined as an investment concluded by a foreign natural or legal person in a host foreign state with the goal of profit maximization and with the intention of controlling and continuously managing the investment.⁸⁰ In that respect, FDI is an economic activity that is actively practiced by Multinational Corporations (MNCs). MNCs, also known as Multinational Enterprises

⁷⁸ Dimopoulos (*Chapter 2, n 72*) p 22.

⁷⁹ *ibid* at 32-33

⁸⁰ This is similar to Talamo's definition. The only difference between the two being that Talamo suggested the existence of a long-term relationship. This long-term relationship was also suggested and present in most instruments defining FDI.

See;

Giuseppina MariaChiara Talamo, 'Institution, FDI and the Gravity Model', Workshop PRIN 2005 SU, Economic Growth; Institutional and Social Dynamics (2007) p 5.

The article can be found at:

<http://growthgroup3.ec.unipi.it/Siena2007/paper_talamo_siena.pdf>

Last accessed on the 12th of June 2013.

(MNEs) are corporations engaging in foreign direct investment through owning and controlling other value-added activities in various states.⁸¹ Whereas indirect investment is one made with the intention of holding a short-to-medium term interest in the investment in order to maximize profits and without the intention of controlling or managing the investment. It can be done by holding stocks, shares or through investing in hedge funds to name a few. Based on that *foreign indirect investment* (FII) is an investment concluded by a foreign natural or legal person in a host foreign state with a goal of profit maximization through the purchase of financial instruments and holding it for a short-to-medium term period without having the intention to control or manage the investment.

Knowing what qualifies as a foreign investment and, therefore, who is a foreign investor, will allow us to further examine the limits of their protection in the host state's laws and regulations and in international agreements, as well as, the protection they may have from public or private agencies against any risk they may encounter.⁸²

2.2. The Relationship between National and International Legal Regimes and FDI

The ideal way to view the role of the host states' legal system in promoting and attracting FDI is through looking at their approach towards such investments.⁸³ For that, the

⁸¹ Dunning & Lundan, (*Chapter 2, n 10*), p. 3.

⁸² The role of ECAs, MIGA, BITs and other measures of protection to foreign investors will further be discussed in chapters 4.

⁸³ Another view suggests that laws of the host state are seen as either being on the "side of the foreign investor or not" This view was cited by Brink.

classic approach is to distinguish between an open-door and a closed-door approach. Though this has been a helpful way to distinguish between various legal regimes, it is, however, an inaccurate distinction since they suggest either an absolute open environment or an absolute closed one to foreign investors. The thesis, therefore, recommends differentiating between a friendly environment and a less-friendly one towards foreign investors. This is true since states that have been classified to follow the closed-door approach like Cuba and China, have allowed, within their investment regulations, certain rights to be awarded to foreign investors, as it will be elaborated in this section and in the following section as well.

Another way to look at investment protection, as it will be presented later in this thesis, is through the pre-investment protection, which takes place before the MNC or the investor decides to explore a new market and through the post-investment protection which takes place after the investor or the MNC invests overseas. These suggestions are thought to help make protection granted to investors more transparent and easily comprehended by investors willing to invest in a certain state.⁸⁴

The host state may decide to open the doors to foreign investors in order to benefit from their technology, know-how or in order to improve its economic and financial performances as is the case, for example, in the Middle East and Latin America where these states require that foreign investors have a local partner.⁸⁵ The foreign investor, on the other hand, is keen to invest abroad basically to for the expected economic gains.

See;
Brink, (*Chapter 2, n 3*) p 2.

⁸⁴ This will be discussed in section 3.4. of this thesis.

⁸⁵ For example, it was recorded that Middle Eastern states and those in Latin America do require from foreign inves-

For that, the host state may opt to regulate entry of foreign capital into the local market, as it will be further elaborated in the next section,⁸⁶ in order to ensure that its natural resources will not be exploited by the investor or to limit foreign investors' access to certain sectors due to the sectors' sensitivity. As such, the host state may decide to introduce codes and laws that govern the entry of foreign investment and perhaps grant certain incentives or apply certain restrictions directed at foreign investors.⁸⁷

On the other hand, the home state may issue a series of recommendations directed at its investors who are willing to invest abroad. These describe the host state's market are, the extent of protection granted to the foreign investor, any difficulties investors may find while investing in the host state and certain measures that investors may need to consider before investing in the host state. This is for example what the U.K and the U.S governments do where they issue recommendations to their investors who wish to invest overseas.⁸⁸ Home states' may also, for that purpose, sign BITs and MITs or other IIAs, as it will be further elaborated in later chapters.

tors to have a local partner to ensure technology transfer to the host state.

See;

Theodore H Moran ,*Harnessing Foreign Direct Investment for Development: Policies for Developed And Developing Countries* (CGD Books 2006). pp 6-7.

⁸⁶ This will further be elaborated in section 2.3.

⁸⁷ Salacuse (n 8) p 31.

And;

Jacques Morisset and Kelly Andrews-Johnson, *The Effectiveness of Promotion Agencies at Attracting Foreign Direct Investment* (World Bank Publications 2004) p 24.

⁸⁸ This will be further elaborated in chapter 3.4.

In general, national legal regimes of the host state play a vital role in promoting the inflow of foreign capital.⁸⁹ In principle, any given state has the right to apply its own laws and regulations on its territories. For that, it has the right to introduce regulations that govern certain aspects. For example, it has the right to regulate the investment of foreign capital in its territories. In addition, making sure that national laws are not imposing unreasonable restrictions on the making of payments and transfers with relation to the foreign investment is also an important point that the host state needs to consider.⁹⁰ This is true even in investments made in the financial sector where it was proven that there is a positive relationship between such investments and economic development.⁹¹

⁸⁹ See;

Simon Crotti, Tony Cavoli and John K. Wilson, 'The Impact of Trade and Investment Agreements on Australia's Inward FDI Flows' (2010) 40 Australian Economic Reports 4, p 270.

According to Alfaro, countries basing its laws on common law traditions do offer greater protection to investors.

See;

Laura Alfaro, Sebnem Kalemli-Ozcan, Selin Sayek and Areendam Chanda, 'FDI and Economic Growth: The Role of Local Financial Markets' (2004) 64 Journal of International Economics, pp 18-19.

⁹⁰ Ibrahim FI Shihata, *Legal Treatment of Foreign Investment* (Martinus Nijhoff Publishers 1993) p 267 - 309.

And;

Maria V Carkovic and Ross Levine, 'Does Foreign Direct Investment Accelerate Economic Growth?' (Social Science Research Network 2002) p 1.

Article can be found at:

<<http://papers.ssrn.com/abstract=314924>>

Last accessed on the 18th of January 2013.

And;

Other resources for the idea presented in the body of the work include:

Beata Javorcik, 'Does Foreign Direct Investment Increase the Productivity of Domestic Firms? In Search of Spillovers Through Backward Linkages' (Social Science Research Network 2003) p 1.

Article can be found at:

<<http://papers.ssrn.com/abstract=337740>>

Last accessed on the 18th of January 2013.

And;

D.N Rao, 'Analysing Risks of Foreign Direct Investment in Emerging Economies: A Case-Study of Saudi Arabia' (Social Science Research Network 2007) p 1.

Article can be found at:

<<http://papers.ssrn.com/abstract=955264>>

Last accessed on the 18th of January 2013.

And;

Blanca Sanchez-Robles and Marta Bengoa-Calvo, 'Foreign Direct Investment, Economic Freedom and Growth: New Evidence from Latin-America' (Social Science Research Network 2003) p 4.

Article can be found at:

<<http://papers.ssrn.com/abstract=353940>>

Last accessed on the 18th of January 2013.

And;

Nathan M Jensen, *Nation-States and the Multinational Corporation: A Political Economy of Foreign Direct Investment*, (Princeton University Press 2010) p 1

⁹¹ This idea was cited by Eller, Harris and Steiner's work.

See;

Markus Eller, Peter Haiss and Katharina Steiner K, 'Foreign Direct Investment in the Financial Sector: The Engine

The introduction of such regulation by the host state, i.e. one regarding foreign capital's access to the host state's market is a method taken by the host state to encourage the inflow of foreign capital in order to stimulate local economy and improve labor skills and to advance technologically.⁹²

Normally, investors are lured by what foreign markets have to offer and they are attracted to the markets that offer them security for their investments and offer them, at the same time, the freedom to invest in various sectors without limitations and with favorable trade policies.⁹³ Whereas, on the other hand, investors, due to the market's capacity and potentials, may consider investing in certain places that does not offer proper or minimum protection for their investments and property rights.⁹⁴

For that purpose, investors normally, even when investing in developing markets that do not offer much protection, may decide to invest there due to the coordination present

of Growth for Central and Eastern Europe?' (Social Science Research Network 2006) p 31.

Article can be found at:

<<http://papers.ssrn.com/abstract=875614>>

Last accessed on the 18th of January 2013.

⁹² Javorcik (*Chapter 2, n 90*) p 1.

And;

Rao (*Chapter 2, n 90*) p 1.

And;

Sanchez-Robles and Bengoa-Calvo (*Chapter 2, n 89*) p 4.

And;

Jensen (*Chapter 2, n 91*) p 1.

And;

According to Jürgen, these mentioned incentives are some of what the host state can introduce in order to facilitate and attract foreign investments.

See;

Jürgen, (*Chapter 2, n 7*) pp 689- 690.

⁹³ Yi Wu, Dimitri G. Demelcas, Balazs Horvath and Elina Ribakova, 'Foreign Direct Investment in Southeastern Europe: How (and How Much) Can Policies Help?' (International Monetary Fund 2005) pp 5-6.

⁹⁴ Depending on the protection granted, investors may opt for different types of investments. For example, some may opt for JVs while others may opt for licensing.

See;

Kamal Saggi, 'Trade, Foreign Direct Investment, and International Technology Transfer: A Survey' (2002) 17 The World Bank Research Observer, p 38.

between home and host states. Such coordination is through agreements ratified and signed by both states. As such, Foreign investors may feel more at ease when they know that their properties will not be subject to expropriation or that, if an action of such nature takes place, they won't end up without compensation that is fair, equitable or prompt, as this will be examined later on. Once investors feel their property rights are threatened, investors will leave the host state. This was, for example the case of Coca Cola in India. Before returning to India in 1993, the Coca Cola Company left India in 1977 after it refused giving its recipe to the Indian government.⁹⁵

MITs as well as BITs pose the perfect example for drawing measures of expropriation and protection of investments. For example, the Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur of 1994 stated, in article 4, measures of expropriation where it prohibited any action leading to expropriation or nationalization unless such actions were taken for the public's interest and on a non-discriminative basis.⁹⁶

Foreign investors may feel more at ease, even with the presence of BIT or MIT between the home and host states, if there is insurance or a guarantee provider who is willing to insure or guarantee against some of the high-risks that they may encounter while investing abroad. This is where ECAs, the MIGA and insurance companies come in, as it will

⁹⁵ This information on Coca Cola's investment in India can be found at:
Paul Gallant, '10 Biggest Overseas Blunders' (*HSBC Global Connections*, 10 April 2014).
Article can be found at:
<<https://globalconnections.hsbc.com/brazil/en/articles/10-biggest-overseas-blunders-en>>
Last accessed on the 3rd of December 2015.

⁹⁶ Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur (1994) Article 4
This article also calls for the indemnification of the investor for expropriation and for damages caused by war or other armed conflicts.
Article 4 was Translated from Spanish.

be examined in chapter 4. ECAs, MIGA and other political and investment risk insurance providers are considered as a *pre-investment* protection since the investor seeks the services of such agencies prior to embarking on an investment venture abroad.

Some of the forms of cooperation between the home and host states, with respect to promoting investment, could be inspired by the example of the movement made by Luxembourg and Belgium. The Belgium-Luxembourg Economic Union (BLEU) founded in 1921, recommended the establishment of a united market between Belgium and Luxembourg.⁹⁷ This Agreement led, in 1948, to the Benelux Customs Union.⁹⁸

Moreover, with respect to the effort directed at the protection of foreign investors' property rights, arbitration is considered as a *post-investment protection* mechanism. As it will be further highlighted in coming chapters, arbitration plays a vital role in retrieving the investors' property rights that have been unlawfully taken from them by the host state or by any of its representatives.⁹⁹ Indeed, the International Center for Settlement of Investment Disputes (ICSID) has been created for that purpose and, as it will be examined later on, it has been used by many investors to retrieve their property rights. Another dispute resolution center that is concerned with commercial disputes is the International Chamber of Commerce (ICC).¹⁰⁰

In that sense, the first and most important step in the protection of investors and investments is the one offered by the home state and that offered by the host state. This is

⁹⁷ Rudolf Bernhardt, *Regional Cooperation, Organizations and Problems* (Elsevier Publishings 1983) pp 30-31.

⁹⁸ James Edward Meade, 'Benelux: The Formation of the Common Customs' (1956) 23 *Economica* p 201.

⁹⁹ The role of arbitration will be discussed in chapters 3.1, 3.2, 3.4.

¹⁰⁰ *ibid.*

normally followed by the protection offered in public international law to investors through diplomacy, BITs, MITs and the general rules of public international law as it will be explained in detail in the coming chapters. Then comes contractual obligations and the role of arbitration as a protection mechanism as it will be examined in the coming chapters and finally the role of ECAs, multilateral investment agencies and insurance companies. Though it shall be clarified that these won't be discussed in this order rather they will be presented in accordance with the theme of each of the following chapters.¹⁰¹

It can be concluded that the relationship between the legal regimes of the home state and the host state, in one hand, and foreign investors, on the other, is as follows; the more the applied regulations of the host state are towards the protection of foreign investors, the more secure and confident investors feels while investing there and, therefore, the more likely they will decide to invest there. Whereas, the more complicated the regulations of the host state are towards foreign investors, the further consideration investors will put in and, possibly, dissuade them from investing there.¹⁰² It is noted that this is not always the case where investors, at many times, choose to take risks due to the market potential of the host state. This risk is mainly a political one. Though there maybe restriction to foreign investors' access to the host state's market, still investors will find a way around it, take the risk, and invest in order to maximize their profits.

¹⁰¹ Arbitration per se is not a protective measure rather it is a way to ensure that any infringement to the property rights of the investor will not go without proper compensation. Though, and because of that, as it will be elaborated in Chapter 3, arbitration could be a protective measure as is the case with ICSID.

¹⁰² This has also been suggested in the work of Lim.

See;

Ewe-Ghee Lim, *Determinants of, and the Relation Between, Foreign Direct Investment and Growth: A Summary of the Recent Literature* (International Monetary Fund 2001) pp 12-13.

2.3. Entry Requirement into Foreign Markets for FDIs

The mainstream view of entry requirements of foreign investors is seen through two approaches. These are the open-door approach and the closed-door approach. Though this in theory is a helpful distinction it is however, inaccurate.

The thesis recommends distinguishing between a foreign investment-friendly environment and a less-friendly environment opposed to open-door and closed-door since there is no absolute open-door or closed-door towards foreign investors. This is true since host states claiming to be open to investors do have certain limits and restrictions as to which sector foreign investors may invest in and as to the number of shares they are allowed to hold. Same applies with states following the closed-door approach where, even those, do, to a certain extent, allow foreign investors to invest in its territories within certain sectors and with limited shares.

Rules of entry into the local market are left to the host state's discretion. The host state may limit foreign investment to certain sectors or even to a proportion of shareholding. For example, it has been suggested that foreign investors may face certain restrictions when investing in properties whether such investments were movable or immovable ones.¹⁰³ The host state has also the right to reserve to its investors or to itself the right to invest in certain sectors.

¹⁰³Myers S. McDougal, Harold D. Lasswell and Lung-Chu Chen, 'The Protection of Aliens from Discrimination and World Public Order: Responsibility of States Conjoined with Human Rights' (1976) 70 *The American Journal of International Law*, p 435.

In that respect, we have two types of approaches adopted by the host state, the open-door approach that allows foreign investors to invest in any sector they may wish to invest in. Though there is no complete open-door approach, it is noted that some markets are more liberal and welcoming to foreign investors than others. The United States, United Kingdom and the European Union have followed this approach for example.

On the other hand, there are states that have opted not to open their doors to foreign investors or they have allowed them to enter into their markets with a set of restrictions and allowed them to invest only in certain locations and/or in certain sectors. Normally, countries that do not wish to allow investors to enter into their market but still want to benefit from the know-how that foreign investors possess or the technology they have or to benefit economically from them, have established what is known as Free Economic Zones. These Economic Zones have helped host states like Malaysia, for example, attract FDIs in the manufacturing sector.¹⁰⁴ This is a popular approach followed by China and the UAE as well as a number of other states in the Middle East. As a result, the UAE was ranked as the 42nd state in receiving foreign capital and China was the 5th.¹⁰⁵

¹⁰⁴ See;

Theodore H. Moran, *Harnessing Foreign Direct Investment for Development: Policies for Developed and Developing Countries* (CGD Books 2006). p 6.

¹⁰⁵ These statistics can be found at the CIA Factbook website:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#ch>>

Last accessed on the 20th of August 2015.

China, according to the Global Opportunity Index on Attracting Foreign Investment ranked 52nd internationally while the UAE came in 51st.

With Regard to Quality of Regulations, China came in 42nd while the UAE ranked 17th.

As for the Rule of Law, China ranked 42nd while the UAE ranked 40th.

Finally, as for the Ease of doing business in these countries, China came in 75th while the UAE came in 29th.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

And at;

Information on this can be found at:

<<http://www.globalopportunityindex.org/pdf/2015-Global-Opportunity-Index.pdf>>

This aside, foreign investors when investing abroad, may be subject to a minimum capital requirement in order to set up their investments in a given geographical zone. Indeed, foreign investors are expected to enhance the host state's economy. In order to ensure the host states' benefits from the investor, it may require that the investor invest a minimum capital. For example, in Ethiopia foreign investors are expected to contribute a minimum of 100,000 U.S. Dollars towards their investment and in Kenya 500,000 Dollars.¹⁰⁶

Once foreign investors decide to invest in a given state and after they fulfill the entry requirements, investors may need to seek prior approval from the local authorities.¹⁰⁷ It should be stated, however, that this might be relaxed if the host state and home state agreed on such matter in a BIT or in a MIT. An example to that is France. Before 1990, in France, any foreign investor willing to invest there had to seek prior approval from a governmental agency. This changed after 1990 for EU investors as a result of the EU's initiative to apply articles 34 and 35 of the Treaty on Functioning of the European Union (TFEU) on the freedom of movement of capital and persons.¹⁰⁸

Last Accessed on the 1st of September 2015

And;

<<http://www.globalopportunityindex.org/opportunity.taf?page=methodology>>

Last Accessed on the 1st of September 2015

In general, and perhaps the highest ranked state in the Middle East with regard to the Quality of Regulations is Oman in the 16th place internationally whereas when it comes to the Rule of Law matrix Israel came in 1st in the Middle East and 7th Internationally. As for the Ease of Doing Business in the Middle East, Oman came in 1st and 14th internationally.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

¹⁰⁶ This information can be found at:

Investing Policy Review: Kenya, (UN Conference on Trade and Development 2005) p 54.

And;

De La Medina Soto and Ghossein, (*Chapter 1, n 2*) p15

¹⁰⁷ Alan C Swan and John F Murphy, *Cases and Materials on the Regulation of International Business and Economic Relations* (Matthew Bender and Company 1999) p 707.

¹⁰⁸ Treaty on Functioning of the European Union articles 34 and 35.

To elaborate more on the EU's system, Article 49 of the TFEU grants EU nationals the right to freely move and establish any form of investment including branches of existing investments in any member state.¹⁰⁹ While articles 28 and 29 of the TFEU, on the other hand, handled the issue of establishment of a unified tariff system where goods transported are expected to enjoy "free circulation" between member states once they have been subjected to customs duty in one of the member states.¹¹⁰

Not only that, the treaty also added the concept of freedom of movement of capital in article 63.¹¹¹ The TFEU in article 207 talked about foreign investment specifically in relation to unification of certain investment-related measures.¹¹² Add to that, with regard to FDI, the treaty suggested the complete liberalization between member states of the EU on the movement of capital and, as well, between EU member states and third countries.¹¹³ In that respect and in order to consider the application of said articles with regard to movement of capital, the actual movement of capital may occur, physically, as transfer of financial assets only if it was in relation to the investment fund and not as a remuneration for a service.¹¹⁴

Though the EU has adopted an open-door policy towards foreign investors it did, however, introduce a special regulation directed at mergers and acquisitions. Council Regulation (EC) No 139/2004 is introduced with the purpose of regulating Mergers and Ac-

¹⁰⁹ *ibid*, Article 49.

¹¹⁰ *ibid*, Articles 28(1) And 29.

¹¹¹ *ibid*, Article 63.

¹¹² *ibid* Article 207.

¹¹³ *ibid* Articles 63 and 66.

¹¹⁴ See:

Casiti Case: Case 203/80 *Casiti* [1981] ECR 2595.

and;

Luisi and Carbone Case: Joined Cases 286/82 & 26/83 *Luisi and Carbone* [1984] ECR 377.

and;

Dimopoulos (*Chapter 2, n 72*) pp 36-39.

quisitions and it stipulates the acquisition of a prior notification from the Commission of Mergers and Acquisitions before the merger can be approved.¹¹⁵ This open-door approach resulted in having a number of EU states being ranked as top destinations desired by foreign investors. For example, Germany, Belgium, France, Spain, Ireland, Netherlands, Italy and Sweden all ranking within the top 20 destinations.¹¹⁶

The TFEU is a detailed multilateral treaty establishing a number of rights and eliminating restrictions and working towards the establishment of a single market as well as for the harmonization of laws and regulations covering matters related to education, environment, freedom of movement of goods and services, capital and persons and works, as well, for the establishment of a central European bank. It also suggests a number of matters related to the financial and economic system of member states.

¹¹⁵ E.U. Council Regulation (EC) No 139/2004, Article 4.

Retrieved From:

<<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2004:024:0001:0022:en:PDF>>

Accessed on the 9th of August 2012

¹¹⁶ Germany topped the list ranked 4th just after another member of the EU, the United Kingdom which was the 3rd proffered destination desired by foreign investors. In the 6th place was Belgium followed by France in the 7th. Switzerland, which has many agreements signed with EU, came in 8th. Spain and Ireland came in 11th and 12th respectively followed by the Netherlands in the 15th place and Italy in the 17th. Sweden came in the 18th place.

The full list can be found on the CIA Factbook website:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

Germany, according to the Global Opportunity Index on attracting foreign Investment ranked 18th internationally while the Belgium came in 23rd. Whereas France ranked 32nd and Spain came in 40th. Ireland ranked 9th and Netherlands came in 11th. Finally, Italy came in 61st while Sweden came in 5th.

With Regard to Quality of Regulations, Germany ranked 14th while the Belgium ranked 23rd. France ranked 32nd and Spain came in 49th. Ireland ranked 20th and Netherlands came in 7th. Finally, Italy came in 86th while Sweden came in 5th.

As for the Rule of Law, Germany ranked 21st while the Belgium ranked 15th. France ranked 29th and Spain came in 53rd. Ireland ranked 5th and Netherlands came in 28th. Finally, Italy came in 77th while Sweden came in 10th.

Finally, as for the Ease of doing business enthuse countries, Germany ranked 12th while the Belgium ranked 36th. France ranked 47th and Spain came in 61st. Ireland ranked 8th and Netherlands came in 10th. Finally, Italy came in 73rd while Sweden came in 15th.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

The TFEU sets a good example of a multilateral effort directed at easing up investments and eliminating restriction imposed on investors. It is also an example of the role that legal regimes play in encouraging foreign investment and in protection and facilitation of these investments as it will be further elaborated in further chapters.

To take this further, one of the EU's member states, Italy which earned the 17th spot in attracting foreign investment and the 14th as a capital exporting state,¹¹⁷ followed a more welcoming approach to foreign investors where it did not impose many requirements on them while granting them with adequate protection. This is viewed in the Italian Civil Law where foreign investors, on the basis of reciprocity, are granted national treatment.¹¹⁸ It shall be noted, however, that such reciprocity comes in the form of a prior agreement through BITs or other forms of IIAs between Italy and another state.¹¹⁹ Not only that but the Italian Court of Cassation and in light of the Italian constitution opted to grant total freedom to protect the rights an investor may possess.¹²⁰

¹¹⁷ The data was provided by the CIA Factbook and is available at:

For Capital Exporting Countries Ranking please visit:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2199rank.html#sp>>

Last Accessed on the 10th of August 2015.

For Attracting Foreign Investment Country Ranking please visit:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

¹¹⁸ Il Codice Civile Italiano, Capitolo 1, Articolo 16 (Translated from Italian)

This can be found at:

<[http://www.jus.unitn.it/cardozo/obiter dictum/codciv/Prel.htm](http://www.jus.unitn.it/cardozo/obiter_dictum/codciv/Prel.htm)>

Accessed on the 23rd of August 2012

¹¹⁹ Ministero degli Affari Esteri website (Translated from Italian)

Under:

Lo Straniero E La Condizione Di Reciprocità

<<http://www.esteri.it/MAE/IT/Ministero/Servizi/Stranieri/CondizReciprocita/default.htm?LANG=IT>>

Accessed on the 21st of May 2015

¹²⁰ Dennis Campbell (ed), *International Protection of Foreign Investment* (Volume II, Bloomsbury Professional 2008) p. 56.

The Italian law, when it comes to remittance, has no restrictions whatsoever on the exportation of capital and profits or on the choice of currency.¹²¹ However, there are some restriction on the entry into the Italian market by foreign investors as it was cited in article 2510 of the Italian Civil Law.¹²² These, according to the Italian text, are certain activities excised by companies in which foreign interest is represented.¹²³

In North America, a similar movement to that in the EU designed to encourage foreign investment took place. As it will be examined later on in the research in more details, the North American Free Trade Agreement (NAFTA) adopted certain measures directed at attracting and promoting investments.¹²⁴ In that sense, the NAFTA introduced certain provisions aimed at eliminating tariffs completely, removing investment barriers and at removing non-tariff barriers like import licenses for example.¹²⁵ This agreement is considered the first one concluded between developed states and developing ones.¹²⁶

The treaty is thought to ensure that investments will not be subjected to government policies aimed at restricting investors' right to benefit from their property. Applying the provisions of NAFTA means that investors will be able to receive treatment equal to domestic investors in the United States, Mexico and in Canada.¹²⁷ It also means that temporary entry for business persons of member states to conduct their investments will

¹²¹ *ibid* at 59.

¹²² Il Codice Civile Italiano (n 124) Capitolo XI, Articolo 2510 (Translated from Italian)

Retrieved from:

<<http://www.altalex.com/index.php?idnot=37062>>

Accessed on the 21st of May 2015

¹²³ *ibid*.

¹²⁴ This will be elaborated in chapters 3.2 and 3.4.

¹²⁵ M. Ayhan Kose, Guy M. Meredith and Christopher M Towe, *How Has NAFTA Affected the Mexican Economy?: Review and Evidence* (International Monetary Fund 2004) pp 7-8.

¹²⁶ *ibid* at 6.

¹²⁷ These will be further elaborated in chapter 3.2.

be allowed and eased up.¹²⁸

For that, the NAFTA may be considered to have an open-door approach towards investors from member states. This may not be as open to investors coming from third states, unlike the case in the EU. This is true since investors coming from non-NAFTA member states will still be subjected, in Mexico for example, to certain laws limiting their investments in some sectors.¹²⁹

TFEU is thought to have an open-door approach to member states and third-party investors alike where, even in member states' local laws that have been adjusted to fit the spirit of the EU's approach, are still able to make investments in more sectors than those available in NAFTA member states. Though sometimes certain investments may require the prior approval of local bodies of the host state, it is still however more open and more liberal than that in NAFTA.¹³⁰

In Latin America, the Andean community had a similar approach towards foreign investors to that of the EU. Though it is not as open as the EU's it is, however, considered more liberal than other developing countries and then capital importing countries like

¹²⁸ Some information on Canada and Mexico:

Mexico, according to the Global Opportunity Index on Attracting Foreign Investment ranked 69th internationally while the Canada came in 6th.

With Regard to Quality of Regulations, Mexico ranked 67th internationally while the Canada came in 11th place.

As for the Rule of Law, Mexico ranked 77th internationally while the Canada came in 5th place.

Finally, as for the Ease of doing business, Mexico ranked 71st internationally while the Canada came in 7th place. This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

As for attracting foreign investment, Mexico came in 19th while Canada was 9th internationally

The data was provided by the CIA Factbook and is available at:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

¹²⁹ Mexican Foreign Investment Law of 1993. Capital 1, Chapters II-III.

¹³⁰ This will further be discussed in chapter 3.2.

China. The Andean Commission which, was formed and created between the Andean nations in 1969, as a result of the Cartagena Pact, to attract foreign investment into the region and resulted in the creation of the Andean Sub-Regional Common Market known as the ANCOM.¹³¹ Though Bolivia, Colombia, Ecuador and Peru opted for the creation of this common market, Ecuador, however, is now considering leaving this common market since the Andean Community (CAN) decided to eliminate Ecuador's trade safeguards.¹³²

In Decisions 291 and 292 of the Andean Commission, the Andean community established the rules of engagement for foreign investors. Decision 292 was said to be tool of encouragement for sub-regional investors to get involved in multinational companies and it deals with ownership, nationality, origin, domicile and the purpose of invest-

¹³¹ Thomas Andrew O'keefe, 'How the Andean Pact Transformed Itself into a Friend of Foreign Enterprise' [1996] American Bar Association Issue 4, 30 The International Lawyer, p 812.

This article can be found at:

<http://0-www.heinonline.org.catalogue.urls.lon.ac.uk/HOL/Page?public=false&handle=hein.journals/intlyr30&men_hide=false&men_tab=citnav&collection=abajournals&id=821

Last accessed on the the 9th of August 2012

¹³² News Article:

Liz Scherffius, 'Ecuador Considering Withdrawal from Andean Community of Nations' TeleSur TV, (11 Feb 2015).

Article can be found at:

<http://www.telesurtv.net/english/news/Ecuador-Considering-Withdrawal-from-Andean-Community-of-Nations-20150211-0023.html>

Last Accessed on the 20th of August 2015

Andean Community member states ranked as follows with regard to attracting FDI; In first place came in Columbia ranked in the 34th place followed by Peru in the 49th, Ecuador in the 85th and finally Bolivia in the 88th.

This information can be found at:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last accessed on the 10th of August 2015.

Colombia, according to the Global Opportunity Index on Attracting Foreign Investment ranked 59th internationally while the Peru came in 64th. Whereas Bolivia ranked 91st and Ecuador came in 93rd.

With Regard to Quality of Regulations, Colombia ranked 73rd internationally while the Peru came in 58th. Whereas Bolivia ranked 52nd and Ecuador came in 34th.

As for the Rule of Law, Colombia ranked 753rd internationally while the Peru came in 59th. Whereas Bolivia ranked 119th and Ecuador came in 124th.

Finally, as for the Ease of doing business, Columbia, according to the Global Opportunity Index on attracting foreign Investment ranked 80th internationally while the Peru came in 86th. Whereas Bolivia ranked 95th and Ecuador came in 115th.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

ments.¹³³ Both decisions were specifically concerned with the treatment of foreign capital, trademarks, patents, licenses and royalties granted to investors in the technological sector. A new form of partnership as a mean for a foreign investor to enter the Andean Market was suggested through the formation of what is referred to as the Andean Multi-national Enterprise (AME). This method is open to member states investors who may own 100% of the shares of their investment and for non-member state investors who may own up to 40% of the shares of the investment through creating a normal partnership with a local investor.¹³⁴

Decision 292 introduced the AME and defined such investment as an enterprise of which foreign investors may own up to 40% of its shares and is domiciled or merged in one member state with investors from, at least, two different member states owning up to 60% of the equity of this enterprise or investment.¹³⁵ In this type of investment, the foreigner is expected to give up their right of management and control in the enterprise.¹³⁶

¹³³ John R Pate, 'Andean Group: Commission Decision 291 -- Common Code for the Treatment of Foreign Capital and on Trademarks, Patents, Licenses and Royalties' (1991) 30 International Legal Materials 1283. Paragraph 4.

Article can be found at:

<<http://0-www.lexisnexis.com.catalogue.ulrls.lon.ac.uk/uk/legal/search/homesubmitForm.do>>

Last accessed on the 9th of August 2012

¹³⁴ See;

Dominic A. Perenzin, 'Multi-national companies Under the Andean Pact - A Sweetener for Foreign Investor' International Lawyer. (1973), pp. 398-401.

Article can be found at:

<<http://0-www.heinonline.org.catalogue.ulrls.lon.ac.uk/HOL/Page?public=false&handle=hein.journals/intlyr7&collection=journals&id=406>>

Last accessed on the 9th of August 2012

¹³⁵ Andean Group: Commission Decision 292 - Uniform Code on Andean Multinational Enterprise, American Society of International Law, Washington, D.C. International Legal Materials, Volume 30, Number 5 (September 1991) Decision No. 292 of March 21st 1991.

Chapter I Articles 1(a), 1(c), and 1(d).

Article can be found at:

<<http://0-www.lexisnexis.com.catalogue.ulrls.lon.ac.uk/uk/legal/search/homesubmitForm.do>>

Last accessed on the 9th of August 2012

And;

Perenzin (*Chapter 2, n134*) p. 398.

¹³⁶ Decision No. 292, Chapter I Articles 1(f).

It is worth mentioning that contributions made by foreigners in such investments, may be in any convertible currency as well as in the use of tangible or intangible goods.¹³⁷

The Community, also, suggested a mechanism of oversight over the behavior of foreign investors through the creation of national agencies in each member state. These agencies are in charge of monitoring foreign investors' compliance with Decision 291. They are also responsible for overlooking the operations of foreign investors and making sure they are complying with the spirit of the decision.¹³⁸ With regard to treatment of foreign investors within member states of the Andean Community suggested that such treatment should not be less or more than that accorded to national investors.¹³⁹

Normally, entry into the Andean Community member states by foreign investors, according to Decision 291, is open without any restrictions.¹⁴⁰ This decision has granted investors in the technological sector a special treatment with the right to choose a freely convertible currency and without any restrictions on their right to remittance of capitalization no matter, according to the text, what nature or form it was and whether these were to be sent to the home state or elsewhere.¹⁴¹ The Decision also granted investors the option to choose a freely convertible currency and the right to repatriate their capital

¹³⁷ *ibid* Chapter I Article 3.

¹³⁸ Decision No. 291, Chapter III Article 11.

¹³⁹ Covey T. Oliver, *The Andean Foreign Investment Code: A New Phase in the Quest for Normative Order as to Direct Foreign Investment*, 66 *Am. J. Int'l L.* (1972), p.767

Article can be found at:

<http://0-www.heinonline.org.catalogue.urls.lon.ac.uk/HOL/Page?public=false&handle=hein.journals/ajil66&men_hide=false&men_tab=citnav&collection=journals&id=770>

Last accessed on the 9th of August 2012

¹⁴⁰ Pate (*Chapter 2, n133*) paragraph 4.

¹⁴¹ *ibid*

And;

Decision No. 291, Chapter II Articles 2 to 5.

anytime and granted investors, as well, the right to take advantage of the Andean Free-Trade Zone.¹⁴²

Finally, as for tariffs, the EU, as examined earlier, granted the right of transfer of goods between member states without any extra tariffs imposed on the investor. Member states of the Andean Community imposed a similar measure directed at producers of goods and services in member states. In that sense, foreign investors in a member state of the Cartagena Agreement may benefit from the tariff reduction program upon transfer of products produced in one of the member state to another member state.¹⁴³

The United States is ranked the first in attracting foreign investment and in exporting capital and also follows the open-door policy towards foreign investors.¹⁴⁴ However, there is a reserved right to the American Congress to regulate or to deny the establishment of a foreign investment.¹⁴⁵

Moreover, there are a number of sectors that are closed to foreign investors in the U.S. or require strict conditions. These, for example, include owning U.S. aircrafts, unless the

¹⁴² O'keefe, (*Chapter 2, n131*) p 819

¹⁴³ Decision No. 291, Chapter II Article 8.

¹⁴⁴ The data was provided by the CIA Factbook and is available at:

For Capital Exporting Country Ranking please visit:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2199rank.html#sp>>

Last Accessed on the 10th of August 2015.

For Ranking of Countries Attracting Foreign Investment please visit:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

¹⁴⁵ Robert H Mundheim and David W Heliak, 'American Attitudes Toward Foreign Direct Investment In The United States' (1979) 2 *Journal of Comparative Corporate Law and Securities Regulation* 225

Article can be found at:

<[https://www.law.upenn.edu/journals/jil/articles/volume2/issue4/MundheimHeliak2J.Comp.Corp.L.&Sec.Reg.221\(1979\).pdf](https://www.law.upenn.edu/journals/jil/articles/volume2/issue4/MundheimHeliak2J.Comp.Corp.L.&Sec.Reg.221(1979).pdf)>

Last accessed on the 9th of August 2012.

owner is a permanent resident of the U.S.¹⁴⁶ Foreign investment in the defense sector, TV & Radio and other communications mediums along with the energy and mineral resources sectors and in the maritime industry have all been closed to foreign investments.¹⁴⁷

On the other side, the closed-door policy was followed in China. China holds the 5th position in attracting foreign investments and 12th in exporting investment.¹⁴⁸ Investors were, and still are, attracted to the Chinese market due to its size, low cost of production and to the cheap labour costs it has to offer.¹⁴⁹ For that, the Chinese government took significant steps to attract foreign investors, through the creation of special economic zones, introduction of tax and land incentives and through applying priority status to certain foreign investors in some cities.¹⁵⁰

¹⁴⁶ *ibid* at 228.

¹⁴⁷ *ibid* at 228-229.

¹⁴⁸ The data was provided by the CIA Factbook and is available at:

For Capital Exporting Country Ranking please visit:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2199rank.html#sp>>

Last Accessed on the 10th of August 2015

For Ranking of Countries Attracting Foreign Investment please visit:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on 10th August 2015.

¹⁴⁹ Mike Saxon, *An American's Guide to Doing Business in China: Negotiating Contracts and Agreements; Understanding Culture and Customs; Marketing Products and Services*, vol 1 (Adams Media 2006) p 8.

And;

Jun Fu, *Institutions and Investments: Foreign Direct Investment in China During an Era of Reforms* (University of Michigan Press 2000) pp 8-9.

And;

Main Determinants and Impacts of Foreign Direct Investment on China's Economy (Directorate for Financial, Fiscal And Enterprise Affairs, Working Papers On International Investment, Number 2000/4, December 2000) p 15.

Document can be found at:

<<http://www.oecd.org/dataoecd/57/23/1922648.pdf>>

Last accessed on the 23rd of August 2012.

¹⁵⁰ Main Determinants and Impacts of Foreign Direct Investment on China's Economy (*Chapter 2, n149*) p 15.

Obtaining an approval from the Chinese government is the first step to enter the Chinese market.¹⁵¹ That said, foreign investors often opt to invest in China through forming a JV with an existing Chinese investor in order to minimize any risks associated with their investment. It shall be noted, however, that nowadays the trend is heading towards having foreign investors owning in full their investment with a wholly-owned foreign enterprise reaching up to 77% of the total foreign investments in China in 2012.¹⁵² It is observed that in the Chinese Equity Joint Venture Law expropriation of a Chinese JV may take place when the public interest requires such action and, in this case, an adequate compensation will be granted.¹⁵³

As for tax exemptions, according to the Chinese Joint Venture law, foreign investors may benefit from a partial tax exemption should he decide to reinvest their earnings within China.¹⁵⁴ Not only that, but the law goes further with regard to remittance and allows remittance of earnings only after the parties have performed their legal and contractual obligations and only in the currency specified in JV contract.¹⁵⁵

Under any circumstance, investors need to consider the legal form of their investment and whether they wish to maintain controlling powers over it or they consider giving it up throughout the process of the investment. It is also worthwhile mentioning that these

¹⁵¹ Shoushuang Li, *The legal environment and risks for foreign investment in China*, (Springer-Verlag Berlin and Heidelberg GmbH & Co. KG, 2007) P 7.

¹⁵² KPMG, *Investment in the People's Republic of China* (KPMG 2013)

Document can be found at:

< <https://www.kpmg.com/CN/en/IssuesAndInsights/ArticlesPublications/Documents/Investment-in-China-201311.pdf>>

Last accessed on the 18th of February 2016.

¹⁵³ The Chinese Equity Joint Ventures Law. Article 2.

The law can be found at:

<<http://www.china.org.cn/english/DAT/214773.htm>>

Last accessed on the 9th of August 2012.

¹⁵⁴ *ibid.* Article 8

¹⁵⁵ *ibid.* at Articles 8 & 11.

entry requirements are normally present in order to protect the local market from being exploited by foreign investors. In that respect, ethical behavior of the foreign investor plays a role here, as well, when it comes to the lack or absence of regulation in the host state.

Moreover, the home state may have regulations preventing their investors from engaging in unethical behavior such as bribery. This is the case for example with U.S. investors who are prohibited from engaging in bribery throughout their course of investment overseas.¹⁵⁶ Similarly, the U.K. put in force an Act prohibiting UK investors from engaging in acts of bribery in their ventures overseas.¹⁵⁷

It is noted that some ECAs included clauses in their investment guarantee contracts that the investor acknowledges that his contractual right would be null and void should he be found guilty of bribing public officials of the host state.¹⁵⁸

BITs and MITs tend to have certain clauses related to the access and admission of investors to the host state's market. As such, they would include clauses stating that any investment being admitted to the host state should only be granted such admission in accordance with the legislations of such state.¹⁵⁹ This clause may take one of many forms.

To elaborate more, a BIT or MIT may include a clause like the following:

“Each State shall encourage and create favorable conditions for nationals and companies of the other State to invest capital in its terri-

¹⁵⁶ Gary Clyde Hufbauer and Rita M Rodriguez, *The Ex-Im Bank in the 21st Century: A New Approach?* (Peterson Institute 2001) p 202.

¹⁵⁷ UK Bribery Act of 2010, Chapter 23, Clause 6.

¹⁵⁸ Gordon (*Chapter 1, n32*) p 100.

¹⁵⁹ Shihata (*Chapter 2, n90*) p 232.

tory, and, subject to its right to exercise powers conferred by its laws, shall admit such capital [such investment].”¹⁶⁰

This clause is one used in both German and UK BITs.¹⁶¹

It is noted that there is still no absolute open-door policy towards foreign investors in the sense that there are still some restrictions as to which economic sector can a foreigner invest in.

As stated earlier, in the U.S., a foreign investor is restricted from investing in areas related to national security.¹⁶² While something like this is seen as a restriction, it is however a protective measure to the security of a nation. Therefore, the comparison made between the two policies is rather made between a friendly and a less-friendly policy towards foreign investors and as such it would have been more accurate to rename the open-door policy as the foreign investor-friendly policy, since there are some restrictions.

Normally, whichever is the desired approach of the host state while designing foreign investment policies, there are common basis between all of them in the sense that they specify, both, the prohibited and favored sectors for foreigners, set their desired economic contribution expected from the foreign investment, draw the JV requirements and any

¹⁶⁰ This was quoted from:
Shihata (*Chapter 2, n90*). p 232 under Admission-Representative Provisions Type B.

¹⁶¹ *ibid* at 233.

¹⁶² More information on the sectors open for foreign investment and those restricted to them can be found at the US Foreign Investment and National Security Act of 2007 and the Exon-Florio Amendment of 1988.

performance requirements and finally, they provide rules on the ownership and acquisition of land and natural resources.¹⁶³

When talking about Free Trade Zones (FTZs), these are not necessarily a product of developing states rather may, as well, be found in developed ones. For example, the USA has established a number of FTZs that it refers to as Foreign Trade Zones in various states. These are specific location in various cities across the United States where companies can use special procedures that help encourage U.S. trade by allowing delayed or reduced duty payments on foreign merchandise.¹⁶⁴

Investors, in the U.S., resorting to such zones benefit from duty exemption on re-exporting of goods and services, deferral of custom duties and federal taxes imposed on importing goods and services, introverted tariffs, special tax exemption for foreign imports and exports and sometimes the eligibility for state or city benefits.¹⁶⁵ For example, in the state of New York there are fifteen Free Trade Zones while in the state of California there is up to seven Free Trade Zones.¹⁶⁶ These are, typically, designed to encourage foreign investors to enter into the local market and import their goods and services without having to worry about tax duties or other tariffs and allows investors producing finished goods and services in such zones, specific incentives and exemptions.¹⁶⁷

¹⁶³ Salacuse (*Chapter 1, n11*) p 92.

¹⁶⁴ Article can be found at:

<<http://enforcement.trade.gov/ftzpage/info/zone.html>>

Last accessed on the 25th of August 2015.

¹⁶⁵ This information can be found at:

<<http://enforcement.trade.gov/ftzpage/info/userbenefits.html>>

Last accessed on the 25th of August 2015.

¹⁶⁶ Number Free Trade Zones in the USA.

This information can be found at:

<<http://enforcement.trade.gov/ftzpage/letters/ftzlist-map.html#new%20york>>

Last accessed on the 18th of February 2016

¹⁶⁷ Free Trade Zones in the USA

What can be noticed from studying the open-door and closed-door approaches towards investments in various states is that there is no absolute freedom of investment of foreign capital across all sectors. Though imposing restrictions may be understandable, this means, however, that such open-door is not so open and is still restricted in certain areas. For that it may be referred to the open-door approach as a friendly or liberal approach while the closed door is more of a less-friendly or restrictive approach towards foreign investments.

In that sense, some countries undertake measures to limit the investment in certain sectors, as seen previously, for the fear that a foreign investor may have access to sensitive information which would lead to the endangerment of the public's interest and, perhaps, the public's safety as well.¹⁶⁸

This issue is quite clear and present in investments made in the media sector. For example, India allows foreign investors to own equity partnership in publishing companies as long as such investment does not exceed 26% of the total shares of the publishing company.¹⁶⁹ In the U.S. there are some limitations imposed on foreign investors wishing to invest in the media sector as well.¹⁷⁰

Information can be found at:

<<http://www.cbp.gov/border-security/ports-entry/cargo-security/cargo-control/foreign-trade-zones/about>>

Last accessed on the 18th of February 2016

¹⁶⁸ De La Medina Soto and Ghossein (*Chapter 1, n2*) p 4.

¹⁶⁹ Salacuse (*Chapter 1, n11*) pp. 92-93.

¹⁷⁰ Mundheim and Heleniak, (*Chapter 2, n145*), p 228

Chile, on the other hand, is one of the countries that are more open towards foreign investments. In that respect, Chile is a restriction-free state when it comes to foreign investment in the media where foreign investors are allowed to own, in full, the equity of television and radio companies and in newspapers.¹⁷¹

Perhaps it would be safe to state that there is no state that is closed completely on itself or one that is hostile towards foreign investors. For example, Cuba developed a law in 1997 that is designed to attract, promote and protect foreign investment in Cuba. This country which suffered, until recently, from economic sanction imposed by the United States have managed to produce a somewhat open approach towards foreign investors where the law governing foreign investments can be compared with that applied within China.¹⁷² In general, save for some exceptions, the law permits foreign investors to own, in full, the equity of their investment.¹⁷³

The means to engage into financial, commercial or economic activities in Cuba is through one of the three following methods; Foreign investors may own 100% of the equity of an investment or they may choose to enter the Cuban market through JV with a Cuban partner or through what is known as an International Economic Association.¹⁷⁴

The law allows investing in almost all sectors excluding health and education. The law

¹⁷¹ Salacuse (*Chapter 1, n11*) p 93.

¹⁷² Cuba, Vietnam and some Caribbean and South East Asian states revised their investment regulations and opted for a more welcoming and open approach towards such investors.

This information can be found at:

Cheryl W. Gray and William W. Jarosz, 'Law and the Regulation of Foreign Direct Investment: The Experience from Central and Eastern Europe' (1995) 33 *Columbia Journal of Transnational Law*, p7.

¹⁷³ These exceptions include investments in the health and education sectors and in the armed forces institutions.

Law No. 77 Foreign Investment in Cuba Act 1997, Article 10.

¹⁷⁴ This information can be found under:

Cuban Foreign Investment Legislation

This is in the website of the Swiss Cuban Chamber of Commerce

<https://www.monroecollege.edu/uploadedFiles/_Site_Assets/PDF/Cuban-Economy-Foreign-Investment.pdf>

Last accessed on the 18th of February 2016

also protects foreign investors against expropriation unless such act took place for the public's interest and, if happened, such an act, entitles its owner the right to seek compensation which is to be reached by a recognized international assessment of business assets that is authorized by local authorities in case there was a disagreement on the amount of initial compensation.¹⁷⁵ Finally, the Cuban foreign investment law grants foreign investors the right to remittance and the right to convert and transfer their earning into a freely convertible currency without being subjected to taxes.¹⁷⁶

Investors are attracted to friendly and attractive investment laws and the more unattractive these laws are the more the host state loses both foreign and national investors.¹⁷⁷ The friendlier investment laws are of a given state, the more likely it attracts foreign investors. For example, Luxembourg was able to incorporate a number of companies due to its attractive investment laws.¹⁷⁸

In general, tax breaks, friendly labor and investment laws and proper protection of investments will encourage foreign investors to invest in the host state.¹⁷⁹ Though this may be true in developing countries that were able to attract investments, it is nevertheless still something that developing countries need to work on especially in places where the government still has a strong influence and pose a high risk to foreign investors. For that, ECAs play a role in the protection against political risk and against some commercial and financial risks as well.

¹⁷⁵ Law No. 77 Foreign Investment Act 1997 (*Chapter 2, n173*) Article 3.

¹⁷⁶ *ibid* Article 8.

¹⁷⁷ Guido Ferrarini and E Wymeersch, *Investor Protection in Europe* (Oxford University Press 2006), p 67.

And;

Checklist for Foreign Direct Investment Incentives Policies, (OECD 2003) p. 7.

¹⁷⁸ *ibid* at 91.

¹⁷⁹ Lim (*Chapter 2, n140*) pp 12-13.

2.4. Types of FDI Related Risks

The classic view towards FDI-related risks is based on a three-risk approach differentiating between political, commercial, and financial risks. This distinction is a good starting point; however, it is not accurate and doesn't help the investor or agencies covering these risks well especially due to the changing nature of risks. For that the thesis recommends distinguishing between five risks. The political, commercial and financial risks along with the political commercial risk and the political financial risk. The reason behind the suggested distinction is the fact that both acts falling under commercial and financial risks may be considered political and labeling them as purely as political risks would deny such acts their true nature.

Understanding clearly what a political risk is and what a financial and commercial risks are would help in understanding the need behind further elaboration of the different types of risks. This is true when talking about services covered by insurance companies and national, regional and international insurance programs where most of these agencies state that they cover against political risks. This is true since each agency covers against certain acts falling under various risk-categories and what is considered a covered political risk for one agency might not be covered by another. For that, the research recommends the use of the five-risk approach which should make things more transparent for both investors and insurance providers. This distinction is needed since it will help ECAs, Ex-Im Banks, insurance companies and other investment risk insurance providers state the category of risk they cover rather than stating actions they cover. For

example, MIGA is considered as one of the PRI providers along with national insurance programs. This may be true but it covers, as well, against other risks such as the financial risk.

The research recommends a new definition for risk after examining various definitions of the term and after examining its components. The various examined definitions in this section share in common an expectation of occurrence or nonoccurrence of an event or an action which will have an adverse effect. Risk is, therefore, the probability of occurrence of certain foreseen and unforeseen actions or events.¹⁸⁰ Based on that, investment risk is the probability of occurrence of foreseen or un-foreseen actions or events that could have a negative effect on the investment's expected gains or financial returns.¹⁸¹

Due to the changing nature of risk and since investments are becoming more advanced, new risks are more likely to emerge. For example, the thesis introduces cyber risk and discuss its nature in an attempt of being one of the early studies of such risk. For that, and after examining cyber risk in this section and in the following sections, the thesis recommends defining cyber risk as the losses encountered by investors financially or otherwise, and as the loss in reputation as a result of an organized attack or attacks on the investor.¹⁸²

¹⁸⁰ This is based and inspired by the definitions presented in the work of Aven.

See;

Terje Aven and Ortwin Renn, *Risk Management and Governance: Concepts, Guidelines and Applications* (Springer Science & Business Media 2010) pp 3-7.

¹⁸¹ *ibid.*

¹⁸² This will further be elaborated within this section.

The importance of defining what investment risks stands for would help in creating a more comprehensive approach that will allow a better understanding of investment related risks. In that respect having a universal comprehensive definition as the one presented here is considered as one of the few attempts in understanding investment related risks. This will be the basis to critically study the nature of the various risks related to investments.

Investors who go overseas to establish an economic presence for them in a country other than their home state may, at times, be at risk of losing their property rights due to actions undertaken by the host state. They may encounter other risks, as well, that they could experience in their home state.

In general, foreign investors may face three different types of risks. They may encounter what is known as political risk, commercial risk or financial risks. Along with these risks there is *Force Majeure* or the Act of God which is a risk that investors may encounter while investing in their home state as well.

Risks related to Act of God happens when one of the parties to a contract cannot carry on one or more of their contractual obligations due to events occurring outside of their control, which makes the performance of such obligations impossible.¹⁸³ Normally, *Force Majeure* is covered only in the presence of actual physical damage rather than an economical one.¹⁸⁴ *Force Majeure*, Act of God and generally commercial risks along

¹⁸³ Rubins and Kinsella (*Chapter 2, n65*) p 57.

¹⁸⁴ ER Yescombe, *Principles of Project Finance* (2nd edn, Academic Press 2014) p 242.

Force Majeure risks are divided into natural and political with political Force Majeure includes acts like terrorism, war and civil unrest.

with certain aspects of the financial risks are types of risks that investors' may encounter at their home state.

On the other hand, it shall, also, be stated that the cyber risk is not necessarily considered to have a category of its own as a risk, rather could fall under the commercial or political risk classification.

Historically, foreign investors had been the subject of discrimination against their own property rights. Perhaps political risk is the most important risk for foreign investors. Since such risk, as it will be explained in this chapter, threatens the property rights of investors' and may, possibly, deprive them of such rights without proper compensation, many investors seek prior protection against such risk.¹⁸⁵ One of the earliest attempts to protect property rights of home state's investors was diplomatic protection. And, one of the important incidents was the Battle of Veracruz or what is known as the Pastry War as it will be examined and further explained in chapter 4.¹⁸⁶

Commercial and financial risks are normally risks related to the nature of the investment activity abroad.¹⁸⁷ It could take the form of a contractual relationship formed between

See,

ER Yescombe (*Chapter 1, n18*) pp 89-90.

¹⁸⁵ Mihri A. Desai and Alberto Moel, 'Czech Mate: Expropriation and Investor Protection in a Converging World' (Social Science Research Network 2004) pp

Article can be found at:

<<http://papers.ssrn.com/abstract=585843>>

Last accessed on the 18th of January 2013.

¹⁸⁶ This will be elaborated in chapter 4.4.

¹⁸⁷ Aven and Renn (*Chapter 2, n180*) pp 2-3.

And;

Angelos Dimopoulos, 'Foreign Investment Insurance and EU Law' (Social Science Research Network 2012) p 2.

Article can be found at:

<<http://papers.ssrn.com/abstract=2112053>>

Last accessed on the 18th of January 2013.

foreign investors and national investors of the host state or, in case of trade, between the importer and exporter of goods and services or they related to the financial and economic situation of the host state. For example, and in the case of a commercial risk, foreign investors may enter into a JV agreement with host state's investors'. And as a result, loss of control and conflict between partners are typical risks associated with JVs and are considered purely commercial risks.¹⁸⁸ It shall be noted that some authors ignored the presence of financial risk and only suggested the presence of commercial and political risks.¹⁸⁹

In general, risk can be defined as the probability of occurrence of certain foreseen or unforeseen actions or events. This definition has been developed after examining a number of various definitions of risks. Risk was also defined as the probability that the expected returns will not be realized.¹⁹⁰ And as the expected losses while others defined it as the probability of an adverse outcome and as the uncertainty of an outcome or an event or even the uncertainty of actions.¹⁹¹ Among all of these definitions the common factor present is the expectation of the occurrence or non-occurrence of certain actions or events.

¹⁸⁸ Siri Terjesen, 'Joint Ventures: Synergies and Benefits' (Q Finance) pp 2-3.

Article can be found at:

<http://isites.harvard.edu/fs/docs/icb.topic1157739.files/joint-ventures-synergies-and-benefits.pdf>

Last accessed on the 18th of February 2016.

And;

Dimopoulos (*Chapter 2, n187*) p 2.

¹⁸⁹ See;

Salacuse (*Chapter 1, n11*) p 245.

¹⁹⁰ Salacuse (*Chapter 1, n11*) p 245.

¹⁹¹ There have been many different definitions of risk presented each related to the sector of which risk is taking place in rather the majority of those related to investment have been gathered and presented in the work of Terje Aven and in the literature of Ortwin Renn:

Terje Aven, *Risk Analysis: Assessing Uncertainties Beyond Expected Values and Probabilities* (John Wiley & Sons 2008) pp 154-155.

And:

Aven and Renn (*Chapter 2, n180*) pp 2-3.

For that it would be more accurate to define risks associated with investments as the probability of occurrence of certain foreseen or un-foreseen actions or events that could have negative effects on the expected gains return.

No matter what type of risk investors may experience in the host state, they would take some protective measures before investing there. Some of those measures, as it will be explained in chapters 4 and 5, may include seeking commercial insurance against some of the risks. Such insurance may come in the form of policies and coverage against specific risks while others may be after the investment takes place and after the risk is realized in the host state, through resorting to arbitration for example.

It should, however, be briefly highlighted that foreign investors were known to take certain actions to counter certain commercial-related-risks. In that respect, and in order to overcome the fear of the importer's insolvency in import-export relationships, exporters were known to seek certain type of protection and insurance from banks. This is known as the Letter of Credit (LC).¹⁹² The LC is considered as one of the most important means of hedging trade-related risks.¹⁹³ It has also been regarded as one of the most important aspects of international trade and commerce in the landmark case *United City Merchants (Limited) v the Royal Bank of Canada*.¹⁹⁴ This landmark case in interna-

¹⁹² Indira Carr, *International Trade Law* (4th edn, Routledge Cavendish 2010) pp 463 and 468.

¹⁹³ Friederike Niepmann and Tim Schmidt-Eisenlohr, 'International Trade, Risk, and the Role of Banks' (2014) Staff Report No. 633 Federal Reserve Bank of New York. p 2.

Document can be found at:

<http://www.newyorkfed.org/research/staff_reports/sr633.pdf>

Last Accessed on the 10th of August 2015

¹⁹⁴ The information was found at:

United City Merchants (investments) Ltd v Royal Bank of Canada [1983] House of Lords [1983] 1 AC 168.

Letters of Credit were described as the 'life blood of international commerce' by Indira Carr.

See;

Carr (*Chapter 2, n192*) p 468.

tional trade, dealt with the refusal of a bank to pay under the LC due to fraud. The court discussed that the whole purpose of the LC is to assure the exporter's rights of payment in exchange for the goods exported prior to exporting the goods.¹⁹⁵

With technological advancements, investors use the private and public networks on daily basis as part of promoting their goods or services or as a part of facilitating their investments. This has allowed the emergence of a new type of investors who are home state investors yet, at the same time, share the qualities of an international one. This is true with companies like Amazon which act as a virtual shopping mall where buyers and sellers from across the world meet to buy and sell products. These company now has a US headquarters and an EU headquarters along with a number of warehouses based in various parts of the world to service the needs of its users. Amazon does not offer its services locally, wherever it has an office or warehouse rather, it is open for users across the world who have access to the internet as long as suppliers on Amazon agree to ship to certain locations and as long as Amazon agrees to ship products offered and sold by it, and not those sold by third party supplier, to a certain location and as long as there are no restrictions on shipping specific products in certain countries.¹⁹⁶

Financial institutions have provided their clients with special services via the internet. Banks for example, nowadays, allow their clients to access their accounts, make transaction and pay bills through the internet and without the need to go to the bank physically. Companies in the entertainment sector found the internet to be another medium which

¹⁹⁵ *ibid.*

¹⁹⁶ Panos Mourdoukoutas, 'What's Wrong with Amazon's Business Model?', (Forbes 27 Oct 2014)

Found online at:

<http://www.forbes.com/sites/panosmourdoukoutas/2014/10/27/whats-wrong-with-amazons-business-model/#4f1b11c36a40>
Last accessed on the 18th of February 2016.

allowed them to offer their products on and for that, internet users can go online and look for a certain song, movie or book and buy it digitally.

Most investors saw in the internet a useful medium of marketing their goods and services and, sometimes, a way to offer such services without the need of a physical presence in a given host state. This offered profit maximization potential and yet unveiled a new type of risk associated with it known as the cyber risk. Cyber risk, as it will be examined later on in this chapter when talking about the borderline between the different types of risks associated with FDI, entails the financial loss or losses related to the reputation of an investor due to a cyber-attack carried on by a person or an organized group known as hackers. Such hackers may limit or prevent accessing the private networks used by investors to share confidential information about the investment or the public network offered to users all over the world like the internet. These acts could originate from anywhere in the globe and target any given investor at any state as long as this investor has network access.

Exploring the various types of risks, here, serves as an example on how the nature of risk is changing and evolving and how these are tackled and avoided. It is also of importance to explore all these various types of risks and how far they are from one another yet at the same time could be quite related and very difficult to distinguish. All these differentiations that will be examined throughout this section of the thesis are presented to make it clearer how risk does not always have one nature or classification rather, at times, they could interlink.

Not only that, but throughout this section, it will be explained how different ECAs and different institutions have decided to include specific activities to fall under certain type of risks and how such decision is different from one institution to another. For the purpose of this research, the focus will fall on political risk, commercial risk and on financial risk. Though the distinction between the three may seem easy at first, the matter is more complicated, nevertheless, and there are many instances where one may be falling under the other.

The distinction between the three is of importance in order to find out, later on, which agency can cover against such risk or if investors may have to invest and take the risk without being properly covered. And since political risk is one of the most important risks faced by foreign investors, it will be elaborated more than the other types of risks.

2.4.1. Political Risk

Political risk can be defined as a threat to investments made by foreigners through means of interference by the host state's government or any of its representatives acting on its behalf which would result in limiting investors from benefiting from their property rights.¹⁹⁷ This definition was recommended after examining various views on what is

¹⁹⁷ Similar definition was suggested by many. These were presented in the work of Kobrin.

For example, one of the definitions saw that political risk is one which the 'host state government interferes with the business operations.' another saw it as one that 'arises from actions of the national government which interfere with or prevent business transactions or change terms of agreement or cause the confiscation of wholly or privately foreign owned business property.' Some authors do suggest the presence of instability, violence, expropriations or other types of constraints on the operations of the foreign investor.

It could also be when "discontinuities occur in the business environment; when they are difficult to anticipate, when they result from political change. To constitute a 'risk' these changes in the business environment must have the

considered political risk, which will be elaborated hereafter, in a number of international agreements and from the point of view of insurance providers. Though the suggested definition is straightforward, the reality of political risk is far more complicated especially since there is no universal or unified definition for such risk and especially when it comes to what ECAs consider as political risk and what the Multinational Investment Guarantee Agency believes is political risk.¹⁹⁸

To Korbin, one of the definitions saw that political risk is one which the ‘host state government interferes with the business operations.’ another saw it as one that ‘arises from actions of the national government which interfere with or prevent business transactions or change terms of agreement or cause the confiscation of wholly or privately foreign owned business property.’” Some authors do suggest the presence of instability, violence, expropriations or other types of constraints on the operations of the foreign investor.

It could also be when “discontinuities occur in the business environment; when they are difficult to anticipate, when they result from political change. To constitute a ‘risk’ these changes in the business environment must have the potential for significantly affecting the profit or other goals of particular enterprise.’ These are some of the views are some of the views on political risk cited by Kobrin.¹⁹⁹

potential for significantly affecting the profit or other goals of particular enterprise.’

These are some of the views are some of the views on political risk cited by Kobrin.

See;

Stephen J. Kobrin, ‘Political Risk: A Review and Reconsideration’ 10 *Journal of International Business Studies* pp. 67-68.

Mora suggested that political risk, among other definitions, relates to the “corporate exposure to risk of a political event that diminishes the value of an asset.”

See;

Thodore H. Mora (ed), *International Political Risk Management: Exploring New Frontiers*, (World Bank 2001) p 80.

¹⁹⁸ Kobrin (*Chapter 2, n197*) pp. 67-68.

¹⁹⁹ *ibid*

One of these definitions suggests that political risk is a result of political development or governmental actions.²⁰⁰ Others, however, defined political risk as the losses resulting through expropriation and policy shifts.²⁰¹ The suggested definition is inspired by the MIGA's definition of political risk which states that "political risks are associated with government actions which deny or restrict the right if an investor/owner (i) to use or benefit from his/her assets; or (ii) which reduce the value of the firm."²⁰²

The thesis also recommends distinguishing between two types of political risk. The first being *internal political risk* which includes acts resulting from decisions of the host state's government leading to civil unrest or a change in the laws governing investors. The second being *external political risk* which is a result of a decision made by third party states or even by the home state resulting in acts of war against the host state or any restrictions on economic and financial exchanges with the host state's government.

Political risk is one of the major risks faced by foreign investors and perhaps the oldest. This risk is said to be influenced by political environment of the host state and by the sector as well as by the investor-state relationship.²⁰³ It poses a major threat to foreign investors due to its nature. It also includes certain actions that may be seen to fall under the financial or commercial risks. For that it will form a big part of this research com-

²⁰⁰ Salacuse (*Chapter 1, n11*) p 245.

²⁰¹ Various definitions of political risks were gathered and presented in the work of Philipp Harms.

See:

Philipp Harms, *International Investment, Political Risk, and Growth* (Springer Science & Business Media 2012) pp. 72-72.

²⁰² The definition of political risk according to the can be found in:

Salacuse (*Chapter 1, n11*) p 245.

²⁰³ Gordon (*Chapter 1, n327*) p 93.

pared to the other investment related risks. The key component to this risk is a political behavior through the interference of the host state government.²⁰⁴

Generally, acts constituting political risk include political violence such as war in the host state, revolutions, terrorism, riots and civil commotions, strikes and malicious damage. It also includes expropriation and creeping expropriation, acts of war and civil unrest, changes in legislation and in tax regimes and finally corruption.²⁰⁵ Expropriation is the act taken by the state to strip investors from their property rights in full or in part. It is also known as direct expropriation and known, in common law, as *eminent domain*.²⁰⁶

Expropriation is regarded as an inherent power of the state over properties located in its territories and only when it is affected regarding citizen's properties.²⁰⁷ Not only that, but expropriation normally comes in hand with just or unjust compensation.²⁰⁸ It is one of the major risks by FDIs.²⁰⁹ It is worth mentioning that normally what constitutes political risk and expropriation are not defined per se rather they are explained and left to customary international law to define.

²⁰⁴ Robert McKellar, *A Short Guide to Political Risk* (Gower Publishing, Ltd 2012). p 1.

²⁰⁵ They are tied up to the performance and quality of political institutions of the host state.

See;

Matthias Busse and Carsten Hefeker, 'Political Risk, Institutions and Foreign Direct Investment' (Social Science Research Network 2005) p 3.

Article can be found at:

<<http://papers.ssrn.com/abstract=704283>>

Last accessed on the 18th of January 2013.

²⁰⁶ Defining what expropriation stands for was not an easy task since it was suggested that such definition must include creeping expropriation.

See;

Martin EM (*Chapter 2, n31*) pp 293-294.

²⁰⁷ Dugan, Wallace, Rubins and Sabahi (*Chapter 2, n65*) p 429.

And;

Sebastian Lopez Escarcena, *Indirect Expropriation in International Law* (Edward Elgar Publishing 2014). p 6.

²⁰⁸ Yescombe (*Chapter 2, n184*) p 304.

²⁰⁹ Peter Egger and Michael Pfaffermayr, 'The Impact of Bilateral Investment Treaties on Foreign Direct Investment' (2004) 32 *Journal of Comparative Economics* p 1536.

On the opposite side of expropriation lies privatization, which may be regarded as one of the means to stimulate investment. Privatization may also be considered as a way to counter the risk of expropriation by which, the host state does the opposite and rather than stripping investors from their property rights and claim ownership of the said property for the public benefit, the host state does exactly the opposite through privatizing a public-sector company.²¹⁰ Privatization is, therefore, an action by which the host state transfers the ownership of a company from the public sector to the private sector.²¹¹ Privatization comes in three different forms. The first form known as formal privatization appears when an administrative public entity is transformed into a solely-owned private sector corporation.²¹² The second form of privatization known as the functional privatization and it entails the transfer of functions that was originally performed by the public sector to a private company.²¹³ This type of privatization is also known as the Public Private Partnership (PPP). The last form of privatization is referred to as material privatization and occurs when both, assets and functions of one company, are transferred to a private company.²¹⁴ Privatization is seen, therefore, as a new form of investment open for foreign investors if it was implemented properly where, in this case, the foreign investor may opt to acquire an already established investment rather than starting a new one.²¹⁵ Through privatization, the technology and experience of foreign investors may be

²¹⁰ Basu and Srinivasan supported the idea that privatization attracts FDI.

Anupam Basu and Krishna Srinivasan, *Foreign Direct Investment in Africa--Some Case Studies (EPub)* (International Monetary Fund 2002) p 9.

N.B. Expropriation comes to counter one of the fundamental rights. This right is the right to own a property.

FV Garcia Amador and Louis B Sohn, R.R. Baxter, *Recent Codification of the Law of State Responsibility for Injuries to Aliens* (Brill 1974) pp 6-7.

²¹¹ Privatization is seen as the "transfer of assets or service functions from public to private ownership control"

See;

Marc Holzer, Seck-Hwan Lee, *Public Productivity Handbook*, (2nd edn Marcel Dekker 2005) p 90.

²¹² Salacuse (*Chapter 1, n11*) p. 110.

²¹³ *ibid.*

²¹⁴ *ibid.*

²¹⁵ This idea was presented by J.W. Salacuse:

Salacuse (*Chapter 1, n11*) pp 110-120.

used effectively for the public benefit. Not only privatization opens the door to foreign direct investors to invest in the host state, it, at the same time, opens the door to other types of foreign investors as well. For example, foreign banks, financial institutions and lawyers have helped host states plan privatization programs.²¹⁶

The other side of expropriation is referred to as creeping or indirect expropriation or, according to Jürgen, disguised expropriation.²¹⁷ Creeping expropriation includes a number of actions that limit investors from benefiting from their property rights. Such actions when taken alone wouldn't, normally, violate or infringe investors' property rights.²¹⁸

This type of expropriation may be referred to as the indirect expropriation as well.²¹⁹ It shall be noted that the act of expropriation may entail nationalization.²²⁰ Nationalization is one of the means of expropriation where the host state decides to put its hand on foreign investors' property and claim it a national property.²²¹

²¹⁶ *ibid* at 112.

N.B. Privatization will not be discussed further since it is not directly related to the theme of the thesis. It was beneficial, however, to explore that area and make the contrast between the different types of governments existing in the sense that some expropriate investments for the public's interest while others privatize also for the same reason.

²¹⁷ See;

Jürgen (*Chapter 2, n7*) p 703.

²¹⁸ *ibid*

²¹⁹ *ibid*.

²²⁰ Expropriation refers to the "application of sovereign right of eminent domain; a seizure of private property for some definite public-sector purpose and with the intention and expectation that the property would be paid for in accordance with the legal system of the country."

Nationalization is the "determination that a certain business would thereafter be operated by the government."

These were found in the work of Reeves.

See;

William Harvey Reeves, "Expropriation," "Confiscation," "Nationalization" What One Can Do About Them' (1969) 24 *The Business Lawyer*, p 867.

²²¹ This view is similar to that proposed by Reeves.

See;

ibid.

It is worthwhile mentioning that the action of expropriation may be a legal action and not necessarily an illegal one condemned by international law. It is legal if it fulfills three conditions; if it is done for the interest of the public and in a non-discriminatory manner and once this action is compensated by the state.²²²

It doesn't matter how the investment agreement refers to 'public interest', where some may use 'public benefit' or 'public purpose' while others may use 'public interest' or even 'social interest'. As long as it is understood that the expropriation is taking place for the interest of the public and, of course, as long as it fulfils the other conditions, then such expiration is legal. For example, In the BIT between the United States of America and Morocco that was put into force in 1991, the word 'public purpose' was used to convey 'public interest' and so did the BIT between the United Kingdom and Morocco in 2003 and the Agreement between Canada and Argentina and Agreement between Brazil and the Belgium-Luxemburg Economic Integration.²²³ Other treaties used 'national interest' and 'public purpose' where some used both phrases in their BIT like the agreement between New Zealand and Chile.²²⁴ Some BITs opted for 'public interest' like the case with the BIT between Spain and Lebanon, the BIT between Ja-

²²² Rubins and Kinsella (*Chapter 2, n65*) p 8.

²²³ See;

Treaty between the United States of America and the Kingdom of Morocco Concerning the Encouragement and Reciprocal Protection of Investment. Article III (1).

And;

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Kingdom of Morocco for the Promotion and Protection of Investments. (1990). Article 6 (1).

And;

Agreement between the Government of Canada and the Government of the Republic of Argentina for the Promotion and Protection of Investment. (1991). Article VII (1).

And;

Agreement between the Belgo-Luxemburg Economic Union and the Government of the Federative Republic of Brazil on the Reciprocal Promotion and Protection of Investments. (1999). Article 4(2).

²²⁴ See;

Agreement between the Government of New Zealand and the Government of the Republic of Chile for the Promotion and Protection of Investment. (1999) Article 6.

maica and Switzerland, and the BIT between Austria and Saudi Arabia.²²⁵ Some states used ‘Public benefit’ in some BITs to convey ‘public interest’ like the case with the BIT between Germany and Lebanon.²²⁶ Finally, in the China and Albania BIT, ‘social interest’ was used to reflect ‘public interest’.²²⁷

It can be understood that states are allowed to use expropriatory measures when there is a collective interest justifying such action and not on the basis of a personal motivation.²²⁸

Investors, in general, are more concerned with indirect or *de facto* expropriation than the direct one and for that creeping expropriation can be defined as any action that may deprive foreign investors from benefiting from their property rights even though such actions when taken alone would not necessarily lead to such outcome.²²⁹

²²⁵ See;

Agreement between the Republic of Lebanon and the Kingdom of Spain on Reciprocal Promotion and Protection of Investment. (1996). Article V(1).

And;

Agreement between the Government of Jamaica and the Government of the Swiss Confederation for the Reciprocal Promotion and Protection of Investment. (1990). Article 5(1).

And;

Agreement between the Kingdom of Saudi Arabia and the Republic of Austria concerning the Encouragement and Reciprocal Protection of Investments. (2001). Article 4(2).

²²⁶ See;

Agreement between the Lebanese Republic and the Federal Republic of Germany on the Promotion and Reciprocal Protection of Investments. (1997). Article 5(2).

²²⁷ See;

Agreement between the Government of the People’s Republic of China and the Government of the Republic of Albania Concerning the Encouragement Reciprocal Protection of Investments. (1993). Article 4(1)a.

²²⁸ Alan C Swan and John F Murphy, *Cases and Materials on the Regulation of International Business and Economic Relations* (Matthew Bender and Company 1999) p 27.

And;

Restatement of the Law Third, Foreign Relations Law of the United States, [American Law Institute 1987] Article § 721 (1).

Article § 721 of the Restatement of the Law Third, Foreign Relations Law of the United States holds that the host state is responsible towards injuries to foreign nationals caused by, as the text describes it ‘the taking’ of the property of the foreigner if it was not made for the public interest; or was based on discriminatory measures or if the host state did not provide the foreign investor a just compensation.

²²⁹ ER Yescombe (*Chapter 2, n184*) p 307.

And;

Escarcena (*Chapter 2, n207*). p 6-11.

An example of some of the actions constituting creeping expropriation includes holding up the imports of the investor at the docks of the host state or having politically motivated strikes.²³⁰ Import and export restrictions may also be considered to form the legislative part of political risk since they normally involve legislative interference through change of law. In that respect, import restriction is referred to when the host state's government implements new laws or regulations prohibiting the importation of goods. While export Restriction, on the other hand is related to the host state's decision to limit the exportation of goods.²³¹

When it comes to compensation for expropriation, prior to the introduction of IIAs as a mean of promotion and protection of FDIs, investors' rights were protected through customary international law, which ensured the application of minimum standard of protection to foreign investors' property rights. Such minimum standard was included in what is known as the *Hull Standard*. This standard granted to investors compensation for the loss of their property rights due to an act of expropriation carried out by the host state against the investors' property rights.²³² Nowadays, many states signing BITs require a compensation on basis of the *Hull Standard* and some of them even go a bit further with their request, and perhaps that is the reason why some of the developing host

²³⁰ *ibid*

²³¹ This was discussed in chapter 2.1.

Jürgen argued that foreign investment policy may be different from trade policy. This is true, for example, when talking about imposing import restrictions. Such restrictions are in violation of trade policy while restrictions on raw material are not seen as such.

See;

Jürgen (*Chapter 2, n7*) p 696.

²³² See;

Mary H. Mourra, *Latin American Investment Treaty Arbitration: The Controversies and Conflicts*, (Kluwer 2008) pp 23-28.

Also see:

Sauvant and Sachs (*Chapter 1, n22*) pp 228 - 229.

And;

Olivier De Schutter, Johan F.M. Swinnen and Jan Wouters, *Foreign Direct Investment and Human Development: The Law and Economics of International Investment Agreements*, (Routledge 2013) p 28.

states refused to sign a number of MITs, such as the UNCTAD.²³³ This standard helps in determining the amount of compensation payable to the property owner.²³⁴ The *Hull Standard* entails the payment of a ‘prompt, adequate and effective’ compensation. Historically, The Hull Standard was introduced as a result of an expropriated oil fields in Mexico belonging to the United States. Upon this action the Secretary of State, Cordell Hull wrote a letter to the Mexican government stating that international law requires that Mexico pays a ‘prompt, adequate and effective’ compensation. This standard is not represented in customary international law.²³⁵

Investors normally need to consider the presence of legal restrictions. While investing abroad, legal restrictions may seem to be as a type of risk on its own but in reality, it is not. Legislation and the change of law is something that is controlled by a given state where laws and regulations may be changed overnight to restrict foreign investors from benefiting from their property rights. For that, and since the host state interferes, controls and changes the laws, legal risk falls under the umbrella of political risk.²³⁶ This, in theory may make sense but, as mentioned earlier, there is no one standard definition of political risk rather the acts constituting political risk differs from one ECA to another and these are, also, different from those of the MIGA and from what legal practitioners

²³³ Rubins and Kinsella (*Chapter 2, n65*) p 229.

²³⁴ *ibid.*

²³⁵ This can be found at:

Mary H. Moura, *Latin American Investment Treaty Arbitration: The Controversies and Conflicts*, (Kluwer 2008) pp 23-28.

Also see:

Sauvant and Sachs (n 20) pp 228 - 229.

²³⁶ This is true since some ECAs, as it will be examined in chapter 4, include in their PRI policies the risk of change in regulations.

For more information visit OPICS website on the following link;

<<https://www.opic.gov/what-we-offer/political-risk-insurance/types-of-coverages/regulatory-risk>>

Last accessed on the 3rd of March 2016.

And;

Gustavo Ferro, ‘Political Risk and Regulatory Risk: Issues in Emerging Markets Infrastructure Concessions’, Centro de Estudios de la Regulacion, Universidad de la Empresa, Working Papers (2001) Paper No 15. p 7

or researches may define as political risk. And for this reason, in this chapter, a small list of what is considered political risk by different agencies will be presented.

Another type of risk related to the legislative risk is the one that restricts repatriation of foreign investors' funds.²³⁷ Though this is more of a financial risk than a political one, the fact that the host state can change the laws to restrict such action makes it political, as it will be explained later on in this research. It also includes the changes in the taxation regimes, environmental laws or in securities regulations as well as the change in the methods of dispute settlement.²³⁸

It may, as well, include restrictions on trade.²³⁹ It is worthwhile mentioning that political risk does not only involve the central government of the host state interfering and preventing investors from benefiting from their property rights, it is also the case with regional governments of the host state. Regional governments, for example, may pass on regulations limiting investors from benefiting from their property rights.²⁴⁰

In addition, the host state's government, may introduces new bills of which allows it to acquire shares in the MNC's investment. This was, for example, the case of the Spanish Oil MNC, Repsol, which, while investing in Argentina, found itself in a battle against the Argentinian state to protect its property rights after the state issued a bill in which it seized 51% of the shares of the MNC.²⁴¹ Needless to say, these instabilities had a nega-

²³⁷ Swan and Murphy (*Chapter 2, n228*) p 708.

²³⁸ *ibid.*

²³⁹ Rubins and Kinsella (*Chapter 2, n65*) pp 23-24.

²⁴⁰ Yescombe (*Chapter 2, n184*) pp 308 -309.

²⁴¹ See;

Spanish oil company Repsol ends operations in Argentina (BBC News) 23rd of May 2014.
The article can be found at:

tive effect on the state's attitude towards investors. Such introduction of new bills is an example of how the host state can introduce laws or regulations to limit the investor from enjoying his property rights.

It shall be noted that, and as part of the regulatory risk and change of law, regulations governing operations of factories and greenfield investments in general may face the risk of changes in regulations governing its activities when it comes to investments in developing countries. Such geopolitical issues, the host state may take place, for example, when the host state decide to change labour laws and introduce stricter safety conditions or when it introduces new regulations governing immersions from factories in order to become a greener environment and an eco-friendly state. This is for example the case in China where the government, recently, introduced new stricter regulations governing the safety of factory workers.²⁴²

This type of risk, though geopolitical, is heading more towards the regulatory risk where regulations play a vital role in the changing attitudes of the host state. And as such, is a result of a political decision that may not necessarily be taken to limit foreign investors' right to benefit from their property rather made and undertaken for the public interest and general health.

<<http://www.bbc.co.uk/news/world-latin-america-27549309>>

Last accessed on the 8th of February 2016.

and;

Tracy Rucinski, Andres Gonzalez and Kevin Gray, Spain's Repsol agrees to \$5 billion settlement with Argentina over YPF (Reuters) 25th of February 2014.

The article can be found at:

<<http://uk.reuters.com/article/uk-repsol-argentina-idUKBREA1O1N220140225>>

Last accessed on the 8th of February 2016.

²⁴² For more information, please refer to:

<<https://www.twobirds.com/en/news/articles/2017/china/china-employment-law-update-march-2017>>

Last accessed on the 20th of April 2017.

As mentioned the change of law for example, occurs when the host state decides to change certain laws or regulations that are applied in order to limit investors benefiting from their property rights. In this case such change of law is a discriminatory change law and deprives the foreign investor from his property right on purpose and since it is made through a decision it is, therefore, classified as a political risk.

It shall be noted that there is another action falling under political risk cited by Rubins and Kinsella which is corruption.²⁴³ According to them, it is considered political risk since government officials of the host state may demand personal benefit in order to fulfill a financial function.²⁴⁴ Such act was thought to have a negative effect on inward FDI through discouraging foreign investors from entering such states or markets.²⁴⁵

In addition, there is a more controversial risk that may arguably fall under both commercial and political risk. It is limiting the number of foreign employees an investor is allowed to hire. For example, recently, Saudi Arabia introduced a new legislation aimed at reducing the number of foreign employees in companies operating in the Kingdom.²⁴⁶ Until this day, such risk has not been covered by any public or private insurance company including ECAs or even the MIGA. This type of risk is more of a Legislative Risk,

²⁴³ Rubins and Kinsella (*Chapter 2, n65*) p 22.

²⁴⁴ *ibid.*

²⁴⁵ See,

Joel S. Hellman, Geraint Jones and Daniel Kaufmann, 'Far from Home: Do Foreign Investors Import Higher Standards of Governance in Transition Economies?' (Social Science Research Network 2003) p. 3.

Found at

<<http://papers.ssrn.com/abstract=3886900>>

Last accessed 18 January 2013.

²⁴⁶ See NY Times Article:

Sara Hamdan 'Saudi Arabia to fine Firms with Too Many Foreign Workers', NY Times (21 November 2012).

Article can be found online at:

<http://www.nytimes.com/2012/11/22/world/middleeast/saudi-arabia-to-fine-firms-with-too-many-foreign-workers.html?_r=0>

Last accessed on the 3rd of March 2016.

which, in its turn, can be, at times, considered as political risk. The probable reason behind not insuring against such risk is that it does not pose a high risk compared to other political, commercial or financial risks.

Finally, Yescombe considered the application of sanctions or blockade on the host state to be a political risk.²⁴⁷ This may be true but it is not an action taken by the host state to deprive investors from benefiting from their property rights rather it is a political decision imposed on the host state and affects all investors alike rather than one segment. Therefore, this type of action cannot be treated like other actions falling under the political risk label and, thus, this risk shall be treated as a risk on its own. In that sense, a distinction can be made between *internal political risk* and *external political risk* where *internal political risk* refers to the measures taken by the host state's government whereas *external political risk* refers to the actions imposed on the host state's government by another state's government.

From a practical point of view, insurance companies, ECAs and the MIGA provide their own list of actions that they label as political risk. For example, one of the biggest players in the private sector that specialize in the field of political risk insurance (PRI), Lloyd's of London corporation describes political risk as one that includes war in the host state, terrorism, riots and civil commotions, and strikes and malicious damage.²⁴⁸

²⁴⁷ Yescombe (*Chapter 2, n184*) p 305.

²⁴⁸ This information can be found at:

'Political Risk Insurance' (*Lloyd's of London*):

<http://www.lloyds.com/redirect-pages/risk_locator/political_risks_insurance>

Last accessed on the 18th of May 2015.

The Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE), which is the official French ECA, considers the acts of expropriation, nationalization and confiscation and breach of government undertakings as political risk. These aforementioned acts are categorized, according to COFACE as voluntary acts by the host state's government. Political risk, as well, according to COFACE, includes acts of political violence such as war, revolution and riots. It, also, includes restrictions on remittance.²⁴⁹ The company covers against such risks as long as they will totally affect the operating of the investors' assets.

On the other hand, MIGA defines political risk as actions undertaken by the host state's government which would restrict investors' from benefiting or using their assets or those that would reduce the value of the firm.²⁵⁰ MIGA, as well, considers war, revolutions, actions restricting the movement of profits and any type of revenue from the host state as well as seizure of investors' property by the host state to fall under the political risk's definition.²⁵¹

When it comes to determining the host state's liability for expropriation, the measurement is the extent to which the negative effect of the measures taken by the host state affects foreign investors' rights. It is worth mentioning that the intention to expropriate the property rights of investors' and the justification for such action are not part of the consideration on indirect expropriation according to the dominant view.²⁵²

²⁴⁹ Based on a phone conference with Mr. Christophe Viprey (Director of Public Guarantees of COFACE) on the 18th of May 2015.

²⁵⁰ Gordon (*Chapter 1, n32*) p 92.

²⁵¹ *ibid* at 92.

²⁵² Rubins and Kinsella (*Chapter 2, n65*) pp 206 - 211.

As far as what concerns investors the most while investing, it was observed in a report prepared by Lloyd's of London that strict regulations and change in legislation along with poor or incomplete regulations, fraud and corruption, asset expropriation and regime changes, civil commotions and riots and terrorism were presented, accordingly, among other risks, as some of the concerns of investors.²⁵³

It is concluded that political risk includes expropriation, nationalization, creeping expropriation, wars and civil unrest, terrorism and change of law including currency transfer risks.²⁵⁴ These are some of the actions that foreign investors may encounter while investing in the host state.

2.4.2. Commercial Risk

Some times, foreign investors, while investing abroad, are faced with a number of factors that may cause them to lose their investment in part or in full. In that respect these losses may be caused due to the nature of the investment or while the investment is

²⁵³ The list included 50 different risks related to the main three risks faced by investors; i.e. political, commercial and financial risks.

These related to political risk were the ones mentioned and on top of the political risk rank came strict regulations and change in legislation, which came in 5th place among all other risks faced by investors followed by poor or incomplete legislation in the 15th place. Fraud and corruption came in the 17th place while asset expropriation came in the 36th place. In the bottom 10 risks came change of regime along with riots and civil commotion in the 41st place and, finally, terrorism in the 44th place.

The full list can be found in the study prepared by Lloyd's for the 2013 period on its 6th and 7th pages and made available online through:

<<http://www.lloyds.com/~media/Files/News%20and%20Insight/Risk%20Insight/Risk%20Index%202013/Report/Lloyds%20Risk%20Index%202013report100713.pdf>>

Last accessed on 20th August/ 2015.

²⁵⁴ Theodore H. Moran, *Harnessing Foreign Direct Investment for Development: Policies for Developed And Developing Countries* (CGD Books 2006) pp 81-87.

being established or during the construction.²⁵⁵ These normally happen through, for example, taking longer time to finalize the project or investment than expected or by incurring extra expenses throughout the establishment of the investment.²⁵⁶ It may also be due to contract mismatch or due to unexpected effects that the project has on the surrounding environment.²⁵⁷ These risks, among others, are called commercial risks.

Other actions that may constitute commercial risk are construction risks which, normally happen during the establishment phase, the expected commercial gain or loss from the investment, raw material changing costs, the presence of uninsured risks, the investment's fate after termination of the project contract or what is known as residual value risk and the limit of sponsor support.²⁵⁸ Buyer's insolvency or refusal to accept goods or services subject of the contract is also considered as a commercial risk.²⁵⁹

Payment default and repudiation are also considered commercial risks.²⁶⁰

²⁵⁵ Dimopoulos (*Chapter 2, n187*) p 2.

²⁵⁶ Yescombe (*Chapter 2, n184*) p 200.

²⁵⁷ *ibid.*

And;

Along with contract mismatch, not respecting the international contractual obligations by the host state's partner is one of these risks. And in case the host state partner is a representative of the host state, then this falls more into the political risk category as it will be highlighted in this chapter in section 2.5. In this last scenario, this is thought to be the host states responsibility since it was caused by the host state.

See;

John R Pate, *The Laws of Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners'* (1929) 23 Special Number Supplement to the American Journal of International Law. p 134. Article 8.

²⁵⁸ *ibid.*

²⁵⁹ Stephens (*Chapter 1, n9*) p 14.

Buyer's insolvency was also named as buyer's risk according to Sachs and Abegg.

See;

Rudolf Sachs, Birgit Abegg, *Commercial correspondence: Hauptbd., Volume 1* (Hueber Verlag, 2001) p 163.

More on Byer's insolvency can be found at:

Zlatko Salcic, *Export Credit Insurance and Guarantees: A Practitioner's Guide* (Springer 2014) under Chapter 3.4.

And;

Miran Jus, *Credit Insurance* (Academic Press 2013) p 79.

²⁶⁰ *ibid.*

It shall be noted that these risks are closely tied to trade matters. Since ECAs insurance covers trade as well, this matter is referred to occasionally but the differentiation between Trade and FDI will not take.

N.B. In the export credit sense, commercial risk refers to the non-payment due to insolvency and/or inability to take goods shipped in accordance with a shipping contract.

This can be found at:

<<https://stats.oecd.org/glossary/detail.asp?ID=5896>>

Along with these examples of commercial risk, contractual risk falls under its scope where, for example, foreign investors who are entering a new foreign market may choose to become partners with home state investors who probably have connections and would make the investment run easier and smoother.²⁶¹ Or an exporter may be at risk of not having the contractual obligations honored by the importer due to the buyer's insolvency.²⁶²

When foreign investors enter a new markets through partnering with local partners, both parties have specific contributions towards the investment and in order to achieve the common goal, i.e. profit maximization, both parties will have certain contributions where, for example, the local party, i.e. the home state investors, will contribute with their connections with the local authorities which will make the investment smoother and easier and in return, foreign investors will bring in their know-how or the secret recipe that gave them the competitive edge.

This is the case in China for example where foreign investors choose to go into JVs with local Chinese investors in order to hedge the risks that they may face. In such scenario, foreign investors may be at risk of not having the contractual obligations respected by their local partner or by suppliers or other host state parties of which they have a contractual relationship with. Foreign investors may go into a partnership with the host

Last accessed on the 3rd of March 2016.

²⁶¹ This can be found at:

<<https://stats.oecd.org/glossary/detail.asp?ID=5896>>

Last accessed on the 3rd of March 2016.

²⁶² *ibid.*

state's government or have an existing contractual relationship with the host state's government.²⁶³

Following this example, commercial risk may be very much tied to regulatory risk which is associated with the political risk and in this case such action, i.e. the contractual risk may not fall under the commercial risk. This matter will be further discussed later in this chapter. Contractual risk includes what is known as contract frustration. This happens when the host state's government undertakes measures or decisions preventing investors from performing their contractual obligations whether in full or in part.

Another example of the types of risks falling under the commercial risk label would be the market's perception of the goods or services the foreign investor is introducing. This risk is actually something that investors are also concerned about while investing in their home state though there is no known insurance or guarantee against such risk.

In addition, there is another type of commercial risk that investors may encounter in both home and host states which is related closely to the market perception of the goods or services. This is concerned with investors' strategy or their investment plan to market and promote their goods or services. This type of commercial risk is not covered by any insurance program and as such is considered as an inherent part of any investment.

This was, for example, the case with the Walt Disney Company's investment in France. This investment was said to be one of the biggest foreign investments in Europe. After

²⁶³ M. Sornarajah, *The International Law on Foreign Investment* (Cambridge University Press 2010) p 107.

the opening of the Disney theme park in France during the Olympic games in Barcelona in 1992, the company noticed that the number of visitors was not quite what was expected and soon they have discovered that this was due to poor strategy planning and lack of understanding of the culture through the 'copy-and-paste' strategy they followed.²⁶⁴

As far as what concerns investors the most while investing, it was observed in a report prepared by Lloyd's of London that the main concerns of investors were those related to commercial risk.²⁶⁵ The list includes loss of customers, cyber related risks, prices of materials needed by investors, rapid change in technologies, lack of skilled labour, risks related to the reputation of the investor, corporate liability, asset price volatility, asset theft, failed investments, internal oversight failure or failure to properly apply corporate governance, infrastructure failure, failure of the supply chain, increased protectionism, insolvency, energy security, shift in the demographics of the host state, workplace accidents, piracy, population growth, urbanization and the harmful effects of new technologies among other risks.²⁶⁶

²⁶⁴ Bill Faulkner, Eric Laws and Gianna Moscardo, *Embracing and Managing Change in Tourism: International Case Studies* (Routledge 2003) pp 371- 384.

And:

Tanya Spyridakis, 'EuroDisneyland' [1999] Thunderbird, The American Graduate School of International Management. pp 7-11.

Article can be found at:

<http://web.archive.org/web/20060830055144/http://www.thunderbird.edu/wwwfiles/pdf/about_thunderbird/case_series/a15990007.pdf>

Last Accessed on 11th August 2015.

²⁶⁵ Information is available online through:

<<http://www.lloyds.com/~media/Files/News%20and%20Insight/Risk%20Insight/Risk%20Index%202013/Report/Lloyds%20Risk%20Index%202013report100713.pdf>>

Last accessed on 20th August 2015.

²⁶⁶ These are some of the risks related to commercial risk. They were ranked, among other risks, as follows:

Loss of customers came in 2nd as the highest type of risk followed by cyber related risks in the 3rd place and prices of materials needed by investors in the 4th place. Rapid change in technologies came in the 9th place while the lack of skilled labor came in 11th and risks related to the reputation of the investor came in 13th, Corporate liability was the 14th in the list followed by asset price volatility in the 15th place. In the 19th place came asset theft followed by failed investments in the 20th and internal oversight failure or failure to properly apply corporate governance in the 21st place. Infrastructure failure ranked as the 22nd and failure of the supply chain as the 23rd while increased protectionism was the 24th on the list followed by insolvency in the 25th, energy security in the 26th, shift in the demographics of the host state in the 27th and workplace accidents in the 28th place followed by population growth

As mentioned, cyber risk is a direct result of development in the IT sector. This cyber risk may also be considered as an IT risk. IT risks may, therefore, be defined as one that results from the adoption of information technology within a certain investment and from the ownership and the operation or involvement of IT in such investment.²⁶⁷ It is, according to the United Kingdom's government, one of the most significant risks facing investors in the UK.²⁶⁸ This type of risk may fall under the commercial risk able since it is, nowadays, an inherent risk associated with an investment. In that respect, it has been recorded that in the United Kingdom, 81% of big corporations in 2014 suffered from cyber-related risks with an average cost of security breach reaching one million British pounds.²⁶⁹

Cyber risk, generally, includes eleven different threats. Intellectual property theft, business interruption including distributed denial-of-service (DDoS) attacks, cyber extortion, data loss, cyber fraud and crime, network failure, breach of privacy, bodily injury including death as a result of a cyber-attack, any damage to the physical asset of the investor, any negative impact on the reputation of the investor and any form of incident investiga-

29th place and piracy in the 31st place. On the bottom of the List came urbanization in the 37th place followed by the harmful effects of new technologies in the 39th place.

The full list can be found in the study prepared by Lloyd's for the 2013 period on its 6th and 7th pages and made available online through:

<<http://www.lloyds.com/~media/Files/News%20and%20Insight/Risk%20Insight/Risk%20Index%202013/Report/Lloyds%20Risk%20Index%202013report100713.pdf>>

Last accessed on 20th August 2015.

²⁶⁷ *UK Cyber Security: The Role of Insurance in Managing and Mitigating the Risk* (HM Government and Marsh 2015). p 8.

The document can be found at:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/415354/UK_Cyber_Security_Report_Final.pdf>

Last Accessed on 25th August 2015

²⁶⁸ *ibid* at 9.

²⁶⁹ Information can be found at:

<<https://www.abi.org.uk/Insurance-and-savings/Products/Business-insurance/Cyber-risk-insurance>>

Last Accessed on 20th of August 2015

tion and response costs as a result of a cyber-attack.²⁷⁰

One might question the extent to which a cyber-attack may result in a physical loss or damage. This may have been uncommon in the past but it is, nowadays, a growing concern for investors where such investors fear that hackers might gain access into their network and have the ability to control the information of the investment and organize unscheduled shutdowns for certain machinery used to produce the goods sold by the investor. Such shutdowns may cause losses in the investment. This was, for the example, what happened to a German steel company in 2014.²⁷¹

Some of the most common means of information theft communicated over private and public networks happens through phishing scams or emails containing link to malicious software which, once installed, subjects the investor to the loss of confidential information and theft of the confidential information by the sender of such email.

As examined, commercial risk is that related to the direct operations of the investor and is an inherent part of any investment. Due to the advancements we are experiencing every day, new risks are emerging and threatening investments.

²⁷⁰ *ibid* at 11.

Distributed Denial-of-Service (DDoS) attacks are attacks on the investor's network that cause interruption or business outage which could result in making the investor's network inaccessible for an undefined period of time.

This information can be found at:

ibid at p 12.

²⁷¹ Hack attack causes 'massive damage' at steel works, BBC Technology (22 December 2014)

News Article can be found at:

<<http://www.bbc.co.uk/news/technology-30575104>>

Last Accessed on the 20th of September 2015

2.4.3. Financial Risk

At times, foreign investors may face certain risks affecting the host state's currency or the home state's inflation rates. These risks are related to external economic factors are related to the investment or the project itself. They could include currency exchange rate, change in the interest rates or changes in the inflation rates. They could also include the availability of credit to investors and the cost of such credit.²⁷² These types of risks are not directly related to the investment rather they are related to the host state's economic and financial system.

Generally, this type of risk could be a risk on its own or one that is closely related to the political system of the host state.

When the financial risk emerges due to the political system of the host state, it then falls under the political risk classification. As it will be discussed later on this chapter, there are certain borderlines that exist and could make it challenging to label one action under certain risk without it being, directly or indirectly, falling under another risk.

In that respect, distinguishing the borderline between these risks would allow us to successfully determine what category of risks each action falls under. It shall be noted that in this section, financial risk will be discussed as a risk on its own and not as one related to the political risk.

²⁷² Kazunobo Hayakawa, Fukumari Kimura, Hyun-Hoon Lee, 'How Does Country Risk Matter For Foreign Direct Investment?', IDE Discussion Paper (Institute of Developing Economy 2011) p 5.
The article can be found at:
<<http://www.ide.go.jp/English/Publish/Download/Dp/pdf/281.pdf>>
Last accessed on the 20th of February 2016.

The change in interest rates is a risk that foreign investors may encounter especially when such investors resort to long-term financing since banks and loan providers do not provide long-term loans at fixed rates. This occurs when the financial institution that granted investors a loan changes the interest rate on such loan affecting negatively the operations of the foreign investor.²⁷³

Changes in the inflation rate may, also, affect negatively or positively of investors' investment. This risk, along with the change in the interest rate, is, typically, related to project financing. Generally speaking, inflation refers to the increase in the price of goods and services while the purchasing power decreases.²⁷⁴ Though inflation has positive impacts on the economy, yet, at the same time, it may lead to discouraging long-term investments and therefore affect negatively on investors. It was suggested that when inflation rate increases, uncertainty increases as well, and this uncertainty discourages long-term investments.²⁷⁵ This type of risk maybe closely tied with the political decision of the host state. This will be examined in the practical example of Argentina presented in this section.

Currency exchange risk, on the other hand, is related to market's behaviour towards currencies. It is the result of the market's demand. Currency exchange rates are affected by the political situation and to the economic system and standings of the host state. The sounder the economic and financial systems of the host state and the more stable the

²⁷³ Yescombe (*Chapter 2, n9*) pp 257 & 265-278.

²⁷⁴ *ibid* at 257.

²⁷⁵ Alex Ehimare Omarkhanlen, 'The Effect of Exchange Rate and Inflation on Foreign Direct Investment and Its Relationship with Economic Growth in Nigeria', (2011) n1 Annals of "Dunarea de Jos" University - Fascicle I. Economics and Applied Informatics. p 8.

political situation is the sounder and stronger is the currency of that state. A sound and strong currency would encourage investors to invest in a given state since it normally signals a strong economic standing. The weaker the currency is, the more discouraged investors will be to invest in the host state using the host state's currency. Investors are normally encouraged by the host state's limited intervention in the determination of the currency's exchange rates.

The major type of risk encountered by investors in that respect would be the loss of value of the local currency. This is true when the investment is made using the local currency that, later on, suffers from devaluation or from a catastrophic loss in its value.²⁷⁶ This may happen due to major economic disturbances or due to war. This is, for example, what happened in Lebanon during to the civil war which started in 1970's. As a result of the war, the Lebanese Pound, lost its value. In the early 1980's, 1 U.S Dollar was equivalent to 3-5 Lebanese pounds then the value of 1 U.S. Dollar was equivalent to 22 pounds until the currency, finally, devaluated and reached 2755 Lebanese Pounds for 1 U.S Dollar.²⁷⁷

²⁷⁶ Yescombe (*Chapter 2, n184*)pp 286 - 290.

This is for example what happened with Argentina, as it will be elaborated later on within this section.

²⁷⁷ More information can be found at:

Noura Boustany, 'Devaluated Currency Terrorizes Beirut' (*Washington Post* 29 Novemeber 1987). Also published on (*L.A. Times*).

Found at:

<http://articles.latimes.com/1987-11-29/news/mn-25239_1_west-beirut/2>

Last Accessed on 3 December 2015.

And at;

<<http://www.tradingeconomics.com/lebanon/currency>>

Last Accessed on the 3rd of December 2015.

Another type of risk considered as a financial one is the refinancing risk. Refinancing is, basically, a short-term loan that is refinanced by long-term loans.²⁷⁸ The risk here may be the lack of liquidity in the bonds or loans market during the refinancing period.²⁷⁹

Financial risk can be considered a risk on its own as long as it is occurring in a free market whereas, as it will be examined later, in controlled markets these, ideally, would be considered as political financial risks. In addition, the host state's government may impose on remittance through, for example, allowing investors' application for hard currency while blocking, at the same time, the exchange rate necessary for the remittance.²⁸⁰ This risk would also be a political financial risk.

A good example involving financial risk would be Argentina. As it will be proved at the end of this example, Argentina's case is an illustration of the political financial risk. In 1989 Argentina decided to free up its market and started a series of privatization and denationalization of companies belonging to the public sector.²⁸¹ In addition, and in order to attract foreign investments, Argentina started signing a number of BITs and introduced favorable regulations to foreign investors and started to promote its market and its

²⁷⁸ This is, for example, the practice in the U.S.

For more information please refer to:

Yescombe (*Chapter 2, n184*) pp 293 -294.

²⁷⁹ *ibid* at 294.

²⁸⁰ Rubins and Kinsella (*Chapter 2, n65*) pp 17.

²⁸¹ For more information on Argentina please refer to the following:

JF Hornbeck, 'The Argentine Financial Crisis: A Chronology of Events' [2001] CRS Report for Congress. p 1.

Document can be found at:

<<http://fpc.state.gov/documents/organization/8040.pdf>>

Last Accessed on the 3rd of December 2015.

And;

William W Burke-White, 'Argentine Financial Crisis: State Liability Under BITs and the Legitimacy of the ICSID System', (2008) 3 Asian Journal of WTO and International Health Law and Policy. p 203.

Document can be found at:

<<http://heinonline.org/HOL/LandingPage?handle=hein.journals/aihlp3&div=11&id=&page=>>

Last Accessed on the 3rd of December 2015.

And;

Swan and Murphy (*Chapter 2, n228*) pp 52 - 54.

economic and financial stability to foreign investors and for that, Argentina paired its currency, the Peso, to the U.S. Dollar on the basis of one-to-one.²⁸²

By the end of 1990s, the system followed by Argentina was not able to sustain itself and, as a result, Argentina was not able to keep the Peso paired to the Dollar at the one-to-one rate due to the economic situation it was experiencing. The International Monetary Fund (IMF) offered a rescue package but Argentina refused to take it and ended up with a financial crisis that reached its peak in 2001-2002.²⁸³ As a result of the crisis, Argentina unpaired the Peso from the Dollar in order to reduce the effect of financial crisis it is experiencing. This soon led to the devaluation and crash of the Peso. Argentina also introduced certain regulations allowing the state to freeze and to limit bank deposits and transfers done by investors and imposed, as well, limitations on cash withdrawals.²⁸⁴

Since Argentina, the host state, imposed limitations and introduced regulations that affect the financial and economic situation of the host state and limiting the access of investors to their property rights, this could be considered as a political financial risk rather than being considered as a pure political or pure financial risk.

²⁸² Swan and Murphy (*Chapter 2, n228*) pp 52 – 54.

²⁸³ For more information on Argentina please refer to the following:

Hornbeck (*Chapter 2, n281*) pp 3-6.

And;

Burke-White (*Chapter 2, n278*) p 203

And;

JF Hornbeck, 'Argentina's Defaulted Sovereign Debt: Dealing with the "Holdouts"' [February 2013] CRS Report for Congress. pp 2-3.

This article can be found at:

<<https://www.fas.org/sgp/crs/row/R41029.pdf>>

Last accessed on the 20th of February 2016.

²⁸⁴ The ideas in this paragraph were reported by:

Swan and Murphy (*Chapter 2, n228*) pp 52 - 54.

And;

Burke-White (*Chapter 2, n278*) p 203.

Change in the taxation regime could be, at first, considered as a financial risk but it is, however, more of a political risk rather than a financial one since it is connected to the legal system of a given state as it will be explained in the following section. However, in the next paragraph, this type of risk was classified as a financial risk. The classification of the change in taxation regime depends on the level of the tax introduced. A normal increase on the tax rate would not stand as a financial risk while if the increase in the rate was abnormal, then this becomes a financial risk.

It shall be noted, however, that in order to consider such abnormal increase as a pure financial risk, it should affect all investments of the same nature in the host state while if only affected one given investor, this could be more of a political risk and therefore would rather be political risk.

To elaborate further on the matter of financial risk and in order to understand the investors' concern while investing in a given state, it would be helpful to refer to the list prepared by Lloyd's of London as part of the study on what concerns investors the most while investing. It is noted that financial related risks topped the chart with high taxation being ranked as the highest concern of investors. On the list was also, inflation, availability of credit, currency fluctuation, change in the interest rates and government spending cuts.²⁸⁵

²⁸⁵ The list ranked financial related risks as follows:

High taxation ranked in first place being the biggest and highest concern to investors followed by inflation in the 7th place and availability of credit in the 8th place. Currency fluctuation ranked 10th while change in the interest rates ranked 11th and, finally, government spending cuts in the 18th place concluding the presence of financial risk in the list of risks.

The full list can be found in the study prepared by Lloyd's for the 2013 period on its 6th and 7th pages and is made available online through:

2.5. The Disputed Borderline Between FDI Related Risks

Though these three major types of risks seem to be easy to distinguish at first, they are, however, pretty much integrated and, at times, it may be difficult to label a particular action under a specific risk. This uncertainty is a source of many disputes and has created controversies.

The conundrum normally lies in the commercial and political risks.²⁸⁶ As such, the following findings and differentiations is a new approach to further help in classifying the risks faced by investors. Since sometimes these risks tend to be integrated with one another they, could easily be misinterpreted. For that, insurance companies, MIGA and ECAs have clearly stated the actions that they cover against. This research will suggest new set of risks based on various actions covered by MIGA, ECAs and insurance companies. These risks are presented throughout this section and in Table A.²⁸⁷ The reason behind this further classification is the fact that sometimes actions falling under specific type of risk may be falling under another one and in that sense its components belong to two different risks and for that cannot be classified under one risk without the other.

<<http://www.lloyds.com/~media/Files/News%20and%20Insight/Risk%20Insight/Risk%20Index%202013/Report/Lloyds%20Risk%20Index%202013report100713.pdf>>

Last accessed on the 20th of August 2015.

²⁸⁶ Moran (*Chapter 2, n85*). p 80.

²⁸⁷ Table A at p 131.

2.5.1. Borderline Between Political and Financial Risks

In states that adopted the theory of a free market, the performance of the local currency and inflation and interest rates are totally up to the market's behavior. In these states, the political intervention is from minimal to null depending on the markets performance. Normally, governments that opted for a free market will not interfere in the market's performance unless there was a catastrophic event threatening the economic and financial stability of the host state. But this case is actually an exception to the rule.

It shall be noted that prior to the crisis in Latin America and in Asia, the stream was going towards referring to such risks as either commercial or financial after the crisis this view changed and it was thought that this crisis occurred due to the intervention of the governments in the markets.²⁸⁸

On the other hand, there are countries whose government monitor closely and control the financial economic performance and interferes in the currency exchange rate, interest rate and in the inflation rate. These are normally done in a way that may, sometimes, be for the purpose of depriving the foreign investors from gaining maximum benefit from their investment and to limit their performance. In this case, these actions, though they constitute financial risk, they do, however, fall under the political risk due to the direct or indirect involvement of the host state's government or local authorities in this matter.

²⁸⁸ Rubins and Kinsella (*Chapter 2, n65*) p18.

This may also apply to countries that opted for a free-financial market. For that, and for the purpose of simplification, this situation where the financial risk is actually a political one, it would be of help to label it as a political financial risk. The Overseas Private Investment Corporation, OPIC, which is the ECA of the United States of America, puts under political risk one aspect falling under the financial risk. This is, according to OPIC called the “Currency Inconvertibility” and this happens when investors are not able to legally convert their earnings from local currency of the host state to U.S. Dollars for a period of 90 days.²⁸⁹ Protection against this type of risk will be discussed in later chapters.²⁹⁰

Financial risk is one not related to the investment made in the host state rather it is related to the host state’s economic and financial system. For example, currency exchange rate, refinancing risk, any change in interest rates or in the inflation rate of the host state are some of the examples of financial risk.²⁹¹

As discussed in earlier chapters, changes in the inflation rate may affect negatively or positively the investor’s investment. The same applies to changes in interest rates; however, currency exchange risk is related to the market’s assessment of currencies.²⁹²

²⁸⁹ Information on OPIC can be found at:
What We Do’ (*Overseas Private Investment Corporation (OPIC)*)
<<https://www.opic.gov/what-we-offer/political-risk-insurance>>
Last accessed on the 19th of May 2015
and at:

Rubins and Kinsella (*Chapter 2, n65*) p 17.

²⁹⁰ This topic will be examined within the scope of chapter 4 of this research.

²⁹¹ This matter was elaborated in chapter 2.4.3.

²⁹² *ibid.*

The loss of value of the local currency, therefore, would be one of the major risks an investor may encounter. This is true when the investment is made using the local currency of the host state and this currency suffers from devaluation or a catastrophic loss in its value due to a major economic disturbance or due to war.²⁹³

The borderline between financial and political risk occurs when the host state has a controlled financial market. Therefore, as long as the host state enjoys a free financial system where interest rate, inflation and currency exchange rates are not as controlled and rather left to the market to determine its value, then this is considered as a pure financial risk.²⁹⁴ Once the host state has a direct control on and manipulates with the financial situation and controls interest rates, inflation rates and currency exchange rates to preclude investors from enjoying their property rights and from benefiting from them, then, this is classified as a political financial risk.

2.5.2. Borderline Between Political and Commercial Risks

Political risk implies a threat to foreign investments through means of interference by the host state which may act in ways that prevent investors from benefiting from their investment or may pose a threat to investors' property rights.²⁹⁵ Political risk comprises

²⁹³ As was the case in Lebanon in the 1980s and Argentina in early 2000s.

See, Chapter 2.4.3.

²⁹⁴ *ibid.*

²⁹⁵ Kobrin (*Chapter 2, n197*) p 4.

And;

Theodore H. Moran, *International Political Risk Management: Exploring New Frontiers* (World Bank 2001) p 80.

And;

Busse and Hefeker (*Chapter 2, n205*) p 3.

of various actions that presented earlier in this thesis.²⁹⁶ In addition, political risk also includes legislative risk, which includes changes in laws and regulations affecting investors. It refers to restrictions on repatriation of the foreign investor's funds, changes in the taxation regimes, environmental laws or in securities regulations as well as the change in the methods of dispute settlement or even restrictions on trade.²⁹⁷ It may also include import or export restrictions.²⁹⁸ These are normally tied up with the decision of the host state's government and that is the reason for considering them as political.

Sometimes foreign investors may encounter number of factors that may lead them to lose their investment partially or fully. Such losses may take place while the investment is in the construction phase. This is especially true when talking about investments in project finance. Such risks can be considered as commercial risks.²⁹⁹ As mentioned earlier, the market's perception of the goods or services foreign investor is offerings are offering are considered commercial risk. As such it is one that they may encounter while investing, in both, home and host states and has no known insurance or cover against it.³⁰⁰

Commercial risk, notably, includes contractual risk. In that respect, foreign investors entering foreign markets may choose to partner with local investors who probably have 'connections' that would make the investment run easier or smoother. This is chosen by

²⁹⁶ This was examined in chapter 2.4.1.

²⁹⁷ For more information please refer to chapter 2.4.1.

²⁹⁸ *ibid.*

²⁹⁹ See;

Yescombe (*Chapter 1, n18*) p 14.

According to Yescombe, these actions falling under the commercial risk with regard to project finance take place in the construction phase.

³⁰⁰ *ibid.*

foreign investors in order to hedge the risks that they may face. In such scenario, the foreign investors may be at risk of not having their contractual obligations respected by local partners or by the suppliers or other host state parties with which they have a contractual relationship with.³⁰¹

Alternatively, foreign investors may partner with the host state's government.³⁰² Following this scenario, commercial risk may be closely tied to political risk and in this case such action, i.e. the contractual risk may not be a commercial risk rather be a political commercial one. In that respect, this contractual risk includes what is known as contract frustration. This happens when the host state's government undertakes measures or decisions preventing investors from performing their contractual obligations whether in full or in part.³⁰³ This also applies if foreign investors have a contractual relationship with the host state's its representative. Here, and in case the host state or any of its representatives did not respect their contractual obligation, such act would be considered as a political commercial risk rather than a commercial one. This is, mainly, due to the fact that the party involved in the contract is the host state or its representative and the fact that it is more difficult for an investor to force the host state to honor the contractual obligations. This is true since the government or its representative, may use their position to escape honoring the contractual obligations with foreign investors.

³⁰¹ *ibid.*

This could also include corruption on part of the host state party in JVs as examined earlier in this chapter.

See:

Muchlinski, Ortino, Schreuer (*Chapter 2, n13*)

³⁰² John R Pate, *The Laws of Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners* (1929) 23 Special Number Supplement to the American Journal of International Law. p 134. Article 8.

And;

See chapter 2.5.

³⁰³ Wenhua Shan and Jinyuan Su, *China International Investment Law: Twenty Years of ICSID Membership*, (Brill Nijhoff 2015) pp 153 – 155.

Though this action is straightforward and may happen even with non-governmental parties, it is, however, of a higher risk to be borne by the foreign investor since the non-performance of the contractual obligations, in this case, is closely related to a political or official decision rather than a personal and market related corporate decision.³⁰⁴

For that, and since it is more difficult for an investor to oblige the host state to perform its contractual obligations or to indemnify him without having to resort to international investment arbitration or other form of *post-investment protection* method to claim his rights, this should fall under the considered as as the political commercial risk.

In addition, and as mentioned earlier, there is another new type of risk that could be considered both a commercial and political risk referred to as the cyber risk. This type of risk is closely related to technological advancements and could lead to losses suffered by investors financially or any form of image or reputation disruption that an investor suffers as a result of an organized attack on its private or public networks. It may, also, be the disruption of the services they offer over such networks.

Such attacks may originate from any given state and not necessarily from the host state or the home state and may also originate from the decision of a government of a given state who may not necessarily a direct relation with the investor or exporter of goods or services.³⁰⁵

³⁰⁴ This point of view is also supported by Noah Rubins and N. Stephan Kinsella in: Rubins and Kinsella (*Chapter 2, n65*) pp 22-23.

³⁰⁵ This matter was discussed earlier in Chapter 2.

Cyber risk can be considered as a commercial risk that investors in certain sectors are expected to face where hackers could hack the private networks of a financial institution or a given business in return of financial gains.³⁰⁶ While it could be, as well, a political risk once a given state decides to use this tool as a mean to threaten investors' property rights.

For example, in a recent case, an ATM machine that belongs to one of the Ukrainian banks started dispensing money randomly and after investigation it was discovered that this bank was subject of a cyber-attack.³⁰⁷

This passes as an example of the cyber risk falling under the commercial risk category while in the case of Sony Pictures and North Korea cyber risk is one closely falling under political risk. This happened when Sony Pictures Entertainment, a movie production company, was about to show in theatres worldwide a movie depicting the North Korean President Kim Jung-Un when Sony was hacked by a group which was later confirmed to be North Korean as an opposition to showing this movie and contained, as well, a threat of a devastating cyber-attack if the movie was shown which resulted in the cancelation of the movie release in theatres.³⁰⁸

³⁰⁶ This can be concluded from Lloyd's Quick Guide to Cyber Risk. 'A Quick Guide to Cyber Risk', Lloyds.

The document is available at:

<<https://www.lloyds.com/news-and-insight/news-and-features/emerging-risk/emerging-risk-2015/a-quick-guide-to-cyber-risk>>

Last accessed on the 20th of February 2016.

³⁰⁷ This is found in an article written by David E. Sanger and Nicole Perlroth and published by NY Times: David E Sanger and Nicole Perlroth, 'Bank Hackers Steal Millions via Malware' *New York Times* (18 February 2015).

News article can be found at:

<<http://www.nytimes.com/2015/02/15/world/bank-hackers-steal-millions-via-malware.html>>

Last Accessed on the 25th of August 2015.

³⁰⁸ Found in articles written by Lori Grisham in the USA Today and by Alec Ross published by the Huffington Post:

Though this does not directly entail a risk that an investor in a host state faces it is, however, considered a cross-border investment where movie production companies distribute their movies worldwide in order to achieve financial gains. And though this type of investment might not necessarily reach or be broadcast in a given state the investor could suffer from financial losses due to a politically-driven attack against a certain investment.

Both types of cyber risks have no known insurance coverage through ECAs or MIGA and for that they are not yet covered by them. On the other hand, a limited number of insurance companies offer limited coverage against cyber risks and at times they offer consultancies and management of such risks rather than proper coverage.

These are nowadays, considered major risks and, at least, cyber-attacks falling under the political risk label should be covered against on a global basis rather than the traditional host state/ home state basis. This risk poses, as well, grave dangers to IT companies that provide services such as cloud computing where incidents of breach of users' copyrights were recorded.³⁰⁹

Lori Grisham, *Timeline: North Korea and the Sony Pictures hack*, USA Today (5 Jan 2015)

News article can be found at:

<<http://www.usatoday.com/story/news/nation-now/2014/12/18/sony-hack-timeline-interview-north-korea/20601645/>>

Last Accessed on 25th of August 2015.

And;

Alec Ross, Sony Hack Attacks Presage New Warfare: The Weaponization of Code, '*Huffington Post*' (updated 15 Feb 2015).

News article can be found at:

http://www.huffingtonpost.com/alec-ross/sony-hack-weaponization-of-code_b_6334168.html

Last Accessed on 25th of August 2015.

³⁰⁹ Though these breaches were directed at end users of the investor's service, it could, however mean that a breach of the investor's property rights available on the cloud service maybe compromised.

An example for the breach of end user's property rights available through cloud computing services would be the

Table A at the end of this chapter explains, elaborates and highlights the various types of risks faces by foreign investors. Since the matter of cyber risk is fairly new and due to the lack of information and lack of widespread offering of protection against such risk, this risk was not included in any of the explanatory tables attached within this research.

It can be concluded that, provided there is no government interference, commercial risk is considered a pure risk but once the government is a party to the contract with the foreign investor then there is the risk of having such commercial risk becoming a commercial political one.

2.5.3. Borderline Between Commercial and Financial Risks

The borderline between financial and commercial risks is clearer than that between political and commercial risks or that between financial and political risks. This is, mainly, due to the fact that actions considered commercial are closely related to investors and their relations with those involved in the investment rather than with the host state. Whereas financial risk is more related to the host state's situation rather than that of the investor.³¹⁰

famous case of celebrity photographs leakage from Apple's iCloud.
Leo Kelion, Apple toughens iCloud security after celebrity breach, 'BBC' (17 September 2014).
News article can be found at:
<<http://www.bbc.co.uk/news/technology-29237469>>
Last Accessed on the 20th of August 2015.

³¹⁰ Yescombe (*Chapter 2, n184*) p 197.

To elaborate more, commercial risk would entail any breach of contract, barriers on imports of goods to the host state or delays in the projects delivered or any increase to the raw material's prices or due to a contract mismatch.³¹¹ On the other hand, financial risk would relate to any action posing a threat to investments due to the financial situation of the host state and this may include currency exchange rates, inflation or deflation or even the change in interest rates.³¹²

It was in Yescombe's work that the suggestion of separation of commercial risk and financial risk was presented where the financial risk was thought to fall, normally, under the commercial risk classification.³¹³ This view is more accurate and allows an easier distinction between the various risks involved in foreign investment.

As has been examined, the distinction between commercial and financial risk is not as challenging as that between commercial and political risk or that between financial or political risk.

2.6. Conclusion

Foreign investors are those who are investing in a foreign state. They may choose to invest directly into the host state through owning at least 10% of the ordinary shares or

³¹¹ N.B. Such risks are directly related to the project or investment made in the host state.

See;

ibid.

³¹² *ibid* at p 257.

³¹³ Yescombe (*Chapter 1, n18*) pp 183-199.

voting powers of the company and this, in return, involves the transfer of organizational expertise, management, capital, technology, access to national market of the host state and the transfer of entrepreneurship incentives. Alternatively, they may choose to invest indirectly into the host state through acquiring shares, as long as the threshold of ownership of the shares does not exceed 10%, bonds or through acquiring any other financial instrument.³¹⁴

Investors, prior to deciding whether to invest in a certain state or not conclude a series of studies and analysis in order to decide whether it is feasible or not to go through such venture. Among these, is one that handles, in details, all the risks associated with the investment. Another factor that investors consider, as well, prior to their investment, is the legal regime of the host state. It is advisable that investors seek a state with a well-developed legal system and advanced regulatory framework, which may help them benefit from favorable taxation and investment laws.³¹⁵

It is up to investors to do their due diligence and properly investigate foreign investment laws and regulations applied in the host state. Not only that, but it is of importance that investors learn to what extent the laws are applied and how they are interpreted. Certainly, investors need to examine the host state's situation and market reception of similar goods or services offered and they need, as well, to be aware of cultural and historical background of the host state since these, normally, have an effect on the attitude of the

³¹⁴ This is based on the IMF distinction discussed earlier in this chapter in section 2.1.

³¹⁵ Malcolm D Rowat, 'Multinational Approach to Improving the Investment Climate in Developing Countries: The Case of ICSID and MIGA' (1992) 33 Harvard International Law Journal, p 104.

And;

Michael A Geist, 'Toward a General Agreement on the Regulation of Foreign Direct Investment' (1995) 26 Law and Policy in International Business, pp 673-706 (1995).

market and have an influence on the laws and regulations as well as on the political and financial systems. In that sense, investors are expected to be knowledgeable about the legal procedures accompanying the establishment of a new investment in the host state. As such, the host state may have an open-door policy towards foreign investors and in this case, they are welcoming to foreign investors and impose minimal restrictions on the investor's entry into the local market or it may follow the closed-door policy towards investors and in this case, impose a number of restrictions on the entry of foreign capital and on the exiting of foreign capital as well.

Investors will study the economic and financial systems of the host state in order to find out how the market performs and how solid and stable is the host state's economic system.³¹⁶ For that, they analyze and go through inflation and exchange rates of the prospective host state. What is important in studying the economic and financial systems in the host state is that if the economic system is weak and unstable then, this will probably lead to the increase in the risk incurred by the foreign investor, especially the political risk.³¹⁷

Classically, there are three major types of risks a foreign investor may encounter while investing abroad and these are political risk, financial risk and commercial risk. These risks, though clear and easily distinguished at first, may actually be more complicated and may be heading, at times, more towards the political risk. For that it was emphasized in this chapter that the introduction of two new separate categories of investment-related risks. These were the political financial risk and the political commercial risk. To hedge the said risks and in order to

³¹⁶ Yi (*Chapter 2, n93*) p 5.

³¹⁷ Rubins and Kinsella (*Chapter 2, n65*) p 27.

minimize them, the investor may seek reducing these risks by knowing the legal system of the host state, looking for BITs, MITs and other existing IIAs between the home state and the host state.

As examined, political risk includes expropriation, creeping expropriation and nationalization. Expropriation is argued to include direct and indirect expropriation, creeping and de facto expropriation and even regulatory expropriation.³¹⁸ It also include any changes in the laws and regulations of the host state directed at limiting investors from benefiting from their property rights.³¹⁹ In addition, political risk may include, as well, some aspects of the commercial and financial risks only once the host state's government interferes. In that case, it is rather more accurate to refer to these risks as political commercial risks or political financial risks since they are neither pure political risks or pure financial or commercial risks. As mentioned, both the financial and commercial risks can fall under the political risk classification. Commercial risk and political risk can be merged together in limited situations whereas the financial and political risks may be much easier to determine.

It is not always black and white when determining the types of risks that the investor may face. There are cases that may fall in the gray area and therefore analyzing its background will help in determining where it absolutely belongs to. It is not always that we have pure commercial risk or pure financial risk, rather, at times; one of these two will be closely related to the major risk that foreign investors face when investing abroad and

³¹⁸ This point of view was adopted by Christopher Dugan, Don Wallace., Noah Rubins and Borzu Sabahi. For more information please refer to:

Dugan, Wallace, Rubins and Sabahi (*Chapter 2, n210*) p 450.

³¹⁹ Ferro (n 231) pp 6-7.

that is the political risk. Therefore, and as it was explained earlier, we would have, according to the mentioned justification, political risk and under political risk we have political financial risk and political commercial risk.

In the end, it is up to the investor to decide whether he is willing to take the risks associated with his investment abroad or not and upon his decision, the investor who decided to invest in a risky market would, ideally, seek some means of protection against these risks.

Risk Category	Acts Falling Under These Risks	Acts Falling Under These Risks	Acts Falling Under These Risks	Acts Falling Under These Risks
Political Risk	<ul style="list-style-type: none"> • Expropriation • Nationalization • Confiscation 	Change in the laws and regulations including: <ul style="list-style-type: none"> • limitations on transfer of proceeds and remittance • change in taxation regimes affecting one specific investor • Trade Restrictions 	<ul style="list-style-type: none"> • War • Civil Unrest and Violence • Terrorism 	Creeping Expropriation
Commercial Risk	Breach of Contract with Importer or Private Party	Project Related Risks like delays in date of finalization of project or ensuring extra expenses	<ul style="list-style-type: none"> • Gain or loss from the investment • Changing costs of material • Cyber Risk 	<ul style="list-style-type: none"> • Buyer's insolvency • Payment default and repudiation
Financial Risk	Change in Interest and Exchange Rates	Inflation and price stability	Currency inconvertibility	Unnormal Change in Taxation Regime
Political Financial Risk	Political Interference in determining Interest Rate	Political Interference in determining Exchange Rate	Political Interference in the Inflation	
Political Commercial Risk	Breach of contract by host state	Non Payment of investor debt by the host state	Corruption	Cyber Risk (When initiated by a given state to cause losses to an investor's interest)

Table

A

(FDI-Related

Risks)

Chapter Three: Risk Minimization through Home and Host States' Coordination

In order to facilitate foreign investments, and to reduce risks associated with such investments, many national and international movements have been taking place requesting the protection of investors. For that, many states adopted favorable legal systems towards foreign investors allowing them more freedom to invest in various sectors, more freedom with regard to the limits of ownership of investments, more protection for their rights, and better means for dispute settlement. Such policies allowed the inflow of investors.¹

This was a result of international effort and cooperation directed at granting foreign investors more favorable treatment and more protection for their property rights while investing internationally. Along with that, foreign investors may seek to protect themselves or minimize risks associated with their foreign investment through means other than legal regimes.

International agreements between home and host states and recommendations made by international bodies from the Harvard Draft to the agreements made by the OECD and WTO as well as the establishment of ICSID have all been efforts directed at the promotion and protection of foreign investors. Not only that, these are, as well, considered

¹ Thomas L. Brewer, *Foreign Direct Investment in Developing Countries: Patterns, Policies, and Prospects* (World Bank Publications 1991). p 1.

means of cooperation and coordination between home and host states to protect foreign investors.

Along with that a movement to unify commercial related laws was introduced through UNIDROIT. Harmonization of law is of minor importance when it is compared to tort and property laws where, in commercial and contract law, the law of choice normally prevails as a measure of protection of investors.

Not only that, but unilateral movements by the home state through diplomatic protection or the host state's initiative to protect investors through introduction of favorable laws and regulations are considered, as well, some of the means of promotion and protection of foreign investments. These are regarded as a starting point in the protection of investors.

In addition, Investors can, generally, start the process of protecting their property rights through the agreements they make with other parties. As such, investors can protect themselves by adding certain clauses in the contract that could protect them against the loss of their property. This is especially true when the investor is entering into a contractual relationship with the host state's government. These may include an arbitration clause, a stabilization clause which is thought to protect the investor against the changes in laws of the host state, a *force majeure* clause, a damages clause which, is thought to allow the investor to obtain a wider range of remedies in a resulting dispute resolution procedure,² an interest rate clause and, finally, local remedies and conversion of curren-

² Rubins and Kinsella (*Chapter 2, n65*) p 59.

cy clauses which grant investors the right to transfer proceeds of the investment from currency of the host state into another currency.³

Despite these legal movements, which will be the core concentration of this chapter, both home and host states have realized that the legal effort may not be enough and should be complemented by a more practical approach that should add an extra layer of security and protection to investors. This is through national and regional insurance programs and through arbitration. For example, and as it will be explained in the next chapter, MIGA is an attempt to cover investors of member states against certain political risks while investing in another member state. Along with this regional movement there is a national insurance program, offered by agencies based in exporting countries, that is also in charge of covering against certain risks encountered by investors. These agencies are known as ECA.⁴

Though the presence of all these mechanisms have helped in the reduction of international trade and investment-related risks, it was important to reassure investors further through allowing them the right to claim their property rights through international investment arbitration. Some host states have taking further initiatives to promote foreign investments through assuring investors that no further regulatory burdens shall be imposed on investors.⁵ Other host states encouraged foreign investments through purchasing the products produced by foreign investors.⁶

³ *ibid* at 31-67.

⁴ Please note that MIGA will be referred to and elaborated in this chapter in section (3.3) and ECAs will be discussed in detail in chapter 4 of this thesis.

⁵ Salacuse (*Chapter 1, n11*) p. 13

⁶ *ibid*.

In this chapter, a presentation of how protection of foreign investors was possible by studying the international effort directed at protecting foreign investments, passing through the role played by IIAs through, mainly BITs and MITs, and it will study how international organizations have helped in enhancing the protection granted to foreign investors until, finally, discussing the coordination between the home state and the host state in that respect.

3.1. International Effort Directed at Protecting FDI

Since many countries are competing to attract foreign capital every day, it is crucial that host states enact certain regulations and adopt a number of laws that ensures the protection of such capital. Developing countries are the main destination of foreign investors from the developed world. Investors are lured to what these states enjoy from vast richness in natural resources and fertile land for investment to their, somewhat, relatively cheap operating expenses, labor, and relatively reduced environmental costs. Not only that, but host states are interested in what investors have to offer from new technology and skilled labour to their capital.⁷

Regions like Latin America, the Middle East and South-East Asia are some of the main attractions of foreign capital. Though these enjoy many promising investment opportu-

⁷ Nicholas Apergis, Katerina Lyroudi and Athanasios Vamvakidis, 'The Relationship between Foreign Direct Investment and Economic Growth: Evidence from Transitional Countries' (Social Science Research Network 2007) p 11.

Article can be found at:

<<http://papers.ssrn.com/abstract=990251>>

Last accessed on the 18th of January 2013.

And;

Crotti, Cavoli and Wilson, (*Chapter 2, n89*) p 259.

nities they do, however, present certain risks. In order to ease up the flow of FDI, especially those flowing from developed nations to developing ones, high levels of protection are needed to reduce any risks investors may encounter. For that reason, states as well as international organizations have directed their efforts and coordinated with one another to help in reducing such risks.

For example, international movements and agreements like the GATT and GATS have been introduced to facilitate and ease up trade between signatory states until the GATT was extended to include investments following the introduction of TRIMS in 1994.⁸ Such initiatives along with the Bilateral and Multilateral Investment Treaties, which will be discussed later in this chapter, are considered some of the forms of IIAs.⁹ BITs were used as a mean to facilitate and encourage investments.¹⁰

These instruments have been popular ways to attract and promote investments since they are designed to protect and liberalize foreign investors.¹¹ For example a new

⁸ See;

Campbell McLachlan, 'Investment Treaties and General International Law' (2008) 57 *International & Comparative Law Quarterly*, p 367.

⁹ Through this economic integration, investors are attracted and more investments are stimulated.

See;

Paul Brenton, Francesca Di Mauro and Matthias Lücke, 'Economic Integration and FDI: An Empirical Analysis of Foreign Investment in the EU and in Central and Eastern Europe' (Social Science Research Network 1998) pp 1 & 22.

This article can be found at:

<<http://papers.ssrn.com/abstract=139908>>

Last accessed on the 18th of January 2013.

¹⁰ See;

Efraim Chalamish, 'An Oasis in the Desert: The Emergence of Israeli Investment Treaties in the Global Economy' (2010) 32 *Loy. L.A. Int'l & Comp. L. Rev.* p 123.

And;

Michael J. Trebilcock, Robert Howse and Antonia Elison, *The Regulation of International Trade* (4th edn Routledge 2013). p 11.

¹¹ Sauvans and Sachs (*Chapter 1, n22*) p 3.

And;

Trebilcock, Howse and Elison (*Chapter 3, n10*). p 11.

And;

Brenton, Di Mauro and Lücke (*Chapter 3, n11*) pp 1 & 22.

movement between the EU block and the US has resulted in the formation of the Transatlantic Trade and Investment Partnership (TTIP).¹² This agreement, which still in the negotiation phase, is said to have a positive impact on EU investors and on export and import in general.¹³

In addition, one type of IIAs, the BITs, which will be discussed in the next section of this chapter, is designed to regulate issues related to admission of foreign direct investment, treatment of these investments and how to settle disputes arising between the host state and foreign investors.

BITs, also, normally, address the issue of expropriation and in that respect, they serve as means of transparency with regard to any risks that may be faced by foreign investors and this, in return, helps in the reduction of any risks investors may encounter.¹⁴ BITs, therefore, should offer protection to foreign investors' rights, help host states and encourage them to adopt market-oriented policies that ensures a fair treatment to investors and to, finally, support the development of international law standards.¹⁵

¹² Shayerah Ilias Akhtar and Vivian C. Jones, 'Proposed Transatlantic Trade and Investment Partnership (T-TIP): In Brief', (11 June 2014) Congressional Research Service Report. p 1.

This document can be found online at:

<<http://www.fredsakademiet.dk/ordbog/tord/ttip.pdf>>

Last accessed on the 22nd of February 2016.

And;

For list of member states of the EU please refer to Appendix IV.

¹³ Since the text of this agreement is yet to be determined the research will not analyze it later on and the topic was presented as a source of up-to-date information on the recent movements in the protection of foreign investments.

More information, including the one written can be found at:

<http://ec.europa.eu/trade/policy/in-focus/ttip/about-ttip/>

Last accessed on the 12th of August 2015.

¹⁴ Sauvart and Sachs (*Chapter 1, n22*) p 253.

¹⁵ *ibid* at 253 - 254.

In general, MITs are one of the forms of IIAs which are similar to BITs. The only difference being between the two is that MITs are conducted between three or more states whereas BITs are between two states. They both share similar components from the protection and promotion of investment to the treatment granted to investors and to the means of dispute settlement.

On the other hand, there has been a movement towards the unification of commercial related laws between number of states in order to improve the protection granted to investors. The international Institute for the Unification of Private Law (UNIDROIT) is in charge of attempting to harmonize commercial law between its 63 member states and to formulate uniform law instruments rules to realize this objective. This intergovernmental organization could be considered a form of international cooperation between member states.¹⁶

The International Finance Corporation and the World Bank established what is known as the Foreign Investment Advisory Service (FIAS) which helps in advising governments on matters related to policy and promotion through studying the investment climate of the prospective host states, grants advocacy services on the taxation system and on the investment climate of the host state and assists in removing any administrative existing barriers which would make attracting foreign investors more difficult.¹⁷

Another World Bank member involved in the promotion and facilitation of internation-

¹⁶ More information on UNIDROIT can be found at:
< <http://www.unidroit.org/about-unidroit/overview>>

Last Accessed on the 10th of August 2015

¹⁷ More Information can be found at:

<<http://www.oecd.org/investment/investmentfordevelopment/28096934.pdf>>

Last Accessed on the 23rd of August 2015

al investments is the International Finance Cooperation (IFC) which helps the private sector in developing countries.¹⁸

Regionally, and in Europe, the European Bank for Reconstruction and Development (EBRD) was founded in the early 1990's to help reconstructing and promoting investments and the economic reform in Central Eastern European countries. Nowadays services of the EBRD reaches beyond Europe reaching Middle Eastern and Asian states.¹⁹

Recently, the European Union have been calling for the creation of an investment court that settles disputes arising between the host state and investors. This proposal comes side by side with the TTIP, which will be discussed in the following chapter, and other forms of IIAs.²⁰

The matter of protection of foreign investors' property was, historically, subject to many international non-binding treaties. These efforts then were transformed into binding treaties were states created a form of international cooperation that resulted in Bilateral Investment Treaties (BITs), and these treaties are the most common type of International Investment Treaties;²¹ not to mention that international organizations, such

¹⁸ Information can be found at:

<http://www.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/about+ifc_new>

Last Accessed on the 23rd of August 2015

¹⁹ Information can be Found at:

<<http://www.ebrd.com/what-we-do/products-and-services.html>>

Last Accessed on the 23rd of August 2015

and;

<<http://www.ebrd.com/who-we-are.html>>

Last Accessed on the 23rd of August 2015

²⁰ More information can be found at:

<http://europa.eu/rapid/press-release_IP-15-5651_en.htm>

Last accessed on the 19th of September 2015

²¹ Sauvart and Sachs (*Chapter 2, n65*) p 37.

as the WTO and the OECD, produced a number of recommendations to facilitate and promote international investments.²²

Add to that, many states decided to organize themselves and form a more collective form of investment treaties referred to as MITs or the Multilateral Agreement on Investment (MAI). This group of nations decided, later, to cooperate with other regional bodies to ease up trade and investments between them.²³

Lastly, and most importantly, both the home and host states are playing, nowadays, a vital role in facilitating and easing the flow of FDIs and in reducing the risks that such investors may encounter in their international quests. This last matter will lead to the introduction of ECAs and how they play a role in the promotion and protection of FDI.

3.2. The Role of BITs and other IIAs in Protection of Foreign Investment

There have been a number of international efforts directed at protecting foreign investors. Though not all of these efforts enjoyed a binding nature, they may be considered, however, as a cornerstone in the modern international efforts directed at investment protection. Such efforts started within the last century.

²² This will be further elaborated within this chapter in section 3.3. and in section 4.4.

²³ These forms will be discussed in section 3.2.

One of the earliest drafts designed to protect foreign investors came from Harvard in 1929.²⁴ The Harvard draft on International Responsibility of States for Injuries to Aliens acknowledged the right of foreign investors to hold the host state responsible for an injury that such investors may suffer from due to the host state's actions. Though this draft was not a binding one, it suggested the host state's liability towards aliens, as the text described, for injuries caused by it.²⁵

A year later, at the Hague Codification Conference in 1930, the issue of responsibility of States was present where, according to the text, a state is responsible for its failure to carry out international obligations leading to the damage of an alien's property.²⁶ This responsibility was delegated to state's representatives or, as the text described them, "organs acting under its name and for its benefit."²⁷ The responsibility of the host state towards an alien is present once the latter suffers from damages due to the host state's actions through introducing new legislations limiting the investor's ability from benefiting from his property rights.²⁸

²⁴ 'Part II: Responsibility of States for Damage Done in Their Territory to the Person or Property of Foreigners' (1929) 23 Special Number Supplement to the American Journal of International Law. pp 133- 239.

²⁵ The Harvard Draft Convention stated that the Host State is responsible for a number of acts highlighted in its 18 Articles.

For more information refer to:

ibid pp 133-135.

And;

Harvard Draft Convention on the Responsibility of States for Damages Done in their Territory to the Person or Property of Foreigners (1929).

Available at:

(1929) 23 AM J INT'L LAW Special Supplement, p 133.

And;

Louis B Sohn and R.R. Baxter, 'Responsibility of States for Injuries to the Economic Interests of Aliens' (1961) 55 American Journal of International Law p 548. Section A Article 1.

²⁶ Edwin M. Borchard, "'Responsibility of States,'" at The Hague Codification Conference' (1930) 24 The American Journal of International Law, pp 518 & 520.

And;

Shabati Rosenne, *The International Law Commission's Draft Articles on State Responsibility: Part 1, Articles 1-35* (Martinus Nijhoff Publishers 1991) p 1.

²⁷ Borchard (*Chapter 3, n26*) pp 517-518.

²⁸ Hague Codification Conference [1930] Article 6.

And,

Abs-Shawcross Draft Convention on Investment Abroad is another landmark effort to protect foreign investors against host state actions. This convention, dated 1959, requested the abolishment of discriminatory measures and introduced the notion of fair and equitable treatment.²⁹ It also introduced special measures for lawful expropriation which includes that expropriation can only be legal once it is made without prejudice, and without discrimination and, finally, once it is made for the public interest.³⁰

Fair and equitable treatment is, nowadays, one of the main components of any BIT, as it will be clarified hereafter. The draft cited limited occasions when the property of an alien may not be, for a limited time only, subject to the privileges of fair and equitable treatment measure. These are, according to Article V, public emergencies including war and hostilities.³¹ The draft suggested resorting to arbitration to resolve disputes arising from the application of the draft.³²

In 1961, the idea of the host state's responsibility of injuries caused by it towards foreign investors evolved. In that year, UN's Yearbook of the International Law Commis-

Green H. Hackworth, 'Responsibility of States for Damages Caused in Their Territory to the Person or Property of Foreigners: The Hague Conference for the Codification of International Law' (1930) 24 *The American Journal of International Law*. p 503.

²⁹ See Article I of the Abs-Shawcross Draft Convention.

The Abs-Shawcross Draft Convention of 1959 was republished in Volume V of the UN's International Investments Instruments: A Compendium, published in 2000.

The document can be found at:

<http://unctad.org/en/Docs/dite2vol5_en.pdf>

Last accessed on the 9th of October 2014.

The draft can also be found at:

UNCTAD, United Nations Conference on Trade and Development, 'Draft Convention on Investments Abroad (Abs-Shawcross Draft Convention)', 1959.

³⁰ These can be found at:

George Schwarzenberger G, 'ABS-Shawcross Draft Convention on Investments Abroad: A Critical Commentary, The' (1960) 9 *Journal of Public Law*, pp 155-161.

³¹ See Abs-Shawcross Draft Convention (*Chapter 3, n29*), Article V.

³² *ibid*, Article VII.

sion, the issue of repatriation, on part of host state, for injuries to aliens caused by it was discussed heavily.³³

The Convention on the Organization for Economic Co-operation and Development (OECD) was signed by 20 member states in 1960.³⁴ The OECD issued in 1967 a list of binding recommendations and guidelines related to the protection of foreign property.³⁵ Like its predecessor conventions and drafts, it adopted notions present in previous texts and added to it a new set of recommendations. For example, Article 3 of the said draft convention, which set the limits of host state expropriation of foreign property, adopted the limits drawn in Abs-Shawcross Draft Convention related to non-discriminatory measures and elaborated more on the conditions for such act.³⁶ Along that, the justification of compensation, which was present in the UN's 1961 Yearbook of the International Law Commission had been transformed into a recommendation in the aforesaid OECD Draft.³⁷ This recommendation of Just and Equitable Compensation is nowadays present in BITs and its one of the major components of such treaties.

The new concept that the OECD Draft suggested, back then, was granting aliens the freedom of repatriation of their immovable property or income, profit or any other fruits and rights gained from ownership of the property owned in a foreign territory.³⁸

³³ United Nations, *Yearbook of The International Law Commission 1961*, vol. II (United Nations Publications 1962) pp 1-45.

³⁴ 'List of OECD Member countries - Ratification of the Convention on the OECD' can be found at Appendix III.

³⁵ Convention on the Organization for Economic Co-operation and Development OECD, 'Draft Convention on protection of foreign Property' (OECD 1967).

³⁶ *ibid*, Article 3. p 17.

And;

Abs-Shawcross Draft Convention 1959 (*Chapter 3, n29*). Article I.

³⁷ Convention on protection of foreign Property 1967, Notes on Article 3, B. p 20.

³⁸ *ibid* Article 4. p 23.

Though BITs have a clause requesting national treatment of foreign investors, this concept has been present for a while. In 1868, a request was made by the Argentinian jurist Carlos Calvo to offer foreign investors national treatment.³⁹ The intended national treatment suggested by the Argentinian jurist entails that a foreigner should not be given special treatment differing from that granted to a national investor.⁴⁰

Calvo suggested that foreign investors should waive their right to diplomatic protection while investing in the host state.⁴¹ This doctrine was adopted by the international Conference of American States of 1889-1890.⁴² To some, the Calvo doctrine is considered more as a contractual relationship between the host state and the foreign investor and because of that it may be subject to disputes with regard to the application, interpretation, and preference and contract performance.⁴³

The Calvo Doctrine was not the only doctrine found to minimize or weaken the role of diplomatic protection and reduce home state's protection by force, the Drago Doctrine,

³⁹ R. Doak Bishop, James Crawford, and William Michael Reisman, *Foreign Investment Disputes: Cases, Materials and Commentary* (Kluwer Law International 2005) p 3.

N.B. The revised draft on international responsibility of the state for injuries caused in its territory to the person or property of aliens introduced the notion National Treatment in Article 1.

See;

United Nations, Yearbook of The International Law Commission 1961, vol II (United Nations Publications 1962) p 46.

And;

This was also one of the views reflected by early european institutional writings.

See;

Sornarajah (*Chapter 2, n612*) p 18.

⁴⁰ Christopher K Dalrymple, 'Politics and Foreign Direct Investment: The Multilateral Investment Guarantee Agency and the Calvo Clause' (1996) 29 Cornell International Law Journal, p 163.

⁴¹ *ibid.*

N.B. The Calvo Doctrine was adopted by the international Conference of American States 1889-1890.

See;

Myers S. McDougal, Harold D. Lasswell and Lung-Chu Chen, 'The Protection of Aliens From Discrimination and World Public Order: Responsibility of States Conjoined with Human Rights' (1976) 70 The American Journal of International Law, p 445.

⁴² See;

McDougal, Lasswell and Chen, (*Chapter 3, n41*), p 445.

⁴³ This is found in the work of Amerasinghe:

Chittharanjan F Amerasinghe, *Diplomatic Protection (Oxford Monographs in International Law)* (Oxford University Press, USA 2008) p 193.

which was later codified in the Potter Convention in 1907 forbids intervention of home state by force to collect public debt and considers such act to be illegal.⁴⁴

These requests did not differ from today's BIT clause of National Treatment in offering foreign investors the right to resort to local courts while waiving their right to 'diplomatic protection'.⁴⁵ The difference lies in the foreign investor's right to resort to international arbitration, which is present in most of nowadays BITs.

It is worthwhile mentioning that the waiver of diplomatic protection suggested by the Calvo Doctrine is not absolute. The doctrine cites special cases where foreign investors may seek diplomatic protection if the host state, for example, denied foreign investors justice.⁴⁶ Add to that, the Calvo doctrine suggests that foreign investors would not have the right to resort to international tribunals and applying, therefore, international laws.⁴⁷ It shall be noted that some Latin American countries enacted the Calvo doctrine with a friendly investment arbitration approach.⁴⁸

BITs are a mean of cooperation between home and host states. They are not only an investment promotion tool, which is the aim of developing states, rather they act as a

⁴⁴ *ibid* at 191.

And;

Amos Hershey AS, 'The Calvo and Drago Doctrines' (1907) 1 *The American Journal of International Law*, p 31.

⁴⁵ Bishop, Crawford, and Reisman (*Chapter 3, n39*) p 3.

And;

This treatment is also present in the Convention for Protection of Industrial Property.

See;

George Hendrick Christiaan Bodenhausen, *Guide to the Application of the Paris Convention for the Protection of Industrial Property, as Revised at Stockholm in 1967*, vol 611 (World Intellectual Property 1968) p 16.

⁴⁶ Dalrymple (n 331) p 165.

⁴⁷ Bernardo M Cremades, 'Resurgence of the Calvo Doctrine in Latin America' (2006) 7 *Business Law International*, p 54.

And;

Hershey (*Chapter 3, n44*) p 31

⁴⁸ Daniel de Andrade Levy, Ana Gerda de Borja and Adriana Noemi Pucci (eds), *Investment Protection in Brazil* (Wolters Kluwer, Law & Business 2014) p.10.

mechanism for market liberalization, which, is the aim of developed countries.⁴⁹ In addition, BITs act as a fundamental source of international law with regards to foreign investments.⁵⁰ These are enforceable rules directed at the protection of foreign investors and to reduce some of the risks they may encounter.⁵¹ These risks are mostly political risks.⁵²

Germany & Pakistan were among the first states to use BITs as a mean to facilitate and protect their investors' investments in 1959.⁵³ The goal behind this move was to adequately and effectively manage compensations for expropriation as proposed by Developed Countries.⁵⁴

BITs are signed in order to facilitate foreign investment from developing countries that enjoy abundant capital and good and skilled labour force to a less developed country.⁵⁵ Not only that, it is, also, for some states like the U.S., a mean of protection of home state's investors.⁵⁶ Since BITs are a tool of commitment taken by parties of the treaty to assure that the rights of foreigners are to be protected, policy makers in developing countries tend to believe that signing these will help them increase the inflow of FDI

⁴⁹ Sauvart and Sachs (n 20) p 121.

⁵⁰ Martins Paporinkis, *Basic Documents on International Investment Protection* (Hart Publishing Ltd 2012) p.7.

⁵¹ Rose-Ackerman and Tobin (n 19) p 6.

⁵² Salacuse (n 8) p. 13.

⁵³ Eric Neumayer and Laura Spess, 'Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?' *World Development*, Volume 33, (2009) pp. 349, 350.

And;

Paporinkis (*Chapter 3, n50*) p.7.

⁵⁴ Kenneth J Vandevelde, *Bilateral Investment Treaties: History, Policy, and Interpretation* (Oxford University Press 2010) p 77.

⁵⁵ Sauvart and Sachs (*Chapter 1, n22*) p 253.

⁵⁶ For example, the US's interest in conducting and signing BITs and IIAs, in general, is for the protection of their investors investing abroad.

See;

Herman J.R Walker, 'Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice' (1956) 5 *The American Journal of Comparative Law*, p 229.

thus, increasing their attractiveness among investors.⁵⁷ They, as other IIAs, grant foreign investors with a number of substantive rights.⁵⁸

BITs grant investors the right to take legal actions against the host state should the last infringe any of the investors' property rights through expropriation and nationalization. This is true when such acts by the host state take place under discriminatory situations and without any justification as if the property was expropriated for public purposes or if the expropriation was done without any just and equitable compensation.⁵⁹

Many BITs include, in matters related to expropriations, clauses that consider any act equivalent to expropriation as 'expropriation'.⁶⁰ This is known as creeping expropriation as it was elaborated earlier in the thesis.⁶¹

Although many countries wishing to attract inward foreign investment find themselves signing BITs, a number of those, which enjoy rich natural resources, tend to sign agreements that include Most Favored Nation clauses (MFN).⁶² A practice that states are following sometimes, is to favor one state over the other using BITs' through giv-

⁵⁷ Eric Neumayer and Laura Spess, 'Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?' *World Development*, Volume 33, (2009), pp. 349, 350.

And;

Hallward-Driemeier (*Chapter 1, n21*) p.2.

⁵⁸ Susan Franck S, 'Foreign Direct Investment, Investment Treaty Arbitration and the Rule of Law' (Social Science Research Network 2006) p 342.

Found at

<<http://papers.ssrn.com/abstract=882443>>

Last accessed on the 18th of January 2013.

⁵⁹ Hallward-Driemeier (n 19) p.4.

⁶⁰ *ibid* at 6.

⁶¹ Please refer to chapter 3 section (3.4.1) for more information on expropriation and creeping expropriation.

⁶² Rose-Ackerman and Tobin (*Chapter 1, n21*) p 10.

ing them more rights. Such clause gives investors a better treatment in investment-related matters among investors from other nations.⁶³

The notion of Fair and Equitable Treatment in BITs, as explained earlier, was borrowed from 1959's Abs-Shawcross Draft Convention.⁶⁴ It is one of the measures the host state undertakes in BITs to attract inward investments.⁶⁵ In that respect it can be considered one of the important components of BITs. It is then related to the standard of treatment of investors where foreign investors are granted a fair and equitable treatment and one that is not less favored than that of their national investors.

For example, the Multilateral Investment Agreement between Argentina, Brazil, Paraguay and Uruguay, and later joined by Venezuela, known as the Mercosur emphasizes on granting the investors treatment not less favorable than that granted to local investors.⁶⁶

To sum it up, the protection offered to foreign investors by BITs includes National Treatment, Most Favored Nation Treatment (MFN), Fair and Equitable Treatment, Security and Investment Protection, Non-discriminatory measures taken against investors, an Umbrella Clause,⁶⁷ where the host state offers to honor its agreement with foreign

⁶³ Wael Saghir, 'Andean Commission's FDI Decision on Technology Transfer a Comparative Study of FDI Laws and Regulations' (Institute of Advanced Legal Studies, School of Advanced Study, University of London LLm Collection 2012) p 9.

⁶⁴ Abs- Showcross Draft Convention on Investment Abroad [1959], (n 327).

N.B. It is noted that the notion of Fair and Equitable Treatment was first introduced in the Havana Charter of 1948. See;

Havana Convention for an International Trade Organization [1948], Article 11(2) a.i.

⁶⁵ Saghir, (*Chapter 3, n63*) p 7.

N.B. These clauses are present in all investment agreements nowadays and not only in BITs.

⁶⁶ Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur, (*Chapter 2, n96*) Article 2.

⁶⁷ Jarrod Wong, 'Umbrella Clauses in Bilateral Investment Treaties: Of Breaches of Contract, Treaty Violations, and

investors, and, lastly, protection against expropriation.⁶⁸ Along those, the common layout of a Bilateral Investment Treaty includes general obligations towards the investment, some standards for expropriation, currency transfer and dispute settlement procedure.⁶⁹

Another important clause included in a number of BIT is one related to the transfer of proceeds of the investment. An example of such clause would be the following:

“Each State shall extend to investments established in its territory by nationals and companies of the other State fair and equitable treatment. Such treatment shall not be less favorable than that accorded by the State to its own nationals and companies, or to nationals and companies of any other state, whichever is more favorable. Without restructuring the generality of the above each state shall allow the transfer without delay of the proceeds of investment in its territory by nationals and companies of the other State”.⁷⁰

In general, most BITs offer similar protection and dispute resolution mechanisms.⁷¹

The only difference is the types of investments that are subject to protection. For ex-

the Divide Between Developing and Developed Countries in Foreign Investment Disputes’ (2006) 14 *George Mason Law Review*, p 138.

Article can be found at:

<http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1260897>

Last accessed on the 28th of January 2013.

⁶⁸ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 10.

⁶⁹ *ibid.*

⁷⁰ This was quoted from:

Shihata (*Chapter 2, n90*) p 242

⁷¹ Rose-Ackerman and Tobin (*Chapter 1, n21*) p 7.

ample, many BITs do not protect the telecommunication sector as well as the security or the financial sectors.⁷²

It may be worthwhile mentioning that some investors would overlook the fact that a given state has no BIT and, therefore, agree to invest in it due to the richness of its natural resources; while in other situations investors look at the fact whether the host state succeeded in protecting the property rights belonging to investors or not.⁷³ Normally, countries with high political risk are more likely to attract less foreign investors than those enjoying lower levels of risks.⁷⁴

BITs may also be referred to as Foreign Investment Promotion and Protection agreements (FIPA). Canada for example negotiated and signed many FIPA agreements that have conditions similar to those of the BITs.⁷⁵ The first Canadian FIPA was signed with Poland in 1990.⁷⁶ It is of importance to mention that this FIPA stated that resolving any disputes between investors and the host state should be within conformity with the United Nations Commission on International Trade Law rules.⁷⁷ On the other hand, the FIPA between Argentina and Canada signed in 1999 stated that courts of the host state, as a rule, are the competent body to resolve disputes and as an exception, arbitral

⁷² *ibid.*

⁷³ *ibid* at 11.

⁷⁴ *ibid* at 17.

⁷⁵ Canada's Foreign Investment Promotion and Protection Agreements (FIPAs).

Found online through:

<<http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/fipa-apie.aspx?lang=eng>>

Last accessed on the 22nd of February 2016.

⁷⁶ List of Canadian Foreign Investment Promotion and Protection (FIPAs) Signed and in Force.

Found online through:

<<http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/index.aspx?lang=eng>>

Last accessed on the 22 of February 2016.

⁷⁷ Agreement Between the Government of Canada and the Government of the Republic of Poland for the Promotion and Reciprocal Protection of Investments, E101511 - CTS 1990 No. 43. Article IX(3)

Treaty can be found online at :

<<http://www.treaty-accord.gc.ca/text-texte.aspx?id=101511&lang=eng>>

Last Accessed on the 30th of August 2013

bodies should have the right to resolve these disputes should the investor agree on that, and only when the host state's tribunal does not reach a final decision after eighteen months of submission of the papers to the host state's tribunal; or if the host state's tribunal reached a final decision but the parties are still in dispute.⁷⁸

It shall be noted that before the presence of BITs, agreements on Friendship, Navigation and Commerce, (FNCs) were quite a common practice among European countries in the 1820s.⁷⁹ According to Walker, these treaties were concluded for the purpose of providing 'judicial basis' for their economic ventures. FNCs were more of an economic instrument rather than political one. FNCs were also a cross Atlantic mechanism to enhance development relations between states. Notably, the U.S. and France signed a treaty of Amity and Commerce in 1778.⁸⁰ One of the notable FNCs was the one concluded in 1886 between Greece and the UK. These FNCs may be considered as an earlier form of modern BITs, were able to regulate how foreign investors are treated by the host state.⁸¹

Based on the aforementioned, BITs contain distinctive features and as such they include components like the Umbrella Clause, Most Favored Nation Clause, Provisions

⁷⁸ Agreement Between the Government of Canada and the Government of the Republic of Argentina for the Promotion and Protection of Investments, E101514 - CTS 1993 No. 11, Article X(2)

Treaty can be found online at :

<<http://www.treaty-accord.gc.ca/text-texte.aspx?id=101514&lang=eng>>

Last Accessed on the 30th of August 2013

⁷⁹ Vandeveldelde (*Chapter 3, n54*) p.7.

⁸⁰ See;

Herman J.R. Walker, 'Treaties for the Encouragement and Protection of Foreign Investment: Present United States Practice' (1956) 5 *The American Journal of Comparative Law*, pp 230.

And;

Herman J.R. Walker, 'Modern Treaties of Friendship, Commerce and Navigation' (1957) 42 *Minnesota Law Review*, pp 805-806.

⁸¹ Bishop, Crawford and M Reisman (*Chapter 3, n39*) p 4.

related to Non-Precluded Measures and clauses related to the application of the concept of the State of Necessity.

According to Rudolf Dolzer & Margaret Stevens “Purpose of the Umbrella clause is to ensure that each party will respect specific undertakings towards nationals of the other party.”⁸² The presence of an Umbrella clause would increase confidence of investors and protect investors investing in sectors not always covered in the provisions of a BITs.⁸³ Though it may be thought that an Umbrella clause would be of specific importance, it, nevertheless has no effect in the decision making of a given investor.⁸⁴

On the other hand, NPM or Non-Precluded Measures, may include the concept of the State of Necessity.⁸⁵ The State of Necessity is present when a state refrains from performing certain international obligations of a lesser weight to protect a threatened and essential interest, from a grave and imminent danger.⁸⁶

It is worth noting that public order and national security do not prevent a state from applying the state of necessity concept.⁸⁷ In addition, many MFN clauses may include the application of non-discriminatory measures. These non-discriminatory measures are not novel concepts presented in BITs, rather they have been already embedded in customary international law.⁸⁸

⁸² T.J Girerson Weiler, *Investment Treaty Arbitration and International Law* (JurisNet 2008) pp. 6-7.

⁸³ *ibid* at 6-7.

⁸⁴ *ibid*

⁸⁵ *ibid* at 150

⁸⁶ *ibid* at 148

⁸⁷ *ibid* at 183

⁸⁸ *ibid* at 270

To further encourage investors, promote investments and protect investors' property rights, BITs included an expropriation clause that is thought to identify the measures of expropriation, the measures of compensation against such act and the measures of transferring such compensation.⁸⁹ What is noted is that, as mentioned earlier, BITs are not standardized documents with standard provisions, clauses and wordings rather they are tailored to the needs and agreements of contracting states and for that, there may be some differences between one BIT and another but in general they are thought to share similar qualities and outcomes. For that, when it comes to expropriation, for example, some BITs required the existence of public interest in order for expropriation to be legal while others added that such act needs to be done in a non-discriminatory manner.⁹⁰ On the other hand other BITs just found it enough to state that expropriation need not to be without the payment of compensation.⁹¹ Not only that, but differences exist, as well, in determining the compensation for such action where some BITs considers the prompt, adequate and effective compensation while others asks for the payment of fair and equitable compensation, reasonable compensation, full compensation or the payment of a just compensation.⁹²

The same applies for the transfer of compensation where some BITs required the payment of interest at a normal commercial rate if the transfer of compensation was delayed, other BITs considered the payment of such interest a matter to be agreed on between the contracting parties.⁹³

⁸⁹ *See*; Shihata (*Chapter 2, n90*) pp 256-257.

⁹⁰ *ibid* at 256.

⁹¹ *ibid*.

⁹² *ibid*.

⁹³ *ibid* at 257.

An example for an expropriation clause in a BIT would be as follows:

“Each State agrees not to expropriate, nationalize or take any other measure having the same or similar effect with respect to investments established in its territory by nationals and companies of the other State except in the furtherance of the public interest [and not in contravention of any special of any special commitment] , and against adequate, prompt and effective compensation . Such compensation shall amount to the market value of the investment expropriated immediately before the expropriation, or before the intention to embark thereon became public knowledge, shall be made without delay, be effectively realizable and be freely transferable.”⁹⁴

Another component of BITs concerned with post-investment protection is the Dispute Settlement Clause. Many of the bilateral investment treaties resorts to ICSID proceedings where ICSID settles disputes arising between host state and foreign investor or between two states on the interpretation of a BIT.⁹⁵

⁹⁴ This was quoted from:
ibid at p 258 Type A.

⁹⁵ This is for example used in the BIT between Italy and Lebanon and in the BIT between Spain and the Philippines.
See;

Agreement Between the Italian Republic and the Lebanese Republic on the Promotion and Reciprocal Protection of Investments (1997). Article 7(2)b.

And;

Agreement Between the Kingdom of Spain and the Republic of Philippines on the Promotion and Reciprocal Protection of Investments (1993) Article 9(2)b. (Translated from Spanish)

An example of a Dispute Settlement Clause in BITs is as follows:

“1. Any dispute relating to an investment established in the territory of either Contracting State by a national or company of the other Contracting State shall, as far as possible, be settled amicably through consultation by parties to the dispute. Should the parties fail to arrive at an amicable settlement within three (six) months from the date of the first written request to enter into such consultation, the dispute shall be settled by arbitration in accordance with the following provisions of this Article.

2. The dispute shall be settled by a Tribunal consisting of three members appointed in the following manner. Within two months of the request for arbitration each party shall appoint one member of the Tribunal, and the two members shall, within two months of their appointment, agree on a third who shall act as a Chairman of the Tribunal.

3. If within the periods specified in paragraph (2) of this Article the appointment therein mentioned have not been made either of the parties to the dispute may request the [Secretary-General of the International Center for Settlement of Investment Disputes/ Chairman of the International Court of Arbitration of the International Chamber of Commerce] to make the necessary appointments.

4. The tribunal shall reach its decision by a majority of votes. Such decision shall be final and shall be binding on both parties. Each party shall bear the cost of its own member of the Tribunal and of its representation in the arbitration proceedings; the cost of the Chairman

and the remaining costs shall, unless the Tribunal decides otherwise, be borne by the parties equally. The Tribunal shall determine its own procedures.”⁹⁶

Some BITs go one step further and add an extra clause related to the prospective position of insurance companies should there be a dispute arising between the host state and a foreign investor. The Subrogation Clause is thought to have an effect on the promotion of investment where an insurance provider that an investor restored to, prior to investing in the host state, is entitled to any of the investors’ rights and as such the subrogation is valid. This is, for example, found in the BIT between Canada and Russia.⁹⁷

Historically, capital-exporting countries created BITs to protect their investors and facilitate new ones.⁹⁸ Though facilitation, protection and promotion of foreign investment are the main goals behind concluding BITs, it is not always the case that a state needs to sign or ratify one to attract foreign investments.

A state can incorporate the substance of BIT in its laws and regulations and offer the same protection without necessarily drafting a BIT.⁹⁹ Investors cannot, nevertheless, rely on such existence of the legislation.¹⁰⁰ Brazil has, so far, signed only 14 BITs none of which are in force. Despite that it managed to be the 13th most desired state for

⁹⁶ This was quoted from:

Shihata, (*Chapter 2, n90*) pp 264-265 Type B.

⁹⁷ Agreement between the Government of Canada and the Government of the Union of the Soviet Socialist Republic for the Encouragement and the Reciprocal Protection of Investment; Signed 1991; Article VIII.

⁹⁸ Vandeveldt (*Chapter 3, n54*) p 3.

⁹⁹ *ibid* at 4.

¹⁰⁰ *Ibid*.

foreign investment¹⁰¹ and is considered safe for foreign capital and it is still able to attract more capital significantly from the EU.¹⁰²

It has been noted that BITs include inter-state rights and obligations. Nevertheless, investors are covered within these agreements and granted a special treatment that entitles them to procedural rights which allow them to seek their property rights through submitting a claim against the host state.¹⁰³ This idea was presented in an arbitral judgment held by ICSID concerning Archer Daniels Midland (ADM) and the Mexican government where Archer Daniels Midland, an American Company, formed a JV with a Mexican company and created ALMEX. Mexico, later on, imposed new taxes, which had a negative direct impact on ADM. As such ADM claimed that such an action was contrary to the NAFTA's National Treatment Clause.¹⁰⁴

In principal, BITs take the first place in the hierarchy of laws. In that respect, any form of BIT whether it was labeled as a protocol or an agreement, it is still considered highest in the hierarchy of laws.¹⁰⁵ And these treaties are governed by another convention, the Vienna Convention, which draws the lines with regard to interpretation of BITs and other international treaties.¹⁰⁶

¹⁰¹ Brazil the ranks in attracting foreign investment compared to other Mercosur states. It came in the 13th place followed by Argentina in the 40th place and Venezuela in the 55th. Uruguay and Paraguay came in the 73rd and the 94th place respectively.

This data was made available through the CIA Factbook at:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

¹⁰² De Andrade Levy, de Borja and Pucci (eds), (*Chapter 3, n48*) pp 4 & 6.

¹⁰³ *Archer Daniels Midland Company and Tate & Lyle Ingredients Americas, Inc v The United Mexican States* [2007] ICSID Case No. ARB(AF)04/05., 21 November 2007.

¹⁰⁴ *ibid.*

¹⁰⁵ Christopher Greenwood, 'Sources of International Law: An Introduction', (United Nations 2008)

The article can be found at:

<http://legal.un.org/avl/pdf/ls/Greenwood_outline.pdf>

Last accessed on the 23rd of February 2016.

¹⁰⁶ Rules of interpretation of the treaties can be found in Section 3 of the Vienna Convention.

The issue, with regard to the effectiveness of BITs as a mean to reduce foreign investment-related risks, is present when it comes to application of the BIT itself. In that respect, the host state may decide to terminate the investment treaty. Not only that, but the host state may also decide to terminate it retroactively.¹⁰⁷ This would basically strip the investor from the protection and any other benefits granted to him as a result of a BIT and any of these special treatments and rights would be considered as if they never existed and that the investor is not entitled to resort to arbitration anymore to claim rights established under the BIT.¹⁰⁸ It is worth noting that BITs have a duration of 10 years with some of them having an automatic renewal.¹⁰⁹

The German BITs normally provides for a no less-favourable treatment to be awarded to foreign investors with regards to any measures taken by the respective member states in cases of “public security and order, public health or morality”.¹¹⁰ Such treatment is accorded on a non-discriminatory basis.

See;

Vienna Convention on the Law of Treaties (1969) Section 3.

¹⁰⁷ This matter was discussed in an article published by UNCTAD in 2010.

‘Denunciation of the ICSID Convention and BITs: Impact on Investor-State Claims’, IIA issue No 2 (December 2010), UNCTAD. pp 1-8.

Document can be found online at:

< http://unctad.org/en/Docs/webdiaeia20106_en.pdf >

Last accessed on the 23rd of February 2016.

Basically, this document suggests that the impact of terminating a BIT would only be limited to cases presented to ICSID which have Survival Clauses included within them. For example, such clause can be found in the BIT between the U.S. and Argentina in Article XIV.(2).

See;

Treaty between United States of America and the Argentine Republic Concerning the Reciprocal Encouragement and Protection of Investment. (1991) Article XIV.(2).

¹⁰⁸ James D. Fry, Odysseas G. Repousis, ‘Intertemporality and International Investment Arbitration: Protecting the Jurisdiction of Established Tribunals’, *Arbitration International* Volume 31 number 2, pp 257-258.

¹⁰⁹ See;

Federico Lapova, Lucas Barrieros, Victoria Bruno, ‘How to Kill a BIT and not Die Trying: Legal and Political Challenges of Denouncing or Renegotiating Bilateral Investment Treaty’, (2012) *Society of Economic Law*, p 11.

¹¹⁰ Agreement between the People’s Republic of China and the Federal Republic of Germany on the Encouragement and the Reciprocal Protection of Investment; Signed 2003, paragraph 4(a).

Generally, BITs fall under the scope of IIAs. IIAs are normally designed to attract, promote and facilitate investment as well as to protect it. Such agreements share similar structure and goal of BITs and therefore are not the different from one another rather complimenting one another. IIAs may include Bilateral Agreements, Multilateral Agreements, Free Trade Agreements on the basis of bilateral relationship or a multilateral one.

Sometimes they may differ with the amount of incentives granted to investors or with protection granted to them against losses of property rights. In general, as mentioned, IIAs are all similar in concept since they are all directed at the promotion of international trade and the protection of investors property rights. The only, somewhat, difference between the various types of IIAs is the amount of protection granted to investors, the treatment of investors, the conflict resolution strategies and the approach towards trade barriers including trade tariffs. These differences may be traced to the various base models followed by respective states who are conducting such agreements.

Briefly, there is the U.S. model of BITs and other trade related agreements, a U.K model and a German model to name a few. The differences exist mainly in the definition of what is considered an investment and what national treatment consists of, for example. To elaborate on that point, in the U.S. BIT model and on the treatment of investors, National Treatment includes granting a no less favorable treatment to investors of the signatory states in all aspects of the investment from the time of its access to a

signatory state and even in cases where such investors resort to governmental or regional bodies.¹¹¹

On the other hand, the U.K. model BIT when talking about treatment of investors state that an investor of a signatory state gets a treatment that is in accordance with customary international law. This means that investors are entitled to ‘fair and equitable treatment’ and to a ‘full protection and security’ and such treatment is granted on the basis of being more than that awarded to aliens.¹¹²

Whereas in the German BIT model, the treatment awarded to investors shall be based on a fair and equitable treatment and on the basis of no less favorable treatment than that awarded to national investors.¹¹³

Some states have organized themselves and unified their investment regulations easing up the transportation of goods, transformation of technology, protection of property rights and eliminating or reducing tax barriers. Such cooperation has been highlighted

¹¹¹ Treaty Between the United States of America and The Original Republic of Uruguay Concerning the Enforcement and Reciprocal Protection of Investment [2006] Article 3.

Found at:

<https://ustr.gov/sites/default/files/uploads/agreements/bit/asset_upload_file748_9005.pdf>

Last accessed on the 20th of August 2015

¹¹² Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the United Mexican States for the Promotion and Reciprocal Protection of Investments [2006] Article 3.

The law can be found at:

<<http://investmentpolicyhub.unctad.org/Download/TreatyFile/2009>>

Last accessed on the 20th of August 2015

¹¹³ Agreement Between People’s Republic of China and the Federal Republic of Germany on the Encouragement and Reciprocal Protection of Investments [2003] Article 3.

The Article reads as follows:

The law can be found at:

<<http://investmentpolicyhub.unctad.org/Download/TreatyFile/736>>

Last accessed on the 20th of August 2015

by signing agreements between these countries. Agreements that take similar form to BITs known as MITs.

The North and South American Continents are full of examples in that respect. The United States, Mexico and Canada in 1992 agreed to eliminate the tariff and trade barriers for goods moving between them allowing open-door trade policy along with the adoption of the fair and equitable treatment of investors and encouraging fair competition.¹¹⁴ This agreement is known as the North American Free Trade Agreement (NAFTA), is said to include provisions related to investment protection that would encourage and promote investments in member states.¹¹⁵ Some of the important topics covered by the NAFTA can be found in Chapters 3, 11, 16 and 17. Though certain treatments awarded to investors have been spread throughout the treaty on sector-to-sector basis, however, these mentioned Chapters cover the important aspects of this treaty.

Chapter 3 of the NAFTA discusses the National Treatment awarded to investors and the elimination of trade related barriers.¹¹⁶ Chapter 11, on the other hand, discusses various investment related measure and entails a number of special benefits designed to attract and promote investors of respective member states. For example, it allows foreign investors national treatment. It also guarantees investors the right of remittance of

¹¹⁴ Neumayer and Spess (*Chapter 3, n53*) p 9.

And;

NAFTA (*Chapter 2, n58*) Part One, Article 102.

¹¹⁵ This point of view was adopted by Eric Neumayer and Laura Spess in an article titled 'Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries?'

This article and information are found at:

Neumayer and Spess (*Chapter 3, n53*) pp 231.

¹¹⁶ NAFTA (*Chapter 2, n58*) Chapter 3.

Chapter 3 of NAFTA will be examined later on within this chapter.

the proceeds of their investments along with granting them a minimum standard of treatment which includes the duty of ‘full protection and security’ and the ‘fair and equitable treatment’.¹¹⁷ Finally, Chapter 16 is concerned with easing access of investors to member states and Chapter 17 discusses the intellectual property rights of investors and its protection.

In general, NAFTA, like other IIAs grants investors and their investments from member states a set of favorable treatments directed at protecting them. For that it granted investors a National Treatment and a Most Favored Nation Treatment along with the standard treatment found in international law and highlighted in the agreement.

The NAFTA made it clear that investors may benefit from a National Treatment and, as such, be treated as if they were nationals of the state of which they are investing in without any prejudice. This National Treatment extends to the establishment and expansion of an investment and to the management, acquisition and operation of foreign investors including sale of such investments.¹¹⁸ In that respect, as suggested in the Loewen case, National Treatment, in principal, should extend to cases where foreign investors or their investments have resorted to local courts of law or in case they were subjected to such measures.¹¹⁹

¹¹⁷ NAFTA (*Chapter 2, n58*) Chapter 11.

Chapter 11 of NAFTA will be examined later on within this chapter.

¹¹⁸ NAFTA (*Chapter 2, n58*) Chapter 3, Article 301; Chapter 11, Article 1102 & 1105; Chapter 12, Article 1202; and Chapter 14 Article 1405.

These discuss the National Treatment under NAFTA. Article 301 presents the National Treatment in matters related to the treatment of goods while Articles 1102, 1202 and 1405 present it in the perspectives of investments in general, in trade and in financial services respectively.

¹¹⁹ The Loewen Group, Inc and Raymond L Loewen v United States Case reference is:

Loewen Group, Inc and Raymond L Loewen v United States, ICSID Case No ARB(AF)/98/3, 26 June 2003, Awarded para 39.

The NAFTA have worked for the elimination of customs duties and called for not increasing already existing customs duties.¹²⁰ The agreement abolishes any restrictions on the importation or exportation of goods.¹²¹ It also provides for the elimination of taxes imposed on exports.¹²² The Treaty, also, suggested a treatment not less favorable than that accorded to national investors of member states. Such treatment is thought, as previously examined, to stimulate and promote investment within respective member states. This treatment is present in Chapters 11, 12 and 14 of the NAFTA Agreement.¹²³

With the presence of all these benefits aimed at promoting investment present in the NAFTA, it is still, however, entails certain restrictions or, more specifically, certain exceptions to the treatment awarded to investors. This is true, for example when looking at the matter of Most-Favored Nation Treatment where Canada, the United States and Mexico allowed themselves not to extend the MFN treatment to investors in aviation, maritime, fisheries and in certain investments in the telecommunication sector.¹²⁴

However, when looking at this agreement and comparing it with that of the EU, one can notice that both have many similarities. Moreover, the protection and promotion aspects of both instruments are, mainly, directed, like any other IIA, at investors of member states. It also has a direct effect on attracting third party investors who do not come from a member state. For example, the TFEU allows investors from third states

¹²⁰ NAFTA (*Chapter 2, n58*), Chapter 3 Article 302.

¹²¹ NAFTA (*Chapter 2, n58*), Chapter 3, Article 309 (1).

¹²² Article 309: Import and Export Restrictions

¹²³ North American Free Trade Agreement, Chapter, 3 Article 314.

¹²⁴ North American Free Trade Agreement, Chapter 11, Article 1103; 12, Article 1203; Chapter 14, Article 1406

¹²⁴ NAFTA (*Chapter 2, n58*) Annex IV: Exceptions from Most-Favored-Nation Treatment, Schedule of Canada, Schedule of United States and Schedule of Mexico.

who have established an economic presence in a member state to freely move goods, capital and people from one country to another without being exposed to extra tariffs, taxes or restrictions.¹²⁵

As it was examined, BITs normally enjoy a similar structure with regard to the sets of rights, obligations and benefits or special treatments awarded to respective member states. BITs may take a more collective form that includes more than one country and this is referred to as MITs or MAI. Both forms, i.e. BITs and MITs are considered IIA and they are all undertaken in order to promote and protect foreign investments. NAFTA, the North American Free Trade Agreement, was said to have influenced IIAs negotiated.¹²⁶

It may be concluded that states enter into IIAs with one another to limit restrictions on capital movement and investments between the contracting states. They draft BITs to address specific circumstances.¹²⁷ These agreements are thought to increase the host state's attractiveness when it comes to foreign investments.¹²⁸ Though they may appear to have the same layout and structure, they, nevertheless, do not share the same components where some IIAs, especially when talking about BITs, tend to offer more pro-

¹²⁵ Treaty of the Functioning of the European Union. Article 63.

"...all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited."

¹²⁶ Christopher Wilkie, 'FDI, development and investment rules: a critique of the UNCTAD Series on Issues in International Investment Agreements', Volume 10 Transnational Corporations UNCTD (2001) number 2 p. 138.

Found at:

<<http://unctad.org/en/Docs/psiteiid27v10n2.en.pdf#page=138>>

Last Accessed on the 25th of August 2015.

¹²⁷ Vandeveldelde (*Chapter 3, n54*) p 1.

And;

Sauvant and Sachs, (*Chapter 1, n22*) p 15.

¹²⁸ See:

Tim Büthe and Burke-White Milner, 'The Politics of Foreign Direct Investment into Developing Countries: Increasing FDI through International Trade Agreements?' (2008) 52 American Journal of Political Science, p Conclusion.

tection to their home Investors than that offered by other home states entering into BITs as is the case with the United States' BITs.¹²⁹

IAs, in general, whether between two member states or more, are a mean of cooperation and coordination between these states and, as such, play a vital role in the promotion of foreign investments. They are designed specifically to liberalize, protect and promote the investment.¹³⁰ Liberalizing means, in the view of the developed home state, creating a climate favorable to foreign investors where they can make their investments that fall within their interest.¹³¹

The majority of these agreements are designed to protect investments and protection results in the promotion of investments.¹³² As an example for investment protection clauses present in BITs, MFN, dispute resolution clauses and nondiscriminatory measures fall under the umbrella of investment protection.¹³³

BITs are also created to achieve certain goals. These include the creation of favorable conditions for foreign investments and to increase prosperity in both, home state and host state.¹³⁴ These offer a safeguard net for such investors protecting and shielding them from infringements on their properties and investments at the host states and grants them special incentives that helps them in conducting their investments there.

¹²⁹ The United States of America's BITs are more proactive in covering certain issues more than other BITs and, therefore, offer a higher level of protection to their investors.

More information found at:

Sauvant and Sachs (*Chapter 1, n22*) p. 133.

¹³⁰ Vandeveldel (*Chapter 3, n54*) p 4.

¹³¹ Sauvant and Sachs (*Chapter 1, n22*) p 122.

¹³² Vandeveldel (*Chapter 3, n54*) p 5.

¹³³ *ibid* at 6.

¹³⁴ *ibid* at 78.

For that, it has been said that BITs often impose too many obligations on the host state and less obligations on the investor according to K. J. Vandeveld.¹³⁵

Not only they are important for foreign investors, they are also of grave importance to the host state where the host state may be rich in natural resources but lacks the ‘know-how’ to benefit from these resources or it does not have the proper technology or even does not possess the adequate education or skills that would allow it to benefit from these resources.¹³⁶ For that, Multinational Corporations and foreign investors from a developing country could help in importing their technology, goods or services and help in building up the host state’s economy. These treaties are, therefore, the first step of the protection phase offered by member states to their investors while engaging in an investment at another member state.

It shall be noted that, though these treaties are the first step to protect MNCs and foreign investors in general, they do not, however, eliminate political risk.¹³⁷ The next phase of protection could come in the form of seeking coverage against risks that have not been covered by these agreements.

¹³⁵ *ibid* at 7.

¹³⁶ Rakash Loungani and Assaf Razin, ‘How Beneficial Is Foreign Direct Investment for Developing Countries?’ (June 2001) Vol 38 Finance and development, Number 2.

Article can be found at:

<<http://www.imf.org/external/pubs/ft/fandd/2001/06/loungani.htm>>

Last accessed on the 23rd of February 2016.

¹³⁷ For more information please refer to the following article:
Hallward-Driemeier (*Chapter 1, n21*).

3.3. The Role of International Organizations in Management of the Political Risks Associated with Foreign Investment

Since international law did not offer foreign investors proper protection mechanism in the form of pursuing claims against host states, MNCs and investors needed some sort of an assurance that the agreements they've made with the host state or any contract, in that respect, would not be subject to unilateral changes or breaches by the host state's government.¹³⁸

For that purpose, an international movement directed at the protection of foreign investors by international organizations was led by the Washington Convention. This convention that was directed at discussing the settlement of investment Disputes between States and Nationals of Other States in 1965. The said convention was the basis of the creation of a Center directed at the settlement of Investment-related disputes in 1966 named the International Center for Settlement of Investment Disputes, ICSID.¹³⁹

ICSID is an investment-related arbitration center that applies a uniform set of rules with no substantive values. It offers procedural support to tribunal and conciliation bodies. To resort to ICSID the matter should be of a legal nature arising directly out of an investment.¹⁴⁰ That said, ICSID looks into disputes arising between a host state and a private investor who is a member of a contracting state.¹⁴¹ It also looks into disputes arising between two states with respect to interpretation of a BIT between these

¹³⁸ Sauvant and Sachs (*Chapter 1, n22*) pp 111 -112.

¹³⁹ Full list of ICSID member states available in Appendix III.

¹⁴⁰ Weiler (*Chapter 3, n82*) p 61.

¹⁴¹ *Ibid* at 85-86.

states.¹⁴² In that respect, any dispute settlement center, has the right to look into and challenge any public policy regulation enacted by the host state as long as such policy has an effect on the foreign investors' property rights.¹⁴³

However, the main function behind arbitration and other forms of dispute resolution is to resolve conflict arising between host states and investors, to make sure that property rights and contractual rights are applied and enforced and to discourage, both, host states and investors from breaching any of their contractual duties.¹⁴⁴

The concept of a 'foreign investor' bringing a claim against a host state in a dispute settlement center is considered revolutionary.¹⁴⁵ Not only it is considered a safeguard for the foreign investor's right, but it is considered a disciplinary tool for wrongful actions made by the host state.¹⁴⁶

ICSID helped in resolving many disputes between host states and foreign investors. For example, it resolved the case of *Emilio Maffezini vs Spain* which discussed the matter

¹⁴² Arbitration clauses were seen as a medium of protection that investors resorted to when negotiating their investment contracts. This is, for example, the case in project finance.

See:

Dinesh D. Banani, 'International Arbitration and Project Finance in Developing Countries: Blurring the Public/Private Distinction' (2003) 26 BC Int'l & Comp. L. Rev. p 356.

¹⁴³ Sauvant and Sachs (n 20) p 230.

¹⁴⁴ Salacuse (*Chapter 1, n11*) pp 33-34.

¹⁴⁵ Sauvant and Sachs (*Chapter 1, n22*) p 131.

¹⁴⁶ *ibid* at 132.

of existence of MFN clauses.¹⁴⁷ The tribunal concluded that those are unfair to other states.¹⁴⁸

Becoming a member at ICSID is a mean to protect investors where at times taking a legal action in the country of which the investment is conducted may be bias and unfair. Investors wishing to resort to ICSID can only do so if they choose to invest in a member state at ICSID and only if they hold the nationality of a member state or if the majority shareholders of the company resorting to ICSID are held by investors of member states. This has been determined in a number of cases settled by ICSID one of which is the case of *Soufraki v U.A.E.*¹⁴⁹ In short, the case handled an investor who attempted to obtain the Italian nationality to relay on the BIT concluded between Italy and the UAE to raise a claim against the latter with respect to a breach of one of the rights granted to investors under the said BIT. The court rejected the claim and concluded that the investor could have incorporated in Italy and by doing so he would've avoided this misfortune.¹⁵⁰

It is worth noting that ICSID is not only available for investors. States can resort to ICSID and submit a claim against an MNC or an investor. This was the case of *Nicaragua v Barcelo*.¹⁵¹ This is a unique case where the sate of Nicaragua brought a claim against an investor who bought a privatized property owned by the Nicaraguan. The

¹⁴⁷ *Emilio Augustin Maffezini v the Kingdom of Spain* [2000] ICSID Case No. ARB/97/7 (25 January 2000).

The case can be found online through:

<https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC565_E n&caseId=C163>

Last accessed on the 19th of September 2013.

¹⁴⁸ *ibid.*

¹⁴⁹ *Soufraki v UAE*, Awarded, supra note 1, para 83.

¹⁵⁰ *ibid.*

¹⁵¹ De Andrade Levy, de Borja and Pucci (*Chapter 3, n48*) p 32.

Nicaraguan state, shortly after, requested that the investor returns the property due to the investor's failure to comply with the agreement. Interestingly, this case was never seen by ICSID.¹⁵²

As far as determining the validity of an investor to resort to ICSID to settle any disputes, this is possible after the application of what is known as the *Salini* Test.¹⁵³ This test was used in the *Deutsche Bank AG v Sri Lanka case*.¹⁵⁴ In this case, an agreement between the investor and the state of Sri Lanka took place. Within this agreement a state-owned corporation was to make payments to the investor who have been constantly defaulting on such obligation which resulted in the termination of the agreement and resulted in a case being brought against the state of Sri Lanka in ICSID on the basis of a breach of a BIT between Sri-Lanka and Germany. The tribunal concluded that assets and rights do not have to be connected to a physical business operation in order to be considered a protected investment.¹⁵⁵

It shall be stated that some countries did not become members at ICSID. Among those is Brazil. Brazil, who also, as noted earlier, did not put in force any of the BITs it signed, subjects any disputes arising with foreign investors to its local arbitral bodies in certain circumstances.¹⁵⁶ Investors have the freedom to choose the law and the language of which they would like to have the arbitration procedures be conducted in ex-

¹⁵² This can be found at:

Jonathan C Hamilton, Omar E Garcia-Bolivar and Hernando Otero (eds), *Latin American Investment Protections: Comparative Perspectives on Laws, Treaties, and Disputes for Investors, States and Counsel* (Martinus Nijhoff Publishers 2012) pp 421-422.

¹⁵³ Weiler (*Chapter 3, n82*) p 67.

¹⁵⁴ *Deutsche Bank AG v Sri Lanka* [2012] International Centre for Settlement of Investment Disputes, ICSID Case No ARB/09/02.

¹⁵⁵ *ibid.*

¹⁵⁶ De Andrade Levy, de Borja and Pucci (*Chapter 3, n48*) pp 6 and 66.

cept if the other party to the dispute was a state-owned company or the state of Brazil, then Portuguese is the language of the proceedings and the Brazilian law is the one applicable in the arbitral proceedings commencing in Brazil.¹⁵⁷ One of the reasons why Brazil decided not to sign on the ICSID agreement is that it would not affect investment attractiveness.¹⁵⁸

Since arbitration is perceived as a mean of protection granted to investors after they conduct their investment in the host state and in case any dispute arises, some Latin American states that refused to become members at ICSID have decided to form their own arbitral body. This was based on a proposal brought forward by Ecuador to member states of the UNSA, or the Union de Naciones Suramericanas,¹⁵⁹ which called for the creation of a new dispute settlement center would rival ICSID.¹⁶⁰ It should be stat-

¹⁵⁷ *ibid* at pp 6 and 66.

¹⁵⁸ *ibid* at 4.

¹⁵⁹ Member states of the UNSA are: Argentina, Bolivia, Brazil, Colombia, Chile, Guyana, Paraguay, Peru, Surinam, Uruguay, and Venezuela.

Some information on Chile:

Chile, according to the Global Opportunity Index on Attracting Foreign Investment ranked 20th internationally making it the top ranked Latin American State.

With Regard to Quality of Regulations, Chile came in 11th internationally making it the top state in Latin America in this category.

As for the Rule of Law, Chile was the 20th internationally and once again the first in Latin America.

Finally, as for the Ease of doing business, Mexico ranked 42nd internationally.

This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last accessed on the 1st of September 2015

As for attracting foreign investment, Chile came in 29th place internationally

The data was provided by the CIA Factbook and is available at:

<<https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last accessed on the 10th of August 2015.

¹⁶⁰ This information can be found at:

<<http://www.iisd.org/itn/2012/01/12/unasur/>>

Last accessed on the 14th of October 2014

and;

<<http://www.peruthisweek.com/news-unasur-to-discuss-creation-of-dispute-resolution-center-102553>>

Last accessed on the 14th of October 2014

and;

<<http://www.unasursg.org/inicio/organizacion/estados-miembros/>>

Last accessed on the 14th of October 2014

ed, in that respect, that 36% of disputes presented to ICSID for settlement are those against Latin American Nations.¹⁶¹

The 1950's witnessed a landmark convention sponsored by the World Bank, which led to the formation of the MIGA in 1985. MIGA, which will be further discussed in the next chapter, helps reduce risks faced by MNCs and foreign investors through insuring them against political risks especially those that the investors' home state does not cover.¹⁶² This organization belongs to another agency known for providing lending services. This agency is the World Bank.¹⁶³ It is the purpose of MIGA to promote investment in developing states through providing insurance and reinsurance services against certain types of risks. Political risk to be exact.¹⁶⁴

This risk coverage is only available to investors willing to invest in member states of the said organization and does not extend to third party nations. It does, however, offer its services to investors who do not have a local national insurance program offered by their home state.¹⁶⁵

As for the insurance and guarantee services that MIGA offers to investors and how such services differ from those offered by other agencies, this topic will be discussed in the following chapter. Add to the insurance services that MIGA offers, it differs from Ex-Im Banks and ECAs by providing mediation services to reduce the tension between

¹⁶¹ De Andrade Levy, de Borja and Pucci (*Chapter 3, n48*) p 20.

¹⁶² Bishop, Crawford and Reisman (*Chapter 3, n39*) p 6.

¹⁶³ Rubins and Kinsella (*Chapter 2, n65*) p 98.

¹⁶⁴ *ibid* at 99.

¹⁶⁵ *ibid* at 100.

investors and the host state in order to avoid any situation that could lead to claim the insurance taken against political risk.

It shall be noted that MIGA is not the only initiative taken by the World Bank to protect foreign investors. Indeed, the World Bank presented the Guidelines on Treatment of Foreign Direct Investment that is meant to protect foreign investors and set the limits and borderlines for expropriation and termination of contract.¹⁶⁶ It highlighted the importance of the application of the fair and equitable treatment of foreign nationals investing at the host state.¹⁶⁷

In 1962, the United Nations' General Assembly introduced a resolution entitled the Permanent Sovereignty Over Natural Resources or resolution 1803 (XVII) which is concerned with the promotion of economic development in developing countries. This document suggested that the host state assumes sovereignty over its natural resources and over the capital imported by the foreign investor and any earnings derived from that capital.¹⁶⁸ The sovereignty over the capital and its earnings takes place through the application of local laws as long as they do not contradict with international law. As such, nationalization was permitted only if it was for the purpose of public interest or security and only after the payment of an 'appropriate' compensation.¹⁶⁹ The concept of sovereignty of the host state and its freedom from intervention from any other state had been present earlier in 1868 in the Calvo doctrine.¹⁷⁰

¹⁶⁶ Guidelines on the treatment of Foreign Direct Investment, World Bank, IV. Available at Appendix VI.

¹⁶⁷ *ibid* at III(2).

¹⁶⁸ Permanent Sovereignty Over Natural Resources, resolution 1803 (XVII), (1962) UN, Article I(1) & (3).

¹⁶⁹ *ibid* at Article I(4).

¹⁷⁰ Dalrymple (*Chapter 3, n40p* 165).

Later, in 1974, the United Nation's General Assembly introduced a Declaration for the Establishment of a New Economic Order. This declaration which highlighted the rights of developing countries to develop their own regulations with regards to the operations of multinational corporations operating on their soil. The declaration also recommended that investors receive no discriminatory tariff preferences.¹⁷¹ It recommended the allowance of expropriation or nationalization under circumstances favorable to the home state.¹⁷² This Declaration is known as UN Resolution 3201 (S-VI).

In addition, the Charter of Economic Rights and Duties of the States, known as UN Resolution 3281 (XXIX), was introduced. This resolution granted the host state's courts the right to resolve disputes arising from the expropriation of a foreign investor's property.¹⁷³ Both resolutions have introduced the right of a host state to assume and exercise sovereignty over its natural resources.¹⁷⁴

Also in 1985, the United Nations drafted a document concerned with a specific type of foreign investments, the transfer of technology. The document, entitled the Draft of International Code of Conduct on the Transfer of Technology, in its permeable, believed that the code can help developing countries benefit from the technological advances of developed nations to improve the economical nature of the developing na-

¹⁷¹ Declaration for the Establishment of a New Economic Order, UN Resolution 3201 (S-VI), (1974), Article 4(j).

¹⁷² *ibid* at Article 4(e).

¹⁷³ See;

Charter of Economic Rights and Duties of the States, known as UN Resolution 3281 (XXIX). Article 2(2)c.

¹⁷⁴ See;

ibid at Article 2(1)

And;

Declaration for the Establishment of a New Economic Order, UN Resolution 3201 (S-VI), (1974), Article 4(e).

tions.¹⁷⁵ In chapter 2 of the draft, article 2.2 (ii) insisted that host state should adopt measures that allows it to benefit from the foreign investor's technology and at the same time protect the investor's rights.¹⁷⁶ It also insisted on the international cooperation between states in order to facilitate and promote economic growth.¹⁷⁷ The draft also encouraged host states to adapt an equitable treatment towards foreign investors.¹⁷⁸ It requested, among others, what many BIT's include, the right of foreign investors to benefit from favorable tax treatments and the right to remit their earnings.¹⁷⁹

In 1994 and after an effort lead by the World Trade Organization (WTO), member states have agreed on the application of Trade Related Measures within their local regulations.¹⁸⁰ These Trade Related Measures, known as TRIMs, are said to promote foreign investment and for that, they prohibit restrictions on foreign investors. Among these prohibited restrictions is preferring domestic firms over foreign ones and prohibiting any restrictions on foreign exchange or export.¹⁸¹

Another effort by the WTO had resulted in the agreement known as the WTO's General Agreement on Trade in Services (GATS) which prohibits any discriminatory provisions within national and regional laws that might lead to unjust treatment of foreign investors.¹⁸²

¹⁷⁵ Draft of International Code of Conduct on the Transfer of Technology, United Nations (1985), Preamble 9.

¹⁷⁶ *ibid* chapter 2.2 (ii) & (viii).

¹⁷⁷ *ibid* chapter 2.2 (iv).

¹⁷⁸ *ibid* chapter 3.1 (ii), (iii), (iv) & 3.2.

¹⁷⁹ *ibid* chapter 3.4. (a) & (d).

¹⁸⁰ Uruguay Round Agreement, Agreement on Trade-Related Investment Measures (TRIMs). Article 2(1).

¹⁸¹ This information can be found at:

<https://www.wto.org/english/tratop_e/invest_e/invest_e.htm>

Accessed on the 26th of February 2016.

¹⁸² General Agreement on Trade in Services, WTO, (1995). Part III Article XVII.

And;

Along with the GATs there is the GATT which was designed on a reciprocity basis and on a non-discriminatory

The World Trade Organization is an international organization responsible for setting up rules governing trade between nations.¹⁸³ Its goal and aim is to promote trade between member states, to lower trade barriers and to open the market for producers and consumers alike.¹⁸⁴

Mercosur is another example of the cooperation between member states of a given region to attract foreign investments and ease trade between investors belonging to these states. Argentina, Paraguay, Brazil, Uruguay and Venezuela are the current member states of this agreement which was signed in 1991. This agreement established the right of investors of signatory member states to freely transport their goods from one member state to another and encouraged the unification of the tariff system as well as the harmonization of their legislation with relation to facilitation of the concept of free movement of goods and services and the protection of their investors' rights.¹⁸⁵

measure.

See;

Trebilcock, Howse and Eliason (n 301) p 11.

¹⁸³ Found at the official WTO Website under the title 'What Is WTO?'

Retrieved from:

<http://www.wto.org/english/thewto_e/whatis_e/whatis_e.htm>

Accessed on the 25th of August 2012

¹⁸⁴ Found at the official WTO Website under the title 'The WTO In Brief'

Retrieved from:

<http://www.wto.org/english/thewto_e/whatis_e/inbrief_e/inbr00_e.htm>

Accessed on the 25th of August 2012

¹⁸⁵ Mercosur member states ranked as follows with regard to attracting FDI; In first place came Brazil ranked in the 13th place followed by Argentina in the 40th place, Venezuela in 55th 85th Uruguay in the 73rd and finally Paraguay in the 94th.

This information is found at:

< <https://www.cia.gov/library/publications/the-world-factbook/rankorder/2198rank.html#sp>>

Last Accessed on the 10th of August 2015.

Information regarding the new Mercosur related regulations is from:

Mercosur Free Trade Agreement, Articles 1,4 & 5.

Document can be found at:

<http://idatd.eclac.cl/controversias/Normativas/MERCOSUR/Ingles/Treaty_of_Asuncion.pdf>

Accessed on the 19th of September 2013.

Argentina, according to the Global Opportunity Index on Attracting Foreign Investment ranked 96th internationally while the Brazil came in 85th. Whereas Venezuela ranked 88th and Paraguay came in 94th and, finally, Uruguay came in the 69th place.

The Andean Community have taken a step similar to that of the Mercosur and NAFTA. In order to attract foreign investors to invest in Bolivia, Columbia, Ecuador and Peru, the Andean Subregional Common Market or the Andean Common Market (ANCOM), introduced a number of landmark decisions that are thought to pave the way and establish the FTZ between these member nations and adopted new regulations directed at the protection of intellectual property.¹⁸⁶ Decisions 344, 345, 351, 291 & 293 of the Andean Community dealt with intellectual property rights and with the unification of the tariff system and freedom of movement of goods as well as easing up the conditions related to foreign investments in the technology transfer sector.¹⁸⁷

In Europe, the European Union enacted a treaty known as the Treaty on Functioning of the European Union, TFEU, which stipulated the elimination of the *de minimis* rule. In other words, it presented the notion of freedom of movement of goods and citizens among member states and prohibited any type of restriction to this freedom.¹⁸⁸

Along with the TFEU, the NAFTA is perhaps one of the most comprehensive International IIAs. This trilateral investment treaty differs from the EU's agreement in speci-

With Regard to Quality of Regulations, Argentina ranked 111th internationally while the Brazil came in 79th. Whereas Venezuela ranked 130th and Paraguay came in 83rd and, finally, Uruguay came in the 20th place. As for the Rule of Law, Argentina ranked 124th internationally while the Brazil came in 94th. Whereas Venezuela ranked 135th and Paraguay came in 108th and, finally, Uruguay came in the 59th place. Finally, as for the Ease of doing business, Argentina ranked 75th internationally while the Brazil came in 102nd. Whereas Venezuela ranked 88th and Paraguay came in 79th and, finally, Uruguay came in the 21st place. This information can be found at:

<<http://www.globalopportunityindex.org/opportunity.taf?page=rankings>>

Last Accessed on the 1st of September 2015

¹⁸⁶ O'keefe (*Chapter 2, n131*) pp 819 & 821.

¹⁸⁷ *ibid.*

¹⁸⁸ The Treaty On the Functioning of The European Union, Chapter 3.

The treaty can be found at:

<<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2010:083:0047:0200:en:PDF>>

Accessed on the 19th of September 2013.

fyng certain rights, exemptions and benefits for specific investors and it has detailed the amounts and material that can be subjected to the Agreement. This can, for example, be found in the Annex of Chapter 3.¹⁸⁹ It can also be found in Chapter 7 with regard to trade in agricultural products.¹⁹⁰

The OECD Draft Convention on the Protection of Foreign Property of 1967 discussed in articles 1, 3, 4 and 5 the issues of treatment of foreign property, expropriation and the issues of remittance and transfer of capital where in article 1 it granted foreign investors fair and equitable treatment by stating:

“(a) Each Party shall at all times ensure fair and equitable treatment to the property of the nationals of the other Parties. It shall accord within its territory the most constant protection and security to such property and shall not in any way impair the management, maintenance, use, enjoyment or disposal thereof by unreasonable or discriminatory measures. The fact that certain nationals of any State are accorded treatment more favourable than that provided for in this Convention shall not be regarded as discriminatory against nationals of a Party by reason only of the fact that such treatment is not accorded to the latter.

¹⁸⁹ The Annex specifies the limits for trade in Textile and Apparel Goods and in the Automotive sector. This information is found at;

North American Free Trade Agreement, Chapter 3, Annex 300-A and Annex 300-B.

¹⁹⁰ NAFTA (*Chapter 2, n58*) Chapter 7, Article 708.

(b) The provisions of this Convention shall not affect the right of any Party to allow or prohibit the acquisition of property or the investment of capital within its territory by nationals of another Party.”¹⁹¹

While article 3 discussed the matter of expropriation and recommend such action not to be taken unless it was for the public interest and in a non-discriminatory matter after the payment of a just compensation through stating:

“No Party shall take any measures depriving, directly or indirectly, of his property a national of another Party unless the following conditions are complied with:

- i) The measures are taken in the public interest and under due process of law;
- ii) The measures are not discriminatory; and
- iii) The measures are accompanied by provision for the payment of just compensation. Such compensation shall represent the genuine value of the property affected, shall be paid without undue delay, and shall be transferable to the extent necessary to make it effective for the national entitled thereto.”¹⁹²

Article 4 recommended that no measures shall be taking against the repatriation or transfer of capital or proceeds from the host state to the home state and it stated:

“Each Party recognises, with respect to property in its territory owned by a national of another Party, the principle of the freedom of

¹⁹¹ OECD Draft Convention on the Protection of Foreign Property (1967) Article 1.

¹⁹² *ibid* Article 3.

transfer of the current income from, and proceeds upon liquidation of, such property, to such national of a Party as is entitled to them. While this Recommendation does not contain any obligation in this respect, each Party will endeavour to grant the necessary authorisations for such transfers to the country of the residence of that national and in the currency thereof.”¹⁹³

And, finally, article 5 of the Draft talked about consequences of the breach of the convention and called for the ‘Full Reparation’ through stating:

“Any breach of this Convention shall entail the obligation of the Party responsible therefore to make full reparation.”¹⁹⁴

Some of the other big movements by the World Bank was the Guidelines on the Treatment of Foreign Direct Investment of 1992 where it encouraged, like the former movements, easing up the admission of foreign capital into the host state’s market through investment of capital, technology and/or managerial skills.¹⁹⁵ It also asked for granting foreign investors a fair and equitable treatment.¹⁹⁶ As for expropriation, it stated that such act is only possible when it is done in good faith and for the public’s interest and as long as it is done in a non-discriminatory measure on basis of nationality and after the payment of an appropriate compensation.¹⁹⁷

¹⁹³ *ibid* Article 4.

¹⁹⁴ *ibid* Article 5.

¹⁹⁵ World Bank was the Guidelines on the Treatment of Foreign Direct Investment (1992) II.(2).

¹⁹⁶ *ibid*, III.(6).

¹⁹⁷ *ibid*, IV.(1).

Another example, is the agreement on Promotion, Protection and Guarantee of Investment established by member countries of the Islamic Conference which includes fifty-seven states.¹⁹⁸ Though this agreement asks for the adoption of certain incentives to attract foreign investors such as special tax, commercial and financial incentives, it does not, however allow the unconditional freedom of movement of persons between member states, unlike the EU.¹⁹⁹ It also called for allowing investors the freedom to transfer remittance, profit, proceeds or capital of their investment.²⁰⁰

Formation of regional bodies and ratification of MITs between the member states attracted investors of these states to invest within one another. These bodies also signed agreements with other regional bodies to help facilitate and increase foreign investments between their respective member states. The Lome Conventions between the African Nations and the European Community is one of the examples of the cooperation between two regional bodies. Another example is the one made between the European Union and the Pacific and Caribbean nations which includes clauses related to Fair and Equitable Treatment.²⁰¹

It can be concluded, therefore, that protection of foreign investor, starts with the host state and ends with the home state passing by MIGA.

¹⁹⁸ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 8.

¹⁹⁹ Agreement For Promotion, Protection and Guarantee of Investments Among Member States of The Organisation Of The Islamic Conference, Article 4.

This information can be found at:

< http://www.comcec.org/TR_YE/Yeni_Site_Dokumanlar/Agreements/APPGI.pdf>

Last accessed on the 19th of September 2013.

²⁰⁰ *ibid* at III.

²⁰¹ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 6.

And;

Campbell McLachlan, 'Investment Treaties and General International Law' (2008) 57 *International & Comparative Law Quarterly*, p 369.

To sum up, all national and international effort directed at the promotion and protection of foreign investors share common grounds. They are all directed at granting the foreign investor a broader scope of freedom while investing in the host state without the fear of unfair nationalization or any sort of expropriation. They have also envisaged certain situations where nationalization may take place and came to the conclusion that if an act of nationalization or expropriation is to take place, investors are entitled an adequate compensation.

Fair and equitable treatment is the basis of how a foreign investor should be treated by the host state.²⁰² It is argued that fair and equitable treatment is in fact different than granting the investor national treatment. Though both standards could be violated in the same time.²⁰³ In addition, National and international efforts had finally supported foreign investors' right to resort to international arbitration to seek fair settlement for any prospective disagreement.²⁰⁴

All of these measures would help attracting foreign investors and protecting their rights. It should also be noted that BITs, MITs, IIAs, international organizations, insurance companies and MIGA offer services that complements one another.

It could be, therefore, conclude that many international organizations helped, in a way or another, in the protection of foreign investors and host states. Through recommenda-

²⁰² This is for example, the standard required by MIGA in order for the agency to guarantee an investment. See;

MIGA Convention, Article 12(e)iv.

< https://www.miga.org/documents/miga_convention_november_2010.pdf>

Last accessed on the 26th of February 2016.

²⁰³ Roland Klager, *Fair and Equitable Treatment in International Investment Law*, (Cambridge University Press 2011) p 285.

²⁰⁴ These, as examined in this section and in the previous one, were present in international agreements.

tions emerging from international organizations like the United Nations to the creation of special bodies dealing with matters related to foreign investments like MIGA or IC-SID, these efforts have helped in minimizing some of the risks associated with foreign investments.

Thus, allowing the host states to benefit from the investors' knowledge and expertise without exploiting one another's property. These efforts, nevertheless, have not been quite sufficient in fully protecting foreign investors and MNCs against risks that they may encounter and, therefore, investors and MNCs required further protection from the host and the home states.

This protection could be a multilateral one through international agreements or it could be a unilateral one initiated by the home state, through diplomatic protection or through services it provides or delegates to ECAs, or it could also be through a host state initiative which primarily takes the form of friendly economic, financial, legal and political environments.

3.4. The Roles of Home and Host States

The cooperation between home state and host state in the protection of foreign investors extends beyond the scope of BITs. Historically, and based on the Nationality Principle present in the International Law, "Diplomatic Protection" was a mean of organi-

zation between home and host states to protect foreign investors.²⁰⁵ The home state, normally, invokes diplomatic protection in order to seek repatriation of loss suffered by its investor in the host state due to an unlawful conduct by the latter.²⁰⁶ This type of protection starts with exchanging diplomatic notes between the home state and the host state as a mean of objection over actions of expropriation of the home state's investor's property.²⁰⁷

The home state, in such objection, requests the full compensation against the property or the return of the property itself.²⁰⁸ Rules governing the application of diplomatic protection or diplomatic espousal are as follows: the home state must comply with the international rules governing nationality of claims and the use of diplomatic protection is only possible after resorting to other mediums of local remedies such as filing claims at the municipal courts of the host state. Finally, it is up to the home state's discretion to choose when and what to use as means for diplomatic protection.²⁰⁹ In that sense, diplomatic espousal is a form of host state's intervention through diplomatic remedies to protect their investors. Diplomatic protection may, also, take the form of governmental cooperation where, as a result of such cooperation, a commission is created to address the claimed actions of the host state.²¹⁰

²⁰⁵ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 3.

²⁰⁶ De Andrade Levy, De Borja and Pucci (*Chapter 3, n48*) p 73.

²⁰⁷ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 3.

And;

Garcia Amador, Sohn and Baxter (*Chapter 2, n201*) p 2.

²⁰⁸ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 3.

²⁰⁹ De Andrade Levy, De Borja and Pucci (*Chapter 3, n48*) p 74.

²¹⁰ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 3.

A good example of diplomatic protection took place in Mexico between 1838 and 1839 where French bakers living in Mexico were stripped out of their investments.²¹¹ After the Mexican government undertook this action, the French government decided to step in and protect its citizens' investments through the means of a 'diplomatic protection' which resulted in what is known today as the "Pastry War" or the Battle of Veracruz.²¹² It was also recorded that Germany, Britain and Italy, all resorted to diplomatic protection in 1902 against Venezuela.²¹³

It has been noted that the rules of diplomatic protection have been established in a number of treaties, which governed the means of seeking such protection, by investors. Notably the Pinckney Treaty (U.S.A & Spain in 1795) and the Jay Treaty (1794 U.S.A & Great Britain).²¹⁴ The Jay Treaty has, notably, witnessed the first use of special tribunals directed at resolving investment related disputes.²¹⁵

According to the International Law Commission, 'diplomatic protection' is an invocation by the home state through peaceful means of settlement of the responsibility of the host state for injuries caused by the latter towards a national of the former.²¹⁶

²¹¹ Peter Tamony, 'Sourdough and French Bread' (1973) 32 *Western Folklore*, p 265.

²¹² Ramon Beteta, 'Mexico's Foreign Relations' (1940) 208 *Annals of the American Academy of Political and Social Science*, pp 170-171.

More details on the Battle of Veracruz and the French intervention in Mexico can be found at: William Spence Robertson, 'French Intervention in Mexico in 1838' (1944) 24 *The Hispanic American Historical Review*, pp 222-252.

²¹³ Amerasinghe (*Chapter 3, n43*) p 191.

²¹⁴ De Andrade Levy, De Borja and Pucci (*Chapter 3, n48*) p 74.

²¹⁵ Dugan, Wallace, Rubins and Sabahi (*Chapter 2, n10*) p 34.

²¹⁶ International Law Commission's Articles on Diplomatic Protection, General Assembly, Sixty First Session, Supplement No. 10. UN Doc A/56/10. Article 1.

The view of diplomatic protection changed, from the time it was suggested by the jurist Emmerich Vattel in 1758, from the home state protecting its citizens through acts of force against the host state to just realizing such protection of home state's nationals through peaceful means.²¹⁷

The key in such protection is nationality of the investor which should be the same as that of the home state and, in case of a corporation, then the nationality is determined through finding out under which laws the company was incorporated.²¹⁸ Nevertheless, the condition to the application of such protection is the exhaustion of local remedies, which means that injured investors should resort to the judicial system of the host state to seek protection of their property right before seeking diplomatic protection.²¹⁹

The notion of diplomatic protection can, currently, be found at Article 1 of the Seventh Report on Diplomatic Protection published by the U.N. where this article rejects the idea of military intervention to protect nationals of the home state and insists on the adoption of diplomatic means to resolve any conflict arising from the breach of a home

²¹⁷ The Swiss jurist Emmerich Vattel explained the notion of diplomatic protection as "Whoever uses a citizen ill, indirectly offends the state, which is bound to protect this citizen."

See;

Emmirich Vattel, *Law of Nations; Principals of the Law of Nature Applied to the Conduct and Affair of Nations and Sovereigns*. (6th American ed, T. & J. W. Johnson, Law Booksellers 1844). Chapter VI, Page 161 under Use of Force.

Can be found online at:

<http://www.loc.gov/tr/frd/Military_Law/Lieber_Collection/pdf/DeVattel_LawOfNations.pdf>

Last accessed on the 26th of February 2016.

And;

John Dugard, 'Articles on Diplomatic Protection' (2006) Under 'Use of Force'

Found online at:

<<http://legal.un.org/avl/ha/adp/adp.html>>

Last accessed on the 26th of February 2016.

²¹⁸ International Law Commission's Articles on Diplomatic Protection, General Assembly, Sixty First Session, Supplement No. 10. UN Doc A/56/10. Article 9.

²¹⁹ *ibid* at Articles 14 and 15.

And;

Campbell McLachlan, 'Investment Treaties and General International Law' (2008) 57 *International & Comparative Law Quarterly*, p 366.

state citizens' rights by the host state.²²⁰ Diplomatic protection, as suggested by the UN's publication, can also be found, nowadays, under Article 20 of the TFEU and Article 46 of the European Union Charter on Fundamental Rights where EU nationals are entitled for diplomatic protection.²²¹

In 1923 the United States America and the United Mexican States established the US-Mexican General Claims Commission, which was entitled to settle disputes between host states and foreign investors regarding property rights in either Mexico or the US.²²² Such a measure may be an example of how both home and host states can coordinate with one another in order to protect their investors.

Free trade agreements, another form of IIAs that are similar bilateral or multilateral investment agreements in concept, basically, include the elimination or reduction of trade related tariffs and tax barriers between respective states. USA, for example, have conducted a number of free trade agreements with various states and trade blocs. The NAFTA, CAFTA TTIP and the TPP. The NAFAT and the CAFTA are both concerned with promoting free trade within the North and Central American regions. The TTIP, which is has not been put into force yet, is concerned with promoting investments between the U.S. and the E.U. while the TPP promotes trade between the U.S and the pa-

²²⁰ Dugard (*Chapter 3, n217*) at Chapter I A. Article 1.

Available at:

<http://legal.un.org/ilc/documentation/english/a_cn4_567.pdf>

Last Accessed on the 20th of August 2015.

²²¹ Treaty of Functioning of the European Union, Article 20(2)C.

and;

Charter of Fundamental Rights of the European Union (2000) 2012/C 326/02, Article 46.

Found at:

<<http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:12012P/TXT>>

Last Accessed on the 20th of August 2015

²²² Dalrymple (*Chapter 3, n40*) p 167.

cific region that includes Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam.²²³

Nowadays, cooperation between home and host states is highlighted within BITs signed between these countries. It may also be governed through their membership in one of the international bodies in charge of protecting foreign investors' property rights such as the MIGA. In that respect, it is useful to distinguish between *pre-investment protection* of the property rights and *post-investment protection*.

The *pre-investment protection* phase takes place before foreign investors reaches the decision to invest in a given state. In that respect, investors are encouraged to seek advice of whether their home states have any type of an investment agreement with the host state. This would help investors find out the limits of protection of their rights and the extent of which their investment may be treated as a local investment rather than a foreign one. This may include any recommendations published by the home state directed at its investors considering investing abroad and includes insurance national or regional insurance programs or those offered through commercial insurance companies.

The United Kingdom and the United States, both, present a good example of how the home state can issue recommendations to their investors. The U.K.'s government, for

²²³ Information of the TTIP can be found at:
<http://ec.europa.eu/trade/policy/in-focus/ttip/about-ttip/>

Last accessed on the 26th of February 2016

And;

Information on free trade agreements between the U.S. and other countries can be found at the following website:

<<https://ustr.gov/trade-agreements/free-trade-agreements>>

Last accessed on the 25th of August 2015

example, publishes a list of recommendations towards its investors considering investing abroad, like the one it published for U.K. investors considering investing in the Emirati market.²²⁴ Similarly, the U.S. Bureau of Economic, Energy and Business Affairs issued some guidelines and recommendation directed at informing U.S. investors considering investing in China, for example.²²⁵

The host state, on the other hand can offer pre-investment protection to foreign investors through laws and regulations it enacts to draw the lines of which foreign investors may act upon. In general, regulations and laws play a vital role in the facilitation of foreign investment. Among those local laws are international laws known as Customary International law or the Law of the Nations which is accepted rule of conduct, as it has been explained by the U.S Supreme Court, and it recognizes the existence of a minimum threshold of protection to be granted to a foreign investor.²²⁶

The lack of regulations directed at the protection of foreign investors' property is a major discouragement for foreign investors who expect to have their investments protected.²²⁷ This latter was the driver behind the creation of a unified code of protection and promotion of technology-related foreign investments in the Andean community.

²²⁴ See;

Investing in UAE (UK Recommendations):

Found online at:

<<https://www.gov.uk/government/publications/exporting-to-the-united-arab-emirates/exporting-to-the-united-arab-emirates>>

Last accessed on the 26th of February 2016.

²²⁵ See;

Investment Climate Statement in China Report: Openness to, and Restrictions upon, Foreign Investment, (Bureau of Economic, Energy and Business Affairs 2011), March 2011.

This can be found at:

<m.state.gov/md157258.htm>

Last accessed on the 8th of February 2016.

²²⁶ De Andrade Levy, de Borja and Pucci (*Chapter 3, n48*) p 61.

²²⁷ De La Medina Soto, Ghossein (*Chapter 1, n2*) p 4.

The *post-investment protection* phase takes place after the investor invests in the host state. This phase may include any steps or measures that host state has undertaken to protect foreign investors' property right in case that right was violated. In that respect, the presence of the host state in ICSID as a member may be of help to assure investors that in case their right was violated they still can resort to international arbitration to seek their right or compensation for the loss of such right.

Some states may not be member at ICSID and, instead, in their agreements with the home state or the foreign investor may decide to seek local arbitration as a mean to settle disagreements between the host state and investors. Such protection, i.e. arbitration, is normally called upon in agreements binding two or more states like the BITs for example.²²⁸

For example, NAFTA includes several procedures to settle disputes involving the application or interpretation of the agreement. As such it permits investors to take the host government directly to international arbitration for settlement of disputes involving monetary damages arising from violations of the NAFTA's investment provisions.²²⁹ NAFTA had also created a Trilateral Free Trade Commission which will regu-

Article can be found at:

<<http://iab.worldbank.org/~media/FPDKM/IAB/Documents/FDI-Starting-a-Foreign-Investment.pdf>>

Last accessed on the 18th February 2016.

²²⁸ An example of arbitration could be found in the BIT between the U.K. and Venezuela.

See;

Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Republic of Venezuela for the Promotion and Protection of Investments (1995). Article 8.

²²⁹ Found under Settlement of Disputes between a Party and an Investor of Another Party, at:

<<https://www.nafta-sec-alena.org/Home/Dispute-Settlement/Overview-of-the-Dispute-Settlement-Provisions#Chapter11>>

Last Accessed on the 20th of August 2015.

larly reviews trade relations among the three countries and discuss specific problems. The Free Trade Commission may create bilateral or trilateral panels, as appropriate, of private sector experts to hear disputes involving interpretations or application of the NAFTA. Dispute resolution will normally be completed in less than one year.²³⁰

On the other side, the Chinese government, for example, state, in some of their agreements, that their arbitral bodies have capacity to examine any dispute between the Chinese government and foreign investors. This is especially true when foreign investors forms JV with Chinese investors in China in order to minimize their risk. This form of investment, popular among foreign investors investing in China, though, to a certain extent, protects the property rights of foreign investors, it, nevertheless, makes them vulnerable in case a dispute arises between themselves and their Chinese partners where Chinese tribunals and Arbitral bodies have the priority to settle such disputes.²³¹

Another form of *post-investment protection* by the home state may take the form of export credit guarantees against a number of risks that may be uncovered by conventional insurance. Such service is granted by what is widely known as Export Credit Agencies. These agencies, as will be discussed in the next chapter, basically provide insurance services, for investors willing to invest internationally, against, mainly, political and certain economical risks that they may encounter overseas. It shall be noted,

²³⁰ Information can be found at:
<<http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/nafta-alena/celeb2.aspx?lang=eng>>
Last Accessed on the 20th of August 2015.

²³¹ The Chinese Equity Joint Ventures Law. Article 15.
The law can be found at:
<<http://www.china.org.cn/english/DAT/214773.htm>>
Last accessed on the 19th of September 2013.

nevertheless, that the protection granted through ECAs or Ex-Im Banks are not to be mixed with that of the MIGA.²³²

MIGA is a coordination between member states and, thus, considered a bilateral or multilateral movement of protection unlike that of Ex-Im Banks and ECAs that are unilateral initiatives taken by the exporting home state.

In general, the host state can encourage foreign investment by ensuring that investors' rights are all to be protected. This is possible, as mentioned earlier in the thesis, through the adoption of favorable laws and regulations that grant investors the right to resort to arbitration, whether that was national or international; the right to remit the earnings of their capital without any burdensome conditions. Through ratifying international investment protection treaties and applying them. And lastly, the host state should make it easy for the foreign investor to operate within their territories.

Foreign investors are attracted to foreign markets for many reasons. One of those is profit maximization. For that, when they decide to invest in a given state, they look for a friendly legal environment; free and unrestricted market access, fair treatment, protection against expropriation, an effective dispute settlement mechanism and compensation against the violation of their property rights.²³³

²³² A thorough analysis of the insurance and guarantee services offered by ECAs will be presented in chapters 5 and 6.

²³³ Erin Anderson, Hubert Gatignon, 'Modes of Foreign Entry: A transaction Cost Analysis and Propositions' (1986) 17 *Journal of International Business Studies*, pp 2 & 5.

And;

Buckley and Casson (*Chapter 1, n5*), p 548.

And;

Sanchez-Robles and Bengoa-Calvo (*Chapter 1, n1*) p 8.

And;

Ferrarini and Wymeersch (*Chapter 2, n177*), p 67.

The host state on the other hand seeks to attract foreign investor, mainly, to stimulate local economy since foreign investors will provide the host state with capital. They also wish to attract foreign investors to benefit from their technology and to provide the local labor with professional training and management skills.²³⁴

It shall be noted that the host state's legal system plays a major role in the attraction of foreign investment, hence, in its protection. As such, introducing laws favorable to foreign investors, granting them same rights as to those granted to the host state's investors and at the same time offer them more protection than those of the host state's investors and, finally, having a just and fair legal system will help improving the image of the host state as an investment-friendly environment.²³⁵

Since the loss of property rights is a major concern for MNCs and international investors, it may be valuable for the host state to enact a number of laws and regulations that ensures the protection of investors' rights. It is also vital to have these regulations applied in local courts in a fair and just manner and without any political or other type of interference in the court's decisions.

The importance of discussing the various types of policies enacted by host state revolves around the role that home state would have to play. For example, regulations

And;

Checklist for Foreign Direct Investment Incentives Policies, (OECD 2003) p. 7.

²³⁴ Javorcik (*Chapter 2, n90*) p 1.

And;

Rao (*Chapter 2, n90*) p 1.

²³⁵ De La Medina Soto and Ghossein, (*Chapter 1, n2*) p 4.

play a role in the promotion, attraction and protection of investment is the Mercosur Agreement. Article 5 of the Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur grants investors the right of remittance and transfer of earnings, capital, interests, dividends and other proceeds and benefits from the investment.²³⁶

With policies playing a vital role in attracting foreign capital, states have variant attitudes and adaptations to what they believe would protect their natural wealth and foreign investors. A number of host states adopted the open-door policy towards foreign investors allowing them to invest in any sector they desire.²³⁷ This approach stems from the belief that the absence of governmental intervention in the investment process will allow it to flow more efficiently.²³⁸ The approach had also been driven by the fear of application of the reciprocity concept.²³⁹ This means, if a given host state was to make it more difficult for foreigners to invest, the home state might also apply similar measures towards investors coming from the host state. This is the approach followed in the United States of America where it is believed that the open-door policy is traced to the belief in the open market system.²⁴⁰ This approach is also followed in the European Union.²⁴¹

²³⁶ Protocolo de Colonia Para la Promoción y Protección Reciproca de Inversiones en el Mercosur (1994) Article 5.

The list of proceeds in the transfer section is an exhaustive list and it includes, but not limited to, the capital, additional sums necessary for the maintenance of the investment, benefits, proceeds, interests, dividends and other benefits. (The article was translated from Spanish)

²³⁷ Mundheim and Heleniak (*Chapter 2, n145*) p 221.

²³⁸ *ibid.*

²³⁹ *ibid.*

²⁴⁰ *ibid.* at 222.

²⁴¹ As mentioned earlier in the thesis, this is present in the TFEU.

Though the U.S. enjoys an open-door policy, it nevertheless, has certain limitations to certain types of investments where it has the right to deny or regulate the establishment of foreign investments in certain sectors.²⁴² For example, foreign investments can be denied under the plea of national security. Not to mention, the restrictions imposed on foreigners who wish to invest in the maritime or defense sectors in the U.S.²⁴³

In the E.U. the open-door approach is widely applicable within member states where foreigners do not only have the freedom to invest in any sector they desire, they also benefit from the freedom of movement of goods and people between member states of the E.U. without any restriction on such movements.²⁴⁴ Add to that, investors who have presence in a member state of the E.U. can transfer goods from one member state to another without worrying about paying double tariffs.²⁴⁵ It is noted that restrictions on foreign investment in the EU have been declining.²⁴⁶

If the host state adopts the open-door policy, this would make the role played by home state agencies less vital, hence, the risk that their investors will face is going to be lower. For example, if an investor from the U.S. decides to invest in the U.K., OPIC, which is the U.S. export credit agency, as well as the investor, would not be worried about losing the value of the investment due to the intervention of the U.K. government in the devaluation of the British pound, for example.

²⁴² Mundheim and Heliak (*Chapter 2, n145*) p 225.

²⁴³ *ibid* at 228-229.

²⁴⁴ The Treaty on The Functioning of the European Union, Article 26(2).

²⁴⁵ *ibid* at Article 30.

²⁴⁶ European Competitiveness Report 2012, Chapter 4. p. 125.

The report can be found at:

<http://ec.europa.eu/enterprise/policies/industrial-competitiveness/competitiveness-analysis/european-competitiveness-report/files/ecr2012_ch4_en.pdf>

Last accessed on the 5th of January 2014.

Opposed to the open-door policy, some countries believe foreign investors should not have the right of full ownership of their investments or the freedom to choose which sectors to invest in. Countries such as China and the UAE may allow the flow of foreign investment but they will highly regulate their presence. At times, they may forbid foreigners from fully owning their property and at other times, grant them the freedom to such ownership but only in certain areas branded as special economic zones.²⁴⁷

It is worth mentioning that the Chinese authorities have improved their treatment towards foreign investors in recent years with the creation of the said economic zones and through allowing certain tax incentives to foreign investors.²⁴⁸ Ultimately, the Chinese authorities need to approve an investment before its establishment in the Chinese market.²⁴⁹ Similarly, The United Arab Emirates and Qatar requires that local investors hold the majority of shares of the investment.

Another example of limitations on inward FDI may include the United Mexican States. In Mexico, as the case is in China, prior approval from the authorities is needed before a foreign investor enters the Mexican market.²⁵⁰ In addition, foreigner investors are al-

²⁴⁷ This was examined in chapter 3.

²⁴⁸ Main Determinants and Impacts of Foreign Direct Investment on China's Economy (Directorate for Financial, Fiscal and Enterprise Affairs, Working Papers on International Investment, Number 2000/4, December 2000) p 15.

Document can be found at:

<<http://www.oecd.org/dataoecd/57/23/1922648.pdf>>

Last accessed on the 23rd of January 2014.

²⁴⁹ *Department of State: 2014 Investment Climate Statement (Executive Summary)* (US Department of State 2014) p 4.

The document can be found at:

<<https://www.google.co.uk/url?sa=t&rct=j&q=&esrc=s&source=web&cd=4&cad=rja&uact=8&ved=0ahUKEwiB3Pm35MjJAhXCWxQKHUF5A4YQFggwMAM&url=http%3A%2F%2Fwww.state.gov%2Fdocuments%2Forganization%2F228504.pdf&usq=AFQjCNHpgjT1eCUCcHFPAUUPAZmauF5zew>>

Last accessed on the 7th of December 2015.

²⁵⁰ Mexican Foreign Investment Laws and Regulations

lowed to invest in all sectors that the law does not reserve for Mexican investors only. Some sectors are completely prohibited for foreigners, while others are partially open to them where they can own minimal shares in them.²⁵¹

In such states, the role that the home state plays would be more important than that of the previous policy system. For instance, when U.S. investors decide to invest in China, U.S. investors would have a higher risk of having their property expropriated than it is the case in Spain or Italy, for instance, and therefore, the role played by OPIC would be more important in China than it is in Spain.

The notion of variation of the role played by the home state through ECAs may also apply in the case of BITs whereas if a BIT exists between home and host states, then the role played by ECAs will be relatively smaller than that played in case there were no BITs signed between the two states since the risk will be relatively smaller.

Investors contribution to the local economy plays a vital role in designing investment-related policies. The attraction of inward foreign investment through the open-door policy had proven to be of benefit where both the U.S. and the E.U. have been placed high on the list of investor friendly environments.²⁵²

The contribution on the local economy attracting inward FDI goes hand in hand with the contribution of outward FDI. In that previous scenario, the state which was hosting

The law can be found at:
<<http://www.mexicolaw.com/LawInfo26.htm>>
Last accessed on the 9th of January 2014

²⁵¹ For more information refer to Mexican Foreign Investment Laws and Regulations.

²⁵² As examined in chapter 2.

the foreign investment, labeled as the host state, becomes now the home state of the outward foreign investor.

Since outward foreign investors are interested in capitalizing their profits through exploring new markets, they have been experiencing difficulties in certain countries from destruction of their property due to the constant loss of value of the local currency of the host state. For that, the private sector offered certain types of services covering a range of investment-associated risks, these services will be discussed in chapter 4.

Unfortunately, investors still experienced a number of risks and this led to the creation of MIGA. Despite the services offered by MIGA, which also will be discussed in chapter 5, investors have not been covered against more specific risks.

That led exporting nations to create organization that would cover against those risks that both international organizations resulting from multilateral investment treaties and the private sector failed to cover. These organizations labeled ECAs offer a range of products and services like investment credit and risk coverage.²⁵³

In general, a state wishing to attract foreign capital to invest in its territories, needs to apply: a fair and stable treatment, an appropriate financial system and exchange rate policies, liberal trade policies, reasonable taxation levels, protection against competition as well as adopting favorable economic condition and the adopting of micro eco-

²⁵³ The list of products and services and the nature of governance of ECAs will be discussed in detail in Chapters 4 and 5.

conomic policies.²⁵⁴ It shall be noted, however, that the minimum protection granted to a foreign investor should not be at a level lower than that recognized in international law which, sometimes, grants the foreign investors more protection than local investors of the host state.²⁵⁵

Both home and host states find it of their interest to protect investors in general since they help in building the economy. Nevertheless, investors who wish to invest abroad may be subject to many risks of which they need to be familiar with. For that, the role of the home state emerges as a guardian of its citizens advising them about what to look for in a host state before undergoing any investments. This guardian may also offer services, which cover investors against certain risks they may encounter.

The host state, on the other hand, is expected to treat foreign investors with care as if they were its own national investors. It is supposed to protect them and pave the way for them for less trade barriers that would help them undergo their investments. This may be done through ratification of international decisions, having a solid and fair legal system that is trusted internationally and, lastly, being a member of international investment agreements with other states.

Another mean of attracting and facilitating foreign investments that a number of states have followed was the establishment of investment promotion authorities. Host states established Foreign Investment Authorities to promote host states as a friendly-foreign investment environment. These are a marketing tool to promote and attract foreign in-

²⁵⁴ De Andrade Levy, de Borja and (*Chapter 3, n48*) pp 8-10.

²⁵⁵ *ibid* at 64

vestors to the host state. They are primarily designed for oversee foreign investors' operations within the host state. They, also, act as advocates for foreign investors' rights in order to improve the investment climate within the state and make it friendlier to foreign investors. This kind of promotion tool is present in developing and developed states alike. For example, in Saudi Arabia there is the Saudi Arabian General Investment Authority (SAGIA) and in the United States, autonomous states have their own investment authorities where in New York the Empire State Development, a governmental agency, is in charge of promoting foreign investment in the state of New York and to encourage New York based companies export their goods and services in order to stimulate the local economy.²⁵⁶ In the state of California, The Governor's Office of Business and Economic Development (GO-Biz) is the one in charge of promoting foreign investment and aiding local investments as well.²⁵⁷ While in Spain, on the other hand, the Invest in Spain which, is part of the ICEX-España Exportación e Inversiones, is in charge of promoting Spain as a foreign investor friendly hub along with other investment promotion authorities for the autonomous regions of the country like Invest in Madrid for example.²⁵⁸

²⁵⁶ For more information on these authorities please visit the following links:

1- For the Saudi Arabian General Investment Authority:

<<https://www.sagia.gov.sa>>

Last accessed on the 25th of August 2015

2- For Empire State Development (State of New York):

<<http://esd.ny.gov/International/InvestNY.html>>

Last accessed on the 25th of August 2015

²⁵⁷ For more information on GO-Biz please visit the following links:

Governor's Office of Business and Economic Development (State of California)

<<http://business.ca.gov/RelocateExpand/ForeignInvestment.aspx>>

Last accessed on the 25th of August 2015

²⁵⁸ For more information on these authorities please visit the following links:

1- For Invest in Spain:

<<http://www.investinspain.org>>

Last accessed on 25th August 2015

2- For Invest in Madrid:

<<http://www.investinmadrid.com>>

Last accessed on 25th August 2015

As mentioned, the host state may decide to form a body which it sponsors in order to promote foreign investment in its territories, like the Saudi Arabian General Investment Authority (SAIGA). Such a movement is considered a self-managed marketing strategy designed and managed by the host state. Another marketing strategy that the host state may follow is delegating the management of investment promotion activities to the private sector like it is the case in the City of London where London & Partners is the company in charge of promoting investments in London.²⁵⁹

Another example for the coordination between the home and host states in the promotion and protection of foreign investment may include what is known as a Joint Economic Commission. For example, the Republic of Ireland and in an attempt, encourage its investors to invest in countries like Saudi Arabia, Korea, China and Russia, created what is known as the Joint Economic Commission. Such commission, through its meetings, aims at increasing Irish investments in these states.²⁶⁰

A similar mean of coordination can be found in Joint Chambers of Commerce that encourage investment in respective member states. For example, in the United Kingdom, there is the Arab British Chamber of Commerce which aims at promoting and facilitating investment flow in Arab states and in the U.K. For example, the Chamber helps in acquiring the needed visas and in aiding British exporters, for example, in meeting the

²⁵⁹ For more information on London & Partners please visit:

<<http://www.londonandpartners.com/about-us/>>

Last accessed on the 5th of March 2016.

²⁶⁰ This information can be found at:

<<https://www.dfa.ie/our-role-policies/trade-and-promotion/our-trade-role/>>

Last accessed on the 20th of September 2015

qualifications for exporting goods to Arab states.²⁶¹ This can be considered as a joint movement between the member states and, hence, a multilateral movement.

Similarly, there could be a unilateral movement taken by the prospective host state in establishing a body in the targeted home state in order to encourage the inflow of investment to its territories from the home state. In that sense, such bodies may play a role in commercial and economic relations between both home and host states and to aid in developing and promoting investment in these states.

It shall be noted though, that these bodies may not necessarily be the result of a governmental action. They could be, as well a result of cooperation of investors from the home and host states. This is for example the case in the Spanish Chamber of Commerce in Great Britain.²⁶²

Based on the previous findings, it can be safely concluded that if the host state is able to grant foreign investors a proper protection scheme within its laws and regulations and encourage them to invest while granting them proper and adequate protection of all their rights with no restrictions, then the role played by the home state will be reduced, if not eliminated, once the protection granted in the host state to foreign investors and MNC reaches a high level. In that respect, the protection granted to investors by their home state changes depending on the amount of protection granted to investors in the

²⁶¹ This information can be found at:
<http://www.abcc.org.uk/ABCC_Services>
Last accessed on the 25th of August 2015

²⁶² This information can be found at:
<<http://www.spanishchamber.co.uk/about-us>>
Last accessed on the 25th of August 2015.

host state. If there were high levels of protection in the host state, then the home state would not have to introduce a complex form of protection and vice versa.

3.5. Conclusion

Developing countries are attractive to foreign investors. These countries normally suffer from absence of fair laws and regulations, political and economic instability as well as unjust nationalization of the foreign investor's properties. In the absence of any means of protection to foreign investors those latter are at huge risk of losing their investments.

Changes in the political regimes and the fear of expropriation of foreign-owned property are what many developing countries suffer from. This is, for example, the case in Uganda between 1971 and 1979 when a shift in the political regime happened. Idi Amin, the new president of Uganda then, expelled British and Asian nationals and expropriated their properties and investments.²⁶³

Property rights of foreign investors and stability of the political and legal systems are some of the driving forces of the attraction of foreign capital. A similar situation to that of Uganda appeared in one of Latin America's major oil producers, Venezuela. After the inauguration of Hugo Chavez as the new president of the country he began a

²⁶³ University of Pennsylvania, African Studies Center.
This information can be found at:
<<http://www.africa.upenn.edu/NEH/ueconomy.htm>>
Last accessed on the 30th of August 2013.

movement of expropriation and naturalization of investments related to oil extraction and production.²⁶⁴

Political risk and economic instability are some of the main reasons behind the disappearance of existing capital from developing countries. In recent years, some of the Middle Eastern nations have been experiencing major political instability accompanied with economical turbulences. This is the case of Lebanon in recent years, which have been suffering from the flight of foreign capital that previously had been placed in the form of investments in different sectors, especially the hospitality sector.²⁶⁵

While investing abroad, foreign investors look for a friendly legal environment; infrastructure, strong economy, political and economic stability.²⁶⁶ They also look for dispute resolution mechanism as well as an unrestricted admission to the local markets of the host state, fair treatment, protection against expropriation and compensation against the violation of their property rights. On the other hand, the host state on the other hand seeks to attract foreign investor, mainly, to stimulate local economy since the foreign investor will provide the host state with capital. They also wish to attract the foreign investor to benefit from the technology that the investor possesses and to provide the local labor with professional training and management skills.²⁶⁷

²⁶⁴ Expropriations in Venezuela: Full Speed Ahead, The Economist Online (Oct 29th, 2010).

<http://www.economist.com/blogs/americasview/2010/10/expropriations_venezuela>

Last accessed on the 26th of February 2016.

²⁶⁵ MIDEAST MONEY-Politics, policy dismay Gulf investors in Lebanon (Wed Jul 11, 2012)

Article can be found at:

<<http://www.reuters.com/article/lebanon-economy-politics-idUSL6E8HQ7H520120711>>

Last accessed on the 26th of February 2016

²⁶⁶ Mangus Blomstorm, 'The Economies of international Investment incentives', (2002) OECD International Investment Prospective, pp 168-170.

And;

Checklist for Foreign Direct Investment Incentives Policies, (OECD 2003) p. 7.

²⁶⁷ As it was examined earlier in this chapter and in chapter 2.

Host states need to ensure the proper protection of foreign capital. In that sense, the host state can improve its laws and regulation on the treatment of foreign capital. They can grant the foreign investor a national and favorable treatment and grant him the right to remit their earnings and capital freely without imposing many restrictions. All of this should be done while taking international law into consideration.

Host state may become a member of ICSID which will give assurance to the foreign investor that their rights, should they be subject to expropriation, creeping expropriation, limitation on practicing their rights or any other infringements of their rights, are protected and that they have an independent trusted party to settle any disputes related to such matters.

Host states can also improve their legal system and adopt favorable laws and regulations towards foreign investors as well as ensuring their courts of law apply the laws in a fair and just manner with conformity with international law and without any discrimination between foreign or national investors as well as without any interference, whatsoever, in the court's decisions from any political or independent parties. ICSID looks at disputes arising between two member states on the interpretation of a BIT or between a contracting state and an investor.²⁶⁸

²⁶⁸ Convention on the Settlement of Investment Disputes between States and Nationals of Other States (1965) Articles 36 and 64. According to the Washington Convention of 1965, those seeking ICSID's arbitration should be bound by Article 36. Article 64 talks about disputes arising between two contracting states and it limits their ability to seek arbitration through ICSID to having the dispute on the interpretation of a BIT.

In general, Investors are expected to be knowledgeable about the legal procedures accompanying the establishment of a new investment in the host state. In that respect, transparency by the host state may be helpful. Such transparency is said to be present in one of the IIAs instruments, which is the BIT.

Some states may enjoy an open policy towards foreign investors and in this case, they are welcoming to foreign investors and impose minimal restrictions on the entry into the local market or it may follow the closed-door policy towards investors and in this case, impose a number of restrictions on the entry of foreign capital and on the exiting of foreign capital as well.²⁶⁹

Table B, at the end of this chapter, elaborates on the role of IIAs and shows the number of BITs and other IIA instruments signed by a number and shows whether these states are member of some of international organizations established for the purpose of facilitating and protecting investments or not.

Home states are expected to advice their investors about certain aspects they need to look for while investing abroad. Home states can recommend to their investors not to invest in a certain territory or visa-versa. It can also set the guidelines on choosing the country of which investors can invest in or the means of how to protect their property and limit his risks. Home states will also recommend to their investors, while going overseas, to seek for the presence of BITs between home and host states or the presence of positive and fair protection of property rights are some of these aspects. BITs

²⁶⁹ As it was examined earlier in this chapter and in chapter 2.

are considered a form of cooperation and coordination between home and host states dedicated at facilitating and protecting investors. This is especially true since BITs facilitate economic development and cooperation between a state with an advanced economy with another state enjoying skilled labor and rich in natural resources. These BITs share a common structure where they include MFN clause, an Umbrella Clause, Clauses governing Expropriation and a clause governing Dispute Settlement.

Another form of BITs involves more than two states. These are known as MITs. The NAFTA, Mercosur, ANCOM and the EU are some of the examples of MITs that help foreign investors, in most cases depending on the agreements, to move freely between member states and grants them special tax exemptions.

Home states can also present their investors with protection against a number of risks they may encounter in the host state in the form of export credit insurance through ECAs or through regional multilateral agencies. Such multilateral movements result in the creation of certain international bodies like the Multilateral Investment Guaranty Agency (MIGA) which was established with the goal of minimization of foreign investment associated risks through insuring against risks not covered by national insurance programs offered by the home state.²⁷⁰

MIGA was not able to cover against risks not falling under the definition of political risk, private insurance companies began to offer their services on the basis of division of types of risks and relating these risks to the investment directly rather than to the

²⁷⁰ Rubins and Kinsella (*Chapter 2, n65*) p 99.

host state's situation, as it is the case with MIGA.²⁷¹ Though this division of risks made by the private sector may be labeled differently, it, nevertheless, have some similarities in the services with those offered by MIGA, as will be shown in the next chapter of this thesis. The differences in this case will be in the terms that the services are based on.

Due to the inability of both, private sector and international organization at one end and the BITs and investment agreements and policies at another end, investors were still uncomfortable in investing in certain nations.

MNCs and investors were afraid they would not get compensated for any loss of property they may encounter due to political, commercial or financial risks that the host state may suffer from. For that, home states decided to take action and create organizations that may be operated by, either, the government, or by the private sector, which offers protection against the risks that neither insurance companies nor policies and international agreements were able to cover.²⁷²

²⁷¹ This will be elaborated in Chapter 4.

²⁷² This will be elaborated in Chapter 4.

Country	Number of BITs Signed	Other Trade Agreements Signed	MIGA	OECD	OECD ECG	Paris Club	TRIMS	TRIPS	GATT
Argentina	58	15	Yes	No	No	No	Yes	Yes	Yes
Brazil	14	19	Yes	No	No	No	Yes	Yes	Yes
Canada	40	18	Yes	Yes	No	Yes	Yes	Yes	Yes
France	103	67	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Germany	134	67	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Italy	106	67	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Spain	82	67	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Switzerland	118	31	Yes	Yes	Yes	Yes	Yes	Yes	Yes
United Kingdom	104	67	Yes	Yes	Yes	Yes	Yes	Yes	Yes
United States of America	48	64	Yes	Yes	No	Yes	Yes	Yes	Yes

Table B (Membership at International Organizations a IIAs Signed)

Chapter Four: ECAs and Other FDI Protection Schemes

Investors are always seeking friendly investment environments and that is why it is in the interest of the home state to provide such an environment to foreign investors, since attracting them will stimulate its economy. At times, the host state may undertake certain measures that restrict investors from benefiting from their property rights in part or in full. This was, for example, the case in Venezuela where the Venezuelan government expropriated a number of foreign investors and multinationals, including Exxon's.¹ For that, many unilateral movements, like recommendations published by the home state, diplomatic protection and multilateral initiatives, like IIAs and ICSID to name a few, took place in order to help investors hedge these risks and ensure that investors will have their property rights adequately protected. Though such initiatives were effective in reducing the risks associated with foreign investments, they were still, however, not enough to restore investors' confidence in certain host states.

For that, the need for an extra layer of protection for investors was needed and private sector insurance companies started providing political risk insurance. Companies like the American International Group (AIG) from the United States and Lloyds of London from the United Kingdom, which are part of the Big Five, have been offering political risk

¹ Chris Hajzler, 'Expropriation of Foreign Direct Investments: Sectorial Patterns from 1993 to 2006', (September 2010) University of Otago Discussion Paper No. 1011, p 19.
Available at:
<https://ourarchive.otago.ac.nz/bitstream/handle/10523/1076/DP_1011.pdf>
Last accessed on the 30th of November 2016.

insurance for investors.² Although due to the failure to offer a comprehensive coverage against investment risks, Export Credit Agencies were created to offer insurance and credit support. As such, these agencies were established to fill in the gap existing from the lack of coverage of specific risks by the private sector.³ That said, and according to a study published by the OECD in 2008, the value of investment guarantees reached an average of 3% of the total FDI flow.⁴

Along with ECAs and insurance companies lies another insurance provider that was established through a multilateral initiative rather than a unilateral one known as Multilateral Investment Guarantee Agency (MIGA). These new forms of protection will be discussed throughout this chapter.

Since ECAs are considered to be one of the methods of promotion of international trade and foreign investment, an analysis of the services offered by ECAs will be present and a comparison between the services offered by these agencies and those offered by the MIGA and the private sector will be present.

Generally speaking, insurance is a contract where the insurer, in this case MIGA, ECA or the commercial insurance company, agrees to compensate the investor, who is the insured party, for specific losses that both parties agreed on in exchange of a paid premium that the insured

² Bishop, Crawford and Reisman (n 330) p 616.

³ Jian-Ye Wang, Yo Kikuchi, Siddhartha Choudhury, Mario Mansilla, *Officially Supported Export Credits in a Changing World* (International Monetary Fund 2005) p 25.

⁴ Gordon (*Chapter 1, n32*) p 92

pays.⁵ This contract includes a subrogation clause which would entail the substitution of investor by the insurer in insurance-related claims.

It is worth noting that, ECAs, Ex-Im Banks, and the MIGA, mainly, cover against political risks. The difference lies in the acts constituting a political risk where MIGA's coverage is broader than that of ECAs and Ex-Im banks. MIGA and some ECAs, Ex-Im banks and private insurance companies provide coverage against certain types of commercial risks. Although the PRI coverage varies from one agency to another and depends on the host state.⁶

Ex-Im banks are similar to ECAs. The only difference between the two is that Ex-Im banks provide import guarantee and insurance services in addition to export credit guarantee, unlike ECAs.

As it will be explained in this chapter, capital exporting countries, and in an attempt to stimulate their economy through encouraging exporting of goods and services, developed insurance programs offered by governmental agencies directed at helping investors willing to invest abroad counter a number of investment-related risks.⁷ These agencies are organizations providing export credit guarantee, export credit insurance and other forms of support to investors and exporters on behalf of the home state.⁸ It shall be not-

⁵ Salacuse (*Chapter 1, n11*) p 246.

⁶ Available at:

<<https://www.miga.org/Pages/Resources/AboutPoliticalRiskInsurance.aspx>>

Last accessed on the 2nd of January 2017.

⁷ *ibid* p 247.

⁸ Carole Murray, David Holloway and Daren Timson-Hunt, *Schmitthoff: The Law and Practice of International Trade* (12th edn, Sweet and Maxwell 2012) p 453.

ed, however, that the thesis focuses only on the insurances services offered by these agencies.

This chapter will discuss the various organizations involved in the protection of foreign investors and will also look into the various ownership structures of ECAs and will present examples of each ownership structure of these ECAs. In addition, it will discuss some of the new emerging private companies and some of the big five companies to elaborate on the public-sectors roles. The thesis will discuss the ownership structure of these agencies and their governance in order to emphasize on the fact that though they may be governed differently from one another, they do still offer similar products and similar services that help in facilitating and protecting foreign investments. It will also include, at the end, a series of tables to compare, briefly the services offered by each of the selected agencies presented in the thesis.⁹ It will, also, include a table that is directed at showing the ownership structure of each one of the selected agencies.

4.1. Commercial Insurance and its Role in the Protection Against Various Investment-Related Risks.

In general, there have been five major players in the private sector in the protection of investors against political risks. Among those are the American International Group (AIG) from the United States and Lloyds of London from the United Kingdom.¹⁰ Though more companies in the private sector are emerging and offering similar services,

⁹ This will be elaborated in Table D at p 280.

¹⁰ Bishop, Crawford and Reisman (*Chapter 3, n39*) p 616.

such as Citicorp International Trade Indemnity (CITI), Professional Indemnity Association (PIA), Pan Financial and Pool d'Assurance des Risques Internationaux et Speciaux (P.A.R.I.S.) to name a few, these services are still, nevertheless, not the same as those offered by these five companies or by the public sector.

Companies like Lloyd's of London, AIG and Zurich offer insurance and guarantee services against a number of political risks.¹¹ Notably, Lloyd's of London, which is considered as an insurance market rather than an insurance company, was able to offer insurance and guarantee products against, as it will be further elaborated in this chapter, political risk including wars and civil unrest and against currency exchange risks, as well as, against defaults on contracts and against embargo on export and import.¹² These cover almost all types of the major risks. It covers the pure political risk, the political financial risk, political commercial risk and commercial risk.

Some insurance companies, on the other hand, have decided to handle commercial risk only. This is primary due to the fact that covering against political risk incurs high transaction costs or service.¹³

Nevertheless, as mentioned earlier, the private sector is catching on with some companies trying to have a bigger role in the protection against political-related-risks through offering PRI and other export credit services these private sector companies emerging into the field include, along with Lloyd's of London, AIG and Zurich, Citicorp Interna-

¹¹ Orellana (*Chapter 1, n32*)

¹² More information about Lloyd's can be found at:
<<https://www.lloyds.com/lloyds/about-us/what-is-lloyds>>
Last accessed on the 26th of February 2016

¹³ Gordon (*Chapter 1, n32*) p 104.

tional Trade Indemnity (CITI), Professional Indemnity Association (PIA), Pan Financial and Pool d'Assurance des Risques Internationaux et Speciaux (P.A.R.I.S.).¹⁴ These companies are considered to be among the major providers of export credit guarantee and political risk insurance providers in the private sector.

When it comes to risk assessment, each insurance provider has its own way to assess risks. For example, some may rely on commercial ratings of risks while others may resort to an in-house risk evaluation. This is for example the case with COFACE.¹⁵

Both national and private insurance programs complement one another. This true especially since national agencies step in to offer their services to investors whenever commercial insurance providers fail to provide similar program. In that respect, COFACE for example is considered an insurer of the last resort where an investor may resort to COFACE's insurance only if the investor was not able to find coverage against such risk through other insurance programs.¹⁶

¹⁴ More information about these companies can be found on the following links:

1- For AIG Insurance:

< <https://www.aig.co.uk/about-aig>>

Last accessed on the 5th of March 2016.

2- For Zurich Insurance Group:

< <https://www.zurich.co.uk/en/about-us>>

Last Accessed on the 5th of March 2016

¹⁵ Gordon (n 29) p 100.

¹⁶ Based on an interview with Mr. Christophe Viprey, Director of Public Guarantees of the Compagnie Francaise d'Assurance pour le Commerce Exterior (COFACE) on the 18th of May 2015.

4.2. Export Credit Agencies, their Services, Ownership Structure and Governance

The need to encourage and support exports, protect investors and to reduce foreign investment-related risks were some of the reasons behind the formation of ECAs.¹⁷ They have been, primarily, created to give exporters the confidence to export goods or services and to protect these exporters against any losses.¹⁸ Governments created these agencies for the purpose of enhancing the economy, reducing unemployment, to fill in the gap present in the market and to promote the welfare of the host state, as is the case with the U.S. ECA the Overseas Private Investment Corporation (OPIC).¹⁹ They provide state-backed coverage against certain cross-border investment-related risks. They are considered the largest source of public financial support for foreign investors.²⁰

There is no typical structure of ECAs where they could be government-operated agencies or privately held ones. They may be ones that are owned jointly by the private and public sectors and may also be a private sector agency delegated by the government to offer services reserved to ECAs.

¹⁷ Stephens (*Chapter 1, n9*) p. 1.

And;

Christoph Moser, Thorsten Nestmann and Michael Wedow, 'Political Risk and Export Promotion: Evidence From Germany' (2008) 31 *The World Economy*, p. Abstract.

The article can be found at:

<<http://onlinelibrary.wiley.com/doi/10.1111/j.1467-9701.2008.01102.x/full>>

Last accessed on the 19th of November 2013

¹⁸ Stephens (n 27) p 13.

¹⁹ See:

Stephens (*Chapter 1, n9*) p 1 & 2.

And;

Gordon (*Chapter 1, n32*) p103.

²⁰ Marcos A. Orellana, (*Chapter 1, n32*)

4.2.1. History of Export Credit Agencies

ECAs are defined as public agencies that provide guarantees, insurance or loans backed by the home state's government to investors willing to invest in or export to a developing host state.²¹

Contrary to what is believed, the first ECA was a private entity in Switzerland established in 1906.²² The Export Credit Guarantees Department of the UK (ECGD), now known as the UK Export Finance (UKEF) was the first governmental ECA established in 1919.²³ It shall be stated that though the export credit guarantee services of Switzerland started out with the private sector, however, it is, currently delegated by the Federal Government of Switzerland to Schweizerische Exportrisikoversicherung (SERV).²⁴

These reasons behind the creation of ECAs are normally mentioned in the mission statement of these agencies. For example, some agencies have been established for the purpose of promotion and development of the economic status of the host state while others were established to realize diplomatic objectives of the home state as is the case with the Belgian ECA Delcredere | Ducroire.²⁵

²¹ Jason Chuah, 'Export Credit and Credit Guarantee Institutions - Balancing Values in the Regulatory Environment' (Social Science Research Network 2010) p 155.

Article can be found at:

<<http://papers.ssrn.com/abstract=1702287>>

Last accessed on the 19th of November 2013.

²² Delio E Gianturco, *Export Credit Agencies: The Unsung Giants of International Trade and Finance* (Greenwood Publishing Group 2001) p 70.

²³ This point of view was adopted by Malcolm Stephens:

See:

Stephens (*Chapter 1, n9*) p 1.

²⁴ More information about SERV can be found at:

<<http://www.serv-ch.com/en/organisation/about-serv/>>

Last accessed on the 6th of March 2016.

²⁵ For more information please refer to:

Gordon, (*Chapter 1, n32*) p 96.

In 1934 a union was formed between international credit and investment insurers known as the International Union of Credit and Investment Insurers or the Bern Union.²⁶ This union promotes the exchange of information on investment insurance and on export credits.²⁷ This union was formed by publicly and privately held ECAs.²⁸ Its four founding members are Spain, Italy, the United Kingdom and France.²⁹ This Union is aimed at facilitating cross-border trade and to provide exchanges among the Union's members.³⁰ The list of members of this union includes, majorly, all official public sector ECAs as well as some agencies belonging to the private sector.³¹ Along with the Berne Union there is also the Prague Club, Paris Club (PC)³² and the OECD Export Credit Group (ECG). The Prague Club is an information exchange network for new Export Credit Agencies and has 37 member agencies.³³ The Paris Club, on the other hand, is a group of official creditors who aim to coordinate and find sustainable solutions to the payment difficulties experienced by countries in debt.³⁴ PC works with IMF and the World Bank (WB) to help states in the repayment of their debt obligations including those to ECAs.

²⁶ Information on the date of forming the Berne Union can be found at:

<<http://www.berneunion.org/about-the-berne-union/>>

Last accessed on the 7th of December 2015.

²⁷ Yescombe (*Chapter 2, n184*) p 446.

²⁸ Chauffour and Malouche (n 26) p 338.

And;

Chuah (*Chapter 4, n21*) p163.

And;

'About the Berne Union' (*Berne Union Official Website*)

<<http://www.berneunion.org/about-the-berne-union/our-principles/>>

Last Accessed on the 19th of November 2013.

²⁹ Stephens (*Chapter 1, n9*) p 115.

³⁰ More information can be found at the Berne Union Official Website:

<<http://www.berneunion.org/about-the-berne-union/our-principles/>>

Last accessed on the 19th of November 2013

³¹ List of Members of the Berne Union can be found at Appendix I.

³² Chuah (*Chapter 4, n21*) p160.

³³ More Information on the Prague Club can be found at:

<<http://www.berneunion.org/berne-union-prague-club/prague-club-members/>>

Last accessed on the 28th of May 2015

³⁴ More information on the Paris Club can be found at:

<<http://www.clubdeparis.org/en/>>

Last accessed on the 28th of May 2015

On the other hand, ECG's members are those of EU OECD member states and these members presented guidelines to promote sustainable lending practices and they are working on development of anti-bribery measures.³⁵

Table C at the end of this chapter lists a number of ECAs and Insurance Companies as well as MIGA and their membership status in the Berne Union and the Prague Club.³⁶

On the other hand, the products and services offered by ECAs are governed by the Arrangement on Guidelines for Officially Supported Export Credits of the OECD. This arrangement which is also known as the OECD Consensus of 1978, ensures the operation of an orderly export credit market and attempts to limit competition on offering favorable financing terms for exporters but allows competition between countries on the basis of the amount of credit support made available.³⁷ The arrangement, which is considered as a 'gentleman's agreement' since it is a set of recommendations rather than a set of rules that participants are bound to apply, has undergone a number of improvements with the introduction of the Helsinki Package in 1991, the Schaerer Package in

³⁵ For more information see;
ECG Sustainable Lending:
OECD countries agree sustainable lending principles for official export credits
<<http://www.oecd.org/general/oecdcountriesagreesustainablelendingprinciplesforofficialexportcredits.htm>>
Last accessed on the 26th of February 2016.

And;
Anti-Bribery Measures and Export Credits (ECG)
<<http://www.oecd.org/tad/xcred/anti-bribery-measures.htm>>
Last accessed on the 26th of February 2016.

And;
For Paris Club:
Paris Club:
Under: About.
<<http://www.clubdeparis.org/en/>>
Last accessed on the 26th of February 2016.

³⁶ Table C at p 279

³⁷ Yescombe (*Chapter 1, n18*) p 448.

1994 and finally the Knaepen Package in 1997.³⁸ This ‘soft law’ instrument was subsequently followed by other OECD movements with the most recent being in 2016.³⁹

It shall be noted that there may be more than one export credit support provider in the same country. Some may be public sector agencies while others may be private sector. For example, in France COFACE, as will be elaborated more throughout this research, was a government export credit provider until it was privatized. This company is not the only company providing export credit support in France since the Société de Promotion et de Participation pour la Coopération Economique (Proparco) provides export credit support but, unlike COFACE, it does not offer any insurance or guarantees against investment-risks.⁴⁰

In General, export credit refers to the agreement where someone in a given state is allowed to differ payments for the goods or services that were purchased from another person in different state for a specific period of time.⁴¹ It is, therefore an insurance, guarantee or even financing arrangement.⁴² Export credit financing, along with PRI, is of-

³⁸ More information on the Helsinki Package of 1991 and the Schaerer Package of 1994, can be found at:

Export Credit Financing System in OECD Member Countries and Non-Member Economies, OECD (2001).

³⁹ OECD, The Export Credit Arrangement 1978/2008: Achievements and Challenges-Continued! (Organisation for Economic Co-operation and Development 2008) p 5.

Document can be found at the OECD official website.

PDF Hyperlink:

<<http://www.oecd.org/tad/xcred/40594872.pdf>>

Last accessed on the 19th of December 2013

And;

Arrangement on Guidelines for Officially Supported Export Credits (OECD 2016).

⁴⁰ Full list of the services offered by Proparco can be found at:

<http://www.proparco.fr/lang/en/Accueil_PROPARGO/produits-services>

Last accessed at the 19th of May 2015.

⁴¹ Murray, Holloway and Timson-Hunt (n 572) p 44.

⁴² Information can be found at the OECD official website

See:

<<http://www.oecd.org/trade/exportcredits.htm>>

Last accessed on the 12th of June 2016.

ferred through export agencies delegated by the home state's government.⁴³ In that sense, these agencies are thought to be acting on behalf of the home state to influence and promote investment in the host state.⁴⁴ The home state may delegate one agency to offer support for investors and exporters or it may delegate more than one. For example, the federal government of Germany has delegated Euler Hermes Deutschland AG and PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft(PwC) to offer federal export credit guarantees, referred to as the Hermes Cover.⁴⁵

Moreover, some ECAs may attempt to use diplomatic means through home state's government to avoid potential problems just before they become major and have a higher threat rate.⁴⁶ This is true since ECAs have access to the home state's diplomatic resources to avoid any potential dispute. For example, OPIC negotiate government-to-government agreements with each country it operates in and obtains special arrangements to recover salvage.⁴⁷

Along with ECAs there is another agency that provides its services to importers and exporters alike. The services provided by this agency are pretty much similar to those of ECAs save the fact that it offers its services to importers and exporters alike. This agency is known as Export Import Banks or Ex-Im Bank for short. Ex-Im Banks offer export credit insurance and import credit guarantees. This is the only difference between these

⁴³ Delio E Gianturco, *Export Credit Agencies: The Unsung Giants of International Trade and Finance* (Greenwood Publishing Group 2001) p 17.

⁴⁴ Gordon (*Chapter 1, n32*) p 101.

⁴⁵ Information can be found at:

<<http://www.agaportal.de/en/aga/index.html>>

Last accessed on the 29th of February 2016.

This will be further elaborated in this chapters.

⁴⁶ Gordon (*Chapter 1, n32*) at 102

⁴⁷ Gordon (*Chapter 1, n32*) at 105

two agencies and as such both are basically different faces of the same coin. For that, there is no value at differentiating, in this research, between Ex-Im Banks and ECA especially since they both offer export credit insurance support.

4.2.2. Services Offered by ECAs

ECAs offer a wide range of services. From providing credit or loans to providing insurance against specific risks. These agencies help home state companies win contracts through offering attractive financing terms to the buyers of these companies in addition to insuring against buyer's default.⁴⁸ For the purpose of this research, the focus will be on the services offered by ECAs in their capacity as insurers not as credit providers. Generally, ECAs insurance, as is the case with the UKEF, covers against confiscation, currency inconvertibility, political violence and riots, expropriation and nationalization, remittance and transfer restrictions and against defaults on certain obligations including loans and arbitral claims and contracts.⁴⁹

The Compagnie Francaise d'Assurance pour le Commerce Exteriorur (COFACE) which, is a member of the Berne Union, would not insure against political risk only if the insured was in a situation that would have been reasonably avoidable.⁵⁰ The company, basically, covers against political risk and covers against terrorism under certain condi-

⁴⁸ This is, for example, what the UKEF offers.

Found at:

<<https://www.gov.uk/government/organisations/uk-export-finance/about>>

Last accessed on the 2nd of January 2017.

⁴⁹ Gordon (*Chapter 1, n32*) at 98.

⁵⁰ Gordon (*Chapter 1, n32*) at 94.

tions. In case of terrorism, the company does not cover against the losses incurred by the investor, rather it covers against the inability of investors to benefiting from their property rights.⁵¹ COFACE offers its services to French equity investors who are willing to establish a branch or a representative office overseas and to royalties and to bonds provided in return for medium or long term local loans as well as to long term shareholders', or advances to restricted current accounts and, finally, to accompanying bank loans.⁵² It may, also, extend its support to foreign investors who have an actual presence in France as long as they will be exporting the goods and services from France.⁵³ Finally, COFACE considers itself as the insurer of the last resort. In that sense, they would insure and cover risks only in case these risks are not offered by the private sector.⁵⁴ It shall be stated that COFACE is not the only agency covering against terrorism. Italy's SACE covers against terrorism and considers it a separate risk with its own separate coverage. The same applies to OPIC, the American Export Credit Agency and to the German Export Credit Program as well.⁵⁵

In Spain, the Spanish ECA la Compañía Española de Seguros de Credito a la Exportacion (CESCE), offers insurance and guarantees against expropriation, nationalization, and against confiscation of property. It also covers against regulatory risks, contractual risk and non-transfer risks. It extends its services to cover against what it refers to as political violence which includes terrorism and other alterations of public order.⁵⁶

⁵¹ Based on an interview with Mr. Christophe Viprey, Director of Public Guarantees of the Compagnie Francaise d'Assurance pour le Commerce Exterior (COFACE) on the 18th of May 2015.

⁵² *ibid.*

⁵³ *ibid.*

⁵⁴ *ibid.*

⁵⁵ Gordon (*Chapter 1, n32*) p 117.

⁵⁶ More information can be found at:

<<http://inglaterra.cesce.es/web/eng/Products/Foreign-Investment-Policy.aspx#s2>>

Last accessed on the 23rd May 2015

CESCE's model is based on pure cover where companies normally export or invest while banks lend or issue performance/advance payment guarantees and then CESCE as an ECA mitigates the risks faced both by exporters and banks.⁵⁷ CESCE's relationship with the private sector, as with other ECAs, is not to compete but rather complete and fill in the gap not covered by the private sector.⁵⁸ It is worth noting that there are number of state-owned institutions as well as private ones in Spain, that offer some services complementing those of CESCE. These services are financing services nevertheless, not insurance or guarantee services. In that respect CESCE which, is also a member of the Berne Union, along with a number of private sector insurance companies offer services and guarantees against risks faced by exporters in the host state.⁵⁹ As for the other companies in Spain providing credit financing services, these include the Instituto de Crédito Oficial (ICO) which is state owned and the Compañía Española de Financiación del Desarrollo (COFIDES) which is jointly owned between the state and the private sector.⁶⁰

CESCE's cover percentage reaches up to a maximum of 99% while COFACE's coverage reaches 95%. OPIC's coverage on the other hand, reaches to 90 % and so does MIGA's coverage for equity investments.⁶¹ The German model, however has a more de-

⁵⁷ Based on an interview with Mrs. Rocío Uriarte Chavarri, Senior Analyst and Head for International Relations of la Compañía Española de Seguros de Crédito a la Exportación (CESCE) on the 29th of April 2015.

⁵⁸ *ibid.*

⁵⁹ List of Berne Union member states can be found in Appendix I.

⁶⁰ More information can be found at the following links:

ICEX España Exportación e Inversiones:

<<http://www.icex.es/icex/es/navegacion-principal/que-es-icex/contacto/ventana-global/index.html>> (In Spanish)

Last accessed on the 23rd of May 2015

and Instituto de Crédito Oficial;

<http://www.ico.es/en/web/ico_en/what-ico-is> (Available in English & Spanish)

Last accessed on the 23rd of May 2015

and Compañía Española de Financiación del Desarrollo;

<<https://www.cofides.es/index.php>> (Available in English & Spanish)

Last accessed on the 23rd of May 2015

⁶¹ More information can be found at:

<<http://inglaterra.cesce.es/web/eng/Products/Foreign-Investment-Policy.aspx#s2>>

Last accessed on the 23rd May 2015

tailed maximum coverage structure; for political risk, if it is related to a single transaction and revolving cover, the cover reaches up to 95% while it is 85% for commercial risks and protracted default. If the investor chose a Wholeturnover policy then the coverage for political risk will reach 95% while it is 90% for commercial risk. If the German investor chose a Wholeturnover Policy Light then the coverage will reach 90% for all types of risks while it reaches 95% in cases of buyer credit cover for private and public buyers and in case of manufacturing risk cover for private and public buyers.⁶² Canada's EDC cover reaches up to 90% of the losses while the Ex-Im Bank of the U.S cover reaches up to 95% of the losses for commercial and political risks of the export credit insurance policy.⁶³

It has been observed that some ECAs do offer insurance and guarantees against commercial risk though these agencies are quite limited in number whereas the majority are specialized in offering guarantees and insurance against political risk.

⁶² For more information please refer to:

For CESCE please visit:

<<http://inglaterra.cesce.es/web/eng/Products/Foreign-Investment-Policy.aspx#s2>>

Last accessed on the 23rd of May 2015

For COFACE, information was provided by Mr. Christophe Viprey Director of Public Guarantees at COFACE.

For USA's OPIC please visit:

<<https://www.opic.gov/what-we-offer/political-risk-insurance/extent-of-coverage>>

Last accessed on the 23rd of May 2015

For MIGA please visit:

<<http://www.miga.org/whoweare/index.cfm?stid=1792#con3>>

Last accessed on the 23rd of May 2015

For Germany please visit:

<<http://www.agaportal.de/en/aga/entgelt.html>>

Last accessed on the 23rd of May 2015

⁶³ For more information please visit:

For Canada's EDC:

<<http://www.edc.ca/EN/Canadian-Financial-Institutions/Documents/brochure-solutions-guide-for-fis.pdf>>

Last accessed on the 26 of February 2016.

For U.S. Ex-Im Bank:

<<http://www.exim.gov/what-we-do/export-credit-insurance>>

Last accessed on the 26 of February 2016.

Some ECAs have gone a step further from the traditional political risk insurance that includes coverage against expropriation, nationalization, confiscation, seizure, civil disorder, war, riots, sabotage, non-transfer of currency and the termination of contracts agreed with local public counter-parties,⁶⁴ and offers, as well, covers against natural disaster as it is the case with SACE the Italian ECA. SACE, a member of the Berne Union, covers against terrorism and considers it a separate risk with its own separate coverage.⁶⁵ This agency offers its services to Italian exporters and to foreign companies that are controlled by Italian investors.⁶⁶ This Berne Union agency also covers against terrorism.

One of the important services offered by some ECAs is the use of the home state government's diplomatic resources to avoid potential problems.⁶⁷ In that respect, it may be one of the main advantages of Governmentally-sponsored agencies since such agencies are able to produce welfare-enhancing services at low cost.⁶⁸ Additionally, some agencies offer their services not only to their exporters, they offer their services, as well, to foreign investors who have investments in the state of which the said ECA belongs to. This is for example the case of the Australian's ECA, The Export Finance and Insurance Corporation (EFIC).⁶⁹

⁶⁴ Dimopoulos (*Chapter 2, n187*) p 7

⁶⁵ Gordon (*Chapter 1, n32*) p. 117

⁶⁶ This information can be found at the following link in Italian:

<http://www.sace.it/GruppoSACE/content/it/consumer/products/investments_protection/investments/ind_ex.html?tab=1>

Last accessed on the 25th of May 2015

⁶⁷ Gordon (*Chapter 1, n32*) at 102.

⁶⁸ Gordon (*Chapter 1, n32*) at 105.

⁶⁹ Gordon (*Chapter 1, n32*) p 98.

Not only that, but some agencies require that investors should respect host states decisions, laws and regulations and not provoke the host state's government to expropriate investors' property or limit their access to the property rights. This is for example the case with the UK's Export Credit Guarantee Department (ECGD) which is known today as the UK Export Finance (UKEF).⁷⁰ Additionally, the UKEF may request from the investor that he proves that the host state is satisfied with the project proposal the investor intends to carry out within its territories before the insurance is given.⁷¹ The agency stated that they do not exist to compete with the private sector by the private sector.⁷² In that sense, like other agencies, it completes not compete with the private sector.

Ex-Im Bank of the United States, a Berne Union member company, offers to a number of investors willing to invest in certain host states some tailored products and services. The Bank has a specialized division for U.S. small business exporters and financial institutions and they offer products related to U.S exporters.⁷³ The Bank provides services for U.S. exporters and lenders who are willing to invest in the African region. They also grant a number of products and services to exporters willing to invest in Brazil, Turkey, India, Mexico, Colombia, China, Vietnam, Nigeria, South Africa and in Indonesia but they do not cover investors who wishes to invest in states like Cuba and Afghanistan.⁷⁴

⁷⁰ *ibid.*

⁷¹ Gordon (*Chapter 1, n32*) at 102

⁷² Available at:

<<https://www.gov.uk/government/organisations/uk-export-finance/about>>

Last accessed on the 2nd of January 2017.

⁷³ For more information please visit:

<<http://www.exim.gov/what-we-do/export-credit-insurance>>

Last accessed on the 26 of February 2016.

And;

<<http://www.exim.gov/what-we-do/export-credit-insurance/financial-institution-buyer-credit-export-insurance>>

Last accessed on the 26 of February 2016.

⁷⁴ This information can be found at:

US Ex-Im Bank: Country Limitation Schedule

<<http://www.exim.gov/tools-for-exporters/country-limitation-schedule>>

Last accessed on the 26th of February 2016.

The Export-Import Bank covers against certain types of political risks including war, and its services are offered on a short to medium term basis.⁷⁵

As for the Overseas Private Investment Corporation (OPIC), another ECA and a member at the Berne Union, this agency offers to U.S. investors, willing to invest in emerging markets, covers against political risk and a number of debt funding services.⁷⁶ Though there is no specific requirement for the type of investment covered, it, nevertheless, offers its financial services on a medium- to long-term funding basis. OPIC covers political risks, which, according to OPIC, includes acts of war, political violence and terrorism as well as expropriation and currency inconvertibility.⁷⁷ OPIC offers insurance and guarantee against a number of political risks, political financial risk and political commercial risks. These include acts of war, terrorism, politically-motivated violence and civil strife along with restrictions on conversion and transfer of local-currency earnings, expropriation, abrogation, repudiation, impairment of contract and other improper host state interference.⁷⁸ These services are offered to U.S investors or U.S corporations exporting to a host state that has concluded an OPIC BIT and also to investments that are thought to be able to contribute to the improvement of the host state's condition and

⁷⁵ For more information please visit:

<<http://www.exim.gov/what-we-do/export-credit-insurance>>

Last accessed on the 26th of February 2016.

And;

<<http://www.exim.gov/what-we-do/export-credit-insurance/financial-institution-buyer-credit-export-insurance>>

Last accessed on the 26th of February 2016.

⁷⁶ This information can be found at the following links:

Under:

1- What We Offer

<https://www.opic.gov/what-we-offer/overview>

Last accessed on the 26th of February 2016.

2- Political Risk OPIC:

<https://www.opic.gov/what-we-offer/overview>

Last accessed on the 26th of February 2016.

⁷⁷ These could fall under the regulatory risk which form part of the political risk category.

⁷⁸ This information can be found at:

<<https://www.opic.gov/what-we-offer/political-risk-insurance>>

Last accessed on the 27th of May 2015.

which would elevate the level of competition in the home state and contribute, positively, to the economy of the home state.⁷⁹

On the other hand, and in Germany, the Federal export credit guarantee is provided by Euler Hermes Deutschland AG and PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, known as PwC act on behalf of the Federal Government of Germany in serving the Hermes Cover.⁸⁰ Both companies are members at the Berne Union and they offer to German banks and exporters specific products and services from which exporters and banks are able to benefit from.⁸¹ They offer a range services that covers political and commercial risks. Political risk, according to the conditions of the Federal Export Credit Guarantee of Germany through these two private companies, includes war, civil unrest and revolution taking place in the host state. Repatriation of capital and conversion rate risk of local currency of the host state.⁸² As for the commercial risk covered by the German model, this includes loss of receivables due to non-payment or bankruptcy of the buyer or any settlement happening before or after resorting to the legal system. They, also, offer short-term, medium-term and long-term cover policies covering areas of manufacturing, project finance and tied finance credits.⁸³ In addition, they offer export credits for exporters of services, construction works, airbus guarantees, ship financing, revolving supplier credit, framework credit, securitiza-

⁷⁹ Rubins and Kinsella (*Chapter 2, n65*) pp 70-86.

⁸⁰ More information on the Federal Export Credit Guarantees can be found at:

<<http://www.agaportal.de/en/aga/>>

Last accessed on the 26th of February 2016.

More information on the list of Services offered by the Federal Export Credit Guarantees of Germany:

<<http://www.agaportal.de/en/aga/produkte.html>>

Last accessed on the 26th of February 2016.

⁸¹ Full list of Berne Union member states available on Appendix I.

⁸² More information on the list of Services offered by the Federal Export Credit Guarantees of Germany:

<<http://www.agaportal.de/en/aga/produkte.html>>

Last accessed on the 26th of February 2016.

⁸³ *ibid.*

tion guarantee and confiscation risk to name a few.⁸⁴ It shall be finally stated that services offered by the delegate of the Federal Government of Germany are available for private and public investors as well.⁸⁵

It is of importance to mention that some ECAs offer their services to exporters only within the scope of a BIT. i.e. the agency's relation with the host state is governed and determined within the scope of a BIT. This is for example the case with OPIC.⁸⁶ Finally, some ECAs would ask to sign a direct agreement with the host state's government where the host state's government accepts liability for any payments that have been made to the lender by the ECA.⁸⁷

As it was examined, ECAs emerged due to the need of coverage against political risks associated with foreign investments and to promote and facilitate foreign investment through offering export credit support and financing. Insurance programs were created by ECAs and directed at covering against expropriation, breach of contract by the host state's government, political violence and riots and any restrictions imposed on the transfer of the investment proceeds among other political risks.⁸⁸

These services may be offered to nationals of the home state where the ECA is based or to foreign investors alike.⁸⁹ It may also be offered to importers or exporters of goods as

⁸⁴ *ibid.*

⁸⁵ *ibid.*

⁸⁶ Gordon (*Chapter 1, n32*) p 102.

⁸⁷ Yescombe (*Chapter 2, n184*) p 450.

⁸⁸ John Anthony VanDuzer, Penelope Simons, Graham Mayeda, 'Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators', Commonwealth Secretariat (2013) pp 391-392.

⁸⁹ Like it is the case with the UK's ECGD which offer its services to investors who are not necessarily UK investors. Gordon (*Chapter 1, n32*) p 118.

it will be highlighted in the next chapter.

4.2.3. Public/Private Structure of ECAs

Since there is no one standard structure for ECAs, their nature and structure may, in general, differ from one country to another. Furthermore, they may differ from one agency to another within the same state. It is noted that services offered by one agency are not necessarily offered by another agency internationally or even in the same state. ECAs may be supported by the home state's government in which case they are publicly-owned ECAs, or they may be owned by private investors, in which case they are privately-held ECAs.⁹⁰ They may be owned, on the other hand, by both the state and private investors and in this case, they are considered a quasi-governmental agency.⁹¹ Knowing how these agencies are governed will show how different these agencies are and why such difference is present (and how the services may be affected by such differences).

The United Kingdom was one of the first states to introduce the first governmentally export credit services through the Export Credits Guarantee Department (ECGD) in

⁹⁰ Yescombe (*Chapter 2, n184*) p 218.

And;

Stephens (*Chapter 1, n9*) p 5.

⁹¹ Judith Neyer, 'The Ilisu Dam Project Europe's Money Would Move Turkey Away from the Acquis Communautaire' [2006] European ECA Reform Campaign (Published by FERN). p 1.

This article can be found at:

<http://www.eca-watch.org/sites/eca-watch.org/files/Ilisu_dam_briefing.pdf>

Last accessed on the 19th of December 2013

1919.⁹² But the ECGD or UK Export Finance (UKEF) which, is the operating name of ECGD, is not the only insurance provider in the Kingdom.⁹³

The international private insurance provider Euler Hermes, is owned by Allianz Company, is also another insurance provider. Though the main difference between those two companies is their nature. Euler Hermes has a presence in many states including France, Spain, Argentina, Chile, Mexico and the USA.⁹⁴ Hermes is also active in Germany where it provides export credit guarantees with its peer the privately-owned PwC Deutsche Revision. Both companies, jointly, manage such products on the behalf of the federal government of Germany.⁹⁵

In the United States, export credit insurance is delegated to a number of providers. Among these is the Export Import Bank of the United States (Ex-Im Bank), which was founded in the 1930s.⁹⁶ Another US export credit guarantees provider is a self-sufficient government-owned agency established in 1971 called the Overseas Private Investment Corporation (OPIC).⁹⁷

⁹² *ibid.*

⁹³ Lloyd's of London, a private sector agency, is another PRI provider in the U.K.

More information on Lloyd's of London Corporation PRI please visit:

'Political Risk Insurance' (*Lloyd's of London*):

<http://www.lloyds.com/redirect-pages/risk_locator/political_risks_insurance>

Last accessed on the 18th of May 2015.

⁹⁴ More information about locations where Euler Hermes provide their services can be found at:

<<http://www.eulerhermes.com/group/Pages/worldwide-presence.aspx?>

Last accessed on the 7th of March 2016.

⁹⁵ This information can be found at:

<<http://www.agaportal.de/en/aga/>>

Last accessed on the 19th of December 2013

⁹⁶ This information on the Ex-Im Bank can be found at:

<<http://www.exim.gov/about/whoweare/>>

Last accessed on the 19th of December 2013

And;

<<http://www.exim.gov/about/whoweare/history.cfm>>

Last accessed on the 19th of December 2013

⁹⁷ This information on OPIC of the USA can be found at:

<<http://www.opic.gov/who-we-are/overview>>

Euler Hermes, American International Group (AIG) and Zurich Insurance Group are some of the privately held insurance providers. Though Zurich is mainly an insurance company, it is listed in the Bern Union as export credit guarantee providers.⁹⁸ AIG is one of the biggest private political risk insurance provider which offers PRI under its own commercial name. Euler Hermes is not as big as AIG but nevertheless it has been successful and gained fame from being delegated by the Federal Government of Germany to provide the Hermes Cover.⁹⁹

In France, the official ECA, Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE), was established in 1946 and was a governmental agency until 1994.¹⁰⁰ It still provides export credit guarantee services on behalf of the French government.¹⁰¹ Currently, the majority of COFACE's shares (58.50%) are owned by the public, while Natxis, its previous owner, holds 41.24% of the shares and the remaining 0.26% are shares owned by employees of the company.¹⁰² COFACE is currently delegated by the French state to offer, on behalf of the state, export credit guarantee services to French exporters and investors.

Last accessed on the 19th of December 2013

⁹⁸ List of Berne Union members is available at Appendix I.

⁹⁹ More information about the Hermes Cover can be found at:

<<http://www.agaportal.de/en/aga/>>

Last accessed on the 7th of March 2016.

¹⁰⁰ This information on France's COFACE can be found at:

<<http://www.coface.com/Group/Our-history>>

Last accessed on 19th of December 2013

¹⁰¹ Based on a phone conference with Mr. Christophe Viprey (Director of Public Guarantees of COFACE) on the 18th of May 2015.

¹⁰² This information on France's COFACE can be found at:

<<http://www.coface.com/Group/Our-history>>

Last accessed on the 18th of May 2015

As it is the case in Germany, the UK and the US, COFACE is not the sole export credit guarantee and insurance provider. The private insurance companies Euler Hermes and PwC have a presence in France too.¹⁰³

From studying those examples, it is observed that there are some differences in the nature of ownership of export credit insurance and guarantee providers from one country to another (and even in the same state at times). It is also noticeable that there could be one official provider of such services or many providers. These differences may be traced back to the needs of each state where certain exporting states have to cover against more risks than others especially since its investors and exporters may be at risk of losing their property rights, hence the differences in structure and the differences in services. As such, the difference in the services provided is due to having different market needs, whereas the difference of structure could probably be as a means of governing of the agency and distributing the gains and losses among different partners involved. Due to these facts, there will be a distinction presented between the different types of export credit guarantee providers in a number of states and some new examples will also be presented.

Export credit guarantee and insurance can be delegated to providers that are, generally, owned by the home state's government, jointly owned between public and private sector or to the private sector. For example, the UK Export Finance is government-backed ECA while COFACE is an example of a privately-owned agency delegated by the home state government. CESCE of Spain is an example of a jointly-owned ECA while AIG, on the

¹⁰³ More information about locations where Euler Hermes provide their services can be found at: <http://www.eulerhermes.com/group/Pages/worldwide-presence.aspx?>>
Last accessed on the 7th of March 2016.

other hand, is an example of a private insurance company offering PRI. The distinction does not stop here, governmentally-owned export credit agencies can be an emanation from the state or a state-owned corporation. Likewise, privately-owned companies may be acting on their own behalf in providing export credit guarantee and political risk insurance or acting on the behalf of the home state's government. For example, the UKEF is an emanation of the government while Canada's EDC is an example of a corporation established by the government. On the other hand, Euler Hermes and PwC are an example of two private companies delegated by the federal government of Germany to offer Export Credit Guarantee support on its behalf while Lloyd's of London Corporation is an example of a commercial insurance company that provides PRI under its own name.

It is worth mentioning that some authors regarded the presence of the following types of ECAs as: emanation from the state, a state owned ECA and, finally, a private company.¹⁰⁴ This distinction, though accurate with regards to the clear distinction between state-owned and privately-owned companies, nevertheless failed to distinguish the cases where the state holds shares with a private corporation in a company offering export credit insurance and guarantee support. It also failed to address the cases where export credit insurance and guarantee support is offered by a private company acting on its own and not on the behalf of the state. These matters will be addressed in the following examples, highlighting the different types of ECA.

Publicly-owned ECAs are those managed, established and operated by the government. ECGD of the United Kingdom, known now as the UK Export Finance, is an example of

¹⁰⁴ Murray, Holloway and Timson-Hunt (*Chapter 4, n8*) p 454.

a government-operated agency that is under the umbrella of the Department of Business, Innovation and Skills reporting to both the Minister of State for Trade and Investment and the Secretary of State for Business, Innovations and Skills.¹⁰⁵ This body is an emanation from the government.¹⁰⁶ As will be elaborated hereafter, it is composed of an Executive Committee, a Management Board and Advisory Council.¹⁰⁷ The justification behind such a type of ECA, i.e. publicly-sponsored one, can be traced to the fact that governments have a unique competitive strength that may be used to bring low cost enhanced welfare.¹⁰⁸ The UKEF is a member at the Berne Union and offers a number of services to UK exporters that wish to invest overseas. It provides bond insurance and support, buyer credit facility, export working capital scheme, debt conversion, overseas investment insurance, supplier credit finance, lines of credit, direct lending scheme and letter of credit guarantee and export insurance.¹⁰⁹ The UKEF is a member at the Berne Union and the OECD 1978 Consensus. This arrangement, the OECD Consensus, came into effect in 1978 and has an indefinite duration.¹¹⁰

US Ex-Im Bank, a government-run export credit insurer, established in 1934 by President Roosevelt, is composed of an Advisory Board, a Board of Directors and a number of officers.¹¹¹ There is also an additional advisory body which advises on Sub-Saharan

¹⁰⁵ Information on the UK's Export Credit Finance can be found at:

<<https://www.gov.uk/government/organisations/uk-export-finance>>

Last Accessed on the 19th of December 2013

¹⁰⁶ Murray, Holloway and Timson-Hunt (n 572) p 454.

¹⁰⁷ More information on the UK's Export Credit Finance can be found at:

<<https://www.gov.uk/government/organisations/uk-export-finance/about/our-governance>>

Last accessed on the 19th of December 2013

¹⁰⁸ Gordon (n 29) p 105.

¹⁰⁹ More information can be found at:

<https://www.gov.uk/government/collections/uk-export-finance-products-and-services#group_2523>

Last Accessed on the 19th of December 2013

¹¹⁰ Agreement on Officially Supported Export Credits (OECD 2016 Consensus), Feb 2016.

¹¹¹ More information of the Ex-Im Bank can be found at:

<<http://www.exim.gov/about/whoweare/leadership/boardofdirectors/index.cfm>>

Last Accessed on the 19th of December 2013

Africa.¹¹² It, also, has an Auditing Committee.¹¹³ The bank offers a number of services to US investors. These include risk-protection, extended credit to buyers, direct loans, loan guarantee, finance lease guarantee, supply chain finance guarantee, term financing and working capital.¹¹⁴ As it was mentioned earlier in this chapter, the Bank has introduced a number of new services directed at investors in the medical technology field, transportation security, environmental sector, investors who are willing to invest in Sub-Saharan Africa and some tailored services to small businesses.¹¹⁵ The Bank is the official ECA of the United States and is a member at the Berne Union and the OECD Arrangement on Officially Supported Export Credit of 1978 and it offers import credit guarantees, insurances and services as well.

Another U.S. government owned ECA is OPIC. Unlike its counterpart Ex-Im Bank, OPIC cater private investors in emerging markets and developing economies and it offers PRI. OPIC it is only a member of the Berne Union and solely offers export credit related products.¹¹⁶

It is worth mentioning that Ex-im Banks and ECAs are different faces of the same coin. They are both an initiative from the home state directed at facilitating the exportation of local products and services internationally. They both cover against specific risks associ-

¹¹² *ibid.*

¹¹³ Ex-Im Bank of USA Bylaws Section 7, Exhibit B.

The bylaws can be found at:

<<http://www.exim.gov/about/whoware/charterbylaws/bylaws.cfm>>

Last accessed on the 19th of December 2013

¹¹⁴ More information of Ex-Im Bank's products and services can be found at:

<<http://www.exim.gov/products/>>

Last accessed on the 19th of December 2013

¹¹⁵ See;

<<http://www.exim.gov/products/>>

Last accessed on the 19th of December 2013

¹¹⁶ List of Berne Union members can be found at Appendix I.

ated with foreign investment in emerging markets specifically. These services complement those offered by other private agencies whose objective is insuring against a number of risks associated with international investments.

Both, ECAs and Ex-im banks are members of the Bern Union, which is directed at joining the forces of ECAs around the world to organize themselves under one umbrella and discuss the challenges they are facing and how to overcome these challenges. The only difference that exists is that ECAs, unlike Ex-Im Banks, only offer export credit support whereas Ex-Im Banks offers, in addition to export credit support, import credit guarantees. For these reasons, there is no value in differentiating, in this research, between Ex-Im Banks and ECA since they both offer export credit insurance services.¹¹⁷

It is noted the export credit guarantees of the Federal Government of Germany are offered by two German private insurance companies jointly. Euler Hermes Aktiengesellschaft, now known as Euler Hermes Deutschland AG, and PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC). These products are jointly offered products in the name of the federal state of Germany. And for that reason, the German ECA model falls under the umbrella of privately held ECA offering services on behalf of the state.¹¹⁸

¹¹⁷ For example, this is the case with the U.S. Ex-Im Bank.

See:

<<http://www.exim.gov/who-we-serve/us-product-importer>>

Last accessed on the 27th of February 2016.

¹¹⁸ Carole Murray, David Holloway and Daren Timson-Hunt, *Schmitthoff: The Law and Practice of International Trade* (12th edn, Sweet and Maxwell 2012) p 454.

The Canadian export credit insurance service is offered by the Export Development Canada (EDC). It presents another side of a governmental ECA. This version is governed by the Export Development Act of 1985, and is established for the purpose of supporting and developing Canada's domestic trade and to support and improve Canada's export trade.¹¹⁹ EDC offers a number of products and services that complement those offered by private insurance companies and financial institutions.¹²⁰ What makes this model ECA special is the fact that it is a governmental ECA but at the same time does not rely on the government for funding.¹²¹ This corporation also provides its services to potential exporters through partnering with other financial institutions and through collaborating with the government. This way they reduce the risk associated with such investment by having the government being a partner with the exporter.¹²² For those reasons, the Canadian ECA model can be regarded as a Governmental ECA falling under the label of a state-owned corporation.¹²³

On the other hand, in Italy, the Istituto per i Servizi Assicurativi del Commercio Estero (SACE) which is a joint stock company, is responsible for offering export credit insurance for foreign companies, banks or financial institutions that contribute to the improvement of the Italian economy; and to Italian companies, banks or financial institu-

¹¹⁹ Canada's Export Development Act of 1985. Purpose and Powers Art. 10(1) a&b.

The Export Development act of Canada can be found at:

<<http://laws.justice.gc.ca/eng/acts/E-20/>>

Last accessed on the 20th of January 2014.

¹²⁰ *ibid*, Art. 10(1.01)

¹²¹ More information on Canada's EDC can be found at:

<<http://www.edc.ca/EN/About-Us/Pages/default.aspx>>

Last accessed on the 20th of January 2014.

¹²² More information is made available through:

<<http://www.edc.ca/EN/About-Us/Pages/default.aspx>>

Last accessed on the 20th of January 2014

And;

Under 'Purpose' in the following link:

<<http://www.edc.ca/EN/About-Us/Disclosure/Documents/disclosure-policy.pdf>>

Last accessed on the 20th of January 2014.

¹²³ Murray, Holloway and Timson-Hunt (*Chapter 4, n8*) p 454.

tions wishing to export their products and services abroad either directly through becoming partners in such services or indirectly through offering such services as a third party foreign to the investment.¹²⁴ It is worthwhile mentioning that SACE is currently under the ownership of one of Italy's largest investment banks, the Casa Depositi e Prestiti S.p.A. (CDP).¹²⁵

What makes this model a special one is the fact that though it is a privately-operated company, its dividends are paid by the Italian Government.¹²⁶ At first, this may lead to the conclusion that it is a governmental ECA falling under the label of a state-owned corporation since the state is involved directly and is responsible for the payments of its dividends. Add to that the fact that this company's members are appointed by the Ministry of Economy and Finance, as this will be shown in the section of this chapter. Nevertheless, this is not a true conclusion since the ownership of the company owning SACE, CDP, reveals otherwise, as it will be elaborated.

Another governmental body that is responsible for providing export credit products in Italy is the Societa Italiana per le Imprese all'Estero, also known as (SIMEST). Like its sister company SACE, SIMEST is currently under the ownership of Casa Depositi e

¹²⁴ Articles of Association of SACE. Art. 1 & Art. 4.
The Articles of Association of SCAE is available on:
<http://www.sace.it/GruppoSACE/export/sites/default/download/normativa/Articles_of_Association_23_05_2013_EN.pdf>
Last accessed on the 20th of January 2014.

¹²⁵ SACE Ownership,
Available under '3. Ownership' on the following link:
<http://www.sace.it/GruppoSACE/content/download/normativa/InfoMemo_SACE-EN.pdf>
Last accessed on the 20th of January 2014.

¹²⁶ SACE Ownership,
Available under '3. Ownership' on the following link:
<http://www.sace.it/GruppoSACE/content/download/normativa/InfoMemo_SACE-EN.pdf>
Last Accessed on the 20th of January 2014.

Prestiti S.p.A.¹²⁷ SIMEST offers its services and products to Italian exports and improves their operations abroad and reduces the risks they may face by becoming their partner in their business abroad.¹²⁸

The Casa Depositi e Prestiti's ownership is divided into shares where the Italian government owns the majority holding 80.1% of the shares. The private sector owns 18.4% of the shares. This sector is represented by a number of banks. The remaining 1.5% are treasury shares.¹²⁹ This is of importance in determining the ownership of SACE and SIMEST since the Casa Depositi e Prestiti owns 100% of the shares of SACE and 76% of SIMEST. The ownership of the Casa Depositi e Prestiti can lead us to conclude that such an agency is a quasi-governmental agency or company where the majority shareholder is the local government and minority shareholders are investor from the private sector.¹³⁰

The last type of ECAs is one that is fully owned and operated by the private sector. The French Company COFACE presents a good example of such model where they are present in an international environment and provide their products, under their own name

¹²⁷ For more information please visit:

<<http://www.cdp.it/en/company-profile/mission-and-role/mission-and-role.html>>

Last accessed on the 27th of February 2016.

And;

<<http://www.cdp.it/en/media/press-releases/cdp-approva-l-esercizio-del-diritto-di-opzione-all-acquisto-di-sace-e-simest.html>>

Last accessed on the 27th of February 2016.

¹²⁸ For more information about SIMEST's services please visit:

<<http://www.simest.it/page-en.php?id=24>>

Last accessed on the 27th of February 2016.

¹²⁹ For more information please visit the following link:

<<http://www.cdp.it/en/company-profile/mission-and-role/mission-and-role.html>>

Last accessed on the 27th of March 2016.

¹³⁰ Information on the ownership structure of SACE and SIMEST can be found at:

<<http://www.cdp.it/en/media/press-releases/cdp-approva-l-esercizio-del-diritto-di-opzione-all-acquisto-di-sace-e-simest.html>>

Last accessed on the 27th of February 2016.

and on their own behalf, to a number of investors. In addition, commercial insurance companies like AIG and Lloyd's of London are a good example of private companies offering, under their own name, PRI support.

The American Insurance Group offer covers against, among other type of risks, political risk.¹³¹ This publicly-traded company has its shares listed in stock markets and it owns and operates other financial and insurance services companies.¹³² The UK based insurance company Lloyd's of London is one of the oldest insurance providers in the world.¹³³ It is more of a market than it is a traditional company.¹³⁴ Among the many risks covered by Lloyd's lies political risk.¹³⁵ What is different about Lloyd's is that this corporation brings its members as syndicates to insure against risks.¹³⁶ Lloyd's structure of ownership, though it is a privately-held company, differs from other insurance companies. Lloyd's prides itself on being called a market rather than a company.¹³⁷ In other matters, it acts under the umbrella of the corporation of Lloyd's and this is specifically

¹³¹ For more information about AIG's PRI please visit the following links:

<<https://www.aig.co.uk/business/products-and-services/political-risks>>

Last accessed on the 27th of February 2016.

¹³² For more information about AIG's ownership please visit the following links:

Under: (About):

<https://www.aig.co.uk/about-aig#pr_c1_cr_inpagetitle>

Last accessed on the 27th of February 2016.

¹³³ For more information about Lloyd's of London Corporation please visit the following links:

For the History of Lloyd's:

<<http://www.lloyds.com/lloyds/about-us/history>>

Last accessed on the 27th of February 2016.

And;

<<http://www.lloyds.com/lloyds>>

Last accessed on the 27th of February 2016.

¹³⁴ For more information about Lloyd's of London The Market:

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds/the-lloyds-market>>

Last accessed on the 27th of February 2016.

¹³⁵ For more information about Lloyd's of London PRI:

<<https://www.lloyds.com/the-market/tools-and-resources/tools-e-services/risk-locator/risk-locator-class-of-business/political-risk>>

Last accessed on the 27th of February 2016.

¹³⁶ More information about Lloyd's of London The Market can be found at:

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds/the-lloyds-market>>

Last accessed on the 27th of February 2016.

¹³⁷ *ibid.*

true in matters related to monitoring the Market's operations.¹³⁸ As far as the structure of Lloyd's, the Lloyd's Market has an interesting structure not familiar to other insurance companies. Basically, in the Corporation, there are managing agents and syndicates.¹³⁹ Members of Lloyd's are those who provide the capital to support the underwriting process.¹⁴⁰ For that, Lloyds may be regarded as the trading floor of insurance brokers in the stock market where sellers and buyers of insurance meet up and where the Corporation of Lloyd's manages the trading taking place under its roof. Lloyd's of London, therefore, provides a market for insurance products.

In Spain, CESCE is the official export credit insurance provider. Like the Italian version, CESCE's shares are split between public and private sectors where the state holds 50.25% of the shares, 45.85% are held by Spanish banks and the remaining 3.9% are held by Spanish insurance companies.¹⁴¹ La Compañía Española de Seguros de Crédito a la Exportación, CESCE, was established in 1970 though the law regulating export credit insurance in Spain was released by 1928.¹⁴² It, i.e. CESCE, has the right to grant insurance under the name of the government or under its own private name. Now, CESCE is

¹³⁸ Information about Lloyds of London can be found at:

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds>>

Last accessed on the 1st of April 2014

And;

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds/the-lloyds-market>>

Last accessed on the 1st of April 2014

And;

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds/the-corporation-of-lloyds>>

Last accessed on the 1st of April 2014

¹³⁹ This information can be found under Lloyd's of London The Market:

<<http://www.lloyds.com/lloyds/about-us/what-is-lloyds/the-lloyds-market>>

Last accessed on the 27th of February 2016.

¹⁴⁰ *ibid.*

¹⁴¹ The information about ownership is available on the official website of CESCE:

<http://www.CESCE.es/web/sp/Corporativo/quienes_somos/index.aspx>

Last accessed on the 10th of November 2014

The link is available in Spanish

¹⁴² Bernardo M. Cremades (ed), *Business Law in Spain* (2nd edn, Butterworths Law 1992) pp. 334-335.

active in Spain, France and Portugal not to mention in a number of Latin-American states.¹⁴³

Table G, at the end of this chapter, explains the ownership structure of various ECA in different countries and, as well, lists the dates when they were established while table H will elaborate on the aim of establishment of such agencies as to whether they were established to promote home state welfare, host state's welfare or both.¹⁴⁴

Based on the aforementioned, it is noted that the nature of ownership of ECAs is not the same. They may be established and ran by local authorities or maybe an emanation from the government. They could be jointly owned between the public and private sectors or may be fully owned by the private sector offering their services on their own behalf or managing these services and offering them on the behalf of the government. The only difference that may be present in relation to the nature or ownership of these agencies would be that a publicly-owned ECA promotes international standards for business conduct (unlike private political risk insurers). Add to that the fact that publicly sponsored agencies, like OPIC, when in negotiations with the host state's government, it is more of a government-to-government agreement where they reach to special agreements with regard to certain type of risks.¹⁴⁵

¹⁴³ For list of countries where CESCE offer its services please visit:
<<http://inglaterra.cesce.es/web/eng/Cesce-Group/index.aspx>>

Last accessed on the 27th of February 2016.

¹⁴⁴ Table G at p 283.

Table H at p 284.

¹⁴⁵ Gordon (*Chapter 1, n32*) p 105.

4.2.4. Corporate Governance and ECAs

The Cadbury Report of 1992 and the Hampel Report of 1998 are considered the foundation of corporate governance. Managing, directing and controlling the corporation is what corporate governance stands for, according to the Hampel Report.¹⁴⁶

In order to actively manage a company, while prioritizing interests of the shareholders, accountability and transparency are of importance. These two aspects were shared by the Hampel Report.¹⁴⁷ The Board of Directors (BoD) is entrusted with the application of the elements of corporate governance and, therefore, is accountable to shareholders.¹⁴⁸ Fairness, democracy and integrity of the Board constitute the elements of sound governance.¹⁴⁹ The BoD is responsible for leadership of the company and is responsible in front of the shareholders and stakeholders of the company as well.¹⁵⁰

This brief introduction about corporate governance will assist in looking at how ECAs apply the aforementioned elements of corporate governance.

Generally speaking, the structure of ECAs may differ from one agency to another; therefore, their governance may not be alike. Normally, if the agency is run by the government, its corporate governance would differ from a privately-ran agency. Similarly, a

¹⁴⁶ Sir Ronnie Hampel, *Committee on Corporate Governance: Final Report (Hampel Report on Corporate Governance)* (Gee Publishing 1998) Article 1(15)

¹⁴⁷ *ibid*, Article 1(1).

¹⁴⁸ *ibid*, Articles 2(1) & 1(19).

¹⁴⁹ Adrian Cadbury, *Report of the Committee on The Financial Aspects of Corporate Governance* (Gee and Co Ltd 1992). Article 3(3).

¹⁵⁰ Thomas Clarke, *International Corporate Governance: A Comparative Approach* (Routledge); under What do Boards do?.

privately-ran agency would have to follow certain rules and regulations in its governance if its shares are publicly traded.

The importance of discussing the aspects related to application of corporate governance in ECA serves to elaborate further the differences between ECAs. As there is no standard structure of ownership for these agencies, similarly, there is no standard governance for such agencies and the same applies for the services offered.

Euler Hermes is an example of a private PRI provider whose shares are traded in the stock markets. The governance of this agency, as it is the case with any corporation, is in the hands of its directors. These directors manage the agency to fulfill the goals of the shareholders.

To do so, there are independent executives, i.e. non-executive members that form, for example, the audit committee. Duties of the supervisory board of Euler Hermes are set out in the Charter and Internal Regulations Governing the Supervisory Board of Euler Hermes SA¹⁵¹, which can be highlighted as follows:

- Members should seek shareholders' interests and avoid conflict between their 'moral and material interest.'¹⁵² This reflects the element of accountability towards shareholders highlighted in the Hampel Report of 1998.

¹⁵¹ Information about Hermes can be found at:
<<http://www.eulerhermes.com/finance/corporate-govern-ance/Documents/Charter%20and%20internal%20regulations%20governing%20the%20Supervisory%20Board%20of%20Euler%20Hermes%20SA.pdf>>

Last accessed on the 21st of December 2013.

¹⁵² *ibid*, Articles 6 & 7.

- Members should undergo their duties with care, attention and integrity.¹⁵³ This constitutes the application of the integrity element mentioned in the Cadbury Report of 1992
- The duty of disclosing relevant information including any payments made, acquisitions or sale of property.¹⁵⁴ This is an application of the transparency element mentioned in the Cadbury Report of 1992.
- Prohibition of granting third parties information relevant to the company that would affect negatively on shareholders or those labeled insider trading.¹⁵⁵ This stems from the duty of the board to prioritize shareholders' interests.
- Each member of the board holds shares in the company. Though this is not what the element of democracy in corporate governance entails where employees of the company should hold shares, it is, however, a means to engage the board in achieving better decisions for the interest of the company and limiting the presence of conflict of interest.

Among the committees that are entrusted with monitoring the governance of the company is one responsible for Nomination and Remuneration. Another one is responsible for Audit and Risk.

¹⁵³ *ibid*, Articles 9.

¹⁵⁴ *ibid*, Articles 10.

¹⁵⁵ *ibid*, Articles 12.

The second model to examine is a the Ex-Im Bank of the United States of America. This agency is headed, as the case is with Euler Hermes, by a number of executives, according to its Charter and Bylaws.¹⁵⁶ There is a Board of Directors (BoD) that consists of five members who are all appointed by the U.S. President with the consent of the Senate.¹⁵⁷ Along with the board there is an audit committee responsible for aiding the BoD in fulfilling certain duties.¹⁵⁸

This board is responsible for, among other responsibilities, accounting and reporting duties.¹⁵⁹ They are responsible, along with the audit committee, for determining whether the Bank has sound administrative and financial controls or not. Both, the BoD and the audit committee have to review the financial statements prepared by management for the purpose of distribution to the Congress and the public, and for providing direction over the internal audit function and the external accountants.¹⁶⁰

After examining those two models, it can be safely concluded that due to the differences in the ownership of ECAs, corporate governance, in return, is affected. There are, however, common standards that a number of privately-operated and government-operated agencies follow.

¹⁵⁶ Bylaws and Charter of Ex-Im Bank of USA can be found at:
The Bylaws can be found at:
<<http://www.exim.gov/about/whoweare/charterbylaws/bylaws.cfm>>
Last accessed on the 21st of December 2013.

And;
The Charter can be found at:
<http://www.exim.gov/about/whoweare/charterbylaws/upload/Updated_2012_EXIM_Charter_August_2012_Final.pdf>

Last accessed on the 21st of December 2013.

¹⁵⁷ The Charter of the Export-Import Bank of the United States, Section 3(c)(1).

¹⁵⁸ *ibid*, Section 7.

¹⁵⁹ *ibid*.

¹⁶⁰ *ibid*.

They both, as the case is in the corporate context, have directors who overlook the operations of the ECA and seek the application of the shareholders of the agency.¹⁶¹ Above these directors there is a Chairman or a CEO who is a member of the BoD and is also the head of the BoD. Next to the board there are a number of auditors, internal and external, which help in the process of making the decisions made by the board be more transparent. There may, also, be a number of external directors. All of these members work together to ensure that decisions made are made in a manner that reflects the shareholders' interests.

Due to these differences in the governance of mentioned agencies, it is noted that the services of these two agencies are different from one another. Despite the fact the Euler Hermes, the private agency with headquarters in Paris, and the government-backed Ex-Im Bank of the U.S.A., are in two different countries but, generally speaking, ECAs backed by the government offer wider services that the private sector is unwilling to provide.

With that mentioned, it will be of help to take a couple of examples from a number of export credit agencies. A list of two export credit agencies from the U.S. and the services they offer will be present and another example from Germany will be presented as well.

In the United States of America there are two government-backed agencies. Ex-Im Bank and OPIC. Along those, Euler Hermes has presence in the U.S. offering a number of

¹⁶¹ N.B. The meaning of Shareholders in this context refers to the investors, when talking about publicly traded or privately-owned companies, and to the government as the operator of such agencies, in case such agencies are government-backed or operated by the government.

services. Starting with Ex-Im Bank, this bank offers a number of services for a diverse list of clients. There is a specialized division for U.S. small business exporters and financial institutions.¹⁶² They also offer products related to U.S environmental exporters, transportation security exporters and medical technology exporters.¹⁶³ The bank also provides services for U.S. exporters and lenders who are willing to invest in the African region. They also provide a number of services to exporters willing to invest in Brazil, Turkey, India, Mexico, Colombia, China, Vietnam, Nigeria, South Africa and Indonesia.¹⁶⁴ The Ex-Im Bank is interested in investors in the oil and gas and mining sectors as well as in the renewable energy and agribusiness sectors. Add to that aircraft and medical equipment and services sectors are among its area of interest. The bank also supports investors in power generation and related services and in the construction equipment and services.¹⁶⁵ It is worthwhile mentioning that the Bank covers against certain types of political risks that includes war and its services are provided on a short to medium term basis.¹⁶⁶

¹⁶² Information about Ex-Im Bank of USA regarding small business can be found at:

<<http://www.exim.gov/smallbusiness/>>

Last accessed the 21st of December 2013

¹⁶³ Services about Ex-Im Bank of USA's services can be found at:

<<http://www.exim.gov/about/whatwedo/specialinitiatives/environment/>>

Last accessed the 21st of December 2013

And;

<<http://www.exim.gov/about/whatwedo/specialinitiatives/medicaltechnologies/>>

Last accessed the 21st of December 2013

And;

<<http://www.exim.gov/about/whatwedo/specialinitiatives/medicaltechnologies/>>

Last accessed the 21st of December 2013

¹⁶⁴ More information about U.S. Ex-Im Bank is found at:

<<http://www.exim.gov/about/whatwedo/markets/index.cfm>>

Last accessed on the 21st of December 2013

¹⁶⁵ More information about U.S. Ex-Im Bank is found at:

<<http://www.exim.gov/about/whatwedo/keyindustries/>>

Last accessed the 21st of December 2013

¹⁶⁶ More information about U.S. Ex-Im Bank is found at:

<<http://www.exim.gov/products/exportercrreditinsurance/index.cfm>>

Last accessed the 21st of December 2013

As for OPIC, this agency offers to U.S. investors, willing to expand their investments into emerging markets, political risk insurance, guarantees, loans and support for investment funds.¹⁶⁷ The list of countries that this agency covers is more comprehensive than that of the Ex-Im Bank.¹⁶⁸ Though there is no specific requirement for the type of investment covered, it, nevertheless, offers its financial services on a medium- to long-term funding basis.¹⁶⁹ OPIC covers political risks, which, according to this agency, include acts of war, political violence and terrorism as well as expropriation and currency inconvertibility.¹⁷⁰ OPIC provides U.S. exporters investment funds support as well as provides support for small to medium sized companies who want to invest in developing countries in enterprise developing networks.¹⁷¹ OPIC reports its actions to the competent legislative body in the U.S and publishes annual reports as part of its disclosure and reporting obligations. Its stated mission is to mobilize and facilitate the U.S.'s private capital participation in the development in developing countries.¹⁷²

In comparison, Euler Hermes, unlike traditional ECAs and in its capacity as a private insurer, provides its services to all types and sizes of enterprises from the U.S and from other parts of the world rather than just to investors or enterprises which share the same

¹⁶⁷ More information about OPIC is found at:

<<http://www.opic.gov/what-we-offer/overview>>

Last accessed the 21st of December 2013

¹⁶⁸ The full list of countries covered by OPIC can be found at:

<<http://www.opic.gov/doing-business-us/OPIC-policies/where-we-operate>>

Last accessed on 21st December 2013

¹⁶⁹ For more information about services offered by Ex-Im Bank of the U.S.A.:

<<http://www.exim.gov/what-we-do/loan-guarantee>>

Last accessed on the 27th of February 2016.

¹⁷⁰ More information about OPIC can be found at:

<<http://www.opic.gov/what-we-offer/overview>>

Last accessed on the 21st of December 2013.

¹⁷¹ More information about services offered by OPIC can be found at:

<<http://www.opic.gov/what-we-offer/investment-funds>>

Last accessed on the 21st of December 2013.

And,

<<http://www.opic.gov/what-we-offer/enterprise-development-network>>

Last accessed on the 21st of December 2013.

¹⁷² Gordon (*Chapter 1, n32*) p 113.

domicile of the ECA. Though the list of services offered by Euler Hermes, in its capacity as a private insurer, is not as comprehensive as its predecessors, OPIC and Ex-Im Bank, it is able to present to a wider range of investors a number of services that the latter agencies do not offer. Euler Hermes offers investors debt collection services for example.¹⁷³

In Germany, there is a Federal export credit guarantees provided by Euler Hermes Deutschland AG and PwC. Both companies act on behalf of the Federal government of Germany in serving what is known as the Hermes Cover.¹⁷⁴ German banks and exporters are able to benefit from a range of services that cover political and commercial risks. As for political risk, this includes acts of war, civil unrest and revolution taking place in the host state. Add to that repatriation of capital and conversion rates of local currency of the host state.¹⁷⁵ With regard to commercial risk, this includes loss of receivables due to non-payment or bankruptcy of the buyer or any settlement happening before or after resorting to the legal system.¹⁷⁶ It is worth noting that services offered by the delegate of the Federal Government of Germany are available for private and public investors alike.¹⁷⁷

Going back to the products offered, they offer short-term, medium-term and long-term cover policies covering areas of manufacturing, project finance and trade finance cred-

¹⁷³ More information about Euler Hermes can be found at:

<<http://www.eulerhermes.us/international-debt-collection/Pages/default.aspx>>

Last accessed on the 21st of December 2013.

¹⁷⁴ This can be found on the following link:

<<http://www.agaportal.de/en/aga/index.html>>

Last accessed on the 21st of December 2013.

¹⁷⁵ More information about Export Credit Guarantees of the Federal Republic of Germany can be found at:

<http://www.agaportal.de/en/aga/grundzuege/gedeckte_risiken.html>

Last accessed on the 21st of December 2013

¹⁷⁶ *ibid.*

¹⁷⁷ *ibid.*

its.¹⁷⁸ They also cover export credits for exporters of services, construction works and offer airbus guarantees, ship financing, revolving supplier credit, framework credit, securitization guarantee and confiscation risk to name a few.¹⁷⁹ Euler Hermes is the leading partner providing these products and services.¹⁸⁰ It is not clear how this body is governed but it may be safely assumed that both companies, Euler Hermes and PwC, report to the Federal Ministry of Economy and energy. In a way, since Euler Hermes is a private company with shareholders, it has to report to its shareholders its activities along with its duty to report to the said federal ministry.

As per PwC, it is a company that has shareholders as well. For that, it has a duty to report to its shareholders. Along with that, it also has to report to the federal ministry. And as mentioned in section 5.2.3. of this chapter, the Hermes Cover is offered by the private sector on behalf of the German Federal Government. As for reporting and disclosure, PwC publishes annual reports and it only reports to the parliament to discuss the annual budget. Through PwC and Hermes, the German government supports activities of German investors abroad.¹⁸¹ As for a privately-healed PRI, Euler Hermes is present in Germany providing similar services to those it offers in the U.S.

In Canada, on the other hand, The Export Development Act of Canada stated that there is a BoD which is responsible for appointing overlooking and supervising the direction

¹⁷⁸ More information about Export Credit Guarantees of the Federal Republic of Germany can be found at: <http://www.agaportal.de/en/aga/grundzuege/deckungsformen.html>

Last accessed on the 21st of December 2013.

¹⁷⁹ More information about Export Credit Guarantees of the Federal Republic of Germany can be found at: <http://www.agaportal.de/en/aga/produkte.html>

Last accessed on the 21st of December 2013

¹⁸⁰ More information about Export Credit Guarantees of the Federal Republic of Germany can be found at: <http://www.agaportal.de/en/aga/index.html>

Last accessed on the 21st of December 2013

¹⁸¹ Kathryn Gordon, *Investment Guarantees and Political Risk Insurance: Institutions, Incentives and Development* (Organization for Economic Co-operation and Development (OECD) 2008) p 112.

of the management.¹⁸² The Board is responsible for the election of the Vice-chairperson who is chosen from amongst them.¹⁸³ As for the Board members' appointment, it is delegated to the Government of Canada and reports to the Canadian Parliament through the minister of International Trade. On the other hand, all thirteen of the corporation's directors are appointed for a 4-year term by the Governor in Council except for the Chairperson and the President who is appointed for a period deemed appropriate by the Governor in Council.¹⁸⁴ This may be regarded, primarily, to the fact that, though, it is self-sufficient, it is, however, owned by the Canadian Government.¹⁸⁵ The Act also encouraged the formation of an Executive Committee that is composed of four directors and a Chairperson elected by the BoD to perform duties delegated to it by the said board.¹⁸⁶ Finally, auditing duties of the corporation are delegated to the Auditor General of Canada.¹⁸⁷ As far as disclosure and reporting, the EDC, as an agency, publishes annual reports and it reports to the parliament. EDC's mission is to support and develop Ca-

¹⁸² More information about EDC is available at:

<<http://www.edc.ca/EN/About-Us/Management-and-Governance/Pages/default.aspx#sthash.cgpk0sgV.dpuf>>
Last accessed on the 20th of January 2014.

And;

<<http://www.edc.ca/EN/About-Us/Management-and-Governance/Pages/default.aspx>>
Last accessed on the 20th of January 2014.

¹⁸³ Canada's Export Development Act of 1985. Purpose and Powers Art. 4(3).
Available on the following link:

<<http://laws.justice.gc.ca/eng/acts/E-20/>>
Last accessed on the 20th of January 2014.

¹⁸⁴ Canada's Export Development Act of 1985. Purpose and Powers Art. 4(1)&(2) and Art 8(1).
Available on the following link:

<<http://laws.justice.gc.ca/eng/acts/E-20/>>
Last accessed on the 20th of January 2014.

¹⁸⁵ More information about Canada's EDC is available at:

<<http://www.edc.ca/EN/About-Us/Corporate-Social-Responsibility/Pages/default.aspx>>
Last accessed on the 20th of January 2014.

And;

<<http://www.edc.ca/EN/About-Us/Pages/default.aspx>>
Last accessed on 20th January 2014.

¹⁸⁶ Canada's Export Development Act of 1985. Purpose and Powers Art. 7(1) & (2).
Available on the following link:

<<http://laws.justice.gc.ca/eng/acts/E-20/>>
Last accessed on the 20th of January 2014.

¹⁸⁷ Canada's Export Development Act of 1985. Purpose and Powers Art. 21(1).
Available on the following link:

<<http://laws.justice.gc.ca/eng/acts/E-20/>>
Last accessed on the 20th of January 2014.

nadian investments abroad.¹⁸⁸ It is worth mentioning that this Governmental Corporation applies the aspects of transparency and social responsibility through sharing information about their operations with the public. They do also encourage investors using their services to be socially responsible.¹⁸⁹

In Italy, The BoD of SACE is made up of three members and a chairperson who supervises management's decisions and makes sure they fall within the plans of the company.¹⁹⁰ It is noted that members of this company are appointed by the Ministry of Economy and Finance.¹⁹¹ This may be traced to the fact that the Italian government is responsible for paying the dividends of the company.¹⁹² It can be assumed that this company enjoys a similar status to the one present in Canada since both are independent institutions in terms of ownership, but members of both agencies are appointed by the authorities and both enjoy monetary incentives from the government. Since it is also not clear whether the Italian ECA applies aspects of corporate governance, it can be assumed that, since this company is a joint stock one, it is, therefore, assumed that it complies with

¹⁸⁸ Gordon (n 29) p 112.

¹⁸⁹ More information about EDC is available at the following links:

<<http://www.edc.ca/EN/About-Us/Disclosure/Pages/default.aspx>>

Last accessed on the 20th of January 2014.

And;

<<http://www.edc.ca/EN/About-Us/Corporate-Social-Responsibility/Documents/corporate-social%20responsibility-brochure.pdf>>

Last accessed on the 20th of January 2014.

And;

<<http://www.edc.ca/EN/About-Us/Disclosure/Documents/disclosure-policy.pdf>>

Last accessed on the 20th of January 2014.

¹⁹⁰ Articles of Association of SACE S.p.A. Art. 13(1).

Available on the following link:

<http://www.sace.it/GruppoSACE/export/sites/default/download/normativa/Articles_of_Association_23_05_2013_EN.pdf>

Last accessed on the 20th of January 2014.

¹⁹¹ More information about SACE is available under '3. Ownership' at the following link:

<http://www.sace.it/GruppoSACE/content/download/normativa/InfoMemo_SACE-EN.pdf>

Last accessed on the 20th of January 2014.

¹⁹² More information about SACE is available under '3. Ownership' at the following link:

<http://www.sace.it/GruppoSACE/content/download/normativa/InfoMemo_SACE-EN.pdf>

Last accessed on the 20th of January 2014.

regulations related to transparency and disclosure of its information. These findings can be traced to the fact that the SACE is wholly-owned by the Cassa Depositi e Prestiti Company. This later, as examined earlier, is a publicly-held corporation with the majority of its shares owned by the Italian Government and minority shares having been held by both the Treasury and a number of banking foundations.¹⁹³ Same rules are assumed in the case of SIMEST since 76% of its shares are also owned by the Casa Depositi e Prestiti. It is worth mentioning that as far as disclosure and reporting are concerned, SACE publishes annual reports and reports to the parliament. SACE's mission is to support the internationalization of Italian economy.¹⁹⁴

Finally, in Spain, the Compañía Española de Seguros de Credito a la Exportacion, CESCE, which is also a founding member of the Berne Union, has half of its board members, being government representatives.¹⁹⁵ This may be traced to the fact that the government's investment comprises of majority holding. Its stated objective is to facilitate investments in foreign markets.

Based on the above mentioned, ECAs in general, no matter if they are public, private or a department of the government, have governing bodies to supervise their actions. These supervisory bodies may be the BoD, the supervisory board or the management board. They are all committed to disclosure of information, though disclosure itself and the amount of information disclosed may differ from one agency to another. It is clear that

¹⁹³ More information about Casa Depositi e Prestiti can be found at the following link: <<http://www.cassaddpp.it/en/company-profile/mission-and-role/mission-and-role.html>> Last accessed on the 20th of January 2014.

¹⁹⁴ Kathryn Gordon, *Investment Guarantees and Political Risk Insurance: Institutions, Incentives and Development* (Organization for Economic Co-operation and Development (OECD) 2008) p 112.

¹⁹⁵ Cremades (*Chapter 3, n37*) p 336.

difference in ownership of ECAs does not necessarily have an effect on aspects related to their corporate governance. Each type has the obligation to report to their respective higher authorities and, therefore, responsible for their actions and decisions. The reason behind that is that ECAs offer sensitive products. It is noted, nevertheless, that most agencies disclose information related to environmental matters. Despite these differences in governance, a significant amount of them share the same mission. They provide their services with the mission to enhance the host state's economic performance and to fill the gap present due to failure of the private sectors to cover some types of risks.¹⁹⁶

As it has been discussed, the most important aspect of corporate governance, i.e. transparency, is shown in state-owned corporations, as is the case with the EDC since its code of conduct clearly states the duty the corporation has with regards to transparency. It is also present in agencies emanating from the government, such as the UKEF, since this agency reports directly to the Department of Business, Innovation and Skills (reporting to both the minister of State for Trade and Investment and the Secretary of State for Business, Innovations and Skills). Comparable rules apply in the U.S. in the case of Ex-Im Bank and OPIC. On the other hand, in the Case of Germany, it is assumed that since the offering of export credit products and services is delegated to two private companies, these companies report to their shareholders and to the government alike. Finally, in Italy the two companies offering export credit services are owned by the same owner which, in return is owned by both the public and private sectors. In this case these two

¹⁹⁶ Gordon (*Chapter 1, n32*) p 96.

companies report directly to their mother company, which in return, reports to its public and private sector shareholders.¹⁹⁷

As for the accountability aspect of corporate governance, the same justification applies. The importance of application of corporate governance theories is of special importance in the private and public companies where there should be proper management and disclosure since there are private investors involved in the ownership of the company. Unlike the case where the insurance provider is the state, there are provisions for disclosure and reporting as well as management to ensure that the services offered are proper and granted upon meeting the condition set forth and to ensure that funds of the state are properly managed.

4.4. Services Offered By MIGA, World Bank, Insurance Companies and Development Finance Institutions

Development Finance Institutions have been playing a role in foreign investments along with ECAs and MIGA. For example, CDC Capital partners is a UK based company which offers services to potential investors. The CDC is a publicly-traded company whose shares are solely owned by the UK government.¹⁹⁸ The company's services are

¹⁹⁷ N.B. both SACE and SIMEST report to the Casa Depositi e Prestiti. Along with reporting to this investment bank, SIMEST reports to its other shareholders and the Casa Depositi e Prestiti reports to its shareholders, which include a range of private banks and the Italian government.

¹⁹⁸ This information can be found at:

<<http://www.cdcgroup.com/Who-we-are/Corporate-structure/>>

Last accessed on the 19th of December 2013

focused on supporting investments in, primarily, two markets. These are the South Asian and the African markets.¹⁹⁹

The World Bank is considered as a Multilateral Development Finance Institution. Though it does not provide any guarantee or insurance against risks encountered by foreign investors like ECAs do, they, nevertheless, provide project-financing services to investors.²⁰⁰ They do, however, provide coverage against political risk through its risk guarantee services. The main difference between such guarantee and that of an ECA is that the one offered by ECAs is granted to exporters of goods or services whereas the one offered by World Bank is provided to support infrastructure projects.²⁰¹ The coverage in this type of guarantee is related to the failure of government performance, which could be considered as a political commercial risk, and it covers, as well, against a number of political risks that include expropriation, change of law and obstruction of arbitration process.²⁰² The guarantee policy offered by the World Bank also covers against some aspects of financial risks that include foreign currency convertibility and availability.²⁰³

Since its creation in 1988, MIGA's primary purpose has been to encourage the flow of investment in developing states and it helped in filling the gap left by national insurance

¹⁹⁹ This information can be found at:
<<http://www.cdcgroup.com/What-we-do/Our-Mission/>>
Last Accessed on the 19th of December 2013.

²⁰⁰ Yescombe (n 189) p 462.

²⁰¹ For more information on the World Bank products and services please visit:
<<http://www.worldbank.org/en/projects-operations/products-and-services>>
Last accessed on the 26th of February 2016.

²⁰² This Information can be found at:
<<http://web.worldbank.org/external/default/main?theSitePK=3985219&pagePK=64143534&contentMDK=20260268&menuPK=64143504&piPK=64143448>>

Last accessed on the 19th of May 2015.

²⁰³ *ibid.*

program.²⁰⁴ At times, MIGA which, is a member at the Berne Union, may decide to co-guaranty an investment with a national insurance provider.²⁰⁵ MIGA has its own financial autonomy and it offers its insurance services independent of any involvement from other World Bank members but, it does, however, cooperate closely with the International Bank for Reconstruction and Development, with the International Development Association, with the International Finance Corporation and with the International Centre for Settlement of Investment Disputes which are all part of the World Bank Group.²⁰⁶ This agency is an affiliate of the World Bank and it covers against political risk which includes, according to MIGA, currency inconvertibility, expropriation, war, terrorism, civil disturbances and against breach of contractual obligations and non-honoring of financial obligations.²⁰⁷

MIGA also provides its services to investors from developing countries who do not have their own national insurance program.²⁰⁸ It covers against currency transfer risks due to the host states intervention and it includes applying measures restricting the investor from transferring his earnings or from converting these earnings into another currency but it excludes freezing of the accounts of the investor by the host state.²⁰⁹ Investors, who wish to be compensated, in this case, might need to transfer their rights to the local

²⁰⁴ Rubins and Kinsella (*Chapter 2, n65*) p 99.

²⁰⁵ *ibid* at 99-100.

²⁰⁶ Information found at:

<<https://www.miga.org/who-we-are/frequently-asked-questions>>

Last accessed on the 2nd of January 2017.

²⁰⁷ Information can be found at:

<<http://www.miga.org/documents/IGGenglish.pdf>>

Last accessed on the 19th of May 2015.

²⁰⁸ Rubins and Kinsella (*Chapter 2, n65*) at 100.

²⁰⁹ Ibrahim FI Shihata, *MIGA and Foreign Investment: Origins, Operations, Policies, and Basic Documents of the Multilateral Investment Guarantee Agency* (Martinus Nijhoff 1988) p 123 -124.

N.B. The full list of MIGA member states is available in Appendix II.

currency to MIGA.²¹⁰ In addition, MIGA guarantees against expropriation, breach of contract and against war and civil disturbances.²¹¹ Expropriation, to MIGA, is an act taken by the host state against an investor with the purpose of taking the investor's property through actions like nationalization.²¹² The political risk coverage offered by MIGA includes measures of expropriation, nationalization, confiscation, sequestration, attachment and freezing of assets and seizure but it is not limited to those acts.²¹³ It includes, as well, cases where the host state, for example, refuses to grant a license, agreed on under an investment contract, to an investor if it was proven that such action caused a direct loss to the investor.²¹⁴ Another service that MIGA offers is mediation where, through this service, the agency aims to avoid any potential claims and to reduce any tension between an investor and the host state.²¹⁵

To MIGA, in order to cover against political risk, the risk needs to be assessable and quantifiable and it should be an unpredictable risk which threatens a number of investors.²¹⁶

In cases of civil disturbances or war, MIGA's coverage only includes the cases where the investment project was removed, damaged, encountered substantial loss or was destroyed or even suffered from any substantial interference within its operations.²¹⁷ It does not, however cover against losses or reduction in the investment's operations.²¹⁸ To

²¹⁰ *ibid* at 124.

²¹¹ *ibid* at 124 – 138.

²¹² *ibid* at 124.

²¹³ *ibid* at 125

²¹⁴ *ibid*

²¹⁵ Gordon (n 29) p 102.

²¹⁶ *ibid* at 93.

²¹⁷ Shihata (*Chapter 4, n209*) at 136

²¹⁸ Shihata (*Chapter 4, n209*) at 136

MIGA, civil disturbances includes organized violence against the government of the host state and includes riots and civil commotion directed against the host state's government as well.²¹⁹

Currency transfer risks and breach of contract risks are also covered by MIGA where according to article 11 of the Convention establishing MIGA, they should occur as a result of the host state's action. This means that the host state needs to breach the contract binding it with an investor or that the host state's government took measures depriving investors from, or making it difficult for investors to, transfer the proceeds of their investments into another currency or back to his home state.²²⁰

There is, however, a special cover offered by MIGA and not widely offered by ECAs; this is known as the Contractual Direct Investment Cover and this covers production, licensing agreement, franchising agreement, profit sharing contracts, turnkey contracts, subordinated debentures issued by the project interpose and, finally, operating leasing agreement.²²¹ In addition, one of the tools that foreign investors resorted to in order to protect their property rights, and available through MIGA, was the introduction of a Stability Clause in their contracts with the host state government. Such clause is meant to refrain and forbid the host state's government from changing the laws governing an investment into a less favorable ones. MIGA offers coverage against the breach of contract risk and offers coverage, specifically, against such action taken by the host state.²²²

²¹⁹ Shihata (*Chapter 4, n209*) at 125

²²⁰ Convention Establishing the Multilateral Investment Guarantee Agency (MIGA Convention 1985) Chapter III, Article 11

²²¹ Shihata (*Chapter 4, n209*) p 114.

²²² *ibid* at 131

According to MIGA, in articles 12, 13 and 14, in order to benefit from its services and be eligible to apply for coverage against the risks covered by MIGA, investors need to be national of a member state, but not of the host state, and, in case of a judicial person, have their principal place of business at a member state or having majority of the judicial person's capital owned by a national of a member state and, the investment needs to be made in a developing member state.²²³

One of the main differences between the services offered by ECAs and other political risk insurers and that of MIGA's is that MIGA offers mediation services. The agency mediates between the host state and the investor prior to any political insurance claim.²²⁴

Basically, both MIGA and ECAs, offer guarantee and insurance against a range of risks from expropriation, nationalization, breach of contract, change of investment-related measures and laws, creeping expropriation or *de facto* expropriation, to restrictions on the exchange of currency and restrictions on remittance. They both offer financing services such as long-term, short-term, or medium-term financing and they offer, as well, what is known as export credit financing.²²⁵

²²³ Convention Establishing the Multilateral Investment Guarantee Agency (1985) Articles 12, 13 & 14. Article 12 of the Convention Establishing the Multilateral Investment Guarantee Agency is concerned with investments that may be covered by MIGA. Article 13 of the Convention Establishing the Multilateral Investment Guarantee Agency is concerned with the nationality of the investor and his eligibility. Article 14 of the Convention Establishing the Multilateral Investment Guarantee Agency is concerned with the Host State itself.

²²⁴ *Approached to Enterprise Risk Management* (Bloomsbury 2010) p 146.

²²⁵ This was the result of examining various services offered by ECAs and services offered by MIGA.

MIGA coordinates with the private sector and ECAs in a given home state and in that respect they both act as insurers of the last resort.²²⁶ This means that investors and exporters are expected to seek guarantee and insurance or financing from their home state where they should first resort to the private sector and in case the product or service was not provided by the private sector or in case the private sector refused to grant such product or service, investors may, then, resort to the ECA of his home state.²²⁷ If this ECA fails to accommodate investors' needs and if investors were unable to find the product or service they are seeking through the official ECA or in case their home state had no ECA, then, and only then, they may resort to MIGA. In that respect MIGA's role can be considered as a complementary role to that of national agencies.²²⁸

Private insurance companies, in general cover against currency inconvertibility and transfer restrictions. Some cover against similar risks that export credit agencies cover against. For example, insurance companies may cover against confiscation, nationalization and acts of expropriation as well as against political violence and defaults on contracts or on arbitral claims or loans.²²⁹ This is the case, for example, with the Corporation of Lloyd's of London where Lloyd's offers insurance against political risk.²³⁰ Unlike Lloyd's of London, and even though they are considered private sector companies, the American Insurance Group (AIG) and the Zurich Insurance Company are both members at the Berne Union.

²²⁶ For more information on MIGA's cooperation with the private and public sectors please visit:

<<https://www.miga.org/who-we-are/frequently-asked-questions/>>

Last accessed on the 26th of February 2016.

²²⁷ Gordon (*Chapter 1, n32*) p 104.

²²⁸ *Approaches to Enterprise Risk Management (Chapter 4, n224)* p 146.

²²⁹ Gordon (*Chapter 1, n32*) p 103.

²³⁰ This information about Lloyd's of London can be found at:

<http://www.lloyds.com/redirect-pages/risk_locator/political_risks_insurance>

Last accessed on the 18th of May 2015

Another difference between ECAs and insurance companies is that ECAs offer their political risk coverage to investments invested in countries labeled high risk more than insurance companies do in such countries.²³¹ However, the private sector may offer what is known as a ‘bridging cover’ to investors who are seeking services offered by ECAs if the procedures to acquire such services by ECAs will take long time.²³²

On the other hand, Development Finance Institutions (DFI) are institutions that give, in general, united loans and political risk insurance to any exporter. These types of institutions work with local ECAs and they are either a bilateral or a multilateral effort.²³³ The German DEG or the Deutsche Investitions- und Entwicklungsgesellschaft is a bilateral Development Finance Institution that promotes development of emerging markets through financing direct investments or by providing long-term investment capital for example.²³⁴ Since the services offered by DFIs do not include insurance or guarantees against any of the risks encountered by foreign investors, the research will not elaborate more on their nature and their services.

As for private insurance companies, Euler Hermes, for example, in its capacity as a private sector insurer, offers, along with its traditional insurance services, what is known as credit insurance where it covers against, as it stated, commercial and political risks that

²³¹ Yescombe (*Chapter 2, n184*) p 311.

²³² *ibid* at 311.

²³³ Gordon (*Chapter 1, n32*) p 444.

²³⁴ This information can be found at:

<<https://www.deginvest.de/International-financing/DEG/Die-DEG/Was-wir-tun/>>
Last accessed on the 19th of May 2015.

are beyond investors' control.²³⁵ However, it is not clear what is considered as commercial or political risk according to Euler Hermes. The company also offers coverage against political risk through a product called the political risk insurance. This product covers against confiscation, expropriation and nationalization of foreign investors' property.²³⁶

It is worth noting that the private sector was more attentive to cover against new risks emerging, such as the cyber-risk. In that respect, some private sector companies, like Hiscox, were able to offer insurance services covering various aspects of cyber-risk.²³⁷ Hiscox, one of the biggest insurance companies in the world and an official ECA for Bermuda, offers cyber-risk insurance known as E-Risk Insurance. Such insurance covers, according to Hiscox, against damages caused by viruses and by hackers. It also covers against any infringement to intellectual property rights of the insured investors and against online identity fraud.²³⁸ This coverage extends to all E-mails, websites and all internet-related marketing means used to market the covered investment.²³⁹ In addition, Lloyd's of London, Zurich and AIG are among the providers of cyber risk insurance.²⁴⁰

²³⁵ This information Euler Hermes can be found at:
<<http://www.eulerhermes.co.uk/credit-insurance/Pages/default.aspx>>
Last accessed on the 27th of May 2015

²³⁶ This information on Euler Hermes can be found at:
<<http://www.eulerhermes.com/products-solutions/multinationals/Pages/political-risk-insurance.aspx>>
Last accessed on the 27th of May 2015

²³⁷ For more information on Hiscox Cyber Risk Insurance please visit:
<<https://www.hiscox.co.uk/business-insurance/cyber-and-data-insurance/>>
Last accessed on the 26th of February 2016.

²³⁸ This information on Hiscox can be found at:
<<https://www.hiscox.co.uk/business-insurance/e-risks-insurance/cover-information/>>
Last accessed on the 25th of August 2015

²³⁹ This information on Hiscox can be found at:
<<https://www.hiscox.co.uk/shared-documents/Hiscox-Business-Insurance-E-risks-policy-wording-03-11-6076.pdf>>

Last accessed on the 25th of August 2015

²⁴⁰ This information Lloyd's of London, Zurich Insurance Group, and AIG can be found at:

On the other hand, Marsh, an insurance broker and risk management company, offers cyber-risk management services.²⁴¹ Cyber-risk management and governance services offer a risk and recovery planning services where such firms may help investors to consider their sources of cash, to seek alternative supply and to convey the message they intend to disclose to the stakeholders to name a few.²⁴² In the field of cyber risk insurance, London is considered a major centre for cyber insurance.²⁴³

Some insurance companies like AIG and Lloyd's of London are considering offering insurance and coverage against Solar Storms. Such cover may come as a complementary coverage to cyber risk insurance since solar storms are thought to have direct effect on adopted technologies.²⁴⁴ Not only that, some had even gone further than just offering insurance to cover classical risks on a yield bases. For example, Lloyd's of London offers insurance against weather designed for investors in the Agribusiness.²⁴⁵

<<https://www.lloyds.com/news-and-insight/news-and-features/emerging-risk/emerging-risk-2015/a-quick-guide-to-cyber-risk>>

Last accessed on the 25th of August 2015

And;

<https://www.zurich.ch/en/corporate-customers/insurance-of-assets/cyber-security-and-privacy>

Last accessed on the 25th of August 2015

And;

http://www.aig.com/CyberEdge_3171_417963.html

Last accessed on the 25th of August 2015

²⁴¹ This Information on Marsh can be found at:

<https://www.marsh.com/us/services/cyber-risk.html>

Last Accessed on the 25th of August 2015

²⁴² *UK Cyber Security: The Role of Insurance in Managing and Mitigating the Risk* (HM Government and Marsh 2015) p 15.

This document can be found at:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/415354/UK_Cyber_Security_Report_Final.pdf>

Last accessed on the 25th of August 2015

²⁴³ *ibid* at 7.

²⁴⁴ This Information can be found at:

<<https://www.lloyds.com/news-and-insight/news-and-features/emerging-risk/emerging-risk-2013/insuring-the-unknown>>

Last accessed on 23rd September 2015.

²⁴⁵ This Information on Lloyd's of London can be found at:

<<https://www.lloyds.com/news-and-insight/news-and-features/emerging-risk/emerging-risk-2013/weather-based->

One of the private sector Big Five company, Lloyd's of London, offer political risk insurance that covers war, terrorism, riots, strikes, civil commotion and malicious damage, inconvertibility of foreign currency, confiscation, import and export embargo as well as political commercial risks related to contractual obligations or cancellation of license.²⁴⁶

Generally speaking, the private sector's coverage against political risk is similar to that offered by ECAs the only difference being that coverage of acts of war or political violence in the private sector does not include cases where the home state and host state are at war with one another.²⁴⁷ It shall be noted that the private sector divides political risk into two major categories; asset coverage which, includes confiscation and any act of expropriation, and, contract coverage, which includes loss from contract repudiation due to acts of political violence cancellation or any issues with currency convertibility.²⁴⁸

Insurance companies have a slight upper hand when it comes to their attentiveness to new risks faced by investors where they are able to offer services enabling perspective clients to benefit from wider coverage against emerging new risks. This is, for example, true when it comes to covering against cyber-risk. The high demand on coverage against the emergence of new risks faced by investors also plays a role in offering coverage against these risks.

[insurance-for-farmers](#)>

Last accessed on the 23rd of September 2015

²⁴⁶ This Information on Lloyd's of London can be found at:

<http://www.lloyds.com/redirect-pages/risk_locator/political_risks_insurance>

Last accessed on the 27th of May 2015.

²⁴⁷ Rubins and Kinsella (*Chapter 1, n65*) p 110.

²⁴⁸ *ibid*

Basically, investors may be subjected to a group of risks in a given host state while, doing the same investment in another host state, they may be subjected to only one risk. Depending on that, investors may choose to seek certain services offered by an ECA, MIGA or by an insurance company or a combination of services some offered by an insurance company and others offered by MIGA or by an ECA.

An advantage of resorting to the private sector's guarantee and insurance services is that it can be customized to suit the needs of investors and the time frame of negotiations, in that respect, is relatively shorter whereas the main advantage of resorting to ECAs means a less expensive product or services compared to that offered by insurance companies and means that the investor may benefit from a longer-term coverage than that offered by the private sector. Not only that but it has been noticed that some ECAs offer better services with regard to coverage against currency inconvertibility than those offered by insurance companies.²⁴⁹ Another possible advantage of seeking the services of a publicly-sponsored insurance providers or ECA is that, in case of expropriation, reaching an acceptable settlement is much higher and more probable and that's something that investors are attracted to. Add to that, the fact that ECAs operated by the government have a competitive edge over other companies where dealings take place on the basis of state-to-state.

In the EU, there is the Euro- Mediterranean Investment and Partnership (FEMIP) offer services considered similar to those offered by ECAs.²⁵⁰ Though this is not an official

²⁴⁹ This was concluded after analysing services offered by ECAs and comparing them to those offered by insurance companies.

²⁵⁰ Regulation (EC) No 1638/2006 of the European Parliament and of the Council of 24 October 2006 laying down general provisions establishing a European Neighborhood and Partnership Instrument, OJ L310, 9.11.2006.

EU ECA, it does however have the same objective. It offers, for example, investment guarantees in an attempt to promote investment in the host state, which is also the same aim behind the establishment of ECAs.²⁵¹

At the end of this chapter, Table C covers ECAs membership at the Berne Union and the Prague Club while Table D elaborates on the different types of risks covered by ECAs, the MIGA and insurance companies and Table E describes to whom the services of such agencies are offered and, finally, Table F offers an insight on the cover limit offered by a number of ECAs, MIGA and insurance companies.²⁵²

4.5. Conclusion

The need for extra protection against risks encountered abroad by investors was one of the main reasons behind the creation of ECAs. They were created by home states' governments to encourage the exporting of goods and to fill in the gap existing in mitigating investment risks and trade finance.²⁵³ After their creation for the first time in Switzerland in 1906 as a private entity, the U.K followed the footsteps of Switzerland and adopted the same concept and established an agency owned by the Government. It was thought that having a governmental-backed agency will provide investors with more trust in the

²⁵¹ Dimopoulos (*Chapter 2, n187*) p 16.

²⁵² Table C at p 279.

Table D at p 280.

Table E at p 281.

Table F at p 282.

²⁵³ Stephens (*Chapter 1, n9*) p xi and 1.

And;

Wang, Kikuchi, Choudhury, Mansilla (*Chapter 4, n3*) p 25.

sense that dealings will not be on the basis of private sector to host state, rather it would be on the basis of home state-to-host state negotiations. In that respect, many exporting countries adopted the idea of ECAs. Not all these agencies share the same ownership structure.

Investor may, mainly, seek the services of an ECA once the service they are require is not offered by the private sector. Not only that, investors may also seek, if they are a national of one of the member states and if they were not able to find the services they require through the private sector or through their national ECAs, the services of MIGA. MIGA, which was established by the World Bank, is thought to have a role that complements the role of national ECAs as well as that of private insurance companies in the same way that ECAs complements the private sector.

ECAs and MIGA play a complementary role to IIAs where IIAs are the starting point for promotion and protection of foreign investments, and, at the same time, it draws the borderline for such protection and defines what falls under its umbrella. ECAs then steps in to add an extra layer of security protect investors against a set of risks that includes pure political risks, political commercial risk, political financial risk and certain aspects of commercial risks. These products and services offered by ECAs complement the protection drawn in IIAs.

The question arises as to why the private sector has become more involved in such types of investment guarantees and insurance especially since the risks covered are higher than that the private sector normally agrees to cover?

The private sector's involvement in the protection of such risks may be the result of the private sector's observation of the profitability that the public sector has been gaining from providing such support. It may also be due to the failure of the public sector to cover specific types of new emerging risks due to the lack of attentiveness of the public sector to the changing nature of risk and due to the public sector's reliance on the private sector to offer a more general insurance coverage to investors. Through allowing the private sector to be more involved in providing such support, together with the fact that the private sector is becoming more interested in providing these products, whether solely or through partnering with the public sector or even through owning minimal shares in specific agencies with the public sector that offer such products or services, gives investors a wider range of choices to suit their investment and their desired location.

Though many private sector insurance companies may offer political risk insurance, such support, however is not as comprehensive as those offered by national programs, i.e. ECAs. Nevertheless, there is an exception to this rule, which is the case Lloyd's of London Corporation. Lloyd's offers a political risk insurance that covers aspects that are covered by national ECAs. It covers against terrorism, war and political unrest in general and against expropriation, currency transfer and inconvertibility risks as well as against a number of political contractual risks.²⁵⁴ These are exactly the same products offered by national ECAs. However, it shall be noted that ECAs operated by the government have a competitive edge over other companies where dealings are on the basis of government-to-government relationship.

²⁵⁴ For more information about Lloyd's Political Risk Insurance please visit:
<<https://www.lloyds.com/the-market/tools-and-resources/tools-e-services/risk-locator/risk-locator-class-of-business/political-risk>>
Last accessed on the 27th of February 2016.

In order to enhance their role and provide better services in the continuously developing sector of political risk insurance and export credit guarantees, there are, nowadays, a number of organizations and recommendations that govern the behavior of ECAs. Such movements include the Berne Union, the Paris Club, the Prague Club, the OECD ECG and the Arrangement on Guidelines for Officially Supported Export Credits of the OECD to name a few.

Generally, services offered by ECAs may differ from one country to another and from one ECA to another in the same country. They may offer their services to exporters willing to invest in certain sectors or in certain countries or they may offer their services to any exporter investing in any location. Not only that but the ownership structure of ECAs is not always the same where some states may have a governmental ECAs while others may have a private one or even a hybrid of both. They also may have different governance structure, which is primarily the effect of the ownership structure of such agencies. They might provide insurance, guarantees or lending services or even do both. They could provide export credit insurance, investment insurance or both. They may additionally cover against political, financial or commercial risks or combination of the mentioned risks. And finally, they may be referred to as ECAs, Ex-Im Bank or an insurer.²⁵⁵

²⁵⁵ Stephens (n 27). p 7

For a company to be referred to as an ECA, it should provide a combination of export credit guarantee, insurance and loan services to exporters or investors who share the same nationality and in the name of the home state's government whereas an insurance company and/or an investment bank can provide similar services, under their own name, to those of ECAs to any investor who wishes to carry their business abroad.

Country	Agency	Berne Union (ECAs)	Prague Club (ECAs)
Canada	EDC	Yes	No
France	COFACE	Yes	No
Germany	Euler Hermes & PwC	<ul style="list-style-type: none"> • Hermes: Yes • PwC: Yes 	<ul style="list-style-type: none"> • Hermes: No • PwC: No
Italy	SACE	Yes	No
Multinational	MIGA	Yes	No
Spain	CESCE	Yes	No
Switzerland	Zurich	Yes	No
United Kingdom	UKEF	Yes	No
United Kingdom	Lloyd's	No	No
United States of America	AIG	Yes	No
United States of America	Ex-Im Bank	Yes	No
United States of America	OPIC	Yes	No

Table C (Berne Union and Prague Club Membership)

Agency	Ownership Status	Political Financial Risks (Currency Inconvertibility and Transfer and Remittance Risks)	Expropriation and Nationalization	Political Violence	Political Commercial Risk (Breach of Contract by Host State)	Terrorism
AIG	Private	Yes	Yes	Yes	Yes	Yes
CESCE	Quasi-Governmental	Yes	Yes	Yes	Yes	Yes
COFACE	Private	Yes	Yes	Yes	Yes	Yes
UKEF	Governmental	Yes	Yes	Yes	Yes	No
EDC Canada	Governmental	Yes	Yes	Yes	Yes	Yes
Euler Hermes	1.Private. 2.Offers services with PwC German Government.	Under its own name: Only political risk is covered On behalf of the German Government: Yes	Under its own name: Yes On behalf of the German Government: Yes	Under its own name: Yes On behalf of the German Government: Yes	Under its own name: only political risk is covered On behalf of the German Government: Yes	Under its own name: No On behalf of the German Government: Yes
Lloyd's of London	Private	Yes	Yes	Yes	Yes	Yes
MIGA	Multilateral Agency	Yes	Yes	Yes	Yes	Yes
OPIC	Governmental	Yes	Yes	Yes	Yes	Yes
SACE	Privately owned by a Quasi-Governmental agency (Casa Depositi e Prestiti S.p.A)	Yes	Yes	Yes	Yes	Yes
U.S Ex-Im Bank	Governmental	Yes	No	Yes	No	Yes
Zurich	Private	Yes	Yes	Yes	No	No

Table D (Risks Covered)

Agency	National Clients	Foreign Clients
AIG	Yes	Yes
CESCE	Yes	No
COFACE	Yes	Yes as long as they are exporting from France
UKEF	Yes	No
EDC Canada	Yes	Yes as long as it provides economic benefit to Canada
Euler Hermes	When offering services as a Private Company: Yes When offering services on behalf of the German Federal Government with PwC: Yes	When offering services as a Private Company: Yes When offering services on behalf of the German Federal Government with PwC: No
Lloyd's of London	Yes	Yes
MIGA	Yes (Nationals of member States)	If they are incorporated and have their principal place of business in a member State or if they are majority-owned by nationals of member States
OPIC	Yes	No
SACE	Yes	Yes (to foreign companies controlled by Italian Investors)
U.S. Ex-Im Bank	Yes Available for Small Business	Not clear. It states that it offers its services to reporters exporting U.S. made products and/or services provided by U.S. workers.
Zurich	Yes	Yes

Table E (National & Foreign Investor Support)

Agency	Insurance Limit
AIG	Up to 95% of the value of the Guarantee
CESCE	Up to 99%
COFACE	Up to 95%
UKEF	Up to 95% for Export Insurance Policy Up to 90% of losses for Overseas Investment Insurance Policy
EDC Canada	Up to 90%
Euler Hermes	<p>1. On behalf of the German Federal Government:</p> <ul style="list-style-type: none"> • Up to 95% for single transaction and revolving Political Risk cover • Up to 85% commercial risks and protracted default • Up to 95% for Wholturnover Political Risk Policy • Up to 90% for Wholturnover Commercial Risk Policy • Up to 90% for Wholturnover Policy Light for all types of risks <p>2. On its behalf and under its name: 100% indemnity for confiscation, expropriation and nationalization insurance</p>
Lloyd's of London	Lloyd's is an Insurance Broker
MIGA	Up to 90%
OPIC	Up to 90%
SACE	Zero impact on Capital Absorption
U.S. Ex-Im Bank	Up to 95% of losses for Commercial and Political Risks of the Export Credit Insurance Policy
Zurich	Capacity of up to 150 Mil US Dollars per Transaction

Table F (Insurance Limit)

Country	Agency	Ownership Status	Owner	Date of Establishment
Canada	EDC	Government	Self Sufficient Crown Corporation	1969 (And formerly as ECIC since 1944)
France	COFACE	Private (With stocks traded at Euronext Paris)	<ol style="list-style-type: none"> Public 58.50% Natixis: 41.24% Employees: 0.26%. 	1946
Germany	Euler Hermes & PwC	<ol style="list-style-type: none"> Private. Delegated by German Government to act as ECA 	<ol style="list-style-type: none"> Privately owned by: <ul style="list-style-type: none"> Euler Hermes: Owned by Allianz SE PwC: Privately owned by: PricewaterhouseCoopers On behalf of the German Government: They both act under the government's umbrella and on its behalf as the official export credit agency and offer the Hermes Cover. 	<ol style="list-style-type: none"> Private: <ul style="list-style-type: none"> Euler Hermes: 1893 as ACI PwC: 1998 On behalf of the German Government: <ul style="list-style-type: none"> Hermes Cover First Introduced in 1949
Italy	SACE	Private	<p>Casa Depositi e Prestiti S.p.A.</p> <p>CDP is owned by:</p> <ol style="list-style-type: none"> Italian Government 80.1% Private Sector (Banks) 18.4% Treasury Shares 1.5% 	1998
Multinational	MIGA	Multilateral Agency	World Bank	1985
Spain	CESCE	Quasi-Governmental	<ol style="list-style-type: none"> Spanish State 50.25% Private Sector: <ul style="list-style-type: none"> Spanish Banks 45.85% Spanish Insurance Companies 3.9% 	1970
Switzerland	Zurich	Private	Privately owned by: Zurich Insurance Group Ltd.	1872
United Kingdom	UKEF	Governmental	Operates as a department of the Department for Business, Innovation and Skills of the UK	1919
	Lloyd's	Insurance Market which is a Corporate Body Governed by an Act	It is governed by the Lloyd's Act of 1871	1688
United States of America	AIG	Private	American International Group, Inc.	1919
	Ex-Im Bank	Governmental	It is the U.S self-sustaining Branch Agency.	1934
	OPIC	Governmental	It is the U.S self-sustaining Government's development finance institution.	1971

Table G (Ownership Structure) ²⁵⁶

²⁵⁶ Information in this table was gathered from the official websites of the mentioned agencies.

Country	Agency	Economic Benefit for Home State	Economic Benefit for Host State
Canada	EDC	Yes	Yes
France	COFACE	Yes	Yes
Germany	Euler Hermes & PwC	1. As Private Company: • Euler Hermes: Yes • PwC: Yes 2. On behalf of the Federal German Government: Yes	1. As Private Company: • Euler Hermes: Yes • PwC: Yes 2. On behalf of the Federal German Government: Yes
Italy	SACE	Yes	Yes
Multinational	MIGA	Yes	Yes
Spain	CESCE	Yes	Yes
Switzerland	Zurich	Yes	Yes
United Kingdom	UKEF	Yes	Yes
	Lloyd's	Yes	Yes
United States of America	AIG	Yes	Yes
	Ex-Im Bank	Yes	Yes
	OPIC	Yes	Yes

Table H (Home State & Host State Economic Benefit) ²⁵⁷

²⁵⁷ Information presented in this table can be found on official websites of these agencies and concluded from the information presented in this thesis. It was found in their Mission Statements.

N.B. There is an inherent assumption that companies providing PRI have an economic benefit to the home state since demand on their products means demand on the home states' companies and businesses. This also means, that through offer-

ing PRI these companies are helping, whether directly or indirectly, host states' economy. This is especially true since foreign investments in the host states means the creation of new jobs and the injection of money in the host state.

Chapter Five: Effectiveness of the Role EACs Play in Promoting FDI

Through the insurance, guarantee and credit services they offer, ECAs have promoted the export of goods and services and outward investment from the more developed home state to less-developed host ones.¹ For example, ECA's, in 2004, were credited for financing through loans, project guarantees and investment insurance projects that averaged around 90 billion U.S. Dollars.² Additionally, Berne Union Member Agencies were responsible for facilitating around 11% of the world's cross border trade of goods and services.³ Not only that, but figures also show that ECAs share of new businesses in 2016 was equivalent to 49%.⁴ On the other hand, the ECGD/UKEF managed up to 20 billion pounds sterling in financial risk supporting companies investing in emerging markets.⁵

The other side of the ECA coin, the Export-Import Banks, helped in promoting the importation of goods and services (along with the exportation of goods and services). The-

¹ It was suggested that these products offered by ECAs were developed in order to promote exports.

See;

Bettina Lange, Fiona Haines, Dania Thomas, *Regulatory Transformations, Rethinking Economy-Society Interactions* (Bloomsbury Publishing 2015) p 85.

Stephens suggested that the creation of such agencies was for the purpose of encouraging outward investment.

Stephens (*Chapter 1, n9*) p xi.

² Cedric Hilbert, 'International Energy Technology Collaboration and Climate Change Mitigation', OECD (2004). P 16.

³ Information can be found at:

<<https://www.berneunion.org>>

Last accessed on the 10th of July 2017.

⁴ Berne Union Statistics 2012-2016 (updated on 03/07/2017), p 4.

Found at:

<<https://www.berneunion.org/DataReports>>

Last accessed on the 5th of July 2017.

⁵ Found at:

<<https://www.gov.uk/government/publications/uk-export-finance-performance-highlights-2015/uk-export-finance-performance-highlights-june-2015>>

Last accessed on the 7th of April 2017

se agencies have been credited for encouraging outward investment through providing coverage against risks associated with the exportation of goods and services.⁶ They were criticized by some to have negative effects on the host state. Such criticism claimed that ECAs could lead the host state to debt.⁷

This chapter covers the effectiveness of ECAs in the reduction of the various risks encountered by MNC and foreign investors in the host state. It will also address ECA views on the borderline between the different type of risks in order to find out if there is lack of clarity in the definition of the risks covered or not. The latter will accompany the discussion the discussed previously on the different types of risks and the borderline between them.

Finally, this chapter will present the regions covered by certain ECAs and the percentage of coverage of these regions in order to find out the extent to which ECAs are encouraging investments in developing countries.

5.1. Ability in Reducing Investment-Risks

ECAs with through their insurance and guarantee services were able to protect investors and exporters against some of the major risks associated with FDI. They offer coverage

⁶ Stephens (*Chapter 1, n9*) p xi.

⁷ N.B. This is not the theme of the thesis.

Aron Goldzimer, 'Globalization's Most Preserved Secrete: The Role of Export Credit and Investment Insurance Agencies' [2002] World A01. pp 7-8.

against risks that the private sector does not cover against due to the high-risk status of such risks enjoy.⁸

The home state, and in an attempt to protect its investors, stimulate national economy and at the same time to promote exporting goods and services abroad, created ECAs.⁹ This was not the only reason though behind their creation. The home state, with such a move, is wishing to enhance its economic standing where exporting is one of the major contributors to the economy of a given state especially of an industrialized one.¹⁰

Though covering certain risks are said to be hefty and expensive, which is the case with political risk insurance, home states were keen on introducing mechanisms and products that would restore confidence of exporters and investors and allow them to be compensated for any losses he may encounter in the host state that are covered by PRIs.

One of the examples on that is the claim made by Sector Resources LTD. Sector Resources is a U.S.-owned Cayman Island Company that made an investment of 3.5 million U.S Dollars in Tolima, Colombia, for the acquisition and expansion of an underground

⁸ These, mainly, include political risks and some aspects of commercial and financial risks as it was examined earlier through this thesis.

See;

Soh Young In, 'Do export credit agencies benefit the economy?' (Sep 24 2014) Stanford International Policy Review, Stanford University Journal of International Policy Studies, p.1, Introduction.

<<http://www.stanfordpolicyreview.org/essay/do-export-credit-agencies-benefit-the-economy/>>

Last accessed on the 17th of February 2016

⁹ Stephens, (*Chapter 1, n9*) p xi.

And;

Lange, Haines and Thomas (*Chapter 5, n1*) p 85.

¹⁰ Some ECAs require a minimum national content. For example, the U.S. Ex-Im Bank requires a minimum of 85%.

See;

Shayerah Ilias, 'Reauthorization of the Export-Import Bank: Issues and Policy Options for Congress, CSR Report for congress (7 May 2012) p 13.

Article can be found at:

<<https://www.fas.org/sgp/crs/misc/R41829.pdf>>

Last accessed on the 28th of February 2016.

site that contains quartz, gold and silver and invested in equipment lease for 2 million U.S. Dollars. For that, the company purchased two insurance contracts from OPIC in 1999.¹¹

Though the company has undertaken measures to reduce any political risks that they may encounter in Colombia through employing 24-hour security guards on site, through complying with all security and safety requirements on the site and through building ties with the local community, the company, however, was threatened by FARC to have its site blown. Under these threats and after representatives of the company and the town failed to reach any settlements with the FARC and since the threat of having the mine being blown up by the FARC was a serious threat, employees of the site protested and refused to work under these threats. As a result, Sector Resources had to suspend its operations in Tolima and it shut-down its operations.¹²

Since Sector Resources Ltd purchased two insurance policies covering Political Violence, the company was reimbursed of 2,430,759.59 U.S Dollars by OPIC after the company's claims were found to be valid.¹³

ECAs have been argued to have a role at combating bribery though applying the “OECD Convention Combating Bribery of Foreign Public Officials in International Business Transactions”.¹⁴

¹¹ Memorandum of Determinations: Political Violence Claim of Sector Resources Ltd., pp. 1-2

Found at:

<<https://www.opic.gov/sites/default/files/docs/Sectorclaim2002.pdf>>

Last accessed on the 1st of February 2017.

¹² *ibid* at pp. 4-6.

¹³ *ibid* at p. 13.

¹⁴ Goldzimer (*Chapter 5, n7*) pp 12-13.

These examples show that the support granted by ECAs to investors through insuring against a number of investment risks or through guarantees and loans adds an extra layer of security where banks, investors and multinationals will be more confident that they will be covered financially in case something goes wrong while investing abroad.¹⁵

These ECAs, mainly the governmental ones, may have to bear high expenses to do that but exporting goods and services means high demand for such products which leads to creation of new jobs and injection of capital in order to suit the growing needs for these products or services. What the governmentally-supported ECAs seek by insuring against these risks is to stimulate the home state's economy and allowing it flourish.¹⁶

5.2. Ability to Promote and Facilitate FDI

Having an agency that is able to offer insurance and guarantee services against risks not covered by conventional or private sector insurance companies is thought, to be helpful in the process of promoting trade and investment.¹⁷ This true since many investors would have not considered to invest in certain risky markets had there been no insurance, or a protection scheme offered to them while investing overseas. The success of

¹⁵ *ibid* at p. 2

¹⁶ See;

Young In (*Chapter 1, n32*).

Also see;

Table A2.1. In the Promoting National Exports where all ECAs in the said table have had promoting national exports as one of their objectives.

Wang, Kikuchi, Choudhury, Mansilla (*Chapter 4, n3*) Appendix II p 30.

¹⁷ Stephens (*Chapter 1, n9*) p 1.

these agencies in promoting investment can be measured through a number of practical examples where ECAs were successful in protecting investors' properties, such as that of the Seaboard Overseas Limited.

Seaboard Overseas Limited suffered losses on its tangible and properties in Zambia as a result of riots and political violence. The company which owned the National Milling Company Limited, a Zambian company, made a claim to OPIC and as a result, was compensated in the amount of 38,027.37 US Dollars out of the active amount of coverage of 1,294,362 US Dollars. The losses incurred by the Company took place after three of its depots were looted during the riots taking place in the country during the presidential elections of 2011.¹⁸

In the UK, the UK Export Finance (UKEF) known also as Export Credit Guarantee Department of the UK (ECGD) reported that 36% of its services offered to support exporters were granted to those exporting to the Middle East and to Africa while support to exporters exporting to Asia accounts for 25%.¹⁹ It was also reported that support to UK exporters exporting to the Americas counts for 24% and those exporting to Europe reached 15%.²⁰ In addition, the ECGD/UKEF offered to 44 investments Export Insur-

¹⁸ Memorandum of Determination: Political Violence Claim of Seaboard Overseas Limited. pp. 1-4.

Found at:

<<https://www.opic.gov/sites/default/files/files/seaboard-overseas-limited-zambia.pdf>>

Last accessed on the 12th of December 2016.

¹⁹ These numbers were found at:

Annual Report and Accounts 2013/2015, UK Export Credit Guarantee Department, p.18.

Document is available at the following link:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/326210/10132-UKEF-Annual_Report_and_Accounts_2013-14_ACCESSIBLE16_3.pdf>

Last accessed on the 25th of May 2015.

²⁰ *ibid.*

ance products from a total 279 investments using its services.²¹ In addition, the UKEF has been continuously supporting the aviation and aerospace industry where one of the agency's clients is Airbus. The ECGD/UKEF supported 6% of the total aircrafts delivered by Airbus in 2015-2016 through the funding services offered by it.²²

However, it has been recorded that not all ECAs aim to promote investment in developing countries. On the contrary, their focus was more on protection of the national exporter and investor rather than promotion of investment in the host state. The exception to this was the Canadian and U.S. ECAs, ECD and OPIC. For example, one of OPIC's main aims is the contribution to the host state's development.²³

It was stated that ECAs aim to promote international trade and they are considered as an effective tool to achieve this.²⁴ An example of that is the recent support the UKEF has given to one of the British companies that won a bid to provide triathlon equipment's at the Rio Olympics of 2016. ES Global Solutions, an event strategy company, used the UKEF's Export Insurance product after winning a 1.2 million pounds sterling to provide equipment for Rio Olympic Games' triathlon and, as a result of a claim, the company received 400,000 pounds sterling from UKEF.²⁵

²¹ This was concluded after analyzing information found at:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/537235/UK-Export-Finance-list-business-supported-2015-to-2016.csv/preview>

Last accessed on the 25th of August 2016.

²² UK Export Finance Annual Reports and Accounts 2015-16

Found at:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/536579/ukef-uk-export-finance-annual-report-2015-16-web.PDF>

Last accessed on the 21st of August 2016.

²³ Gordon (*Chapter 1, n32*) p 105.

²⁴ Schutter, Swinnen, Wouters (*Chapter 1, n26*) p 190.

²⁵ Found at:

<<https://www.gov.uk/government/case-studies/ukef-helps-es-global-undertake-olympic-triathlon-contract-in-rio>>

Originally, Export Credit Agencies were not created to enhance the welfare of the host state, rather to enhance the home state's economic standing.²⁶ This is especially true since supporting exporters and investors will help create jobs and positively stimulate the home state's economy. For example, the U.S. Ex-Im bank helped in creating 1.4 million jobs in the U.S. market as a result of demand on its services.²⁷

This promotion of investment in developing host states is believed to have a positive effect on its economy. It is believed that it will allow the host state to benefit from the technology that the foreign investor is bringing and from the management skills, workers, training and will also allow the host state to benefit from having a positive effect on its labor market.²⁸

FDIs aim to promote better practices and quality standards and introduce new skills to the local market of the host state.²⁹ For example, Malaysia and Thailand were able to benefit from the growing FDI flow into their territories and that allowed these states to expand and diversify their manufactured exports which led them to improve their international competitiveness.³⁰

Last accessed on the 8th of October 2016.

And at:

<https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/537235/UK-Export-Finance-list-business-supported-2015-to-2016.csv/preview>

Last accessed on the 8th of October 2016.

²⁶ Schutter, Swinnen, Wouters (*Chapter 1, n26*) 192.

²⁷ Information can be found at:

<<http://grow.exim.gov/blog/what-is-an-export-credit-agency-eca-why-do-we-have-one>>

Last accessed on the 1st of March 2017.

²⁸ Shihata (*Chapter 2, n90*) p 11.

And;

Apergis, Lyroudi and Vamvakidis (n 300) p 1.

²⁹ Shihata (*Chapter 2, n90*) p 12.

³⁰ *ibid* at 11.

Investment promotion, from the host state's prospective, means that attraction of foreign investment and capital is within its best interests since it stimulates local economy and improve the living standards in the host state.³¹

It may be argued that the fact that ECAs are present have helped in promoting exports and investments to developing states; thus, helping in exporting technology, know-how, capital and contributing to the improvement of the economic standard of the host state.³²

This may, possibly, be true since such agencies are willing to provide insurance and cover against risks that are considered to fall under the high-risk category. Not only that, but the fact that such agencies offer these guarantee and insurance services at a relatively inexpensive premium, compared to other insurance providers.³³ In that respect, government -sponsored insurance providers would encourage exporters or investors to engage into business ventures in a developing state that might enjoy a high-risk status. It may be helpful to consult Table A to have a clearer view on the various types of risks associated with foreign investment.³⁴

5.3. Conclusion

Historically, ECAs were created for the purpose of encouraging the export of goods and services from the home state, which is normally a developed state, to the host state,

³¹ Sauvart and Sachs (*Chapter 1, n22*) p 122.

³² Chuah (*Chapter 4, n2*)p 155.

³³ Stephens (*Chapter 1, n9*) p 52.

³⁴ Table A, p 131.

which is normally a developing one. Nowadays, it is noted that developing and transitional economies have their own ECAs.³⁵ For example, India, Indonesia and Malaysia have their own ECAs where India has the Export Credit Guarantee Corporation of India while Indonesia has the PT. Asuransi Asei Indonesia and Malaysia has the Export Import Bank of Malaysia Berhad.³⁶ This encouragement of exporting goods and services is for the purpose of stimulating the home state's economy (the more demand on the goods and services exported the greater the probability of job creation).³⁷

It was also thought that with such agencies and with such encouragement for exporting goods and capital, the host developing state will be able to benefit from the technology, know-how, capital, labor skills and services of the exporter or the investor will contribute to the local economy of the host state.³⁸

The hypothesis remains that with more foreign investment and trade going to developing states, the more that these states will benefit and, as a result, the need to cater investor's protection needs will increase. This is especially true, since the share of ECAs in facilitating new business was 49% in 2016.³⁹

³⁵ Please refer to the Berne Union Members' List at Appendix I of this thesis.

³⁶ *ibid* at pp 384-385.

³⁷ This idea was reflected in the work of Giantruco.

See;

Gianturco (*Chapter 3, n22*) pp 3-4.

³⁸ Gordon (*Chapter 1, n32*) p 96.

N.B. This may be true since FDIs are thought to have a positive effect on the host state with technology transfer.

See;

Damijan, Knell, Majcen and Rojec (*Chapter 2, n1*) p 2.

³⁹ Berne Union Statistics 2012-2016 (updated on 03/07/2017), p 4.

Some ECAs, like the U.S. OPIC, included in their mission statement that their objective is to contribute to the host state's development as well as to promote the home state's development and welfare.⁴⁰

But in order to seek the services of ECAs and benefit from their products, a well-informed investor is likely the key. Investors are expected to know the types of risks they may encounter in the host state and accordingly look for the product or service that will suit them the best. In that respect, investors are expected to highlight the types of risks they will be facing from political to commercial and financial risks and seek the best insurance or guarantee provider who would cover them against these.

The three major types of risks may interlock and be a bit difficult to distinguish, while at times it may be much clearer and easier. In this chapter, the distinction presented was between financial and political risk on one side and between financial and commercial risks on the other side.

As it was shown, there are situations where financial risk may be considered more as a financial political one while, on the other hand, this problem would not be present in connection with financial and commercial risks and that is due to the fact that actions considered to be commercial are closely related to the investor and exporter rather than the host state, whereas financial risk is more related to the host state's financial situation rather than that of the exporter's.

⁴⁰ Gordon (*Chapter 1, n32*) p 96.

Chapter Six: Conclusion

In the age of globalization where investors and multinationals are seeking to explore new territories and new investments, it is of grave to clearly understand what kind of risks these investors and multinationals might encounter in their news ventures and how they could protect themselves against these risks. For that, the thesis formulated a number of suggestions.

The thesis followed a comparative analysis research methodology and compared between a number of Export Credit Agencies and between a number of states. It used a combination of primary and secondary resources and also conducted interviews with ECAs representatives. The thesis examined a number of Bilateral Investment Treaties to demonstrate the similarities/ differences between them. It resorted to various legislations in North America and Latin America. It also examined EU legislation and referred to the Qatari legislation as well. The thesis also referred to the work of Peter Muchilinski, M. Sornarajah, Jeswald Salacuse and to the work of Shihata to name a few. In addition, the thesis resorted to the official websites of the companies and agencies it examined and also used the websites of some news media outlets. Finally, the thesis examined a number of cases and international agreements.

The thesis demonstrated the various risks associated with foreign direct investment. It started with defining what foreign investment is through examining various definitions of the term available in national and in international law. For that, the thesis presented the definition of Foreign investment in the Chilean and Qatari Law then it presented that of the IMF.

It also presented the definition of investment according to Peter Muchlinski and according to M. Sornarajah then this thesis compared between the various descriptions of Foreign Investment available in Bilateral Investment Treaties. After this examination, the thesis defined foreign direct investment as an investment concluded by a foreign natural or legal person in a host foreign state with the goal of profit maximization and with the intention of controlling and continuously managing the investment.¹ It suggested looking at three factors to determine if an investment is a direct investment or not. These are the: time of holding the shares, interest behind the share ownership and at the location of the investment.²

The thesis thoroughly analyzed Political Risk, Commercial Risk and Financial Risk. It recommended that Political Risk be defined as a threat to investments made by foreigners through means of interference by the host state's government or any of its representatives acting on its behalf which would result in limiting investors from benefiting from their property rights.³ This risk is, therefore, closely related to the host state's government, or representatives', decision to limit investors' access to their property rights. In addition, it described Commercial Risk as any losses incurred by the investor due to the nature of the investment or while the investment is being established or during the construction.⁴ This risk is closely related to the markets perception of the goods or services offered by the investor and by any contractual relationship between the investor and third parties in the host state. Finally, the thesis described Financial Risk as risks closely related to external economic factors affecting the investment or the project itself and as such they are related to the home state's

¹ This was discussed in chapter 2 in sections 2.1.

² *ibid.*

³ This was discussed in chapter 2 in sections 2.4.1

⁴ This was discussed in chapter 2 in sections 2.4.2

currency exchange rate and to the interest and inflations rates in the host state.⁵

Upon studying these various investment-related risks, the thesis recommended a more detailed approach in the form of five-risk approach where it suggested differentiating between Political Risk, Financial Risk, Commercial Risk, Political Financial Risk and, finally, Political Commercial Risk.⁶

This more detailed approach stems from the fact that the borderline between the classic three-risk approach can, at times, interlink and rather be difficult to distinguish. This is true, especially since the political risk is the most prominent one among the classic three risks. Both commercial and financial risks can easily become political risk. This happens whenever there is a political intervention in these two risks. For example, currency exchange rate can easily turn from financial risk to a political financial one, once the home state controls the exchange rate and manipulates with the exchange rate to limit investors from benefitting from their property rights.⁷

The same may also happen in commercial risk where, for example, when investors have a contractual relationship with host state parties or representatives and the host state party does not honor their contractual obligations using their political influence, then this can become political commercial risk.⁸

⁵ This was discussed in chapter 2 in sections 2.4.3

⁶ This was discussed in chapter 2 in sections 2.4 and 2.5.

⁷ This was proved in chapter 2 in section 2.5

⁸ *ibid*

As such, labeling these commercial risks or financial risks as political simply because of political intervention, denies these risks their true nature. For that the suggested the five-risk approach which will help, both, multinationals and investors, on the one hand, and insurance providers, on the other, state the risk category that they insure/ seek insurance against rather than listing the actions formulating a specific risk category. In that respect, the thesis provided some examples of ECAs providing insurance coverage against certain risks. For example, it noted that SACE, the Italian official ECA and the UKEF where UKEF's political risk coverage includes confiscation, currency inconvertibility, political violence and riots, expropriation and nationalization, remittance and transfer restrictions and against defaults on certain obligations including loans and arbitral claims and contracts while SACE, on the other hand, cover against expropriation, nationalization, confiscation, seizure, civil disorder, war, riots, sabotage, non-transfer of currency and the termination of contracts agreed with local public counter-parties in its political risk insurance support.⁹

The thesis examined the ownership structure and governance of a number of ECAs in order to elaborate that though these agencies may differ from one another, they still, however provide similar services. These agencies may be publically sponsored agencies. As such, they could be an emanation from the government, like the UKEF, or they could be a corporation established by the government, like the CDF. They could be quasi-governmental agencies where, both, the government and the private sector own shares in a specific agency, like CESCE. Lastly, they could be private companies that are either delegated by the government to provide export credit support and under the govern-

⁹ This was examined in chapter 4 in section in section 4.2.2 and in section 4.4.

ment's name, like Euler Hermes, or they could be acting on their own behalf and providing the support under their own name, like AIG.¹⁰

The thesis looked at the services offered by ECAs and emphasized that they all offer similar services. That said, there could be some minor differences between a given ECA and another in the same host state or even internationally. For example, SACE covers terrorism in its insurance policies while the UKEF, on the other hand, doesn't. The Ex-Im Bank of the USA offers insurance for exporters while OPIC offers insurance for investors and, in that sense, both complete one another.¹¹

The thesis proved that the home state of the investor has a role in protecting such investor through various means. These can be through recommendations that the home state regularly publish explaining the investment climate of the perspective host state and the limit of protection offered for investors there.¹² It may also take the form of diplomatic protection where the home state steps in to protect its own national's property rights.¹³ Finally, the home state may protect its investors through offering export credit guarantee and insurance support through privately-held, publicly-held or even quasi-governmental agencies.¹⁴

Additionally, the home state may coordinate and cooperate with the host state through means of international diplomacy. As such, they may negotiate International Investment Treaties which could be either bilateral or multilateral. Or they could decide to join an

¹⁰ This was examined in chapter 3 in section 3.4

¹¹ This was examined in chapter 4 in section 4.2.2.

¹² This was examined in chapter 4 in section 4.2.3.

¹³ *ibid.*

¹⁴ This was examined in chapter 4 in section 4.2.3 and in section 4.2.4

existing multilateral organization to promote, protect and facilitate investment. For example, many states have signed Bilateral Investment Treaties which are directed at promoting, protecting and facilitating investments between signatory states.¹⁵ These states may also do the same agreement on a multilateral basis. The Treaty of Functioning of the EU and the North American Free Trade Agreement are examples of Multilateral Investment Treaties.¹⁶ These states, i.e., home and host states, may decide to become members at the Multilateral Investment Guarantee Agency which offers export credit support to investors of signatory members who are seeking to invest in another signatory member state.¹⁷ In addition, these states may decide to coordinate and cooperate to promote cross-border investing through establishing a joint chamber of commerce.¹⁸

The host state, on the other hand, may take various measures to help promoting itself as a foreign investment-friendly environment. As such, it may design new sets of laws and policies liberalizing the market and eliminating any investment barriers while ensuring adequate measures of property rights protection are met. In that respect, the thesis recommended the use of foreign investment-friendly investment/ less-friendly environment rather than the classic open-door/ closed-door approach since, as proven in the thesis, there is no absolute closed-door state where even the states who were considered to follow the closed-door approach like Cuba and china, have certain means for foreign investors to engage into investment activities within their territories.¹⁹ Additionally, the host state may become a member at the International Center for Settlement of Invest-

¹⁵ This was examined in chapter 3 in section 3.2.

¹⁶ *ibid.*

¹⁷ This was examined in chapter 3 in section 3.3.

¹⁸ This was examined in chapter 3 in section 3.4.

¹⁹ This was examined in chapter 2 in section 2.3.

ment Disputes.²⁰ This will give investors a certain degree of confidence that should they lose access to their property rights, in part or in full, an independent international body will be there to enforce the rule of law. Some host states have also attempted to attract FDI through the creation of Investment Authorities. These, like the Saudi Arabian Investment Authority, is a foreign investment license provider that aims to reach economic liberalization.²¹

Next to the home and host states' protection, investors can protect themselves through making their own due diligence. For example, they can protect themselves within the agreements they sign with the host state or its representatives or with the host state party. This takes place through including a number of clauses that are aimed at protecting the investor's property rights.²² Adding stabilization clause, force majeure clause, damages clause or even an arbitration clause could add considerable protection to the investor to start with.²³ In addition to protecting themselves through contracts, investors may seek the assistance of insurance providers. They are expected to seek, first, any commercial insurance providers to cover against the risks they expect to encounter. Should they be unsuccessful in finding the policy they are looking for, they may resort to government-supported agencies where they will probably find the policy they are seeking. Should their attempt in finding insurance against specific risks with the government-supported agency be unsuccessful, they may resort to the Multilateral Investment Guarantee Agency, upon meeting the agency's requirements.²⁴

²⁰ This was examined in chapter 3 in section 3.3.

²¹ This was examined in chapter 2 in section 3.4.

²² This was examined in chapter 2 in section 2.4.2. and in section 2.5.2.

²³ *ibid.*

²⁴ This was examined in chapter 3 in section 3.3. and in chapter 4 in section 4.4.

The thesis discussed a new approach to investment protection through differentiating between *pre-investment protection* and *post-investment protection* where *pre-investment protection* includes recommendations from the home state, any International Investment Agreements between the home and host states, insurance through MIGA, ECAs and insurance companies and through addition of specific clauses in the contract with the host state. *Post-investment agreement* on the other hand includes, arbitration in case of disputes between investors and multinationals, on the one hand, and the host state, on the other. It also includes Diplomatic Protection.²⁵

The thesis discussed the various risks covered by ECAs and compared it to those offered by MIGA and commercial insurance companies. As such, since the thesis's main focus was on the insurance support offered by ECAs, it did not handle the other services offered by these agencies. While comparing these services, it was clear that the private sector is catching up and offering similar support to that of ECAs.²⁶ Nevertheless, public sector ECAs state that they exist to complete and not compete with the private sector. This is true since public ECAs offer government backed coverage which means that dealings will be on a government-to-government basis and this is something the private sector cannot offer.²⁷

The thesis examined the effectiveness of ECAs through presenting a number of examples from OPIC and the UKEF. For example, the thesis demonstrated how OPIC was able to successfully insure Seaboard Overseas Limited and Sector Resources Ltd against Political

²⁵ This was examined in chapter 3 in section 3.4.

²⁶ Berne Union Yearbook 2016. p 45.

Also see:

Table D

²⁷ This was examined in chapter 4 in section 4.2.2.

Risks.²⁸ The thesis concluded that there is demand on ECAs support visible through the statistics prepared by the UKEF.²⁹ For example, it showed that the agency have been continuously supporting various sectors including the aviation sector of which it has funded 6% of the total aircrafts delivered by Airbus, although the main focus and examples presented in the thesis covered only the insurance support offered by ECAs.³⁰ As such, according to a study published by the OECD in 2008, the value of investment guarantees reached an average of 3% of the total FDI flow.³¹

The thesis also examined two successful claims made by investors and multinationals who resorted to OPIC's insurance support.³² It also highlighted an example where the UKEF has also successfully helped a UK company acquire losses incurred by it on the basis of an insurance support offered by the UKEF. This was done through presenting the example of ES Global Solutions.³³

On these basis, the thesis concludes that the step in the protection and promotion of investors and multinationals, is the one offered by the home state and that offered by the host state. These take the form of diplomatic relations and investment agreements. It includes protection offered in public international law to investors through diplomacy, BITs, MITs and the general rules of public international law. Then comes contractual obligations and the role of arbitration as a protection mechanism. Finally, the investors' and multinationals' may be protected through ECAs, multilateral investment agencies

²⁸ This was examined in chapter 5 in section 5.1. and in section 5.2.

²⁹ This was examined in chapter 5 in section 5.1. and in section 5.2.

³⁰ This was examined in chapter 5 in section 5.2.

³¹ This was presented in Kathryn Gordon's work: Gordon (*Chapter 1, n32*) p 92.

³² This was examined in chapter 5 in section 5.1.

³³ This was examined in chapter 5 in section 5.2.

and through insurance companies. All of these mechanisms shall present investors and multinationals a more comprehensive protection while exploring new markets.

Appendix I

Berne Union Members List

List of Members of the International Union of Credit and Investment Insurers (Berne Union)

Found at:

<http://www.berneunion.org/about-the-berne-union/berne-union-members/>

Last Accessed on 22 May 2015

Australia:

The Export Finance and Insurance Corporation *(EFIC)*

Austria:

Oesterreichische Kontrollbank Aktiengesellschaft *(OeKB)*

Belgium:

CREDENDO GROUP *(ONDD)*

Bermuda:

Hiscox Political Risk *(HISCOX)*

Sovereign Risk Insurance Ltd. *(SOVEREIGN)*

Canada:

Export Development Canada *(EDC)*

China

China Export & Credit Insurance Corporation *(SINOSURE)*

Chinese Taipei

Taipei Export-Import Bank of China *(TEBC)*

Czech Republic:

Export Guarantee & Insurance Corporation *(EGAP)*

Denmark:

Eksport Kredit Fonde *(EKF)*

Finland:

Finnvera Plc. *(FINNVERA)*

France:

Compagnie Française d'Assurance pour le Commerce Extérieur *(COFACE)*

Germany:

Euler Hermes Deutschland AG *(EH GERMANY)*

PricewaterhouseCoopers AG *(PwC)*

Hong Kong:

Hong Kong Export Credit Insurance Corporation *(HKEC)*

Hungary:

Hungarian Export-Import Bank Plc.

&

(EX-IM HUNGARY)

Hungarian Export Credit Insurance Plc.

India:

Export Credit Guarantee Corporation of India Ltd.

(ECGC)

Indonesia:

PT. Asuransi Asei Indonesia

(ASEI)

Israel:

Israel Export Insurance Corp Ltd.

(ASHRA)

Italy:

Servizi Assicurativi del Credito all'Esportazione

(SACE)

Jamaica:

National Export-Import Bank of Jamaica Limited

(EX-IM J.)

Japan:

Nippon Export and Investment Insurance

(NEXI)

Korea:

Korea Trade Insurance Corporation

(KSURE)

Luxembourg:

Luxembourg Export Credit Agency *(ODL)*

Malaysia:

Export-Import Bank of Malaysia Berhad *(MEXIM)*

Multilateral Agencies:

African Trade Insurance Agency *(ATI)*

Islamic Corp for the Insurance of Investment & Export Credit *(ICIEC)*

Multilateral Investment Guarantee Agency *(MIGA)*

Netherlands:

Atradius NV *(ATRADIUS)*

Norway:

Garanti-Instituttet for Eksportkreditt *(GIEK)*

Poland:

Export Credit Insurance Corporation Joint Stock Company *(KUKE)*

Portugal:

Companhia de Seguro de Créditos, S.A. *(COSEC)*

Singapore:

ECICS Limited *(ECICS)*

Slovak Republic:

Export-Import Bank of the Slovak Republic

*(EX-IM BANKA SR)***Slovenia**

SID Inc, Ljubljana

*(SID)***South Africa:**

Export Credit Insurance Corporation of South Africa Ltd.

*(ECIC SA)***Spain:**

Compañía Española de Seguros de Credito a la Exportacion

*(CESCE)***Sri Lanka**

Sri Lanka Export Credit Insurance Corporation

*(SLECIC)***Sweden:**

Exportkreditnämnden

*(EKN)***Switzerland**

Swiss Export Risk Insurance

*(SERV)***Thailand**

Export-Import Bank of Thailand

*(THAI EX-**IMB ANK)***Turkey**

Export Credit Bank of Turkey

(TURK EX-

IM BANK)

United Kingdom:

UK EXPORT FINANCE {Export Credits Gurantee Department} *(ECGD)*

United States of America:

American International Group, Inc. *(AIG)*

FCIA Management Company, Inc. *(FCIA)*

Overseas Private Investment Corporation *(OPIC)*

Export-Import Bank of the United States *(US EX-IM BANK)*

Zurich Surety, Credit & Political Risk *(ZURICH)*

Appendix II

Multilateral Investment Guarantee Agency (MIGA) Member States

List of Members of the Multilateral Investment Guarantee Agency (MIGA)

Found at:

<http://www.worldbank.org/en/about/leadership/members#4>

and at:

<http://www.miga.org/whoweare/index.cfm?stid=1789>

Last Accessed on 22 May 2015

Developing Countries

ASIA AND THE PACIFIC:

Afghanistan	Malaysia	Samoa
Bangladesh	Maldives	Singapore
Bhutan	Micronesia	Solomon Islands
Cambodia	Mongolia	Sri Lanka
China	Myanmar	Thailand
Fiji	Nepal	Timor Leste
India	Pakistan	Vanuatu
Indonesia	Palau	Vietnam
Korea	Papua New Guinea	
Lao People's Democratic Republic	Philippines	

EUROPE AND CENTRAL ASIA:

Albania	Hungary	Poland
Armenia	Kazakhstan	Russian Federation
Azerbaijan	Kosovo	Romania
Belarus	Kyrgyz Republic	Serbia
Bulgaria	Latvia	Slovak Republic
Bosnia-Herzegovina	Lithuania	Tajikistan
Croatia	Macedonia	Turkey
Cyprus	Malta	Turkmenistan
Estonia	Moldova	Ukraine
Georgia	Montenegro	Uzbekistan

LATIN AMERICA AND THE CARIBBEAN:

Antigua and Barbuda	Dominican Republic	Panama
Argentina	Ecuador	Paraguay
Bahamas	El Salvador	Peru
Barbados	Grenada	St. Kitts & Nevis
Belize	Guatemala	St. Lucia
Bolivia	Guyana	St. Vincent and the Grenadines
Brazil	Haiti	Suriname
Chile	Honduras	Trinidad & Tobago
Colombia	Jamaica	Uruguay
Costa Rica	Mexico	Venezuela
Dominica	Nicaragua	

MIDDLE EAST AND NORTH AFRICA:

Algeria	Jordan	Saudi Arabia
Bahrain	Kuwait	Syrian Arab Republic
Djibouti	Lebanon	Tunisia
Egypt	Libya	United Arab Emirates
Iran	Morocco	Yemen
Iraq	Oman	
Israel	Qatar	

SUB- SAHARAN AFRICA:

Angola	Gabon	Nigeria
Benin	Gambia	Rwanda
Botswana	Ghana	São Tomé and Príncipe
Burkina Faso	Guinea	Senegal
Burundi	Guinea-Bissau	Sierra Leone
Cameroon	Kenya	Seychelles
Cabo Verde	Lesotho	South Africa
Central African Republic	Liberia	South Sudan
Chad	Madagascar	Sudan
Comoros	Malawi	Swaziland
Democratic Republic of Congo	Mali	Tanzania
Republic of Congo	Mauritania	Togo
Côte d'Ivoire	Mauritius	Uganda
Equatorial Guinea	Mozambique	Zambia
Eritrea	Namibia	Zimbabwe
Ethiopia	Niger	

Industrialized Countries:

Australia	Greece	Portugal
Austria	Iceland	Slovenia
Belgium	Ireland	Spain
Canada	Italy	Sweden
Czech Republic	Japan	Switzerland
Denmark	Luxembourg	United Kingdom
Finland	Netherlands	United States
France	New Zealand	
Germany	Norway	

Appendix III

International Court for Settlement of Investment Disputes (ICSID) Member States

List of Contracting States and Other Signatories of the International Court for Settlement of Investment Disputes Convention (ICSID)

Found at:

<https://icsid.worldbank.org/apps/ICSIDWEB/about/Pages/Database-of-Member-States.aspx>

Last Accessed on 22 May 2015

Afghanistan	El Salvador	Malawi	Solomon Islands
Albania	Estonia	Malaysia	Somalia
Algeria	Ethiopia	Mali	South Sudan
Argentina	Fiji	Malta	Spain
Armenia	Finland	Mauritania	Sri Lanka
Australia	France	Mauritius	St. Kitts & Nevis
Austria	Gabon	Micronesia	St. Lucia
Azerbaijan	Gambia	Moldova	St. Vincent and the Grenadines
Bahamas	Georgia	Mongolia	Sudan
Bahrain	Germany	Montenegro	Swaziland
Bangladesh	Ghana	Morocco	Sweden
Barbados	Greece	Mozambique	Syria
Belarus	Grenada	Namibia	Tanzania
Belgium	Guatemala	Nepal	Thailand

Belize	Guinea	Netherlands	Timor-Leste
Benin	Guinea-Bissau	New Zealand	Togo
Bosnia and Herzegovina	Guyana	Nicaragua	Tonga
Botswana	Haiti	Niger	Trinidad and Tobago
Brunei Darussalam	Honduras	Nigeria	Tunisia
Bulgaria	Hungary	Norway	Turkey
Burkina Faso	Iceland	Oman	Turkmenistan
Burundi	Indonesia	Pakistan	Uganda
Cambodia	Ireland	Panama	Ukraine
Cameroon	Israel	Papua New Guinea	United Arab Emirates
Canada	Italy	Paraguay	United Kingdom and Northern Ireland
Cape Verde	Jamaica	Peru	United States of America
Central African Republic	Japan	Philippines	Uruguay
Chad	Jordan	Portugal	Uzbekistan
Chile	Kazakhstan	Qatar	Yemen
China	Kenya	Romania	Zambia
Colombia	Republic of Korea	Russian Federation	Zimbabwe
Comoros	Republic Kosovo	Rwanda	
Democratic Rep. of Congo	Kuwait	Samoa	
Republic of Congo	Kyrgyz Republic	Sao Tome and Principe	
Costa Rica	Latvia	Saudi Arabia	
Côte d'Ivoire	Lebanon	Senegal	
Croatia	Lesotho	Serbia	
Cyprus	Liberia	Seychelles	
Czech Republic	Lithuania	Sierra Leone	
Denmark	Luxembourg	Singapore	
Dominican Republic	Macedonia	Slovak Republic	

Egypt

Madagascar

Slovenia

Appendix IV

List of European Union Member States and Potential Members Until May 2015:

Available at:

<http://europa.eu/about-eu/countries/index_en.htm>

Last Accessed on 23rd of May 2015

MEMBER STATES:

Austria	Germany	Poland
Belgium	Greece	Portugal
Bulgaria	Hungary	Romania
Croatia	Ireland	Slovakia
Cyprus	Italy	Slovenia
Czech Republic	Latvia	Spain
Denmark	Lithuania	Sweden
Estonia	Luxembourg	United Kingdom
Finland	Malta	
France	Netherlands	

ON THE ROAD TO EU MEMBERSHIP:

Candidate States:

Albania

Iceland

Montenegro

Serbia

The former Yugoslav Republic of Macedonia

Turkey

Potential Candidates:

Bosnia and Herzegovina

Kosovo

Appendix V

World Bank

Guidelines on the Treatment of Foreign Direct Investment

Available at:

<<http://www.italaw.com/documents/WorldBank.pdf>>

Last Accessed on 23rd of May 2015

The Development Committee

Recognizing

that a greater flow of foreign direct investment brings substantial benefits to bear on the world economy and on the economies of developing countries in particular, in terms of improving the long term efficiency of the host country through greater competition, transfer of capital, technology and managerial skills and enhancement of market access and in terms of the expansion of international trade;

that the promotion of private foreign investment is a common purpose of the International Bank for Reconstruction and Development, the International Finance Corporation and the Multilateral Investment Guarantee Agency;

that these institutions have pursued this common objective through their operations, advisory services and research;

that at the request of the Development Committee, a working group established by the President of these institutions and consisting of their respective General Counsel has,

after reviewing existing legal instruments and literature, as well as best available practice identified by these institutions, prepared a set of guidelines representing a desirable overall framework which embodies essential principles meant to promote foreign direct investment in the common interest of all members;

that these guidelines, which have benefitted from a process of broad consultation inside and outside these institutions, constitute a further step in the evolutionary process where several international efforts aim to establish a favorable investment environment free from non-commercial risks in all countries, and thereby foster the confidence of international investors; and that these guidelines are not ultimate standards but an important step in the evolution of generally acceptable international standards which complement, but do not substitute for, bilateral investment treaties,

therefore calls the attention of member countries to the following Guidelines as useful parameters in the admission and treatment of private foreign investment in their territories, without prejudice to the binding rules of international law at this stage of its development.

I

SCOPE OF APPLICATION

1. These Guidelines may be applied by members of the World Bank Group institutions to private foreign investment in their respective territories, as a complement to applicable bilateral and multilateral treaties and other international instruments, to the extent that these Guidelines do not conflict with such treaties and binding instruments, and as a possible source on which national legislation governing the treatment of private foreign investment may draw. Reference to the "State" in these Guidelines, unless the context

otherwise indicates, includes the State or any constituent subdivision, agency or instrumentality of the State and reference to "nationals" includes natural and juridical persons who enjoy the nationality of the State.

2. The application of these Guidelines extends to existing and new investments established and operating at all times as bona fide private foreign investments, in full conformity with the laws and regulations of the host State.

3. These Guidelines are based on the general premise that equal treatment of investors in similar circumstances and free competition among them are prerequisites of a positive investment environment. Nothing in these Guidelines therefore suggests that foreign investors should receive a privileged treatment denied to national investors in similar circumstances.

II

ADMISSION

1. Each State will encourage nationals of other States to invest capital, technology and managerial skill in its territory and, to that end, is expected to admit such investments in accordance with the following provisions.

2. In furtherance of the foregoing principle, each State will:

(a) facilitate the admission and establishment of investments by nationals of other States,

and

(b) avoid making unduly cumbersome or complicated procedural regulations for, or imposing

unnecessary conditions on, the admission of such investments.

3. Each State maintains the right to make regulations to govern the admission of private foreign

investments. In the formulation and application of such regulations, States will note that experience suggests that certain performance requirements introduced as conditions of admission are often counterproductive and that open admission, possibly subject to a restricted list of investments (which are either prohibited or require screening and licensing), is a more effective approach. Such performance requirements often discourage foreign investors from initiating investment in the State concerned or encourage evasion and corruption. Under the restricted list approach, investments in nonlisted activities, which proceed without approval, remain subject to the laws and regulations applicable to investments in the State concerned.

4. Without prejudice to the general approach of free admission recommended in Section 3 above, a State may, as an exception, refuse admission to a proposed investment:

(i) which is, in the considered opinion of the State, inconsistent with clearly defined requirements of national security; or

(ii) which belongs to sectors reserved by the law of the State to its nationals on account of

the State's economic development objectives or the strict exigencies of its national interest.

5. Restrictions applicable to national investment on account of public policy (ordre public), public health and the protection of the environment will equally apply to foreign investment.

6. Each State is encouraged to publish, in the form of a handbook or other medium easily accessible to other States and their investors, adequate and regularly updated information about its legislation, regulations and procedures relevant to foreign investment and other information relating to its investment policies including, *inter alia*, an indication of any classes of investment which it regards as falling under Sections 4 and 5 of this Guideline.

III

TREATMENT

1. For the promotion of international economic cooperation through the medium of private foreign investment, the establishment, operation, management, control, and exercise of rights in such an investment, as well as such other associated activities necessary therefor or incidental thereto, will be consistent with the following standards which are meant to apply simultaneously to all States without prejudice to the provisions of applicable international instruments, and to firmly established rules of customary international law.

2. Each State will extend to investments established in its territory by nationals of any other State fair and equitable treatment according to the standards recommended in these Guidelines.

3. (a) With respect to the protection and security of their person, property rights and interests, and to the granting of permits, import and export licenses and the authorization to employ, and the issuance of the necessary entry and stay visas to their foreign personnel, and other legal matters relevant to the treatment of foreign investors as described in Section 1 above, such treatment will, subject to the requirement of fair and equitable treatment mentioned above, be as favorable as that accorded by the State to national investors in similar circumstances. In all cases, full protection and security will be accorded to the investor's rights regarding ownership, control and substantial benefits over his property, including intellectual property.

(b) As concerns such other matters as are not relevant to national investors, treatment under the State's legislation and regulations will not discriminate among foreign investors on grounds of nationality.

4. Nothing in this Guideline will automatically entitle nationals of other States to the more favorable standards of treatment accorded to the nationals of certain States under any customs union or free trade area agreement.

5. Without restricting the generality of the foregoing, each State will:

(a) promptly issue such licenses and permits and grant such concessions as may be necessary for the uninterrupted operation of the admitted investment; and

(b) to the extent necessary for the efficient operation of the investment, authorize the employment of foreign personnel. While a State may require the foreign investor to reasonably establish his inability to recruit the required personnel locally, e.g., through

local advertisement, before he resorts to the recruitment of foreign personnel, labor market flexibility in this and other areas is recognized as an important element in a positive investment environment. Of particular importance in this respect is the investor's freedom to employ top managers regardless of their nationality.

6. (1) Each State will, with respect to private investment in its territory by nationals of the other States:

(a) freely allow regular periodic transfer of a reasonable part of the salaries and wages of foreign personnel; and, on liquidation of the investment or earlier termination of the employment, allow immediate transfer of all savings from such salaries and wages;

(b) freely allow transfer of the net revenues realized from the investment;

(c) allow the transfer of such sums as may be necessary for the payment of debts contracted, or the discharge of other contractual obligations incurred in connection with the investment as they fall due;

(d) on liquidation or sale of the investment (whether covering the investment as a whole or a part thereof), allow the repatriation and transfer of the net proceeds of such liquidation or sale and all accretions thereto all at once; in the exceptional cases where the State faces foreign exchange stringencies, such transfer may as an exception be made in installments within a period which will be as short as possible and will not in any case exceed five years from the date of liquidation or sale, subject to interest as provided for in Section 6 (3) of this Guideline;

and

(e) allow the transfer of any other amounts to which the investor is entitled such as those which become due under the conditions provided for in Guidelines IV and V.

(2) Such transfer as provided for in Section 6 (1) of this Guideline will be made (a) in the currency brought in by the investor where it remains convertible, in another currency designated as freely usable currency by the International Monetary Fund or in any other currency accepted by the investor, and (b) at the applicable market rate of exchange at the time of the transfer.

(3) In the case of transfers under Section 6 (1) of this Guideline, and without prejudice to Sections 7 and 8 of Guideline IV where they apply, any delay in effecting the transfers to be made through the central bank (or another authorized public authority) of the host State will be subject to interest at the normal rate applicable to the local currency involved in respect of any period intervening between the date on which such local currency has been provided to the central bank (or the other authorized public authority) for transfer and the date on which the transfer is actually effected.

(4) The provisions set forth in this Guideline with regard to the transfer of capital will also apply to the transfer of any compensation for loss due to war, armed conflict, revolution or insurrection to the extent that such compensation may be due to the investor under applicable law.

7. Each State will permit and facilitate the reinvestment in its territory of the profits realized from existing investments and the proceeds of sale or liquidation of such in-

vestments.

8. Each State will take appropriate measures for the prevention and control of corrupt business practices and the promotion of accountability and transparency in its dealings with foreign investors, and will cooperate with other States in developing international procedures and mechanisms to ensure the same.

9. Nothing in this Guideline suggests that a State should provide foreign investors with tax exemptions or other fiscal incentives. Where such incentives are deemed to be justified by the State, they may to the extent possible be automatically granted, directly linked to the type of activity to be encouraged and equally extended to national investors in similar circumstances. Competition among States in providing such incentives, especially tax exemptions, is not recommended. Reasonable and stable tax rates are deemed to provide a better incentive than exemptions followed by uncertain or excessive rates.

10. Developed and capital surplus States will not obstruct flows of investment from their territories to developing States and are encouraged to adopt appropriate measures to facilitate such flows, including taxation agreements, investment guarantees, technical assistance and the provision of information. Fiscal incentives provided by some investors' governments for the purpose of encouraging investment in developing States are recognized in particular as a possibly effective element in promoting such investment.

IV

EXPROPRIATION AND UNILATERAL ALTERATIONS OR TERMINATION OF CONTRACTS

1. A State may not expropriate or otherwise take in whole or in part a foreign private investment in its territory, or take measures which have similar effects, except where this is done in accordance with applicable legal procedures, in pursuance in good faith of a public purpose, without discrimination on the basis of nationality and against the payment of appropriate compensation.

2. Compensation for a specific investment taken by the State will, according to the details provided below,

be deemed "appropriate" if it is adequate, effective and prompt.

3. Compensation will be deemed "adequate" if it is based on the fair market value of the taken asset as such value is determined immediately before the time at which the taking occurred or the decision to take the asset became publicly known.

4. Determination of the "fair market value" will be acceptable if conducted according to a method agreed by the State and the foreign investor (hereinafter referred to as the parties) or by a tribunal or another body designated by the parties.

5. In the absence of a determination on agreed by, or based on the agreement of, the parties, the fair market value will be acceptable if determined by the State according to reasonable criteria related to the market value of the investment, i.e., in an amount that a willing buyer would normally pay to a willing seller after taking into account the nature of the investment, the circumstances in which it would operate in the future and its specific characteristics, including the period in which it has been in existence, the propor-

tion of tangible assets in the total investment and other relevant factors pertinent to the specific circumstances of each case.

6. Without implying the exclusive validity of a single standard for the fairness by which compensation is to be determined and as an illustration of the reasonable determination by a State of the market value of the investment under Section 5 above, such determination will be deemed reasonable if conducted as follows:

(i) for a going concern with a proven record of profitability, on the basis of the discounted cash flow value;

(ii) for an enterprise which, not being a proven going concern, demonstrates lack of profitability, on the basis of the liquidation value;

(iii) for other assets, on the basis of (a) the replacement value or (b) the book value in case such value has been recently assessed or has been determined as of the date of the taking and can therefore be deemed to represent a reasonable replacement value.

For the purpose of this provision:

-a “going concern” means an enterprise consisting of income-producing assets which has been in

operation for a sufficient period of time to generate the data required for the calculation of future income and which could have been expected with reasonable certainty, if the taking had not occurred, to continue producing legitimate income over the course of its

economic life in the general circumstances following the taking by the State;

-“discounted cash flow value” means the cash receipts realistically expected from the enterprise in each future year of its economic life as reasonably projected minus that year's expected cash expenditure, after discounting this net cash flow for each year by a factor which reflects the time value of money, expected inflation, and the risk associated with such cash flow under realistic circumstances. Such discount rate may be measured by examining the rate of return available in the same market on alternative investments of comparable risk on the basis of their present value;

-“liquidation value” means the amounts at which individual assets comprising the enterprise or the entire assets of the enterprise could be sold under conditions of liquidation to a willing buyer less any liabilities which the enterprise has to meet;

-“replacement value” means the cash amount required to replace the individual assets of the enterprise in their actual state as of the date of the taking; and

-“book value” means the difference between the enterprise's assets and liabilities as recorded on its financial statements or the amount at which the taken tangible assets appear on the balance sheet of the enterprise, representing their cost after deducting accumulated depreciation in accordance with generally accepted accounting principles.

7. Compensation will be deemed “effective” if it is paid in the currency brought in by the investor where it remains convertible, in another currency designated as freely usable by

the International Monetary Fund or in any other currency accepted by the investor.

8. Compensation will be deemed to be "prompt" in normal circumstances if paid without delay. In cases where the State faces exceptional circumstances, as reflected in an arrangement for the use of the resources of the International Monetary Fund or under similar objective circumstances of established foreign exchange stringencies, compensation in the currency designated under Section 7 above may be paid in installments within a period which will be as short as possible and which will not in any case exceed five years from the time of the taking, provided that reasonable, market-related interest applies to the deferred payments in the same currency.

9. Compensation according to the above criteria will not be due, or will be reduced in case the investment is taken by the State as a sanction against an investor who has violated the State's law and regulations which have been in force prior to the taking, as such violation is determined by a court of law. Further disputes regarding claims for compensation in such a case will be settled in accordance with the provisions of Guideline V.

10. In case of comprehensive non-discriminatory nationalizations effected in the process of large scale social reforms under exceptional circumstances of revolution, war and similar exigencies, the compensation may be determined through negotiations between the host State and the investors' home State and failing this, through international arbitration.

11. The provisions of Section I of this Guideline will apply with respect to the conditions under which a State may unilaterally terminate, amend or otherwise disclaim liability under a contract with a foreign private investor for other than commercial reasons, i.e.,

where the State acts as a sovereign and not as a contracting party. Compensation due to the investor in such cases will be determined in the light of the provisions of Sections 2 to 9 of this Guideline. Liability for repudiation of contract for commercial reasons, i.e., where the State acts as a contracting party, will be determined under the applicable law of the contract.

V

SETTLEMENT OF DISPUTES

1. Disputes between private foreign investors and the host State will normally be settled through

negotiations between them and failing this, through national courts or through other agreed mechanisms including conciliation and binding independent arbitration.

2. Independent arbitration for the purpose of this Guideline will include any ad hoc or institutional arbitration agreed upon in writing by the State and the investor or between the State and the investor's home State where the majority of the arbitrators are not solely appointed by one party to the dispute.

3. In case of agreement on independent arbitration, each State is encouraged to accept the settlement of such disputes through arbitration under the Convention establishing the International Centre for Settlement of Investment Disputes (ICSID) if it is a party to the ICSID Convention or through the "ICSID Additional Facility" if it is not a party to the ICSID Convention.

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