Would Reference to the Decisions of Investment Treaty Tribunals be of Assistance in the Interpretation of Political Risk Insurance Policies?

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Readers of this blog are likely to be familiar with the existence of Bilateral Investment Treaties ("BITs") and the wealth of arbitral awards made publicly available through the International Centre for the Settlement of Investment Disputes ("ICSID"). Given the publicity afforded to proceedings under BITs, or multilateral investment treaties such as NAFTA, one might be led to believe that recourse to investment treaty arbitration is the sole remedy for a seemingly wronged investor. This is incorrect. While it is true that recompense for a State's breach of its treaty obligations on account of a failure to provide full protection and security to the investor, or for treatment that was not considered to be fair or equitable, may primarily be found via the investment treaty arbitration route, alternatives are available to compensate an investor's loss caused by the expropriation by a host State, such as political risk insurance.

Political risk insurance is available from some of the world's leading insurance companies, and/or insurance syndicates at Lloyd's of London. An investor with the foresight to identify a risk of expropriation may well take a policy that, while differing in coverage from contract to contract, can provide an indemnity for loss(es) caused by perils such as confiscation, seizure, appropriation, expropriation and/or requisition for title, to name but a few. Such policies are often subject to the law of England and Wales and it is fair to say that English law is somewhat underdeveloped in its consideration of the concept of expropriation, certainly when compared to the body of arbitral awards rendered pursuant to BITs.

This blog addresses the concept of creeping expropriation as determined in various investment treaty arbitral awards, and asks whether deference to the body of such awards could assist insurers and insureds in ascertaining whether a loss is covered.

The difficult concept of creeping expropriation

Political risk insurance wordings rarely go into great detail as to what is to be defined as an "expropriatory event" for the purposes of coverage, often referring only to "loss and/or damage caused by *expropriation*". In the "classic" scenario – the blatant seizure of assets by a host State, often accompanied by significant rhetoric and a lack of (adequate) compensation – it can be relatively straightforward for an insured investor to establish that their loss is covered by a political risk insurance policy (subject to potential defences an insurer may have against a claim, that are beyond the scope of this blog). The situation is far more complicated when a claim is made on the basis of an alleged creeping expropriation.

"Creeping" expropriation is defined by the United Nations Conference on Trade and Development as "a slow and incremental encroachment on one or more of the ownership rights of a foreign investor that diminishes the value of its investment". Reference to English law as to whether a series of incremental steps taken by a State is sufficient to collectively amount to an expropriatory act for the purpose of insurance coverage is likely to be of limited benefit. The lack of clarity surrounding creeping expropriations can often lead to a great deal of time (and money) being spent by all parties in establishing whether an indemnity is due. Would the addition of a clause noting that reference can be made to publicly available investment treaty awards for the sole purpose of determining whether a creeping expropriation has occurred be of use in reducing this burden, or would it make things more difficult?

Requirements for creeping expropriation

It has long been established that investment treaty tribunals are not bound by previously rendered awards. Arbitral tribunals proceed on a case-by-case basis as to whether the actions of a particular State amount to a creeping expropriation. This is not to say, however, that previously rendered decisions do not offer guidance as to the particular components that, if apparent, will lead to a finding that a creeping expropriation has occurred.

I. Substantial interference

The need to establish "substantial interference" is controversial. Although not a traditional "taking" of an investment, if the State in question interferes to such a degree as to deprive the investor of the enjoyment, use or benefit derived of its investment, a creeping expropriation may be deemed to have occurred. Numerous decisions endorse the view that a *significant degree* of interference is required before a tribunal will establish a creeping expropriation to be apparent. *Metaclad Corp v United Mexican States* (NAFTA) is particularly pertinent on this:

> "…expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property…but also covert or incidental interference with the use of property which has the effect of depriving the owner in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not to the obvious benefit of the host State."

So far so good for insurers and insureds. However, the real difficulty comes when determining whether the level of interference is of the requisite degree.

An insignificant restriction or interference with property rights is not generally considered to be sufficient for a finding of creeping expropriation; the decisive element is the "substantial loss of control or economic value of a foreign investment", as referred to by James Crawford AC SC in "Brownlie's Principles of Public International Law (8th ed. 2012). For example, the tribunal in *Pope & Talbot Inc. v Government of Canada* rejected the investor's claim that Canada's export control regime constituted an expropriation as it interfered with its exports to the US, holding that "the test [should be] whether that interference is sufficiently restrictive to support the conclusion that the property has been 'taken' from the owner." While the interference may have reduced profits, the investor still exported considerable quantities of its product and earned substantial returns, rendering its argument unsuccessful.

Numerous decisions have held that an investor's continued control of an enterprise goes against the finding of a creeping expropriation. The requirement of either total or substantial deprivation has led to numerous decisions denying that an expropriation had occurred owing to the investor's retention of control over the investment.

II. The irreversibility and permanence of the contested measures

The requirement of a certain degree of permanence to the State's interference is also controversial. While *Tecnicas Medioambientales Tecmed SA v United Mexican States* referred to a "de facto expropriation [being] irreversible and permanent", subsequent decisions have taken a more pragmatic approach, preferring to look at the effect of the State action, even if it amounted to a temporary measure. For example, the tribunal in *Wena Hotels Ltd v Arab Republic of Egypt* held that an Egyptian public sector company's one-year seizure of two hotels pursuant to a dispute over lease terms was more than an "ephemeral interference" and amounted to an expropriation.

III. Intention versus effect

Often referred to as the "sole effect doctrine", many tribunals have endorsed the view that it is the *effect* of the State measure on the economic benefit, value and control over the assets that must be considered and that the state's *intention* to expropriate, though of potential assistance, is not decisive.

Given the fact that investment treaty tribunals are not bound by previously rendered awards, it is perhaps unsurprising that the requirements for a creeping expropriation are not particularly clear-cut. For both insurers and insureds, this is problematic and would likely be a significant argument against allowing for reference to such awards for the purposes of coverage determination under a political risk policy. But is there any element of the treatment afforded to the concept of creeping expropriation on the investment treaty level that could be of significant beneficial use?

The date of loss

The date of loss is one of the first issues considered in any coverage analysis under any insurance claim. If the insured's loss falls outside of the designated policy period, it does not fall within the confines of the contract and no further analysis is required – no indemnity is due. While a date of loss is simple to establish in a number of cases (i.e. in the case of a home-contents insurance policy claim following a break-in), the issue is somewhat more complicated when considering a claim under a political risk policy, especially when considering creeping expropriation. Is the date of loss to be determined from the first of the incremental steps taken by a host State, or the last? What happens when the former falls within a policy period and latter falls outside? Is investment treaty case-law of potential benefit here?

In *Siemens A.G. v Argentine Republic*, the tribunal found that the State committed both a direct expropriation via issuing a decree unilaterally terminating the investor's service contract, and a creeping expropriation by measures leading to the decree, including suspending certain services under the contract and attempting to impose a "non-negotiable" renewed agreement. Significantly, for political risk policy claims, the tribunal stated:

> "By definition, creeping expropriation refers to…steps that eventually have the effect of an expropriation. If the process stops before it reaches that point, then expropriation would not occur. This does not necessarily mean that no adverse effects would have

> occurred…the last step in a creeping expropriation that tilts the balance is similar to the straw that breaks the camel's back." (emphasis added)

The above appears to provide clarity; it is the final action that one should be concerned with in any coverage analysis under a political risk policy. However, as noted by the tribunal in *Azurix Corp v Argentine Republic*, "[t]here is no specific time set under international law for measures constituting creeping expropriation to produce the effect…How much time is needed must be judged by the specific circumstances of each case".

The waters are somewhat muddied once again.

Conclusion

Should political risk policies include a standard clause allowing for the consideration of investment treaty awards for the purposes of coverage analysis? It is difficult to say. In the scenario of an insured's loss that happens to closely mirror the facts of a case previously considered by an investment treaty tribunal, the answer is likely to be yes. However, as the brief analysis above demonstrates, any deviation from similar facts, and the wealth of consideration given to the concept of creeping expropriation by investment treaty tribunals could well make the sometimes difficult task of coverage analysis under a political risk policy even harder.