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Enforceability of Stabilization Clauses in Oil and Gas Contracts

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DEDICATION

To Almighty God.

To my late father.

To my beloved mother.

To my beloved sisters.

DECLARATION

I, **KARASIRA Denis** do hereby declare that the work presented in the dissertation entitled "**Enforceability of Stabilization Clauses in Oil and Gas Contracts**" is my wholly own work unless otherwise referenced in footnotes and bibliography. It has not been presented elsewhere for any academic qualification at any University or higher learning Institution.

Date: 04/11/2019.

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I wholeheartedly thank Almighty God to provide me a gift of life, good health and any other kind of empowerment that enabled me to undertake the work at hand.

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ABBREVIATIONS AND ACRONYMS

AGIP: *Azienda Generale Italiana Petroli.*

AMINOIL: American Independent Oil Company.

Art.: Article.

BIT: Bilateral Investment Treaty.

CAOC: California Asiatic Oil Company.

COL: City Oriente Limited.

Ibid: Same author, same book, same page.

ICC: International Chamber of Commerce.

ICJ: International Court of Justice.

ICSID: International Centre for Settlement of Investment Disputes.

Id: Same author, same book.

IFC: International Finance Corporation.

IPIECA: International Petroleum Industry Environmental Conservation Association.

IRCAN: Iranian Canada Oil Company.

JVA: Joint Venture Agreement.

LCIA: London Court of International Arbitration

LG&E: Louisville Gas and Electric

LIAMCO: Libyan American Oil Company.

Ltd: Limited.

NIOC: National Iranian Oil Company.

Nº: Number.

OECD: Organization for Economic Co-operation and Development.

OPEC: Organization of the Petroleum Exporting Countries.

p.: page.

Par.: paragraph

pp.: pages.

PSNR: Principle of Sovereignty of States over their Natural Resources.

RCC: Revolutionary Command Council.

RPSNR: Resolution on Permanent Sovereignty over Natural Resources.

TGN: *Transportadora de Gas del Norte*.

TOPCO: Texaco Overseas Petroleum Company.

UN: United Nations.

UNDP: United Nations Development Programme.

US: United States.

USA: United States of America.

US-PPI: United States Producer Price Index.

VAT: Value added tax.

Vol: Volume.

Vs.: Versus.

ABSTRACT

Stabilization clauses refer to the clauses in the investment contract that provide that any future changes of the host state's law that are detrimental to the investor will not be applied to the concerned contract.

Despite the actuality of stabilization clauses, the sovereignty of states enables states to put in place needed laws and applies in all sectors and activities. Economically, sovereignty enables a state to control its national economic life. In 1950s, there arose the principle of permanent sovereignty of states over their natural resources and basing on that principle, many developing countries to started contesting the validity of concession agreements which their governments had entered into with foreign investors. This research is concerned with examining that discrepancy in oil and gas contracts.

Even if the sovereignty of host states has been regarded as a justification of not enforcing stabilization clauses, under international investment law, it is provided that the agreement of the parties to an investment contract prevails, to the extent that the applicable law that they choose is the one to be referred to by the tribunal in case of dispute settlement. In the same vein, the principle of freedom of the contract allows the parties to determine the law that they want to govern their contract. This is the reason why stabilization clauses should be enforced in accordance with the principle of freedom of the contract as they are concerned with the law that governs the investment contract during its life.

However, a certain host state may be in the situation where it is requested to put in place laws to comply with international obligations especially those related to human rights and environment protection. Consequently, instead of preventing a certain state to manage its internal affairs through needed and relevant laws, stabilization clauses that are concerned with providing for the compensation in case of a host state action that is prejudicial to the investment project, are recommended.

Contents

0. GENERAL INTRODUCTION

I. BACKGROUND TO THE STUDY

This work entitled "**Enforceability of Stabilization Clauses in Oil and Gas Contracts**" is concerned with the assessment of the legal nature and implications of stabilization clauses integrated in long term international investment agreements in the sector of Oil and Gas.

Both the investor and the host state benefit from the project subject to the contract they entered into. However, in some cases, the host state may prefer other interests than those it sought in the investment agreement and this may make it rescind the said contract. In seeking the way they would be protected in such a case; international investors rely on the clauses that allow them not to be affected by any change in case the host states use their power in deciding the termination of the investment agreement. Those clauses are called stabilization clauses.

Stabilization clauses refer to the contractual protections that are incorporated into long term international investment agreements or concessions to make the said contract not be subject to comply with the change in law. The reason behind this kind of clauses is that over the life of the contract entered into by the foreign investor and the host state; the change in the laws and regulations in the host state may take place and this is likely to negatively affect the interests of the concerned investor especially in the economic perspective. Stabilization clauses aim at protecting the project from the risks that may be produced by such a change[1].

The law-making is one of the obligations of governments because it is presumed to be in the best interest of the public and it is obvious that it is in their power. The incorporation of stabilization clauses in investment agreement is often regarded as the way of limiting the government's power of making laws. This leads to wondering the legal basis of stabilization clauses, applicable rules to the stabilization clauses as well as their enforcement in the concerned host state. The work at hand is expected to examine those issues.

[1] J. Gjuzi, *Stabilization Clauses in International Investment Law: A sustainable Development Approach*, Bucerius, Law School, Springer, 2018, p.11, available at < https://www.springer.com/gp/book/9783319972312> accessed on January 16, 2019.

Various scholars agree that stabilization clauses can be traced to the period between the first and second World wars when there were increasing instances of host governments that were taking over concessionary contracts of foreign investors and this led to introducing stabilization clauses in concessionary agreements to ensure that those concessions would run their full term[2].

Stabilization clauses became popular in the 1960s due to nationalization and expropriation of petroleum industry assets by some oil producing nations who wanted to benefit from the increase in oil prices. Afterward, the interest in the use of stabilization clauses was remarkably diminishing and the scholars attributed that decrease to the UN Resolutions and writings of scholars in the 1970s that considered the stabilization clauses as being in conflict with the principle of sovereignty of states over their natural resources (PSNR) which must be exercised in the interest of their national development and wellbeing of their people[3].

Due to the mid-1980s terrible fall in mineral prices that greatly reduced the revenue developing countries received from their extractive industries, the concerned governments were encouraged to enact policies intended to attract foreign direct investment as a strategy of obtaining more revenue and this led to the unexpected comeback of stabilization clauses[4].

Nowadays, some jurisdictions have established legal principles that have the effect of invalidating stabilization clauses whereby it is deemed that the executive powers of the state may not be restrained by a contract with a private individual or corporation[5]. So long as there are some challenges in the enforcement of stabilization clauses, there arises the issue of effectiveness as well as the validity of those clauses.

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[2] J.N. Emeka, 'Anchoring Stabilization Clauses in International Petroleum Contracts' (2008) 42:4, *The International Lawyer*, at 1319, available at < https://scholar.smu.edu/cgi/viewcontent.cgi?article=1227&context=til > accessed on June 10, 2019.

[3] F. Sotonye, *Stabilisation Clauses and Sustainable Development in Developing Countries,* University of Nottingham, 2014, pp 10-12.

[4] *Id*, p.12

[5] D. Clinch and J. Watson, Stabilisation clauses -issues and trends', *Herbert Smith Freehills LLP*, 30 June, 2010, <https://www.lexology.com/library/detail.aspx?g=c5976193-1acd-4082-b9e7-87c0414b5328 >, (accessed on 23 May 2018).

II. PROBLEM STATEMENT

Stabilization clauses are contractual clauses in private contracts between investors and host states that address the issue of changes in law in the host state during the life of the project. Due to the fact that investments are subject to the laws of the host states, there is a risk for changes in domestic laws that may impact the investment. Particularly, the investment contract is affected in case the host state uses its power and expropriates the investor. Such incidents of expropriations have occurred at the global level, and caused investors to mitigate the risk of expropriation or ensure compensation for it[6].

According to S. H. Ingolfsson, the purpose of stabilization clauses is to ensure a certain degree of stability for the investment contract since those clauses are expected to limit the potential risk. Even though stabilization clauses are not incorporated in all investment contracts, they are common in long-term investment contracts like those concerning public infrastructure or in the extractive industries[7].

The author further stated that stabilization clauses are of a paramount importance for investors who believe that without that kind of clauses, foreign investment would not be possible in many parts of the world because stabilization clauses are necessary to ensure the legal and financial stability as well as predictability. Besides, it is crucial to note that the majority of lenders require the investors who are borrowers to incorporate the stabilization clauses in the investments agreements because they consider them a necessary means to ensure that the commercial security of a project is not damaged through amendments in legislation by the host state, something that might make the repayment of the loan impossible[8].

Stabilization clauses are regarded as the way of encouraging the investment since they provide a favorable investment climate. They are beneficial to both the investor itself and the lender of the project[9].

[6] S. H. Ingolfsson, *Stabilization Clauses in Investment Agreements*, Lund, Lund University, 2012, p.20
[7] *Id*, p.19
[8] *Id*, pp.20-21
[9] *Id*, p.21

Despite the necessity and the importance of stabilization clauses as illustrated above, this kind of clauses is said to be in conflict with the principle of state sovereignty in general, that allows a particular state to decide how to manage its internal affairs and in particular, the principle of sovereignty of states over their natural resources (PSNR) because the latter enables the host state to explore and exploit its natural resources without any interference[10].

The principle of permanent sovereignty over their natural resources is regarded by some states as a justification for the state's unilateral abrogation of a concession agreement irrespective of a stabilization clause incorporated in that investment agreement[11].

The said principle conceives that the right of peoples and nations to permanent sovereignty over their natural wealth and resources must be exercised in the interest of their national development and of the well-being of the people of the state concerned[12]. Besides, the UN Resolution 626 (VII) provides that the right of peoples to use and exploit their natural wealth and resources is inherent in their sovereignty while it also refers to the right of all member States to freely use and exploit their natural wealth and resources[13].

Furthermore, while, stabilization clauses are intended to protect investors, some advocacies on sustainable development, environment and human rights are of the view that the protection of investor rights in international agreements is not being balanced with the state duty to oblige investors to protect human rights since the investors' responsibility to respect those rights is being ignored. The advocates are of the opinion that investors' rights are being more privileged than the investors' obligations and they argue that the investors' rights are meant to meet some wider goal

[10] S.P. Ng'ambi, 'Permanent Sovereignty Over Natural Resources and the Sanctity of Contracts, From the Angle of Lucrum Cessans' (2015) 12: 2, *Loyola University Chicago International Law Review*, at 154, available at <https://lawecommons.luc.edu/cgi/viewcontent.cgi?article=1176&context=lucilr > accessed on June 10, 2019`
[11] *Ibid*.
[12] U.N General Assembly Resolution 1803 (XVII), 14 December 1962 available at <https://www.ohchr.org/Documents/ProfessionalInterest/resources.pdf > accessed on January 7, 2019.
[13] U.N General Assembly Resolution 626 (VII), 21 December 1952 available at <http://www.un-documents.net/a7-2361.pdf > accessed on January 7, 2019.

such as sustainable human development and economic growth and as a result, their rights and their responsibilities should go hand in hand[14].

Despite the fact that the foreign investor and the host state are the parties to an investment agreement; it is obvious that each party has its own interest. Furthermore, on the one hand, an investor is protected by the sanctity of the contract. On the other hand, the state has the duty to enact laws in the interest of its people and it thinks it has the justification of not enforcing contracts containing stabilization clauses whenever they are contrary to a state's freedom of exploiting its natural resources.

Clearly, investors are in need of contractual stability whereas host states are more concerned with the flexibility in order to maximize the benefit from their natural resources[15]. Stabilization clauses seek to protect investors' rights while the sovereignty of states empowers them to regulate in the public interest for the protection of human rights and for sustainable development. This kind of conflict is due to the discrepancy between international investment law and other fields of international law namely the international social and environmental law. While investment law in first place purports to protect economic human rights related to business, other human rights issues related to social and environmental issues are not in first place subject to international investment law since they belong to international social and environmental law domains. The problem arises at the stage of enforcement because host states balance the investment protection and public interest regulation and this necessitates the specific legal regime to produce the needed legal answers to the said issues[16].

Furthermore, as K. Gehne and R. Brillo point out, investment protection standards are broad and leave a margin of interpretation. The used interpretation may be in favor of either stabilization

[14] A. Shemberg, 'Stabilization Clauses and Human Rights', 28 March 2008, <http://www.oecd.org/investment/globalforum/40314647.pdf > accessed on 24 May 2018.
[15] Norton Rose Fulbright, *International Arbitration Report*, Report N° 7 (2016), at 20, available at <https://www.nortonrosefulbright.com/404?item=%2ffiles%2finternational-arbitration-report-issue-7-142408&user=extranet%5cAnonymous&site=NRFWeb> accessed on January 08, 2019.

[16]K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, March, p.5 available at < http://telc.jura.uni-halle.de/sites/default/files/BeitraegeTWR/Heft%20143.pdf > accessed on January 08, 2019.

commitments or of the view that states' obligations in terms of social and environmental fields that compel the concerned state to put in place the needed laws and regulations for public interest even though they may be detrimental to the stabilization clauses existing in the investment agreement in force[17].

The conflict of interests by the parties to an investment agreement where one party namely the host state is with the opinion that it is justified by its power to act in the interests of its people may push it to invalidate stabilization clauses whenever it finds it necessary and this would result in difficulties in the enforcement of the investment agreement.

The validity and enforceability of stabilization clauses are interdependent because in a given investment agreement, the enforcement may be affected by the validity of those clauses while in general, the validity of international investment agreements may also be affected by the reality of enforcement of such clauses. In this study, the following questions are to be assessed.

III. RESEARCH QUESTIONS

1. What is the legal nature of stabilization clauses both at the international level and in the host state?
2. Should the investors' interests overweigh public interest?
3. Are stabilization clauses against the principle of sovereignty of states over their natural resources?
4. Is the principle of sovereignty of states over their natural resources a justification of ignoring the sanctity of contracts?

[17] *Ibid.*

IV. HYPOTHESES

1. At the international level, stabilization clauses are governed by relevant international treaties and agreements and the customary international law of investment while at the domestic level, they are governed by the relevant legal rules existing in the host state at the time of entering into an agreement. However, in both cases, other law domains that are not investment law are also to be considered.

2. The investors' interests do not overweigh public interest and the latter's interests do not prevail the former's interests. The legal framework must allow each side to enjoy its rights without infringing the other's rights.

3. Stabilization clauses are not against the principle of sovereignty of states over their natural resources as long as the concerned host state freely entered into an agreement with the said clauses because the fact of entering into such an agreement is itself exercising the sovereignty power over the state's natural resources.

4. The principle of sovereignty of states over their natural resources does not imply a justification of ignoring the sanctity of contracts. However, in some instances, unforeseeable social and economic changes in a host state may necessitate not to comply with the stabilization clauses integrated in a given investment agreement entered into by the said host state. In this case, there arises the need of an adequate legal framework to regulate that situation.

V. PURPOSE AND SIGNIFICANCE OF THE STUDY

This study intends to examine the validity of stabilization clauses and hence whether they can easily be effective taking into consideration the interdependence of validity and enforcement of international investment agreements. Taking into account that stabilization clauses play a paramount role in protecting the rights and interests of investors and that the investment is beneficial for both the investor and the host state; this research is relevant since it intends to assess the validity and the enforcement of those important clauses incorporated in international

investment agreements in case of changes in law in order to examine whether the rationale and the purpose of the said clauses are in harmony with the expected outcomes.

VI. METHODOLOGY

The research at hand is a legal one; it means that various legal texts, decided cases, literatures, journals and on line sources shall be explored. In addition to exploring them, the emphasis will be put on case law analysis.

VII. SCOPE OF THE RESEARCH

This work is concerned with and limited to assessing the enforceability of stabilization clauses in the Oil and gas contracts. Though some concepts of international investment agreements may be referred to, in a strict sense, what shall be taken into account is the applicability of stabilization clauses in international investment agreements in the oil and gas sector. To be precise, this research assesses the applicability of the principle of state sovereignty in oil and gas contracts that a particular state enters into with foreign investors.

VIII. OUTLINE

The research comprises of four parts namely a general introduction, two chapters and a conclusion and recommendations.

The general introduction is made up of presentation of the topic, background of the study, problem statement, research questions, purpose of the study, significance of the study, the methodology, scope of the research, and outline.

The first chapter is entitled **the concept and rationale of stabilization clauses in international investment agreements**. This chapter deals with the notion of stabilization clauses, their logic, raison d'être, scope of stabilization clauses and opinions of various scholars vis-à-vis the enforcement of the said clauses. The chapter also makes a general overview of international investment agreements. The second chapter is entitled **analysis of selected tribunal awards**

concerned with stabilization clauses in the oil and gas contracts. It will assess the way in which arbitral tribunals have interpreted stabilization clauses and the challenges faced by investors in the execution of the said clauses. A general conclusion and recommendations close the study.

CHAPTER I: CONCEPT AND RATIONALE OF STABILIZATION CLAUSES IN INTERNATIONAL INVESTMENT AGREEMENTS

This chapter is concerned with the notion of stabilization clauses; the logic of the said clauses and the challenges they face. It examines the raison d'être of the stabilization clauses, their scope and the opinions of various scholars vis-à-vis the enforcement of the said clauses.

I.1. Concept of Stabilization Clauses

In some investment agreements between foreign investors and certain states, stabilization clauses are included. Stabilization clauses refer to the clauses in the investment contract that provide that any future changes of the host state's law that are detrimental to the investor will not be applied to the concerned contract. In this case, the interests of the host state and those of an investor are balanced and the long-term contract remains stabilized due to that it is not subject to regulatory changes[18].

According to L. Cotula, stabilization clauses imply a commitment by a host government not to alter the regulatory framework governing an investment contract either by legislation or any other means. In this case, the law applicable to the investment project is frozen on the time the agreement was entered into and remains during the life of the contract. The said clauses aim at stabilizing the terms and conditions of an investment project and thus contribute to the management of risks of that investment project. Stabilization clauses exist in various forms as they may preclude a state to nationalize, expropriate, modify the contract, etc.[19].

It is admitted that despite the above attempt to define stabilization clauses, their precise legal meaning and effect have never been fully clarified since some scholars and practitioners argue that the sovereignty of the states allows them to enact or change a law whenever the circumstances so necessitate and that stabilization clauses only oblige the host state to compensate the foreign

[18] R. Dolzer and C. Schreuer, *Principles of International Investment Law*, New York, Oxford University Press, 2008, p.75.

[19] L. Cotula, Regulatory Takings, Stabilization Clauses and Sustainable Development, a paper prepared for the OECD Global Forum on International Investment VII "Best Practices in promoting investment and development", in Paris 27-28 March 2008, available at <http://www.oecd.org/investment/globalforum/40311122.pdf> accessed on January 16, 2019.

investor protected by those clauses in case the said investor is affected by the regulatory change by the host state[20].

Though stabilization clauses in general are intended to protect a certain investment project during its life, there exist various types of stabilization clauses to which the following section will be devoted.

I.2. Types of Stabilization Clauses

There are three types of stabilization clauses that are categorized basing on the way in which they aim to protect the investor. Those are freezing clauses, economic equilibrium clauses and hybrid clauses[21].

I.2.1. Freezing Clauses

A freezing clause is a type of stabilization clause that aims at ensuring that a legal regime be it general or specific applicable to the investment project will not change over the life of the project. As M. Polkinghorne points out, this type of stabilization clause freezes the legal regime on the day the agreement was made and thus prohibits any future legislative change to be applicable to the investor. Despite the said intent of that kind of protection, freezing clauses are considered as inefficient since they cannot be a guarantee against the host state's sovereignty that allows the latter to put in place the needed laws and regulations in public interest. However, they may entitle the aggrieved investor to be compensated[22]. In oil contracts, freezing clauses are regarded as the most used clauses[23].

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[20] R. Dolzer and C. Schreuer, *Principles of International Investment Law*, see supra note 18.
[21] A. Shemberg, 'Stabilization Clauses and Human Rights, A Research project conducted for IFC and the United Nations Special Representative to the Secretary General on Business and Human Rights, March 2008' available at < http://documents.worldbank.org/curated/en/502401468157193496/pdf/452340WP0Box331ation1Paper01PUBLIC1.pdf > accessed on January 17, 2019.
[22] M. Polkinghorne, 'Stabilization Clauses and Periodic Review Outline' available at <https://energycharter.org/fileadmin/DocumentsMedia/Events/CCNG_2015_Michael_Polkinghorne.pdf> accessed on January 17, 2019.
[23] Impact of Stabilization Clause on Petroleum Agreements, available at < https://www.lawteacher.net/free-law-essays/commercial-law/impact-of-stabilization-clause-on-petroluem-agreements-commercial-law-essay.php > accessed on June 26, 2019.

I.2.2. Economic Equilibrium Clauses

For M. Polkinghorne, this type of stabilization clauses implies that although the new legal regime will apply to the investment project, the concerned investor will be compensated for the incurred loss in the course of complying with the new enacted laws. This kind of stabilization clauses considers that in case the host state enacts a legislation or takes an administrative measure that is prejudicial to the investor, the latter will be compensated by the host state according to the negotiations between the parties. As a result, economic equilibrium clauses do not restrict the host state in terms of law enactment or change but mitigate the impact of that legal change on the investor[24].

I.2.3. Hybrid Clauses

As A. Shemberg explains, hybrid clauses are a type of stabilization clauses that share some aspects of both the freezing clauses and the economic equilibrium clauses. Hybrid clauses aim at restoring the investor to the situation it had prior to the legal change and the said restoration may occur by exemption in a newly enacted law, by contract adjustment or by compensation to ensure that the investor is not financially affected by new laws[25].

In those three types of stabilization clauses, it is stated that the most used ones are freezing clauses which aim at ensuring that the law, fiscal regime or other economic conditions applicable to the investment will not change over the life of the project. Though they are regarded by some as unreliable because they are not a guarantee that the host state will not exercise the sovereign authority in public interest, freezing clauses remain important because in case they are violated, they entitle the aggrieved party to a higher amount of compensation than in the case where those clauses are not included in the contract[26].

[24] M. Polkinghorne, 'Stabilization Clauses and Periodic Review Outline', see supra note 22.
[25] A. Shemberg, 'Stabilization Clauses and Human Rights, A Research project conducted for IFC and the United Nations Special Representative to the Secretary General on Business and Human Rights, March 2008', see supra note 21.
[26] M. Polkinghorne, 'Stabilization Clauses and Periodic Review Outline', see supra note 22.

Despite the fact that those three types of stabilization clauses depend on the way in which they aim to protect the investor, all of them share a common rationale as discussed in the following section.

I.3. Rationale of Stabilization Clauses

Scholars opine that stabilization clauses are mostly integrated in investment contracts that are concerned with projects demanding huge amount of capital. The mostly concerned projects are related to infrastructure and extractive industry in the sectors of mining, oil, electricity, water and sewage, telecommunications and transport. Since these are capital-intensive and long-term projects, the concerned investors seem to be vulnerable in case of legal change while they need to recover the costs and generate profits. In this case, they seek the guarantee that changing investment conditions do not harm the cost-benefit equilibrium of the investment. Furthermore, through stabilization clauses, host states consider investors' interests and attract future investments as the latter believe and expect that they are guaranteed[27].

The same authors also assert that the rationale of stabilization clauses is the risk management for investment and it is obvious that the said clauses are beneficial for both the host state and the investor since the latter is protected through stabilization clauses whereas the former uses them as a tool of attracting investors[28].

A. Faruque opines that the primary function of stabilization clauses is to protect a foreign investor from subsequent changes in law of the host state which may be the source of governmental actions like nationalization or expropriation. In the presence of stabilization clauses, the prerogatives of the host state that would allow it to unilaterally modify the legal environment of the agreement already entered into, become inactive. The author further states that stabilization clauses result in a legal predictability and certainty which is important as it avoids the speculation as to what the law provides. Bearing in mind that certainty promotes efficiency for investment transactions while

[27] K. Gehne and R. Brillo, (2014), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, January, a working paper No 2013/46 available at <https://www.nccr-trade.org/fileadmin/user_upload/nccr-trade.ch/wp2/Stab_clauses_final_final.pdf > accessed on January 18, 2019.
[28] *Ibid*.

the future behavior of any government is uncertain, stabilization clauses are expected to play a significant role by providing in the present the solutions to the risks that may arise in the future[29].

I.4. Actuality of Stabilization Clauses

Stabilization clauses are not a myth or ideal, they are practical. It is reported that stabilization clauses began to be applied between the first and second World Wars when companies from the USA decided to include them in concession contracts in order to be safe from acts of nationalization by Latin American governments. From the mid-20th century till 1970s, stabilization clauses were used as a defense against expropriation especially in the petroleum sector[30].

Stabilization clauses went on to be applied till twenty first century. In 2008, a legal advisor to the United Nations Special Representative to the Secretary General on Business and Human Rights, Andrea Shemberg, conducted a research for IFC and her advisee. It was intended to examine whether stabilization clauses that are widely considered as a risk management tool in investment contracts, may affect a state's action in implementing its international human rights obligations[31].

In the said research, as A. Shemberg pointed out, 76 state-investor contracts with stabilization clauses constituted a sample: 24 contracts from the 1990s, 49 contracts from 2000s and 3 undated contracts but which were indicated to be from one of those two periods. The said contracts were concerned with various industries including the extraction of natural resources like oil and gas and their duration generally ranged from 10 years to 25 years or more and that implied that some of them are still in force[32].

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[29] A. Faruque, 'Validity and Efficacy of Stabilization Clauses: Legal Protection vs. Functional Value' (2006), 23:4 *Journal of International Arbitration,* at 321-322, available at <https://is.muni.cz/www/seidel/23073893/Faruque-Validity.pdf> accessed on January 18, 2019.

[30] P.D. Cameron, 'Stabilisation in Investment Contracts and Changes of Rules in Host Countries: Tools for Oil & Gas Investors' available at <https://www.international-arbitration-attorney.com/wp-content/uploads/arbitrationlaw4-Stabilisation-Paper.pdf > accessed on January 22, 2019.

[31] A. Shemberg, 'Stabilization Clauses and Human Rights, A Research project conducted for IFC and the United Nations Special Representative to the Secretary General on Business and Human Rights, March 2008', see supra note 21

[32] *Ibid.*

The states that were parties in the said contracts were located in Sub-Saharan Africa, East Asia and Pacific, Middle East and North Africa, Eastern Europe, Southern Europe, Central Asia, South Asia, Latin America and the Caribbean[33].

Those are the facts that clearly show that stabilization clauses are considered for a long time in various parts of the World and in various sectors of activity. The fact that stabilization clauses are practical necessitates an efficient legal framework for them to be productive.

Stabilization clauses have been subject to criticisms from some human rights advocates. The latter argue that human rights law requires states to protect human rights from interference by private parties including investors. In that case, enactment and enforcement of laws that are concerned with the behavior of investors is one of the methods by which a state fulfills its international human rights obligations. As a result, a state's failure to regulate and enforce its regulations against investors' companies constitutes the violation of state's international human rights law obligations in the areas of non-discrimination, health and safety, employment and environment. The said human rights advocates also argue that stabilization clauses can lead to making foreign investors immune from social and environmental legal instruments, regulations and policies that come into existence after the date of investment contract conclusion[34].

Despite the said criticisms, some authors indicate that stabilization clauses did not cease to be included in investment contracts. However, the practice reveals that the preference of investors has gradually shifted from freezing clauses to economic equilibrium clauses because the latter are more favorable than the former due to the fact that in case of arbitration as a dispute settlement method, economic equilibrium clauses are easily enforceable compared to freezing clauses[35].

[33] *Ibid.*
[34] *Ibid.*
[35] D. Clinch and J. Watson, Stabilisation clauses -issues and trends', *Herbert Smith Freehills LLP*, see supra note 5.

I.5. Legal nature of Stabilization Clauses

The legal nature of a particular matter implies the legal rules applicable to it. Stabilization clauses being the terms of an international investment contract, are governed by international investment law which among others is concerned with contracts between an investor and a host state.

R. Dolzer and C. Shreuer note that the rules governing contracts between an investor and a host state are of a hybrid nature since they are subject to both private and public law. They also establish a link between domestic law and public international law[36]. This is explained by S. W. Schill who considers that on the one hand, international investment law is a public law domain since it conceives the relationship among states by putting in place the standards for the protection of investors and hence harmonizes the way in which investors must be treated at the global level. So long as, it creates those states' obligations, it becomes a public law domain since it is concerned with the relationship among public entities namely the states[37].

On the other hand, as S.W. Schill also points out, international investment law becomes a private domain since it deals with investment contracts that are considered as private contracts between private parties since in that situation a concerned host state behaves as a private party acting by way of doing business (*de jure gestionis*)[38].

The governments retain the power to enact laws including those governing investment. Though the said laws are subject to international standards as stated above, they remain domestic laws. Besides, the core purpose of stabilization clauses is to make the investment contract be governed by the applicable law in the host state at the time of contract conclusion. For this reason, the domestic law is pertinent especially when chosen by the parties as the applicable law.

The principle is that international standards have the primacy over the domestic law[39]. So long as, international investment in general and stabilization clauses in particular are dealt with by both

[36] R. Dolzer and C. Schreuer, *Principles of International Investment Law*, see supra note 18, p.3.
[37] S.W. Schill, *International Investment Law and Comparative Public Law*, Oxford, Oxford University Press, 2010, p. 836.
[38] *Ibid*.
[39] *Ibid*.

international and domestic law, and since they are subject to both public and private law, they necessitate a separate and specific legal regime to regulate them, and that is none other than international investment law. The said field of law is concerned with international law, domestic law, public law and private law, something that makes international investment as well as stabilization clauses to fall under the said field of international investment law.

Taking into consideration the pertinence of the host state's law vis-à-vis investment project as discussed above and considering the sovereignty of a state which involves legislation whenever deemed necessary, the sovereignty has much to do with stabilization clauses and it may even be prejudicial to the enforcement of the said clauses if it is exercised in a manner that is contrary to the investment agreement.

I.6. Sovereignty of States as a major threat to Stabilization Clauses

According to K. Hossain, under international law, sovereignty has been considered peremptory norm (*jus cogens*). In this regard, sovereignty is a rule to which no derogation is permitted[40]. In sub-sections below, that norm is discussed vis-à-vis stabilization clauses.

I.6.1. Sovereignty of States in general

Generally, national sovereignty means non-interference by external powers in the internal affairs of a particular state[41]. It is a principle that is recognized under international law as it is provided for by the UN Charter that "*nothing contained in the present Charter shall authorize the United Nations to intervene in matters which are essentially within the domestic jurisdiction of any state or shall require the Members to submit such matters to settlement under the present Charter*"[42].

Thus, in principle, internal affairs of a particular state are exclusively in the power of the concerned government since other states and international organizations are prohibited to interfere.

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[40] K. Hossain, 'The Concept of Jus Cogens and the Obligation Under The U.N. Charter' (2005) 3:1 *Santa Clara Journal of International Law*, at 89, available at <https://digitalcommons.law.scu.edu/cgi/viewcontent.cgi?article=1011&context=scujil> accessed on August 6, 2019.

[41] R.M. Wallace, *International Law*, 4th Ed, London, Sweet & Maxwell, 2002, p.58.

[42] Charter of the United Nations, art.2 (7), available at <https://treaties.un.org/doc/publication/ctc/uncharter.pdf> accessed on February 19, 2019.

I.6.2. Principle of Permanent Sovereignty of States over their Natural Resources

The sovereignty of states is not limited and hence applies in all sectors and activities. Economically, sovereignty enables a state to control its national economic life. In this perspective, since 1952, there arose the principle of permanent sovereignty of states over their natural resources which was considered as a right to development for the countries that were colonized because in the said countries, economic activities were dominated by foreign companies[43].

R. Pereira and O. Gough indicated that the decolonization period facilitated many developing countries to start contesting the validity of concession agreements which their governments had entered into with foreign investors or which were imposed during the colonization for exploration and exploitation of natural resources. The major argument supporting the contention of the said concession agreements was that they tended to be largely one-sided as the developing countries used to consider them as strongly favoring the interests of the concerned foreign investors[44].

It is reported that in a bid to reinforce the sovereignty of newly independent and other developing states and to secure the benefits of natural resource exploitation, on December 14th, 1962, the UN General Assembly Resolution on Permanent Sovereignty over Natural Resources (RPSNR) was adopted[45].

The RPSNR recognized the right of the host state to nationalize and expropriate the property of the foreign investor, provided that appropriate compensation is paid. The said Resolution also

[43] N.Q.Dinh, *Droit International Public*, 6th Ed, Paris, L.G.D.J, 1999, pp.996-997.
[44] R. Pereira and O. Gough, 'Permanent Sovereignty over Natural Resources in the 21st Century: Natural Resource Governance and the Right to Self-determination of Indigenous Peoples under International Law' (2013) 14, *Melbourne Journal of International Law*, at 455-456, available at <http://classic.austlii.edu.au/au/journals/MelbJIL/2013/15.pdf > accessed on February 19, 2019.
[45] Preamble of the General Assembly resolution 1803 (XVII) of 14 December 1962, "Permanent sovereignty over natural resources" available at <https://www.ohchr.org/EN/ProfessionalInterest/Pages/NaturalResources.aspx > accessed on August 6, 2019.

stated that it is each country's rights to choose its own economic system and exercise sovereignty over natural resources[46].

In addition to the Resolution on Permanent Sovereignty over Natural Resources (RPSNR), in 1974, the UN General Assembly adopted the Charter of Economic Rights and Duties of States.

This said charter provides that every state is allowed to freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities. It also provides that each state has the right to regulate and exercise authority over foreign investment within its national jurisdiction according to its laws and regulations and in conformity with its national objectives and priorities, and that no State shall be compelled to grant preferential treatment to foreign investment[47].

The UN Charter of Economic Rights and Duties of States in its article 2, paragraph 2, also provides that each state has the right to regulate and supervise the activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its laws, rules and regulations and conform to its economic and social policies. It also provides that transnational corporations are not permitted to intervene in the internal affairs of a host State and that in case of a compensation dispute, the applicable law will be the domestic law of the host state[48].

While stabilization clauses seek that the concerned investment contracts do not be concerned with newly elected laws, the principle of sovereignty and the aforementioned legal instruments assert that the concerned host states can put in place the needed law whenever necessary and that the said states should not be subjected to being interfered by multinational companies.

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[46] Declaration of General Assembly through Resolution on Permanent Sovereignty over Natural Resources, available at <https://www.ohchr.org/EN/ProfessionalInterest/Pages/NaturalResources.aspx > accessed on August 6, 2019.

[47] UN Charter of of Economic Rights and Duties of States, art.2 (1), available at <https://www.aaas.org/sites/default/files/SRHRL/PDF/IHRDArticle15/Charter_of_Economic_Rights_and_Duties of_States_Eng.pdf > accessed on February 19, 2019.

[48] *Id*, art.2 (2, b).

In particular, the concerned host states have the right to regulate and supervise the activities of transnational corporations within their national jurisdictions and take measures to ensure that those activities comply with their laws, rules and regulations; to freely exercise full permanent sovereignty, including possession, use and disposal, over all its wealth and natural resources. They have also the power to nationalize and expropriate the property of the foreign investor[49].

In our analysis; it is evident that the said host states 'prerogatives of making laws, ensuring their enforcement, regulating and supervising transnational companies and the right to the countries' national resources are prejudicial to the core purpose of stabilization clauses. As a result, the enforcement of the said clauses is likely to be challenged by the said host states 'prerogatives.

I. 6.3. Exercise of Permanent Sovereignty over Natural Resources by some States: Case Study of Tanzania

Basing on the principle of Permanent Sovereignty over Natural Resources and the relevant international legal instruments as said above, some states have put in place the relevant domestic legal instruments that are concerned with the exploitation or extraction of their natural resources. For instance, in July 2017, the United Republic of Tanzania enacted the Natural Wealth and Resources (Permanent Sovereignty) Act which proclaims that the people of the United Republic of Tanzania have permanent sovereignty over all natural wealth and resources and that the ownership and control over them are exercised by and through the government on behalf of the people[50].

The said Act also provides that the natural wealth and resources are inalienable in any manner, that they remain the property of the people of the United Republic of Tanzania and that they are held in trust by the President of the said Republic on behalf of its people. For that purpose, all activities and undertakings related to the exploitation of wealth and natural resources in that

[49] A.F.M. Maniruzzaman, 'Damages for Breach of Stabilisation Clauses in International Investment Law: Where Do We Stand Today?' available at <https://www.academia.edu/586614/Damages_for_Breach_of_Stabilisation_Clauses_in_International_Investment_Law_Where_Do_We_Stand_Today > accessed on June 13, 2019.

[50] The Natural Wealth and Resources (Permanent Sovereignty) Act, 2017, the Gazette of the United Republic of Tanzania No 27 Vol. 98 dated 7th July, 2017, Section 4.

country are to be conducted by the government on behalf of the people of the very country even though that government where it considers necessary, may authorize any other person to do so in accordance with the laws of Tanzania[51].

The said permanent sovereignty Act further provides that any arrangement or agreement for the extraction, exploitation or acquisition and use of natural wealth and resources that does not fully secure the interests of the people is prohibited and becomes unlawful once occurs. In the same vein, any related investment must ensure the respect of the principle of permanent sovereignty over natural wealth and resources[52].

Regarding the Permanent Sovereignty Act, it protects permanent sovereignty over natural wealth and resources through the prohibition of judicial proceedings in foreign courts[53], while it obliges state organs including the judicial authorities to respect the said principle of permanent sovereignty over natural wealth and resources[54]. In this case, only the courts and tribunals of Tanzania are competent over the disputes arising from the extraction, exploitation, acquisition or use of natural wealth and resources while it is also their duty to protect it. As long as, the government is presumed to conduct the activities related to the exploitation of wealth and natural resources on behalf of the people, it is also presumed that whatever the government does, is in the interest of the people. Consequently, the seized courts and tribunals seem to be subjected to decide in favor of the government for the sake of protecting the permanent sovereignty over natural wealth and resources due to the fact that in that context, it is their duty to protect what is conducted by the government.

In July 2017, Tanzania did not only enact the Natural Wealth and Resources (Permanent Sovereignty) Act but also enacted the Natural Wealth and Resources Contracts (Review and Re-negotiation of Unconscionable Terms) Act. The latter empowers the Parliament to review any arrangement or agreement relating to natural wealth and resources made by the government. This is provided for the effectiveness of the principle of permanent sovereignty over natural wealth and

[51] *Id*, section 5.
[52] *Id*, section 6.
[53] *Id*, *section* 11.
[54] Id, s*ection* 6 (3).

resources that implies that the negotiation in every arrangement or agreement is concluded in good faith and in a fair manner so as to observe the interests of the people of Tanzania[55].

For the execution of that, all contracts are subject to being reported to the Parliament (National Assembly) within six (6) sitting days of National Assembly starting to count from the day the said contracts were made. In case a concerned contract is found to contain unconscionable terms or when it is considered to be prejudicial to the interests of the People of the United Republic of Tanzania, the National Assembly through resolution, advises the government to initiate the re-negotiation for the purpose of rectifying the terms of the contract[56].

As per the Natural Wealth and Resources Contracts (Review and Re-negotiation of Unconscionable Terms) Act, 2017, the terms of the contract are deemed unconscionable and treated as such when they contain any provision with aims that include but not limited to restricting the right of the State to exercise full permanent sovereignty over its wealth, natural resources and economic activity; restricting the right of the State to exercise authority over foreign investment within the country and in accordance with the laws of Tanzania; restricting periodic review of a contract which purports to last for life time; restricting the right of the State to regulate activities of transnational corporations within the country and to take measures to ensure that such activities comply with the laws of the land; or which are by nature empowering transnational corporations to intervene in the internal affairs of Tanzania[57].

In this regard, the stabilization clauses may be qualified as unconscionable terms since they seek that the contracts that they are a part of be governed by the law applicable at the time the contract is made. The fact that contracts are tied to the law applicable at the time the contract is made, might be considered as a way of restricting the periodic review of the contract that they are subjected to, or the way to restrict a state to exercise authority over foreign investment within the country and in accordance with the laws of the host State namely Tanzania or also the way of restricting the right of the State to regulate activities of transnational corporations within the country. In his case,

[55] The Natural Wealth and Resources Contracts (Review and Re-negotiation of Unconscionable Terms) Act, 2017, the Gazette of the United Republic of Tanzania No. 27 Vol. 98 dated 7th July, 2017, section 4.
[56] *Id*, section 5.
[57] *Id*, section 6.

the stabilization clauses may face the challenge of not being enforced as expected by the concerned investor due to being considered as unconscionable terms.

The provisions of the two Acts mentioned above are in conformity with the Constitution of the United of the Republic of Tanzania since the latter provides that the activities of the government are to be conducted in a manner that ensures that the natural wealth is preserved and exploited for common good and that it is used for the development of the people[58].

With regard to dispute settlement, the Natural Wealth and Resources (Permanent Sovereignty) Act, 2017 provides that permanent sovereignty over natural wealth and resources is not a subject of proceedings in any foreign court or tribunal and that disputes arising from extraction, exploitation or acquisition and use of natural wealth and resources must be adjudicated by judicial bodies or other organs established by the laws of the United Republic of Tanzania. As a result, the said judicial bodies or other related bodies and application of laws of Tanzania must be acknowledged and incorporated in any arrangement or agreement[59].

This does not guarantee the protection of investors since decision makers in a dispute settlement are one sided as they may be influenced by the government of which they are employees and nationals. In an investment dispute settlement, as K.V.S.K Nathan points out, every decision maker must be and remain impartial and independent of the parties to a dispute. He or she must not have a personal or professional relationship with any of the parties because prior and ongoing relationships with the parties may affect his or her independence and impartiality[60].

In 2001, Tanzania and the Netherlands had entered into a bilateral investment treaty (BIT) on encouragement and reciprocal protection of investments. The said BIT entered into force on April 01, 2004. The said BIT has been opposed by civil society in both Tanzania and the Netherlands as biased towards the Netherlands and not in public interests. It is reported that the said BIT was not

[58] The Constitution of the United Republic of Tanzania of 1977 as amended in 2005, art.9, available at <https://www.wipo.int/edocs/lexdocs/laws/en/tz/tz008en.pdf> accessed on February 21, 2019.
[59] The Natural Wealth and Resources (Permanent Sovereignty) Act, 2017, see supra note 50, section 11.
[60] K.V.S.K. Nathan, 'The Independence of Arbitrators' (2006), Issue No: 68, *Amicus Curiae*, at 18, available at <https://sas-space.sas.ac.uk/2927/1/Amicus68_Nathan.pdf> accessed on June 26, 2019.

consistent with legal reforms that Tanzania has recently adopted since its newly Acts related to permanent sovereignty over natural resources and wealth provide that disputes settlements are in the power of local arbitration and national courts while the BIT provided that investors could sue a host state at the International Centre for the Settlement of Investment Disputes.[61]

The said BIT provided that unless notice of termination has been given by either contracting party at least six months before the date of expiry of its validity, it should be extended tacitly for periods of ten years whereby each contracting party reserves the right to terminate the agreement upon notice of at least six months before the date of expiry of the current period of validity[62].

As it is so provided, the Government of Tanzania notified the Government of the Netherlands of its intention to terminate the BIT between both nations. As a result of that notice, the BIT was terminated on April 01, 2019 as the date of its expiry. Proponents of BIT termination complained among other issues that the said BIT did not provide for the right of the host country to introduce new laws, rules and regulations on investment which would apply to every investor, including those protected under the BIT[63].

Article 14 (3) of the said BIT provides that investments made before the termination of the BIT agreement are to be governed by BIT agreement articles within a further period of fifteen (15) years[64]. This is a kind of stabilization clauses since it implies that any government action cannot affect existing investment contracts within a period of 15 years.

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61 Tanzania Terminates Bilateral Investment Treaty with the Netherlands available at < https://www.africalegalnetwork.com/tanzania/news/legal-alert-tanzania-terminates-bilateral-investment-treaty-netherlands/ > accessed on June 26, 2019.

62 Agreement on encouragement and reciprocal protection of investments between the United Republic of Tanzania and the Kingdom of Netherlands, art.14 (2) available at <https://arbitration.org/sites/default/files/bit/netherlands_united_republic_of_tanzania_english.pdf > accessed on June 13, 2019.

63 Tanzania Terminates Bilateral Investment Treaty with the Netherlands available at < https://www.africalegalnetwork.com/tanzania/news/legal-alert-tanzania-terminates-bilateral-investment-treaty-netherlands/ >, see supra note 61.

64 Agreement on encouragement and reciprocal protection of investments between the United Republic of Tanzania and the Kingdom of Netherlands, see supra note 62, art.14 (3).

However, despite the sovereignty of host states that is regarded as a justification of not enforcing stabilization clauses, under international investment law, it is provided that the agreement of the parties to an investment contract prevails, to the extent that the applicable law that they choose is the one to be referred to by the tribunal in case of dispute settlement[65]. In the same vein, the principle of freedom of the contract allows the parties to determine the law that they want to govern their contract. For that reason, stabilization clauses should be enforced in accordance with the principle of freedom of the contract as they are concerned with the law that governs the investment contract during its life.

Besides, some scholars are of the view that stabilization clauses do not limit the state's sovereignty. They instead argue that a state's agreement to be bound by a stabilization clause should be considered a valid exercise of that state's sovereignty[66].

According to S. Ng'ambi, stabilization clauses aim at ensuring that the future changes in the legislation of a host state will not affect the investment agreement entered into by a certain investor and the concerned host state. In this case, the investment agreement is fixed to the applicable law at the time the investment contract is concluded[67].

In international law, the principle of sovereignty of states entails the power to make laws and enforce them[68]. It is also a duty of a government to enact the laws whenever it is in the interest of the public[69].

In particular, the principle of permanent sovereignty allows states to freely use and exploit natural wealth and resources for their economic development. Some states consider the said principle as a

[65] Convention on the Settlement of Investment Disputes between States and Nationals of other States, art.42 (1) available at <https://icsid.worldbank.org/en/documents/icsiddocs/icsid%20convention%20english.pdf> accessed on February 20, 2019.
[66] D. Clinch and J. Watson, Stabilisation clauses -issues and trends', see supra note 5.
[67] S. Ng'ambi, 'Stabilisation Clauses and the Zambian Windfall Tax' (2011) 1:1 *Zambia Social Science Journal*, at 109, available at < https://scholarship.law.cornell.edu/cgi/viewcontent.cgi?article=1006&context=zssj> accessed on February 22, 2019.
[68] W.P. Nagan and C. Hammer, 'The Changing Character of Sovereignty in International Law and International Relations', *University of Florida Levin College of Law*, 2004, available at <https://scholarship.law.ufl.edu/cgi/viewcontent.cgi?article=1592&context=facultypub> accessed on June 05, 2018.
[69] I.Bogdanovskaia, 'The Legislative Bodies in the Law-making Process' available at <https://www.nato.int/acad/fellow/97-99/bogdanovskaia.pdf > accessed on June 05, 2018.

justification to unilaterally abrogate a concessionary agreement notwithstanding the stabilization clauses incorporated therein[70].

The main concern is that in practice; even courts and arbitration tribunals have different approaches on whether host states have the power that justifies them in not enforcing stabilization clauses. One of the reasons behind interpreting stabilization clauses differently is the discrepancy between international investment law and other law domains like international social and environment law[71].

I.7. Discrepancy between International Investment Law and International Social and Environment Law

Law of investment is a branch of a law that specifically regulates investment. Investment law may be either international law on foreign investment or national law. International law on foreign investment is a set of rules that govern international investment. In this case, it regulates the entry of foreign investment in a host country and also addresses how a foreign investor is treated in a host state[72].

Regarding, international social law, it is concerned with human rights. The said human rights are categorized in civil, political, economic and cultural rights. Civil rights aim at ensuring people's integrity and safety, whereas political rights are concerned with taking part in public affairs, freedom of opinion and expression and the right to vote or to be elected. As for economic, social and cultural rights, they aim at ensuring that individuals can access economic, social and cultural aspects. They include right to education, adequate housing, food, water, the highest standard of health, right to work and rights at work, right to social security, the cultural rights of minorities, etc.[73]

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[70] S.P. Ng'ambi, see supra note 10.
[71] K. Gehne and R. Brillo, Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 27.
[72] T. Abate, 'Definition and Nature of Investment Law', April 09, 2012, available at <https://www.abyssinialaw.com/about-us/item/486-definition-and-nature-of-investment-law> accessed on February 22, 2019.
[73] E.G. Çamur, 'Civil and Political Rights vs. Social and Economic Rights: A Brief Overview' (2017) 6:1 *Journal of Bitlis Eren University Institute of Social Sciences,* at 205-214, available at <http://dergipark.gov.tr/download/article-file/318915 > accessed on February 22, 2019.

With respect to international environmental law, it refers to a body of rules that are concerned with the protection of environment primarily through multilateral and bilateral international agreements. Its sources are customary international law, international treaties and judicial decisions of international courts. Sovereignty is one of the principles that the international environmental law is based on. It implies that states have sovereign rights over their natural resources, that such a right of peoples and nations to permanent sovereignty over their natural resources and wealth must be exercised in the interest of their national development and of the wellbeing of the people of a given state. International agreements and tribunals recognize permanent sovereignty over natural resources and wealth as a reflection of international customs[74].

It is evident that international investment law, international social law and international environmental law are all of great importance. A given State is duty bound to promote all those fields of law since it is subject to the promotion of investment and to the promotion and protection of human rights and environment.

As said above, there is a kind of discrepancy between international investment law and other fields of law such as international social and environment law. Developing law on the protection of human rights and environment creates instability on the law that was designed with a single objective of foreign investment protection. In order to efficiently protect human rights and environment, a government must exercise its regulatory right and intervene in circumstances where investors' activities abuse human rights or endanger environment. Though the government has the duty of promoting investment, it has also the duty of protecting human rights and environment and these may be protected through regulating investment activities[75].

Though investment is beneficial due to its commercial interests, wider societal values must also be considered because investment activities are of economic nature while other aspects such as human rights and environment must not be ignored. In case some investment activities go on

[74] M.V. Soto, 'General Principles of International Environmental Law' (1996) 3:19, *ILSA Journal of Int'l & Comparative Law*, at 194, available at <https://core.ac.uk/download/pdf/51089370.pdf> accessed on February 22, 2019.
[75] M. Sornarajah, *The International Law on Foreign Investment*, 3rd Ed, New York, Cambridge University Press, 2010, pp 77-79.

disregarding human rights and environment, they will be undermined since some principles of human rights are fundamental to the extent that no derogation to them is permitted (*ius cogens* status)[76].

That challenge that the investors may face with regard to the compliance with other laws other than investment law, is due to the discrepancy between international investment law and other fields of law such as international social and environment law. The purpose of investment law in the first place is the protection of economic human rights such as freedom to trade and property rights related to business activities whereas other human rights that are relevant to social and environmental issues are not primarily subject to international investment law because they fall under the regulation of other domains of international law such as international social or environmental law[77].

As long as stabilization clauses serve as intermediary between the investment contracts and the application of other laws including those regulating environment, they are more concerned with the said discrepancy between international investment law and other fields of law such as international social and environment law with regard to what each of these domains regulates in the first place.

However, the discrepancy between investment protection and other fields of human rights and environmental protection standards mostly arises in case of interpretation as the investment protection standards remain relatively broad and subsequently leave a margin of interpretation that allows to reconcile obligations of states in the social, environmental and investment fields[78]. An adequate interpretation of stabilization clauses inserted in international investment contracts emanates from an appropriate understanding of purpose and scope of the said stabilization clauses.

[76] *Ibid*.
[77] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 16.
[78] *Ibid*.

I.8. Scope of application of Stabilization Clauses

Stabilization clauses are concerned with any law that affects the economic conditions of the contract. As a result, the scope of stabilization clauses includes but is not limited to property; fiscal regime; labor legislation and export-import provisions[79]. As stated above, concerns have been raised that stabilization clauses limit a State's ability to effectively legislate in terms of its international environmental and international human rights obligations. Due to those concerns, States do not like to be restrained and it becomes harder for investors to legitimately argue that amendments in environmental or human rights laws should not be introduced[80].

In any case, contract provisions regarding stabilization clauses must be constitutional and legal. The constitutionality and legality of the stabilization clauses remain important because in case they are illegal or inconsistent with the constitution of a concerned host state, they would be unenforceable, something that makes them become inefficient[81].

Indeed, for stabilization clauses to be enforceable, they need to be legal and valid. Their purpose and scope also play a significant role when it comes to the stage of their implementation. As the stabilization clauses were said to violate the sovereignty of host states, there are some interpretative approaches that are helpful in the assessment of what stabilization clauses intend and whether they are really prejudicial to the sovereignty of states.

As K. Gehne and R. Brillo point out, those approaches are the argument of implicit compliance with international law exceptions; the argument referring to general law; the argument referring to national law of fundamental importance; the argument referring to evolutionary new norms and standards; the argument of good faith and the investor's due diligence; and the argument of systematic integration and harmonized law interpretation[82].

[79] M. Polkinghorne, 'Stabilization Clauses and Periodic Review Outline', see supra note 22.
[80] *Ibid*.
[81] P.D. Cameron, 'Stabilisation in Investment Contracts and Changes of Rules in Host Countries: Tools for Oil & Gas Investors' see supra note 30.
[82] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 71.

I.8.1. Argument of implicit compliance with International Law exceptions

States are bound to respect core human rights treaties[83]. Besides, though states have the sovereign right to exploit their own resources, they have also the duty to ensure that the activities within their jurisdiction or control do not harm environment[84]. The argument of "implicit compliance with international law exceptions" considers those international human rights obligations and environmental protection obligation to be excluded from being concerned with the stabilization clauses since a host state is bound to comply with them and hence obliged to regulate in those domains whenever it is deemed necessary[85].

This argument implies the interpretation by excluding social and environmental public interest regulation from the scope of stabilization clauses. In this case, stabilization clauses are regarded as that they do not prevent host states to progressively realize human rights because a state sovereignty is limited by international obligation to recognize fundamental human rights. Stabilization clauses are implicitly limited by compliance with international law exceptions because a host state cannot impair the human rights held by individuals that may be affected by an investment project.[86]

K. Gehne and R. Brillo note that as a matter of fact, States do not commit themselves not to comply with international obligations. That is the reason why they prefer to compensate investors for regulating with the purpose of acting in conformity with the said international obligations. As a result, stabilization clauses do not hinder states to adopt public interest measures. Instead, they provide for compensation for a loss incurred by an investor due to the changes in regulation[87].

[83] *Id.* p.30.
[84]The Rio Declaration on Environment and Development (1992), Principle 2, available at <http://www.unesco.org/education/pdf/RIO_E.PDF> accessed on February 27, 2019.
[85] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, pp. 30-31see supra note 82.
[86] *Ibid*.
[87] *Id*, p.30.

I.8.2. Argument referring to general law

As K. Gehne and R. Brillo also point out, this argument is concerned with the interpretation that is given to the meaning of "changes in law". It suggests that the changes or measures based on international obligations or constitutional principles that were existing at the time the investment contract was concluded but which have not yet been fully implemented by the host state, do not constitute a change in applicable law[88].

The abovementioned authors further state that in case a host state takes the measures to implement those international obligations or national constitutional principles, it applies those norms but does not change the existing general law and they are not subject to the compensation for any changes in the applicable laws stipulated by stabilization clauses[89].

It is aldo K. Gehne and R. Brillo's view that a specific law that is enacted in order to implement general norms of international or constitutional law ought to be considered as *lex specialis* intended to protect fundamental human rights and hence fulfill the relevant obligations. However, this does not make the said *lex specialis* the new law because there is an existing general law being implemented by that *lex specialis*[90].

As a result, the foregoing authors opine that even when stabilization clauses provide for compensation in case of changes in law, states measures implementing the requirements of constitutional law or international obligations of the state that existed at the time when the contract was concluded, would not be in the scope of stabilization clauses; those measures would not be subject to compensation because the enacted laws are to be interpreted as the mere interpretation of the law that existed at the time of contract conclusion[91].

[88] *Id*, p.31.
[89] *Id*, p.32.
[90] *Ibid*.
[91] *Ibid*.

I.8.3. Argument referring to national law of fundamental importance

K. Gehne and R. Brillo also recall the principle of international law stipulating that a state party to an international treaty may not invoke the provisions of its internal law as a justification for its failure to perform the obligations conceived by a particular international treaty[92]. However, there is an exception to that principle because a state is allowed not to comply with an international treaty to which it is a party when that state expressed the consent to be bound by that treaty that is contrary to its internal law of fundamental importance[93].

According to K. Gehne and R. Brillo, the argument referring to national law of fundamental importance is operational when an investor-state contractual relationship is elevated to international law as the governing law in the contract. In such a case, the said investment contract may face the challenge of not being enforced due to that it affects the fundamental constitutional principles of the host state. This is for instance when the government entered into an investment agreement without the consent of the parliament that is constitutionally required[94].

The abovementioned scholars explain that in this case, it is up to the investor to be diligent and be aware of the national law of fundamental importance when negotiating and concluding contracts with the host state. When stabilization clauses constitute the terms of an investment contract that was elevated to international law as the governing law, they cannot be effective as long as their enforcement cannot in conformity with the national law of fundamental importance[95].

I.8.4. Argument referring to evolutionary new norms and standards

The argument referring to evolutionary new norms and standards implies that though there exist the contractual obligations between the parties to a contract that must be executed, new norms and

[92] Vienna Convention on the Law of Treaties, art.27, available at <https://treaties.un.org/doc/publication/unts/volume%201155/volume-1155-i-18232-english.pdf> accessed on February 27, 2019.
[93] *Id*, art.46.
[94] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 85, pp.32-33.
[95] *Id*, p.33.

standards that may arise are also to be considered as there is an exception (*rebus sic stantibus*) to the principle *pacta sunt servanda*[96].

The argument referring to evolutionary new norms and standards was developed by International Court of Justice in the *Gabcikovo-Nagymaros* case (Hungary vs. Slovakia). As far as the facts of this case are concerned, in 1977, Hungary and Czechoslovakia signed a Treaty for the construction of dams and other projects along the Danube River that bordered those both nations. It was concerned with the development of water resources, energy, agriculture, transport and other sectors of national economy of contracting countries[97].

The treaty provided for the building of two series of locks, one at Gabcikovo (in Czechoslovak territory) and the other at Nagymaros (in Hungarian territory), to constitute a single and indivisible operational system of works. Both Czechoslovakia and Hungary began works on their respective territories but in 1989, Hungary stopped performing the expected obligations on her territory due to reasons of changes of circumstances required by environment protection norms as it has so invoked. The two parties entered into negotiation about the issue but failed to reach an agreement. Hungary unilaterally terminated the contract and Slovakia (that succeeded Czechoslovakia) took an action against Hungary before ICJ[98].

In the *Gabcikovo-Nagymaros* case, ICJ concluded that new circumstances like environment norms and standards need to be taken into consideration to the extent that a party cannot execute the project commitments on the detriment of newly developed environment norms[99].

The argument referring to evolutionary new norms and standards suggests balancing the economic interests of parties to an investment contract and the needs in the social and developmental domains that constitute the newly established and widely recognized standards in the field of public interest. It is worth noting that that in any case, those new circumstances are to be taken into consideration. However, the argument that implies the interpretation by referring to evolutionary new norms and

[96] *Id*, pp.33-34.
[97] Hungary vs. Slovakia, ICJ, Judgment of September 25, 1997, par.15, available at < https://www.icj-cij.org/files/case-related/92/092-19970925-JUD-01-00-EN.pdf> accessed on February 27, 2019.
[98] *Id*, pp.37-39.
[99] *Id*, par.112 and 140.

standards is weak in terms of recalling the re-negotiation without providing a solution in case of failure of re-negotiation[100].

I.8.5. Argument of good faith and the investor's due diligence

According to M. Paparinskis, the use of principle of good faith is considered the main instrument that allows equity in case of law interpretation. Good faith avoids unfair advantage in the light of the obligation that is assumed. In this case, a reasonable exercise of the right is the one that is compatible with the obligation whereas the exercise of the right in a manner that is prejudicial to the interests of the other contracting party is unreasonable and contrary to the principle of good faith[101].

Opinions of R. Moloo and A. Khachaturian reveal that the principles of good faith and due diligence are interdependent. The due diligence implies the duty to refrain from unconscionable conduct, the duty to invest with adequate knowledge of risk and the duty to conduct business in a reasonable manner. Consequently, investors cannot expect states to compensate for regulation that implements widely recognized international standards in the public interest[102].

However, J. W. Yackee points out that every public measure related to human rights or environmental public interest does not automatically become exempt from compensation because good faith works for both sides. In this case, in the interpretation, there is a need of balancing different rights and obligations when the principled conflict of law needs to be resolved[103].

Sometimes, the legitimacy of public authority action infringing a private person's legally protected rights and related interests is subject to review. In the case of investors, the source of those rights may be the contract between a foreign investor and a host state. In such a case, the principle of proportionality might be useful when the two opposing rights are present. The said principle of

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[100] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 94, pp.33-35.
[101] M. Paparinskis, 'Good Faith and Fair and Equitable Treatment in International Investment Law' available at <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2512664&download=yes > accessed on August 7, 2019.
[102] R. Moloo and A. Khachaturian, 'The Compliance with the Law Requirement in International Investment Law' (2011) 34:6 *Fordham International Law Journal*, pp. 1481, 1485 and 1495 available at <https://ir.lawnet.fordham.edu/cgi/viewcontent.cgi?article=2310&context=ilj> accessed on August 7, 2019.
[103] J.W. Yackee, 'Pacta Sunt Servanda and State Promises to Foreign Investors Before Bilateral Investment Treaties: Myth and Reality' (2008) 32:5 *Fordham International Law Journal*, p. 1570, available at <https://ir.lawnet.fordham.edu/cgi/viewcontent.cgi?article=2165&context=ilj> accessed on June 30, 2019.

proportionality can help in balancing the investors' rights and the rights of others that are protected by the host state measure[104]. F. Marshall opines that good faith implies transparency, stability and investors' rights legitimate expectation. In this regard, it also implies the predictability. [105] In our own analysis, good faith may even include the responsibility of host states to consult investors or negotiating with them before enforcing a certain legislation whereby states can explain to investors circumstances that arose to change what investors would predict.

I.8.6. Argument of systematic integration and harmonized law interpretation

According to this approach, the conflict between legitimate rights of host states and investors depends on the way the relevant rules are interpreted. This approach suggests the need of legislative intervention to clarify the scope of stabilization clauses through systematic law interpretation because there is a presumption that parties intended something not inconsistent with generally recognized principles of international law or with previous treaty obligations towards third states[106].

In this regard, a suitable interpretation that refers to the normal meaning, party will, legitimate expectations, good faith and subsequent practice as well as the object and purpose and the principle of effectiveness[107].

In our analysis, we deduce from the discussion above that though a legally concluded contract binds parties thereto, investors need to be diligent when negotiating and concluding contracts because host states may be in the position of not executing their contractual obligations due to internal law of fundamental importance, existing international obligations and new norms and standards that may arise. However, despite all those legal duties that a host state is required to comply with, an interpretation that respects good faith remains fair since it balances the parties' obligations and rights and results in avoiding unfair advantages.

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[104] T. Cottier and others, 'The Principle of Proportionality in International Law' available at <https://www.wti.org/media/filer_public/9f/1b/9f1bd3cf-dafd-4e14-b07d-8934a0c66b8f/proportionality_final_29102012_with_nccr_coversheet.pdf> accessed on August 7, 2019.
[105] F. Marshall, 'Fair and Equitable Treatment in International Investment Agreements' available at <https://www.iisd.org/pdf/2007/inv_fair_treatment.pdf> accessed on August 7, 2019.
[106] K. Gehne and R. Brillo, (2017), Stabilisation Clauses in International Investment Law: Beyond Balancing and Fair and Equitable Treatment, see supra note 100, p.40
[107] *Ibid.*

The main findings in this chapter illustrate that stabilization clauses aim at protecting investment projects as it addresses investment risks that may be caused by a change in a legal framework. The sovereignty of states appears to be the major threat since it obliges states to enact the needed laws in public interests especially in terms of existing and new international norms and standards in social and environmental fields. All in all, what matters is the interpretation given to stabilization clauses. In order to avoid unfair advantages, good faith is considered the right instrument in case of interpreting stabilization clauses vis-à-vis applicable law.

It is better to assess how the stabilization clauses have been practically interpreted. In the next chapter of the research at hand, decided cases concerned with stabilization clauses in the oil and gas contracts are going to be analyzed. In this case, inductive reasoning is to be used as in each case, the conclusion will be reached after analyzing the decision made and its general implications regarding stabilization clauses and sovereignty of states.

CHAPTER II: ANALYSIS OF SELECTED TRIBUNAL AWARDS CONCERNED WITH STABILIZATION CLAUSES IN THE OIL AND GAS CONTRACTS

The oil and gas sector plays a paramount role in the life and activities of world's community especially in the economic perspective. Oil and gas are the necessary resources since when combined; they provide over half of the world's energy[108].

A report jointly produced by IFC, UNDP and IPIECA called -*Mapping the Oil and Gas Industry to the Sustainable Development Goals: An Atlas,* stated that the oil and gas industry is central to the global economy and many economies in various countries including developing ones. It also demonstrated that the Oil and Gas sector is central to sustainable development, as oil and gas are key pillars of the global energy system and thus, drivers of economic and social development [109].

The said report also highlighted that although the Oil and Gas industry positively affects the global economy and sustainable development, it also has negative effects due to their role in climate change. In this regard, even if oil and gas have enabled industrialization and human development, in doing so, their use has also contributed to the rise in atmospheric carbon dioxide, which in turn has contributed to a warming of the climate system and this necessitates the adequate regulation for environment protection[110].

Since oil and gas are natural resources, their extraction is more concerned with the principle of permanent sovereignty of natural resources and that extraction is also pertinent in respect of environment protection. Besides, the oil and gas industry is a very important sector in economy. This makes stabilization clauses in the oil and gas sector become an issue especially in terms of enforcement. The analysis of the following cases is useful in assessing that enforcement of stabilization clauses in oil and gas sector according to the related tribunal awards. The analysis of each case comprises of summary of the case and applicant's claim, legal issues and tribunal findings, and the researcher's observations.

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[108] M. Overholt, 'The importance of Oil and Gas in Today's Economy', *Tiger General*, 23 August 2016, available at <https://www.tigergeneral.com/the-importance-of-oil-and-gas-in-today-s-economy/> accessed on February 28, 2019.
[109] IFC, IPIECA and UNDP, 'Mapping the Oil and Gas Industry to the Sustainable Development Goals: An Atlas', available at <http://www.ipieca.org/media/4404/online-mappingoilandgastosdgatlas.pdf > accessed on February 28, 2019.
[110] *Ibid.*

II.1. The case of LIAMCO vs. Libya

LIAMCO vs. Libya is a popular case that is concerned with stabilization clauses in the petroleum sector. The analysis of this case contributes a lot in assessing the enforceability of stabilization clauses particularly in the petroleum sector.

II.1.1. Case summary and the applicant's claim

LIAMCO was an American corporation established for the purposes of research, exploration and exploitation of petroleum and natural gas, particularly in Libya whereas the latter was recognized as an independent sovereign State by the United Nations in 1949, effective 2 January 1952. Its form of government was monarchical[111].

For the purpose of improving its economic conditions, encouraging the inflow of foreign capital and ensuring the exploitation and protection of its natural resources, Libya enacted Petroleum Law N° 25 in 1955. The said law established a framework for the exploration and production of petroleum within Libya. It provided a concessionary system for the exploitation of petroleum products, and established an autonomous Petroleum Commission which was vested in the power of granting the relevant concessions[112].

After the adoption of the said Petroleum Law of 1955, the Libyan Government invited applications for petroleum exploration permits and concessions from companies which could meet the requirements provided by the law. LIAMCO was among the invitees and was subsequently granted the concessions from 16 to 22. LIAMCO voluntarily surrendered 18, 19, 21 and 22 to retain the concessions 16, 17 and 20 which became subject to the dispute and arbitration[113].

In September 1969, the Revolutionary Command Council (RCC) headed by Colonel Muammar Gaddafi took over from King Idriss and announced the formation of the Libyan Arab Republic. In 1973, the said RCC put in place Law N° 66 nationalizing 51% of the concession rights of various

[111] *LIAMCO v The Government of the Libyan Arab Republic*, Ad hoc Arbitration Tribunal award of April 12, 1977 , case summary, p.2 available at <https://www.biicl.org/files/3939_1977_liamco_v_libya.pdf > accessed on March 17, 2019.
[112] *Ibid.*
[113] *Id*, pp.2-3.

companies that include LIAMCO. In February 1974, RCC issued Law N° 10 of 1974 nationalizing LIAMCO's remaining 49% of concession interests[114].

The agreement between LIAMCO and Libya contained a clause that provides that the concession would be governed by the Petroleum Law and the related regulations in force at the time of the contract conclusion and that any amendment or repealing of those legal instruments would not affect the rights of the company. It also contained a clause that prohibits the unilateral alteration of contractual rights[115].

The said nationalization raised the dispute between the concerned parties. LIAMCO and Libya entered into negotiations with regard to compensation for both nationalization measures but they failed to solve the dispute as they did not reach an agreement on that [116].

In November 1973, LIAMCO initiated arbitral proceedings alleging that the said nationalizations constitute unlawful breach of the contract and were contrary to both the principles of domestic law of Libya and to the principles of international law. LIAMCO requested the tribunal to order as a principal relief, the restoration of its concession rights together with all the benefits accruing from such restoration (*restitution in integrum*); as an alternative relief, the payment of adequate damages (*damnun emergens* and *lucrum cessans*), in the amount of US $ 207,652,667 plus interest at 12% from January 01, 1974 till the date of payment of recovery of the award in full[117].

II.1.2. Legal issues and Tribunal's findings

In this case, the prominent legal issue was whether the right of a state to nationalize constitutes its sovereignty and if so or no, the corresponding attached effects.

The Tribunal found that concession rights constitute property as long as those rights had a pecuniary or monetary value. It held that the right of property including incorporeal property of concession rights was inviolable in principle, as recognized by both Libyan and international law;

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[114] *Ibid.*
[115] P.E. Comeaux and N.S. Kinsella, 'Reducing the Political Risk of Investing in Russia and other C.I.S Republics: International Arbitration and Stabilization Clauses' available at <http://www.kinsellalaw.com/wp-content/uploads/publications/comeaux-kinsella_reducing-risk-stabilization.pdf > accessed on March 17, 2019.
[116] *LIAMCO v The Government of the Libyan Arab Republic*, Ad hoc Arbitration Tribunal award of April 12, 1977, case summary, see supra note 111, p.3.
[117] *Ibid.*

that however, the right of a State to nationalize was held to be sovereign but subject to compensation for premature termination of concession agreements. In the motivation of the tribunal, the nationalization of concession rights, that was not discriminatory and not accompanied by a wrongful conduct, was not unlawful, but a source of liability to compensate the investor for the premature termination of the Concession Agreements[118].

II.1.3. Observations

According to the agreement between LIAMCO and Libya, the concession was to be governed by the Petroleum Law and related regulations in force at the time of the contract conclusion and any amendment or repealing of those legal instruments would not affect the rights of the company. In addition to that, the parties agreed on the prerequisite of their mutual consent to modify contractual rights secured by the concession. All these imply stabilization clauses and thus, any future legal or regulatory change by the government and any action that would result in modifying the agreement that it entered into with LIAMCO would be contrary to the contract between those two parties.

In the case at hand, the Arbitral Tribunal ruled that stabilization clauses do not preclude the state's sovereign right to expropriate a concession. It is evident that the arbitral tribunal considered the state's sovereign rights as overweighing the investors' rights as it ruled that compelling a State to make restitution would constitute an intolerable interference in the internal sovereignty of States and basing on that ground, it dismissed the LIAMCO's requested principal relief of the restoration of its concession rights together with all the benefits accruing from such restoration (*restitutio in integrum*). Basing on the principle of equity, the Tribunal concluded that LIAMCO deserved to be compensated for the damages it suffered and lost profits (*damnum emergens* and *lucrum cessans*).

Even if the arbitral tribunal decided in favor of LIAMCO, the execution of the award faced a challenge of act of state doctrine. This doctrine implies the limit of government's authorities in

[118] *LIAMCO v The Government of the Libyan Arab Republic*, Ad hoc Arbitration Tribunal award of April 12, 1977, par.255, available at <https://jusmundi.com/en/document/decision/en-libyan-american-oil-company-v-the-government-of-the-libyan-arab-republic-award-tuesday-12th-april-1977 > accessed on June 28, 2019.

matters involving foreign governments. In this case, courts of a certain state are prohibited from inquiring the validity of laws of other governments and their acts performed on their territories[119].

LIAMCO tried to enforce the award in the United States of America to the extent of seizing a court requesting for a forced execution. Libya opposed that enforcement alleging that the subject matter namely oil concession nationalization was not subject to arbitration. US District Court for the District of Columbia refused to enforce that arbitral award as it accepted Libya's argument that the subject matter in dispute was the oil concession nationalization which constitutes an act of state, and that concession terms were abrogated by nationalization laws. The court's motivation is that it would not enforce an award rendered by a tribunal by violating an act of state. The court opined that since arbitration would necessarily review the validity of nationalization; that arbitration constitutes a violation of act of state[120].

Libya also raised sovereign immunity as an opposition but the Court dismissed it on grounds that by agreeing to arbitration (to be conducted by International Conference Center of Geneva) governed by a foreign law, Libya waived its sovereign immunity. LIAMCO appealed the district court's decision but before the appeal was decided, parties settled and as a result; the appeal was dismissed[121].

The procedure of exequatur on that case also took place in Switzerland, France and Sweden. In Switzerland, the proceedings were interrupted by agreement of parties. In France, having been inspired by sovereignty matters, the Tribunal de Grande Instance de Paris did not allow the execution of arbitral award. It opined that Libya's funds in that country are meant for public services whereas the relationship between Libya and LIAMCO were of private nature. In Sweden, the Court of Appeal of Stockholm developed a different approach. It decided that the request for award enforcement should be accepted as it opined that having consented to arbitration clause, Libya freely renounced its right to invoke immunity of execution. It opined that consenting to

[119] N.J. Kleinman, 'The Act of State Doctrine-From Abstention to Activism' (1984) *Journal of Comparative Business and Capital Market Law,* at 115, available at <https://www.law.upenn.edu/journals/jil/articles/volume6/issue2/Kleinman6J.Comp.Bus.&Cap.MarketL.115%281984%29.pdf> accessed on August 8, 2019.

[120] I. Amro, *Recognition and Enforcement of Foreign Arbitral Awards in Theory and in Practice: A comparative Study in Common Law and Civil Law Countries*, Newcastle, Cambridge Scholars Publishing, 2013, p.155.

[121] R. Martinez, 'Recognition and Enforcement of International Arbitral Awards under the United Nations Convention of 1958: The "Refusal" Provisions' (1990) 24:2 *The International Lawyer*, pp. 507-508, available at <https://scholar.smu.edu/cgi/viewcontent.cgi?article=2726&context=til> accessed on August 8, 2019.

arbitration clause implies the renunciation of immunity of jurisdiction and consequently acceptance of arbitral procedure effects which involve the execution of award. The Court further stated that State's immunity does not allow it to disregard the contract it entered into due to that the said immunity does not hinder from the application of fundamental principles of law of contract[122].

II.2. The case of Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co. vs Libya

This is also a popular case in the petroleum sector. It is useful in assessing how a tribunal balanced the sovereignty of states and stabilization clauses.

II.2.1. Summary of the case and the applicant's claim

The Libyan government granted 14 deeds of concession to Texaco Overseas Petroleum Company (TOPCO) and California Asiatic Oil Company (CAOC) for petrol exploitation. These were concluded between 1958 and 1968 for the purpose of allowing the said companies to jointly exploit the petrol[123].

In Libya, the concessions were subject to the model contract which was provided in the annex to the text of the Petroleum Law of 1955. As a result, the agreements entered into by Libya and TOPCO and CAOC were a reproduction of the said model contract[124].

Clause 16 of that model contract provided that the Libyan Government, the Petroleum Commission and the competent authorities in various provinces should take all the steps that were necessary to ensure that the companies enjoyed all the rights conferred upon them by the concessions, and the contractual rights expressly provided for the concessions might not be infringed except by agreement of both parties[125].

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[122] Y. Dinstein and M. Tabory, *International Law at a Time of Perplexity: Essays in Honour of Shabtai Rosenne*, Dordrecht, Martinus Nijhoff Publishers, 1988, p. 378.
[123] Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co. vs Libya, Ad hoc Award of January 19, 1977 available at< https://www.trans-lex.org/261700/_/texaco-overseas-petroleum-company-v-the-government-of-the-libyan-arab-republic-yca-1979-at-177-et-seq-/ > accessed on March 19, 2019.

[124] *Ibid.*
[125] *Ibid.*

It added that during the period of their effectiveness, the concessions were to be interpreted in accordance with the provisions of the Petroleum Law and the Regulations in force at the time of the grant of the concession, and that any amendments or cancellations of those Regulations should not apply to the contractual rights of the concessionaire except with its consent[126].

In 1973 and in 1974, Libya promulgated the decrees to nationalize all rights, interests and property of petroleum companies including Texaco Overseas Petroleum Company (TOPCO) and California Asiatic Oil Company (CAOC). That action of the Libyan Government led those two companies to request for arbitration claiming for *restitutio in integrum* as they were alleging that Libya breached the contract. Libya refused the requested arbitration but that refusal did not prevent from the appointment of a sole arbitrator[127].

II.2.2. Legal issues and arbitrator's findings

In this case, the prominent legal issue is whether the nationalization of concessions by the government of Libya constitutes a breach of the contract.

Referring to the principle of the binding force of contracts recognized by Libyan law and to the principle of *pacta sunt servanda* which is a general principle of law constituting an essential foundation of international law, the arbitrator found that the principles of Libyan law were in conformity with international law and concluded that the Deeds of Concession in dispute had a binding force[128].

The arbitrator also found that in the exercise of its sovereignty, a State has the power to make international commitments with a private party but that in such a framework, it must respect the said international commitments. As a result, a State cannot invoke its sovereignty to disregard the commitments freely undertaken through the exercise of this same sovereignty, and its internal order does not allow taking measures that result in making null and void the rights of the contracting party which has performed its various obligations under the contract[129].

[126] *Ibid.*
[127] *Ibid.*
[128] *Ibid.*
[129] *Ibid.*

The arbitrator invited the government of Libya to perform its obligations and re-establish *in integrum* the situation that would have resulted from the execution of the contract[130].

II.2.3. Observations

In Texaco Overseas Oil Petroleum Co. /California Asiatic Oil Co. vs Libya, the arbitrator recognizes the significance of state sovereignty but also balances it with the principle of *pacta sunt servanda.*

For the arbitrator, a stabilization clause that is inserted in an international investment contract does not limit the state's sovereignty. The fact that a certain state undertakes to be bound by a stabilization clause is considered a valid exercise of that state's sovereignty.

This is a good reasoning because the sovereignty over natural resources is intended to prevent from exploiting natural resources of a certain country by another country without the owner's consent. However, in case the country owner has consented for that exploitation, its sovereignty is not prejudiced because its natural resources are being exploited in manner that it freely sought. That reasoning led to inviting the government of Libya to restore the situation.

We analytically conclude that Libya was ordered to compensate TOPCO because nationalization of concessions by Libya was found to be inconsistent with stabilization clauses that were present in the contract between TOPCO and Libya and thus illegal. T. Begic points out that the case of TOPCO vs. Libya upheld the validity and binding nature of stabilization clauses under international law. In that case, the tribunal opined that a stabilization clause contained in parties 'contract has the effect of stabilizing the position of the contacting party though it does not in principle impair the legislative and regulatory sovereignty of the host state. The latter reserves all its prerogatives to issue laws and regulations that bind national or foreign persons with which it has not undertaken such a commitment[131].

T. Begic also points out that the tribunal accepted that it was unquestionable that the host state may adopt or change its laws but such changes cannot affect freely undertaken commitments under

[130] *Ibid.*
[131] T. Begic, *Applicable Law in International Investment Disputes*, Utrecht, Eleven International Publishing, 2005, pp. 85-86.

an international agreement. In this regard; by virtue of stabilization clauses, a host state makes a binding legal commitment not to exercise its sovereign power. In case of a change that leads to the abrogation of parties' agreement without mutual consent, such an act is invalid under international law and constitutes the breach of contract[132].

The aforementioned author further states that as a result, a State cannot invoke its sovereignty to disregard commitments freely undertaken through the exercise of that same sovereignty. It can't also invoke its internal order as a justification of taking measures that make null and void the rights of the contracting party which has performed its contractual obligations. It is worthy to note that the fact that international law recognizes the right to nationalize is not a sufficient ground to allow a State to disregard its commitments because the same law recognizes the power of a state to commit itself internationally and such a commitment includes the inclusion of stabilization clauses in a contract with a foreign investor[133].

II.3. The case of AGIP vs. Popular Republic of Congo

This case is concerned with the nationalization of a company whose area of business was petroleum distribution. A summary of the case is provided below.

II.3.1. Summary of the case and the applicant's claim

AGIP (*Azienda Generale Italiana Petroli*) was an Italian Company that invested in Congo by forming a Congolese Company named AGIP Brazzaville SA. This company commenced its commercial activity of petroleum distribution in May 1965[134].

On 12 January 1974, the government put in place Law N° 1/74 which nationalized the petroleum distribution sector as it transferred the assets of the nationalized companies to the State-owned company Hydro-Congo. The nationalization affected all the companies operating within the sector

[132] *Id*, p.86.
[133] *Ibid*.
[134] *AGIP vs. People's Republic of the Congo*, ICSID Case N° ARB/77/1, Arbitral award of November 30, 1979, par.16, available at <https://jusmundi.com/en/document/decision/en-agip-s-p-a-v-peoples-republic-of-the-congo-award-friday-30th-november-1979 > accessed on March 19, 2019.

of petroleum distribution save only AGIP which had concluded an agreement with the Government ten days before that nationalization[135].

In that agreement, AGIP undertook to transfer to the Government a number of shares in the company representing 50% of its capital whereas the Government undertook among others that AGIP should retain the character of a private joint-stock company despite its share and to adopt appropriate provisions to ensure that future modifications to the company laws with respect to the structure and composition of corporate bodies would not apply to AGIP[136].

The government also undertook to do what was necessary to ensure that it was AGIP that would supply all petroleum products and lubricants needed by the government and quasi-government agencies[137].

From the beginning of 1974, AGIP started to face increasing and aggressive competition from the said state-owned company namely Hydro-Congo. The government did not comply with its undertaking towards AGIP as many state or quasi-state customers of AGIP became customers of Hydro-Congo after the approval of the Ministry for Energy. This caused AGIP to face some difficulties that included poor performance[138].

On April 12, 1975, through the Ordinance N^{o} 6/75, the President of the Republic decided to nationalize AGIP. The establishment of Hydro-Congo and the fact that AGIP Brazzaville SA had ceased all commercial activities and was incapable of meeting its obligations, were referred to as motives of that nationalization. Subsequently, the registered office and the offices of AGIP were occupied by the army and the latter also took possession of all the assets, documents, records and books of the Company, something that made AGIP unable to manage its affairs[139].

AGIP requested arbitration at ICSID whereby among the grievances it alleged included stabilization of the juridical status of the company (AGIP) as the nationalization changed private joint-stock status of AGIP. Government's action of nationalizing AGIP and establishment of

[135] *Id,* par.17.
[136]*Id,* par.18.
[137]*Ibid.*
[138]*Id,* par. 21.
[139]*Id,* par.28.

Hydro-Congo as said above was contrary to parties 'contract since AGIP undertook in the Agreement to transfer to the Government a number of shares in the Company representing 50% of its capital while the Government undertook to ensure that it was AGIP that would supply all petroleum products and lubricants needed by the government and quasi-government agencies and accepted that AGIP should retain the character of a private joint-stock company despite its share in AGIP.

II.3.2. Legal issues and tribunal's findings

The fact that AGIP Brazzaville SA was nationalized changed its private joint-stock status and the applicable rules to that company. The legal issue in *AGIP vs. Popular Republic of Congo* that is relevant to the present research is whether the ordinance that nationalized AGIP Brazzaville SA violated an agreement between AGIP and the government of Popular Republic of Congo that guaranteed the stabilization of the juridical status of AGIP Brazzaville SA.

Article 4 of the said agreement provided that the government undertook to abstain from applying ordinances and decrees which would change the private joint-stock company character of AGIP. Article 11 of the same agreement provided in case of changes in company laws, appropriate provisions would be enacted to ensure that those modifications do not affect the structure and composition of the organs of AGIP provided for in the Agreement and the Articles of Association of that company which provide its duration of 99 years[140].

Basing on those provisions of the agreement between the government of Popular Republic of Congo and AGIP Brazzaville SA, the Tribunal opined that in this case the government was linked to AGIP by a contract which, under Congolese Law bound it not to modify the status of the company unilaterally[141].

The tribunal opined that when a state participates in the constitution of a capital of the company, it performs an act of private administration (*gestion privée*) similar to that of a private individual and it does not act in general interest. Consequently, the nationalization carried out by the

[140] *Id*, par.70.
[141] *Id*, par.76.

government of Popular Republic of Congo would not be considered as an act of general interest. It went on opining that if the Government intended to protect its interests as a shareholder, it was under an obligation to respect legal procedures which were applicable to the matter and that could be done by either calling an extraordinary General Meeting of the Company by the Board of Directors or seizing of the competent court requesting the dissolution of the Company as provided by relevant laws[142].

The tribunal found that the dissolution by unilateral means decided upon by Ordinance Nº 6/75 rejected these stabilization clauses while their applicability resulted from common will of the parties. It opined that the stabilization clauses which were freely entered into by the Government, did not affect the principle of its legislative and regulatory sovereignty since the concerned government retained the power to apply it to third parties, be it foreigners or nationals[143].

In that case, the tribunal argued that under international law, when a state enters into an international agreement with a private individual; the concerned state exercises a sovereign power as long as it freely consented to that agreement[144].

II.3.3. Observations

According to the tribunal in *AGIP vs. Popular Republic of Congo,* the sovereignty of states should not be a pretext of disregarding stabilization clauses. Instead, it should be a reason of enforcing those clauses since entering into an international agreement with a private individual, that may even contain stabilization clauses, constitutes a modality by which a state exercises a sovereign power.

Furthermore, in case a state enters into an agreement that establishes a commercial relationship, it is admitted that in this case the state is not acting in general interest since in such a case it performs an act of private administration similar to that of a private individual.

[142] *Id*, par.75.
[143] *Id*, par.85.
[144] *Id*, par.81 and 86.

That states' status was emphasized by R. Rayfuse who pointed out that with regard to the case of AGIP vs Congo, the Government of Congo did not act in general interest of the national community because what it did was the performance of private administration. The said author asserts that Congo was linked to AGIP with a contract and consequently, Congo was bound by civil law which lays down the principle that contracts legally made have force of law for those who made them[145].

The said author pointed out that the nationalization by Congo constituted the unilateral dissolution of the contract. She further pointed out that dissolution by unilateral means was decided by the aforesaid Ordinance Nº 6/75 repudiates stabilization clauses whose application results from common will of contract parties not from the sovereignty of the Contracting State. She went on arguing that stabilization clauses which were freely entered into by a certain government, do not affect its legislative and regulatory sovereignty since it retains those both powers with respect to third parties[146].

II.4. The case of Aminoil vs. Kuwait

Aminoil vs. Kuwait is a case that relates to the exploration and exploitation of oil and gas. It is relevant to this research since Aminoil and Kuwait entered into an agreement that contained a stabilization clause.

II.4.1. Summary of the case and the applicant's claim

In 1948, Kuwait granted to a US company called AMINOIL (American Independent Oil Company) a 60 years concession for the exploration and exploitation of oil and gas in a designated territory in Kuwait. The Concession Agreement contained a stabilization clause that prevented Kuwait from unilaterally annulling or altering the terms of the Agreement[147].

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[145] R. Rayfuse, *ICSID Reports: Reports of Cases Decided under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, 1965*, Vol. I, New York, Cambridge University Press, 1993, pp.322-323.
[146] *Id*, p.324.
[147] *Aminoil v Kuwait*, Ad hoc Arbitration Tribunal award of March 24, 1982, case summary, p.2, available at <https://www.biicl.org/files/3938_1982_kuwait_v_aminoil.pdf> accessed on March 20, 2019.

In 1954, AMINOIL began commercial production and exportation of petroleum products and later, both parties have agreed on some modifications of the agreement. Following the dramatic increase of oil prices in 1973, the OPEC took a decision to introduce the agreement reached by the producing governments in Abu Dhabi, which increased the tax rate to be imposed on oil companies (Abu Dhabi formula). Kuwait and AMINOIL failed to reach compromise on this issue and on 19 September 1977, Kuwait enacted the Decree Law N°.124 that provided that AMINOIL's concession should be terminated; that AMINOIL's assets in Kuwait should be converted into the State; and that fair compensation should be paid to AMINOIL[148].

Afterwards, both parties concluded a separate Arbitration Agreement that was concerned with the settlement of disputes between the parties. One of the claims that had to be examined by the arbitration tribunal was the liabilities for nationalization[149].

II.4.2. Legal issues and tribunal's findings

The concession was terminated before the expected period of sixty (60) years that was provided by the agreement concluded by the concerned parties namely AMINOIL and Kuwait. The validity of an act of nationalization that was established by the Decree Law N° 124 of 1977 was a crucial issue in *Aminoil vs. Kuwait* because it was concerned with the stabilization clause of the Concession Agreement which prevented Kuwait from unilaterally modifying or annulling the concession[150].

The tribunal found that the nationalization was due to changed circumstances and Kuwait's development as an independent State. It opined that a stabilization clause no longer possesses its former absolute character and argued that although there was a stabilization clause in agreements between the Kuwait government and AMINOIL, these stabilization clauses themselves did not expressly prohibit nationalizing the concerned property[151].

[148] *Id*, p.4.
[149] *Id*, p.2.
[150] *Id*, p.4.
[151] *Id*, p.3.

For the tribunal, stabilization agreements are intended to prevent from confiscatory termination and take over. If the takeover is not confiscatory, it would not be regarded as a breach of stabilization clause. The tribunal argued that since the government had made an offer of monetary compensation, the takeover was not confiscatory[152].

II.4.3. Observations

The tribunal argued that stabilization clauses evolved as their former absolute character that hinders any change by the government is no longer appropriate. In the case of *Aminoil vs. Kuwait,* the tribunal recognized that a host state may be in the situation of changed circumstances that compels the government of the host state to react accordingly. As a result, in case the government of a host state reacts to such a change of circumstances without the intention of confiscating the property of the investor but proposing a proper indemnification, the nationalization is lawful since it has no confiscatory character. The tribunal also considered the unpredictability of the circumstances that the government reacted on.

It is worthy to note that stabilization clauses that existed in the contract between AMINOIL and Kuwait were intended to stabilize the concession. In our own analysis, it is obvious that Kuwait did not change the contract but terminated it through nationalization. It is evident that such a nationalization was more detrimental to the stability of the contract between AMINOIL and Kuwait but unfortunately, the tribunal did not decide in favour of AMINOIL on ground that only measures having a confiscatory character were prohibited by the stabilization clauses.

P.Y. Tschanz points out that the case of *Aminoil vs Kuwait* has established a new distinction between stabilization clauses and non-nationalization clauses. The conclusion to be drawn from *Aminoil vs Kuwait* award is that it would be advisable to expressly provide against "nationalization". An undertaking not to nationalize must be express but in the contract between AMINOIL and Kuwait, no such undertaking was found as stabilization clauses did not expressly mention nationalization[153].

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[152] *Id*, p.2.

[153] P.Y. Tschanz, 'The Contributions of the Aminoil Award to the Law of State Contracts' (1984) 18:2 *International Lawyer*, at 276 available at <https://scholar.smu.edu/cgi/viewcontent.cgi?article=3691&context=til> accessed on August 18, 2019.

Despite that view of P.Y. Tschanz, other scholars such as W. Peter, J. Quentin de Kuyper and B. de Candolle opine that the term stabilization clauses should be used in a broad sense and includes non-nationalization and other similar clauses. We agree with their reason that supports their view whereby they assert that behind the great diversity of stabilization clauses lies a one and sole objective which is the preclusion of application to an agreement of any subsequent legal or regulatory act issued by the government that modifies the legal situation of an investor[154].

II.5. The case of CMS vs. Argentina

CMS vs. Argentina is a case in the gas sector. In this case, stabilization clauses were referred on when assessing whether the BIT umbrella clauses were duly observed.

II.5.1. Summary of the case and the applicant's claim

In the management of its internal affairs, the government of Argentina decided to privatize some government-owned industries and public utilities, the gas sector being included. In the course of that privatization, under the Gas law, the national state gas-owned company was divided in various companies including TGN (*Transportadora de Gas del Norte*). In 1992, TGN was granted license to transport gas in Argentina[155].

It also enacted various new laws, including a 1991 Currency Convertibility Law and a 1992 Gas Law establishing the legal framework for the privatization of the gas industry and regulation of the transport and distribution of natural gas[156].

As part of its privatization incentives, Argentina granted TGN the right to calculate tariffs in US dollars and then convert them to pesos[157] at the prevailing exchange rate, and to adjust tariffs every six months to reflect changes in inflation in accordance with US-PPI (Producer Price Index). Those rights were recognized by the above-mentioned laws[158].

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[154] W. Peter and others, *Arbitration and Renegotiation of International Investment Agreements,* 2nd Ed, The Hague, Kluwer Law International, 1995, p.214.
[155] CMS v. Argentina (ICSID Award of 2005)', Case Nº ARB/01/8, par. 53-56, available at <https://www.italaw.com/documents/CMS_FinalAward.pdf> accessed on June 30, 2019.
[156] *Id*, par.53-54.
[157] Peso is the Argentinean currency.
[158] *Id*, par.57.

In 1995, CMS, a US company acquired approximately 30% of TGN's shares. In late 1990s, Argentina faced a serious economic crisis. At that time, she temporarily suspended and then permanently terminated both TGN's right to calculate tariffs in US dollars and its right to make inflation adjustments. That measure led to a great decrease in TGN's profits and to the loss of value of the TGN as a company[159].

In 2001, CMS filed a case before ICSID Tribunal claiming that those Argentinean measures were in violation of several of Argentina's obligations under the Argentina-US BIT including fair and equitable treatment, and requested US $ 261 million of compensation for the decreased value of its shares in TGN plus interest and costs. It also claimed that Argentina had the obligations not to alter the basic rules governing the license without TGN's written consent[160].

II.5.2. Legal issues and tribunal's findings

The interesting legal issue is whether terminating both TGN's right to calculate tariffs in US dollars and its right to make inflation adjustments and the fact that Argentina altered the basic rules governing the license by terminating it before its expiry of 35 years without TGN's written consent constitute the breach of stabilization clauses[161]. The tribunal found that there were two stabilization clauses contained in the license namely provisions that prohibited freezing the tariff regime and those that prohibited altering the basic rules governing the license without TGN's written consent. The Tribunal concluded that by failing to observe these clauses, Argentina was in breach of the BIT's umbrella clause and hence the breach of stabilization clauses and this made the tribunal award CMS US$133.2 million[162].

In this case, before the tribunal, Argentina raised the necessity and emergence defense invoking that the said measures were adopted to safeguard essential economic, social and political interests. It argued that the said measures were adopted due to severe risks that were present in Argentina in

[159] *Id*, par.396 and 464.
[160] *Id*, par.4, 86 and 89.
[161] *Id*, par.86 and 197.
[162] *Id*, par. 302, par.468 and the verdict at p. 139.

2000. The tribunal rejected the invoked defense for the reasons of failing to demonstrate that Argentina's measures were the only means available[163].

However, after the application for annulment by Argentina, the Annulment Committee at ICSID took a different view holding that there were difficulties with the broad interpretation of the umbrella clause in the Tribunal's award. The Committee emphasized that the umbrella clause did not change parties to the obligation, and it was quite unclear how the Tribunal had concluded that CMS was concerned with the obligations of Argentina to TGN. As a result, the arbitral award was annulled for failure to give reasons[164].

II.5.3. Observations

The tribunal found that Argentina violated stabilization clauses that were contained in a license. Should CMS has been a party to a contract, it would have been awarded a just compensation.

Interestingly, the tribunal rejected the necessity defense raised by Argentina that its measures were in response to internal problems the country was going through. Though those measures were in line with public interests and the government had obligation to find an adequate solution, that would be acceptable only if Argentina did not contribute to the same situation it sought to address and if that was the only means available.

As Harout Samra points out, the most significant development in the CMS case that will undoubtedly have a bearing on future cases was a principle of fair and equitable treatment. Peter Muchlinski notes that the said principle is a cornerstone of the evolving international law on the protection of investors and their investments since it requires a particular approach to governance

[163] *Id.* par.315-324.

[164] F.Marshall, 'CMS Gas Transmission Co. v. Republic of Argentina, ICSID Case No. ARB/01/8' available at <https://www.iisd.org/itn/2018/10/18/cms-v-argentina/ > accessed on June 30, 2019.

on the part of the host country that must act in a consistent manner, free from ambiguity and in total transparency, without arbitrariness and in accordance with the principle of good faith[165].

In such a case, investors can expect host authorities act in a manner that is non-discriminatory and proportionate to the policy aims involved. Investors can also expect due process in the handling of their claims. As a result, host states will need to observe the goal of creating favorable investment conditions and the observance of the legitimate commercial expectations of the investor[166].

II.6. The case of EnCana vs. Ecuador

As stabilization clauses are considered a contractor's commitment, the case of *Encana vs. Ecuador* serves to illustrate that foreign investor's expectations must be grounded on a host state's commitment.

II.6.1. Summary of the case and the applicant's claim

The government of Ecuador entered into four contracts with two companies namely AEC and COL. The said contracts provided for rights of exploration and exploitation of oil and gas in Ecuador. AEC was owned by a Canadian company called Pacalta Resources Ltd while COL was owned by AEC. Pacalta Resources Ltd was later acquired by another Canadian company called EnCana and that made AEC and COL become wholly owned by EnCana[167].

According to the laws of Ecuador, at the time of entering into the aforementioned contracts; manufacturers could seek a VAT refund paid on goods produced in Ecuador for export. However, the government of Ecuador later on took the measures of changing the said legal provisions that provide for the said rights to the companies. As EnCana was permitted to carry out the activities of exploration and exploitation of oil and gas within the territory of Ecuador, it thought it was a

[165] H. Samra, 'Five Years Later: The CMS Award Placed in the Context of the Argentine Financial Crisis and the ICSID Arbitration Boom' (2007) 38:3 *Inter-American Law Review*, at pp.689-690, available at <https://repository.law.miami.edu/cgi/viewcontent.cgi?article=1070&context=umialr> accessed on June 30, 2019.
[166] *Ibid.*
[167] EnCana Corporation vs. Republic of Ecuador, London Court of International Arbitration, Award of February 03, 2006, par.21, available at <https://www.italaw.com/sites/default/files/case-documents/ita0285_0.pdf > accessed on April 3, 2019.

manufacturer and hence a beneficiary to the said VAT reimbursement but it disagreed with the government of Ecuador on that[168]. Due to the disputes over VAT refunds, EnCana initiated arbitration proceedings claiming for rights it had prior to a change in tax law regime[169].

However, the Ecuadorian government argued that the VAT only applied to manufacturing companies and that oil companies did not qualify as manufacturers. It further argued that the oil companies were already receiving the equivalent of a VAT refund because the contracts the oil companies negotiated with Ecuador were supposed to include all costs[170].

The aforementioned arbitration proceedings were initiated before the London Court of International Arbitration according (LCIA).

II.6.2. Legal issues and Tribunal's findings

The legal issue that is relevant to the present research is concerned with the state's right to regulate vis-à-vis the rights of an investor.

In *EnCana vs. Ecuador*, the Tribunal held that in the absence of a specific commitment from the host State, the foreign investor had neither the right nor any legitimate expectation that a certain law regime like the tax law regime would not change during the period of the investment[171].

The Tribunal also opined that although the EnCana subsidiaries suffered financially from the denial of VAT and the recovery of VAT refunds; it had been able to continue to function profitably and to engage in the normal range of activities, extracting and exporting oil the price of which increased during the period of investment. For the Tribunal, the change in VAT laws or their interpretation did not bring the companies to an end[172].

II.6.3. Observations on the arbitral award

[168] *Id*, par.41 and 42.
[169] *Id*, par.1.
[170] *Id*, par.98.
[171] *Id*, par.173.
[172] *Id*, par.174.

Stabilization clauses are inserted in a certain international investment agreement to ensure that the said contract entered into by a foreign investor and a host state is fixed to legal instruments applicable at the time of entering into the same concerned contract. This implies that in case of the presence of stabilization clauses, the latter are considered a commitment by the parties to a contract. Even though in the contracts entered into by the government of Ecuador and AEC and COL, there was no stabilization clauses; in *EnCana vs. Ecuador*, the Tribunal opined that the change in regulation by the government of Ecuador would only be non-applicable to the contracts it entered into with AEC and COL in case of a particular commitment.

As long as the absence of stabilization clauses releases a host state from a certain duty, the presence of the said clauses puts in place a duty that binds a host state. Thus, the investor-host state relationship is affected by the presence or absence of stabilization clauses especially in the regulatory power perspective.

Stabilization clauses are of great importance and their presence in a certain contract has a great impact. Peter D. Cameron points out that stabilization clauses are considered a tool that is used by international investors who seek guarantees of long-term contract stability[173]. In case parties to investment contracts including oil and gas contracts agree on the said clauses, contract terms are not subject to a change[174].

In *Parkerings vs. Lithuania*, it was held that stabilization clauses are an exception to a sovereign legislative power. It was held that even if a state has the right to enact or modify a law at its own discretion, a stabilization clause serves as a derogation whenever it exists in a contract a certain state may have entered into with an investor. In the presence of a stabilization clause, a state should not normally exercise its legislative power over its contractual relationship with an investor because that legislative power would be exercised in unfair, unreasonable and inequitable

[173] P.D. Cameron, 'Stabilization and the impact of changing patterns of energy investment' (2017) 10: 5 *Journal of World Energy Law and Business*, at 392, available at <https://academic.oup.com/jwelb/article/10/5/389/4555404> accessed on June 30, 2019.
[174] *Id*, at 390.

manner[175]. Stabilization clauses help investors to protect their legitimate expectations and to prevent from business risks that may be caused by changes of laws[176].

II.7. The case of Svenska Petroleum Exploration AB v. Lithuania

Svenska Petroleum Exploration AB v. Lithuania is a case that can serve to assess the enforcement of state's contractual undertaking. Taking into consideration that stabilization clauses constitute a state's commitment emanating from an international investment contract to which a host state is a party, *Svenska Petroleum Exploration AB v. Lithuania* plays a paramount role in the assessment of enforceability of the said stabilization clauses in case a concerned state is unwilling to enforce them.

II.7.1. Summary of the case and the applicant's claim

This case originates from a Joint Venture Agreement entered into by three parties namely Svenska, Geonafta and the Government of Republic of Lithuania on April 28, 1993. Svenska is a Swedish company employed in the business of oil exploration and extraction whereas Geonafta was formerly a Lithuanian State Enterprise which was later privatized in 2000. The said two parties together with the Government of Republic of Lithuania signed a Joint Venture Agreement that was concerned with the planned exploitation of various oil fields in Lithuania[177].

The Government of the Republic of Lithuania undertook the obligations as a signatory to the Joint Venture Agreement. Even though, Svenska and Geonafta were considered as founders of the Joint Venture, each owning 50 percent of the shares; the Government of Lithuania approved the said agreement and declared itself as bound by the Joint Venture Agreement. When signing at the last page of the document containing the agreement, the Government of Lithuania jotted down a statement that accompanies its signature. The said statement reads "*The Government of the*

[175]*Parkerings-Compangiet AS vs. Republic of Lithuania* (2007), ICSID Arbitration Case No. ARB/05/8, par.332, available at <https://www.italaw.com/sites/default/files/case-documents/ita0619.pdf> accessed on June 30, 2019.
[176]*Id*, par.336.
[177] *Svenska Petroleum Exploration AB vs. Government of Lithuania*, High Court of Justice Queen's Bench Division, Commercial Court, Case Nº 2004 Folio 272, Judgment of November 04, 2005, par.1, available at <https://www.italaw.com/sites/default/files/case-documents/italaw7449.pdf> accessed on April 4, 2019.

Republic of Lithuania hereby approves the above agreement and acknowledges itself to be legally and contractually bound as if the Government were a signatory to the Agreement"[178].

By Government Resolution of March 27, 1993, the State approved the terms of the said JVA as it authorized the Minister in charge of energy to approve the founding agreement. The said resolution was also concerned with issuing the related licenses[179].

In June 2000, a dispute arose between the parties as to who was entitled to exploit certain specific oil fields. The said dispute made Svenska initiate a claim against both Geonafta and the State of Lithuania before an International Chamber of Commerce's arbitral panel sitting in Denmark. The State took the preliminary objection that it was not a party to the arbitration agreement that was provided for by Article 9 of the Joint Venture Agreement and invoked the state immunity[180].

II.7.2. Legal issues and Tribunal's findings

The legal issue to examine in this case is whether a state can invoke state immunity and sovereignty as an excuse of not executing a contract that it duly consented to.

Relying on the words of a Joint Venture Agreement which expressed the consent of the State of Lithuania to be contractually bound by the Joint Venture Agreement, the Tribunal held that the Government of Lithuania was a party to a Joint Venture Agreement[181].

The arbitral tribunal opined that by signing a Joint Venture Agreement and acknowledging itself to be legally and contractually bound as if the Government was a signatory to that agreement and through the Government Resolution Nº 205 of March 27, 1993 in which the Government authorized the Minster of Energy to approve the very founding agreement on behalf of the Government; the Government of Lithuania became a party to a Joint Venture Agreement with Svenska and Geonafta[182].

[178] *Id*, par.13.
[179] *Id*, par.17.
[180] *Id*, par.3 and 6.
[181] *Id*, par.46.
[182] *Id*, par.17.

As a result, the arbitral tribunal found that since the Government of Lithuania was bound by the provisions of the Joint Venture Agreement, it was also bound by the arbitration clause that was provided by Article 9 of that agreement unless there was a support that the Government of Lithuania intended a different dispute resolution mechanism but that such a support did not exist[183]. The arbitral Tribunal thus opined that the Joint Venture Agreement was between three parties, each having its rights and obligations and that in the said agreement, the concerned parties had agreed to the same dispute resolution which was none else but arbitration[184].

II.7.3. Observations on the arbitral award

As long as a particular state entered into a given contract, it is bound by the terms of that contract. In the case of *Svenska Petroleum Exploration AB v. Lithuania*, the government of Lithuania objected to the arbitration alleging that only Svenska and Geonafta were concerned with the arbitration clause. However, the Government of Lithuania signed on the contract and acknowledged itself as a party to the contract and this made it also a party to it. As a result, it had to be bound by all terms of the said contract, the arbitration clauses being included. The fact that the government of Lithuania consented to being bound by the contract brought the Tribunal to consider it as a party that was subject to arbitration as a mechanism of dispute settlement in any case a relevant dispute would arise.

Though the Joint Venture Agreement did not contain a stabilization clause, the latter is one form of a state contractual undertakings and the *Svenska Petroleum Exploration AB v. Lithuania* established that a state is bound by its contractual commitment and must not hinder their enforcement.

II. 8. The case of Sapphire International Petroleum Ltd vs. National Iranian Oil Co. (NIOC)

Sapphire International Petroleum Ltd vs. National Iranian Oil Co. (NIOC) is a case that involves an international investment contract in the oil sector. In the context of this research, it is useful

[183] *Ibid.*
[184] *Ibid.*

with regard to the enforcement of contractual undertakings. This case established that contractual undertakings must be respected since the rule *pacta sunt servanda* is a basis of every contractual relationship.

Like in any other international investment contract, the rule *pacta sunt servanda* is also applicable in the oil and gas sector.

II.8.1. Summary of the case and the applicant's claim

On June 16, 1958, a Canadian company called Sapphire Petroleums Ltd (Sapphire) and an Iranian government-owned company called the National Iranian Oil Company (NIOC) entered into a contract that was intended to expand the production and exportation of Iranian oil. The contract provided that Sapphire must make a minimum investment of f $8 million in four years, an obligation that Sapphire executed[185].

Sapphire Petroleums Ltd and the National Iranian Oil Company (NIOC) set up the Iranian Canada Oil Company (IRCAN), a joint stock company and non-profit corporation to carry out the operations under the contract on behalf of the two parties. Both parties subscribed to half the share capital of IRCAN at a cost of US $ 5,000 each[186].

In August 1958, Sapphire Petroleums Ltd assigned its rights and obligations to Sapphire International Petroleums Limited (Sapphire International), a company that was wholly owned by Sapphire[187].

Sapphire International started work in the designated concession area. In May 1959, it sent two reports on the expenses incurred from the date of the contract until 31 March 1959. According to those reports, the total amount of the expenses was $302,545.25. Unfortunately, NIOC refused to

[185] *Sapphire International Petroleum Ltd vs. National Iranian Oil Co. (NIOC),* Ad hoc Tribunal, award of March 15, 1963, p.2, case summary available at <https://www.biicl.org/files/3940_1963_sapphire_v_nioc.pdf> accessed on April 05, 2019.
[186] *Ibid.*
[187] *Ibid.*

refund the expenses alleging that it had not been consulted before the operations as required by the contract[188].

In July 1959, through a letter that Sapphire International sent to the Shah of Iran, it requested a refund of their losses. On 5 September 1959, the Prime Minister of Iran replied that Sapphire International had not fulfilled its obligations and as a result NIOC had the right not to refund. The Prime Minister referred Sapphire International to NIOC for the settlement of the dispute[189].

Afterwards, NIOC notified Sapphire International that it repudiated the contract on the ground that Sapphire International failed to perform the expected contractual obligations. It also proposed to pay an indemnity equivalent to $350,000 but Sapphire International objected that[190].

Sapphire requested for arbitration claiming that NIOC breached the contract. Sapphire requested for compensation for expenses incurred before the contract plus interest, compensation for expenses incurred after the contract plus interest, and the refund of $350,000 indemnity[191].

II.8.2. Legal issues and Tribunal's findings

As far as the present study is concerned, an interesting legal issue is the enforcement of the contractual undertaking in international investment contract.

In the case of *Sapphire International Petroleum Ltd vs. National Iranian Oil Co. (NIOC)*, the dispute was about the performance of the contract. The Tribunal found that Sapphire fulfilled its contractual obligations and that NIOC deliberately refused to carry out certain of its obligations and that this failure was a breach of contract[192].

[188] *Ibid.*
[189] *Id*, p.3.
[190] *Id.* p.2.
[191] *Ibid.*
[192] *Id*, p.5.

It opined that such a failure was a reason for Sapphire not to carry out further obligations since in a bilateral contract; the failure of one party to perform its obligations releases the other party from its obligations and gives the right to pecuniary compensation[193].

The tribunal put an emphasis on the rule of *pacta sunt servanda* as a basis for every contractual relationship. So long as there was a contractual relationship between Sapphire International Petroleum Ltd and National Iranian Oil Co.; each party had obligations to fulfill and the parties have to enforce the obligations of the contract that they consented to[194].

II. 8.3. Observations

The case of *Sapphire International Petroleum Ltd vs. National Iranian Oil Co*. was concerned with the fulfillment of contractual undertakings. Though the contract between Sapphire and National Iranian Oil Co. did not involve stabilization clauses, *Sapphire International Petroleum Ltd vs. National Iranian Oil Co. (NIOC)* case is concerned with contractual undertakings in general terms which stabilization clauses may be a part of.

Analytically, the rule *pacta sunt servanda* implies that in case of a contract that involves stabilization clauses, each party to that contract is bound to execute them since it freely consented to the contract with such clauses.

The rule *pacta sunt servanda* means that parties to a contract are bound by reciprocal promises. Stabilization clauses constitute promises to be kept by host states in case of investment contracts that they enter into foreign investors. It is reported that in 1990s, some countries were freely used to breaking their promises alleging that UN resolutions related to permanent sovereignty over natural resources so allow them and they could carry out petroleum concession nationalizations and this led to legal impunity. However, this changed as international jurisprudence demonstrates that investors' rights were later recognized. Arbitral tribunals rejected a claim by host states that their sovereign rights would be a justification of breaching foreign investment contracts that they

[193] *Ibid.*
[194] *Ibid.*

freely entered into. As a result, should it be established that a certain state breached a contractual promise to an investor; the latter would be awarded a significant compensation[195].

II. 9. The case of LG&E vs. Argentina

LG&E vs. Argentina is a case that is concerned with the equilibrium between the state's power to regulate and its obligation towards foreign investors. It is a case of the investment in the gas distribution.

II.9.1. Summary of the case and the applicant's claim

Three Argentinean gas companies *Distribuidora de Gas del Centro, Distribuidora de Gas Cuyana* and *Gas Natural BAN S.A.* were created in the 1990s as a result of the privatization of Argentina's national natural gas transport and distribution monopoly. Three US investors LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc collectively referred to as "LG&E" held shareholding interest in the three Argentinean companies mentioned above. The said Argentinean companies were granted licenses until 2027[196].

In order to attract foreign investors, Argentina enacted a legislation which guaranteed that tariffs for gas distribution would be calculated in U.S. dollars and that automatic semi-annual adjustments of tariffs would be calculated basing on the U.S. Producer Price Index[197].

Due to the economic crisis that developed in Argentina in the late 1990s and early 2000s, through the Emergency Law, the Government of Argentina abrogated the guarantees provided at the time of privatization namely the calculation of tariffs in U.S. dollars and the semi-annual adjustments of tariffs according to PPI. That measure led to a great reduction in the profitability of the gas distribution business and this affected the investment of LG&E[198]. LG&E alleged that if legal protections offered by the tariff regime were still in effect, gas distribution company stocks would

[195] J.W. Yackee, 'Pacta Sunt Servanda and State Promises to Foreign Investors Before Bilateral Investment Treaties: Myth and Reality' (2008) 32:5 *Fordham International Law Journal*, pp.1550-1552, see supra note 103.
[196] *LG&E vs. Argentina Republic*, ICSID Award of July 25, 2007, p.2, case summary available at <https://www.biicl.org/files/3908_2007_lg&e_v_argentina.pdf > accessed on April 05, 2019.
[197] *Ibid.*
[198] *Ibid.*

remain stable and retained their value despite the recession but for the elimination of the requirement that tariffs be calculated in U.S. dollars, the value of LG&E's investment would have safely addressed a devaluation of the peso[199].

LG&E initiated ICSID arbitral proceedings under Argentina-US BIT. LG&E argued that Argentina's failure to observe the guarantees that it made with respect to the LG&E's investment implied the breach of fair and equitable treatment standard. LG&E also claimed that Argentina indirectly expropriated their investments without observing due process. LG&E requested full compensation ranging between US$ 248 million and US$ 268 million[200].

II.9.2. Legal issues and the Tribunal's findings

In the context of the present research, the interesting legal issue is concerned with balancing the contractual undertaking of a host state and the latter's necessity to regulate.

The Tribunal found that the "Emergency Law" which abolished both the calculation of tariffs in U.S. dollars and the semi-annual adjustments of tariffs according to PPI, seriously affected LG&E's rate of return while Argentina took no steps to compensate LG&E[201].

The Tribunal recognized the economic hardships that Argentina had faced during the said period of economic crisis but held that Argentina went too far by completely dismantling the legal framework constructed to attract investors. The Tribunal recognized a need of the stability of the legal and business framework and investors' expectations at the time of investment that should have been taken into consideration[202].

II.9.3. Observations

Despite the absence of stabilization clauses in the case between LG&E and Argentina, this case is interesting with regard to the host state's regulation and its contractual obligations that it freely

[199] LG&E vs. Argentina (2007), ICSID Case No. ARB/02/1, par.19, available at < https://www.italaw.com/sites/default/files/case-documents/ita0462.pdf > accessed on June 30, 2019.
[200] *Id*, par.1 and 15
[201] *LG&E vs. Argentina Republic,* ICSID Award of July 25, 2007, see supra note 194, p.4.
[202] *Ibid*.

consented to. Though a host state has the right and duty to regulate in the interest of its people, it has also the duty to consider the obligations it owes to investors. The way Argentina behaved by refusing to compensate LG&E illustrates that Argentina was not recognizant of its duties and was in bad faith; that is why the Tribunal decided in favor of LG&E in terms of tariffs guarantees it undertook to provide to the investors.

It is a fundamental principle of law that contractual undertakings must be respected. The rule *pacta sunt servanda* applies to all types of agreements, including those between investors and host states. Logically, a party entering into an agreement expects that the other party will act in good faith and fulfill its promises. In addition to that, the principle of good faith has also been universally applied as a general legal principle; it is well established that good faith is a key principle of international law, just as it is in domestic law. Consequently, international obligations had to be performed in good faith[203].

This principle of good faith has also been recognized in the context of foreign investment agreements. Currently, it is widely held that international minimum standards of protection to be afforded by a host state to a foreign investor in the territory of the host state involve the requirement of good faith. In light of the good faith principle, evolution of international minimum standards led to a duty of governments to treat foreign investors with transparency and to protect their legitimate expectations[204].

II.10. CONCLUSION ON ANALYSED SELECTED CASES

Arbitration tribunals differently interpreted the effectiveness of stabilization clauses but it is only in *LIAMCO vs. Libya* that the Tribunal held that sovereign rights of a host state authorize it to disregard contractual undertakings including stabilization clauses. In other cases, the Tribunals held that a host state is bound by the stabilization clauses that constitute the agreement that it freely consented to.

[203] D.E. Vielleville and B.S. Vasani, 'Sovereignty over Natural Resources versus Rights under Investment Contracts: Which one prevails?' available at <https://www.crowell.com/documents/Sovereignty-Over-Natural-Resources-Versus-Rights-Under-Investment-Contracts_Transnational-Dispute-Management.pdf> accessed on June 30, 2019.
[204] *Ibid.*

Analyzed selected cases are concerned with stabilization clauses in oil and gas contracts. Generally, in those cases; tribunals opined that what matters is an agreement between an investor and a host state.

Analyzed cases revealed that the essence of sovereignty over natural resources is to ensure that natural resources like oil and gas of a particular country benefit its people and to avoid that they can be exploited by another country or its people. In case of an agreement between a particular state and a foreign investor to exploit or distribute oil or gas, that agreement constitutes a concerned host state's choice of the way to exploit its natural resources.

Analyzed cases also demonstrated that the sovereignty of states is not limited by stabilization clauses. In contrast, stabilization clauses have been considered a valid exercise of sovereignty since it is concerned with a choice that is made by a particular state on the use and management of its natural resources.

The rule *pacta sunt servanda* is applicable under international investment law. Consequently, parties to an investment contract are bound by their contractual commitments. Furthermore, good faith is also a principle in international investment law. The said principle obliges a party to act reasonably and execute a contract that it entered into. It also implies that even in case of necessity to regulate or administrative measures that are contrary to stabilization clauses due to unpredictable circumstances, there is a need of a proper indemnification as a consideration of investor's legitimate commercial expectations.

In such a case, parties' agreement governs their relationships and binds them. Even in case of a change that necessitates a measure to be taken by a host state in a manner that is likely to affect an investment contract to which it is party, a host state' s unilateral action is not encouraged because consent of both parties is required. So long as it is a mutual consent that establishes a contractual relationship, the same consent from both parties is needed to produce any modification.

However, even though several arbitral tribunals have decided in favor of investors relying on stabilization clauses, it has been realized that the enforcement of arbitral awards remains a problem due to sovereign immunity of states that have obligation of executing them.

III. CONCLUSION

Stabilization clauses aim at ensuring legal stability governing business of foreign investors. This legal stability results in the predictability of the business environment and financial security. The oil and gas sector is one of the sectors whereby stabilization clauses are inserted in the contracts as the said clauses became popular in 1960s due to nationalization and expropriation of petroleum industry assets by some oil producing nations that wanted to benefit from the increase in oil prices.

Despite the usefulness of stabilization clauses, they are regarded by some people as a limit to the sovereignty of host states. Generally, the sovereignty of states allows them to manage their internal affairs including enacting the legal instruments needed to regulate certain matters. The principle of sovereignty of States over their natural resources has been particularly a justification of nationalizing and expropriating assets of foreign investors including those in the oil and gas sector. Stabilization clauses have been problematic in terms of nationalization, expropriation and in tax regime.

The fact that the principle of sovereignty of states in general and the principle of sovereignty of States over their natural resources in particular are regarded by some people as prejudiced by stabilization clauses, is due to the discrepancy between international investment law and other areas of law such as international social and environment law. Whereas international investment law in the first place aims at protecting economic human rights related to business, other human rights that are relevant to social and environmental issues are not primarily subject to international investment law because they fall under the regulation of other domains of international law, namely international social or environmental law. However, the said discrepancy between investment protection and other fields of human rights and environmental protection standards mostly arises in case of interpretation.

International investment law recognizes the principle of *pacta sunt servanda*. The said principle implies that a state cannot invoke its sovereignty and its internal order to disregard the commitments freely undertaken. In contrast to allegations that stabilization clauses limit the sovereignty of states, it was demonstrated that a state's agreement to be bound by a stabilization clause is considered a valid exercise of that state's sovereignty.

It is evident that one of the purposes of the principle of sovereignty of states over their natural resources is the protection of the countries that were under colonization whereby the economic activities were dominated by foreign companies. In this case, a host state is protected by the said principle if the investor exploits natural resources of the said state without the latter's consent. But, in case a host state freely consents to the exploitation of its natural resources, it is bound by the agreement it entered into with the investor and is not justified by the principle of sovereignty of states over their natural resources for not executing its contractual obligations.

It is obvious that though a host state has the duty to regulate its internal affairs for the best interests of its people; it has also the duty to execute contractual obligations that it undertakes. As long as a certain host state freely entered into an agreement with a foreign investor, that agreement binds both parties including that concerned host state. In this case, stabilization clauses should not be regarded as a prejudice to the sovereignty of states since a contractual relationship exists between an investor and a host state which retains the power of enacting laws that are enforceable to third parties.

Furthermore, some types of stabilization clauses aim at ensuring that a legal regime applicable to the investment project will not change over the life of the project; those are freezing clauses. Freezing clauses are reported to be the most used type of stabilization clauses in oil and gas contracts. However, it is evident that they have become less relevant since in practice host states are prone to compensate foreign investors instead of being prohibited to enact the needed legal instruments. As a result, stabilization clauses such as economic equilibrium clauses that provide for the compensation in case of legal change would be preferred since their enforcement is possible and advantageous. Instead of freezing clauses, we recommend for stabilization clauses that are concerned with providing for the compensation in case of a host state action that is prejudicial to the investment project especially in oil and gas sector whereby contracts are long-term and capital intensive.

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