EXPROPRIATION OF PRIVATE FOREIGN INVESTMENT: WHAT IS "ADEQUATE" COMPENSATION?

BY
KISAKIU POSMAN

I. INTRODUCTION

Third World nations have been subjected to a massive inflow of capital from the fathers of international law, the capital-exporting nations of the West. It is argued by some economic observers of the West and Japan that capital inflow coupled with appropriate government policies will be beneficial to a nation's socio-economic sectors. Arguments for foreign investment are based upon the 'capital shortage' of the developing States; economic growth is said to lead to an increase in the 'rate of growth of GNP', an increase in areas of employment and technological transfer from the developed industrial stages to the poor ones.

Acceptance of this argument has led in Papua New Guinea to investment by foreigners being concentrated in areas like mining, banking, engineering, oil and mineral exploration, plantations and metal working. Major capital investments in turn 'spins off' supporting investments. For example the huge Bougainville Copper Ltd. mining operation has created other business activities to service its operational needs as well as those of it's employees. Such characteristics, it is argued generate a more stable and predictable investment climate which subsequently leads to the encouragement of still more investment from outside and within.

However, production of goods, creation of employment opportunities and acquisition of new skills should not be allowed to camouflage the reality that foreign investment to a great degree is not capable of generating real economic growth beneficial to the bulk of the population in rural Papua New Guinea. Concentration of investment in urban areas (Port Moresby, Lae, Rabaul, Arawa, Goroka, etc.) has created a steady and widening gap in the nation's socio-economic development. On the one hand, one observes the steady and rapid growth of the urban sphere while on the other and lagging behind at a slow pace is the massive rural sector. A situation which is related to the obvious fact that an investor's primary objective is to make profit, not to develop the nation.(1)

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1. See the article by Short, K. 'Australian Investment in Indonesia: the case against', in McLeod, K.J. and Utrecht, E., (eds.) **The Asean Papers** Brisbane, 1978) 120-146.

Another negative aspect of foreign investment is that the host State does not in most cases, receive what is fully due to it. Foreign corporations are well known in practice for accumulating large profits through tax avoidance schemes, transfer pricing and over-invoicing. By virtue of such schemes part of the profits generated within are repatriated for investment elsewhere instead of being reinvested in the host nation. Apart from these exists the reality that private foreign investors possess the management skills and financial backing to out compete any domestic rival in their way, to gain both ownership and control of most major spheres of the economy of a Third World nation.

Against this background the principal capital-importing countries have resorted occasionally to expropriation of foreign owned property and interests. The process of expropriation is viewed by the international legal order as being a sovereign right of each and every nation whether big or small, powerful or weak. International law, however, has for a long time accepted that a nation may acquire ownership of a foreign national's property only if it is carried out for a public purpose, is not discriminatory, and is accompanied by compensation.

It is with the compensation aspect of expropriation that differences and controversies have arisen between the industrialized capital-exporters and the capital-importers of the Third World. This reflects the political and economic importance of this area of international law.

Thus the capital-exporting nations, generally still hold to a traditional western notion of 'adequate compensation'. By that is meant 'full market value' at the point when expropriation took place. On the other hand, the capital-importing Third World argues that a lower level of compensation should be accepted: one that is based on the interests of the host nations and as prescribed by their domestic legislation. They argue that only by such methods can the investment relationship be accounted for in arriving at the amount that should be paid. In short, the Third World argues that compensation should be determined by the expropriating nation's standards.

It is in the light of the controversies surrounding the compensation on expropriation that this article will attempt to determine which standard is the requirement of international law. This study will also attempt to determine Papua New Guinea's position on the issue.

II. INTERNATIONAL ACCEPTANCE OF EXPROPRIATION

This will not be an exhaustive study of how expropriation came to enjoy its present status at international law. However, a brief historical background of the subject may aid the reader in understanding the controversies associated with this state-owned right.

The year 1917 is significant to expropriation only for the reason that events of State acquisition that occurred thereafter finally led to the international acceptance of the notion as a right inherent to the sovereignty of all nations. During the pre-1917 era, acquisition of private foreign property by a State resulted in an immediate claim of State responsibility arising out of an act or omission in breach of a rule of international law and which causes injury to another state or to foreign persons.(2) State responsibility arises where a state breaches a legal obligation placed on it by international law. Hence, expropriation being the sovereign right of all States to exercise in conformity with the requirements of international law operated on a different level to that of the post 1917 period.

How the pre-1917 position prevailed was no accident. It developed out of the fact that during this period expansion within the Western sphere led the nations thereof to push out into what is now the Third World and resulting in the ownership and control of their then colonies. Acceptance of expropriation as a nation's international legal right was strongly viewed as a threat to their desire to maintain a stronghold over the economies of their colonies.(3)

The massive take-overs of foreign-owned property belonging to the West in 1917 and thereafter, forced the Western states to see and accept expropriation from a new perspective. This development is perhaps well summed up by Williams and de Mestral in the following language:

> The influence of the Soviet Union's policy of nationalization after the 1917 revolution gave impetus to the growing trend of newly-independent states to regain control of the economy and policy-making in their countries. Thus, international law in this area has done an about-face from advocating strict liability for expropriations to adhering to the view of a State's absolute right over it's resources".(4)

Today, expropriation continues to take place in many States, especially in the capital-importing nations of the Third World. And to argue against, and to doubt its legitimacy would be baseless. Despite the universial acceptance of the notion, many controversies have arisen between the Third World and the principal capital-exporting States regarding the subject.

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2. Refer to Williams, S.A. and de Mestral, A.L.C. **An Introductio to International Law** (Toronto, 1979) 95. Here the writers briefly touched on how the notion of expropriation was viewed during the pre-1917 period.

3. Williams and de mestral **Loc. cit.** citing Shaw, M., **International Law** (London, 1977) 329.

4. **Id.** 96.

State practice indicates that compensation is the most controversial aspect of expropriation in the present international environment. That is to say, if a nation possesses the capacity to pay compensation then traditional notions of international law permit the expropriation of foreign property. Some Third World countries, however, realize that to be subject to such limitation would lead to the continued ownership of their economy by foreign investors. Therefore in their endeavour to divorce from this foreign economic strong-hold they have opted to expropriate regardless of whether or not they possess the capacity to make indemnity payments.

III. THE ISSUE OF COMPENSATION

Stripped to its essentials the dispute is whether an objective or subjective measure of compensation is mandated by international law. First world capital-exporting states have argued that compensation must be 'prompt, adequate and effective'. This may be termed the traditional standard because until recently it has been applied substantially without dispute. However, Third World nations have begun to assert that, although compensation may be obligatory under international law, its measure should be determined by the expropriating state.

The Traditional Standard for Compensation.

If this is presently the situation, what then has been the traditional standard for compensation payment? Written literature in the form of official notes of States, books, and court decisions of nations have for long been supportive of the traditionally advocated western standard for compensation. This compensatory standard makes the prescription that indemnity for foreign-owned property be prompt, adequate and paid in an effective manner. The standard has been able to survive into today's global economic order although it now lacks global acceptance, especially among the Third World. Despite the discomfort the standard finds today it remains important.

The well known **Rose Mary Case,(5)** disputed before the Supreme Court of Aden is a case that illustrates the western view well. The Court held that expropriation of foreign-owned property is contrary to international legal requirements if the expropriating State does not make allowance for the prompt, and adequate payment of compensation in an effective manner. An official note in support of the standard was delivered by the United States in the following words; "that it's citizens will receive prompt, adequate and effective compensation from the expropriating country".**(6)**

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5. **Anglo-Iranian Oil Co. v. Jaffrate** (1953) 1 W.L.R. 246.

6. See the United States: Department of State Statement on Foreign Investment and Nationalization (1976) 15, I.L.M. 186.

Its continued vitality is also illustrated by two bilateral agreements concluded between the United Kingdom and Egypt, and between United Kingdom and Singapore which have opted for the traditional western standard of compensation.(7)

Similarly most States that have membership with the Organization for Economic Co-operation and Development (O.E.C.D.), especially the capital-exporting powers, accept and subject themselves "to the theory that for expropriation to comply with international law,...the person whose property has been taken over must be given prompt, adequate and effective compensation".(8) In other words these powers accept the view that not to pay such compensation is a breach of international law. Nor is the traditional western standard without theoretical advocates: O'Connel for example claims that expropriation must be accompanied by adequate compensation with effective measures that would ensure prompt payment.(9)

Obviously, the terms 'prompt', 'adequate', and 'effective' are descriptive words which have been adopted so that they may be interpreted to accommodate the circumstances of each individual case. What have these terms meant to those that advocate them?

(i) Promptness

The requirement that payment be prompt led the court in the **Norwegian Claims** case to speak for "just compensation in due time."(10) In the dispute between Germany and Rumania in 1928, the tribunal announced that "payment shall be quickly as possible...".(11) And in the **Norwegian Shipowners** claim the court held that payment should have been made "at the latest day of the effective taking."(12) All these interpretations accorded to promptness are well summarized by section 189 of the **Restatement (Second) Foreign Relations Law** of the United States. This section

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7. Egypt-UK Agreement for the Promotion and Protection of Investments, 11 June 1975 (1975) I.L.M. 1470; Singapore-UK Agreement for Promotion Protection of Investments, 22 July 1976 (1976) 15 I.L.M. 591. See article 5 of both Agreements for the adoption of prompt, adequate and effective payment as the standard for compensation.

8. This was observed by Williams, and de Mestral **loc.cit.**

9. O'Connel, D.P. **International Law** (Vol.2. London, 1965) 852.

10. **The Norwegian Claims Case** (1922). The Hague Courts Report (ed. by Scott, J.B. 1932) 66 as quoted in Gracia-Amador et.al. **Opt,cit** 56.

11. See also the same page of Gracia-Amador **et.al.**

12. Refer to O'Connell, **Op.cit.**, 857.

defined promptness as meaning "payment as soon as is reasonable under the circumstances in the light of the international justice."(13)

One qualification to this is provided by the United Kingdom in the **Rose Mary Case** . The United Kingdom suggested that the international law condition of promptness would be satisfied if, first, the total quantum to be paid is promptly fixed; second, that allowance be made for interest on any late payment; third, the deprived owner should be given guarantees that would satisfactorily enforce the making of future payments. This would allow the foreigner who is to be compensated to "raise the full sum at once on the security of the future payment"(14)

(ii) Effectiveness.

The condition of effectiveness of compensation is well exposed by the following:

> "The recipient of the compensation must be able to make use of it. He must, for instance, be able, if he wishes, to use it to set up a new enterprise to replace the one that has been expropriated or to use it for such other purpose as he wishes.
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> Monetary currency which is in blocked currency is not effective because, where the person to be compensated is a foreigner, he is not in a position to use it or to obtain the benefit of it. The compensation must therefore be freely transferable from the country paying it and so far as the country's restrictions are concerned, convertible into other currencies".(15)

In other words the compensation paid must be in a form that is negotiable and transferable, and which is easily convertible so that the divested property-holder may use it in whatever way he pleases. It was because of this that United Kingdom viewed the Iranian Nationalization Law as having no fixed criteria which would satisfy the requirement of effectiveness.

(iii) Adequacy.

'Adequacy' concerns the amount of compensation that should be paid by the expropriator. The **Charzow Factory Case**, resolved by the P.C.I.J. defined this as "the value of the undertaking at the

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13. Parts of this legislative enactment are contained, and discussed in Steiner, H.J. and Vagts, D.F., **Transnational Legal Problems** (New York, 1968) 330-331.

14. (1951) I.C.J. Rep. 106' see pleadings.

15. Ibid. It may also be located in O'Connel, **Opt.cit.** 860.

moment of dispossession plus interest to the day of payment."(16) This definition has been adopted by the **Restatement (Second) Foreign Relations Law** of the United States in similar language. Section 186 states "the amount must be equivalent to the full value of the property taken together with interest to the date of payment". 'Full value' according to this legislative enactment "means fair market value if ascertainable. If fair market value is not ascertainable, it means the fair value as reasonably determined in the light of international standards of justice".(17)

The two investment agreements to which the United Kingdom is a party, entered into with Egypt and Singapore, accepted adequate compensation to mean the market value of the dispossessed investment together with interests on late payments,(18) Another agreement between Egypt and Japan also accepted the market value standard but was even more generous in that it provided for compensation for loss of profit at the time of the taking.(19) It may be generalized from these definitions that basically 'adequate compensation' refers to the payment of the market value of the expropriated investment.

If this is the case, what then is 'market value'? The Ontario Law Reform Commission has defined market value as "the price at which a prudent seller under no compulsion to sell would sell a property to a prudent buyer under no compulsion to buy. Most property has a readily appraisable market value relating to its use and location".(20) This however, is qualified by O'Connell who makes the observation that "the market value of an investment depends on the security the investment enjoys" together with the fact that "due to abnormal economic circumstances the market value of assets [may be] temporarily inflated or deflated".(21)

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16. (1928) P.C.I.J. Series A. No.17. A good brief of the case may be seen in Steiner and Vagts Op.cit. 315-318. The P.I.C.J.'S definition of 'adequate' may be found in p.317 of the book.

17. Section 188 is in Steiner and Vagts Op.cit. 331.

18. Egypt-UK Agreement (1975) 14 I.L.M. 1470; Singapore-UK Agreement (1976) 15 I.L.M. 591. Refer to article 5 of both agreements.

19. Egypt-Japan: Agreement on the Encouragement and Reciprocal Protection of Investment, 28 January 1977 (1979) 18, I.L.M. 44. See article 5 of the agreement.

20. Refer to the Report by the Ontario Law Reform Commission on **The Basis for Compensation on Expropriation**. (Toronto, 1967) 18.

21. O'Connell, op. **cit. 857-858**

How Adequate is Adequate?

We have noted that most disputes concerning expropriation concern compensation. In turn, most disputes concerning compensation have revolved around the question of adequacy. That is so because despite the continued assertion of the capital-exporting nations that compensation must be adequate, as defined above, there is neither agreement to that effect in the relevant juristics writings, nor is it inconformity to the standard universally evident in tribunal holdings, diplomatic correspondence and decisions of municipal courts. Accordingly, each of these sources of international law will be examined in turn, in order to illustrate the diversity of practice and theory which applies to the claim.

(i) Holdings of international tribunals.

It is important to note at the outset that the P.C.I.J. has announced rulings which have been supportive of the requirements that adequate compensation be paid to deprived property owners as was the situation in the **Chorzow Factory Case**. Here the Court was concerned with 1920 legislation passed by Poland which allowed for the acquisition of all properties, titles to which flowed from the German State. In 1922 a Polish Court decreed that registered land in Chorzow be transferred to the ownership of the Polish Treasury. Although the terms of the legislation were general, it was purposely enacted against German citizens in violation of Polands treaty obligations to Germany as contained in the 1919 Treaty of Versailles.

Reliance has been placed on this case as a precedent in support of the principle of adequate compensation, but the decision must be read in the context it was made. The P.C.I.J. held that compensation should be paid by the Polish Government to two German companies whose land was acquired based on "the value of the undertaking at the moment of dispossession, plus interest to the day of payment".(22)

This case however, should not be seen as one which best supports the notion of adequate compensation for two reasons. Although there was an actual taking of property resulting in an order of the P.C.I.J. for "restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear" of nationalized property, it should be noted that the holding was greatly influenced by the fact that Poland breached her treaty obligations with Germany. Hence the Court saw the act as being illegal, and not a mere act of expropriation as the Polish state argued it was. The acquisition of rights to adequate compensation by virtue of treaty provisions should not be employed interchangeably with other

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22. Charzow Factory (1928) P.C.I.J. Series A No.17

situations where the taking of property does not violate treaty obligations conferring such rights, or where there is no acquired right to this compensatory standard.

Furthermore and equally important, the decision was made in 1928, a period when the Western nations were in the majority in the family of nations. Today, the situation has altered; the Third World now possess this majority and within this majority there is a continuous struggle to develop without being subjected to foreign domination and influence on the economic front. From this one finds the emergence of new compensatory standards. It is debateable therefore that the rule developed by the case has outlived it's relevance.

The dissenting opinion of judge Levi Carneiro in the Anglo-Iranian oil dispute between U.K. and Iran, however, provides a recent illustration of arguments in support of the requirement for adequate compensation. Justice Carneiro held that payments of partial compensation involved the host nation is subjecting the foreigner to a "more extensive sacrifice". The judge also held "that present day conditions of international life have not done away with the proposition" of adequate compensation. Present conditions "have given added weight to this proposition which has become a prerequisite of international co-operation in the economic and financial fields".(23)

Carneiro's views reflect the concept held by most peoples of the principal capital-exporting sphere that foreign investment brings with it nothing but goodness to the Third World. To say that the nonpayment of adequate compensation means subjecting foreigners to "more extensive sacrifices" reflects an inability to appreciate the negative aspects of such investments, i.e. the repatriation of large profits through tax schemes. To base the argument in support of adequate compensation upon the contention that foreign investment is naturally beneficial to the development of the capital-importing State's economy is a rather shaky assumption.

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23. (1952) 1 I.C.J. Rep. 93. See P.151-171, and Carneiro's reasonings for adequate compensation may be located at P.162.

(ii) The Views of Writers.

Jurists in the principal capital-exporting nations do not all accept that adequate compensation is an international legal requirement. With regard to the issue of the quantum of compensation, writers fall into three schools of thought. The first is of the view that there need be no payment of compensation provided the property-holder is not discriminated against. The second says that account may be taken of the expropriating nations financial capacity to pay and the third asserts that adequate compensation must be paid.(24)

Writers like Garcia-Amador, Sohn and Baxter claim that the test of adequate compensation still applies today. This they argue is illustrated by the general acceptance of international case-law in individual expropriation proceedings.(25) The difficulty here, as acknowledged by them, is that the precedents are neither abundant nor explicit. Even if adequate compensation is the requirement, that in itself does not provide a complete measure to calculate the quantum of compensation.

The doctrine of 'unjust enrichment' is argued by Cheng to support the standard of adequate compensation. He views the host nation's acquisition of private property as enriching it, i.e. the State is enriched by the value of the property together with any future profits it may generate.(26) The significance of this view appears to be that aspects of the deprived investors loss are not taken into account, but rather the enrichment that would be obtained by the expropriating State. It is clear therefore that

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24. The three distinct schools of thought on the standard of compensation may be seen, and are clearly discussed,in O'Connell Op. cit. 858-859.

25. Garcia-Amador, F.V. et.al. **Recent Codification of the Law of State Responsibility for Injuries to Aliens.** (New York, 1974) 54-55. These writers have also taken note of the argument advanced by Strupp and Kaeckenbeek that payment of compensation is not essential, what is important is that expropriation with or without compensation should not be performed in a discriminating manner.

26. This observation is made by Cheng, B. 'The RationaleTransactions 267.
Transactions 267.

this is intended to be an equitable principle. Hence, it "requires the taking into account of all the circumstances of each specific situation and the balancing of the claims of the dispossessed alien with the undue advantages that he may have enjoyed prior to nationalization".(27) This clearly indicates that the doctrine works both ways, i.e. for and against the deprived investor. It follows that where the investor has been unduly enriched because he enjoyed a period of monopoly control, or a highly privileged business position, the principle may be employed against him.(28)

Another writer throws a different light on the issue of compensation. Friedmann separates expropriation into two distinct categories, that which he calls 'individual expropriation' and 'general expropriation'. In his pursuit to analyse the problem of indemnity he argues that in the former the investor should be compensated for an unlawful act taken against him, and in the latter, where all foreign-owned properties are expropriated, any compensation payment would be regarded as exgratia.(29) The view projected here is that compensation depends on whether the expropriation is lawful or unlawful. If not lawful, the writer asserts that the owner should be paid compensation. Does this mean therefore that if it is lawful, the owner gets no compensation? From Friedmann'perspective the answer is yes. However, Fatouros argues that interference though lawful still creates an obligation to pay compensation. He further explains that the distinction between lawful and unlawful only helps to calculate the quantum of compensation.(30)

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27. See de Arechaga, E.J. 'State Responsibility for the Nationalization of Foreign Owned Property' (1978) 11 New York Uni. of int. Law and Politics 179.

28. Refer to Friedmann, W. **The Changing Structure of International Law** (London, 1964) 209, cited in Sornarajah, Mr. 'Compensation for Expropriation: The Emergence of New Standards' (1979) 13 J.W.T.L. 108. Friedman clearly illustrates how 'unjust enrichment' may be employed against the investor.

29. See Friedmann, S. Expropriation in International Law (1953) 213, cited in Cheng, B. **The Rationale of Compensation for Expropriation** (1958-59) 44 Groitus Transactions 267.

30. Fatourous, A.A. **Government Guarantees to Foreign Investors** (London, 1962) 307-315. In unlawful acquisitions compensation covers the investors' loss, and different considerations apply in the case of lawful measures.

Thus while the principal capital-exporting nations of the West advocate that compensation payments must be adequate the writers thereof offer conflicting views on the accepted standard to be applied. There are those like Strupp and Kaekenbeek who support the first school of thought, i.e. compensation should only be paid where acquisition of property is discriminatory. Others like de Arechaga argue in favour of the view that a nations' financial capacity and policies be accounted for in determining compensation payment, while others like Garcia-Amador support 'adequacy' as the standard. Then there is Friedmann who offers another argument based on two distinct types of expropriation. One may conclude therefore that the standard of 'adequate compensation' does not find total acceptance by writers, even those of the capital-exporting sphere.

(iii) Official claims of nations

Investment disputes between governments and foreign investors have often revolved around the issue of standards of compensation. Claims by the states concerned demonstrates the parties understanding and acceptance of the problem of compensation. Diplomatic or other official notes aid us by illustrating where a government stands regarding the standard by which payment of compensation may be calculated.

The well-known dispute between Mexico and the Untied States concerning compensation for agrarian and oil properties owned by United States nationals and corporations, which were expropriated by Mexico from 1915 to 1940 cannot escape discussion.(31) Mass demonstrations led by the dispossessed owners in the United States forced their government to exchange several diplomatic notes with it's Mexican counterpart. The notes sent by Secretary of State Hull continued to push for the payment of full compensation. A note dated July 21, 1938 read in part:

> "The taking of property without compensation is not expropriation. It is no less confiscation because there may be no expressed intent to pay at sometime in the future.
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> If it were permissible for a government to take the property of the citizens of other countries and pay for it as and when in the judgment of the government, it's economic circumstances and it's local legislation may perhaps permit, the safeguard which the constitution of most countries and established international law have sought to provide would be illusory. Governments would be

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31. See a discussion of the disputein Steiner and Vagts op.cit. 319-323.

free to take property far beyond their ability or willingness to pay, and the owners thereof would be without recourse."(32)

In response to this the Mexican State on August 3, 1938, stated that "there does not exist in international law any principle universally accepted by countries, nor by writers of treatises on this subject, that would render obligatory the giving to adequate compensation for expropriations of a general and impersonal nature".(33) However, the Mexican Minister admitted that Mexico was under an obligation, by virtue of her municipal laws to indemnify the deprived United States propertyowners in an adequate manner. The Minister claimed that the time and manner in which compensatory payments would be made would be decided by Mexican national law. However, in spite of it's insistance that that 'adequate' compensation was not a universally accepted standard in international law, Mexico eventually agreed with U.S.A. to pay a sum proposed by an internal commission.

More recently expropriation of the Marcona Mining Company's subsidiary in Peru on July 25, 1975, resulted in the U.S. Government claiming that compensation should be negotiated between the Peruvian State and Marcona in accordance with the generally accepted principles of international law.(34) A month later however, the U.S. Government opted for the usual Western sponsored terms of seeking prompt, adequate and effective compensation.

By October 1975, Peru officially expressed its disinterest in negotiating with Marcona but favouring dialogue with the Government of U.S.A. as it felt such a dialogue would lead to the negotiation of favourable terms for Peru. With pressure from the company, the U.S. eventually consented to act as an intermediary in an effort to settle terms acceptable to both disputing parties. Under U.S. law, failure to provide prompt, adequate and effective compensation would have exposed Peru to the risk of losing "its eligibility for trade preferences and bilateral assistance as well as U.S. support for lending from the international financial institutions".(35)

The Peruvian Government on the other hand "had assessed a variety of takes and other charges against the Marcona Company which, if sustained would substantially reduce the value of any final

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32. **Id.**, 320.

33. **Id.**, 321.

34. In discussing this dispute reliance was placed on the article by Gant Z., D.A. 'The Marcona settlement: New Forms of Negotiation and Compensation for Nationalized Property' (1977) 71. Amer. J. of Int. Law, 474-493.

35. **Id.** 480.

settlement paid to Marcona".(36) The U.S. after consultation with the company finally concluded that if a settlement was to be reached, concessions in the standard of compensation were necessary. Hence the parties settled for the payment of compensation that would be fair to both Marcona and the host State.

It may be generalised from those two cases that whilst theoretically it is arguable that 'adequate' is the standard by which compensation is to be measured the practice of States operates on a different level because not only are economic considerations taken into account, as in theory, but also political and social factors are considered, especially where a foreign State is negotiating for its citizens who have been deprived by the host State. In other words while capital-exporting powers advocate and support 'adequate compensation', practice shows that at times they have had to accept a lower standard.

(iv) Decisions of municipal courts

In 1933 a concession agreement was concluded between Iran and the Anglo-Iranian Oil Company (A.I.O.C.), an English owned company. By virtue of this agreement the company acquired exclusive right to exploit oil within the concession area. A change in government in Iran was followed in 1951 by the expropriation of all A.I.O.C. property and interests. This action opened a number of municipal curial decisions. One such was the **Rose Mary Case** which was brought before the Supreme Court of Aden.

This dispute arosed out of the following facts. An Italian company had contracted to import nationalized oil from Iran and sell it to a Swiss firm. The "Rose Mary" was a vessel chartered by the Swiss firm. It loaded oil extracted from the concession area of th A.I.O.C. Returning it stopped at Aden and the A.I.O.C. instituted proceedings in that Court demanding delivery to it of the oil claiming the Iranian nationalization law had been contrary to international law. This claim was based on the argument that there had been no provision for compensation in the Iranian law. Justice Campbell held for the plaintiff. He stated that without prompt, adequate and effective compensation the disputed oil remained the property of the English company. He ordered that the cargo be returned to A.I.O.C.

In reaching this decision the Court held that articles 2 and 3 of the Iranian Law were not capable of being read so as to confer a right to compensation.(37) Article 2 reads:

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36. **Ibid.**

37. Anglo-Iranian Oil Co. v. Jaffarate (1953) 1 W.L.R. 246. Discussion and analysis of the compensation issue with reerence to articles 2 and 3 of the Iranian Nationalization Law may be located in p.252 and 253.

> The Government is bound to dispossess at once the former Anglo-Iranian Oil Company under the supervision of the mixed board. If the Company refuses to hand over at once on the grounds of existing claims on the Government, the Government can, by mutual agreement, deposit in the Bank Milli Iran or in any other bank up to 25% of current revenue from the oil after deduction of exploitation expenses in order to meet the probable claims of the Company."

The Court argued that strictly construed in it's grammatical sense article 2 did not amount to an offer to pay compensation. Why article 2 should be construed strictly was a matter not clarified by the judge.

Article 3 reads:

> "The Government is bound to examine the rightful claims of the company under the supervision of the mixed board and to submit its suggestions to the two Houses of Parliament in order that the same may be implemented after the approval by the two Houses."

The Court held that article 3, like article 2 placed the company at the mercy of the expropriator. Campbell, J. reasoned that even if the mixed board, established under article 3, concluded that adequate compensation should be promptly paid, implementation of it's determination would depend on the approval of the two Houses. and there is no guarantee that the Houses will accept the board's determinations. Nor did the Court.

Another case in consequence of Iran's expropriation of the A.I.O.C. operation was pursued before the High Court of Japan. A.I.O.C. applied for an interim order to place imported oil in the custody of the Court. It claimed that the Japanese company which had purchased the oil acquired no title to it. It contended that Iran possessed no right to sell the oil because A.I.O.C. had received no compensation payment. In short the company argued it still owned the oil. However, the Japanese Court held that expropriation without payment of adequate compensation was valid under international law.**(38)** This conclusion was also arrived at by the Civil Court of Rome which sat in judgment over a similar A.I.O.C. suit against an Italian company.**(39)**

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38. **Anglo-Iranian Oil Co. v. Indemitzu Kosan Kabushiki Kaisha** (1953) 20 I.L.R. 305.

39. **Anglo-Iranian Oil Co. v. S.U.P.O.R. Company (1955) 2 I.L.R** 23.

Finally, Upjohn, J. in Helbert **Wagg's Case(40)** discussed the decision in the **Rose Mary Case** and conceeded that, contrary to Campbell, J's views, both domestic and foreign authorities do not give rise to a general rule that any "legislation that expropriates without compensation is contrary to international law...".**(41)**

It is evident from the three subsequent cases that expropriation without payment of compensation, that is to say confiscation is now not widely regarded as a violation of international law. The **Rose Mary Case,** however, is clearly a case which demonstrates the conception held by many capital-exporting powers on the issue where no compensation is paid. The extent to which the **Rose Mary Case** holding survives the other three decisions lies on the issue of effectiveness. Campbell, J. ruled that the Iranian law provided no guarantee that compensation would be effectively paid at a latter date.

(v) Bilateral agreements.

The idea of 'adequate compensation' has been incorporated into many treaties, to which the United States is a party. These agreements have generally provided that not only should compensation be 'adequate' but it should also be 'prompt' and 'effective'. This practice is clearly reflected in the number of bilateral treaties of Friendship, Commerce and Navigation concluded between the United States and other countries.

For instance article (vii) of the Treaty of Friendship, Commerce and Navigation entered into with Greece on August 3, 1951 makes provision for "the prompt payment of just compensation...in an effectively realizable form" of "the full equivalent of the property taken...". Another, entered into with Japan on April 2, 1958 contains similar expressions on compensation, and the November 14, 1946 agreement with Czechoslovakia requires that "adequate and effective compensation be paid on expropriation".**(42)**

Similar clauses have been negotiated in contracts between sovereign States and multinational corporations. Thus the Ghana-Valco Agreement of November 17, 1960, between Ghana and the Volta Aluminium Company requires the host government to abstain from expropriating any company property or interests for a period of

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40. **In re Claim by Helbert Wagg & Co. Ltd.** (1956) 1 Ch. 323.

41. **Id.,** 346.

42. These agreements are briefly discussed, and parts thereof cited in Garcia-Amador et.al. **Op.cit.** 55.

thirty years".(43) Article 38 of the Agreement adds that after the thirty year period, any expropriation proceeding must be supported by the payment of 'prompt', 'fair', and 'adequate' compensation.

Nations other than the U.S. have also concluded such treaties. Egypt and Japan entered into an investment agreement on Janaury 14, 1978. This is a bilateral undertaking between the States to strengthen their economic ties by creating conditions favourable both in the encouragement and protection of investments by citizens and corporations of each party.(44) Obviously, the agreement is most advantageous to Japan, because there is little Egyptian investment in Japan. Egypt, nonetheless, agreed that the process of expropriation should not be undertaken by either contracting party, unless pursued for a public reason without discrimination and followed by prompt adequate and effective compensation.(45)

The agreement clarifies the adequacy aspect of compensation by stating that:

> "The compensation referred to ... shall represent the equivalent of the normal market value of the investments and returns affected at the time of when expropriation ... was publicly announced or when such measure was taken, ... without reduction in that value due to the prospect of the very seizure which ultimately occurs."(46)

What can be observed here is the mutual desire of both contracting parties to equate the compensation standard of 'adequacy' with the 'normal market value' requirement, at the time of the acquisition.

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43. The parts of the agreement concerning expropriation and compensation are briefly discussed by Nwogugu, I. **The Legal Problems of Foreign Investment in Developing Countries** (USA, 1965) 170-172.

44. Egypt-Japan: Agreement on the Encouragement and Reciprocal Protection of Investment (1979) 18 no.1 I.L.M. 44-48.

45. See article 5.2 of the Egypt-Japan Agreement.

46. See article 5.3 of the Egypt-Japan Agreement.

From the sample of bilateral agreements discussed and mentioned, it may be generalized that where a capital-exporting power is a party, 'adequacy' will, more likely than not, be adopted as the quantum of compensation. Third World States contracting with their capital-exporters have had to accept 'adequacy' basically because of the lack of bargaining power they possess on the economic front. Where both parties are capital-exporting forces, they will always opt for 'adequacy' as illustrated by the number of Treaties of Friendship, Commerce and Navigation discussed. However, even where treaties adopt 'adequate' as a standard, that does not mean that practice will always result in the application of the standard.

Third World State Practices.

To discuss emerging compensatory notions requires focusing upon State practices of the capital-importing nations of the Third World. Those nations in recent times have exercised their sovereign rights to expropriate more than their Western counterparts. This trend is obviously not accidental. Many countries of the Third World have now come to the view that the global economic order is controlled by a powerful minority comprising of the Western European States, U.S.A., Japan, South Africa, New Zealand and Australia. For example, Chile has argued that international relations are founded on an unjust system, imposing on dependent capital-importing Third World nations uniletral decisions made by their capital-exporting opposites.(47)

Some Third World countries are further aggrieved by the lack of adequate legislation to regulate and control activities of foreign monopoly enterprises.(48) Parts of profits which they see as legitimately theirs have been repatriated through such methods as transfer pricing, over-invoicing, and payments for management and technology. Some States, eg. Chile, have asserted that while these economic realities exist on the international level, the argument that foreign investment is advantageous to the capital-importing State is weak. They claim that there is evidence that the capital-exporter is the most advantaged party, getting the biggest reward "at the expense of the underdevelopment and backwardness of the masses in those countries in which they establish themselves".(49) It is accordingly not surprising that expropriation has occurred more frequently in the Third World which is struggling to take control of it's own economic destiny.

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47. Refer to the Chilean Decree concerning Excess Profits of Copper Companies of September 28, 1971 (1973) 12 I.L.M. 983.

48. Ibid.

49. Ibid

Recent state practices have shown a remarkable diversion from the traditional and long advocated Western view of compensation payment. Developing countries even though aware that to depart from the standard advocated by their capital exporters may result in economic and political pressures and sanctions, have not been entirely unwilling to do so. An example is the Republic of Chile, which issued a decree on September 28, 1971 for the expropriation of copper enterprises. It formulated it's own rules to govern compensation based on equitable social terms. The measure of compensation involved looking back into the past and making allowances for the exploitation of natural resources of large copper mines by private foreign investors at a time when there was no proper legal machinery to retain benefits that rightfully belonged to the State. Chile accordingly developed the notion of 'excess profits' which was to be deducted from the compensation claims of the private foreign investors. Chile consented to meet her obligation to compensate, but only on the condition that any excess profits made by the investors was to be deducted from their claims.

The three dispossessed foreign corporations appealed to the Special Copper Tribunal. All three argued that deduction of excess profit was not only improper but it also violated the concept of compensation payment. The tribunal however, rejected this claim. It agreed that under civil law, 'compensation' meant "payment for loss or injury caused by negligence, fault or dolus of an individual outside the contract".(50) The tribunal however, ruled that such concepts did not apply in a situation where one party is a State and a compensation claim is being pursued as a result of an act of State. So long as that act is lawful 'excess profits' may be deducted from the compensatory claims of private investors.(51)

In consequence Chile applied it's own measure of compensation. That measure was determined initially by taking into account the balance sheets of the foreign investing companies, from May 5, 1955 to December 31, 1971. The sheets however, omitted mention of benefits which the parent enterprises had successfully drained from their subsidiaries through tax avoidance schemes. Accordingly, the balance sheets were adjusted to reflect the 'real' profit and loss of the companies. After this adjustment a 'normal profit' margin was calculated. The State then held that any profits over that which is 'normal profit' were 'excess profits' which the subsidiaries were not entitled to because they rightfully belonged to the host State. The then Chilean Constitution made specific mention of this principle by requiring

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50. See the Special Copper Tribunal Decision on the Question of Excess Profits of Nationalized Copper Companies of August 11, 1972 (1972) 11 I.L.M. 1013. Discussion on the civil law aspects of compensation may be seen at p.1027.

51. Ibid.

the deduction of excess profits procured by foreign companies "as a means of restoring to the country the legitimate participation it should have obtained from [it's] natural resources".(52) Brutal military intervention brought the Allende regime to an end in 1973.(53) The part C.I.A. played in this episode is common knowledge today. On gaining control of the Chilean State, the military junta announced that it was prepared to settle and reach a new agreement with the deprived foreign investors on the issue of compensation.(54) The military junta was dependent upon the support demonstrated by the United States, hence it was hardly surprising that compensatory payments were reviewed using the standard of 'adequacy'.

Another modern example of expropriation in the Third World worthy of study is that of Libya in 1971. Under the Libyan Petroleum Law of 1955 the Petroleum Commission possessed the authority to grant concessions in conformity with the Petroleum Law. Through this legal machinery the British Petroleum Company (B.P.C.) entered into a Concession Agreement in 1960 with the State to explore and exploit a defined concession area for 50 years. B.P.C. however, was only able to operate the concession area for about 12 years. On December 7, 1971 the British Petroleum Nationalization Law was passed authorising the acquisition of the company's properties, rights, assets, and shares by the State, and their transfer to the State-owned Arabian Gulf Exploration Corporation,(55)

The B.P. Nationalization Law prescribed that the host "State shall pay the party concerned compensation for all property of funds, rights and assets transferred to it" and that "such compensation shall be determined by a Committee..."(56) In determining the amount of compensation to be paid the Committee was to determine the quantum payable after taxes, fees and any other debts due to

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52. See the Chilean Decree **Loc. cit.**

53. Girvan N. **Corporate Imperialism: Conflict and Expropriation**, (London, 1978) 85-94. Here, the writer traces the chain of events and factors which eventually led to the overthrow of Allende's government.

54. Illustrations of payments made by the military junta may be seen, **id.**, 94.

55. A good brief of the B.P. Concession Agreement is provided by White, R.C.A. 'Expropriation of the Libyan Concessions - Two Conflicting International Arbitrations' (1981) 30, part 1. Int. Comp. Law Quarterly 3-4.

56. See article 5 of the Law Nationalizing British Petroleum Company (Libya) (1972) 11 I.L.M. 381.

the State from the nationalized activities had been deducted from the value of the compensation.(57) The Nationalization Law further provided in article 7 that the Committee was to be given a maximum of three months within which to determine the actual amount to be paid, i.e. after the deductions have been made. The article further provided that the Committee's determination was to be final and could not be appealed against by the affected party. The Committee was obliged to bring its decision to the notice of the Minister of Petroleum and he in turn was obliged to convey it to the dispossessed corporation within 30 days.

Following the expropriation of the B.P. concession area, the State failed to forward notice of the determination of the Committee within the 30 days required by article 7 of the Nationalization Law. British Petroleum also claimed that the B.P. Nationalization Law was discriminatory because other concessionaires were left untouched. The company and Libya argued and this dispute when arbitrated centered around those two factors. The claimant also requested the arbitrator to order the State to perform her obligations as contained in the Concession Agreement. Clause 16 of that Agreement provided that:

> "The Government of Libya will take all steps necessary to ensure that the company enjoys all the rights conferred by this concession. The contractual rights expressly created by this concession shall not be altered except by mutual consent of the parties."

The sole arbitrator noted that in a dispute as this, most cases had been resolved through the remedy of compensation payment, not restitutio in integrum. There was no consent given by the disputing parties to apply the rules of specific performance or restitutio in integrum nor was there evidence to warrant the adoption of those rules as part of international law. Judge Lagergren,(58) the sole arbitrator, accordingly held that although the British Petroleum Nationalization Law was contrary to Libya's obligations to the claimant under the Concession Agreement, it merely entitled the company to compensation and not the remedy of restitutio in integrum. The rule which is illustrated by this dispute is where a State has breached contractual obligations owed to an investor, the State must pay "the full measure of the investors loss". That measure can be contrasted with the notion of "appropriate compensation payable in the case of a lawful"(59) take-over. This rule however, is not absolute. Where the

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57. See article 6 of the B.P. Nationalization Law.

58. Judge Lagergren is the President of the Court of Appeal for Western Sweden.

59. See White **Op.cit.**, 16.

nationalization law is effective to terminate the contractual relationship of the parties, effect can be given to any claims due to the State as prescribed by the legal instrument of nationalization.

It was in this way that compensation paid to British Petroleum was calculated. The full value of the company's loss was agreed to be £62.4 million and what was due to Libya in the form of royalties, takes plus other claims amounted to £45 million. After deducting Libya's counter-claim, the host State paid a net amount of £17.4 million.**(60)** This judgment of Lagergren, J. explicitly illustrates that the expropriation was unlawful, not because of failure to comply with the Nationalization Law and the method of it's implementation were a breach of the State's obligations under the concession Agreement, but, because the nationalization instrument and the act of expropriation which flowed from it were unlawful because they were a violation of the obligations conferred on the State by the concession Agreement. Despite this the Nationalization Law was effective to bring the Agreement to an end.

Another example of Third World practice is that of bauxite nationalization in the State of Guyan.**(61)** 1916 saw the incorporation of the Damerara Bauxite Company (Demba) in the then British Guiana. The company was incorporated to operate and exploit a number of bauxite concessions. Demba in reality was the subsidiary of a North American enterprise, Alcan Aluminium Ltd., and it made a massive contribution to the growth of it's parent company. Girvan illustrates this by showing that Demba formed the foundation on which Alcan's assets increased from $45 million in 1928 to $423 million in 1950, and the foundation for the great jump in Alcan's aluminium production from nearly nothing to well over 400,000 tons per year during that period. Despite the subsidiary's generation of large profits, its tax payments were comparatively small because prices for Demba sales to Alcan were fixed by the parent company purposely to reduce Demba's overall tax burden.

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60. These figures may be located **id.** 17. Apart from this the writer also pointed out that the final settlement of £17.4 million represented close to 28% of B.P.'s claimed interest in the concession, this level of settlement, argued by the writer, falls in line with the 25-30% of value which seems to be the most commonly accepted level according to State practice.

61. This basically represents asummary of the writers discussion and analysis of the 'Bauxite Nationalization in Guyana'. The reader should be wary of the fact that in some judgments and conclusions drawn by the writer, he neither provides nor refers to supportive evidence. See Girvan **Op.cit** 160-187.

Guyana as a consequence was paid some of the lowest taxes per ton of bauxite mined in the Caribbean. Demba also secured a ten year tax holiday from the colonial administration for a small aluminium plant it decided to erect in 1961, despite having been there for over 40 years. Without giving any supporting evidence, Girvan also noted that Demba's operations established a firm link between Guyana's natural resources and the industrialization of the North American economy. However, Guyana continued to be underdeveloped, with her masses poor and economically impotent.

Such economic inequality prompted the government of Forbes Burnham to nationalize the Demerara Bauxite Company in July 1971. This step was not the State's initial intention. Earlier in 1970 the government had been more interested in securing effective majority control and participation in Demba. It realized that to consent to a 'management contract' and to allow the existence of 'minority shareholder's rights' would in total mean paralysing the State as the majority shareholder to make decisions.

The government's suggestion for compensating the company for the proposed majority holding, was that it be determined in accordance with the book value of Demba's assets. The book value was that which was used for calculating income tax as at December 31, 1969 and any 1970 additions. The government proposed that payments for the States holding would be paid from future profits due to the nation.

In support of these proposals the government argued that by adopting the 'income tax value' it could avoid paying 'full market value'. Compensation based on 'market value' would result in Guyana paying two to three times the 'income tax value'. The lesser compensation would in part redress the previous imbalance of economic benefit. Secondly, the proposition that payments be made from future profits obviously emerged out of the Zambian lessons. Basically it was intended to place the State on a safer footing so that Guyana would only pay when profit was generated. Thus, if accepted, it would force the parent company to co-operate as a minority shareholder in ensuring that future profits were actually made.

Caught unaware, the company lodged a counter proposal requesting that a partnership be formed with a 51% holding to the Company and 49% to the State. This was subsequently altered to, 51% to the State and 49% to Alcan, but with the entire amount of the subsidiaries assets to be contributed as a loan. Alcan's obvious reason for this was that the company would in time recover the full amount of it's assets in cash together with interest at a commercial rate. Neither party was prepared to accept the others proposals. A dead-lock resulted which subsequently prompted the host nation's decision to nationalize in July of 1971. After nationalizing the government still maintained that compensation should be paid out of future profits. To permit this, the

Constitution of Guyana was amended. Furthermore, Guyana also asserted that compensation need only be 'reasonable', and not also 'prompt and adequate'.(62)

Each of the examples of Third World State practice discussed above illustrate the growing willingness of the capital receiving States to insist upon a compensatory standard that is lower than that which the capital-exporters support. This attitude is reflected in recent United Nation's resolution on the subject of expropriation and compensation payment thereof.

The United Nations Attitude

The United Nations General Assembly Resolution 1803 (xvii) on Permanent Sovereignty over National Resources adopted in 1962(63) provided that a deprived foreign property-holder "shall be paid appropriate compensation, in accordance with rules in force in the State taking such measures in the exercise of it's sovereignty and in accordance with international law". In coming to this resolution Australia and the United States voted with the Third World block in accepting 'appropriate' as the standard.(64) The socialist nations abstained for the obvious reason that they accept expropriation as a sovereign right of each State which when pursued should never be accompanied with compensation payment.

The capital-exporting powers however argued that only the term 'adequate' had been replaced by 'appropriate', but the standard employed in determining the quantum of compensation remained unchanged. This view was based on the contention that 'appropriate compensation' if read in accordance with international law meant a standard no different to 'adequate compensation'. Such a view however was beyond the question of the requirement that it should be in accordance with the expropriator's municipal laws. Here is where the difficulty arises, whether to interpret 'appropriate compensation' in the spirit of the expropriator's domestic laws, or in accordance with rules of international law, or in accordance with both. If in accordance with both, how does a State provide an interpretation where both offer conflicting compensatory determinations?

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62. **Ibid.**

63. Parts of the Resolution are contained in Holder and Breunau **Op. cit** 697-698.

64. This is revealed **id.** 697.

This difficulty was resolved when, by a vote of 120 to 6 (10 absentions) the United Nations General Assembly in December 1974 adopted what today forms the foundation of the New Economic Order, in the form of the Charter of Economic Rights and Duties of States.(65) The Charter provides:

> "Every State has the sovereign and inalienable right to choose its economic system as well as its political, social and cultural systems in accordance with the will of it's a people, without outside interference, coercion or threat in any form whatsoever."(66)

The Charter then proceeds to state that every nation possesses the right to control and regulate foreign investment within it's territory as prescribed by it's municipal laws and in line with its own objectives and priorities.(67) This same right of control and regulation is also specifically expressed to apply to the "activities of transnational corporations".(68) As to the subject of private property being transferred to the ownership of the State, the Charter prescribes that every sovereign nation owns the right:

> "To nationalize, expropriate or transfer ownership of property in which case appropriate compensation should be paid by the State adopting such measures, taking into account it's relevant laws and regulations and all circumstances the State considers pertinent. In any case where the question of compensation gives rise to a controversy, it shall be settled under the domestic law of the nationalizing State and by it's tribunals, unless it is freely and mutually agreed by all States concerned that other peaceful means be sought."(69)

From these provisions one can see the departure from the requirement that 'appropriate compensation' be determined in accordance with both international law and the domestic laws of the expropriator, and it's replacement with a requirement that compensation be determined by the prescriptions of the municipal laws of the expropriating State. Article 2 of the Charter provides for the domestication of the problem of compensation payment "unless it is

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65. The Charter's impact on the Third World and the Capital-exporting powers are brought to light in the commentary by Weston, B.H. 'The Charter of Economic Rights and Duties of States and the Deprivation of Foreign-owned Wealth (1981) 75 Amer. J. of Int. Law 437-475.

66. See article 1 of the U.N. Charter of Economic Rights and Duties of States, 1974.

67. See article 2, paragraph 2 (a) of the Charter.

68. See article 2, paragraph 2 (b) of the Charter.

69. See Article 2, paragraph 2(c) of the Charter.

freely and mutually agreed by all the States concerned that other peaceful means be sought...". This change of attitude obviously reflects the Third World's increasing dissent from the notion of compensation which has for years been articulated by the capital-exporting forces. Whether the capital-exporters like it or not, their investments to a large extent are in the control and regulation of the host States. The host States may expropriate the foreign-held properties and when it comes to the matter of paying compensation, the parties rights are determined by the laws of the host nation. In other words, on the issue of compensation, the foreign investor is at the mercy of the host State.

IV. THE P.N.G. POSITION

Prior to the attainment of self-government, 68% of the then territory's formal economy was in the hands of foreign investors, with Australians dominant in agriculture, commerce and manufacturing. This was a situation which had been encouraged by the passage of the **Industrial Development (Pioneer Industries) Act 1965** and the '**Development Capital Guarantee Declaration**' which gave emphasis to the protection of property and interests of foreign investors.

1973, however, saw a shift in the emphasis of economic development. Since then it has been accepted that while it is necessary to attract foreign investors, overseas investments would be welcome only insofar as they met the needs of the government and the people. To ensure this, investors were required to agree to adhere to certain conditions which were intended at the same time to give the investor a 'fair deal'. Legal instruments in the form of the **National Investment and Development Act**, the **Income Tax Act** were enacted to regulate and control foreign investment. Other legislation on mining, petroleum exploration, land and fishing also illustrate the government's desire to exercise at least some degree of control over investment from outside.**(70)**

Since Independence in 1975 the Constitution has operated as 'superior law'. It is therefore only appropriate that reference be made to the National Constitution to see how it applies to the problem of compensation payment before other legal instruments are examined. The Constitution provides generally that State acquisition of property (or rights and interests therein) is unlawful if not pursued in conformity with an Organic Law or an Act of Parliament and unless the take-over of property is performed for a public reason.**(71)** Generally compensation payment to the dispossessed property-owner must be based on the standard of "just"

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70. These two paragraphs in total are a summary of an article by Ottley, B.L. 'Legal Control of Foreign Investment in Papua New Guinea' (1976) 4 no. 2 M.L.J. 147-183.

71. See Section 53 (1) of the PNG Constitution.

compensation.(72) However, the last subsection of section 53 makes it clear that this rule does not apply "to or in relation to the property of any person who is not a citizen and the power to compulsorily take possession of, or acquire an interest in, or right over, the property of any such person shall be as provided by an Act of Parliament.(73)

Accordingly, the Constitutional yardstick of 'just compensation', only applies to the citizens of the State. Foreign property-holders possess no such right under the Constitution. Non-citizens whose properties have been divested by the State are thus left at the mercy of the relevant Acts of Parliament under which the dispossessions were performed.

PNG Legislation

(i) Land Acquisition Act 1974

The Land Acquisition Act applies to land acquisition by the State. S19 of the Act sets out the methods by which the amount of compensation is to be determined. For land lacking any development, the State is obliged to pay the "prescribed amount". The 'prescribed amount' is an amount determined by the Valuer General who is required to take into account "each class of land in the country; or each class of land in different parts of the country; or the use to which each class of land in the country or in different parts of the country is being put, or a particular parcel or particular parcels of land".(74)

Where land is either fully or partially developed, but such development has not been for profit making the State must pay for "the product of the value of improvements,...and the prescribed factor of the land". Where land has been partially or fully developed for the purpose of generating profit, the determination of compensation can fall into one of four categories.

First, where "land has been in production for not less than five financial years,...at the date of acquisition" compensation is subject to "the product of the average annual net profit received in relation to the land over the five financial years...and the prescribed factor of the land". Second, where the production period exceeds one financial year but less than five, compensation is based on "the product of the average annual net profit that would have been received in relation to the land over a period of five financial years" plus "the prescribed factor for the land". Third, where loss rather than profit is incurred, compensation is based upon the 'prescribed factor' less "an average annual net loss for the period that it has been in production". And fourth,

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72. See Section 53 (2) of the PNG Constitution.

73. See Section 53 (7) of the PNG Constitution.

74. Refer to Section 20 of the Lands Acquisition Act, 1974.

where land has not yet commenced production, or has, but for a period less than one financial year, then compensation is based on "the product of the value of the improvements" plus "the prescribed factor the land."

What compensatory standards do these methods for calculating compensation payment represent? They all accept that compensation payments ought to be based on the market value of the acquired property together with returns at the time of the taking. Accordingly, the Act implements 'adequacy' as the compensatory standard for property acquired under it.

(ii) Bougainville Copper Agreement 1967, and Agreement Amendment Act 1974.

Clause 17(1) of the 1967 Agreement sets out that:

> "The Company shall be at all times entitled and permitted fully to enjoy all the rights, benefits and privileges granted and intended to be granted by or as a result of this Agreement...."

This paragraph is clearly designed to discourage the State from exercising it's sovereign right of expropriation. A qualification is however found in Clause 14 of the **Agreement Amendment Act** which states:

> PROVIDED THAT this paragraph shall be read and construed subject to the laws of Papua New Guinea of general application whether enacted before on or after the Amendment Date which do not discriminate against....the Company...."

By virtue of the 1974 **Agreement amendment Act,** the State might appear to be able to exercise it's right to expropriate pursuant to any relevant law of general application. This possibility however disappears when one reads Clause 17(b) of the **1967 Agreement** which reads:

> "So long as the Company complies with this Agreement..., the Administration shall not...expropriate or permit the... expropriation of any assets (whether moveable or not) of the Company used in connection with any of it's operations under this Agreement, any of the products (whether processed or otherwise) resulting from such operations, the business of the Company, or any shares held or owned by any person in the Company."

This provision demonstrates that the State elected to contract away it's sovereign right of expropriation.

(iii) Ok Tedi Agreement 1976

Clause 122 of the **Ok Tedi Agreement Act** 1976, as amended by Clause 12.1 of the Mining **(Ok Tedi Supplemental Agreement Act** 1980, provides that the special mining lease shall enjoy an initial life

of twentyone years "with a right of renewal for "the same period of twenty-one years "upon the same terms as apply to the initial term". It adds that the lease shall come to an end on the Agreement's termination" but shall not be liable to forfeiture under 5.18 of the **Mining Act (Amalgamated) 1977".**

Before the State may acquire land in relation to the grant of leases and other rights, it is required to consult and negotiate with the Company for the settlement of compensation payment and costs arising out of the taking, "at the cost of the Company".(75) With regard to the issue of acquisition by the State of facilities owned by the Ok Tedi Copper Company, Clause 21.3 (a) of the **1976 Agreement Act** provides explicitly that "the state may require the Company to transfer to it's ownership of any or all of the facilities referred to in Clauses 14 to 20... constructed, established and provided by the Company" with the exception of certain specified facilities. Compensation is to be made after "deductions made from "the original cost of that facility".

If there is a termination of the whole agreement, Clause 35.3 of the **1976 Agreement Act** provides unless the reason for so doing is one contained in clause 34.2(c) "all structures and installations and all other plant equipment and non-moveable assets of the Company in the Mining Area shall "be transferred to the ownership of the State without compensation payment. This also applies where the Company has breached one of its obligations as specified under clause 34 of the Agreement.

There is no clause in the Agreement, with a similar effect as Clause 17(a) and (b) of the **1967 Bougainville Copper Agreement.** In other words there is no restriction on the State's right of expropriation. If the State expropriates the whole operation matters related to the expropriation are required to be argued before either a single arbitrator or three arbitrators as provided for by Clause 38. The applicable law covering any such expropriation (see Clause 39.1 of the Agreement Act 1976) is that of PNG. Hence, if expropriation took place pursuant to a Nationalization Law as in Iran in 1951 or Libya in 1971, compensation would be determined by the terms of the authorizing legislative enactment.

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75. See Clause 12.5 of the Mining **(Ok Tedi Agreement** Act, 1976.

P.N.G.'s Courts

The attitudes of the courts to the question of compensation is important to know but unfortunately, the cases are not plentiful. However, in the case of **Minister for Lands v. Frame**,(76) some light is thrown on the position of a foreign investor whose property has been acquired by virtue of the **Lands Acquistion Act 1974**. Frame, a citizen, owned a coffee estate in the Eastern Highlands and on May 15, 1978 the State expropriated parts of his property pursuant to the Act. The aggrieved owner, by virtue of S.12 of the Act had the right to compensation which the State did not dispute. However, difficulties arose in the determination of the quantum of compensation. The matter finally came before the Supreme Court. Even though it was a case concerning the compensation claim of a citizen, the judges took time to analyse the position of foreigners who may fall subject to the Act.

The three judges attempted to develop a compensatory standard from the methods of calculating compensation payment set out in Section 19 of the Act. According to Pratt J., compensation payment under the Act means "the full money equivalent of the things of which he has been deprived".(77) Pratt, J. thus accepts that section 19 of the Act supports the notion of adequate compensation; that is to say the divested owner should get the full market value of this property of just terms. The other two judges, Greville-Smith and Kapi, JJ. provide a contrary interpretation. They concurred in asserting that a non-citizen whose property is expropriated under the Act should receive compensation payment only as prescribed by the Act. In other words the dispossessed owner should only be entitled to the money value of the land due "to him in accordance with the machinery provided Section 19 of the Act" because "Section 16 of the Act precludes the concept of 'just terms' under Section 53 of the **Constitution** being read into the Act".(78) Presumably, they considered that this standard is one which is less than 'just compensation' as provided under the **Constitution**. Nonetheless, there is little doubt that such a standard would be considered 'adequate' for the purposes of international law.

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76. (1980) PNGLR 433.

77. (1980) PNGLR 433 at P.485. Here one sees Pratt J. citing Dixon J, in **Nelungaloo Property Ltd. v. The Commonwealth and Others** (1974) 75 CLR 495 at P.571.

78. **Id.** 434.

There is no guarantee however that this standard will not be modified. Frame's case illustrates that the Constitutional right to 'just compensation' only applies to citizens, not non-citizens. It is clear therefore that the private foreign investor in PNG is potentially at the mercy of legislative enactments. There are some exceptions, for example, Clause 17 of the 1967 Agreement stops the State from acquiring the Bougainville Copper Company. However, if the Libyan precedent of 1971 is accepted the State may validly legislate to take ownership of the operation. This would likewise apply to the Ok Tedi mining complex.

V. CONCLUSION

Since it has been accepted that expropriation is a sovereign right of all States, the subject of compensation has emerged as the most controversial aspect of that right. The principal capital-exporting nations have to the present continued to support the view that compensation must be paid in conformity with the standard of 'adequacy'. The case most supporters of that view commonly refer to is the **Chorzow Factory** dispute, despite the fact that the case was decided not upon the point of expropriation but rather, upon the breach of treaty obligations between two States, and despite the fact that it was resolved in 1928.

A lot has changed since 1928. Colonies have emerged into States. The Third World sector is now the majority in the family of nations; a majority that used to be in the hands of the capital-exporting powers when the **Chorzow Factory Case** was decided. Aware of their economic needs and aspirations, and the desire to break away from their continued dependency on the principal capital-exporters, and bitter at the realities that prevail in investment relationships, Third World States have not hesitated to expropriate foreign-held property.

Some of these capital-receiving nations have applied compensatory standards they feel to be more just than that of 'adequacy'. Even more striking is the fact that some Third World States have managed to make capital-exporting powers accept these lower standards. This is clearly demonstrated by the **Marcona** dispute of 1975.

In spite of this capital-exporting nations still advance the argument that 'adequacy' remains the standard for compensation payment at international law. What then is international law? According to Lord Atkin in **Chung Chi Cheung v. Rex**,(79) the foundation of international law is the settled practice of States. If international law looks to the practice of all nations, and not the practice of capital-expropriating nations, one may doubt the reasons advanced in support of the Western contention that their standard remains the requirement under rules of international law.

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79. (1939) AC 160, 168.

However, despite the fact that no settled practice of nations exists as yet on the issue of indemnifying a dispossessed foreign property-holder, the current majority view of the issue is reflected in the United Nations' attitude. The U.N. accepts, as provided in the **Charter of Economic Rights and Duties of States**, that a deprived property-owner be paid appropriate compensation in accordance with the host nation's domestic laws. In this context PNG stands with the majority.