An Analysis of Expropriation and Nationalization Risk in China

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I. CHINA IN THE EMERGING GLOBAL ECONOMY

World economic power is shifting to the Far East. Some observers suggest that the next century will be the "Asian era." If the prediction of an "Asian era" connotes world economic dominance by Asian nations, it is undoubtedly overstated. The far more likely scenario, and what observers probably mean, is that the global economy of the twenty-first century will be seamless, with the nations of East Asia becoming increasingly important and perhaps even indispensable participants.

In either case, Asia will not play a full role in the world economy until China approaches the status of a newly industrialized country.

Observers have offered various explanations of China's strategic significance in the Asian, as well as global, economy. One commentator has noted, for example, that while Japan prospers and Taiwan and South Korea continue to develop, these economies are merely "tiny prosperous islands on the edge of a sea of poverty." That sea is China. Although China is no longer as poor as it once was, its still-backward economy poses significant problems for these "tiny prosperous islands." Thus, China will not be left alone. Another theory posits that the world economy will complete its evolution from the U.S.-dominated regime of the first postwar generation to a tripolar system consisting of an economically united Europe, the United States, and the Pacific region. In this tripolar structure, China, with a population of one billion and the highest rate of economic growth in the world, cannot be excluded. An American economist observed the prefigurations of the third theory ten years ago: the likelihood of China's becoming a machine for economic growth that could easily drive the economies of East and Southeast Asia well into the twenty-first century.

China presents a host of economic opportunities. Its rich natural resources and potentially huge market have strong appeal for foreign investors. Direct foreign investment in China has increased greatly in recent years, reaching a

4. Id.
5. See Fred Bergsten, From Cold War to Trade War, ECON. INSIGHTS, July-Aug. 1990, at 1, 2.
cumulative total of approximately $22 billion in 1991. For a number of reasons, however, this critically needed foreign investment remains far below its potential level, despite the economic appeal of China as a site for direct foreign investment.

First, the Chinese market is not right for every company, and it poses challenges for most that enter it. China's inadequate infrastructure, continued administrative red tape, and unstable financial and monetary system make it a difficult place to do business. While important, these internal challenges are beyond the scope of this article.

Second, many prospective investors still consider major investments in China risky. International investment always involves a number of risks. Businesses must make decisions based on a "pragmatic calculation of risk" and predicted return. If non-Chinese enterprises perceive that investing in China carries risks that outweigh the potential rewards, many of them will be deterred from doing so. Risks likely to concern prospective investors in China include those typically associated with foreign exchange transfers, a country's external debt (and the concomitant risk of default, resulting in a far less favorable economic climate in general), the exercise of sovereign immunity in the event of a dispute with a state-owned enterprise, and the nationalization or expropriation of foreign assets by a host government.

Some of the risks often associated with investing in China are more imagined than real. When investors assess risk before choosing any course of action, however, their perception is the reality. Because China holds tremendous investment opportunities, and because many potential foreign investors are wary of investing there, foreign businesspeople must be fully informed about investment risk in China. Toward that end, this Article explores one particular kind of risk: the risk of nationalization or expropriation with insufficient compensation for the taking. Part II briefly examines the basic concept of host-government takings of direct private foreign investments. There are many forms of takings, the two most important being nationalization and expropriation. After we define terms, however, we usually use "expropriation" in the remainder of the article as a convenient generic term for the various forms. Part III explores the unsettled debate over the proper compensation standard for expropriations. This debate concerns not only

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9. Direct investment in China has taken the form of equity and contractual joint ventures, oil exploration by foreign companies, and wholly foreign-owned business enterprises. PHILLIP D. GRUB & JIAN HAI LIN, FOREIGN DIRECT INVESTMENT IN CHINA 77 (1991). Indirect investment, primarily lending and bond purchasing by non-Chinese private and public entities, constitutes China's external debt. Id. at 78.
China, but practically all of the world's sovereign states. To understand how this debate affects contemporary assessments of expropriation risk in China, one must explore its broader theoretical and practical context.

Part IV offers a detailed analysis of expropriation risk in China, focusing both on the risk of expropriatory events occurring and the question of compensation if such events take place. The analysis includes a study of relevant Chinese scholarly writings, explicit and implicit expressions of government policy, pertinent provisions of the Chinese Constitution and Chinese statutes, and actual Chinese practice.

The thesis of this Article is that a thorough analysis of expropriation risk (along with other risks not discussed herein) is essential to making a fully informed decision about whether to invest in China and, if so, to what extent. Based upon this analysis, we conclude that, in light of the remaining ambiguity about China's intentions, expropriation-related risks remain meaningful, even if not great. Nevertheless, the assessments of American investors, based as they are on political rhetoric over tensions between West and East and between developed and developing nations, overestimate these risks. The meaningful risks that do remain should not forestall foreign investment, given the combination of economic imperatives in China, recent Chinese practices, and the enormous opportunities for prospective investors.

II. NATIONALIZATION, EXPROPRIATION, AND OTHER HOST-GOVERNMENT TAKINGS OF FOREIGN ASSETS

Nationalization, expropriation, and other host-government takings are among the most frequently cited examples of political risk associated with foreign investment. Potential foreign investors often treat the presence of this class of risk as a key factor in decisions not to invest. This is true regardless of tax breaks and other incentives the host government may offer, because, in the end, investment incentives matter little in the face of a significant expropriation risk.13

The controversy surrounding nationalization, expropriation, and the standard for compensation is a longstanding one. Although massive waves of nationalization and expropriation took place after World War II, there have been even more takings-related disputes in the last two decades.14 In recent years, nationalization and expropriation activity of various types has been common in Africa, Asia, Western Europe, and other locales.15

Many terms are used to describe the various circumstances in which a host government appropriates foreign-owned property. The most important are expropriation and nationalization.\textsuperscript{16} International business practitioners, business journals, and the general news media have used the term "expropriation" to describe a range of host government actions, from "the sudden enforcement of previously unenforced foreign controls to outright confiscation and physical takeover."\textsuperscript{17} The classical definition of expropriation is simply the taking of an isolated item of foreign-owned property. Some commentators distinguish between individual expropriation and general expropriation.\textsuperscript{18} In individual expropriation, the seizing government expressly mentions both the person and the property affected by the dispossession. In the case of general expropriation, the seizing government does not direct the action against the specific private property of a particular individual. General expropriation may either be connected with changes in the economic or social structure in a

\textsuperscript{16} Other forms of host-government takings of foreign assets include "creeping expropriation," "requisition," and "confiscation."

Creeping expropriation has been defined as "any act, or series of acts, for which the state is responsible, which are illegal under domestic or international law, and which have a substantial adverse effect on either the enterprise or the investor's rights under the enterprise." Robert B. Shanks, Insuring Investment and Loans Against Currency Inconvertibility, Expropriation, and Political Violence, 9 Hastings Int'l \\& Comp. L. Rev. 417, 425 (1986). In its standard contract, the Overseas Private Investment Corporation provides that a covered expropriatory action includes any action that (1) is authorized by the government of the project country, and (2) prevents the investor from (a) receiving payment when due, (b) effectively exercising its fundamental rights with a foreign enterprise, (c) disposing of securities or any rights accruing therefrom, (d) exercising effective control over the use and disposition of a substantial portion of its property, (e) constructing or operating a project, or (f) repatriating investment earnings or capital. De Lupis, supra note 13, at 148.

Another examples of creeping expropriation include the state's exercising monopoly power over a sector of the economy in a way that deprives the foreign investor of anticipated economic freedom in a related sector, subjecting necessary economic activities to onerous licensing requirements, giving preferential treatment to citizens over noncitizens, and applying taxation and regulatory measures to a foreign enterprise so as to make the operation of the enterprise ultimately fruitless. K.C. Kotecha, Comparative Analysis of Nationalization Laws: Objectives and Techniques, 8 Comp. \\& Int'l L.J. S. Afr. 87, 92-98 (1975).

Another form of host-government taking is "requisition," a state's temporary taking of private property, usually under exigent circumstances. Requisition is usually a war-time measure, and may or may not be compensated. Subhash C. Jain, Nationalization of Foreign Property — A Study in North-South Dialogue 30 (1983). Requisition differs from traditional expropriation not only in its motive and surrounding circumstances, but also in the fact that payment, if any, is commonly made after the seizure of the property, with the state using the urgency of its need to justify ex post facto payment. Id. at 30-31 (citing Ben A. Worton, Expropriation in Public International Law 36-37 (1959)).

"Confiscation" denotes any taking without compensation. In its legitimate punitive sense, the term frequently describes actions such as government seizure of criminals' property, illegally transported goods (such as narcotics or pornography), or property detrimental to national security. When the motive is more political than penal, it may describe the uncompensated taking of property from a class of persons because of their nationality. See Michael Bogdan, Expropriation in Private International Law 12 (1975). Thus, the absence of compensation and a punitive motive, whether legitimate or illegitimate, are the hallmarks of a confiscation. See also Hans Raj, Protection of Foreign Investment: Property and Nationalization in India 22-23 (1989) (arguing that punitive nature of taking is even more important than absence of compensation in characterizing taking as confiscation).

There are many other kinds of takings, some involving mixed forms and motives. See Bogdan, supra, at 12.


18. See, e.g., Samy Friedman, Expropriation in International Law 5-6 (1953).
particular country or may be aimed at the exclusion of private capital from a particular sector of the national economy. In many instances, the term general expropriation is essentially synonymous with "nationalization."

When properly used, the term "nationalization" refers to a state's undertaking a number of individual expropriations with the common aim of partially or totally restructuring the country's economy. The government takes property not because it belongs to certain owners, but because it is of a certain type. Although nationalization and individual expropriation are not precisely equivalent, they both involve the exercise of sovereign authority by a state over property within its borders for the purpose of accomplishing a compulsory transfer of property rights from private to public ownership.

For private international investors, the only significant differences between expropriation and nationalization are the implications for compensation and for the future of other investments in the host country. The key to evaluating the future of other investments is to assess the motivation of the expropriating nation: "The prototype of a nationalization is the taking of an entire industry or a natural resource as part of a plan to restructure the nation's economic system. In this instance, the values underlying sovereign rights theories are most strongly implicated, and full compensation is typically not required." In contrast, if a government expropriates an investment, it singles out the foreign investor as the target of governmental action that is not part of a national public plan; the expropriation can be viewed as discriminatory. In this case, the argument for full compensation is stronger.

From the perspective of a private international investor trying to assess risk by predicting the future behavior of a host government, news of an individual expropriation consequently suggests a lower degree of risk than does news of a nationalization in one part of the country's economy. Such an investor is likely to be less interested in the stronger argument for full compensation in the case of an individual expropriation than in the signal about future trends that a widespread nationalization conveys.

19. Id. at 6.
20. See TRUITT, supra note 17, at 5 ("An expropriation may be an isolated and even arbitrary act of government, but a nationalization usually signifies 'pursuance of some national political programme intended to create out of existing enterprises, or to strengthen, a nationally controlled industry.'") (citing WORTLEY, supra note 16, at 120-21).
22. TRUITT, supra note 17, at 6.
24. Id.
25. See TRUITT, supra note 17, at 6.
III. THE COMPENSATION STANDARD: FROM THE HULL RULE TO APPROPRIATE COMPENSATION AND PERHAPS BACK AGAIN

In assessing expropriation risk, a prospective foreign investor is concerned not only with the probability of government actions negatively affecting the investment's value to the investor, but also with the likelihood of receiving compensation that approximates the actual value of the investor's loss. Once an alleged expropriatory action has occurred, two issues are usually the most significant for the foreign investor. First is whether the relevant conduct constitutes an expropriation for which the state is liable and, if so, the date on which the taking occurred. Second is the extent to which the investor should be compensated. Because there is less fundamental theoretical disagreement about the first issue than about the second, this Article does not explore the general international law concepts relating to the first. It does, however, examine the second issue from a theoretical perspective, because that issue continues to engender uncertainty throughout the world. Furthermore, an explication of the general theoretical debate about compensation standards is necessary to understand fully China's attitude toward the compensation question. An adequate assessment of this complex aspect of Chinese investment risk demands a corresponding sensitivity to the nation's historical, recently evolving, and current policies. Consequently, when the Article moves its focus specifically to the outlook for foreign investors in today's China, it discusses the evidence as it relates both to the risk of expropriatory actions actually occurring there, and to the Chinese view of the compensation issue.

Few subjects of international law have generated more controversy than the standard for payment of compensation when governments expropriate foreign-owned property. Government officials, investors, practitioners, and scholars have long debated the proper standard — specifically, whether the expropriating state is obligated to pay "full" or merely "appropriate" compensation. Developed and developing countries have favored different approaches. Some developed countries, especially the United States, have long viewed a standard of "prompt, adequate, and effective" compensation as the "traditional" rule of general international law. U.S. Secretary of State Cordell Hull first articulated the rule in his 1938 notes to the Mexican government.

27. Id. at 658.
demanding compensation for expropriated lands owned by American nationals. The United States has since repeatedly asserted the Hull rule in formal government documents, statements by government officials, commercial treaties, and notes to other countries. Moreover, in 1964 and 1965, Congress reaffirmed the Hull rule as the American view of customary international law in the Hickenlooper Amendments to the Foreign Assistance Act. American courts, however, remain somewhat less convinced that the Hull rule actually represents customary international law.

Although one may explicate the traditional Hull rule in several ways, a relatively succinct statement may take the following form. "Prompt" means that the government must either pay compensation from the time of taking or make a definitive commitment at or before the taking to determine, by an expressed future date, the amount of compensation with interest at reasonable rates. "Effective" essentially translates to "readily convertible and repatriable." Payment with nonconvertible currency or relatively illiquid assets, such as bonds not tradable on an established market, is not effective compensation, nor is payment accompanied by significant restrictions on repatriation. "Adequate" generally has been interpreted as "full." In the case of an operating enterprise with reasonable prospects of continuing as such, "full" compensation usually means the recovery of the going-concern value of the business.

33. E.g., Lofus E. Becker, Just Compensation in Expropriation Cases: Decline and Partial Recovery, 1959 Am. Soc'y Int'l. L. Proc. 336, 341. Mr. Becker was Legal Adviser to the U.S. Department of State.
35. E.g., U.S. Informs Cuba of Views on Agrarian Reform Law, 40 Dep't St. Bull. 958 (1959); U.S. Protests Cuban Property Seizures, 42 Dep't St. Bull. 158 (1960); U.S. Protests Cuban Seizures of Property, 43 Dep't St. Bull. 316 (1960); U.S. Calls Attention to Cuban Inconsistencies on Sugar Trade, 43 Dep't St. Bull. 360 (1960).
37. For example, in Banco Nacional de Cuba v. Chase Manhattan Bank, 658 F.2d 875 (2d Cir. 1981), the United States Court of Appeals for the Second Circuit recognized the "appropriate compensation" standard, not the Hull rule, as customary international law, although the court noted that "appropriate" does not always mean "less than full." See infra text accompanying notes 81 to 87.
38. Clagett, Present State, supra note 14, at 12-3. Going-concern value, a fundamental concept of finance and accounting, is commonly
Satisfying the demands of the Hull rule has proved to be beyond the means of many developing countries, and, consequently, many of them have continued to reject the rule. They have offered various justifications for paying less than full compensation. For example, they have claimed that they may deduct "excess" profits from the compensation, with excessiveness sometimes determined by objective standards such as whether the original investment has been essentially recouped, and sometimes determined by the whim of the host government. Developing countries have also claimed that the taking is a form of recompense for past colonial exploitation by the investor, and that no compensation is necessary. Where expropriation is of a punitive nature, they have argued that no compensation need be paid, with the rationale for punitive action ranging from alleged colonial exploitation to other actions of the foreign investor deemed culpable by the host government, such as payment of low wages to native workers. In addition, developing countries have suggested that an ad hoc decision of the host government, which might weigh such factors as its ability to pay, should set the level of compensation.

The commonly proposed alternative to the Hull rule is the standard of "appropriate compensation," which, unsurprisingly, has received consistent support from the practices of developing countries. The principle also has received support, however, from U.N. resolutions and other documents, three important international arbitral decisions, and, somewhat surprisingly, understood as including the reasonable market value of the business as a viable going concern with the anticipation of future profits. If an active market exists in the locale for the particular type of business as a going concern, the market price of the company's shares or evidence of prices paid for sales of comparable businesses may suffice to determine going-concern value. 

Brice M. Clagett & Daniel B. Poneman, The Treatment of Economic Injury to Aliens in the Revised Restatement of Foreign Relations Law, 22 INT'L LAW. 35, 64 (1988). In many cases, however, there is insufficient evidence of this type to value the business as a whole. In such instances, the appraiser must ascertain the individual market values of tangible and intangible assets, as well as the discounted present value of anticipated future profits. See, e.g., Banco Nacional de Cuba v. Chase Manhattan Bank, 638 F.2d at 892; see also Clagett & Poneman, supra, at 64-65 ("The most commonly used method for measuring the present value of anticipated future profits is the "discounted cash-flow" method.").


40. When the government of Chile expropriated a foreign firm's shares in the national copper industry, for example, the power to determine the amount deducted was within the sole competence of the Chilean president. Id. at 124.


42. Sornarajah, supra note 39, at 127 (citing RICHARD D. ROBINSON, NATIONAL CONTROL OF FOREIGN BUSINESS ENTRY (1976)).


45. Kuwait v. American Independent Oil Co. (AMINOIL), 21 L.L.M. 976, 1032-34 (Reuter, Fitzmaurice & Sultan, Arbs., 1982); Libyan American Oil Co. (LIAMCO) v. Libyan Arab Republic, 20 L.L.M. 1 (Mahmassani, Arbs., 1977); Texas Overseas Petroleum Co. (TOPCO) v. Libyan Arab Republic,
the U.S. Court of Appeals for the Second Circuit.\textsuperscript{46} None of these practices, documents, or decisions describe the "prompt, adequate, and effective" requirement of the Hull rule as a customary principle of international law or as an otherwise authoritative standard.\textsuperscript{47} Although the term "appropriate compensation" is defined in different ways in different contexts, it has been consistently interpreted as a less-than-market-value standard that usually takes into account the host nation's ability to pay.\textsuperscript{48} In its various forms, the appropriate compensation standard arguably has become a majority rule in expropriation cases since World War II by means of the continual explicit and implicit rejection of the Hull rule in favor of other theories.\textsuperscript{49} We now examine some of the highlights of this trend. We close the discussion with evidence that the debate is far from over and that the Hull rule actually may be regaining some of its lost vitality.

**A. U.N. Documents and Their Interpretation**

A series of documents adopted by the United Nations has played an important role in the evolution of the appropriate compensation standard. In 1962, the U.N. General Assembly adopted Resolution 1803, which concerned sovereign control over natural resources. Article 4 of the resolution specified that the remedy for expropriation of an alien's property is payment of appropriate compensation in accordance with the rules of the expropriating state and in compliance with international law.\textsuperscript{50} As is often the case with legislative "solutions" to controversial political or diplomatic issues, the difficult questions associated with specific application were left unanswered. In this case, the General Assembly left the word "appropriate" undefined.

Developed countries naturally supposed that the term "appropriate compensation" indicated the Hull rule.\textsuperscript{51} For instance, Adlai Stevenson, American Ambassador to the United Nations, stated that "appropriate compensation referred to in the section meant prompt, adequate and effective compensation."\textsuperscript{52} It has been argued that the lack of opposition to Stevenson's letter was written in opposition to the Soviet Union's proposed amendment to Resolution 1803, which would have provided for compensation to be paid only according to the host nation's law. Letter from Ambassador Adlai Stevenson (Dec. 21, 1962), \textit{reprinted in}
son's statement, the United Nation's rejection of a Soviet-proposed amend-
ment that assessed compensation in accordance with only national laws, and
an explicit acceptance in Article 4 of international standards, indicate that the
"traditional" norm of prompt, adequate, and effective compensation remains
inviolate.53

Scholars and officials in developing countries have demonstrated different
understandings of Article 4 of Resolution 1803. Chinese scholar Weicheng
Wang asserts that through express recognition in U.N. documents such as
Resolution 1803 and consistent rejection of the prompt, adequate, and
effective standard in actual practice, the new "appropriate compensation"
principle became the accepted standard.54 Subrata Roy Chowdhury, Senior
Advocate of the Supreme Court of India, observes that developed nations are
probably incorrect to assume that the "appropriate compensation" principle in
Resolution 1803 mirrors the Hull rule. After examining the origins of the
principle and its relevance to equity, unjust enrichment, and good faith, he
concludes that something akin to the developing nations' notion of appropriate
compensation has been a customary rule of international law at least since the
adoption of Resolution 1803 in 1962.55

Several later U.N. resolutions have attempted to resolve the ambiguity of
Resolution 1803. Resolution 3171, adopted in 1974, provides that "each State
is entitled to determine the amount of possible compensation and the mode of
payment, and that any disputes which might arise should be settled in
accordance with the national legislation of each state carrying out such
measures."56 In the same year, the U.N. Declaration on the New Interna-
tional Economic Order (NIEO) asserted that host countries should have the
power to determine the amount of compensation.57 The resolutions of several
agencies within the United Nations reveal similar trends. For instance, Article
2 of Resolution 88 of the U.N. Commission for Trade and Development states
that "it is for each state to fix the amount of compensation."58 Furthermore,
the Charter of Economic Rights and Duties of States, adopted in 1974 as
General Assembly Resolution 3281, requires that "appropriate compensation

Contemporary Practice of the United States Relating to International Law, 57 Am. J. Int'l L. 403, 406-07
(1963).


55. See Chowdhury, supra note 51, at 59, 71.

56. Resolution on Permanent Sovereignty Over Natural Resources, G.A. Res. 3171, U.N. GAOR,

that political and economic power should be shifted from developed to developing nations. Jonathan I.
countries have not, of course, embraced this view. They have, however, recognized the validity of NIEO's
primary procedural point: developing countries, usually acting as a group, have the right to negotiate with
developed nations on issues of power and wealth shifting. Id.

should be paid . . . taking into account the relevant laws and regulations and all the circumstances that the state considers pertinent.59 The Charter's language appears to make payment of any compensation optional, while Resolution 1803 requires "appropriate" compensation as an element of a legal expropriation.60

The U.N. General Assembly resolutions, and, to a lesser extent, the resolutions of U.N. agencies, have generated significant controversy. Some commentators from developed countries claim that U.N. resolutions are recommendations rather than lawmaking instruments, and are therefore not legally binding.61 According to the most extreme version of this argument, the resolutions of the early 1970s pointing toward recognition of an appropriate compensation standard do not even furnish evidence of a newly emerging customary rule.62 Academic commentators and government officials from countries with relatively underdeveloped economies, however, normally take the view that U.N. General Assembly resolutions can create new rules of international law.63

As Ian Brownlie, a noted British international law scholar, has written:

In general these resolutions are not binding on member states, but, when they are concerned with general norms of international law, then acceptance by a majority vote constitutes evidence of the opinions of governments in the widest forum for the expression of such opinions. Even when they are framed as general principles, resolutions of this kind provide a basis for the progressive development of the law and the speedy consolidation of customary rules.64

After listing a number of important "lawmaking" resolutions,65 he concludes: "Literature in English all too often fails to indicate the significance of such instruments. In some cases a resolution may have direct legal effect as an authoritative interpretation and application of the principles of the Charter."66

64. IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 14 (3d ed. 1979).
66. BROWNLIE, supra note 64, at 15.
A noted Chinese scholar relying on Brownlie's analysis has asserted that U.N. General Assembly resolutions are sufficient to show that the appropriate compensation principle is a generally accepted rule of international law.\textsuperscript{67} On balance, we believe that, because the United Nations is not a lawmaking body and has no real power to enforce law, U.N. resolutions cannot be viewed as establishing binding legal principles. When very large majorities of the world's sovereign states agree to them, however, they carry substantial moral authority, so much so that they ought to be treated as powerful evidence of customary international principles. Therefore, a flexible compensation standard, whether labeled "appropriate" or something else, should be treated as a rule of customary international law. If so, the expropriation risk faced by prospective investors in China is theoretically greater than it would be if the Hull rule represented customary international law. Indeed, the Hull rule is seldom controlling in actual disputes. Given the questionable status of the Hull rule, trends in claims settlement are likely to be more important to investors assessing investment risk than anyone's view of an international principle's label or content.

B. Decisional Authority

Decisions in several important adjudications between 1977 and 1982 provide support for the argument that a flexible appropriate compensation standard has emerged as customary international law. The first was the 1977 arbitration award in \textit{Texas Overseas Petroleum Company (TOPCO) v. Libyan Arab Republic},\textsuperscript{68} one of a series of disputes arising from Colonel Muammar el-Qadaffi's nationalization of the Libyan oil industry in the mid-1970s. The President of the International Court of Justice appointed Rene-Jean Dupuy, Secretary General of the Hague Academy of International Law and Professor of Law at the University of Nice, as the Arbitrator.\textsuperscript{69} In his decision, Dupuy stated that because a majority of member states supported Resolution 1803's mandate of appropriate compensation, the Resolution expressed an "opinion juris communis" (common legal opinion), and thus reflected "the state of customary law existing in the field."\textsuperscript{70} Oscar Schachter has emphasized that Dupuy did not mention that the United States, when voting in favor of Resolution 1803, expressly interpreted the appropriate compensation provision as meaning prompt, adequate, and effective compensation.\textsuperscript{71} Although this interpretation was quite controversial, the United States withdrew a proposal to include this language in the resolution, supposedly because of its "confi-

\textsuperscript{67} See Wang, Appropriate Compensation, supra note 43, at 13.
\textsuperscript{68} 17 I.L.M. 1, 3 (Dupuy, Arb., 1977).
\textsuperscript{69} \textit{Id}. at 2.
\textsuperscript{70} \textit{Id}. at 30.
\textsuperscript{71} Schachter, supra note 28, at 127-28.
dence" that the appropriate compensation provision would be so interpreted.72 Schachter concludes that Dupuy's silence on the U.S. position in the face of strident controversy, and the overwhelming vote for the resolution without any qualification of the term "appropriate compensation," precludes one from interpreting Dupuy's opinion as incorporating the U.S. position in his recognition of Resolution 1803 as customary international law.73

The 1977 arbitration award in Libyan American Oil Co. (LIAMCO) v. Libyan Arab Republic74 arose in the same context as TOPCO. Like contracts underlying other oil concessions expropriated by Libya, the LIAMCO contract included a choice-of-law provision specifying that Libyan law was to be applied in the event of a dispute to the extent that it was consistent with principles of international law. Where Libyan law and international law conflicted, "general principles of law, including such of those principles as may have been applied by international tribunals," prevail. The arbitrator held that Libyan law required payment of full damages, including lost asset values and discounted future profits, for Libya's breach of the concession agreement.75 He found that under both Libyan and international law the claimant was entitled to the market value of its tangible assets, which he calculated to be $14 million. With respect to the loss of intangible property rights and lost profits, however, the arbitrator concluded that international law was much less clear. International arbitral decisions predating World War II called for full compensation, but were too dated to be relied on as precedent;76 post-World War II lump sum settlements did not meet a full compensation standard.77 The arbitrator thus concluded that, although the classical formula of prompt, adequate (full), and effective compensation continued as a "maximum and a practical guide," it was not the only compensation standard under international

72. Id.
73. Id. Although Dupuy recognized Resolution 1803 as customary international law, he ultimately did not have to apply the Resolution's appropriate compensation standard to the TOPCO case. The concession agreement between TOPCO and Libya included a choice-of-law clause calling for application of both international law and Libyan law, with international law to prevail in the event of conflict. Dupuy found that Libya had breached its oil concession contract to retaliate against the United States and thus violated both international and Libyan law. Because the expropriation lacked a legitimate purpose, the preferred remedy was not compensatory damages but restitution in kind — return of the concession. This remedy, of course, was unenforceable and impracticable, and the case was ultimately settled for what was almost certainly an inadequate amount of compensation ($152 million of crude oil). Because Dupuy did not have to reach the issue of what amounted to adequate compensation, his statements about Resolution 1803 and appropriate compensation were technically dicta; still, expropriation questions are so rarely adjudicated in either judicial or arbitral tribunals that any statement by a respected tribunal is significant. See Robert B. von Mehren & P. Nicholas Kourides, International Arbitrations Between States and Foreign Private Parties: The Libyan Nationalization Cases, 75 AM. J. INT'L L. 476, 539-46 (1981) (discussing principle of restitutio in integrum applied in arbitration).
75. Id. at 54-56, 68.
76. Id. at 70.
77. Id. at 71-72. Lump sum settlements are those entered into by the expropriating government and the government of which the claimant is a citizen, the latter government acting as a representative of the claimant and perhaps other similarly situated citizens.
Because Libyan and international law conflicted on the question of compensation for intangibles and lost profits, the final portion of the choice-of-law clause governed, and thus required the arbitrator to apply "general principles of law." Without any real basis for interpreting the phrase, the arbitrator found that such "general principles" authorized him to award "equitable compensation." His award ultimately included an amount for lost profits of $66 million (far short of LIAMCO's lost-profits claim of $186 million), bringing the total award to $80 million. Whether the award restored the full value of the company's tangible assets or even came close to compensating for lost profits is unclear.

Banco Nacional de Cuba v. Chase Manhattan Bank, arose out of Cuba's expropriation of property owned by American companies in the wake of the Castro-led Communist revolution in the late 1950s. The new Cuban government expropriated four Chase Manhattan branches in 1960. At the time, Chase had held substantial collateral on a loan that it had made to Banco Nacional. Chase sold the collateral for an amount that exceeded the unpaid loan balance by $7.2 million. It refused to surrender these excess proceeds as well as over $2.5 million in deposits belonging to Banco Nacional. Banco Nacional sued Chase in U.S. federal court for $9.8 million. Chase did not dispute this amount, but counterclaimed for the value of its expropriated Cuban branches.

Early in its analysis the U.S. Court of Appeals for the Second Circuit stated, "We begin with the recognition that our task in determining the standard of compensation with respect to Chase's expropriation claims is to apply principles of international, not merely local, law." After reviewing much of the literature on the subject, the court concluded:

It may well be the consensus of nations that full compensation need not be paid "in all circumstances" ... and that requiring an expropriating state to pay "appropriate compensation" — even considering the lack of precise definition of that term — would come closest to reflecting what international law requires. But the adoption of an "appropriate compensation" requirement would not exclude the possibility that in some cases full compensation would be appropriate.

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78. Id. at 86.
79. Id. at 76.
81. 658 F.2d 875, 877 (2d Cir. 1981).
82. Id. at 887-88. Prior to reaching the compensation issue, the court had concluded that the Cuban-owned bank was not protected from Chase's counterclaim by the act of state doctrine, for several reasons. First, the government seeking sovereign immunity for its actions had initiated the suit, and the private claimant was merely seeking an offset rather than affirmative relief. Second, the U.S. executive branch (acting through the State Department) had advised the court that the act of state doctrine should not be applied. Third, there was no evidence that the court's adjudication of Chase's claim would interfere with delicate foreign relations. Id. at 884.
83. Id. at 892 (footnotes and citation omitted). The court explicitly rejected Cuba's contention that
Chase had sought $8.6 million in compensation for the full going-concern value of its four expropriated branches, including lost future profits. The district court had placed a going-concern value of $6.9 million on the branches. The court of appeals held, however, that Chase was entitled only to the value of its expropriated tangible assets, and reduced the compensable value of the branches to $5.5 million. The court reasoned that, given the nature of the Cuban economy, the Chase branches in Cuba had no reasonable expectation of future profits and thus no going-concern value. The court of appeals thus subtracted from the district court's calculation the discounted present value of future profits from the branches. While recognizing the appropriate compensation standard as a principle of customary international law, the court reiterated that appropriate compensation and full compensation sometimes overlap. In fact, the court viewed its valuation of $5.5 million as constituting full compensation under the particular economic circumstances of Cuba at that time.

The fourth decision arguably supporting a more flexible adequate compensation standard was the 1982 arbitration award in Kuwait v. American Independent Oil Co. (AMINOIL). As part of a plan of progressive nationalization of its oil industry, in 1977 the government of Kuwait expropriated the oil exploration and production assets of AMINOIL, which had operated in that country under an oil concession agreement since 1948. The concession was to last for sixty years, after which AMINOIL's assets in Kuwait would devolve upon the government without compensation. Kuwait's expropriation of AMINOIL's assets, however, took place thirty-one years before the agreed termination date of the concession. As compensation for the taking, AMINOIL demanded the full going-concern value of its property — that is, the market value of its assets and the present value of anticipated future profits. Kuwait contended that, to the contrary, it should pay only the net book value of AMINOIL's tangible assets. By 1979 the parties had not negotiated a settlement and AMINOIL instituted arbitration pursuant to a more detailed agreement executed by both parties in that year. The arbitration tribunal included two of the most respected Western European jurists, Professor Paul

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85. 658 F.2d at 894.
86. Id. at 893-94.
87. Id.
88. 21 I.L.M. 976 (Reuter, Fitzmaurice & Sultan, Arbs., 1982).
89. See Derman, supra note 30, at 135.
90. 21 I.L.M. at 1031.
Reuter and Sir Gerald Fitzmaurice, as well as Professor Hamed Sultan of Kuwait. The arbitrators found that Kuwait's expropriatory action was a lawful exercise of sovereignty and that the proper remedy was therefore compensation rather than return of the concession. In determining the proper compensation standard, the tribunal relied upon the "appropriate compensation" provision in Article 4 of Resolution 1803, which, it concluded, represented the most general formulation of the compensation standard and "codified positive principles." The arbitrators also emphasized that appropriate compensation was best determined through a contextual, case-by-case approach, rather than an abstract, theoretical approach.

A contextual approach to calculating adequate compensation requires a determination of the "legitimate expectations" of the parties, through examination of all the formal and informal agreements between them and their past dealings with one another. Countries interested in attracting and maintaining an inflow of foreign investment would legitimately expect to compensate adequately for expropriated assets. However, the legitimate expectations of foreign investors are also important. Consequently, the tribunal concluded that an assessment of legitimate expectations could not lead to a standard of compensation that would render foreign investments economically useless — that is, "make nonsense of foreign investment." AMINOIL and Kuwait had never agreed on specific compensation standards in the event of expropriation, yet the tribunal found that both parties legitimately expected that AMINOIL would receive a reasonable rate of return on its investment. Ultimately, the tribunal determined that a reasonable rate of return would include the depreciated replacement cost of AMINOIL's tangible assets plus the present value of expected future profits to the end of the concession term. Although the arbitrators in AMINOIL expressly adopted a flexible "appropriate compensation" standard, they ultimately awarded AMINOIL the equivalent of the full going-concern value of its business. Given the tribunal's explicit recognition of a flexible "appropriate compensation" standard as the international norm, the case should not be interpreted as equating "appropriate" with the Hull rule. Like the Second Circuit in Banco Nacional, the arbitral tribunal in AMINOIL simply held that "appropriate" and "flexible" mean exactly that: under particular circumstances, a flexible attempt to ascertain appropriate compensation may lead to the
conclusion that full compensation is appropriate. Appropriate does not always mean less than full. Under different circumstances, this arbitral tribunal might have awarded less than full compensation.

After discussing the decisions in TOPCO, Banco Nacional, and AMINOIL, Oscar Schachter concludes: "In view of these well-considered opinions, a case can be made for considering that just compensation should now be replaced by ‘appropriate compensation.’" Former President of the International Court of Justice Jiménez de Aréchaga has written that he favors the appropriate compensation standard because "it conveys better [than ‘just’ or ‘adequate’] the complex circumstances which may be present in each case." He argues that the principle of prompt, adequate, and effective compensation does not represent a consensus of nations and therefore cannot be treated as a rule of customary law.100

These arbitral and judicial adjudications are instructive in two ways. First, they support the proposition that today’s standard for determining compensation for expropriated foreign investments is more flexible than the Hull rule. Second, they support the position that a flexible standard, however denominated, may or may not result in less than full compensation for the investor’s loss, depending on the circumstances.

C. Actual Claims-Settlement Practices of Developing Countries

The court in Banco Nacional and the arbitral tribunal in AMINOIL declined to treat the results of past negotiated settlements as creating rules of customary international law. This view is undoubtedly correct from the perspective of international lawmaking, because negotiated settlements depend entirely too much on idiosyncratic and often confounding variables to serve any precedential role. Still, foreign investors should be mindful of the actual settlement practices of expropriating governments. Settlement practices reveal patterns that ultimately may develop into customary rules of international law through treaties, conventions, and agreements. Moreover, regardless of the effect that actual settlement practices have on the development of international law, a prospective foreign investor’s calculation of risk should focus more on what does happen than on what courts, arbitral tribunals, or scholars believe should happen.

In general, developing countries have followed the practice of paying some compensation under various negotiated or unilaterally imposed methods of calculation, instead of compensation that developed nations would view as

98. Schachter, supra note 28, at 128.
In the early 1970s, Zouhair Kronfol examined many of the "lump sum" expropriation settlement agreements made since 1945 and concluded that the claimants clearly had not received prompt, adequate, and effective compensation. Sornarajah points out that developing countries generally prefer to decide each dispute on an ad hoc basis, where the details of compensation depend on the host government's balancing of the equities.

Sornarajah observes that Asian states have uniformly accepted the proposition that they pay some compensation; however, the amount often can be relatively small because of compulsory "indigenization" statutes, which typically require foreign investors to sell their shares of the nationalized enterprise in the local stock market and accept the proceeds of the sale as compensation. Because the shares must be sold within a limited period of time and local capital is often inadequate, foreign investors are not likely to recover the actual value of their business.

The experience of oil companies in India in the late 1970s and early 1980s is illustrative. In a series of legislative enactments, the Indian government nationalized most foreign oil company assets. Although one Indian writer, Raj, claims that the history of nationalization in India demonstrates a pattern of prompt and adequate compensation for appropriated foreign assets, Sornarajah sees it otherwise. Sornarajah points to India's nationalization of Burmah Shell as an example of grossly inadequate compensation for an expropriatory action. Specifically, he observes that India's requirement that Burmah Shell sell its shares in the extremely capital-poor Indian domestic market precluded the company's receipt of adequate compensation.

102. Zouhair A. Kronfol, Protection of Foreign Investment 118-22 (1972). For a definition of lump sum settlements, see supra note 77. Lillich and Weston conducted a similar study of 139 lump sum settlements between World War II and 1975 that revealed a general settlement range of 30%-60% of the plausible amount of claims. Richard B. Lillich & Burns H. Weston, International Claims: Their Settlement by Lump Sum Agreements (1975); see also Richard B. Lillich & Burns H. Weston, Lump Sum Agreements: Their Continuing Contribution to the Law of International Claims, 82 Am. J. Int'l L. 69, 78-80 (1988) (updating their study by examining an additional 29 lump sum settlements through 1987, and finding no significant difference in pattern).
103. Sornarajah, supra note 39, at 131.
104. Id. at 129. In the case of an ongoing business, "actual value" would be full going-concern value. See supra note 38.
107. Sornarajah, supra note 39, at 129.
In another study, after surveying compensation practices in Africa, Leslie Rood concludes that the nations of British Africa paid less for takeovers of foreign industry than the reasonable values owners attached to their assets. Likewise, Ingrid Detter De Lupis cites the Egyptian nationalization of the Suez Canal's corporate owner in 1956 as an example of inadequate compensation. The Egyptian government promised to compensate shareholders only after Egypt had acquired actual possession of all the company's assets, wherever those assets were located. Egypt's action effectively froze British assets valued at approximately $410 million and U.S. assets valued at approximately $50 million. In 1958 the United Arab Republic (a temporary union of Egypt and Syria from 1958 to 1961) relinquished all claims to the corporation's assets outside of Egypt and agreed to pay its foreign shareholders for the present value of future profits. This compensation, along with payment of the net value of the company's external assets, amounted to little more than half of the actual market value of the company's shares.

Similar examples can be found in Latin America. In 1975, Peru nationalized the holdings of the Marcona Mining Company, a Peruvian subsidiary of a U.S. corporation. The U.S. parent company sought compensation of nearly $100 million, an amount that reasonably approximated actual value; however, the Peruvian government provided only an estimated $62–75 million in compensation. Also illustrative is the 1973 Argentinian expropriation of five foreign-owned banks. Chase Manhattan bank characterized the compensation provided by Argentina as "considerably below what we would consider fair value."

D. Continued Vitality of the Traditional Standard

In part because the United States has continued to press for the Hull standard of prompt, adequate, and effective compensation, the formula is "by no means dead." One indication that the Hull standard retains a degree of vitality is the latest version of the Restatement of the Foreign Relations Law of the United States. The previous version specified in its black-letter text that companies should pay "just compensation" for expropriated property, and

109. DE LUPIS, supra note 13, at 103.
110. The United Arab Republic paid 28.3 million British pounds (which was then equivalent to 28.4 billion French francs) to the company's foreign shareholders. The net value of company's external assets was approximately 15.2 billion French francs. Thus, the shareholders received total compensation of approximately 43.6 billion French francs (15.2 billion asset value plus 28.4 billion payment for present value of future profits), which represented just over half of the actual market value of the company's shares (81.7 billion French francs). Id. at 103-04.
114. RESTATEMENT (SECOND) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 185
defined "just" in terms that were the equivalent of prompt, adequate, and effective.115 Early drafts of the latest revision retained the "just compensation" terminology in the black-letter text, but defined the term only in a comment and indicated that this Hull-based definition represented the U.S. view rather than customary international law.116 Facing substantial opposition from the State Department, other concerned U.S. government agencies, and many members of the private American bar, the drafters returned to the language of the earlier Restatement.117 The final revised version defines just compensation as the value of the property taken (fair market value in the absence of exceptional circumstances), and presents the standard as customary international law rather than as just the U.S. position.118 Thus the Restatement (Third) continues to embody the Hull standard without actually using the terms "prompt, adequate, and effective."119 Despite the new Restatement's assertion that this standard represents customary international law, the Restatement is, after all, only an effort to capsulize American law. It is thus not surprising to find that the new Restatement reaffirms the standard long espoused by developed nations, and that its treatment of the issue does not provide especially strong evidence of the Hull rule's resurrection.

A second, more substantive indication that the Hull formulation retains substantial vitality can be found in decisions of the Iran-U.S. Claims Tribunal. Created as part of the "Algiers Accords," under which the U.S. diplomatic hostages in Iran were released, the Tribunal was vested with jurisdiction to decide property-related disputes involving the governments or citizens of the United States and Iran.120 Most of the Tribunal's work has involved hearing expropriation claims by U.S. nationals against the government of Iran.121 The Tribunal's three-member panels ("chambers") have adjudicated at least eight major expropriation cases in the past decade, all of which have been decided by a majority consisting of the American and neutral arbitrators, with the Iranian arbitrator dissenting.122 In the first of these decisions, American

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116. See Robinson, supra note 115, at 176.
117. See Clagett & Poneman, supra note 38, at 36.
118. While acknowledging that the full value formulation "has met strong resistance from developing states" in comment c, the Restatement (Third) purports to codify "[r]esponsibility under general principles of international law." RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES § 712 cmts. a & c (1987). See generally, id. cmts. a-d.
119. See Clagett & Poneman, supra note 38, at 68.
120. The Declaration of the Government of the Democratic and Popular Republic of Algeria Concerning the Settlement of Claims by the Government of the United States of America and the Government of the Islamic Republic of Iran, Jan. 18, 1981, 20 I.L.M. 230, 231. Despite a title indicating that the agreement envisioned resolution only of disputes between the two governments, Article II(1) & (2) make it clear that the tribunal's jurisdiction also includes claims by the nationals of one state against the government of the other state. Id. at 230-31.
121. See Norton, supra note 80, at 483.
122. Id.
International Group, Inc. (AIG) v. Iran, a panel of the Tribunal held that "it is a general principle of public international law that even in a case of lawful nationalization the former owner of the nationalized property is normally entitled to compensation for the value of the property taken," and that the proper measure of that value is "fair market value... at the date of nationalization." The Tribunal's subsequent decisions have essentially followed suit and employed a standard of full going-concern value.

We noted that the Restatement (Third) represents a purely American view of the compensation standard. In a similar vein, the decisions of the Iran-U.S. Claims Tribunal could be vulnerable to a charge of American dominance because they have all favored the American claimant over the dissent of the Iranian arbitrator. We believe, however, that the Tribunal has served as an impartial body applying international norms, and that its decisions constitute more than just another manifestation of the American view. The provisions of the agreement for forming the Tribunal were as unbiased as possible under the circumstances. When the Algiers Accords were negotiated, Iran possessed a considerable amount of bargaining strength because the Carter administration desperately needed to resolve the hostage crisis. Given its leverage, Iran probably would not have agreed to establish a tribunal whose composition or ideological disposition had been manipulated by the United States. Further, the agreement expressly required that the Tribunal apply established principles of commercial and international law, whether or not the

124. Two decisions, however, encountered difficulties with the "exceptional circumstances" exception to the Hull rule and with methods of valuation. See Clagett, Present State, supra note 14, § 12.03[4], at 12-13; Norton, supra note 80, at 482-86.
125. Article III(1) of the treaty provides:
The Tribunal shall consist of nine members or such larger multiple of three as Iran and the United States may agree are necessary to conduct its business expeditiously. Within ninety days after the entry into force of this agreement, each government shall appoint one-third of the members. Within thirty days after their appointment, the members so appointed shall by mutual agreement select the remaining third of the members and appoint one of the remaining third President of the Tribunal. Claims may be decided by the full Tribunal or by a panel of three members of the Tribunal as the President shall determine. Each such panel shall be composed by the President and shall consist of one member appointed by each of the three methods set forth above.
20 I.L.M. at 231. That is, each panel must consist of one member from the group selected by Iran, one from the group selected by the United States, and one from the third group, the latter being neither an Iranian nor American national.
126. During the later stages of the negotiations, Carter lost the 1980 presidential election, but his administration undoubtedly wanted to resolve the crisis before Reagan's inauguration, so that Reagan could not take credit for any aspect of the hostage release. It is ironic that the agreement was signed on Carter's last day in office, and the 52 hostages released on the day of Reagan's inauguration. See, e.g., Terence Smith, Carter is Thwarted in Wish to Welcome 52 as President, N.Y. TIMES, Jan. 20, 1981, at A2. Rumors circulated for years that Reagan had used George Bush as an envoy shortly before the November 1980 election to obtain the Iranians' agreement to delay release of the hostages until after the election. Ultimately, a congressional inquiry concluded that there was no evidence to support these rumors. See Neil A. Lewis, House Inquiry Finds No Evidence of Deal on Hostages in 1980, N.Y. TIMES, Jan. 13, 1993, at A1.
United States favored these principles. The Tribunal’s panels interpreted international law as calling for compensation of the full, going-concern value of an appropriated business. Thus, we can characterize the decisions of the Tribunal as representing unbiased support for the view that a standard in line with the Hull rule remains viable.

A third indication that the Hull formulation retains some significance is that even during the late 1970s and early 1980s, when the four "anti-Hull" adjudications took place, the principles enunciated in these adjudications were not universally followed. To be sure, they were quite important because adjudications dealing with questions of compensation for expropriatory acts are relatively rare. Unlike the four adjudications previously discussed, however, two arbitration decisions in 1979 and 1980 conducted under the auspices of the International Centre for Settlement of Investment Disputes (ICSID) indicated that full compensation is still the generally accepted international norm. Both cases involved claims arising from Congolese expropriation of Italian investments, with no choice-of-law clauses in any of the relevant agreements. In the first, AGIP Co. v. People’s Republic of the Congo, the tribunal applied Congolese and international law to find that the claimant was entitled to full asset value and lost profits. In the second ICSID case, Benvenuti et Bonfant v. People’s Republic of the Congo, the tribunal reasoned in a similar fashion, evidently operating from the premise that the governing standard called for an award of the full going-concern value.

The fourth and arguably strongest evidence of the Hull rule’s viability — and perhaps even its resurgence — is the content of relatively recent investment protection treaties. Today there is a network of more than three hundred bilateral investment treaties between developed and developing nations and a number of multilateral treaties that reveal some developing
nations' partial movement away from the position that they should have the unilateral right to determine the amount of compensation.\textsuperscript{130} Such treaties, often after intense negotiation over the particular language, "typically incorporate some or all of the traditional legal rules concerning expropriation and compensation therefor, and provide for arbitration" or litigation of disputes.\textsuperscript{131} Brice Clagett asserts that these newer investment protection treaties help validate a principle of just compensation that is closer to the Hull rule than what developing nations have been willing to acknowledge.\textsuperscript{132} He observes, "Western European States have taken the lead in initiating and expanding this treaty network."\textsuperscript{133} The United States has lagged substantially behind, however. At the time of Clagett's study just over three years ago, the United States had concluded no BITs with developing nations, although many developed European nations had each concluded BITs with dozens of developing nations.\textsuperscript{134} Only in the past year has the United States' BIT program begun to bear real fruit, with most of the success coming in the last several months. With a few exceptions, these new United States BITs with developing nations have involved several nations in the former Eastern Bloc and the former Soviet Union, as well as a handful of South American nations.\textsuperscript{135}

Clagett theorizes that several factors are responsible for what he views as a recent resurgence of the traditional compensation standard. First, as states develop, they find foreign investment no longer represents unjust exploitation. They are thus less likely to view foreign businesses as fair game for uncompensated seizure. Second, some developing countries have actually become exporters of capital and thus are acquiring a deeper appreciation for property rights. Finally, a growing number of developing countries recognize that foreign investment can in fact be beneficial. As a result, according to

\begin{itemize}
\item \textsuperscript{130} Zhuhua Shi, Guoji Guanli Yu Zhongguo Shiji De Youji Jihe — Ping Zhongwai Hezi Jingying Qie Fa De Xiuding [Organic Combination of International Practice and China's Condition — Comments on the Revised Joint Venture Law], 1991 ZHONGHAN ZHENGFA XUEYUAN XUEBAO [J. MID-S. CHINA POL. & L.C.] 36, 38; see also Clagett, Protection Under the Restatement, supra note 62, at 71-77.

\item \textsuperscript{131} Clagett, Present State, supra note 14, § 12.03(2) at 12-10, 12-11.

\item \textsuperscript{132} See Brice Clagett, Just Compensation in International Law: The Issues Before the Iran—United States Claims Tribunal, in 4 THE VALUATION OF NATIONALIZED PROPERTY IN INTERNATIONAL LAW 31, 74-76 (Richard B. Lillich ed., 1987).

\item \textsuperscript{133} Clagett, Present State, supra note 14, § 12.03(3) at 12-11.

\item \textsuperscript{134} Id.

\item \textsuperscript{135} On November 17, 1993, the Senate approved BITs with Argentina, Armenia, Bulgaria, Ecuador, Moldova, Kyrgyzstan, and Romania. Also in the News, INT’L TR. REP. (BNA) 1989, 1990 (Nov. 24, 1993). On October 21, 1993, the Senate approved a BIT with Kazakhstan. Senate Ratifies U.S.—Kazakh Pact to Encourage, Protect Investments, 10 INT’L TR. REP. (BNA) 1821 (Oct. 27, 1993). The United States has negotiated several other BITs with developing nations, and some of these have gotten as far as the Senate Foreign Relations Committee. For example, in August 1992, the Foreign Relations Committee approved BITs with Russia, the Czech and Slovak Federal Republics, Sri Lanka, Tunisia, and the People’s Republic of the Congo. Senate Foreign Relations Committee Backs Investment Treaties with Russia, C.S.F.R., 9 INT’L TR. REP. (BNA) 1994, 1394-95 (Aug. 12, 1992).
\end{itemize}
Expropriation and Nationalization Risk in China

Clagett, many developing countries have moderated both their rhetoric and their behavior.\textsuperscript{136}

Relevant judicial and arbitral adjudications, U.N. resolutions, actual claims-settlement practices, and investment treaties leave us with no clear, generally accepted international compensation standard for nationalized or expropriated property, much less any specific model for computing the amount of compensation. Nonetheless, the most recent evidence, in the form of bilateral and multilateral investment treaties, seem to indicate that developed and developing nations are moving toward a rough consensus on a standard that generally envisions full compensation, but allows more flexibility in application than the traditional Hull rule.

IV. Expropriation Risk in China: Theory, Policy, Law, and Practice

After having examined the international debate over compensation for expropriated property, we now turn to an analysis of expropriation-related risk in China. Expropriation-related risk gives rise to more uncertainty in investment than many foreign businesses would wish. There are, however, signs that the degree of this uncertainty has diminished in recent times and will continue to do so.

Admittedly, China’s modern history has witnessed substantial expropriation of foreign investment. This history, coupled with the negative international perceptions created by the events in Tiananmen Square in 1989 and ambiguity in China’s official position, have reinforced wariness on the part of some prospective foreign investors.

China’s expropriatory actions have taken several forms, including formal nationalization of entire economic sectors in pursuit of socialist policy, repudiation of its predecessor government’s obligations, and the retaliatory freezing of non-Chinese assets within the country. When the People’s Republic of China was created in 1949, the Communist government nationalized financial institutions, railroads, shipping companies, and other industries, as well as American consular properties.\textsuperscript{137} The new government also refused to honor the ousted government’s financial obligations.\textsuperscript{138} The second large expropriatory action occurred in 1950, when China froze American assets in retaliation for America’s freezing of Chinese assets after China intervened in the Korean War.\textsuperscript{139} Compensation to Americans for

\textsuperscript{136} Clagett, \textit{Present State}, supra note 14, §12.02, at 12-9 to 12-10.


\textsuperscript{138} Id.

their losses was delayed and inadequate. Americans asserted a total of approximately $250 million in claims against the Chinese government. The U.S. Foreign Claims Settlement Commission certified nearly $197 million of these claims as of July 6, 1972, the date for closure of the Commission’s activities relating to China.\textsuperscript{140} The Commission transmitted this certified amount to the Secretary of State for the latter’s conduct of settlement negotiations.\textsuperscript{141} A settlement between the two countries was not reached until 1979.\textsuperscript{142} Under the terms of the claims settlement, China agreed to pay $80.5 million to the U.S. government for distribution to U.S. claimants, and the U.S. agreed to unblock frozen Chinese assets in return.\textsuperscript{143}

Given the history and authoritarian political system of China, one can never completely rule out the possibility that it will carry out expropriatory acts in the future. We may, for example, envision political instabilities or changes in its foreign investment policies, all of which may result in expropriation.\textsuperscript{144} Despite some continuing uncertainty about expropriation-related risks in China, however, this Article suggests that recent changes in the views of Chinese academics, and in governmental policy, law, and practice, point toward a conclusion that these risks have diminished significantly and are likely to continue to do so.\textsuperscript{145}

A. Chinese Academic Theory

The writings of Chinese legal scholars on various subjects are important for at least three reasons. First, because of the practical limits on expression in China, as well as the constraints on scholars’ own formative intellectual development in its education system, these writings generally reflect the current official thinking of China and provide much valuable insight into and elaboration on that thinking. Second, they often shed light on some of the fundamental philosophical differences between the participants in both Western-Eastern and developed-developing nation dialogues. Third, China is still in the midst of a lengthy process of developing a comprehensive legal system to undergird economic development, and Chinese legal scholars will surely play a role in that development.

\textsuperscript{141} Id.
\textsuperscript{142} Agreement Concerning the Settlement of Claims, May 11, 1979, U.S.-P.R.C., 30 U.S.T. 1957.
\textsuperscript{143} Id. art. II.
\textsuperscript{144} Laffman, supra note 137, at 329.
\textsuperscript{145} See Grub & Lin, supra note 9, at 206.
Chinese legal scholars have long debated whether China should enact a law guaranteeing foreign enterprises immunity from expropriation. Scholars have split into two opposing schools of thought. Understanding how the two camps have cast the debate will help shed light on the current and future status of Chinese expropriation legislation.

The debate first arose when the government considered economic legislation for the special economic zones (SEZs) and open coastal cities of China. Both schools of thought agree that in order to attract more foreign investment, which is likely to promote long-term economic growth, legislation concerning foreign enterprises should be explicit about China's attitude toward foreign investment. Only a precise statement of the legal protections available to foreign enterprises will provide prospective foreign investors with certainty and predictability. Chinese scholars disagree, however, about the extent of protection that should be offered to foreign investors.146

The "Traditionalist School" maintains that it is neither necessary nor justified to provide foreign enterprises with an absolute guarantee against nationalization. The "Immunity School" contends that absolute immunity from nationalization for foreign investment in the SEZs and open coastal cities is essential to attracting investment.147 These opposing positions result from different approaches to several issues, including national sovereignty, the distinction between legal doctrine and economic imperatives, and China's true place in the world order.

a. Sovereignty and Self-Restraint

The Traditionalist School maintains that a country, as a sovereign, should be able to nationalize foreign investment within its territories in order to protect its own public interest and uphold national independence. To restrict, transfer, or waive China's power to deal with all relevant matters independently would be "tantamount to tying one's own hands" under circumstances in which any other nation would have the right to take private property for public purposes.148

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146. See Chen An, Should An Immunity From Nationalization For Foreign Investment Be Enacted in China's Economic Law?, in LEGAL ASPECTS OF FOREIGN INVESTMENT IN THE PEOPLE'S REPUBLIC OF CHINA 39, 49 (William Tai ed., 1988). Chen, Dean of the Law School at Xiamen University, is widely recognized within China as an expert on international law generally and, more specifically, on Chinese law on international trade and investment and the question of expropriation and nationalization. He has published widely on these subjects in Chinese- and English-language journals since the late 1970s. Xiamen University lies within an SEZ, and Chen tends to have more progressive views than other Chinese scholars.

147. Id. at 40.

148. Id.
The Immunity School contends that, although a country has the power to handle its internal and external affairs independently, the exercise of sovereignty is never entirely free from constraint. Typically, rights and obligations are reciprocal. All international agreements or treaties concluded on the basis of equality and mutual benefit embody this principle. For example, in 1984 China and the United Kingdom reached an agreement providing for the resumption of Chinese sovereignty over Hong Kong upon expiration of the United Kingdom's lease on July 1, 1997. The Chinese Government agreed, however, that for fifty years thereafter it would not change the current social and economic systems in Hong Kong. This restriction illustrates voluntary restraint in China's exercise of sovereignty. China similarly restricts its sovereignty when it allows foreign capitalists to make limited profits. This self-restraint is designed to help China accelerate the growth of productive forces and modernize its economy — and thereby to achieve greater self-development, economic efficiency, and political independence. Self-restraint, in this case, serves to maintain and strengthen sovereignty. Following this line of reasoning, members of the Immunity School contend that Chinese foreign economic legislation should codify this self-restraint, by assuring that foreign capital will not be expropriated.

b. The Right of Expropriation

The Traditionalist School argues that having the right to expropriate a foreign enterprise does not necessarily translate into exercising this right. It is extremely important, however, for a sovereign nation to possess the right to expropriate so that it has sufficient maneuvering room if circumstances change substantially. The Immunity School, on the other hand, contends that China does not possess an absolute right to expropriate, because Article 18 of the Chinese Constitution provides that Chinese law protects the lawful rights and interests of foreign investors. The right of property ownership is the primary legal right of a foreign investor. Therefore, an absolute immunity provision would require China to relinquish little more sovereignty than it has already relinquished under its own constitution. A legislative expression of immunity would simply provide further evidence of China's determination to protect the lawful property rights of foreign businesses and encourage them to invest actively in China.

150. Id. annex I, § I.
151. Chen, supra note 146, at 42.
152. Id. at 41.
154. See Chen, supra note 146, at 40.
Although the Immunity School attempts to base its argument on China’s constitutional provisions, the debate is a philosophical rather than a constitutional one. The language of Article 18 is too vague and general to form the basis for the sort of parsing to which scholars in the United States and other Western nations are accustomed. Furthermore, China has no counterpart to our Supreme Court capable of setting forth definitive interpretations of ambiguous constitutional language.¹⁵⁵

c. China and the Third World

The Traditionalist School further argues that China, in truth, belongs to the Third World. When dealing with major international issues, China should remain in step with other Third World countries. Developing nations generally consider the power to nationalize foreign enterprises important to achieving economic independence. Most Third World countries currently take the position that the right to expropriate foreign capital enterprises, subject to appropriate compensation, is a central attribute of their sovereignty. A legislative waiver of this right by China would be contrary to the fundamental theoretical perspective and general practice of Third World countries.¹⁵⁶

The Immunity School contends that even though China is a Third World country, it is different in that most Third World countries, despite their political independence, have not yet achieved China’s level of economic independence. Unlike many other developing countries, China is not plagued by remnants of colonialism. Encouraging foreign investment in a controlled and selective manner to expedite modernization of the economy would neither lead to foreign economic domination over China nor adversely affect its people. Thus, China’s position and incentives are sufficiently different from those of most other Third World nations that its policies should not necessarily move in lockstep with those of other nations.¹⁵⁷

2. Academic Debate on Other Issues

In addition to the basic question of whether legislation should protect foreign investment from expropriation, Chinese legal scholars have addressed

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¹⁵⁵. Article 18 states:
The People's Republic of China permits foreign enterprises, other foreign economic organizations and individual foreigners to invest in China and to enter into various forms of economic co-operation with Chinese enterprises and other economic organizations in accordance with the law of the People's Republic of China.

All foreign enterprises and other foreign economic organizations in China, as well as joint ventures with Chinese and foreign investment located in China, shall abide by the law of the People's Republic of China. Their lawful rights and interests are protected by the law of the People's Republic of China.

P.R.C. CONSTITUTION, supra note 153, art. 18.

¹⁵⁶. Chen, supra note 146, at 41.

¹⁵⁷. Id. at 43.
a number of other related expropriation issues. Their views are often strikingly similar to those of their counterparts in the United States and other similarly situated nations. There is general agreement, for example, that under certain circumstances expropriation of alien property is legitimate. According to the Western view of international law, a taking by a sovereign state is legal if it is (1) for a public purpose; (2) not discriminatory; (3) accomplished according to legal procedures, incorporating the basic elements of due process, including the right to advance notice and an opportunity to contest an action on its merits; and (4) compensated in a manner that comports with some formulation of the Hull rule. Chinese scholars, along with the Chinese government, accept the public purpose and nondiscrimination principles, and essentially agree that established legal procedures are necessary when expropriation is proposed. They have, however, a philosophical view of certain issues that is quite different from that of the United States and other developed nations. Nevertheless, the difference, in practical terms, boils down to the question of compensation for expropriated assets.

a. The Nature of Property

Li Haopei observes that the Western theory of expropriation "is obviously based upon the sanctity and inviolability of private property advocated by the bourgeoisie." The Western view is, in short, "This is mine, you took it, now pay me for it." This view has two underlying premises. The first is that one can "own" something, that is, possess an unqualified right of exclusive use of the thing "owned." The second is that one (including the government) cannot take something that another "owns" without a very good reason (public purpose) and without paying the owner compensation. Yao argued that the "bourgeois" notion of private property as sacred is at the root of any challenge to the legitimacy of an expropriatory act or to the compensation offered. Post-1949 China, however, does not recognize private property ownership. People can possess and use land and other property, but they cannot own it. State ownership of property continues today despite China's new policies encouraging various forms of entrepreneurship: what the entrepreneur gains under these new policies is not property ownership but a greater right to benefit personally from more productive uses of the state's property.

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158. See Shaw, supra note 15, at 430.
159. Derman, supra note 30, at 131.
163. The Chinese Constitution was amended in March 1988 to give certain Chinese-owned business enterprises the power to buy and sell the right to use property. John P. Powelson, Property in Chinese Development: Some Historical Comparisons, in Economic Reform in China: Problems and Prospects
These fundamental differences in the philosophical view of property help to explain the continuing difficulty that China and the United States have had in agreeing on compensation standards for expropriation.

b. *A Question of Domestic or International Law?*

Western thought on expropriation springs from conceptions of private property ownership and the individual’s consent to be subject to state action. In contrast, the Chinese view expropriation from the perspective that state sovereignty is part of the natural order and that state consent to international law represents an exception to that sovereignty. Although Chinese scholars agree that territorial sovereignty provides the basis for any right to expropriate, some still disagree about whether expropriation is purely an issue of domestic law or whether it involves questions of international law. If it were only an issue of domestic law, a nation would have the unfettered right to determine unilaterally all issues pertaining to expropriation. On the other hand, if it involved questions of international law, international norms would constrain the host nation. Professor Chou Keng-sheng argues that nationalization is "a sovereign act of a state within its territory and therefore is a question of domestic law and not a question of international law." Professor Li, however, characterizes nationalization as a public international law question. Since Chinese scholars base the right to expropriate foreign property on territorial sovereignty, their disagreement boils down to one about the level of priority given to territorial sovereignty in today’s interdependent world. Chou views territorial sovereignty as trumping international law considerations while Li and Yao argue that expropriation, while based on territorial sovereignty, must still conform to the principles of public international law.

Some Chinese scholars also base the right to expropriate foreign property on their nation’s fundamental right to economic self-determination, free from the influences of foreign capital. Such attitudes stem from the notion that a country that was "exploited and plundered by foreign states" before its independence has the right to regain its "national rights and interests" through

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165. 172 (James A. Dorn & Wang Xi eds., 1990) [hereinafter ECONOMIC REFORM IN CHINA]. However, "the ultimate ownership of land still vests in the government." Id. at 178. But see Chen Weishu, Comment, Reforming China’s Property System, in ECONOMIC REFORM IN CHINA, supra, at 187, 190-91; see also Susan Young, Wealth But Not Security: Attitudes Towards Private Business in the 1980s, in ECONOMIC REFORM AND SOCIAL CHANGE IN CHINA 63, 77 (Andrew Watson ed., 1992)

164. Chou Keng-sheng et al., The Legal Basis for the Nationalization of the Sues Canal Company, in COHEN & CHIU, supra note 139, at 730.

166. See Ferguson, supra note 161, at 19 (comparing views of Chinese scholars).
expropriation. Yao also claims that international law sanctions nationalization in order to free a country from domination by foreign capital.169

The practical effect of these varying philosophical viewpoints on the basic nature of the right to expropriate remains to be seen. The existence of a scholarly dispute means, of course, that the nation’s future leadership will be able to find jurisprudential support regardless of the stance it takes, so long as that stance remains faithful to the fundamental principles on which scholars do agree.

c. The Nondiscrimination Principle

Developed nations have long viewed takings of property that single out foreigners in general, or foreigners of a particular nationality or other grouping, as contrary to international law.170 Chinese writers essentially accept this position by supporting the so called "Calvo doctrine," named after an early Argentinean jurist and statesman. This doctrine posits that in entering a host country, foreign investors agree not to invoke the assistance of their own nation to obtain special treatment.171 This principle emerged from the lessons of nineteenth-century South America, when certain foreign investors used their nations’ diplomatic and even military influence to secure preferred treatment.172

Yao observes that this doctrine is based on the notion that a foreign business constructively consents to be treated in the same manner as a country’s nationals by investing there.173 Thus, foreign investors cannot expect to receive better treatment than nationals.174 Chen emphasizes that this equal treatment principle extends to the subordination of private to public interests in China, whether those private interests are held by Chinese citizens or foreigners.175 Most Chinese writers reject the contrary view — that aliens deserve better treatment than nationals — as "imperialist and colonialist, although some believe that China should grant foreign investors in the SEZs and open coastal cities special treatment."176 On balance, however, the Chinese view of the nondiscrimination principle is essentially the same as the Western view.

171. Id. at 168.
172. HENRY J. STEINER & DETLEV F. VAGTS, TRANSNATIONAL LEGAL PROBLEMS 553 (1986).
173. See Yao, supra note 169, at 133-34.
174. See Li, supra note 160, at 728; Chen, supra note 146, at 50.
175. See Chen, supra note 146, at 50.
176. Yao, supra note 169, at 134. In actual practice, however, the Chinese government’s efforts to attract foreign investors have included some limited preferences for foreign investment over Chinese state-owned enterprises, such as a lower income tax rate. See infra text accompanying notes 232 & 259 to 260.
d. The Compensation Standard

As previously noted, Western authorities, in the United States in particular, often assert that international law requires prompt, adequate, and effective compensation for expropriation. A number of bilateral investment treaties also contain this standard.177 One American commentator has captured the Western position especially well, stating, "Recognition of the obligation to pay compensation can be meaningless if the valuation of nationalized property does not compensate an investor for his book value plus a portion of his legitimately anticipated future profits."178

Chinese legal writers all reject "prompt, adequate, and effective" as the customary international legal standard of compensation for expropriated investments. Professor Chen, for example, maintains that under the compensation principles advocated by the United States, claims were usually excessive and would have abrogated the sovereign right of expropriation if satisfied.179 He further states that developing countries believe they need to compensate expropriations only to the extent that their national laws require. Because of the huge profits already amassed by foreign investors since the beginning of the colonial period and the weak financial position of the host countries, developing countries need flexible compensation standards to maintain their political and economic sovereignty. Chen concludes that the dispute over the compensation standard is really a dispute over the right of poor countries to take over foreign investment when necessary; it is nothing more than an extension of the longstanding rhetorical battle over the existence of the right to expropriate.180

While most Chinese legal scholars know which compensation standard they wish to reject, they disagree over which standard of compensation China should adopt. Some have advocated no compensation at all, an unrealistic position if China wishes to attract any foreign investment. Even the Chinese government has completely abandoned this position.181 Others, like Li, argue that the nationalizing state's only obligation is not to discriminate. If the government would not compensate nationals for a taking, the state has no obligation to compensate foreigners.182 Scholars have rarely expressed such extreme positions in recent years. This development reflects the unrealistic nature of these views in a global economy as well as the changing attitude of China's leadership. Most scholars espouse views consistent with those of other developing nations interested in attracting foreign capital and encouraging freer trade. As one Chinese commentator has suggested, "[A]ppropriate

177. See, e.g., Robinson, supra note 115, at 176, 178.
178. Derman, supra note 30, at 131.
179. Chen, supra note 146, at 45.
180. Id.
181. See infra text accompanying notes 188 & 190 to 192.
182. Li, supra note 160, at 722.
compensation has become a principle and custom of contemporary international law and it is supported by most nations and international legal scholarship. Still, Chinese writers have not fully embraced the U.S. position on the issue of compensation. They are unlikely to do so in the near future, especially if the U.S. formulation continues to be couched in the traditional terms of the Hull rule.

B. China's Expressions of Government Policy

Policy is not made or communicated in China as it is in the West. Although China is attempting to build a structure of policy and law in order to modernize its economy, it does not have a tradition of formality in policymaking or lawmaking. Rather, China has the tradition of an authoritarian state, where communication and formality in policymaking is not the norm. For example, a change in policy is often simply communicated in a speech, with the typewritten text passed out to reporters and published in newspapers or magazines. Thus, policy pronouncements concerning justifiable circumstances for expropriation and the appropriate standard for compensation are typically very informal, even though all of these statements are made by high-ranking officials who have the authority to speak for the government.

1. Justifications for Expropriatory Actions

The Chinese government, after considering whether to grant absolute immunity from expropriation in its SEZs and open coastal cities, has maintained the position that nationalization is a sovereign right that must be retained but never abused. Thus, even in these special areas of the country, Chinese legislation permits nationalization when necessary. As Chen has observed, this approach is not inconsistent with the approach of developed countries, where "private properties have never been absolutely free from expropriation or nationalisation." Looking back two hundred years, for example, Chen points out that although the Declaration of Human Rights resulting from the French Revolution elevated private property ownership to the same level as personal liberties by characterizing property rights as "sacred and inviolable," the same document also recognized the right of the sovereign to take private property for a public purpose upon payment of

183. Yao, supra note 169, at 142; see also Wang, Appropriate Compensation, supra note 43, at 13-18 (arguing that appropriate compensation is both customary international standard and Chinese rule).

184. See, e.g., infra text accompanying note 189. Unfortunately, this informality in policy formation makes many of the original sources inaccessible to those outside China, and sometimes even to scholars within China. Scholars often must rely upon secondary sources to a greater extent than in other nations. See, e.g., sources cited in infra notes 190, 192, 195 & 197.

185. See Chen, supra note 146, at 51.

186. Id.
"equitable" compensation. In the United States and other Western nations, the same principle applies: private property may be taken upon payment of compensation that is labeled and calculated in somewhat different ways in different countries. He notes that Western nations have taken entire residential or industrial sections for the construction of highways, railways, utility plants, military facilities, and other endeavors linked to the public interest, subject to the payment of compensation. It would be strange, indeed, Chen argues, for China to deny itself the power of eminent domain in its SEZs and open coastal cities and then to grant foreign investors property rights more extensive than those they possess in their home countries.

Many foreign scholars and business practitioners have argued that the investment climate in Asia and the Pacific rim will be extremely favorable in the coming decades. Moreover, they view China as leading the way because of its rapidly developing economy, living standards, and increasing demand for consumer goods and technology. Moreover, on several occasions Chinese leaders have publicly assured prospective foreign investors that China’s modern expropriation policy should pose no major concern for them.

Perhaps the most important official government pronouncement regarding expropriation policy was made during the 1982 China Investment Promotion Conference. At the conference, China’s Ministry of Foreign Economic Relations and Trade issued a document that attempted to address forty-four categories of questions posed by foreign investors. The fourth category included questions relating to (a) the existence of meaningful assurances that foreign capital in China would be safe, (b) the circumstances under which expropriation might occur, and (c) the extent of compensation, if any, in the event of expropriation. To these questions the ministry answered:

Under normal circumstances, the Chinese government will not resort to the practice of expropriation of the properties belonging to foreign investors in China. If such expropriation should become necessary as a result of an event of force majeure or for the public interest, China would act by due process of law and would give reasonable compensation.

187. Id.
188. Id. at 50-51. Even if one focuses solely on the exercise of eminent domain in the United States, where one term — "just compensation" — is the constitutional norm, methods of calculation are disparate. The sheer number of legal challenges by dispossessed property owners provides substantial evidence that they often feel inadequately compensated by their own government. See, e.g., JOHN E. NOWAK ET AL., CONSTITUTIONAL LAW § 11.14 (3d ed. 1986).
189. Gu Ming, Investment Environment Seen as Favourable, BEIJING REV., July 16, 1984, at 16, 17 [hereinafter Gu, Investment Environment]. Mr. Gu was Deputy Secretary-General of the State Council at that time. The position of Secretary-General is similar to that of the President’s Chief of Staff in the United States, and is just below the premier and vice premier. A legal expert, Mr. Gu spoke with the full authority of the Chinese government in the Beijing Review.
190. The Conference was organized in Guangzhou by the Ministry of Foreign Economic Relations and Trade in conjunction with the Industrial Development Organization of the United Nations. Chen, supra note 146, at 51.
191. Id. at 47.
Most other nations likewise follow this public purpose requirement for valid nationalizations. Even in the freest of nations, public interests sometimes transcend private interests. Where the two interests directly conflict, a private interest must be subordinated to the public interest. If the private interest is substantially devalued as a consequence of this subordination, the state provides the private owner with reasonable compensation according to established legal standards.

Chinese policy apparently construes the term *force majeure* to describe an event or natural disaster that suddenly requires the subordination of certain private property interests to the public interest. If, for instance, China were to go to war, the government may need to take over enterprises operated by foreign investors in strategic industries such as petroleum refining. Similarly, in the event of a natural disaster, the Chinese government might find it necessary to take over those foreign enterprises whose operations relate closely to emergency relief requirements.

Also at the 1982 conference, which was essentially a vehicle for publicizing the post-Mao open-door policy, the Vice Minister of Foreign Economic Relations and Trade stated that, except in the case of a true emergency (*force majeure*), the government would not even consider expropriatory actions unless foreign investors violated Chinese law or otherwise acted in ways that substantially undermined Chinese national interests or public order. Even if foreign investment were to be expropriated because of *force majeure*, the government would act with due process of law and provide equitable and reasonable compensation.

2. Compensation for Expropriated Investments

Gu Ming, Deputy Secretary-General of the State Council, set forth China's official policy on compensation for expropriatory actions in 1984. According to Gu, China "must abide by" the appropriate compensation standard because a 1974 U.N. resolution, a source of customary international law, incorporates that standard. Elaborating on the term "appropriate compensation," for example, he stated that "the compensation shall be paid according to legal procedures," that the method of payment must be "convertible and freely transferable," and that payment must be made "without

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194. Id.
198. See *supra* part III.A.
delay unless with justified reasons." With these elaborations, the Chinese version of appropriate compensation seems quite close to the "adequate, prompt, and effective" standard. An American writer, Jay Laifman, observes that no meaningful distinction exists between "appropriate" as elaborated by this Chinese policy pronouncement and "adequate." Indeed, both standards are quite vague and provide no principled formulation for determining the amount of compensation. Laifman also notes that the phrase "without delay unless with justified reasons" is synonymous with the term "prompt," and that the phrase "convertible and fully transferable" is the functional equivalent of the term "effective" and is even preferable because of its greater clarity.

Gu's statements suggest that China may no longer equate the term "appropriate" with partial payment, but rather with a standard that is close to the Hull rule. China's recent recognition of its need to create a low-risk environment for foreign investment explains this change in approach. China's view during the 1950s and 1960s that the expropriation of property required no compensation reflected its "closed door" policy of economic self-sufficiency. Its current expropriation policy, on the other hand, reflects the "open door" economic policy that China began to develop in the 1970s and to which it formally committed in the 1980s.

Although Gu's interpretation of China's appropriate compensation policy may have been designed more as a public relations maneuver than an announcement of any substantive policy change, the same can probably be said about the longstanding U.S. insistence on the prompt, adequate, and effective compensation standard in all of its relevant communications. China wanted its newly announced compensation policy to reassure prospective foreign investors that it will not nationalize foreign property, and that if it must do so, it will fairly compensate the property owner.

Recent Chinese government policy statements concerning expropriation and compensation should encourage the tentative foreign investor for at least two reasons. First, although these statements are carefully framed to convey that the government still controls the economy, they also exhibit a moderate, reform-oriented tone. This tone is intended to signal that China will do what it takes to attract and retain enough foreign investment to support its drive toward economic modernization. Second, even though policy pronouncements are much less formal in China than in the West, they are still the most reliable sources of information about social and economic policy in an authoritarian system like China's.

199. Gu, Concerning Investment, supra note 197, at 19.
200. Laifman, supra note 137, at 344.
201. Id.
203. Id.
C. The Chinese Legal Structure

Despite assurances by government officials that China intends to expropriate only in extraordinary circumstances, and to compensate fairly in such an event, many prospective foreign investors continue to shy away from substantial investments in the Chinese economy. The highly fluid and continually disputed nature of expropriation law in the modern international community has undoubtedly contributed to this reluctance. China has found it particularly difficult to overcome these problems because, when it first adopted an open-door policy to encourage foreign investment, China lacked a legal framework capable of adequately protecting the interests of foreign investors. Many prospective investors undoubtedly would like special legislation of the type supported by proponents of the Immunity School to protect their interests. Chinese officials who oppose such legislation have pointed out, however, that even when China lacked adequate legal protection for foreign investors, it continued to honor economic commitments in the international community.

Recognizing that foreign investors need the assurance and predictability of formal legal structures before they commit large resources, since 1979 the Chinese government has enacted over one hundred laws and regulations pertaining to foreign economic affairs. As China’s foreign economic dealings grow, these laws will have to be refined and better integrated. Presumably, these laws will also become more accessible to investors, as Chinese collections of laws are made available for translation to commercial publishers and electronic data bases for worldwide distribution. Until then, potential investors must attempt to better understand the fundamental changes in China’s legal framework, including its new constitution, its most important legislative enactments relating to foreign economic matters, and its treatment of treaties and other sources of international law.

1. The New Constitution

If adhered to in practice, a constitutional guarantee is the most powerful of all legal assurances. No other law, regulation, or decree may lawfully conflict with the Constitution. In 1982, the Chinese government substantially rewrote its constitution and expanded the guarantees it contained. One of the main goals of the revision was to open up the country so that it might become a major participant in the world economic community. Article 18 of the Constitution permits foreign enterprises, economic organizations, and

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204. See Henry & Bainbridge, supra note 29, at 996.
205. See Gu, Investment Environment, supra note 189, at 16.
207. P.R.C. CONST., supra note 153, pmbl.
individual entrepreneurs to invest in China and to form various alliances with Chinese counterparts.\textsuperscript{208} The same provision also protects the lawful rights and interests of foreign investors as long as they act in accordance with Chinese law.\textsuperscript{209}

The 1982 Constitution grants a foreign citizen or business property rights only, not political rights or freedoms. Likewise, foreign nationals or enterprises have certain civil obligations in connection with their economic activities, such as fulfilling contractual commitments, paying taxes, and observing other applicable Chinese laws. Foreigners and Chinese citizens enjoy the same rights with respect to proprietary interests in patents, copyrights, and most other kinds of property. Since foreign investors are most concerned with property rights, they should view the new Constitution's provisions regarding such rights as a significant step toward a guarantee of stability.

The 1982 Constitution does not, however, guarantee that the government will never seize foreign property interests. As noted earlier, property owners rarely, if ever, enjoy absolute freedom from seizure in their own countries. The Constitution provides that Chinese citizens may not infringe upon the public interest in exercising their rights, including the right to own property.\textsuperscript{210} Article 10 states, "The state may in the public interest take over land for its use in accordance with the law."\textsuperscript{211} Although this provision purports to deal only with the property of Chinese nationals, China's position that the Constitution applies to all those within its borders would necessarily extend this "public interest" requirement to foreign-owned property.\textsuperscript{212} Moreover, although Article 10 refers only to land, the requirement that the government only take private property as necessary for the public interest should also apply to other forms of property. After all, the main reason for adopting the new constitution was to create a foundation for economic reform, much of which depends on foreign investment; the predominant assets of a foreign investor will typically not take the form of an ownership interest in Chinese land, even in the Chinese sense of "ownership."\textsuperscript{213} Even if a public interest

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\textsuperscript{208} Id. art. 18.
\textsuperscript{209} Id.
\textsuperscript{210} Id. art. 51.
\textsuperscript{211} Id. art. 10.
\textsuperscript{212} See, e.g., id. pmbl. ("The people of all nationalities, all state organs, the armed forces, all political parties and public organizations and all enterprises and undertakings in the country must take the Constitution as the basic norm of conduct, and they have the duty to uphold the dignity of the Constitution and ensure its implementation.").
\textsuperscript{213} A foreign investor's assets are more likely to take the form of structures, equipment, inventory, technology, and perhaps some form of real property lease. In any event, the Chinese concept of land ownership is the ownership of the right to use it; the state ultimately owns the land itself. If, as most signs indicate, one of the Chinese government's primary purposes in adopting a new constitution was to make foreign investment more attractive, it would be counterintuitive to suppose that no public interest requirement would apply to an expropriation of foreign-owned assets other than land.
requirement applies to all forms of property, however, what constitutes a valid public interest is as vague in China as it is in the Western world.\textsuperscript{214}

2. Legislative Enactments

Of the more than one hundred laws passed since 1979 dealing with foreign economic affairs, two speak directly to the expropriation issue: the Joint Venture Law\textsuperscript{215} and the Wholly Foreign-Owned Enterprise Law.\textsuperscript{216} When taken together with other signals of the Chinese government, these laws suggest that China is developing a more favorable climate for foreign investment.

The National People's Congress enacted the country's first Law on Chinese-Foreign Joint Ventures in July 1979, only seven months after the Communist Party Central Committee established the open-door policy. The first version of the Joint Venture Law addressed the expropriation issue only vaguely, stating in Article 2, "The Chinese government protects, by the legislation in force, the resources invested by a foreign participant in a joint venture and the profits due him pursuant to the agreements, contracts and articles of association authorized by the Chinese Government as well as his other lawful rights and interests."\textsuperscript{217} The law left unclear the contemplated circumstances of expropriation as well as the nature and extent of compensation for expropriated properties.

The 1990 revision of the Joint Venture Law addressed the expropriation question more directly. Article 2 now includes a separate paragraph stating, "The State shall not nationalise or expropriate enterprises with sole foreign investment but in special circumstances . . . . [W]here it is necessary to the public interest, an enterprise with sole foreign investment may be expropriated in accordance with legal procedures, and appropriate compensation paid."\textsuperscript{218} Article 5 of the Wholly Foreign-Owned Enterprise Law states, "Except under special circumstances, the State shall not nationalize or expropriate wholly-owned foreign enterprises. Should it prove necessary to do so in the public interest, legal procedures will be followed and reasonable compensation will be made."\textsuperscript{219}

\textsuperscript{214} Ferguson, supra note 161, at 21.
\textsuperscript{217} Joint Venture Law, supra note 215, art. 2.
\textsuperscript{218} See Revised Joint Venture Law, supra note 215.
\textsuperscript{219} Wholly Foreign-Owned Enterprise Law, supra note 216, ¶ 13,506.
The revised Article 2 of the Joint Venture Law and Article 5 of the Wholly Foreign-Owned Enterprise Law provide more concrete guidance on expropriation than previously existed in China. The terms of these two provisions, however, remain less than precise. There is no attempt in the legislation itself to define "special circumstances," "public interest," "appropriate compensation," or "reasonable compensation." Nevertheless, the two provisions formally codify the principle that the government is to expropriate a foreign enterprise only under exceptional circumstances and that the government must pay meaningful compensation. The essential message of the legislation seems to be that China will expropriate only under circumstances that Western nations traditionally consider justifiable and, then, pay compensation in an amount it deems fair. This message comes across more clearly when one reads the legislation alongside relevant constitutional provisions, policy pronouncements, and the various signals that indicate China officially desires a substantial infusion of foreign capital. Even with all of these new assurances, the methodology for determining compensation is still indeterminate. If full asset value, including the present value of future profits, is to be the standard, will the starting point for calculation be value to the Chinese, value to the investor, or some type of external market-value benchmark? These unresolved issues, however, should not discourage investment in China. The answers to these questions are no less certain in China than in many other developing nations; in fact, they are probably more certain.

3. Application of International Law and Practice

Several recent legal developments indicate that China is becoming increasingly amenable to adhering to norms of customary international law and practice. Although these developments do not specifically involve expropriation issues, they certainly are relevant to an overall assessment of expropriation risk. The more a nation comes to respect international legal order in any context, the less likely it is to deviate from international norms in the specific context of compensation for expropriatory actions.

The 1985 Foreign Economic Contract Law, which applies to all contracts between Chinese and foreign entities except international transport contracts, provides significant evidence that China is willing to subordinate some of its own sovereignty to international legal norms in order to participate in the global economy. Article 5 provides that the contracting parties may choose the law to be applied in disputes that might arise from the contract. In the absence of such a choice-of-law clause, the law of the jurisdiction having

the closest connection with the contract applies. The second paragraph of Article 5 specifies, however, that Chinese law governs contracts for Chinese-foreign equity joint ventures, Chinese-foreign cooperative enterprises, and Chinese-foreign cooperative exploitation and development of natural resources. In the event that there is no relevant provision of Chinese law, the third paragraph provides that "international practice may apply." 221

It is noteworthy that China formally recognizes the validity of "international practice" and provides for its application, in the absence of Chinese law, even to the three enumerated contract types performed within China. Nevertheless, Article 5's provision that "international practice may apply" when Chinese law is silent on a relevant point, does not send to foreign investors a definitive signal of China's commitment to participate fully in the world community — a commitment that the word "shall" would have unambiguously conveyed. Still, this portion of Article 5 codifies a principle that occasionally had been followed in investment contracts with Chinese firms (particularly offshore petroleum development contracts), which allowed parties to invoke precedents created by international practice in the event of a dispute. 222

International practice refers to the principles, rules, and dispute resolution mechanisms that govern international investment, management of international business enterprises, and adjustment of economic relationships in the international business community. Settlement of disputes through arbitration is one example of an international practice accepted by China. Article 37 of the Foreign Economic Contract Law, for example, provides that any contractual dispute between Chinese and foreign entities should be resolved by party-to-party negotiation or through the use of mediation. If the parties are unwilling or unable to settle their dispute, they may resort to binding arbitration as provided by the arbitration clause in their contract or an arbitration agreement made after the dispute arises. 223 Moreover, they may submit the dispute "to a Chinese arbitration body or other arbitration body." This provision indicates that the government views international arbitration tribunals and their awards to be valid in China. 224 Similarly, the Regulations Concerning Joint Offshore Oil Exploitation state, "Mediation and arbitration may be conducted by an arbitration body of the People's Republic of China, or the parties to the contract may agree upon arbitration by another arbitration body." 225 The Joint Venture Law includes a nearly identical provision. 226

221. Id. art. 5.
223. Foreign Economic Contract Law, art. 37.
224. Id. (emphasis added). If a dispute is not resolved by negotiation, mediation, or arbitration, suit may be brought by either party in People's Court. Id. art. 38.
Chinese government officials have augmented legislative provisions calling for the application of international norms in the absence of Chinese law by offering their own assurances that they will enforce the letter of the law.\textsuperscript{227} Because it is frequently difficult to ascertain the applicable Chinese law on a particular subject, however, investors cannot be sure whether international law applies or whether they have simply failed to discover the applicable Chinese law. Thus, legislative provisions in combination with the assurances of Chinese officials do not definitively determine the law to be applied in any given situation.\textsuperscript{228} Moreover, we still do not know what China's position would be in the event of a true conflict of laws. Such a conflict would occur when a Chinese law in fact could apply, but legitimate choice-of-law principles — either created by agreement or found in the choice-of-law rules of another country with a close connection to the dispute — call for application of a provision of another nation's law that conflicts with the relevant Chinese law. Either additional Chinese legislation or regulations, or decisions made on a case-by-case basis, will have to address these questions. Leaving the resolution to future ad hoc determination is, however, unlikely to quiet the fears of foreign investors.

Whether investors can assume that China will apply international law when no Chinese law is available remains uncertain. China may, rather than submit to international law, create a new domestic law or policy. In other words, if international law currently applies because of a void in Chinese law, will China later upset the reasonable investment-backed expectations of foreign investors by filling the void with a Chinese law substantially different from the relevant international norm? If, in such an event, the effect on a foreign investor is serious enough, the measure could constitute an expropriatory act. Other countries have used such tactics for the sole purpose of limiting the rights of a foreign investor.\textsuperscript{229}

On several occasions, Chinese government officials have sought to assuage investors' fears that China might undermine their reasonable expectations by subsequent laws or regulations. While China adheres to the principle that newer laws prevail over older ones, a foreign investor whose contract is undermined by a change in law may petition the Chinese government for an exemption from the law's application to the contract. Although the government is not required by any current law to respond positively to such a petition, the government has followed an informal policy to do so. In 1982, Wei Yuming, Vice-Minister of Foreign Economic Relations and Trade, announced that once the contracts signed by Chinese and foreign firms are approved by the Ministry of Foreign Economic Relations and Trade

\begin{itemize}
  \item \textsuperscript{226} Joint Venture Law, art. 14.
  \item \textsuperscript{227} See Laifman, supra note 137, at 337 (citing Wei Jiaju, Law on Economic Contracts Involving Foreign Interests, 3 CHINA L. REP. 166, 167 (1986)).
  \item \textsuperscript{228} Id. at 337.
  \item \textsuperscript{229} Id. (citing De Lupis, supra note 13, at 27-29).
\end{itemize}
or its authorized institutions, the contracts themselves bind both sides. If, however, the contracts' provisions conflict with new laws and regulations issued by the Chinese government after the approval of the contracts, Wei stated that "common international practices will be followed." Although the original contracts would be subject to new laws and regulations, "those conflicting parts of the original contracts could be dealt with in accordance with the stipulations in the original contracts through mutual consultation and confirmation." For example, the Ministry of Finance takes the position that tax provisions favorable to foreigners in existing contracts should survive new tax legislation. This precedent, however, could be set aside at any time. Indeed, the Ministry of Foreign Economic Relations and Trade, which approves investment contracts, has consistently rejected draft contract language protecting foreign investors from the effects of subsequent legislation. It has thus retained its power to determine the issue on a case-by-case basis.

The 1985 Foreign Economic Contract Law offers foreign investors their first legislatively based promise that subsequent changes in the law will not undermine contract rights and investments. Article 40 provides that contracts for Chinese-foreign equity joint ventures, cooperative enterprises, and natural resource development projects "may still be implemented according to the provisions of those contracts" if a new law conflicts with the contractual terms. Jerome Cohen cautions, however, that neither implementing regulations nor authoritative interpretations have clarified the meaning of this phrase. Article 40's use of the word "may" perpetuates uncertainty about China's commitment; as Cohen argues, few investors will find a legislative provision granting Chinese officials discretion to decide whether to apply subsequent law to existing contracts very reassuring. Regardless of how it is interpreted, Cohen emphasizes that Article 40 does not protect other long-term contracts, such as arrangements for the licensing of technology, compensation trade, or wholly foreign-owned investments. These arrangements are functionally equivalent to the equity joint ventures and cooperative enterprises protected by Article 40. Thus, foreign companies would welcome an amendment of Article 40 to cover all such transactions.

230. Wei, supra note 195, at 20.
231. Id.
232. Id.
233. See Cohen, New Law, supra note 222, at 52.
234. Foreign Economic Contract Law, art. 40.
236. Compensation trade involves long-term arrangements based on barter, as opposed to currency, payment.
238. Id.
D. Practice: Treaties in the Chinese System

1. The Status of Treaties in Chinese Law

We have previously noted that treaties, particularly the network of BITs concluded in recent years, are an important element of the investment risk calculus. Much of the impetus for signing these treaties is found in the continuing uncertainty over various expropriation issues.

China neither signed nor ratified the 1969 Vienna Convention on the Law of Treaties, which was the product of twenty years' work by the U.N. International Law Commission. The Convention codifies customary international law principles pertaining to the effect and interpretation of treaties. China's failure to assent to the Convention creates obvious questions about China's attitude toward the legitimacy of treaties as a source of positive international law, and the relationship between treaties and Chinese domestic law. For answers, one may look to several sources, including the writings of Chinese legal scholars, applicable Chinese laws, and actual Chinese practice.

China has not yet drafted a comprehensive code of private international law separate from its other laws. As a result, its conflict-of-law rules concerning the status of treaties in Chinese domestic laws are scattered among a number of laws and regulations, including the Code of Civil Procedure and the General Principles of Civil Law. China's Code of Civil Procedure stipulates that, where China is a party to an international treaty or convention containing provisions that conflict with Chinese domestic laws, the pertinent treaty or convention rules shall apply. However, when China agrees to a treaty it may declare its reservation to any specific provisions, over which Chinese law will then prevail. Similarly, the General Principles of Civil Law provide that treaty law shall prevail over Chinese civil law if the two conflict, unless the treaty provision in question was the subject of an express

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239. See supra text accompanying notes 130 to 135.
240. WALLACE, supra note 101, at 197.
243. Professor Chiu observes, however, that Chinese treatise writers generally agree that treaties are the most important source of international law, and that this position does not differ in any meaningful way from that of Western writers. Chiu Hungdah, Chinese Views on Sources of International Law, 28 HARV. INT'L L.J. 289, 295 (1987).
reservation by China. The Foreign Economic Contract Law contains an almost identical provision.246 Two Chinese writers have suggested, however, that treaty provisions should not prevail over China's Constitution.247

2. China's Position on Expropriation in Its Bilateral Investment Treaties

When prospective foreign investors know that their investments will be protected by a treaty, and that the host government has a history of fully implementing and honoring its treaty obligations, the investment environment becomes dramatically more attractive. Bilateral investment treaties typically address the various issues relating to expropriations.248 There are basically two types of bilateral treaties: Friendship, Commerce, and Navigation Treaties (FCNs) and Bilateral Investment Treaties (BITs). FCN treaties, many of which were adopted during the decade after World War II, establish in very broad terms the conditions under which the governments and nationals of two countries will conduct commercial relations.249 BITs, the newer form of agreement, usually protect economic interests more broadly and include clearer terms than FCNs. The United States considers BITs to be the prototype for future treaties and as a replacement for the older FCN treaties.250 BITs, which the Chinese call "international investment protection agreements," aim primarily to identify, clarify, and protect the interests of each nation's investors.251 Thus far, China has executed BITs covering many issues, including reciprocal most-favored-nation treatment, expropriation-related issues, repatriation of profits and principal, and dispute resolution.252

China has signed BITs with fifty-two countries.253 Without exception, these BITs recognize that the host country has the sovereign right to expropriate foreign property within its territory for a public purpose. Although they sometimes use different terms, the provisions are identical in substance. When one contracting state must, for a public purpose, expropriate investments made by entities of the other contracting state, the expropriating nation has a binding obligation to pay convertible, freely transferable forms of compensation according to established legal procedures. For example, the China-Denmark BIT stipulates:

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246. Foreign Economic Contract Law, art. 6.
248. See KRONFOL, supra note 102, at 52.
250. Laifman, supra note 137, at 341.
251. See Gu, Concerning Investment, supra note 197, at 18-19.
252. Id. at 18-19.
Expropriation and Nationalization Risk in China

The investment or income of a national or corporation of either contracting state in the other country's territory may be nationalized, expropriated or subject to measures which have the same effect as nationalization or expropriation, only for public purposes relevant to the needs of the country, on a non-discriminatory basis and subject to the provision of compensation.\textsuperscript{244}

Similarly, the China-Singapore BIT states that "no expropriation or nationalization shall be made, except in the public interest, under due process of law and subject to compensation." This "compensation shall be paid without unjustified delay and shall be convertible and freely transferable."\textsuperscript{255} The China-France BIT also specifically covers issues of expropriation and compensation.\textsuperscript{256} The treaty states that compensation must be appropriate, timely, and fully transferable; however, it does not specify a method for determining the appropriate amount. Furthermore, while compensation must be \textit{determined} within a set period, there is no time constraint for the actual payment of an award.\textsuperscript{257}

According to Gu Ming, China has encountered two major sticking points during BIT negotiations: national treatment and compensation. China did not use the term "national treatment" in the agreements to describe its desire to treat foreigners and nationals equally. Instead, its BITs specified that "each contracting state should, under the condition that its laws and regulations concerning foreign investments are not infringed upon, not discriminate against investments and investment activities of foreign investors."\textsuperscript{258} Additional protocols further explained and elaborated on this provision. Gu explains that China has taken this approach because foreign investors cannot adapt to its planned socialist economy if they are accorded exact national treatment.\textsuperscript{259} In fact, Gu argues, in some instances Chinese law actually treats foreign investors preferentially. For example, the income tax rate is 55\% for state-owned enterprises, but always lower for foreign investors.\textsuperscript{260} This would not have been the case, argues Gu, if the BITs included a national treatment clause.

The second problem is the familiar one of compensation for expropriated properties. During negotiations, many countries insisted that their BIT with China provide for "full, timely, and effective" compensation. China, however, insisted on different language. China’s negotiating position was that it should

\begin{enumerate}
\item[{\textsuperscript{244}}] Zhonghua Renmin Gongheguo he Danmai Wanguo Zhengfu Guanyu Guli he Xianghu Baohu Touzi Xieding [Agreement Concerning the Reciprocal Encouragement and Protection of Investments], Apr. 29, 1985, P.R.C.-Den., art. 4(1), 1986 CHINESE Y.B. INT’L L. 547, 549.
\item[{\textsuperscript{255}}] Zhonghua Renmin Gongheguo Zhengfu he Xinjiapo Gongheguo Zhengfu Guanyu Cujin he Baohu Touzi Xieding he Huanwen [Agreement Concerning the Reciprocal Encouragement and Protection of Investments], Nov. 21, 1985, P.R.C.-Sing., art. 6(1), 1986 CHINESE Y.B. INT’L L. 575, 577.
\item[{\textsuperscript{248}}] Zhonghua Renmin Gongheguo he Falanxi Gongheguo Zhengfu Guanyu Xianghu Guli he Baohu Touzi de Xieding [Agreement Concerning the Reciprocal Encouragement and Protection of Investments], Mar. 10, 1984, P.R.C.-Fr., art. 4, 1985 CHINESE Y.B. INT’L L. 542, 544.
\item[{\textsuperscript{247}}] \textit{Id.} art. 8.
\item[{\textsuperscript{258}}] \textit{Gu, Concerning Investment, supra} note 197, at 18.
\item[{\textsuperscript{259}}] \textit{Id.} at 18.
\item[{\textsuperscript{260}}] \textit{Id.}
compensate for "liquidated" investment, and should pay only "the value of the investment at the time of the liquidation, and with interest if payment is delayed." Gu does not explain the meaning of "liquidation value." However, Western scholars contend that it is, in essence, the book value of the company. Yet book value has been consistently rejected by the Iran-U.S. Claims Tribunal as a measure of compensation for expropriation.

Despite its objection to including in its BITs the words "prompt, adequate, and effective," or other language equivalent to the Hull rule, China's official government pronouncements in the early 1980s set forth a compensation standard close to the Hull formulation. Ultimately, the BITs executed by China used considerably more liberal language regarding compensation than did official policy pronouncements or legislation. For example, the 1988 China-Australia BIT stipulates that the compensation for expropriation should be calculated on the basis of market value before the taking becomes public. Where the market value is difficult to determine, the compensation should be calculated according to recognized evaluation standards and equity principles — taking into account the amount of invested capital, depreciation, remitted capital abroad, renewal value, and other factors.

3. Bilateral Investment Treaty Negotiations with the United States

The existing trade-related treaties between China and the United States do not adequately address expropriation. For instance, the Investment Guaranties Treaty deals with expropriatory actions only to the extent that it recognizes the power of the United States to transfer its rights to the Overseas Private Investment Corporation (OPIC). OPIC only will insure investment projects in nations that have signed a treaty recognizing OPIC's right to acquire by subrogation the insureds' claims. The Investment Guaranties Treaty does not, however, require China to pay compensation. Since it does not provide for compensation at all, it obviously sets no standards for compensation. Thus, the treaty's specific recognition of a subrogation right for claims against China may be meaningless in practice. On the other hand, the

261. Id. at 19.
262. Henry & Bainbridge, supra note 29, at 1009.
263. The Tribunal's rejection of book value as a measure of compensation is in accordance with modern financial theory. Id.
264. See supra text accompanying notes 199 to 202.
266. Id.
268. Investment Guaranties Treaty, supra note 267, arts. 1, 3.
inclusion of an OPIC subrogation right suggests that the treaty contemplates some reasonable amount of compensation. In any event, the lacunae in these treaties further underscore the need for a U.S.-China BIT.

Even after ten years of negotiation, the United States and China have been unable to reach agreement on a mutual investment protection treaty.269 The principal point of contention has not been the inherent sovereign right to expropriate, but rather the standard for compensation.270 In May 1982, the United States delivered to the Chinese government a draft Treaty for Bilateral Protection of Investment, which provided that "investment shall not be expropriated or nationalized either directly or indirectly through measures tantamount to expropriation or nationalization except for a public purpose, in a non-discriminatory manner, upon payment of prompt, adequate and effective compensation."271 An official of the Chinese Government responded:

None of the investment protection agreements signed by China adopts the principle of "prompt, adequate and effective" indemnity as advocated by the developed countries. This principle is not sufficiently reasonable because expropriation and nationalization are the sovereign acts of a country and the Charter of Economic Rights and Duties of States passed by the United Nations in 1974 prescribes that "appropriate compensation should be paid." As a signatory to the Charter, China cannot contravene the reasonable principle enshrined in the Charter.272

China's objections to the prompt, adequate, and effective standard are supposedly based on the economic burden that meeting the standard would entail. In the view of many Chinese commentators, "payment of full compensation would make nationalization meaningless since it would undermine the benefits of the expropriation."273 Moreover, the prompt, adequate, and effective compensation standard is an "outmoded concept" and "out of pace with the trend of the times."274 China is simply not willing to put into formal treaty language what it has essentially already agreed to, using different language in policy pronouncements and in other BITs. Presumably, China is reluctant to limit its sovereignty for the long term. The crux of the problem may be that the Hull formulation of "prompt, adequate, and effective" has become a term of art, a symbol of domination by developed over developing nations. Thus, many developing nations, including China, may accede to an almost identical standard using different terms. Under these


274. Chen, supra note 146, at 47.
circumstances, it might be more productive for the United States to abandon its insistence on the precise language of the Hull rule.

V. CONCLUSION

China presents enormous opportunities for foreign investors in the next several decades. Its markets are extremely large, its demand for an almost infinite array of products and services untapped, and its need for foreign capital massive. Of the many uncertainties associated with foreign investment, the likelihood of expropriation without adequate compensation continues to trouble many foreign investors. Before committing large resources to China, prospective investors must be reasonably convinced that their property will not be expropriated except in the most compelling circumstances and that, if their property is expropriated, they will be compensated fairly.

In order to illuminate the nature and magnitude of expropriation risk in today's China, we examined the longstanding international debate over the proper standard of compensation for expropriation. Developed nations, led by the United States, have traditionally insisted on the "prompt, adequate, and effective" formulation of the Hull rule. The international community has never completely agreed on what this phrase means. It essentially translates into payment of full going-concern value in a convertible and freely transferable form. Despite the Western insistence on this standard, expropriation disputes have almost always been settled for amounts representing only a fraction of what the Hull rule would call for.

Although some developing countries historically insisted that no compensation was due, particularly when they expropriated properties as part of a movement from colonial to independent status, most states now view "appropriate compensation" as a norm. Although no one has ever defined appropriate compensation, flexibility is the hallmark of the concept. Under this standard, the exact amount of compensation is determined on an ad hoc basis after taking into account a wide variety of factors, such as the returns already earned by the investor and the host government's ability to pay.

At a theoretical level, the views of the United States and a number of other developed countries continue to be at odds with the views of most developing nations. As a practical matter, however, the two sides have been moving closer together. Movement toward a middle ground has taken the form of bilateral investment treaties (BITs), which generally avoid value-laden terms like "prompt, adequate, and effective" or "appropriate," and instead spell out the methods for calculating compensation with as much precision as possible. They also generally create dispute resolution mechanisms. In general, the compensation standards adopted in these BITs have not differed greatly from the Hull formulation.
China has been sending relatively clear signals that it wishes to become a full participant in the world economic order while maintaining its planned socialist economy. Its new constitution and legislation form part of an overall plan to modernize China's economy. Nevertheless, constitutional and statutory provisions relevant to expropriation risk, especially the compensation standard, remain vague enough to give pause to many potential foreign investors. Although Chinese officials have attempted to reassure investors, greater clarity in legislation would be more effective. The crux of the problem is that while China is probably willing to protect foreign investors' interests in actual practice, it is not willing to surrender its discretion to choose to behave otherwise. It has, for instance, surrendered its unilateral discretion to determine compensation in the fifty-two BITs recently executed. In both theory and practice, China takes its economic treaty commitments very seriously.

In the end, there is obviously no way to remove all expropriation-related risk from foreign investment. Carefully crafted BITs are almost certainly the best solution to the differences that remain between China and other nations whose businesses are interested in investing in China. The United States needs to conclude a BIT with China. In this regard, it would be prudent for the United States to abandon its insistence on the use of the words "prompt, adequate, and effective" when describing the compensation standard. These words are so heavily laden with symbolic baggage that the Chinese will never accept them. The United States loses little by abandoning the precise terms of the Hull rule, because it can achieve the same result by using other language more acceptable to China. China, on the other hand, should avoid the "appropriate compensation" phrase when attempting to conclude a BIT with the United States because its symbolism is likewise politically unacceptable to the U.S. government and its investors.275

China's economic incentives will determine the terms of these BITs and the extent to which they are ultimately honored. There is always some risk that China's current or future leadership could revert to its earlier closed-door policy. In such an event, China would no longer desire major foreign investment and would have no economic incentive to protect it. In our view, China has come too far economically to reverse its current policies. Given the

275. We are fully aware that the partly rhetorical and partly substantive debate over the expropriation compensation standard is not the only reason for the failure of the United States and China to conclude a bilateral investment treaty. Thus, the United States insistence on improvement in China's human rights record and guarantees of weapons nonproliferation have also been sticking points. See, e.g., China: Trade Surplus with the U.S., MFN Status Face Clinton, 10 Int'l'TR. REP. (BNA) 157 (Jan. 27, 1993). Although beyond the scope of this article, there is at least a plausible argument to be made that focusing only on the economic aspects of a BIT would not undermine any leverage we might have to influence noneconomic concerns such as human rights improvements in China. If the economic and noneconomic issues are decoupled and a U.S.-China BIT results, one could argue that the increased U.S. investment and consequent commercial interdependence which almost certainly would follow could place the United States in an even better position over time to positively influence noneconomic issues such as human rights.
tragic example of the former Soviet Union's economy, and the success of China's economic reform efforts to date, the nation is unlikely to close its doors again. The probability seems quite high, then, that China will continue to take action to attract substantial foreign investment by making investment sufficiently safe and remunerative to the investor.

Foreign investment in China is now a reasonably attractive prospect, with very substantial potential rewards. To further calm the fears of foreign investors, China must take the next step of consummating more BITs — especially with the United States.