The concept of government guarantees to protect foreign investors against non-commercial or political risks has a long lineage, having been used extensively by the British to fund the construction of Indian railways from the mid-19th century onward.¹ In the modern era, the first publicly backed investment guarantee program was established by the United States (U.S.) as part of the Marshall Plan for European reconstruction (1948).² The basic idea was simple enough. By agreeing to indemnify U.S. foreign investors against losses arising from the inability to convert local currency revenues into U.S. dollars, the government sought to encourage the flow of private investment capital and expertise as a supplement to public aid expenditures. Later, during the 1950s, the suite of compensable risks would be expanded to include the illegal ‘taking’ of foreign owned property (expropriation and confiscation), while the focus of the program shifted from Europe to ‘friendly developing countries’.

Initial corporate concerns regarding government interference in private investment decision-making, however, meant that the volume of insurance issued would remain low until the early 1960s, wherein demand rose rapidly. Faced with rising demand from an ever increasing array of U.S. multinational investors and a record number of insurance claims, but burdened with limited resources the guaranty program was in 1971 transferred to an independent agency operating as a wholly U.S. government-owned statutory corporation, the Overseas Private Investment Corporation (OPIC). Its mission: ‘to mobilize and facilitate the participation of U.S. private capital and skills in the economic and social development of less developed countries and areas’.³

³ Today, OPIC’s operations are overseen by a fifteen member Board, eight of whom are drawn from the private sector, with the remaining seven members drawn from the federal government. The President appoints all Board members for three-year terms, and the Senate must approve each appointment. The following government agencies and departments are represented on OPIC’s Board: Department of State, Department of Commerce, Department of Treasury, Department of Labor, the Office of the U.S. Trade Representative and the Agency for International Development (USAID). The board meets four times a year and their approval is required for all project finance investments and major insurance contracts. Theodore H. Moran, Reforming OPIC for the 21st Century (Washington D.C: International Institute for Economics, 2003). See also www.OPIC.gov
Today, the agency pursues this mission by insuring U.S. investors against political risks including: expropriation, nationalization, confiscation, currency inconvertibility, war, terrorism, sabotage and political violence for periods of up to twenty years. The agency also provides direct loans through its ‘Direct Loan Fund’, as well as loan guarantees for commercial lenders. Finally, OPIC also operates investment funds, which provide investment capital to private equity fund managers for the purpose of portfolio investment in less developed countries (LDCs).

More technically, the economic rationale underpinning the provision of investment insurance is two-fold. First, the provision of insurance is intended to stimulate additional FDI as a supplement to the foreign-aid program, though the empirical evidence in support of such claims is scant at best. More particularly, it is claimed that obtaining political risk insurance (PRI) serves to reduce the average ‘cost of capital’ as well as conferring additional capital raising capacities due to the market signaling function, thereby, enabling marginal projects to proceed. Beyond this, OPIC advocacy and mediation provides U.S. foreign investors with an ‘umbrella of protection’ backed by the United States government.

In this manner, OPIC claims to have created 264,000 jobs in the U.S. and $69 billion in exports since the program’s inception. While externally, OPIC insured investments are claimed to have supported 3,100 projects in LDCs, generating more than $11 billion in host government revenues and 680,000 jobs. Finally, OPIC-supported

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4 For definitions of Expropriation in OPIC Contracts See Appendix C: ‘OPIC Expropriation Cover’.  
5 The Multilateral Guarantee Agency (MIGA) claim MIGA insured investments generate an investment exposure ratio (IER) of 6.73. In this manner, MIGA estimate that the $7.145 billion of insurance issued by the agency since 1989 has generated FDI equivalent to $36 billion. The IER, using a sample of 52 MIGA insured investments, was calculated by dividing the total amount of investment facilitated by the net exposure to political risks. See Gerald T. West, and, Ethel I. Tarazona, Investment-insurance and Developmental Impact: Evaluating MIGA’s Experience (Washington: The International Bank for Reconstruction and Development, 2001). Anecdotal evidence collected by OPIC supports the assertion. For instance, ‘The manager of Newbridge Andean Partners Fund, has estimated that OPIC’s initial $100 million loan stimulated $137 million in new investments, $74.7 million in equity coninvestments, and $330 million in vendor financing, for a total of $542 million flowing from OPIC’s original commitment.’ See Theodore H. Moran, Reforming OPIC for the 21st Century (2003), p. 94. The problem, however, as noted by Moran, is that ‘MIGA’s approach contains some fundamental problems’ as it does not adjust for country risk-premiums. The result is that contrary to logic, the method frames MIGA insurance as ‘most effective’ where its services were least needed.’ See Theodore H. Moran, Reforming OPIC for the 21st Century (2003), p. 45.  
6 Referring specifically to debt-financed investments (commercial bank loans etc), it is held that because PRI serves to transfer a portion of the investor’s risk-suite to a third party, then the lender’s credit risk profile is reduced so as to reduce the minimum loan-loss reserves held by the debt-provider, which in turn lowers average the cost of capital.
investment funds have invested $1.9 billion in 216 firms in 40 developing countries. Which in turn are claimed to have created an additional 45,000 jobs and $695 million in host state tax revenues.\(^7\)

In issuing insurance and providing loans and loan guarantees OPIC is required to follow standard risk-management practices so as to ensure that premium income plus its statutory reserves are capable of meeting any claims paid plus operating expenses. For this reason, Elizabeth Kessler contends that OPIC, in following the reserves principle and the law of large numbers, functions much the same private insurers.\(^8\) It does so, through limiting its exposure to any single country or investor to a maximum of ten percent of its total exposure or liabilities. Apart from these basic principles of insurance, the agency like any other type of insurance provider must confront two classic insurance phenomena, adverse-selection and moral hazard (asymmetric information problems). Adverse-selection refers to the risk that for any given pool of investors, it is more likely that those projects with higher risk profiles will seek out insurance while those with a low expectation of loss will opt out of the insurance pool or self-insure. The agency attempts to counter this by charging different premiums depending on the country in which the project is located, the risks covered and finally, the investment type. The second problem, moral hazard, arises when the insured changes their behavior, due to the presence of insurance, so as to make losses more probable. The agency attempts to minimize this by limiting indemnity to 90 percent of total exposures as well as monitoring investments to ensure investors ’act in good faith.’\(^9\)

This thesis is concerned to understand the role of the United States investment insurer, OPIC, in the international property rights regime. Specifically, its role in underwriting the ‘rules of the game’—where rules are understood to ‘permit, prescribe or prohibit certain actions’—through the provision of investment insurance and financing on

\(^7\) See Theodore H. Moran, Reforming OPIC for the 21st Century (2003), p. 93. In assessing the developmental impact of a project, the following are examined: foreign exchange benefits (project imports and capital outflows); net annual taxes, initial local expenditures, and local employment effects for five years after the commencement of operations.


behalf of U.S. foreign infrastructure investors in the developing world. Second, the thesis seeks to explain the evolution of U.S. anti-expropriation policy viewed through the lens of the OPIC administered insurance program. The aim, to understand the policy drivers underpinning the agency’s contemporary role in the settlement of investor-state breach of regulatory contract disputes. That is, how the agency, and by proxy its sponsor the U.S., came to perform this role. Putting the two parts together, the thesis is thus principally concerned to understand the relationship between OPIC policy and practice (U.S. policy-making) and contemporary international law norms as concern breach of regulatory contracts.

Having thus far outlined the contours of the research the remainder of the chapter is organized as follows. The first task will be to detail the significance of the current study, including its economic and political importance as well as its scholarly significance for the discipline of International Relations (IR) and its sub-discipline of International Political Economy (IPE). Having detailed the significance of a study of OPIC in investment dispute settlement and as an instrument of U.S. foreign economic policy, the second task for the chapter will be to spell out the thesis itself as concerns the two parts of the research. The third and penultimate task will be to detail the methods and research techniques before then outlining the sequence of the research on a chapter-by-chapter basis, including the specific arguments to be advanced therein.


The purpose of this section is to outline the economic, political and scholarly significance of the current study. It begins by considering the rapid expansion of national investment insurance programs (including OPIC) underpinned by the expansion of private infrastructure service providers to LDCs during the 1990s. Having done so, attention will then shift to consider the significance of the current research for both contemporary and long-standing conceptual controversies within IR.

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10 Technically, investment insurance is one type of political risk insurance (PRI), as exporters can also purchase PRI. The two terms will, however, be used interchangeably, for the purposes of this study. 11 International Relations when capitalized refers to the discipline, whereas the non-capitalized form refers to relations between states. The same applies with International Political Economy (IPE).
and IPE concerning the role of state power and law in investment dispute settlement, the role of the state in regulating international economic exchange amidst economic globalization, as well as the role of state and domestic interests in determining national foreign economic policy-making. The final section will then detail the political significance of the current research.

In one very real sense this thesis is thus concerned with the study of a small and obscure Washington-based federal government agency (employing less than two hundred staff) that is but one small component of the United States Trade Policy Staff Committee, that is itself, but one tiny part of an enormous foreign policy bureaucracy, charged with promoting and protecting U.S. interests in international affairs. Moreover, the agency judging by its continued operation has been successfully insuring and financing private U.S. foreign investors for more than three decades. Why then is such a study warranted and what does it offer to the reader?

To begin, the changes associated with economic globalization defined, as the processes of factor, product and market integration across geographical boundaries, have been both diverse and far-reaching. Of critical importance in this respect as far as LDCs are concerned has been the rapid expansion of foreign direct investment (FDI) in infrastructure services organized as Build-Own-Operate-Transfer (BOOT) projects. Infrastructure services—energy, telecommunications, transport, and water—are critical to the efficient functioning of a modern economy. They begin as critical inputs in the provision of goods and services and significantly affect the productivity, cost, and competitiveness of the economy and the alleviation of poverty. For this reason, governments have traditionally entrusted delivery of these vital services to state-owned monopolies.

Today, however, in the wake of privatisation and deregulation the pattern of ownership is markedly different. The shift reflects a revolution as governments in LDCs, faced with a scarcity of public sources of investment capital, eagerly embraced

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private infrastructure provision. As a result, the volume of private FDI in LDC infrastructure expanded rapidly from just $1 billion per annum in 1990 to $128 billion in 1997 before declining post 2001. In sum, private foreign investors participated in some 2,500-infrastructure projects in 132 developing countries, with a total expenditure of more than $750 billion from 1990-2001, equivalent to 8 percent of all FDI in LDCs from 1990-1998.15

Judging by the incidence of ‘enforced contractual renegotiation’ the transformation has not always been smooth. In this regard, the World Bank’s ‘Private Participation in Infrastructure Advisory Group’ reports that more than 40 percent of the 2,500 contracts signed between private investors and host authorities have already needed to be renegotiated.17 In one sense, the difficulties observed can be understood as the contemporary face of the ‘obsolescing bargain’.18 That is, the structural vulnerability of projects with large sunk costs to ‘enforced renegotiation’ as host authorities, sometimes opportunistically sometimes not unreasonably, seek to claw back some of the initial risk-premium paid to ‘frontier’ investors once a project is operating

14 The scale of the shift in terms of sources of financing was further exacerbated by the 47% decline in World Bank lending for infrastructure projects between 1990-2001, to just 8% of total infrastructure financing in LDCs. See World Bank, Global Development Finance, 2004, p. 163.
15 Clive Harris, Private Participation in Infrastructure in Developing Countries: Trends, Impacts and Policy Lessons (World Bank Working Paper No. 5, Washington D.C., 2003), p. 6. A project is considered foreign if it includes at least one foreign entity as a member of the project company involving operational responsibilities and equity participation. $ refer to USD unless indicated.
16 Clive Harris, Private Participation in Infrastructure: (World Bank, 2003), p. v. See Appendix A ‘Economies with Private Participation in Infrastructure by No. of Sectors, 1990-2001’, Private Participation in Infrastructure 1990-2001, (PPI Advisory Group, World Bank, Washington D.C., 2001), 1-167. Frank Sader, ‘Attracting Foreign Investment in Infrastructure: Why is it so Difficult?’ Foreign Investment Advisory Service (FIAS), May 1999, p. 5 and 15. Moreover, the true impact is greater than suggested because in Mexico and China, which account for a large portion of total FDI to LDCs, infrastructure investments totalled only 5% and 1% of the respective total volume of FDI. For example, the equivalent figures for Brazil and the Philippines were 33% and 14% respectively. Of the total expenditure: Latin American and Caribbean received 47%, East Asia 27%, Eastern Europe and Central Asia 12%, with the remainder apportioned among South Asia, Sub-Saharan Africa and the Middle East and North Africa. Of the total flows, 43% were directed towards telecommunications, followed by energy (electricity and gas) 32%, and transport 18% (roads, railways, ports and airports), with the remainder directed toward water related services. Figures calculated from Sectoral Breakdown, Clive Harris, Private Participation in Infrastructure (World Bank, 2003), p. 6-7.
17 Guasch tells us ‘Renegotiation has occurred if a concession contract underwent a significant change or amendment not envisioned or driven by stated contingencies in any of the following areas: tariffs, investment plans and levels, exclusivity rights, guarantees, lump-sum payments or annual fees, covered targets, service standards, and concession periods. Guasch finds that 48 or approximately 3% of these projects have since been cancelled, renationalized, or expropriated. The incidence by sector excluding telecommunications was as follows: electricity 9.7%, transport 54.7% and water and sanitation 74.4%.
successfully. Equally, judging by the fact that according to Guasch in the majority of instances it has been the investor that has sought to modify the terms of the initial bargain it appears the obsolescing bargain captures only a part of the difficulties faced.\textsuperscript{19}

Of particular concern is the fact that when contracting over such long periods, often more than 30 years, it is simply not possible to accurately forecast and, therefore, ‘price’ all future scenarios. To understand why this is so, it is necessary to appreciate that in investments of this type there are a large number of risks that on their own or in combination can have an enormous impact on the capacity of either party to fulfill contractual obligations.\textsuperscript{20} With many of these long-term concession contracts not due to expire until past 2025, it is therefore not surprising that private infrastructure investment in LDCs has been dubbed ‘the new political risk.’\textsuperscript{21} The assertion is supported by the fact that of the 71 cases of disputes pending before the World Bank sponsored International Centre for the Settlement of Investment Disputes (ICSID) as at 2005, 35 were infrastructure related disputes.\textsuperscript{22}

The inherent difficulties associated with long-term contracting have led private foreign infrastructure investors to devise a variety of risk-management strategies. Foremost in this regard has been the use of BOOT investment model. BOOT is a generic label for privately owned and operated infrastructure projects financed on a non-recourse basis under a concession type arrangement.\textsuperscript{23} ‘Under such an arrangement a private company or consortium (the project sponsors) typically forms a “project company” based on the right to build or re-build a facility and to operate it for a fixed period of time.’\textsuperscript{24} ‘The company recoups the investment and operating costs as well as an annual rate of return exclusively from the revenue stream generated by the project through charges levied on the service ‘user(s)’ without any

\textsuperscript{19} J. Luis Guasch, \textit{Granting and Renegotiating Infrastructure Concessions} (2004), p. 15. Renegotiation was initiated in 61\% of cases by the concessionaire, versus just 26\% from the government.

\textsuperscript{20} The typical risk suite that must be forecast in the case of BOOT projects include the following: construction risk, market risk, interest rate risk, foreign exchange risk, supply risks and political risks.


\textsuperscript{23} See Appendix B ‘Build-Own-Operate-Transfer (BOOT) Project Structure’.

recourse to the balance sheets of sponsors or the host government. The unique feature of this investment vehicle is the manner in which it enables the ‘risk-suite’ to be disaggregated among the project partners, including commercial lenders (debt providers), project sponsors (equity providers), construction contractors, and finally, the host authorities.

Apart from the use of limited-recourse financing, foreign investors have also sought additional layers of ‘deal protection’ from multilateral development banks and their respective home governments. The primary vehicle through which home states have responded has been through the provision of PRI issued by Export Credit Agencies (ECAs) to protect against losses arising from politically motivated contract repudiation. In consequence, the volume of investment insurance has increased concomitant with increases in private FDI in LDC infrastructure. For example, from just $11 billion in 1990, the total volume of insurance issued increased to $65 billion in 2002, a rise of almost 600 percent. Although it is not possible to verify exactly how much of this figure was directed toward insuring infrastructure investments, high-end estimates suggest as much as half. In addition, private infrastructure investors have also sought direct loans from their respective national insurers (ECAs) to supplement the available private finance. In this regard, Peter Bosshard estimates that 11 percent of all private investment in LDC infrastructure from 1990-2000, equivalent to more than $70 billion, was sourced from ECAs directly. Similarly, the World Resources Institute estimate that ECA financing and insurance accounted for

26 The scale of the shift in terms of sources of financing was further exacerbated by the concomitant 47% in World Bank lending for infrastructure projects between 1990-2001, to just 8% of total infrastructure financing in LDCs. See World Bank, Global Development Finance, 2004, p. 163.
27 Today, 39 national insurance agencies (ECAs) offer insurance against political risks.
29 Sharon Bedder, Power Play: The fight for control of the world’s electricity (Victoria: Scribe Publications, 2003), p. 289. The reason it is not possible to verify how much of this total is comprised of insurance for infrastructure investors is that, with the exception of the U.S. insurer, OPIC, no other national investment-insurer (ECA) is required to publish insurance data. Even in the case of OPIC, however, subject as it is to the United States Freedom of Information Act (1977), the rules permit the agency to refuse to release ‘sensitive’ information, at its own discretion ostensibly to protect commercial (client) confidences, as well as for fear of offending countries owing to differences in risk-premiums, indicating as they do a negative or positive assessment of the investment climate in the country in question. This right extends to not only the public but also the legislative branch (Congress), a fact that has raised the ire of U.S. legislators, on more than one occasion. This secrecy is necessary, ECAs claim, in order to protect commercial (client) confidentiality.
approximately 20 percent of total private investment in LDC infrastructure from 1990-1998.31

The practice of insuring and financing BOOT based infrastructure investments has attracted critical attention from a number of prominent sources, however. In particular, concerns have been raised regarding the appropriateness of the Changing Role of Export Credit Agencies (1999) in resolving investor-state breach of regulatory contract disputes.32 These concerns are ably articulated by the former head of the Berne Union of Investment Insurers, Malcolm Stephens, who in a candid assessment of the problems faced by investment insurers notes the problem is that these long-term contracts ‘blur the boundaries between commercial and political risks.’33 Continuing on, he explains, ‘many risks are both political and commercial depending on the circumstances.’ The key point is not artificial distinctions but ‘identifying and defining the various risks and deciding who shall carry them’ before the contract is executed. Unfortunately, this is not the case, so that when disputes arise, it is ECAs who are called on to make a distinction between the cause of loss as political or economic that is arbitrary by design.34

It is not only PRI practitioners that have voiced concerns, having also been the subject of critical attention from a number of prominent non-governmental organizations (NGOs), including Human Rights Watch and Transparency International (TI). For example, TI has criticized the failure of ECAs to combat corruption. Indeed, according to TI, in what amounts to a withering criticism of ECA practices, ‘the continued lack of action by ECAs to address this issue is bringing some ECAs close to complicity with a criminal offense.’35 It is these concerns that prompted the Jakarta

35 Transparency International, (letter to OECD and European Union), dated September 1999. Among the recommendations made were the following: that ‘export credit applicants must state in writing that no illegal payments related to a contract were made, and that any contravention of the ban on illegal payment should entail cancellation of the state's obligation to pay. Companies found guilty of corruption should be banned from further support for five years, and export credit agencies should not underwrite commissions as part of the contracts they support.’
Declaration in May 2000, endorsed by 347 NGOs from 45 countries, calling on ECAs to cease financing unproductive investments in developing countries.36

From the perspective of LDCs, the concerns expressed are further compounded by the practice of ‘subrogating claims.’ The practice is common to most national investment insurance providers and is formally recognized in international law.37 It refers to the fact that when a claim is paid by an ECA, title to the asset (ownership) passes to the agency, along with the original claim against the host authorities. In so doing, the payment of claims transforms investor-state disputes into state-state disputes. The practice is defended on the grounds that the knowledge that politically motivated action will result in additional debts serves as a deterrent against opportunistic rent seeking, so as to in the lexicon of project finance ‘enhance the credibility of commitments.’38

As the largest public or private program in operation today, OPIC has been at the vanguard of these trends.39 Even before this, however, OPIC, as the oldest dedicated

36 The Jakarta Declaration was drafted by 47 NGOs and endorsed by a further 300 NGOs at a summit jointly convened in Jakarta and Sumatra, May 1-7, 2000. The Declaration followed an earlier campaign culminating in April 1998, with a ‘Call of National and International Non-Governmental Agencies for the Reform of Export Credit and Investment-insurance Agencies’ the provisions of which were then sent to the Finance and Foreign Ministries of every member of the OECD. The NGOs called for transparency in ECA decision-making, environmental assessment and screening of ECA financial commitments, including participation of affected populations, social sustainability (equity and human rights concerns) in appraisal of ECA commitments, and for an international agreement in the OECD and/or G8 on common environmental and social standards for ECAs. For a good overview of the concerns of NGOs directed at the operations of ECAs See www.ecawatch.org.
37 See Theodor Meron, Investment-insurance in International Law (New York: Oceania Publications, Inc., 1979), for a comparative analysis of ECA practices in this regard, including U.S. (OPIC) and France (COFACE), Canada (EDC) and the UK (ECGD). For example, of the 275 claims paid to U.S. investors to 2005 by OPIC and its predecessors, the United States has successfully recovered more than 96% of total claims by value from the respective host governments thereby enabling it to generate reserves of approximately $4.2 billion. Statement before the Committee on International Relations, House Of Representatives 1st Session, 106th Congress, Sept. 17, 1999 by the then President of OPIC, George Munoz.
38 More technically, the practice assists in overcoming private market failure stemming from imperfect contracts so as to theoretically at least stimulate additional FDI. See Oliver E. Williamson, ‘Transaction-Cost Economics: The Governance of Contractual Relations’, Journal of Law and Economics, 22(2), 1975, 233-261. Williamson distinguishes between normal contracts that display ‘presentation’ and what he terms ‘relational’ or more typically ‘contingent’ contracting. Contingent contracts are so called because not all future contingencies can be foreseen. In these circumstances, Williams tells us that the contractual relationship is transformed into one of bilateral monopoly, so called because the benefits from such contracts can only be realized if the relationship is maintained.
public scheme has traditionally provided the blueprint for other national programs.\textsuperscript{40} Thus, and in accord with the position of its sponsor as the preeminent source of FDI in LDCs, the agency has since its inception issued more insurance and paid more claims than any other national insurer, as well as being at the forefront among its counterparts in developing new insurance products.\textsuperscript{41} In this regard, the agency, alongside its sister agency the Export-Import Bank has led the way in insuring and financing infrastructure from the mid-1990s, with the result that more than half the agency’s total insurance portfolio was comprised of infrastructure investments by 2000.\textsuperscript{42} Indeed, according to one estimate, the agency approved insurance and/or financing for some 128 infrastructure related investments in more than thirty LDCs from 1992-2001.\textsuperscript{43}

To conclude, the current study thus offers a unique opportunity to examine how the ‘rules of the game’ emerge with respect to a critical issue in contemporary FDI—investor-state expropriation disputes arising from breach of regulatory contracts. An issue that directly effects the profitability and thus continued viability of hundreds of projects and with it the development prospects of more than 130 countries playing host to private foreign infrastructure providers worldwide. Moreover, while these issues have a particular import for infrastructure investments, it is anticipated that the findings will have a wider applicability being germane to all concession based foreign investments, including resource extraction projects as have been the subject of recent expropriations in Venezuela and Bolivia (2006).\textsuperscript{44}

\textsuperscript{40} The following is a list of the Group of Seven’s (G7) respective national investment insurance program operators who together account for approximately 90% of total investment insurance exposures: United States, (OPIC); Japan, Nippon Export and Investment-insurance (NEXI); Germany, the Hermes Kreditversicherungs-Aktiengesellschaft AG (Hermes); France, Francaise D. Assurance Pour Le Commerce Extérieur (CoFace - 1967); Italy, the Instituto Per I Servizi Assicurativi Del Commercio Estero (SACE - 1971); U.K., Export Credit Guarantee Department (ECGD - 1972), and Canada (Export Development Corporation (EDC – 1968).

\textsuperscript{41} While OPIC leads the field, strictly speaking the agency is not an ECA, as when the U.S. began offering investment insurance it did so under the aegis of a separate agency, rather, than simply utilizing its own ECA, the United States Export Import Bank for this purpose. In all bar one other country, Germany, the two insurance programs: export credit and investment insurance are administered by the one agency, albeit with dedicated underwriting teams.


\textsuperscript{43} For the full list See ‘Organisation Profile: Overseas Private Investment Corporation’ available online at http://www.seen.org/db/Dispatch?action-OrgWidget:196-detail=1.

\textsuperscript{44} On May 1st 2006, Bolivian President Evo Morales issued a supreme decree ‘nationalizing Bolivian hydrocarbons’. The decree gave foreign firms 180 days to renegotiate contracts with the Bolivian
In so doing, the current study also offers a chance to examine and thus better understand the role of national investment insurance programs, but particularly that of the regime leader, OPIC, in establishing the rules of the game on behalf of private infrastructure service providers. Activities that until now have been closely guarded with the result that they have been unflatteringly labeled ‘dirty little secrets;’ and ‘secret engines of economic globalization’. Finally, the current research thus provides a unique vantage point to view evolving modes of state protection (government-business relations), as exemplified by the more prominent role of OPIC in disputes of this kind: the basic problematique—how to secure private property and contract rights on behalf of foreign investors consistent with the norms of state sovereignty—being as familiar to a 19th century statesmen as to today’s.

Apart from the immediate concern with the processes whereby the rules governing breach of regulatory contracts are produced, the research is significant as it bears upon long-standing concerns within the discipline of IR and IPE aimed at explaining shifting standards of investor-protection, i.e. the nature and functioning of the international property rights regime. The conceptual focus being the role of state power (material resources) and interests in underwriting the ‘rights’ and ‘duties’ of foreign investors and by implication the impact of international law norms (expropriation and compensation) on state behaviour (state interest formation) and ultimately the ‘outcomes’ of investment disputes. Prior to the current transformation in the modes of investment dispute settlement associated with economic globalization two perspectives predominated in accord with broader theoretical divisions within the discipline of IR, realism and institutionalism.

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government to increase the government’s share of revenue to 82%. In Venezuela, President Hugo Chavez has voided contracts with foreign oil firms operating 32 oil fields, while also disclosing plans to review and likely revoke all foreign-owned mining concessions. See Tucker Herbert, ‘Expropriation in Vogue’ in The Stamford Review, Volume XXXVI, Issue No. 8, May 12, 2006.


46 For the two classic realist accounts of international politics, See E.H. Carr, The Twenty Years Crisis 1919-1939, (New York: Harper & Row, Publishers Inc., 1964), and see also Hans J. Morgenthau, Politics Among Nations (New York: Knopf, 1948, Reprinted, 1966). The liberal institutionalist perspective, associated with Wilsonian liberalism, (President Woodrow Wilson, 1913-1921) emphasizes the constraining effects of international law and more broadly international institutions on state behaviour, hence Wilson’s efforts to construct the League of Nations following World War I. Early Realists such as E.H. Carr and Hans Morgenthau derisively labelled such initiatives as utopian as they ignored the basic ‘will to power’ that drives international politics.
The basic image in this regard is provided by realism. The approach holds that in the absence of an overarching sovereign (supra-national authority) capable of enforcing stable and effective property rights, as is provided at the national level by state governments, then property rules, and the distribution of economic rents arise from bilateral bargaining (diplomacy) between self-interested and ‘rational’ sovereign states. From this perspective, the international law of foreign investment is understood to reflect the underlying distribution of state power. More particularly, realism emphasizes coercive bargaining, wherein the more powerful state (typically the capital-exporter) will seek to manipulate the payoffs facing the weaker state through cross-linking of issue areas to motivate compliance with legal obligations.

The institutionalist approach retained states as the primary actors but sought to challenge realism’s state power centric focus, emphasizing instead, the effect of rules and norms on state behaviour. In particular, rules and norms are understood to furnish a baseline for expectations, thereby acting as an intervening variable between state power and outcomes. Seen from here, the rules and norms of the international property rights regime, developed over time through practice as well as formal treaty obligations, serve to delimit acceptable bargaining strategies and thus the outcomes of disputes. That is, in contrast to realism’s state power centric focus, for institutionalists state behaviour and disputation is constrained by a ‘logic of appropriateness’ rather than a ‘logic of consequences’.


48 James G. March and Johan P. Olsen, ‘Change and Continuity in International Orders’, *International Organization*, Autumn 1998, vol.52, i4, 943-969. In many respects, the basic point of divide mimics the disciplinary boundaries separating IR and International Law centered on the role of power (state) politics versus the power of law in delimiting modes of bargaining and ultimately outcomes in world affairs. As a secondary aim, the research also seeks therefore to build upon the tentative rapprochement between the two disciplines, characterized by a greater willingness on the part of both sets of scholars to re-consider the impact of legal rules on world politics or alternatively, the impact of international power politics on international law. For a good account of how and why the two disciplines became estranged and recent works that seek to bridge the divide, see Martti Koskenniemi, ‘Carl Schmitt, Hans Morgenthau, and the Image of Law in International Relations’, and See also Friedrich V. Kratochwil, ‘How do Norms Matter?’ in Michael Byers (ed.), *The Role Of Law In International Politics: Essays in International Relations and International Law* (Oxford: Oxford University Press, 2000). For accounts that attempt to overcome the divide see Robert J. Beck, Anthony C. Arend, and Robert D. Vander Lugt, *International Rules, Approaches from International Law and International Relations* (New York: Oxford University Press, 1996), and See also Judith Goldstein, Miles Kahler, Robert Keohane, and
In addition, to these more long standing disciplinary concerns, a study of the role of OPIC, and by implication of U.S. power in the international property rights regime is also important for contemporary research programs within both International Law and IR concerned to understand the impact of shifting governance arrangements or rather the ‘legalization’ of dispute settlement. The conceptual issue at the heart of these debates being to what extent do the processes of economic globalization and more specifically evolving arrangements for dispute settlement empower non-state actors thereby undermining the states traditional monopoly as regards the construction and enforcement of international law norms (expropriation and compensation)? To understand the issues at stake, the proceeding section will briefly outline the rights and duties of direct investment partners as prescribed by the customary international law (CIL) of foreign investment, and as concern standards of expropriation and appropriate compensation. The second task will then be to examine shifting arrangements for dispute settlement, as is the concern of the contemporary research program aimed at understanding the effects of shifting patterns of global governance.

Stable and effective international property rights have long been recognized as the foundation stone of cross-border trade and investment—literally, the building blocks of the world economy. At the same time, the rights of foreign investors must be balanced against sovereign (states) rights as the constitutive principle of the interstate


51 See Hedley Bull for whom ‘promise keeping and measures to protect the stability of possessions constitute two of three elements of international order alongside those measures aimed at preserving life and liberty’, Hedley Bull, The Anarchical Society: A Study of Order in World Politics 2nd ed. (New York: Columbia University Press, 1995), p. 18-19. Strictly speaking, property and contract rights are different. They are so because property rights are held to establish a general right against all citizens, whilst contract rights establish rights between those parties to the contract only.
system. In recognition of the enduring tension between the two constitutive elements of international order, states long since formulated rules to govern international property and contract rights consistent with sovereign prerogatives. The basic rule governing cross-border direct investment is that ‘expropriation’ is *prima facie* legal if accompanied by compensation. Where expropriation is defined as ‘an official taking by a sovereign state of a [foreign] direct investment.’ The rule reflects the sovereign right of states to exclusive territorial jurisdiction. Absent the payment of compensation, expropriation, which is lawful, becomes confiscation, which is unlawful. Applied to breach of regulatory contract disputes, the basic principle holds insofar as where a ‘taking’ is held to have occurred through the unilateral suspension or termination of a contract by a sovereign contracting party, then such action is deemed to be expropriatory. That is, any unilateral termination or modification of a contract is not illegal *per se* but is subject to fair compensation.

The expropriation rule derives from two long established principles of CIL. The first principle is ‘the law of state responsibility to Aliens and their property’, which holds that states are responsible for injuries to aliens residing in their national-jurisdictions. While the second principle, ‘Unjust Enrichment’ (*Enrichissement Sans Cause*), holds that, a state may not enrich itself at the expense of an alien, hence the requirement to pay compensation. The two principles or secondary doctrines of international law were developed over time through reciprocal treaty arrangements among European states (Friendship, Commerce and Navigation treaties) hardened into principles of CIL. Later, the newly independent United States of America accepted the basic

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55 ‘The right of a state to control the entry of foreign investment is unlimited as it is a right that flows from sovereignty.’ M. Somarajah, *The International Law of Foreign Investment* (2004), p. 97. International law traditionally makes a distinction between direct and portfolio investment so that the international law of foreign investment, including the right of states to extend diplomatic protection, applies only to direct investments. Needless to say, the boundary is not as clear in practice as in theory.
framework as a condition of membership of the society of states. Where reciprocal interests did not exist, CIL norms governing foreign trade and investment were extended through a combination of persuasion, coercion (gunboat diplomacy), and where this failed, outright annexation (colonialism).

The two principles hold that where compensation is not forthcoming, the home state may intervene on the investor’s behalf to extend what is known as ‘diplomatic protection’ in order to affect restitution or alternately, the payment of compensation equal to the value of the property taken. The reason for this is that only states have *locus standi* (literally, standing) to bring claims against other states under public international law, according to which, states are the *subjects* of law, while investors are deemed *objects* of law. In exercising this right, it is generally accepted that home state actions are constrained by two further principles of CIL. The first of these is the principle of ‘proportionality’ which holds that measures taken to affect the payment of compensation must be proportionate to the value of property taken. The second delimits acceptable measures by outlawing ‘the use of force.’ Beyond this, states are

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58 See M. Sornarajah, *International Law of Foreign Investment* (2004), p. 209. He notes that the first such treaty was signed between France and the newly independent United States of America in 1778. It should also be noted, however, that the signing of the treaty was not so much driven by legal norms, as it was a desire to ally with the chief rival of the former colonial power, Great Britain.


60 The right of states in this regard is derived from the Vatellian notion (1758) that ‘an injury to the material interests of a citizen abroad is an injury to the home state and that such an injury engages a right to intervene’ in order to affect restitution or compensation. Vatell, *Droit des gens; ou, Principes de la loi naturelle appliqués à la conduite et aux affaires des nations et des souverains* (1758), (Law of Nations), First English Edition, 1759. Later, the Permanent Court of Justice would articulate the principle as follows: [I]n taking up the case of one of its nationals, by resorting to diplomatic action or international judicial proceedings on his behalf, a state is in reality asserting its own right, the right to ensure in the person of its nationals respect for the rules of law.’ Quoted in M. Sornarajah, *International Law of Foreign Investment* (2004), p. 139 from Panevezys-Saldutiskis Railway Case (1939) Series A/B No. 76, 16.

61 The principle of *locus standi* was established Brigitte Stern tells us in the *S.S. Lotus Case* in 1927, Permanent Court of International Justice, Reports, Series A, no. 10, 18-19, which established the principle that states are the *subjects* of law and investors *objects* of law. See Brigitte Stern, ‘How to Regulate Globalization?’ in Michael Byers (ed.), *The Role Of Law In International Politic* (2000), p. 257.

free to pursue claims by whatever means available to them, including the seizure of property equal to the value of the claim.

The rules derived from CIL are complicated, however, by the existence of a second source of international law, treaty law, i.e. treaty making between states, including bilateral and multilateral treaties. Treaties themselves are governed by the foundational doctrine of international law, *pacta sunt servanda* meaning literally, ‘treaties are to be observed’. More particularly, the doctrine holds that treaties and contracts entail binding reciprocal obligations that cannot be modified without the consent of both parties. Of principal importance in this regard concerns the rapid increase in the number of bilateral investment treaties (BITs). The first BIT was signed in 1959, but it was not until the late 1980s that bilateral treaties of this type became the primary vehicle adopted by states to govern FDI. For example, some 176 countries had signed more than 2,300 BITs by 2004, equal to a tenfold increase in just fifteen years. What is significant here is that states may cede rights accruing to them through such treaties, including as concerns the choice of national jurisdiction.

Foremost in terms of the changes wrought by the emergence of BITs as the principal form of investment related treaty making between the industrialized states and their developing counterparts concerns the inclusion of ‘legalized’ dispute settlement mechanisms wherein investment disputes are delegated to an independent (offshore) arbitral body. These bodies are typically comprised of a three-person tribunal, one member being appointed by each of the parties (defendant and plaintiff), with a third independent arbitrator. Arbitral agreements such as these are then covered by a second layer of treaty law, as contained in a variety of multilateral treaties, which make enforcement of awards mandatory subject to limited public policy exceptions.

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63 Article 2 of the Vienna Convention on the Law of Treaties (1969) defines a treaty as: ‘an international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation.’


65 While 176 countries have signed BITs, none of these has been signed between industrialized states, being limited to FDI between the industrialized states and their developing country counterparts.

As might be expected, the rapid increase in the number of BITs has been mirrored by a rapid increase in the number of investment disputes being referred to arbitration. For example, where the World Bank Group’s arbitration body, the International Centre for the Settlement of Investment Disputes (ICSID) heard just 11 disputes from 1966-1980, during the next decade it would hear some 24 disputes, before increasing to 96 in the years from 1991-2004. Similarly, these trends are also evident in the increasing number of cases heard by the International Chamber of Commerce (ICC). For example, from 1923-1978, the ICC heard on average 63 cases per year, from 1979-1991 this would increase to 291 cases per year, while from 1992-2001 the average number of cases increased still further to an average of 450 per year.

For a growing number of IR scholars the effects of shifting institutional arrangements for dispute settlement but particularly the increased use of arbitration is not limited to merely a change in venue. Two competing perspectives as regards the effects of the legalization of dispute retirement can be identified: liberal-institutionalist and critical. Turning firstly to the orthodox or liberal accounts. For the authors of *Legalization and World Politics* (2001) the traditional image of dispute resolution as coercive, bilateral interstate bargaining derived from realist and to a lesser extent institutionalist accounts is outmoded owing to the current transformation wherein investment disputes are increasingly decided as ‘legal cases’ as part of a more general ‘move to law’ in world politics. The reason for this they contend is that legal rules engender different forms of obligation from those resulting from ‘coercion, comity or morality alone.’ In consequence, it is becoming increasingly difficult to trace ‘individual

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67 The figures refer to the date the dispute in question was registered, rather than the settlement date.
judicial decisions and states’ responses to them back to any simple ‘short-term matrix of state or social preferences, power capabilities and cross-issues.’

In this manner, inter-national dispute settlement is increasingly giving way to transnational dispute settlement. Two variables are held as critical in this regard. The first of these is delegation, while the second is access. Thus, where dispute resolution functions are delegated to third-party arbitral forums and where foreign investors are provided with access so as to enable them to initiate legal proceedings absent the need for traditional home state diplomatic protection then the international dispute settlement is giving way to transnational dispute settlement.

In contrast, for scholars working within the critical tradition the consequences of the ‘juridification’ of investment dispute settlement cannot be understood separate from its causes, associated with the transition from multinational to transnational production, the globalization of markets and with it the emergence of global political economy. The approach therefore emphasizes not so much the disjuncture between power and outcomes as between state power and outcomes. State power as a variable thus being replaced with that of an emergent transnational class—mercatorocracy—at the vanguard of which are transnational corporations (TNCs).

In particular for Cutler, these new arrangements (access and delegation) serve to confer power on TNCs insofar as they effectively grant them de facto status as subjects rather than objects of law (i.e. with personality in law) as provided for under public international law (state law). In the new transnational commercial and legal order, TNCs have thus emerged as crucial participants in the creation and enforcement of merchant laws so as to challenge the state’s monopoly over legislative

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and adjudicative functions in international commerce.\textsuperscript{72} Other non-state sources of authority in addition to TNCs include private international lawyers, accountancy firms, insurers, bankers and their private associations such as the International Chamber of Commerce. To this end, the new transnational legal order does more than simply regulate conflict at the interface of national and international politics and law, instead it provides ‘the basic norms governing property, contract and dispute resolution’, i.e. juridical foundations of late modern (transnational) capitalism.

If such assessments are correct, or even partially so, then one might reasonably ask, to what extent do these new arrangements, bypassing as they do the need for traditional home state diplomatic protection, undermine the centrality of state power and interests in governing the global economy, including the monopoly of states in underwriting the rules of the game on behalf of foreign investors? In short, what role for national investment insurers and by proxy state power and interests in the new ‘transnational’ legal order? By extension, to what extent do these new arrangements possess authority to motivate compliance with arbitral awards absent the need for home state enforcement? Second, are the methods of norm creation changing? More narrowly, what role for U.S. power and interests (and OPIC) in underwriting international property rules in the new transnational legal order? That is, what is the relationship between U.S. foreign policy-making and institutional practices and law norms as concern breach of regulatory contracts? Finally, what is the role of the state in mediating cross-border corporate expansion in the 21\textsuperscript{st} century, and with it strategies of multinational capital accumulation? In this respect, this research is significant as the findings bear upon each of these prominent, contemporary conceptual controversies within the disciplines of IR, IPE and International Law.

Of course, the effects of economic globalization are not limited to the international sphere. To this end, the emergence of a global economy thereby empowering footloose multinational corporations is also held to influence the process of state interest formation. That is, foreign policy-making, but particularly foreign trade and investment policies of states. The question being thus, as barriers to entry and exit are removed so as to make MNC exit-threats more credible, what role for state or

‘national interests’ in the new order? Alternatively, to what extent do new arrangements for economic governance privilege corporate interests in state foreign policy-making as they are held to in the international sphere?

Even before the current transformation associated with economic globalization, corporate or foreign investor interests have been held as central in determining the goals sought by U.S. foreign economic policy makers, including as concerns the policy and practice of OPIC. For example, Charles Lipson (1985) contends that U.S. government policies to protect direct foreign investments generally conform to the predominant preferences of the most vitally affected large corporations. That is, ‘the program’s legislative history repeatedly reaffirms the central role of corporate preferences’ consistent with evolving strategies of corporate adaptation and risk-management. Moreover, it is notable that even members of Congress have expressed concerns regarding the unusually close relationship between OPIC and Enron that saw critics of the program label it ‘corporate welfare’ and ‘Enron’s Pawn’. In this respect, contemporary concerns regarding the influence of multinational firms in determining state interests amidst economic globalization can be seen to be part of a more long-standing research program concerning the drivers of U.S. anti-expropriation policy.

More generally, however, the interest in U.S. anti-expropriation policy-making itself bears upon more long standing conceptual issues associated with the study of foreign policy-making in IR. Prominent in this respect are the following issues. First, what is the role of international versus domestic politics in determining the goals sought by states? Second, and by implication, to what extent do state policy makers possess

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75 The tenor of the criticisms directed at the agency is ably captured by the comments of Nita M. Lowey (D-N.Y.), who noted before Congress on March 7th 2002, ‘I do have concerns with respect to the amount of business EX-IM and OPIC have done with the Enron Corporation over the past 10 years . . . All three agencies before us today enjoy almost complete autonomy from Congressional and Executive branch oversight when it comes to responding to specific proposals from the private sector’. Quoted in ‘Public Institutions and the Globalization of Enron’ *Enron’s Pawns: How Public Institutions Bankrolled Enron’s Globalization Game*, Sustainable Energy and Economy Network, Institute for Policy Studies, March 22, 2002, p. 20 of 46. For a sample of the criticisms from NGOs directed at OPIC See Jim Vallette, Daphne Wysham and Jon Sohn, ‘OPIC, Ex-Im and Climate Change: Business as Usual? An Analysis of U.S. Government Support for Fossil Fueled Development Abroad, 1992-98’ (1-113). A report prepared for the *Institute for Policy Studies, Friends of the Earth, and the International Trade Information Service*, April 28, 1999.
autonomy from domestic interest groups in formulating foreign policy? Third, to what extent are state preferences hierarchically ordered to give priority to the high politics of security over the low politics of economics? Fourth, to what extents is state interest formation impacted by international law norms or do material interests determine the goals sought by national foreign policymakers? Fifth, and finally, to what extent does the concept of the ‘national interest’ retain its analytical validity in the study of contemporary foreign policy-making? Once again, in seeking to explain the OPIC administered program’s long-term evolution, the current research is important for each of these conceptual issues associated with the study of foreign policy-making.

Putting the two parts together, the present study therefore offers an invaluable opportunity to understand the relationship between U.S. anti-expropriation policy-making and the international law norms governing international investment disputes. Specifically, the extent to which OPIC’s and thus U.S. policy is delimited by institutional rules or alternatively the extent to which institutional rules and norms reflect U.S. foreign policy and material interests. In short, to examine the international and domestic politics of expropriation rule making in the ‘new’ legal order.

The final task remaining, having detailed the economic and scholarly significance of the current research is to outline its political significance. In the first instance, the research findings bear upon current and long-standing efforts to codify the ‘rights’ and ‘duties’ of foreign investors. As such, it is expected that the findings will assist in furthering our understanding of the following issues. Most immediately, are such efforts justified in terms of strengthened property rights and ultimately increased flows of investment capital, or would the resources expended in promulgating FDI related treaties be better directed elsewhere, such as toward developing non-legal dispute resolution mechanisms, i.e. mediation? Referring specifically to provisions contained in BITs, does delegating judicial oversight to offshore arbitration result in depoliticized dispute settlement. Second, should LDCs sign BITs providing for the automatic subrogation of insurance claims? Also from the perspective of LDCs, what is the optimum framework in terms of regulatory and contract structures (allocation of risk)? Finally, referring specifically to the public provision of investment insurance: to what extent is there a need to regulate and thus harmonize the practices of national investment insurers? In addition, should NGO efforts aimed at reforming ECA
practices be directed at national policy makers or toward multilateral organizations such as the Berne Union of Investment Insurers and or the OECD? To conclude, the research is politically significant as the findings are expected to bear upon each of these critical issues in contemporary FDI rule making.

Realism Revisited: Re-considering the Role of State Power and Interests in the ‘New’ Legal Order and State Interests in U.S. Anti-Expropriation Policy-Making

The purpose of this section, having outlined the conceptual issues at stake, is to detail the overall argument to be advanced, i.e. the thesis. To begin, the evidence will show that while the shift towards third-party arbitration to resolve investor-state disputes is not merely cosmetic, in the final analysis states remain the central actors in dispute settlement and expropriation rule making, even in the ‘new’ legal order. More specifically, the evidence will show that far from being beyond the state, as is implied by the use of the term transnational, these new arrangements (including the use of arbitration) to resolve disputes, are wholly manipulable by states where such awards are deemed antithetical to state interests so conceived. Put simply, the efficacy of these new ‘legalized’ arrangements is dependent on state power and interests as states seek to enforce and or resist sanctions and thus legal obligations consistent with evolving conceptions of national interests and relative material capabilities. In this manner, the evidence serves to underscore the continued centrality of international dispute settlement and the international politics of expropriation rule making.

Where U.S. infrastructure investors are concerned, the evidence will show that OPIC investment insurance is critical in underwriting the rules of the game as concerns breach of regulatory contract disputes. More fundamentally, the evidence will show that where treaties provide for the automatic subrogation of insurance claims as are standard in U.S. BITs then the agency, in paying or rejecting investor claims, can unilaterally determine the boundaries of economic and political risks, legitimate (lawful) and illegitimate (unlawful) modes of regulating foreign owned infrastructure and by implication those actions that constitute a violation of international law, i.e. the meaning of expropriation as concerns breach of regulatory contracts.
The public provision of PRI thus provides the U.S. with a secondary judicial mechanism supplementary to the existing hard law treaty framework to enable it to determine the outcomes of disputes consistent with broader foreign policy goals. In this manner, the agency does more than simply regulate conflict at the interface of national and international law and politics. Instead, it reaches inside of states to harmonize dissonant national property norms as concern ‘regulatory takings’, so as to in turn provide a soft-infrastructure for the expansion of U.S. infrastructure investors to the developing world.

From a theoretical standpoint, the evidence thus attests to the continued explanatory advantage of a classical realist conception of expropriation rule making. And while the findings, framing as they do institutional rule making as a continuation of international power politics, are from far from radical they are no less significant in light of the claims of scholars concerning what is interpreted as a growing disconnect between underlying state power and interests, the outcomes of disputes and international law norms of expropriation and compensation. The thesis contends therefore that the theoretical pendulum has swung too far in favour of a conception of dispute settlement as rule-governed and transnational rather than the product of state power and interests. Albeit in the case of U.S. infrastructure investors, this is a bifurcated power consisting of OPIC investment insurance (governance) and the U.S. government at the point of enforcement.

Turning now to the second of the research questions, the thesis contends that state initiatives or state interests are best able to explain the long-term evolution of the OPIC administered insurance program. From this perspective, shifts in the policy and practice of OPIC must be understood as driven by state officials, comprised of the executive and legislative branches of government, consistent with evolving conceptions of U.S. national interests and in response to shifting configurations of power in the interstate system and international political economy more broadly.

In asserting the centrality of state initiatives the intention, however, is not to frame U.S. anti-expropriation policy as coherent. The reason for this, as the evidence will show, is that U.S. anti-expropriation policy has always been ill defined at best, subject as it is to the exigencies of international politics. More generally, however, there is
little evidence to suggest that U.S. policy in this respect is driven by anything other than material interests, rather than shifting international law norms. In this respect, changes to the program must be understood as driven by broader foreign policy goals sought by states officials’ vis-à-vis the developing world.

Viewed from this perspective, the program’s one-off expansion in 1994 so as to facilitate the agency’s participation in BOOT based private infrastructure provision, reflected a broader state led shift in U.S. foreign economic policy characterized by the aggressive pursuit of markets for U.S. exporters and foreign investors in the developing world. Thus, while corporate preferences and state economic interests increasingly overlapped by the mid-1990s, where the goals of the state and corporate America diverged, it was the interests of the former that prevailed over those of the latter. In this manner, the U.S. pursued a consistent albeit evolving conception of the national interest unrelated to party politics or Presidential whim.

In this respect, the evidence therefore attests to the continued explanatory capability of a realist conception of foreign policy-making, emphasizing as it does the primacy of international power politics in determining the goals sought by states. And while far from radical, once again the findings are no less significant in light of the image of U.S. foreign policy-making as inchoate and beholden to corporate interests in an age of economic globalization. In this regard, the current study thus provides a substantive reinterpretation of the long-term evolution of the OPIC administered investment insurance program from its inception through until the mid-1990s including as concerns the causal mechanism but perhaps more importantly its characterization in terms of where the program sits among the plethora of foreign policy goals sought by U.S. officials.

Methods and Research Techniques

The research, consistent with the two question framework, will proceed in two stages: parts ‘A’ and ‘B.’ The first task therefore will be to detail the methods that will be used in part ‘A’ of the research concerned with the role of OPIC in resolving investor-state disputes. This will be followed by an outline of the methods that will be used in
part ‘B’ of the research that seeks to explain the evolution of the OPIC administered investment insurance program.

Part ‘A’ of the research will draw upon empirical evidence from two recent high profile investor-state disputes. The first dispute to be examined arose from a contractual disagreement between the Nebraska-based CalEnergy Company Inc. (later renamed MidAmerican), insured by OPIC, and the Indonesian government-owned natural gas company Perusahaan Listrik Negara (PLN).\(^{26}\) Despite considerable efforts to resolve the dispute amicably, including arbitral hearings at the International Court of Justice at The Hague, OPIC eventually paid two insurance claims in late 1999. In reaching a judgment as to validity of the claims, OPIC opined that the investor’s ‘fundamental rights in the project’ had been contravened, thereby, violating international law. As a result, CalEnergy was awarded $290 million in compensation. Subsequent to the payment of the claim, an agreement was reached in mid-2001 wherein the Indonesian government agreed to repay OPIC, pursuant to the applicable bilateral treaty provisions (1967).

The second dispute to be investigated arose from a contractual disagreement between the Dabhol Power Company (DPC), sponsored by Enron and insured by OPIC, and the state-owned Maharashtra Electricity Board (MSEB) in mid-2001. A negotiated settlement was eventually reached in mid-2005, following four years of shuttle diplomacy between the U.S. and India and literally dozens of legal hearings. In the meantime, the dispute resulted in the payment of six separate claims to DPC investors, totalling $125 million. Once again, in reaching its determination, OPIC opined that the investor’s ‘fundamental rights in the project’ had been violated thereby violating the international law of expropriation.

The basic method is therefore the case study method, where following George a case is defined as a discrete history of a ‘class of events’ or historical phenomena.\(^{27}\) In this


\(^{27}\) Alexander L. George and Andrew Bennett, *Case Studies and Theory Development in the Social Sciences* (Cambridge, Massachusetts: MIT Press, 2005), p. 17. The differences between the definition of a case study forwarded by George and Bennett and other widely used formulations, notably that of King, Keohane and Verba (*Designing Social Inquiry*) and also Eckstein ‘Case Studies and Theory in Political Science’ concerns the fact that for these scholars a case is a phenomena for which the
instance, the research is concerned with a subclass of expropriation disputes (breach of regulatory contract) where the investor is insured against political risks. More narrowly, the method employed conforms to the method of ‘structured-focussed comparison’ insofar as ‘general questions are posed . . . of each case study . . . thereby making systematic comparison and cumulation of the findings of the cases possible.’ Second, it is focussed insofar as it is ‘undertaken with a specific research objective in mind and a theoretical focus appropriate for that objective.’ In this regard, the case study investigation seeks to understand the nature of contemporary institutional restraints against expropriation. To do this, the case studies will employ a type of ‘within-case-analysis’ termed ‘process-tracing’, which seeks to ‘infer and construct a causal chain account of how various conditions and variables interacted over time to produce the historical outcome.’

More practically, the first task in each of the two cases will be to construct a chronological narrative detailing the key events in the dispute from its inception through until the final settlement. The second task to be undertaken will then be to construct an explanation of the outcomes of the two disputes. The explanation will be broken down into two parts for the sake of ease. Part one will examine the impact of PRI and the role of OPIC in mediating a settlement, while part two will then consider the impact of legal rules and norms as well as state power and interests in determining the final settlements.

researcher reports on only a single measure on any pertinent variable, though typically variance in the dependent variable. To this end, the research concurs with George and Bennett that the ‘logic of inference’ articulated by the authors of DSI, and that underpins such a narrow definition prevents research into what are often the most interesting phenomena, See George and Bennett, p. 17-18. In this regard, although the definition employed serves to broaden the understanding of that category of case studies that can be used for the purposes of developing theory so as to overlap with the historical method, the research explicitly seeks to go beyond merely the construction of a historical narrative, so as to link the empirical data from the case studies to particular theoretical concerns and associated research agendas. In this regard, the method employed explicitly recognizes the difference between history and political science.

78 George and Bennett, Case Studies and Theory Development (2005), p. 67 In this respect it is worth noting that the two cases approximate the method of cross-case comparison (as a subtype of the comparative case study method) insofar as the two cases to be examined are similar in many respects bar one – variation in the dependent variable. Equally, this is not the intention of the research here, insofar as the aim is not link variance in the independent variables to variance in the dependent variable as is the goal of theory-testing case studies used to deduce covering laws. The method may be likened in Eckstein’s influential typology of case study methods to a disciplined-idiographic study, See Harry Eckstein, ‘Case study and theory in political science’ in, Fred I. Greenstein and Nelson W. Polsby, (eds.), Handbook of Political Science, Vol. 7 Strategies of Inquiry, (Reading, Mass.: Addison Wesley, 1975), p. 79-139.

79 George and Bennett, Case Studies and Theory Development (2005), p. 13.
Having outlined the basic method to be employed, two questions must be addressed before continuing. The first of these is why study actual investment disputes. In the first place, such a study offers valuable insights into the nature of institutional rule making. It does so, because while legal rules governing FDI have proliferated, ultimately ‘there are no relevant treaties among a large number of states which furnish a comprehensive code of law on foreign investment.’ For this reason, and in the absence of a multilateral organization capable of promulgating binding rules for direct investors as is provided on questions of international trade by the World Trade Organization, the rules and norms governing dispute settlement including their scope and applicability to particular cases are produced in the course of resolving actual disputes. Where norms are defined as implicit prescriptions that establish legitimate (lawful) and deviant (unlawful) behaviour by disputants, and rules are defined as ‘the codification of norms into legal obligations.’

The significance of disputes in delimiting the meaning of rules is succinctly articulated by Lipson as follows: ‘because international property rules do not have fixed meanings or de-contextualized significance’ they must ‘be continually reproduced and redefined in the dispute process as the actors use or resist existing standards.’ The point to note is that legal rules and norms are ‘neither intrinsic nor immutable’. That is, they are contested in both theory and practice (disputes) so that legal norms, which prescribe acceptable standards of behaviour, including with respect to host state regulation of foreign enterprises, notions of ‘fundamental rights’ and the standards of compensation to be applied are continually evolving. These challenges and the outcomes of disputes serve cumulatively, therefore, to delimit the meaning of expropriation and appropriate compensation.

The second question that must be addressed concerns ‘case selection’ That is, why the focus on the disputes between CalEnergy and Enron and Indonesia and India

80 M. Sornarajah, International Law of Foreign Investment (2004), ‘The sources of international law on foreign investment’ p. 87-96, He writes: ‘The claims relating norms of an international law of foreign investment can be accepted as principles of international law only if they are based on an accepted source of public international law. These sources of international law are stated in Article 38 (2) of the Statute of the International Court of Justice.’ p. 87.
82 Charles Lipson, Standing Guard (1985), p. 32.
respectively, and not any number of other disputes in for example Argentina, Peru, Nigeria, Turkey and Pakistan to name a few? Most immediately, the two disputes have attracted extensive coverage in both local and international media. This interest arose for a number of reasons. Thus, the Dabhol dispute attracted significant attention owing to the involvement of Enron and the intense scrutiny afforded the company’s activities in the wake of its bankruptcy in early 2002. To this might also be added the sheer scale of the investment, involving as it did the construction of the largest combined cycle-gas fired power plant in the world, at an estimated cost of $3.5 billion, equivalent to ten percent of all FDI in India from 1993-2000. In the case of Indonesia, the dispute attracted widespread attention in light of the fact that the claim paid by OPIC is the single largest by an insurer to date. Moreover, the CalEnergy dispute was but one of a dozen such disputes between foreign owned independent power producers and the Indonesian authorities. Apart from media interest, the two disputes have also been the subject of critical attention from NGOs.

More importantly, however, the two disputes were selected because they are the first of their kind. That is, they are the first of many such disputes between OPIC (ECA) insured infrastructure investors and foreign governments to result in the payment of significant claims under the contracts of insurance. In consequence, the processes used to reach the respective settlements have implications for all OPIC, and indeed, all ECA insured infrastructure investments in LDCs. In short, the two disputes go a long way to determine the ‘rules of the game’ for breach of regulatory contracts.

For this reason, the two disputes have attracted significant cross-disciplinary academic interest. This interest has stemmed from three sources in particular. The first of these is from scholars of international business, for whom the two cases have been used to illustrate the many risks facing foreign investors. Of greater significance for

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83 Indeed, even the normally conservative and pro-business *Financial Times* of London attributed, many of the problems facing Indonesia during this time to the ‘careless industrialized country export credit agencies’ who in its words must ‘share a major responsibility for violence in East Timor and economic disaster in Indonesia.’, *Financial Times*, April 22nd, 1999. See also Jeffrey A. Winters, ‘Criminal Debt in the Indonesian Context’, *Center for International and Comparative Studies*, Northwestern University, July 3rd, 2000, 1-29.


this study, however, concerns the widespread interest in the two disputes from PRI professionals. In this regard, one leading expert in the field has noted ‘[T]he presentation of actual or potential claims associated with the Mid-American [CalEnergy] case in Indonesia in 1999, and with the Enron-Dabhol case in India in 2002, raises new questions—broader than what may be associated with these individual projects—for a political risk insurance agency such as OPIC.’86 Not surprisingly, however, the focus of interest has tended to centre on a narrow range of concerns such as contractual provisions making claims payable on the failure to honour arbitral awards, raising as it does the issue of moral hazard.87

Overlapping such concerns, are those of international law experts who together constitute the second main source of academic interest. In this regard, the predominant focus of attention has centered on the provisions relating to the use of arbitration to resolve disputes of this kind, invoking as it does the perennial international law issue of choice of jurisdiction.88 In addition, the two disputes have sparked renewed interest from legal scholars concerning ‘enforced renegotiation’, and ‘appropriate standards of compensation’.89

While the concerns expressed are perfectly valid, and have yielded valuable insights the range of issues to have been considered is necessarily restricted. In the first instance, this research seeks to complement these more narrowly focussed studies. At

See also Enron and the Dabhol Power Company, Thunderbird, The American Graduate School of Management, 2002.


the same time, this study will be different from previous analyses in two particular ways. The first difference concerns the focus of attention. In particular, this study is concerned to understand the impact of OPIC PRI on the processes (politics) of disputes resolution. Specifically what impact did the presence, as well as particular provisions of the contracts of insurance have on the bargaining strategies employed by the disputants, including the host authorities as well as of the insured investors?

Apart from the particular interest in the role of OPIC, the perspective that informs this study is broader than the range of concerns that informed these earlier studies. For example, to the extent that international law seeks to understand outcomes of ‘cases’, it does so as a product of the hierarchy of legal rules and norms. In contrast, this study is concerned with explaining outcomes from the perspective of not only legal rules and norms but also the politics of dispute resolution and rule making. That is, with the processes of diplomatic bargaining (parallel to legal processes) in the context of national foreign policy-making and thus strategic interest calculations, i.e. bilateral economic and security objectives of the home and host states.

Most immediately, the focus concerns therefore what role U.S. power, and how was this exercised? In particular, what means were utilized by the U.S. to ensure compliance with legal obligations such as threats of economic sanctions and to what effect? In the same vein, to what extent was national foreign policy-making determined by strategic interest calculations and or institutional rules governing investment disputes? In order to sustain such an explanation, the analysis will look for some level of agreement between the disputants concerning the applicable legal rules

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90 Of course, such a statement might be seen as a caricature, but it does represent a common proclivity among international lawyers and jurists to examine law and its development as a separate entity from the political process, particularly at the international level. For example, Sepulveda has written: ‘[I]n the preoccupation of international jurists to preserve the purity of international law, they abjured politics, also international, since they considered these unstable or as a dangerous, disruptive and malevolent influence, capable of contaminating the law of nations with uncertainty and infiltrating it with anarchy, for which reason a kind of asepsis for the juridical process was instinctively expected.’. See Cesar Sepulveda, ‘Methods and Procedures for the Creation of Legal Norms in the International System of States: An Inquiry into the Progressive Development of International Law in the Present Era’, (1990) 33 German Yearbook of International Law 432, p. 441. In defence of why this is typically so, Higgins explains, ‘if international law is regarded as more than rules … international law becomes confused with other phenomenon, such as power or social or humanitarian factors’. As a result, ‘only by insisting on international law as rules to be impartially applied will it be possible to avoid the manifestation of international legal argument for political ends.’ Rosalyn Higgins, Problems and Process: International Law and How We Use It, (Oxford: Clarendon Press, 1994), p.3.
and principles of international law as well as actual legal cases, i.e. precedent. Finally, what was the style of bargaining and reasoning?

While there is no suggestion that the limited number of cases will resolve the age old question concerning the relative explanatory weight of power and law in determining outcomes in international politics, permitting only contingent generalizations, it is intended that the case study research will enable us to move beyond neat but meaningless aphorisms that ‘law operates in the shadow of power.’ To this end, a study of OPIC in resolving the two case study disputes provides a valuable opportunity to better understand how contemporary and thus historically specific expressions of power—state power, the power of multinational capital, and power in law—combine to delimit economic and political risks, and ultimately, ‘markets’ for infrastructure investors in what are the second (India) and the fourth (Indonesia) most populous nations on earth.

The second significant difference concerns the method of investigation. Foremost in this respect is the use of interviews with participants, including: international organizations such as the World Bank, company representatives, local contractual obligors, legal counsel of both defendants and the plaintiffs and elected and unelected (bureaucracy) foreign policy officials charged with negotiating a solution to the disputes. Interviews are advantageous for two reasons in comparison with simply relying on the available documentary evidence, comprised of press releases, court records, arbitral hearings and confidential memos etc. Firstly, interviews are useful in establishing the facts of a case, specifically concerning behind the scenes diplomatic efforts, which are typically excluded from view. This is especially so in investment disputes involving national insurers, excluded as they are from normal public sector reporting requirements, and where contractual provisions prevent information being made public, as was the case in the two case study disputes.

92 In terms of declassified documents, the author has made two separate requests to the United States government using the Freedom of Information Act (1966), as well as using materials from two other such requests.
93 The result of this secrecy according to Thomas Waelde is that ‘with the exception of the odd press report, there is no way for governments, international organizations, or the public to track . . . the number of cases, the issues involved, and the costs to governments of awards.’ Thomas Waelde, CEPMLP, Journal of Transnational Dispute Management, Vol. 1. Issue # 02 – May 2004-05.
Second, interviews are critical in establishing the motivations underpinning actions taken by disputants. This is particularly useful in an investigation of this type, as while certain actions may be compliant with legal rules, it may not be the rule that motivates compliance.

At the same time, such an approach is not without its drawbacks, given the possibility that such interviews will be used *ex post facto* to justify certain decisions, with an eye to the historical record. The basic rule in this regard is to look for independent streams of evidence, with one confirming the other so to speak. As such, every effort has been made to corroborate interview information with that received from other interviewees as well as the available documentary evidence (public and declassified). Beyond this, however, where statements could not be verified, then this has been made clear.

Part ‘B’ of the research will address the second of the research questions concerning how best to explain shifts in the policy and practice of OPIC. In order to address the question, the research will examine the program’s evolution from 1969 wherein discussions to transfer administrative responsibility for the program from USAID to a newly created organization—OPIC—began, through until 1994. More particularly, the investigation will be split into two sections. Period one spans the years 1969-1980, while the second period will detail changes to the program from 1981-1994. This has been done in the first instance for the sake of ease but also, and as will become apparent, because the policy drivers underpinning amendments to the program were quite different in each of the two periods.

A number of factors underpinned the choice of the dates from which to begin and conclude the analysis. In this first instance, the choice to begin the study as far back as 1969 reflects the fact that the only previous analysis of the program as an instrument of U.S. expropriation policy to date concluded in 1974.94 Furthermore, that the two periods overlap also provides an opportunity to compare the explanation presented here with that of Charles Lipson’s study, while also meaning there is no gap in the legislative history of the program. Perhaps more importantly, 1994 was chosen as the date to conclude the analysis rather than a later date for two specific reasons. First,

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1994 is a particularly significant date in the history of the program, marking as it does
the program’s one-off expansion so as to facilitate the agency’s participation in the
insuring and financing of U.S. infrastructure investors utilizing the BOOT investment
model, as underpinned the expansion of CalEnergy and Enron to Indonesia and India
respectively. Second, the year 1994 represents the end-date of a period of
transformation for the agency from its original foreign-aid role to that of a foreign
trade and investment promotion function, after which time the basic policy rationale
underpinning the public provision of investment insurance to U.S. foreign investors
has remained largely unchanged. Put simply, while the program has continued to
evolve in the intervening period, the amendments enacted in 1994 established the
terms under which OPIC would insure and finance U.S. infrastructure investors as is
the primary concern of the current study.

An investigation of OPIC policy changes is assisted by the agency’s terms of
incorporation. The reason for this, apart from the fact that the agency under its terms
of incorporation must seek Congressional reauthorization quadrennially, is that any
amendment to the statutes under which OPIC operates—Foreign Assistance Act
(1961)—must be approved by Congress. Typically, this has meant that proposed
amendments are debated within designated committees, including the House
International Relations Committee and in the Senate, the Foreign Relations
Committee as well as a variety of related subcommittees. These committee hearings
thus provide the forums wherein supporters and opponents of specific amendments
are given an opportunity to present their views and make formal submissions. As
such, they also provide a unique window through which to view the program’s
evolution and more broadly social forces within the U.S. polity, as domestic interest
groups compete to influence the specific form of the program and thus the level of
support offered U.S. foreign investors.

In terms of the basic method, for each of the two periods the investigation will begin
by detailing the changes to the program resulting from the reauthorization hearings,
including an overview of both corporate and non-corporate lobbying and the
legislative history of the bills. The second task will then be to consider the evidence
with respect to the relative explanatory weight of state-initiatives and corporate
preferences in determining the program’s long-term evolution. In this regard, the
explanation of OPIC policy shifts is concerned with the following issues: first, what role have U.S. foreign investors played in determining the practices of OPIC? More particularly, which companies and or industry-bodies have been the main supporters of the program and how have they sought to impose their preferences on the policy-making process, i.e. through formal submissions or direct lobbying with their Congressional representatives? Second, which elements of the U.S. foreign policy bureaucracy have sought to influence the direction of the program and where does the program and ‘investment protection’ more broadly sit in terms of competing goals sought by U.S. foreign policy-makers vis-à-vis the developing world?

Chapter Outline

The previous section was intended to detail the methods and research techniques. This section by contrast will expand on the thesis outline by detailing the main points to be addressed in each chapter as well as the arguments to be advanced. Chapter two begins by detailing the international politics of expropriation rule making from 1945 to the present day. The second task will then be to expand on the initial sketch of competing theories of the international property rights regime, including in the latter instance those accounts aimed at understanding the effects of the ‘legalization’ of dispute settlement. Attention will then turn to U.S. anti-expropriation policy-making. The chapter will therefore firstly outline post war U.S. practice in this regard before then examining competing theories held to explain shifting U.S. policy.

The focus of attention in chapter three switches from theory to practice beginning with the dispute between CalEnergy and Indonesia. Viewed from afar, the dispute settlement process appears to epitomize the new legal orthodoxy in investment dispute settlement. The chapter seeks to challenge this view. In this regard, the chapter will show that while U.S. power was not without its limits, ultimately it was critical in underwriting the final settlement, unrelated to the ‘facts of the case’ or the strength of the legal arguments, given overarching norms of the international law of foreign investment. Thus to the extent that the outcome was consistent with existing legal obligations it is because the U.S. was able to manipulate the incentives (payoff matrix) facing Indonesia through a combination of threats and inducements sufficient
to motivate compliance. More narrowly, the evidence will show that OPIC PRI was critical in determining the bargaining strategies employed as well as the final settlement itself, including critically, the decision to litigate rather than pursue a negotiated settlement.

Chapter four examines the dispute between the Enron sponsored DPC and India. From a distance, the dispute appears to have played out in accord with the new legal orthodoxy. Once again, however, the image is misleading. To this end, the final settlement agreed in 2006 must be understood as the continuation of international power politics, central to which was a re-appraisal of the importance of the bilateral security and economic relationship between the two nations, so as to facilitate a final settlement to the long-running dispute. From the U.S. perspective, the presence of OPIC insurance was once again critical insofar as the payment of claims enabled it to sidestep a five-year long diplomatic and legal stalemate. More particularly, and as the evidence will show, in paying six claims to DPC investors the agency was able to determine the outcome according to U.S. legal statutes governing expropriation. In this respect, the presence of insurance provided the U.S. with a mechanism for extraterritorial application of U.S. law so as to violate not only the principles of international law concerning ‘corporate personality’ but with it Indian sovereignty.

Having examined the role of OPIC PRI in contemporary dispute settlement, the focus of attention in chapter five shifts to the determinants of OPIC policy and practice. That is, the long-term evolution of the insurance program. In the first period (1969-1980), the evidence will show that the program’s establishment and early evolution must be understood as driven by state-initiatives. This was not, however, part of a coherent anti-expropriation policy. Rather, the program’s long-term evolution reflected ongoing tensions between the executive and the legislative branch in the context of a series of failed attempts to reform foreign-aid spending in the context of Cold War competition for influence among LDCs. In this regard, U.S. officials showed a consistent willingness to forego corporate interests in pursuit of broader political goals vis-à-vis the developing world.

During the second period (1981-1994), the public policy rationale underpinning the program shifted from that of adjunct to the foreign-aid program to a foreign trade and
investment promotion function. Critical in this regard was the desire of U.S. officials to respond to what was interpreted as declining U.S. competitiveness in the face of intensified competition for markets and exports. And although the changes observed were beneficial to U.S. foreign investors, once again the evidence will show that corporate preferences played a secondary role to state-interests. The program’s evolution to 1994 must therefore be understood as part of a broader state-led shift in U.S. foreign economic policy towards the developing world as the U.S. sought to reverse the concessions made to LDCs during the Cold War, wherein economic interests were typically sacrificed to security concerns.

The final task for the thesis, as is the focus of the seventh and final chapter will be to draw together the findings from the two parts of the research. To this end, if OPIC PRI (and by proxy, U.S. power) is central in determining the rights and duties of U.S. infrastructure investors in the new legal order and if what OPIC does is determined by U.S. material interests unrelated to shifting international law norms then the thesis can reveal that the rules of the game (breach of regulatory contracts) should be understood as the product of U.S. power and (material) interests. Critical to which has been the desire of U.S. officials to expand markets for U.S. exporters and foreign investors in accord with evolving perceptions of U.S. national interests and configurations of power in the interstate system, but particularly the collapse of the bipolar world order.

More than this, however, the chapter will argue that in paying seven claims to U.S. investors in the two disputes, the agency’s actions serve to more firmly establish breach of regulatory contract as a violation of international law, while at the same time narrowing the scope of permissible public policy exceptions in the enforcement of arbitral awards. In this manner, international law norms of expropriation and compensation can be seen to be moving toward a uniquely American vision of private property rights as embodied in the Fifth Amendment to the American Constitution, the doctrine of ‘regulatory taking’. In this respect, the thesis reveals OPIC PRI as more than simply a risk-transfer mechanism but instead an instrument of U.S. power and interests in the new legal order, and as a conduit for the transmission of shifting property norms (regulatory taking) from the U.S. to the world economy at large.
The second part of the chapter by contrast seeks to examine the practical implications of the findings as concerns public and foreign policy-making. This will include a review of the implications for OPIC if it is to continue in its new more prominent role in dispute settlement as well as for U.S. foreign policy makers arising from the presence of insured investors, raising as it does the issue of foreign policy autonomy in dispute settlement. Attention will then shift to consider the implications for states playing host to insured infrastructure investors, including as concerns the design of regulatory frameworks and contract structures. The third and final part of the chapter will then examine the future of the practice of insuring and financing private foreign infrastructure investors.
Chapter 2: International Relations: State Power and Interests in the ‘New’ Legal Order and the Role of State Interests in U.S. Anti-Expropriation Policy-Making

The objective of this chapter is to build on the initial theory review presented in the introductory chapter concerning first, accounts of the structure and functioning of the international property rights regime, and second, explanations of U.S. anti-expropriation policy-making. To recap, the introductory chapter first outlined the postulates of realist and institutionalist approaches to understanding international politics and more narrowly shifting standards of investor protection as indicated by evolving international law norms of expropriation and compensation. Following this, the chapter briefly introduced the two competing explanations of the consequences of shifting arrangements for investment dispute settlement. The review presented here will follow much the same sequence. Rather than focus on broader paradigmatic divisions between realism and institutionalism, however, the review will detail specific accounts forwarded by scholars falling within each of the two camps. Finally, attention will then turn to the two accounts of the consequences of contemporary trends characterized by the ‘legalization’ of investment dispute resolution.

The second task for the chapter will then be to expand on the initial critique as presented in chapter one. The chapter will argue that orthodox accounts of shifting arrangements for dispute settlement overplay the extent to which the ‘legal process’ determines outcomes separate from home state enforcement dependent as it is on relative bargaining capabilities. In this manner, the approach serves to obscure the continued centrality of state power in the new legal order, i.e. the extent to which expropriation rule making is determined by international power politics. Second, and more broadly, the approach also obscures the manner in which in the judicial machinery established to resolve investor-state disputes embodies power relations where capital flows are uni-directional, as they are almost exclusively between capital-exporting states and their developing country counterparts. By contrast, the problem with critical accounts is not so much that they obscure power relations; rather, it is that they overplay the extent to which these new arrangements are beyond the state, i.e. transnational. By implication, the critical approach also obscures the extent to which states remain central in underwriting corporate expansion even in the new global economy, and in the case of infrastructure investors the national character
of MNCs. To this end, the chapter contends there is a need to reconsider the insights of a classical realist conception of international law and more narrowly the international property rights regime as founded on the political process.

The focus of the second part of the chapter by contrast will be competing accounts forwarded by scholars to explain shifts in U.S. anti-expropriation policy. The first task will be to outline U.S. anti-expropriation policy as practiced in the post war period. Having done so, the section will then outline competing explanations of shifts in U.S. policy. To recap, the introductory chapter briefly sketched Charles Lipson’s domestic politics explanation, positing as it does the centrality of corporate interests in determining OPIC policy and practice and more broadly U.S. policies to protect its foreign investors. The review presented here will expand on the initial sketch, but before doing so will introduce ‘statist’ accounts, for whom shifts in U.S. policy are understood to originate with U.S. government officials in accord with broader, hierarchically ordered, foreign policy goals.

The chapter will argue that domestic politics explanations such as Lipson’s corporate preferences hypothesis, not only obscures the central role of state officials in determining the policy and practice of the OPIC administered insurance program, but also it also serves to wrongly frame the program as a coherent response to the shifting security of foreign capital in LDCs. In this manner, the theory wrongly frames U.S. policy makers as possessing little autonomy from domestic interest groups, and second, the policy-making process as inchoate, so as to obscure the continued centrality of the ‘national interest’ in determining OPIC policy and practice (U.S. foreign economic policy). Finally, the chapter will also argue that the theory overplays the influence of institutional law norms of expropriation and compensation in determining U.S. policy and by implication underplays the centrality of material interests in state interest formation.

Before commencing, however, the first task will be to review post war struggles from 1960-2000 regarding international law norms of expropriation and compensation. The purpose of doing so is twofold. First, the overview will provide context for the subsequent theory review and second, it provides the historical context to the actual case study research immediately following this chapter.
At the end of WWII, it was widely expected that prewar property and contract rights, which held that ‘the taking of an aliens property required the state to pay prompt and adequate compensation’ would be reaffirmed. In many respects, despite the failure to ratify the International Trade Organization in 1947, initial expectations were fulfilled. That is, evidenced by the small number of expropriation disputes, the reconstituted international property rights regime remained secure throughout the 1950s. From the early-1960s onwards, however, the security of foreign capital in developing countries declined rapidly. Thus, while there were just 12 cases of expropriation of U.S. foreign affiliates from 1945-61, there would be 158 in the ensuing 12 years. Beginning in the mid-1960s the number of expropriations significantly increased, from just five in 1967, to 25 in 1968, peaking at 83 in 1975. In sum, of the more than 1,760 foreign affiliates either expropriated or nationalized between 1960 and 1979, 58 percent occurred in the five years to 1975. In terms of the geographical spread, approximately 600 were in the Middle East, 900 in Africa, with Latin America accounting for much of the remainder. Finally, while no one sector

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95 Steiner and Vagts write of the period prior to WWI that ‘despite the initial proclamation by Calvo (1871), the core principle established among European nations appeared to hold . . . ’ Henry Steiner and Detlev Vagts, *Transnational Legal Problems: Material and Text*, (Mineola, N.Y.: The Foundation Press, 1968), p. 314. Undoubtedly, the most high profile exception to the alleged consensus was the expropriation and nationalization of all foreign owned assets by the Soviet Union in 1917. Paradoxically, however, and as Charles Lipson’s cogently notes, ‘Because the Soviet expropriations were embedded in a larger program of anti-capitalist revolution, they italicized the politically deviant nature of expropriation,’ Charles Lipson, *Standing Guard* (1985), p. 83.

96 Brewer and Young tell us, the failure of the ITO in 1948 meant that the GATT rules, which were intended to be only temporary, became the main vehicle for trade talks. The problem was that unlike the ITO, the GATT did not include provisions for FDI, with the result that there were no multilateral rules governing FDI, as was the case in trade. Brewer and Young, *The Multilateral Investment System*, (2000), p. 51.

97 Although there were exceptions, the much-feared Soviet-style nationalization programs had failed to materialize. Key among the exceptions during the 1950s was the enforced renegotiation of the Saudi-Aramco agreement as well as the nationalization of British Petroleum’s ‘Anglo-Iranian’ subsidiary, in 1951 by Mohammed Mossadegh. See Daniel Yergin, *The Prize*, (1993), p. 450-478.


100 Michael S. Minor ‘The Demise of Expropriation as an Instrument of LDC Policy, 1980-1992’, *Journal of International Business Studies* vol. 25, No. 1, (First Quarter, 1994). It is worth noting that there is considerable discrepancy in the figures reported, so that where Minor identifies 1,761 instances of expropriation or nationalization, Kobrin identifies just 575 cases.
was immune, expropriations were particularly concentrated in resource extraction and manufacturing, accounting for 41 percent and 27 percent respectively of all forced divestments from 1960-1979.101

From the foreign investor’s standpoint, the attendant difficulties were further compounded by the increasing sophistication of host state rent-seeking techniques. Thus, where once nationalization was the preferred method of forced divestment, such non-discriminatory, (and high profile), techniques increasingly gave way to more selective and targeted modes of rent seeking. For example, while approximately 60 percent of all expropriations between 1946 and 1966 involved outright nationalization, by 1972-73, this figure had fallen to approximately 25 percent.102 Among the new instruments aimed at redistributing rents were the following: local equity obligations; controls on profit and principal remittances; licensing restrictions; local content requirements; the imposition of excess profits taxes (often applied retrospectively) and restrictions on transfer-pricing.103

Opposition to the traditional standards of protection and compensation provided foreign investors was not, however, limited to direct challenges to existing patterns of ownership and the distribution of economic rents. That is, opposition to the status-quo was also manifest in formal challenges to institutional rules and norms governing FDI. The United Nations (U.N.) provided the principal forum in this regard wherein developing countries enjoyed a numerical superiority over their industrialized counterparts. The earliest expression of dissent by developing states was the 1952 U.N. Declaration of ‘Permanent Sovereignty Over Natural Resources.’104 In many respects, however, this was merely the precursor to a more sustained and broad based attack on investor privileges. Thus, in December 1962, the U.N. General Assembly passed resolution 1803, ‘Permanent Sovereignty over Natural Resources.’ Where the previous declaration had sought merely to modify investor rights in their dealings

102 Quoted in Charles Lipson, Standing Guard, 1985, p. 121.
104 The declaration was significant as it proclaimed the rights of states to nationalize and freely exploit their natural resources, absent of references to traditional standards of compensation, noting only that member states ‘have due regard, consistent with their sovereignty, to the need for maintaining the flow of capital in conditions of security.’ (U.N. General Assembly Resolution 626 (VII).
with host authorities, the 1962 declaration was in comparison an overt challenge to the basic legal principles underpinning existing standards of protection. In particular, the successive declarations were notable for the manner in which standards of compensation were progressively diluted, the latter declaration prescribing only ‘appropriate payments’ absent the inclusion of ‘minimum standards’ as had typically circumscribed the legal right of states to expropriate.\(^{105}\)

Less than one decade later, a third resolution was passed proclaiming nationalization as an ‘expression of sovereign power . . . in virtue of which it is for each state to fix the amount of compensation.’\(^{106}\) Finally in 1974, the logical conclusion to the trend was reached, with the passage of the ‘Charter of Economic Rights and Duties of States.’\(^ {107}\) The charter reaffirmed the rights of states to: expropriate and/or nationalize foreign property, abrogate contractual arrangements (absent of judicial or arbitral review), and to determine disputes with foreign investors including as concerned compensation through the municipal court of the host state, thereby, signaling the beginning of a new era in core-periphery relations.\(^ {108}\) In this manner, the charter as but one facet of the New International Economic Order (NIEO) represented an unequivocal rejection of the traditional standards of investor protection.\(^ {109}\)

Of course, capital-exporting states did not simply sit idly by as standards deteriorated. The U.S. in particular made significant efforts to maintain existing rules and norms and to counter what was interpreted as ‘G77 position-taking’ in the U.N. In this regard, the Organization for Economic Cooperation and Development (OECD) served as the primary forum for capital-exporting states.\(^ {110}\) Apart from the OECD, the U.S.

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\(^{105}\) The inclusion of ‘minimum standards’ was intended to undermine LDC efforts to determine compensation subject to national standards, i.e. national-treatment.


\(^{107}\) The affect, as was the intention, was to emphasize to multinationals that they operate at the discretion of sovereign host states and this could be revoked at any point. Quoted in Charles Lipson, *Standing Guard*, (1985), p. 185.

\(^{108}\) The Charter declared that ‘every state has . . . full permanent sovereignty, including possession, use and disposal, over all its wealth, natural resources and economic activities.’ Further, the issue of appropriate compensation was to be ‘settled under the domestic law of the nationalizing states.’ Quoted in Charles Lipson, *Standing Guard*, (1985), p. 185.

\(^{109}\) The extent of the turn-around is demonstrated by the fact that of the 120 nations to participate in the vote, 104 voted in favor, while ten abstained, leaving just six states to oppose the motion. The states to oppose the Charter were the United States, United Kingdom, West Germany, Denmark, Belgium and Luxembourg. Quoted in Charles Lipson, *Standing Guard*, (1985), p. 88-89.

\(^{110}\) The OECD served as the primary forum for the advanced industrialized states in this regard, passing the Code of Liberalization of Capital Movements (1961), the Code of Liberalization of Current
also led efforts to establish the International Centre for the Settlement of Investment Disputes (ICSID) under the aegis of the World Bank Group. ICSID (1966) was intended to provide a binding and impartial forum for the arbitration of investor-state disputes, to avoid the involvement of the home country the effect of which was to exacerbate nationalistic tendencies where disputes arose. Unfortunately, ICSID was mired in ‘north-south’ politics from its inception, with the result that while eighty states ratified the convention, no Latin American states did so.112

The expenditure of diplomatic capital by the U.S. in particular failed, however, to achieve the desired objectives, resulting in little more than a proliferation of international organizations with ‘an interest in, and partial jurisdiction over’ dispute settlement, rather than as was intended to reach agreement on the basic ‘rights’ and ‘duties’ of foreign investors in their dealings with host authorities. The problem, was that while each organization could ‘appeal to the normative authority of international law’ ultimately, ‘no international body has [had] the authority to set investment rules, and none has [had] broad regulatory powers.’113

Unfortunately for developing states, these initial gains would prove temporary so as to reveal the achievements of the 1960s and 1970s, as aberrations, if not—given the symbolism manifest in the challenge itself—Pyrrhic victories. With the benefit of hindsight, the first sign of a reversal in the capacity of developing nations to act in

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Invisible Operations (1963), and the Draft Convention on the Protection of Foreign Property (1967). Thomas L. Brewer and Stephen Young contend, however that the effectiveness of the codes was weakened by the inclusion of several articles permitting exceptions to the basic principles, which in practice provided member states with significant leeway in the application of the codes. The articles reflected the failure to reach consensus on a number of significant issues, and widespread opposition from among others, Australia, New Zealand, Japan and Canada. See Thomas L. Brewer and, Stephen Young, The Multilateral Investment System and Multinational Enterprises (Oxford: Oxford University Press, 2000). Part II ‘Evolution of the System’, p. 65-79. Edward Graham agrees with the assessment of the Codes, arguing that although binding in principle, the effect was of little importance, as there were no mechanisms for enforcement, and in this regard he interprets the Codes merely attempts to codify the practices that existed between the OECD nations, and firms based within them. See Edward M. Graham, ‘Should there be Multilateral Rules on FDI?’ in John H. Dunning (ed.), Governments, Globalization and International Business, (Oxford: Oxford University Press, 1997), 481-505.

112 The problem with the ICSID is not that it has no legitimacy judging by the record of states enforcing awards handed down, rather, it is that because it is seen as relatively legitimate, states have been unwilling to submit disputes to it, so that as at 1980 only 11 disputes had been submitted to the ICSID. More recently, according to one prominent international arbitrator only on three occasions have states refused to implement an ICSID award (See Mark Kantor private research, 2004). For this reason, he opines few disputes are permitted to be heard by the ICSID by host states.
concert to frustrate the efforts of capital-exporting states aimed at forestalling further weakening of the rights of investors was apparent before the end of the 1970s. Initial evidence of this was provided in 1976 when private capital flows to LDCs fell by more than half in comparison with the previous year, thereby reversing the prevailing trend of the previous two decades.\footnote{World Bank, \textit{Global Development Finance} database: Data set for the years 1970-1999.} The fall reflected among other things the declining security of foreign capital, shifting strategies of corporate adaptation and declining demand for raw materials.

Worse still than declining rates of FDI was the growing disunity among the G77 itself.\footnote{The split was exacerbated by the divergent interests of oil-exporting and importing LDCs, following the first oil price-hike (1973) and then again in 1979.} The situation contrasted sharply with that of the early 1970s, revealing the establishment of the NIEO in 1974 as the high-water mark for LDC power and solidarity. Indeed, the reversal was swift. As early as the late 1970s developing country governments abandoned attempts to establish the Integrated Program for Commodities (IPC), which had sought to cartelize commodity production along the lines of OPEC.\footnote{Susan Strange and John Stopford with John S. Henley, \textit{Rival States, Rival Firms: Competition for World Market Shares}, (Cambridge: Cambridge University Press, 1991), p. 53. Note, OPEC always denied that it was a cartel on the basis that a cartel sought to control production and price whereas OPEC aimed only at agreeing production quotas. Moreover, in what was a sign of the times, the power of OPEC had already been weakened by the emergence of non-OPEC oil producers such as Norway and Britain, the latter of whom was producing more oil than Algeria, Libya and Nigeria combined by 1983. See Daniel Yergin, \textit{The Prize}, (New York, London: Free Press, 1992), p. 720.} Subsequent efforts to establish a ‘Common Fund’ to stabilize commodity prices, agreed at the Conference on International Economic Cooperation in 1976 also failed.\footnote{Stopford and Strange, \textit{Rival States, Rival Firms} (1991), p. 54, The Common fund was designed to stabilize the prices of eighteen commodities. The initiative failed; however, as it was not until 1986 that sufficient countries ratified the agreement for it to enter into force. Even then, however, proposals were effectively abandoned for lack of financial support by the U.S. and the U.S.S.R.} G77 disunity was further apparent in the abandonment of the U.N. ‘Code of Conduct on Transnational Corporations’ in 1983.\footnote{The negotiations foundered following failure to agree on the use of the mandatory ‘shall’ in opposition to developed country preference for the advisory ‘should’ in one section of the draft code. Quoted in Stopford and Strange, \textit{Rival States, Rival Firms} (1991), p. 54. See also Brewer and Young, \textit{The Multilateral Investment System} (2000), p. 109, Appendix 4.2 for a list of the provisions of the Draft Code. Discussions for the drafting of a comprehensive U.N agreement on a code of conduct for Transnational Corporations were conducted under the aegis of the UN Economic and Social Council (ECOSOC) under resolution 1721, dated March 1972.} The result was that after more than a decade of negotiations, all that remained to regulate MNCs were the non-binding and thus largely hortatory OECD ‘Guidelines for Multinational
Enterprises’ (1976), and the International Labour Organization’s voluntary labour-codes.\textsuperscript{119}

The failure of LDCs to ratify the U.N. code on multinational corporations was, however, merely the forerunner to a more damaging turn of events for LDCs, following the announcement by Mexico of a moratorium on all debt payments that same year, so as to signal the beginning of the LDC debt-crisis. In hindsight, signs of a reversal in the fortunes of LDCs were evident much earlier than 1983, beginning with the rapid buildup of debt from the late 1970s, as developing country governments sought to supplement declining private investment inflows by borrowing in the international capital markets to fund national economic development.\textsuperscript{120} To this end, the strategy was aided, initially at least, by the historically low cost of borrowing because of the excess of petrodollars following the first OPEC oil price rise in 1973.\textsuperscript{121}

The easy availability of credit on international capital markets, with loans to LDCs peaking at more than four percent of GDP in 1980, masked growing structural imbalances in the external accounts (trade and capital account = current account).\textsuperscript{122} The reversal was underpinned by a combination of factors, including reduced demand for raw materials, and a decline in the terms of trade for primary producers.\textsuperscript{123} This was further exacerbated from 1980 as the U.S. Federal Reserve raised interest rates (peaking at 21 percent) in an attempt to rein in rising inflation in the U.S. as well as to attract foreign capital to finance spiraling U.S. budget deficits.\textsuperscript{124} As a result, the cost

\textsuperscript{120} See \textit{Global Development Finance}, World Bank, 2004 Tables, Calculated from database.
\textsuperscript{121} Susan George has calculated that real interest rates (nominal rates less inflation) for LDCs (excluding China) averaged –0.8 percent during the 1970s. Susan George \textit{A Fate Worse Than Debt}, (London: Penguin Publishers, 1988), p. 197.
\textsuperscript{123} See Table 5.6 World Macroeconomic Indicators, ‘Brazilian Debt Crises: Past and Present’ Eliana A. Cardoso and Rudiger Dornbusch, in Barry Eichengreen and Peter H. Lindert (eds.), \textit{The International Debt Crisis in Historical Perspective} (Cambridge, Mass.: MIT Press, 1989), p. 126. For non-oil exporting LDCs the effects of the shift were dramatic. For example, William Cline calculated that increases in the cost of oil during the 1970s meant an effective increase in the cost of oil-imports for non-oil exporting LDCs between 1974 and 1992 of $260 billion. Quoted in Susan George, \textit{A Fate Worse Than Debt} (1988), p. 28.
\textsuperscript{124} Most LDC loans were agreed on as variable rate loans tied to the London Interbank Overnight Rate (LIBOR), hence when interest rates rose, so too did the cost of debt service.
of debt servicing increased from just $7.7 billion in 1975 to $32 billion by 1980, peaking at $61 billion in 1988. Moreover, the effect of increased debt payments was further compounded by corporate disinvestments in LDCs by foreign investors equivalent to $109 billion from 1970-1987. As a result, by October 1983 just three months after the announcement of the Mexican debt moratorium a further 27 LDCs had requested some $239 billion of debt be rescheduled.

The scale of the debt crisis to engulf many LDCs was unparalleled. For LDCs, the difficulties of pursuing export-led recovery were compounded by the poor performance of many newly nationalized industries. Moreover, the simultaneous imposition of export-led recovery strategies served to worsen the terms of trade, with the Commodity Index falling to 66 in 1986, the lowest point since records began in 1957. That same year LDC debts passed the symbolically significant $1 trillion mark.

The contrast between the position of LDCs vis-à-vis private foreign investors and capital-exporting states in the mid-1980s compared with that of the previous two decades was stark. Perhaps most telling in this regard concerns the increased role of the International Monetary Fund (IMF). Thus, where as late as 1978 LDCs repaid

126 World Bank, Global Development Finance, 1999 (figures calculated from GDF, 1999). The effect was further compounded because as debt levels rose borrowing terms worsened with the result that average maturities on private commercial debt fell rapidly from an average of 10.9 years in 1973 to just 4.6 years in 1977. See Jane D’Arista ‘Private Overseas Lending, Too Far Too Fast’ in Jonathan Aronson (ed.), Debt and Less Developed Countries, (Boulder, Colorado: Westview Press Inc., 1979), Table 4 and Table 5, p. 71-75.
130 Susan George A Fate Worse Than Debt (1988), Chapter 1: ‘How Much is $1 trillion?’, p. 11-29.
131 The Mexican bailout coordinated by the IMF became the model for other major debt workouts. The terms were as follows: the IMF provided $1.3 billion, OECD governments $2 billion (primarily the United States), while the commercial banks somewhat reluctantly agreed to provide new loans of $5 billion. In return, the IMF imposed what would become known as a ‘Structural Adjustment Plan’ (SAP) on Mexico aimed at reducing government expenditure and increasing revenues through export led economic growth. The critical features of the Mexican SAP were: devaluation of the Peso; cuts in central and state government fiscal expenditure through elimination of fuel and food subsidies, privatization of state-owned enterprises and or deregulation of markets through the abolition of price
to the IMF $500 million more than was borrowed, from 1982-1992 the IMF instituted structural adjustment plans (SAPs) in more than 80 developing countries. Moreover, despite perilous financial positions, and despite the high social and political costs of IMF adjustment programs, of the 144 instances of debt rescheduling that took place in the decade to 1985, only a handful of countries unilaterally suspended debt obligations. In addition, of those that did, most recanted once the realities of the situation became clear.\textsuperscript{132}

Saddled with debt, LDCs could do little to halt OECD government efforts to reverse the trend of the previous two decades by strengthening the legal rights of foreign investors. Thus, in 1984 the OECD modified the 1977 ‘Guidelines for Multinational Enterprises’ by strengthening the right of establishment provisions where earlier efforts had stalled for fear of offending LDCs.\textsuperscript{133} Although voluntary and applicable only to member-states, Brewer and Young cogently note that these early, ‘OECD agreements . . . became important building blocks during the concerted efforts of the 1990s to develop more encompassing multilateral agreements on investment issues.’\textsuperscript{134}

Efforts of capital-exporting states to strengthen the treaty framework for foreign investors were not limited to the OECD, however. Foremost in this respect concerned the proliferation of BITs, which from the mid-1980s ‘emerged as the principal form of investment agreements for FDI issues.’\textsuperscript{135} The use of BITs is noteworthy apart from their being negotiated bilaterally because they explicitly incorporate the principles of

\textsuperscript{132} Susan George, \textit{A Fate Worse Than Debt} (1988), p. 59. For example ‘In early 1986 Latin debtor governments had hammered out a more aggressive unified position. A press conference was called for the next morning to announce unilaterally determined measures. During the night the Mexican representative received pressing telephone calls from Washington; he was informed that Mexico should expect no new loans from any US bank, northern government, or multilateral agency if it persisted in joining this declaration. Next morning Mexico’s representative was nowhere to be found, support for the measures crumbled and the press conference was called off.’ p. 213.

\textsuperscript{133} For Hamilton, the OECD guidelines were the product of strong U.S. pressure aimed at countering developing country position taking at the U.N. designed to curb the expansion of U.S. MNEs. Quoted in Thomas L. Brewer and Stephen Young, \textit{The Multilateral Investment System} (2000), p. 90 and p. 55.

\textsuperscript{134} Brewer and Young, \textit{The Multilateral Investment System} (2000), p. 74. Apart from the manner in which the OECD code set the agenda for LDC and OECD member negotiations on FDI rules the most direct link between the earlier OECD codes and later FDI discussions was the failed Multilateral Agreement of Investment (MAI), negotiations for which were abandoned in 1998.

\textsuperscript{135} Brewer and Young, \textit{The Multilateral Investment System} (2000), p. 74 and p. 78. The first BIT was signed in 1959, but it was not until the mid-1980s that their use increased.
investor protection agreed as part of the OECD code, including the expanded
definition of property to include tangible and intangible property as well as
strengthening investor rights with respect to ‘national treatment’ and ‘unrestricted
profit remittances.’ Moreover, although national models differed slightly, almost
without exception, these treaties expressly provide for binding commercial arbitration,
and the subrogation of insurance claims, provisions once deemed by LDCs an
inimical to their development aspirations and sovereignty.

In hindsight, the inclusion of strengthened investor protection in bilateral treaties was
merely the forerunner to more expansive efforts, aimed at promulgating similar
conventions in multilateral treaty making forums, beginning with the Uruguay Round
of GATT trade talks in 1986. Once again, while the specific provisions are important
insofar as they extended investor rights in dealings with host governments’ what is
perhaps more significant is that capital-exporting states, led by a combination of
‘Western (mainly U.S.) corporations and governments’ were able to include
discussion of a number of critical FDI related issues in the negotiations. The inclusion
of which had been successfully resisted on previous occasions.

Foremost in this regard was the Agreement on Trade Related Intellectual Property
(TRIPs), pursuant to the conclusion of the Uruguay Round in 1994. The agreement,
governing all cross-border transfers between parents and affiliates provided for: ‘the
establishment of uniform standards for national laws for the protection of intellectual
property, including patents, copyrights, trademarks, industrial designs and designs of
integrated circuits, as well as the establishment of procedures for judicial settlement
and enforcement of TRIPs disputes. The second significant measure was the
Agreement on Trade Related Investment Measures (TRIMs). Previously developing
countries had successfully resisted an agreement on TRIMs in the Tokyo Round
(1973-1979) of GATT trade talks, arguing that such measures constitute a useful tool

136 For a fuller discussion of the provisions of BITs, and their effects, as well as examples of different
BITs, See M. Sornarajah, The International Law on Foreign Investment (2004), p. 239-274.
in FDI entry negotiations with MNEs to counter restrictive business practices and as part of ‘industrial policies’ aimed at protecting infant-industries.138

On the bright side for LDCs, the early 1990s witnessed a nascent recovery, as interest payments on debt steadied at approximately $60 billion p.a. 139 Perhaps the most telling sign of recovery concerned the steadily increasing volume of FDI, which outpaced corporate profit remittances in 1988 for the first time since 1970. Thereafter FDI levels continued to climb steadily reaching $34 billion in 1991 and $88 billion in 1994.140 This was also aided by the reemergence of fixed-income debt issues as LDCs reentered the bond market, new issues climbing from $1.1 billion to $38 billion from 1991-1994.141 More than a decade of under investment in infrastructure and industrial markets meant, however, the need for new sources of investment capital was no less pressing.

In consequence, almost without exception, LDC governments in an ever-intensifying competition for capital began in earnest to dismantle what were once vigilantly guarded legislative barricades against FDI. For example, in the four years to 1994, an average of 46 countries (LDCs) per year introduced changes to the regime for FDI, the net effect of which was to liberalize ‘entry requirements’ and strengthen standards of investor-protection.142 The magnitude of the reversal in the fortunes of capital-importing states is underscored by the falling incidence of expropriation. For instance, UNCTAD calculated that while there were 336 cases of expropriation and nationalization from 1970-75, there were just fifteen from 1980-85.143 These figures are supported by Michael Minor, who found that where between 1976-1979 there were 21 incidents of expropriation per annum in LDCs, the annual average rate fell to

138 Quoted in Brewer and Young, The Multilateral Investment System (2000), p. 121 and 124. As they cogently note, ‘[B]y the early 1980s, however, the political and analytical conditions that had deterred GATT from addressing investment issues in the past were much less problematic.’ p. 122.
141 World Bank, Global Development Finance. These changes included: removal of foreign ownership restrictions, including limitations of maximum share ownership; liberalization of approval procedures for FDI applications, government guarantees and the removal of restrictions on profit repatriation and proceeds from asset divestitures.
143 Quoted in Brewer and Young, The Multilateral Investment System (2000). While the falling rate of expropriation disputes in the second period can be accounted for in part by the large number of expropriation and nationalizations in the previous period, the changing incidence must also be held to reflect the changing environment for FDI more broadly.
just 2.5 per year for the years 1980-1985, while there were no cases of expropriation from 1986-1992.\textsuperscript{144}

Falling rates of expropriation did not however forestall further attempts to the strengthen property rules on behalf of foreign investors. In contrast to earlier efforts centered on the WTO, after 1995 the focus of attention once again shifted to the OECD. Thus in May 1995, after five years of preparatory work, formal negotiations commenced concerning the Multilateral Agreement on Investment (MAI). The MAI had it been passed would have created a comprehensive binding agreement codifying the rights and duties of foreign investors as well as dispute settlement procedures. Right from the beginning, however, the negotiations were characterized by broad disagreement, with a number of states seeking ‘carve-outs’ to protect sensitive industries, while there was general criticism of the fact that developing states were assigned observer status only, an attitude that was widely interpreted as paternalistic.\textsuperscript{145} Thus, having submitted a draft text to the OECD Ministerial Council in May 1998, the negotiations were abandoned in October that same year, following the withdrawal of the French government.

While debate continues to the present day as to the reasons for the failure, what is clear is that the failure of the MAI some forty years after the failure of the ITO meant, as at 2000 there was still no comprehensive agreement providing clear and consensually defined rules governing FDI and dispute settlement. Instead, the rules of the game emerge from an overlapping patchwork of bilateral, multilateral, and regional treaties, each prescribing different and sometimes conflicting rights and duties for foreign investors and host states. And while the lines of demarcation between North and South, or expressed differently between capital-importing and exporting states, are no longer as clear as they once were, as is exemplified by the position of the United States as the largest source and recipient of FDI, it remains the


\textsuperscript{145} Brewer and Young, \textit{The Multilateral Investment System} (2000), p. 275-76.
case that traditional divisions remain as important today as they ever were. Moreover, the prospects of concluding a comprehensive agreement appear only to have worsened following a backlash against further market liberalization among domestic constituencies in the capital-exporting states, leading to the abandonment of efforts to launch a new Millennium Round of WTO trade talks. With the momentum of the mid-1990s having dissipated, and in the absence of a renewed commitment to multilateralism, it would therefore appear that investors and host states will need to muddle through what is a morass of conflicting standards for the foreseeable future.

To conclude the narrative account, the years spanning 1960-2000 can be divided into two distinct phases. In the first period, circa 1960-1980, the rate of expropriation disputes reached unprecedented levels, as LDCs sought to redistribute economic rents and with it the terms of their engagement with the world economy more broadly. Widespread nationalization was also accompanied by a weakening of the traditional standards of protection afforded foreign investors. This included in legal terms, an expanded conception of the right of Eminent Domain, as the legal basis for expropriation, the dilution of ‘minimum standards’ in favour of the right to ‘national treatment’ and lowered standards of compensation. Viewed from the perspective of the mid-1970s, it appeared that the meaning of expropriation had forever changed so that ‘[W]hat was once a symbolic, highly-charged issue—marked by uncompromising appeals to sovereign rights and legal obligations—became rather a matter of dividing and preserving economic gains.’

In the second period by contrast, the pendulum swung back in favour of foreign investors. The shift was manifest most obviously in the dramatic fall in the incidence of investment disputes. Once again, however, shifting patterns of expropriation were merely the forerunner to changes to the rules governing FDI and dispute settlement. Thus, where from 1960-1980 the right of states to expropriate and nationalize as provided for under the principle of Eminent Domain was expanded, from 1980-2000 it once again narrowed. In practice, this meant a shift from ‘national treatment’ to clauses prescribing ‘minimum standards of treatment’ as prescribed by ‘international

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146 Evidence in support of such an assertion is provided by the trenchant opposition to further liberalization from demonstrators at the 3rd WTO Ministerial Conference in Seattle in late 1999, dubbed the ‘Battle of Seattle.’
law.’ In the final analysis, although the changes described were not radical, being better viewed as an evolving bargain, by the late 1990s it was nonetheless clear that successive efforts undertaken by capital-exporting states had succeeded in creating a multilayered treaty framework of bilateral, regional and multilateral treaties, the net effect of which was to strengthen international property and contract rights on behalf of private foreign investors in the developing world.

Thus far, the chapter has sought to detail the shifting environment for direct investors in LDCs. By contrast, the next part of the chapter will outline the competing accounts of the causes and consequences of the observed changes.

*Reconsidering the Role of State Power and Interests in the ‘New’ Legal Order*

Thus far, no specific attempt has yet been made by IR scholars to investigate the role of national investment insurers, including OPIC, in investor-state dispute settlement and the new legal order more broadly. This can be contrasted with a number of legal studies, focussed on the agency’s ‘jurisprudence’ as well as a smaller number of studies concerned to assess the developmental impact of the program. In the first instance, the research seeks to fill this lacuna in the body of IR theory. There is, however, within the corpus of IR theory a substantive body of work that seeks to understand the role of state power and interests and legal norms in delimiting the outcomes of disputes and thus shifting standards of investor protection.

To recap, the dominant approach to understanding international politics and more specifically the international property rights regime, realism, holds that in the absence of an overarching sovereign (supra-national authority) capable of enforcing stable and effective property rights at the international level, then property rules, and the distribution of economic rents arise from bilateral bargaining between self-interested

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and ‘rational’ sovereign states. For Robert Gilpin, in accord with realist precepts, the spread of FDI from the 1950s must be understood as a product of the U.S.’s capacity and willingness to underwrite stable and effective international property rights, i.e. U.S. hegemony, consistent with its own self-interests and as part of the construction of an international order in its own self-image (Pax Americana). The primary tool utilized by the U.S. in this regard was the suspension of bilateral aid to expropriating states. In this respect, Gilpin did not seek to deny the importance of technological factors in the spread of multinational capital. Instead, ‘economic and technological factors have been able to exercise their profound effects because the United States—sometimes with the cooperation of other states and sometimes over their opposition—has created the necessary political framework for economic interdependence and corporate expansionism.’

The problem in short, however, concerned the fact that contrary to initial expectations, declining U.S. power did not presage the collapse cross-border direct investment in LDCs. Moreover, the state power centric focus of the theory was at

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149 The condition of anarchy is not equated with disorder, however. Instead, it refers to the absence of an overarching legitimate authority, above the units of the system – states. For this reason, international and domestic politics are understood as qualitatively different and, thus analytically separate domains. Second, in making this statement, realists’ do not contend that all state action is rational, rather, the statement reflects the belief that individual states must behave rationally in the main because if they do not and other states do, their survival and independence will be threatened. Moreover, realism tells us despite capital-exporting states sharing an interest in stable property rights, the condition of anarchy forces states to prioritize relative gains over absolute gains, with the result that coordinating sanctions among self-interested states is extremely difficult. For the classic Realist informed theoretical statement to this effect see Joseph M. Grieco ‘Anarchy and the Limits of Cooperation: A Realist Critique of the Newest Liberal Institutionalism’ and for the neo-liberal institutional response that contends that states can overcome the relative gains problem through institutions See Helen Milner, ‘The Assumption of Anarchy in International Relations Theory: A Critique’ both in David A. Baldwin (ed.), Neorealism and Neoliberalism: The Contemporary Debate (New York: Columbia University Press, 1993).

150 Robert Gilpin, U.S. Power and the Multinational Corporation: The Political Economy of Foreign Direct Investment (New York: Basic Books, 1975). The theory has been widely criticized for promoting the status quo, i.e. equating the U.S.’s role as system enforcer in the world economy as a ‘public-good.’ For criticism of the theory applied to international property rights, specifically their characterization as a public good See Duncan Snidal, ‘Public Goods, Property Rights, and Political Organizations’ International Studies Quarterly 23 (December 1979), 532-566.

151 The U.S. passed the Johnson-Bridges Amendment (1959), the Hickenlooper Amendment (1962) and the Gonzales Amendment (1972 and repealed one year later in 1973) all of which provided for the suspension of aid to expropriating states. The Hickenlooper amendment was only applied twice, in Ceylon (Sri Lanka) in 1962, and again the following year against Ethiopia. The purpose of the Gonzales amendment was to remove Presidential discretion in the application of sanctions. See Charles Lipson Standing Guard, chapter five ‘Foreign Aid Sanctions and Investment Protection’ (1985).


153 Foremost in this regard concerned the changing structure of international production, as the U.S.’s share of total world production fell. Of particular import was the U.S.’s declining share of total manufacturing output, which declined from 60% in 1955 to just 43% by 1972. As its share of total
odds with the demonstrated capacity of ostensibly small, weak states to overcome powerful capital-exporting states in expropriation disputes. This observation served to stimulate a new research program centered on the effects of international regimes in facilitating cooperation among self-interested states and thus the maintenance of an open international economic order, *(After Hegemony)* dubbed ‘regime theory.’

The insights of regime theory were incorporated into the next major work seeking to explain shifting standards of protection afforded foreign investors in LDCs, Charles Lipson’s *(Standing Guard)* (1985). For Lipson, no matter how important state power might be it cannot explain changes to the institutional rules governing dispute settlement. More significantly, for Lipson, the task of enforcing property rules has always been a joint-effort, undertaken by states and private investors. He writes, ‘the regulation of foreign investment has always been a many-sided contest involving international organizations, host states, home states and multinational investors.’ Of critical importance in determining the efficacy of both public (state) and private (market) sanctions is the degree to which power is concentrated. Hence, for Lipson,

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156 For Lipson, the inclusion of public and private sanctions is worth the additional complexity because it enables him to explain the divergent treatment (security) of direct and portfolio investment capital during the 1970s. In particular, he ascribes the greater security of portfolio capital in LDCs to the fact that because financial markets are better integrated, their collective capacity to impose (coordinate) effective sanctions is greater, hence the divergent treatment of the two modes of foreign investment.


158 To which he adds in the case of market-power, secondary variables such as the maturity of the technology utilized, whether the investment is in manufacturing or natural resource extraction, and finally, whether the creditor operates in financial or industrial markets.
The weakening of standards of investor protection during the 1970s reflected not only the diffusion of state power but also the erosion of oligopolistic market structures as European and Japanese MNCs began to challenge the dominance of U.S. investors, which in turn reduced their capacity to punish perceived transgressions by withholding capital and technical expertise.\(^{159}\)

The second significant difference between Lipson’s account and what he dubs the ‘basic-force’ model concerns the explanatory weight assigned to institutional rules and norms in delimiting outcomes. From this perspective, the rules and norms of the institution developed over time through practice as well as formal treaty obligations serve to delimit acceptable bargaining strategies and thus the outcomes of disputes. They do so because the rules and norms ‘furnish a common baseline for expectations’ regarding appropriate behaviour by disputants. In support of the assertion, he claims that irrespective of host state economic structures ‘negotiations are almost always limited to compensation’ rather than debating the legitimacy of the host state’s right to expropriate, excepting of course the most capricious seizures.\(^{160}\) More generally, however, for Lipson that the changes to the property rights regime during the 1970s were norm governed is held to be somewhat self-evident, owing to the fact that shifts in the underlying configuration of state power (decline of U.S. power) did not presage the collapse of the institution.

The second institutionalist account forwarded was Kenneth Rodman’s *Sanctity Vs. Sovereignty* (1988).\(^{161}\) Rodman proposed his ‘weak-cognitivist’ or alternatively sociological account of the regime explicitly as a supplement to what he dubbed more ‘traditional legal-institutional accounts.’ His account departs from Lipson’s in two specific ways. First, while U.S. power in enforcing international property and contract

\(^{159}\) For example, Raymond Vernon measured this trend for the period 1950-1975 using the Herfindahl Index, noting that concentration ratios fell in all the major commodity markets, as well as key consumer markets. The Index measures market concentration by adding the squares of the market share of individual firms operating in that market. See Raymond Vernon, *Storm over Multinationals: The Real Issues* (Cambridge, Mass.: Harvard University Press, 1977), p. 81. Another notable trend during this period that served to undermine traditional property rules was the transformation in the composition of the stock of FDI in LDCs, as the focus for investors’ increasingly turned to manufacturing away from extractive resource investments. The significance of this is two-fold, first manufacturing covers a bewildering array of products, second manufacturing and extractive investments share few overlapping interest, thereby compounding the difficulties of coordinating private market sanctions against expropriating states. Quoted in Lipson *Standing Guard* (1985), p. 158.


rights is still significant, for Rodman the task of protecting foreign investments has historically speaking been the preserve of private foreign investors rather than home states. He writes of the concession regime, the ‘rules were enforced by the bargaining power of a small number of vertically integrated MNCs, reinforced by American economic power where necessary.’

The second departure concerns the basis for regime rules. Thus, where Lipson interprets the durability of institutional rules as reflecting norms concerning the role of the state in economic development, for Rodman, the cognitive basis reflected the following: the shared experience of interwar economic stability, adherence to neo-classical economics and Lockean precepts concerning private property. He writes ‘despite the erosion of a tight regime, a discernable pattern of norms, rules, and expectations persisted.’ That this was the case, is interpreted by Rodman as signalling the shared belief that while the interests of capital-exporting and importing states may on occasion diverge, ultimately ‘the global rule of law—in this case, the sanctity of contracts—was equated with a public good.

More recently, the image of investment dispute settlement and the international property rights regime derived from realist and institutionalist accounts, has been challenged in the wake of economic globalization. In particular, changes associated with advances in information and communications technologies, shifting production structures associated with the transition from multinational to transnational production networks and the integration of global financial markets are understood to create a dissonance between economic and political spaces, with the result that the power and

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163 Kenneth Rodman, *Sanctity Vs. Sovereignty* (1988), p. 16. In referring to a Lockean conception of the state and private property, Rodman is referring to what Isaiah Berlin terms negative liberty that he himself derived from Kant. Negative liberty, as enshrined in the American Constitution, provides for a space in which the individual is free to pursue actions of his own volition. It merges with notion of private property in the American constitution in the protection of private property as the domain of the individual against the state. The critical point made by Berlin was that, negative and positive liberty are not merely two distinct kinds of liberty; they can be seen as rival, incompatible interpretations of a single political ideal that defines the relation of the individual to the collective, i.e. the fundamental means of ordering societies. See ‘Two Concepts of Liberty’ in I. Berlin, *Four Essays on Liberty*, (London: Oxford University Press, 2002).

Applied to contemporary developments within the international property rights regime, characterized by proliferating FDI related legal obligations, two explanations can be identified, including orthodox and critical perspectives. The two accounts can be differentiated according to the theorized causes and consequences of the ‘legalization’ of investment dispute settlement, and ultimately, as will become apparent, their conception of the international law of foreign investment itself.

The neo-liberal institutionalist or orthodox perspective is exemplified by Legalization and World Politics (2001), the main focus of which is the consequences of ‘legalization’, rather than its causes.\footnote{See also Robert O. Keohane, Andrew Moravcsik and Anne-Marie Slaughter ‘Legalized Dispute Resolution: Interstate and Transnational’, in Goldstein, Kahler, Keohane, and, Slaughter, (eds.), Legalization and World Politics (2001). See also Anne-Marie Slaughter, ‘Governing the Global Economy through Government Networks’, in Michael Byers (ed.), The Role of Law in International Politics (2000), p. 177-205. By the same author See also ‘Breaking Out: The Proliferation of Actors in the International System’, in Yves Dezalay and Bryant G. Garth (eds.), Global Prescriptions: The Production, Exportation, and Importation of a New Legal Orthodoxy, (Ann Arbor: University of Michigan Press, 2002), p. 12-36.} For its authors, shifting institutional arrangements for dispute settlement, underpinned by the explosion of FDI related treaties (bilateral, multilateral, sectoral and regional), providing as they do for the delegation of judicial authority to resolve disputes, serve to transform the traditional dynamics of international investment dispute resolution and law making. In particular, these new arrangements serve to uncouple the link between underlying state power and outcomes thus presaging the emergence of transnational dispute settlement. In this manner, investment dispute resolution is understood to be moving away from traditional patterns of institutionalized interstate bargaining towards a rules-based system of governance.

The reason for this, they contend, is that legal rules produce different patterns of politics than do non-legal institutional rules. They do so because governing the
various treaty rules is the fundamental international legal principle of *pacta sunt servanda*. That is, although the parties may disagree about the interpretation of a rule, or its application, legal rules prohibit ‘discussion of issues purely in terms of interests or power.’ They do so, because the invocation of legal rules, ‘implies a discourse primarily in terms of the text, purpose, and history of the rules, their interpretation, admissible exceptions, applicability to classes of situations, and particular facts.’

More specifically, three variables are held to determine the extent to which dispute settlement will be legalized, including: the degree to which rules are obligatory, the precision of those rules, and the extent to which the functions of interpretation, monitoring, and implementation are delegated to a third party. Delegation to third parties to resolve disputes through the application of general legal principles and specific legal rules is the key variable from this perspective, because the ‘act of delegation means that disputes must be framed as “cases” between two or more parties, at least one of which—the defendant—will be a state or an individual acting on behalf of a state’ while the plaintiff can be either states or private parties.

Finally, they contend that delegation will have the greatest effect on the ensuing ‘politics of dispute resolution’ where the investor is granted the right to directly access or initiate arbitration, thereby obviating the need for home state diplomatic protection and by extension, the conflation of political aims with the ‘facts of a case.’ From this perspective, the international institution for investment dispute settlement is highly legalized, and increasingly transnational in character.

Critical approaches overlap with more conventional accounts to the extent that both emphasize the manner in which the provision of access and the act of delegation serve to transform the politics of dispute settlement, with the result that ‘State-based, positivist international law and “public” notions of authority are being combined with

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168 The doctrine they contend prescribes that the ‘rules and commitments contained in legalized international agreements are regarded as obligatory, subject to various defenses or exceptions and not to be disregarded as preferences change.’ Goldstein, Kahler, Keohane, and Slaughter (eds.), *Legalization and World Politics* (2001), p. 25.


or, in some cases superseded by non-state law, informal normative structures, and private economic power.\textsuperscript{171}

More than this, for Cutler, these new arrangements are significant because they serve to transform not only the balance of public and private authority with respect to the creation of commercial law norms, but in a very real way the rights and duties of foreign investors and host states. That is, because private international trade law does not recognize the distinction between states and investors and \textit{subjects} and \textit{objects} of law respectively then arbitral tribunals can apply a different interpretation of contractual sanctity and thus the doctrine of \textit{Clausula rebus sic stantibus} as the corollary doctrine to \textit{pacta sunt servanda}.\textsuperscript{172} The practical effect being to narrow the range of permissible public policy defences, thus expanding the scope of those actions taken by the host state that may be considered a violation of international law.\textsuperscript{173}

While the two accounts broadly concur with respect to the significance of the growing use of arbitration, critical accounts depart from what Cutler terms liberal or orthodox approaches in two particular ways. First, the move to offshore arbitration is

\textsuperscript{171} Claire A. Cutler, \textit{Private Power and Global Authority} (2003), p. 1. For Cutler, while the result is the creation of a transnational legal system at arms length from states (public control and authority), it is significant to note that in many instances governments are not just complicit in this process but actively support it, and not just capital exporters. In particular, governments in the developed world have participated in the construction of a new legal order by limiting their powers of review of arbitration decisions whilst simultaneously committing themselves to enforcement and execution of foreign arbitral awards.

\textsuperscript{172} The doctrine of \textit{clausula rebus sic stantibus} holds that states may rescind treaties where the circumstances in which the treaty was signed have changed so as to make performance of said obligations injurious to the state concerned. It was first articulated by the Italian jurist Alberico Gentili more than four centuries ago. See Philip Bobbitt, \textit{The Shield of Achilles: War, Peace and the Course of History} (London: Penguin Books, 2002), p. 496-500. While some may doubt its applicability to investment related treaty making, it is as Hedley Bull explains a vital principle of international law. He writes of the addendum: ‘This is a doctrine which is sometimes said to be an invitation to international lawlessness, but in the view of nineteenth century positivists it provided a means of securing some place for international agreements in the historical process, while also coming to terms with the forces of change.’ Hedley Bull, \textit{The Anarchical Society: A Study of Order in World Politics} (1977), p. 35. The doctrine is included in the Vienna Convention on the Law of Treaties (1969), Article 62.

understood as but one facet of a more fundamental transformation in global politics presaged by the construction of a transnational legal order, itself associated with the emergence of transnational corporations, and a global political economy, i.e. the transnationalization of capitalism. For Cutler, the new transnational legal order is working significant transformations in governance arrangements, the effect of which is to blur the boundaries between public and private authority.

More particularly, the emergent transnational legal order is associated with three major trends in contemporary governance arrangements. The first of these is the *juridification* of political, social and economic life as legal and judicial concepts, institutions and ideologies are used with increasing intensity, in terms of the expanded scope of their application so that they penetrate ever deeper into national and local legal, social and political orders, so as to substantiate and legitimate claims to private political authority. The second is increasing *pluralism* in sources and subjects of international law while the third, is the enhanced significance of *privatized* governance arrangements.

The second significant departure from orthodox accounts is that for critical theorists, the emergence of a transnational legal order is significant because it provides norms, practices and a common language that binds together an emergent global corporate elite, the *mercatocracy*. The mercatocracy is comprised of transnational merchants, private international lawyers, and other professionals and their associations, government officials, and representatives of international organizations: the national affiliations of who are being replaced by a shared interest in the unification and harmonization of transnational merchant law and with it the creation of a borderless (global) economy.174 From this perspective the emergent transnational legal order serves as a crucial mediator of domestic and global political/legal orders and thus as a constitutive element of economic globalization. It is so because it provides the constitutional foundations of the global political economy through rules governing the

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protection and enforcement of private property and contractual rights and obligations across a range of international commercial activities.  

The previous section was intended to outline competing accounts of the international property rights regime. By contrast, this next section will expand on the initial critique of the two theories of legalized dispute settlement. The fundamental weakness of the orthodox approach is the manner in which it obscures the continued centrality of state power in the new legal order and by extension the inter-national politics of expropriation rule making. More particularly, the theory assigns too great an explanatory weight to the twin variables of access and delegation at the cost of a proper understanding of ‘embeddedness’ to adopt the nomenclature employed or more simply home state enforcement, dependent as it is on relative bargaining capabilities. Second, the theory overplays the extent to which the provision of access and delegation serve to transform inter-national dispute settlement into transnational absent independent enforcement mechanisms. In short, enforcement remains the key variable in determining the politics of dispute resolution.

In making this criticism of the legalization hypothesis, while the intention is not to be drawn into legal meta-theory debates arising from the question of whether international law is really law at all, the problem with the theory is that because it portrays law as separate from politics and power and because it denudes law of its normative content and therefore sanction, compliance must be explained as a product of the legal process. And although the authors of the theory explicitly note that their conception of international law draws on that of H. L. A. Hart so as to emphasize law-as-process, the effect is to elevate ‘process’ to unsustainable explanatory heights where the settlement of investor-state expropriation disputes is concerned.

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177 See H.L.A. Hart, ‘International Law’ in Robert J. Beck, Anthony C. Arend, and Robert D. Vander Lugt, *International Rules, Approaches from International Law and International Relations* (New York: Oxford University Press, 1996), p. 75-98. For Hart, who sought to rebuff the criticisms of law from neo-realists who sought to deny international law the status of law, ‘it’s not what judges do, Hart told us; it is how they do it. Granting the Legal Realists argument that assessing the substantive fairness of a particular outcome is a matter of ideology; Hart’s approach holds that fairness will nevertheless result
Perhaps more fundamentally, however, concerns the fact that the theory obscures the manner in which power is embodied in these new arrangements, but particularly, the growing use of offshore arbitration and private international trade law to resolve disputes. The point is forcefully made by Sornarajah, who writes ‘[T]he argument is that, as a result of an accumulation of arbitral awards and the consistency with which arbitrators have adopted certain doctrines, a system of law applicable to transnational business disputes has now been created.’ He continues, ‘[T]here are many defects with this thesis’ including, ‘[T]here are no objective criteria by which the principles of this so-called legal system can be identified and no benchmark by which it could be tested except its acceptance by a select group of European arbitrators and scholars who promote it through their incestuous writings.’178 Similarly, Cutler contends what is significant about the shift to arbitration is the fact that it necessitates the supersession of national jurisdiction(s) with a transnational jurisdiction.179

It is not only with respect to the power relations embodied in the use of offshore arbitration that the theory obscures the role of power, being germane to all facets of the observed juridification of dispute settlement. For example, and applied to the proliferation of BITs, and as Guzzman notes, while such treaties theoretically confer equal rights on the investors of both countries party to the agreement, where capital flows are one-directional such arrangements systematically benefit the capital-exporting state.180 The same logic applies to the public provision of insurance and financing for infrastructure investors by OPIC, alongside other ECAs from the major

if methods of legal decision-making that all parties concede to be fair are scrupulously adhered to. That adherence, not the substantive fairness of the rules, will in turn deliver legitimacy, and legitimacy will bring about compliance. Thus the International Legal Process School denies that law is altogether manipulable by the parties—and thus it retains its distinction from politics—because the legal process is distinct unto itself, and is assessed by legal, not political standards.’ Quoted in Philip Bobbitt, The Shield of Achilles (2002), p. 643.

178 Sornarajah notes ‘There is no accepted definition of lex mercatoria, but it generally refers to a body of commercial rules that are applied frequently by international arbitrators who short circuit the need for determining the law applicable to the dispute by discovering a commercial legal principle which is a common denominator to all possible legal systems applicable to the dispute or discovering some trade usage or custom that may be relevant, and converting that into a legal principle.’ M. Sornarajah, The International Law on Foreign Investment (2004), p. 431.

179 Claire A. Cutler, Private Power and Global Authority (2003). Cutler notes the effect of which is nothing less than to ‘disembed commercial law and practice from the “public” sphere and to reembed it in the “private” sphere, free from democratic and social control.’ p. 13.

capital-exporting states. Thus, while it is true that arrangements providing for the automatic subrogation of insurance claims, as are a pre-requisite for OPIC insurance and financing, theoretically provide both parties to the contract with equal rights, where capital flows are not reciprocal the arrangements embody power relations. They do so because in providing for the sanctity of private property and where investment flows almost exclusively in one direction then these arrangements systematically favour the interests of the capital-exporting treaty partner. In this regard, the legalization hypothesis serves to obscure the central fact that institutional rules and norms serve as repositories of power and privilege.

The point is well made by Barnett and Duvall who write, ‘[I]n other words ‘A’ does not possess the resources of power but because ‘A’ stands in a particular relation to the relevant institutional arrangements its actions exercise power over ‘B’.’\footnote{Michael Barnett and Raymond Duvall (eds.), \textit{Power in Global Governance} (Cambridge: Cambridge University Press, 2005), p. 16.} They continue, with direct relevance to the international institution for investment dispute settlement, ‘[T]emporally, institutions established at one point in time can have ongoing and unintended effects at later point. Long established institutions represent frozen configurations of privilege and bias that can continue to shape the future choices of actors.’\footnote{Michael Barnett and Raymond Duvall (eds.), \textit{Power in Global Governance} (2005), p. 16.}

By contrast, while critical accounts explicitly link shifting arrangements for dispute settlement to the exercise of power, and while they rightfully acknowledge power embodied in institutional arrangements, they wrongly obscure the yet still central role of states in the new legal order. By implication, these theories also overplay the power of transnational corporations relative to state enforcement, upon which the efficacy of these new arrangements depends. That is, and once again, the continued centrality of state power and interests in dispute settlement and by implication the inter-national politics of expropriation rule making.

Expressed differently, the approach overplays the power of transnational actors but particularly TNCs in underwriting international law norms of expropriation and compensation, relative to the power of states in the new legal order. By logical
extension, these accounts also overplay the authority of privatized dispute settlement arrangements, in terms of their capacity to motivate compliance absent home state enforcement. Put simply, while production structures are increasingly transnational rather than multinational, and while markets are increasingly globalized, in the final analysis, even the most powerful TNCs still rely on the power of their respective home states to enforce arbitral awards and property rights on their behalf. In this manner, the theory obscures the still central role of states in underwriting the legal institutional environment within which transnationals must function: the nature of the legal system, the specification of legitimate organizational forms . . . [and] the determination of acceptable modes of political action.¹⁸³ That is, the continued centrality of the state in mediating corporate expansion amidst economic globalization, including strategies of multinational capital accumulation.

Although the conceptual focus of this review concerns the theorized consequences or effects of shifting governance arrangements, one further criticism of institutionalist or rules-based accounts must be noted.¹⁸⁴ It concerns their inability to explain changes in international law norms and dispute resolution practices over time. To explain, because these theories fail to fully elucidate the non-material bases of international law, i.e. its normative foundations, then they are left with no way of explaining the causes of contemporary developments characterized by the legalization of dispute settlement. Thus, while it is true that ideas concerning the role of FDI in national economic development have shifted it is also the case that power has once again shifted in favour of capital-exporting states and MNCs following the LDC debt crisis.

In this environment, the capacity of capital-exporting states to promulgate treaties governing direct investment must be understood as a function of the overriding need


¹⁸⁴ In this respect, Lipson acknowledges that his approach displays a ‘tendency to skim over the shift in property norms.’ Charles Lipson, *Standing Guard* (1985), p. 263. Clearly, therefore the criticism applies to traditional institutionalist accounts and the legalization hypothesis to different degrees. Thus, while Lipson and Rodman’s accounts can be criticized for their failure to properly articulate why property norms change and the modes of transmission linking changing ideas to changing institutional rules and practices, at least they attempt to do so. This can be contrasted with the authors of the legalization hypothesis who appear content merely to observe the ‘move to law’ in world politics, absent any attempt at an explanation as to why international politics should be undergoing what, viewed from the broad sweep of history (longue durée), would constitute the single most fundamental change in the nature of international politics dating back to the Treaty of Westphalia (1648).
for investment capital hence the willingness of states to ‘voluntarily’ forego sovereign rights as is the effect of proliferating legal obligations governing investment dispute resolution. Treaties signed under the compulsion of economic necessity as is the case with LDCs post debt-crisis are no more the product of shared norms concerning the benefits of FDI and the use of legalized modes of dispute settlement than are the terms to which the vanquished submit after defeat in war. Claims to the contrary serve not to strengthen the rule of law but merely to strengthen the claims of critics of the international law of foreign investment who contend that it is used as a bulwark to protect the status-quo, which serves the interests of multinational capital, and ultimately, the national interests of capital-exporting states.185

Finally, the intention in pointing to the weakness of rules-based accounts in this regard is not to suggest that institutional rules and norms plays no role in structuring the behaviour of disputants, and ultimately outcomes as is associated with neo-realists for whom the structure of the interstate system determines national interests and behaviour.186 That is, contrary to the neo-realist view of law, the international law of foreign investment does serve as a baseline for expectations.187 That this is the case reflects not as Rodman contends shared norms borne of shared historical experiences (Lockean property precepts) but rather the recurrent act of enforcement through a combination of threats and promises sufficient to regularize expectations.188 In this

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185 To suggest that international politics is not the basis of the international law of foreign investment, as is the implication of the legalization hypothesis appears to exemplify what one German writer in the 1920s mocking described (with reference to attempts by Britain and France to portray the Versailles Treaty as immutable) as suffering from a bad case of pacta-sunt-servanda-ism. Quoted in E.H. Carr, The Twenty Years Crisis (1964), p. 181.

186 Waltz labels his own theory structural realism. He contends that the structure of the international state system forces the units of the system to prioritize the pursuit of survival above all else. In this manner, he deductively defines state interests from the structure and functioning of the interstate system. In so doing, however, his theory serves to frame the pursuit of national interests and adherence to the rules and norms of international law as mutually exclusive so as to wrongly frame law and national interests dichotomy. See Kenneth Waltz, Theory of International Politics (Reading, Mass.: Addison-Wesley, 1979).

187 The position is exemplified by the comments of then U.S. Secretary of State, Dean Acheson, who wrote of international law ‘[t]hose who devote themselves to international relations . . . are understandably reticent about the role of law. They knew, Acheson said, that law was what government officials said it was—no more—and that the study of law was the assessment of what, in fact, authoritative legal decision-makers would do when law was invoked as a basis for decision making.’ Similarly, Acheson’s successor, John Foster Dulles, later declared, ‘I must confess to being one of those lawyers who do not regard international law as law at all.’ Quoted in Philip Bobbitt, The Shield of Achilles (2002), p. 640-641. Parenthesis in original.

188 That is, by way of ‘tactical issue-linkages (threats and or promises) a state with more abundant resources can manipulate the weaker state’s preference ordering so as to transform the game into one where there is only one ‘Pareto-efficient solution’ left, the one favored by the more powerful actor.’
respect, the thesis seeks to chart a middle ground between a sterile neo-realist conception of law, and what might be described as a utopian view of international law embodied in the legalization thesis wherein the international law of foreign investment is portrayed as neutral and somehow apart from state power and interests. In so doing, the thesis consciously draws on E.H. Carr’s notion of international law, for whom the ‘shortcomings of international law, serious as they are, do not however deprive it of the title to be considered as law.’\textsuperscript{189} Whilst at the same time recognizing that ‘[L]aw cannot be self-contained; for the obligation to obey it must rest on something outside itself.’\textsuperscript{190}

\textit{Reconsidering the Role of State Interests in U.S. Anti-Expropriation Policy-Making}

The purpose of this section is to expand on the initial sketch of theories of U.S. anti-expropriation policy-making. Before doing so, however, the section will chart the contours of post war U.S. policy as concerns expropriation. Though official U.S. anti-expropriation policy has remained unchanged in almost seventy years, in reality U.S. policies to protect its foreign investors have shifted over time concordant with evolving international law norms and configurations of power in the international system.\textsuperscript{191} This includes not only the instruments of state protection, but also the standards of compensation demanded as well as the definition of expropriation, i.e. lawful and unlawful behaviour. To explain, formally the position of the U.S. with respect to expropriation has remained unchanged since first articulated by the then U.S. Secretary of State, Cordell Hull in 1938.\textsuperscript{192} The ‘Hull formula’ holds that

\textsuperscript{191} See for U.S. Law on Expropriation: \textit{Restatement (third) Foreign Relations Law of the United States} (1987); U.S. Code 22, Chapter 21 ‘Settlement of International Claims. ‘The guidelines for expropriation are contained in the following U.S. civil code, See § 620(a), (g), (j), (l), (o), Foreign Assistance Act of 1961 (Public Law 87-195; 22 USC 2370). From an administrative perspective, expropriation claims are referred to The Office of the Assistant Legal Adviser for International Claims and Investment Disputes, Department of State. A second body, the Foreign Claims Settlement Commission, operating as a quasi-judicial independent agency within the Department of Justice also adjudicates claims of U.S. nationals against foreign governments.
\textsuperscript{192} The Hull Formula was articulated in response to the Mexican nationalization of the oil-industry. For Secretary of State, Cordell Hull, ‘The whole structure of friendly intercourse of international trade and commerce . . . rests on the respect of governments and peoples for each other’s rights under
expropriation is legal if it is accompanied by ‘prompt, adequate and effective compensation.’ Where appropriate compensation was defined as the payment of compensation equivalent to the market value in hard currency within six months from the date of seizure.

In the early post war period, U.S. policy-makers displayed a willingness to uphold the standard using all the available means at their disposal. This meant taking whatever steps were deemed necessary to confront expropriating states. This included underwriting right wing coups in order to sustain U.S. investor privileges, as occurred for example in Guatemala (1954) and Iran (1953). Later, during the 1960s such overt action, though not obsolete, would give way to less high profile means of state-protection. In particular, the suspension of foreign-aid to expropriating states became the preferred means of protecting U.S. foreign investors, as provided for by the Hickenlooper (1962) and Gonzales Amendments (1972). It was in this environment that OPIC was established in 1971, as part of a more conciliatory approach to dispute settlement.

The evolution of the instruments used to protect U.S. corporate property abroad during the 1960s and 1970s was also mirrored by evolving standards as regards expropriation and compensation. In particular as U.S. policymakers gradually and indeed belatedly recognized that expropriation need not be considered a precursor to Communist revolution and thus a frontal assault on the citadels of capitalism itself, then U.S. expropriation policy shifted: a shift Rodman has labeled the move from ‘principle to pragmatism’.193 The softening of U.S. policy during this period was manifest in the evolving standards of appropriate compensation demanded by the U.S., which shifted from market value to the lesser standard of book value plus some ongoing contractual relationship.194 As Rodman has cogently noted, ‘[T]his adaptation [was] not a rejection of the principle that nations must make good for

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194 Indicative of the softening of U.S. policy during this period are the following comments: ‘Generally speaking, The Department of State does not intervene in cases involving breaches of contract between a foreign state and a national of the United States. The practice . . . is based on the proposition that the Government of the United States is not a collection agency and cannot assume the role of endeavouring to enforce contractual undertakings freely entered into by nationals with foreign states.’ Quoted in M. Sornarajah, International Law of Foreign Investment (2004), p. 405.
deprivatory wrongs against aliens. Rather, it [was] a redefinition of what is [was] considered wrongful.195

According to Vance Koven, based on his analysis of the agency’s ‘jurisprudence’ during this time, this position was mirrored in the practice of OPIC insofar as the agency refused ‘to take a position on whether breach of a long-term concession agreement would create a liability cognizable under the Contract’, i.e. would be considered a violation of the international law of foreign investment.196 Though whether this reflected de facto acknowledgement of the ambiguity of international law as concerns breach of contract by a sovereign party, specifically the contested applicability of the clausula doctrine or, instrumental calculations based on previous experience with such disputes, raising as they do issues of independence and sovereignty cannot be verified one way or another. What is clear, is that while the number of claims made by U.S. investors for losses arising from breach of contract by a sovereign contracting party previous to the current period is limited, in general OPIC’s practice in paying or rejecting claims has served to frame subsequent losses as commercial rather than as political risks.197

Where in the two decades to the end of the 1970s, U.S. policy evolved towards a less doctrinaire stance, in the two decades to the end of the 1990s U.S. anti-expropriation policy has once again shifted albeit in the opposite direction.198 That is, towards a more stringent application of formal U.S. expropriation statutes, so as to effectively expand those actions considered to be wrongful and second, to return standards of

197 In so doing, however, it is significant to note that where an investor’s claim has been rejected on these grounds, the agency’s interpretation has been challenged so as to in one instance force the program’s administrators to pay the investor’s claim. The assertion is based on OPIC’s interpretation with respect to the claim made by RJA (Jamaican subsidiary of Revere Copper, USA) wherein OPIC denied RJA’s claim, arguing that the Jamaican government’s breach of the ‘stabilization clause’ could not be considered as expropriatory on the basis that RJA ‘still has all the rights and property that it had before the events of 1974: it is still in possession of the plants and other facilities; it has its mining lease; it can operate as it did before.’ Quoted in M. Somarajah, International Law of Foreign Investment (2004), p. 379. On the agency’s jurisprudence during the 1970s See also Peter R. Gilbert, ‘Expropriation and the Overseas Private Investment Corporation,’ Law and Policy in International Business Vol. 9 (1977), p. 515-550.
compensation to market value. That this is the case can be seen by the expanded
definition of expropriation contained in U.S. investment treaties and OPIC (from
1985) and EXIM PRI contracts. For example, where expropriation once referred to an
official taking, contemporary U.S. investment treaties and OPIC contracts now define
expropriation as ‘any measure or series of measures the effect of which would be
tantamount to expropriation or nationalization.’\textsuperscript{199} Similarly, Vanderveldt tell us that
the second wave of U.S. BITs, first introduced in 1988, also incorporated language,
the effect of which was to increase the rights of U.S. foreign investors and the duties
of host states in their dealings with one another.\textsuperscript{200} In this manner, U.S. anti-
expropriation policy can be seen to have shifted incrementally towards heightened
standards of investor protection during the 1980s and 1990s.

Having outlined the post war record of the U.S. in brief, the final task for the chapter
is to outline the competing accounts of the changes observed. To recap, the first
chapter introduced what has been labelled as the prevailing theoretical orthodoxy as
far as explanations of OPIC policy and practice are concerned. The approach holds
that OPIC policy and practice has been determined by corporate preferences in accord
with shifting strategies of corporate adaptation in response to shifting standards of
security for FDI in LDCs. In making this statement, Lipson cautions, however, the
U.S. has on occasion foregone its immediate material interests in order to uphold the
sanctity of institutional rules.\textsuperscript{201} The alternative perspective by contrast emphasizes
the role of state officials (U.S. government) in driving U.S. policy aimed at protecting
U.S. foreign investor interests. From this perspective, the OPIC insurance program is
subordinate to the pursuit of broader foreign policy goals; shifts in the program thus
reflecting shifting foreign policy objectives of state policy-makers in response to
evolving external constraints, i.e. configurations of power in the international system.
Exactly how those policy objectives are formulated, however, is different for each of
the two ‘statist’ accounts.\textsuperscript{202}

\textsuperscript{200} Kenneth J. Vandeveldt, ‘Of Politics and Markets: The Shifting Ideology of BITs’, 11 \textit{Int'l Tax &
\textsuperscript{201} Charles Lipson, \textit{Standing Guard} (1985). On this Lipson thus concurs with Henkin’s assertion that
international law has a significant impact on state foreign policy-making. See Louis Henkin, \textit{How
\textsuperscript{202} A third statist account, which emphasizes policy outcomes as the product of bureaucratic infighting,
was forwarded by Jessica Einhorn, \textit{Expropriation Politics} ((Lexington, Mass.: D. C. Heath, 1974)..
Drawing on evidence from the dispute between Peru and the U.S. owned International Petroleum
The first statist account of U.S. anti-expropriation policy-making, Stephen Krasner’s *Defending the National Interest* (1978), drew on evidence from actual expropriation disputes to explain the causal mechanism underpinning U.S. policy responses. As the title of the work makes clear, Krasner rejects the notion that U.S. anti-expropriation policy-making can be reduced to the summation of societal wants. In particular, for Krasner U.S. policy reflected a clear conception of the U.S. national interests, defined as ‘a set of transitively ordered preferences that persist over time and are related to general societal goals.’ He defines these goals in the case of raw materials and in ascending order as the following: 1) increase competition, 2) ensure security of supply and 3) promote broad foreign policy objectives. That is, the U.S. never had an ‘anti-expropriation policy’, instead, U.S. policy responses reflected the hierarchy of goals sought, atop which sat the pursuit of national security in the context of Cold War competition for power and influence among the developing world.

More particularly, he contends that U.S. ‘objectives were associated with broader political goals and not with the desires of American firms.’ In support of the assertion, he claims that the U.S. only intervened on behalf of its foreign investors...
where it perceived (rightly or wrongly) expropriation of U.S. property to be part of a move towards Communism.\textsuperscript{208} In this regard, he cites divisions within the business community as underpinning the observed policy autonomy.\textsuperscript{209} In arguing that U.S. policy-makers were relatively insulated from corporate demands it should not be thought that Krasner denies the impact of private investment decision-making on the goals sought by U.S. policy makers, which he acknowledges influenced the precise form of U.S. policy responses.\textsuperscript{210} Ultimately, for Krasner, however, the state undertook to educate U.S. investors as to the political realities of doing business in LDCs by withholding their support, hence the realignment of corporate investment strategies towards adaptation with a pervasive LDC economic nationalism.

The second statist account of note was forwarded by Kenneth Rodman, \textit{Sanctity Vs. Sovereignty} (1988).\textsuperscript{211} He too drew on evidence from actual disputes to understand the determinants of U.S. policy but unlike Krasner, the objective for Rodman was to construct a typological account of U.S. expropriation policy-making. He did so, because while competing theories succeed ‘on occasion in providing a parsimonious explanation of the decisive causal locus of policy determination’ none successfully explains U.S. policy responses across the universe of cases.\textsuperscript{212} He found that prior to 1968 U.S. policy was best explained as a product of national interest calculations. In contrast, in the period 1968-1973, which he labels the era of ‘regime stress’, U.S. policy emerged from bureaucratic infighting. Finally, from 1973 onwards (‘era of regime transformation’), U.S. policy was best explained by ‘policy-learning.’ That is, systemic changes ‘which made themselves indelibly manifest in the OPEC revolution demonstrated the costs and inefficacy of economic reprisals’ so as to force U.S. policy-makers to adapt their strategy from ‘principled opposition to ideological détente.’\textsuperscript{213} The problem with Rodman’s account, however, is that ‘policy-learning’ is

\textsuperscript{208} Stephen Krasner, \textit{Defending the National Interest} (1978), p. 337.
\textsuperscript{210} In this regard, Krasner labels the U.S. a ‘weak-state’ insofar as while the state can withhold support it cannot cajole private firms into investing or divesting their interests.
\textsuperscript{212} Kenneth A. Rodman, \textit{Sanctity Vs. Sovereignty} (1988). His model begins by identifying three options available to U.S. policy makers: intervention, economic sanctions or accommodation. In each instance, the policy chosen is understood as a product of one of three independent variables: diplomatic milieu goals (national interest), economic milieu goals (corporate preferences) or bureaucratic politics.
underspecified, with the result that it is unclear what evidence would substantiate such an account distinct from material interests and external constraints.

The third and final theory to be examined is Charles Lipson’s specialist study that seeks to identify the causal locus of U.S. anti-expropriation policy-making through an examination of the long-term evolution of the investment guaranty program (1948-74). In this respect, he characterizes ‘state-sponsored guaranty insurance’ as the most coherent and specific U.S. government plan to protect foreign investments. His self-titled ‘radical hypothesis’ is explicitly framed as an alternative to what he dubs ‘the dominant statist paradigm.’ He contends that shifts in the investment guaranty program are best understood as the product of corporate preferences, where corporate preferences refer to companies in the Fortune 500, plus the 50 largest commercial banks. From this standpoint, the establishment of OPIC in 1971—as part of a ‘long-term shift away from public policies that vigorously resist forced divestment’ in favour of a more accommodative and less hostile anti-expropriation policy—was underpinned by extraordinary corporate support in accord with evolving corporate strategies of adaptation to economic nationalism in LDCs aimed at lowering the profile of investments.

More generally, he emphasizes the impact of private investment decision-making on U.S. foreign policy. He writes ‘[W]hile the state played both a dependent and intervening role, its initiatives were continually shaped by corporate preferences.’ In this regard, he explicitly rejects the notion that state policy-makers possess autonomy from corporate America in formulating U.S. anti-expropriation policy. In so doing, he does not seek to deny the impact of broader goals sought by U.S. foreign policy makers, rather, it is that these wider ‘state’ objectives did not significantly effect the program as ‘the goal of that policy, challenged but still pre-eminent, is private capital accumulation’ and it is this that explains ‘the most striking feature of

guaranty policy: the basic identity between corporate preferences, state initiatives and policy outcomes.\(^{219}\)

His emphasis on the close links between state officials, corporate America and policy outcomes has led Krasner to label it a variant of instrumental Marxism, albeit a sophisticated one.\(^{220}\) And while esoteric debates concerning classificatory theoretical schemas (typologies) are in the final analysis just that, the point is noteworthy. It is so, because Lipson’s claims are more qualified than the label would suggest. In particular, although the capacity of corporate America to determine policy outcomes reflected the ‘structural relationship between multinational firms and foreign economic policy’, he is careful to make explicit that his findings are not generalizable to foreign economic policy-making as a whole, such as foreign trade policy, wherein non-corporate interest groups are more active in policy debates, with the result that the corporate community has ‘a less coherent and influential voice.’\(^{221}\)

To conclude, the review has detailed two different approaches to explaining U.S. anti-expropriation policy-making: state initiatives (national interest) and corporate preferences. In this respect, while both theories offer persuasive accounts of the causal locus of U.S. foreign economic policy-making, ultimately ascribing changes to the program as the product of corporate preferences is difficult. Thus, while U.S. foreign policy-makers clearly sought to accommodate corporate interests, and while private investment decision-making no doubt impacts policy considerations among the


\(^{220}\) He distinguishes between what he terms Instrumental Marxism and Structural Marxism. The former, he associates with the work of Ralph Miliband, *The State in Capitalist Society* (New York: Basic Books, 1969). Instrumental Marxist accounts emphasize the close relationships between corporate leaders and state policy makers, so as to in more extreme formulations frame the state as the executive of the bourgeois. The classic structural Marxist account for Krasner is Harry Magdoff’s *The Age of Imperialism* (New York: Monthly Review Press, 1969). Structural Marxists, he explains, view the state as less beholden to particularistic capitalist class interests, and are able as a result to play an independent role, albeit one that is aimed at maintaining the integrity of the capitalist system in response to capitalism’s inherent tendency toward crisis, including where necessary to the capacity to forego the immediate interests of capitalist classes.

\(^{221}\) Charles Lipson, *Standing Guard* (1985), p. 27-28. While he posits a structural relationship between U.S. policy-making and the preferences of U.S. MNC, he does so absent of more traditional Marxist formulations, wherein the creation of markets for private capital accumulation is understood as directly related to the imperatives of the capitalist order, specifically endemic capitalist crises arising from declining profit rates and or inherent class-conflict. Second, he implicitly frames the structural relationship between U.S. foreign policy-making and the needs of U.S. multinational investors as reflecting the position of the U.S. as the largest source of FDI in LDCs rather than as an attempt to protect the capitalist order though he acknowledges the practical outcome was the same.
executive, the ‘timing’ of changes to the investment guaranty program appear to be best explained by the shifting goals sought by the foreign policy bureaucracy vis-à-vis the developing world.

In particular, while Lipson focuses on the impact of bureaucratic differences which he contends enabled corporate leaders to step in to determine the outcomes of policy debates, he overlooks divisions among corporate America. In particular, while it may appear as obvious that foreign investors would favour increased state support, in reality the response of corporate America to the program has been more ‘convoluted’ so as to weaken the impact of corporate pressure.222 Thus, while the program enjoyed corporate support, as often as not corporate lobbying has been directed against the program. The point is significant as it reflects a second trend that mitigates against corporate preferences, the shifting composition of direct investment in LDCs so as to lessen shared interests—as is the practical result of the spread of manufacturing investment, and latterly service sector based FDI—and thus the corporate voice. This trend is further exacerbated by the fact that firms with ostensibly the same interests operating in the same sector in the same country have often displayed divergent attitudes towards the insurance program, a point Lipson himself concedes.223

Finally, his assertion that OPIC was indeed the most coherent of all state sponsored programs aimed at protecting and promoting U.S. investor interests serves to wrongly characterize the program and U.S. anti-expropriation policy more generally. It does so, because U.S. policy responses were not consistent. Indeed, apart from the shared view that expropriation was lawful there was no consensus as to what U.S policy should be and this was reflected in policy responses to individual disputes as well the evolution of the insurance program. That this was the case, can only be explained if one understands the basic fact that the U.S. guaranty program was subordinate to the pursuit of U.S. national interests wherein economic interests were held to be secondary to security interests in the context of the Cold War.

223 Lipson writes, ‘Specific characteristics of individual firms do not seem to predict policy preferences, and industrial groupings were internally split.’ See Charles Lipson, *Standing Guard* (1985), p. 234.
The assertion that a statist (national interest) account is best able to explain the evolution of the OPIC administered investment insurance program, rather, than corporate preferences must be qualified, however. Thus, the intention is not to deny the impact of private decision-making, i.e. corporate decisions to invest or divest interests, on the goals sought by U.S. foreign policy officials’ vis-à-vis LDCs.

Second, the intention is not to deny the privileged position of business where accessing state officials is concerned, including among the executive and Congressional branch. In this respect, the thesis explicitly accepts the notion that corporate America enjoys a special relationship with foreign policy officials in comparison with other interested lobby groups, where the investment insurance program is concerned. Third, in forwarding a national interest account of the program’s evolution, the intention is not to deny that the U.S. political system disperses and fragments power so as to provide domestic interest groups with veto points. Foremost in this regard, concerns the special place of the legislative branch in formulating U.S. foreign policy in comparison with other industrialized nations. In this respect, the thesis concurs with Krasner when he cautions that the degree of autonomy afforded the executive will depend on whether the issues reaches Congress. This is so, for two reasons explains Krasner, first ‘the political needs of Congressmen are different from those of the President. Second, power within Congress itself is fragmented and dispersed, offering many points of access for societal groups.’

In summary, the chapter has reviewed two bodies of IR theory, including theories of investment dispute settlement and theories of U.S. anti-expropriation policy-making.

Conclusions

In summary, the chapter has reviewed two bodies of IR theory, including theories of investment dispute settlement and theories of U.S. anti-expropriation policy-making.

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The chapter has shown that explanations of changes to the U.S. insurance program differ with respect to the causal mechanism as well as the characterization of the program. In particular, should the program be understood it as a coherent response to shifting U.S. foreign investor strategies (as framed by corporate preferences), or alternatively (as framed by state-initiatives), a useful adjunct to the pursuit of broader political goals and ultimately U.S. national interests vis-à-vis the developing world?

Before this, the chapter reviewed competing accounts of the theorized effects of shifting institutional arrangements for dispute settlement and expropriation rule making, arguing that these accounts obscure the still central role of state power and interests in underwriting international standards on behalf of foreign investors.

Having detailed the postulates of the competing theories held to explain the outcomes of disputes and the nature of international property and contract rights, the focus of attention now switches from theory to practice, beginning with the dispute between the U.S. energy company CalEnergy and the Indonesian government-owned, PLN.
Chapter 3: Indonesia, CalEnergy and OPIC

The first case study to be examined concerns an investor-state dispute between the Nebraska-based CalEnergy Company Inc. and the Indonesian government-owned natural gas supplier, Perusahaan Listrik Negara (PLN).225 The dispute arose following suspension of PLN’s contractual obligations by the then President Suharto in September 1997. Following failure to resolve the dispute, CalEnergy sought third-party arbitration pursuant to the Energy Sales Contract (ESC). Having obtained an arbitral award in its favor, CalEnergy then filed a claim with the U.S. investment insurance agency, the Overseas Private Investment Corporation (OPIC).226 In assessing the validity of the claim, OPIC found that in abrogating the contractual agreements, as well as the subsequent failure by the Republic of Indonesia to honour the arbitral award, CalEnergy’s ‘fundamental rights in the projects’ had been violated in contravention of the customary international law principles concerning ‘expropriation’ thereby awarding CalEnergy $290 million in compensation. Following payment of the claim and further negotiations, a final settlement was concluded in late-2001, wherein Indonesia agreed to reimburse OPIC pursuant to the U.S.-Indonesia Investment Agreement (1967).

To recap, the first task will be to detail the key events in the dispute from its inception through until the point of final settlement. Attention will then turn to explaining the observed processes and outcome of the dispute. In the first instance, this will include analysis of the impact of PRI on the bargaining strategies employed by the disputants. The focus of the analysis will then turn to the impact of OPIC’s advocacy and mediation role in seeking a negotiated solution, as well as the agency’s judicial role in determining the validity of the claims under the contracts of insurance. The second

225 CalEnergy was established in 1971 as a geothermal power producer, operating geothermal facilities in Coso and Imperial Valley in California. Having enjoyed modest but steady growth throughout the 1980s the company embraced energy market deregulation during the early 1990s, expanding its operations to the Philippines, Indonesia and the United Kingdom, providing the company with an interest in more than 10,000 MW of power generating facilities spanning three continents. In 1998, CalEnergy Company Inc. acquired MidAmerican Energy and was reorganized that same year as MidAmerican Energy Holdings Company (MidAmerican). For the sake of simplicity, the chapter will refer to CalEnergy, however, as it was CalEnergy’s Indonesian subsidiary, Himpurna California Energy Limited (HCE) that was party to the dispute. For an introduction to the company’s offshore production facilities See www.calenergy.com and See also www.midamerican.com.

part of the explanation will then broaden the focus of inquiry to consider the relative explanatory weight of state power and the power of legal rules and legalized modes of dispute resolution in determining the processes of resolution and ultimately the final settlement.

Before beginning, however, it is important to note that the CalEnergy dispute cannot be understood in isolation. That is, it must be understood in the context of the broader process of investment dispute resolution, as concerned more than a dozen other foreign private independent power producers (IPPs) faced with identical demands for contractual renegotiation in the wake of the Asian financial crisis. For this reason, the chapter will also seek to make clear how and when consideration of other IPP disputes and the broader financial crisis impacted the CalEnergy dispute. The empirical evidence will show that a three-track dispute resolution process ensued: first, a legal track centered on the arbitral hearings; second, an ECA led track that included OPIC as one of six national insurers with exposure to the IPP disputes, and third, the more traditional diplomatic path, which included in the U.S. case, the State, Treasury and Commerce Department’s, but centered on the World Bank chaired Consultative Group on Indonesia (CGI).

The evidence will show that not only did the provisions of the contracts of insurance delimit acceptable modes of disputation but that OPIC performed a critical diplomatic in seeking a settlement as well as what amounts to a judicial role in paying CalEnergy’s claim. In this manner, the provision of insurance and financing for U.S. infrastructure investors serves as a flexible mechanism for economic governance where governance may be understood as the enforcement of ‘bargains’ and the establishment of the ‘rules of the game’ so as to effectively delimit international property and contract rights and thus markets for private infrastructure service providers in Indonesia. More narrowly, the evidence will show that the significance of the increased use of PRI by U.S. infrastructure investors is not limited to the ‘international’ politics of dispute resolution. Foremost in this regard concerned the manner in which the presence of insurance served to transform in a small but significant manner the relationship between the state and the multinational capital (the insured investor) in the formulation of U.S. anti-expropriation policy-making so as to delimit the executive’s policy autonomy.
While the instruments utilized by the United States to protect its foreign investors and thus its own interests continue to evolve, at the same time the evidence will show that the efficacy of the institutional rules and norms governing dispute settlement remain a function of underlying state power and interests. That is, compliance with legal rules, and even the use of legalized modes of dispute settlement such as offshore arbitration, reflected not the normative sanction of international law but instead U.S. power and interests at the point of enforcement. In this regard, judging by the evidence from the CalEnergy case study, the emergence of OPIC governance is best understood as a shift in the instruments of state-protection rather than the politics of dispute settlement and law making.

In order to consider the empirical evidence the remainder of the chapter is organized as follows. The first task will be to construct the chronological narrative. Having done so, focus will then shift to analyze the impact of PRI and the role of OPIC in the resolution process before broadening the scope of inquiry to consider the role of state power and interests and institutional legal rules in determining the outcome of the dispute.

Background: Power Sector Liberalization in Indonesia

Like many resource rich but capital poor nations, Indonesia has traditionally welcomed foreign direct investment (FDI). Efforts to attract FDI accelerated from the late 1960s, however, as the new President Suharto, under the tutelage of a group of western-trained economists dubbed the ‘Berkeley Mafia,’ began to actively seek foreign investment to develop Indonesia’s abundant oil and gas deposits.227 And although the policy was a success, judged by the influx of investors, the operating environment in Indonesia remained difficult owing to the lack of separation between the different branches of government and economic and political elites.228 Despite the

227 See Andrew MacIntyre, Business and Politics in Indonesia (Sydney: Allen and Unwin, 1990), p. 1. Indonesia is the largest LNG exporter in the world, and holds the largest known gas reserves, estimated at 92.5 trillion cubic feet. Indonesia also possesses proven oil reserves of 4.7 billion barrels.
228 See Lucian W. Pye Asian Power and Politics: The Cultural Dimensions of Authority, (Cambridge Massachusetts, Harvard University Press, 1985), for an excellent introduction to Indonesia’s post-colonial history. For Lucian Pye, the model of limited political participation and state-led economic
uncertain operating environment, foreign investors in Indonesia managed, however, to avoid the widespread programs of nationalization that accompanied de-colonization and the assertion of statehood elsewhere in the developing world.

The inherent difficulties of operating in Indonesia and high levels of U.S. FDI have meant that OPIC and its predecessor, the USAID administered guarantee program have a long history of involvement in the country.\textsuperscript{229} Moreover, although OPIC has traditionally supported investments in Indonesia consistent with U.S foreign policy support for Suharto, the relationship has not always been harmonious, as indicated by the Indo-Sat dispute between OPIC-insured U.S. investors and Indonesia in the 1970s, as well as the suspension of Indonesia’s eligibility in 1982 following failure to comply with OPIC labour regulations.\textsuperscript{230}

Notwithstanding these difficulties, by the late 1980s Indonesia was beginning to show signs of renewed economic vigor. During the fifth REPELITA (five-year plan 1988-1993), GDP grew by 6-8 percent per annum, while improving budgetary discipline meant that Indonesian sovereign debt achieved an ‘investment grade’ rating for the first time. Investment in infrastructure had failed to keep pace with the rapid pace of economic development, however, leading to bottlenecks. Among the sectors identified as most in need of reform and additional investment was the power sector. For example, according to a study conducted by the state-owned gas company more than development put in place following the establishment of Suharto’s ‘New Order’ in 1966 and resulting in a burgeoning bureaucracy served to facilitate the continuation of the system of patron-client relations that had underpinned Javanese society for centuries (\textit{Bapakism}). He likens the system in its modern guise to a form of ‘bureaucratic capitalism.’ Among the explanations forwarded to explain the weakness of the private business sector in Indonesia relative to the political elite is the fact that the majority of small and medium sized enterprises are owned by the minority ethnic Chinese community, who despite their economic wealth and a history in Indonesia dating back centuries occupy, to this day, an uncertain position in Indonesian society as evidenced by the ethnic riots in Jakarta in 1998 during which Chinese owned business were looted, and ethnic Chinese residents were forced to flee.\textsuperscript{229}

\textsuperscript{229} Perhaps the best example of the significant benefits as well as the inherent difficulties of operating in Indonesia, owing to the need to cultivate close personnel ties with the ruling elite, is that of the U.S. based resource company, Freeport McMoran who established and operate to this day the Grassberg mine in Irian Jaya (West Papua). The mine is the largest gold, copper and silver mine operating in the world. It is estimated that the royalties and taxes from the mine have provided as much as 20 percent of the government budget for the past three decades. However, close ties with the elite have led to accusations of complicity in human rights abuses and has made Freeport the target of a sustained NGO campaign in Indonesia and abroad. It is for this reason that OPIC cancelled Freeport’s $100 million investment insurance policy in 1995, following accusations that the mine covered up widespread environmental damage.

\textsuperscript{230} See Alan C. Brennglass, \textit{The Overseas Private Investment Corporation: A Study in Political Risk} (New York: Praeger, 1983). Indonesia has traditionally been one of the largest recipients of OPIC insurance, since the agency’s establishment in 1971.
$30 billion in additional power generation investment would be required during the sixth REPELITA, of which an estimated $7.5 billion would need to be sourced from foreign investment.231

In response, the Electricity Restructuring Commission was formed in 1990 to oversee the power sector reform process. Among the priorities identified by the Commission in its ‘General Plan for Electricity Development’ was the development of the country’s geothermal resources for domestic power generation so as to free up demand for hydrocarbon reserves for export.232 Included among the reforms were the following: a ‘geothermal team’ was established within the Ministry of Mines and Energy, the reduction of corporate taxes levied on geothermal investors from 47 percent to 34 percent, and the conversion of the state-owned natural gas company, PLN, from PERUM (public company) to PERSERO (limited liability) in order to enhance the management of public-private partnerships with foreign investors.233

In May 1992, the Ministry of Mines and Energy invited companies to submit proposals for the first privately financed, owned and operated electrical generating facility in Indonesia. The project to build and operate the ‘Paiton I’ coal-fired power plant was won by a consortium of foreign investors comprised of Edison Mission Electric, Mitsui & Co and General Electric Corporation, while the local partner PT Batu Hitam Perkasa was allocated 15 percent of the equity in accordance with

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232 Geothermal has a number of advantages for Indonesia. First, geothermal reserves cannot be transported, and must be converted to electricity on site for delivery to the national electricity grid. Second, Indonesia is situated in a region of intense geothermal activities, providing the country with geothermal power equivalent to 20,000 MW, the largest in the world. The third advantage was the incentives being offered by the Clean Development Mechanism (CDM) agreed at the United Nations Framework Convention on Climate Change (UNFCC). According to the terms of the CDM, developed countries could offset their own greenhouse gas emissions (GHG) by purchasing GHG reductions from developing countries. According to PLN’s calculations the potential of the CDM incentives was significant. According to the report published by PLN, ‘Compared to coal-fired systems, Indonesia has the potential to reduce GHG emissions by about 4.8 billion tons of carbon dioxide equivalent (tCO2-e) per year at a cost as low as US$ 1 / tCO2-e (depending on the project’s finance mix) . . .’ the result would still be $4.8 billion per annum. Calculations from Professor Zuhal, ‘Investment Opportunities in the Power Sector’, 1996.

Indonesian companies law.234 The power purchase agreement (PPA) that underpinned the investment was signed on February 12th, 1994. The Paiton I project as the ‘frontier’ project would become the model for all future IPPs in Indonesia, including that of CalEnergy. The PPA committed PLN to purchase electricity from the Paiton I plant for a period of thirty years at a fixed rate denominated in U.S. dollars. In the lexicon of project finance, the contract was known as a ‘take-and-pay’ contract (‘hell or high water’) because the agreement committed PLN to pay for the power produced regardless of demand.

Even after the signing of the contract, however, the World Bank expressed serious concerns about a number of features of both the PPA and the manner in which the tender process had been conducted. 235 As a result, the World Bank advised the International Finance Corporation against providing funding for the project, and informed the Indonesian government that they would not provide funding for power projects until the existing tariff structure was overhauled to properly reflect the cost of supply, i.e. make PLN commercially viable and stop subsidizing power.236 The Asian Development Bank (ADB) was similarly concerned, with the result that they too declined to provide financing for the project.

Despite a lack of support from the multilateral development banks, project financing for Paiton I was eventually completed ready for President Clinton to announce the

234 Equity was sourced from Edison Mission Energy (32.5%), Mitsui (32.5%), General Electric (10%), while the local partner BHP was assigned 15%. The deal structure would provide the blueprint for all the future IPP contracts, leading to allegations of corruption as BHP were lent the money to purchase their 15 percent equity share, to be repaid from future dividends, in a practice that is known as ‘free-carry.’ The agreement reached between the consortium and BHP was structured as follows, ‘To facilitate the contributions . . . EME, Mitsui and GE Capital extended loans to BHP to be repaid out of BHP’s project dividends. The loans carry a market rate of interest and other commercial terms. Until the loans are repaid in full, BHP is permitted to receive only 35% of the dividends to which it would otherwise be entitled.’ See Letter from the Senior Vice-President Asia Pacific Region, Edison Mission Energy to Ralph A. Mathews, Acting Vice-President for Finance, OPIC. Released under the U.S. FOIA Act, Request made by Charles R. Smith, January 27, 2001.

235 Declassified Diplomatic Cable, Released under the U.S. FOIA Act, Request made by Charles R. Smith, January 27, 2001. The minority shareholder referred to in the cable in P.T. Batu Hitam Perkasa was former Head of Indonesia’s notorious Kopassus (special-forces) who was widely implicated in atrocities in East Timor and Aceh, General Prabowo, who is married to Siti Hedian Prabowo (formerly Hariyadi, Suharto’s second daughter). The shareholding estimated at 0.75% of the Paiton I project was estimated to be worth $15 million. The second shareholder of concern to the ADB and World Bank was 33% ownership of PT Batu Hitam Perkasa by PT Tirtamas Majulasma, the majority shareholder in which is Mr. Hashim S. Djiojohadikusumo, the brother-in-law of Ms. Siti Hariyadi (Suharto’s daughter).

236 The International Finance Corporation is part of the World Bank Group. Interview Notes: World Bank, Jakarta.
deal at the Asia Pacific Economic Conference (APEC) held in Jakarta in December 1994. Also in attendance at the conference were representatives from CalEnergy and Enron as well as a number of other prospective IPPs.\(^{237}\) Despite proclamations extolling the virtues of private-enterprise and FDI, the reality behind the Paiton I project was very different. Of the total financing package of $2.5 billion, more than $1.8 billion had been sourced directly from JEXIM, MITI, US Ex-Im and OPIC. OPIC also provided a further $200 million of PRI to cover the private debt syndicate, comprised of 45 international lenders.\(^{238}\) In so doing, they completed the largest ECA financing and insurance of a single project to date. Moreover, the message was clear; the risks although not insignificant were manageable, and the IPPs themselves knew it to be profitable, as is evidenced by the fact that within three years (1993-1996), a further 26 IPPs had signed identical agreements to operate private power plants in Indonesia ranging in value from $100 million to $2,500 million, including the Dieng and Patuha projects to be operated by CalEnergy Company Inc.\(^{239}\)

Despite the fanfare attendant to the APEC conference, for CalEnergy the real work had taken place the year before with the signing of the Dieng Geothermal Project Joint Development Agreement together with the Indonesian state owned oil company, Pertamina, in August 1993.\(^{240}\) The ESC was signed on December 2\(^{nd}\) 1994.\(^{241}\) The contract between Himpurna California Energy Ltd., a subsidiary of CalEnergy Inc. (USA), and PLN, contemplated the supply of electricity up to a maximum of 400 MW from the Dieng and Patuha Geothermal fields in Java. The ESC committed PLN to purchase electricity from the two plants for a period of thirty-years at a fixed price, after which ownership of the plants would be transferred to Pertamina.\(^{242}\)


\(^{238}\) The acronyms refer to the following government agencies: Japanese Export-Import Bank, the Ministry of Trade and Industry (Japan), the Export-Import Bank of the United States.

\(^{239}\) CalEnergy was also awarded a third contract to develop the Bedugul geothermal field in Bali in November 1994. The tripartite contract contemplated the construction of four 55 MW units.

\(^{240}\) According to CalEnergy, they were awarded the projects because they had experience in developing what are known in the industry as ‘dirty fields.’ A dirty field contains high levels of sulphur dioxide, and can be dangerous to operate due to the presence of non-condensable gases. Pertamina had attempted to develop the field themselves in 1997 before abandoning the project after an explosion killed a number of workers, See Interview Notes, former CalEnergy executive.

\(^{241}\) The ESC was one of eleven signed with geothermal IPPs, for the production of an estimated 1,950 MWs of power by the Ministry of Energy and Mines, from 1994-1996, none of which were tendered.

\(^{242}\) The three-step tariff structure for Dieng was priced as follows: years 1-14, 8.39 c KWh; 15-22, 7.41 c KWh; and 23-30, 6.21 c KWh, making it the most expensive of the 27 power purchase agreements signed with foreign IPPs. The Patuha structure was as follows: years 1-15: 7.26 and years 16-22: 3.46.
CalEnergy had different local partners for each of the projects. For the Dieng facility CalEnergy partnered with P.T. Himpurna Enersindo Abadi, an association of retired Indonesian Generals. As in the Paiton I deal, the local partner was assigned a minimum equity stake in the project company, Himpurna California Energy Limited, to be paid for from future dividends. The agreement with the local partner also provided for CalEnergy’s Indonesian subsidiary to pay its local partner $5,000 per month for the ‘upkeep’ of their offices in Jakarta.243 In the case of the Dieng project, CalEnergy was assigned its local partner by the head of the Geothermal Team, former General, Purnomo Yusgiantoro.244 For their second project, operated by Patuha Power Ltd, the local partner was PT Enersindo Supra Abadi, the President of whom was Fadel Muhammed, son in law of the then Coordinating Minster for the Economy, Minister Hartarto.245

Under the provisions of the ESC, the two power plants were to be built as separate units, so as to stagger the power coming on-line. Development of the Dieng field commenced with the drilling of core holes and 19 wells in February 1995. Construction of Unit 1 began in March 1996, with an initial expected completion date of December 1996. This was later delayed until to August 1997, before being delayed for a second time to March 1998, due to technical difficulties at the site. Finally, in April 1998, CalEnergy informed PLN that the facility was ready for testing and connection to the electricity-grid. On the 29th April 1998, the first invoice for power from the plant was sent to Pertamina, under which PLN was to make payment in full within 30 days. PLN neither made payment nor availed itself of the power, however. As a result, work on the construction of Patuha Unit 1, and Dieng Unit 2, was halted in April 1998, with Patuha Unit 1 30 percent complete.246

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243 Private correspondence, Donald M. O’Shei, Jr. Vice President and General Manager Himpurna California energy Ltd. to Retired General Mr. J. Henuhili, P.T. Himpurna Enersindo Abadi, Jakarta, 1st November, 1996. Himpurna is the Indonesian Armed Forces Retired Officers Club.

244 Purnomo Yusgiantoro is currently the Minister for Mines and Energy as at 01.09.06.

245 Interview Notes, former CalEnergy executive.

246 The 30 percent figure was provided by CalEnergy in the subsequent arbitral hearings, but was not independently corroborated.
Despite the delays in the construction of the Dieng facility, the development of Dieng and Patuha appeared to be on track until the onset of the Asian financial crisis in early 1997. Unfortunately, for Indonesia, initial expectations that it, unlike Thailand and Malaysia, would be able to ride-out the financial storm owing to its petro-dollar revenues (foreign currency) proved misplaced. By mid-1997, the Indonesian economy was in crisis, compounded by capital flight and the irresponsible lending practices of the domestic banking sector. According to one study, almost all of the nation’s major conglomerates were technically insolvent, along with most of the major banks.\textsuperscript{247} As the economy worsened speculation by currency traders that the Rupiah-dollar currency peg, maintained by the Central Bank at 2,400 to the dollar, would be adjusted downwards mounted. The collapse of the Rupiah when it arrived was spectacular. Between July 1997 and February 1998, the Rupiah depreciated to a low of 18,000 to the dollar, effectively increasing U.S. dollar denominated debt-servicing requirements by approximately 700 percent. At the same time, the economy contracted by 22 percent in twelve months, with the effect of substantially reducing budget revenues and the government’s borrowing capacity.\textsuperscript{248}

In recognition of the growing crisis, the International Monetary Fund (IMF) dispatched a consultative team to Jakarta in July 1997, including the then head of the IMF, Michael Camdeuss, to meet with the President and his advisors. Two months later, President Suharto signed new loan agreements with Michael Camdeuss pictured standing over him before the gathered media.\textsuperscript{249} The IMF package was designed to stabilize the Indonesian economy, in particular to provide funds to recapitalize the


\textsuperscript{248} For an excellent overview of the economic crisis in Indonesia see Hal Hill, \textit{The Indonesian Economic in Crisis: Causes, Consequences and Lessons} (Australia, Allen and Unwin, 1999).

\textsuperscript{249} While one may assume that the picture was intended to demonstrate the close working relationship between Indonesia and the IMF, the photo depicting the head of the IMF literally standing over the President of Indonesia was widely interpreted in the local media as symbolic of the manner in which the IMF agreement derogated the country’s sovereignty and independence. Moreover, that it was printed widely in the Indonesian media enabled President Suharto to present the agreement in such a way as to suggest it was forced upon him thus evoking nationalism in Indonesia, as well as enabling him to defray the political costs to his Presidency arising from the resulting economic hardships.
banking sector through the purchase of non-performing loans by the newly established Indonesian Bank Restructuring Agency (IBRA). The ‘bailout’, the then largest agreed in a single tranche by the IMF, amounted to $47 billion. Under the terms of the package, and according to unconfirmed reports at the insistence of the IMF, President Suharto was instructed to inform the IPPs that Indonesia could not meet its obligations, and that the projects would need to be renegotiated. And although the role of the IMF cannot be confirmed conclusively in the absence of written documentation, the conjecture is supported by interview evidence and is consistent with the IMF’s initial strategy to renew financial market confidence in Indonesia through a tightening of fiscal and monetary policy. Moreover, given the events that preceded the crisis wherein the former President appeared to actively support ‘first family’ involvement in the power deals, it is unlikely that such action would have been taken in the absence of sustained pressure from the IMF evidenced by the fact that at the first opportunity the president rescinded the agreement to this effect with the IMF.

Later that month on September 23rd 1997 Suharto issued Presidential Decree (PD) 39/1997. The decree divided IPP projects into three categories: ‘continued’, ‘reviewed’ or ‘postponed.’ Dieng Units 1, 2 and 3 were listed as ‘continued’, whilst Unit 4 was listed as ‘postponed.’ Patuha Unit 1 was placed under ‘review’ while Units 2, 3 and 4 were declared as ‘postponed.’ A second PD (PD 47/1997) was later issued, dated November 1st 1997, succeeding and modifying PD 39, which restored Patuha Unit 1 to ‘continued’ status. A third decree PD 5/1998 issued on January 10th 1998, expressly rescinded PD 47/1997 according to which Patuha Unit 1 was again listed as under ‘review, and 12 projects not yet having completed financing were cancelled outright. According to OPIC, the final policy reversal occurred as a direct result of

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250 Although it cannot be conclusively confirmed that the IMF directed Suharto to rescind the contracts with the IPPs, the story was confirmed by numerous Indonesian officials, as well a then World Bank representative in Jakarta. A subsequent letter to the Indonesian government from the U.S. Congress in January 1998 would also allude to the IMF’s role in the contractual dispute. The condition was allegedly one of 80 attached to the IMF loan package.

251 Again, the assertion appears as likely given that during this time it was widely reported that the President’s eldest daughter ‘Tutut’ was effectively operating as the country’s de facto power broker with the President’s knowledge and connivance and she was intimately involved in the power sector deals, including receiving shares in one of the IPPs, valued at $49 million.

252 According to information provided by a former CalEnergy executive, at this point construction on Patuha Unit 1 had not even begun although financing had been closed.
conditions attached to the ‘Letter of Intent’ signed by the Indonesian government, with the IMF.  

In the meantime, CalEnergy had in the December of 1997 written to PLN seeking assurance that it would continue to meet its obligations ‘notwithstanding anything to the contrary’ in the Presidential Decrees. PLN did not respond to the letter. Later in testimony before the Arbitral Tribunal, the then President of PLN informed the court that the government had expressly ordered PLN not to respond. The initial letter addressed to the Indonesian authorities was later followed by a second latter, subsequent to the third PD, including to the Ministry of Mines and Energy and the Ministry of Finance, informing them of PLN’s failure to meet its contractual obligations, and requesting assurances so as to prevent the private lenders to the Dieng facility from foreclosing on their loans.  

On March 5th 1998, the President Director of PLN wrote to Himpurna and Patuha Power Ltd., re-affirming the effect of PD 39/1997 and 5/1998, according to which ‘Dieng (unit 4) had been categorized as postponed, as well as PLN and Pertamina’s intention to be bound by the decrees.’ In June, the CEO of CalEnergy Indonesia, Don O’Shea, wrote to PLN formally invoking the ‘commencement of the initial thirty day discussion period’ on the basis that PLN had failed to comply with certain identified provisions, subsequent to which CalEnergy could begin formal arbitration under Article 8.1 of the ESC.  

One month later, an emergency meeting of the Dieng and Patuha Joint Operating Committees was convened (9th July), comprised of representatives from Pertamina,  

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256 Interview notes, former CalEnergy executive.

PLN and CalEnergy, though no agreement could be reached.\textsuperscript{258} CalEnergy responded on August 14\textsuperscript{th} by initiating proceedings under the arbitral provisions in the ESC, by serving a ‘Notice of Demand for Arbitration’ to PLN and the Republic of Indonesia.\textsuperscript{259} With respect to the Republic of Indonesia, the Notice was served pursuant to two letters from the Minister of Finance of Indonesia, to each of the Project Companies, dated April 1996.\textsuperscript{260}

At the preliminary procedural meeting of the Arbitral Tribunal (October 5\textsuperscript{th} and 6\textsuperscript{th}), it was agreed that the arbitral hearing would proceed in two stages. The first Tribunal would hear the case against PLN, pursuant to which it would then hear the case against the Indonesian government. When the first hearing commenced on January 21\textsuperscript{st} 1999, CalEnergy immediately requested that the ESC be terminated, informing the Tribunal that it would be seeking restitution for costs incurred, associated with the development and construction of the Dieng and Patuha geothermal facilities in the amount of $315 million, plus unpaid invoices of $64 million from March 1998 to March 1999. In addition, to the costs claim, CalEnergy then sought damages for lost profits of $1.946 billion. PLN for their part denied the alleged breach of the ESC. They also challenged the jurisdiction of the court to hear the case, which they claimed violated the Indonesian Civil Code, as the contracts were tripartite, and the case could not therefore be heard without Pertamina being enjoined to the case.

The tribunal rejected PLN’s arguments, but took the opportunity to comment on what they termed the ‘deficient normative environment that is the Indonesian Legal Code.’\textsuperscript{261} In particular, they noted that there existed a ‘frustrating confusion of hierarchies of laws and decrees, leading to a situation where today PLN is reduced to arguing that important contracts signed with foreign investors actively promoted by

\textsuperscript{258} Interview Notes former CalEnergy executive.
\textsuperscript{259} \textit{Mealey’s International Arbitration Report}, Vol. 14, #12, December, 1999, 1-165.
\textsuperscript{260} The claim against the Government of Indonesia resulted from a letter provided CalEnergy from the Ministry of Finance committing it to ‘ensure PLN met its financial obligations under the contracts.’ CalEnergy would later claim the letter was a Ministry of Finance guarantee, whereas the Ministry of Finance claimed that it was a ‘comfort letter’, citing the Indonesian constitution as expressly prohibiting the granting of guarantees as interpreted by CalEnergy.
\textsuperscript{261} \textit{Mealey’s International Arbitration Report}, Vol. 14, #12, December, 1999, p. 70. The code, it was noted, was derived from the Dutch criminal and commercial code, enacted by the colonial administration in 1847, itself based on the Napoleonic civil code, long since modified by Holland and France. The seriousness of the situation was noted by the Tribunal insofar as not only were certain fundamental contract law concepts such as \textit{force majeure} absent, but more basically, it was written in a language that most of the Indonesian legal community did not speak.
the Government and indeed approved by a Minister, are illegal. Indeed, that it was ‘forced by the most powerful levels of government to enter into contracts that were designed to benefit a politico-financial oligarchy, without heed to the public welfare.’ To this, the Tribunal appeared sympathetic, stating, ‘Thus far the Arbitral Tribunal is in agreement with what counsel to PLN has so eloquently advocated. But what the Tribunal cannot allow is for PLN to benefit from the deficiencies of its own legal system, or from the absence of proper checks and balances in the public sector.’

In keeping with these comments, the Tribunal found that PLN had breached the ESC, and in consequence of its breach ordered PLN to pay CalEnergy the sums of $391,711,652 (Dieng) and Patuha $180,570,322. Explaining the basis for the awards, the Tribunal noted that the amounts were comprised of damages for costs (damnum emergens) and lost profits (lucrum cessans). Commenting on the award for lost-profits in particular, the Tribunal averred that while it agrees that the figure should include some amount beyond merely costs to recognize the benefits from the ‘bargain-struck’, the claim presented to the Arbitral Tribunal—‘A US$2.3 billion return—including the unpaid invoices —would represent a 630% profit on a US$315 million investment.’ Consequently, the award for lost profits was reduced to $117,244,000.

The judgment served to spark an immediate escalation of the dispute. PLN filed an application for an annulment of the award while Pertamina immediately filed a suit in the Jakarta Central Court requesting to be enjoined to the proceedings, failing which they filed an application for an injunction that was immediately granted. Lawyers representing the Indonesian government then informed the Arbitral Tribunal and CalEnergy that they could not proceed with the second arbitration against the Indonesian government while the Jakarta Court injunction was still in-effect, without breaking the law, the penalty for which carried a fine of $1 million per day.

264 The CalEnergy appointed arbitrator, Mr. A.A. de Fina added an annexe to the award stating that the method of valuation of the lucrum cessans penalizes the Claimant unfairly, in the absence of findings of malicious intent or lack of good faith.
The Arbitral Tribunal rejected the legal pleadings of PLN and Pertamina, reminding the Indonesian government of the seriousness of the affair, warning it not to attempt to "use the instrumentality of its own court system to subvert the Terms of Appointment." On September 7th 1999, the Arbitral Tribunal delivered the Procedural Order to the effect that it was not persuaded that the government of Indonesia does not have ‘statutory domain’ over Pertamina, whilst also reminding the Indonesian authorities that the State is responsible for acts of its judiciary under international law. Finally, in violating the contractual terms of appointment with regard to the ESC arbitration provisions, the Indonesian government has violated ‘the sanctity of agreements’ which ‘is a fundamental rule of international law.’ Consistent with the reasoning, the Tribunal ordered the second hearing against the government to convene in the Peace Palace at The Hague under UNCITRAL Rules, ostensibly to avoid breaching the Jakarta Central Court injunction. Despite the change of venue, however, the ‘legal seat of arbitration’ would remain in Jakarta as per the ESC.

The Indonesian government then wrote to the Arbitral Tribunal expressing its ‘outrage’ at the manner in which a Tribunal ‘sitting in a dispute governed by the law of Indonesia has deemed it unnecessary to give any consideration of such laws and has deemed it appropriate not only to disregard an order of, but to issue official insults to, the courts of such jurisdiction.’ The law firm representing Indonesia then wrote to the Secretary-General of the International Centre for the Settlement of Investment Disputes (ICSID) seeking to have the president of the Tribunal removed on the grounds that the Republic of Indonesia has ‘lost confidence in the Tribunal’s fairness, impartiality and respect for the law.’ ICSID denied the request, however, with the result that Indonesia then filed an injunction before the District Court of The Hague seeking to restrain CalEnergy from ‘entering the Peace Palace at the Hague’ or

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267 The principle to which the arbitrator was referring is that of Statutory or Eminent Domain. In this instance, the assumption of statutory domain meant that although the Indonesian government need not be in control of each and every decision made by its parastatals, it could still be held responsible for their actions, as it possessed statutory domain over both PLN and Pertamina, including the legal action brought by the latter.
participating in the hearings anywhere within the Kingdom of the Netherlands.\footnote{Mealey’s International Arbitration Report, Vol. 14, #12, December, 1999, B-23.} Again, the application was denied, the hearing date set for September 22\textsuperscript{nd} 1999.

However, when the Tribunal was convened on the morning of the 22\textsuperscript{nd}, the Indonesian appointed arbitrator, Professor Priyatna, failed to appear. Explaining why this was the case, Mr. Paulsson (the chairman) detailed what he noted were confusing events that had allegedly taken place the day before. The events concerned allegations that Professor Priyatna was forcibly prevented from appearing by unidentified members of the Indonesian government domiciled at the Embassy. Statements to this effect were taken from two Dutch nationals present at Schiphol airport, where the alleged incident took place, as well as, from the CalEnergy appointed arbitrator, who confirmed the testimony of the two Dutch nationals.\footnote{Professor Priyatna while not confirming the allegations did confirm that he had been met at the airport by a Mr. Warrow and that he had been handed a letter instructing him not to attend the arbitration hearings \textit{Mealey’s International Arbitration Report}, Vol. 14, #12, December, 1999, B-27.} Despite the absence of one of the three arbitrators the Chairman decided to continue with the hearings noting that the law on Truncated Tribunals was well established, while reminding those present that the “The behaviour of counsel [Indonesian] is contrary to the spirit and purpose of Resolution 31/98 of the United Nations adopted by the General Assembly on 15 December 1976.”\footnote{Mealey’s International Arbitration Report, Vol. 14, #12, December, 1999, B1-B49, B-24. parenthesis added.}

In handing down the decision of the truncated (two person) Tribunal, the Chairman, noted, despite the attempt by Indonesia and to some extent CalEnergy to pit ‘the the authority of the Arbitral Tribunal against that of the Indonesian Courts . . . this case does not, in the Arbitral Tribunal’s view, require general pronouncements on the relative allocation of authority between the courts and arbitrators.”\footnote{Mealey’s International Arbitration Report, Vol. 14, #12, December, 1999, B-28.} Referring specifically to the legal arguments forwarded by the Indonesian legal team, regarding the injunction issued by the Jakarta Central Court, the Tribunal noted, while ‘it is recognized that nations may have some leeway in determining how an award may be enforced, the same is not true with respect to enforcement of agreements to arbitrate, which are covered by Article II of the 1958 New York Convention.’\footnote{Mealey’s International Arbitration Report, Vol. 14, #12, December, 1999, B-29.} A failure to
fulfill obligations that are undeniably international in character thereby gives ‘rise to the international responsibility of the State.’ Concordant with the reasoning, the Tribunal found Indonesia to have defaulted under the terms of appointment insofar as it had failed ‘to cause’ PLN met its contractual obligations as it had undertaken to do, thereby reaffirming the original arbitral award granting CalEnergy damages of $591 million in respect of the Dieng and Patuha power plants.

ECA and Diplomatic Efforts to Mediate and Settle the Dispute(s)

The dispute between PLN, Indonesia, and CalEnergy was, however, only one a number of similar disputes with foreign IPPs. Of the 27 projects, 12 had been permanently cancelled owing to their not having completed financing at the time PD 5/1998 was issued. Of the remaining projects, the anecdotal evidence suggests that all bar two were either partially financed or insured against political risks by national insurance agencies. And of the two projects not insured by ECAs, one was insured by the World Bank Group’s insurance provider, the Multilateral Investment Guarantee Agency (MIGA).276 At least six ECAs provided direct loans, or political risk covers for the power projects. The Japanese and United States insurers’ had the largest exposures, with Germany’s Hermes also having significant exposure to the sector.277 Given the significant financial exposure of the ECAs to the power-sector in Indonesia, OPIC and other ECAs were among the first to arrive in Jakarta at the onset of the financial crisis.

Indeed, CalEnergy had written to OPIC immediately following PD 39/1997 that had reclassified the Dieng and Patuha projects.278 The letter noted that CalEnergy had received the letter from the Republic of Indonesia (PD 39/1997) but that they would

276 Enron’s Pasuran project was the only IPP insured against political risks, by the Multilateral Investment Guarantee Agency (MIGA), a subsidiary of the World Bank Group. Enron made a claim under the contracts of insurance as soon as the dispute began in September 1997, receiving $25 million in compensation from MIGA, despite never having begun construction. After lengthy negotiations, the Indonesian government reached an agreement with MIGA to refund it for the payment in September 2001, two months after a similar agreement was concluded with OPIC.

277 Charles R. Smith, FOIA Request, September ‘U.S. Pays for Clinton-Riady-China Connection’, Thursday, Feb. 1, 2001. According to a declassified diplomatic communiqué sent by the then U.S. Ambassador to Indonesia, Stapleton Roy, ‘OPIC’s combined exposure in Indonesia is $1 billion, or 5% of OPIC’s global exposure, all in the electric power sector.’ The figure was later confirmed in testimony before the U.S. Congress by the then President of OPIC, George Munoz.

278 Interview Notes former CalEnergy executive.
keep building the plants in the hope that classification of the projects would later be amended. In addition to informing OPIC, CalEnergy also enlisted the support of two influential Nebraska Congressmen, John Christiansen, and the Doug Bereuter, Chairman House International Relations Subcommittee on Asia and the Pacific. The Congressmen, along with the Commerce Secretary, William Daley, the Energy Secretary, Federico F. Pefir, Secretary of State Madeleine Albright, and the Secretary of Treasury, Robert E. Rubin then wrote to the Indonesian Parliament in a letter dated 12.01.98. The letter urged ‘in the strongest possible terms to remove CalEnergy’s geothermal projects at Patuha and Dieng from the "Review" and "Postponed" lists established by Presidential Decree No. 39 (P.D. No.39).’ The letter continued, ‘We do not believe that efforts by the Government of Indonesia to comply with the IMF program should come at the cost of its contractual obligations. In addition, it would be wrong for the U.S. Government to support an IMF austerity program that, in the case of CalEnergy's projects, would subject the U.S. Government to significant expense under OPIC political risk insurance policies.’

The U.S. position was clear and unified. It supported Indonesia’s efforts to regain economic stability but not at expense of U.S. foreign investors. Later that same month, Jakarta also played host to U.S. Defense Secretary, William H. Cohen and Treasury Secretary, Larry Summers in quick succession, each of whom reaffirmed the U.S. position in talks with their Indonesian counterparts. At the end of January, Michael Camdessus once again arrived in Jakarta, warning the Indonesian’s of the seriousness of failure to adhere to the economic restructuring program agreed the previous October. Later that same month, the IMF announced that it was considering

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279 Interview Notes former CalEnergy executive.
283 Although the U.S.’s position concerning Suharto’s future appears at this stage to have been undecided, by early 1998, the U.S. was clearly hedging its bets. Evidence of this was provided by the fact that the U.S. was already publicly courting leading political figures including Dr. Amien Rais and Megawati Sukarnoputri, both of whom met the U.S. Ambassador to Indonesia during this period in what were very public circumstances. In this respect, it is notable that both undertook to support the IMF’s stabilisation program with U.S. backing.
284 Interview notes, former President Director PLN 1990-1992, Professor Zuhal.
halting further loan disbursement for Indonesia pending resolution of several outstanding issues.\(^{285}\)

While pressure from abroad mounted on Suharto, his position at home, despite the worsening economic situation appeared secure. On March 12\(^{th}\) 1998, he was unanimously reelected by the Derwan Perwakilan Rakyat (DPR) for a seventh five-year term, taking the opportunity to again renounce many of the IMF reforms. The response from the IMF was immediate. Within weeks the Deputy Managing Director of the IMF, Stanley Fischer arrived in Jakarta for ‘crisis talks.’ A compromise was agreed, under which the IMF agreed that existing food subsidies could be maintained in return for which Indonesia agreed to the sale of twelve state-owned enterprises and the abandonment of the proposed currency peg.\(^{286}\)

That same month CalEnergy CEO, David Sokol arrived in Jakarta, for the second time in four months, making clear his preference for immediate arbitration, rather, than continued mediation and renegotiation.\(^{287}\) Soon after, his second visit at the end of April, the decision was taken to temporarily evacuate all expatriate employees and their families, bar a skeleton staff, to Singapore because of the worsening security situation. The decision was in hindsight prescient, as ethnic tensions between the Chinese and Indonesian communities spilled over into violence. In addition to ethnic tensions, clashes between pro-democracy student demonstrators and pro-Suharto supporters, organized as Panca-Sila, also turned violent. On May 12\(^{th}\) members of the armed forces opened fire on student demonstrators occupying the Parliament building, killing six.\(^{288}\) The military crackdown failed, however, to dampen growing opposition. Moreover, in what was a critical development, Indonesian Marines were reported to have marched with the pro-democracy protesters, ostensibly to protect them from the police. That same week, the head of the Indonesian army, General Wiranto made a public apology for the deaths of the six pro-democracy supporters.\(^{289}\)


\(^{287}\) Interview Notes former CalEnergy executive.

\(^{288}\) Kar-yiu Wong (ed.), ‘The Asian Crisis: What has happened and why?’ p. 38. In total, an estimated 1,200 people died in the violence in and around Jakarta during this period, though conclusive data is unavailable.

With his main support base split—the armed forces—and the country in economic and political turmoil, Suharto announced his decision to retire on national television on May 21st, 1998, designating the then Vice-President and long-time confidante B.J. Habibie as his successor.\textsuperscript{290} However, the move failed to restore political order as hoped, with demonstrators and the media now turning on the relatives and associates of the former President, calling for their prosecution for ‘korrupsi, kolusi, and nepotism’ (KKN).

By June 1998, the worsening security situation in Jakarta appears to have precipitated a reappraisal of U.S. policy toward Indonesia in Washington. The concern of the Treasury, Commerce and State Department’s switching from the protection of U.S. investor interests and Indonesian economic austerity to facilitate implementation of the IMF program to the more immediate concern in the words of a Commerce Department report, of stopping Indonesia from ‘falling over.’\textsuperscript{291} As a result, the U.S.’s, contribution to the IMF bailout package, previously held up in Congress by Democrats wishing to see human rights conditions attached to the loans, was passed without further amendment.\textsuperscript{292}

In July, the World Bank announced the formation of a Consultative Group on Indonesia (CGI), comprising more than 80 members, from twenty countries, and fourteen different International Organizations. Chaired by the World Bank, the CGI

\textsuperscript{290} It was widely reported that the Indonesian military, specifically, General Wiranto engineered Habibie’s accession, much to the annoyance of General Prabowo, who purportedly threatened the incumbent President lest he not be appointed head of Indonesia’s armed forces in preference to Wiranto, in what became known as the ‘Prabowo Incident.’ Prabowo was at one time rumoured to be a likely successor to Suharto, being Suharto’s son-in-law. Later, Prabowo was removed from the military by Wiranto placing Johny Lumintang as head of Kostrad (the army’s strategic command). See Donald K. Emerson Political Legacies and Prospects for Democratic Development in South East Asia: Burma and Indonesia (The National Bureau of Asian Research). See Patrick Walters ‘The Indonesian Armed Forces in the Post-Soeharto Era’ in \textit{Post-Soeharto Indonesia: Renewal or Chaos} (Geoff Forrester ed.), (Singapore: Institute of South East Asian Studies, 1999), p. 62-63.

\textsuperscript{291} The report entitled ‘Dealing with Unwanted Partners’ was prepared by the \textit{Commerce Department} as a brief for the visit of Commerce Secretary William H. Daley. See \textit{Sustainable Energy and Economy Network}, Corruption, Collusion and Nepotism’, available online at http://www.seen.org/pages/ifis/ECAs/paiton.shtml Date accessed 27.02.04.

\textsuperscript{292} This may also be explained by the fact that when Democrats first blocked the package on April 22nd Suharto was in power, whereas by the time Congress voted to pass the bill, Suharto had stepped down, replaced by the more moderate Habibie. It is significant to note that the U.S. contribution of $18 billion to the $47 billion package was by far the largest, with the Japanese contribution as the second largest being limited to just $5 billion.
was designed to enable a diverse collection of stakeholders to formulate strategies to assist Indonesia, including overseeing loan disbursement and the monitoring of policy initiatives and assistance programs. That same month, the ADB announced it had agreed a $1.8 billion emergency package for Indonesia to finance balance of payments obligations.

In the meantime, any lingering doubts that OPIC may have had about the validity of allegations concerning corruption in the Dieng and Patuha projects were surely dispelled by a confidential Commerce Department Report prepared for the Secretary of Commerce, William H. Daley’s visit to Singapore in June 1998. The report entitled ‘Dealing with Unwanted Partners’ noted, ‘the corrupt Suharto regime purchased 25 power projects similar in size to Paiton, while there was only demand for one of these, meaning that the IPPs were competing against one another to be the single survivor.’ Moreover, OPIC must have been aware of this as the same report noted that ‘Both Ex-Im and OPIC confirmed that if the 1200 MW Paiton project were to go on line, it would most likely wipe out any further GOI need for other power plants. Thus, several other major U.S. power developers with other projects, in varying stages of completion, are potential competitors with Edison for Power Purchase Agreements.’ By way of final confirmation the report concludes, ‘that Unocal, CalEnergy and El Paso Energy were all subject to corruption, collusion and nepotism.’

Within two months of the drafting of the Commerce Department Report, the first OPIC mission arrived in Jakarta in August 1998. During the visit, OPIC’s ‘Advocacy Mission’ met with PLN and Indonesian government officials, as well as with representatives from CalEnergy. Meetings were also held with the World Bank and the ADB. According to reports, several proposals were discussed, including the need to renegotiate the PPAs. The agency’s efforts to engage the support of the World Bank and ADB in their attempt to ensure the contracts were honoured by the Indonesians were declined, however. The World Bank in particular making clear that

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293 The $1.8 billion loan made Indonesia the largest recipient of ADB loans, while it was the second largest recipient of World Bank loans during 1998-99.
295 FOIA Request, September 2002, Marcus Chadwick.
296 FOIA Request, September 2002, Marcus Chadwick.
they had not supported the contractual model in the first place, second they had paid a significant price for their opposition, and they were not about to step in now to support OPIC or any of the other ECAs that participated in financing and insurance.\textsuperscript{297}

Despite the initial setback a second OPIC ‘advocacy mission’ arrived in Jakarta a month later in August, 1998, to attend a World Bank sponsored conference on power sector restructuring.\textsuperscript{298} The policy cleavages that had surfaced in the first meeting were again underscored on this occasion by the proposals put forward by the multilateral Banks’ for ‘Power Sector Restructuring.’ The model called for immediate cancellation of the original contracts followed by negotiation of new contracts to better reflect Indonesia’s parlous financial position. The proposals amounted to a rejection of the BOOT investment-model, supported by the ECAs, under which foreign power companies were contracted to a single off-taker (buyer) in favor of giving the foreign producers direct access to consumers, beginning with industry. During the mission, OPIC officials also met again with PLN, the Indonesian government and CalEnergy.

Following OPIC’s Mission to Jakarta, representatives from CalEnergy, including their legal counsel, flew to Washington in late August. It is at this point according to unconfirmed reports that tensions between OPIC and CalEnergy began to surface.\textsuperscript{299} OPIC advised CalEnergy to hold on, and not to press for arbitration. Their position was apparently based on the belief that the Indonesian’s were taking steps to re-finance PLN direct from the central government budget. This information they noted had been given to them by the U.S. Ambassador to Indonesia who in a cable to the agency in August 1998, reported that he had met with the CEO of PT Energi Sengkang, who claimed to have seen evidence laying out a new payment plan for the IPPs. Further, ‘Sengkang, CalEnergy, Unocal and Arco will be paid directly with monies from the state budget currently set aside for PLN.’\textsuperscript{300}

A fortnight later, OPIC President, George Munoz arrived in Jakarta for discussions with PLN and Indonesian officials. Following the visit, CalEnergy officials travelled

\textsuperscript{297} Interview Notes World Bank, Jakarta.
\textsuperscript{298} FOIA Request, September 2002, Marcus Chadwick.
\textsuperscript{299} Interview Notes former CalEnergy executive.
\textsuperscript{300} Interview Notes former CalEnergy executive.
to Washington to meet with OPIC, again being told to hang-on. During the meeting CalEnergy officials informed the agency of their intention to pursue arbitration and make a claim under the contracts of insurance.301 OPIC, for their part, again affirmed their preference for a negotiated settlement, warning CalEnergy that they would have to take the matter to arbitration as they would not pay the claim willingly.302 A third OPIC mission to Jakarta took place at the beginning of November 1998. On this occasion, however, CalEnergy officials refused to attend the scheduled meeting with PLN, claiming it to be a waste of time.303 When a fourth OPIC mission visited Jakarta in January of 1995, CalEnergy again refused to attend negotiations despite having received a written offer from PLN, to renegotiate the ESC, albeit with a 25 percent reduction in the tariff rate.304

Although Indonesia’s economy began to stabilize towards the end of 1998, the government’s budget position remained in a parlous state. In order to continue funding balance of payments expenses and ongoing reforms, both the ADB and the World Bank committed additional funds to Indonesia in March 1999. The World Bank working closely with the IMF developed an interim Country Assistance Strategy that would guide the Bank’s lending and technical assistance programs for the next twelve to eighteen months. The Bank also noted that according to its estimates power-sector restructuring would cost Indonesia $7 billion in the three years to 2001.305 Also in March, the ADB announced it had agreed a $400 million ‘Power-Sector Restructuring Loan Program.’ According to unconfirmed reports, however, the U.S. purportedly blocked the loan disbursement pending the successful resolution of the outstanding contractual claims of the IPPs.306 Additional bilateral support was also forthcoming, from Indonesia’s largest foreign investor and bilateral donor Japan, in the form of the ‘New Miyazawa Initiative’, announced at the beginning of April 1999. The funding package earmarked $3.8 billion of new funds for Indonesia, including

301 Interview Notes former CalEnergy executive.
302 The OPIC contracts of insurance provide that disputes between the insured and the insurer regarding claims payments are to be heard by the American Arbitration Association (AAA). The AAA is a not-for-profit dispute resolution body operating under New York State law. See www.adr.org
303 Interview Notes former CalEnergy executive.
304 PLN’s offer was confirmed in an interview with a former CalEnergy executive.
306 Interview notes World Bank, Jakarta.
$400 million for power-sector restructuring to be supplemented by an additional contribution of $65 million from Germany’s ECA, the Kreditanstalt für Wiederaufbau (KfW).307

The following month, the specially convened UNCITRAL Tribunal handed down the first of the two arbitration awards in CalEnergy’s favour. Following the award, and Pertamina’s successful application for an injunction against CalEnergy, a third meeting was convened in Washington between CalEnergy and OPIC. Also at the meeting were representatives from the U.S. State Department and Treasury. According to unconfirmed reports, Treasury made clear that although they supported CalEnergy in principle their main concern was Indonesia’s financial and political stability and for this reason they pressed CalEnergy to hold-off, whilst lobbying OPIC not to pay claims.308 - The State Department on the other hand expressed their sympathy for CalEnergy’s plight but like Treasury made clear that the claim was not their first priority.309 - The message was clear; according to CalEnergy, they would receive only minimal support because the priority for the State Department and Treasury was the Paiton I project.310

Facing tacit opposition from the IMF, the World Bank and the ADB in the form of their alternative plan for power sector restructuring in Indonesia, as well as from the State Department and Treasury, OPIC along with other exposed national insurers appear at this juncture to have changed track. Thus where previous diplomatic negotiations between OPIC and the Indonesian government were conducted bilaterally, in June of 1999 the first ‘Joint ECA Mission’ arrived in Jakarta.311 The mission according to unconfirmed reports was strategically timed, to enable the ECAs to literally get-in-first, before the Indonesian’s met with the World Bank chaired CGI in Paris, scheduled for 26-27th of June.312 Also invited to attend the meetings arranged

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307 See http://www.seen.org/db/Dispatch?action-OrgWidget:880-detail=1 Date Accessed: 30.05.05.
308 Interview Notes former CalEnergy executive.
309 According to David Sokol (CEO CalEnergy), Treasury informed him that $290 million—the value of the claim—did not even appear as a blip on its radar.
310 Interview Notes former CalEnergy executive.
311 FOIA Request Marcus Chadwick, September 2002.
312 Six agencies from five different countries participated in the joint mission, including the Ministry of International Trade and Industry (MITI) and the Japan Export Import Bank, the Export Risk Guarantee Department (ERG Switzerland), OPIC, the U.S. Ex-Im Bank, HERMES (Germany) and the People’s
with PLN and Indonesian officials were the World Bank and the ADB, although only as observers.  

According to reports from Indonesian officials who attended the meetings, the ECAs presented a unified position in their negotiations, thus thwarting attempts by PLN to renegotiate the power contracts individually. The new President Director of PLN, Adhi Satriya, made clear during the meetings that first, he was opposed to the Paiton I project, and second, he would instruct PLN’s legal counsel to pursue the illegal contracts line of defence in the forthcoming CalEnergy arbitration against Indonesia, scheduled for October (1999). According to reports, the position angered the Japanese who made clear their preference that the issue of corruption was a separate one that should be dealt with following the resolution of the ‘commercial’ disputes. The mission was concluded with each of the ECAs signing a joint letter to the Minister of Finance warning, ‘The future investment climate will be shaped by a long term resolution that protects the fundamental rights of investors’ adding that a refusal to pay would ‘impair Indonesia and our ability to work with you in the future.’

That the ECA-Indonesian government negotiations had reached a stalemate did not halt events in Jakarta, however, which continued apace, culminating in the country’s first democratic elections in October 1999. The result, Abdurrachman Wahid (Gus Dur) was elected as Indonesia’s first democratically elected President. The win was widely acclaimed as a victory for moderate reformers, clearing the way for the implementation of the remaining economic reforms and in the words of the new President, the ‘clean up of the power sector.’ In order to achieve the last of these goals, he immediately established an Inter-Ministerial team to renegotiate the

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313 FOIA Request Marcus Chadwick, September 2002.

314 Interview Notes former Head of PLN.

315 Although impossible to prove, the diplomatic muscle of JEXIM (or the Japanese) appears to have been flexed when Adhi Satriya was removed as President Director of PLN at the end of the year, just twelve months after succeeding the former Head, Djiteng Marsudi. The removal of Satriya for pursuing the illegal contracts defence in the CalEnergy case at the request of the Japanese was also confirmed by a former representative of the World Bank in Jakarta who was closely involved in the workout. Interview Notes World Bank, Jakarta.


317 Wahid was the head of the country’s largest Muslim organization, Nahdlatul Ulama. His victory was widely reported to have been engineered by Dr. Amien Rais, head of the DPR.
outstanding contractual disputes. The move was immediately welcomed by IPPs and ECAs alike as a signal that the impasse had been broken.

Hoping to capitalize on the apparent momentum, a second ‘Joint ECA-mission’ arrived in Jakarta within a fortnight of Wahid’s victory. The focus of the second joint-mission according to reports was the Paiton I project, who the week before had an injunction placed on it by the Central Jakarta Court at the request of Pertamina. In addition to discussing Paiton I, the ECAs again sought to enlist the support of the World Bank and the ADB, but again to no avail. Later that month, the second arbitral hearing held in The Hague would confirm the original PLN Award, ordering Indonesia to make payment to CalEnergy. The second arbitral award was the signal that CalEnergy had been waiting for.

Within a week of obtaining the final award, a fourth meeting was convened in Washington between CalEnergy and OPIC. This fourth meeting was held in the Congressional Office of Jon Christiansen (Republican). Also in attendance was the second Nebraska Congressmen, Doug Bereuter (Republican), as well as Nebraska Senator’s Chuck Hagel (Republican) and Bob Kerry (Democrat). Representing Treasury was Tim Geitner (Under-Secretary for International Affairs), while Jane Charmers represented the U.S. State Department. Finally, also in attendance were the President of OPIC, George Munoz, as well as the in-house legal counsel for OPIC, Thomas Mahaffey. During the meeting, according to unconfirmed reports, it became clear that Treasury firmly opposed OPIC paying CalEnergy’s claim. The State Department for its part was more understanding but offered little more than platitudes. Finally, OPIC reaffirmed its preference for continued negotiation solution, while noting the difficult position it faced, owing to the fact that the dispute was increasingly viewed as a litmus test of the agency’s PRI coverage for infrastructure investors, many of whom were purportedly monitoring the outcome.

It seemed likely that the meeting would end in a stalemate, preparing the way for CalEnergy to begin arbitration against OPIC, until Jon Christiansen weighed in on

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318 Interview Notes former Head of PLN.
319 Interview Notes former CalEnergy executive.
320 Interview Notes former CalEnergy executive.
321 Interview Notes former CalEnergy executive.
behalf of CalEnergy. According to the information received, Christiansen, and to a lesser extent Bereuter asked OPIC President, George Munoz whether he was seriously stating that a U.S. company’s claim was being denied after they had evacuated their personnel, the Indonesians had kidnapped their own arbitrator, they had not been paid for 10 months and had received two arbitration hearings in their favor?322 Faced with the prospect of additional Congressional scrutiny OPIC acquiesced, agreeing to pay the claim in full.323

Having agreed to CalEnergy’s claim, OPIC then set about recovering the money from the Indonesian government pursuant to the applicable treaty arrangements concerning subrogated claims. To this end, a delegation from the agency flew to Singapore to meet with the Indonesian Minister of Economic Affairs to resolve the outstanding claim in early November 1999.324 According to the Indonesian magazine, Gatra, ‘the US government warned at the same time that it would invoke the so-called Helms amendment. This, it was reported, ‘would have led the U.S. to vote against Indonesian interests in multilateral financial institutions, including the Paris Club, while reserving the right to take further additional measures as required.’325

From this point forward the focus for OPIC and to a lesser extent the other ECAs, split into two. The first and original aim was to force Indonesia to renegotiate the contracts as fast as possible. The secondary aim led by OPIC but with support from the other ECAs, was to enforce OPIC’s claim against the Indonesia. To this end, a third joint ECA Mission arrived in Jakarta in November 1999.326 On this occasion, though relations remained cordial, the ECAs made clear their displeasure at the injunction issued by the Jakarta Central Court against the Paiton I project investors. In

322 According to unconfirmed reports, the subtext underlying the question posed to OPIC by Doug Bereuter was clear If OPIC did not pay the claim, Bereuter was in a position, to make OPIC’s next reauthorization hearing particularly uncomfortable. Interview Notes former CalEnergy executive. Doug Bereuter is the Chairman of the House of Reps. Subcommittee Asia and the Pacific as well as being a member of the House International Relations Committee as well as being represented on the House Subcommittee International Economic Policy and Trade.
323 Again, according to unconfirmed reports, the company on hearing the claim would be paid, made an offer to OPIC to forego the 90 day statutory waiting period in return for a reduction in compensation of $50 million. Further, they offered to receive the money as a side-payment, rather, than a claim, so that there would be no need to subrogate the claim, and increase the debt burden on Indonesia. The offer, however, was flatly rejected. See Interview notes former CalEnergy executive.
324 Interview Notes former Head of PLN.
a follow-up letter to the Republic of Indonesia, dated December 9th 1999, the six ECAs again warned that ‘the private power problem . . . should be settled as among first priority and as soon as possible.’

In early January 2000, OPIC officials again traveled to Jakarta to pressure the Indonesian government to settle the outstanding debt owed to the agency, though once again no settlement could be reached. OPIC officials returned to Jakarta in March 2000, to begin negotiating for compensation and to persuade Indonesia to drop the court action against Paiton I. The initial prognosis was not, however, promising. On March 7th the Finance Minister, Bambang Sudibyo stated in a speech before the DPR, ‘the government will not pay the OPIC claim, because the government doesn’t have the money.’ OPIC’s response was forthright. The following day, Indonesian officials were warned that their assets in the U.S. were subject to seizure unless the claim was settled. That same day, representatives of the German, Japanese, and Swiss ECAs also arrived in Jakarta so that in the words of the Head of ERG (Swiss ECA), Peter Silberschmidt, they could ‘join together to exercise pressure on Indonesia.’ Also, on March 8th the U.S. Ambassador to Indonesia, Robert Gelbard held a press conference in which he formally indicated U.S. government dismay at the statements made by the Finance Minister, whilst privately warning that the U.S. would block Indonesian efforts to reschedule $5.45 billion of Paris Club debts due to be negotiated in mid-April, if a settlement could not be reached.

Although somewhat delayed, it appeared that the escalation of the rhetoric was beginning to pay dividends, when on April 18th Indonesia announced that it was dropping its legal action against the Paiton I project. That same month, PLN and Indonesian officials from the Ministry of Finance (Edi Karsanto, Director General of External Affairs, and Fuad Barwazier, Minister of Finance) and the Minister of Mines

329 Interview Notes former Head PLN.
334 Business Times (Singapore) April 25th ‘Foreign Bullies’
and Energy flew to Washington on two separate occasions for further talks with OPIC.\textsuperscript{335} According to Kuntoro Mangkusubroto, President Director of PLN (2000-2002), he along with his Indonesian colleagues left the first meeting in disgust.\textsuperscript{336} Explaining the decision, he noted that the Indonesian delegation had arrived under the pretense that they would be negotiating pursuant to the U.S-Indonesia Investment Agreement (1967). They were, however, curtly informed by the President of OPIC that they should forget about that, at the same time handing them a document. The document, it was explained to them, contained OPIC’s acceptable ‘Terms of Settlement.’ Further, when they had agreed to the terms, they should knock on his door, where he would be waiting for them. At which point he abruptly left the room and returned to his office.\textsuperscript{337} The second meeting was according to reports more amicable, though no agreement was reached.

In the June of 2000, a fourth Joint ECA Mission visited Jakarta.\textsuperscript{338} According to reports, the focus of ECA efforts now switched from the CalEnergy-OPIC claim to resolving the remaining IPP disputes, though again they made clear that any settlements would need to be negotiated jointly with the ECAs. Following the mission, PLN officials again traveled to Washington for ten days of scheduled talks with OPIC.\textsuperscript{339} In an acutely timed press conference one day before the negotiations were due to finish, the U.S. Ambassador to Indonesia, took the opportunity to again remind his hosts that their assets in the U.S. were subject to seizure if the OPIC claim was not finalized.\textsuperscript{340}

There followed a lull in diplomatic activity until January 2001, when the \textit{Electric Utility Weekly} reported that Indonesia had made an offer to settle the OPIC debt, in the amount of $240 million, but the offer had been rejected by OPIC officials.\textsuperscript{341} Following the offer, PLN and Indonesian officials once again traveled to Washington

\textsuperscript{335} Interview Notes former Head of PLN.
\textsuperscript{336} Kuntoro was replaced as the Minister of Energy and Mineral Resources by the current President Susilo Bambang Yudhoyono.
\textsuperscript{337} Interview Notes former Head of PLN. This story was also recounted to Professor Louis T. Wells Jr., Harvard Business School, by two separate individuals who were present at the meeting.
\textsuperscript{338} Freedom of Information Act, Marcus Chadwick, September, 2002.
\textsuperscript{339} Interview Notes former Head of PLN.
to present a modified offer, according to which Indonesia agreed to settle the debt in full, on the proviso it be included with Paris Club debts. The modified offer was rejected by OPIC, however.\footnote{OPIC, Indonesia’s PLN Reach Agreement Over Failed Power Deals,’ Asia Pulse, June 2nd, 2001. Interview Notes former Head of PLN.}

Once again there followed an lull in diplomatic efforts to resolve the dispute, until May 1\textsuperscript{st}, when Minister for the Economy, Rizal Ramli suddenly announced that Indonesia had agreed to pay OPIC debt in full, under Houston Terms.\footnote{OPIC, Indonesia’s PLN Reach Agreement Over Failed Power Deals,’ Asia Pulse, June 2nd, 2001. According to the terms of the agreement, Indonesia would be given an initial three year grace period, after which the principal and interest was payable at an interest rate of 6.125\% over eleven years. Houston terms were agreed as part of the Paris Club rescheduling.} According to documents later released by OPIC, the initial agreement had been reached on May 2\textsuperscript{nd}, providing for final closure on May 31\textsuperscript{st}.\footnote{Freedom of Information Act Request Marcus Chadwick, September, 2002.} The deadline was later extended at the request of Indonesia to July 31\textsuperscript{st}, however, due to the difficulties created by the impending political transition, following the impeachment of President Wahid by the DPR in May 2001.\footnote{The reason for Wahid’s impeachment is not entirely clear. It would seem, however, that the claims of corruption against the Muslim cleric ostensibly the reason for his impeachment were an extension of party politics. To elaborate, Wahid dismissed two senior cabinet members, Laksamana Sukardi and Yusf Kalla, in April 2001, on the grounds that both were guilty of corruption. Sukardi (former Minister for Investment and State Enterprises) was a member of the PDI-P, while Kalla (former Industry and Trade Minister) was a member of Golkar. As part of the reshuffle, Wahid also announced his new cabinet. Unlike his first ‘cabinet of national unity’, comprised of 35 members drawn from a broad spectrum of political parties, his new cabinet was comprised largely of Wahid ‘associates’ from his own National Awakening Party (PKB). Perhaps more importantly, of the new cabinet, only two members were drawn from the PDI-P (the Vice-President Megawati’s party), while the Golkar party (Suharto’s party) retained only the post of Attorney General, handed to Marsuki Darusman. However, in a curious move, the post was removed from cabinet rank. As a result, the impeachment was widely interpreted as a continuation of party politics, with few believing the claims that Gus Dur had misappropriated S2 million, as was alleged. It is also likely that the ABRI (TNI) had a hand in the Muslim Cleric’s downfall, following their public anger at the President for his decision to grant independence to East Timor, following that country’s referendum in September 1999.}

On July 23\textsuperscript{rd}, former Vice-President Megawati Soekarnoputri was sworn in as Indonesia’s second democratically elected President. The media immediately began asking questions about the deal announced by the now former Finance Minister, Rizal Ramli.\footnote{No author, ‘Government urged to explain OPIC deal to the public’, The Jakarta Post, Saturday, September 01, 2001.} In particular, why had a deal been signed that left Indonesia in a worse position than the agreement reached between his predecessor, Prijadi Praptosuhardjo and OPIC? Second, who authorized the agreement, as immediately after President
Megawati took office on July 23rd, she declared the cabinet of her predecessor, Abdurrachman Wahid, to have non-active status, thereby preventing Minister’s from making decisions without consulting her.

Fearing the agreement would again fall through, OPIC officials flew to Jakarta on July 31st with a mandate to shore up the agreement with the new President. Finally, after nearly two years of negotiations, the Ministry of Finance and OPIC announced that they had reached a final agreement dated August 27th 2001. According to the joint press release, Indonesia was to pay OPIC $260 million plus interest, and a further $140 million to the lending syndicate. Finally, on August 31st 2001, a ‘Settlement, Agreement, Assignment and Release’ was signed between the Indonesia and OPIC under which title to the project would be transferred to Indonesia upon payment of $260,000,000 (the principal) plus a daily interest charge equivalent to $43,630 per day from the date of agreement. The Settlement Agreement in respect of CalEnergy’s claim between OPIC and Indonesia signalled the final resolution of a dispute that had dragged on for more than four years. CalEnergy for its part exited Indonesia and have made no new foreign investments since. Dieng is now operated jointly by Pertamina and PLN as a 60 MW plant, while the Patuha plant remains only 30 percent finished.

In agreeing to a final settlement, OPIC and PLN concluded a dispute that had been damaging for all concerned. For both parties, however, the conclusion of the

348 http://www.usindo.org/Briefs/Peter%20Watson.htm, Date accessed 05.10.04, USINDO Economic Briefing, Update on Indonesia's Settlement with OPIC Hon. Peter Watson President and CEO, Overseas Private Investment Corporation (OPIC), September 6, 2001, Washington DC.
349 No author, ‘Government urged to explain OPIC deal to the public’, The Jakarta Post, Saturday, September 01, 2001. Credit Suisse First Boston was the lead arranger. Note, the agreement calculated the interest on the debt at approximately $43,000 per day for 11 years.
351 See, ‘Settlement, Agreement, Assignment and Release’ “[T]he parties agree to keep this Agreement and related Documents and the subject matter hereof and thereof confidential; provided that nothing shall prevent ABC from disclosing such information pursuant to the United State Freedom of Information Act (FOIA) consistent with its character as “business confidential information” (and the parties hereby declare that for the purposes of the FOIA this Agreement and Related Documents and the subject matter hereof and thereof constitute “business confidential information”).’
352 For an up to date overview (as at early 2006) of the current status of the foreign IPPs, See ‘Field Development and Contractor Status’ http://www.indonext.com/report/report433.html. Date Accessed 01.02.06. The funds for the recommissioning of the Dieng plant were provided by an OPIC Recommissioning Loan. See www.usembassyjakarta.org/download/geo2002.pdf
CalEnergy dispute was merely the beginning of even more protracted negotiations that would last a further eighteen months before the issue of Paiton I was finally resolved. In this respect, it is significant to note that to tell the story of the CalEnergy dispute, is to tell but one story of many such IPP disputes that is itself but one small part of the crisis that beset Indonesia, which in turn is but one story of the Asian financial crisis that began some four years earlier with the devaluation of the Thai Baht. In this regard, it is hardly surprising that the CalEnergy dispute resolution process was highly complex, drawing in a large number of parties each offering competing policy prescriptions owing to its becoming entangled with the financial crisis as well as the more than a dozen other IPP disputes. Consequentially, for the disputants this meant the need to balance competing interests.

For the U.S. government in particular, the dispute required a delicate diplomatic touch to balance its immediate economic interests against long-term political interests. In the first instance, this included an overriding desire to ensure the continued political stability of its long-time regional partner and former bulwark against Communist expansion, whilst also encouraging the transition to democratic rule. At the same time, in light of the significant number of U.S. IPP investors, the U.S. also needed to be seen to uphold the sanctity of contract whilst at the same time being wary of increasing Indonesia’s already crippling debt-burden. Moreover, in seeking a resolution to the IPP disputes and the unfolding financial crisis the United States faced opposition to its proposals from the IMF, whose initial recommendation to then President Suharto to abrogate the contracts as part of its record bailout had sparked the CalEnergy dispute in the first place.

For OPIC, like the U.S. government, the dispute was highly complex, requiring the agency to balance numerous competing interests. Most immediately, given the manner in which the dispute became a yardstick by which private infrastructure investors measured the value of its breach of contract cover, and given the need to make threats credible in its dealings with the Indonesia authorities, the agency needed to be seen to be prepared to pay claims, whilst at the same time being mindful of broader U.S. foreign policy goals. It was not only U.S. infrastructure investors that were watching the outcome of the claim, however. That is, the agency also had to bear in mind the response of its Congressional constituents who were also keeping an eye
on the outcome as a means to judge the worth of the investment insurance program.\(^{353}\) In particular, the agency needed to be mindful of the fact that paying CalEnergy’s claim would likely precipitate additional claims by U.S. IPP operators’, the total value of which potentially exceeded $1 billion. Had this occurred, although OPIC possessed sufficient reserves to cover the exposure, it would no doubt have attracted additional and unwanted scrutiny from Congressional critics.

It is perhaps because of these conflicting goals that OPIC occupied such a prominent role with respect to diplomatic bargaining separate from World Bank chaired CGI and other more established instruments of U.S. economic diplomacy. It is to the role of OPIC in resolving the CalEnergy dispute that the next section now turns. In particular, where the previous section sought to detail the key events culminating in the resolution of the dispute, this next section by contrast is principally concerned to analyse the role played by the agency through its advocacy and mediation efforts, and more broadly the impact of PRI on the resulting ‘politics’ of dispute resolution.

**OPIC Investment Insurance and the Politics of Dispute Resolution**

In order to address the questions outlined, the first task will be to consider the evidence with respect to the impact of OPIC PRI on the bargaining strategies employed by CalEnergy. The second task will then be to examine OPIC’s judicial role in the course of paying or rejecting claims under the contracts of insurance, including consideration of the implications of OPIC’s actions for the customary international law of expropriation. This will be followed by an analysis of the agency’s diplomatic role in seeking a settlement on behalf of CalEnergy.

To begin, the empirical evidence makes clear that not only was the availability of PRI critical to CalEnergy’s investment decision-making process but the provision of investment insurance by OPIC altered the incentives facing the insured investor(s)

\(^{353}\) That this was the case is supported by two pieces of evidence, first, the meeting in Washington D.C. in which the Nebraska Senator’s and Congressional representatives were alleged to have asked what is the point in PRI if OPIC rejects the claim given the circumstances of the dispute? Second, George Munoz, the then OPIC President was called before Congress on more than one occasion in 1998 and again in 1999, to explain what OPIC’s position was with respect to the disputed claims, as well as the agency’s total exposure to the Indonesian power sector.
even before the onset of the financial crisis and abrogation of the contracts by PLN.\textsuperscript{354} It did so, in the initial instance because the provision of PRI signalled \textit{de facto} home state support so as to effectively legitimize the investment-vehicle (BOOT contracted to a single off-taker). This, in turn, impacted the terms of financing available to CalEnergy, so as to, in turn, provide the company with incentives to litigate rather than accept a negotiated settlement.

Evidence that OPIC support was interpreted by prospective lenders (non-recourse debt providers) in this manner is provided by the terms of financing available to the successive IPPs entering the Indonesian market, specifically the credit protection mechanisms applied to the non-recourse debt.\textsuperscript{355} Foremost in this regard concerns the fact that because the commercial lenders to later IPP projects interpreted OPIC and ECA support as signalling that the risks associated with these transactions were manageable, CalEnergy’s non-recourse debt providers did not, in contrast to the Paiton I financing (the ‘frontier’ project), demand what is known as a ‘first-lien’ on the PRI contract, or in the parlance of PRI a lender’s ‘carve-out.’

The lender’s ‘carve-out’ provides that any proceeds from a PRI claim made by project sponsors (equity providers) are paid to the lending syndicate. The absence of a ‘carve-out’ in the Dieng and Patuha financing thereby created incentives for CalEnergy to pursue litigation rather than seeking to renegotiate the ESC. It did so, because unlike the Paiton I project sponsors, for whom the proceeds from a PRI claim would be used to automatically pay down any outstanding non-recourse debt, CalEnergy made the claim under the contracts of insurance in the knowledge that any monies received

\textsuperscript{354} The CEO of CalEnergy, David Sokol, had made clear prior to serious consideration of CalEnergy undertaking projects in foreign countries that PRI was a pre-requisite. This information was later confirmed in testimony before Congress by Mr. Sokol himself, wherein he was quoted as saying ‘And I can tell you, we would not have invested in Indonesia if we'd not been able to obtain OPIC insurance, because the transparency issues were absolutely clear to us.’ (Financial Crisis in Asia: Hearing Before the Subcommittee on Asia and the Pacific and International Economic Policy and Trade of the Committee of International Relations House of Representatives One Hundred and Fifth Congress Second Session, February 14\textsuperscript{th}, 1998). With this stipulation in mind, CalEnergy wrote to OPIC requesting PRI even prior to the signing of the PPA in December 1994. See Interview notes former CalEnergy executive.

\textsuperscript{355} Interview Notes former CalEnergy executive. CalEnergy’s average cost of capital was approximately eight percent, whereas Edison Mission Energy and Sumitomo Corporation’s average cost of capital for Paiton I was 10.5 percent. According to the information received, the difference was accounted for the by the fact that the Paiton I lender’s (non-recourse debt providers) demanded a $200 million cash-collateral to be held in an escrow account and to be drawn on in the event of a dispute, whereas CalEnergy’s lenders demanded no such collateral.
would be theirs to keep, thereby enabling them to effectively divest their interests in the two projects without losing their original equity stake. In contrast, even had OPIC agreed to indemnify Paiton I, the project sponsors would have lost most if not all of their original equity stake, amounting to several hundred million dollars.

Apart from the manner in which the provision of OPIC financing and insurance informed the terms of financing available to successive IPPs, the second critical feature of the insurance contract in terms of the incentives facing CalEnergy was the inclusion of what one eminent arbitrator labeled ‘a highly unusual clause’ making claims payable on the failure to honour an arbitral award.\(^{356}\) The inclusion of the clause, in combination with the absence of a lender’s carve-out created incentives for CalEnergy to pursue litigation as a means to expedite the PRI claims—the ultimate goal—rather than renegotiate the ESC with PLN.\(^{357}\) In this regard, although the different outcomes of the two disputes should not be attributed to variations in the project financing structures alone, nor even the particular clause concerning arbitral awards, it is notable that while CalEnergy chose to pursue litigation, and to subsequently exit the market, the Paiton I project is today operating profitably, albeit at reduced tariff levels.

The impact of OPIC PRI was not limited to shifting the incentives associated with particular bargaining strategies for the disputants however. Turning firstly to the evidence with respect to the quasi-judicial powers conferred on the agency in the course of paying or rejecting claims, although the claim was ostensibly paid as a result of the non-performance of the arbitral award, being considered a breach of international law by OPIC (the ‘B’ claim), in paying the claim OPIC effectively validated the findings of the arbitrators, and thus by implication CalEnergy’s claims to the effect that its interests in Dieng and Patuha had been expropriated in


\(^{357}\) Section 4.01(b) of the OPIC Contracts of Insurance provides that compensation is payable if valid, final arbitral awards have been obtained against PLN or Pertamina pursuant to the project agreements as a result of acts not covered by section 4.01(a), such awards have also been attained against the GOI pursuant to the GOI Support Letters, such awards have not been paid for 90 days, the non payments constitutes a violation of international law and deprives the investor of its fundamental rights in the insured investment, and the Foreign Enterprises were not in breach of the Project Agreements.’ The non-payment of the award was considered a violation of international law by OPIC as Indonesia is a signatory to the New York Convention on the Enforcement of Arbitral Awards (1957), having ratified the treaty in October, 1981.
contravention of the international law of foreign investment (‘A’ claim). Moreover, in so doing the agency sanctioned CalEnergy’s bargaining strategy, specifically, their refusal to negotiate after mid-1999, while at the same time de-legitimizing the Indonesian government’s legal defence under the clausula doctrine even in instances of economic contagion as beset Indonesia during the dispute.

Apart from the impact of PRI on the insured investor’s bargaining strategy and the quasi-judicial powers manifest in the decision to pay or reject CalEnergy’s claim, the empirical evidence also makes clear that OPIC’s advocacy and mediation role materially altered the observed processes of dispute resolution, as well as the final settlement. Most immediately, the agency’s decision to permit CalEnergy to keep building the Dieng facility in contravention of PD 39 (September 1997) materially altered the outcome of the dispute. It did so because the Dieng facility was, by CalEnergy’s own admission, only 30 percent complete when the decree was issued, thus suggesting that had construction stopped in accord with the decree, the compensation payable would have been significantly, if not proportionally reduced.

Of greater significance, however, concerns the key role played by the agency in overseeing diplomatic negotiations with PLN and the Republic of Indonesia. In this regard, OPIC occupied the key bilateral diplomatic role normally reserved for the State Department and executive more broadly. The second critical mediation function performed by OPIC concerned its efforts to coordinate the response of other ECAs and the multilateral development banks to the IPP disputes, separate from the parallel Paris Club negotiations and the financial rescue package provided Indonesia by the

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358 See OPIC, ‘Expropriation Claim of MidAmerican Energy Holdings Company (formerly CalEnergy Company Inc.),’ Memorandum of Determinations, Contracts of Insurance Nos. E374, E453, E527 and E759. CalEnergy made two separate claims under the contracts of insurance. An initial claim for expropriation, the ‘A’ claim and a second claim (the ‘B’ claim) subsequent to its receipt of the arbitral awards against PLN and the Republic of Indonesia. Ultimately, the claim was paid for the non-performance of the arbitral award, as per Section 4.01 (a) of the Contracts of Insurance.

359 And although such statements must in the absence of a counterfactual remain conjecture, using the formula outlined by the arbitral tribunal as well as OPIC’s published claims determination the compensation payable would have been substantially reduced, even allowing for the inclusion of damages for lost profits (lucrum cessans), i.e. compensation for in the words of the chief arbitrator ‘the bargain-struck.’ Further, it is reasonable to assume that OPIC would have been aware of this given the customary international law norms regarding ‘date of valuation.’ For this reason it was incumbent upon OPIC, if not imperative, to find an alternative legal basis on which to pay the claim, and more importantly, an alternative date of valuation, which fortunately for OPIC arose through the non-performance of the arbitral award.
IMF. To this end, it is clear that OPIC took the lead in seeking support from the World Bank and the ADB for its proposed IPP workout, as well as coordinating the four ‘Joint ECA-missions’ to Indonesia. And although its efforts with the World Bank and the ADB were unsuccessful, the anecdotal evidence suggests that the unified ECA position served its purpose insofar as it closed off one potential bargaining strategy aimed at settling each of the IPP disputes individually, i.e. foreclosed attempts by the Indonesian government to play the IPPs off against one another. In this respect, the threat was clear, acting in unison the ECAs could seriously hamper Indonesian efforts to attract new FDI. Moreover, they could also stall efforts to renegotiate the remaining IPP contracts. Had this occurred, the cost to Indonesia would potentially have dwarfed the value of the disputed CalEnergy claim. In this regard, the empirical evidence makes clear that OPIC fulfilled what amounted to a critical bilateral diplomatic role.

Moreover, although the State Department retains overall administrative control of OPIC, the evidence shows that the agency enjoyed considerable autonomy in mediating the dispute, and therefore in the formulation of U.S. anti-expropriation policy. Most immediately, the anecdotal evidence suggests that OPIC paid the claims contrary to the wishes of both the State Department and Treasury, each of whom made clear their preference for a negotiated solution or failing that, the claim should be delayed until after Indonesia has managed to regain both economic and political stability. Furthermore, OPIC, then, twice rejected offers to settle the subrogated claim made by the Indonesian authorities between 2000 and 2001, despite overt pressure from the State Department and Treasury for a final settlement as a means to expediting the negotiations for the remaining IPPs.

To conclude the analysis of the role of OPIC in dispute resolution, the empirical evidence from the CalEnergy dispute makes clear that OPIC PRI influenced the bargaining strategies employed by the disputants far beyond that which is normally associated with the failure to control for moral hazard. More particularly, the evidence demonstrates that OPIC fulfilled a critical role with regards to both diplomatic bargaining as well as exercising judicial powers in determining the validity of the

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360 See Interview Notes former CalEnergy executive.
361 See Interview Notes former Head of PLN.
CalEnergy claim. It did so in the latter instance because in accepting CalEnergy’s claim the agency was effectively in a position to make unilateral assessments regarding the legitimacy of the actions of the Indonesian government. To this end, in agreeing to indemnify the insured, OPIC’s actions served to denote the government of Indonesia’s behaviour as a violation of the international law of expropriation. As such OPIC is not only an insurance provider but instead, the agency serves as a governance mechanism in contemporary investor-state disputes. It does so because as Lake notes, ‘the design, construction, and maintenance of mechanisms to enforce agreed upon behaviours . . . lies at the heart of contracting, as a process, and governance, as both an analytic concept and the set of mechanisms actually employed.’

At the same time, however, while the evidence makes clear that OPIC now occupies a central role in terms of the enforcement of international property and contract rights on behalf of U.S. infrastructure investors, the result is not so much a radical as a qualitative shift in the resulting politics of disputes resolution. It is so because in the absence of PRI many if not all the tasks of diplomatic protection performed by the agency would have been performed by the State and or Commerce Departments. Moreover, it is important to note that in deciding to espouse CalEnergy’s claim or otherwise, the State Department is guided by the same statutes concerning ‘expropriation’ as is OPIC, and as contained in the U.S. Foreign Assistance Act, 1961. That this is the case suggests that the major difference in terms of the resulting politics of dispute resolution concerns therefore the fact that it is likely that the State Department could not have coordinated the joint ECA Missions as OPIC did, owing to the latter’s sub-state contacts; one may assume, not equally available to State Department officials.

Similarly, although the payment of the PRI claims by OPIC amounted to a judicial determination of the validity of CalEnergy’s grievances against PLN, had OPIC not performed this function, the task would have fallen to the State Department. While the latter would not have paid compensation direct to CalEnergy, in seeking

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363 The guidelines for expropriation are contained in the following U.S. civil code, See § 620(a), (g), (j), (1), (o), Foreign Assistance Act of 1961 (Public Law 87-195; 22 USC 2370). Furthermore, both the State Department and OPIC would likely have sought legal advice from the Foreign Claims Settlement Commission (FCSC) of the Department of Justice regarding the validity of the claim.
compensation from Indonesia on the company’s behalf, it would in effect have validated CalEnergy’s claims of expropriation, tantamount to a de facto judicial determination of their legality. Moreover, given that this is the case, it may also be assumed that the effect, with respect to the implications for the body of customary international law of expropriation would be little different insofar as the judgement would have created interstitial legal norms.

Finally, it must also be noted that while the inclusion of the arbitral clause in the PRI contracts issued by OPIC to CalEnergy was unusual, the non-performance of an arbitral award would create a state-state claim under the applicable bilateral and multilateral treaty provisions governing FDI between the U.S. and Indonesia, irrespective of the particulars of the PRI contracts. Turning firstly to the applicable bilateral treaty, the U.S.-Indonesia Investment Agreement (1967) explicitly states that the non-performance of a valid arbitral award is sufficient to create a state-state claim. Similarly, and turning to the multilateral treaty commitments, Indonesia has ratified the UNCITRAL Model Law on arbitration (1976), under which the arbitrations were held, as well as the New York Convention on the Enforcement of Arbitral Awards (1958), both of which provide that the non-performance of such awards may be considered a violation of international law.364 The point to note therefore is that although the linking of PRI claims to arbitral awards is unusual, the incentives to litigate provided by such a clause are not unique. Instead, the governing treaty provisions create similar incentives to litigate.

While the use of OPIC as a tool of economic governance did not result in a radical shift in the politics of dispute resolution, serving instead as a second layer of protection for CalEnergy and as a complement to the existing investment-related treaty framework, the presence of PRI did effect a second change. However, on this occasion the change concerned not the international politics of dispute settlement so much as the politics of U.S. foreign policy-making. Of critical importance in this regard, concerns the manner in which the presence of PRI served to diffuse policy-making power away from the executive to CalEnergy (insured investor). It did so because of the pressure that CalEnergy were able to bring to bear upon OPIC through

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364 Indonesia is also a signatory to the International Convention on the Settlement of Investment Disputes, World Bank Group, as of 1966.
their home state Congressional and Senatorial representatives so as to force the agency to pay their claim in opposition to both the State Department and Treasury’s preference for a negotiated solution. The presence of OPIC PRI served, therefore, to delimit U.S. expropriation policy leeway, which until that point had been characterized by the overriding desire to avoid political and economic chaos in Indonesia over and above the narrow interests of U.S. IPP investors, including those of CalEnergy.

From the perspective of the U.S. foreign policy-makers, the increase in the use of PRI is therefore significant because OPIC’s expropriation policy is subject to domestic political pressure in a way that the State Department is not. Foremost in this respect concerns the fact that OPIC must seek Congressional reauthorization whereas the State Department and or other instruments of U.S. foreign economic policy-making need not. The result is that the State Department is shielded from domestic politics whereas OPIC must always bear in mind the response of its Congressional constituents, who are themselves bound to the insured investors, i.e. corporate America.

Thus far, the chapter has examined the role of OPIC and the impact of the contracts of insurance on the politics of dispute resolution and U.S. foreign policy-making. The final task remaining therefore is to consider the implications of the findings regarding OPIC governance in terms of the theorized institutional restraints against expropriation, beginning with theories that posit the efficacy of legalised modes of dispute settlement.

**OPIC Governance: State power Vs. Power of Legal Rules**

Turning firstly to the theory of legalized modes of investment dispute resolution, the empirical evidence makes clear that international law played a role insofar as it

365 It is important to note that although the pressure applied was significant in itself, CalEnergy’s leverage and thus that of the company’s home state representatives was amplified by the knowledge that should the immediate pressure be unsuccessful, CalEnergy could challenge OPIC’s decision under the arbitral provisions contained in the contracts of insurance wherein disputes between the insured and the agency are to be heard by the American Arbitration Association (AAA).
delimited the acceptable modes of argumentation. To this end, Indonesia sought to
base its defence on the international law doctrine of *clausula rebus sic stantibus*,
whilst CalEnergy proclaimed the need to adhere to the corollary legal doctrine of
*pacta sunt servanda*. Against this, however, and contrary to the theory of legalized
dispute resolution the negotiations and bargaining during the course of the dispute
was not as the theory states characterized by a casuistic style of argumentation
drawing on established precedent concerning breach of contract in investor state-
contracting, including debates over the applicability to the facts at hand of particular
legal principles, rules and norms.

That is, although the discourse was not framed solely in terms of naked state power
and interests, apart from the arbitral channel as one of three separate resolution tracks,
the negotiations were notable for the absence of a legalized discourse between the
disputants. And although this may be attributed in part to the under-developed state of
customary international law concerning expropriation, i.e. the apparent lack of a clear
legal precedent, the ambiguity and therefore inadequacy of international law in this
respect does not explain the tenor of the negotiations. Indeed, the absence of
secondary legal rules that enable judgements to be determined in accord with
overarching legal doctrines where primary rules do not provide clear precedent, as
was the case in the CalEnergy dispute, could be expected to result in more rather than
less legalistic discussion.

That this is the case serves, however, to reveal not the patent ambiguity and therefore
inadequacy of international law so much as it does the true character of the
international law of foreign investment and the use of legalized modes of dispute
settlement more broadly, specifically, the observed increase in the use of offshore
arbitration to resolve disputes. It does so because it must be recalled that CalEnergy’s
decision to pursue arbitration reflected not some assessment of the normative sanction
of law nor even the perception that offshore arbitration is a particularly efficacious
mode of settling disagreements of this type, instead it reflected the belief that
obtaining an arbitral award was the most efficient means of expediting the PRI claim.\textsuperscript{366}

In making this assertion, the intention is not; however, to argue that legalized modes of dispute resolution had no impact on the processes of resolution and the final settlement. In particular, the capacity of CalEnergy to initiate (access) arbitral proceedings did alter the politics of dispute resolution. Foremost in this respect was the manner in which the arbitral provisions enabled CalEnergy to transfer jurisdiction from the Indonesian court system, as explicitly provided for in the underlying ESC, to The Hague, i.e. international jurisdiction, when faced with the legal injunction issued by the Jakarta Central Court. In the absence of such provisions, it is likely that the injunction would have been used to either delay the proceedings indefinitely or, alternatively and more probably, for sufficiently long a period as to force CalEnergy to accept the renegotiation of the tariff schedule (pricing) consistent with the desires of the Indonesian authorities.

That this is the case should not, however, be allowed to deflect attention from the fact that in seeking arbitration, CalEnergy were responding to the incentives provided them by the inclusion of the clause in the contracts of insurance linking claims to the non-performance of an arbitral award, and more broadly, the overarching treaty framework consisting of both bilateral and multilateral treaties governing FDI. Moreover, it is abundantly clear that the arbitral awards cannot explain the outcome, i.e. that compliance was a product of the normative authority embodied in transnational commercial law. Indeed, the empirical evidence makes clear that even after the two arbitral awards the Indonesia authorities did not intend to enforce the awards in accord with bilateral and multilateral treaty commitments. In this respect, the significance of third-party arbitration concerned the fact that by obtaining the awards, CalEnergy left OPIC with little room for manoeuvre when called upon to determine the validity of the claim under the contracts of insurance.

\textsuperscript{366} That this was the case was confirmed by two interviewees both of whom were intimately involved with the workout, and were therefore privy to private information concerning the motivations underpinning the pursuit of arbitration.
Perhaps more fundamentally, the empirical evidence makes clear that the decision to pay CalEnergy’s insurance claim was taken at the fourth meeting in Washington between the insured investor, the executive and OPIC in November 1999. And although it is conceivable that the pressure applied to OPIC to pay the claim by the investor’s home state representatives (Nebraska) may have reflected some understanding of the legal merits of CalEnergy’s expropriation claim (i.e. its validity under treaty and customary international law) that the decision was taken in this manner is difficult to reconcile with the notion of legalized dispute resolution. That is, despite the allusions to the contrary in OPIC’s published claims determination; evidenced by the apparently painstaking efforts to construct a legal argument, the decision to pay the claim was not solely a product of consideration of the applicable legal rules derived from the principles of customary international law of expropriation. Instead, international law was used as a means of justifying a decision made according to the diktats of domestic politics in Washington, rather than being the basis for that judgement.

That the principles of international law did not underpin the decision to pay the claim, Karen Mills contends, is attested to by the fact that despite OPIC’s efforts to construct a legal argument, the published reasoning concerning the legal basis for the claim payment—the failure to honour an arbitral award—appears to have contravened what amounts to a well-established principle of customary international law that requires the ‘insureds to exhaust all remedies against the subject government before making a claim on the political risk insurance.’ And although such an assertion cannot be substantiated, the evidence, as Karen Mills points out, suggests that ‘OPIC, too must have been aware of the invalidity of the awards to which it had been subrogated, for it did not make any attempt to enforce these awards in any jurisdiction but rather

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367 The point here is not to deny that the Nebraska Congressmen and Senators may have some understanding of the law in this respect, or may at least have received advice on the merits of the claim from among others the Foreign Claims Settlement Commission (FCSC is part of the U.S. Department of Justice) before pressuring OPIC. It is, however, to argue that even if this was the case, the FCSC applies U.S. statutes not customary international law, thus the understanding to the extent that it reflected an appreciation of the applicable legal principles most likely reflected a particular interpretation of the law, centred on the ‘U.S. law of regulatory takings’ which applies a very different interpretation of ‘acts of state’ i.e. eminent domain than is traditionally applied by international courts, i.e. the right of the state to regulate in the public interests, including with respect to private property.


369 See Karen Mills, ‘Judicial; Attitudes to the Enforcement of Arbitral Awards – Indonesia, Karim Sani Law Firm, Jakarta.’
proceeded to pressure the Indonesian Government to agree to reimbursement, still without seeking legal clarification nor relief anywhere.\textsuperscript{370}

The empirical evidence therefore makes clear that power-in-law informs the use of ostensibly ‘legalized modes of dispute resolution.’ It does so, apart from the fact that the pursuit of arbitration reflected the belief that it would be enforced, because as has been noted offshore arbitration is not some consensually agreed ‘independent’ mechanism for dispute resolution. Instead, the use of arbitration represents in legal parlance what is known as ‘the internationalisation of state contracts.’\textsuperscript{371} The term is used to denote the process wherein local jurisdiction is \textit{superseded} in favour of international or transnational jurisdiction. In this instance, Indonesian civil law as the ‘seat’ of jurisdiction was effectively displaced in favour of private international trade law. And this, as the evidence makes clear, is rarely a consensual process, particularly where the law is opaque, as it clearly was in this instance. In this regard, it is clear that international property and contract rights, and more narrowly the use of legalized modes of resolution are a function of state power, as it is power that determines which set of legal rules will be used to adjudicate disputes and ultimately be enforced.

Perhaps more fundamentally still, however, U.S. power and interests dictated not only the use of legalized modes of dispute resolution, but also their non-use. To elaborate, immediately following the claim payment the Indonesian government signalled its intention in both private and public not to pay the agency as the contracts were obtained through fraud and misrepresentation (KKN) and were therefore invalid.

\textsuperscript{370} See Karen Mills, ‘Judicial; Attitudes to the Enforcement of Arbitral Awards – Indonesia, Karim Sani Law Firm, Jakarta, p. 6. For a critical analysis of the legal basis forwarded to explain the transfer of the seat of the arbitral tribunal from Jakarta to The Hague, and then the decision to proceed with the second arbitral hearing before a truncated tribunal see Karen Mills, ‘Judicial Attitudes to the Enforcement of Arbitral Awards – Indonesia, Karim Sani Law Firm, Jakarta. According to Karen Mills, the removal of the tribunal to The Hague, as well as the decision to hear the dispute before the truncated tribunal following the non-appearance of the Indonesian appointed arbitrator, Priatna, violated UNCITRAL arbitration rules (Article 54) which sets out the procedure for truncated tribunals. The article states that where one party’s appointed arbitrator cannot be present that the tribunal must allow that party two weeks to either appoint another one, at which point, if it fails to do so, then a truncated tribunal may hear the dispute. Yet, in the CalEnergy case, the Tribunal chairman, Paulsson chose to go ahead on the same day, foregoing the two week grace period provided for in the UNCITRAL Model Law (1976). To this end, she rightly notes that the questionable nature of the move is reflected in the fact that although the case against the GOI brought by CalEnergy was heard in The Hague, the published hearings do not specify the ‘location of the court that rendered the award.’

\textsuperscript{371} For a critical analysis of the legal reasoning underpinning the internationalization of state contracts, see M. Sornarajah (2\textsuperscript{nd} ed.), ‘The Internationalisation of state contracts’ in \textit{The International Law of Foreign Investment}, (Cambridge: Cambridge University Press, 2004), p. 416-429.
according to Indonesian civil law. This being the case, according to the terms of the U.S.-Indonesia Investment Agreement (1967), Indonesia could have contested the claim against it by initiating an ad hoc state-state arbitral forum. That it did not exercise this right can only be understood as a product of the capacity of the United States to coax a significant policy shift through a combination of threats and inducements sufficient to defray the political costs to the Megawati administration vis-à-vis the Indonesia electorate (nationalists) of agreeing to reimburse the agency.

The U.S. in particular, did not want to see Indonesia contest the claim in a high profile, and potentially politically damaging, court case. Of immediate concern in this respect was the fear that the hearing would be used as a platform to reopen the issue of whether the Dieng and Patuha plants (and indeed all the IPP deals) were subject to corruption. For OPIC in particular, this issue was of upmost concern as it would no doubt have led to questions about what the agency knew of the alleged improprieties before issuing the insurance, and again, before paying the PRI claim, so as to cast doubt on whether such arbitration would be successful.372

The second motivating factor underpinning U.S. expropriation policy concerned the fact that a lengthy arbitration would likely weaken the ability of the U.S. government and OPIC to force the remaining U.S. investors to accept negotiated settlements rather than mimicking CalEnergy’s strategy of litigation, followed by a PRI claim. Of upmost concern to OPIC in this respect was the Paiton I project owing to the fact that the agency and by implication the U.S. government had invested considerable diplomatic capital in bringing the project to fruition. More broadly, however, it was feared that such arbitration might further enflame Indonesian nationalism, which could in turn threaten other U.S. corporate interests in Indonesia, the value of which far outweighed U.S. interests in the power sector.373

372 This outcome was made more likely because whereas the first President after Suharto, B.J. Habibie, drew his power in part from the former president, the Megawati administration had no such ties, and therefore did not need to seek to protect Suharto’s former associates by withholding information that might have proved corruption in the IPP deals. Moreover, from the perspective of the new administration, releasing such information would have been politically beneficial, as not only was there a backlash against the former associates of the Suharto regime occurring during this time, but Megawati had campaigned on a reformist platform, promising era reformasi. Proving corruption would, therefore, have been politically popular as well as strengthening her reformist credentials.

373 Indeed, enflamed by the local media and anti-U.S. rhetoric, the issue became a rallying point for Indonesian nationalists’, including among both the ruling and opposition parties, members of whom
Two facets of U.S. power, given the aforementioned policy interests, appear as critical to the success of the U.S. government to avoid such a scenario. The first of these concerns unilateral economic sanctions. To this end, the U.S. repeatedly made clear that should Indonesia fail to honour the terms of the Investment-Agreement it was within its rights to seize Indonesian government property in the U.S. equal to the value of the disputed OPIC claim payment.\(^{374}\) The second plank of U.S. sanctions concerned the removal of Indonesia from OPIC and Ex-Im Bank ‘eligibility’ thereby depriving Indonesia of new investment, as occurred in 2000. And although the precise effect cannot be known, denial of OPIC coverage was one may assume significant as few investments in the Indonesian resource sector proceed without some form of ECA support.\(^{375}\)

The second and perhaps the most critical factor of U.S. power concerned its capacity to coordinate both public and private creditors, including through the Paris Club and the World Bank chaired CGI, so as to deny Indonesia access to new loans and or the rescheduling of existing debts in the event that a settlement was not forthcoming. In this respect, the empirical evidence makes clear that the U.S. repeatedly threatened to derail Indonesian efforts to reschedule its debts, including in June 2000, and again in April 2001, on the latter occasion just weeks prior to the CGI organized meeting of Indonesian creditors scheduled for April 23\(^{rd}\)-24\(^{th}\). Faced with denial of access to new loans, the inability to reschedule existing debts and a potentially significant reduction in FDI, President Megawati had little choice but to forego Indonesia’s legal rights under the treaty framework and settle the outstanding debt owed to OPIC.\(^{376}\)

sought to frame the disputed claim as an Indonesia-U.S. issue, so as to bolster their ‘independent’ credentials and with it the spectre of U.S. imperialism.

\(^{374}\) See *Dow Jones International News* ‘US Dismayed at Indonesian Minster’s OPIC Statement’, March 8\(^{th}\), 2000.

\(^{375}\) What is certain this regard, is that the removal of Indonesia from OPIC eligibility delayed UNOCAL’s investment in gas facilities in East Kalimantan the estimated value of which approached one billion dollars, as in order to secure financing UNOCAL needed OPIC support, including both insurance and financing.

\(^{376}\) Settlement of the debt offered the prospect of both significant new investments, as well as improved military ties that in the latter case had been further strained since September 1999, following the imposition of restrictions by the U.S. on the Indonesian armed forces (TNI), in the wake of alleged TNI involvement in paramilitary activities in East Timor. The restrictions included a total ban of sales of U.S. military hardware, and the suspension of all joint military exercises and training programs offered to TNI military personnel. See International Crisis Group (ICG) ‘Indonesia-U.S. Military Ties’ Asia Briefing, No. 17, 17th July 2001 for a good overview of the military ties between the two, and the shared security interests. Evidence of the closer relationship and the importance placed on it by both
It was not only in respect of the CalEnergy dispute and the IPP disputes more broadly that politics and U.S. government power was critical, however. That is, U.S. power informed every aspect of the post-crisis workout. To this end, the U.S. blocked Japanese proposals forwarded as early as September 1997 to establish an ‘Asian Monetary Fund (AMF)’377 The proposals provided for the establishment of a new multilateral financial institution financed with a $100 billion initial cash-injection from Japan that would provide credit facilities for ailing Asian economies, including Indonesia. Fearing that the AMF would increase Japan’s regional influence whilst diluting that of the U.S. sponsored IMF and by proxy U.S. power and influence throughout Asia, the proposals were scuttled by the U.S. In this regard, state power and interests, specifically U.S.-Japanese jockeying, informed every aspect of the IPP workout and financial stabilization package provided Indonesia by the IMF.378

While the U.S. sought to forestall a weakening of IMF influence, and while U.S. power was derived in part from its capacity to deny Indonesia access to new loans, it is significant to note that the IMF displayed considerable autonomy in responding to the crisis, so as to in many instances undermine U.S. policy goals. In particular, there is substantial anecdotal evidence to suggest that the initial decision to rescind the IPP contracts announced by Suharto in September 1997 was forced on him as part of the IMF bailout package concluded two months previously.379 While assertions to this
denations was again apparent when President Megawati became only the second leader to visit Washington D.C. following September 11th. The visit appears to have cemented the relationship, as Indonesia became in the words of the U.S. Ambassador to Indonesia a front-line partner in the ‘war on terror.’ And although the restrictions imposed on the Indonesian military (TNI) remained in place, they were gradually relaxed, beginning with the resumption of U.S. military training for the TNi in 2002.377 See for a good in-depth overview of the politics surrounding the proposal Phillip Y. Lipsey ‘Japan’s Asian Monetary Fund Proposal’ Stamford Journal of East Asian Affairs. 378 There is also evidence to suggest that the U.S. blocked the proposed institution and the Japanese bailout because it provided an opportunity for the IMF to force market (trade and investment) liberalization upon previously recalcitrant Asian governments, as part of the loan conditionalities. Evidence for the assertion is provided by the then Deputy Treasury Secretary, Lawrence Summers who noted ‘The IMF has done more to promote America’s trade and investment agenda in Korea than 30 years of bilateral trade talks’, Quoted in Linda Weiss, ‘State Power and the Asian Financial Crisis’ New Political Economy, Millennium, 1999, p. 31. In support of the assertion Weiss quotes from Chalmers Johnson, ‘Economic crisis in East Asia: the Clash of Capitalisms’, Cambridge Journal of Economics, Vol. 22, No. 6 (1998), p. 653-62. Further, the U.S. did put its money where its mouth was so to speak evidenced by the fact that the U.S. contribution to the IMF’s then record $47 billion bailout was more than three times larger than that of the second largest contribution, Japan’s, contributing some $13 billion more than its Asian rival. 379 As is the case with assertions of this kind, there is no way of proving it. The assertion was widely reported in the Indonesian media, however, on the basis that members of DPR and Suharto’s inner-
effect cannot be independently corroborated, what is certain is that the allegation caused considerable consternation within Congress, sufficient to threaten the U.S.’s $18 billion contribution to the IMF bailout. More generally, the point of division between the U.S. government, OPIC and the IMF centred on the sequence of the proposed bailout and restructuring. The IMF making clear their preference that the IPP workout should be secondary to the major goal of restoring economic stability in Indonesia. Whereas the U.S. government, sought to have the IPP obligations included as part of the debt-workout from the very beginning. Policy autonomy was not, however, limited to the IMF. That is, from the outset, both the World Bank and the Asian Development Bank had refused, despite U.S. pressure, to support the IPP deals. Later, the World Bank and the ADB would again block U.S. and ECA power-sector restructuring proposals.

Conclusions

To conclude the first of the two case studies, the empirical evidence makes clear that OPIC is not just an insurance provider. Instead, the provision of investment insurance and financing serves as a mechanism for economic governance in contemporary dispute resolution, thereby, supplementing the existing bilateral and multilateral treaty-framework. In this regard, the agency fulfils a central role on behalf of U.S. infrastructure investors in enforcing private property and contract rights (‘bargains’), and in establishing the ‘rules of the game.’ It does so, because in agreeing to pay CalEnergy’s claim, the agency effectively delimited the boundaries between normal commercial risks and political risks and thus legitimate and illegitimate modes of host state regulation, i.e. ‘markets’ for the private provision of infrastructure services in

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380 ‘Financial Crisis in Asia’: House of Representatives One Hundred and Fifth Congress Second Session, February 14th, 1998. Despite denials from Treasury and the State Department that they or the IMF had instructed the abrogation of the IPP contracts, the reality is that it was not so much a split between the U.S. government and the IMF as between the executive (State Department and Treasury) and the IMF on the one hand, for whom the restoration of Indonesia’s economic and political stability was the overriding goal (post January 1998) and the legislative branch, OPIC and CalEnergy on the other hand, each of whom felt that Indonesia’s recovery should not be bought at the expense of U.S. corporate interests.

381 Judging by the timing of new loans, it does appear, however, that the U.S. government was successful in its efforts to block a $400 million ADB loan for the purposes of power-sector restructuring pending the final settlement of the OPIC debt.
Indonesia. To this end, the payment of the claim serves to frame breach of contract by a sovereign contracting party as a violation of the international law of foreign investment, even in instances of economic contagion as beset Indonesia; so as to effectively narrow the permissible legal defences for contract derogation under the international law doctrine of *clausula rebus sic stantibus*.

Moreover, the evidence makes clear that OPIC governance was not confined to its quasi-judicial role in determining the validity of investor claims under the contracts of insurance. In particular, the agency also fulfilled a critical diplomatic role in advocating on behalf of CalEnergy (insured investor) through coordinating the joint-ECA missions and in mediating a final settlement. Equally, however, other more established elements of the U.S. foreign policy bureaucracy such as the State Department would have fulfilled a similar role in providing normal diplomatic protection in the absence of PRI. Second, the existing treaty framework provides similar incentives to litigate as did the particular provisions of the contracts of insurance linking claims to the non-performance of valid arbitral awards. In this manner, OPIC governance does not replace the existing hard-law treaty framework instead it provides U.S. infrastructure investors with a second layer of protection, and the U.S. government with a secondary judicial mechanism with which to enforce compliance with legal obligations.

It is not only when things go wrong that OPIC governance is significant, however. That is, the evidence has shown that right from the very beginning the provision of investment insurance and financing for CalEnergy and its U.S. counterparts was critical in enabling the projects to proceed. Thus, in the first instance, the provision of OPIC insurance and financing signalled to U.S. infrastructure investors’ *de facto* home state support for the BOOT investment-vehicle underpinned by limited-recourse financing. In this manner, the provision of PRI directly informed not only the terms of financing but in so doing it structured the incentives for CalEnergy to litigate or pursue a negotiated settlement when the dispute broke-out. In the second instance, the payment of the claim to CalEnergy signalled to the Indonesian authorities U.S. intent with regards to the outstanding IPP disputes involving U.S. investors. In this respect and judging by Indonesia’s apparent policy u-turn, OPIC’s actions in resolving the CalEnergy dispute can be seen to have had repercussions far beyond the case at hand.
so as to inform all of the subsequent IPP settlements including the final-settlement of the flagship Paiton I project in mid-2002.

The question must be asked, however, did OPIC fail to control for moral hazard in this regard? On one level, the answer to this question must be yes. That is, the failure to ensure a ‘lender’s carve-out and the specific provisions linking claims to the failure to honour an arbitral award created incentives for CalEnergy to litigate rather than accept a negotiated solution as did the remainder of the IPP operators. Against this, it must also be acknowledged that the decision to pay the claim was forced on the program’s administrators by Congressional representatives. Indeed, the evidence suggests that OPIC showed real restraint in seeking a mediated solution. Whether this reflected acknowledgement of the dubious nature of the claim given the allegations of corruption attending the project or overarching U.S. policy goals (executive) aimed at preventing economic and political collapse is unclear, however.

What is clear, however, is that while it is certainly the case that OPIC could have made greater efforts to ascertain the identity of CalEnergy’s local partners, it is also the case that greater efforts must be made by both parties if corruption is to be avoided in the awarding of contracts of this sort. In short, it is simply unreasonable to lay the blame squarely on the shoulders of companies such as CalEnergy and insurers such as OPIC, if efforts are not forthcoming from host authorities to control corruption in contracts of this sort. Of particular significance in this regard was Indonesia’s decision in September 2000 not to prosecute the former President (Suharto) and his associates.382 The decision indicates not only a lack of political will but points to a more fundamental issue in Indonesia, arising from the lack of separation between the judiciary and the legislative branch, as well as more importantly economic and political elites. In this regard, the solution requires a complete overhaul of the political culture in Indonesia that will not be accomplished in the near to medium term as is evident from the fact that some five years after the

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382 The decision made by the then President of Indonesia, Abdurrahman Wahid (Gus Dur) in September 2000 was defended on the grounds that a series of strokes had left the former President incapacitated and therefore too unwell to face trial. However, the lack of political will was again in evidence when the conviction of his son, Hutomo Mandala Putra (Tommy) Suharto, (only one of two former relatives and associates convicted), was overturned in 2002.
dispute the current President, Susilo Bambang Yudhiyono also declined to prosecute his predecessor (May, 2006) for fear of alienating his former military colleagues.\footnote{See Ellen Nakashima, ‘Indonesia drops Suharto prosecution citing his health’, \textit{Washington Post}, (p.A14), May 13, 2006. In the case of Indonesia, the lack of separation between economic and political elites is exacerbated by the still central role of the Indonesian military in both economic and political life. As a result, even if the current President, also a former general, wanted to prosecute Suharto, doing so would be politically risky as Suharto actively protected the dual role for the army in Indonesian politics (\textit{dwifungsi}) throughout his thirty-year reign, as it would endanger his power-base base vis-à-vis the Indonesian military. See Heda Bayron, ‘Indonesia drops Graft Case Against Former President Suharto’, \textit{Voice of America}, May 12\textsuperscript{th}, 2006.}

That such issues were avoided, is however, testament to the fact that ultimately the outcome of the dispute must be understood as the continuation of international power politics, central to which was U.S. power and interests. That is, the evidence makes clear, consistent with realist formulations of investment dispute settlement, the U.S. manipulated the incentives facing Indonesia, through a combination of threats and inducements so as to delimit not only the use of legalized modes of disputes resolution but also as has been shown their non-use. To this end, while the instruments of protection continue to evolve, exemplified by the emergence of OPIC governance, and while legal rules governing dispute settlement have proliferated state power remains central in determining the processes and ultimately the outcomes of international investment disputes, i.e. the \textit{politics} of dispute settlement and law making.

In the final analysis, while U.S. power was not without its limits, the evidence from the CalEnergy dispute makes clear that to the extent that institutional rules and norms were efficacious in delimiting the final outcome it is because the U.S. undertook to enforce them rather than because there was any sign of broad agreement as to the legitimacy of the rules. In short, there is no evidence to suggest that compliance with either the arbitral awards or the subsequent subrogated claim was motivated by the normative sanction of law. In this regard, the evidence makes clear that as far as the CalEnergy dispute was concerned, U.S. power and interests at the point of enforcement underpinned the use of legalized modes of dispute settlement such as arbitration. Thus, while delegation and the provision of access to CalEnergy to initiate arbitration were not insignificant in terms of the ensuing processes of resolution, enforcement remains the key variable in determining the politics of dispute settlement.
and by implication international property and contract rights, and ultimately, this is a function of relative power capabilities of the home and host states. In short, the expansion of the ‘market for the contract,’ and with it the expansion of U.S. IPPs to Indonesia was mediated by state power and interests, albeit in this instance a bifurcated power consisting of OPIC governance and the U.S. government.
Chapter 4: India, Dabhol and OPIC

The second case study to be examined concerns an investor-state dispute between the Dabhol Power Company (DPC), the western Indian state of Maharashtra and the government of India. The dispute in question arose following a contractual disagreement between DPC investors, led by Enron but also including minority shareholders, G.E. and Bechtel and the state-owned local partner the Maharashtra State Electricity Board (MSEB). In this regard, the DPC dispute displays both similarities and differences with that of CalEnergy in Indonesia. Foremost in terms of the differences concerns the fact that because the disagreement arose at sufficiently an early stage to scare off prospective foreign infrastructure investors prior to their having begun construction, the DPC dispute was not hampered by the concurrent workout of other IPP disputes. Resolving the dispute was no less complex, however, owing to the project’s financing structure.

Moreover, the DPC dispute was in fact two disputes. The first occurred in early 1995; just two years after the signing of the power purchase agreement (PPA), but was resolved without the need for arbitration within twelve months. Opposition to the project at the State and Federal level did not dissipate, however, with the result that a second dispute broke out in late 2000, less than a year after the opening of phase I. By the time a settlement was reached in mid-2005 the dispute had resulted in the payment of six PRI claims by OPIC to a value of $120 million, and had, since its inception in 1995, spanned four Presidential terms, three Indian Prime Ministers, four changes of government in Maharashtra, and Enron had ceased to exist.

384 Maharashtra is India’s second most populous state, with a population of 96 million, and includes the financial and industrial hub of Mumbai (formerly Bombay) responsible for 35% of national industrial production.
385 The Dabhol power project was the first overseas power project undertaken by Enron in a developing country. Enron as the project sponsor owned 65% of the equity in DPC, with G.E. and Bechtel holding 10% each, while the local partner MSEB was allocated a 15% equity share in DPC.
386 The significance of this is made clear by the fact that Indian states signed 130 Memorandums of Understanding (MOUs) with prospective foreign IPPs 1993-1995. However, none came to fruition due to negative publicity surrounding Dabhol. Interview Notes Ministry of Finance, New Delhi.
387 This included not one but four equity share owners (both Indian and U.S.), while the non-recourse debt was sourced from four state-owned Indian banks, four ECAs acting as both lenders and insurers as well as a private lending syndicate comprising more than 60 banks from Europe, Japan and America, each of whom was governed by one of eight separate bilateral investment agreements.
According to the terms of the final settlement, the equity stake in DPC held by G.E. and Bechtel, as the majority owners following the collapse of Enron, was purchased by a consortium of Indian investors, led by the Indian government-owned National Thermal Power Company, and the Gas Authority of India Limited.\(^{388}\) While the outstanding non-recourse debt owed to public and private offshore lenders was purchased by a consortium of state-owned Indian banks, led by the Industrial Development Bank of India. Today, the DPC is no more, having been renamed by its new Indian owners the Ratnagiri Gas and Power Private Ltd. Co. Phase I of the newly renamed plant commenced operations at the end of 2005, while the larger phase II of the plant is expected to commence production towards the end of 2006.\(^{389}\)

The research will follow the same basic pattern as did the previous case study. The first task therefore will be to outline the dispute settlement process from its inception through until the final settlement in mid-2005, including both the legal and diplomatic channels of resolution. Having detailed the key events in the dispute the focus of attention will then turn to consider first, the impact of the provisions of the contracts of insurance on the bargaining strategies employed and second, the role of OPIC in mediating a settlement to the long-running dispute. In this regard, the evidence will show that not only did OPIC fulfill the central role in overseeing diplomatic bargaining but in paying six claims to DPC investors the agency fulfilled what amounted to a judicial role. It did so because in paying the claims the agency effectively validated DPC investor claims of expropriation so as to delimit the boundaries between commercial and political risks so as to in turn delimit markets for private infrastructure providers in India. In this manner, the provision of investment insurance serves as a flexible mechanism for economic governance of investor-state disputes so as to provide U.S. infrastructure investors with an additional layer of protection, as a supplement to the hard-law treaty framework. For the U.S. the benefits accruing in this regard must, however, be weighed against the fact that the presence of insurance once again served to delimit U.S. foreign policy autonomy so as to threaten, if anecdotal evidence is to be believed, not only the dispute settlement process but for a time, diplomatic relations between the two nations.

\(^{388}\) G.E. and Bechtel purchased Enron’s 65 percent equity stake in the project in 2004 from the Enron creditor committee, giving the two previously minority shareholders a majority stake equivalent to 85 percent equity ownership in the DPC.

\(^{389}\) N.A. ‘Dabhol Renamed Ratnagiri Gas’ The Economic Times of India, Friday, July 8th, 2005.
The second part of the analysis will then consider the relative explanatory weight of the two competing hypotheses, held to explain the outcomes of disputes. The chapter will argue that the emergence of OPIC governance is best understood as signaling a shift in the instruments of protection rather than the politics of dispute settlement and law making. It is so because as the evidence will show the final settlement and thus the efficacy of the rules and norms governing dispute settlement must be understood in the final analysis as products of underlying state power and interests. Foremost in this respect, and as will become apparent, concerns the fact that both the U.S. and India displayed a willingness to set aside the relevant legal provisions where the rules of the game were felt not to further their respective national interests. In this regard, the evidence will show that not only did India violate treaty provisions so as to render agreed legal mechanisms for dispute settlement as an irrelevancy, but the U.S. violated the customary international law principle of ‘corporate personality’ in extending diplomatic protection on behalf of Mauritian registered DPC investors. That this is the case makes clear therefore that while the modes of state protection and investment dispute settlement continue to evolve so as to confer upon OPIC a central regulatory role where U.S. infrastructure investors are concerned, the outcomes of disputes and thus international property and contract rights remain as firmly rooted in state power and interests as ever they were.

In order to consider the evidence, the remainder of the chapter is organized as follows. The first task will be to outline the key events of the dispute from the time the project was first mooted in 1993 until the final settlement of the second Dabhol dispute in 2005. The focus of attention will then turn to consider the role of OPIC and the impact of PRI. The final part of the chapter will then consider the relative explanatory weight of the two competing theories beginning with rules-based accounts before then examining the impact of state power in determining a final settlement.

*Background: Power Sector Liberalization in India (Maharashtra)*

India adopted a socialist-oriented (though officially non-aligned) economic system after gaining independence in 1947. The policy yielded moderate economic growth
for the first two decades.\textsuperscript{390} By the early 1970s, however, a burgeoning bureaucracy, and moribund industrial sector, dominated by inefficient state-owned monopolies saw economic growth stagnate. Moreover, nationalist sentiment and the negative perception of multinational companies (MNCs) cultivated by the ruling Congress Party, added to often stifling bureaucratic controls, meant that a number of high profile foreign investors exited the Indian market during the 1980s.\textsuperscript{391} Despite widespread acknowledgment of the need for reform, it was not until the election of P.V. Rao in 1991, and the subsequent establishment of the Rao Committee that India began to dismantle what was unflatteringly labeled ‘License Raj.’\textsuperscript{392}

While the initial results were encouraging, it soon became apparent that higher levels of economic growth were being impeded by infrastructure bottlenecks, particularly in the state-controlled power sector. Indeed, the Indian electricity sector had remained little changed since independence, with each state operating state electricity boards (SEB) as fully vertically integrated companies, with generation, intra-state transmission and distribution assets, regulated by the Central Electricity Authority (CEA) in New Delhi.\textsuperscript{393} Over the years, however, state governments resorted to populist decisions to increase levels of power subsidies, in particular, to the rural poor, as the single largest voting bloc.

The result according to a CEA report was that the entire sector suffered from under-investment leading to capacity constraints in generation, transmission and


\textsuperscript{391} These included Coca Cola and IBM amongst others, See \textit{Enron and the Dabhol Power Company}, \textit{Thunderbird}, The American Graduate School of Management, 2002, p. 3. The negative image of MNCs in India was further damaged in 1984 when the U.S. owned Union Carbide Plant in the town of Bhopal in the Indian state of Madiya Pradesh leaked toxic chemicals (methyl isocyanate) into the atmosphere, killing an estimated 3,800, and injuring a further 150,000.

\textsuperscript{392} P.V. Narasimha Rao elected in 1991, was the first Congress Party leader for thirty years not to come from the Gandhi/Nehru families, who have dominated Congress Party and thus Indian politics since independence from Britain in 1947. Rao was elected as head of the Congress Party in 1991, following the assassination of Rajiv Gandhi by Tamil extremists during the 1991 elections. He would lead India until May 1996, when the Congress Party suffered their worst electoral showing since independence, losing to the Hindu-nationalist Bharatiya Janata Party (BJP), led by Atal Behari Vajpayee. For an excellent albeit slightly dated account of post-independence politics in India, See Paul R. Brass, \textit{The Politics of India Since Independence} (Cambridge: Cambridge University Press, 2\textsuperscript{nd} ed., 1994).

distribution, equivalent to 19 percent of energy requirements. Moreover, the report continued, ‘apart from operational deficiencies,’ the SEBs continue to suffer from an ‘irrational tariff structure, involving heavy subsidies, which promotes the inefficient use of electricity.’ In order to rectify the acknowledged deficit, the CEA report recommended an additional generating capacity of 35,000 MWs would be required by the end of 1997, at an estimated cost of $55 billion.

The deficit in India’s second most populous state, Maharashtra was identified as particularly acute, with capacity having failed to keep pace with economic growth. According to the same CEA report (14th annual survey), the state faced an estimated shortfall of 1,771 MW for the period to 1997, with an additional 1,662 MW of electricity required by 2002. MSEB’s projections for power demand in the state were even higher, estimating an additional 5,000 MW was needed by 1997 and 10,000 MW by 2002, based on already ‘paid pending applications for power’ by industrial and agricultural users alone.

In order to address the shortfall, the Indian government enacted a series of reforms, designed to attract foreign investors to the power sector in October 1991. Among the raft of legislative changes introduced were the following: foreign producers were entitled to 100 percent foreign equity ownership, and guaranteed dollar repatriation of foreign capital and dividend remittances. Second, provisions were also introduced to facilitate project-finance type transactions for the first time in India, with a permissible debt-equity ratio of 4:1. Finally, investors were also offered a guaranteed

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395 Eighth Five-Year Plan (1992-1997), Planning Commission, India, p. 191. According to the report, ‘the average price of power charged by the SEB’s in 1992 was 86 paise per unit, about 50 percent of the long run marginal cost.’ Collectively, the SEB’s lost an estimated Rs. 4363 in 1992-93, equating to an annual rate of return of minus 11.4 percent. See also N. Raghunathan, ‘The Enron Power Project’ Memories, Men and Matters, (Mumbai: Bharatiya Vidya Bhavan, 1999), p. 3 and p. 8.
397 Growth in installed capacity in the state of Maharashtra, the center of industrial production in the country, was maintained at the national average level of 8.8 percent compound annual growth rate for the period 1960-1990. From 1986 to 1990, electricity supply growth rates fell to less than half the national average however. In 1992-93, just 9 MW of new capacity was added in the state, with the result that the state’s share of national power production fell from 14 to 11 percent in two decades. See N. Raghunathan, ‘The Enron Power Project’ Memories, Men and Matters (1999), p. 3.
The problem facing both the Maharashtra and Indian government was how to raise the necessary finance, owing to a worsening current account deficit, a severe foreign-exchange shortage, and rapidly rising inflation that saw India’s sovereign debt rating fall below ‘investment grade’ in early 1992, for the first time since independence. Indeed, the worsening economic situation prompted the arrival of the IMF later that same year who issued new sovereign loans, to avoid India falling off the edge of what the Ministry of Finance publicly referred to as a ‘calamitous economic precipice.’

While the Indian government’s worst fears were avoided, it soon became apparent, later confirmed in a Ministry of Finance commissioned report, that even if India guaranteed loan commitments in U.S. dollars, it was unlikely that it would be able to raise loans on a non-recourse basis for infrastructure financing, being limited to short-term loans and trade financing only. The predictions proved all too prescient, evidenced by the subsequent withdrawal of the three initial expressions of interests from foreign consortiums, citing concerns over the regulatory environment.

Undeterred by the setback, a Cabinet delegation was established in May 1992, charged with seeking out potential foreign investors. That same month, having already visited London and Singapore, the delegation arrived in Houston for a

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399 A second set of legislative changes were enacted in March 1992, setting out the tariff determination, followed by a third piece of legislation in January 1994, under which the permissible return on equity for investors was linked to plant-load-factors (PLF) allowing a maximum return on equity of 31.05% for a PLF of 90%. The high rates of return were supposed to reflect the efficiency improvements that would result from foreign ownership and enhanced technological expertise. The returns were justified in part by the fact that, according to an MSEB commissioned study, the average PLF for MSEB operated power projects in 1994 was just 55 percent. The comparison, claimed critics of the project, was spurious, however, as the new Dabhol plant was to run on LNG, whereas the MSEB plants were predominantly coal-fired and local coal is of a poor quality hence the comparatively low average PLF.

400 The worsening payments position was underscored by new restrictions imposed on sovereign borrowing in 1992, according to which new loans were to be issued only if India pledged its gold reserves as collateral to be held in escrow accounts.


403 Interview Notes Naresh Chandra.

404 The delegation, included the Joint Secretary’s of the Ministries of Power and Finance respectively (S. Rajagopal, and K. Geethkrishan), and was headed by the then Cabinet Secretary, Naresh Chandra. See interview notes Naresh Chandra.
meeting with Enron Corporation.405 Less than one month later, representatives from Enron International (a subsidiary of Enron Corp.) flew to Mumbai, where Maharashtra officials met them.406 Following inspection of potential sites courtesy of an Indian government helicopter, the Dabhol site was chosen, approximately 180 kms south of Mumbai on the Arabian Sea.407 On June 20th 1992, less than a week after Enron’s arrival, a Memorandum of Understanding (MOU) was signed between Dabhol Power Company, MSEB and India.408 Despite some opposition to the proposed project, high-level government support, including state and federal, ensured that the negotiations were speedily resolved, leading to the signing of the power purchase agreement (PPA) for phase I in December 1992.409

The PPA contemplated the construction of an integrated energy complex comprising a power-generation facility, constructed in two phases. Phase I of the project provided for the construction of a 695 MW naphtha-fueled plant, whilst the larger but as then optional phase II contemplated the construction of a 1,484 MW LNG-fueled plant, which would, if completed, make the Dabhol power project the largest combined-cycle gas-fired power plant in the world.410 According to the terms of the PPA, MSEB

405 According to the head of the delegation, Naresh Chandra, Enron was not the only firm to express an interest. See Interview notes, Naresh Chandra.


407 The Dabhol site was in fact recommended to Enron by the MSEB and the Maharashtra state government, both of whom had previously applied to the CEA, first in 1978 and again in 1989 to develop an LNG-fired power plant at the site. The applications had been rejected, however, citing the technical feasibility of the project, and the high foreign exchange requirements associated with importing LNG when abundant, if poor quality, coal reserves were locally available. Interview Notes N. Raghunathan. See also N. Raghunathan ‘The Enron Power Project’ Memories, Men and Matters, (1999), p. 14.

408 The signing of the MOU was greeted enthusiastically by the then head of the international division, Joe Sutton, who on his return to Houston was quoted as saying that ‘We’re very, very excited about it. We’re forging the way forward. This will be the cornerstone of other agreements.’ ‘In the future, Enron’s business will be 10% domestic and 90% overseas.’ Quoted in ‘India Draws Private Firms to Power Sector,’ Asian Wall Street Journal, Jan. 29, 1993. It is worth noting that the entire process, despite later claims to the contrary was overseen and ratified by the Federal government, including the Indian foreign investment review board (FIRB) and the CEA, who in a published report, noted that ‘the scheme is found to be technically acceptable and the estimated cost ($1,844 million) in foreign exchange plus equivalent $615 million in Rupee is seen to be generally in order.’ See Interview Notes, and See also N. Raghunathan, ‘The Enron Power Project’ Memories, Men and Matters, (1999), p. 9.

409 Later, the speed with which such a large contract was negotiated would become the subject of much criticism. For example, one former high ranking government official noted that the whole process was highly unusual in an Indian context, citing the fact that when the MSEB had applied to the Central Electricity Authority to develop the Dabhol site in 1989, the MSEB did not receive a reply for three years, with the latter (as was typical) offering no explanation for the delay. See Interview notes N. Raghunathan.

410 Under the terms of the original PPA, phase II of the plant had yet to be agreed definitely, being dependent on the success or otherwise of phase I. Should phase II be completed, it would also require a
was to purchase power from the plant at a fixed-rate denominated in U.S. dollars over a twenty-year period, beginning in 1997. In contrast with other IPPs in India that operated under a ‘cost plus’ arrangement which provides for compensation based on running costs (including debt servicing) plus a fixed return on equity, DPC was able to negotiate what is known as a ‘levelized tariff’ structure. A levelized tariff structure links the average cost per unit of power to production, i.e. plant load factor (PLF). For example, under the terms of the original PPA (later renegotiated in 1996), at an assumed PLF of 86 percent then the projected cost of power for phase I was U.S. 7.5 cents (Rs. 2.40) per Kilowatt hour (p/kWh). Of this cost 3.808 cents p/kWh was allocated to pay capital charges, including to pay debt and provide the equity providers with a return of equity (ROE). Of the remainder, 0.000625 cents was allocated to cover operating expenses, while 3.698 cents p/kWh was allocated to cover fuel costs (with MSEB to bear any increases in fuel costs under the contract). However, if the PLF fell below 86 percent then MSEB still had to make fixed payments, the effect of which was to increase the cost per unit of power produced. 411

LNG re-gasification plant to be built, at which point phase I would switch from Naphtha to LNG also. In order to facilitate a dependable supply of LNG, Enron subsequently signed two ‘take and pay’ contracts with Oman LNG LLC and Abu Dhabi Liquefaction Gas Co., committing the DPC to purchase LNG at a fixed rate for the duration of the PPA. 411 There were many problems with such an agreement from the perspective of MSEB. First, the plant was a base load plant rather than as was required a peak load plant. As a result, MSEB had to purchase power from the plant 86% of the time otherwise the projected unit cost of 7.5 cents p/kWh would increase proportionally, but the average base load demand in Maharashtra is on average only 60% (Load factor is the ratio of average demand over the day to peak demand during the day). In simple terms, this meant that MSEB had to buy power from the plant when it could buy power from other providers in the system at a lesser cost, i.e. when it didn’t need it. For example, the average cost of power purchased by MSEB from providers other than DPC has been estimated at 30% lower than DPC power. As a result, the more power MSEB purchased the more it lost relative to the situation had the power been purchased from incumbent providers. Kirit Parikh explains, ‘[S]ince electricity cannot be stored easily, at the night time off-peak hours when the demand is often less than half the peak demand, some power plants have to be backed down. Providing a high load factor of 86 percent to DPC would imply that during off peak hours (at night) MSEB would be backing down its own power plants, i.e. it would be purchasing power at Rs.2.40 from DPC when it could have been generating power from its own coal based plants at a lower marginal cost per unit.’ The additional costs per annum as a result of this clause alone have been estimated by Kirit Parikh at $55-84 million per annum over twenty years. It is for this reason that the World Bank and the Central Electric Authority refused to support the project, stating that it was unsuitable for Maharashtra’s power needs, which required an increase in peak-load plants. Second, MSEB’s average transmission and distribution (T&D) losses at the time were 50%. What this meant in effect was that to recover the fixed payments to DPC of 7.5 cents p/kWh then the power had to be sold at 15 cents p/kWh, which is approximately 500% more than average electricity charges in Maharashtra. The practical effects of this are well articulated by Kirit Parikh who has written, ‘[A]t that price industrial consumers would generate their own power rather than buy it from MSEB.’ Third, MSEB was also exposed to exchange rate risk. This was significant given the average annual depreciation of the Rupiah versus the dollar in the decade previously of 8% per annum. Yet, MSEB did not include this in their projected cost calculations. Fourth, MSEB had to bear the cost of fuel increases. By 1999, the average cost of Naphtha had risen by 42%. Fifth, in allocating a fixed payment towards capital charges then DPC had inbuilt incentives to artificially inflate the cost of the

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Finally, under the terms of the agreement, should MSEB be unable to meet scheduled payments to DPC at any point, then a ‘termination clause’ would be triggered, wherein ownership of the DPC would pass to the Maharashtra government, in return for immediate payment of all outstanding debt, as well as purchase of Enron’s equity stake in the project, including an amount for lost revenues accruing to the project.\footnote{Narayan Naik, \textit{Dabhol Power Company}, London Business School, 2003 (CS-04-004), p. 7.}

Finally, the PPA also provided for arbitration in London, (UNCITRAL rules).

DPC also negotiated a second level of credit protection in order to allay the fears of prospective non-recourse lenders. These included, a Maharashtra government guarantee in respect of MSEB’s contracted obligations, as well as an additional guarantee agreed as part of the ‘State Support Agreements’ wherein the Maharashtra government also undertook to support DPC’s efforts to obtain the necessary permits. The State Support Agreements also provided for an additional counter-guarantee from the Federal government in lieu of the state-government’s obligations subject to a cap of $300 million. Finally, both the state and Federal government guarantees were to be governed by English civil law, subject to UNCITRAL arbitration in London.

Significantly, the Indian government counter-guarantee also contained an explicit waiver of sovereign immunity in connection with any enforcement proceedings brought against it or its assets.\footnote{Memorandum of Determinations, Expropriation Claim of Bank of America, as Trustee India – Contract of Insurance No. F041, 30\textsuperscript{th} September, 2003, p. 1-28.}
Having concluded the PPA, the next move for Enron was to arrange financing. With this in mind, Enron wrote to OPIC in May 1994 seeking a commitment from the agency of $200 million in equity PRI.\(^{414}\) Two months later, OPIC issued a ‘commitment letter’ to DPC, agreeing to reserve covers for a period of six months for a non-returnable fee of $200,000.\(^{415}\) The next step for Enron was to finalize arrangements with the project lenders. To this end, the company received considerable support from the then U.S. Commerce Secretary, Ron Brown, who in October 1994, wrote personally to his Indian counterpart urging ‘support in facilitating financial closure’ of the project ‘in time to be celebrated during my visit.’\(^{416}\) The letter appears to have allayed the fears of potential lenders, with the result that in January 1995 Enron CEO, Ken Lay, Commerce Secretary, Ron Brown, representatives from OPIC, and Ex-Im Bank traveled to India for the signing of the DPC loan agreements.\(^{417}\) Two months later on March 1\(^{st}\), Enron announced financial closure for phase I of DPC thereby completing the single largest financing ever undertaken in the Indian Term Lending Market, and the first non-recourse financing in Indian history.\(^{418}\) Having completed financing, Enron commenced negotiating with OPIC regarding the contract wording in April 1995 before signing the contracts of insurance in August.\(^{419}\)

**Dispute Number One: 1995-1996**


\(^{415}\) Bechtel Enterprises -against- Overseas Private Investment Corporation.

\(^{416}\) ‘Financing for Indian Plant Secured’, *Houston Chronicle* (Jan. 17, 1995).


\(^{418}\) The financing structure for phase I was as follows: U.S. EX-IM Bank agreed to provide US$298 million, guaranteed by four Indian government owned Banks. OPIC provided loans of $100 million, secured against a Federal government counter guarantee. OPIC and EX-IM financing was supplemented by loans from the four Indian financial institutions totalling 306 crore. Finally, a consortium of lenders, led by ABN Amro, Citibank (London), ANZ Grindlays and Bank of America agreed to provide non-recourse loans totalling $150 million, guaranteed by the Indian lenders, Canara Bank and additionally secured by assignment of the Indian government counter-guarantee. See Industrial Development Bank of India & Others (plaintiffs) v. ’s Dabhol Power Company & Ors. (Defendants), Affidavit in Rejoinder, 24th February, 2004, Notice of Motion No. 819 of 2002 in Suit No. 875 of 2002, Bombay High Court.

\(^{419}\) Bechtel Enterprises International -against- Overseas Private Investment Corporation, Respondent, p. 6.
DPC’s announcement of financial closure attracted immediate negative publicity. Even before this, however, Dabhol had become an issue in the 1995 Maharashtra state elections, with the opposition Bhartiya Janata Party (BJP) (Indian People’s Party) vowing to ‘throw the project and Enron into the Arabian Sea’ if it won the election.\textsuperscript{420} The worst fears of Enron appear to have been realized when contrary to expectation the BJP defeated the Congress Party, forming a government with the nationalist Shiv Sena party.\textsuperscript{421} True to their word, the first task undertaken by the administration was to establish the Munde Committee, with a remit to review every aspect of the deal. The omens were not promising, however, with the new Chief Minister of Maharashtra likening Enron to a modern-day Caesar.\textsuperscript{422}

The Munde Committee submitted its report in June 1995, recommending that the project be scrapped. The recommendation was accepted without question, and the following month the government of Maharashtra formally rescinded the PPA. Then, in a highly unusual move the state authorities proceeded to file suit in the Bombay High Court against its own constituent the MSEB, as well as DPC, seeking to have the project agreements declared null and void owing to their having been obtained through bribery, fraud and misrepresentation.\textsuperscript{423} And although the allegations were not supported, and were later dropped as a condition of arbitration, they reflected the commonly held belief that ‘it is inconceivable that a transaction [this large] . . . could proceed without adequate kickbacks and payoffs.’\textsuperscript{424} To this end, it was apparent that what began as a commercial issue had become a political one.

DPC’s response was immediate. The company filed for arbitration in London pursuant to the PPA, seeking $300 million in compensation thereby presaging the first

\textsuperscript{420} Human Rights Watch, \textit{The Enron Corporation: Corporate Complicity in Human Rights Violations} (January, 1999).
\textsuperscript{421} Although not officially the leader of the two-party alliance, a number of Maharashtra government interviewees confirmed that Bal Thackeray was the power broker behind the scenes from 1995-1999.
\textsuperscript{422} According to the statement made by Manohar Joshi, ‘From the speed with which the memorandum of understanding was signed it seemed as if Enron came, it saw and it conquered.’ See Harvard Business School, \textit{Enron Development Corporation: The Dabhol Power Project in Maharashtra, India} (a), p. 9-10 (revised July 6, 1998).
\textsuperscript{423} See Civil Suit No. 3392 of September 6, 1995 (Bombay High Court). The allegations although obtuse seemed to focus on the fact that India’s Commerce Minister P. Chidambaram (currently Finance Minister as at end 2005) had ‘strongly supported Enron’s Dabhol Power Project in public forums in India and abroad without disclosing the fact that he had given a paid legal opinion to Enron’ See ‘The Enron Corporation: Corporate Complicity in Human Rights Violations’, \textit{Human Rights Watch}.
of many rounds of shuttle diplomacy by U.S. officials on behalf of Enron. Energy Secretary, Hazel O’Leary was the first to arrive in New Delhi, cautioning the Maharashtra government that it was ‘discouraging foreign investment in India.’ The comments mirrored those of the then U.S. Treasury Secretary, Robert E. Rubin, who on a visit to India in the April had warned India of the need to stand by commitments to investors. Additional support for DPC in Washington was also provided by the appointment of a White House Counselor, Mick McLarty, to monitor the project and to work with the U.S. Ambassador to India, keeping Ken Lay informed of the administration’s efforts. In a final bid to head off arbitration, Enron dispatched Rebecca Mark (Head of Enron’s Global operations) and Joe Sutton (Head of Enron India) to Mumbai. During their visit, the pair met with among others local political power broker and leader of the Maharashtra-based Shiv Sena party, Bal Thackeray.

The meeting proved a success, evidenced by the sudden announcement by Maharashtra government on January 6th that it was dropping the lawsuit against the DPC, thereby staving off arbitration. Six weeks later, it was announced that it had agreed a revised PPA. Under the terms of the new PPA, the government agreed to commit to phase II of the project, in return for which MSEB was given the right to double its equity stake in DPC to 30 percent, while the tariff rate per unit was also lowered in comparison with the original PPA from a projected 7.5 cents p/kWh (Rs. 2.40) to 5.906 cents (Rs. 1.89).

Both parties immediately proclaimed the new

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429 The figures here are highly misleading, however. There are a number of reasons for this. First, according to the revised PPA the levelized tariff was to be calculated using an average PLF of 90% from the original 86%. This meant that MSEB had to purchase even more power from the plant than it did previously, thus increasing the loss per unit if MSEB took less than 90% of power produced. The real hammer-blow as far as MSEB was concerned, however, was that under the revised PPA, which committed to the much larger phase II, then MSEB was committed to buy power 90% of the time but this time from a power plant that was more than three times as large (2184 MW versus 695MW). If the original PPA had been contrary to Maharashtra’s power needs, then the second PPA was quite simply beyond comprehension from the perspective of MSEB. Thus, while the Maharashtra government claimed it had beaten Enron on price, in actual fact under the revised PPA, according to Kirit Parikh Enron’s return on equity actually rose to approximately 50% p.a. while the IRR also rose to approximately 40% p.a. See Kirit S. Parikh, ‘Thinking Through the Enron Issue’ Available online at http://www.ccsiindia.org/ccsiindia/people_kp_enron.htm Date Accessed 15.03.07. It is partly for this reason that MSEB, when the dispute broke out, not unreasonably believed that Enron would back
agreement to be a victory. The BJP claimed that they had beaten Enron on price, while Enron made clear their satisfaction at having negotiated a commitment to the larger phase II.\footnote{430}

The revised PPA was ratified by the State parliament in April 1996. As part of the agreement, the state authorities agreed to drop all remaining lawsuits. Despite the commitment, a second suit was filed in the Bombay High Court before the end of year.\footnote{431} The writ questioned how the government could conclude a second and much larger deal with the same party it had earlier accused of fraud. However, before the Court could address the question, the Maharashtra government in a \textit{volt farce}, acknowledged that the accusations, having been made with a view to the upcoming (1995) state elections, were totally without substance.\footnote{432} And although the Court declined to comment on whether the government was guilty of perjury they did take the opportunity to express their disappointment that ‘50 years after independence’ it ‘is distressing to note the extent to which political compulsions take priority over the public interest.’\footnote{433} The dismissal of the court action removed the remaining obstacles to the re-closure of financing, which was duly announced on December 9\textsuperscript{th} 1996.

The government’s climb down did not diffuse further criticism of the project, however, with local opposition intensifying, including campaigns by trade unions, as well as local and international NGOs who criticized every aspect of the project.\footnote{434} In February 1997, the local police arrested 1400 union demonstrators at the Dabhol
down, as there was in the lexicon of project finance ‘plenty of fat’ still left in it for Enron even if the original deal was renegotiated to include a lower tariff structure. Unfortunately, for the people of Maharashtra MSEB’s gamble did not pay off.

\footnote{430} Apart form the commitment to phase II, one senior Enron executive on returning to Houston labelled the tariff reduction as a ‘price reduction that was not really a price reduction . . . Why? Because of technological advances, falling hardware costs, weakening Rupee . . . ’ Quoted in Arthur Gott-Schalk, ‘Cabinet’s OK Brings Enron Closer to Completing India Power Deal,’ \textit{Journal of Commerce}, January 9, 1996. This was later confirmed by the Godbole committee who estimated that capital costs had fallen by $300 million since the PPA was signed in 1993, as the technology became more common, thereby supporting claims of critics that the new agreement had not cost Enron anything, while on the plus side of the ledger from Enron’s perspective, it had negotiated a commitment to the much larger phase II plant, thus increasing pre-existing economies of scale so as to lower average operating costs.

\footnote{431} Civil Suit WP 2456 and 2912 of December 1996 (Bombay High Court).


\footnote{434} The environmental effects of the project were a point of particular criticism, with NGO groups claiming that the project was damaging local drinking water and reducing fish stocks, on which the local community relied for their livelihood.
According to reports from Human Rights Watch, what ensued was ‘a pattern of serious human rights violations that the project provoked.’ The report went on to claim that police beat protesters, tear-gassed demonstrators, and placed suspected leaders in preventative detention. Amnesty International later investigated these claims, concluding that ‘suppression of local protests’ had taken place, and people protesting against the project were liable to ‘harassment, arbitrary arrest, preventive detention under the ordinary criminal law and ill-treatment.’ Despite the unwanted attention, construction of phase I proceeded throughout 1997.

Undeterred by continued criticism, DPC announced on May 6th 1999 that it had completed financial closure for phase II. As was the case with phase I financing, numerous credit support mechanisms were included at the request of the lenders. In addition to the revised PPA that provided for DPC to terminate the agreement if MSEB failed to perform its obligations, two further contracts were agreed in order to facilitate the debt financing. The first of these, ‘The Common Agreement’ detailed the criteria under which loan disbursements would be made and the circumstances under which lenders could terminate their lending obligations. It also gave the project lenders control over DPC’s ability to terminate the PPA and demand payment of the Transfer Amount. The Inter-creditor Agreement, to which DPC was not a party, governed the relationship among the lenders. Crucially, the agreement assigned to OPIC the unilateral right to consent to the termination of the PPA.

437 ‘Bidding Set for Enron’s India Project, Reuters (Jan. 21, 2001).
438 The financing structure for phase II was as follows: The Japanese ECA, JEXIM provided loans of $433 million, guaranteed by the four Indian banks. The Belgian ECA, the Office National du Croie (OND) provided loans of $91 million, also guaranteed by the Indian lenders. OPIC agreed to provide loans totaling $138 million, but these were not guaranteed. An additional $202 million of loans was sourced from EX-IM Bank. ECA financing was supplemented by loans from private offshore banks, totaling $272 million. In sum, the total offshore debt financing amounted to $1,081 million, equivalent to Rs. 1,594 crores. The remainder of the debt financing was provided by a consortium of four government-owned banks, led by the Industrial Development Bank. The total exposure of the four Indian lenders, including the offshore debt guaranties, amounted to Rs. 5,207 crores.
439 Further protection was provided by the establishment of an escrow account to be operated by a Trustee. Receipts, received by MSEB for power in certain regions of the state would be placed directly in the escrow account. The facility was further supported by a ‘Letter of Credit’ issued by the Indian government-owned Canara Bank.
Exactly a week after the announcement of phase II closure, DPC phase I began operations. The relative calm of the next three months would be disturbed in October, however, with the news that the BJP-Shiv Sena alliance had lost the Maharashtra elections, returning the Congress Party to power. Like their predecessors, the new administration immediately attempted to distance themselves from the politically unpopular project, establishing the Godbole Committee to review the DPC.

The news for DPC was not, however, to improve. In the November MSEB announced that it could not afford to purchase power from phase II. Its financial difficulties were again in evidence in December when insufficient funds forced it to announce that certain rural areas would only receive power for five days in seven. The situation continued to worsen throughout 2000, prompting MSEB to announce in November 2000 that it had agreed to sell half its stake in DPC (equivalent to 15 percent, acquired in the 1996 Munde renegotiations) to Enron, thereby restoring Enron’s original equity stake to 65 percent. A month later in December 2000, MSEB reduced the power purchased from DPC to just 33 percent of the plant’s capacity, citing the depreciation of the Rupee and the rising cost of Naphtha.

Dispute Number Two: 2000-2005

The reduction in power signaled the beginning of the second dispute. That same month MSEB failed to make payment for the December invoice totaling $22 million. Despite this on January 28th 2001, MSEB issued ‘Dispatch Instructions’ to DPC for full capacity generation based on DPC’s ‘Declared Availability.’ Contrary to the PPA, however, the plant failed to reach the declared capacity within the prescribed

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440 The new government was a coalition led by the Congress –I and the Nationalist Congress Party (a breakaway faction of the Congress-I party). The coalition also included the People’s Party, which was openly opposed to the DPC. Worse still, Phase II of DPC was now associated with the newly deposed Shiv-Sena party. See Narayan Naik, *Dabhol Power Company*, London Business School, 2003 (CS-04-004), p. 13.

441 *Enron and the Dabhol Power Company*, The American School of Graduate Management, p. 12.


443 Interview Notes MSEB Chairman, Mumbai. According to whom the importation price of Naphtha had risen by 45% in real terms since the PPA was signed.

time limit, taking six hours instead of the agreed three. DPC’s response was immediate; on February 6th it formally invoked the Indian government counter-guarantee for unpaid invoice totaling $17 million. This was followed a week later with a letter to MSEB querying the ‘dispatch order’ claiming it to have been inconsistent with the agreed procedure. The Maharashtra government responded by denying the existence of said procedures, while Federal authorities refused to honour the counter-guarantee, on the basis that the guarantee covered only ‘valid claims.’ That same month, an Energy Review Committee (ERC) was established by the state-government to review the Maharashtra power sector.

Two months later in March, MSEB wrote to the state regulatory authority, the Maharashtra Electricity Regulatory Commission (MERC), claiming that DPC owed it $86 million for rebates for non-availability of declared capacity. Finally, the same month (March 15th), in what amounted to a significant escalation of the dispute, DPC phase II lenders halted draw-down on the available funds. DPC responded by immediately canceling the engineering-procurement-construction (EPC) contracts, including those of G.E. and Bechtel. The announcement was followed one month later by the publication of the long-awaited findings of the Godbole Committee on April 10th. The report noted amongst other things that there were ‘numerous infirmities . . . in the project, which brings into question the propriety of decisions.’ The Maharashtra authorities duly accepted the findings, and authorized the Committee to oversee the tariff renegotiation, who immediately recommended that each party take a ‘hair-cut’, i.e. reduce their margins.

The seriousness with which the U.S. viewed the escalation of the dispute was apparent when the then U.S. Secretary of State, Colin Powell in a visit to India in the

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445 This was confirmed by numerous Indian officials, including both State and Federal in interviews as well as by the Chairman of MSEB. In addition, DPC acknowledged the failure, but in its defence argued that no power station in the world was capable of meeting the key dynamic load profile included in the PPA, and that the load profile would need to be modified.

446 Interview Notes MSEB Chairman, Mumbai. According to whom it was no coincidence that the amount claimed was roughly equal to the amount claimed by DPC for unpaid invoices plus interest for November, December and January.

447 According to a subsequent affidavit provided by DPC, phase II was at this stage 85 percent complete, while the regasification facility was 98 percent complete. EPC refers to ‘Engineering, Procurement and Construction.’

448 See Godbole Committee Report, April 10th, 2001, p. 3.

April raised the issue of Dabhol in discussion with India’s foreign minister.\textsuperscript{450} The trip appeared to have paid dividends when on April 27\textsuperscript{th} MSEB announced that it would make payment for the March invoice.\textsuperscript{451} However, the payment failed to placate DPC who in the May served a ‘Preliminary Termination Notice’ (PTN) to MSEB, alleging payment default by MSEB. A second PTN stated that officers of MSEB had made oral representations to DPC regarding their disinclination to accept phase II power, effectively repudiating the PPA.\textsuperscript{452}

The response from MSEB was immediate. On May 23\textsuperscript{rd} 2001, MSEB gave written notice that it was rescinding the contract with immediate effect. The letter alleged that DPC had acknowledged in a letter dated 28.01.01 that the ‘Power Plant does not conform to the PPA and is not capable of meeting the contractual terms in respect of crucial operating characteristics and dynamic parameters.’ The letter continued, ‘It was thus clear that you have made material misrepresentation and our consent to the PPA as cause, \textit{inter alia} by the representation on your part in respect of the capacity and capability of the Power Station.’ Despite the list of grievances, however, the notice sent by MSEB to DPC confirmed that ‘we are agreeable to continue the present arrangements of purchase of power and payment till the disputes are resolved by the appropriate forum’ subject to retrospective compensation.\textsuperscript{453}

DPC responded by instructing the Bank of America to return the cheque sent with the letter by MSEB, purportedly in settlement of DPC’s monthly invoice for April 2001.\textsuperscript{454} DPC then wrote to MSEB denying the allegations whilst noting that any future payments made by MSEB would viewed by DPC as ‘constituting an irrevocable and unequivocal affirmation of the validity of the PPA on the part of MSEB’, failing which the cheque would be returned. The MSEB responded by filing a petition (No. 3) before MERC claming that newly created regulatory commission has exclusive jurisdiction to determine disputes, including the legality of the PPA.\textsuperscript{455}

\textsuperscript{451} Interview Notes Ministry of Finance, New Delhi. 
\textsuperscript{453} Interview Notes MSEB Chairman. 
\textsuperscript{454} Interview Notes MSEB Chairman. 
\textsuperscript{455} In April 1998, the Lok Sabha (Indian National Parliament) passed a number of legislative reforms designed to entice further foreign investment in the Indian power sector. Among the major reforms promulgated was the Electricity Regulatory Commissions Act (ERC) of 1998. The Act authorized the establishment of independent state based regulatory commissions, with a mandate to regulate all

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DPC’s pleas to the contrary were rejected, however, and MERC ruled that it alone had exclusive jurisdiction, by virtue of the fact that first, DPC was an Indian registered company and second, the 1998 ERC Act superseded any dispute resolution mechanisms put in place per the PPA. The MERC order was then followed by the formal rescission of the PPA (dated May 29th, 2001) by MSEB, with the effect that MSEB would take no more power from DPC, make no further payments, and would not abide by the phase II PPA. DPC responded in writing by filing for arbitration pursuant to the PPA. Less than a month later, DPC wrote to MSEB, and in a curious about-face requested that their letter (dated 25.01.01) be retracted to the effect that ‘we will not treat any such payments made or such actions taken by MSEB on or after May 23, 2001 as an affirmation of the PPA.’

That DPC was now adopting a more conciliatory stance did not lessen the diplomatic pressure exerted on India, however. On June 27th U.S. Vice-President, Dick Cheney met with the leader of the opposition Congress Party, Sonia Gandhi, taking the opportunity to impress upon her the urgent need to resolve the DPC dispute. One month later Lay himself arrived in New Delhi for talks with both state and Federal representatives, but his request to meet with the Indian Prime Minister was declined.

aspects of the SEBs, and IPPs in each state. Accordingly, the Maharashtra State government established the Maharashtra Electricity Regulatory Commission (MERC) early in 1999, with the exclusive power to set tariff levels, and adjudicate disputes between the MSEB and IPPs.456
456 Interview Notes Chairman MERC, Mumbai.

457 Interview Notes MSEB Chairman, Mumbai.

458 The meeting followed three previous meetings between the Vice-President and Enron CEO, Ken Lay in Washington D.C. between February and April, 2001. The meetings took place on February 22nd, March 7th and April 17th at the White House. Later, Cheney and the Bush administration would describe the meetings as part of the ‘non-public energy taskforce sessions’, held to discuss the ‘White House Energy Plan.’ And although neither story can be confirmed, the close relationship between the Bush administration and Enron was clear judging by the fact that although ostensibly a ‘national security document’ it contained a provision calling on India to expand its use of LNG for power generation, thereby benefiting the only U.S. IPP operating in India with plans to build a natural gas pipeline across India. The provision read as follows: ‘the president direct the Secretaries of State and Energy to work with India's Ministry of Petroleum and Natural Gas to help India maximize its domestic oil and gas production.’ The provision would later become a source of embarrassment for the administration, evidenced by their refusal to release documents when requested by the Government Accountability Office, as the pipeline in question was intended to link India to the proposed Trans-Caspian pipeline (owned and operated by a consortium of six foreign companies led by California based UNOCAL) being negotiated with the Taliban. See U.S. House of Representatives, ‘Background on Enron’s Dabhol Project’, February 22, 2002., p. 2. Confirmation that Cheney raised Dabhol with Sonia Gandhi was later confirmed by an internal memo obtained through the FOIA Act in which an NSC staffer wrote to a colleague, ‘Good news’ ‘The Veep mentioned Enron in his meeting with Sonia Gandhi.’
However, he did meet with the Indian National Security Advisor, Brajesh Mishra, though his offer to sell DPC was flatly rejected.459

Despite the failure to agree a sale, negotiations between DPC and the Maharashtra government continued throughout July and August.460 Direct negotiations were further supplemented by continued diplomatic pressure from the U.S. In the July, U.S. Assistant Secretary of State, Christina B. Rocca flew to Delhi to meet with Indian officials on Dabhol.461 In discussing India’s investment image, she is reported as saying, ‘many of India’s problems in this regard can be summed up in the five letter word E-n-r-o-n.’462 That same month National Security Council (NSC) Advisor, Condoleezza Rice, was appointed to head the ‘Dabhol Working Group’ within the Security Council, which also included officials from Treasury, the State Department, the Ex-Im Bank, and OPIC.463 This was followed up by a meeting in August between Indian officials and the U.S. Ambassador to India, Robert Blackwell where Enron was again discussed.464

American diplomatic cajoling appears to have prompted a change in attitude by Indian officials, evidenced by the formation of ‘Committee for Developing Road Map for DPC’ in August.465 Any progress that had been made, however, was soon undone by Lay himself, who in an interview with the London based Financial Times, conducted the very same day as the committee was announced, threatened that the U.S. would apply economic sanctions against India, if Enron did not receive a fair price for its

459 Interview Notes Ministry of Finance, New Delhi. The request and the consternation it affected were confirmed to me in two separate interviews with Indian officials, both of whom felt that the request was inappropriate, as the Prime Minister was a head of a country, while Ken Lay was merely the head of a company, and one for that matter who flagrantly disregarded Indian law.

460 Interview Notes, Former, Chief Minister, Maharashtra Government, Mumbai.


463 U.S. House of Representatives, ‘Background on Enron’s Dabhol Project’, February 22, 2002, p. 3. According to information received through a Washington Post FOIA, the NSC recommended broadening the ‘advocacy efforts’ on behalf of Enron. Indeed, according to the Post, the NSC went so far that it ‘acted as a sort of concierge service for Enron Chairman Kenneth L. Lay and India’s national security adviser, Brajesh Mishra’ in trying to arrange a dinner meeting between the Indian official and Lay.’ See ‘NSC Aided Enron’s Efforts: Agency Sought Lay Meeting With Indians on Plant’ by Dana Milbank and Alan Sipress, Washington Post Staff Writers, Friday, January 25, 2002; Page A18

464 Available online at http://www.corpwatch.org/article.php?id=2278 Date Accessed 24.07.05

465 Interview Notes Ministry of Finance, New Delhi. The Committee also included representatives from the Ministry of Finance, the Central Electricity Authority, the Ministry of Petroleum and Natural Gas, the three other Indian lenders and the MSEB and Maharashtra government.
assets. The comments were greeted with dismay by both U.S. and Indian government officials, the latter of whom in a strongly worded statement accused Lay of employing ‘strong arm tactics’ while the U.S. Ambassador immediately convened a press conference, refuting the allegations. U.S. diplomatic pressure did not lessen, however. On September 1st U.S. Trade Representative Robert Zoellick arrived in Delhi for talks with Indian officials, with a mandate from Treasury to get the World Bank to express concern to the Government of India over Enron problems. Later in mid-September, Lay would write personally to the Indian Prime Minister urging that serious consideration be given to the proposed sale, noting the price of $2.3 billion ‘strikes me as exceptionally reasonable compared to the size of our legal claim’ which he estimated at between $4-5 billion.

The pressure did not, however, deter MSEB, who promptly responded by filing a Notice of Motion (No. 284-2001) in the Bombay High Court seeking to restrain DPC from recovering monies from Canara Bank under the letter of credit. The notice was granted, with the result that DPC defaulted on its phase I debt. Later in October (3rd), U.S. Vice-President Dick Cheney held a second ‘Dabhol’ meeting with the Indian External Affairs Minister, Jaswant Singh. A meeting in Delhi followed this between the U.S. Undersecretary for Economic, Business and Agricultural Affairs, Alan Larson, and the Indian Finance Minister and the Indian National Security

466 Lay was quoted as saying: ‘There are laws that could prevent the U.S. government from providing any aid or assistance to India going forward if, in fact, they expropriate property of U.S. companies’ See ‘Enron Issues Veiled Threat to India’, Financial Times (Aug. 24, 2001).

467 See http://www.corpwatch.org/archive/article.php?id=2278 Date Accessed 24.07.05.

468 See http://www.corpwatch.org/archive/article.php?id=183 Date Accessed 10.05.05. The second letter was dated September 14, 2001. The talking points had been prepared by OPIC at the request of the NSC Dabhol Working Group.

469 Available online at http://www.corpwatch.org/article.php?id=2278 Date Accessed 24.07.05.

470 Interview Notes MSEB Chairman, Mumbai. As part of phase II financing, a portion of revenues accruing to MSEB were automatically placed in an escrow account that was covered by a Letter of Credit issued by Canara Bank.

471 See http://www.corpwatch.org/archive/article.php?id=183 Date Accessed 10.05.05. The $2.3 billion included $1.2 billion for Enron’s 65 percent equity stake plus $1.1 billion for the purchase of the offshore lender’s debt. The letter also went on to note, ‘Our experience would indicate that contracts with governmental authorities in India really do not seem to represent anything more than a starting point for a later renegotiation and are broken by Indian governmental authorities whenever and as often as they prove inconvenient or burdensome.’ See ‘White House Aided Enron in Dispute: Cheney and Others Intervened Over Indian Power Plant’, Washington Post (Jan. 19, 2002).
Advisor, resulting in a ‘commitment from each to get the government energized on this issue prior to the PM’s visit to Washington on November 9.’

Once again, U.S. diplomacy appeared to have paid dividends when in November, MSEB wrote to DPC inviting them to attend a meeting with both the Indian and Maharashtra government’s to finalize arrangements for the sale of Dabhol. DPC refused the offer, however, and offered no explanation as to why they had failed to respond to MSEB’s earlier request to assist in rearranging the LNG contracts with Oman as a precondition of sale. The day after receiving DPC’s reply, the Indian lenders filed a joint-action on November 6th, seeking preservation of the assets and protection of their security. The Bombay High Court duly granted the request, thereby restraining DPC from issuing the Final Termination Notice.

The action caused consternation from OPIC President, Peter Watson, who on the very same day drafted a letter to the Indian Prime Minister warning that ‘[T]he acute lack of progress in this matter has forced Dabhol to rise to the highest levels of the United States government.’ Just two days later, however, it appears that the United States was forced to reconsider its position. Initially, President Bush had planned to raise the Dabhol issue in his meeting with the Indian PM on November 9th, evidenced by the preparation of ‘Dabhol Talking Points’ by the NSC Dabhol Working Group. The day before the meeting was due to take place; however, Enron disclosed $586 million in previously unreported losses. As a result, the Dabhol issue was removed from the agenda.

The revelations do not appear to have softened DPC’s position, however. Thus, having attended a preliminary meeting with government officials on November 9th, DPC refused to attend the scheduled meeting, with the institutional lenders held in Singapore (November 10-12th). Having failed to attend the meeting with the offshore

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472 Available online at http://www.corpwatch.org/article.php?id=2278. Date Accessed 24.07.05.
473 Interview Notes MSEB Chairman, Mumbai.
475 It was not so much the unreported losses that concerned market watchers, so much as the other ‘accounting adjustments’ resulting in the addition of $ 2.59 billion of previously unreported debts
sponsors, DPC then wrote to the Indian lenders a week after the Singapore meeting, requesting additional time to negotiate with the offshore lenders.\textsuperscript{476} Less than a week after sending the letter, the dispute would change irrevocably, with the announcement on December 2\textsuperscript{nd}, 2001 that Enron had filed for ‘Chapter Eleven Bankruptcy.’\textsuperscript{477}

Two days later, OPIC and the lead arranger for the Indian government-owned lending syndicate received a letter from DPC informing them that it was terminating all ancillary contracts.\textsuperscript{478} A second series of meetings was immediately convened by OPIC for December 13-14\textsuperscript{th}, during which a consensus appears to have been reached regarding the sale of DPC. Despite the apparent progress, DPC announced in the last week of 2001 that it had decided to lay off all its remaining employees in India, including those based at the Dabhol plant site.\textsuperscript{479}

Within days of the announcement, the Industrial Development Bank of India (IDBI) received the first of two anonymous letters alleging that DPC had illegally removed e-chips, CDs and manuals from the plant.\textsuperscript{480} On January 3\textsuperscript{rd}, DPC acknowledged the removal of the items, claiming it had been done for safekeeping while maintaining that the chips were still in India.\textsuperscript{481} It also informed the IDBI that all the project documents had been shipped to London, in preparation for arbitration. The IDBI replied, stating that the removal of the chips was a violation of the PPA, and Indian Customs Law. On January 16\textsuperscript{th}, a second anonymous letter was then received alleging that the DPC management had ordered the destruction of documents and plant records.\textsuperscript{482} The Indian onshore lenders again wrote to DPC on January 16\textsuperscript{th} to inquire

\textsuperscript{476} Interview Notes Industrial Development Bank of India, Mumbai.
\textsuperscript{477} For a good account of the last minute jockeying that preceded the announcement, including personal calls to the White House from Lay himself, See Loren Fox, \textit{Enron, The Rise and Fall}, (New Jersey: John Wiley and Sons Inc, 2003).
\textsuperscript{478} Interview Notes, Industrial Development Bank of India, Mumbai.
\textsuperscript{479} ‘Dabhol Power Company to Sack all Employees’\texttt{http://www.rediff.com/money/2001/dec/06dpc.htm}
Date Accessed 05.02.04.
\textsuperscript{480} The chips or E-Proms contained the plant’s operating data, which was then used to automatically calibrate the correct operating parameters, given fluctuations in ambient air temperature and humidity etc. Without the ‘E-Proms’, the plant could not operate.
\textsuperscript{481} Interview Notes MSEB Chairman, Mumbai. Contrary to repeated assurances from DPC, two separate but unconfirmed reports by interviewees allege that the chips and manuals were being held by Enron appointed Trustees in Rotterdam.
\textsuperscript{482} Once again, although the allegations have never been proven, given the destruction of similar records by Enron in Houston, and by the company’s auditors, Arthur Andersen the allegations appear credible.
about the veracity of the claims, stating that DPC’s actions had jeopardized their security over the assets in violation of the Bombay High Court Order.483

Despite a pending MERC ruling on the removal of the e-chips, a third round of meetings of what was now entitled the ‘Working Group of Lenders’ took place in Mumbai during the week of January 17-24th. With the preparations for the sale of the project concluded, the head of Indian lending syndicate invited expressions of interest on January 30th, 2002. Three bidders, Tata Power Company, BSES Ltd. and Gas Authority of India immediately submitted expressions of interest.484 The following day, the U.S. Ambassador to India confirmed in a hastily arranged press conference that Enron had collapsed, whilst taking the opportunity to make clear that despite Enron’s demise, the U.S. government’s position regarding the ‘sanctity of contract’ had not changed.485

The announcement sparked off another round of legal position taking. In the February, Bechtel filed suit in New York, seeking to recover from the Enron Creditor Committee $55 million in unpaid fees from Dabhol.486 Recognizing that the suit could impede the proposed asset sale, the four Indian lenders responded in kind, filing suit in the Bombay High Court on March 9th seeking to restrain the New York Court from taking actions that could impair DPC’s assets.487 The request was summarily granted and a receiver was appointed. Three days later, the legal deadlock was consummated, when the IDBI received a letter from the ‘Official Committee of Unsecured Creditors of Enron Corp.’ stating that disposition of any Enron related special-purpose-vehicle (SPV) assets without prior approval of the Court would be deemed a violation of said order.

483 Interview Notes, Industrial Development Bank of India, Mumbai.
484 Interview Notes Industrial Development Bank of India, Mumbai.
486 The application was made to the Supreme Court of the State of New York, on behalf on Bechtel International Corporation, registered in Mauritius and Enron Affiliates with regard to construction, supply and service contracts.
The resulting legal impasse did not prevent further position taking by the disputants. In May, MSEB instructed its nominee to resign as Director of DPC, leaving only two Directors on the Board of DPC.\(^{488}\) Under Indian Company Law, the Board was effectively prevented from functioning due to the lack of a quorum. MSEB followed up in August 2002 by directing its subsidiary Maharashtra Power Development Corporation Ltd. (MPDCL) to file a petition (C.P. No. 45 of 2002) and to file appeals in the Bombay High Court challenging the reconstitution of the DPC Board. The appeal was immediately granted thereby restraining the Board of Directors of DPC (September 9th, 2002). In addition, that same month, MSEB filed a petition with MERC for an *ad hoc* power supply agreement for one year at a rate to be fixed by MERC, the Maharashtra authorities, MSEB and the four Indian government-owned banks.\(^{489}\) Under the terms of the High Court Order, DPC, despite still owning the plant, was prevented from participating in the proceedings. In September, the Bombay High Court granted stays of the arbitration agreements in favor of MPDCL and the Maharashtra government. By enjoining DPC, the court order effectively prevented the company from pursuing offshore arbitration, a situation that would remain unchanged for six months.

By the following April, the patience of the offshore lenders had run out. In a press release, ABN Amro, stated that the ‘offshore-lenders’ had filed ‘a notice of arbitration under the rules of the United Nations Commission on International Trade Law’ seeking to recover $339 million in respect of phase I.\(^{490}\) One month later on May 12th, the Supreme Court of India ordered MERC to refrain from issuing any more ‘Orders’, and DPC to refrain from pursuing arbitration pending the final settlement of the appeal.\(^{491}\) Any thoughts that the Supreme Court’s public rebuke of the MERC signaled a softening of the Indian government’s stance were soon dispelled, however, when six weeks later it applied for and obtained an injunction in the Delhi High Court restraining DPC from pursuing arbitral proceedings against the Union of India.

\(^{488}\) Interview Notes MSEB Chairman, Mumbai.
\(^{489}\) Interview Notes, MSEB Chairman, Mumbai. The petition (No. 19/2002) was filed with MERC in the Bombay High Court.
\(^{490}\) ‘DPC’s foreign lenders go for arbitration in London’
http://www.rediff.com/money/2003/apr/17dpc.htm Date Accessed, 05.02.04.
\(^{491}\) Interview Notes MERC Chairman, Mumbai.
The ensuing deadlock did not last long, however. At the beginning of September a joint statement issued by G.E. and Bechtel confirmed reports that the International Centre for Dispute Resolution of the American Arbitration Association (AAA) had ruled in their favour ordering OPIC to pay their claims in full, amounting to $57 million. According to the published determination, the claimants had initiated the arbitral hearings against the agency only after they learned through unidentified sources that OPIC had no intention of paying their claims no matter what the circumstances. In handing down their judgment, the three person tribunal rejected OPIC’s argument that the actions of MSEB in rescinding the PPA were taken as a commercial operator and were, therefore, subject to exclusions in Sections 10.05 and 10.07 of the contracts of insurance. To this end, the tribunal found that a ‘total expropriation within the meaning of Section 4.01 of the OPIC policies had taken place’ judging the exclusions concerning actions taken by Indian government authorities in commercial capacities listed in Section 4.03(b), not to apply.

In making their determination, the tribunal noted that it had relied upon what it termed ‘fundamental rules of insurance contract construction’ which state that ‘[i]n the event of uncertainty or ambiguity, insurance contracts are construed against the drafting party . . . and in favour of the insured and indemnity.’ The tribunal also took the opportunity to castigate OPIC, with regards to its refusal to issue the Final Termination Notice (October 15th, 2001), which in its judgment closed whatever window of opportunity was available to DPC to exercise its rights under the PPA.

Finally, the tribunal also rebuked OPIC for the unreasonable pressure placed on the claimants to participate in what they termed a ‘deeply flawed and disingenuous auction process,’ noting claimants only agreed to do so, for fear that OPIC’s threats to Enron that it would never pay any claim unless the company cooperated in the sale

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493 The claims were initiated under Section 8.05 of OPIC Policy Nos. E418 and E 839 and Section 8.05 of OPIC Policy No. F153.

would apply equally to them. Buoyed by the award, G.E. and Bechtel then filed for arbitration in London, pursuant to the PPA, seeking compensation of $1.2 billion also in the September.

The government, for its part, acknowledged that the Tribunal’s award created a claim against it under the terms of the Investment Incentive Agreement, whilst confirming that it had not yet received word from OPIC whether it intended to pursue the subrogated claim. Privately, however, Indian government representatives expressed consternation bordering on fury, at the perceived slight to the country’s sovereignty. On hearing of the case through the press, a letter was sent to OPIC offering assistance with its defence, including making available all records to that effect. The agency refused the offer of assistance, however, and in a move that angered India informed the Ministry of Finance chaired committee that it would only be contesting the case on ‘matters of law’ relating to the Tribunal’s jurisdictional competence to hear the case, rather than on ‘the facts of the case.’ Indian officials likened the proceedings to a ‘charade’ intended to divert attention from what in reality was ‘USA inc.’ closing ranks. The response from the Indian government was forthright; on September 24th, the Indian Minister of Finance stated before the gathered media that India would use all its resources to fight the arbitration.

If the news of the AAA award, and what was interpreted as OPIC’s less than spirited defence enflamed relations between the two governments, the news that the agency had paid a third claim to the Bank of America threatened to derail negotiations.

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495 Bechtel Enterprises International (Bermuda) Ltd; BEn Dabhol Holdings Ltd; and Capital India Power Mauritius I, Claimants, -against- Overseas Private Investment Corporation, Respondent, 25 September, 2003.
496 Katakam Anupama, ‘The issue of arbitration’ Frontline Vol. 20, Issue 20, September, 27th, 2003. The arbitration action was filed by the two companies' affiliates, Energy Enterprises (Mauritius) Company and Capital India Power Mauritius I, pursuant to the bilateral investment agreement between the Republic of Mauritius and India, under UNCITRAL Rules.
498 Interview notes Ministry of Finance, New Delhi and Interview Notes, Head of the Dabhol Inter-Ministerial Group, New Delhi.
499 Interview Notes Ministry of Finance, New Delhi. Time and again, Indian officials confirmed in interviews that the move although technically legal, was an affront to India’s sovereignty.
altogether. The payment for $27 million was made following the determination by OPIC that loans made by Bank of America to DPC had been expropriated thereby fulfilling the requirements laid out in Section 4.01 of the contracts of insurance. Aware of mounting anger among Indian officials, OPIC then wrote to the government of India in an attempt to mollify it, inviting them to commence negotiations under the terms of Investment Incentive Agreement. The invitation was refused. The initial approach was followed by a second letter and then a third, on November 18th and December 30th respectively, but each was declined by the Indian authorities.

Despite the Indian government’s demonstrable reluctance to continue negotiations, OPIC officials again arrived in Delhi on January 16th, for three days of scheduled talks with DPC stakeholders. During the visit, OPIC also met with prospective bidders for DPC, including Reliance Energy Ltd (REL) and the Tata Power Company. One week after departing Delhi, the agency announced that it had reached an agreement to purchase Enron’s remaining equity stake in the project from the Enron creditor committee for just $22 million.

The situation remained little changed until March, when in a surprise announcement, the U.K. Trade Minister, Mike O’Brien, confirmed before the British Parliament that the Export Credit Guarantee Department (ECGD) had been contacted by a syndicate of commercial banks seeking compensation in the amount of $60 million for losses arising from expropriation of loans to the Dabhol power project. On learning of the

501 Interview Notes Head of the Dabhol Inter-Ministerial Group, New Delhi. If unconfirmed reports from interviews with senior Indian officials are to be believed, those calling for India to break-off diplomatic relations with the United States were, temporarily at least, in the ascendancy.
502 See OPIC Memorandum of Determination, Bank of America as Trustee, Contract of Insurance No. F041
504 State-State Arbitration Request, United States and India, Nov. 4, 2004. p.5.
506 Interview Notes Ministry Of Finance, New Delhi. REL is predominantly a natural gas company whereas Tata is India’s largest conglomerate, with diversified holdings across a range of industrial goods.
508 Sanjay Jog, ‘Foreign Lenders Pressure ECGD’, Financial Express, March 8, 2004. According to the information provided by the Minister, the ECGD had first received a claim application in 2001, before receiving a second in mid 2003. However, when contacted by the Financial Times of London both
involvement of the ECGD, the Indian government immediately wrote to the British government seeking confirmation but no reply was ever received.509 One week later, the Federal government committee established to oversee the negotiations with DPC announced that it had received word from OPIC that the agency had cancelled the scheduled meetings until after the upcoming Indian elections, before which time no progress could be made.510

On April 8th, G.E. and Bechtel announced that they had purchased Enron’s equity stake in DPC. The announcement, noted Indian officials, was a surprise given OPIC’s recent communications regarding the sale of the assets, and the decision to suspend negotiations pending the Indian election scheduled for April 20th.511 According to unconfirmed reports, the U.S. Bankruptcy Court had rejected REL’s $25 million bid, despite it being higher than the offers made by G.E. and Bechtel.512 Moreover, it appeared that the deal had been prearranged, thus bolstering claims that the entire auction was a sham, when it was revealed that the two companies had approached the Court on March 5th seeking its approval of the settlement.513 Sensing this consternation, G.E. and Bechtel then issued a joint press release refuting allegations by the Indian media that the move was designed to convert a private dispute into a US versus India issue.514

Having completed the sale of Enron’s equity stake, OPIC now sought to revive the ongoing negotiations between the onshore and offshore lenders previously stalled, pending agreement on the debt discount rate. Meetings were held in Singapore on

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509 Interview Notes Head of the Dabhol Inter-Ministerial Group, New Delhi.
510 Interview Notes Head of the Dabhol Inter-Ministerial Group, New Delhi.
511 Interview Notes MSEB Chairman, Mumbai.
512 Sanjay Jog, ‘REL Plea on Enron Stake Rejected’, Financial Express, April 19, 2004. Although the Indian authorities were widely castigated for not supporting the REL bid, sources in the government stated that the REL bid was not serious, and they did not therefore want to be associated with it. Interview Notes Ministry of Finance, New Delhi.
513 Furthermore, it was subsequently revealed that having received the request to approve the settlement on March 5th the Court then sent letters to the Indian lenders and the Indian authorities inquiring whether they objected to the sale. REL had, it turns out, filed its affidavit objecting to the closed sale, but the Court rejected the REL plea, suo moto, on the grounds that because it was not a party to the PPA it had no standing to object. If this were true, however, it begs the question why the Indian government did not object as a party to the PPA? See, Sanjay Jog, ‘REL Plea on Enron Stake Rejected’, Financial Express, April 19, 2004.
April 22\textsuperscript{nd}-23\textsuperscript{rd}, and again in London on May 12\textsuperscript{th}.\textsuperscript{515} A fourth meeting was then convened in Mumbai at the beginning of June attended by all the project lenders.\textsuperscript{516} According to information provided by the Indian lending syndicate, the offshore lenders comprised of some 60 commercial banks, supported by OPIC, demanded 80 percent of face value (approximately $260 million), while the onshore lenders comprised of the four Indian government owned banks refused to pay more than 60 percent for the loans (the Indian lenders were reported to have offered $146 million), arguing that the default was a commercial issue not a political one. Once again, no agreement was reached.\textsuperscript{517}

Buoyed by the sale of Enron’s equity stake, and ignoring the recent interim injunction issued by the Bombay High Court, OPIC then set about reviving the talks with the new administration.\textsuperscript{518} On June 1\textsuperscript{st}, a letter was sent to the new Indian Minister of Finance, Palaniappan Chidambaram requesting the commencement of negotiations. This was followed up on July 16\textsuperscript{th}, with a letter to the newly elected Indian Prime Minister, Manmohan Singh, informing him that OPIC was ‘exploring imminent action’ under the Bilateral Agreement in the absence of meaningful progress.’ Moreover, although, the Indian government declined the offer, the new administration announced on August 2\textsuperscript{nd} that it had formed an Inter-Ministerial Group to oversee a final settlement and the revival of Dabhol.\textsuperscript{519} Under the terms of the proposed settlement, an SPV would purchase the offshore debt and equity, with money raised from Indian banks through an Indian government guarantee to a maximum of $500 million.\textsuperscript{520}

Sensing that the mood in Delhi had shifted, OPIC officials again arrived in the Indian capital for talks with Indian officials, scheduled for September 9\textsuperscript{th}. And although the talks were reportedly amicable, the two sides failed to agree on the sequence of the

\textsuperscript{515} Interview Notes, Industrial Development Bank of India, Mumbai.
\textsuperscript{516} Interview Notes, Industrial Development Bank of India, Mumbai.
\textsuperscript{518} DPC had filed for arbitration on May 21\textsuperscript{st} seeking damages of Rs. Crore 26.000 (approx. $550 million). In so doing it had violated the terms of the injunction granted by the Bombay High Court and the Indian Supreme Court. MSEB had responded on June 2\textsuperscript{nd} by filing an additional suit alleging that DPC had violated the interim injunctions, which was subsequently granted.
\textsuperscript{519} Interview Notes Head of the Inter-Ministerial Group, New Delhi and See also Sanjay Jog ‘FinMin, OPIC Lock Horns Over Claims By GE, Bechtel in DPC’, \textit{Financial Express}, September 9, 2004.
proposed buyout, owing to OPIC’s refusal to agree to the proposed sale absent the inclusion of its unsecured loans in any offshore debt buyout.\(^{521}\) The Inter-Ministerial negotiating team, on the other hand, indicated that they were prepared to accept the contractor’s claims, and settlement of OPIC’s subrogated PRI claims against the Indian government but not the unsecured loans, the settlement of which should be arranged with the new owners.\(^{522}\) Following the meeting, the Ministry of Finance released a statement noting that ‘For the equity claims of GE and Bechtel, it has been indicated to OPIC that any proposal to allow equity holders a better deal that the debt holders would violate well established international norms.’\(^{523}\) Despite the failure to agree a compromise solution, further talks between the Ministry of Finance and OPIC were scheduled for the middle of October. Before that could happen, however, the Ministry of Finance received word from the Indian lending syndicate that OPIC, along with the other ECAs had sent notice that they were preparing to foreclose on the outstanding loans, pending a final settlement.\(^{524}\) Should this have occurred, it would have prevented the sale, leaving the disputants back at stage one.\(^{525}\)

OPIC again upped the ante in the November, filing for \textit{ad hoc} state-state arbitration with respect to the $110 million paid by the agency to DPC investors.\(^{526}\) According to the notice, the Indian government had ‘violated established principles of public international law’ so as to ‘render the GOI liable for reparation, therefore and, hence, are arbitrable under Article 6 (c) of the Bilateral Agreement.’\(^{527}\) The amount represented reparations due to OPIC for five separate claims, including Bank of America, G.E. and Bechtel, as well as two further claims paid by OPIC to the Enron Creditor Committee for $23.9 million in April 2004.\(^{528}\)

\(^{521}\) Interview Notes Ministry of Finance, New Delhi. The Inter-creditor Agreement ranked OPIC’s unsecured loan to phase II \textit{pari passu} with the commercial lender’s debt.

\(^{522}\) Interview Notes Ministry of Finance and Head of the Inter-Ministerial Group, New Delhi.


\(^{524}\) Interview Notes Ministry of Finance New Delhi, according to whom the information was received from the Chairman of the Industrial Development Bank of India who in turn had been informed by JBIC.

\(^{525}\) Sanjay Jog, ‘GOM on Dabhol Revival to Meet on Friday,’ \textit{Financial Express} and See also Sanjay Jog, ‘Dabhol GOM to Meet on October 26\textsuperscript{th}’, \textit{Financial Express}, October 19, 2004.


\(^{527}\) Request for Arbitration under the Investment Incentive Agreement, p. 5.

\(^{528}\) Request for Arbitration under the Investment Incentive Agreement, p. 16. The additional claim of $23 million was in fact three separate claims paid to Enron affiliates, including Bechtel India Power Investment ($9.995 million), G.E. EFS India Holdings ($9.995 million) and Offshore Power Production CV. ($400,000).
Having filed for arbitration, OPIC representatives flew again to Delhi to meet with Indian officials on December 21st. There followed a lull in activity until the new year, when OPIC officials once again arrived in Delhi (January 12th) for talks with Indian officials, led by the Joint-Secretary of the Ministry of Finance, Anoop Mishra. The meeting ended in stalemate, however, due to the failure to agree on a price, G.E. and Bechtel purportedly seeking $460 million against the government’s valuation of $158 million, later increased to $213 million. Just ten days later, OPIC officials completed an intensive round of shuttle diplomacy with their arrival in Singapore for two days of scheduled talks with the offshore lenders, including: ABN Amro; ANZEF; BN Paribas; Credit Lyonnais; Este Bank der Oesterreichischen Sparkassen A.G., Credit Suisse First Boston and Standard Chartered Bank.

With the April 21st deadline drawing ever closer and still no sign that the impasse had been broken, the resolution process received some welcome news on February 19th in the form of leaked minutes of a meeting of the Cabinet Committee on Economic Affairs, held the previous day. The memo detailed the terms of settlement agreed, including with respect to all the outstanding amounts owed to the offshore lenders, the ECA-lenders as well as OPIC’s PRI claims. Having reached what they believed to be an acceptable compromise, Indian officials then flew to Washington to meet with OPIC. Two separate meetings were held on March 7th and March 9th, though no agreement was finalized.

On March 12th G.E. and Bechtel wrote to the Indian government, stating that the $213 million offer was ‘well below the $250 million verbally offered by Mr Damodaran (former chairman of the Industrial Development Bank of India) in Scott Bayman’s (CEO, G.E. India) last meeting with him.’ Undeterred, the Mishra-led Indian-government negotiating team arrived in New York to meet with OPIC on March 17th,

529 Interview Notes Ministry of Finance, New Delhi.
530 Rajesh Ramachandran, ‘ENRON Big Payoff In Small Print’ Outlook India, Monday 25, April 2005.
531 Sanjay Jog, ‘OPIC to meet government panels on settling Dabhol project claims, December 22, 2004 Financial Express, India.
532 To view a copy of the memo of the CCEA meeting, See http://india.eu.org/2396.html Date Accessed 30.11.05.
533 Interview Notes Head of the Inter-Ministerial Group, New Delhi.
534 Rajesh Ramachandran, ‘ENRON Big Payoff In Small Print’ Outlook India, Monday 25, April 2005.
with a mandate to finalize the settlement.\textsuperscript{536} To the surprise of the Indian negotiators, however, their increased offer of $250 million was flatly rejected, having been informed that G.E. and Bechtel now sought $350 million.\textsuperscript{537} Dismayed by the apparent u-turn, the government appointed negotiating team departed empty-handed.

The apparent failure was the final straw for Bechtel, who immediately filed for arbitration at the International Court of Arbitration (ICC) in Paris pursuant to the India-Mauritius Bilateral Investment Treaty.\textsuperscript{538} Upon receiving the request, the ICC immediately sent a letter to the ‘Indian respondents’ informing them of the upcoming hearing, scheduled for April 27\textsuperscript{th}. In their reply, Maharashtra, acting through the Indian government appointed legal counsel, challenged the tribunal’s jurisdiction, informing them of their decision not to participate. Despite the setback, the hearing went ahead as scheduled. The tribunal found that taken collectively the Maharashtra government and affiliate agencies, including the MPDCL and the MSEB had expropriated Bechtel’s 42.5 percent holding in Dabhol, ordering the defendants to pay damages of $125 million. Continuing on, the tribunal averred that, ‘aware of the unusual circumstances . . . [it had] conducted the proceedings before it with rigorous attention to the rights of the absent respondents.’\textsuperscript{539}

Despite its best efforts, the comments of the tribunal appear to have done little to placate the Indian government, as evidenced by its failure to comply with the award and make payment to Bechtel by the May 27\textsuperscript{th} deadline. Three days later, Bechtel launched a separate action in the Southern District Bankruptcy Court of New York

\textsuperscript{536} According to unconfirmed reports in the Business Standard of India, a deal had been reached two days previously between OPIC, the offshore lenders and the Indian authorities. Under the terms of the deal, the parties signed an MOU providing for the purchase of OPIC’s loans at 80 percent of face and the offshore debt for $230 million. See Kavita Nair, ‘Indian lenders, Opic ink deal over Dabhol debt Banks, FIs may buy out foreign lenders, Opic at a 20% discount’, Indian Business Standard Mumbai March 15, 2005.

\textsuperscript{537} Interview Notes Ministry of Finance New Delhi.

\textsuperscript{538} See ICC Case No. 12913/MS 1. Capital India Power (Mauritius) and 2. Energy Enterprises (Mauritius) Company (Mauritius) vs. 1. MPDCL, 2. MSEB and 3. State of Maharashtra. The proceedings were brought by Bechtel’s Mauritius-based subsidiary Bechtel Enterprises Holdings Ltd. that owned a ten percent equity stake in DPC, and was domiciled in Mauritius and the Netherlands, hence the applicable treaty was the India-Mauritius Treaty. Foreign investors in India often register in Mauritius due to the tax benefits the foreign location provides. Should the action under the India-Mauritius Treaty have failed, Bechtel had already filed for a second arbitration with the ICC, scheduled for July 2006 (‘the Netherlands proceedings’).

seeking to seize the assets of MSEB subsidiary, MPDCL in lieu of its unmet claim against Maharashtra. The request was duly granted, thereby triggering three days of intensive talks between Bechtel and the Federal authorities, beginning on July 4th. The negotiations concluded just one day prior to the commencement of a second arbitral hearing scheduled for July 8th in Paris, with the announcement that Bechtel had accepted the Indian offer of $160 million to settle all outstanding claims.540

Seven days later, the Indian government announced that it reached a final settlement of the dispute, enabling the sale of DPC’s assets to an SPV, the Gas and Power Investment Company (GAPIC), to proceed. The newly created entity, it was later revealed, was owned by a consortium of Indian investors, including the National Thermal Power Company, the Gas Authority of India Limited, and two Indian government owned banks, the IDBI and the ICICI bank, each of whom contributed 500 crore to participate.541 Ownership of the newly created entity was split 28.5 percent apiece, shared in the case of the Indian lenders equally, while MSEB retained its original 14.85 percent equity stake.

According to the terms of final settlement, the offshore lenders debt was purchased for $230 million, a discount of approximately $180 million, including outstanding interest. OPIC, on the other hand, received $110 million for the six PRI claims paid, of which $20.7 million was payable in cash immediately, with the outstanding balance due over eight years, at a nominal interest rate of 2 percent.542 The deferred payment of $91 million was guaranteed by the SPV as well as being counter-guaranteed by the Indian government. In addition to the subrogated claims payment, OPIC negotiated a final settlement of $128 million for its loans, representing a discount on principal of $10 million as well as foregoing all interest owed. Of the money owed, $108 million was payable immediately with the rest deferred. Finally, the outstanding ECA debt,

540 Kandula Subramaniam ‘Govt puts foot down on Bechtel Dabhol revival: However, the Indian side has agreed to sweeten Bechtel deal’ The Indian Express, posted online: Tuesday, July 05, 2005.
541 Rajesh Ramachandran, ‘ENRON Big Payoff In Small Print’ Outlook India, Monday 25, April 2005. A crore is a unit in a traditional number system still widely used in India and Bangladesh. It represents 100 Lakh or ten million Rupees (Rs), equivalent to approximately $221,000 (USD).
542 Interview Notes Ministry of Finance New Delhi.
totalling $500 million owed to Ex-Im, JBIC, and OND was purchased at 80 percent of face, equivalent to $400 million.\textsuperscript{543}

On July 8\textsuperscript{th} it was revealed that the new company would be called the ‘Ratnagiri Gas and Power Private Limited.’\textsuperscript{544} The total cost of the buyout had amounted to $900 million or Rs. 4,000 crore, leaving the four Indian lenders with outstanding liabilities approaching Rs. 10,000 crore. In addition to the outstanding debt, a further Rs. 2,000 crore was needed to restore the plant’s operational capacity as well as to complete the construction of phase II.\textsuperscript{545} Phase I of the renamed Ratnagiri power project began operating at the end of 2005, while phase II power was due to come on line in mid-2006. Finally, on September 23\textsuperscript{rd} the Bombay High Court issued an order of consent, thus enabling the final transfer of assets from DPC to Ratnagiri and Gas and Power Private Ltd.

To conclude the narrative account, in many respects Enron’s Dabhol project was emblematic of the company’s success and its failure. It was so, not only because both ended in a legal quagmire and personal acrimony, but because the fate of the DPC was in many ways tied to struggles within top-level management as to the future direction of Enron as either an ‘asset-heavy’ energy supplier or an ‘asset-lite’ energy-trading firm.\textsuperscript{546} Even before this, however, the fortunes of Enron and the DPC appeared intertwined with one another. Thus, the DPC agreement concluded in 1993 was the company’s first foray into developing markets, and was to have been the springboard for the company’s transformation from a U.S.-based energy company to the first truly global energy company. By the time the DPC was ready to begin production some seven years later in late-2000, the vision despite setbacks appeared

\textsuperscript{543} When the deal was announced the precise terms of repayment for the outstanding ECA debt had not yet been finalized, with a date of December 1\textsuperscript{st} having been agreed upon to resolve all outstanding issues. At the time of writing it was unclear whether the deadline had been met.

\textsuperscript{544} ‘Dabhol project renamed’, ENS Economic, Posted online: Friday, July 08, 2005.

\textsuperscript{545} G.E.’s support appears to have been rewarded, with the announcement that it had been chosen as one of the contractors employed to restore the plant to operational capacity.

\textsuperscript{546} As with any story of this kind, while there were many losers, there were also winners. Thus, while reputations were battered, for some Enron’s expansion in to India yielded considerable financial reward. Foremost in this respect, was the former Head of Enron International and later ‘Azurix’ (the company’s ill-fated Water services arm), Rebecca P. Mark, dubbed ‘Mark the Shark’ or alternately ‘Hell in High Heels.’ Mark, having been Jeffrey Skilling’s main rival to take-over from Ken Lay was pushed aside in August 2000 as part of the Skilling’s transformation of the company from energy supplier to energy-trading firm, leaving her free to walk-away with an estimated personal fortune of $82.5 million. Despite being named in a number of Congressional hearings, Mark, who once graced the cover of Forbes magazine, has thus far escaped civil and criminal action.
within grasp; Enron had grown from mid-sized energy company into a diversified energy-giant, making it the seventh largest company in America measured by market capitalization. Yet within twelve months, the Dabhol project was mired in political and legal wrangling and the former darling of the investment community had filed for chapter eleven bankruptcy. In India and in the U.S., the reality of Enron was far removed from the hubris.

For OPIC, Enron’s bankruptcy was both a curse and a blessing. Most immediately, the company’s collapse, followed by a Congressional inquiry into the company revealed an unusually close working relationship between the agency and Enron, which saw the program labelled a ‘corporate subsidy.’ On the flipside, the collapse of the main project sponsor provided the agency with the required breathing space to pursue a negotiated settlement. Second and by extension, because Enron had collapsed, OPIC was able to arrange the sale of the company’s equity stake for just $22 million, representing a discount on book value of more than a billion dollars. The difference in price effectively provided the remaining disputants with a billion-dollar buffer so as to facilitate a settlement. Thus far the chapter has sought to detail the critical events from the inception of the dispute through until the final settlement in late 2005. This next part of the chapter by contrast is concerned with the first of the two questions that guide the case study research: regarding the impact of OPIC investment insurance on the processes of resolution, as well as the final settlement.

**OPIC Investment Insurance and the Politics of Dispute Resolution**

In order to address the question, the section will analyze the agency’s judicial role in paying or rejecting claims, followed by an analysis of the agency’s diplomatic role in

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547 From the signing of the PPA in 1993 through until the start of the second dispute in 2000 Enron had grown from a mid-sized U.S. natural gas-supplier with revenues of $4.6 billion p.a. to become a diversified energy trading company with operations in more than forty countries and revenues in excess of $100 billion p.a., making it the seventh largest company in America See Loren Fox, *Enron: The Rise and Fall* (New Jersey: John Wiley and Sons Inc., 2003), p. 2.

548 To explain, recall that Lay’s asking price in September 2001 was $2.2 billion versus a final settlement cost of approximately $1.2 billion. The difference, fortuitously for the remaining disputants including OPIC, was roughly equivalent to the different valuations placed on the assets by the investors and the Indian government. In this sense, the billion-dollar buffer enabled the negotiated settlement so desired by OPIC to be realized. Thus, the remaining equity holders’ equity was purchased for a total sum of $305 million versus the original book-valuation of $1.2 billion.
seeking a negotiated solution to the dispute. Before considering the evidence in this regard, however, the first task will be to examine the impact of the provisions of the contracts of insurance in terms of the bargaining strategies employed by the disputants.

The most striking feature in this regard concerns the manner in which the contracts of insurance created incentives for Enron to litigate rather than to seek a negotiated settlement. They did so, on this occasion, however, not because of provisions linking claims to the non-performance of an arbitral award but because in the words of the AAA tribunal, the exclusions contained in the contracts concerning acts taken by MSEB as a ‘commercial operator’ were so onerous as to ‘exclude all political risks except the non-payment of an arbitral award confirmed by an Indian Court of last resort.’\(^{549}\) In this regard, it is clear that both the insurer and the insured were aware of the significance of the provisions of the contracts in delimiting bargaining strategies.\(^{550}\) Evidence of this is provided by way of the lengthy negotiations which took place between OPIC and Enron, concerning the wording of the contracts of insurance. The negotiations centred on the specific provisions as concerned ‘exclusions for acts of MSEB taken as a commercial operator’ following the establishment of the Munde Committee by the newly elected Maharashtra government in 1995 (the subsequent amendments were dubbed the ‘Munde carve-out’).\(^{551}\)

The issue of the contractual wording did not end here, however, as OPIC again received a request to modify the wording for a second time in March 1997, and for a

\(^{549}\) See Bechtel -against- Overseas Private Investment Corporation, American Arbitration Association (International Centre for Dispute Resolution), AAA Case No. 50 T195 00509 02, 25 September, 2003.

\(^{550}\) An OPIC internal memo subpoenaed by the AAA serves to underscore that OPIC in particular was aware of the ramifications of the negotiations, and the final wording, insofar as the memo states that for OPIC the negotiations were designed to prevent the agency, ‘walking into a claim situation.’ See Bechtel -against- Overseas Private Investment Corporation, American Arbitration Association (International Centre for Dispute Resolution), AAA Case No. 50 T195 00509 02, 25 September, 2003. The memo went on to note that the purpose of the changes is to ensure ‘no compensation [would] be payable under expropriation coverage unless DPC [had] exhausted its available remedies under the project agreements . . .’ (underlining in original).

\(^{551}\) To recap, Enron contacted OPIC soon after completing financing in June 1995 with a request to finalize the wording. The ensuing negotiations, concerning Section 4.02(a) which covers exclusions for acts taken by MSEB in its capacity as a commercial operator, lasted more than three months. The first meeting took place on June 6\(^{6}\), while a second and third meeting between the two occurred on July 12, and August 23\(^{rd}\) respectively. It is also significant that Enron accepted the changes. In so doing, it was de facto acknowledging that without OPIC insurance, the project could not go ahead; thereby further refuting the claims of the AAA, that OPIC merely joined other banks in providing loans to the project.
third time in March 1999. On the latter occasion, G.E. had written to OPIC requesting the agency confirm the types of behavior that would fall within the ‘boundaries of expropriatory action.’ OPIC’s refusal to answer the letter clearly shows that both parties were acutely aware that the discussions, ostensibly to finalize a minor point of wording, were in actual fact negotiations concerning the boundaries between legitimate and illegitimate behavior and by extension between commercial and political risks, and as would determine the success or otherwise of claims under the contracts of insurance.

Once again, however, the impact of PRI was not limited to delimiting the payoff matrix facing disputants associated with particular modes of bargaining. In particular, by paying a total of six claims to DPC investors, the agency effectively sanctioned the bargaining strategies of DPC investor’s vis-à-vis the MSEB and the state and federal governments. Of particular note in this regard concerns Enron’s removal of the e-chips required to operate the plant in contravention of Indian customs law. The second issue in this respect concerns the failure of the company to fulfil its duties to make available to potential buyers DPC’s financial records and the operating performance of the plant as were necessary to ensure the success of OPIC’s ‘roadmap for the sale of DPC.’ And although Enron and G.E. and Bechtel would later claim that the chips were removed for safekeeping, and that the financial records were sent to London in preparation for the scheduled arbitral hearing, these actions appear difficult to reconcile with the contractual duties of the insured to ‘negotiate in good faith’ appearing more as an act of overt hostage taking.

Apart from the paying of claims so as to effectively legitimize and de-legitimize the bargaining strategies of the two parties the evidence also demonstrates that OPIC performed a critical diplomatic role in mediating a negotiated settlement between the various stakeholders, though particularly after the collapse of Enron. Even before this, however, the decisions made by OPIC materially impacted the processes of dispute resolution observed. Of principal importance in this regard, was the agency’s refusal

552 The dates were provided by G.E. and Bechtel in the Bechtel—against—Overseas Private Investment Corporation, American Arbitration Association (International Centre for Dispute Resolution), AAA Case No. 50 T195 00509 02, hearing, 25 September, 2003.
553 To recap, OPIC paid the following PRI claims to DPC investors: G.E $31 million; Bechtel $31 million; Bank of America $30 million; Bechtel Indian Power Investment $9.95 million; G.E. EFS India Holdings $9.95 million and Offshore Power Production CV $400,000 (Enron subsidiary).
to permit Enron to issue the final termination notice (FTN) in October 2001 that would have triggered arbitral hearings under the PPA dispute resolution provisions, had it occurred. And while it is unclear what the final outcome might have been had OPIC permitted the notice to be served, specifically whether it did close the window of opportunity available to DPC to exercise their rights as the AAA tribunal averred, it is clear that OPIC’s refusal altered the incentives associated with particular bargaining strategies for both parties at what was a critical period in the process of dispute resolution.\textsuperscript{554}

Having blocked the issuance of the termination notice, the second decision of significance taken by the agency was its rejection of Enron’s PRI claim in the amount of $200 million in early-2002. In explaining the decision, OPIC declared that Enron had breached the contractual warranties stipulating the need to provide true and accurate accounts to the agency.\textsuperscript{555} Irrespective of the reasoning, however, it is clear that had the agency accepted the claim at this juncture, the size of the claim alone would have forced OPIC to pursue subrogation almost immediately thereby foreclosing the possibility of a negotiated settlement. By rejecting the claim, the agency was therefore able to buy some valuable time in which it could negotiate the sale of DPC’s assets thereby avoiding further escalating the dispute into an India-U.S. issue, as the Indian media and certain Maharashtra politicians attempted to portray it.

Later it would become apparent that the denial of claims in conjunction with the refusal to permit the FTN to be issued were part of a concerted strategy pursued by OPIC towards a negotiated solution to the dispute. The third critical mediation function performed by OPIC to this effect concerned the agency’s efforts to coordinate the various offshore lenders, as well as to liaise between the four Indian government-owned lenders and the offshore lenders, so as to prevent either party from foreclosing on their loans, which had it occurred would have prevented the asset sale. In this regard, a division of labour appears to have emerged between the agency and its Japanese counterparts, JBIC and JEXIM, who together undertook to liaise with the

\textsuperscript{554} The dates were provided by G.E. and Bechtel in the Bechtel -against- Overseas Private Investment Corporation, American Arbitration Association (International Centre for Dispute Resolution), AAA Case No. 50 T195 00509 02, hearing, 25 September, 2003.

\textsuperscript{555} See OPIC press release
Indian lenders, so as to persuade them not to foreclose on their loans to DPC.\footnote{It is clear from interviews that the four Indian lenders would not have been happy to work with OPIC in the manner they did with the Japanese because they felt OPIC was too closely allied to the U.S. and its investors, whereas they felt the Japanese agencies were more objective and sensitive to their financial and political needs vis-à-vis their owners, the Indian government.} Persuading the offshore lenders to hold off was, however, only the first of many steps taken by the agency toward the negotiated sale it desired. In this regard, OPIC continued to play a critical in mediating a settlement throughout 2003 and 2004, culminating in its proposed road map for the sale of DPC’s assets, eventually realized in mid-2005.

To conclude the analysis of the role of OPIC, it is clear that the agency performed the central diplomatic role insofar as it oversaw negotiations directly with the Maharashtra and Indian governments, normally the preserve of more established elements of the U.S. foreign policy bureaucracy. More fundamentally in accepting the six claims from DPC investors, the agency fulfilled what amounted to a judicial role. In particular, the claim payments served to frame DPC investor bargaining strategies as legitimate while at the same time framing the actions of MSEB, and the Maharashtra and Indian governments as unlawful so as to effectively delimit the meaning of expropriation in the context of investor-state breach of contract disputes. To this end, the empirical evidence makes clear that the provision of PRI served not only to stimulate FDI, but more significantly it provided the U.S. with a flexible mechanism for economic governance so as to harmonize international property and contract rights on behalf of DPC investors.

Once again, however, to conclude the analysis here would be to leave it incomplete. In particular, although OPIC’s diplomacy clearly impacted the outcome of the dispute, had the agency not fulfilled this role DPC investors would have sought diplomatic protection from the State Department. Further, in making a judgement as to whether to support U.S. investor claims, the State Department relies on the same statutes regarding expropriation as does OPIC, and as contained in the U.S. Foreign Assistance Act, 1961 (third restatement, 1987).\footnote{Further, as was noted in the CalEnergy case study, should the legal validity of the claim be in doubt, both would receive legal assistance from the Foreign Claims Settlement Commission of the Department of Justice.} For this reason, it may be assumed that although the State Department could not perhaps have coordinated the respective

\footnotetext[556]{It is clear from interviews that the four Indian lenders would not have been happy to work with OPIC in the manner they did with the Japanese because they felt OPIC was too closely allied to the U.S. and its investors, whereas they felt the Japanese agencies were more objective and sensitive to their financial and political needs vis-à-vis their owners, the Indian government.}
ECAs with exposure to the dispute so as to prevent them foreclosing on loans as effectively as OPIC did, it would in the absence of PRI have followed much the same path of mediation and advocacy.

Similarly, and to continue the same line of reasoning, although OPIC paid six claims directly to DPC investors, thereby conferring judicial powers upon the agency, had OPIC not done so, the task of determining the legal validity of the claims would have been performed *(de facto)* by the State Department. That is, although the State Department would not have compensated DPC investors upfront, as PRI provides for, in seeking compensation from the Indian authorities on their behalf the effect would have been little different as it would have been tantamount to a judicial determination of the validity of the expropriation claims. Finally, although OPIC’s position as unsecured lender to DPC phase II clearly impacted the agency’s strategy in pursuing the sale of DPC’s assets, the need to balance individual bureaucratic goals against broader national foreign policy objectives in investment disputes, and indeed, interstate bargaining, is not peculiar to OPIC, though the particular policy tensions that arise may well be.

The final point of note in this regard concerns the fact that although the provisions of the contracts of insurance provided Enron and other DPC investors with incentives to litigate this is not unique to PRI. Instead, the contractual provisions merely codified and therefore reinforced the existing bilateral and multilateral treaty provisions regulating FDI between the two countries. In particular, the U.S.-India Investment Incentive Agreement 1997 also provides that the non-performance of an arbitral award may be considered a violation of international law thereby requiring compensation to be paid the investor in receipt of such award.\(^{558}\) Similarly, India is a signatory to the UNCITRAL Model Law of investment as well as the New York Convention on the Enforcement of Arbitral Awards (1958), both of which contain similar provisions to the bilateral agreement in force.\(^ {559}\)

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558 The U.S. India Investment Incentive Agreement in the absence of a formal bilateral investment treaty between the two nations serves to govern FDI between the two countries. The agreement signed in November, 1997, superseded three earlier agreements between the two dated, 1957, 1959 and 1966.

559 India ratified the UNCITRAL Model Law in 1976, while it ratified the N.Y. Convention in July, 1960. India is not, however, a signatory to the World Bank Group’s ICSID.
In this respect, the empirical evidence demonstrates that the emergence of OPIC governance does not replace the existing state based regulatory arrangements governing FDI dispute resolution, including the bilateral and multilateral arrangements in place. Instead, OPIC governance serves as a second layer of protection for U.S. infrastructure investors in order to supplement the existing arrangements. That this is the case, suggests therefore that the emergence of OPIC governance precipitates a qualitative rather than a fundamental shift in the politics of dispute resolution as would be the case in the absence of PRI.

Once again, however, the impact of PRI and OPIC governance was not limited to the international politics of dispute settlement. In this regard, the contracts of insurance once again served to diffuse policy-making power away from the U.S. executive so as to delimit U.S. policy autonomy. They did so on this occasion, however, not because of Congressional pressure on behalf of the remaining DPC investors, though the effects were similar, but because the contracts of insurance provide insured investors with the right to challenge OPIC’s determination regarding their expropriation claims. The AAA award left OPIC with no room for manoeuvre with respect to the expropriation claims first lodged by G.E. and Bechtel in early 2002 so as to force the agency to pay their claims contrary to the preferred position of both OPIC and the executive more broadly, who in the wake of the collapse of Enron did not wish to be seen to be supporting the narrow interests of the remaining DPC investors over and above broader U.S. national interests vis-à-vis India. Moreover, the AAA award forced OPIC to pay the other outstanding PRI claims, evidenced by the payment of the Bank of America claim just one month later (September 2003) where previously the company’s claim had been rejected. The presence of PRI through the AAA provisions served therefore to force a shift in U.S. policy, so as to in turn transform the dispute resolution process.560 It did so, because the PRI claim payments made by

560 The treaty provides for India to compensate OPIC for claims paid with respect to investment insurance issued by OPIC covering ‘loss of investment, in a whole not in part, in a project due to expropriation or confiscation by action of the Government of India.’ Article 3 of the Agreement continues, ‘(b) If the issuer [OPIC] makes a payment to any person or entity, as Issuer of Investment Insurance or an investment guaranty in connection with any Investment Support, the Government of India shall recognize in connection with any dispute contemplated under the provisions of Article 6(c) hereof [State-to-State arbitration] the transfer to the Insurer in connection with such payment of the right to exercise the rights and assert the claims of such person or entity.’ And Article 3(c) states ‘(c) With respect to any interest transferred to the Issuer or any interests to which the Issuers succeeds under the Article, the Issuer shall assert no greater rights that those of the person or entity from when
OPIC triggered claims against the Indian government under the Investment Agreement in force between the two nations thereby transforming an investor-state dispute into a state-state dispute.561

The empirical evidence therefore demonstrates that OPIC PRI is significant in the formulation of U.S. expropriation policy because the contractual provisions providing for AAA arbitration effectively delimited U.S. policy leeway. Most immediately, in the absence of PRI no such mechanism (quasi-judicial review) exists to enable U.S. investors to effectively challenge the State Department and or other instruments of U.S. foreign economic policy-making, as is the case vis-à-vis OPIC. And although OPIC, and by implication the U.S. government retained a degree of leeway with respect to the timing of the subrogated claim against India, as evidenced by the fact that the U.S. delayed initiating state-state arbitration for a full fourteen months (September 2003–November 2004), the payment of the claims signaled the beginning of the end-game so far as the Dabhol dispute was concerned.562 The presence of PRI is therefore significant as OPIC operates under a different set of legal-institutional constraints than does the State Department, with the result that the latter possess greater autonomy in deciding when and by what means to extend diplomatic protection on behalf of U.S. investors. In this regard, the evidence from the Dabhol dispute demonstrates that PRI modifies in a small but significant manner the basic relationship between the state and MNC in the formulation and implementation of U.S. anti-expropriation policy.

Thus far the chapter has considered the role of OPIC and the impact of PRI on the politics of dispute resolution. The final task to be completed therefore is to consider

such interests were received, without prejudice to any other rights that the two parties may have in their sovereign capacities.’ In this regard, and to borrow from Mark Kantor, the Investment Incentive Agreement effectively codifies ‘as an international law obligation the well-recognized insurance law doctrine of subrogation under which an insurer succeeds to the claims of its insured upon honouring a claim under the policy.’ See Mark Kantor ‘Arbitration Award May Alter Dabhol Debate’, Journal of Transnational Dispute Management, available at http://www.transnational-dispute-management.com/samples/freearticles/tv1-2-articles 179b.html. Date Accessed, 08.10.04, p. 2.

561 OPIC had previously received three separate requests to issue the FTN. First, from Enron in October 2001, and on two further occasions in March 2002, one from Bank of America and one from G.E. and Bechtel following Enron’s bankruptcy.

562 Article 2 of the Investment Incentive Agreement (1997) provides OPIC with six months to seek a negotiated solution following the payment of a claim. Failing this, Article 6 of the Agreement provides for OPIC to initiate ad hoc state-state arbitration against India to recover the monies paid, which it ultimately did on November 4, 2004, See ‘Request for Arbitration’ p. 1-21.

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the implications of the findings regarding OPIC governance in terms of the theorized institutional restraints against expropriation, beginning with the power of legal rules and legalized modes of dispute settlement, before then examining the role of state power and interests in determining the final settlement.

**OPIC Governance: State Power Vs. Power of Legal Rules**

At first glance the processes of dispute settlement appear as highly legalized. Thus, the dispute was by one estimate the subject of some 30 separate court actions in India alone, including in the Bombay High Court and the Supreme Court of India as well as being the subject of at least five pending arbitral hearings at its conclusion in mid-2005. In addition to which, the dispute had already been heard by two separate arbitral bodies, including in London in 1995 as well as the action brought by Bechtel in the International Commercial Court in Paris in 2005. At the same time, however, the number of separate court actions should not obscure the fact that the use of the Indian court system by the Maharashtra and Indian governments’ was part of bargaining between the disputants. That this was the case was publicly acknowledged by the then newly elected government of Maharashtra following the first arbitral award in 1995 when it conceded that the first arbitration (heard in London) had been used to extract more favourable terms from DPC. The use of legal and quasi-legalized modes of dispute settlement reflected, therefore, not some assessment by the Indian authorities of the efficacy of judicial modes of settlement but instead instrumental calculations concerning the most effective means to frustrate DPC investor attempts to exercise their rights to initiate arbitration pursuant to the PPA so as to force the remaining DPC investors into accepting the Indian government’s preferred terms of settlement. More generally, there is scant evidence to suggest that the Indian government viewed the arbitral provisions as in anyway legitimate, i.e. authoritative. Thus, not only did the Indian government wantonly disregard specific rulings, but it did not even bother to mount a defence at the Bechtel initiated arbitration in Paris, the hearing being held in absentia as far the Indian government was concerned. Similarly, once OPIC had paid the claim, Indian government officials repeatedly affirmed that they did not intend to compensate OPIC pursuant to the subrogation provisions

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563 Sanjay Jog, *Financial Express* India, correspondent estimate (Interview Notes).
contained in the Investment Incentive Agreement (1997), as the claim payment was an affront to India’s sovereignty.

Moreover, from the perspective of the theory of legalized dispute resolution, it is striking that while the Indian legal team failed to prepare a coherent legal defence beyond vague and ultimately unsubstantiated assertions of malfeasance on the part of Enron, the DPC settlement terms were far more favourable to India than were the terms of settlement afforded Indonesia. The latter of whom could legitimately trace the abrogation of the contracts to events beyond their control so as to invoke the legal doctrine of *clausula rebus sic stantibus*.\(^{564}\) To this end, the dispute reveals not so much the ‘limitations of arbitration’ as it does the true character of the international law of foreign investment and the contemporary trend toward the juridification of investment dispute settlement.

It does so in the first instance because the empirical evidence makes clear that where prescribed judicial mechanisms of enforcement were felt by the U.S. not to serve its interests, then the U.S. government simply set aside the relevant international law norms. In particular, the extension of diplomatic protection of behalf of the DPC investors by the United States government was a violation of the international law principle of ‘corporate personality.’ The principle of corporate personality holds that only the investor’s home state is entitled (possesses *locus standi*) to extend diplomatic protection on behalf of foreign investors and this, in the first instance at least, is understood to be the state where the company is incorporated. That is, although there is no universally accepted legal rule in this regard (i.e. the principle has not been codified in the statutes of the International Court of Justice) it is generally accepted that the applicable legal norm, is derived from the *obiter dicta* of the Presiding Judge.

\(^{564}\) Although comparing the outcomes of different disputes is extremely difficult, that they were both IPP disputes is beneficial in this respect. That is, as a rule of thumb, remember that the standard calculation for a megawatt of power is approximately $1 million per megawatt. In return for $400 million, Indonesia received one 60 MW power plant, plus another less than a third complete, representing a cost of approximately $7.5 million per megawatt. The Indian government on the other hand got a 2,184 MW plant plus a re-gasification plant and port facility (all but complete) for approximately $3.7 billion, equivalent to $1.6 million per megawatt. Moreover, the technology used in Enron’s Dabhol ‘combined-cycle’ plant (meaning, it could run on two different fuel types – naphtha and LNG) was significantly more advanced and thus costly than the geothermal technology utilized by CalEnergy. Moreover, not only was the settlement amount different, but so too were the settlement terms, thus Indonesian debt was priced at Houston terms – approximately 6 percent per annum plus a three year holiday, whereas the applicable interest rate on Indian debt repayable to OPIC is just two percent per annum.
in the *Barcelona Traction Case* [1970] heard by the International Court of Justice (ICJ). Applying the principles of the judgement to the case at hand, the U.S. was not entitled to extend formal diplomatic protection on behalf of DPC investors, as DPC was actually incorporated in Mauritius for tax reasons, meaning that under international law the Mauritian government should have undertaken the task. Should it have been unsuccessful, then and only then was the U.S. entitled to become involved as the state where the majority of the shareholders permanently reside. While it could be argued that U.S. protection was just and proper, it should not detract from the fact that in taking such action, the U.S. was consciously disregarding public international law principles concerning diplomatic protection.

More fundamentally, however, concerns the fact that when it appeared that a legal impasse had been reached, the U.S. simply substituted customary international law rules and norms governing expropriation with U.S. statutes concerning expropriation. It did so, because in determining the validity of the expropriation claims made by G.E. and Bechtel (in the case against OPIC), which may be held as the primary determinant of the outcome of the dispute, the AAA tribunal by their own admission noted that their determination was guided by a combination of U.S. insurance contract law (Second Restatement) and the U.S. Foreign Assistance Act 1961 (Third Restatement, 1987), the latter of which lays out the U.S. interpretation of expropriation.

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565 *Obiter dicta* is a legal term that is used to refer to the comments or justifications using established legal principles forwarded by a court to justify its findings where a clear legal precedent is not available. And although not assigned the status of law, these judgements are often used to decide cases where primary legal rules are insufficient.

566 The case was heard by the International Court of Justice (I.C.J.). The court is widely acknowledged as the highest source of law derived from individual judicial determinations. The case involved a claim brought against the Spanish government by a foreign company operating in Spain. The company was incorporated in Belgium, but it was majority owned by Canadians, as it was a subsidiary of a publicly listed Canadian company. According to the *obiter dicta* of the presiding judge in the case, only Belgium had *locus standi* to bring claims against Spain on behalf of the company. If, having exhausted all available remedies the Belgian government was unable to obtain compensation then the rights would pass, and only then, to Canada. Further, the principle is further affirmed insofar as the applicable treaty governing the dispute is the India-Mauritius bilateral investment treaty (BIT), as the Investment Agreement which governs FDI disputes between the U.S. and India does not possess treaty status in public (state) international law, with the result that the India-Mauritius BIT takes precedent over the claims of OPIC under the Incentive Agreement. See M. Sornarajah, *The International Law on Foreign Investment* (2004), “Corporate nationality and the protection of shareholders”, p.228-233.

567 See G.E. Bechtel versus OPIC, AAA Award ‘Points of Law’ summary. See AAA p. 27, note 6. According to the findings published by the AAA the tribunal noted with respect to the exclusions under Sections 10.05/10.07 that because ‘the evidence was far from clear as to what claimants or OPIC understood the insertion of 10.05/10.07 to mean, the Panel has applied certain fundamental rules of
The problem with this from the standpoint of international law, and by implication for the efficacy of the theory of legalized dispute resolution, is that the ‘OPIC Contract is a substitute for international law, not a restatement of it.’\textsuperscript{568} That is, and to quote from Vance Koven, ‘OPIC should recognize that the Contract is primarily an instrument of United States investment and foreign policy and not an international legal document. Thus, international law is relevant to it only so far as it affects OPIC’s ability to pursue a subrogated claim against an expropriating foreign government. The reference to international law . . . should therefore be deleted as inconsistent with the philosophy and the purposes of the Contract and of OPIC coverage.’\textsuperscript{569}

In this manner, the OPIC contracts effectively provide the U.S. government, with a mechanism for extra-territoriality (the extra-territorial application of U.S. law), which is at odds with the foundational doctrines of public international law (law of states), and more broadly, the constitutive principle of the international state system—territorial sovereignty.\textsuperscript{570} It does so because OPIC’s claim payment effectively validated the AAA arbitral award—judicial process—wherein Indian civil law was replaced as the seat of jurisdiction contrary to the wishes of the government of India in favour of determination according to U.S. law in a manner that is akin to extra-territoriality in the enforcement of property rights. The capacity of the U.S. to act in insurance contract construction to 10.05/10.07 and its impact on the Contract,’ which reads that: ‘In the event of uncertainty or ambiguity, insurance contracts are generally interpreted and construed against the drafting party. Section 206 of the Restatement (Second) of Contracts confirms this position as does 83.27 of Couch on Insurance, which provides that ‘any ambiguity will be interpreted in favour of the insured and indemnity.’ Referring to the injunction issued by the Indian judiciary, the AAA determination went onto note that: ‘Section 261 of the Restatement (Second) of the Contracts provides, inter alia, that where a party’s performance is made impracticable by the occurrence of an event, the non-occurrence of which was a basic assumption on which the contract was made, the duty on that party to render said performance is discharged.’ See p. 28, note 7.

\textsuperscript{568} Vance R. Koven ‘Jurisprudence of OPIC’ 22 \textit{Harv. Int’l L.J.} (1981), p. 290, footnote no. 97. Koven’s findings concerning ‘OPIC’s Jurisprudence’ were echoed more than a decade later in 1991 by Pablo Zylberglati who also noted that despite pretensions to the contrary the OPIC contracts of insurance are not an international legal document, but instead exist to protect U.S. investors from the vagaries of international law, See Pablo M. Zylberglati, ‘OPIC’s investment insurance: the platypus of governmental programs and its jurisprudence’, \textit{Law and Policy in International Business}, 1993.


\textsuperscript{570} Furthermore, were there to be any doubt remaining as to whether such actions serve to derogate Indian sovereignty, it must surely be dispelled by the fact that upon hearing through a third party that the AAA tribunal was to be convened, Indian authorities then contacted OPIC and the U.S. Justice Department requesting that it be enjoined to the hearing, if only as an observer. Failing this it was requested that it be allowed to assist OPIC in preparing its case, through the provision of documents etc. The AAA tribunal rejected the pleas, however, declaring that India had no standing before the tribunal as it was not a party to the OPIC contracts of insurance, thereby forcing OPIC to decline the assistance offered it by the Indian government.
this way, and indeed India to frustrate arbitration, serves to underscore the continued primacy of state power and interests in determining the outcomes of disputes, and therefore the efficacy of institutional rules and norms governing disputes of this kind. Thus, to the extent that legal rules configured the final settlement of the Dabhol dispute, their effect was underpinned not by the normative authority embodied in international law but instead, the power and interests of states who undertake enforcement consistent with evolving conceptions of national interests, as is the focus of the second of the hypotheses to be examined.

In short, state power and interests were critical in enabling a compromise solution to be reached wherein the government of India arranged for the structured buyout of foreign investor interests in DPC. In this regard, it is important to note that the final settlement reflected not so much U.S. manipulation of the payoff matrix facing India, as was the case with Indonesia wherein naked-power was far more evident, so much as shifting perceptions of the value of bilateral economic and security relations as understood by both nations. That is, by mid-2005 neither the U.S. nor Indian governments perceived a further escalation of the dispute to be in their respective national interests as would have resulted had India chosen to exercise its rights pursuant to the investment incentive agreement (1997), providing for it to challenge the validity of the subrogated claim resulting from the six OPIC payments to DPC investors. That this is the case serves therefore to underscore the manner in which state power and interests continue to inform the settlement of international investment disputes, as while the legal ‘facts of the case’ had not changed, conceptions of state interests had so as to enable a final settlement to be reached pursuant to the OPIC engineered buyout.

Critical in this respect was the broader reappraisal by U.S. and Indian foreign policy makers of the importance of the bilateral security relationship between the two nations. Most immediately, this was evidenced by the public recognition by U.S. officials that India’s problems with Islamic militants across the disputed ‘line of control’ (Kashmir) provided both nations some common ground—‘the war on
terror’—as a basis to improve regional security cooperation.571 In this regard, evolving U.S. security interests in the region increasingly overlapped with those of India, driven by India’s desire to bolster international support for its counter-insurgency operations in Kashmir, as well as U.S. support for its bid to become a permanent member of the U.N. Security Council. Indeed, the signing of the Dabhol agreement appears to have been the conduit for a rash of bilateral security agreements between the two nations. This included, the signing on June 28th 2005 of the ‘U.S-India 10-year Defense Framework Agreement’ as well as the issuance of a ‘Joint Statement to Establish the U.S.-India Global Partnership’ on July 18th by President George W. Bush and Indian Prime Minister, Manmohan Singh, just ten days after the DPC buyout.572 To this end, Condoleezza Rice proclaimed ‘few tasks are more important than building the closest possible relationship between the U.S. and India’.

571 And although the policy reappraisal had begun before the terrorist attacks in New York, as evidenced by the partial lifting of economic sanctions against India by the U.S. in September 2000, as well as the signing of the ‘Next Steps in Strategic Partnerships’ between the Bush administration and the then Indian Prime Minister Vajpayee in early 2001, fears that Al-Qaeda had established links with the Muslim militant organizations in Kashmir provided added impetus to the policy shift. The earlier partial lifting of sanctions by President Clinton in 2000 removed 51 items from the banned list, thus restoring Indian eligibility for amongst other things loans and PRI from OPIC, support from its sister agency, EX-IM Bank as well as the U.S. Trade Development Agency (USTDA). Certain other sanctions concerning ‘dual-use’ items remained, however. The overarching aim, to strengthen ties whilst also denying India access to missile technologies that could be modified for use in Nuclear weapons. The sanctions had initially been imposed by the Clinton administration in May 1998, following five nuclear tests by India on May 11 and 13th 1998. The testing imperilled regional security relations, as evidenced by the tit-for-tat tests carried out by Pakistan two weeks after the Indian tests. In so doing, both sides contravened the Nuclear Test Ban Treaty, with the result that sanctions were imposed on both (neither India nor Pakistan has signed the Nuclear non-proliferation treaty). The thaw in relations was further evidenced by the fact that although sanctions against India were partially lifted, the same sanctions on Pakistan were not lifted until September 2001, as the U.S. sought to build Pakistani support for the invasion of Afghanistan which took place in October and November 2001. See on the lifting of sanction against India, ‘Clinton Lifts Sanctions India Welcomes Move’ Rediff on the Net. Moreover, U.S. support for Indian claims that Pakistan was harboring Islamic militant organizations was viewed as a means to increase the pressure on Pakistan’s powerful intelligence agency (ISI) to curtail such practices, See Tariq Rauf ‘United States Seeks Pakistan’s Assistance Centre for Non-Proliferation Studies, available online at http://cns.miis.edu/research/wtc01/pak.htm Date Accessed 13.10.05.

572 See for a full list of the bilateral agreements Congressional Research Service (CRS) ‘Report for Congress U.S-India Bilateral Agreements in 2005’, dated September 8, 2005, prepared by K. Alan Kronstadt, Analyst in Asian Affairs, Foreign Affairs, Defense and Trade Division. Note, as at the time of writing, however, the deal signed to provide nuclear technologies to India was held up in Congress following criticism by the influential House International Relations Committee (HIRC) of India’s relationship with Tehran and the potential that nuclear technologies could find their way to Iran. See Hearing of the House International Relations Committee, “U.S.-India Relations: A New Entente?” Sep. 8, 2005 see http://wwwc.house.gov/international_relations/fullhear.htm Date accessed 01.12.05. Later this was further supplemented in November 2005 by the signing of the U.S-India Cooperation Framework Agreement. The agreement formalizes the U.S. Trade and Development Agency’s (USTDA) program with public sector entities in India. See Press Release Embassy of the United States New Delhi, November 9th, 2005.
adding ‘that the U.S. welcomed India’s emergence as a global power with which it seeks a “growing strategic partnership.”’

In addition to shifting perceptions of the value of the bilateral security relationship, economic interests also appear to have been central in facilitating a negotiated solution to the Dabhol dispute. Indeed, the increased importance of India as an economic power appears to have been critical in the thoughts of the U.S. in reaching an agreement. Foremost in this respect for the U.S. were the prospects of further liberalization of key sectors of the Indian economy to foreign investors. And although speculation in the Indian media that the price demanded by Washington for its acceptance of the Indian government buyout and the gradual lifting of sanctions was the liberalization of financial services in India cannot be proven, it appears to have been prescient, judging by the timing of the subsequent announcement by the Indian government that it was lifting the ceiling for foreign ownership of Indian insurance companies from 24 to 49 percent on November 9th 2005, just months after the resolution of the dispute. Certainly, both G.E. and Bechtel in agreeing to the reduced purchase price for their equity stake to just $305 million (G.E. accepted $145 while Bechtel accepted $160 million) made public that their doing so was motivated

573 See ‘Bush-Manmohan Meeting will Strengthen US-Indo ties’ Available online at http://english.people.com.cn/20050718/eng20050718_196689.html Date Accessed, 08.12.05. It is by all accounts this concern that led to the U.S. policy reversal regarding the sale by Israel to India in 2003 (blocked by the U.S. since 1999) of Phalcon Radars to be used to establish an Airborne Warning and Control System (AWACS). The significance of the shift is attested to by the fact that the U.S. having agreed to permit Israel to sell AWACS to India immediately announced that it had reached an agreement that same month with Pakistan to provide India’s long-time rival with similar AWACS technology so as to maintain the military balance in the region, See ‘US to increase the number of F-16 back to original strength of 40’ South Asian Defence News, October 2003. http://www.pakistanidefence.com/news/MonthlyNewsArchive/2003/October2003.htm

574 Evidence of this is provided by way of the announcement shortly after the final settlement in December 2005 that the Indian government owned Air India had reached an agreement with U.S. aircraft manufacturer Boeing to purchase 68 long-range passenger jets, at a total cost of 38,000 crore, or approximately $8 billion, See The Hindu Times ‘Air India to buy 68 Boeing Aircraft’ Monday Dec. 26, 2005.

575 Evidence to support this assertion is provided by the timing of a report prepared by the Congressional Research Service in mid-2003 detailing the potential opportunities for U.S. companies in India. See Wayne Morrison and Alan Kronstadt (Foreign Affairs and Defense Trade Division) ‘CRS Special report for Congress: India-US Economic Relations’ Order Code RS21502, April 22nd, 2003.

576 See ‘Marketing Policy for Retail Sector Mooted’, The Hindu, Wednesday, Nov 30, 2005. According to which, ‘Under pressure from the US and other developed countries to throw open the retail space to FDI, the Government proposed the formulation of a marketing policy for the sector.’ To this end, it was widely reported in the Indian media that the U.S. government was acting under pressure from U.S. retail giants such as Wal-Mart, for whom collectively FDI opportunities in India were valued at an estimated $330 billion, based on CRS calculations.
by a desire to be able to continue to operate in India given the expanding commercial opportunities.577

Economic gains resulting from the final settlement were not, however, limited to the U.S. side. In particular, the final settlement paved the way for a resumption of high-technology imports, including the lifting of the U.S.’s decades old policy of denying India access to civilian nuclear technologies.578 And although such an assertion must remain conjecture, the settlement appears to have paid immediate dividends judging by the timing of the subsequent agreement between the U.S. and India on July 19th 2005, (eleven days after the resolution of the Dabhol dispute) on the first visit to Washington by the newly elected Indian Prime Minister Manmohan Singh to allow India access to civilian nuclear technologies.579 More generally, it was hoped that the resolution of the dispute would see private foreign infrastructure investors return to India, having been scared off by the Dabhol dispute and the perceived lack of regulatory independence.580

In this regard, it must be concluded that a final settlement offered both India and the U.S. sufficient prospective gains to enable any remaining hurdles to the final sale to be overcome. Once this was the case, making the necessary arrangements to facilitate the buyout was little more than a formality as the majority of the project debt was held by Indian government-owned financial institutions. Moreover, although the power produced by the DPC (now the Ratnagiri Gas and Power Private Ltd. Co) remains relatively expensive, there was never any suggestion that it was not urgently required

577 In this regard, G.E.’s conciliatory stance, evidenced by its acceptance of a lower valuation on its equity stake than Bechtel demanded, appears already to have paid dividends, as the company was awarded the main contract to restore the Dabhol plant to operating status as part of the final settlement. 578 The apparent U.S. policy shift in this regard should not, however, be viewed solely as a product of the resolution of the Dabhol dispute. In particular, the timing of the policy shift appears to have been connected to the decision by China to sell India civilian nuclear technologies (depending on the source, 5 or 6 nuclear reactors) in a reputed $10 billion deal. For a good overview of the issues involved See Esther Pan, ‘The U.S.-India Nuclear Deal, Council on Foreign Relations, January 25, 2006. http://www.cfr.org/publication/9663/usindia_nuclear_deal.html#8. Date Accessed 01.02.06. 579 See Dana Milbank and Dafna Linzer Staff Writers ‘U.S., India May Share Nuclear Technology: Bush Move to Reverse Policy on Civilian Aid Needs Hill Approval’, Washington Post Tuesday, July 19, 2005; Page A01. 580 On September 26th 2005, the Indian Minister of Finance, P. Chidambaram, on a scheduled five-day visit to Washington, and having met with World Bank Chief Paul Wolfowitz, U.S. Treasury Secretary John Snow and CEOs of major American companies announced in a press conference that India was seeking $150 billion of private infrastructure investment. See Embassy of India Press Release, Press Statement on visit of Indian Finance Minister Mr. P. Chidambaram, Washington DC, September 25, 2005.
given acute and recurrent power shortages in Maharashtra. The findings from the Dabhol case study serve therefore to underscore the continued import of state power and interests in resolving international investment disputes, albeit augmented by OPIC governance where U.S. infrastructure investors are concerned, i.e. the politics of dispute resolution and law making.

As a final comment before concluding, it is significant to note that the outcome reflected not only consideration of international politics but also domestic politics in both the U.S. and India. Thus, in the first instance, the willingness of the U.S. to compromise must be understood as driven in part by the political backlash against Enron in Washington following revelations of accounting scandals in late-2001. In particular, having been stung by criticism from Congress and the media concerning unusually close ties between the CEO of Enron, Ken Lay and the Vice-President, Dick Cheney, neither the White House, nor the State Department wished to be seen to be defending what amounted to narrow sectional interests over and above broader U.S. national interests vis-à-vis India. Thus, where in the six months prior to the beginning of 2002, Enron’s contractual rights were equated with the ‘sanctity of contract’ itself, leading to the unusual step of forming a ‘Dabhol Working Group’ within the NSC, and were aggressively pursued by among others the Secretary’s of State and Commerce and the Vice-President in their meetings with their Indian counterparts, after the company’s collapse the task of settling the dispute was, judging by the conspicuous lack of support afforded DPC investors, delegated to OPIC. Similarly, the settlement also owed something to domestic politics in India itself. Foremost in this regard concerns the unexpected victory of the Congress Party in the May 2004 national elections over the nationalist BJP, who had sought to link Dabhol to the specter of U.S. imperialism to enhance its own nationalist credentials in defence of Indian sovereignty.

581 In particular, industries in the state of Maharashtra had argued that they would be forced to move if the state and the Indian government could not guarantee them a reliable source of power. See Sumila Gulyani, Infrastructure and Industrial Performance in Developing Countries: The Automobile Industry in India, (Delhi: Palgrave Macmillan, 2001).
582 The Dabhol Working Group within the NSC was headed by then head of the NSC, Condoleezza Rice.
To conclude the Dabhol case study, the empirical evidence makes clear that the increased use of the BOOT investment vehicle serves to confer upon OPIC a central role in terms of rule enforcement and rule making with respect to international property and contract rights on behalf of U.S. infrastructure investors. Thus, not only did the contracts of insurance delimit the bargaining strategies employed by the DPC investors but OPIC itself fulfilled what amounted to the central diplomatic role in seeking a negotiated solution to the long-running dispute. More than this, however, in paying six separate claims to DPC investors, including both offshore lenders and the project sponsors (equity providers), OPIC’s actions served to frame the actions of the Indian authorities, including both the state and federal government’s as constituting a violation of the investor’s fundamental rights and thus of the international law of expropriation.

Although the claim payments did not create precedent, insofar as they were, broadly speaking, consistent with the applicable customary international law norms governing expropriation disputes, in agreeing to pay the claims OPIC’s actions, whether acknowledged as such or otherwise, serve to supplement the body of the customary international law of expropriation arising from breach of contract (investor-state) disputes. In particular, the payment of investor claims under the contracts of insurance once again serves to more firmly establish breach of contract by a sovereign contracting party as a political risk rather than a commercial risk, i.e. as a violation of international law requiring compensation. In this regard, while OPIC might officially claim that it merely enforces well established principles of international law, the evidence strongly suggests that OPIC was aware that its actions bear directly upon the body of case law when in paying the final three claims the agency declined to identify the ‘cause of loss’, noting only that ‘[W]ithout determining that expropriatory action had occurred, OPIC and the investor agreed on a negotiated sum in settlement of the claim, avoiding a contest over complex and ambiguous legal and factual issues.’

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583 See OPIC claims record, payments to Bechtel Indian Power Investment $9.95 million; G.E. EFS India Holdings $9.95 million and Offshore Power Production CV $400,000 (Enron subsidiary).
What is perhaps more significant here concerns not so much the specifics of OPIC’s claims determination so much as the manner in which the decision was reached. Specifically, denying a sovereign state the right to contest or even be a party to a judicial hearing (AAA arbitration) where the outcome of a hearing may, as it did in this case, result in the addition of sovereign debt obligations serves to frame the provision of investment insurance as a tool for extra-territorial enforcement. Put simply, this is nothing less than a derogation of India’s sovereignty. To this end, OPIC does more than simply regulate conflicting property norms and or modes of regulating private infrastructure (‘regulatory takings’) instead, the agency reaches inside of states to synchronize international property and contract rights on behalf of U.S. infrastructure investors as a supplement to the existing treaty framework governing direct investment between the two nations.

Moreover, whilst it is clear that the agency fulfilled its diplomatic function by enabling the U.S. government to take a back seat in the resolution of what was by any standard a politically contentious dispute, the capacity of OPIC insured investors to force the agency to pay their claims once again impeded U.S. foreign policy autonomy and threatened to derail not only the resolution process but for a short time diplomatic relations between the two countries. This being the case it is little wonder that OPIC felt compelled to challenge the jurisdictional competency of the specially convened tribunal to hear the case against it. At the same time, however, it is equally the case that this is not the first time that an insured investor has undertaken such action against OPIC, so as to frame the agency’s pleadings more as lip service to India rather than as a genuine challenge to the authority of the tribunal to hear the complaint against it. Ultimately, while OPIC’s motivations in this regard cannot be known for sure, what is clear is that the capacity of the agency and ultimately the U.S. to act in this manner must be understood in the final analysis as a product of power. Why? Because where the rules of the international institution were felt not to sufficiently protect the interests of DPC investors then the provisions of the contracts of insurance provide for the U.S. to sidestep the ambiguities of the international law of foreign investment and to substitute them with U.S. statutes concerning expropriation which apply a different conception of investor rights and duties.
In short, the outcome of the Dabhol dispute must be understood as a product of state power and interests separate from the applicability of specific legal rules and norms to the facts of the case. In this manner, the evidence from the Dabhol dispute makes clear that to the extent that the rules and norms governing dispute settlement are efficacious it is because states to choose to enforce them or otherwise consistent with evolving conceptions of national interests. That is, contrary to the postulates of the legalization hypothesis, enforcement is the key variable in generating distinct patterns of politics of dispute resolution, not as the theory holds delegation and its sub-variable access. And this is a product of the relative material capabilities of the states party to disputes of this kind. Indeed, the entire resolution process was characterized by the attitude that the applicable legal principles and case precedent, to the extent that either existed, were ultimately derivative of the sovereign rights of states and as such could be disregarded at will absent any justification from either state party.

In summary, the efficacy of legal rules to determine outcomes should in the final analysis be understood as a product of state power and interests, as it is power that determines which set of ‘rules’ are used to adjudicate disputes, including their scope and applicability to particular disputes (‘facts of the case’) and therefore their meaning so conceived. To this end, the expansion of Enron to India was foundered on state power because ultimately, and as the evidence has shown, it is states that structure the legal-institutional environment in which multinationals operate albeit where U.S. infrastructure investors are concerned a dual-layered state power comprised of OPIC governance backed by the U.S. government at the point of enforcement.

Before commencing part ‘B’ of the research, aimed at explaining shifts in the policy and practice of OPIC, it is useful to briefly consider the evidence with respect to the role of foreign investor (corporate) preferences in the formulation of U.S. anti-expropriation policy-making. In this regard, the evidence from the two case studies suggests that while the outcomes of the two disputes were ultimately consistent with U.S. investor interests insofar as compensation was paid, in both cases the U.S. government demonstrated a willingness to overlook specific corporate interests where the goals sought by state officials and insured investors collided. In particular, had CalEnergy’s Congressional representatives not weighed in on its behalf the
company’s claims under the contracts of insurance would likely not have been paid. Similarly, following the collapse of Enron, the U.S. government made clear that while it supported the claims of the remaining DPC investors in principle this did not extend as far as paying claims so as to endanger bilateral relations between the two nations. It is to the role of corporate preferences and state initiatives in determining shifts in the policy and practice of OPIC and thus U.S. foreign policy that the next chapter and the second part of the research is concerned. The investigation will begin with the transfer of the insurance program to the newly created OPIC in 1971 continuing through until 1980. While chapter six will examine the changes from 1981 through until 1994, wherein the decision was taken to expand the agency to facilitate its participation in BOOT based infrastructure investments.
Chapter 5: Establishment and Evolution of OPIC, 1969-1980

The aim of this chapter is to consider and explain the establishment and evolution of the OPIC administered investment insurance program from 1969 through until 1980. The period encompassed the agency’s initial establishment in January 1971, as well as the 1974 and 1978 statutory reauthorization hearings. Individually, each of the periods represents a small but significant turning point in the program’s history. In the initial instance the investment insurance program was transferred from the U.S. Agency for International Development (USAID) to the Overseas Private Investment Corporation (OPIC), operating as a wholly U.S. government-owned statutory corporation under the aegis of the Secretary of State (State Department). In the first reauthorization hearing, the very survival of the program was threatened as it became embroiled in wider issues centred on the impact of FDI on the U.S. economy, including the widening balance of payments deficit, U.S. output and employment, as well as U.S. bilateral relations with LDCs. Ultimately, the agency only survived a concerted attack, led by the influential Senate Subcommittee on Multinational Corporations, through a compromise deal providing for the privatization of the agency’s insurance portfolio, which had it occurred would have effectively terminated the program. The second reauthorization hearing in 1978 was no less eventful, resulting in the imposition of additional underwriting criteria, thereby, limiting OPIC insurance to low-income LDCs subject to ‘human rights’ guidelines as well as the abandonment of earlier proposals providing for the transfer of the program to the private sector.

In seeking to explain the establishment of OPIC and the program’s subsequent evolution, the investigation will be organized around the two competing hypotheses outlined: ‘corporate preferences’ and ‘state initiatives.’ To recap, the corporate preferences hypothesis holds that changes to the policy and practice of OPIC were the product of pressure from U.S. foreign investors aimed at strengthening emerging corporate strategies of adaptation in LDCs in response to weakened standards of investor protection up to and including the 1970s. In order to substantiate such an explanation the chapter seeks not only to identify instances of lobbying by U.S. foreign investors and representative organizations, but to identify linkages between specific policy proposals and policy outcomes. This includes, therefore, examination
of where specific proposals originated and the process wherein policy preferences were translated into actual amendments.

The second hypothesis centres on the role of state officials. The hypothesis contends that shifts in the direction of the OPIC administered insurance program cannot be understood as the product of domestic interest groups, including those of corporate America. That is, for proponents of the approach changes in the policy and practice of OPIC must be understood as but one element of the pursuit of the national interest wherein economic policy concerns are typically subordinated to the search for security in world politics, and state officials are held to possess autonomy from domestic interest groups in formulating U.S. foreign policy. Once again, in order to substantiate such an explanation the chapter seeks to link shifts in the OPIC program to broader economic and political foreign policy goals as articulated and pursued by state officials, comprised of the legislative branch (Congress in particular) as well as the executive, which taken together constitute the U.S. foreign policy bureaucracy.

The chapter will argue that the state initiatives hypothesis consistent with a realist notion of foreign policy-making provides the greater explanatory leverage of the two competing explanations. Foremost in terms of the weaknesses in the corporate preferences hypothesis concerns the fact that corporate America was, as far as the OPIC program was concerned, a divided constituency, invoking both support and opposition. It is not only with respect to the causal mechanism that the chapter’s findings diverge from those of Lipson, however. Foremost in this regard, concerns the characterization of the OPIC program as part of a coherent (indeed, the most coherent element) U.S. anti-expropriation policy. In particular, the chapter finds that there was no coherent U.S. anti-expropriation policy vis-à-vis LDCs. Instead, U.S. policy during this period is best understood as the product of ad hoc responses driven by a combination of bureaucratic politics and the exigencies of the bipolar world order.

More particularly, the chapter will argue that shifts in the OPIC suite of programs cohere, insofar as they were logically related to external policy goals, in the context of an incoherent foreign-aid program that itself cohered in the context of Cold War competition for influence in the developing world. To this end, the chapter finds that the U.S. pursued a consistent vision of the national interest in its relations with LDCs
through successive administrations spanning President’s Nixon to Carter, of which the investment insurance program was but one small part.

In order to consider the evidence, the chapter is organized as follows. The first task will be to detail discussions among the executive, including President Nixon, concerning proposals inherited by the newly installed administration to transfer the USAID administered insurance program to an independent statutory corporation, as would eventually pave the way for the establishment of OPIC in 1971. The discussions began as early as 1968, in the wake of Congress’s rejection of the former administration’s foreign-aid appropriations bill and just seven years after the then newly created umbrella agency USAID (1961) had itself been handed the task of administering the investment guaranty program. This has been done in order to provide the necessary background or rather political context to the subsequent Congressional debates (legislative branch) beginning in 1970 concerning the transfer of the program from USAID to OPIC, as well as the two subsequent reauthorization hearings as took place in 1974 and 1978. Both of which, as will become apparent were conducted in the shadow of broader policy debates occurring within the U.S. government concerning the need to reform foreign-aid spending, which was felt to deliver little given the significant expenditures involved.

Having established the background to the issue—the transfer of the USAID program to a newly created independent agency—the second task will then be to commence the investigation proper beginning in 1969 when the transfer of the program to a corporation was first mooted, through to 1980. In each instance, the basic policy issues that informed the three re-authorization hearings will be outlined, followed by an overview of the legislative history, including details of the supporters and opponents of particular amendments as well as Congressional and Senate voting records. Having outlined the changes that the chapter seeks to explain, the final task will be to consider the explanatory leverage of each of the two hypotheses, beginning with the capacity of U.S. foreign investors and corporate America more broadly to influence changes to OPIC, followed by an examination of the role of state officials, including both the executive and legislative branches.
That the question of the transfer of the program to a corporation was understood in the context of ongoing foreign-aid reform is evidenced in the first instance by the recommendation to the newly inaugurated President Nixon early in 1969 to make the ‘final decision’ regarding proposals to transfer the AID administered investment guarantee program to a corporation ‘in the context of your decisions on the aid program in general, following the overall review of aid policy now being prepared for the National Security Council.’\(^{584}\) Even before this, however, the original proposal to establish OPIC originated with President Johnson’s Perkins Commission on Development Assistance, whose recommendations were handed down in October, 1968.

In this regard, the establishment of OPIC was intended as part of a more fundamental overhaul of the foreign-aid program, central to which was the recommendation that AID be abolished and replaced with the Development Corporation Fund.\(^{585}\) The impetus for the review originated with Congress’s failure to pass the previous two Johnson administration’s foreign-aid appropriation bills, which had culminated in 1968 with appropriations of just $1.2 billion, a fifty percent reduction on what was requested.\(^{586}\) The tensions arose in the midst of growing budget constraints driven by Vietnam War spending as well as a more general dissatisfaction from within Congress with what was interpreted as State Department profligacy. In particular, it was felt

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\(^{584}\) 108. Memorandum From the Under Secretary of State (Richardson) to President Nixon/1/. Washington, March 25, 1969. /1/Source: National Archives, RG 59, S/S Files: Lot 73 D 288, NSC/Misc. No classification marking. SUBJECT Proposal for Corporation to Promote Private Investment in Developing Nations Note the referenced review of the foreign-aid program refers to the Peterson Taskforce on Foreign-aid Programs, established by Nixon to review proposals on this issue inherited from the Johnson appointed Perkins Commission on Foreign-aid, the findings of which were handed on to the new administration on the recommendation of the then ‘Special Advisor’ to the President, development economics pioneer, Walt Rostow.


\(^{586}\) 4. Action Memorandum from the Assistant Secretary of State for Economic Affairs (Greenwald) to Secretary of State Rogers/1/. Washington, March 25, 1969. /1/Source: National Archives, RG 59, S/S Files: Lot 80 D 212, NSSM 4. Confidential. Drafted by Thomas O. Enders (E/IMA) and cleared by Sisco (IO), Macomber (H), Barnett (EA), Dantzer (ARA, except for paragraph 6), Westerfield (AF), Clark (AID), and Poats (AID). The memorandum was also addressed to the Under Secretary. SUBJECT NSSM 4--Choices in Foreign-aid
that the State Department’s preferred strategy of spreading U.S. development spending thinly among LDCs rather than targeted programs aimed at a few larger strategic countries resulted in few benefits for the U.S. and left it open to ‘blackmail’ where expropriation disputes did arise.\textsuperscript{587}

In the end, the Perkins Commission’s recommendations were not adopted owing to the pending elections that resulted in the inauguration of President Nixon.\textsuperscript{588} Immediately upon being sworn in, Nixon established the Peterson Taskforce on International Development in anticipation of Congressional opposition to the administration’s first foreign-aid appropriations bill. The taskforce inherited the Perkins Commission proposals, including that recommending the establishment of OPIC. Apart from establishing a corporation to oversee the insurance program, the Taskforce also recommended the abolition of AID, the creation of a U.S. Development Corporation to administer development loans, and finally, the creation of a U.S. Development Institute responsible for administering technical assistance programs.\textsuperscript{589} The three new agencies, including OPIC that together were to constitute the U.S. foreign-aid program, were to be overseen by a newly created International Development Cooperation Agency reporting directly to the President.\textsuperscript{590} Finally, the

\textsuperscript{587} The negative opinion of the State Department’s approach was also shared by the new Nixon administration, including Nixon himself who in a specially convened meeting on foreign-aid in September, 1969 was on the record as stating, "The State Department wants to give aid to every country in the world and the result is lots of "Mickey Mouse programs." See 120. Memorandum of Conversation/1/. San Clemente, September 2, 1969, 11:45 a.m. /1/Source: National Archives, Nixon Presidential Materials, NSC Files, Box 1026, June to December 1969. Confidential. The meeting was held in the Western White House. According to the President's Daily Diary, the meeting lasted until 12:45 p.m. (Ibid. White House Central Files). SUBJECT President's Task Force on Foreign-aid.

\textsuperscript{588} The recommendations of the Commission were passed-on to the incoming Nixon administration, at the recommendation of the then President’s Special Advisor on Economic Development, Walt Rostow, in the knowledge that they would not appease Congressional opposition.

\textsuperscript{589} The decision to abolish AID as part of the restructure was universally agreed within the executive, including with support from both Kissinger and President Nixon, as the following transcript reveals: ‘Dr. Kissinger: We must abolish AID, whose personnel are simply too weak. (The President firmly agreed.). The President noted that he had always been a strong supporter of aid. One of his most frustrating experiences, in his numerous foreign travels, was to see how AID or its predecessors operate abroad. This is partly because they have always been on a temporary basis and therefore cannot get good people.’ See 125. Memorandum of Conversation/1/. Washington, February 11, 1970. /1/Source: National Archives, Nixon Presidential Materials, NSC Files, Box 1023. Nixon-Peterson, et al. 2/11/70. Confidential; Eyes Only. SUBJECT Status Report of Peterson Task Force on International Development.

\textsuperscript{590} See 124. Draft Summary of Korry Report on Foreign Assistance/1/. Washington, undated./1/Source: National Archives, Nixon Presidential Materials, NSC Files, Subject Files, Box 324, President's Foreign-aid Program. Confidential. Marked "Second Draft," the summary is attached to a December 9 memorandum from Bergsten to Kissinger (see Document 123) which identifies it as the second draft of

188
streamlining of the existing aid program was to be undertaken as part of wider reforms wherein the U.S. would where possible channel its development spending through the World Bank and other multilateral institutions, so as to in Kissinger’s words ‘take us out of the line of fire.’

Moreover, there was no real support within the executive for OPIC. Certainly, no one within the Nixon administration actually believed the official rationale underpinning the establishment of the agency. The tenor of the comments is captured by the then Secretary of Commerce, who stated ‘[M]y preliminary judgment is that there is scant evidence that the proposed corporation will help significantly to stimulate new private activity in the developing countries.’ To the same effect, Kissinger noted, ‘[S]uch a proposal is widely expected on the Hill and would reflect a decision to give greater emphasis to private sector participation in our aid effort. However, there is no assurance that it will, even over time, increase the flow of private resources or provide any other concrete benefits.’ The negative perception of the proposals voiced by Kissinger was subsequently echoed by the Secretary of Commerce who concluded, ‘[O]n balance and given the weight of other relevant considerations, I would not favor creation of a private enterprise corporation on the basis of the case made in the IPIAC proposal.’

the summary of Ambassador Korry’s report on foreign assistance undertaken at Under Secretary Richardson’s request pursuant to NSSM 45.

591 The decision to channel an increasing proportion of the aid budget through multilateral channels was driven by the assessment recorded at a specially convened meeting on foreign-aid wherein it was noted that ‘It is apparent that there is wide support in the country--and despite some reports to the contrary, in Congress--for increasing our emphasis on multilateralization of aid.’ 125. Memorandum of Conversation/1/. Washington, February 11, 1970. /1/Source: National Archives, Nixon Presidential Materials, NSC Files, Presidential/HAK Memcons, Box 1023, Nixon-Peterson, et al. 2/11/70. Confidential; Eyes Only. Drafted by Bergsten. According to the President’s Daily Diary, the meeting lasted from 10:07 to 10:55 a.m.; Fried is not listed as one of the attendees. (Ibid., White House Central Files). SUBJECT Status Report of Peterson Task Force on International Development.

592 107. Letter From Secretary of Commerce Stans to Secretary of State Rogers/1/. Washington, March 12, 1969. /1/Source: National Archives, RG 59, Central Files 1967-69, FN 6-1. No classification marking. Attached to an April 3 letter from Rogers to Stans stating that many of the Commerce Department's reactions were similar to those in the Department of State/AID analysis. Rogers enclosed a copy of Richardson's March 25 memorandum to the President and its attachments (Document 108).

593 5. Action Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon/1/. Washington, undated. /1/Source: National Security Council, Secretariat, Schedule of NSC Meetings, Box 83, 3/26/69 NSC Meeting-Foreign-aid. Confidential. This memorandum is the lead item in the President's briefing book for the March 26 NSC meeting. SUBJECT NSC Meeting on Foreign-aid/2/.

594 107. Letter From Secretary of Commerce Stans to Secretary of State Rogers/1/. Washington, March 12, 1969. /1/Source: National Archives, RG 59, Central Files 1967-69, FN 6-1. No classification marking. Attached to an April 3 letter from Rogers to Stans stating that many of the Commerce Department's reactions were similar to those in the Department of State/AID analysis. Rogers enclosed
Ultimately, however, the proposal to establish OPIC was accepted because it represented ‘something new’ in the appropriations package due for presentation to Congress, and this it was hoped would make it easier to ‘sell’.\textsuperscript{595} That this was the case is also supported by the comments of the Nixon’s National Security Advisor, Kissinger who in communicating the results of the NSC meeting convened to discuss ‘Foreign-Aid’ to President Nixon was on the record as recommending the President ‘[P]ropose such a corporation, essentially for cosmetic reasons.’\textsuperscript{596}

Indeed, the entire discussion was circumscribed by the issue of Congress’s rejection of previous foreign-aid packages, and the likelihood in Kissinger’s words that ‘almost any budget request you make (directed to President Nixon) will be emasculated.’ In short, he noted, ‘[T]he U.S. foreign aid program is in major crisis. The basic requirement is to reverse the sharply downward trend of appropriations for AID.’\textsuperscript{597}

To this end, President Nixon informed his Secretary of State that ‘[N]ewspaper accounts indicate that a number of Republican legislators are favorably inclined toward the proposal, and it thus seems likely that you will be asked to support it.’\textsuperscript{598} It

\textsuperscript{595} According to the minutes of the meeting, ‘Dr. Kissinger reaffirmed that this was a very imaginative approach. It was the only way to save foreign-aid.’ Similarly, Nixon himself weighed in at the same meeting and in referring to the creation of OPIC it was noted that, ‘The President agreed that the State Department should buy the approach. Otherwise foreign-aid is dead; he anticipated trouble this year even in getting modest appropriations.’ See 125. Memorandum of Conversation/1/. Washington, February 11, 1970. /1/Source: National Archives, Nixon Presidential Materials, NSC Files, Presidential/HAK Memcons, Box 1023, Nixon-Peterson, et al. 2/11/70. Confidential; Eyes Only. Drafted by Bergsten. According to the President's Daily Diary, the meeting lasted from 10:07 to 10:55 a.m.; Fried is not listed as one of the attendees. (Ibid., White House Central Files). SUBJECT Status Report of Peterson Task Force on International Development.

\textsuperscript{596} 5. Action Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon/1/. Washington, undated. /1/Source: National Security Council, Secretariat, Schedule of NSC Meetings, Box 83, 3/26/69 NSC Meeting-Foreign-aid. Confidential. This memorandum is the lead item in the President's briefing book for the March 26 NSC meeting. SUBJECT NSC Meeting on Foreign-aid/2/. Italics added.

\textsuperscript{597} 5. Action Memorandum From the President's Assistant for National Security Affairs (Kissinger) to President Nixon/1/. Washington, undated. /1/Source: National Security Council, Secretariat, Schedule of NSC Meetings, Box 83, 3/26/69 NSC Meeting-Foreign-aid. Confidential. This memorandum is the lead item in the President's briefing book for the March 26 NSC meeting. SUBJECT NSC Meeting on Foreign-aid/2/.

\textsuperscript{598} 106. Memorandum from President Nixon to Secretary of State Rogers/1/. Washington, February 13, 1969. /1/Source: National Archives, RG 59, S/S Files: Lot 73 D 288, NSC/Misc. No classification
is with this less than ringing endorsement of the investment insurance program that the decision was taken by the newly elected Nixon administration to formally propose the establishment of OPIC in his 1969 foreign-aid address to Congress.

The Establishment of OPIC, 1969-1971

Although, and as has been noted, formal discussions concerning the proposed transfer of the investment guaranty program from USAID to a new corporation operating as an independent agency began in 1968, the concept of a federally chartered corporation to promote FDI through the provision of insurance had a much longer lineage having been first proposed as early as 1950, in a document entitled the ‘Peace by Investment Corporation’. However, it was not until the late 1960s that the proposal gained currency among U.S. policy-makers. The second separate channels can be identified. The first originated with the establishment of an AID permanent advisory committee, the International Private Investment Advisory Council (IPIAC) consisting of six representatives from business and banking. The second track originated with the findings of the Subcommittee on Foreign Economic Policy of the House Committee on Foreign Affairs, who in 1968 held hearings into the involvement of U.S. business in LDCs.

The subsequent report cautiously endorsed Senator Javit’s earlier proposal, with the proviso that the corporation would have to be reviewed ‘in terms of general U.S. foreign policy commitments and with development programs.’ The IPIAC issued its report in December 1968, entitled, ‘The Case for a U.S. Overseas Private Enterprise Development Corporation.’ The report recommended among other things, ‘the organization of an overseas private enterprise development corporation’ so as to ‘further the economic and foreign policy interests of the U.S.’

According to the statement of policy and purpose, OPIC was to conduct ‘investment financing on a financially self-sustaining basis; utilize private sources of financing as the principal means of encouraging investment; increase private participation by selling its direct investments to private investors; apply risk management principles in issuance of insurance; utilize and encourage participation of small business in OPIC programs; support investments in less developed friendly countries that contribute to their economic and social development; take into account the receptivity of LDC governments to private enterprise, encourage private initiative and competition and discourage monopolies, and consider the balance of payments effects of OPIC’s activities.’

The proposals were submitted to the House by New York Congressman Leonard Farbstein, and were then submitted to the Subcommittee on Foreign Economic Policy of the House Committee on Foreign Affairs. In considering the proposals, testimony was heard from a variety of sources, including both opponents and supporters of the plan. Among the latter group was a significant number of business organizations and peak bodies, prominent among which were: the National Foreign Trade Council; the U.S. Chamber of Commerce; the Council for International Chambers of Commerce; the National Association of Manufacturers (NAM); the Committee for Economic Development (CED), as well as a number of prominent banking bodies and personalities, headed by August Maffry, acting as senior consultant for the Bank of America.

The bill, introduced as part of the Foreign Assistance Act (1969) was the subject of relatively little floor debate. The main difference between the new corporation and its predecessor being that OPIC was to be self-funding in the long-term, thereby sidestepping potential opposition in Congress. Despite this, a number of reservations were expressed in the House, centred on the issue of whether the new corporate form would diminish Congressional control of the program. Ultimately, however,

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supporters of the proposed corporation won the day with just two amendments to the original bill being proposed. First, not more than 10 percent of total guarantees could be issued to any single investor. Second, the new agency was prohibited from making loans to finance mining operations or other extractive industries. The aim, in the latter instance, to minimize political involvement of the U.S. government in expropriation disputes. On November 20th 1969, the House passed the bill 176 to 163, whilst noting several reservations.

The passage of the bill through the Senate was not so easy. When first introduced the foreign-aid bill did not contain the provision for the establishment of OPIC. Moreover, on a tie vote, the Senate opted not to hold hearings on OPIC until such time that the newly established Peterson Taskforce on foreign-aid had finished its evaluation of the entire USAID program. Despite the initial resistance to the creation of a government corporation to administer the program, the main supporter of the bill, Senator Jacob Javits pressed ahead regardless, using his position on the Senate Foreign Relations Committee to introduce the Bill to the Senate Floor. He argued that a corporation had several advantages over the existing AID-administered program. Foremost in this regard, was the fact that as a corporation it would be exempt from civil-service hiring requirements, thereby providing it with an enhanced capacity to attract business leaders, as well as providing the agency with added administrative and financial flexibility. The primary opponent of the bill was Senator Fulbright, who although not opposed to the bill in principle felt that it should first be considered by a Senate committee before a vote was held on the floor. Despite this opposition, the Javits amendment passed the Senate, by a vote of 53-34 on December 12th, 1969. On the same day, the Senate passed the Bill containing the OPIC provision, 52-31, thereby, paving the way for the establishment of OPIC, by way of an amendment to the Foreign Assistance Act (1961).

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The main provisions of the amendment as they related to the administrative changes were as follows: OPIC was to be a U.S. government owned corporation, operating under the policy guidance of the Secretary of State. Under the statute, OPIC was permitted to issue investment insurance (renamed from the AID guarantees), and provide insurance against the following risks: expropriation, nationalization, confiscation, currency inconvertibility, war, revolution, insurrection, riots and civil strife. The extended guarantee program was also transferred, enabling OPIC to provide 100 percent cover for loans and up to 75 percent of equity investments, as well as the right to make loans in U.S. dollars and or local currency. The new agency’s capital stock, held by U.S. Treasury totalled $40 million as at January 1971. An eleven-member board was appointed, the majority of who were to be drawn from the private sector, and appointed for three years terms by the President. Of the six non-government directors, at least one was to be drawn from small business while one other was to be experienced in operating cooperatives. Among the minority, one member was appointed from AID, who was to be ex-officio Chairman, while OPIC’s President was to be appointed by the Senate, with the remaining three government members being appointed by the President.612

OPIC inherited all of AID’s outstanding liabilities totalling more than $10 billion, including approximately $3 billion for each of the three main risks, currency inconvertibility, war, and expropriation. AID’s statutory reserves totalling just $27.9 million were also transferred.613 In addition, the agency received Congressional appropriations for fiscal year 1971 of $54.9 million. Under the terms of its incorporation, OPIC was authorized to issue insurance to a maximum contingent liability of $7.5 billion, plus a further $750 million for the extended risk-guarantee program. Further, no loans could be made for investments in mineral exploration or ore mining. Finally, OPIC was to give priority to projects that were sensitive to the development needs of LDCs, specifically those projects that contributed to their ‘economic and social wellbeing’.

The key differences between the AID program and the OPIC administered insurance program were the following: OPIC, due to its corporate form, was permitted greater flexibility in setting premiums, so as to make them responsive to the broader goal of moving towards financial self-sustainability. Second, the agency was permitted to actively seek out new business, and design new products to be responsive to the needs of private investors. Foremost in this regard concerned the fact that OPIC could insure U.S. investors in joint ventures, licensing-agreements and management-contracts, as well as in wholly owned subsidiaries. Further, unlike its predecessor, OPIC was to play an active role in dispute resolution. Finally, in accord with the original IPIAC proposals, the agency was restricted from issuing more than ten percent of total insurance to any single investor or country, in order to protect against losses that might result in its being required to ask for further funding from Treasury which would have exposed an unusually close relationship between the U.S. government and multinational capital. Finally, after more than two years of discussion, OPIC commenced operations in January 1971.

*OPIC’s Formative Years: Reauthorization and Amendments, 1974*

If OPIC’s establishment had been easy, the 1974 reauthorization hearings were anything but as the question of the agency’s continued operation became entangled with broader and indeed, more divisive debates within the U.S. polity concerning the impact of multinational investment on U.S. employment and the balance of payments deficit, which peaked in 1972 at a record $6 billion. More narrowly, the agency was facing claims many times greater than its reserves, arising from the expropriation of U.S. investor property in Chile in 1971. 614 The problem facing OPIC and recognized by legislators was that if the agency paid the outstanding claims if would be forced to request additional funds from Treasury to finance the payments. More generally, the agency faced criticism, due to the geographic and sectoral concentration of its insurance program. For example, and contrary to the original developmental goals, 614 A Government Accountability Office audit estimated OPIC’s liability to AID issued Chilean contracts at $369.5 million as at April 1973, against reserves of just $85 million. The contrast with the record of AID with respect to claims payments was stark. Between 1948-1971 AID had paid just eleven claims from a total of 21, totalling $5.2 million. Of the eleven claims, five were for Currency Inconvertibility (5 of 10), 2 for expropriation (2 of 6), and 4 for war risks (4 of 5 claims paid). Expressed differently, AID had paid claims totalling just 4 percent of premium income received
fully eighty percent of OPIC insurance went to just eight middle and upper-income LDCs, more than half of which was concentrated in just three countries, Brazil, Indonesia, and South Korea.  

Given the wide-ranging criticisms of the program, scheduled hearings began in 1973 some twelve months prior to the formal reauthorization date. Two Subcommittees considered the issues. The first, the Subcommittee on Multinational Corporations, of the Senate Foreign Relations Committee, although not intended to review OPIC per se, used its Congressional mandate to investigate MNCs as a pretext to review the OPIC program. Moreover, the Subcommittee’s self-imposed remit was far broader than that of the House Committee’s, seeking among other things to answer the following questions: would the investments have been made absent OPIC coverage, and if not should the coverage have been offered, i.e. did the program encourage investments that were not commercially sound? Second, to what extent had OPIC fulfilled its mandate, to de-politicize investment disputes? The Subcommittee on Foreign Economic Policy and Trade of the House International Relations Committee was, however, immediately more sympathetic to OPIC, commissioning a Congressional Research Service study of the issues at hand.

The Congressional Research Service report published in September 1973 noted, judging by the amount of insurance issued by OPIC, the agency had been less successful than its predecessor but in its favour found that it was hampered by a dual-mandate according to which OPIC must be self-funding whilst the same time being mindful of the impact of insured investments on host country development. This tension was further exacerbated, the report noted, by the imposition the previous year of new underwriting criteria according to which OPIC was to calculate the impact on the U.S. balance of payments before issuing insurance. However, the Congress

616 The Subcommittee was established to investigate U.S. oil companies. Specifically, allegations that their actions increased the likelihood of U.S. government involvement in sensitive expropriation disputes at the expense of U.S. interests more broadly. In this regard, the posture of the Subcommittee was openly hostile to the oil companies, which were widely seen as having colluded in the OPEC oil price rises earlier that year in order to boost profits and influence with Middle-Eastern producers.
617 Three criteria were laid down: 1) the likelihood of a non-U.S. investor making the investment, the possibility that present U.S. exports might be displaced by the output of the project, and the essentiality of the investment in order to maintain U.S. presence in the market/sector in questions; 2) analysis of the
commissioned report did note that OPIC had been successful in resolving investment disputes before claims arose in more than 60 percent of cases.\textsuperscript{618}

The Senate Subcommittee investigating OPIC was much more critical, and according to critics biased, citing the testimonies heard by the committee. Foremost in this regard, concerned the strident criticism of the program from organized labour, which curiously had played little part in the original hearings from 1969-71. Testimony was heard from the Head of the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO).\textsuperscript{619} The AFL-CIO argued that the program promoted ‘runaway industries’ which reduced U.S. employment and unfairly subsidized foreign competition with U.S. based production.\textsuperscript{620} Negative testimony was also heard from Vincent de Roulet, the U.S. Ambassador to Jamaica, who expressed concerns that the $500 million of investments insured by OPIC in Jamaica served to transform what should have been normal business decisions into major political issues between the United States and Jamaica.\textsuperscript{621} That is, American companies attempted to use the investment insurance program to promote ‘an identity of interest between the U.S. Government and the corporations’ thereby adding to the complexity of bilateral relations between the two countries.\textsuperscript{622} Concern was also expressed that by insuring IT&T in Chile, ($95 million), the U.S. government effectively gave \textit{de facto} support to the company’s meddling in Chilean elections.\textsuperscript{623}

\begin{footnotesize}
\begin{enumerate}
\item short-term import-export effects, and 3) estimate of cumulative financial flows resulting from the capital investment weighted against financial returns. Every project must meet all three criteria.\textsuperscript{618}
\item See \url{www.afl-cio.org} Date Accessed: 01.02.05. See e.g. Senate OPIC Hearings, supra note 47, at 265-66 (testimony of Benjamin Sharman); 129 Cong. Rec. 4093 1974 (letter from Andrew J. Biemiller). The AFL-CIO is a voluntary federation of 56 national and international labour unions, who in 1973 represented 13 million workers in the United States.
\item Senate OPIC Report, \textit{supra} note 45, at 24.
\item Joseph Griffin, ‘Transfer of OPIC’s Investment Insurance Programs \textit{Law and Policy in International Business}, 8: 631-56. (1976), p. 638, \textit{Id}. At 25. Griffin acknowledges that the claims were not without foundation. The criticism reflected the fact that IT&T Chile had attempted to influence the outcome of the 1973 Chilean elections by providing financial support to opponents of then Chilean President, Salvador Allende (socialist), resulting in a \textit{coup d'état} that brought General Augusto Pinochet to power.
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The Senate Subcommittee report was highly critical of OPIC, noting that since the agency’s creation more than 79 percent of all investment insurance measured by dollar volume went to companies in the Fortune 500 list of corporations and commercial banks. Senator Church charged that OPIC’s investment insurance programs are administered primarily for the benefit of those least in need of the programs, i.e. large multinational enterprises. Furthermore, he argued, ‘OPIC guarantees actually encourage equity investments, where the American interest takes the conspicuous form of outright ownership, which then has the effect of acting as an incitement to the local populace to look upon the foreign owners of their resources with envy and anger.’ Second, the Subcommittee noted that ‘because the full faith and credit of the United States’ stands behind OPIC, political complications and involvement in host country politics are inherent in the nature of the program. Moreover, U.S. Government sponsorship of the investment insurance program:

[M]ay lull the companies into a false sense of security and induce them not to make the necessary adjustments to changing local conditions when a healthy relationship between host country and companies would require it. Moreover it is the belief of the Committee the government insurance may at times increase the likelihood of expropriation. Expropriation is viewed by some radical governments as striking a blow at the United States government.

Relying on the conclusions of the MNC Subcommittee, the Senate Committee majority argued that at best OPIC contributed only marginally to U.S. development objectives and that it actually increased the likelihood of government-to-government confrontation. Rather than kill the program, however, the majority voted to report a bill extending OPIC’s authority but providing for transfer of OPIC’s insurance program to the private sector over a five year period and establishing flexible interim

627 OPIC Senate Report Id. At 26. The Senate Report cited three particular examples, Jamaica, Taiwan and Chile, where in the Committee’s opinion OPIC’s exposure to large financial losses due to expropriation coverage had a substantial and detrimental effect on United States foreign policy. See Joseph Griffin, ‘Transfer of OPIC’s Investment Insurance Programs’ Law and Policy in International Business, 8: 631-56. (1976), p. 637, Id. At 20.
goals regarding the percentage of private insurance participation OPIC must achieve by certain dates.\textsuperscript{628}

The House Subcommittee disagreed with these Senate criticisms. It found that OPIC avoids governmental confrontations by maintaining a low, non-official profile during the negotiation of investments disputes and by ‘keeping the investor out in front.’ ‘It was also noted that those investors not insured by OPIC had often sought to involve the State Department in their investment disputes by seeking application of the Hickenlooper and Gonzales Amendments, as well as seeking other methods of official U.S. governmental assistance in resolving the dispute.’\textsuperscript{629} The House committee also found, in contradistinction to the Senate subcommittee findings, OPIC’s existing policy guidelines disfavored support to runaway industries and that the Government Accountability Office and Congressional Research Service studies of OPIC had concluded that the existing procedures, ‘if properly implemented should provide reasonable assurance that U.S. economic interests are protected.’\textsuperscript{630}

Fortunately, for supporters of OPIC, a minority of the Senate Foreign Relations Committee vigorously disputed the majority’s conclusions. A floor-fight ensued, resulting in the Committee minority carrying the day, by just two votes. A compromise bill thus passed the Senate. In the House of Representatives, the report of the Committee on Foreign Affairs generally followed the minority position in the Senate. The House agreed to the Senate compromise and passed the bill providing for the continuation of OPIC until 1977, under certain conditions. In the final analysis, however, the 1974 Amendments were closer in spirit to the findings of the House Subcommittee than the Senate Committee Report.\textsuperscript{631} In this respect, both supporters and opponents of OPIC proclaimed the outcome as a victory.


\textsuperscript{629} The Hickenlooper Amendment passed in 1963 provided for the suspension of U.S. foreign-aid to countries found to have expropriated U.S. property absent the payment of compensation.


Among the key amendments, included among which was the reauthorization of the agency through until 1977, were the following: first, OPIC was to transfer all of its insurance operations to the private sector by December 1980, second, the agency was to conduct its operations on a self-sustaining basis, and third, OPIC was instructed to achieve private reinsurance equal to 25 percent of its exposures for inconvertibility and expropriation risks for contracts issued after 1975, and at least 50 percent for contracts issued after 1978. The quotas were not mandatory however. The legislation also mandated that the insured bear at least ten percent of loss, thereby limiting coverage to 90 percent of the investment. OPIC’s guidelines on runaway plants were codified, and OPIC was required to submit an evaluation within six months of the possibility of requiring investor’s to complete and satisfy environmental guidelines for projects insured by the agency. Finally, the suggestion that OPIC should charge different rates for different countries was rejected as politically unworkable.

**OPIC Re-authorization and Amendments, 1978**

Five issues dominated the 1978 OPIC reauthorization hearings. As was the case in 1974, hearings had begun more than a year prior to the formal reauthorization date in anticipation of a tough floor-fight. In addition, although the proposed legislation met with considerable opposition from a variety of labour representatives and human rights groups, the critical difference this time around was that the future of the program was not the issue at stake. Instead, the focus had in the intervening period shifted to how best to improve coverage for U.S. investors, and refocus the program towards its original development goals. The shift reflected the fact that where in 1974 the central issue was the impact of OPIC on the U.S. Treasury and diplomatic relations with LDCs, the central issue in 1978 was the deteriorating U.S. trade position, evidenced by several high profile closures of steel and electronics plants.

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633 The finding reflected the belief that differential premiums could be interpreted as a negative comment on national economic policies, thereby, in the case of high-cost and presumably high-risk countries, discouraging investors as well as damaging bilateral relations with the country in question.
The second factor underpinning the shift in emphasis was the successful conclusion of the Chilean claims absent the need for additional funds from Treasury.635

While the future of OPIC was no longer in doubt there were, however, several other high profile issues facing the agency. Critical in this regard, was the apparent failure of the proposed privatization of OPIC, owing to lack of interest from private insurers.636 The second issue of note concerned how to reorient the program in accord with President Carter’s ‘New Directions’ program aimed at reinvigorating the economies of the non-oil exporting LDCs (the fourth-world). The other issue of the day concerned ‘Energy policy’ following the dramatic oil price hikes in 1973-74. In order to review these issues, President Carter appointed a Cabinet-level Economic Policy Group soon after his appointment in 1977. The Group’s conclusions augured well for OPIC, with the published report noting that the agency could make a significant contribution to the goals of U.S. foreign economic policy.637

As was the case in 1974, the principal forums for debate were the House International Relations Committee (Subcommittee on International Economic Policy and Trade) and the Senate Foreign Relations Committee (Subcommittee on Foreign Assistance). Hearings were held before the House Subcommittee between June and September, while in the Senate, hearings were heard in July and August 1977. The principal supporter in the Senate was Senator Javits, while opposition was led by long-time supporters...

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635 OPIC managed to cover its position through a variety of innovative credit arrangements. Its main tactic was to negotiate compensation agreements with the Chilean junta. The junta headed by General August Pinochet agreed to pay compensation and issued bonds to raise the capital to do so. The bonds were in turn guaranteed by OPIC. The insured corporation was given the bonds, which it could hold or could sell for cash – discounted plus a cash payment from OPIC. This arrangement saved OPIC’s reserve position but left the agency with substantial long term liabilities owed by foreign governments. As of April 1977, OPIC had paid or guaranteed more than $246 million to investors in over sixty claims. Some $96 million was paid in cash, the rest was in guaranteed bonds. As disputes were settled and bonds repaid about one-third of that money was recovered. But as of April, 1977 OPIC was still liable for $111 million in foreign government bonds, while its reserves amounted to $210 million. The arrangements would serve as the model for future claims wherein the host state would issues bonds, guaranteed by OPIC. These bonds would then be held by OPIC or alternately OPIC could sell the bonds on the open market at a discount, in order to offset losses from the payment of claims.

636 A Government Accountability Office report was highly critical of the privatization plans, noting that privatization would burden OPIC with high-risk investments. Moreover, any insurance sold to the private sector would have to be at a discount because no private insurer could replicate OPIC’s deterrence function, nor its successful record in mediating disputes.

OPIC opponent Frank Church as well as Senator Case. In terms of testimony heard, the principal supporters of OPIC were the U.S. Chamber of Commerce, the National Association of Manufacturers, the Emergency Committee for American Trade, the Associated General Contractors of America, American Agribusiness Associates, the League of Women Voters, the American Bar Association and the Association of the American Chamber of Commerce in Latin America.

The principal opponents were the AFL-CIO, Americans for Democratic Action (comprised of several human rights organizations), and the Centre for International Policy. The director of the Centre for International Policy, William Goodfellow, expressed the views of organized labour and the human rights groups, when he argued that the primary beneficiaries of OPIC coverage were six middle-income LDCs that violated human rights and attracted FDI because they did not enforce labour standards and persecuted labour unions. George Chauncey, Chairman of the Inter-religious Taskforce on U.S. Food Policy, subsequently echoed these views.

In light of the previous hearings, it was expected that any opposition would occur in the Senate. However, this was avoided as the conclusions of the Cabinet Economic Policy Group were endorsed by the Senate Foreign Relations Committee, with the result that the administrative bill passed with little opposition, by a vote of 69-12.

In particular, the Senate Committee noted, contrary to the 1974 committee findings, OPIC’s insurance did not increase the likelihood of government-to-government confrontation arising from investment disputes. The easy passage in the Senate stood in contrast to the opposition faced in the House, where a floor-fight ensued, owing to

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640 Franklin and West, ‘The Overseas Private Investment Corporation Act of 1979’, 14 *TEX. INT’L L.J.*, 2, p. n.a., footnote, 41. Testimony was also heard from academic experts, including J. Kenneth Fasick, director of the international Division of the GAO, C. Fred Bergsten, Assistant Secretary, Treasury, International Affairs Division; former OPIC president Marshall T. Mays; former Secretary of State, Henry A. Kissinger, Stephen J. Kobrin, Assist. Prof. Sloan School of Management (MIT), and Joseph P. Griffin, Chairman of the Committee on Overseas Insurance Investment of the International Law Section of the American Bar Association.
the success of what the President of OPIC referred to as the AFL-CIO’s ‘guilt by association attacks.’

Opposition to the bill resulted in the addition of several new amendments not included in the Senate bill. Of these, one would be enacted, while another was ultimately repealed. The first, later repealed, placed mandatory restrictions on OPIC’s portfolio to ensure that a minimum of 50 percent was directed to small and medium-sized business. The restrictions, would, it was argued, have killed OPIC as was intended. Eventually, the 50 percent mandatory target was watered down to a 30 percent voluntary target. Opponents of the amendment did not give in easily, however, fighting the proposals in the Committee stage and on the House floor.

Ultimately, despite arguments from the executive to the effect that such restrictions would hamper the agency’s capacity to support U.S. investors versus their European and Japanese counterparts, the restrictions were only defeated after a compromise deal was reached with agricultural-interests in the House. Under the terms of the deal, agricultural-interests in the House agreed to vote against the imposition of the mandatory small business amendment so long as new restrictions were placed on the program preventing OPIC from supporting any project to establish or expand the production or processing of palm oil, sugar, or citrus for export to the United States. Despite the last minute horse-trading, the amendments were the subject of three days of intensive debate in the House, before being passed on a vote of 216-185. Once again, supporters and opponents of OPIC were able to claim victory. Supporters, because OPIC had been reauthorized, and the proposed mandatory restrictions had been defeated in favour of retaining OPIC discretion. Opponents, on

642 OPIC President, Rutherford Poats testified that ‘the issue before the House is not the broad strategy or theory of international economic development. OPIC is the issue and OPIC does not rely on general theories contending U.S. private investment is either good or bad for the US economy.’ See Franklin and West, ‘The Overseas Private Investment Corporation Act of 1979’, 14 TEX. INT’L L.J., 2, p. n.a., p. 31-32.

643 The definition utilized was any business not in the Fortune 1000 list of top American companies.


645 According to Footnote, no. 119, ‘In the midst of the House Debate on the 1978 OPIC Amendments, OPIC and the Department of Agriculture announced a joint program to increase the demand for feed grains and other United States farm commodities in LDCs. Essentially, OPIC would assist United States agribusiness companies and cooperatives . . . the ‘announcement was received well by agricultural interest groups.’ (See Statement of John Cavanaugh, OPIC and US Agriculture (124 CONG. REC. H1453 daily ed. Feb 23, 1978).
the other hand, were also satisfied as the restrictions on OPIC insurance for ‘runaway’ plants were strengthened, and its programs were modified to ensure the agency further boosted support for projects in low-income developing countries consistent with its original development goals, and restricted support for projects in countries that consistently violated human rights.

Among the key amendments were the following first, the 1974 amendments under which OPIC was to transfer its insurance business to the private sector were repealed. Second, OPIC was to give preferential consideration to projects in countries with a per capita income of $520 or less (1975 dollars) and to restrict assistance with respect to projects in upper-income LDCs having a per capita income of $1,000 or more.646 The third amendment concerned the lifting of restrictions placed on OPIC in 1974, barring the agency from supporting mineral and resource extraction projects. The fourth amendment concerned the imposition of ‘Additional Statutory Prerequisites and Restrictions Applicable to OPIC Insurance.’ Central in this regard, was the amendment under which OPIC was required to terminate its programs in countries whose government follows a consistent pattern of gross violations of human rights, except for projects benefiting the needy people, and subject to national security exemptions. To this end, Franklin and West cogently write of the 1978 amendments that the result was that, ‘both the Executive Branch and Congressional leadership appeared to be willing to accept a distinction between the public policy implications of encouraging private investment in LDCs for developmental reasons and simply encouraging United States exports.’647

OPIC Policy Amendments: State Initiatives versus Corporate Preferences

Thus far, the chapter has detailed the form of the amendments to the OPIC suite of programs as well as their legislative history through until 1980. Clearly, the period was a tumultuous one for the program, its fortunes seemingly indistinguishable from broader political and economic debates within the U.S polity. And although the focus

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646 Theodor Meron, ‘OPIC Investment is Alive and Well,’ American Journal of International Law 73 (January, 1979), 104-111.
of the debates naturally shifted concomitant with shifts in the focus of the broader policy debates, the question of whether such overt government support for private multinational capital accumulation was appropriate remained unresolved, hence the continued imposition of a dual and necessarily conflicting policy mandate.

Having detailed the changes to the OPIC program, this next section by contrast is concerned to explain the direction of the observed policy shifts. In so doing, the analysis will consider the explanatory leverage of the two competing hypotheses forwarded by scholars. The first explanation to be examined concerns corporate preferences, beginning with the decision to transfer the program from USAID to OPIC, circa 1969.

The decision to transfer the AID administered investment-guaranty program to a newly established corporation originated from the recommendations of the IPIAC and later President Johnson’s Perkins Commission on foreign-aid, both of which were chaired by and comprised of representatives from the private sector. Moreover, it is clear that as U.S. foreign investors began to adapt to the changing environment in LDCs through various strategies aimed at lowering the profile of investments they, in turn, supported moves to establish the new program as a corporation in the hope of depoliticizing expropriation disputes.648

Equally, to substantiate the claim that that the program’s evolution is explainable by corporate pressure on policy-makers, specific corporate preferences must be linked to specific policy outcomes and, put simply, too many of the amendments enacted in 1971 are inconsistent with corporate concerns to validate such a thesis. For example, were corporate complaints regarding the administrative inefficiency of the AID program to have informed the establishment of OPIC, as alleged by Lipson, then one could expect that the new corporation would have enjoyed significantly greater resources than did its predecessor, yet this was not the case. Moreover, not only was the initial pattern to continue throughout the decade but successive amendments actually served to further restrict the capacity of the agency to insure U.S. foreign investors.

Among the first such amendments to this effect was the imposition in 1972 of restrictions directing the agency to refuse insurance for projects deemed to have a negative impact on the U.S. balance of payments.\textsuperscript{649} Such a restriction is clearly antithetical to corporate interests as it severely limited the availability of insurance, as was noted by the 1974 Senate subcommittee on MNCs in seeking an explanation as to why OPIC had issued less insurance than its predecessor. More significantly, however, concerned the amendment passed in the 1974 reauthorization hearings to privatize OPIC through the sale of its insurance portfolio to the private sector. Had the sale been completed it would have reduced both the availability of insurance covers for U.S. foreign investors as well as increased the premiums payable owing to the fact that private insurers could not replicate the agency’s deterrence function and capacity to enforce subrogated claims.\textsuperscript{650} In short, such an outcome is difficult to reconcile with corporate preferences. To the same effect, requiring OPIC to be self-funding cannot be understood as a product of corporate preferences, insofar as the requirement further limited the ability of OPIC to issue insurance in high-risk countries where, one may assume, the need was greatest, as well as to increase the cost of premiums.

The 1978 reauthorization amendments provide further evidence to this effect. First and foremost in this regard concerns the imposition of limits on OPIC insurance in countries exceeding certain per capita income levels.\textsuperscript{651} Although OPIC supporters managed to avoid mandatory restrictions, even voluntary targets curtailed the availability of insurance in key middle-income markets.\textsuperscript{652} Second, and similarly at odds with corporate preferences was the imposition of voluntary targets for OPIC relating to the proportion of insurance issued to small and medium sized enterprises. The third amendment of note imposed on the agency in the 1978 hearings concerned the imposition of human rights criteria on OPIC insurance, the effect of which, even though loosely interpreted, was to limit the capacity of the agency to insure projects in

\textsuperscript{649} The imposition of balance of payments criteria on the program owed much to Treasury’s increasing influence in light of growing U.S. balance of payments deficits, See Jessica Einhorn, \textit{Expropriation Politics} (1974).


\textsuperscript{651} Theodor Meron, ‘OPIC Investment is Alive and Well,’ \textit{American Journal of International Law} 73 (January, 1979), p. 104-111.

key markets for U.S. investors, including Chile, Argentina and Brazil all of whom were under the control of military juntas. And although one might interpret the repeal of the 1974 amendments mandating transfer of OPIC’s insurance portfolio to the private sector as evidence of the power of corporate preferences, there is little evidence to substantiate the claim that corporate America lay behind the reversal beyond the demonstrable reluctance of private insurers to purchase OPIC’s existing portfolio.

In sum, the aforementioned amendments are difficult to reconcile with continued corporate demand for investment insurance. Thus, not only did the sum of insurance issued by the agency as a proportion of total U.S. direct investment in LDCs fall sharply during the decade but the general tenor of changes to the OPIC program are simply inconsistent with the theorized influence of U.S. investors in determining policy shifts, the cumulative effect of which was to raise the cost and limit the availability of insurance covers.

Perhaps more significantly, such an explanation is also militated against by evidence to the effect that corporate America was itself a divided constituency as far as support for OPIC was concerned. That is, although U.S. investor lobbying in formal reauthorization hearings was no doubt the tip of the iceberg, being accompanied by extensive behind-the-scenes lobbying direct with Congressional and Senatorial representatives, this does not undermine the fact that when it came to the future direction of the OPIC insurance program, corporate America was split. Thus, not only did support wax and wane, evidenced by the shifting position of prominent bodies such as the National Association of Manufacturers, but for every corporate backer there were corporate opponents seeking to restrict the program to protect their own interests. Notable in this respect were the efforts of U.S. copper producers and agricultural interest groups both of who lobbied against the program, in each case winning concessions so as to limit insurance availability for foreign copper and agricultural investments.

More fundamentally, the empirical evidence also shows that it was not only U.S. foreign investors who had a voice in reauthorization hearings, and many of these other voices were staunchly opposed to the program. Foremost in this regard concerned the
opposition of organized labour led by the then 13 million strong AFL-CIO. This included vigorous participation in each of the three hearings, the result of which was the passage of several amendments but particularly the ‘runaway’ plants legislation enacted in 1974, which further restricted the availability of insurance for U.S. investors. Taken together these features serve to refute the theorized primacy of investor preferences as posited by Charles Lipson. Equally, in making this assertion the intention is not to deny that investors enjoy privileged access to policy-makers. Second, where possible the program was tailored to accommodate shifting corporate strategies of adaptation in LDCs. It is, however, to affirm that where the interests of the state and corporate America collided the former possessed autonomy from the latter in guiding the U.S. investment insurance program from 1969-1980.

Following the two hypotheses framework, the refutation of corporate preferences as the driving force behind OPIC policy shifts leaves, therefore, state initiatives as the most likely explanation for changes to the OPIC administered insurance program and U.S. anti-expropriation policy-making more broadly. Moreover, while such an explanation is easier to substantiate insofar as the empirical evidence reveals that state policy-makers provided the impetus for the observed policy shifts such an explanation would be mistaken. The reason for this is that changes to the program were not part of a coherent U.S. anti-expropriation policy, as such a policy did not exist.

In the initial instance, the assertion is supported by the varying and on occasion contradictory U.S. responses to individual expropriation disputes involving U.S. foreign investors that occurred during this period. In addition, the assertion can also be substantiated through examination of newly released but previously confidential internal documents detailing the lack of consensus among the executive and legislative branch as to what the appropriate policy response should be in light of overarching policy constraints arising from the need to be seen to support U.S. foreign investors and to maintain access to raw materials while at the same time being cognisant of the need to maintain healthy relations with LDCs given Cold War competition for influence.653

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Most immediately, the entire debate within the executive branch was characterized by indecision and a lack of consensus on even the most basic issues regarding U.S. policy toward expropriating states. Indeed, the only point of consensus with respect to the rising incidence of expropriation disputes (estimated by Kissinger to involve 56 U.S. firms in 1970) was the refrain ‘something needs to be done’. For example, although it was official U.S. policy to view expropriation as legal provided its was accompanied by appropriate compensation, the reality was that the legality of host country action in the eyes of U.S. officials was dependent on an assessment of whether the expropriation in question was understood as an isolated incident or part of a broader shift towards a socialist development model. In consequence, U.S. policy towards the state in question varied considerably, as evidenced by the very different responses to the almost concurrent expropriation of U.S. property in Peru and Chile.654

More narrowly, the lack of a consensus regarding U.S. anti-expropriation policy can be illustrated by the fact that whilst publicly proclaiming the need for ‘prompt, adequate and effective compensation,’ i.e. the ‘Hull formula’, even among high ranking officials within the executive branch there was no consensus as to what this meant in practice. The assertion is supported by the question to this effect to the President’s National Security Advisor, Kissinger from the newly appointed Vice-President of OPIC, where he is on the record as asking, ‘what [do] we mean in today’s real world when we declare a policy of insisting upon “prompt, adequate and effective compensation”?’.655 Perhaps more tellingly, there is no record of any reply being

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654 For good accounts of the two disputes and U.S. policy formulation in the case of the Peruvian expropriation of the International Petroleum Company (IPC) See Jessica Einhorn, *Expropriation Politics* (Lexington Mass.: D.C. Heath, 1974). To illustrate the difference, in the case of Peru the U.S. accepted far less than the standard compensation requested (less than book value) owing to the assessment that the Peruvian expropriations were not part of a broader shift towards a socialist oriented economic development strategy. In contrast, the Chilean expropriations initiated by the socialist leaning President, Salvador Allende were viewed as one-step towards socialism, with the result that the Central Intelligence Agency undertook covert action to undermine Allende’s Presidency.

655 See 160. Memorandum From the Executive Vice President of the Overseas Private Investment Corporation (Salzman) to the President's Assistant for National Security Affairs (Kissinger)/1/,
received. More basically still, the internal discussions reveal disagreement on every aspect of U.S. policy, including even whether it was in U.S. interests to formally delineate its position with respect to expropriation and nationalization.  

Indeed, the entire decision-making process was characterised by bureaucratic infighting, with minor points drawing impassioned responses from the concerned agencies. Broadly speaking, the point of division centred on the question of whether U.S. interests were best served by Treasury’s preferred ‘get-tough’ approach or NSC and State’s preferred position of avoiding confrontation and treating each case on its merits. The aim, in Kissinger’s words, to avoid ‘a few quick, cheap victories over some of the weaker Latin American countries governments, with the costs in terms of intensified economic nationalism, wider anti-Americanism and increased opportunities for the Soviets and their friends at the expense of our broader national-interests.’


For example, having codified five possible U.S. policy responses regarding sanctions towards expropriating states, even after almost two years of intensive, and given the quantum of threatened investments (estimated in 1969 dollars at $875 million) an inordinate amount of discussion from the President on-down, the positions of the concerned departments were recorded as follows: ‘Officially stated agency positions are as follows: OPIC prefers Option 3B. The Export-Import Bank prefers 3C. AID prefers Option 4, with a fall-back to 3C. All agencies that have commented prefer Option 2 of the multilateral voting options. Treasury at the staff level believes there should be no multilateral voting options and that our policy should be the same for both bilateral and multilateral benefits.’ 158. Memorandum From the Deputy Legal Adviser of the Department of State (Aldrich) to the Under Secretary of State (Irwin)/1/ Washington, August 3, 1971. /1/ Source: National Archives, RG 59, S/S Files: Lot 80 D 212, NSSM 131. Confidential. Drafted by Aldrich on August 3.  

The degree to which consideration of bureaucratic politics impacted every decision made is underscored by the following comments attributed to President Nixon himself who in discussing the proposed reorganization of AID was on record as noting ‘... that the Task Force would find it difficult to get agreement in this area. They would get screams from State, Treasury and all the other vested interests, as had occurred on some of the other Government reorganization measures which are under consideration.’ See 125. Memorandum of Conversation/1/. Washington, February 11, 1970. /1/ Source: National Archives, Nixon Presidential Materials, NSC Files, Presidential/HAK Memcons, Box 1023, Nixon-Peterson, et al. 2/11/70. Confidential; Eyes Only. Drafted by Bergsten. SUBJECT: Status Report of Peterson Task Force on International Development.  

159. Information Memorandum From the Acting Assistant Secretary of State for Inter-American Affairs (Crimmins) to the Under Secretary of State (Irwin)/1/. Washington, August 4, 1971. /1/ Source: National Archives, RG 59, S/S Files: Lot 80 D 212, NSSM 131. Confidential. The extent of the division is evidenced by the comments of Dr. Kissinger who in the same exchange in response to what he dubbed Treasury’s ‘doubtful thesis’ wrote, ‘If Secretary Connally really said: “The US can afford to be tough with Latin Americans because we have no friends left there any more”--and there has been no repudiation of the attribution—he has demonstrated only that he is a master of the self-fulfilling prophecy.’
Perhaps more fundamentally, the lack of consensus was not confined to the executive branch. Indeed, perhaps the only consistent motif to emerge from within the executive was the view that if we do not do something Congress will. To this end, the lack of agreement evident in U.S. policy responses towards expropriating states, is perhaps best illustrated by the fact that just as it seemed some consensus had been reached within the executive branch, Congress passed the Gonzales Amendment in March 1972 thereby removing in one-stroke Presidential discretion with respect to the imposition of sanctions and settling the question of whether bilateral sanctions would be accompanied by multilateral sanctions. The divergence of opinion and tension between the executive and Congress on the question of an appropriate U.S. response to still rising rates of expropriation was again evident by the fact that not one agency among the executive supported the Gonzales amendment, as evidenced by Nixon’s instant rebuttal in the form of a new bill introduced pursuant to the passage of the earlier amendment, designed to restore Presidential discretion.

Indecision concerning U.S. expropriation policy, including OPIC’s role therein, if any, was in many respects symptomatic of a wider lack of consensus among successive administrations from Johnson to Ford, regarding fundamental issues such as whether it was in the U.S. interests to encourage direct investment in LDCs for fear of exacerbating economic nationalism and compromising broader national interest goals in the context of the Cold War. Ultimately, the evidence suggests that the issue was never settled, beyond hortatory statements to the effect that the U.S. government should be more ‘selective’ in encouraging direct investment in LDCs though what this meant was never clarified.

659 This amendment required the President to instruct his representatives to vote against any foreign loans to countries that expropriated U.S. investment without compensation and was even more restrictive in its exceptions than the Hickenlooper Amendment by substituting specific requirements, such as good faith negotiations, for the concept of "appropriate steps." Again, even after the amendment was passed, it remained unclear whether it was intended to apply retrospectively, i.e. to existing investment disputes, specifically IPC in Peru or not?

660 See 151. Memorandum of Conversation/1/. Washington, September 8, 1970. /1/Source: National Archives, RG 59, Central Files 1970-73, FM 10-1. Confidential. Drafted by M.B. Feldman (L/ARA). SUBJECT: Encouragement and Protection of Investment. Wherein it was concluded that ‘the group seemed to be agreed on a policy of selective encouragement of investment in the developing countries. No one supported a policy of general encouragement of all investment.’ The comments are attributed in the transcript to John R. Stevenson, Legal Adviser to the President.
In short, there was no coherent U.S. anti-expropriation policy. Second, and as the previous section was intended to make clear, to the extent that consistent policy drivers can be discerned, U.S. policy toward expropriating states appears as a composite of bureaucratic politics of varying intensity, political expediency from within the executive branch vis-à-vis the legislative branch, and finally, *ad hoc* calculations regarding the importance of bilateral relations with the country in question given the exigencies of Cold War politics. In the final analysis while interpretations of the characterization of the OPIC administered insurance program as part of a coherent U.S. anti-expropriation policy or otherwise may differ, what is certain is that conspicuously absent from discussions within the executive was all but the most cursory interest in the needs of U.S. foreign investors in LDCs.

If the impetus for changes to the OPIC administered investment insurance program originated with state officials rather than U.S. foreign investors, but not as part of a coherent U.S. anti-expropriation policy, how then should the observed shifts be understood? The answer to the question is that shifts in OPIC policy and practice should be understood in the context of an *incoherent* foreign-aid program that itself cohered, in the sense that it was logically related to overarching policy concerns, in the context of the pursuit of national interests amidst the Cold War. To elaborate, and in order to chart the manner in which the OPIC amendments were informed by an incoherent foreign-aid program the next section will outline state-led efforts to reform the foreign-aid program that themselves determined the policy and practice of OPIC, beginning with the 1974 amendments, the result of which as has been shown was the effective termination of the investment insurance program.

**OPIC: State Initiatives and Foreign-aid Program Reform**

To explain, having established OPIC as a pre-cursor to what was intended as but one part of a four-pronged overhaul of the foreign-aid program, President Nixon outlined his proposed reforms in his annual foreign-aid address to Congress in September
Unfortunately, for the Nixon administration, the re-branding of the foreign-aid program did little to assuage Congressional opposition, evidenced by the rejection of the foreign-aid appropriations bill for fiscal year 1972. The wholesale rejection of the bill signalled a new low in relations between the executive branch and Congress as concerned the foreign-aid program. In this regard, the delay between the receipt of the Peterson report and its being presented to Congress had proved fatal. It had so, because in the meantime mounting Congressional displeasure meant that Congress itself had earlier that year taken the unusual step of forming its own bipartisan working party to review foreign-aid spending, whose recommendations were handed down in 1973.

The result of the Congressional review, and the subsequent passage of the Congress-initiated reforms in late 1973, was the reorientation of the U.S. foreign-aid program labelled ‘Basic Human Needs.’ The thrust of the new policy was intended to refocus U.S. development spending away from large headline grabbing projects toward meeting the basic human needs of the world’s poor. In particular, the approach called for separate appropriations for specific ‘sectoral’ aid programs, including for ‘education’, ‘population control’ and ‘agricultural productivity’ etc, so as to enable Congress to exert closer control over the aid program and associated expenditures. It is perhaps not therefore surprising that the following year Congress voted to effectively kill off the investment insurance program, the basic rationale for which was patently ill suited to the now redesigned foreign-aid program. For Nixon, the attempt to reform foreign-aid would be his last, owing to his impeachment the following year and his subsequent replacement with the then Vice-President, Gerald Ford (August 9th, 1974). Unfortunately for OPIC, the pattern of abortive AID reform as part of broader reform of foreign-aid spending would continue through the Ford administration underpinned by continuing tensions between the Republican

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662. The wholesale rejection of the 1972 appropriations request for foreign-aid totalling $2.9 billion by Congress was the first time since the foreign-aid program was instituted in 1945 that this had occurred.


664. Indicative of the now relegated status of the role of private foreign investment within the pantheon of the U.S. foreign-aid programs, that same year Congress voted to reduce the budget for the USAID program aimed at encouraging private foreign investment consistent with the developmental needs of LDCs to just $1 million.
administration and the Democratic House majority.665 Once again, the impasse and the absence of a natural constituency for OPIC within the legislative branch meant the investment insurance program would remain stunted as it struggled to find a place for itself within the new Congress instituted foreign-aid regime.

Finally, the 1978 OPIC amendments, like those resulting from the two previous re-authorization hearings, must also be understood in the context of state initiated reform of the foreign-aid program centred on President Carter’s ‘New Directions’ policy.666 Moreover, although by 1977, the earlier proposals to privatize the program had been all but abandoned, the future of the agency, specifically, its place with the foreign-aid program remained uncertain. The uncertainty continued unabated until 1978 when the issue of reforming foreign-aid once again rose to the top of the policy pile for the Carter administration, elected in late 1976. Two policy planks defined the reform package submitted as part of the International Development Cooperation Act (1979).667 First, in accord with what was described as growing public sentiment, U.S. foreign-aid spending was made subject to human rights criteria, including with respect to the provision of bilateral development loans and the provision of insurance by OPIC.668 Indicative of the new direction for aid spending, including the OPIC program, were the comments of the newly appointed Deputy Assistant Secretary of State for Human Rights, Roberta Cohen who stated, ‘[P]olicies designed solely to protect bases or investments in nations with repressive regimes will have to undergo radical change.’669 The reform package also completed earlier moves instigated by

666 Many of the Carter administrations proposals drew directly from earlier reform initiatives proposed by the late Senator Hubert Humphrey, who had introduced a foreign-aid reform package in the Senate the previous year.
667 The International Development Cooperation Act (1979) was passed by Executive Order No. 12163 September 29, 1979 (22 U.S.C. 3501 et seq.).
669 The tenor of the new policy was then confirmed by the Assistant to the Deputy Secretary of State who opined, ‘Human Rights considerations are not distinct from economic considerations’ with the result in the President’s words that the U.S. would no longer ‘embrace any dictator who joined us . . . out of an inordinate fear of Communism.’ See President Carter, speaking at Notre Dame University, 1979, quoted in Nicolai N. Petro, The Predicament of Human Rights: The Carter and Reagan Policies, Volume V, (Boston: University Press of Americas, (1983), p. 20. The passage of the Foreign Corrupt Practices Act (FCPA) 1977 and its application after extensive debate to the OPIC program must be

214
Congress aimed at reorienting U.S. aid spending so as to focus more closely on the developmental needs of the poorest countries, consistent with which OPIC insurance was limited to low-income LDCs. The second and most critical aspect of the reforms took place the following year beginning with the long-awaited reform though not abolition of USAID in 1979 as part of a wider series of reforms. Key among the administrative reforms was the creation of the International Development Cooperation Agency (IDCA) to oversee some 31 separate foreign-aid programs, including the OPIC administered insurance program, and USAID itself.

The creation of the IDCA represented the first major overhaul of the U.S. foreign-aid program since the Kennedy instituted reforms in 1961 that had established USAID. In order to implement the changes providing for the transfer of control of OPIC from the Secretary of State to the New Director of the IDCA, Re-Org. No. 3 was passed pursuant to the reform process by Executive Order 12188 in September 1979. As part of the administrative reform, the IDCA Director was appointed Chairman of the OPIC Board of Directors. Unfortunately, in light of the inadequacies of AID, IDCA never fulfilled its promise. For the time being, however, as far as OPIC’s administrators were concerned, the establishment of the IDCA ended the uncertainty surrounding the insurance program. Although the imagined stability would be short-lived, as will become apparent in the next chapter, for the time being the reforms enacted as part of the general reform of the foreign-aid program achieved their objectives insofar as they served to shore up legislative support for the agency by reaffirming its place among the myriad U.S. foreign-aid programs.

To summarize, the empirical evidence demonstrates that state initiatives provides the best explanation for the observed changes to OPIC policy and practice for the period 1969-1980. These changes must be understood, however, not as part of a coherent anti-expropriation policy by the U.S. so much as part of an incoherent foreign-aid program that itself must be understood as part of the pursuit of U.S. national interests in the context of the bipolar world order. And while the observed changes were no

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doubt informed by the increasing incidence of expropriation in LDCs, ultimately these changes represent not so much a coherent attempt to counter the challenge to existing standards of investor protection so much as an expression of dissatisfaction emanating from within the legislative branch regarding the results of U.S. foreign-aid spending. More precisely, the establishment and evolution of OPIC, specifically the lack of growth and tightened restrictions on insurance availability can only be understood as the product of a series of abortive efforts to reform foreign-aid spending dating back as far as 1967 wherein the proposal to transfer the guarantee program from AID to a corporation was first mooted, and culminating in the establishment of the IDCA in 1979 wherein responsibility for OPIC was transferred to the newly created ‘umbrella’ agency.

Conclusions

To conclude, the chapter has found that of the two competing hypotheses outlined, state initiatives provides greater explanatory leverage than does consideration of U.S. foreign investor preferences. The intention, however, in asserting the primacy of state officials in underpinning the observed changes is not to portray the state as a unitary body. Instead, shifts in the policy and practice of OPIC are best understood as produced by a combination of policy-makers within the executive, and the legislative branch, including on more than one occasion with direct input from the President himself. Of critical importance in this regard concerned the ongoing tensions between successive administrations and Congress in the context of foreign-aid reform. In this respect, the evidence underscores the continued and to some extent unique role of Congress in formulating U.S. foreign policy separate from the executive, but particularly from the mid-1970s thereby reversing the trend of the previous three

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671 The changed emphasis of U.S. foreign-aid spending in LDCs instigated by the Carter administration though more than simple ‘window-dressing’ should not, however, be interpreted as signalling a radical shift in U.S. foreign policy vis-à-vis the developing world. Evidence of this is shown by the fact that whilst proclaiming the need to respect human rights, Carter himself, in a pattern that was repeated elsewhere throughout the developing world, presided over the sale of sensitive military equipment valued at more than $110 million to President Suharto’s Indonesia in contravention of an earlier Congressional ban. Moreover, he did so in the full knowledge that the equipment would be used to suppress insurrections in East Timor. That this is the case suggests that while U.S. policy shifted this was not allowed to interfere with long-standing national security goals, including support for Suharto and Indonesia. See Jennifer Washburn and William D. Hartung, ‘U.S. Arms Transfers to Indonesia, 1975-1997: Who’s Influencing Whom?’ World Policy Institute, Washington, D.C., (1997).
decades characterized by the concentration of foreign policy-making power within the executive branch.

Equally, while the entire process was characterized by tensions between Congress and the executive regarding the purposes of the foreign-aid program such tensions did not extend to the perception of the national interest, which was shared by both branches of the U.S. government. The tensions observed are, therefore, best understood not so much as the product of disagreement as to the national interest so much as divergent views as to how foreign-aid spending could best be tailored towards such ends. In this regard, the empirical evidence makes clear that the OPIC program, as but one minor component element of the foreign-aid program was formulated in the context of a consistent and clearly defined perception of the national interest vis-à-vis LDCs that itself cohered in the context of increasing U.S. influence as a bulwark against Communist expansion. In this respect, successive administrations displayed a readiness to sacrifice U.S. foreign investor interests in favour of the national interest so conceived.

Viewed from a narrow theoretical perspective, the findings of the research diverge from Lipson’s account in two critical ways. First, the assertion of state initiatives diverges from Lipson’s corporate preferences in terms of the casual mechanism. Foremost in terms of the differences concerns the fact that the evidence has shown that there was no coherent capitalist class capable of sustaining such an explanation owing to the split between the interests of domestic producers and multinational capital. Second, and more fundamentally, the findings depart from Lipson’s characterization of the program insofar as they refute the notion of the program as a part of a coherent U.S. response to rising rates of expropriation, being better viewed as part of an incoherent foreign-aid program. In this regard, the findings presented here are consistent with realist notions of foreign policy-making. They are so because although U.S. investors enjoyed a privileged position with respect to the insurance program, ultimately where the interests of the state and foreign investors collided, the interests of the former took precedence over those of the latter.

This chapter will follow the same basic methods as the previous one, the aim to chart and explain the evolution of the OPIC administered insurance program from 1981 through until 1994. The period spanned four re-authorization hearings as well as the special legislation passed in 1994 providing for the one-off expansion of the agency’s total maximum liabilities as well as its per project insurance and financing limits so as to enable it to participate in the financing of private infrastructure projects in LDCs utilizing the BOOT investment model.\textsuperscript{672} Taken together, the four hearings plus the special legislation were characterized by far less opposition and controversy than was the case in the period to 1980.

The shift in the tenor of the debates appears related to the fact that where in the previous period the question of such overt government support for the process of multinational capital accumulation remained unresolved so as to cast a shadow over the legitimacy of the program, in this period by contrast the question no longer dominated the proceedings. Instead, the focus of attention shifted to the question of how the program could best be tailored to better support U.S. foreign investors operating in LDCs. To this end, the hearings were animated, if not by a shared sense of purpose then a greater acceptance of the program as the question of its impact on the U.S. economy was decided in the affirmative by most if not all interested parties. Of particular note in this regard concerns the fact that following successive amendments, wherein labour standards were codified, an unspoken agreement concerning the program appears to have been reached with organized labour. In consequence, what was once a highly controversial program appears by the end of the period to have been transformed into an established instrument of U.S. foreign policy vis-à-vis the developing world, i.e. a part of the institutional furniture, so to speak.

As was the case in the previous chapter, the investigation will be organized around the two competing hypotheses forwarded to explain shifts in the policy and practice of OPIC and U.S. anti-expropriation policy-making more broadly. The first hypothesis, and to recap, holds that changes to the program are driven by corporate preferences

\textsuperscript{672} See the ‘Jobs Through Export Enhancement Act’, 1994 [Public Law No. 103-392].
consistent with evolving strategies of adaptation and risk-management. The state initiatives hypothesis, by contrast, explains changes to the OPIC suite of programs as the product of shifting foreign policy goals vis-à-vis LDCs sought by U.S. officials comprised of the executive and legislative branches. Once again, in order to substantiate one explanation or the other, the chapter seeks to identify not only instances of general corporate and interest group lobbying and or formal and informal state policy initiatives but to link actual proposals to outcomes, including the transmission mechanisms linking the two phases of the policy-making process.

Finally, in order to consider the evidence, the remainder of the chapter is organized as follows. The first task will be to outline the actual policy amendments as provided for through the course of the four re-authorization hearings. This will incorporate an overview of the legislative history, including the specific issues that informed each episode of policy-making as well as detailing supporters and opponents of particular amendments. The overview will then be followed by an analysis of the explanatory capacity of the two accounts of U.S. foreign policy-making, beginning with an assessment of the role of U.S. foreign investors.

The chapter finds that the impetus for the changes in the OPIC program originated with state officials, comprised of both Congress and the executive branch. Thus, although corporate preferences were important, and indeed, increasingly central in the minds of policy-makers, the changes observed were initiated by the state. Once again, however, the empirical evidence refutes the characterization of the program as a coherent element of U.S. anti-expropriation policy-making. The chapter therefore finds that the changes to the OPIC program should be understood as but one element not of the foreign-aid program, rather, an increasingly assertive U.S. foreign trade and investment policy. The shift reflected growing concern within the U.S. government regarding what was perceived as declining U.S. corporate competitiveness (dubbed the ‘American malaise’) in the face of intensified competition for markets from European and Japanese MNCs and latterly LDC producers. Ultimately, therefore, changes in the policy and practice of OPIC pursuant to shifts in U.S. foreign trade and investment policy reflected a consistent albeit evolving conception of U.S. national interests, unrelated to either party politics or Presidential whim.
With OPIC’s statutory authority due to expire in September 1981, the Senate Foreign Relations Committee began preliminary hearings concerning OPIC in June 1980. The bill (S.2186), intended as a ‘trial-balloon’ to test Congressional reaction to the proposed expansion of the agency, was cosponsored by Senator Javits (R-NY) and Senator Abraham Ribicoff (D-CT). It would inter alia extend OPIC’s operating authority through until 1985, remove the per capita income-ceiling imposed in 1978, as well as raise OPIC’s statutory maximum liability from $7.5 billion to $10 billion, and the loan guarantee ceiling from $750 million to $1 billion. The initial response to the bill was negative, with a number of opponents citing the Government Accountability Office report of 1980 that had criticized the agency for failing to meet the development goals set for it in 1978. Among the points noted in the report was that of the 71 projects approved by the agency since 1978 in countries with incomes greater than the $1,000, only five exhibited ‘exceptional development benefits.’ Moreover, the report noted that a large number of projects supported by OPIC appear to have little or no developmental impact as they produce luxury consumer items.

In light of the initial adverse reaction, the preliminary bill was not presented to the House Committee until the following year. When presented, the passage of the bill was relatively easy, however, resulting in the reauthorization of the agency on October 16th, 1981 through until September 1985. With the benefit of hindsight, two

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676 Gary Sampliner, ‘The 1981 OPIC Amendments’, *Journal of Law and Policy in International Business*, (1981). For instance the Government Accountability Office report noted that OPIC had insured the following: General Foods (Philippines), OPIC Contract No. 9775, Johnson Products (Nigeria), OPIC Contract No. 9705. Other OPIC projects, the report noted may even have a negative effect on development. For instance, OPIC insured more than one project whose activities include the sale of infant formula in third-world countries, See Abbott Laboratories, Inc. (Nigeria), OPIC Contract No. 9722. Furthermore, according to OPIC, of the 475 projects proposed to OPIC between 1976 and 1979, only 13 were rejected for having inadequate developmental benefits. Projects rejected under this standard include, munitions factories, casinos. From Interview with David Husband, International Economist, Office of Development, OPIC in Washington D.C. (October 6, 1981). The Government Accountability Office report also criticized the procedure itself for measuring the development benefits, noting that any information to this effect was provided by the prospective investor, and was not checked by OPIC, with the result that ‘OPIC is able to approve applications as long as there is no overtly adverse effect of development.’, p. 210, *Id.* At 34.
events proved propitious for OPIC and its supporters. First, long-time opponents of OPIC, Senator Frank Church (D-IN) and Representative, Lester Wolff (D-NY) had failed in their reelection bids in the November 1980 elections.\textsuperscript{677} Second, as the U.S government agency responsible for third-world development through FDI, OPIC proved to be the major beneficiary of the new administration’s new development policy, which emphasized trade over aid as the principal means of assisting developing countries.\textsuperscript{678}

The change in emphasis concerning the aid program was given added impetus, as it was fully consistent with the other pressing issue of the day, the deterioration in the U.S. trade balance.\textsuperscript{679} To this end, supporters of the program emphasized the trade promotion function performed by the agency, in terms of initial procurement of materials, which would be sourced from the U.S, as well as the opportunity such investments provided U.S MNCs to gain a foothold in foreign markets.\textsuperscript{680} However, the upgrading of the trade promotion function as the \textit{raison d’etre} of investment insurance was resisted by those concerned that the articulation of a trade promotion function might mean OPIC rejected projects with clear development benefits. In this regard, the battle lines for the 1981 reauthorization hearings were established.

The Senate hearings concerning bill S.933, began in June 1981, and were presided over by Charles H. Percy [R-III] and Senator Pell Claiborne [D-RI]. Among the key amendments considered were the following: removal of the 1978 $1,000 ceiling, formal recognition of OPIC’s trade promotion function, increasing the size of the eleven member board to thirteen, including a representative from the Department of Labour, and small business, expanding coverage to include civil strife under the

general war risks cover, and including an additional underwriting criteria that enabled OPIC to support projects absent of development benefits, but with ‘exceptional trade benefits’ for the United States.681

Testimony was heard from both supporters and opponents alike, including among the latter the head of the AFL-CIO, who restated long-standing concerns relating to the impact on U.S. employment, and Fred Bergsten of the Institute for International Economics in Washington. Of particular interest to opponents of the bill was the provision to remove the country income-ceiling imposed on OPIC, citing the Government Accountability Office report which noted that doing so would enable OPIC to support projects in upper-income developing countries such as Turkey and Korea that had demonstrated a successful track record in attracting FDI without OPIC.682 The CEO of OPIC responded by arguing that the current restrictions deprived it of income that could be used to support projects in low-income LDCs.

Second, the restriction prevented the agency from assisting development in strategically important countries such as Turkey and Korea that although at the upper end of the income scale were nonetheless still underdeveloped and politically volatile.683 Opposition to the proposed extension of coverage to include civil strife arose in Congress, with a number of Senators, led by Senator William Goodfellow, noting that there was no formal legal definition of the new risk, and that it could as a result be abused were claims to arise from losses caused by legitimate actions such as worker discontent.684 Two separate lobby groups, representing the interests of U.S.

681 The proposal to have a Department of Labour representative on the OPIC Board was a compromise, the need for which was occasioned by the refusal of organized labour to accept the offer of a position on the OPIC board. See Gary Sampliner, ‘The 1981 OPIC Amendments’, Journal of Law and Policy in International Business, (1981), p. 32.

682 Government Accountability Office report, supra note 60, at 27, 29, 41. Nevertheless, the report recommended the removal of the $1,000 ceiling, with only the representatives of the Departments of State, Labour and the Treasury dissenting. Id. At 40.


684 As Sampliner notes, another valid criticism that was not raised in the 1981 hearings relates to the clause in OPIC’s contract allowing coverage for damage resulting from an insured’s efforts to hinder or combat an insurrection, which would presumably extend to civil strife. Under this clause OPIC might be in a position compensating host government forces for suppressing civil unrest that may have arisen from legitimate grievances. This situation actually arose notes Sampliner, when in 1979 OPIC was obliged to compensate Freeport Moran to support the Indonesian Army’s suppression of a rebellion in West Papua. See also comment on the legal ramifications of the extended coverage in Gary Sampliner, ‘Comment, Acts of Terrorism and Combat by Irregular Forces – An Insurance “War Risk?”’, 4 Cal. W. INT’L J. 315, 333-34 (1974). Furthermore, when Congress requested OPIC to provide legal precedents
investors, led support for the agency. The first of these, the Emergency Committee for American Trade, representing 63 U.S. MNCs called for OPIC to expand coverage, including with respect to the length of contracts and the maximum project limit.685 The second, which provided testimony before the House Committee only, the ‘Council of the Americas’ represented more than 200 private U.S. businesses, including almost every U.S. investor in the Caribbean and Latin America.686 Despite the bill containing almost identical provisions to the earlier rejected bill, it passed the Senate on a voice vote, thus indicating the lack of opposition within the Senate. The passage of the Bill in the House was even easier, also passing with a voice only vote, on September 22nd.687

Among the key provisions of the 1981 amendments were the following: first, the 1978 per capita restrictions were increased from $1,000 (1975 dollars) to $2,950 in 1979 dollars.688 Second, OPIC’s coverage was expanded to include civil strife. Third, OPIC’s Board was increased to thirteen, including the addition of the representative from the Department of Labour. Fourth, OPIC was instructed ‘to seek to support those developmental projects having positive trade benefits for the United States.’ Fifth, OPIC was permitted to continue its Direct Investment Fund, but under new restrictions. Sixth, OPIC was directed to submit a report to Congress on the likelihood that investments would be made without OPIC insurance, i.e. with a view to developing a criterion for ‘additionality.’ Seventh, OPIC was permitted to change its methodology for the valuation of a net-investment to reflect either replacements costs of project assets or net book value of the investment on the date of the loss.’ Finally,

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685 For a guide to the activities of ECAT, See www.ecattrade.com Date Accessed 06.05.05.
OPIC was directed to repay its original start-up costs to the Treasury, equivalent to 25 percent of its annual income until all costs were repaid.689

The amendments represented a victory for supporters of the program, as well as those who favoured the reorientation of the program from its original development goals to that of trade promotion. Several features of the amendments appear as relevant in this regard. First, although the income ceiling was not removed, the increase represented an above inflation increase of $1,200. Further, it achieved its objective insofar as it enabled OPIC to resume coverage in 17 of the 26 countries impacted by the 1978 provision, including critically growing markets such as Brazil, Taiwan, and Turkey. Moreover, the maintenance of the cap was further watered down as OPIC was permitted discretion in approving projects in countries with incomes greater than the new limit, as it had been in 1978 under the Board of Directors Guidelines, but this time applying to the increased ceiling. Third, the decision to maintain the Direct Investment Fund and the Loan Guarantee program had come in the face of opposition from the White House who had proposed cutting the program, on the basis that it was a drain on the U.S. budget, and also that it crowded out private investment. In the end, the administration’s proposals were only defeated through a combination of pressure from the State Department, AID, as well as the Special Trade Representatives Office.690 That the Direct Investment Fund program appeared better suited to development and that it was de-emphasized is, however, Sampliner tells us, perfectly consistent with the Reagan administration’s policy shift.591 In conclusion, although Congress never intended that OPIC substitute for the U.S. foreign-aid program, the result of the 1981 amendments was just such a substitution.

OPIC Reauthorization 1985: Strengthening Labour and Environmental Protection

In comparison with previous reauthorization hearings, the 1985 reauthorization providing for the agency’s renewal through until September 30th 1989 was met with

little opposition in either the House or the Senate. Broader Congressional and executive policy issues linked to the spiraling federal budget deficit did play a role, but any opposition to the agency that may have arisen as a result was avoided as OPIC had since 1981 repaid to Treasury the original start-up costs, and did not request any additional Congressional appropriations for the four years through until 1989. In many respects, the 1985 hearings followed the established pattern with both Houses hearing testimony from opponents and supporters of the agency alike, including Robert O’Neil, President of Emergency Committee for American Trade, as well as the AFL-CIO who again lobbied for restrictions on the program aimed at minimizing the negative impact on U.S. employment. Among the key provisions of the proposed bill was the expansion of OPIC insurance coverage to include ‘business interruption’ insurance, as well as an amendment to restrict OPIC insurance in countries failing to respect workers rights. Neither proposal attracted much controversy, however, though concerns were expressed by organized labour regarding the precise wording of the proposed statutory restrictions on OPIC cover for countries failing to adopt standards of protection as mandated under the Generalized System of Preferences.

Reauthorization hearings began in the House on August 1st, 1985, sponsored by Don Bonker (R-WA), along with seven cosponsors, including the influential head of the House Foreign Affairs Committee, Doug Bereuter (R-NE). The bill (HR.3166), to amend the FAA (1961) was then referred to the House International Relations Committee, who in turn referred the bill to the Subcommittee on International Economic Policy and Trade. Having considered the bill, the Subcommittee then referred the bill back to the House Committee, who then passed the bill on a voice vote on September 23rd 1985. The House bill (S.3166) was then referred to the Senate, who in turn referred it to the Senate Foreign Relations Committee. It was then read twice before being passed also on a voice vote on September 26th 1985.

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693 The point of concern was the wording of the provision mandating that OPIC restrict cover to countries ‘taking steps to adopt and implement laws.’ In particular, there was disagreement about what actions would qualify as ‘taking steps?’ See ‘Workers Rights and Trade Benefits’ Chapter 3, [http://www.solidaritycenter.org/files/JFA_Chapter3.pdf](http://www.solidaritycenter.org/files/JFA_Chapter3.pdf). Date accessed 10.10.05.
694 The six other cosponsors were: Howard L. Berman (Rep. Calif.), Mel Levine (Calif.), Buddy MacKay (Fl.), Daniel Andrew Mica (Fl.), Toby Roth (WI), and Edwin V. W. Zschau (CA.). See H.R. 3166 [www.thomasloc.gov](http://www.thomasloc.gov), 99th Congress. Date accessed 10.10.05.
The key features of the amendments were as follows: first, the per capita income-ceiling was modified from 1979 to 1983 dollars. Second, OPIC was required to develop criteria for assessing the environmental impact of insured projects. Under the terms of the statute OPIC is required to refuse to insure, reinsure, guarantee or finance any investment that poses a ‘major or unreasonable hazard to the environment, health or safety, or resulting in the significant degradation of a national park or similar protected area.’ Further, OPIC is to notify the country where the investment project is located of any ‘U.S. health, safety or environmental restrictions that would apply to the project if the project was undertaken in the United States.’

Third, OPIC was directed to refuse to support any project in countries deemed by the Generalized System of Preferences to have failed to be taking steps to extend internationally recognized worker rights to workers in that country. These rights are defined to include: right of association, right to organize and bargain collectively, prohibition of forced labour, minimum age for employment (15 years of age for middle-income countries, 14 for low-income countries and 18 for work involving hazardous activities in all countries), and acceptable working conditions with regard to the payment of wages (at least the official minimum wage), hours of work (48 hours per week, with at least one 24 hour rest period), and occupational safety and health (standards established by the World Bank). Moreover, although Congress refused to define what would constitute ‘taking steps’ so as to incur the wrath of the AFL-CIO, the provisions were intended to ensure consistency with GSP provisions. To this end, Congress outlined the provisions as they related to OPIC as follows: the country is a member of the International Labour Organisation (ILO), its laws conform to one or more of the five worker rights listed in section 502 (2) (4) of the Trade Act 1974 and it continues to make progress to implement internationally recognized worker rights. The fourth significant amendment concerned the introduction of

696 The GSP provisions, including as they relate to OPIC, are subject to a Presidential waiver on the grounds of national security or national economic interest.
698 The GSP is administered by the Office U.S. Trade Representative.
‘business interruption’ insurance designed to protect against indirect losses.699 Fifth, OPIC was directed to submit to Congress an annual report detailing the employment effects of each OPIC supported project. To this end, OPIC was prohibited from supporting any projects resulting in a ‘net’ job loss to the U.S. economy.700 Sixth, and in light of the establishment that same year of the Multilateral Investment Guarantee Agency, OPIC was permitted to enter into pooling or other risk-sharing arrangements with multilateral insurance or finance agencies. Finally, OPIC was directed to submit to an independent audit at least once every three years.701

OPIC Reauthorization 1988: Business as Usual

The 1988 Congressional Reauthorization hearings followed the pattern established by earlier hearings in 1981 and 1985 insofar as opposition to the proposed extension of the agency’s operating authority was in comparison with the previous decade minimal. In addition, although the investment insurance program was not immune to broader policy issues, arising out of efforts to rein in the federal budget deficit, any opposition that may have arisen in this regard was avoided, as the agency was fully self-financing.702 Two further factors also meant that OPIC was able to escape the kind of widespread opposition that had once threatened the future of the program.

699 Business Interruption insurance is an all risks guarantee designed to protect against indirect losses such as might occur if the supplier to a project were unable to meet contractual obligations due to political risks, and the project were forced to source the materials at additional cost. Congress was not, however, entirely comfortable with the new cover and directed OPIC to submit to it within twelve months a report detailing the underwriting basis for this type of cover.

700 For the purposes of the Act, a net job loss is defined as ‘resulting in a net loss of more than ten person-years of U.S. employment during the first five years of operation.’ Quoted in OPIC Annual Report, 1989, p. 16.


702 According to Virginia Haufler, so severe were the budget constraints, particularly applied to foreign operations, that when the World Bank sought a financial commitment from the United States toward the establishment of the multilateral investment insurance agency, MIGA, as a one-off capital contribution, it appeared as though the U.S. would not be able to contribute, leaving MIGA facing the possibility of proceeding without the U.S. as a charter member. See Virginia Haufler, Dangerous Commerce: Insurance and the Management of International Risk, (Ithaca & London: Cornell University Press, 1988), Footnote No. 136, chapter 4 ‘Redefining Risk and Responsibility 1979-89’ quoted from Meeting, U.S. Council for International Business, May 9, 1986.
First, it was widely perceived that OPIC offered a valuable tool to promote third-world economic development amidst the continuing debt-crisis. For example, OPIC had just the previous year issued for the first time PRI to cover four debt-equity swaps with a combined value of $118 million. In addition, the agency had insured two U.S. equity investments in formerly government owned parastatals in Turkey and the Philippines agreed as part of the respective IMF structural adjustments programs.\(^{703}\)

The second factor that contributed to the agency’s smooth reauthorization was that the forms of support provided U.S. foreign investors by OPIC were by 1988 well established, thereby, occasioning little controversy, including from organized labour, the concerns of whom had largely been addressed in the 1985 amendments. To this end, the normalization of OPIC as a federal government program was demonstrated by its inclusion in the 1987 ‘Foreign Operations, Export Financing and Related Programmes Act’ (HR. 3186), according to which future Congressional appropriations for OPIC were to be assessed alongside other established programs such as the Export-Import Bank and the Peace Corp.\(^{704}\)

The bill to reauthorize the agency (S.2006) was presented on July 6\(^{th}\) 1988, sponsored by Senator Pell Claiborne. That same day, the Senate referred the bill to the Committee on Foreign Affairs who in turn referred it to the Subcommittee on International Economic Policy and Trade.\(^{705}\) The proposed amendments primarily concerned technical modifications, to update the income limits, as well as minor administrative changes. As a result, passage of the amendments required only a voice vote in both Houses, resulting in the reauthorization of the agency through until September 30\(^{th}\) 1992.

\(^{703}\) OPIC Annual Report, 1987, p. 16. The debt-equity swaps were conceived as part of the Baker Plan. The Baker Plan was named after the then Secretary of State, James Baker, who launched the initiative at the World Bank/IMF debtor conference in Seoul in 1985. The plan was well received by the commercial banks, but was rejected by several large debtors such as Mexico and Argentina as too little too late. The plan called for international commercial banks to extend a further $20 billion to the fifteen most indebted countries over a three-year period to fund economic adjustments. Official multilateral institutions would under the plan double their lending over the same period, while the IMF was to establish a $2.7 billion Trust Fund to finance new borrowing to the poorest debtors. In return debtor nations were to sign a pledge to implement IMF structural adjustment programs. See Susan George, A Fate Worse Than Debt, (London: Penguin Books, 1988), p. 193.

\(^{704}\) See HR. 3186 and See also Trade and Export Enhancement Act 1987 [HR.2150].

Among the key provisions of the 1988 OPIC amendments were the following: first, an amendment was passed to update to 1986 dollars and increase the per capita income level restrictions applying to countries for which OPIC is required to provide preferential treatment (the least developed countries) to $984 and or restrict its activities (the higher income developing countries), increased to $4,269.706 Second, the underwriting criteria were amended so as to ensure that in addition to the development criteria, OPIC only issued insurance for projects in countries whose investment policies ‘are consistent with U.S. investment policies.’ Fourth, the operating statute under which OPIC operates was amended to enable the agency to insure existing investments as well as new ones. The aim, to enable investments in countries with deteriorating political conditions to be maintained, where in the absence of insurance the investor might prefer to divest their interests, with implications for the economic stability of the host country. Fifth, in what was perhaps the most significant element of the Act, OPIC was permitted to establish two ‘Growth Funds’ for sub-Saharan Africa and the Caribbean Basin. The funds, initially established as five-year pilot programs were designed to provide ‘limited equity capital’ to eligible projects in each of the designated areas, and were to give preferential consideration to projects sponsored by or significantly involving U.S. small businesses or cooperatives. Sixth, OPIC was directed to undertake cooperative programs with the private insurance industry designed to enhance the private PRI industry in the United States. Seventh, and finally, the definition of an ‘eligible investor’ was modified so as to enable OPIC to support investments with less than 50 percent U.S. ownership, but with a minimum of 45 percent voting stock owned by U.S. citizens.

OPIC Reauthorization 1992: Growth in Eastern Europe

The newly elected Clinton administration viewed OPIC and its sister agency, the Ex-Im Bank as ideal vehicles for expanding U.S. exports and opportunities for U.S. foreign investors. Moreover, an expansion of the two programs was consistent with President Clinton’s vision of a more expansionary foreign economic policy in the

developing world and economies in transition, with the result that the agency’s financing and insurance programs were significantly expanded in the two years to 1994.\footnote{Significant changes were introduced in 1989 with respect to accounting provisions used by the agency to assess maximum investment insurance exposures. Before the amendment, the three categories of political risk were counted separately, as each was listed separately on contracts. After the modification, the insurance exposure was measured as equal to the highest maximum liability of the Corporation to any one of the three risks, as only one of the three could be claimed against. While the accounting provisions adopted brought OPIC in line with standard insurance accounting principles, including those used by private PRI providers for the purpose of calculating loss reserves, it makes comparison of pre and post-1989 maximum insurance exposures (contingent liabilities) of little use.}

More generally, the agency had enjoyed considerable success, judging by the amount of insurance issued in the period since its last reauthorization, underpinned by a rapid increase of private FDI in LDCs and transition economies (emerging markets).\footnote{For example, OPIC issued more insurance and loan guarantees in 1991 than any other previous year since its inception, See 1991 Annual Report.} Moreover, the number of countries eligible for OPIC insurance and financing had expanded rapidly with the addition of the former Soviet Republics and Eastern European countries. All of whom were eligible by 1992, following the signing of BITs with the Baltic States, Bulgaria and Albania, the previous year by the former Vice-President, Dan Quayle.\footnote{OPIC, \textit{Annual Report}, 1991, p.3. By 1992, OPIC insurance was available in 122 countries.} Insurance and financing programs were still not available in China, however, following the revocation of ‘Most Favoured Nation’ status in 1989.\footnote{China’s MFN status was revoked by the Bush administration in 1989, following Tiananmen Square.}

The bill to reauthorize OPIC for four more years (S.2338) through until September 1996 was introduced in the Senate by Senator Pell Claiborne on March 11\textsuperscript{th}, 1992. Following introduction, the bill was subsequently referred to the House Committee on Foreign Relations, who in turn, referred it to the Subcommittee on International Economic Policy, Trade, Oceans and Environment. Hearings were held on July 22\textsuperscript{nd} in the Senate. In the House, the bill (HR.5200), sponsored by William Broomfield [R-MI], was introduced on the May 19\textsuperscript{th} 1992. Once again, there was little opposition to the bill at the committee stage or on the floor in the respective chambers. The lack of opposition is, however, noteworthy as despite it following the recent trend, in contrast with the previous two amendment acts, the 1992 bill provided for a significant...
expansion of the loan guarantee program in particular.\textsuperscript{711} The amendments were first passed in the House on August 5th by a voice vote, and in the Senate, also by a voice vote, on October 1\textsuperscript{st} 1992.

Among the key provisions of the Act were the following: first, the wording concerning OPIC’s mission was amended from the original ‘friendly developing countries and areas’ to read ‘countries and areas, and countries in transition from non-market economies to market economies.’\textsuperscript{712} Second, the ceiling on per capita country incomes below which OPIC was to give projects preferential treatment was increased to $1,091 in 1989 dollars. While the higher per capita limit, above which OPIC was to restrict projects was increased to $4,734 in 1989 dollars. Third, the ceiling placed on the loan guarantee program was significantly expanded from $1.5 billion to $2.5 billion.\textsuperscript{713} Fourth, the two pilot programs established in 1988 were extended for four more years, and the geographical restrictions placed on the program that had previously limited equity investments to the Caribbean Basin and sub-Saharan African countries was removed. Fifth, OPIC received $7 million in appropriations. Sixth, OPIC was directed to report to Congress any project with a negative impact on U.S. employment, where previously the test was net. Seventh, OPIC was permitted to draw on income derived from Treasury holdings to fund its Direct Loan and Loan Guarantee programs for fiscal years 1993-1994. Eighth, OPIC was directed to maintain a loss reserve in accord with standard loan-loss reserve principles. Ninth and finally, OPIC was made subject to the U.S. criminal code with respect to the provision of false information by a borrower in connection with a loan application.

711 Opposition to the agency in Congress had not disappeared entirely, however, as was evident by the introduction of a bill to abolish OPIC in 1992. The ‘OPIC Abolition and Domestic Employment Opportunities Act’ [HR.4376] was sponsored by Representative Robert Andrews [D-NJ], and cosponsored by Jim Jontz [R-IN]. The bill proposed the immediate termination of the agency by the Secretary of Labour, under which all existing OPIC exposures would be transferred to the Office of Budget Management (OMB) and OPIC would be prohibited from issuing new insurance. In its place would be established a ‘Domestic Private Investment Corporation’ operating much the same as OPIC but only for domestic investments. Despite its limited support, and wide support for OPIC among the executive, the bill was not immediately dismissed however. Instead, it was referred to the House Committee on Banking, Finance and Urban Affairs, who in March 1992, referred it to the Subcommittee of Economic Stabilization, while in the House of Representatives it was referred to the Committee on Foreign Affairs, and the Subcommittee on International Economic Policy and Trade. Ultimately, consideration of the bill was postponed indefinitely.


713 Section 235(a)(2) of the Foreign Assistance Act of 1961.

Despite possessing formal operating authority through until 1996, a number of the agency’s suite of programs underwent significant expansion in 1994, as part of the Jobs Through Exports Enhancement Act, 1994 (HR.4950 and S.2438), as the complement to the earlier Jobs Through Exports Act 1992 (HR.4996). Sam Gejdenson [D-CT] first introduced the act in the House on August 12th 1994, before being referred to the House Committee on Foreign Affairs. The Bill was subsequently passed on a voice vote before being referred to the Senate by Senator Paul Sarbanes [D-MD]. The Senate Committee then attempted to modify the bill but this was subsequently defeated. The original bill was then presented to the President on October 10th, before being signed into law on October 22nd (Public Law No. 103-392). Among the key provisions of the Act with respect to OPIC were the following: first, OPIC’s maximum contingent liabilities arising out of investment insurance programs, and as authorized under the Foreign Assistance Act (1961) were increased from $9-12.5 billion. Second, the ceiling on the financing program was increased to $9.5 billion, while the maximum exposure on the loan guarantee program was increased from $2.5 to $5 billion. Third, and finally, the maximum financing available for a single project was increased from $50 million to $200 million, while the maximum insurance available for a single project was doubled from $100 million to $200 million.

OPIC Policy Amendments: State Initiatives versus Corporate Preferences

Thus far, the chapter has detailed the legislative history and the specific form of the amendments to the OPIC administered investment insurance and financing programs between 1981 and 1994. In contrast, this next section is concerned to assess the relative explanatory capacity of the two competing hypotheses with respect to the detailed changes to OPIC during this period. In so doing, the section will follow the

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714 Also passed at the same time was the Environmental Export Promotion Act [H.R. 3813].
715 For full text of the amendment providing for the expansion of OPIC, See http://thomas.loc.gov/cgi-bin/query/D?c103:1.:/temp/~c103Bh0LpK. Date Accessed 03.10.05.
same basic pattern as that of the previous chapter beginning with an analysis of the role of foreign investors and corporate America more broadly. As a precursor, it appears notable that the direction of the amendments, specifically the removal of earlier per capita income restrictions and the general growth of the program during this period, provide support for the importance of corporate preferences unlike the previous period where a number of amendments ran directly counter to foreign investor desires for enhanced investment protection.

The transformation of the OPIC investment insurance program from its original foreign-aid function to a foreign trade promotion function as was the effect of the 1981 amendments, specifically the removal of income ceilings so as to restore OPIC coverage to 17 of the 26 countries made ineligible by the 1978 amendments, was both supported by and in the interests of U.S. foreign investors. Furthermore, there is clear evidence that the particular amendments providing for the reorientation of the agency were strongly supported by high profile lobbying from influential business groups such as the Emergency Committee for American Trade, the Coalition for Employment Through Exports as well as the Business Council of the Americas. The latter, representing more than 200 U.S. foreign investor in Latin America.716 In light of the efforts of the Business Council of the Americas, the amendments exempting Caribbean countries from income restrictions of any kind agreed as part of the ‘Caribbean Basin Initiative’ are therefore noteworthy.

Equally, although there is evidence linking corporate pressure to specific policy amendments, a number of the changes enacted in 1981 appear as contrary to the interests of U.S. foreign investors. Most immediately, it is noteworthy that while the income ceiling was increased, the changes did not restore insurance availability to nine countries, including a number of rapidly emerging developing economies, such as Taiwan. Perhaps more significant was the amendment imposed on the agency requiring it to repay Treasury’s original start-up capital contribution to the agency no

716 The Council of the Americas is a Washington based business lobby group comprised of multinational investors, with a specific focus on Latin America. For an overview of the organization’s membership and advocacy efforts, See http://www.counciloftheamericas.org/coa/index.html. The Coalition for Employment Through Exports abroad was established in 1981 with the specific purpose of lobbying for enhanced state support for foreign investments and export promotion, focussing on OPIC, Ex-Im Bank as well the Trade Development Program, later renamed the Trade and Development Agency (TDA). See http://www.usaexport.org/.
later than 1985, amounting to several hundred million dollars. And although the precise effect on the cost of insurance premiums cannot be accurately calculated, such a provision can only have served to increase the cost of insurance as well as making the agency more risk-averse in its assessments so as to in combination limit the availability of insurance covers for projects designated as marginal. That this is the case, points to the continued significance of state interests in determining the precise form of amendments to the program.

In particular, the requirement to reimburse Treasury must be understood as motivated by fiscal imbalances driven by large tax cuts and sharp increases in military spending in the first year of the Reagan administration that in combination produced a record budget deficit in 1981 of $78 billion. Moreover, the Caribbean Basin Initiative is perhaps best explained by the new administration’s renunciation of the policy of détente with the Soviet Union that had characterized U.S. policy towards its superpower rival during the previous three administrations, dating back to 1972. That is, the decision to grant exemption status for Caribbean nations was consistent with Reagan’s more aggressive stance aimed at projecting U.S. power and influence among its neighbours as a deterrent to expanding Soviet influence in the region. In this respect, it must be concluded that the 1981 amendments provide support for both of the hypotheses outlined.

The 1985 amendments similarly provide support for each of the two explanations. Turning firstly to those amendments that provide support for the corporate preferences thesis, the most significant change enacted in 1985 in this regard concerns the decision to provide ‘business interruption’ coverage for U.S. investors. And although the agency has never had cause to issue such covers in any great volume the change was supported by pro-business lobby groups as it served to strengthen


718 The policy can be traced back to the 1972 signing of the Strategic Arms Limitation Treaty (SALT) by President Nixon with Brezhnev in Moscow in 1972. The policy was then continued by his two successors, Ford and Carter, resulting in the signing of SALT II in 1979 by President Carter.

safeguards against ‘creeping expropriation’ leading to temporary disruptions to production rather than a permanent cessation of activities as is the standard required to make claims under the expropriation covers. In this respect, the new product served as a welcome addition to the suite of insurance covers offered U.S. foreign investors.

Against this, a number of the 1985 amendments are difficult to reconcile with corporate interests. Foremost in this regard concerns the imposition of strengthened employment criteria requiring the agency to refuse to insure projects resulting in a net job loss in the U.S., and second, for countries deemed not to have met internationally recognized labour standards as prescribed by the ILO. To this end, although the evidence suggests that the actual effect on OPIC’s capacity to insure U.S. investors was limited; the new arrangements, however loosely enforced, must be understood as a defeat for foreign investor interests given that the motivation for cross-border expansion in many cases is underpinned by labour cost differentials, resulting in part from the absence of such safeguards and the right to association.720 The second set of changes to this effect concern the imposition of the new environmental regulations requiring the agency to refuse insurance for projects deemed to pose an environmental hazard. And although, given the laxity with which the ‘rule’ was interpreted the actual effects were limited, the same argument holds as for the labour regulations insofar as in many cases foreign investment is motivated by less stringent environmental regulations.

The 1988 amendments also provide mixed evidence. In terms of the changes in support of corporate preferences, one such amendment in particular appears as significant. It concerns the provision enabling OPIC to insure existing investments as well as new foreign projects. To this end, the amendment was on the surface highly significant, and one may assume strongly supported by investors, many of whom were faced with a deteriorating political environment precipitated by the still worsening LDC debt-crisis afflicting many of the agency’s key markets. Somewhat strangely, however, few investors appear to have availed themselves of insurance so as to cast doubt as to the impetus behind the shift, as had it originated from corporate pressure.

720 Although the number of countries falling foul of the new arrangements judging by the number of countries subsequently ruled ineligible for OPIC insurance was minimal the affects were not insignificant judging by the fact that U.S. investors in Indonesia were temporarily denied coverage.
one may assume the result would have been a rise in the volume of insurance issued yet this was not the case.

Moreover, a number of the 1988 amendments suggest themselves as inimicable with corporate interests. Of particular note in this respect concerns the imposition once again of strengthened safeguards against projects resulting in any job loss (in the U.S.) and the requirement that OPIC only issue insurance to projects located in countries with ‘investment practices’ consistent with those of the U.S.. Equally, however, the impact of these changes on the capacity of OPIC to insure investors was limited. In this first instance, this was so because ‘U.S. ‘investment practices’ were never clarified to any meaningful extent. In the second instance, this was so because information regarding the employment impact of projects was supplied by prospective investors absent any independent verification, a fact that did not escape the attention of critics of the program in Congress.

The 1992 amendments provide further evidence in support of the importance of corporate preferences. Critical in this respect was the decision to increase the agency’s exposure ceiling on the loan guarantee program from $2.5 to $3.5 billion. The second change to the OPIC program in this regard concerned the expansion of the ‘equity investment funds’ to include geographical regions other than sub-Saharan Africa and the Caribbean. Finally, and to similar effect concerned the decision to amend the wording of the agency’s mandate to enable it to issue insurance to U.S. investors in the former Eastern European countries thereby increasing the number of eligible countries by a significant margin. Equally, it must be acknowledged that the decision was concordant with broader foreign policy goals in the wake of the end of the Cold War characterized by the general though still uncertain embrace of the formerly Communist nations of Eastern Europe, including after special hearings in the Senate, Russia itself.

Of all the changes to the OPIC program during the review period, it is perhaps those enacted in 1994 pursuant to the ‘Jobs Through Exports Enhancement Act’ that provide the strongest evidence in support of the significance of corporate interests in the formulation of OPIC policy. Of immediate note in this regard concerns the one-off expansion of the agency’s per project and aggregate insurance and financing limits,
the impact of which was clearly in the interests of U.S. foreign investors, but particularly prospective private infrastructure operators. More importantly, from the perspective of substantiating the hypothesis there is considerable evidence to show that the changes were vocally supported by corporate lobby groups. This included the appropriately entitled ‘Coalition for Employment Through Exports’ but also support from individual foreign investors, such as Edison Mission and Enron among others.\(^\text{721}\)

In addition to power producers, support was also forthcoming from engineering contractors and capital equipment suppliers such as Bechtel and General Electric respectively for whom the proposed changes offered significant new business opportunities. Apart from direct lobbying, each of the aforementioned firms also benefited from an unusually close and indeed, productive working relationship with then Commerce Secretary and Democratic House Leader, Ron Brown, in many cases accompanying him as part of official trade delegations. In this respect, it is notable that the recommendation to expand the program through the 1994 Act originated with the Trade Promotion Coordinating Committee (TPCC) chaired by Brown.\(^\text{722}\)

To conclude, in general the direction of the amendments to the insurance program from 1981-1994 is consistent with corporate preferences for increased support for direct investments. Among the key changes in this respect was the introduction of new insurance products such as Business Interruption insurance, as well as general increases in per project and aggregate insurance and financing limits. Second, the

\(^{721}\) Apart from the obvious fact that Enron was the single largest recipient of both OPIC and Ex-Im Bank support during this period, one does not need to look very hard to substantiate the claim that Enron enjoyed special access to OPIC officials. For example, and indicative of the close working relationship, immediately upon being appointed as the President of OPIC in 1997, Munoz invited Enron CEO, Ken Lay to an OPIC staff-retreat so that he might explain the types of support that a company such as his was looking for from OPIC. Speaking of Enron’s aggressive lobbying, one former OPIC employee was quoted as saying, ‘The Enron lobbyist visited OPIC so often that workers joked that he had moved into Himberg’s office . . .’. See [http://www.washingtơnpost.com/wp-dyn/articles/A37365-2002May5.html](http://www.washingtönpost.com/wp-dyn/articles/A37365-2002May5.html).

\(^{722}\) The working relationship was close enough to prompt allegations of corruption. In particular it was alleged that following the Democratic loss to the Newt Gringich led Republicans in the 1994 mid-term elections wherein the Republicans took control of the House, Brown effectively accepted corporate donations to fund Democratic campaigns in return for ‘seats’ on his much vaunted trade missions. While the allegations remain unsubstantiated, the working relationship did cause consternation within the U.S. government sufficient to warrant an investigation into the allegations by the Justice Department after Brown’s death, the findings of which were never made public. Ron Brown would later die in a mysterious plane crash on another trade mission to Croatia, this time lobbying for the conclusion of an IPP contract on behalf of Enron with President Tudjman. Following Brown’s death, it was later revealed through secretly taped meetings that Tudjman contemplated the deal as a means to increase his influence within the White House in the hope of avoiding his earlier indictment for war crimes by the International Criminal Court at The Hague.
evidence has also shown that OPIC and U.S. officials more generally undertook to
tailor the suite of programs to meet the evolving needs of U.S. investors where
possible, an assertion that is perhaps best underscored by the decision to begin
supporting project financed infrastructure investments in LDCs as was the product of
the 1994 amendments. Moreover, the empirical evidence makes clear that in
comparison with the previous review period, far fewer of the amendments from 1981-
1994 were demonstrably antithetical to U.S. foreign investor interests.

Against this, although corporate actors as an interest group enjoyed privileged access
to U.S. policy-makers, theirs was not the only voice with an interest in the form of the
amendments to the program. In particular, the evidence makes clear that organized
labour led by the politically perceptive and well-connected AFL-CIO was also
prominent in the re-authorization hearings, resulting in the addition of further
restrictions on the program designed to protect against negative employment effects
for the U.S. domestic economy. The second interest group of note in this respect
concerned an emergent environmental lobby group that was by the end of the period
increasingly well organized and funded, resulting in the imposition of strengthened
environmental restrictions on OPIC insurance availability from 1985 onwards.

Moreover, despite the success of corporate lobbying it remains the case, as in the
previous period, that the capacity of corporate America to influence the policy process
was weakened by dissenting voices. Thus, in many instances support for particular
proposals was matched by opposition, particularly from the so-called ‘rust-belt’
industries such as steel and the big three auto-manufacturers, aimed at protecting the
competitiveness of domestic producers against low-cost foreign competitors. And
although the protectionist sentiment evident within the U.S. business establishment
decreased from the mid-1980s concomitant with efforts to depreciate the dollar so as to
restore export competitiveness, it remains the case that as far as support for OPIC was
concerned, corporate America was a divided constituency. It must therefore be

723 It is this protectionist sentiment for example that led to the voluntary agreement reached between
the U.S. and Japan limiting the imports of Japanese automobiles to the United States. Similar, agreements
were later concluded to include steel production etc.

724 Protectionist sentiment was spurred in part by the over-valued dollar as ‘Reaganomics’ began to
bite. For example, the value of the dollar versus the Yen had climbed to a record high of 250 by 1985.
It declined however, following coordinated intervention by the G5 (Germany, Japan, United Kingdom,
France and the United States) pursuant to the Plaza Accord in September 1985. Indeed, so successful
concluded that no matter how significant corporate preferences were in the minds of policy-makers, ultimately the changes observed resulted from state policy initiatives consistent with broader foreign policy goals.

Once again, however, the refutation of corporate preferences in favour of state initiatives as the most likely explanation for the observed shifts in the policy and practice of OPIC should not be understood as part of coherent anti-expropriation policy. The reason for this, as in the previous period, is that the U.S. did not pursue a clear and distinct anti-expropriation policy. That is, although U.S. policy-making in this regard was more consistent, centred on efforts to strengthen the treaty framework for direct investment in LDCs through the promulgation of BITs from 1982 onwards, U.S. efforts to this end, like the transformation of OPIC from a foreign-aid to a foreign trade promotion function, must be understood as but one small part of an intensified and state initiated drive to expand markets for U.S. exports and investment capital, i.e. a more aggressive foreign trade and investment policy rather than a distinct anti-expropriation policy.

To elaborate and in order to chart the shift in U.S. foreign trade and investment policy as well as the manner in which it informed the OPIC administered insurance program, the next section will chart the major initiatives undertaken by the U.S. government during the period from 1981-1994. The motivation for which was to restore U.S. corporate competitiveness beginning with the decision to reorient the agency away from its original foreign-aid function to that of trade and investment promotion in 1981.

**OPIC: State Initiatives and Foreign Trade and Investment Promotion Policy Reform**

The 1981 OPIC amendments that transformed the agency’s primary function from that of adjunct to the foreign-aid program to a foreign trade and investment promotion role were driven by growing concerns within the executive and Congress (bipartisan) that a second summit to discuss coordination of monetary and fiscal policies was convened in 1987, the Louvre Accord and attended by the G7 (G5 plus Italy and Canada) wherein it was announced that dollar parity had been restored and that further interventions would only take place to maintain currency stability.
regarding declining U.S. competitiveness. In the initial instance, the disquiet can be traced back to the record 1972 balance of payments deficit. Despite rebounding the following year, fears that the imbalance was structural rather than cyclical proved all too prescient as the deficit continued to grow throughout the decade.\(^\text{725}\) The mounting deficits fuelled long-held fears that the United States was losing its competitive edge in the face of intensified competition for markets as first, European and Japanese and then low-cost LDC producers (particularly the newly industrializing countries of S.E. Asia, dubbed the ‘Asian tigers’) began to expand their market share at the expense of U.S. producers.

Of course, U.S. foreign trade policy had never been entirely sacrificed to national security considerations as evidenced by the passage of the 1962 Trade Expansion Act and the 1974 Trade Act, the latter of which established Section 301, which remains to this day the primary mechanism for the United States to take retaliatory action against countries held to discriminate against U.S. exports.\(^\text{726}\) These initial efforts to reinvigorate U.S. exports were later given added impetus by the record 1978 balance of payments deficit ($33 billion), which prompted the renewed interest in export promotion by President Carter, the primary vehicle for which was Re-Org. No. 3.\(^\text{727}\)

Key in this regard, and indicative of a then still nascent shift in U.S. foreign trade policy were the provisions providing for the upgrading of the Office of the U.S. Trade Representative (USTR) to Cabinet status, and the reconstitution and expansion of the then defunct President’s Export Council (PEC), as well as the directive to the USTR and the State Department to begin work on the model text for future U.S. bilateral investment treaties.\(^\text{728}\)

The changes introduced as part of the reorganization of executive functions can, with the benefit of hindsight, be seen to have laid the foundations for the conversion of the


\(^\text{726}\) For details of the 1974 Trade Act, See Public Law No. 93-618, and for the earlier Kennedy administration 1962 Trade Expansion Act, which established the Trade and Development Program (TDP) See Public Law No. 87-794.


\(^\text{728}\) The President’s Export Council (PEC) was first established by President Nixon in 1973 in response to the record balance of payments deficit the previous year. The Council was however, abandoned by his successor, Gerald Ford. The PEC was then reconstituted and expanded by Carter to include 20 government officials, drawn in equal measure from the legislative branch and the executive.
agency from a foreign-aid to trade role as was undertaken by President Reagan, who
unlike his immediate predecessor, appears to have seen no contradiction between
efforts to increase U.S. exports to LDCs and the latter’s development needs. The tenor
of the changes to U.S. foreign policy vis-à-vis the developing world dubbed ‘aid
through trade’ were first spelled out by President Reagan at the Cancun Summit on
International Cooperation and Development in January 1981.729

The neat fit, between the dual constraints of trade and fiscal imbalances and OPIC,
which operated at no cost to Treasury, did not escape the attention of the newly
reconstituted President’s Export Council. To this end, the Council in their own words,
subsequently ‘made recommendations that ultimately resulted in passage of a bill that
gave the Office of Private Investment Corporation (OPIC) a clear trade mandate and
eased restrictions on the operation of OPIC programs in upper-income countries.’730
For the Reagan administration, the 1981 OPIC amendments as part of a reoriented
U.S. trade and investment policy were, however, merely the precursor to wider efforts
resulting the following year in the passage of the Export Trading Company Act
(1982).731 That same year the U.S. also concluded its first BITs with Panama and
Egypt respectively.732 Renewed U.S. efforts to expand markets in LDCs for U.S.
exports and investment capital did not end here, however. That same year the Trade
and Development Program, (TDP) was assigned separate funding, indicative of its
increased status, while the following year saw the passage of the ‘Trade Expansion
Act’ (1983) which restored the policy of tied-aid spending, which had been abolished
by Nixon in 1970 on the grounds that it risked broader U.S. foreign policy goals vis-à-

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729 The tenor of Reagan’s speech premised on his refusal to allow U.S. trade policy vis-à-vis LDCs to
be determined by the Cold War is demonstrated by the following, included in his Cancun address to the
G77, where he proclaimed that ‘Development was not a question of "East versus West" but of "sense
versus nonsense." See Peter F. Schaefer, “Seven Steps to Improve U.S. Bilateral Aid”, Backgrounder
731 The purpose of the Export Trading Act (Public Law No. 97-290) was ‘To encourage exports by
facilitating the formation and operation of export trading company’s, export associations and the
expansion of export trade services generally.’ See http://www.trade.gov/td/oetca/TitleIII.htm.
732 The United States was in this respect as in many aspects of state-led export promotion a late starter,
evidenced by the fact that European countries had long viewed such treaties as central to the expansion
of national capitals to LDCs, beginning with the first such BIT concluded between Germany and
Pakistan in 1959. To this end, it is notable that responsibility for the drafting of U.S. BITs had since
1979 been removed from the State Department’s remit and handed to the USTR under the aegis of the
Commerce Department, thereby signalling in no uncertain terms that no longer would the U.S. sacrifice
economic interests for national security as had, according to its critics, been the tendency if not the
official policy of the State Department throughout the Cold War.
vis the third-world. Finally, to complete the overhaul, Reagan established the President’s ‘Taskforce on International Private Enterprise’ also in 1983, with a mandate to investigate means to increase the role of the private sector in formulating U.S. foreign-aid and trade policy. The findings of the taskforce would later inform U.S. policies linking the provision of IMF structural-adjustment loans (ESAPs) to mandatory liberalization of trade and investment regimes. To this end, the transformation of OPIC, alongside the growing number of bills and treaties aimed at expanding U.S. exports and strengthening the standards of protection afforded U.S. foreign investors in LDCs signalled a clear shift in U.S. trade and investment policy towards the developing world. It did so because previously such overt state support for U.S. business had been resisted for fear of alienating LDC governments.

The 1985 and 1988 amendments to the OPIC suite of programs, specifically the introduction of Business Interruption covers and the provisions enabling OPIC to insure existing investments, though not radical in their effect must also be understood in the context of heightened concerns regarding U.S. corporate competitiveness, as predominated during this period. What had in the early part of the decade begun as a trickle, however, soon became a torrent of legislation aimed at restoring U.S. economic, and therefore, corporate competitiveness. First off the rank in this regard was the ‘Export Administration Amendments Act’ (1985), followed by a Bill to ‘Enhance the Competitiveness of American Industry.’ That same year, President Reagan created the Council on Economic Policy (CEP). Moreover, although faced with mounting corporate and Congressional displeasure at the overvalued exchange rate, as Cohen notes, the priorities were clear insofar as ‘[T]hrough early summer 1986, approximately two-thirds of the Council’s meetings were related to foreign trade matters.’

Despite these efforts, the balance of payments deficit continued to widen, reaching a record $159 billion in 1987. As a result, additional bills were subsequently introduced, including the ‘Trade and Export Enhancement Act’ (1987) and a second,

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733 Tied-aid refers to the practice of making foreign-aid grants and loans conditional on using the monies received to purchase American goods and services.
734 To view the taskforce’s findings See ‘Findings of the President’s Taskforce on International Private Enterprise’, December 1984 (PN AAR-668).
‘Bill to Enhance the Competitiveness of American Industry and Other Purposes’ (1987). Moreover, that same year and in an effort to emulate the traditional Japanese model of government business relations (dubbed ‘Japan Inc.’), a bill was introduced to establish a ‘Department of Trade,’ modelled on the Ministry of International Trade and Industry in Japan (MITI).736 Finally, lest U.S. policy concerns still be in doubt, that same year, Reagan established the ‘Taskforce on Industrial Competitiveness’ while Congress formed the ‘Council on Economic Competitiveness.’

Eventually the welter of pro-competitiveness related legislation was streamlined into the appropriately entitled ‘Omnibus Trade and Competitiveness Act’ (1988).737 The Act signalled U.S. intentions to no longer sacrifice economic interests to national security considerations. Foremost in this regard was the establishment of ‘Super 301’ (‘the crowbar’), requiring the USTR to maintain ‘watch-lists’ of countries violating free-trade principles.738 In addition, the Act also granted the President the right to negotiate trade and investment treaties for a limited period (through until December 1993), absent of Congressional authorization, dubbed the ‘fast-track authority.’739 Finally, also buried within the voluminous Act were provisions providing for the transfer of administrative responsibility for OPIC from the IDCA to the USTR. In this respect, the legislation removed the last vestiges of the agency’s original foreign-aid role, whilst also leaving the ill-fated IDCA existing only in name.

Perhaps the most telling piece of evidence in support of the theorized shift in the role of the OPIC insurance program from foreign-aid to foreign trade promotion concerns Congressional-led opposition to the proposed establishment of the World Bank investment insurer, the Multilateral Guarantee Agency (MIGA). To elaborate, the first such proposals to establish a multilateral investment insurance agency under the

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736 The Bill, H.R. 1338 ‘A Bill to establish a Department of Trade’ was introduced in the House by Robert E. Wise Jr.[WV-3] (3/12/1987).
737 The 1988 Act (public law No. 100 - 418) ran to more than 1,000 pages.
738 The manner in which politics and power informed the naming of Brazil and India on the list is indicated by the fact that Section 301 was, albeit never articulated formally, aimed squarely at Japan. Placing the second largest economy in the world, and the U.S.’s largest trading partner on the list first, however, was felt to be inappropriate, with the result that Brazil and India were offered up. Japan would subsequently be added to the list.
739 The fast-track legislation gave the USTR the necessary authority to begin, first, the U.S.-Canada free-trade agreement, concluded in 1989, and which would later form the basis of the North American Free Trade Agreement, as well as the Uruguay Round of Trade talks, which themselves culminated in the signing of the Trade Related Investment Measures (TRIMs) and Trade Related Intellectual Property Rights agreements (TRIPS) also in January 1994.
guidance of the World Bank were floated in the 1960s. To this end, the U.S. expended considerable diplomatic capital in its efforts to establish an International Investment Insurance Agency (IIIA). These efforts were thwarted, however, in the face of concerted opposition from LDCs.\(^{740}\)

When the proposals were floated for a second time during the early 1980s, U.S. policy had evidently shifted. Instead of supporting the agency, the U.S. blocked proposals so that for a time it looked as though MIGA might be established without U.S. participation.\(^{741}\) Further, that the issue was tied to shifting U.S. foreign trade and investment policy is evidenced by the fact that the Congressional appropriations for MIGA were eventually rolled into the Omnibus Trade and Competitiveness Act (1988).\(^{742}\) It is for this reason that while the Articles of Agreement providing for the establishment of MIGA were signed in 1985, the agency did not begin issuing insurance until 1988 following the passage of the Act that same year. And although opposition to the agency can be understood as part and parcel of Congressional criticism of the World Bank Group during this period, more narrowly, such opposition can only be understood if one considers the changing purpose of the OPIC program. In particular, when the policy rationale of the insurance program was foreign-aid then a multilateral insurer made perfect sense. Once the goals of the program shifted, however, concomitant with shifting U.S. foreign trade and investment policy then a multilateral insurer made no sense, as were MIGA to replicate OPIC’s role, then this


\(^{741}\) Indicative of widespread opposition to MIGA from within the legislative branch was the Bill entitled ‘A concurrent resolution to express Congresses opposition to participation of the United States in the Multilateral Investment Guarantee Agency.’ Sponsored by Senator Pell Claiborne [D-RI] in the Senate (dated 3/12/1987), and co-sponsored by 209 Republican Senators.

\(^{742}\) To follow the progress of the original bill, and to see its being tied up with the competitiveness concerns which dominated U.S. policy during this period, See in the Senate, S.1406 ‘A Bill for the creation of an Office of Multilateral Development Bank Procurement Department within the Department of Treasury to Authorize the participation of the United States in the Multilateral Investment Guarantee Agency.’ (dated 23/06/1987). The initial bill was then rolled into S.1420 introduced by Senator, Robert Byrd, ‘A Bill to Authorize Negotiation of Reciprocal Trade Agreements and to Strengthen United States Trade laws and for Other Purposes’ (dated 24/06/1987). This Bill was then incorporated into H.R. 3 ‘A bill to Enhance the Competitiveness of American Industry and Other Purposes’ Sponsor, Richard A. Gephardt (dated 01.07.1987). Eventually this bill was rolled into H.R. 4848, ‘A bill to enhance the Competitiveness of American Industry’ that became Public Law. No. 100-418, on 23/8/1988.
could only reduce any competitive advantage that might accrue to U.S. foreign investors.

The 1992 and 1994 OPIC amendments must also be understood in the context of state initiated efforts to expand markets for U.S. exports and investment capital to LDCs, albeit in this instance released from the strictures of the Cold War, following the sudden collapse of its former super-power rival in 1991. Even before this, however, the newly elected Bush administration had made clear that the increased emphasis given to trade and investment issues by the previous administration would only be strengthened under its watch. To this end, the new Deputy Secretary of State proclaimed ‘we as a government and as a society are going to have to acknowledge that our economic health and our ability to trade competitively on the world market may be the single most important component of our national security as we move into the next century.’\textsuperscript{743} Finally, should further confirmation of the now blurred hierarchy of security and economic issues be needed it was surely provided by his acknowledgement that ‘In the past, this Department [State] has been perceived, at times correctly so, too inclined to let economic interests play second fiddle to geopolitics. That era has passed.’\textsuperscript{744}

Among the first task undertaken by the Bush administration was the establishment of a $500 million tied-aid pool, with the unambiguous objective in the words of the Export Council of advancing ‘U.S. development and commercial interests.’\textsuperscript{745} The following year the Trade Promotion Coordinating Committee (TPCC) was also established. These reforms were then codified in the ‘Jobs Through Exports Act’ (1992), providing for the establishment of government funded ‘export assistance centres’ and the replacement of the TDP with the Trade and Development Agency (TDA).\textsuperscript{746} Finally, also included in Section III of the 1992 act, entitled ‘Aid, Trade and Competitiveness’ was a provision directing AID to establish a ‘Capital Projects


\textsuperscript{744} International Business: Foundations of National Strength’ Address by Lawrence S. Eagleburger. Parenthesis added.

\textsuperscript{745} President’s Export Council.

\textsuperscript{746} Jobs Through Exports Act of 1992, [Public Law No. 102-549]
Office’ with a mandate to ‘develop a program that focuses on developmentally sound capital projects for basic infrastructure.’

Before the fruits of these labours could be reaped, however, and suffering the worst recession since the early 1980s, U.S. voters elected a new President, William Clinton early in 1993. Unencumbered by Cold War Realpolitik vis-a-vis the developing world, the priority for the Clinton administration was clear: ‘[I]n the post-Cold War world our national security rests more than ever on our economic strength. Our foreign and commercial policies must be integrated if we are to accomplish our objective at home and abroad.’ Indicative of the new administration’s priorities, among the first tasks performed by Clinton was the establishment of the National Economic Council (NEC) early in 1993, reporting directly to the President, and with an equal status to the National Security Council (NSC). Second, Clinton also took steps to endow the TPCC with additional authority by increasing membership of the committee, to include the NEC and the NSC.

The following year, the ‘Aid for Trade’ bill was introduced in the Senate (S.722). In response, Congress directed the Congressional Research Service to investigate the proposed amendments. The focus of the debate centred on proposals to increase funding for the TDA from the previous year’s allocation of $50 million to $1 billion, so as to facilitate the financing of capital projects in LDCs, and ultimately, the expansion of U.S. capital goods exports. The debate drew heavily on a report

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748 The importance of the economy in the 1992 elections was made clear by the phrase ‘it’s the economy stupid’ that would come to characterize the Clinton Presidency. The phrase is popularly attributed to Democratic strategist, James Carville.


750 The significance of the move and the upgrading of the importance of economic issues by the Clinton administration is underscored according to I.M. Destler, by the fact that the creation of the NEC was the most significant administrative change made by any President to executive functions since Nixon ordered the transformation of the NSC under Kissinger. See Ian M. Destler, The National Economic Council: A Work in Progress, Policy Analyses in International Economics 46, Institute for International Economics, Washington D.C., November, 1996).


published earlier that year, ‘The Economics of Export Promotion.’ Among the key points in the report was the finding that in comparison with Germany, France, the United Kingdom, and especially Japan, U.S. export promotion spending in the area of capital goods was far below that of its industrial competitors.

Eventually after significant deliberation, the proposals to channel the new infrastructure related tied-aid through the TDA were defeated owing to widespread fears that the agency was ill equipped to handle the dramatic increase in its operating budget. At the same time, Congress rejected the provisions of the 1992 ‘Jobs Through Exports Act’ providing for the establishment of a Capital Fund within AID. Frustrated with the apparent lack of progress, the NEC then directed the TPCC to investigate proposals to channel the ‘capital projects initiative’ through OPIC and Ex-Im Bank. The subsequent report duly recommended the agency’s ‘maximum contingent liability’ with respect to the insurance and financing be increased to enable OPIC and Ex-Im Bank to participate in capital projects (infrastructure) in LDCs.

In order to implement the proposal, a bill was introduced in August 1994 entitled the ‘Jobs Through Export Enhancement Act’, providing for the expansion of OPIC (Section II), and the re-authorization of the agency through until 1996. With the support of the President and the NEC, the bill was passed with minimal opposition, ready for the President’s visit to Jakarta in December 1994, to speak at the APEC Conference. His speech to the assembled delegates was, however, merely the icing on the cake to earlier negotiations, the product of which, and the reason for Clinton’s appearance, was the signing of the flagship Paiton I project and CalEnergy’s ill-fated Dieng and Patuha projects along with more than a dozen other IPP deals supported by

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753 See Wayne Morrison, ‘The Economics of Export Promotion’, prepared by the Congressional Research Service, Library of Congress, Report 93-330, March 9th, 1993. The report find that of the total development assistance spending undertaken by Germany, Japan and the United Kingdom, 32%, 39% and 31% respectively was devoted to aid for foreign infrastructure projects versus 8% for the United States foreign-aid program. The report also cited the fact that where from 1946-61 infrastructure related World Bank lending to LDCs comprised 75% of total loans by 1985 this figure had fallen to 32%.


755 The Bill sponsored by Republican Sam Gejdenson [D-CT] became Public Law No. 103-392 as 10th Nov. 1994.
OPIC and Ex-Im’s expanded insurance and financing capabilities.756 The following year representatives from OPIC, Ex-Im Bank, Enron, as well as the Commerce Secretary himself would travel to Delhi to announce the signing of phase I of the Dabhol project underpinned by OPIC and Ex-Im insurance and financing of almost $1 billion.757

In summary, the analysis of the role of the two competing hypotheses reveals that changes to the OPIC program from 1981-1994 originated from state-led policy initiatives rather than as a response to corporate pressure in accord with shifting strategies of adaptation, as is the core postulate of the corporate preferences hypothesis. Once again, however, these changes should not be thought of as part of U.S. anti-expropriation policy as a distinct sub-field of U.S. foreign economic policymaking. Instead, changes to OPIC policy and practice originated with a state-led shift in U.S. foreign trade and investment policy, the characteristic feature of which was the aggressive pursuit of markets for U.S. exporters and investment capital underpinned by a widely held perception of declining U.S. corporate competitiveness.

In the initial instance, the shift may be traced back to the Reagan administration’s transformation of OPIC from its original foreign-aid function to an unambiguous trade promotion function. This continued through the Bush administration but found its fullest expression under President Clinton in the early 1990s, with the decision to expand the agency’s programs to facilitate support for U.S. infrastructure investors and capital goods exporters. In this manner, shifting foreign trade and investment policy reflected deeper shifts in the understanding of the national interest that was by the end of the period, but even before the conclusion of the Cold War, increasingly difficult to distinguish from the pursuit of economic competitiveness. In this manner, the traditional hierarchy of foreign policy goals became increasingly blurred.

756 According to testimony before the House of Rep. by CalEnergy CEO, David Sokol, President Clinton personally congratulated him on winning the deals whilst at the signing ceremony.  
757 Lest the impetus behind the shift in OPIC policy remain unclear, any doubts must surely be dispelled by the comments of the then Vice-President of OPIC who in seeking to justify the agency’s support of the Dabhol project was quoted as stating before a House Congressional Committee in 1995, ‘The Enron and AES projects combined will generate nearly $1 billion in U.S. exports’ See http://www.cpa-watch.org/. Commenting on the alleged pressure to get the Indonesian deals done, Dianne Rudo of the EXIM Bank, responded, ‘The bottom line from our point of view was that we were supporting 25 plus U.S. exporters.’ ‘How U.S. Companies Electrified Indonesia’ Wall Street Journal, Dec. 23rd, 1998.
In asserting the centrality of state policy initiatives, the intention is not, however, to suggest that the preferences of U.S. foreign investors were somehow unimportant in the minds of state officials or that they were simply another domestic interest group. Moreover, as U.S. trade and investment policy shifted, the needs of corporate America loomed larger than ever in U.S. foreign economic policy-making, but particularly after the collapse of Communism in Eastern Europe in 1989. The effect of which was to release the U.S. from the constraints of Cold War foreign policy-making, wherein U.S. economic interests vis-à-vis LDCs were typically sacrificed to the pursuit of national security goals. As a result, U.S. policy was increasingly characterised by the shared goal of multinational capital accumulation. That this was the case, however, should not deflect attention from the fact that where the interests of the state and foreign investors diverged, the interests of the state were invariably preeminent over those of corporate America.

Conclusions

In conclusion, the empirical evidence has shown that state initiatives provide the best explanation of the observed shift in the functions of the OPIC administered investment insurance program during the period from 1981-1994. In this regard, U.S. policy-makers pursued a consistent albeit evolving conception of the national interest in response to intensified competition for markets, the defining feature of which was an upgrading of economic interests to the level of national security. Moreover, while the shift was more apparent after 1989, concomitant with the end of the Cold War, the evidence makes clear that U.S. policy priorities towards the developing world changed even before this, dating back to the early 1980s.

The expansion of OPIC and its reorientation towards a trade and investment promotion function from its original rationale as part of the U.S. foreign-aid program must therefore be understood as part of broader state-led efforts to reverse the concessions made to LDCs during the Cold War, wherein the U.S. permitted, sometimes officially sometimes not, discriminatory practices against U.S. exporters and investors for fear of alienating host governments. In this respect, U.S. policy in
linking IMF debt rescheduling to the liberalization of markets for U.S. producers, efforts to strengthen the treaty framework for investors through BITs and so on must be understood as the external face of internal restructuring aimed at restoring U.S. corporate competitiveness and with it corporate profitability.

That such moves were undertaken in U.S. national interests cannot be doubted. Equally, it must be acknowledged that there was some truth in the oft-heard phrase on Capitol Hill that intensified state support for U.S. exporters and investors served merely to ‘level the playing field’ for U.S. foreign investors in comparison with their European and Japanese rivals. In this respect, the changes to the OPIC suite of programs characterized by increased state support for U.S. investors and exporters can legitimately be interpreted as but one facet of a more fundamental shift wherein the United States for want of a more apt phrase became ‘more like the rest.’ That is, the U.S. rejected its ‘special mission’ to focus squarely on the pursuit of economic interests. In this regard, the analysis reveals that if the rapid expansion of FDI in LDCs during the 1990s was central to economic globalization, then economic globalization was very much the by-product of the pursuit of U.S. national interests as the world’s only remaining super-power sought to throw off the shackles of the Cold War in its relations with the developing world.
Chapter 7: OPIC: Globalizing the Fifth Amendment

Four tasks remain to complete the research for this the seventh and final chapter of the study. First, the chapter will re-cap the findings as concern parts ‘A’ and ‘B’ of the research respectively. To begin, the chapter will therefore consider the evidence from the two case studies regarding the role of OPIC in underwriting the rules of the game, and thus the expansion of U.S. infrastructure investors to the developing world. This will be followed by a review of the findings as concern the policy drivers underpinning the long-term evolution of the OPIC administered insurance program.

The second task for the chapter will then be to draw together the findings of the research so that we might consider the relationship between OPIC policy and practice and more broadly U.S. foreign policy-making and contemporary institutional rules and norms (international law norms of expropriation and compensation). To this end, it will be argued that the actions of OPIC in paying seven claims to U.S. investors in the two disputes, so as to more firmly establish breach of regulatory contract as a violation of international law, serve to move international law norms toward a uniquely American conception of the rights and duties of private property vis-à-vis the state as embodied in the U.S. legal doctrine of regulatory taking. In this manner, shifting international law norms of expropriation and compensation as concern breach of regulatory contracts and second, the transformation of infrastructure services in LDCs bear the imprimatur not only of U.S. power and interests but a specifically American conception of private property and contract rights. As such, it is clear that while modes of state protection of foreign capital and of dispute settlement continue to evolve amidst economic globalization, U.S. power remains of central import in the new legal order.

The penultimate task will then be to consider the public policy implications of the research findings. In the first instance, the focus will be the implications for OPIC if the agency is to continue in its new more prominent role in the resolution of investor-state disputes. This will be followed by an analysis of the findings for U.S. foreign policy-makers, including as concerns the thrust of contemporary U.S. anti-expropriation policy as evidenced by the payment of insurance claims to U.S. infrastructure investors by OPIC. Attention will then turn to consider the implications
of the research findings for countries playing host to insured infrastructure investors. The fourth and final task will be to consider the future of the current practice of insuring and financing infrastructure investors against political risks.

Part ‘A’: OPIC as an Instrument of State Power and Interests in the ‘New’ Legal Order

As this thesis has shown, property rules governing foreign direct investment (FDI) have long been the subject of often-intense struggles between capital-exporting and importing nations. In this respect, contemporary efforts to promulgate legal rules governing direct investment in the form of BITs should be understood not as a radical disjuncture with previous practice so much as the latest in a long line of efforts undertaken by states to codify the rights and duties of foreign investors and host states. While the latest developments thus exhibit a degree of historical continuity, it is also the case that contemporary changes in the structure of the world economy associated with economic globalization have rendered the terrain over which the contest occurs more opaque than ever before.

For example, the traditional lines of division between capital-importing and exporting states are less clear-cut than was the case for much of the post war period. Foremost, in this regard concerns the erstwhile transformation of the regime leader, so that today the U.S. is both the single largest source and recipient of FDI. Similarly, China, long the favourite destination for foreign investors in the developing world, is itself now a source of FDI in LDCs. The blurring of conceptual and analytical boundaries resulting from contemporary changes in the organization of the world economy is not confined to divisions among states, however. In particular, the emergence of decentralized or transnational production networks, increasing as it does the proportion of economic exchange organized as intra-firm trade, serve to blur the boundaries between international trade and investment.

These changes, in many respects, are merely the tip of the iceberg, however. Indeed, some property theorists contend that new modes of organizing economic activity
demand that we reconceptualize what is meant by property.\textsuperscript{758} In particular, the rise of what is dubbed the knowledge economy, wherein tangible and intangible property rights are disaggregated, is held to undermine traditional notions of private property as ‘norms of “airtight” exclusionary rights. Property being better conceptualized as a kind of contractual arrangement.\textsuperscript{759}

The blurring of conceptual boundaries in the current period associated with economic globalization has not been confined to the economic sphere, however. To this end, the legalization of dispute settlement as but one facet of the globalization of law serves in turn to blur the boundaries between national and transnational jurisdiction, while the provision of access to foreign investors to initiate legal proceedings against host states, serves to muddy the conceptual distinction between states and investors and subjects and objects of international law respectively.

Equally, while the boundaries between trade and investment and capital-importing and exporting states are increasingly opaque, and while modes of dispute settlement continue to evolve as part of the construction of a new legal order so as to blur conventional conceptual distinctions, it remains the case that disputes arising from the ‘taking’ of foreign property remain as fiercely contested today as was ever the case. And where this is so, as this thesis has shown, state power and interests remain as critical in determining the rights and duties of foreign investors and thus the efficacy of institutional rules and norms as ever they have been, albeit in the case of U.S. infrastructure investors this is a dual-layered power comprised of OPIC governance backed by the U.S. government at the point of enforcement.

Foremost in this respect, as this thesis has shown, concerns the capacity of the agency in the course of paying or rejecting the claims of insured investors to unilaterally determine legitimate and illegitimate modes of regulation, the boundaries between economic and political risks, i.e. what constitutes a violation of international law, and with it the boundaries of markets for insured U.S. infrastructure operators in LDCs. In


this manner, the agency and by proxy the U.S. government can effectively determine the meaning of institutional rules and norms governing investor-state breach of regulatory contract disputes. This is power in law. It is so as Comaroff and Cohen tell us because ‘[t]he management of meaning is an expression of power, and the meanings so managed a crucial aspect of political relations.’

While the findings concerning the impact of insurance and the role of OPIC in dispute settlement are significant in their own right, dispelling as they do the notion that the provision of investment insurance serves merely as a risk-transfer mechanism, what is perhaps more significant is that investment insurance provides U.S. investors with a second layer of protection. More technically, the use of investment insurance when tied to BITs providing for the automatic subrogation of insurance claims provides the U.S. government with a secondary judicial mechanism with which to enforce host state compliance with legal obligations, supplemental to the existing hard law treaty-framework. Thus, where Indonesia’s refusal to honour the arbitral awards threatened to derail the dispute resolution process, the payment of the insurance claim served to sidestep the legal impasse. So too in India, where the arbitration process was frustrated, the provisions of the PRI contracts providing for AAA determination of OPIC-investor claims enabled the insured investors and thus the U.S. government to substitute one set of legal rules concerning expropriation for another so as to again sidestep the legal impasse thereby ensuring compliance with legal obligations.

In this regard, the use of investment insurance alongside treaty arrangements providing for the use of binding offshore arbitration to resolve disputes forms what may be likened to an interlocking legal structure. Of critical significance in this respect were the provisions of the contracts of insurance linking claims to the non-performance of arbitral awards. They were so, not only because the subsequent claim payment served to validate the tribunal’s findings in the case of Indonesia that CalEnergy’s property had been expropriated, but because in linking claims to arbitral awards, the provisions of the contracts of insurance served to underwrite the use of

offshore arbitration and thus the internationalization of state contracts wherein local jurisdiction was displaced in favour of transnational jurisdiction and adjudication.

The capacity of OPIC to act in this way is not, however, the product of the particular ambiguity of international law, or the normative sanction of law itself, instead, it is a product of U.S. power in enforcing subrogated investment claims. Evidence of this is provided by the fact that neither India nor Indonesia complied with the provisions of the respective investment agreements in force with the United States out of any sense of obligation. They did so because the U.S. was able to manipulate the payoff matrix to leave only one ‘rational’ solution.

It is not only with respect to the public provision of PRI that state power remains central. That is, the empirical evidence from the two case studies demonstrates that compliance with legal obligations and thus the efficacy of institutional rules and norms more generally must be understood as a product of state power at the point of enforcement, which in the final analysis is a function of relative material capabilities and evolving conceptions of national interests. Put simply, the final settlements of the two disputes must be understood as the continuation of international (state) power politics wherein the United States, through a combination of threats and inducements, was able to coax compliance with the legal rules distinct from the normative sanction of the ‘legal process.’

Most immediately, the assertion is supported by the fact that both India and Indonesia made it abundantly clear that they did not intend to comply with the arbitral rulings or the provisions of the respective bilateral investment agreements providing for enforcement of arbitral awards. This refusal was not, however, the product of disagreement with respect to the applicability of the legal rules to the facts of the case or even the interpretation of the applicable legal rule or norm, rather, it reflected a deeper underlying belief that the agreed mechanisms of judicial resolution possessed no legitimacy and therefore authority. Indeed, the dispute settlement process appears as best characterized by the attitude that international law was irrelevant, the disputes being matters of state to be determined through diplomatic bargaining separate from the judicial process, i.e. they were in the lexicon of law ‘non-judiciable.’
Furthermore, and despite U.S. rhetoric to the contrary, it was not only the ‘defendants’ who appear to have held such a view. Thus, in the Dabhol dispute, the U.S. appears to have felt no compunction in violating the principles of diplomatic protection concerning ‘corporate personality’ in extending diplomatic support, as was the practical outcome of U.S. efforts to support Mauritian incorporated DPC investors. The actions of the U.S. in this respect appear as indicative of a broader disregard for the customary international law of foreign investment. They do so because when the legal process was felt to no longer serve its interests, the U.S. simply substituted one set of legal rules concerning expropriation for another so as to engineer its preferred outcome backed by the threat of economic sanctions. In this manner, U.S. actions violated not only specific principles of international law but more fundamentally the founding principle of the interstate system—state sovereignty. It did so because the AAA arbitration followed by the subsequent enforcement of the subrogated insurance claim is tantamount to extra-territorial enforcement of U.S. statutes concerning expropriation and insurance contract law.

Taken together these actions underscore the continued centrality of state power and interests in determining the outcomes of investor-state disputes and therefore the efficacy of institutional rules and norms governing investment dispute settlement. They do so in the final analysis because where the terms of resolution were perceived to offer the respective state parties sufficient gains a settlement was reached after four and five years of legal machinations respectively, absent any change in the facts of the case or the legal rules themselves. In this manner, quasi legal judgments such as for example those handed down by the various arbitral tribunals in the case of the CalEnergy dispute served merely as the precursor to what was considered to be the real business of bilateral diplomatic bargaining.

Moreover, from a U.S. perspective, while it is clear that OPIC was resistant to making claim payments to CalEnergy and the remaining DPC investors, once compensation had been paid the final settlements did not impede broader diplomatic and economic objectives. For example, although the evidence makes clear that OPIC would have preferred CalEnergy renegotiate the energy sales contracts that is failed to do so did not prevent OPIC and the executive from successfully engineering a negotiated solution on behalf of the remaining U.S. independent power producers operating in
Indonesia. To this end, all but two of those power projects that had begun construction at the onset of the financial crisis are today operating profitably, having successfully renegotiated the respective power purchase agreements. Thus, despite very real diplomatic tensions arising from the payment of claims to CalEnergy, lasting damage to the bilateral relationship appears to have been avoided so that today U.S. investors continue to operate across the archipelago in a variety of industrial sectors, while military ties have been gradually strengthened.

Similarly, in India although the evidence makes clear that the payments of claims to DPC investors ran contrary to the preferences of both OPIC and the U.S. government, having been forced on the agency as a result of the AAA arbitration, evidently they did not prevent a negotiated solution to the unfolding crisis, as was the preference of all parties. More broadly, any lasting diplomatic fallout appears to have been avoided as is demonstrated by the rash of economic and military agreements concluded between the two nations in the months immediately following the resolution of the Dabhol imbroglio.

While the findings suggesting as they do the continued explanatory import of a classical realist conception of international law and politics are from a theoretical perspective far from radical, they are no less significant in light of contemporary accounts of the consequences of the legalization of dispute settlement, which portray these trends as somehow apart from underlying state power and interests. More particularly, the findings are significant because they serve to undermine the notion that the act of delegation and the provision of direct access serve to transform contests between unequals into legal cases, wherein outcomes are determined according to the facts of the case and the relative merits of legal arguments ostensibly unrelated to the material capabilities of states.

That is, the findings serve to discredit the idea that the legal-process itself, specifically the act of delegation and the provision of access to investors, dictates the politics of dispute resolution distinct from the relative power of states (home and host) who undertake to enforce or alternately resist legal rules consistent with evolving conceptions of national interests. Thus, to adopt the terminology employed, the key variable in terms of generating distinct non-political patterns of dispute resolution
remains the capacity to enforce rules independent of state actors and not as portrayed by contemporary accounts of legalization the twin variables of delegation and access.

Of course, given the limited number of case studies from which the findings are drawn, there is no suggestion that the evidence presented here disproves these theories as applies to other types of international commercial transactions. What can be said with certainty, however, is that while the current rapprochement between the disciplines of IR and Law is welcome, a renewed focus on rule-governed behaviour is of little benefit if it is purchased at the expense of a proper understanding of the role of state power in determining the efficacy of institutional rules and norms governing investor-state expropriation disputes, as well as associated changes in the use of arbitration and investment insurance over-time. In this regard, there is a critical need to recognize that while rules governing expropriation disputes have proliferated, and while the modes of dispute settlement continue to evolve amidst economic globalization where investors remain subject to the obsolescing bargain state power and interests remain as central in underwriting corporate expansion and in guaranteeing international property rights as ever they were.

To conclude, the intention in emphasizing the continued centrality of state power in the new legal order is not to contend that institutional rules and norms play no role in regulating behaviour and thus the outcomes of disputes. Instead, it is to recognize that '[I]nternational Law is not an isolated and self-contained credo deducible from unassailable premises and as an inescapable logic, it can only be understood in a political context.' That is, '[E]very system of law presupposes an initial political decision, whether explicit or implied, whether achieved by voting or by bargaining or force, as to the authority entitled to make and unmake law.' Put simply, in the words of E.H. Carr ‘The ultimate authority of law derives from politics.’

Part ‘B’: OPIC and United States Foreign Policy-Making

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In the same way that economic globalization and its legal corollary, the globalization of law is held to uncouple the link between state power and the rights and duties of foreign investors, it has become common place to portray U.S. foreign economic policy-making as at best inchoate and at worst ‘a large blundering bureaucratic mass incapable of sustained action and rational behaviour’ in pursuit of U.S. national interests.763 From this perspective, foreign policy initiatives emerge from societal pressures so as to refute the notion of a national interest and so as to in turn frame U.S. foreign economic policy as little more than the summation of particularistic societal goals. Implicit within such a formulation is the view that U.S. foreign policy officials possess little or no autonomy from domestic interest groups owing to the manner in which the United States political system diffuses policy-making powers away from the executive to the various organs of government and domestic interest groups, atop which sits corporate America.

Consistent with this characterization of U.S. foreign economic policy-making, the only sustained analysis of the long-term evolution of the investment insurance program produced to date holds that changes to the program have tended to conform to the narrow interests of U.S. foreign investors over and above U.S. national interests. Of critical importance in this respect concerns the manner in which divisions among the bureaucracy create what may be likened to a policy-vacuum into which business leaders have stepped so as to enable corporate investors to steer the program’s long-term development.

This study has sought to challenge this view by demonstrating the explanatory advantage of a ‘statist’ approach to foreign policy-making wherein the long-term evolution of the insurance program is understood as reflecting the pursuit of broader foreign policy goals sought by U.S. officials in their relations with the developing world, i.e. U.S. national interests. Put simply, while U.S. officials have sought to accommodate foreign investor preferences and second, while it is true that disagreements among state officials as to how the program could best be tailored to further broader foreign policy goals are the norm rather than the exception; where

state and corporate interests have collided, the interests of the ‘state’ have invariably prevailed where the insurance program is concerned.

In the first instance, U.S. government officials drove the transfer of executive responsibility for the insurance program from USAID to the newly created OPIC as took place in 1971. Contrary to prevailing wisdom this was not, however, part of any coherent U.S. government response to the expropriation of U.S. foreign investor property, instead, the program’s establishment reflected ongoing tensions between the executive and Congressional branch concerning foreign-aid spending. The underlying motivation for which was a belief that such spending did little to further U.S. national interests given Cold War competition for power and influence vis-à-vis LDCs. The 1974 amendments which, temporarily at least, effectively terminated the program must also be understood in this context, specifically, the desire of the Congressional branch to reorient U.S. foreign-aid spending towards the newly instituted Basic Human Needs program. Finally, the 1978 amendments were also a product of state-led reform of the foreign-aid program (Carter’s ‘New Directions Policy’) hence the transfer of responsibility for the program to the newly created IDCA. In short, only this can explain the program’s lack of growth as well as the imposition of successive restrictions on the availability of insurance amidst rising demand from corporate America, underpinned by unprecedented rates of expropriation in LDCs.

The amendments to the insurance program between 1981 and 1994, the characteristic feature of which was the agency’s transformation from minor adjunct to the foreign-aid program to that of foreign trade and investment promotion, were also the product of state-led reforms. In this instance, however, reform of the program reflected mounting anxiety among U.S. officials over declining U.S. corporate competitiveness. In this regard, the changes observed though far from universally acclaimed reflected a consistent if evolving conception of the national interest, central to which was the upgrading of economic interests to the status of national security in the minds of U.S. foreign policy-makers.

The transformation pre-dated the collapse of the bipolar world order, however, beginning with the decision in 1981 to remove earlier restrictions on the availability of OPIC insurance for U.S. foreign investors. The 1985 and 1988 amendments must
also be understood in the context of a state initiated reform process, the primary feature of which was the aggressive pursuit of expanded markets in LDCs for U.S. exporters and investors as a means to rectify ever-increasing balance of payments deficits. Finally, the 1992 and 1994 amendments, the latter of which provided for the doubling of the agency’s per project and aggregate exposure ceilings must also be understood as the product of state-led efforts to reinvigorate U.S. corporate competitiveness. In particular, it was envisaged that OPIC support, as but one component of a three-pronged strategy which also included the United States Export-Import Bank and the Trade and Development Agency would not only level the playing field for U.S. infrastructure investors, but would also stimulate additional capital goods exports.

By 1994, the transformation of OPIC was all but complete, the public policy rational underpinning the program having swung from that of foreign-aid to foreign trade and investment promotion. Thus, where in 1971 the agency had been established with the overriding goal of promoting host country economic development as an adjunct to the foreign-aid program, secondary to which were the positive development effects for the United States economy, by 1994 these goals had been reversed. As a result, where once the decision to insure foreign investments relied upon the projected economic impact upon the host-country by 1994 the deciding factor was increasingly the calculated impact on the U.S. economy.

The transformation of the public policy rationale underpinning the program appears therefore as but one small component of a more fundamental shift in U.S. foreign economic policy vis-à-vis the developing world, central to which has been the refusal to continue to subordinate economic interests to security interests as predominated during the Cold War. Among the other changes of note, in this regard include the restoration of ‘tied-aid’ (1983), the promulgation of BITs from 1982 and most importantly, the imposition of loan conditionalities as part of World Bank and IMF debt rescheduling from 1985, all of which were designed to open markets for U.S. exporters and foreign investors. In this regard, while it may be true that ideas regarding economic development began to converge in the immediate aftermath of the end of the Cold War as indicated by the use of the term ‘Washington Consensus’, and
while it is true that OPIC did not lose its development objectives entirely, it is also the case that the observed changes served to further the material interests of the U.S.\textsuperscript{764}

To conclude part ‘B’ of the research, from a narrow theoretical standpoint the findings are once again far from radical, positing as they do the continued explanatory advantage of a statist approach to U.S. foreign economic policy-making, centred on the pursuit of national interests inductively defined. That this is the case makes them no less important, however, given the prevailing image of the U.S. government as incapable of sustained and rational action in pursuit of U.S. national interests. In this regard, the evidence has shown that U.S. officials possess autonomy from domestic interest groups, including corporate America where the OPIC administered insurance program is concerned.

The assertion that state interests are paramount in determining the forms of support offered U.S. foreign investors by OPIC must be qualified, however. To this end, while state interests predominate it is also the case that from the early to mid-1980s the foreign policy goals sought by the state through the program and those of U.S. foreign investors increasingly overlapped so as to make it increasingly difficult to distinguish one from the other. In this respect, the goals sought by U.S. foreign policy-makers through the program were increasingly defined by the shared goal of private multinational capital accumulation. Thus, while the precise form and timing of the 1994 amendments, which underwrote the expansion of U.S. infrastructure investors to some thirty LDCs during the 1990s, was driven by state officials it hardly needs pointing out that such a shift was fully consistent with evolving strategies of corporate adaptation and risk-management. From this perspective, Enron and CalEnergy’s global mis-adventures appear not as an aberration but as a product of the incentives created by the state at home and abroad—as ultimately, it is the state that determines legitimate organizational forms and strategies of private capital accumulation—consistent with evolving conceptions of the national interest and configurations of power in the interstate system.

The aim of the next section is to draw together the findings from parts ‘A’ and ‘B’ of the research so that we might better understand the relationship between U.S. foreign policy-making and contemporary institutional rules as concerns investor-state breach of regulatory contract disputes. To recap, the study has shown that institutional rules and norms—their meaning and applicability to disputes—and more broadly prescribed modes of investment dispute settlement should be understood as a product of state power and interests, as states seek to enforce and or resist legal obligations consistent with evolving perceptions of national interests and configurations of power in the interstate system. More narrowly, the study has shown that in the case of breach of regulatory contract disputes OPIC PRI is critical in underwriting the rules of the game. Second, the research has shown that state initiatives or rather a statist approach to foreign policy-making best explains the long-term evolution of the OPIC administered insurance program, as the U.S. government sought to respond to shifting external constraints in the international state system consistent with evolving conceptions of national (material) interests.

Putting the two parts together, if OPIC investment insurance and by proxy U.S. power is critical in underwriting the rules of the game and if what OPIC does is a product of U.S. material interests then the thesis can reveal shifting international law norms as concern breach of regulatory contracts and second the transformation of infrastructure services in LDCs, as but one facet of the globalization of law and economic globalization respectively, as the product of the power and material interests of the United States. Central to which was the desire of U.S. officials to expand markets for, and strengthen property and contract rights on behalf of U.S. foreign investors.

In this regard, the direction of causation between institutional rules and norms and U.S. policy-making is clear. It is so because as U.S. policy has shifted toward a more stringent application of U.S. expropriation statutes in accord with U.S. national interests and shifting configurations of power in the international state system, then the rights and duties of foreign investors as prescribed by institutional rules and norms of expropriation and compensation are moving in the direction of the U.S. legal
doctrine of regulatory taking. In this manner, the thesis reveals OPIC PRI, far from simply a risk-transfer device, as an instrument of U.S. power and interests in the new legal order and as a conduit for the transmission of shifting property norms from the United States to the world economy at large.

It is so because in paying seven claims to CalEnergy and DPC investors the agency’s actions serve to supplement the body of case law concerned with investor-state breach of contract disputes. In particular, the seven claims paid to U.S. investors by OPIC serve to establish breach of contract by a sovereign party (obligor) more firmly within the realm of expropriatory action than was previously the case. Second, and by implication, the two cases serve to delimit public policy exceptions to the doctrine of *pacta sunt servanda* as provided for in both the New York Convention on the Enforcement of Arbitral Wards and the UNCITRAL Model Law of arbitration, and more broadly the legal doctrine of *clausula rebus sic stantibus*. In the case of Indonesia, the determination is particularly significant as it serves to invalidate the *clausula* defence even in instances of economic contagion as beset Indonesia and as precipitated the CalEnergy dispute in the initial instance. That this is the case serves to identify the agency not merely as but one of a number of enforcement mechanisms with regards to the rules governing private property and contract rights but as a source of interstitial legal norms separate from formal treaty-making.765

In this manner, the rules of the game increasingly mirror a uniquely American vision of the rights and duties of private property and the state central to which is the inviolability of private property and contract rights unrelated to public policy considerations and claims of sovereign immunity, as embodied in the legal doctrine of regulatory taking.766 The takings clause under the Fifth Amendment of the United

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766 James Ely Jr. tells us that the then Chief Justice of the United States Supreme Court, Holmes in Pennsylvania Coal Co. v. Mahon (1922) introduced the doctrine of regulatory taking into U.S. Supreme Court jurisprudence. He continues, the doctrine was, however, little used for some fifty years following the New Deal jurisprudential revolution in 1937, being revived in 1992 when conservative Justice Scalia found in *Lucas v. South Carolina Coastal Council* (1992) that the actions of the state party amounted to a regulatory taking so as to revive Holmes’s regulatory taking doctrine for the first time in
States Constitution serves as a curb on the government’s powers of *Eminent Domain* by requiring that the exercise of *eminent domain*, where it reduces the value of private property, be accompanied by the payment of compensation equal to the loss of value or income.\(^{767}\) More particularly, as the scope of compensable takings has expanded within U.S. legal practice so as to include losses arising from governmental action not previously considered a ‘taking’, then these changes are first manifest in the policy and practice of OPIC (U.S. foreign policy) and ultimately, in the rules and norms of the international institution for dispute settlement.\(^{768}\) They are so because the effect of the determinations made by OPIC in the two case study disputes serve firstly to expand the scope of compensable takings (expropriation), and secondly, and by implication to narrow the range of permissible public policy defences for breach of regulatory contracts.

As a final point in this respect, it appears as notable that the very idea of judicial protection of private property rights, as is reflected in the contemporary trend towards the use of judicial mechanisms to resolve investment disputes, reflects a specifically *American* conception of private property rights. It does so because as Cole tells us, the notion of judicial as opposed to legislative review of private property and contract rights is unique to the *American* constitutional schema.\(^{769}\) While considerable debate

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\(^{767}\) The clause reads ‘[N]or shall private property be taken for public use without just compensation.’ Dana and Merrill note the takings clause is ‘unique in requiring compensation in conjunction with the exercise of a certain type of governmental power – eminent domain – and it has been held to abrogate any claim of sovereign immunity that might otherwise stand as a barrier to the payment of such compensation.’ See David A. Dana and Thomas W. Merrill, *Property Takings* (New York: New York Foundation Press, 2002), p. 1.

\(^{768}\) According to Dana and Merrill, two recent cases heard by the Supreme Court appear to invite litigation for contract damages and/or just compensation when the federal government alters its regulatory policy and hence devalues supposed property rights in alleged, albeit implicit, regulatory contracts. See *United States v. Winstar Corp.* (1996) and *Mobil Oil Exploration and Producing Southeast Inc. v. United States* (2000) in Dana and Merrill *Property Takings* (2002), p. 249-250.

\(^{769}\) Daniel H. Cole, ‘Political Institutions, Judicial Review and Private Property: A Comparative Institutional Analysis’, unpublished, forthcoming *Supreme Court Economic Review*, November 2005. Cole notes that considerable debate attends the question as to why the framers of the American Constitution sought to delegate such functions to the judicial rather than the legislative branch of government, particularly since the Constitution was based on English Common Law where no such provisions exist. The ostensible rationale was that of ‘vulnerable minority’ wherein it was held that such protection was required to prevent populist governments from violating private property rights of the minority to the benefit of the property-less majority. More practically, James Ely Jr. contends that the inclusion of judicial review was an attempt to minimize anti-federalist opposition to the fledgling constitution. See James Ely Jr. *The Guardian of Every Other Right* (1992), supra note 6 at p. 51-52.
attends the question of why the framers of the American constitution felt the need to include such safeguards against legislative interference with private property rights, what is clear is that as judicial review of property rights has been restored in the United States then these changes are manifest in the contemporary international property rights regime insofar as dispute resolution functions are increasingly delegated to judicial and quasi-judicial bodies.\footnote{James Ely Jr. tells us that by 1990 the primary power with respect to property rights had once again been restored to the judicial branch, displaying an attitude that was far ‘less deferential to state law that infringed on property and contract rights’ than had been the case for a half-century.’ James Ely Jr., The Guardian of Every Other Right (1992), p.152.}

The central point is that the shifting meaning of expropriation as concerns the ‘rights’ and ‘duties’ of foreign infrastructure investors, and the increasing use of judicial mechanisms to resolve investor-state expropriation disputes bear the imprimatur not only of U.S. power and interests, but a specifically American conception of property norms. Property norms that Richard Epstein cogently notes provide no less than the principal means of ordering ‘the proper relationship between the individual and the state.’\footnote{Richard A. Epstein, Takings: Private Property and the Power of Eminent Domain (Cambridge, Massachusetts: Harvard University Press, 1985), p. 3.}

Conclusions: Public Policy Implications of the Research Findings

The penultimate task remaining is to consider the public policy implications of the research findings, beginning with the implications for OPIC. In one very real sense, the insurance program functioned exactly as intended. That is, the provision of insurance and financing by OPIC facilitated both the Dabhol and CalEnergy investments, absent of which neither project(s) would have proceeded. Against this, the evidence from the two case studies suggests a pressing need to rethink a number of aspects of the program, beginning with the provisions of the contracts of insurance. Most critically, although the evidence makes clear that the program’s administrators did not simply rush in to pay the investor claims, displaying considerable restraint in the face of Congressional pressure in the case of CalEnergy, it is also the case that the

\footnote{What is clear, however, and as noted by Cole, is that such a view reflects a deep mistrust of democratic regulations and institutions.}
provisions of the contracts were ambiguous at best as regards commercial exclusions. Put simply, the agency must ensure these provisions are clear thereby avoiding facile suggestions to the effect that any deviation from the concession contract is tantamount to expropriation.

As a further aid to assist contractual stability, the agency might also pause to rethink the inclusion of provisions in the contracts of insurance linking claims to arbitral awards if it is to safeguard against moral hazard. In the same vein, the agency might also reconsider the underlying contractual structure to ensure that the suite of risks are apportioned optimally rather than simply loading risks, including foreign exchange risk, on the local-obligor. This is so not only because these disputes are by their very nature politically sensitive but because from a purely commercial viewpoint the practice of insuring projects that earn no foreign exchange and where debt is denominated in foreign currency is plainly questionable. Further, the agency might also give pause to reconsider the practice of financing investors in addition to the provision of insurance. The reason for this is that the agency’s position as both insurer and unsecured lender in the Dabhol dispute served to further confuse an already complex dispute resolution process insofar as OPIC’s demands that its unsecured loans be recognized by the Indian government before any sale could be agreed served only to impede a final settlement.

More generally, although strictly speaking the agency need not concern itself with the expected profitability of an investment, it is also the case that insuring a project with an expected return on capital of 33 percent per annum over thirty years, as was the case with the Dabhol project, is difficult to reconcile with its developmental mission, however, secondary such a mandate has now become. On a similar note, though it is not the responsibility of the agency to assess the capacity of the host authorities to meet their contractual obligations, OPIC’s actions in insuring multiple projects in Indonesia when it was clear that such onerous contractual terms could not be met were at best dubious from the perspective of encouraging host country development.

What is clear, however, is that if OPIC is to exercise diplomatic and judicial functions on behalf of U.S. infrastructure investors in LDCs then the agency must be more transparent if it is to enjoy the sort of legitimacy required to enable it to perform this
role effectively. Critical in this regard, concerns the need to strengthen safeguards against corruption as is common in the awarding of large infrastructure projects. At a minimum, this should mean the agency refusing to support projects where foreign investors collaborate with local investors with no demonstrable expertise. Second, the agency should also refuse to support projects where the local partner receives their equity stake at no cost, as was the case with the Indonesian projects. To this end, it is clear that the Foreign Corrupt Practices Act (1977) is wholly inadequate, covering as it does only payments to foreign government officials and not their relatives or business associates. At a minimum, OPIC must ensure that safeguards are in place so that when improprieties are alleged the agency is first, equipped with the requisite resources to properly investigate such claims and second, can withdraw insurance should the allegations be proven absent the fear of political interference from the insured investor’s Congressional representatives.

Of course, OPIC does not operate in isolation. In this regard, the agency’s actions in the two disputes have a number of implications for the United States, for whom the presence of insured investors proved a double-edged sword. Thus, on the one hand OPIC insurance operated as intended insofar as it facilitated new investments and therefore profit-making opportunities as well as stimulating demand for capital goods exports. Second, the political objectives underpinning the program were fulfilled to the extent that OPIC advocacy and mediation enabled the executive, but primarily the State and Commerce Departments, to take a backseat in the negotiation process so as to depoliticize the disputes as far as possible. Moreover, this was particularly beneficial in the case of Dabhol enabling as it did the Bush administration to distance itself from the dispute so as to limit the political backlash against it in Washington, as would have resulted had it been seen to be defending the narrow interests of the by then disgraced energy company.

Against this and as the analysis has made clear, the contracts of insurance served to diffuse policy-making power and therefore power over outcomes away from the executive to the insured investor. In this regard, OPIC insurance served to delimit U.S. policy-making autonomy in seeking a negotiated settlement to the two disputes. In this respect, the findings from the two case studies suggest the need to consider whether the benefits accruing from the program’s operation outweigh the resulting
loss of foreign policy autonomy, which served to imperil already fraught diplomatic negotiations with what are the world’s second and fourth most populous nations. Moreover, it is also significant to note that based on anecdotal evidence garnered from interviews, contrary to the intentions of the program’s founders, forcing high ranking democratically elected government representatives to negotiate directly with what they perceived to be a minor agency comprised of low ranking unelected government officials actually worsened relations owing to the perception that doing so was an affront to both India and Indonesia’s sovereignty.

The final point with respect to the policy implications for the United States concerns not the specifics of the insurance program but rather the thrust of contemporary U.S. practice concerning expropriation. While the policy can be defended on economic grounds as securing stability of possession so as to stimulate capital flows, it is also the case that U.S. actions in enforcing contractual obligations resulting from the exercise of political patronage serve to frame U.S. policy as little more than empty rhetoric masking material interests. As Rodman notes, it ‘would be an empty pretense and a cruel hoax if a new government could not divest itself of obligations incurred by . . . irresponsible governments. Such a legal system amounts to an effective veto over a state’s freedom to pursue its own course of economic development and social reform.’772 Yet this is exactly the outcome of U.S. policy in enforcing compliance by Indonesia with its legal obligations.

Apart from the damage to the immediate bilateral relationships with Indonesia and India, the policy also fails insofar as rather than strengthening U.S. foreign investor property rights it serves only to frame the international law of foreign investment as a bulwark of the status-quo. Once again, the point is well made by Rodman who writes ‘[F]or any international law principle to survive, it must advance the common interest not of a limited ideology but that of the wider global community it purports to serve. By this standard, the U.S. position on the sanctity of contracts fails. It assumes a world in which firms are purely economic actors and bargains are freely negotiated. State intervention, it is argued, should be subordinated to an impartial system of

justice.\textsuperscript{773} Put simply, if the yardstick by which the success of U.S. foreign policy is judged is the degree to which the outcomes of the two disputes served to strengthen the ‘rule of law’ and with it private international property and contract rights on behalf U.S. foreign investors, then U.S. policy must be adjudged a failure.

The final task in this the penultimate section is to consider the public policy implications for countries playing host to insured infrastructure investors. Most immediately, the research makes clear that when contracting over such long periods there is a critical need to ensure that the underlying contract contain some in-built adjustment mechanisms to enable the terms of contracts to be renegotiated, as and when pre-agreed trigger events occur. Further, the evidence also suggests a real need to rethink the basic contractual model wherein foreign producers are tied to a single off-taker. Foremost in the regard concerns the need to consider alternative models such as those permitting foreign investors to sell their services direct access to industrial consumers, the effect of which would be to reduce credit risk and thus the risk-premium demanded by investors.

More particularly, there is a real need to make clear so as to avoid future conflict whether or not ‘comfort letters’ are just that or whether as interpreted by both CalEnergy and Enron such letters amount to ‘sovereign guarantees.’ Further, if it is the latter then contingent liabilities must be accurately recorded in the national accounts. Moreover, such a move would also have the added advantage of forcing LDCs to consider whether the benefits of the contractual model, promising as it does the capacity to supplement domestic savings and capital with foreign capital absent any increase in sovereign liabilities, are as great in reality as first appear on paper.

More broadly, and assuming the ultimate goal of deregulation and privatization of markets for infrastructure services is the creation of competitive markets, the evidence from Indonesia and India serves to underscore the maxim of market restructuring that deregulation must be undertaken across the board rather than in a piecemeal fashion. That is, countries considering deregulating infrastructure markets must be aware that half-measures wherein the existing regulatory structure is modified to permit the entry

of foreign investors whilst leaving the basic arrangements untouched will fail to realize the potential benefits accruing from the private provision of infrastructure. The World Bank and the ADB recognized this in both India and Indonesia, hence their refusal to participate in the financing of the IPP projects. Unfortunately, this advice was overshadowed in the rush to attract private investors. More generally, countries considering market deregulation might also consider the advice of the World Bank that such efforts might be better directed at improving the existing infrastructure as a prelude to the arrival of foreign infrastructure operators so as to enable the incumbent providers to compete on an equal footing with their foreign counterparts.

Perhaps more significantly, states playing host to investments of this type must along with the multilateral development banks acknowledge that regulatory practices and frameworks cannot simply be transplanted from one country to another but particularly from the industrialized states to their developing counterparts. The reason for this not least is that the price charged consumers in LDCs did not typically reflect the true cost of provision the arrival of private operators involves, therefore, not only a transfer of ownership of productive assets from the public to the private sector, but very often internal income transfers from consumers to operators as prices are increased. As this research has shown, this has significant political consequences for governments undertaking such market restructuring, but particularly in low-income democracies where the greatest burden is borne by the largest voting bloc.774 In this regard, there is thus a need to acknowledge that market restructuring cannot be undertaken in isolation, requiring as it does a social and political transformation if deregulation is to reap the rewards promised in terms of efficiency and competition.

In the final analysis, governments considering liberalizing markets for infrastructure services must be aware that admitting insured infrastructure investors means importing not only scarce investment capital and valuable technical and managerial expertise but also systems of property rights, which embody normative prescriptions concerning the rights and duties of capital and the state in their relations with one another. They do so because ‘contracts without social structure and stability are rationally unthinkable. Otherwise, how could promises be projected effectively into

the future.'

That is, the very idea of contracting and private property ‘must be understood as elements of a more inclusive normative order that is itself socially constituted and culturally inscribed.’ Unfortunately, as the research has shown, where these property norms collide it is power that determines which will prevail, unrelated to need or equity.

Postscript: OPIC and the Future of Private Infrastructure in the 21st Century

The final task to be completed is to consider the future of private infrastructure provision, and the role that OPIC insurance will play. Most immediately, the future can in one sense be read as ‘more of the same.’ That is, even if OPIC were to issue no new contracts of insurance for infrastructure investors, the length of existing contractual arrangements, extending up to twenty years, means that the current crop of contracts will not expire for at least a decade or more thereby signalling new disputes and possibly new insurance claims. Certainly, such an assessment is supported by a brief examination of current infrastructure projects insured by OPIC, a number of which suggest themselves as candidates for new disputes and new insurance claims. Prominent among these is CalEnergy’s Casecnan Power and Irrigation project in the Philippines supported with $250 million of OPIC insurance and financing, and currently the subject of an intensifying local and international NGO campaign.

According to critics of the deal, in what is by now a familiar litany of complaints, the contracts are grossly disadvantageous to the people of the Philippines and were the result of collusion and nepotism between CalEnergy and the former President, Fidel Ramos. Thus, while the future cannot be forecast with any assuredness, it would appear to be inevitable that new disputes and claims will arise, even if the number is less than was initially feared, in the immediate wake of the Dabhol, Dieng and Patuha cases.

775 Quoted in Charles Lipson, Standing Guard (1985), p. 3.
777 The contracts, like those of CalEnergy’s contracts in Indonesia, were also the product of the personal friendship between CalEnergy executive and former U.S. General (Marine Corp.), Donald O’Shei and former Philippine General and later President, Fidel Ramos. According to interview evidence, the two met and became friends at officer training college in the U.S.
More generally, it is also the true that there is a mounting backlash against privatization and deregulation, as the reform process fails to yield the promised benefits for affected communities. In this regard, Guasch tells us that there is a growing perception that ‘privatization and concession programs have been unfair and have benefited the wealthy and hurt the poor through job losses and higher tariffs and that the process lacks transparency, proceeds have been misused and corruption has run rampant.’

Although evidence such as this does not provide us with any definite image of what the future may hold some things can be said with a degree of certainty. First among these is that the next few years will be crucial in determining whether private provision of infrastructure will become the norm or whether in fact the recent period of privatization and deregulation will be viewed as a failed experiment presaging a return to public infrastructure provision and service delivery as predominated throughout the twentieth-century.

The second thing that can be said with certainty is that simply promulgating more legal obligations and or more precise rules governing breach of contract expropriation disputes will not achieve the desired objective of stabilizing private property and contract rights, and with it additional capital investment in LDC infrastructure. The reason for this, as this research has demonstrated, is that the meaning and thus the significance of institutional rules and norms is ultimately a function of state power and interests at the point of enforcement and no amount of rules will change this fact nor make the existing legal obligations more efficacious in preventing and or delimiting the outcomes of disputes.

The third thing that can be said with a degree of certainty is that OPIC’s actions as the market leader will have a major bearing on the future of private infrastructure provision in LDCs not only for U.S. investors but in terms of the viability of the current investment model. And what OPIC does, as the current research has shown, will depend in the final analysis on the foreign policy goals sought through the

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program by U.S. officials, and second and by extension the broad sweep of U.S. foreign policy towards the developing world. Specifically, the relative import of economic and security goals in constituting U.S. national interests, which in turn will determine the extent to which the OPIC administered insurance program fulfils a foreign-aid or a foreign trade and investment promotion function.

In this respect, changes initiated to the program since 2003 point to the gradual re-emergence of the program’s original foreign-aid function, as part of a more fundamental shift in U.S. foreign policy vis-à-vis the developing world post-9-11. That is, although none of the three subsequent re-authorization hearings, including in 1996-97, 1999 and 2003 have introduced changes of a comparable magnitude to those enacted in 1994, and while the agency’s market-making function remains of central importance, recent reforms suggest that the program is increasingly being used to fulfil political goals as U.S. foreign policy objectives shift. Foremost in this regard concerns efforts to reorient the program to support reconstruction efforts in Afghanistan, and Iraq and in pursuit of security goals. To this end, OPIC signed Investment Incentive Agreements with Iraq and Afghanistan in 2004 making all of OPIC’s services available in these countries, as well as establishing investment ‘Renewal’ funds to be used to make direct investments in these countries, alongside Pakistan.

Among the other changes indicative of a renewed foreign-aid role for the agency, include the introduction of a ‘developmental matrix’ designed to enable the agency to better assess the impact on host country economic and social development. The matrix introduced as part of the agency’s five-year strategic plan to run from 2003 to 2008 aims to refocus the agency on its developmental (foreign-aid) mission. As

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779 While the three subsequent reauthorization hearings have resulted in few major changes to the program since the one-off expansion of the agency in 1994, the three hearings were not without drama. First, in 1996, Republican Toby Roth (R-WI) introduced a bill (H.R. 3759) that would have doubled the agency’s aggregate insurance and financing limits but this proposal was defeated. Second, also in 1996 a unlikely coalition of libertarian groups and environmental groups attempted to kill off the agency, only being defeated after strong pressure from the Chairman of the TPCC, William Daley and President Clinton. The 1999 and 2003 hearings were far less eventful, however, opposition to the agency once again having dissipated, so as to enable the reauthorization to proceed on voice votes only and by a strong majority.


with all such initiatives only time will tell whether these moves actually change the way the agency operates. In this respect, it is significant to note that critics of the program rightfully point out that not only does the matrix not contain objective assessment criteria but also there is no facility to independently verify whether the information received from prospective clients is accurate.782 The second major initiative adopted by OPIC in this regard concerns the ‘Anti-Corruption and Transparency Initiative.’ As part of the initiative, jointly developed with Transparency International, OPIC is committed to publishing an anti-corruption handbook outlining project sponsors requirements to comply with the Foreign Corrupt Practices Act, as well as establishing what it describes as an anti-corruption ‘hotline’ to be used to report potential irregularities.

Perhaps the most significant change from the perspective of this research concerns the introduction of a new insurance product designed to distinguish between expropriation and breach of contract in investor-state contracting. The new product entitled ‘Non-Honouring of Sovereign Guarantees’ and introduced at the end of 2004 remains as yet largely untested but it does signal a willingness by the agency’s administrators to recognize the particular problems that attend insuring and financing large infrastructure projects given its experiences in India and Indonesia.

The basic idea for the cover is to reduce the risk attendant to the non-performance of sovereign guarantees by guaranteeing payments to project lenders for up to six months in the event of a default so as to provide a ‘cushion’ where such an event might otherwise precipitate a claim for expropriation. There are, however, many problems with such a cover, which limit its usefulness for both investors and host countries. In particular, in order for OPIC to insure a project the host government must agree to limit ‘its own flexibility in adapting future regulatory changes’ and second ‘it requires advance definition of the regulatory structures that the government will commit to maintain and any such definition may fail to address other unexpected

782 For criticisms of the Developmental Matrix, see Bruce Rich, Attorney and Director, International Program, Environmental Defence, statement before Committee on International Relations, House of Representatives, June 10, 2003. To illustrate the criticisms, the 2004 OPIC Annual report records that the average developmental score on the new index for OPIC insured projects was 91.1 out of 100. Precisely what this means given the inability to access the individual project reports and given the lack of objective assessment criteria is, however, unclear.
regulatory risks that may become apparent later.783 Third, and finally, it also requires the host to commit to concluding arbitration within three months.

In conclusion, while reforms such as these are to be applauded, demonstrating as they do a willingness to learn from recent experiences ultimately the agency, and indeed governments around the world, must recognize that although foreign investors will always desire strengthened property rules and speedy dispute resolution procedures their needs should not be allowed to override the legitimate desire of local communities to ‘renegotiate property practices piecemeal’ so as to engage and reflect evolving ‘public values and public norms.’ Second, to undermine the process wherein property norms are publicly renegotiated is to risk undermining the legitimacy of the social order in states playing host to insured infrastructure investments. In the final analysis, and in the words of property theorist Marc Poirer, only ‘[W]hen we understand regulatory takings doctrine as part of a process of transition management’ can we see why ‘it ought to remain substantively vaguer and procedurally slower and more transparent than foreign investors would like. While this process approach to regulatory takings does not lead to a comfortable resolution of all the questions raised by an international regulatory takings doctrine, it at least helps us to understand what we are dealing with.’784

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107. Letter From Secretary of Commerce Stans to Secretary of State Rogers/1/. Washington, March 12, 1969. /1/Source: National Archives, RG 59, Central Files 1967-69, FN 6-1. No classification marking. Attached to an April 3 letter from Rogers to Stans stating that many of the Commerce Department's reactions were similar to those in the Department of State/AID analysis. Rogers enclosed a copy of Richardson's March 25 memorandum to the President and its attachments (Document 108).


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List of Interviewees:

Indonesia: Case Study Number 1.

Interview: Direct
Position: Former CalEnergy Executive
Location: Jakarta
Date: 31.08.04

Interview: Telephone
Position: Former CalEnergy Executive
Location: Sydney
Date: 22.08.04

Interview: Direct
Position: Legal Counsel, Ministry of Finance (Indonesia)
Location: Jakarta
Date: 30.08.04

Interview: Telephone
Position: Legal Counsel, Paiton II and UNOCAL (Indonesia)
Location: Washington
Date: 27.08.04

Interview: Direct
Position: Former Head Transport and Infrastructure Division (World Bank, Jakarta)
Location: Jakarta
Date: 02.09.04

Interview: Direct
Location: Jakarta
Date: 03.09.04

Interview: Direct
Position: Chief Legal Advisor, PLN
Location: Jakarta
Date: 01.09.04

Position: Former Head PLN Legal Team
Location: Jakarta
Date: 02.09.04

Interview: Direct
Position: Former President Director, PLN (1992-95), Director General Electricity (1995-98) and Minister for Technology and Science (1998-2001)
Location: Jakarta
Date: 01.09.04

Interview: Direct
Position: Legal Counsel PLN, (1980-Present)
Location: Jakarta
Date: 03.09.04

Interview: Direct
Location: Jakarta
Date: 02.09.04

Interview: Telephone
Position: Former President Director PLN (1998-2001)
Location: Sydney
Date: 15.10.04

India: Case Study Number 2

Interview: Direct
Position: Secretary, MSEB (2000-2005)
Location: Mumbai
Date: 08.09.04

Interview: Direct
Position: Joint-Secretary, Ministry of Finance (Power Sector)
Location: New Delhi
Date: 04.09.04

Interview: Direct
Position: Head of Dabhol Inter-Ministerial Working Group, Former Cabinet Secretary (India), Former Indian Ambassador to the United States,
Location: New Delhi
Date: 14.09.04

Interview: Direct
Position: Chairman, MERC
Location: Mumbai
Date: 07.09.04

308
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