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TEMPLARS ThoughtLab – ISDS Series | Part IV

Expropriation

Introduction

This is the fourth instalment of the TEMPLARS ISDS Series, exploring recent trends in the Investor-State Dispute Settlement (ISDS) system. Previous instalments introduced the ISDS system, addressed the Full Protection and Security (FPS) and Fair and Equitable Treatment (FET) standards while this instalment considers the protection against expropriation, covering both direct and indirect forms of taking.

The Expropriation Standard – Definition and Scope

The protection against expropriation is the oldest and, in many respects, the most fundamental of the substantive protections available to foreign investors. Its origins lie in the post-independence era, when newly sovereign states particularly those from Africa and the Americas asserted their right to nationalise foreign-owned assets especially those owned by developed countries sometimes for economic or political reasons. An oft cited example is the nationalisation of British Petroleum (BP) by the military administration of General Olusegun Obasanjo on 30 July 1979, as a political and economic protest against the United Kingdom's policy under Prime Minister Margaret Thatcher regarding Rhodesia (now Zimbabwe) and potential oil supplies to apartheid South Africa. At the same time, capital-exporting states sought binding guarantees of compensation for their nationals in cases of nationalisation.

The foregoing resulted in the introduction of protection against expropriation as a fundamental provision in investment treaties.

While outright nationalisations are now rare, the standard remains highly relevant, as modern claims increasingly concern regulatory and administrative measures which deprive investors of the value or control of their investments without any formal transfer of title.

It is worth noting that international law does not prohibit expropriation. It rather recognises the sovereign right of a state to take property within its territory but conditions the lawful exercise of that right on compliance with certain requirements. This position was affirmed by the United Nations General Assembly in Resolution 1803 (XVII) of 1962 on Permanent Sovereignty over Natural Resources, which recognised the right to nationalise or expropriate on grounds of public utility, security or the

national interest, subject, however, to the payment of appropriate compensation.[1] In practice, treaty provisions typically establish the four cumulative conditions below for a lawful expropriation, such that an expropriation that fails to satisfy any one of these conditions is unlawful. These are: (i) the taking must be for a **public purpose** or in the public interest; (ii) the measure must **not be discriminatory** or arbitrarily single out the foreign investor, whether by reference to nationality or otherwise; (iii) the taking must be carried out in accordance with **due process** of law, which ordinarily requires a legal basis in domestic law, reasonable notice and a fair opportunity for the investor to be heard and to challenge the measure; and (iv) the taking must be accompanied by "prompt, adequate and effective" **compensation**.

The typical treaty formulation, particularly for older generation BITs, is illustrated by the UK-Nigeria BIT 1990, which provides that investments of nationals or companies of either Contracting Party shall not be nationalised, expropriated or subjected to measures having effect equivalent to nationalisation or expropriation in the territory of the other Contracting Party except for a public purpose related to the internal needs of that Party, on a non-discriminatory basis and against prompt, adequate and effective compensation.[2]

Direct Expropriation

Direct expropriation involves the formal transfer of title to the investment, or its outright physical seizure, by the state or for the benefit of the state or a third party. The classic examples are the waves of nationalisation in the oil, mining and banking sectors during the 1960s and 1970s, which generated the early jurisprudence on compensation, including the Libyan oil nationalisation arbitrations.

Today, direct expropriation is comparatively uncommon, as states are aware of the reputational and financial consequences of an overt taking. When it does occur, the principal contest is usually not whether there has been an expropriation, but whether the conditions for lawfulness were met and how compensation should be assessed.

Indirect Expropriation

Indirect expropriation occurs where the state, without formally taking title, adopts measures which substantially deprive the investor of the use, value or control of its investment. Treaties capture this through language such as "measures having effect equivalent to nationalisation or expropriation". Indirect expropriation is now the dominant form of expropriation claim, and it raises the most difficult questions in this area of the law.

The leading early authority is ***Starrett Housing Corp. v. Iran***,[3] where the Iran-United States Claims Tribunal held that measures taken by a state can interfere with property rights to such an extent that those rights are rendered so useless that they must be deemed to have been expropriated, even though the state does not purport to have expropriated them and legal title formally remains with the original owner.

Creeping Expropriation

A related concept is creeping expropriation, where no single measure amounts to a taking, but a series of measures taken over time has the cumulative effect of depriving the investor of its investment.

[1]United Nations General Assembly Resolution 1803 (XVII), Permanent Sovereignty over Natural Resources, 14 December 1962, paragraph 4.
[2]Article 5(1), Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Federal Republic of Nigeria for the Promotion and Protection of Investments, signed 11 December 1990.
[3]Starrett Housing Corp. v. Islamic Republic of Iran, Iran-US Claims Tribunal, Interlocutory Award of 19 December 1983, 4 Iran-US CTR 122 para 66.

Tribunals assess the measures as a whole, and the date of expropriation is often fixed at the point at which the cumulative effect became irreversible.

The Test for Indirect Expropriation

Arbitral jurisprudence has identified a number of factors relevant to determining whether a measure amounts to an indirect expropriation and they include: (i) the severity of the economic impact and the degree of interference with the investment[4]; (ii) the duration of the as a temporary interference will rarely suffice; (iii) the extent to which the measure interfered with legitimate expectations or frustrated specific commitments made by the state on which the investor relied; and (iv) the character and purpose of the measure as tribunals increasingly examine whether it was a bona fide, non-discriminatory and proportionate exercise of regulatory power.

The Sole Effect and the Police Powers Doctrine

One area of controversy in this field is how to distinguish a compensable indirect expropriation from a legitimate exercise of the state's regulatory power which does not result in compensation. Two broad approaches have emerged.

The "sole effect" doctrine focuses exclusively on the effect of the measure on the investor, regardless of its purpose. In **Metalclad Corporation v. Mexico,**[5] the tribunal held that expropriation includes covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property.

On the other hand, the "police powers" doctrine holds that a bona fide, non-discriminatory regulation adopted in accordance with due process for a public purpose, such as the protection of public health, safety or the environment, does not constitute an expropriation and does not require compensation. In **Methanex v. United States**,[6] the tribunal held that, as a matter of general international law, a non-discriminatory regulation for a public purpose, enacted in accordance with due process, is not deemed expropriatory and compensable unless specific commitments had been given to the investor. Similarly, in **Philip Morris v. Uruguay**,[7] the tribunal held that Uruguay's tobacco packaging regulations were a valid exercise of its police powers for the protection of public health and did not amount to an expropriation.[8]

To address this controversy, modern treaties now contain annexes or interpretive provisions which codify the police powers doctrine and clarify that, except in rare circumstances, non-discriminatory regulatory measures designed to protect legitimate public welfare objectives do not constitute indirect expropriation and do not require compensation.

Compensation and the Measure of Damages

Where an expropriation is lawful, the investor is entitled to the compensation stipulated in the treaty, which is ordinarily the fair market value of the investment immediately before the expropriation or before it became public knowledge. Many treaties specify that compensation shall include interest at a commercial rate from the date of expropriation until the date of payment, and that it shall be

[4] A mere reduction in profitability is insufficient. See *Pope & Talbot v. The Government of Canada,* UNCITRAL Interim Award of 26 June 2000 where the tribunal required a "substantial deprivation" of the investment.
[5] Metalclad Corporation v. The United Mexican States, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000 para. 103.
[6] Methanex Corporation v. United States of America, UNCITRAL Final Award of 3 August 2005, Part IV, Chapter D, para. 7.
[7] Philip Morris Brands Sàrl & Ors v. Oriental Republic of Uruguay, ICSID Case No. ARB/10/7, Award of 8 July 2016.
[8] In Técnicas Medioambientales Tecmed, S.A. v. The United Mexican States, ICSID Case No. ARB(AF)/00/2, Award of 29 May 2003, para. 122 the Tribunal adopted a middle ground by applying a proportional analysis asking whether the measure is proportional to the public interest it pursues and to the protection legally granted to the investment, bearing in mind that the significance of the impact on the investor plays a key role.

freely transferable. Where an expropriation is unlawful, the investor is entitled to full reparation under customary international law.

Expropriation in the Nigerian Context

The Domestic Framework

Nigerian law contains robust protections against uncompensated takings. Section 44(1) of the Constitution of the Federal Republic of Nigeria 1999 (as amended) provides that no movable property or any interest in immovable property shall be taken possession of compulsorily, and no right over or interest in any such property shall be acquired compulsorily, except in the manner and for the purposes prescribed by a law that, among other things, requires the prompt payment of compensation and gives the affected person a right of access to court for the determination of his interest and the amount of compensation.[9] Additionally, section 25 of the Nigerian Investment Promotion Commission (NIPC) Act provides that no enterprise shall be nationalised or expropriated by any government of the Federation, and that no person who owns the whole or any part of the share capital of an enterprise shall be compelled to surrender his interest to any other person, save where the acquisition is in the national interest or for a public purpose and under a law which makes provision for payment of fair and adequate compensation and a right of access to the courts.[10] Section 26 of the NIPC Act further provides for the resolution of investment disputes, including by international arbitration under the ICSID framework.

Nigeria's Treaty Practice

Virtually all of Nigeria's bilateral investment treaties contain provisions protecting investors against expropriation without compensation. As with FET, there is a discernible difference between the older and newer generation treaties. The older generation BITs, such as the UK-Nigeria BIT and the China-Nigeria BIT, contain broadly worded protections covering measures "having effect equivalent to" expropriation. The more modern BITs, such as the Canada-Nigeria BIT 2014, the Nigeria-Singapore BIT 2016 and the Morocco-Nigeria BIT 2016, reflect the contemporary trend towards preserving the state's right to regulate, including through clarification of the circumstances in which non-discriminatory regulatory measures will not constitute indirect expropriation.

ISDS Cases Involving Nigeria

Zhongshan Fucheng Industrial Investment Co. Ltd. v. Nigeria[11] remains the only case in which Nigeria has been held liable in investment treaty arbitration. In addition to the breaches of the FPS and FET standards, the claim concerned the termination of Zhongfu's rights in respect of the Ogun Guangdong Free Trade Zone through the coordinated actions of Ogun State, NEPZA and the Nigerian police, and the tribunal found that Nigeria had unlawfully expropriated Zhongfu's investment in breach of the China-Nigeria BIT.

The two pending cases against Nigeria, Korea National Oil Corporation & Ors v. Federal Republic of Nigeria and Jupiter Lithium Ltd & Ors v. Federal Republic of Nigeria, both arise in the extractive sector, which has historically generated a significant proportion of expropriation claims globally, and may yield further jurisprudence on the application of the expropriation standard to Nigeria's treatment of foreign investors.

[9]Section 44(1)(a) and (b), Constitution of the Federal Republic of Nigeria 1999 (as amended).
[10]Section 25, Nigerian Investment Promotion Commission Act, Cap. N117, Laws of the Federation of Nigeria 2004.
[11]Zhongshan Fucheng Industrial Investment Co. Ltd. v. Federal Republic of Nigeria, UNCITRAL ad hoc arbitration, Final Award of 26 March 2021.

Practical Guidance

For foreign investors in Nigeria: investors should ensure that their rights – particularly licenses, leases, concessions and allocations of land – are properly documented and perfected under Nigerian law, as a tribunal will first look to domestic law to determine whether the investor held the property rights it claims were expropriated. Investors should also keep contemporaneous records of the value and performance of the investment, as these will be critical to establishing quantum, and should engage promptly with available administrative and judicial remedies where adverse measures are threatened.

For the Nigerian state and its agencies: where the revocation of a licence, the termination of a concession or the acquisition of property is genuinely required in the public interest, the relevant authority should ensure that it acts under a clear legal basis, follows due process, avoids discrimination, and makes provision for compensation. Federal and sub-national authorities alike should recognise that their conduct is attributable to the Federal Republic of Nigeria on the international plane, as Zhongshan Fucheng demonstrates.

For Nigerian investors abroad: the expropriation protection is equally available to Nigerian investors operating abroad under the BITs to which Nigeria is a party. By way of illustration, a Nigerian telecommunications operator whose licence is revoked without justification and transferred to a state-owned competitor, or a Nigerian manufacturer whose plant is seized by a host government, may have a basis for an expropriation claim. Nigerian investors should therefore structure their investments so as to fall within the scope of an applicable treaty, before any dispute arises.

Conclusion

The protection against expropriation remains a cornerstone of international investment law. While international law recognises the sovereign right of a state to take property, it requires that any taking (i) be for a public purpose, (ii) non-discriminatory, (iii) in accordance with due process and (iv) accompanied by compensation. The modern focus of the standard has shifted from outright nationalisations to indirect and creeping expropriation, where the central challenge is to distinguish compensable takings from legitimate regulation in the public interest.

For Nigeria, the standard presents both risks and opportunities. As a host state with a significant extractive sector, Nigeria faces exposure to expropriation claims where licences, concessions and other rights are revoked or interfered with without due process or compensation. At the same time, Nigerian investors operating abroad may invoke the protection under Nigeria's BITs that are in force to safeguard their investments.

The next instalment in the TEMPLARS ISDS Series will examine the Most-Favoured-Nation and National Treatment standards, while the final instalment will address the defences available to Host States, and conclude the Series.

If you require any further information, do not hesitate to contact us.