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Özge Tosun

The Law of Political Risk Insurance

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Preface

I am thankful to King's College London for the research allowances; this book meets its readers in the end of opportunities King's provided to me. Many thanks are due to Claire Jervis, distinguished visiting researcher from King's College London who provided me with insight despite the paucity of her time and taught me the insignificance of the borders. And my gratitude goes to Ms. *Laura HOFMANN* from Springer whose endless support and understanding have allowed this book to reach readers. Warm thanks should go to my family, my mother *Peruze TOSUN*, my father *Metin TOSUN* and my sister Dr. *Özlem Deniz TOSUN* who have always stood by me in pursuit of my dream.

In preparing this book, I have benefited from the dissertations, articles or books of numerous academics; profound however, I must mention in particular two esteemed academics. I want to express my thanks to Associate Professor Kübra YETİŞ ŞAMLI from Istanbul University Faculty of Law who supervised me during my PhD studies. It was her persistence and dedication which encouraged me to publish my first book and which formed the very basis of this project.

In June 2021, in the shadow of COVID-19 outbreak and while strict travel restrictions were still in force, the feedback of Professor *Özlem GÜRSES* from King's College London on my research was the beginning of this journey, and without her supervision, never-ending support, sharp guidance and belief, this journey could have not been accomplished. I want to express my deepest and special gratitude to Professor *GÜRSES* for her outstanding contribution to my academic career and for everything in making this book possible. This book is dedicated to *Professor Özlem GÜRSES*.

Istanbul, Türkiye — Özge Tosun

Contents

Abbreviations

AAD	Arbitration award default
ACIA	ASEAN Comprehensive Investment Agreement
Arb.	Arbitration
art.	Article
BIT	Bilateral investment treaty
DFC	International Development Finance Corporation
DHAMAN	The Arab Investment & Export Credit Guarantee Corporation
DOJ	Denial of justice
ECA	Export Credit Agencies
ECHR	European Court of Human Rights
Ed	Editor
ed.	Edition
e.g.	Example
et al.	et alia 'and others'
etc.	Et cetera
et seq.	*et sequens*, *sequential* 'and the following'
FDI	Foreign direct investment
fn.	footnote
Ibid	ibidem 'in the same place,'
ICIEC	The Islamic Corporation for The Insurance of Investment and Export Credit
ICC	International Chamber of Commerce
ICISA	International Credit Insurance & Surety Association
ICSID	International Centre for Settlement of Investment Disputes
i.e.	id est
ILC	International Law Commission
ILO	International Labour Organization
IMF	International Monetary Fund
MIGA	Multilateral Investment Guarantee Agency

no.	Number
OECD	Organisation for Economic Co-operation and Development
OFAC	U.S. Treasury's Office of the Foreign Asset Control
OPIC	The Overseas Private Investment Corporation
para.	Paragraph
P	Page
PCA	Permanent Court of Arbitration
pp	Pages
SEC	The U.S. Securities and Exchange Commission
UNCITRAL	The United Nations Commission on International Trade Law
UNCTAD	United Nations Conference on Trade and Development
v.	versus
Vol.	Volume
WTO	World Trade Organization

Chapter 1
Introduction

An investment made with the purpose of obtaining a lasting interest in a country other than that of the investor, as is the case in developing countries, may face risks associated with doing business in a territory that does not enjoy a stable legal framework, political composition or governance. In the world of foreign investment, risky lands offer concessions or means alike to attract investments. However, reliance on the host country's statements can be an obedience to the unexpected. Once the investment is underway, it may be a point of no return, where the statements blur, and the host state takes advantage of the investor and behave recklessly. Therefore, in exchange for the potential of the risk exposure, investors should receive more than just words from the party with whom they enter into a transaction. In that regard, a third party's backing in the form of insurance coverage may address the investor's concerns.

Conventional insurance contracts are designed to mitigate losses, however, as this book will reveal, the presence of political risk insurance (PRI) may serve to avoid the occurrence of risks. In addition, PRI establishes a different relationship compared to conventional insurance; hence, it can be said that PRI is insurance for exceptional circumstances. Put differently, the gamut of perils that are covered by PRI policies does not fall within the scope of the conventional insurance, on the contrary, they are the 'excluded perils' of the customary insurance practices. In most cases, it is the sovereign who causes the peril whether through its direct or indirect actions. The primal need for the PRI coverage rests on the fact that sovereign powers may be predisposed towards interfering in the business activities of foreign investors. Thus, PRI acts as a form of protection to deter the wrongful sovereigns.

Political risks possess several defining attributes; They often develop gradually, and the consequences thereof may unfold over months or years. Tangible harm can arise without a physical injury befalling the investor's assets. Hence, one should anticipate that such risks may manifest in various forms and make it troublesome to trace the wrongdoer's footprints. The means by which the sovereign may achieve its objectives can take one of the following forms: unfair or arbitrary treatment by the sovereign power that deprives investors of their proprietary rights, transfer

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restrictions; currency inconvertibility; the sovereign power's failure to honor its financial obligations; wrongful or unfair calling of guarantees, denial of justice; and arbitration award default.

In fact, certain political risks do not require deliberate actions from the sovereign, by contrast, these events are the ones over which sovereigns have no or limited control. Thus, risks such as war, terrorist attacks and other means of political force majeure or political violence deserve a distinct focus. International investments are shaped based on the mutual benefits and interests of the parties involved. While developing or less developed countries need capital export to support their economic growth and infrastructure projects, investors from the developed countries on the other hand engage in business with developing countries for various purposes, including political reasons, and for the purposes of expanding and diversifying their operations, accessing necessary natural resource and skilled labor force, lowering production costs and lastly even mitigating global warming. Despite the global economy having been following this economic trend within the last decades, wars and turmoil of every sort began to grip the world. Decision-makers of sovereigns kept pace with nationalist trends, and in so doing, led the foreign capitals to encounter severe reactions. Consequently, it may be accurate to say that PRI functions like an airbag, allowing investors to obviate the disaster when foreign capital and the sovereign clash.

The second chapter in this book recaps the history of PRI and the circumstances that led to the development of PRI. The following chapter employs a comparative analysis to make a distinction between regular insurance contracts and PRI contracts. Chapter 4 establishes the link between the three columns of international investment. The fifth chapter introduces the parties to PRI contract, provides an overview of the operations of global players, aims to fill the gap in the terminological differences and evaluates virtual form of investment along with the old-fashioned forms. In addition, it puts forward a brief discussion on recent political facts. In the sixth chapter, the discussion focuses on the techniques in mitigating the risks and losses.

The seventh chapter outlines forms of protection that investment treaties or agreements concluded between foreign investors and host states can offer. Chapter 8 presents the incidents that foreign investors fear the most. This chapter sets forth each political risk in great detail, and in doing so and by bearing the technological advancement in mind, visualizes what may be on the horizon. Moreover, it examines the legal concepts within the meaning of investment arbitration that serve to protect foreign investments. Chapter 9 addresses the incidents that are not covered by the PRI policies. The subsequent chapter explores the extent of the insurer's monetary obligation and distinguishes the mechanics of compensation. The book then proceeds to argue the concept of subrogation, assesses the place where the insurer stands and tackles the question by touching upon the immunity of the Sovereign. The same chapter provides a quasi-fruitful basis for insurers to induce treaty provisions to enable subrogation. And Chap. 12 concludes with the dispute resolution clauses and laws to govern both the PRI and the investment contract.

Chapter 2
The Origins of and the Need for the PRI

International trade gained momentum within the twentieth century, and less developed countries became more familiar with the concept of capital export. Investors were attracted by opportunities such as building and operating infrastructure projects in foreign countries or extracting and processing raw materials. While some of these less developed countries embraced liberalization as an end in itself, the idea of foreign nationals owning or controlling resources were seen as exploitation in the eyes of nationals of countries that either failed in or stood against liberalization. In addition, the way that the benefits were distributed intensified the social pressures leading to unpredictable interventions by the host states in foreign investments.[1]

The potential political risks compelled investors to seek assurance for their overseas transactions. In response to these needs, governments endeavored to provide guarantees to their investors. In the nineteenth century, state governments in the United States provided guarantees for the payment of interest and principal on railroad bonds sold in the capital markets of London and Paris.[2] As alluded, PRI did not arise miraculously; opinions diverge on its timeline. Some scholars assert that it originated from the marine insurance coverages provided to exporters.[3] Some authors suggest that PRI can be traced back to the inception of UK Export Finance in 1919 and the establishment of a guarantee facility for US investors in war-torn Europe under the Marshall Plan.[4] Some scholars on the other hand opine that true birth of private political risk insurance industry dates back to the 1930s when Lloyds of London began offering coverage for political risks.[5] The experience of the

[1] Rubins and Kinsella (2005), p. 5.

[2] For detail See Martin (1967), p. 282.

[3] Paul (1987), p. 710.

[4] Tan (2015), p. 175. Also see Jensen and Young (2008), p. 529. Also see Karagöz (2018), pp. 119, 131–134. Also see Papanastasiou (2021), p. 161, also see Khachaturian (2006), pp. 1044–1045, finally see Diaconis (1989), p. 272.

[5] DeLeonardo (2005), p. 742.

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U.S. with PRI coverage began in 1948 through the 1948 Economic Corporation Act.[6] The US government launched a national investment program to contribute to rebuilding of Western Europe.[7] Initially, the US Investment Guarantee Program only covered non-convertibility risk. Eventually, the coverage expanded to include expropriation risk and after 1956 war risk.[8] From this date onwards the coverage broadened to encompass the risks of revolution and insurrection.[9]

In the late 1950s, a working group of Council of Europe's Consultative Assembly proposed a scheme to provide coverage against non-commercial risks.[10] This scheme was one of the first ones designed on a multinational level.[11] Following attempts to establish a multinational insurance program that designed to cover investments by the Europeans in the African countries failed. These attempts were not an end point but marked the beginning of a promising process. OECD drafted a report on 'Establishment of a Multilateral Investment Guarantee Corporation'.[12] On a global scale, the idea of establishing a political risk insurance provider was discussed at UNCTAD I. After pressure of OECD as well as the United Nations, the World Bank drafted the International Investment Insurance Agency's Articles of Agreement in 1966. However, U.S., the U.K., Japan, Canada and Germany had reservations. This insurance scheme was criticized due to the lack of the host state's financial participation and its bearing of a portion of the risk. Subrogation of the insurance agency to the claim of a compensated investor was another intractable problem.[13] Although amendments were made in 1972, differences in opinions stalled the negotiations.[14] In order for a political risk insurance, fruitless attempts did not come only from institutions; private bankers also made proposals for an insurance concept against political risks.[15]

In the twentieth century, a considerable number of foreign investments were exposed to political risks.[16] In the 1960s, widespread expropriation by the Castro regime after the Cuban revolution increased the need for insurance coverage at a multinational level. For the same reason, under the US insurance program, the

[6] See Peinhardt and Allee (2016), p. 211 and Martin (1967), p. 284, also see Dolzer and Schreuer (2012), pp. 228–229, McKellar (2010), p. 11.

[7] Rowat (1992), p. 119.

[8] Martin (1967), p. 284.

[9] Diaconis (1989), p. 272.

[10] Also see Radi (2020), p. 231.

[11] Berger (1988), pp. 23–24.

[12] Martin (1967), p. 286.

[13] Karagöz (2018), p. 106.

[14] Khachaturian (2006), pp. 1048–1049.

[15] Berger (1988), p. 22.

[16] Salacuse (2016), p. 382.

definitions of war and expropriation were implemented with broad language in the Foreign Assistance Act of 1961.[17]

The twenty-first century has also witnessed significant incidents giving rise to political risks. In the last twenty or so years, foreign investments in developing countries have boosted.[18] September 11, 2001[19] was a threshold in PRI that led to the inclusion of terrorism risk coverage alongside other risks, requiring an additional premium. Furthermore, the Turkey and Madrid bombings shifted the perception of the region as risky, and terrorist attacks added a remarkable level of uncertainty to the so-called risk-free legacy of the developed countries.[20] These attacks delivered a clear message that every place can be a potential target for political violence,[21] and due to the interdependent nature of national economies, political risks can have an effect similar to that of a butterfly. The occurrence of a political risk in one state may pose an economic threat to any other state or its exporters.

Terrorism coverage responded to the needs by offering investors a means for insuring against losses arising out of any form of violence that results in mass destruction. According to some scholars, after September 11, despite the obvious need, Exim banks ('ECAs'[22]) unexpectedly, inclined to stop offering coverage.[23] In this century, the US subprime mortgage crisis and global economic crisis drove sovereign powers to act with nationalist motives and threaten the profitability or continuity of investments. Moreover, investors encountered the quasi-war concepts of proxy wars and annexations. Viewed from this perspective, political risks are akin to taking a risky leap, and PRI acts as a parachute, providing a safe landing. The insurance coverage is vital for the investor insomuch as in its absence, the investor may not ever need it again. However, PRI was not then and is not now the main mechanism investors prefer, as we shall explore in the subsequent chapters, investors are prone to opt for protections provided by international law.

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[17] Peinhardt and Allee (2016) p. 213, also see Martin (1967), p. 286. With the passage of this Act, investment(political) insurance against political risks began to be supported by the US government. See Hansen (2004), p. 80.

[18] Torrado (2005), p. 304.

[19] McKellar (2010), pp. 18, 49.

[20] Also see Jarvis Darryl and Griffiths (2007), p. 9.

[21] DeLeonardo (2005), p. 772.

[22] ECAs may be in the form of Export-Import banks and abbreviated to 'Exim bank'. Export Credit Agency is an agency in a creditor country that provides insurance, guarantees, or loans for the export of goods and services. Please visit IMF library, available at https://www.elibrary.imf.org/display/book/9781589060609/back-1.xml accessed 02.09.2024. *Heard* and *Laryea* define them as "*governmental or intergovernmental agencies or institutions in creditor-countries that provide insurance, guarantees or loans for the export of goods, services or capital by businesses and entities from the creditor-countries to other countries, usually debtor-countries considered to present high sovereign risks*." See Heard and Laryea (2021), p. 616. For Exim banks also see Williams (1993), p. 89 et seq. For more about ECAs, please visit: https://www.eca-watch.org/ accessed 02.09.2024.

[23] Brown (2004), p. 20.

Online Database

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Chapter 3
Insuring the Loss Through a Contract

3.1 Identifying Insurance Contracts

Insurance contracts can be defined in numerous ways, according to *Merkin*, an insurance contract is "*a contract under which one person (the insurer) is legally bound to pay a sum of money or its equivalent to another person (the insured), upon the happening of a specified event involving some element of uncertainty as to whether it will occur (or, if it is certain to occur, as to when it will occur), and which event adversely affects the insured's interest in the subject matter of the insurance.*"[1] Another esteemed scholar contributed to terminology with the following definition, in his view; "*insurance is a contract whereby one person (the insurer), agrees to pay money or to provide a corresponding benefit on the occurrence of an event, which is both certain and adverse in return for money, usually called a premium*".[2]

The definition of a contract should be both broad and narrow in scope.[3] Put differently, it should be broad enough to encompass the basic elements of the contract, such as what parties owe to one another and the relation upon which the contract is built. In addition, the definition should also be narrow and disregard the issues that are not vital to readers. The definitions provided above encompass essential components of an insurance contract and offer different perspectives. However, in our opinion, insurance can be characterized as involving the following:

[1] Merkin (2013), pp. 1–3, for other definitions please see Merkin and Steele (2013), pp. 27, 28, 42, 43.

[2] Clarke (2013), p. 5, for another definition see Eggers and Picken (2018), p. 9. Another scholar defines in the following way "*a contract by which one party (the insurer) for a stipulated consideration or "premium" agrees to compensate another party (the insured) for loss on a specified subject by the happening of specified perils*." Salacuse (2013), p. 246.

[3] According to one scholar, "*Definitions are like belts. The shorter they are, the more elastic they need to be. A short belt reveals nothing about its wearer: by stretching, it can be made to fit almost anybody*." For the quotation of Stephen Toulmin, see Rubins (2004), p. 284.

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the meaning, uncertainty and the impact of the risk, parties' monetary obligations and form of those obligations (if any). Moreover, as the following chapters will reveal, the party entitled to compensation can be referred to by different terms in different jurisdictions. Finally, one must note that the insured must have an insurable interest.[4] In the exercise of PRI, the insured must hold a title to tangible or intangible asset (own the asset or hold a right of enjoyment over the asset) and moreover, its interest must be 'at risk'.[5]

Even if one were to argue that the subject matter to be insured is of no consequence and that interest of any kind can be insurable, the loss caused by the materialization of the risk must have a calculable monetary value.[6] It's important to note that mental distress, being subjective in nature, are types of harm whose value cannot be objectively determined. Grief, anger, agony or disappointment -feelings specific to human beings- cannot be assessed and be fixed by monetary means.[7] It is a hazy area where a fine line cannot easily be drawn. Damages of a moral character are subjective; consequences of the incident may vary from one person to another. Valuation of an incorporeal damage is difficult to estimate or incapable of quantification and thus, its reparation function does not place the legal person in the situation where it could have been prior to occurrence of the risk, and neither monetary means can eradicate the signs of moral harm. In light of these facts and within the context of investment law, we define the insurance contract as *a contract by which the insurer undertakes; in exchange for the agreed contribution (premium), to provide coverage to insured or policyholder against an event occurrence of which is uncertain, adverse and upon the occurrence of this insured event, whether in cash or in kind, to compensate the concerned person's interest that is measurable by money.*

Insurance contracts are synallagmatic, executed on a reciprocal basis. The obligation of one party is correlative to the obligation of the other. The insurer assumes the duty to cover and is responsible for the compensation if the insured event occurs. The commencement of the insurer's liability may differ among jurisdictions, unless the law governing the contract states otherwise, the insurer's liability should begin when the premium is paid or in case of installments, when the first installment is paid. However, in an unconventional insurance concept like PRI, to the extent

[4] Also see Roach et al. (2022), chapter 27.

[5] Budd (1993), p. 30.

[6] In the view of the OECD Insurance Committee, the technical conditions that make a risk insurable are: "assessability (probability and severity of losses should be quantifiable); randomness (the time at which the insured event occurs should be unpredictable when the policy is underwritten, and the occurrence itself must be independent of the will of the insured); mutuality (numerous persons exposed to a given hazard should be able to join together to form a risk community within which the risk is shared and diversified)." See Gordon (2008), p. 93.

[7] *Dumberry* argues that even if the amount allocated will admittedly often be largely symbolic, monetary compensation remains the appropriate remedy for moral damages affecting a corporation. See Dumberry (2012), p. 228.

possible,[8] it should be left to the parties' discretion. For instance, the period of coverage is of significant importance in construction projects, hence, parties must state the dates when the liability of the insurer commences and expires.

Insurance contracts may be classified as guarantee contracts. However, the warranty function they serve is not identical to the ones provided by banks. As some may know, under German and Turkish law, insurance contracts differ from letter of guarantees on the basis of; the conditional nature of the insurance contract, the law applied thereto and the obligation of the parties. Finally, although an ECA incorporated in the form of an Exim bank may provide a PRI coverage, insurance contracts are not blanket guarantees,[9] the insured party is a juridical person and a merchant rather than a real person consumer, and the insured item is not money deposited in a bank.

Insurance contracts are also aleatory in nature. In this regard, it is worth noting the difference between wagering contracts and insurance contracts. In a wagering contract each party, by entering into the contract, takes the risk of a certain loss and depending on the occurrence or non-occurrence of an event, one party wins from the other. Simply put, a wagering contract is not built upon a win-win basis. In a PRI contract however, one party pays a premium for the protection of his/her interest and even if the risk is not materialized and notwithstanding the fact that the premium is paid, the insured still benefits from being relieved from a possible financial loss. Besides, if the insured is a bank, it may take advantage of risk mitigation by using the insured credit amounts in calculating its capital requirements. In accordance with the Basel Accord, banks are allowed to utilize insurance policies for capital relief so that they may allocate less capital against the risk of debtors' default.[10]

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[8] Turkish Commercial Code (TCC) deals with the obligations of the parties to insurance contracts. In accordance with art. 1421 of the TCC, insurance coverage begins upon the payment of the premium or its installment. TCC is available at http://www.aida.org.uk/pdf/turkish%20insurance%20contract%20law.pdf accessed 02.09.2024. A similar provision exists in German Insurance Contract Act 2008, according to section 51 "*The commencement of the insurance cover may be made dependent on the payment of the premium insofar as the insurer has drawn the policyholder's attention to this condition in writing in a separate communication or by means of a conspicuous note in the insurance policy.*" However, if PRI is assumed to cover jumbo risks, (it may be so in accordance with the subparagraph 2(2) of section 210), parties will be free to decide the terms of their PRI contract since section 210 of the same Act states "*The restrictions on the freedom of contract under this Act shall not apply to jumbo risks*". English version of the Act is available at https://www.gesetze-im-internet.de/englisch_vvg/englisch_vvg.html#p0015 accessed 02.09.2024.

[9] A blanket guarantee is a declaration by authorities that, in addition to the protection provided by limited coverage deposit insurance or other arrangements, certain deposits and perhaps other financial instruments will be protected. Please visit: https://www.dicgc.org.in/pdf/CorePrinciplesOfIADI_Nov2014.pdf accessed 02.09.2024. Also see HAY (1997), p. 158.

[10] Section 30.19 of Basel framework reads as follows "*Under the AMA (Advanced Measurement Approaches), a bank will be allowed to recognize the risk mitigating impact of insurance in the measures of operational risk used for regulatory minimum capital requirements. The recognition of insurance mitigation will be limited to 20% of the total operational risk capital requirements calculated under the AMA*". For the criteria set for insurance policy as well as insurance companies,

Finally, in conventional practice, agents and brokers may execute the contracts. Using intermediaries, however, may raise some concerns regarding the scope of the authority conferred upon the intermediary. Therefore, actions of the intermediary may require a ratification. Put differently, in order to justify whether the insurer is directly bound by the transactions concluded by the intermediary, the insured may wish to ascertain whether the intermediary has actual or apparent authority. Besides, in conventional insurance practice, intermediaries may assume pre-contractual onuses namely the duty to inform, to advise or to warn. The relation between intermediary and the insurer sets whom to bear the consequences of violating these duties. Prudent merchant foreign investors, however, cannot benefit from the principles meant to protect real person insureds. PRI might seem old-fashioned; due to specificity of the investments and the amount of the coverage, due diligence is a must. Thus, the last thing parties may want is an envoy (intermediary) who may, even unintentionally, bar or hinder a direct correspondence and cause delays in the circulation of documents.[11]

3.2 PRI Defined by Artificial Intelligence

Artificial intelligence (AI) has literally taken the world by storm; its use has proliferated in insurance practice, as well as in all aspects of life. In insurance, AI can provide accurate data and lower the number of human-induced errors, in addition AI can facilitate the performance of contractual obligations. In the following sections, we will discuss the impact of artificial intelligence on the PRI, in doing so we wanted to shed light on the prospective role of technology in PRI. As we applied to AI (namely 'ChatGPT') it provided a basic and expected definition for PRI,[12] surprisingly, it claimed that PRI might offer coverage for evacuation costs or expenses related to relocating the insured's operations. The coverage for these expenses is not irrational; by contrast, it will serve to mitigate the insurer's loss. By way of illustration, in trade credit insurance, in case the buyer refuses to receive the goods, the insurance policy may cover the additional costs (such as freight, demurrage, customs clearance, and storage at customs or insurance) accrued at the time of repatriation of the goods to the country of the supplier (exporter).

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also see section 30.20 Available at https://www.bis.org/basel_framework/index.htm?export=pdf accessed 02.09.2024.

[11] Also see Gilbert (1986), pp. 407–415.

[12] According to ChatGPT, PRI is "*a type of insurance that protects businesses, investors, lenders, and other parties from losses resulting from political risks such as political violence, expropriation, currency inconvertibility, and other forms of government action or inaction that can adversely affect investments or operations in foreign countries*."

3.3 A Humble Attempt to Define PRI

PRI can serve as a management strategy in unfamiliar environments that require attention.[13] It covers a composite of different threats[14] and serves as a major tool; to shift political risks from the foreign investor to the insurance provider[15] and to assist investors and lenders in reducing the probability or severity arising from the adverse actions or inactions by host governments.[16] This specialized line of insurance protects traders, investors and lenders against non-commercial risks that can disrupt the successful completion of trade contracts, and the effective ownership or operation of investments.[17]

As the name suggests PRI, in short, is the insurer's payment guarantee to natural or juridical persons (investors) against losses arising from political risks. This simplified definition fails to highlight the most notable part of PRI, which is the various forms of political risk and is therefore far from being accurate. As will be elucidated below, expecting a consensus on a single definition is impractical; however, some may wish to delve into its meaning.

Risk stands as the probability of an event; in insurance practice, it signifies the deteriorative nature of the event. For instance, in life insurance, it takes the form of an event, the occurrence of which is only a matter of time. In PRI, however, it indicates the possibility of investors not reaping benefits from their investment due to events beyond their control. The term 'country-risk' on the other hand captures various risks, including those political.[18] Country risk denotes a variety of instances such as macroeconomic risks (instability, inflation) and environmental risks (natural disasters and labor disruptions).[19] Hence, the meaning of the term is broad in scope and echoes the risks of all forms with regard to the country in question. Amidst

[13] Brink (2016), p. 4.

[14] DeLeonardo (2005), p. 739.

[15] Hyder and Attanasio (2021), pp. 450–451.

[16] Baroudi (2017), p. 406.

[17] Wagner (2012), p. 97.

[18] OECD classifies countries into eight categories (according to the likelihood of whether they will service their external debts). The indictors are basically as follows; general moratorium on repayments, political events and/or economic difficulties which prevent or delay the transfer of funds paid in respect of the credit, legal provisions adopted in the obligor's/guarantor's country declaring repayments made in local currency to be a valid discharge of the debt, any other measure or decision which prevents repayment under a credit, cases of force majeure (war [including civil war]), expropriation, revolution, riot, civil disturbances, cyclones, floods, earthquakes, eruptions, tidal waves and nuclear accidents) See OECD's Arrangement on Officially Supported Export Credits available at https://one.oecd.org/document/TAD/PG(2022)1/en/pdf accessed 02.09.2024. Also see Burnett and Bret (2017), pp. 30–31.

[19] In the wording of the *Tidewater* tribunal "*country risk premium quantifies the general risks, including political risks, of doing business in the particular country, as they applied on that date and as they might then reasonably have been expected to affect the prospects, and thus the value to be ascribed to the likely cash flow of the business going forward*." see para. 186 of the award dated 13.03.2015. Available at https://www.italaw.com/sites/default/files/case-documents/italaw4206_0.

almost unlimited definitions of 'political risk' we simply chose to quote a few to create a distinction. In the narrowest sense it is "the amalgam of unwanted consequences of political activity[20]", or "*the possibility that investments will be impaired by certain types of government measures*".[21] One scholar proposes the following definition which is "*governmental or societal actions and policies, originating either within or outside the host country, and negatively affecting either a select group of, or the majority of, foreign business operations and investments*.[22]" While other scholars extend this definition to "*governmental or societal actions, policies or omissions that negatively affect the business operations and investments of a specific firm or a group of firms in the form of physical damages or economic losses in its home or a host country*[23]". Finally, *Rubins and Kinsella* introduced a definition and referred to facet of political risk insurance that is most salient. According to authors, political risk is "*the probability that a host government will, by act or omission, reduce the investor's ability to realize an expected return on his investment*[24]".

Political risks manifest in foreign lands, and the sources of this risk are multifaceted, but they mainly involve politically motivated actions/omissions by the ruler of those lands that sweep away foreign investments. It is therefore, prior to defining PRI, it is essential to explain some key terms peculiar to this concept of insurance. Every sovereign craves to control, whether of its nationals or of others, the actions taken on its territory. Hence, *sovereignty* can be defined as the public authority that commands in civil society, and orders and directs what each citizen is to perform to obtain the end of its institution.[25] S*overeign* on the other hand, is the person invested

pdf accessed 02.09.2024. Also see Burgstaller and Ketcheson (2017), p. 195 and Dorobantu et al. (2016), p. 219, also see the chapter dealing with the valuation of investment.

[20] Jarvis Darryl and Griffiths (2007), p. 11.

[21] Kantor et al. (2011), p. xx. (Introduction part).

[22] Simon (1982), p. 68.

[23] See Braun and Fischer (2018), p. 4. Due to its broad scope, political risk has been defined in several ways, for instance, in some authors' view, political risk is "*the risk associated with the effect that actions of agents pursuing political objectives may have on the value of the assets of agents pursuing economic objectives.*" See Restrepo et al. (2012). Another scholar defines political risk in the following words: "*the probability that the profitability of an investment be negatively affected by circumstances ascribable either to unforeseen changes (e.g. revolutions, even when linked to democratization processes) in the domestic or international political arena, or to governmental policy choices affecting the international investor's property rights.*" See Emma Sottilota (2013), p. 6. One author opines that political risks are "*threats to the profitability of a project that derive from some sort of governmental action or non-action rather than from changes in economic conditions in the marketplace*." See Moran Theodore (1999), at 3 [citing Harvard Professor Louis Wells, Jr.] as cited in Ibid, p. 3. Some scholars also define as "*the risk that a sovereign host government will unexpectedly change the 'rules of the game' under which businesses operate*." See Butler and Joaquin (1998), p. 599. For other definitions please see Jiang et al. (2021), p. 127. Also see Han et al. (2018), p. 124. Similarly, see McDowell (2021), p. 639 and finally, see Tan (2015), p. 180.

[24] Rubins and Kinsella (2005), p. 3.

[25] Sovereignty is also defined as "*the supreme and independent authority of the nation state within its own territory*". For the quoted definition and detail, please see Salacuse (2013), p. 76.

in with the authority.[26] Lastly, the term '*political*' denotes matters pertaining to politics; of or relating to the conduct of government.[27]

Despite its scope, the literal interpretation of '*political risk insurance*' may mislead those unfamiliar with this concept. At first glance, for some, PRI may connote an insurance coverage against the harms resulting from political disputes. A more accurate phrase could have been 'sovereign risk insurance[28] (SRI)' which better captures what this insurance protects against. Although practitioners employ the term 'investment insurance', some may suppose that it provides coverage against physical damage that investments incur, whereas most political risks are intangible in nature. In order to avoid confusion and to highlight its substantial component, in this study we opt for 'political risk insurance' ('PRI').

As all contracts do, PRI contracts encompass a purposive activity where the foreign investor and the insurer aim to gain a benefit. Since risks are diversified and complex, in our view, PRI in the broadest sense can be defined as an *insurance that provides coverage against losses foreign investors incur as a result of: a) events, namely; arbitrary, discriminatory or unfair measures or decisions attributable to the host state that deprive the investor of the enjoyment of proprietary rights and adversely affect fair, reasonable, justifiable and legitimate expectations*[29] *from*

[26] de Vattel (1852), pp. 71, 84. After discussions at the deliberations of 'Draft articles on Jurisdictional Immunities of States and Their Property', the International Law Commission(ILC) employed "sovereign authority" as the corresponding term for "prerogatives de la puissance publique de I'Etat". According to some members of the ILC, this French text appeared to be intended to refer to public institutions and to distinguish them from private institutions. Although some members took the view that "sovereign authority" was associated with the international personality of the state they expressed that "governmental authority" was the nearest translation of this French term within the context of the draft articles. Please see footnote 36 at page 16 and 17 of the commentary to 'Draft articles on Jurisdictional Immunities of States and Their Property'available at https://legal.un.org/ilc/texts/instruments/english/commentaries/4_1_1991.pdf accessed 02.09.2024. Also see Fox and Webb (2013), pp. 302–303.

[27] Definition can be found in the Black's Law Dictionary. (In this book references in regard to the Black's law Dictionary were made to its ninth ed.).

[28] Also, see Heard and Laryea (2021), p. 617.

[29] The ECHR uses this concept in its jurisprudence, See Ratner (2008), p. 498. According to *Newcombe*, legitimate expectations of the investor must also be assessed in the context that investments are made for commercial returns and inevitably involve risk. See Newcombe and Paradell (2009), p. 350. In *Potočnik's view*, legitimate expectations are based on the concept of specific assurances made by the host state to the investor at the time the investment was made. See Potočnik (2019), p. 158. According to *Tudor*, following criteria are of significance. Investor's expectations must stem from an authority's (State) conduct, the expectations must be reasonable and justifiable in the light of circumstances and finally the investor's loss must be directly linked to or caused by the host state's failure to respect these expectations. Tudor (2008), pp. 166, 168. And finally, in the view of the ECHR, to be legitimate, the expectation must be of a nature more concrete than a mere hope and be based on a legal provision or a legal act such as a judicial decision, bearing on the property interest in question. The court also opines that a license provided to a company becomes component part of its property and if a contract is signed then the legitimate expectation is based on a legal act which has a sound legal basis. See "page 9 of the Guide on Article 1 of Protocol

his/her investment or b) acts and/or omissions in the form of political violence/force majeure that takes place in the territory of and attributable to the host state.

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