

HIDDEN EXPROPRIATION

AND INVESTMENT PROTECTION –

GLOBAL BEST PRACTICES

AND GEORGIA'S

PATH FORWARD

Georgia has long been committed to becoming a regional leader in attracting foreign investments. Achieving this goal requires excellence in many areas, but the competition for foreign capital is largely a competition of attractive legal frameworks. Investors are naturally drawn to jurisdictions that offer clear, robust guarantees of their rights, along with swift dispute resolution by competent and impartial bodies.

Among the most crucial guarantees for investors are protections against uncompensated seizure, nationalization, or the loss of economic value of their investments. This uncompensated “expropriation,” as referred to in legal documents, can take many forms:

- **Direct expropriation** occurs when an investor is deprived of the ownership of an investment or when the investment is physically and permanently seized.
- **Indirect expropriation**, while not meeting the formal criteria of direct expropriation, has the equivalent economic effect, effectively “hollowing out” the elements of ownership.

Indirect expropriation typically occurs when an investor retains ownership or possession of the investment, but

state measures deprive the investment of its economic value and purpose. Such measures may serve legitimate public interests, such as regulations for environmental protection, health, or taxation. However, they may also constitute unjustified and uncompensated expropriation.

For instance, arbitral tribunals have, on numerous occasions, found that regulations imposed for environmental, health, or taxation purposes led to expropriation, even when the investor technically remained the owner. These regulations stripped the investment of its economic value, effectively hollowing out the investor’s ownership rights.

By its nature, indirect expropriation is concealed, making its detection and proof significantly more challenging. Importantly, there is no mechanical formula to distinguish it from genuine regulation.

INTERNATIONAL TRENDS IN DEFINING “INDIRECT EXPROPRIATION”

Although most international treaties and laws governing investor-state relations protect against indirect expropriation, they often leave the term undefined, subjecting it to tribunal interpretation.

According to the Organisation for Economic Co-operation and Development (OECD) – one of the primary contributors to global investment policies – 82% of international investment treaties in force as of 2021 provided protection against indirect expropriation without specifying the scope or conditions of the concept.

However, this status quo is evolving. In May 2003 the first treaty definition of “indirect expropriation” was agreed upon between the United States and the Republic of Singapore. Since then, more treaties have included definitions of what constitutes indirect expropriation.

Currently, 24 percent of bilateral international investment treaties define indirect expropriation, and this figure rises to 73 percent in multilateral treaties. Notably, the trend is accelerating, with nearly all recently concluded treaties including a definition of indirect expropriation.

“INDIRECT EXPROPRIATION” IN GEORGIA AND FUTURE PROSPECTS

Expropriation in the absence of pressing social need and without compensation is prohibited by the Constitution of Georgia. Moreover, protections against expropriation are commonly found in Georgia’s international treaties. However, what constitutes hidden or “indirect” expropriation remains largely unaddressed.

This may soon change. The draft Law of Georgia on Investment Protection, which is expected to replace the current Law of Georgia on the Promotion and Guarantees of Investment Activity, is anticipated to include a definition of indirect expropriation. As a result, this national law will directly define indirect expropriation, offering clarity and protection to all investors, regardless of their country of origin or any applicable bilateral investment treaty (BIT).

This development means that courts and tribunals will have a clear set of criteria for determining whether indirect expropriation has occurred. Additionally, Georgia’s executive and legislative branches will have guidelines for future regulations,

and investors will have a better understanding of the feasibility of their potential disputes.

Ultimately, this will create a clearer, more predictable legal environment for investors, contributing to a more competitive business climate in Georgia. BLC Law Office, under a mandate from the international donor organizations, and in collaboration with the Ministry of Economy and Sustainable Development of Georgia, continues to support this important initiative by adapting global best practices to the Georgian context.



Giga Batlidze

Partner of BLC Law Office



Giorgi Leluashvili

Associate at BLC Law Office

FOR MORE INFORMATION AND ADVISE
PLEASE CONTACT US:

129th David Aghmashenebeli Ave, Tbilisi, 0102, Georgia
Tel.: +995 32 292 24 91, 292 00 86, 200 04 91
blc@blc.ge blc.ge