Approaches to Bilateral Loan Agreements between Developed and Developing States: Some Lessons from the Practice of Denmark, the United Kingdom and the United States

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1. Introduction

An earlier study, relying upon texts of bilateral loan agreements concluded between Denmark and certain developing countries, and between the United Kingdom and certain developing countries, discloses that there is a need for further examination of the subject for the purposes of updating and assessing the trend of developments in this area of international law.

This paper is accordingly designed to offer comparative analysis of the more recent approaches to bilateral loan agreements concluded by Denmark, the United Kingdom and the United States with a number of developing countries. The selection of these three developed, market economy States for the comparative analysis here is based on the realization that their approaches reflect most of the major legal, economic, and policy issues which may be regarded as relevant to loan agreements. At best, their practices offer readily available examples of points which this writer seeks to bring out in

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3. See Agreement between the United Kingdom and: Peru, Cmnd. 3379; Indonesia, Cmnd. 3770, 3771, 3280, 4535; Jordan, Cmnd. 4252; Afghanistan, Cmnd. 4597; Ecuador, Cmnd. 4344; and Turkey, Cmnd. 3374, 3876, 4231, 3472, 4586, 4602. As cited in Mann, *supra*, note 1 at 254 and nn. 1-6
connection with the issues enumerated at the end of this introductory section and discussed in the ensuing sections.

In order to limit the analysis to its subject matter, the paper does not intend to go into the details of equally engaging issues raised by loan agreements between foreign, private commercial banks and developing countries, or loan agreements between States and public international lending institutions such as the International Monetary Fund and the International Bank of Reconstruction and Development.

It is useful also to keep in mind at the outset that we are dealing here with specific agreements for loans, as distinct from general agreements for economic co-operation between States covering foreign public grants and other forms of official assistance to developing countries. The expression "loan agreement" as used here is to be understood as including agreements with agencies of a State such as Government Ministries, Departments, or any other instrumentalities which are clearly empowered to act on behalf of a State in this specific area.

It should be pointed out also that the loan agreements examined here are of various types and that the particular purposes for which they are concluded determine the nature of the provisions they contain. There are, for example, loans concluded for the purpose of enabling the borrower to purchase particular goods and services from the lender country in the form of a credit line. Such loan agreements usually contain only a few clauses expressed in less complicated paragraphs. These are to be distinguished from the provisions.

4. For some discussion on this, see, e.g., Adede, "Loan Agreements Between Developing Countries and Foreign Commercial Banks: Reflections on Some Legal and Economic Issues" (1977-78), 5 Syr. J. Intl. L. & Com.
6. See, e.g., the Agreement between United Kingdom and Ceylon (Sri Lanka), July 25, 1971, Cmnd. 4815; the agreement between United Kingdom and Mozambique, August 17, 1976, Cmnd. 6824; the Agreement between New Zealand and Indonesia, November 22, 1972. The Agreement is already deposited...
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loan agreements concluded for the purposes of financing certain projects or for general economic development. The agreements in this category are usually more detailed and include clauses dealing, among other things, with: conditions under which further contracts may be concluded by the borrower for executing aspects of a project being financed by the loan; privileges of experts from the lending country working in the borrowing country under the loan agreement; and the question of expropriation of property of the lender connected with the loan project. In both of these categories of loan agreements, there are to be found those which are interest-free, and those which bear interest, thereby necessitating the inclusion of detailed payment schedules of both the principal and interests at various rates.

Having regard, therefore, to the foregoing, the analysis shall focus upon the examination of how the loan agreements have treated the following crucial issues: the law governing the agreements; the degree of discretion of the borrower in using the loan; protection of the interests of the lender; special cases such as expropriation and protection of foreign experts; the settlement of disputes clause; and the entry into force clause.

with the United Nations for registration and publication in the U.N.T.S., pursuant to Art. 102 of the United Nations Charter (not yet published).

7. See, e.g., Agreement between United States and Egypt for financing industrial and agricultural production, September 30, 1976, T.I.A.S. 8679; Agreement between United Kingdom and Indonesia for financing development projects, July 4, 1972, in Cmnd. 5214; and any of the Danish agreements cited, supra, note 2 and infra, note 22.


10. All the loan agreements by Denmark cited, supra, note 2 and infra, note 22 are interest free.

11. According to the United States practice, loans given by the Agency for International Development (AID) are usually subject to a 2% interest rate per annum for the first ten years and thereafter the rate of 3% annually is charged. See, e.g., a standard clause in Agreement between United States and Kenya for livestock development, September 11, 1974, Article II, T.I.A.S. 8650. Loans given by the United States through the Export-Import Bank are also subject to an interest now allowed to range between 7% and 8.5%. For discussion, see, e.g., Streng, Government Supported Export Credit: United States Competitiveness (1976), 10 Int. Law. 401; Rendell, Export Financing and the Role of the Export-Import Bank of the United States (1976), 11 J. Int. Law & Econ. 91.
II. Legal, Economic and Policy Issues Reflected in the Loan Agreements

A. The Question of Applicable Law

Between 1966 and 1968 the Government of Denmark entered into loan agreements with five developing countries and used a standard approach\(^\text{12}\) which included the following provision on the law governing the agreements:

Unless otherwise provided for in the Agreement, the Agreement and all other rights and obligations deriving from it shall be governed by Danish law.\(^\text{13}\)

As rightfully noted elsewhere,\(^\text{14}\) the real effect of the above provision depends primarily upon the extent to which the conflict of law rules to be observed by the arbitral tribunal provided for in the agreement for the settlement of disputes between the parties,\(^\text{15}\) allows reference to and application of Danish law. Thus, where it is certain that the forum established for the settlement of disputes is to function under public international law, as defined either in a compromisory clause or in a specific *compromis*,\(^\text{16}\) the extent of application of Danish law in that situation becomes problematic. Also, where the forum envisaged for the settlement of disputes is to function under a national law, there is always a confusion arising from the competition between the view seeking to apply the conflict of law rules of the national law stipulated (Denmark) and the views supporting the application of the conflict of law rules of the country of the seat of the arbitral tribunal.

The United Kingdom has given both interest free loans and those bearing interest at different rates per annum: A 2% interest rate was, for example, charged on loan agreements with: Egypt, September 5, 1972, Cmnd. 5172; with Turkey, November 27, 1971, Cmnd. 4778; Tunisia, November 16, 1972, Cmnd. 5229. A 3% interest was charged in the Loan Agreement with: Colombia, May 28, 1973, Cmnd. 5497; and Ecuador, October 2, 1973, Cmnd. 5503. A 5% interest was charged in the Loan Agreement with Brazil, November 20, 1973, Cmnd. 5572. A 6% interest was charged in the Loan Agreement with Costa Rica, February 15, 1973, Cmnd. 5436. A 7\(\frac{3}{4}\)% interest was charged in the Loan Agreement with Brazil, March 11, 1969, Cmnd. 5406. A 7\(\frac{3}{8}\)% interest was charged in the Loan Agreement with Ceylon (Sri Lanka), July 25, 1971, Cmnd. 4815

12. See, *supra*, note 2
13. Agreement between Denmark and Malawi, *supra*, note 9 at Art. XII
14. F. Mann, *supra*, note 1 at 250
15. Most of the Danish loan agreements contain a settlement of disputes clause as discussed, *infra*, at pp. 35-37
16. See, *infra*, note 69
This emphasizes the fact that the negotiators of these agreements must always strive towards the achievement of a proper and clear interplay between the applicable law clause and the dispute settlement clause of the agreements, so as to remove such difficulties.

The submission of treaties between States or other subjects of international law to a particular municipal law has been tried before. Reference is being made here to the early practice by which the International Bank of Reconstruction and Development (IBRD) made loan agreements with member Governments subject to New York law. But this practice has now been abandoned. As for submission of a treaty between two States to a municipal system of law, some evidence was provided in the 1957 Agreement between the United Kingdom and the Export-Import Bank on behalf of the United States, in which the Bank provided for a Line of Credit. The Agreement had the following relevant provision:

All questions with respect to the execution or interpretation of this Agreement and the notes or with respect to performance or non-performance hereunder or thereunder shall be interpreted according to New York law.

A similar provision was contained in a comparable Agreement between the United Kingdom and the United States, through the Export-Import Bank, in 1965. Thus the Danish practice which also stipulated the law of the lender as the proper law of the agreement was not without some recent precedent.

Like the practice of the IBRD stated above, these examples of subjecting an agreement between sovereign States to a municipal law of the lender seems to have been abandoned. In point of fact, quite a number of bilateral loan agreements negotiated by Denmark between 1969-1977 do not contain the above clause making the agreements subject to the Danish law.

17. This process has been referred to as "commercialization of treaties". See F. Mann, supra, note 1 at 238 et seq.
18. See G. Delaume, supra, note 5 at 84-85 and R. Lavalle, supra, note 5 at 226
19. Agreement between the United Kingdom and The Bank, February 25, 1957, in Cmnd. 104 as also discussed in F. Mann, supra, note 1 at 241-42, n.5
20. Art. XIV of the 1957 Agreement, id.
21. See Art. X in Cmd. 2610
agreements are also different in format from the earlier series mentioned above. Instead of being drafted in the form of a single document containing a standard 15 articles, supplemented by one Exchange of Letters, these later series are in the following three parts: a standard main part comprising eleven articles; annex I made up usually of two articles; and Annex II describing specific projects to be financed by the loan. These three parts are supplemented by one or more Exchange of Letters. A standard Exchange of Letters found in all of them deals with the details of loan repayment schedules.


23. Article I gives the amount of loan; Article II stipulates for the opening of a loan account in Denmark in favour of the borrower, Article III states that the loan is free of interest; Article IV deals with terms of repayment; Article V specifies designated place of payment in Denmark; Article VI is a detailed one and usually describes the uses of the loan; Article VII deals with the question of equal treatment of foreign creditors of the borrower — non-discrimination; Article VIII seeks to ensure that the terms of the loan are enforceable locally (see, infra, p. 36 on entry into force); Article IX deals with particular covenants; Article X stipulates entry into force and duration of the agreement and the last Article, XI, specifies the relevant addresses of both the Lender and the Borrower for the purposes of communication and other activities related to the loan.

24. The first article deals with questions of cancellation and suspension of the loan. The second one deals with settlement of disputes.

25. These vary according to the nature of the purpose for which the loan is extended.

26. This is always an amplification of Article VI on the use of the loan and it describes conditions of further contracts under the loan.
The approach followed in the other loan agreements between the United Kingdom and several developing countries and similar agreements concluded by the United States further confirm that the designation of the law of the lender country as the proper law of a loan agreement has not been a popular practice.

In the case of the United Kingdom, although the loan agreements, usually in the form of Exchange of Letters, are silent about the applicable law, they all contain a standard clause requiring the borrower to open a bank account in England. Arguably, this provision would make specific activities related to the bank account subject to English law. This does not, however, mean that the other questions related to the agreements in general such as their validity, interpretation, breach of rights and obligations including those derived from them, are also subject to English law. Let it be observed in this connection that the Danish approach also included a standard clause providing for the opening of a loan account in Denmark in favour of the borrower. This clause is found in both the earlier series which, as mentioned above, included the applicable law clause, and the later versions of the agreements which have abandoned the applicable law clause.

In the case of agreements with the United States, there is no clause requiring the borrower to open a loan account in the United States. A comparable clause is, however, the standard provision on disbursement and letter of commitment which allows the borrower from time to time to request A.I.D. to issue Letters of Commitments for specified amounts to certain local banks for payments made to contractors or suppliers connected with the terms of a particular loan agreement. Thus, only those aspects of the loan agreement are clearly subject to the local laws in the United States and not the loan agreement itself.

27. See, e.g., Agreement between United Kingdom and: Mozambique, August 17, 1976, Cmnd. 6824 at para. 4; Peru, May 7, 1975, Cmnd. 6237 at para. 2(a); Nicaragua, March 24, 1974, Cmnd. 5739 at para. 2(a); Indonesia, July 16, 1973, Cmnd. 5559 at para. 2(a); Pakistan, September 7, 1972, Cmnd. 5278 at para. 2(a); Ethiopia, August 6, 1971, Cmnd. 4896 at para. 2(a); Turkey, November 12, 1970, Cmnd. 4602 at para. 2(a); Chile, March 11, 1969, Cmnd. 5406 at para. 2(a)


29. AID evidently abandoned its earlier practice of subjecting loan agreements to the laws of the District of Columbia. See G. Delaume, supra, note 5 at 79, n.22. A
The point we wish to emphasize here is that, except in cases of validity and enforcement of bonds issued under the loan agreement and made subject to an agreed domestic law, no unambiguous evidence exists supporting the conclusion that States have demonstrated a widespread willingness to make the validity, interpretation and application of a loan agreement subject to a municipal system of law. The Danish example and those before it, as indicated above, seem to have been abandoned.

B. The Degree of Discretion of the Borrower in the Use of the Loan

The loans extended for the purposes of enabling the borrower to purchase specific goods and services from the lender always contain an approved list of those specific items. It is accordingly unavoidable that the borrower has no discretion in applying the loan except in paying for the goods and services from the lending country listed in the agreement. This means that, even if comparable goods and services were available elsewhere on terms which are more favourable, the borrower cannot use the loan to pay for such goods and services, as doing so would violate the specific purpose of the loan. The borrower, in accepting the loan, is clearly under obligations deliberately assumed to buy goods and services from the lender of the loan.

One hopes, however, that a degree of discretion may exist for the borrower in applying the loan extended for the purposes of financing a specific project or general economic development. The argument here is that the execution of such projects and the carrying out of such developmental activities usually entail the exercise of some discretion by the borrower in the purchase of goods and services either from the lending country or in the open market, using sound economic judgement. Thus, where the execution of the projects under a loan agreement calls for the negotiation of further specific contracts for the supply of goods and services, the borrower would be free to enter into such contracts to be financed by the loan without being compelled to seek approval of the lender. The terms of the loan agreements analyzed here confirm that such a discretion does not exist. A typical article found in the 1976 agreement between the United States and Egypt for a loan financing industrial and agricultural production is instructive. Since it represents the

recent exception stipulating the application of such local law is found in agreement with Malagasy Republic, July 25, 1973, T.I.A.S. 7731 at s.10.4 Cf, supra, note 85
most stringent example, its relevant provisions are set out in their entirety below for ease of reference.

ARTICLE IV
Procurement, Utilization, and Eligibility of Commodities

SECTION 4.01. A.I.D. Regulation 1. Except as A.I.D. may otherwise specify in writing, this Loan and the procurement and utilization of Eligible Items financed under it are subject to the terms and conditions of A.I.D. Regulation 1 as from time to time amended and in effect, which is incorporated and made a part hereof. If any provision of A.I.D. Regulation 1 is inconsistent with a provision of this Agreement, the provision of this Agreement shall govern.

SECTION 4.02. Source of Procurement. Except as A.I.D. may specify in Implementation Letters or Commodity Procurement Instructions, or as it may otherwise agree in writing, all Eligible Items shall have their source and origin in the United States of America.

SECTION 4.03. Date of Procurement. Except as A.I.D. may otherwise agree in writing, only those commodities licensed by the Borrower on or after the date that the first Letter of Commitment under this loan becomes operative, and services related to such commodities, shall be eligible for financing under this Loan.

SECTION 4.04 Eligible Items.

(a) The commodities eligible for financing under this Loan shall be those specified in the A.I.D. Commodity Eligibility Listing as set forth in the Implementation Letters and Commodity Procurement Instructions issued to Borrower. Commodity-related services as defined in A.I.D. Regulation 1 are eligible for financing under this Loan. Other items shall become eligible for financing only with the written agreement of A.I.D. A.I.D. may decline to finance any specific commodity or commodity-related service when in its judgment such financing would be inconsistent with the purposes of the Loan or of the Foreign Assistance Act of 1961, as amended.

(b) A.I.D. reserves the right in exceptional situations to delete commodity categories or items within commodity categories described in Schedule B codes on the Commodity Eligibility Listing. Such right will be exercised at a point in time no later than commodity prevalidation by A.I.D. (Form 11 approval) or, if no commodity prevalidation is required, no later than the date on which an irrevocable Letter of Credit is confirmed by a U.S. bank in favor of the supplier.

(c) If no prevalidation is required and payment is not by Letter
of Credit, A.I.D. will exercise this right no later than the date on which it expends funds made available to the Borrower under this Agreement for the financing of the commodity. In any event, however, the Borrower will be notified through the A.I.D. Mission in its country of any decision by A.I.D. to exercise its right pursuant to a determination that financing the commodity would adversely affect A.I.D. or foreign-policy objectives of the United States or could jeopardize the safety or health of people in the importing country.

SECTION 4.05. Procurement for Public Sector. With respect to procurement hereunder by or for the Borrower, its departments and instrumentalities except public sector undertakings:

(a) The provision of Section 201.22 of A.I.D. Regulation I regarding competitive bid procedures shall apply unless A.I.D. otherwise agrees in writing; and

(b) Borrower will undertake to assure that public sector end-users under this Loan establish adequate logistic management facilities and that adequate funds are available to pay banking charges, customs, duties and other commodity-related charges in connection with commodities imported by public sector end-users.

SECTION 4.06. Financing Physical Facilities. Except as A.I.D. may otherwise agree in writing, not more than $1,000,000 from the proceeds of this Loan shall be used for the purchase of commodities or commodity-related services for use in the construction, expansion, equipping, or alteration of any one physical facility or related physical facilities without prior A.I.D. approval, additional to the approvals required by A.I.D. Regulation I. “Related physical facilities” shall mean those facilities which, taking into account such factors as functional interdependence, geographic proximity and ownership, constitute a single enterprise in the judgment of A.I.D.

SECTION 4.07. Utilization of Commodities.

(a) Borrower shall insure that commodities financed under this Agreement shall be effectively used for the purpose for which the assistance is made available. Such effective use shall include:

(i) The maintenance of accurate arrival and clearance records by customs authorities and the prompt processing of commodity imports through customs at ports of entry and removal from customs and/or customs-bonded warehouses of such commodities, the total time for which (from date commodities arrive at port of entry to date importer removes them from customs) shall not exceed ninety (90) calendar
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days unless the importer is hindered by force majeure or A.I.D. otherwise agrees in writing;

(ii) The consumption or use not later than one (1) year from the date the commodities arrive at the port of entry unless a longer period can be justified to the satisfaction of A.I.D. by reasons of force majeure or special market or other circumstances;

and

(iii) The proper surveillance and supervision by Borrower to reduce breakage and pilferage in ports resulting from careless or deliberately improper cargo handling practices, as specified in detail in Implementation Letters.

(b) Borrower shall use its best efforts to prevent the use of commodities financed under this Agreement to promote or assist any project or activity associated with or financed by any country not included in Code 935 of the A.I.D. Geographic Code Book as in effect at the time of such projected use except with the prior written consent of A.I.D.

SECTION 4.08. Motor Vehicles. Except as A.I.D. may otherwise agree in writing, none of the proceeds of this Loan may be used to finance the purchase, sale, long-term lease, exchange or guaranty of a sale of motor vehicles unless such motor vehicles are manufactured in the United States.

SECTION 4.09. Minimum Size of Transactions. Except where authorized by A.I.D. in writing, no foreign exchange allocation or Letter of Credit issued pursuant to this Agreement shall be in an amount less than ten thousand Dollars ($10,000). The minimum size of transaction restriction is not applicable for end-use importers.

SECTION 4.10. Procedures. A.I.D. will issue binding Implementation Letters and Commodity Procurement Instructions which will prescribe the procedures applicable in connection with the implementation of this Agreement.30

The above article may give the impression that the United States completely denies borrowers the option to buy goods and services outside the United States. That is not entirely correct since evidence is available showing that, in certain loan agreements, such an option is available. Closer examination of the matter, however, reveals that where some discretion is allowed the borrower to use the loan for buying goods and services not originating from the United States, a typical procurement clause in the agreement is included restricting the borrower to buy such goods only from Selected Free World

30. T.I.A.S. 8679
Countries as defined in the A.I.D. Geographical Code Book.\textsuperscript{31} Thus the discretion is a limited one. The lender still controls the conditions of procurement.

The above A.I.D. approach is an expression of the United States policy of attempting to secure markets for United States technology through such procurement policies. Generally, therefore, the A.I.D. loans are directed towards infrastructure developments which would result in the use of United States technology. This same policy is followed by another United States institution: the Export-Import Bank (Eximbank), dealing primarily with export financing programmes.\textsuperscript{32} As distinguished from the A.I.D., the Eximbank provides loans for larger projects for which repayment periods of longer than five years are required. The Eximbank, unlike A.I.D., also structures its repayment schedules on the basis of the ability of the cash flow from the project to liquidate the indebtedness.\textsuperscript{33} Both of these institutions, however, do follow the policy of tying their loans to the purchase of United States goods and services.

It is beyond the scope of the present discussion to evaluate further the recently made claim that ‘The Americans are well equipped to — and do — provide developing countries with aid loans tied to the purchase of American goods. It happens that they are less well placed to compete on straight export credit’ in the race with the other Western countries which have export credit programmes.\textsuperscript{34} Our basic aim here has been to identify the American approach for the purposes of the ensuing comparative analysis of approaches reflected in the loan agreements concluded by the two other developed countries selected for the study.

Comprehensive provisions tying the loan exclusively to \textit{all} goods and services available in the lending country are also found in the

\textsuperscript{31} See, \textit{e.g.}, Art. V, s.501 of Agreement with Philippines, December 23, 1975, T.I.A.S. 8489; and Art. VI, s.601 of Agreement with Kenya, September 11, 1974, T.I.A.S. 8650. There is also in these agreements a provision preventing the borrower from using the items bought under the loan for promoting or aiding any projects or activities associated with or financed by another foreign lender or donor not included in the AID Geographic Code Book. See, \textit{e.g.}, Art. IV, s.407(b) of Agreement with Egypt, September 30, 1976, T.I.A.S. 8679; Article IV, s.405(b) of the Agreement with Philippines cited earlier in this footnote; Article V, s.513(b) of the Agreement with Kenya cited earlier in this footnote; Article VI, s.605(b) of Agreement with Bangladesh, September 19, 1974, T.I.A.S. 7948

\textsuperscript{32} See Streng, \textit{supra}, note 11

\textsuperscript{33} \textit{Id.}

\textsuperscript{34} See discussion in ‘Exporters are not Gentlemen’ (March 4, 1978), The Economist Survey at 65
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loan agreements concluded by the United Kingdom. In the case of the United Kingdom, the Crown Agent must always examine and approve any contract concluded by the borrower to establish the contract’s eligibility for payment from the loan. The standard for eligibility is clearly that goods and services must be from the United Kingdom. There is, however, a case in which the use of the loan envisages purchase of goods from other developing countries although the approval of such contracts still rests with the British Crown Agents, viz:

**Eligible Contracts**

6. Save to the extent (if any) to which the Government of the United Kingdom notify the Government of Mozambique otherwise in writing, drawings from the loan will be used as provided in paragraph 3 of this Note only:

(a) for payments under a contract for the purchase in the United Kingdom (which expression in this Note will be deemed to include the Channel Islands and the Isle of Man) of goods wholly produced or manufactured in the United Kingdom or, in the case of chemical or allied products, goods which are duly declared to be of United Kingdom origin on the form set out in Appendix C (Chemicals) to this Note, or for work to be done or for services to be rendered by persons ordinarily resident or carrying on business in the United Kingdom (or for two or more such purposes), being a contract which:

(i) provides for payment in sterling to persons carrying on business in the United Kingdom;

(ii) is approved by the Government of Mozambique and accepted by the Crown Agents acting on behalf of the Government of the United Kingdom for financing from the loan; and

(iii) is entered into after the date of this Note and before 31 March 1977 save as may be otherwise agreed between the two Governments;

(b) for payments under a contract for the purchase of goods wholly produced in certain developing countries;

(c) for payment of sterling charges and commission payable in the United Kingdom to the Crown Agents in respect of their services on behalf of the Government of Mozambique in connection with the loan.

**Approval of Contracts**

7. Where the Government of Mozambique proposes that part of the loan should be applied to payments under a contract as
described in paragraph 6(a) or 6(b) of this Note, that Government will ensure that the Crown Agents acting on their behalf, obtain at the earliest opportunity;

(a) a copy of the contract; and

(b) two copies of a certificate from the United Kingdom contractor concerned in the form set out in Appendix C or Appendix C (Chemicals) (whichever is appropriate) to this Note.

Payments from the Account
8. After the Crown Agents, acting on behalf of the Government of the United Kingdom, have considered the documents referred to in paragraph 7 of this Note they will decide whether and to what extent a contract is eligible for payment from the loan.35

The practice reflected in the agreements concluded by Denmark, however, follows a slightly different policy in which the borrower is given some option of using a certain percentage of the loan for purchasing goods not originating from Denmark. A typical such clause is contained in Article VI of the 1974 loan agreement between Denmark and Tanzania reading thus:

ARTICLE VI

Use of the Loan

Section 1. The Borrower will use not less than 75 per cent of the Loan to finance imports from Denmark (including costs of transport from Denmark to Tanzania) of such Danish capital goods as are to be used for identifiable projects and are needed for the economic development of Tanzania. An indicative list of such goods is contained in Annex II.

Section 2. The Loan may also be used to pay for Danish services required for the implementation of development projects in Tanzania, including in particular pre-investment studies, preparation of projects, provision of consultants during the implementation of projects, assembly or construction of plants or buildings and technical and administrative assistance during the initial period of undertakings established by means of the Loan.

Section 3. A proportion of the Loan not exceeding 25 per cent may be drawn for the purpose of financing fully or in part non-Danish capital investment costs (including transport charges) related to projects for which contracts for supplies of Danish capital equipment or services have been approved by the Lender for financing under this Agreement. The total amount of drawings for the financing of such costs cannot at any time

35. Agreement between United Kingdom and Mozambique, supra, note 27
exceed 33 1/3 per cent of the total amount for which contracts for supplies of Danish capital equipment and services have been approved by the Lender for financing under this Agreement.

Section 4. All contracts to be financed under the Loan shall be subject to approval by the Borrower and the Lender.

Section 5. The approval by the Lender of a contract for financing under the Loan shall not imply any responsibility for the proper performance of such contracts.

The Lender also disclaims responsibility for the efficient use of supplies and services financed under the Loan and for the proper operation of the projects etc. to which such supplies have been made and such services have been rendered.

Section 6. A contract under the Loan shall contain no clause involving any special credit facilities from the Danish party to the contract.

Section 7. The proceeds of the Loan may be used only for payment of capital goods and services contracted for after the entry into force of the Agreement, unless otherwise agreed by the Borrower and the Lender.

Section 8. The proceeds of the Loan shall not be used for payment to the Borrower of any import duty, tax, national or other public charge such as import surcharges, duties to compensate for domestic excise taxes, charges or deposits in connection with the issuance of payments licences or import licences imposed by laws in force from time to time in Tanzania.

Section 9. The Borrower may draw against the Loan Account in fulfilment of contracts approved by the Parties for up to three years after the entry into force of the Agreement or such other date as may be mutually agreed by the Borrower and the Lender.36

From the text of Sections 4, 7 and 9 of the above article, it can also be seen that the approval of further contracts under the loan agreement is to be done by both "the Borrower and the Lender" sharing mutually in the decision and clearly assigns the borrower a role in that process. The approach is appreciably different from that followed in the agreements concluded, for example, by the United States. As can be seen from the text of Article IV of the United States-Egypt agreement set out above, the decision to enter into further contracts under the loan agreement is left exclusively to the discretion of A.I.D. The expression "Except as A.I.D. may

36. Denmark-Tanzania Agreement of June 22, 1974, already transmitted to the United Nations for registration and publication, Reg. No. 13594
otherwise agree in writing” used in that article clearly signifies that, while the borrower may presumably suggest the conclusion of certain additional service contracts it deems necessary under the loan project, the actual decision and discretion approving the additional contracts rests with A.I.D. alone. If that were not the intended result, then perhaps a clause such as, “except as the Lender and Borrower (Parties) may otherwise agree”, could have been used in the said United States agreement so as to ensure a certain degree of mutuality in the process of reaching a decision with respect to such additional contracts.

It seems prudent to avoid clauses which encourage the tendency of looking at a loan as a favour being done by the developed lending State, which is then entitled to dictate all the terms of the loan for all time. A loan agreement should, instead, be viewed through the prism of what distinguishes it from an outright grant or other form of official assistance. A loan, whether interest-free or otherwise, creates for the borrower an obligation to repay. It does seem fair that the borrower should be allowed a reasonable degree of discretion in its application for the purposes of achieving the desired goal. The recognition of such a discretion would arguably accord the borrower a right which is commensurate with the obligation to repay. The borrower would thus be free to use part of the loan, as economically justifiable, for buying certain goods and services from the lending country, and also in the open market.

It is true that the lenders are naturally keen in ensuring that favourable conditions exist in the borrowing country for the eventual repayment of the loan. This legitimate desire ought, however, not to create a one-sided unmitigated discretion for the lender, exercising a sometimes onerous surveillance over the borrower in the form of endless tie-in contracts and unilateral approval clauses. It is the view of this writer that the legal relationship created between the lender and the borrower by a loan agreement should be expected to work for the benefit of both parties. The burden of the argument is that one of the reasonable ways of achieving this aim is to allow the borrower of a project and general development loan appreciable discretion to apply the loan, as appropriate, for purchasing the necessary goods and services in the open market instead of exclusively from the lending country. As noted above, Denmark already allows at least 25 per cent of the loan

37. See the relevant provisions of the text set out, supra, at pp. 10-13
to be used by the borrower in non-Danish goods and services. Further liberalization of this approach, recognizing developing countries' ability to make economically sound judgements, is worthy of encouragement. 38

C. Special Covenants Protecting the Interest of the Lender

In all the loan agreements concluded by Denmark, there is a standard article entitled "Particular Covenants", which is basically a tax and exchange control clause, reading as follows:

ARTICLE IX

Particular Covenants

The Loan shall be repaid without deduction for, and free from, any taxes and charges, and free from all restrictions imposed under the laws of the Borrower. This Agreement shall be free from any present and future taxes imposed under existing or future laws of the Borrower in connection with the issue, execution, registration, entry into force of the Agreement, or otherwise. 39

The intention of the above provision seems clear. It seeks to establish, in the borrowing country, a kind of legal enclave by freezing, at that point, all the local laws and regulations which may affect particular aspects and terms of the loan. In order to protect the interest of the lender, the borrower is prevented from changing any such relevant local regulations, even those aimed at application to all loans in general, in situations where certain legitimate changes and departures from an existing practice become imperative as a result of unfavourable domestic economic conditions, caused and aggravated by external economic factors beyond the control of the borrower.

With respect to the loan agreements concluded by the United States, the comparable provisions are contained under the heading "General Covenants and Warranties", sometimes exhaustively

38. Some intriguing ideas have been advanced suggesting how to untie the tied project loans. The idea requires a thorough feasibility study of the project and dividing the project into various components in accordance with the type of services and goods required and studying the markets for availability of the specific goods and services in various countries and sending bids for those goods and services in specific countries where they are already available at a rate lower than that of the major lender of the loan. See discussion by De Soto, How to Untie Tied Loans (1 Jan.-Dec. 1975-76), 1 Africa: Int. Perspective
39. See, e.g., Agreement between Denmark and Nigeria, March 29, 1971, Art. IX 797, No. 11356. See also Art. IX of all the agreements cited in note 22, supra
supplemented by clauses under "Special Covenants and Warranties", depending upon the nature of the subject of the loan agreement. The list of items included under these headings may be a short one dealing with: reports required of the borrower about the loan project; disclosure of material facts and circumstances; a taxation clause similar to that of Denmark; and commission fees and other payments under the loan. The list can also be a long one comprising altogether provisions on some nineteen specific items including the minimum four cited above.

Under these headings the lenders have sought to achieve further detailed regulation of their relationship with the borrowers in a manner which, on balance, increases the protection of the interest of only the lender. It is interesting to observe that comparable agreements concluded by the United Kingdom do not contain provisions dealing with such covenants and warranties.

There is also a standard article in the loan agreements concluded by the United States dealing exhaustively with events connected with cancellation and suspension of disbursement of the loan. The provisions first recognize the right of the borrower to cancel any part of the loan with the prior consent of the lender. They are then followed by elaborate clauses describing conditions under which

40. See, e.g., Art. VI of Agreement between United States and Egypt, September 30, 1976, T.I.A.S. 5679
41. See, e.g., Arts. IV and V of Agreement between United States and Philippines, December 23, 1975, T.I.A.S. 8489. Art. IV is entitled "General Covenants" and contains provisions on: execution of the project, funds and other resources to be supplied by the borrower, continuing consultation, management, utilization of goods and services; taxation, operation and maintenances, disclosure of material facts and circumstances, commissions, fees, and other payments, maintenance and audit records, reports and inspections. Art. V is entitled "Special Covenants and Warranties" and contains provisions on: procurement from selected Free World countries, eligibility date, goods and services not financed under the loan, implementation of procurement requirements, contracts, reasonable price, shipping and insurance, port charges, notification to potential suppliers, U.S. Government-owned excess property, and terminal date for disbursement.
42. But the part of the loan to be cancelled cannot be one "(I) which, prior to the giving of such notice, AID has not disbursed or committed itself to disburse or (II) which has not then been utilized through the issuance of irrevocable Letters of Credit or through bank payments made other than under irrevocable Letter of Credit." Agreement between United States and Egypt, September 30, 1976, T.I.A.S. 5679 at Art. VII, s.701. Cf. Agreement between United States and Philippines, December 23, 1975, T.I.A.S. 8489 at Art. VII, s.701; Agreement between United States and Kenya, September 11, 1974, as amended July 20, 1977, T.I.A.S. 8650 at Art. VIII, s.801; Agreement between United States and Bangladesh, September 19, 1974, T.I.A.S. 7948 at Art. VIII, s.801
default by the borrower may be said to have occurred; when the lender may suspend disbursement of the loan; or even cancel the rest of the loan following suspension. Where suspension or cancellation of part of the loan occurs, the agreement itself continues in full force and effect until the payment in full of Principal and any accrued interest is made. These series of provisions are clearly special remedies for the lender and the agreement continues to stipulate that "No delay in exercising or omission to exercise any right, power, or remedy accruing to A.I.D. under this Agreement shall be construed as a waiver of any such rights, powers or remedies".

The Danish agreements also contain comparable clauses on cancellation and supervision, and the clause stipulating that, notwithstanding any cancellation or suspension, all the provisions of the Agreement continue in full effect unless otherwise specifically provided in the relevant Article. As can be seen, the Danish approach deals with the matter less exhaustively than the United States approach. Again it is interesting to note that no such clauses on default, cancellation or suspension including the other details found in these two approaches are found in the agreements concluded by the United Kingdom.

There is, however, one provision which is found in all these approaches deserving mention here. In the Agreements concluded by the United States, it is called "Renegotiation of the Terms of the Loan". Under such a heading one would hope to find provisions dealing with conditions under which the borrower, for example, may renegotiate the terms of the loan for the purposes of achieving changes necessary for fulfillment of its obligation under the loan agreement without undue economic hardship, or the lender may re-evaluate its obligations under the loan. The clause is, however, not intended to take into account the interest of both parties in that way. It is a simple provision giving the borrower the discretion to pay the loan in full at any time earlier than the scheduled dates.

43. See relevant provisions in the agreements cited note 42, supra
44. See relevant provisions in the agreements cited note 42, supra
45. See pertinent provisions of the agreements cited note 42, supra
46. See pertinent provisions of the agreements cited note 42, supra
47. Agreement between United States and Philippines, December 23, 1975, T.I.A.S. 8489 at Art. VII, s. 7.08. See also comparable provisions in agreements cited note 42, supra
48. See Annex I, Article I, sec. 3 of all the agreements cited note 22, supra
49. See, e.g., Art. II, s.2.05 of Agreement between United States and Egypt,
the case of an interest bearing loan, it is arguable that the borrower, if it feels capable, may wish to avail itself of such a discretion and pay the loan earlier, thereby avoiding accumulating huge interest on the principal. The lender may want to renegotiate on the basis of the possible loss of interest. But where the loan itself is interest free, the incentive given in this discretion to the borrower is greatly reduced. It is the view of this writer that a renegotiation clause in a loan agreement should address itself to issues that adversely affect the interest of the parties. For the borrower, it would at least recognize the possibility of renegotiating for re-scheduling payment for later dates instead of the dates fixed by the agreement.

D. The Expropriation Clause as a Special Case

Reference was made at the beginning of this article to a loan agreement which included a clause dealing with expropriation of the property and other investments of the lender. We consider this as a special case of protection of the interest of the lender in a loan agreement beyond those contained in covenants and warranties just discussed. The question of expropriation deserves special attention here also because of the important changes that may be said to have occurred in the international law governing the conduct of States with respect to property of aliens. Below are the relevant paragraphs of the 1971 agreement between Denmark and Malawi:

(7) The Government of Malawi shall take no measures of expropriation, nationalization or any other dispossession either direct or indirect against such investments in the territory of Malawi and belonging to Danish Investors except for public benefit and against compensation.

(8) If the Government of Malawi expropriates or nationalizes such investments of Danish Investors or if it takes any other measures with a view to direct or indirect dispossession of Danish Investors, it shall provide for the payment of effective and adequate compensation.

(9) Such compensation shall represent the equivalent of such investments affected at the time of expropriation, nationalization or any other form of dispossession; it shall be realisable and freely transferable and shall be made without delay. Provision shall be made in an appropriate manner at or prior to the time of dispossession for the determination and payment of such

September 30, 1976, T.I.A.S. 8679 and Art. II, s.2.05 of the other agreements cited note 42, supra
The emphasized portions of the paragraph reflect part of the customary international law which the capital-exporting nations have consistently applied in cases of expropriation of foreign property. Under the orthodox view, a State is first reminded that it should not expropriate foreign property. But if it does, the expropriation must be for public benefit and subject to the payment of compensation. The compensation itself must be just, that is to say, it must be effective, adequate and paid promptly. In case of doubt as to the amount to be paid, the orthodox view stipulates that the compensation should represent the equivalent value of such investments affected at the time of expropriation. The only other attribute of the orthodox view not reflected in the above Danish-Malawi agreement is that expropriation of foreign property is improper under international law if it is discriminatory.

While it is beyond the purpose of the present analysis to go into a detailed discussion on this question, it seems in order to briefly point out certain coherent developments aimed at changing the above view. A series of the United Nations resolutions on permanent sovereignty over natural resources has attempted to assault step-by-step the orthodox view by first making the right of a sovereign State to expropriate no longer unlawful per se and by departing from the old standard in the following manner.

— The "public purpose" limitation upon the State's power to expropriate is no longer mentioned. Instead, emphasis is placed upon expropriation as an act of expression of State sovereignty, undertaken for the purposes of recovering natural resources, having regard to the circumstances which the State exercising the power considers pertinent.

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50. Exchange of Letter of March 2, 1971, paras. 7-9, being part of the Loan Agreement of the same date, 794 U.N.T.S. No. 11294
51. For the controversy on this question see generally R. Lillich, 3 The Valuation of Nationalized Property in International Law (Charlottesville: University Press of Virginia, 1975); Lapers, "Principles of Compensation for Nationalized Property" (1977), 26 Int. & Comp. L.Q. 97-107
52. For a recent discussion of the relevant United Nations resolutions on this question see, e.g., Adede, International Law and Property of Aliens: The Old Order Changeth (1977), 19 Malaya L. Rev. 175-193
54. See, e.g., the Charter of Economic Rights and Duties of States, United
— The principle of "non-discrimination" is also de-emphasized. Expropriation is seen basically as a legitimate process of transfer of ownership of property over which a State is said to have permanent sovereignty and may recover even if it means affecting the interest of foreigners only.

— Compensation is payable only when the nationalizing State has determined that it is appropriate to do so and has fixed the amount to be paid and the mode of payment. The State is, however, required to provide local machinery and procedures for settling any controversies which may arise over the issue of compensation and the foreign company is required to accept such local settlement and determination of the amount of compensation as final. Only in limited instances, where the host State and the other States agree, may there be a resort to third party settlement of the compensation question beyond the local proceedings.

The above developments may be regarded as attributes of the New International Economic Order, prodding the capital-exporting nations to abandon the orthodox view in the light of present emphasis upon mutual economic inter-dependence of States. The degree of acceptance of these new developments concerning treatment of property of aliens certainly depends on the process of their transformation and intention in bilateral or multilateral instruments binding upon sovereign States. In their present form, they are, at best, a guide to action.

Significant examples of such a guide exist in the Kennecott expropriation case in which the Chilean Government deducted "excess profits" from the payable compensation, thereby reducing the compensation amount to zero, and in the Marcano Mining

Nations DOC. A/RES/328 (XXIX), Art. II, in (1975), 69 Am. J. Int. L. 484; (1975), 14 I.L.M. 251
55. Cf. Para. 2(C) of the Economic Charter, supra, note 54 using the term "transfer of ownership of foreign property"
56. See Para. 2(C) of the Economic Charter, supra, note 54. Cf. discussion on compensation in Grantz, infra, note 60
57. See Para. 2(C) of the Economic Charter, supra, note 54. For a discussion indicating the different approaches to the question of dispute settlement by these resolutions, see generally Adede, supra, note 52
59. For a commentary on this case see, e.g., Orrego Vicuna, Some International
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Company expropriation case in which the amount of compensation to the United States by Peru recognized the latter's balance-of-payments problem and was calculated so as to take into account future earnings Peru was to receive by continuing to sell iron ore to the United States. Thus, the settlement included a self-financing aspect of the payable compensation which depended upon a continued relation between the two States.

It is reasonable, therefore, to expect that any loan agreements or general agreements for economic development between States which include provisions on expropriation, will take into account issues such as those raised in the Kennecott case and the Marcano settlement.

E. Clauses in Favour of Experts from the Lending Country Working Under the Loan Project

Reference was made earlier to a Danish agreement which included a special provision dealing with privileges of the Danish experts working in a borrowing country under a loan agreement. The relevant clauses of that agreement deserve examination here as a further illustration of additional issues covered by loan agreements where appropriate. The text of the provision in question is as follows:

ANNEX III

Privileges of Experts in Bolivia

The Government of Bolivia will make provision for the exemption of experts from:

1. all taxes in respect of any emolument paid to them from Danish sources;

2. all duties and taxes imposed on the import and export of durable furniture and personal effects imported by experts and their families for their exclusive use within 6 months after their arrival subject to reexport on completion of tour of duty or payment of customs if sold locally. The term "personal effects" shall include inter alia for each household: one refrigerator, one deep freezer, one radio, one record player, one tape recorder, one

Law Problems Posed by the Nationalization of Copper Industry by Chile (1973), 67 Am. J. Int. L. 711; Adede, supra, note 52 at 183-86
60. For a commentary on the case see e.g., Gantz, The Marcona Settlement: New Forms of Negotiation and compensation for Nationalization (1977), 71 Am. J. Int. L. 474
61. See Agreement between Denmark and Bolivia, supra, note 8
television set, minor electrical appliances, one set of photographic and cineequipment and air conditioning unit;

3. all duties and taxes imposed on the import and export of a motor vehicle, for personal use of the experts, or the purchase of such a motor vehicle in Bolivia out of duty free stock, provided that a motor vehicle imported under these privileges shall be liable for such duties and taxes if resold to a person in Bolivia, unless resold to a person entitled to the same privileges.

The Government of Bolivia shall give assistance in clearance through customs of effects mentioned under 2 and 3 above.

The Government of Bolivia will provide local transport for official journeys of the expert to the same extent as provided for officers of the Government of Bolivia of comparable status. If circumstances require the expert to use his personal motor car for official journeys, he shall be entitled to mileage allowance of the same rates as those paid to officers of the Government of Bolivia.

The Government of Bolivia will assist the experts to find suitable housing. Rent will be paid for by the experts concerned.62

Clauses of this kind are not uncommon in general bilateral agreements for economic and technical co-operation with developing countries, envisaging the services of experts from the developed country concerned.63 The provisions become relevant in situations where the experts in question do not form part of the official personnel of the diplomatic mission of the lender to the borrower country and are, accordingly, not entitled to enjoy the functional privileges enumerated in the above text. Thus, where there exists no other legal instrument in force between the lender and the borrower which contains such provisions, then the loan agreement itself becomes the vehicle for extending the above protection of the interest of the experts from the lending country. There seems to be a basic assumption that the foreign experts deserve the above privileges which the borrowing country is expected to grant, as part of the price of receiving both the loan and qualified personnel to assist in the execution of the loan project.

Evidence is available to show that there are cases in which the

62. Id.
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protection of the interest of experts has gone even further than that accorded by the above text. These are the cases in which, in addition to the above privileges, the experts are shielded, by the host government, from liability and payment of damages arising from tortious and wrongful acts committed against a private person locally. Article VII of the 1970 agreement between Denmark and India is illustrative and reads as follows:

ARTICLE VII

If, in pursuance of or in connection with his duties carried out under this Agreement, the Danish expert causes damage to a third party, the Government of India will be liable for this damage in place of the Danish expert. The Government of India shall be entitled to a refund from the Danish expert of the compensation paid by it, if the Danish expert has acted with premeditation or gross negligence.

It is important to emphasize both what the article is saying and what it is not. According to the article, the experts are not immune from the legal process itself. They are subject to any legal proceedings initiated against them locally. However, if the result of a civil suit is that an expert is found liable to pay damages, then at that point he is insulated by the host government, which is required to assume the liability and to pay the necessary damages. Where the wrongful conduct creating liability was premeditated or was as a result of the gross negligence of the expert, then the host government is to be refunded by the lending State.

The above provision is thus distinguishable from one which applies the principle of indemnification of the expert. As opposed to the practice of insulation from liability and payment of damages, the principle of indemnification would first hold the expert himself liable. Then, it would require the expert himself, as the author of the wrongful act, to pay the actual damages. Then the host government would, as appropriate, indemnify the expert in question. Such a right would, obviously, not be available with respect to a criminal proceeding against the expert.

The indemnity clause is thus clearly distinguishable from complete immunity from the legal process clause and is preferred by this writer over the above text which holds the host government itself liable. The indemnity clause would make the legal sanction applicable directly first to the actual perpetrator of the wrongful act

64. 745 U.N.T.S. 228. But see comment at note 87, infra., and accompanying text.
and only in the second stage to the host government. The financial implications of these clauses in a loan agreement are evident and must remain a factor to be properly weighed by the borrower in negotiating a loan agreement in which issues of protection of experts under the loan become central.

It is important to observe also that there are cases in which the details of privileges for the experts are not contained in a particular bilateral agreement between the parties but left for definition and application in accordance with the standard rules laid down by the host, borrowing State. This version exists, for example, in article 6 of the 1968 Agreement on Technical Co-operation between Denmark and Pakistan.\(^6\)

**F. Settlement of Disputes Clause**

Having created a legal relationship in a loan agreement containing such terms as those analyzed above, the parties may entertain the hope that the relationship will work smoothly and may decide to remain silent about the question of settlement of disputes.\(^6\)

Negotiators of the loan agreement may, on the other hand, address themselves to the question by including in the agreement a simple statement to the effect that all disputes shall be settled through consultations,\(^6\) or by any other means mutually agreed upon by the parties\(^6\) through a promissory clause.

But they may also decide to go further than that and include, in the loan agreement itself, a specific mode of settlement. This is always an attempt to avoid waiting until they are already in dispute and then be faced with the question of agreeing upon a dispute settlement procedure by a special *compromis*.\(^6\) The mode of

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65. 656 U.N.T.S. 166 at 170
66. All the loan agreements concluded by the United States and the United Kingdom do not have any provision on settlement of disputes. But see the Agreement between United States and Ghana providing that disputes arising from the agreement shall be referred to the International Court of Justice. 805 U.N.T.S. No. 11467
67. See, e.g., Agreement between New Zealand and Indonesia, November 27, 1972, United Nations Registration No. 12685 at Para. 7
68. See, e.g., Agreement between Denmark and India, April 24, 1972, United Nations Registration No. 12035 at Annex 1, Art. 11
69. The contents of *compromis* differ with each case. Where the settlement is by an *ad hoc* arbitration the *compromis* addresses the following issues: definition of the question to be referred to the arbitration, method of constituting the arbitration tribunal, procedure to be followed by the tribunal, the law applicable, the publication of the arbitral award, its execution and revision. For an earlier model
settlement usually stipulated in such compromisory clauses is arbitration of which, as cogently summarized elsewhere, there are several versions:

At the lowest end of the scale are clauses which do not specify any particular form of arbitration. A clause may simply state that disputes "shall be settled by recourse to arbitration". Or it may say that settlement shall be "by arbitration in such manner as may hereafter be agreed by a general or special agreement between the contracting parties". The language itself indicates the problem: a separate agreement is required, and such clauses suffer thus from the same disadvantage as those making general reference to pacific settlement. Slightly more precise, but still requiring an agreement between the parties for their implementation, are clauses which offer parties a choice between two or more stated forms of arbitration.

Unique to arbitration clauses in general is the problem that, even where the procedure for its establishment is spelled out, the arbitral tribunal might never be formed because of a party's ability to sabotage the selection procedure. Ideally, the clause should provide for the appointment of the tribunal in such a way that none of the parties would be able to prevent its coming into existence. Many treaty provisions do not reach this goal.\(^7\)

Relevant to our present analysis is the standard clause contained in most of the loan agreements dealing with settlement of disputes and drafted in terms which seek to avoid some of the problems mentioned by Professor Sohn in the above passage. The Danish clause reads as follows:

**ARTICLE II**

**Settlement of Disputes**

Section 1. Any dispute between the Parties arising out of the interpretation or administration of the present Agreement, which has not been settled within six months through diplomatic channels, shall, at the request of either Party, be submitted to a tribunal of arbitration consisting of three members. The chairman of the tribunal shall be a citizen of a third country and shall be appointed by common consent of the Parties. Should the Parties

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\(^7\) Sohn, *Settlement of Disputes Relating to the Interpretation and Application of Treaties*, [II-1956] Recueil des Cours 197 at 268
fail to agree on the appointment of the chairman of the tribunal, either Party may request the President of the International Court of Justice to make the appointment. Each Party appoints its own arbitrator; if a Party abstains from appointing an arbitrator, the latter may be appointed by the chairman of the tribunal.

Section 2. Each Party will observe and carry out awards given by the tribunal.71

The above provision still leaves unsettled several crucial issues, such as: the procedure to be followed by the arbitral tribunal, the applicable law in case of doubt, interpretation of the arbitral award, and its revision and annulment. Such issues may be included in the arbitration clause itself, instead of relegating them to a special compromis. With respect to procedure, examples exist giving the tribunal the power to determine its own procedure;72 others give the power to establish procedure to the Chairman of the tribunal,73 and still others have opted to incorporate by reference the settlement procedures contained in the 1907 Hague Conventions on the Pacific Settlement of Disputes.74 There are also examples in which municipal judicial systems are stipulated for the taking of evidence and the summoning of witnesses.75 A number of compromisory clauses76 merely assert variously that the dispute is to be settled by arbitration on the basis of legality, based on respect of law or on the basis of the agreement and by application of customary interpretation of law and of the generally recognized principles of law.

It is hoped that the above brief discussion gives enough background to the question of settlement of disputes as an issue relevant to bilateral loan agreements. For the purposes of this paper, it is important to observe that, except for the Danish provision set out above, the loan agreements by the United States and United Kingdom do not contain any clause concerning settlement of disputes. The conclusion is inescapable that parties to those agreements decided to rely exclusively on a special compromis to be agreed upon in the event of disputes arising under the loan agreement.

71. See, e.g., the 1977 Agreement between Denmark and Bolivia, supra, note 8 at Annex I, Art. II. The same provision is contained in Annex I, Art. II of all the Danish agreements cited, supra, note 22
72. See, e.g., examples cited in Sohn, supra, note 70 at 269 n. 75.
73. See examples in n. 76, id.
74. See examples in n. 77, id.
75. See examples in n. 78, id.
76. See examples in n. 79, id.
G. Entry into Force Clause

A loan agreement between two sovereign States, being a treaty, enters into force in such a manner and upon such date as it may provide or as the negotiating States may agree.77 The loan agreements examined here have used differing approaches. The first approach is that of the United Kingdom by which the loan agreements enter into force on the date of the last Exchange of Letters accepting the terms set out in the first Exchange of Letters. Thus, if the first Exchange of Letters from the United Kingdom proposing the terms of a loan agreement is dated March 6, 1978 and the Exchange of Letters of the borrowing State accepting the proposed terms is dated April 6, 1978, the date of entry into force for the loan is the latter. This procedure does not indicate what the borrowing State must do before it sends its Exchange of Notes constituting the agreement. Presumably, it is expected that the two parties shall have taken the necessary domestic steps to ensure that nothing would stand in the way of application of the agreement by the time the Exchange of Letters occurs.

The practice followed by Denmark is different. With respect to all loan agreements concluded by Denmark, there is always an article stating that the agreement “shall come into force on the date of signature”. Thus, the parties under this approach would appear to have chosen to express their consent to be bound by the agreement through signing it. At this point the lender is under obligation to put up the money. However, there is an additional provision to the effect that, before the actual drawing on the loan occurs, “the Borrower will satisfy the Lender that all constitutional and other requirements laid down by the Statute in the Borrower’s home country have been met, so that this Loan Agreement will constitute an obligation binding on the Borrower”.78 There is apparently a distinction made in the Danish practice between the extent of obligation created by the loan agreement upon its entry into force by signature and the obligation the agreement establishes when, following its signature and entry into force, the borrower confirms that its domestic constitutional requirements have been met. This practice seems to complicate the legal status of the loan

77. For earlier discussion see, e.g., G. Delaume, supra, note 5 at 22-33
78. See, e.g., the 1977 Agreement between Denmark and Bolivia, supra, note 8 at Art. VIII. The same provision is contained in all the Danish agreements cited, supra, note 22
agreement before the actual drawing on the loan occurs. It would be preferable if the requirements of showing the exhaustion of domestic constitutional requirements in the borrowing States were made to coincide with the date of entry into force.

In this context, the practice of the United States is clearer. In all the loan agreements concluded by the United States, there is a standard clause stating that

An opinion of the Borrower's Attorney-General that this Agreement has been duly authorized or ratified by and executed on behalf of the Borrower, and that it constitutes a valid and legally binding obligation of the Borrower in accordance with all of its terms.\(^{79}\)

The opinion herein requested is usually available during the process of negotiation so that when the agreement is later signed and delivered at a given date, its legal status is not in doubt as to the obligation created with respect to actual drawing under the loan. While there are no entry into force clauses in these United States agreements similar to that contained in the Danish agreement, it seems that the intention in the American agreements is to make them effective upon the date on which they are signed and delivered, as invariably stated in the terminal clause of the agreements. The entry into force provision of loan agreements must thus be drafted with a clear understanding as to the relevant domestic constitutional procedures that the parties are required to exhaust.

III. Conclusions

In the foregoing comparative analysis of the approaches to bilateral loan agreements, certain developments have been pointed out and views defended which merit emphasis in this concluding section.

We have argued that a distinction should be made between the terms of a loan on the one hand and an official grant, donation or any form of financial assistance on the other. Since a loan, whether interest free or interest bearing, is to be repaid in accordance with the terms of agreement, it creates a recognizable obligation upon the borrower to repay. Accordingly, the borrower ought to be allowed an appreciable discretion, commensurate and consistent with such

\(^{79}\) See e.g., the 1977 amendment to the Agreement between United States and Kenya, July 20, 1977, Sec. 2.03(a) of the Amendment, and Art. IV, sec. 401(a) of the 1974 being amended, T.I.A.S. 8650. Similar provisions are contained in all the United States agreements cited in this paper.
obligation to use the loan for its intended purposes without being required to seek approval of the lender in every instance of application of the loan. This desirable discretion would enable the borrower, for example, to use the loan for securing the necessary goods and services from both the lender and, as appropriate, in the open market on the basis of sound economic judgement. The burden of the argument is that the borrower should not be constrained for all times by the terms of the loan agreement only to secure such goods and services from the lender or from the markets specifically approved by the lender. Such tightly tied loans should no longer be the order of the day and a movement away from them, in recognition of the ability of the developing borrowing States to exercise good judgement in using the loan, should be encouraged. It is clear that the discretion defended here for the borrower is easier to exercise in the case of a loan, in the traditional sense, where money passes from the lender to the borrower for disbursement by the latter. A loan is thus distinguishable from the extension of a line of credit by the lender in favour of the borrower for purchase of specific goods and services from the lender and where no money is actually transferred to the borrower. Herein lies some distinction between the grant of a loan and the extension of a credit line.

A bilateral loan agreement should, therefore, reflect a balanced concern with the protection of the interests of both the borrower and the lender. An effort to achieve such a balance would hopefully discourage the inclusion in a loan agreement of complicated and detailed covenants and warranties aimed primarily at protecting the interests of the lender in securing markets for its goods and services in the borrowing country beyond the recognizable interest of securing a repayment of the loan under the agreed terms.

A bilateral loan agreement between two States (international persons) is normally a treaty which, according to the Vienna Convention on the Law of Treaties, is "governed by international law". The earlier attempts made by the United States, through Eximbank and A.I.D., Denmark and the World Bank to

80. See the U.S. practice discussed, supra, at pp. 10-15
81. See the Danish approach discussed, supra, at pp. 17-21 and the United Kingdom example, supra, at pp. 15-16
82. Cf the text set out at pp. 10-13
83. "‘Treaty’ means 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." Vienna Convention on the Law of Treaties, Opened for signature
"commercialize" agreements by subjecting them to particular municipal systems of law have evidently been abandoned. Accordingly there still exists no unambiguous evidence that States have demonstrated a widespread and consistent willingness to contract a loan agreement entirely on the footing of a municipal legal system. International law thus remains the applicable law for the determination of the validity of a bilateral loan agreement, as well as its interpretation and application.

Only in the absence of another instrument in force between the parties such as general agreement for economic and technical co-operation, or for the promotion and protection of foreign investment would a loan agreement be burdened with clauses on expropriation and protection of foreign experts. Our view is, however, that where the inclusion of such clauses becomes necessary in an instrument, the drafters should take into account the coherent onslaught against the orthodox view on the issues concerning expropriation, and the protection of experts by offering functional exceptions and legitimate indemnification for liability in local suits.

84. See note 17, supra
85. But see, e.g., Art. 2 of loan agreement between West Germany and: Tanzania, September 6, 1974; Kenya, August 15, 1974; Mali, July 27, 1974, subjecting the agreement to German law.
86. See, e.g., the recent agreements for the Promotion and Protection of Investment between United Kingdom and Egypt, February 24, 1976, Cmnd. 6638; United Kingdom and Indonesia, April 27, 1976, Cmnd. 1977. Both of them still stipulate for the payment of "prompt, adequate and effective compensation" but recognize the application of local law in determination and review of such compensation if challenged.
87. We have argued, supra, at pp. 31-32 for an indemnification which would compel the expert to be subject to local legal process and, as appropriate, pay the necessary damages for injuries caused and then be indemnified by the host government as warranted. This type of indemnification is different from the example used in a recent agreement of October 30, 1976, between the Netherlands and Egypt reading thus:

ARTICLE III

a. The Government of the Arab Republic of Egypt shall indemnify and hold harmless the Government of the Kingdom of the Netherlands and the Netherlands experts, advisers, agents or employees against any extra-contractual civil liability arising from any act or omission on the part of one or more of the said individuals during the operations governed by or undertaken in virtue of this Agreement which causes the death or physical injury of a third party or damage to the property of a third party — in so far as not covered by insurance — and shall abstain from making any claim or instituting any action
In seeking to bring about a balanced approach to the protection of the interests of the parties, a loan agreement should thus strive towards the establishment of a legal relationship which is intended to work, and not an instrument deliberately skewed to enable one party to point out breaches and claims of derogation from the obligation for the purposes of achieving a premature termination of the relationship under calculated conditions. In this regard, a clause on dispute settlement giving jurisdiction to either an existing forum, 88 or an ad hoc forum, 89 does no harm in a loan agreement.

The question of whether or not to charge interest on a loan seems to defy any generalized observation. We note, for example, that all the loans given by Denmark analyzed here are interest-free. 90 The A.I.D. and Eximbank are, according to their Statutes, required to charge a standard interest rate. Thus the loans extended by them have all been subject to interest rates dictated by local statute. The practice of the United Kingdom remains unclear since the evidence demonstrates that it has given both interest-free loans, and loans bearing interests of 2 per cent, 3 per cent, 5 per cent, 6 per cent, 7\(\frac{3}{4}\) per cent, and 7\(\frac{7}{8}\) per cent between 1969 and 1973 to various developing countries. 91 The rationale behind these varying interest rates is known only to the parties themselves. For us, it is important merely to note here that, unlike Denmark and the United States, the United Kingdom interest rates on loans vary as herein shown.

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88. See, e.g., the loan Agreement between United Kingdom and Ghana, supra, note 66 accepting the jurisdiction of the International Court of Justice for the loan disputes.
89. See the Danish practice, supra, at pp. 34-36, providing for arbitration.
90. See comments in relation to note 10, supra.
91. See agreements cited, supra, note 11.
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