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Euro-Arab Investor-State Dispute Settlement: Recent developments and future perspectives

COMPENSATION IN INVESTMENT ARBITRATION

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Compensation in

- Commercial arbitration
- Investment arbitration

  - are there differences in principle?

Answer: **Not really**

Are issues of compensation in

- Commercial arbitration
- Investment arbitration

different as a practical matter?

Answer: **Yes**

Reparation in international law

- Restitution
- Compensation
- Satisfaction

ICL Draft Articles on State Responsibility, Articles 35-37

However, in Investor-State Arbitration, compensation is the prevailing remedy.

Similarities

Objective of damages

The objective of reinstating a situation that would have existed but for the impeached conduct (“undo the harm caused”)in international law is identical to what applied under municipal law (although “restitution” rather than compensation is the primary remedy under int’l law).

The matter of causation

In international law a number of criteria have not been used (foreseeable, adequate, proximate, direct etc).

Probably more specific under municipal law (foreseeability, and in some jurisdictions “adequate” causation).

Rules on contributory negligence and mitigation of damages

These rules exist in municipal law systems as well as under international law in (Middle East Cement, AMCO v. Indonesia II).

Damages in national and international law

National

- Contract-based
- Asset value
- Backward-looking
- Unjust enrichment sometimes a basis for compensation

International

- Not contract-based
- Business value
- Forward-looking
- No compensation based on unjust enrichment (gives room for ”efficient breach”)

The principle of Chorzów Factory

[---] reparation must, so far as possible, wipe-out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed. [---] *)

*) Factory at Chorzów (Ger. v. Pol.), Indemnity, 1928 PCIJ (ser. A) No. 17 (Sept 13)

INVESTMENT = commitment of resources to create future cash flow, the net present value of which is (hopefully) at least equivalent to the resources committed.

Cost of investment ≠ Value of investment

- The value of an investment is in principle disconnected from the cost of the investment.

Determining the value of income-producing assets

Competing approaches to valuation:

- Book value
- Replacement value

poor indicators of value

- Liquidation value
- Discounted Cash Flow (DCF)

methodologically beyond reproach

- Unjust enrichment

inappropriate

- Peer companies analysis
- Market capitalisation (if available)

helpful proxies for valuation

Business value is today's value of future income

Value of investment = Stream of future income × Time element × Risk (<1,0)

- Business valuation is forward oriented, but historical data *may* provide indications of earnings potential.
- Commitment of resources to create future cash flow, the net present value of which is at least equivalent to the resources committed

Superiority of DCF technique in adversarial proceedings

- Assumptions and projections of Parties will be transparent and available for review on a reciprocal basis
- Degree of relevance and comparability of underlying data and empirical materials will be subject to adversarial review

Market criteria

- Maturity
- Size
- Economy (GDP/inhabitant)
- Growth
- Barriers to entry
- Competition

Business criteria

- Positioning in relation to competitors
- Product focus, niche or standard issue
- Pace of technological change
- Track record

Assumptions with regard to known un-knowns that may occur in the future

- Demand patterns
- Macro-economic conditions
- Investor behaviour
- Price elasticity
- GDP growth
- Real exhange rates
- Domestic inflation
- Tariff adjustment (if applicable)

Risk

- Dispersion of estimated future returns around their expected value (up/downside).

- The risk premium is an expression of risk aversion.

The discount factor to determine present value of future income is the aggregate of

- Risk free rate

\+ Business risk

\+ Financial risk

\+ Liquidity risk

\+ Exchange rate risk

\+ Country risk (a composite indicator of political economic and financial risk)

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