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Reliance Based Damages at ICSID

by David Collins*

Introduction

Compensation for the nationalization of foreign investment has been called “one of the most controversial areas of international law”¹ largely because of the wide range of remedies that are employed by various legal systems for breach of contract as well as for interference with property rights. In awarding damages resulting from investment disputes between private investors and foreign states, tribunals of the International Center for the Settlement of Investment Disputes (‘ICSID’) generally assesses compensation according to the estimated lost profits the injured investor would have derived from the investment, which embodies the familiar “expectation measure” of American contract law. However, on occasion ICSID tribunals have granted recovery for actual costs of the investment, or *damnum emergens* as they are known in international law, much as a domestic court might award “reliance measure” damages. While the reasoning for the tribunal’s decision to fix damages according to losses incurred as opposed to (or sometimes in addition to²) gains foregone is often unclear, there is sound economic

* Lecturer, The City Law School, City University London; Visiting Professorial Fellow, Institute of International Economic Law, Georgetown University Law Center, <david.collins@utoronto.ca>. This research was supported by a grant from the British Academy.

¹ M Sornarajah, *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT*, (Cambridge U Press, 2004) at 437.

² Actual costs are typically argued in the alternative to lost profits by the claimant party.

rationale for a reliance-based standard of compensation. Most importantly, the error costs of imperfect damages based upon the level of actual investment should be lower than those derived from other methods, and secondarily, confidentiality of sensitive information is secured. Both of these advantages create incentives for further foreign direct investment, which is one of the primary objectives of the ICSID Convention and its dispute settlement system.

This article will examine several instances where ICSID tribunals have awarded *damnum emergens* and illustrate how this choice is generally economically efficient. It will begin by outlining standards of damage remedies that are commonly employed in international law and will conclude with some criticisms of the reliance measure in the investment context. As this article is forum-focused it will not examine reliance-based remedies in international investment law under other regimes in any detail, such as UNCITRAL arbitrations or under the Iran-US Claims Tribunal. Moreover, this article will not discuss the highly contentious issue of asset valuation *methods* used in international investment arbitration³ which are rightly viewed as secondary to the finding of the compensation *standard* applicable to the dispute.⁴ Similarly, the limitations of remoteness and foreseeability which feature in the assessment of damages both in common law and international systems will not be explored. An attempt to define the term investment directly is beyond the scope of this article, although some examples of

³ For a recent discussion of valuation methods in international investment law see T.W. Walde and B Sabahi "Compensation, Damages and Valuation in International Investment Law" 4:6 Transnational Dispute Management 1 (2007); Irmgard Marboe, "Compensation and Damages In International Law: The Limits of Fair Market Value" 7:5 Journal of World Investment and Trade 724; C.N. Brower and M Ottolenghi, "Damages in Investor State Arbitration" 4:6 Transnational Dispute Management 1 at 4; Thomas W Merrill, "Incomplete Compensation for Takings" 11 NYU Environmental LJ 110; Mark Kantor "Valuation for Arbitration: Uses and Limits of Income-Based Valuation Methods" 4:6 Transnational Dispute Management <www.transnational-dispute-management.com> .

⁴ SORNARAJAH at 486.

the types of expenses that ICSID tribunals will recognize when granting recovery will be seen. Finally this article will not directly consider the controversial issue of when state regulatory actions amount to an expropriation⁵ for the purposes of assessing compensation. A brief introduction of ICSID is warranted.

ICSID was established by the multilateral Convention on the Settlement of Disputes Between States and Nationals of Other States which entered into force in 1966 and is part of the World Bank, located in Washington DC, USA, although its proceedings may take place elsewhere. Generally speaking, ICSID provides facilities for the conciliation and arbitration of investment disputes between Contracting States and nationals of other Contracting States, although under its Additional Facility rules, states which are not party to the Convention may now use ICSID tribunals for dispute settlement, as well as for certain other fact-finding proceedings. Independent arbitral tribunals are constituted for each case under the procedural framework provided by the ICSID Convention and using the center's facilities. Arbitration or conciliation under ICSID is entirely voluntary, but once consent is given then it cannot be withdrawn unilaterally by either side. There are currently more than 150 countries which have ratified the convention and the caseload of the tribunals has increased substantially in recent years largely due to the proliferation of Bilateral Investment Treaties (BITs)⁶. In the past decade ICSID tribunals have resolved many disputes resulting notably from the economic crisis in Argentina as well as the privatization initiatives in Eastern Europe. Typically ICSID disputes relate to difficulties encountered by Western corporations

⁵ For a recent discussion of this topic see Justin R Marles, "Public Purpose, Private Losses: Regulatory Expropriation and Environmental Protection in International Investment Law" 16 J of Transnational L and Policy 275.

⁶ See generally ICSID website <<http://icsid.worldbank.org/ICSID>> (last accessed 19 March 2008)

which have invested in large projects in the developing world due to political upheavals in those countries.

Before embarking on the discussion of relevant ICSID decisions, let it be said that in establishing remedies in international investment arbitration, the investment contract or BIT is of paramount importance. The first step in the tribunal's assessment of an appropriate measure damages, and indeed its first step with respect to issues of jurisdiction and liability, is to examine the text of the investment contract or relevant treaty itself. This is because under the ICSID Convention the tribunal is required to "decide a dispute in accordance with such rules of law as may be agreed by the parties" and if there is no agreement as to governing law, the tribunal "shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable."⁷ Most of the now more than two thousand BITs require some form of prompt compensation for expropriations or other breaches of investment contracts⁸, as do multilateral treaties such as the North American Free Trade Agreement (NAFTA), under which disputes are also brought before ICSID⁹. It is also not uncommon for a concession contract leave open the nature of damages that will be available for breach, in which case the fixing of damages is expressly granted to

⁷ ICSID Convention Article 42 PROPER CITE FOR THIS?

⁸ The 2004 US Model Bilateral Investment Treaty calls for "prompt compensation" (Art 5.5) based on the "fair market value of the investment" (Art 6.2) but offers no insight as to compensation for lost profits or actual investments: Treaty Between the Government of the United States of America and the Government of [Country] Concerning the Encouragement and Reciprocal Protection of Investment, Office of the United States Trade Representative. < http://www.ustr.gov/assets/Trade_Sectors/Investment/Model_BIT/> (6 March 2008)

⁹ North American Free Trade Agreement, 17 Dec 1992, 32 ILM 612, Art 1110(2) defining "compensation" generally as fair market value immediately before expropriation. For further discussion of compensation for state interference with investors see eg Jeffrey Turk, "Compensation for Measures 'Tantamount to Expropriation' Under NAFTA: What it Means and Why it Matters" 1 International L and Management R 41.

the ICSID tribunal under the Convention¹⁰. In such cases the tribunal will point to the law of the investor state or, more problematically as we shall see in the next section, to the principles of international law¹¹. Any of the above categories can lead the tribunal to a consideration damages linked to the extent of actual investment, however the interplay of sources of authority for principles of international law has rendered remedies in international commercial arbitration highly uncertain, especially in the case of state actions such as expropriation¹² which are often the very type of disputes brought before ICSID.

Assessing Damages in International Law

Although it is conceded that there is no clear principle of compensation nationalization in international law¹³, there is almost universal consensus among international tribunals that the purpose of damages for breach of contract is to place the injured party in the position it would have been in had the contract been performed as promised¹⁴. International jurisprudence appears to suggest that compensation must repair, as far as possible by financial means, the damage caused by the illegal act and this may include both losses incurred as well as gains foregone. Such a goal was pronounced by the Permanent Court of Justice in the *Chorzow Factory* case: reparation must “wipe out all the consequences of the illegal act and re-establish the situation that would, in all probability, have existed

¹⁰ Art 42

¹¹ Art 42

¹² Christine Gray JUDICIAL REMEDIES at 194.

¹³ M Sornarajah, THE INTERNATIONAL LAW ON FOREIGN INVESTMENT, (Cambridge U Press, 2004) at 436. Sornarajah believes that the lack of uniformity is due as much to different jurisdictions’ views on property protection as much as their different approaches to compensation, at 452.

¹⁴ Gotanda “Recovery of Lost Profits” at 99.

had that act not been committed”.¹⁵ This principle of *restitutio in integrum* is mirrored in the International Law Commission’s Draft Articles on State Responsibility which states that the state responsible for an internationally wrongful act “is under an obligation to compensate for the damage caused thereby” and such compensation shall cover “any financially assessable damage including lost profits in so far as it is established.”¹⁶ With respect to breaches of contract in particular, international commercial arbitration similarly established the purpose of damages should be to “place the party to whom they are awarded in the same pecuniary position that they would have been in had the contract been performed”.¹⁷

Civil law systems’ terminology regarding damages are derived from the Roman law principles of *lucrum cessans* (gains prevented) and *damnum emergens* (actual loss suffered) and some combination of these two heads of damages is typically applied in international fora to achieve the objective *restitutio in integrum*¹⁸. *Lucrum cessans* essentially mirrors the primary objective of standard damages remedies in American contract law, which is the fulfillment of expectations that have been induced by the making of a promise – the so-called expectation measure. This is an amount of money that would put the injured party in the position they would have been in had the contract been properly performed, or which would give them the benefit of the bargain.¹⁹ In the context of international investment law, the expectation measure is properly viewed as

¹⁵ Case Concerning the Factory at Chorzow (Germany v Polish Republic), Claim for Indemnity (Merits) 13 September 1928, PCIJ 1928, Series A No. 17 at 47. The significance of Chorzow has been questioned by Sornarajah SEE BELOW NOTE X.

¹⁶ ILC Articles on the Responsibility of States for Internationally Wrongful Acts, Resolution of the General Assembly of the United Nations, 12 December 2001 A/Res/56/83. Annex Arts 36(1) and (2).

¹⁷ *Sapphire International Petroleum Ltd v NIOC*, Award of 15 March 1963, 35 I.L.R. (1967) 136 at 185.

¹⁸ John Y Gotanda, “Recovering Lost Profits in International Disputes” 36 Georgetown J of International L 61 at 65

¹⁹ Restatement of Contract 2d par 344 a); John Edward Murray Jr, Murray on Contracts 4th Edition (Lexis Nexis 2001) par 117.

the loss of profits that would have been earned from the investment, but for the interference of the host state. Lost future profits were awarded, for example, in the *Sapphire* case noted above, despite the inherently speculative nature of the investment concession.²⁰ The second chief category or head of damages for breach of contract in international law, *damnum emergens*, is for the most part conceptually similar to the reliance measure²¹, which compensates an injured party for any actions they undertook to their detriment in anticipation of the other party's contractual performance which result in a loss because of breach. Under this measure damages may be recovered for an amount representing the extent of the investments incurred for the purposes of performance.²² In the context of international investment law, the reliance measure is best seen in awards representing actual or direct investment costs incurred by the investor. Terms such as “sunk costs”, “wasted costs” or “out of pocket expenses” are also used variously to describe this remedy with limited practical differences.

While both *lucrum cessans* and *damnum emergens* are often claimed by the injured party, and often both awarded,²³ *damnum emergens* is typically awarded as an alternative when lost profits as per the expectation or *lucrum cessans* approach cannot be measured with sufficient certainty. Clearly parties whose investment activities have been adversely affected by the actions or omissions of the states in which they invest may receive compensation commensurate with their lost profits before an ICSID tribunal. Moreover, such amounts need not be demonstrated with complete certainty and recovery

²⁰ *Sapphire*, 35 I.L.R. at 187-88.

²¹ The similarity between reliance and *damnum emergens* was observed in the seminal article by Lon Fuller and William Purdue, who noted also that *damnum emergens* typically includes foregone opportunities elsewhere, which reliance does not: *The Reliance Interest in Contract Damages*, 46 Yale LJ 52 (1936) at 55.

²² Restatement of Contracts 2d par 344 b); MURRAY ON CONTRACTS par 117.

²³ Subject to the denial of double-recovery, SEE BELOW SECTION X.

will not be denied solely because the quantum is difficult to determine.²⁴ However the tribunal has also cautioned that compensation for lost profits must not be too remote or speculative. ICSID tribunals are reluctant to award damages based on lost profits if such profits would be highly speculative and result in an amount that was grossly disproportionate to the sum that was invested.²⁵ In particular ICSID tribunals are reluctant to award damages for lost profits for a new industry or one where there is limited record of profits.²⁶ On the other hand, *damnum emergens* appears to be always recoverable.²⁷

Although the assessment of *damnum emergens* has been praised by Gray as straightforward²⁸ in a way that lost profits is not, evaluating the extent of actual investments in a particular project is not as orthodox as it might initially appear. In the words of one ICSID tribunal: “it is a matter of controversy whether to use funds invested as a measure of the value of the investment.”²⁹ This tension may rest upon the often unappreciated difference between the value of the investment that has been seized by a foreign state and the associated damages resulting therefrom, such as, for example, a lost future income stream. This key paradigm is itself founded upon the important distinction between compensation resulting from a lawful government expropriation and damages

²⁴ Maritime International Nominees Establishment (“MINE”) (Claimant) v Republic of Guinea (Defendant) ICSID Case No. ARB/84/4 (AWARD) at 38. This is in keeping with modern US jurisprudence which typically permits recovery of lost profits even for un-established businesses if the losses can be proved with reasonable certainty: see Gotanda, “The Recovery of Lost Profits” at 71.

²⁵ *Metalclad Corporation v United Mexican States*, Case No. Arb(AF)/97/1, 30 August 2000; *Wena Hotels Ltd. v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4, Award (Dec. 8, 2000)

²⁶ *Asian Agricultural Products Limited v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Award of June 27, 1990; *Metalclad Corp. v. United Mexican States*, ICSID Case No. ARB(AF)/97/1, Award (Aug. 30, 2000); DOMESTIC “NEW BUSINESS DOCTRINE”

²⁷ *Amco Asia Corporation (Claimant), Pan American Development Limited (Claimant), PT Amco Indonesia (Claimant) v Republic of Indonesia (Defendant)* ICSID Case No. ARB/81/1 at par 178

²⁸ Christine Gray JUDICIAL REMEDIES at 201 referring to the damages assessment in *Sapphire International Petroleum Ltd. v. National Iranian Oil Co.* 35 ILR 136 (1963) (a non-ICSID arbitration).

²⁹ *Siemens A.G. (Claimant) v Argentine Republic (Respondent)* ICSID Case No. ARB/02/8 AWARD, 6 Feb 2007 at 376.

for an illegal act such as an unlawful expropriation or a breach of contract³⁰. While the latter might properly require assessment by reference to expectation losses, the former may be properly within the sphere of reliance-based damages³¹. However as we shall see, the ICSID tribunals that have awarded actual cost of investment do not appear to acknowledge this distinction when deciding upon a *standard* for assessing damages. Rather, the tribunals seem most concerned with accuracy and the avoidance of speculation through credible verification of amounts invested. Thus the primary objective in the remedy selection process is one of precision, which may be explained according to an underlying motive of efficiency, as we shall discuss in Section XX. Hojer has suggested that ICSID tribunals may view actual investments as a “starting point”³² when assessing an appropriate remedy, but as we shall now see ultimately the decision to implement a reliance-based remedy will depend upon the contents of the particular investment contract or BIT, the circumstances of each case, the type of investment, and importantly the nature of the violation, such as whether it involves an expropriation or the violation of the fair and equitable treatment standard that appears in most investment agreements.

Reliance-Based Damages: Recovery for Actual Investments at ICSID

³⁰ Christine Gray *Judicial Remedies in International Law* (Clarendon Press Oxford 1987) at 194, noting that the significance of the distinction is not entirely clear at 202. Generally, the term “compensation” is used to remedy lawful takings, “damages” is used when the taking was unlawful, although there is no practical difference between the two concepts: C.N. Brower and M Ottolenghi, “Damages in Investor State Arbitration” 4:6 *Transnational Dispute Management* 1 at 4. Sornarajah notes that the seminal dicta from *Chorzow Factory* was limited to unlawful takings, a fact that is not appreciated by many legal scholars: *THE INTERNATIONAL LAW ON FOREIGN INVESTMENT* at 453-456.

³¹ Sornarajah at 470, referring to principles enunciated in *Amoco International Finance Corporation v Iran* (1982) 1 *Iran-US Claims Tribunal* 493.

³² Kaj Hober, “ ‘Fair and Equitable Treatment’ – Determining Compensation” in Rainer Hofmann / Christian J Tams eds *The International Convention on the Settlement of Investment Disputes (ICSID): Taking Stock After 40 Years* (Nomos, Frankfurt, 2007) at 101

In some cases the tribunal has completely ignored a claimant's request for damages based upon out-of-pocket expenses incurred through their activities, preferring instead to focus on the compensation of lost profits.³³ The tribunal has also noted that compensation for investment costs should be considered normal, stating: "previous arbitral tribunals ... have overwhelmingly favoured the award of lost investment costs" a reference to the LIAMCO ad hoc oil concession arbitration which itself urged that at a minimum *damnum emergens* should be awarded in international investment disputes, representing the value of tangible goods and the cost of installations as well as unknown expenses.³⁴ In the very same dispute, the ICSID tribunal commented that the determination of a lost investment is a "relatively simple operation", unlike the calculation of lost profits. In contrast to the enormous quantity of ICSID jurisprudence regarding the valuation of lost profits for the purposes of damages awards, there is startling little ICSID case law concerning investment based compensation. Review of this limited material reveals that the determination of lost investments at ICSID is essentially an accounting exercise, the principle difficulty of which is the veracity and reliability of the evidence presented regarding expenditures.

Actual investment expenses were recovered by the claimant in *Wena Hotels Ltd v Arab Republic of Egypt*³⁵ as an alternative to an award for lost profits to compensate for the expropriation of hotels in Cairo and Luxor. Lost profits were unrecoverable both because there was insufficient record of profits before the seizure on which to base an

³³ See eg, Maritime International Nominees Establishment ("MINE") (Claimant) v Republic of Guinea (Defendant) ICSID Case No. ARB/84/4 (AWARD)

³⁴ ICSID Case No. ARB/83/2 (AWARD) Liberian Eastern Timber Corporation [LETCO] (Claimant) v Republic of Liberia, ICSID Case No. ARB/83/2 (Award) citing LIAMCO v Libya 20 ILM 1 (1981).

³⁵ Wena Hotels Limited v. Arab Republic of Egypt Case No. ARB/98/4 AWARD December 8, 2000

estimate and also because the amount claimed (£46) was grossly disproportionate to the amount invested (£9). In fixing damages based instead on the claimant's actual investments in the hotel projects, the tribunal added that the fact that expenses were incurred by the claimant's affiliates was immaterial, although adjustments were made to account for erroneous double counting of certain unidentified expenses. This determination survived an evidentiary challenge at a later annulment proceeding – the respondent's allegation that various financial documents were missing was rejected, the tribunal noting that it may assess the credibility and completeness of evidence at its own discretion.³⁶ This case underlines the importance of reliable evidence in the establishment of a cost-incurred remedy.

A reliance-based measure of damages was contemplated by ICSID in its high-profile arbitration of a NAFTA dispute between the Metalclad, the subsidiary of a Mexican corporation, and the United States regarding the latter's interference with a landfill development project through both unfair treatment and expropriation. As an alternative to the fair market value of the assessment, the claimant corporation proposed the actual investment in the landfill as an appropriate means of fixing compensation. The tribunal viewed actual investments as the correct mechanism for ascertaining compensation because a claim of market value based on future profits could not be adequately substantiated by reference to past performance as there was insufficient record of the landfill's prior commercial activity. In arriving at this decision the tribunal cited similar practice by the Iran-US Claims Tribunal, which had used a value of investment

³⁶ Wena Hotels Limited v. Arab Republic of Egypt (ICSID Case No. ARB/98/4) Annulment Proceeding 28 January 2002 At 64-65

method to gauge compensation in the absence of a realistic estimate of future profits³⁷.

The actual investment method was also seen as being consistent with the celebrated guidelines from the International Court of Justice in the *Chorzow Factory* case which, as noted above, established that compensation should “wipe out 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.”³⁸ The claimant used US federal income tax documentation and an independent auditor’s reports to substantiate its investment costs which included such items as personnel, insurance, travel, telephone, accounting and legal, consulting, interest, office, property, plant and equipment costs. The tribunal adopted a more stringent approach to preparatory costs, denying recovery for costs incurred in the year prior to Metalclad’s purchase of the company which owned the landfill because such costs were seen as too remote to the investment. This aspect of the ruling illustrates that limiting principles of damages familiar to common law jurisdictions are relevant at ICSID tribunals.

The ICSID tribunal elected to assess damages based on the reliance measure in the recent *PSEG Global Inc. (Claimant), Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi (Claimant) v Turkey (Respondent)*³⁹. As an alternative to a claim for lost profits, claimants PSEG Global Inc. and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi argued that they deserved compensation in the amount of investment by the Turkish government for its legislative interference with the companies’ operations of the newly privatized energy sector in Turkey’s central region. The particular out of pocket

³⁷ *Phelps Dodge Corp. v. Iran* 10 Iran-U.S. C.T.R. 121 (1986)

³⁸ *Chorzow Factory (Claim for Indemnity) (Merits), Germany v. Poland, P.C.I.J. Series A., No. 17 (1928)* at 47 THIS PRINCIPLE IS SEEN NOW ALSO SEEN IN THE DRAFT ARTICLES ON STATE RESPONSIBILITY CITE SECTION (?32?).

³⁹ ICSID Case No. ARB/02/5, 2007 WL 1215067 (APPAWD) 19 January 2007

expenses cited included costs of preparing the power plant project as well as mine studies, contract negotiations and financing, environmental costs, permits and license fees, and legal and consulting fees. The respondent Turkey contended that more than half of the claimed costs were incurred by other companies actually unrelated to the energy project and should consequently not be compensated. More importantly, Turkey argued that investment costs should not be awarded because the project would have ultimately led to a loss, a restriction on the application of the reliance remedy seen in American contract law⁴⁰. In expanding upon the precise expenses for which compensation could be paid, the tribunal stated:

An investment can take many forms before actually reaching the construction stage, including most notably the cost of negotiations and other preparatory work ...even in connection with pre- investment expenditures, particularly when ... there is a valid and binding Contract duly executed between the parties.⁴¹

The tribunal awarded investment-based damages of approximately US \$9M, although only those expenses actually incurred by the claimants themselves were included, not those by related companies, and the award was diminished slightly because of erroneous double-counting for certain smaller expenses. The cost of contract negotiation itself and legal fees therein, meaning some expenses incurred even before the existence of any legal obligation, were also viewed as a legitimate expenses deserving of compensation.⁴²

Previous ICSID case law, notably *Metalclad*, has suggested that preparatory expenses prior to the execution of the investment contract will not be recoverable, even if they

⁴⁰ MURRAY ON CONTRACTS par 121 D.

⁴¹ At 304

⁴² Recovery for detrimental reliance incurred before contract formation was controversially permitted by the British Court of Appeal in *Anglia TV v Reed* 3 All ER 690 (1971) and is now acknowledged under US contract law: Restatement of Contract 2d par 349.

could be considered part of the investment. Whether or not such costs are recoverable may, of course, depend on the wording of the particular investment agreement.⁴³ It is noteworthy that legal fees incurred in establishing an investment (rather than disputing losses from an affected investment) have been explicitly labeled “out of pocket” costs by another ICSID tribunal and compensated accordingly.⁴⁴ The tribunal’s decision to award the investment costs appeared to be based primarily on the fact that the amounts claimed had been subjected to a careful and credible audit. That the electricity project may have ultimately led to a loss had it been completed was influential in preventing the tribunal from awarding lost profits, which it viewed as highly speculative, but a prospective loss on the contract did not appear to undermine the compensation for out of pocket costs, as it might well have in domestic American law had the loss been sufficiently established by the respondent⁴⁵.

Another ICSID tribunal considered the extent of recovery for investment-related expenses in *Autopista Concesionada de Venezuela, C.A. (Claimant) v Bolivarian Republic of Venezuela (Respondent)*⁴⁶ a dispute brought by a Venezuelan company against the Venezuelan government regarding a concession to build and improve a highway system connecting the city of Caracas to the coast which was financially hindered by the government’s decision to freeze highway toll rates due to a citizen uprising. Venezuela argued that under the terms of the concession agreement, the

⁴³ MTD Equity Sdn Bhd. & MTD Chile S.A. (Claimant) v Republic of Chile (Respondent) FIND CITE FOR THIS AWARD Paras 217, 240(ii). 25 May 2004, upheld following Annulment Proceeding ICSID Case No. ARB/01/7. EXPLANATION GIVEN AS TO WHY PREPATORY WORK NOT COMPENSATABLE? LAW OF CHILE?

⁴⁴ Liberian Eastern Timber Corporation [LETCO] (Claimant) v Republic of Liberia, ICSID Case No. ARB/83/2 (Decision on Rectification)

⁴⁵ MURRAY ON CONTRACTS par 121 D. The logic behind this rule is that damages should not be awarded that will allow parties to escape the risk of bad bargains.

⁴⁶ ICSID Case No. ARB/00/5, 2003 WL 24070173 (APPAWD) 23 September 2003

respondent company could only claim out of pocket expenses incurred through activities that fulfilled the terms of the agreement. Although the tribunal allowed the respondent to claim for lost profits as well (pointing to a more broadly phrased provision of the agreement allowing other heads of damages) the tribunal did state that with respect to the investment costs, only those out of pocket costs sustained under the terms of the contract could be compensated. In order to ascertain which particular investment costs could be claimed, the tribunal examined financial statements prepared by the respondent company, which it viewed as presumptively reliable, noting however that an unexplained increase in recorded costs would not be recoverable. Applying Venezuelan law, recovery of bidding costs was not permissible (although they were not in fact claimed) but negotiation costs were. A loan extended by the claimant to an affiliate company was not viewed as a legitimate out of pocket expense because it could not be substantiated through the claimant's expert's uncertain testimony. The tribunal ruled that although legal costs arising out of the highway project (apart from the ICSID arbitration itself) were the valid subject of a claim, only those costs incurred as a result of the respondent's action could be recovered – not those involving litigation with private citizens who had disrupted the highway project. As the claimant did not properly segregate these two categories of legal cost in its financial records, the tribunal awarded half of the claimant's legal costs (an amount representing what the tribunal saw as the expenses relating to dealings with the Venezuelan government). Costs of soil studies prepared by the claimant company in anticipation of the project were awarded, despite the fact that they were incomplete and had no current value to either party. Administrative costs incurred regarding the ongoing operation of the highway project during the disruptions were

recoverable, although the tribunal discounted the claimant's specified amount by 10% to reflect the tribunal's impression that the amount was excessive and given the incompleteness of the expert's report on this matter. The total amount of out-of-pocket expenses awarded to the claimant company was just over 2 billion BS.⁴⁷ Additional amounts were recovered for lost profits which were specifically allowed under the concession agreement, irrespective of any concurrent recovery for expenses.

Out of pocket expenses were examined by the tribunal in *Southern Pacific Properties (Middle East) Limited v Arab Republic of Egypt*⁴⁸ for a claim involving a Hong Kong company's investments in tourist facilities near the Giza Pyramids and on the Mediterranean coast of Egypt which were later opposed by citizens because of concerns of damage to ancient sites and artifacts, resulting in the public expropriation of the designated land. As an alternative to damages based upon the value of the investment project at the time of expropriation, the claimants requested compensation for out of pocket expenses, including a loan to an affiliated company, capital and development costs pre and post project cancellation administrative and legal costs. The tribunal outlined the nature of these expenses:

[C]onsiderable amounts of time and money were spent on negotiating, planning and implementing the project. [The Claimant] made capital contributions and loans [to its affiliate] ... these amounts must be reimbursed as part of ... fair compensation ... [W]hen the project was cancelled, construction was under way and considerable marketing activity had been carried out. Most of the detailed engineering design and specifications for the first phase ... had been completed. A construction contract had been concluded for the infrastructure, construction had begun and lot sales had commenced. To the extent that the expenses associated with this activity have been proven ... reimbursement of such expenses is also part of ... fair compensation...⁴⁹

⁴⁷ Bolivars, the Venezuelan currency.

⁴⁸ CASE NO. ARB/84/3 20 May 1992; 32 I.L.M. 933 (1993)

⁴⁹ At 198.

Recoverable development costs were further elaborated upon to include allocation of salaries, travel and entertainment expenses of executives, recruitment and relocation of personnel as well as consultations for marketing and banking. Again, the recovery of these amounts was contingent upon the production of documentation detailing the specific nature, date and amount of expense incurred in order to confirm that they were legitimately related and directly connected to the project. Such expenses were viewed by the tribunal as irrecoverable losses because of the cancellation of the tourist development project. It is significant that the tribunal did deny recovery for any investment expenses that could not be verified through proper documentation, including those where the individual payee could not be identified. Strangely, the tribunal also included litigation costs associated with its own procedure as legitimate “out of pocket” expenses that should be compensated in order to make whole the party who had suffered the loss.⁵⁰ This does not appear to fit with the American concept of detrimental reliance as litigation costs are not incurred for the purpose of performing the contractual obligation. The *Southern Pacific* tribunal also interestingly distinguished between ordinary out of pocket expenses and those involving the costs of lost opportunity in making a commercial success of the project, illustrating that the parity between the concepts of *damnum emergens* and reliance is not absolute.⁵¹ Most significantly, the tribunal noted that the appropriate situation in which reliance-based damages should be awarded is when the value of the investment at the time of expropriation is either nil or *less than the out of pocket expenses*.⁵² As discussed earlier, this is the exact opposite of American common law which denies reliance-based recovery where there would have been a loss in

⁵⁰ At 207-208.

⁵¹ See earlier footnote FULLER AND PURDUE. Reliance would not typically award opportunity costs.

⁵² At 214

performance⁵³. The tribunal's logic is unclear here as damages should not be awarded in an amount that enables party's to avoid the natural risk of bad bargains. In *Southern Pacific*, the investment value at the time of expropriation of the project was determined to be more than the previously calculated out of pocket expenses. The tribunal consequently awarded the difference between the value of the project at expropriation and the investment costs in addition to the previously calculated out of pocket expenses (approximately US \$3M)⁵⁴.

In the *Amco Asia v Indonesia* case regarding the nationalization of a hotel apartment complex, the ICSID tribunal criticized the asserted method of Net Book Value of invested assets as a means of ascertaining the extent of expenditures, noting that this method had typically been used in international law where compensation for prospective earnings was unavailable for some reason, such as a legislative bar to profit-based recovery in the law of the host state.⁵⁵ While a full treatment of asset valuation methodology is beyond the scope of this article, it should be noted that it is unfortunate that no precise definition of the concept of Net Book Value was given by the tribunal, other than the somewhat unhelpful "assets minus liability."⁵⁶ Further elaboration would have been illuminating because of the important role that depreciation necessarily plays in the valuation of reliance based expenditures. One would expect that capital assets

⁵³ MURRAY ON CONTRACTS par 121.D citing *Bausch & Lomb v Bressler*, 977 F 2d 720 (2d Cir. 1992).

⁵⁴ The tribunal adjusted upwards the investment expenses awarded because of the devaluation of the US dollar that had occurred since the project had begun in 1978.

⁵⁵ At 193. FULL CITE. "DAMNUM EMERGENS" ITEM 6 CASE. The tribunal listed numerous other situations in which Book Value of assets had been used, including, strangely, "where the claimant himself had requested as damages the reimbursement of his invested capital" which would seem to be a very common occurrence.

⁵⁶ At 191. Another ICSID tribunal explained that Book Value is an appropriate means of valuing a recent investment where there is no market for the assets that have been expropriated, however it is often also used to value costs actually incurred which were wasted in the effort to generate revenue: *Siemens A.G. (Claimant) v Argentine Republic (Respondent)* ICSID Case No. ARB/02/8 AWARD, 6 Feb 2007 at 355.

purchased for the purpose of an investment which is subsequently expropriated should be assessed by their initial cost but rather diminished according to the decline in the asset's value over their use i.e. during the profit-earning period prior to the termination of the investment due to expropriation, otherwise over-compensation will result. Without addressing this important issue directly, the tribunal concluded that Book Value methodology was inappropriate with respect to certain types of assets, such as long-term contractual rights, ultimately preferring to focus on projected future profits as the measure of damages, which it ascertained using Discounted Cash Flow analysis.⁵⁷ Interestingly the tribunal noted that the value of physical assets will also inform the result of a future profit analysis, however the approach is not always appropriate:

... the value of the physical assets lost by the investor due to the taking of the investment is added to the discounted cash flow in order to assess the total amount of the damages ...[but] this method might raise serious problems in cases where at the end of the contractual relationship (or of the legal relationship comparable to a contractual one), the injured party would not have been entitled to keep valuable goods previously utilized for the operation of the business. Moreover, the value of physical assets thus utilized is itself essentially based on the earnings that such utilization may yield; therefore, the valuation of the net cash flow may well reflect the commercial value of the physical assets.⁵⁸

The conclusion here appears to be that a future profit analysis may perhaps paradoxically be the best way to assess a past-investment based loss. Other ICSID tribunals have observed this difficult aspect of valuation. This is seen in the concepts of Net Present Cash Flow, which attempts to fix a current value of the investment according to the

⁵⁷ Depreciation issues were relevant for the purposes of assessing future profits as well, at 212-222. Another ICSID tribunal has noted that discounted cash flow is itself a highly speculative measure and should be used with caution: ADC Affiliate Limited (Claimant), ADC & ADMC Management Limited (Claimant) v Republic of Hungary (Respondent) ICSID Case No. ARB/03/16, 2 October 2006 at 502.

⁵⁸ Amco v Indonesia At 271.

projected value of lost future business. Indeed the complexities of the various accounting measures leads one to question the rigidity of the boundaries between the simple categories of reliance and expectation based damages, which may well be the reason that both *lucrum cessans* and *damnum emergens* are typically argued by the claimants in ICSID arbitrations.

Claimant Azurix asserted that the extent of its compensation for the expropriation of its water concession by Argentina should be based on the actual investment method and the tribunal felt that this method was appropriate because the investment in question “is recent and highly ascertainable.”⁵⁹ This case is worthy of recognition because the tribunal was concerned that the “aggressive” price paid for the concession by the claimant was excessive compared to other bids. The tribunal held that in fact no well informed investor would have paid such a high amount based on the modest estimated revenues of the project. Consequently, gauging damages according to amounts invested is not always a sensible approach because such amounts may be commercially unreasonable in the circumstances. In awarding compensation for investment costs based on an amount that an independent well-informed third party would have paid for the concession, which was substantially less than what the claimant actually paid, the tribunal appeared to be merely reiterating a familiar aspect of the reliance remedy: damages will be recovered for the costs of performance *reasonably incurred*.

Although the text of the ICSID awards is not always clear on the point, it must be emphasized that while the tribunal permits recovery for both lost investments and lost profits, it does not permit double recovery (costs and profit) for the same items, which

⁵⁹ Azurix Corp. (Claimant) v Argentine Republic (Respondent) ICSID Case No. ARB/01/1 (Award) at 425

would result in costless gain for any investment and which would be invidious even for the lowest risk commercial activities. In order to avoid double recovery the amount awarded for lost profits must be reduced by the investment amount such that compensation for lost profits is always net.⁶⁰ The adjustment of investment-based compensation because of an award for future profits was seen in *Liberian Eastern Timber Corporation [LETCO] (Claimant) v Republic of Liberia*⁶¹, a dispute involving a concession agreement for the harvesting of forest products. Here the tribunal explicitly reduced the recovery for investment in infrastructure, machinery and equipment because that amount had already been included in the calculation of net profit i.e. the figure for expected profit was derived from gross income expected minus costs incurred. The only investment cost that was not reduced in this way was a bank penalty on a loan, taken out for the purposes of the investment, that was imposed because of Liberia's interference with the project. Although the concept of "profit" necessarily means net rather than total gain, this is not always apparent when ICSID awards include both lost future income and out of pocket expenses. It is often necessary to review the tabulated amounts at the end of the award, rather than the text of the judgment in order for this understanding to emerge.

Efficiency Goals of ICSID Awards

The cases discussed above divulge very little reasoning with respect to the selection of cost-based damages other than the concern for achieving accuracy, primarily by avoiding the prediction of uncertain future profits based on unverifiable evidence. That there is

⁶⁰ See Mark Kantor pages 69-71.

⁶¹ ICSID Case No. ARB/83/2 31 March 1986

little economic analysis of investment law⁶² and certainly none that has focused on ICSID is surprising because although the ICSID tribunals do not attempt to justify their decisions on efficiency grounds, the selection of remedies in this manner is grounded in economic theory. Put simply, compensation based upon amounts actually invested are chosen by ICSID tribunals because such awards serve the obvious function of reducing error costs.

Courts and tribunals suffer from a deficiency in information regarding laws or facts which results in mistakes when applying substantive legal principles. One of the most common mistakes on the part of adjudicatory bodies is their failure to assess the quantum of damages accurately such that a breach of contract (or a tortious injury) is properly compensated. With perfect information available, a court will be able to craft a perfect remedy (which is often seen as the level at which the injured party would be indifferent between performance and breach or injury and cash)⁶³, but as this is a logical impossibility, courts must seek a second-best alternative, which is to apply as much information (facts and law) as possible without the transaction cost of evaluating this information exceeding the advantage of accuracy in pronouncing a judgment. Thus in their attempt to minimize error costs (the inevitable failure to select a perfectly accurate judgment), courts are compelled to craft remedies based on the most reliable available information.⁶⁴ In each of the ICSID cases discussed above there was a large quantity of cost-oriented information readily available to the tribunal in the form of expert testimony

⁶² Exceptions include Fabrizio Marrella and Irmgard Marboe “Efficient Breach and Economic Analysis of International Investment Law” 4:5 Transnational Dispute Management 1 and Alan O Sykes, “Public Versus Private Enforcement of International Economic Law: Standing and Remedy” 34 J of Legal Studies 631 (advocating private claims for monetary damages in international investment law but not in international trade).

⁶³ COOTER FIND CITE

⁶⁴ COOTER at 376

or financial records which can be readily applied to tailor a remedy that approximates perfection. Were a profit-focused or expectation type standard pursued then this information would have less utility (or even none), raising the risk of adjudicative errors because of the consequential reliance on predictive modeling. However, it must be recognized that the provision and examination of extensive cost-based evidence also represents a *process* cost to the disputants that could ultimately result in resistance against the use of ICSID as a means of adjudicating disputes. In contrast, the tribunal's determination of future profits appears to involve essentially the application of one or more formulae to historical revenue data, an exercise which entails a much diminished (and less costly) evidentiary consideration than the assessment of numerous individual assets.⁶⁵

In addition to the error costs borne by the parties to arbitration associated with a tribunal's failure to set an appropriate remedy, there are also social costs that result from the imposition of an imperfect remedy. These are the distortions in incentives that result from either over-compensation or under-compensation of an injury resulting from an expropriation or broken investment agreement.⁶⁶ If the injured company is compensated below the level of perfection, then other companies will be reluctant to engage in foreign direct investment in the future – which as we have seen is one of the purposes of the ICSID Convention.⁶⁷ Merrills has suggested, however, that the failure to compensate an investor fully may result in positive incentives: foreign firms may be discouraged from

⁶⁵ These process cost differentials are the general impression of this author based on a reading of the cases discussed herein (notably *Autopista v Venezuela* and *Azurix v Argentina*) and cannot be verified because litigation costs as disclosed are not segregated according to their mathematical and or evidentiary components.

⁶⁶ COOTER AT 377

⁶⁷ Uncompensated losses associated with government takings have been termed “demoralization costs” : Frank I. Michelman, “Property, Utility, and Fairness: Comments on the Ethical Foundations of ‘Just Compensation’ Law, 80 Harvard L R 1165 (1967).

engaging in investments that are harmful to the foreign state in case such actions result in a regulatory response from that state.⁶⁸ If an injured company is over-compensated, this might be viewed as an interference with a state's sovereign right to nationalize its own industry in the interest of its people. An excessive damages award will then undermine the political legitimacy of investment arbitration.⁶⁹ Moral hazard may also ensue – as investors will allocate the risk of their investments to the respondent state during dispute settlement.⁷⁰ Over-compensating investors may give them the perverse incentive to act irresponsibly⁷¹ for example, by engaging in activities which although profitable, are damaging to the local environment. Furthermore, with excessive damages, host states will be discouraged from terminating economically wasteful projects where to do so would be efficient, a so-called “efficient breach”.⁷² The important point is that in order for a state to engage in a rational assessment of efficiency it will need to be able to calculate *ex ante* the costs of breach and compare them to the cost of compliance.⁷³ The readily discernable, or at least estimable, nature of actual investment costs (again as opposed to estimated future profits) thus represents an attractive remedy from an incentive perspective. Such incentive effects are particularly acute even for a private tribunal like ICSID as most of its cases are now disseminated on the internet and in case reporters and many disputes now receive extensive media coverage.

⁶⁸ Merrills, “Incomplete Compensation for Takings” at 135.

⁶⁹ T.W. Walde and B Sabahi, “Compensation, Damages, and Valuation in International Investment Law” 4:6 Transnational Dispute Management (2007) 1 at 4.

⁷⁰ Walde and Sabahi at 12.

⁷¹ Jeffrey Turk, “Compensation for Measures ‘Tantamount to Expropriation’ at 70

⁷² Fabrizio Marrella and Irmgard Marboe “Efficient Breach and Economic Analysis of International Investment Law” 4:5 Transnational Dispute Management 1 at 8.

⁷³ Marrella and Marboe at 13. The costs to the state may not be simply the payment of damages – there will be reputational costs that could result in difficulty attracting foreign investment in the future.

Although again not directly referenced in any ICSID cases, reliance based damages may be preferable from an efficiency perspective because the proof of expectation damages based upon projected profits may require the innocent party to divulge potentially sensitive information about their own internal business strategy,⁷⁴ unlike investment related information such as labor and equipment costs. Obviating the need to disclose profit information would assuage some of the confidentiality concerns that have cultivated ICSID members' reluctance to publish all awards in their entirety and in so doing lessen the widespread disdain for the forum from the international community because of its lack of transparency. Increased transparency of ICSID awards is of vital importance with respect to the integrity of the arbitral process, the confidence of its users in the system and most importantly from an economic standpoint – the effectiveness of ICSID in encouraging foreign investment.⁷⁵ Since both confidentiality and transparency of the proceedings are highly desirable features of international commercial arbitration, remedies that facilitate both objectives should be pursued. Whereas information regarding lost profits might expose investors to unwanted scrutiny from competitors, actual expenditures would do little more than demonstrate the business acumen associated with a past project.

Suitability of Reliance-Based Remedies

The appropriateness of reliance based compensation may depend on whether the injurious behavior was the result of an expropriation or for violations of the fair and

⁷⁴ RICHARD EPSTEIN, *TORTS*, (Aspen Publishers, New York, NY, 1999) at par 21.3.

⁷⁵ See eg Noah Rubins, "Opening the Investment Arbitration Process: At What Cost, for What Benefit?" in Rainer Hofmann / Christian J Tams eds *The International Convention on the Settlement of Investment Disputes (ICSID): Taking Stock After 40 Years* (Nomos, Frankfurt, 2007); Schreuer BOOK at 827.

equitable treatment standard, as the former terminates an investment whereas the latter may still permit ongoing business activity.⁷⁶ In the case of an expropriation, an award of lost profits may be more appropriate because this will represent the most investor-friendly approximation of the injuries sustained and an award of something less than anticipated missed profits from the seized investment will represent incomplete compensation. If the investment activity continues, however, with some unfair treatment from the host state falling short of expropriation, then an award of profits could well represent a double-recovery given that some profit may be maintained. The difficulty in fixing compensation for breaches of the fair and equitable treatment standard are exacerbated by the lack of reference to compensation for such injuries in treaty language (in contrast to expropriation) and consequently compensation for such violations will often depend on the circumstances of each dispute.⁷⁷

Some commentators have criticized the application of contract law's somewhat rigid categorization of heads of damage to the arena of international investment in part because of this concern for double-recovery engendered by the application of both *damnum emergens* and *lucrum cessans* to activities that comprise both individualized assets and future income streams,⁷⁸ however as suggested above, double recovery should be prevented by the application of a net rather than gross profit determination, which one might expect would amount to *lucrum cessans* minus *damnum emergens* rather than in

⁷⁶ Kaj Hober, " 'Fair and Equitable Treatment' – Determining Compensation" in Rainer Hofmann / Christian J Tams eds *The International Convention on the Settlement of Investment Disputes (ICSID): Taking Stock After 40 Years* (Nomos, Frankfurt, 2007) at 83

⁷⁷ Hober; Iona Tudor "Balancing the Breach of the FET Standard" 4:6 *Transnational Dispute Management* 1; P Mulchinski "Caveat Investor? The Relevance of the Conduct of the Investor Under the Fair and Equitable Treatment Standard" 55 *ICLQ* 527.

⁷⁸ See eg T.W. Walde and B Sabahi "Compensation, Damages and Valuation in International Investment Law" 4:6 *Transnational Dispute Management* 1 (2007) and Irmgard Marboe, "Compensation and Damages In International Law: The Limits of Fair Market Value" 7:5 *Journal of World Investment and Trade* 723.

addition to it – although of course any formula including both heads would require twice the resources in calculation (process costs) and a corresponding increase in error potential. Clearly the circumstances of each case will dictate the optimal remedial approach, which will take into account the risks of under and over-compensation as noted above.

Assessing damages in investment arbitration on the basis of amount of investment has been recommended by Wells because this measure is likely to approximate full market value, at least in the case of recently acquired assets.⁷⁹ It is significant that none of the ICSID cases discussed herein considered recovery for the actual investment costs of intangibles such as business goodwill, customer loyalty or reputation. The use of the *damnum emergens* measure in the investment context has been condemned for its inability to address such losses, as well as for failing to account for incremental increases in value for development activities in an unfinished project beyond their initial acquisition cost.⁸⁰ However, this objection represents more so a criticism of individual asset valuation methodology rather than the standard of compensation, an often blurred distinction that must be kept in mind during the remedy stage of an award. Once the various expenses for which damages will be paid have been identified via a standard of compensation, the evaluation process operates as a separate and very complex aspect of ICSID adjudication. Commentators have observed that arriving at a precise valuation of damages in investment disputes is a much more difficult task than merely establishing the

⁷⁹ FIRST NAME Wells, “Double Dipping in Arbitration Awards? An Economist Questions Damages Awarded to Karaha Bodas Company in Indonesia, 19 *Arbitration International* 471 at 474-475.

⁸⁰ Mark Kantor, “Valuation for Arbitration: Uses and Limits of Income-Based Valuation Methods” 4:6 *Transnational Dispute Management* at 10 and 22-23.

standard to be applied.⁸¹ Although not properly the subject of this article, we have seen some indication in the application of the reliance measure that a wide range of valuation methods are used by ICSID. Indeed a flexible interplay of many methods has been advocated by commentators.⁸² In quantifying the precise value of an investment (via whatever head of damage) the tribunal has stated that its methodology and reasoning should be fully transparent.⁸³ Unfortunately the preceding examination of some limited ICSID case law has shown that there is very little explanation offered as to the precise methodology of evaluation of actual investment-based compensation. This general shortcoming of international arbitration has been acknowledged by commentators⁸⁴ and remains a legitimate grievance of disputants at ICSID as well as those in the academic community.

It is difficult to discern any instructive jurisprudence from ICSID cases regarding awards of actual investment costs, other than the indisputable assertion that they are more likely to be implemented when future profits are highly indeterminate. In addition to the stipulation of actual investment recovery in an investment contract or BIT, we can conclude also that detailed, verifiable financial statements are essential to the success of a claim for actual investment losses. ICSID awards are manifestly fact-oriented and it would not be far wrong to characterize ICSID tribunals as essentially fact finding bodies. This statement is intended to be descriptive rather than judgmental. The extent to which the tribunal focuses on the evidence tendered by the parties for the purposes of assessing

⁸¹ C.N. Brower and M Ottolenghi, "Damages in Investor State Arbitration" 4:6 Transnational Dispute Management 1 at 12 -13

⁸² Walde and Sahadi "Compensation, Damages and Valuation". Suggest that complexity of valuation methods may require the use of the tribunal's own expert: at 22.

⁸³ Amco Asia Corporation (Claimant), Pan American Development Limited (Claimant), PT Amco Indonesia (Claimant) v Republic of Indonesia (Defendant) ICSID Case No. ARB/81/1 at 188

⁸⁴ See eg C.N. Brower and M Ottolenghi, "Damages in Investor-State Arbitration" 4:6 Transnational Dispute Management 1

damages for nationalization claims should be familiar to American observers, as the process of adducing financial evidence for the purposes of valuation, often with the aid of expert testimony, has been compared to that of domestic American takings litigation under the US Constitution.⁸⁵ One must also recall that the under the ICSID Convention, the tribunals are empowered with the total discretion in deciding on the relevance and admissibility of evidence adduced by the parties, as well as in exercising the power to request further information.⁸⁶ This is the type of adjudication that contracting members assent to by virtue of their ratification of the Convention.

The attempt to subject assessment of damages in international arbitration to general rules of law has been opposed in favor of a more pragmatic approach based on, *inter alia*, the relationship between the parties.⁸⁷ Such remedial flexibility is particularly important in disputes that are essentially fact-based.⁸⁸ While remedial flexibility is a worthwhile objective, the process must have determinacy, which is the perhaps the most appealing feature of reliance-based measures, even if fair compensation is ultimately compromised. Complete compensation may not always be the most desirable goal. Indeed international investment law has shown a trend towards partial compensation for many types of takings by foreign states, such as those which are lawful or those where the investor had adopted bad industry practices.⁸⁹

⁸⁵ Merrills, "Incomplete Compensation" at 115-117.

⁸⁶ Christopher Schreuer, *The ICSID Convention: A Commentary* (Cambridge University Press, 2001) at 647. See also *The Arbitration Rules*, 1984, Rule 34(1) The Tribunal shall be the judge of the admissibility of any evidence adduced and of its probative value. 1 ICSID Reports 169 and Article 43 of the ICSID Convention.

⁸⁷ GRAY BOOK at 206.

⁸⁸ Peter Ashford, *Documentary Discovery and International Commercial Arbitration*, 17 *American Review of International Arbitration* 89 at 96.

⁸⁹ Sornarajah at 485.

Conclusion

Gray has termed the quest for a single method of calculating compensation for breach of international contracts “a chimera that has been obsessively pursued by many scholars”⁹⁰ and this article has by no means attempted to suggest that it has found the answer in relation to international investment arbitration. Rather than abandon the common law of contract’s preference for lost profit-based compensation, this article has demonstrated that ICSID’s occasional recourse to actual investment losses is a suitable compliment to expectation-oriented damages, and one that is, perhaps unknowingly, based upon principles of efficiency. In addition to reducing error costs of faulty compensation because of evidentiary reliability, and the associated incentives engendered therein, reliance-based awards at ICSID will also serve to enhance confidentiality without impeding transparency. ICSID’s use of *damnum emergens* may reflect its willingness to escalate the process costs of adjudication through voluminous but verifiable evidence rather than risk raising the error costs of faulty judgments based on uncertain expectations. Given the generally efficient incentives that should ensue from the application of this “safer” measure, the observed application of reliance based damages at ICSID should be applauded and other international fora should be urged to follow suit.

⁹⁰ Christine Gray JUDICIAL REMEDIES at 202