UNCITRAL Secretariat:

Draft note - Assessment of damages and compensation

Webinar on Damages in ISDS
26. August 2021
Previous Discussion

- **Mandate to the WG →** possible reform of ISDS

- **34th session**
  - Inconsistent decisions on damages & compensation

- **37th session**
  - High amount of compensation undermining States’ ability to regulate

- **38th session**
  - **Request to Secretariat →** how could possible work on damages & compensation be undertaken?

- **States**
  - Inconsistency and unpredictability of awards on damages

- **Secretariat**
  - **Initial draft Assessment of damages and compensation**
General Considerations

• Outline of the key issues relevant to the question of assessment of damages & compensation

• [Mandate?]

• Questions for the WG to consider:

→ Could these issues be addressed by developing:

  i. relevant provisions, possibly with a binding effect, on procedural rules related to the damages & compensation to be included in investment treaties, arbitration rules or a multilateral instrument

  ii. guidelines and standards on legal framework for damages & compensation and the application of calculation methods for arbitral tribunals
Complexity and uncertainty

• High degree of complexity and uncertainty of current practice

Development of treaty provisions, guidelines or standards, addressing the following issues:

1. Compensation standard
2. Valuation method
3. Valuation date
4. Potential limitations for compensation
5. Causation standards
6. Evidentiary requirements
7. Interest
8. Selection of experts and their ethical regime
## Compensation standard

### Substantive guarantees and standards in investment treaties:
- Protection against expropriation
- FET
- Non-discrimination

Claim for compensation by breach of these treaty obligations

<table>
<thead>
<tr>
<th>Lawful expropriation</th>
<th>Unlawful expropriation</th>
<th>Other breaches</th>
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<tbody>
<tr>
<td>• Investment treaties</td>
<td>• Differing opinions</td>
<td>• Chorzów decision and ILC Articles OR “full protection and security” standard</td>
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<td>• Compensation as a condition for lawful expropriation</td>
<td>• Full reparation standard</td>
<td>• Problematic cases</td>
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<td>• Fair market value (+) OR a different standard including contextual factors</td>
<td>• PCIJ Factory at Chorzów</td>
<td>• Recent investment treaties → provisions on damages aiming to potentially minimize damages</td>
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- Art 31 ILC Articles
- Full reparation standard
- No differentiation between direct and indirect expropriation
Valuation method and date

Valuation method

- Discretion of the tribunal

Backward-looking
- Asset based
  - Book value
  - Replacement value

Forward looking
- Historical
- Market based
- Income based
  - DCF
    - Adjusted present value
    - Capitalised cash flow

Relevant factors:
- Type of damage
- Type of business
- Past performance

Problems:
- Assumptions and variety of information
- Caution advised
- Difficult for non-operative assets
Limitations for Compensation

Different factors potentially limiting the amount of compensation:

- **State of Necessity**
  - Sole means of preserving an essential national/public interest

- **Contributory fault**
  - Claimant’s conduct contributed to the loss
  
  - **Claimant’s conduct**
    - Reflected in (customary) international law (ILC Articles, CISG, UNIDROIT Principles)
    - Recognized by various tribunals in their decisions
  
  - Violation of domestic law, business risk
  - Discretion of tribunal

- **Mitigation of loses**
  - Failure to take reasonable steps to reduce damage
  
  - Burden of proof on respondent
  - Duty of best efforts, reasonable and prudent steps
Causation standards

Appropriate standards or tests for proving causation are generally not included in the investment treaties

Art 31 ILC commentary

• The loss claimed must not be too:
  – speculative
  – remote
  – Uncertain

• Not necessarily the same in every breach of an international obligation
Evidence

- Burden of proof is governed by the generally accepted principle of international law;
- Standard of proof is rarely addressed in investment treaties and decisions

**Burden of proof**

- **Investor**
  - Causality
  - Amount of loss

- **Government**
  - Circumstances limiting causality or the amount of loss

**Standard of proof**

- Wide discretion of tribunal
- Art 36 (2) ILC Articles
- Common law ↔ civil law systems
  - Balance of probabilities
  - Inner conviction of adjudicator
- In practice → **variety of different standards of proof**
Interest

- Not all elements necessary for calculation of interest are regulated in the treaties

• different options
• potentially higher rates
• permissible?
• different approaches
Experts

There is a wide divergence of compensation presented by claimants’ and respondents’ experts

Role of experts

• Party- or tribunal-appointed
• Content of the expert report
• Statement of independence
• Possibility of a joint report of party-appointed experts

Development of treaty provisions or guidelines, for:

→ Setting up a generalized system of expert(s) appointed by the tribunal to assist decision-making process and replace party-appointed quantum experts

→ Improving the current system of party-appointed experts:
  • Harmonized methodology
  • Alternative calculations in case of disagreement
  • Joint statements in case of divergences
  • Teaming up of the party-appointed experts
High compensation and discrepancies

1. High and increasing amounts of compensation claimed by investors
2. Significant divergence between the amount of compensation claimed and the amount of compensation awarded
3. Wide divergence of compensation presented by claimants’ and respondents’ experts → already discussed

1. Development of treaty provisions or guidelines for ISDS tribunals on:
   → Use of valuation methods and calculation of interest
   → Capping of compensation for instance to the amount actually invested by the investor
   → Consideration of contextual factors

2. Addressing manifest over- or under-statements through guidance:
   → Guidelines on cost allocation
   → Draft provision on cost allocation
Links to other reform options

- Questions related to damages and compensations that arise in the context of other ISDS reform options

  ➔ Mechanisms to address frivolous claims at an early stage of the proceedings and in an expedited process

  ➔ Regulation of third-party funding

  ➔ Reform of appellate and multilateral court mechanism

  ➔ Treaty parties’ involvement in, and control mechanisms, on treaty interpretation

  ➔ Multiple proceedings, shareholder claims and reflective loss
Thank you for your attention!