Chapter 4

Straddling the Divide Between Lawful and Unlawful Expropriation in International Law

Christer Söderlund

§4.01 INTRODUCTION

A basic tenet of customary international law is that the taking of privately-held property is a legitimate exercise of state power, provided specific criteria as to public purpose, non-discrimination, due process and compensation are met. In other words, an act of expropriation which fulfils these criteria is lawful, and, as a consequence, does not engage the state's responsibility for what is termed as an internationally wrongful act. However, if one or more of these criteria is lacking, the taking will be unlawful. This will bring into cause the responsibility of the state which follows from the commission of an internationally wrongful act.

At the heart of actual adjudication of investment disputes based on allegations of unlawful expropriation is, without exception, the matter of absent compensation. At first glance, it may seem that the principles dealing with compensation to the investor who has suffered deprivation of its property are not affected by whether the expropriatory act is qualified as lawful or unlawful. However, in actual fact, there are significant distinctions both as regards the legal qualification to be undertaken and the methodology to be applied. These distinctions may bring about widely differing economic outcomes in a particular case (while they also – despite the application of quite distinct methodologies – may result in much the same economic outcome).

§4.02 EXPROPRIATORY ACTION BY SOVEREIGNS: A BRIEF BACKGROUND

The taking of private property of 'aliens' by sovereigns has taken on different guises throughout recent history. A hundred years ago, foreign investors experienced a total and irreparable deprivation in across-the-board nationalizations in the wake of revolutionary societal transformations (Russia, Mexico). Later on – in the period of decolonization post-WWII – such state measures usually consisted in the taking of foreign stakeholders' investments in the extraction of hydrocarbon and other mineral resources.[1]

Since late 1950, a considerable part of the expropriation debate was conducted within the UN in the context of 'permanent sovereignty over natural resources'. This led to some controversy starting in the second half of the sixties, leading to, *inter alia*, the 1973 UN General Assembly Resolution 71 and Article 2(2) of the 1974 Charter of Economic Rights and Duties of States (also a UN General Assembly Resolution). Essentially, these resolutions affirmed the right of states to determine the matter of compensation and the right of their national judiciaries to deal with these issues (and, *a fortiori*, strongly condemned the so-called gun-boat diplomacy of earlier times).

Even if these United Nations resolutions do not have force of law, they certainly created uncertainty as to the continued applicability of the legality requirements, in particular as regards the level of compensation. This, in turn, brought about the need (experienced by developed, capital-exporting countries) to explicitly deal with the legal requirements to be satisfied in order for an expropriation to be lawful in investment treaties. However, as a general proposition, it is fair to say that the language of BITs only articulate a codification of customary international law.

In recent decades, expropriatory action has taken on more insidious forms where, in essence, formal title to assets is retained by the investor but where – though legislative and regulatory action – the value of the investment is rendered nugatory (i.e., by the withdrawal of a manufacturing licence well before its expiry date). Such action is usually referred to as 'indirect expropriation' or as 'creeping' expropriation, where a series of successive legislative or regulatory acts, or gradual measures of physical dispossession, title to the invested assets eventually becomes economically meaningless.[2]

Generally speaking, outright expropriation rarely occurs nowadays. Cases in recent decades regularly involve what the investor sees as indirect expropriations but where the state party considers that the measures constitute the legitimate exercise of

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1. *BP Exploration Co. (Libya) Ltd. v. Libyan Arab Rep.*, 53 ILR 297, 337-340 (1973); *Texas Overseas Petroleum Co. (TOPCO) v. Libyan Arab Rep.*, 17 ILM 1 (1977); *The Libyan American Oil Company v. Libya* (1977) and *Kuwait v. American Independent Oil Company* (1982); *Libyan American Oil Co. (Liamco) v. Libya*, 20 ILM 1, 59, 61 (1981); *State of Kuwait v. American Independent Oil Co.*, 21 ILM 976, 1024 (1982).
2. Such composite state conduct is foreseen in Art. 15 of the ILC Articles: '15. Breach consisting of a composite act 1. The breach of an international obligation by a State through a series of actions or omissions defined in aggregate as wrongful occurs when the action or omission occurs which, taken with the other actions or omissions, is sufficient to constitute the wrongful act.'

legislative or regulatory authority. As a consequence, no compensation has been offered to the investor, resulting in a large number of investment disputes. Therefore, many investment disputes will unfold in the twilight zone between the state's legitimate regulatory action and unlawful takings.

However, recently and exceptionally, there has been a string of cases dealing, again, with old-style, full-scale expropriations following Russia's unlawful annexation of the Crimean peninsula in 2014. As a consequence, certain Ukrainian entities with establishments (also) in this territory have raised investment claims under the Ukraine-Russia BIT for the loss of assets in Crimea. Russia has chosen not to take part in these proceedings but has resisted jurisdiction on the basis that the relevant BIT covers only investments after 2014 (when the investments attained a 'cross-border' character). As far as I know, in all cases,[3] the tribunals have found in favour of jurisdiction and setting aside actions (in Geneva and Paris) have so far been unsuccessful.

These cases offer certain points of interest as they call for the application of the investment treaty in circumstances which were certainly not anticipated by the drafters and for which it was not designed: The investments were domestic (Ukrainian) investments when made but under Russian de facto control by force of a land grab in breach of international law[4] and not susceptible of recognition by the international community.

§4.03 COMPENSATION UNDER CUSTOMARY INTERNATIONAL LAW

One may not say that the situation under customary international law is altogether settled and precise as to the criteria that render an expropriation lawful. While requirements as to public purpose, non-discrimination, due process and compensation are hardly controversial, different views have been expressed as to the standard of compensation and modalities of payment. While the leading *Factory at Chorzow* case (which concerned an unlawful expropriation) expressed, in passing, that compensation in cases of lawful expropriation should be limited to 'the value of the company at the time of dispossession, plus interest to the date of payment', voices have been heard in favour of a lower standard of compensation,[5] or even, in the context of large scale nationalizations, no compensation at all (invoking the national treatment standard).

There is no reason to believe that the situation under customary international law will be much clarified in the future. This is for the reason that the adjudication of standards and methodologies for determining compensation and other criteria will not

3. *Aeroport Belbek LLC and Mr. Igor Valerievich Kolomoisky v. Russia*; *PJSC CB PrivatBank and Finance Company Finilon LLC v. Russia*; *PJSC Ukrnafta v. Russia*; *Stabil LLC et al. v. Russia*; *Everest Estate LLC et al. v. Russia*; *Lugzor LLC et al. v. Russia*; *PJSC Oschadbank v. Russia*; *NJSC Naftogaz of Ukraine et al. v. Russia*; *PJSC DTEK Krymenergo v. Russia*.
4. A peremptory norm of international law, codified in Art. 2(4) of the UN Charter: 'All Members shall refrain in their international relations from the threat or use of force against the territorial integrity or political independence of any state […].'
5. *See*, for instance, M. Sornarajah, The International Law on Foreign Investment (2nd ed., CUP 2008) at 149 'Within the context of the rules on expropriation, the issue whether full compensation represents international law has remained a contested proposition.'

proceed on the basis of customary international law but will be premised on specific treaty language on what constitutes a lawful expropriation in any particular case. An investment tribunal acting under a particular treaty will not – in the absence of a specific mandate – be competent to determine the modalities of a *lawful* expropriation; the language in the treaty on what constitutes a lawful expropriation will only serve the purpose of providing a benchmark for deciding whether a certain impugned state measure in a particular case constitutes an *unlawful* expropriation or not.

§4.04 THE MANNER IN WHICH INVESTMENT TREATIES DEAL WITH EXPROPRIATION

Paradoxically, investment protection treaties do include, without exception, more or less elaborate guidelines for the determination of the value of expropriated assets in cases of *lawful* expropriation. However, on the subject of unlawful expropriation, the treaties remain silent.

From this follows the odd consequence that investment tribunals are not provided with any guidance in the treaty text on how to deal with different questions which arise from a finding of an expropriatory measure's unlawfulness. The language which is provided on the subject of lawful expropriations in the treaty can be used only for purposes of determining whether certain state conduct complained of in a particular case fits the bill for lawfulness or not. It *does not* provide guidance to determine compensation in case of unlawful expropriations. This gives rise to a series of quandaries as regards the standard of valuation, choice of valuation methodology, time of valuation and a host of related issues.

In view of the treaties' silence, these quandaries have to be resolved by seeking out principles of customary international law, which, in turn, raises issues where customary international law does not provide clear-cut answers. Examples of such questions are: what methodology shall be applied to satisfy the criterion of 'reparation' or 'fair market value'? Do criteria such as 'going concern', 'track record of profit generation', 'proven' or 'speculative' projections affect the choice of methodology? At what date shall the valuation take place? Is there a right of choice between different dates of valuation open to the investor? May parties refrain from asking for fulfilment of the primary remedy of restitution under international law? Can a hypothetical sale of the investment by the investor to a third party serve as a proper measure of 'reparation'? What about issues such as currency of compensation, principles and rates of interest accrual? May circumstances *post factum* occurring or coming to light after the event(s) of expropriation be taken into consideration?

This state of things may explain the diversity of approaches that tribunals have chosen when confronted with a kaleidoscope of issues unfolding in different sets of factual circumstances.

§4.05 LAWFUL EXPROPRIATION IN AN INVESTMENT TREATY CONTEXT

Investment tribunals need not take a position on the lawfulness of expropriations under customary international law. The reason for this is that the criteria for lawfulness are, unexceptionally, laid down in the investment treaty itself (which of course also is the instrument that vests the tribunal with jurisdiction). It is these criteria which have to be reviewed for purposes of determining the (un)lawfulness of the state measure (this is mostly a distinction without substance as investment treaties reflect what their drafters perceive as the position of customary international law).

It may be described as a remarkable fact that investment protection treaties do not deal with unlawful expropriation at all. Instead, such treaties, as stated above, unexceptionally include language that describes, in lesser or greater detail, what is required for an expropriation to be *lawful*.

An example of criteria for a lawful expropriation articulated in a treaty text may be taken from the Finland-Brazil BIT:

> **Article 5**
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> Expropriation (1) Investments of investors of each Contracting Party shall not be nationalized, expropriated or subjected to measures having a similar effect (hereinafter referred to as 'expropriation') in the territory of the other Contracting Party, unless the measures are taken in the public interest on a non-discriminatory basis, under due process of law and provided that provisions have been made for effective, prompt and adequate compensation. (2) Such compensation shall amount to the fair market value of the investment, immediately before the measures of expropriation or impending expropriation was taken or became public knowledge, whichever is earlier. The compensation shall be effected in a freely convertible currency and it shall also include interest at London Interbank Offered Rate (Libor) from the date of expropriation until the date of payment. (3) When a Contracting Party expropriates assets of a company or an enterprise in its territory, which is constituted under its laws, and in which investors of the other Contracting Party own shares, stocks or other interests or rights, the provisions of this Article shall apply to ensure prompt, adequate and effective compensation for those investors for any impairment or diminishment of the market value of such investment resulting from the expropriation.

So, the important conclusion to make is that the jurisdiction of an investment tribunal, acting under an investment treaty, does not extend to the adjudication of the economic consequences of a *lawful* expropriation. The description of what constitutes a lawful expropriation, found in any treaty, only serves the function as a point of reference for purposes of deciding whether certain state action constitutes a lawful or an unlawful expropriation.

§4.06 THE THRESHOLD ISSUE OF THE LAWFULNESS OF THE EXPROPRIATORY MEASURE

As a result of the treaties' structural approach to dealing with allegations concerning unlawful expropriations will limit the avenues open to the tribunal: The threshold issue with which a tribunal is faced is to determine if whatever conduct the state has conducted reaches the level of unlawfulness and, hence, engages the state's responsibility under international law. This enquiry may eventuate in a finding of lawfulness – according to the criteria laid down in the particular treaty – which puts an end to the enquiry or unlawfulness, in which case the enquiry has to be continued. Importantly, the treaty language does not mandate the tribunal to decide – in the place of the host state – what the fair market value (or any other substantive requirement) should be in order to render the expropriation lawful. If the tribunal does not agree with the host state's assertion regarding the impugned state measures' lawfulness, it may only conclude that the expropriatory act was unlawful and proceed accordingly.

§4.07 DOES ABSENT COMPENSATION RENDER THE EXPROPRIATION UNLAWFUL?

Expropriation cases are almost without exception brought to the attention of investment tribunals because state interference leading to impairment or extinction of the investor's business has not been assuaged by compensation, let alone an offer of payment. Not to put too fine a point on it, one may assume that the average investor is less concerned about formal defects in the expropriation process (such as public purpose or due process) as long as it considers itself adequately compensated.

A question that has arisen in adjudicatory practice is if the absence of 'prompt, effective and adequate compensation' (or whatever equivalent description is used in the particular treaty) still makes the expropriation (conditionally) lawful. One would think that the requirement laid down in the investment treaty compels the conclusion that this renders the expropriation unlawful. This has also been concluded in a line of cases.[6]

However, scholars have not seldom argued that expropriations only wanting compensation should still be considered legal. If an expropriation were to be considered illegal as soon as no compensation is granted, then the consequence, according to a prominent legal scholar, would be that in cases in which an expropriation meets all the conditions for a legal expropriation except for a determination of the tribunal that the host State had not paid market value for the property expropriated such an expropriation would have to be considered 'illegal' and compensation would therefore be awarded not on the basis of the valuation standard in the treaty but on the basis of the Chorzów Factory principle and customary international law. It is suggested that such a result would not accord with the intention of the Contracting Parties, as

6. *Wena v. Egypt*, para. 100; *Vivendi v. Argentina*; *Rumeli v. Kazakhstan*.

evidenced by the treaty text.[7] There are also exceptions to this clear reading of the treaty language applied by investment tribunals.

For instance, in the *Goetz* case, lack of payment did not render the expropriation unlawful.[8] This case concerned the revocation of a licence to process precious metals in a free trade area of Burundi. The treaty (Belgium-Burundi BIT) included a customary expropriation provision, stating, specifically, that compensation should reflect the market value of the assets (if the investor could not establish a higher value) and that payment was to be effected 'without delay' in transferable currency.[9] Although no payment was offered, let alone paid by Burundi (the revocation occurred on 29 May 1995, and the award (confirming a settlement between the Parties) was issued on 29 January 1999), the tribunal opined[10] that the matter of lawfulness remained suspended ('*reste en suspens*''] awaiting the state's decision to either effect payment or to reinstate the licence. One may well question this view, pragmatic as it may be, considering that payment had certainly not been made 'without delay' and that the unlawfulness was, therefore, already perfected.[11]

In *Tidewater*, which concerned revocation of rights to operate a deep-water oil exploration, the tribunal arrogated to itself the right to determine the value of the expropriated assets on the assumption that the expropriation was lawful despite the absence of compensation. It differed from other cases insofar as an offer had been made by the state to compensate the 'book value' of the operations which, in the claimant's view, did not represent 'adequate' compensation. The tribunal concluded that 'an expropriation wanting only a determination of compensation by an international tribunal is not to be treated as an illegal expropriation'.[12] The tribunal considered that such determination fell within its jurisdiction on the basis of Article 8 of the Barbados-Venezuela BIT.[13]

However, the requirements laid down in Article 5 of the BIT, among others that compensation shall amount to the 'market value of the investment' to be paid on a 'prompt, adequate and effective' basis, are objective criteria to be used by the tribunal for determining the(un)lawfulness – they are not matters for the tribunal to give substantive content (i.e., determine the scope of the state's primary obligations). This applies, *a fortiori*, in this case, as the dispute resolution provisions provide that '[t]he arbitral award shall be limited to determining whether there is a breach by the Contracting Party concerned of its obligations under this Agreement, whether such breach of obligations has caused damages to the national concerned, and if such is the case, the amount of compensation'.[14,15]

7. Jeswald W. Salacuse, The Law of Investment Treaties (Oxford University Press 2009), 328.
8. *Goetz et al. v. Burundi*, Case No. ARB/95/3, Award 10 February 1999 (the 'Goetz Award').
9. Belgium-Burundi Treaty, Art. 4(1)(c) and Art. 4(2).
10. The Goetz Award, para. 131.
11. As the Parties settled the case, one may also question why a pronouncement by the tribunal on the state action's (un)lawfulness was necessary in the first place.
12. *Tidewater et al. v. Venezuela*, Award, 13 March 2015, ICSID Case No. ARB/10/5, para. 140 (the 'Tidewater Award').
13. The Tidewater Award, para. 82.
14. Barbados-Venezuela BIT, Article 8(3).

As another example may be quoted he proposition advanced by the tribunal in the Venezuela Holdings case:[16]

> 301. It is not disputed that the Claimants did not receive compensation and that Venezuela did not fulfil its obligation to pay compensation in accordance with Article 6(c) of the BIT. However, the mere fact that an investor has not received compensation does not in itself render an expropriation unlawful.

According to the applicable treaty (the Netherlands-Venezuela BIT), Art 6 (c), payment was to be effected 'without delay'.

The above findings of absent payment not rendering an expropriation unlawful may be contrasted with the *Crystallex v. Venezuela* Award:[17]

> 716. Finally, pursuant to Article VII(1) of the Treaty, expropriation must be accompanied by 'prompt, adequate and effective compensation'. It is undisputed that no such compensation was either paid or offered to Crystallex. When a treaty cumulatively requires several conditions for a lawful expropriation, arbitral tribunals seem uniformly to hold that failure of any one of those conditions entails a breach of the expropriation provision.

Fortunately, the Crystallex award is only one of a long line of cases which have concluded – in line with the 'ordinary meaning'[18] of the treaty language – that the absence of compensation renders the expropriation unlawful.[19]

The question of whether, under customary international law, the absence of payment may not render an expropriation unlawful may be left to the side. A tribunal will have to seek guidance in the relevant treaty. If that treaty includes the customary

15. While treating the expropriation as a lawful one (e.g., the Award, para. 162) the tribunal proceeded to determine compensation on a DCF basis with an, in all likelihood, materially appropriate outcome.
16. *Venezuela Holdings v. Venezuela*, ICSID Case No. ARB/07/27, Award of 9 October 2014.
17. ICSID Case No. ARB(AF)/11/2.
18. Article 31(1) of the Vienna Convention on the Law of Treaties (VCLT).
19. *See*, *e.g.*, *Funnekotter et al. v. Zimbabwe*, ICSID Case No. ARB/05/6, Award, 22 April 2009, para. 98 ('The Tribunal observes that the conditions enumerated in Article 6 are cumulative. In other terms, if any of those conditions is violated, there is a breach of Article 6.'); *Saluka Investments BV v. Czech Republic*, PCA/UNCITRAL, Partial Award, 17 March 2006, para. 266 (noncompliance with one or more of the conditions set out in Article 5 of the treaty would lead to the conclusion that the respondent has breached Article 5 of the Treaty); *Kardassopoulos v. Georgia*, ICSID Case Nos ARB/05/18 and ARB/07/15, Award, 28 February 2010, para. 390 (noting that absence of due process is sufficient to support a finding that the expropriation was wrongful); *Compañía de Aguas del Aconquija SA and Vivendi Universal SA v. Argentina*, ICSID Case No. ARB/97/3, Award, 20 August 2007, para. 7.5.21 (lack of compensation makes an expropriation unlawful); *Siag and Vecchi v. Egypt*, ICSID Case No. ARB/05/15, Award, 11 May 2009, para. 428; *Unglaube v. Costa Rica*, ICSID Case Nos ARB/08/1 and ARB/09/20, Award, 16 May 2012, para. 305; *Gemplus and Talsud v. Mexico*, ICSID Case Nos ARB(AF)/04/3 and ARB (AF)/04/4, Award, 16 June 2010, para. 8-25 ('The Tribunal concludes that these expropriations were unlawful under the BITs and international law, given the facts found by the Tribunal and the further fact that the Respondent did not meet the condition required by Article 5 of both treaties regarding the payment of adequate compensation.').

'prompt, adequate and effective' (or equivalent) language[20] as regards compensation, the absence of payment will, without further, render the expropriation unlawful. One cannot, either, ignore the paramount importance of this requirement to the investor, who may be less concerned about the public purpose or due process requirements of any particular course of conduct pursued by the host state.

There are rare cases where the host state actually offered compensation[21] but where the payment was not made, for instance, because the investor did not accept the amount for not, in its estimation, adequately compensating its loss. One would consider that such a situation would constitute a breach as the ensuing situation is not one where 'prompt'[22] payment occurs.

However, it is reasonable to accept as best practice what has been summarized in the Goetz Award that, if all other conditions for a lawful taking have been met, the failure to pay prompt and adequate compensation does not suffice 'to taint this measure as illegal under international law'.[23] Ripinsky and Williams state that 'a good faith offering of, or provision for, compensation (even if not in a sufficient amount, as long as not manifestly unreasonable) should render the expropriation lawful'. Marboe concludes: 'While earlier the mere "promise" of a State to pay any sum at any time was not enough for the lawfulness of an expropriation, today there seems to be consensus that it is sufficient, if a State, at the time of the expropriation, offers compensation or provides for the determination of compensation ... .' One may, therefore, conclude that according to arbitral practice and scholarly writing, 'the mere existence of a dispute about the amount of compensation does not render the expropriation unlawful'.[24] Cf. the position where the State makes no offer of compensation at all[25] or offers an amount that is so negligible as not to be in made in good faith (as in *Rumeli v. Kazakhstan*: 'the valuation […] was manifestly and grossly inadequate', eventuating in a finding that the expropriation was unlawful.[26]

§4.08 THE CONSEQUENCES OF AN UNLAWFUL EXPROPRIATION UNDER INTERNATIONAL LAW

If an investment tribunal concludes that the host state's act amounts to an unlawful expropriation, it has to determine the legal consequences that this finding gives rise to.

20. This language is culled from a diplomatic note from US Secretary of State Cordell Hull to his Mexican counterpart Eduardo Hay in 1938 as a response to widespread expropriations carried out in the course of the Mexican land reform.
21. The Tidewater Award, para. 135.
22. '8. Compensation will be deemed to be "prompt" in normal circumstances if paid without delay. […]' (World Bank Guidelines).
23. The Goetz Award, para. 130 ('Le Tribunal ne considère toutefois pas que cette circonstance suffit à entacher d'illicéité internationale la mesure litigieuse.').
24. *Mondev v. USA*, para. 71.
25. *Wena v. Egypt*, para. 100; *Vivendi v. Argentina* (Resubmission).
26. *Rumeli et al. v. Kazakhstan*, ICID Case No. ARB/05/16, Award of 29 July 2008, para. 706; Salacuse, The Law of Investment Treaties (Oxford University Press 2009) 328; Thomas Wälde and Borzu Sabahi, 'Compensation, Damages and Valuation' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), The Oxford Handbook of International Investment Law (OUP, 2008), 1070.

As the treaties do not offer any guidance on this important question, the answer needs to be sought out on the basis of customary international law. In this regard, investment tribunals frequently rely on the *Factory at Chorzow* case,[27] which is universally held to articulate those principles in the constantly quoted declaration that 'reparation must, as 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'.[28] The principle thus enunciated is neither surprising nor controversial. The challenge consists in the application of this lofty principle to the facts of each particular case.

Just as frequently, reliance is placed on the provisions of the Responsibility of States for Internationally Wrongful Acts ('the ILC Articles') elaborated by the International Law Commission. The ILC Articles deal with so-called secondary rules on the international responsibility of states (i.e., not the substantive, 'primary', rules on what constitutes wrongful conduct, but what consequences the breach of such substantive rules will give rise to). These articles were adopted by the ILC in 2001 and, in that same year, 'commended […] to the attention of Governments without prejudice to the question of their future adoption or other appropriate action'[29] by the UN General Assembly.

For guidance, the ILC has also provided a commentary on the ILC Articles ('the ILC Commentary').

The ILC Articles do not have the force of law, and they are not binding on the states or other international actors by force of treaty or otherwise. However, they possess great authority in view of the eminent scholarly effort that has gone into their drafting.

Article 31 of the ILC Articles spells out the fundamental rule that '[t]he State is under an obligation to make full reparation for the injury caused by the internationally wrongful act'. Article 34 is captioned 'Forms of reparation' and deals with the ways in which 'full reparation' may be achieved; of importance, in an investor-state dispute settlement (ISDS) context is to note the fact that the primary remedy is *restitution*, i.e., an obligation to reinstate the situation that existed before the impugned act was committed (if materially possible and not out of all proportion, Article 35(a) and (b)).

In an investor-state context, the remedy of restitution is usually not a meaningful or even feasible remedy. It has also been stated on more than one occasion that

27. Chorzow is a city centrally located in Poland, today with a population of approximately 100,000. The Chorzow factory was established before World War I with German ownership. The factory produced fertilisers and explosives, commodities of strategic importance. According to the Geneva Convention the German ownership of the factory was to continue. However, in 1922, after an uprising in the eastern part of Silesia, Chorzow was ceded to Poland and the factory was taken over by the Polish state. The German Reich espoused the factory owners' claims and the parties submitted to the jurisdiction of the Permanent Court of International Justice (PCIJ), which resulted in the *Factory at Chorzow* case.
28. Case concerning the *Factory at Chorzow (Germany v. Poland)*, 1927 PCIJ, Series A, No. 9 (Jurisdiction); 1928 PCIJ, Series A, No. 17 (Merit) [hereinafter Chorzów Factory], Award, pp. 47-48.
29. General Assembly Resolution 56/83, para. 3; 12 December 2001.

ordering a state party to effect such specific performance might be an illicit encroachment on the state's sovereignty.[30] However, it is far from infrequent that investment treaties confer on the tribunal an express mandate to order specific performance.[31] Restitution has been pleaded (initially by the respondent) in the odd instance, e.g., *Funnekotter*, concerning farmers having been deprived of their farmlands in Zimbabwe.[32] Also, in a strikingly analogue case to *Funnekotter*, the claimants in the *Pezold* case requested restitution of farmlands, and the tribunal so ordered.[33]

If the remedy of restitution is not available, Article 36(1) of the ILC Article imposes the obligation 'to compensate for the damages caused thereby', an obligation which comprises (Article 36(2) 'any financially assessable damage'.[34]

In line with the above, the dichotomy of lawful and unlawful expropriation may be summarized as follows.

Lawful Expropriation	*Unlawful Expropriation*
The valuation takes place at the date of expropriation (or before the expropriation became public knowledge).	The valuation takes place at the date of the Award.
The valuation is objective (determining the fair market value), i.e., it does not consider the specific adverse consequences to the particular investor.	The valuation takes into consideration the circumstances of the particular investor.
The valuation only considers circumstances known at the time of the expropriation.	The valuation takes into consideration subsequent facts (and prior facts coming to light *post factum*.
Objective determination of fair market value	Actual loss to the particular investor (including incidental cost)

30. 'It is obvious that this Tribunal cannot substitute itself for the Indonesian Government, in order to cancel the revocation and restore the license: such actions are not even claimed, and it is more than doubtful that this kind of restitution could be ordered against a sovereign state.' Also, *LG&E Energy v. Argentina*, Award, para. 87 '[…] The judicial restitution in this case would imply modification of the current legal situation by annulling or enacting legislative or administrative measures that make over the effect of the legislation in breach. The Tribunal cannot compel Argentina to do so without a sentiment of undue reference with its sovereignty. […]'
31. For example, NAFTA, Art. 1135(1): '… the Tribunal may award, separately or in combination, only […]restitution of property, in which the award shall that the disputing Party may pay monetary damages and any applicable interest in lieu of restitution […]'
32. *Funnekotter et al. v. Zimbabwe*, ICSID Case No. ARB/05/6, para. 68.
33. *von Pezold et al. v. Zimbabwe*, ICSID Case No. ARB/10/15.
34. The ILC Articles, Art. 37, also include the remedy of 'satisfaction' which is a non-economic consequence that is not relevant in an investor-state context.

§4.09 THE LAWFUL/UNLAWFUL DICHOTOMY IN INVESTMENT ARBITRATION PRACTICE

In many cases – particularly in the early 2000s – it does not appear that the tribunals attributed any relevance to whether the expropriation was lawful or not as regards valuation methodologies or fixing a point in time for the valuation.[35] This can have many explanations, such that the parties were in agreement on how valuation was to be approached (e.g., fair market value at the time of expropriation) or that the tribunal just assumed that the treaty's provision on lawful expropriation also applied to unlawful acts.[36] In the *Crystallex* arbitration,[37] the parties agreed on the date of expropriation. This was also the case in the *Saint-Gobain v. Venezuela* case,[38] and, in many cases, these choices, in all likelihood, did not have appreciable economic consequences.[39]

There are also awards where it appears that the tribunals, in fact, noted the distinction between law and unlawful expropriation but did not let this categorization play into the valuation process.

Actually, the first case which very clearly opted in favour of selecting the date of the Award as the relevant date for assessing reparation following an unlawful expropriation was the *ADC* case.[40]

The *ADC investment* case concerned an airport outlet concession which was frustrated by state intervention. In ADC's view, this was a clear-cut case of unlawful expropriation. The tribunal agreed. It noted succinctly, that 'Since the BIT does not contain any *lex specialis* rules that govern the issue of the standard for assessing damages in the case of an unlawful expropriation, the Tribunal is required to apply the default standard contained in customary international law in the present case'.[41] As for the point in time at which damages should be determined, the tribunal made the pragmatic observation that previous tribunals had opted for the date of the expropriation because there had been a decline in the value of the investment after regulatory interference.[42] The *ADC* case, however, was described by the tribunal as almost unique 'since the value of the investment after the date of expropriation (1 January 2002) had

35. Metalclad, Award of 30 August 2000, para. 118; Wena Hotels, Award 8 December 2000, para. 118; Middle East Cement, Award 12 April 2000, paras 144, 146; Tecmed, Award 29 May 2003, paras 151, 187-188; Rumeli Telekom, Award 29 July 2008, para. 785; ASistem Muhendislik Insaat Sanayi ve Ticaret, Award 9 September 2009; Occidental Petroleum, Award 5 October 2012, para. 707; Abengoa y Cofides, Award 5 October 20213, para. 681; SAUR, Award 22 March 2014, para. 85; *Tenaris and Talta v. Venezuela*, Award 29 January 2016.
36. *Yukos Universal Ltd v. Russia*, PCA Case No. AA 227, Final Award 18 July 2014, para. 1571.
37. *Crystallex v. Venezuela*, Award 4 April 2016, para. 854.
38. Decision on Liability and the Principles of Quantum of 30 December 2016, paras 611-614.
39. However – occasionally – the choice of date as of the expropriation or as of the date of the award could have significant consequences: The *Yukos* tribunal noted [the Yukos Award, para. 1826,] that a valuation at the earlier date would yield approx. USD 22 billion while a valuation at the award date would represent slightly in excess of USD 66.5 billion.
40. *ADC v. Hungary*, ICSID Case No. ARB/03/16, Award of 2 October 2006 ('ADC Award').
41. ADC Award, para. 483.
42. *Ibid.*, para. 496.

risen very considerably ...'.[43] So, in this particular case, the tribunal concluded that '[h]owever, in the present, *sui generis*, type of case the application of *the Chorzow Factory* standard requires that the date of valuation should be the date of the Award and not the date of expropriation, since this is what is necessary to put the Claimants in the same position as if the expropriation had not been committed'.[44]

For purposes of a fair summary of the respective characteristics of the lawful/unlawful divide, the following quote may serve: 'This distinction also has crucial practical implications. Compensation is calculated by determining the "objective" fair market value of an investment at the time of expropriation [...] whereas damages are usually assessed by ascertaining the actual loss of the investor at the time of the decision, as laid down in the so-called Chorzow factory standard [...]'.[45]

There is definitely a trend in contemporary adjudicatory practice to use the date of the award as the appropriate point in time where the value of the expropriated assets shall be determined. This is also expressed in a number of cases,[46] and it is also taken for a given assumption in modern scholarly works.[47]

Using the date of the award and *post factum* data accumulated until that date for purposes of valuation has been criticized because it allows enterprise value to be determined by exogenous factors – e.g., market fluctuations – which bear no relation to the breach and by such circumstances that could not have been foreseen at the time of expropriation. The timing of the award and, hence, the valuation will be fortuitous, and the attribution of a value to the (hypothetical) business enterprise will constantly be in a flux of changing economic circumstances.

However, these empirically well-recognized considerations do not give cause for concern. Certainly, putting a value on a business enterprise which is a going concern will always be chasing a moving target. Its value will vary over time depending on a number of business-specific and macroeconomic factors. However, it is at the time of rendering the award that the damages to be compensated are quantified, reflecting – at least in theory – the possibility of seeking alternative investment opportunities under comparable market conditions.

As regards the matter of foreseeability, what was possible to foresee at the time of the breach is not a relevant circumstance when it comes to satisfying the requirement of full reparation for an unlawful expropriation.[48]

43. *Ibid.*
44. *Ibid.*, para. 497.
45. August Reinisch and Christoph Schreuer, International Protection of Investments (CUP 2020), para. 118.
46. In the *Quiborax* case it is explicitly stated by the [majority of] the tribunal that the valuation shall use data at the date of the award.
47. *See*, *e.g.*, Marboe, pp. 3.266 & seq.
48. *Amco Asia Corporation v. Republic of Indonesia*, ICSID Case No ARB/81/1 (Resubmitted Case), Award (31 May 1990); para. 186 'foreseeability [...] would anyway be an inappropriate test for damages that approximate to *restitutio in integrum*'.

§4.10 SELECTING THE DATE OF VALUATION

It is clear that in the event of a lawful expropriation, under customary international law, the determination of the fair market value shall be carried out as per the date of the expropriation (or, rather, immediately before the action was undertaken or when the intention to undertake the action became public knowledge). From this point in time, the investor is entitled to interest (only).[49]

However, this rule does not apply to any unlawful expropriation. In order to assess the adverse economic consequences suffered by the investor, it is necessary that the valuation is carried out in close proximity to the date of the award, irrespective of whether the value has risen or fallen after the expropriatory act. Normally – as in the *ADC* case – the impugned state measure will put paid to the enterprise for good, and any lingering effects of the expropriation will not be an issue. However, in case the enterprise somehow continues – e.g., because the regulatory intervention frustrates only one of multiple lines of operations of the investment – the valuation date still has to be the date of the award, but any adverse effect of the expropriation existing at the valuation date will have to be discounted. In such cases, the matter of causation attracts importance or, in the words of one tribunal, '… it is necessary to exclude the effects of actions taken by the nationalizing state in relation to the enterprise which actions may have depressed its value.'[50]

In earlier investment arbitration practice, tribunals have more or less programmatically (and consistently) declared that an unlawfully expropriated asset should (just as in the case of a lawful expropriation) be valued at the time of the expropriation and not, for example, at the date of the award.[51] This practice has in all likelihood been driven by the very pragmatic fact that the asset represented a higher value at the time of the expropriation as compared to later due to a degradation of to business environment as a consequence of the action. This quite arcane circumstance appears to have excluded consideration of any other date of valuation, such as the award date, in a number of cases. In other cases the parties have simply been in agreement that the date of breach be used, or, occasionally, that the tribunal mistakenly has assumed that the prescribed features of a lawful expropriation of the treaty also applies to an unlawful expropriation.

49. Once the indemnifiable amount has been fixed in judicial order, the investor's exposure to commercial risks will be excluded, leaving only the time element of any outstanding payment to be compensated.
50. *American International Group v. Iran* 4 Iran-US CTR (1983) 96, 107.
51. *See*, *e.g.*, *Sedco, Inc v. NIOC and Iran*, Interlocutory Award (27 March 1986) reprinted in 25 ILM 629 (1986); *Tippetts, Abbett, McCarthy, Stratton v. TAMS-AFFA Consulting* Engineers of Iran, Iran, and others, Award (29 June 1984) reprinted in 6 Iran-US CTR 219; *American International Group, Inc v. Iran*, Award (19 December 1983) reprinted in 4 Iran-USCTR 96; *Antoine Goetz et al. v. Burundi*, ICSID Case No ARB/95/3, Award (29 January 1999) paras 124, 135; *Wena Hotels Ltd v. Egypt*, ICSID Case No ARB/98/4, Award (8 December 2000) para. 118; *CME Czech Republic BV v. Czech Republic*, UNCITRAL, Partial Award (13 September 2001) para. 619; *Middle East Cement v. Egypt*, ICSID Case No. ARB/99/6, Award (12 April 2002) para. 107; *Tecmed v. United Mexican States*, ICSID Case No ARB(AF)/00/2, Award (29 May 2003) para. 187; *CMS Gas Transmission Company v. Argentina*, ICSID Case No. ARB/01/8, Award (12 May 2005) para. 410; *Azurix v. Argentina*, ICSID Case No. ARB/01/12, Award (14 July 2006) paras 420, 424.

There is definitely a trend in contemporary adjudicatory practice to use the date of the award as the appropriate point in time where the value of the expropriated assets shall be determined.

Using the date of the award and post-factum data accumulated until that date has occasionally been criticized because it allows enterprise value to be determined by exogenous factors which bear no relation to the breach and by such circumstances that could not have been foreseen at the time of expropriation.[52] The timing of the award and hence the valuation will be fortuitous and the attribution of a value to the (hypothetical) business enterprise will constantly be in a flux of changing economic circumstances.

However, these empirically well recognized considerations do not give cause for concern. Certainly, putting a value on a business enterprise which is a going concern will always be chasing a moving target. Its value will vary over time depending on a number of business-specific and macroeconomic factors. However, it is at the time of rendering the award that the damages to be compensated are quantified, reflecting – at least in theory – the possibility to seek alternative investment opportunities under comparable market conditions.

As regards the matter of foreseeability, it merits mentioning that what was possible to foresee at the time of the breach is not a relevant circumstance when it comes to satisfying the requirement of full reparation for an unlawful expropriation.[53]

§4.11 PRINCIPLES OF VALUATION AND METHODOLOGY

Obviously, there is no controversy as to the propriety of the principle of 'full reparation' as spelt out in the ILC Articles in cases where a state has incurred responsibility for an internationally wrongful act. However, the transformation of this principle in any given set of circumstances into hard and fast numbers is an entirely different matter.[54]

International law (whether customary or treaty-based) does not prescribe any particular methodology for purposes of determining the fair market value or the amount of compensation, respectively, to be paid for an expropriated asset. Methods that are used may be described as asset-based, income-based or market-based. Tribunals are at liberty to select the method they consider appropriate in the circumstances of the particular case.

As a general overview, a brief summary may be made.

Book value is, generally speaking, a very poor means of determining enterprise value as it represents an actuarial, historical accounting method. It starts with the acquisition value of an asset and reduces that amount by depreciation (as calculated

52. *See*, *e.g.*, Prof. Stern's strong dissent in the *Quiborax* case.
53. *Amco Asia Corporation v. Republic of Indonesia*, ICSID Case No. ARB/81/1 (Resubmitted Case), Award (31 May 1990); para. 186 'foreseeability […] would anyway be an inappropriate test for damages that approximate to *restitutio in integrum*'.
54. In any particular treaty context it may be argued that a lawful expropriation requires something less than 'full reparation', e.g., the Respondent's position in the Von Pezold case (Award, para. 753) that the tribunal should consider '[the Respondent's] ability to pay any compensation ordered', implying that any such amount should be 'just'.

over the asset's useful economic life or as allowed by accounting conventions). It says nothing about the investment's potential to generate future income.

Historic value differs from book value only in that the historic acquisition costs are restated with no allowance made for depreciation (whether to distribute the cost over the life-cycle of the asset or in order to adhere to accountancy dictates). Similarly to the book value, the historic cost is a poor indicator of the value of a going concern business enterprise. Still, in the absence of a track record of profitable operations, investment tribunals have occasionally resorted to this measure.

Book value and historic value are retrospective, while enterprise value necessarily has to be forward-looking.

Liquidation value relates to the value that the assets would represent in the context of an orderly liquidation of the enterprise. The liquidation value does indeed provide a definitely relevant measure in cases where the invested assets do not constitute a 'going concern' for purposes of valuation.

Replacement value represents the cost – at the time of expropriation – of acquiring the asset(s) of which the investor may have been deprived by expropriatory action. The method may yield a more adequate outcome for the investor than other base-asset approaches but shares the weaknesses of those alternatives as a poor measure of the investment's 'real' value based on its income-generating potential.

Stock market value, more properly defined as the market capitalization of a company, is hardly ever an available metric in expropriation cases as foreign investment regularly constitutes a subset of any listed company's operations, regularly also held by a wholly-owned SPV ('Special Purpose Vehicle') registered in the host state.

Peer valuation: Comparing the investment's income generation potential by comparing it to a number of 'peers' – i.e., what prices other, similar enterprises fetch in a market with buyers acting on a voluntary basis in like circumstances – is certainly an excellent method. The problem is, however, that it is usually impossible to find comparable 'peers' that may be used for purposes of such a valuation.

The DCF methodology estimates the future earning potential of an asset over a number of years and discounts the aggregate amount to its present value by a discount factor determined by the time value of money and business risk. The DCF methodology is by far the optimal methodology for valuation of a 'going concern'.[55] There are really no objections of principle that can be raised against it on a theoretical level, although, in its practical application, it can lead to significant under- or over-valuation depending on the degree of realism of the different factors that are put into the formula, not least the risk factor (of a multifarious nature) which affects the outcome of the calculation.

55. The World Bank Guidelines on the Treatment of Foreign Direct Investment define 'going concern' as 'an enterprise consisting of income-producing assets which has been in operation for a sufficient period of time to generate the data required for the calculation of future income and which could have been expected with reasonable certainty, if the taking had not occurred, to continue producing legitimate income over the course of its economic life in the general circumstances following the taking by the State'.

The DCF methodology has, at least initially, encountered notable headwinds in scholarly writings[56] as well as in case law.[57]

There can hardly be any doubt that the DCF methodology is the one that is most appropriate for calculating a fair market value of income-generating assets. Occasionally, the method has come under criticism, but this can hardly relate to the methodology as such but to its application. It cannot be denied that spreadsheets displaying DCF projections convey an alluring image of scientific exactitude that can be deceptive. However, these projections are not better than the assumptions that are fed into the formula (if a number of unrealistic assumptions are used, this even compounds the under- or overshoot of the result).

When weighing the pros and cons of different valuation methodologies, it is important to consider that in an increasingly technologically sophisticated and specialized business environment, the value of physical, balance sheet-eligible assets becomes increasingly decoupled from the wealth-creating potential of many types of business operations. To illustrate this phenomenon with a striking – but maybe not run-of-the-mill example – one may take the example of Microsoft Corporation which shows an asset value on its balance sheet of USD 365 billion but a market capitalization of almost USD 2 trillion (2023).

Sunk costs represent expenditure which has not been possible to recapture because the intended venture was stopped by governmental interference before it could be brought to fruition or because the venture in the end was simply not susceptible to profitable operation.

If no case can be made at all for future profitability – the project was, for instance, brought to a premature halt by illicit state intervention – it would appear appropriate to award sunk costs. Such an amount would certainly not represent a 'fair market value'

56. *See* ILC's Commentary in relation to Art. 36 of the ILC Articles: 'The discounted cash flow (DCF) method has gained some favour, especially in the context of calculations involving income over a limited duration, as in the case of wasting assets. Although developed as a tool for assessing commercial value, it can also be useful in the context of calculating value for compensation purposes. But difficulties can arise in the application of the DCF method to establish capital value in the compensation context. The method analyses a wide range of inherently speculative elements, some of which have a significant impact upon the outcome (e.g. discount rates, currency fluctuations, inflation figures, commodity prices, interest rates and other commercial risks). This has led tribunals to adopt a cautious approach to the use of the method. Hence, although income-based methods have been accepted in principle, there has been a decided preference for asset-based methods.'

57. *Metalclad Corporation v. United States of Mexico* (ICSID Case No. ARB(AF)/97/1), Award of 30 August 2000, at para. 118; *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt* (ICSID Case No. 84/3), Award of 20 May 1992; *Wena Hotels Ltd. v. Arab Republic of Egypt* (ICSID Case No. ARB/98/4), Award on Merits of 8 December 2000; *Marvin Roy Feldman Karpa v. United Mexican States* (ICSID Case No. ARB(AF)/99/1), Award of 16 December 2002, at para. 194; *Tecmed*, at para. 186; Rumeli, at para. 811; *Tidewater*, at paras 139, 144, 152-165 and 185. Also in the Iran-US Claims Tribunal practice a reserved posture has been adopted as regards the DCF method. *See*, *e.g.*, the following Iran-US Claims Tribunal awards: *Phillips Petroleum Co. v. Iran*, 21 Iran-US CTR 79 at para. 79, Partial Award No. 425-39-2, 29 June 1989; *American International Corp. v. Iran*, 4 Iran-US CTR 96 at 106, Award No. 93-2-3, 19 December 1983; *INA Corp. v. Iran*, 8 Iran-US CTR 373 at 380, Award No. 184-161-1, 13 August 1985; *James M. Saghi et al. v. Iran*, 29 Iran-US CTR 20 at para. 79, Award No. 544-298-2, 22 January 1993.

of the funds invested, but it would represent a measure of damages arguably indemnifiable under international law as it would, in some sense, represent 'reparation'. If, on the other hand, the business venture proved unprofitable for reasons unrelated to any inappropriate state intervention, the compensation that could be determined should be based on the value of the assets in the context of an orderly liquidation of the business venture.[58] In that context, 'sunk costs' are not relevant at all.

Loss of opportunity has been relied on by some tribunals where the investment was, as it were, nipped in the bud and effectively prevented by state interference from bringing its operations on stream (whether profitably or unprofitably) before accumulating a sufficient track record allowing any assumptions as to its income-generating potential.[59] This is really nothing else than a variant of the market value approach, recognizing that ventures based on such flimsy underpinnings are regularly traded by willing actors in the M&A markets.

'Lucrum cessans and damnum emergens'

The age-worn compensation measure based on *lucrum cessans* and *damnum ermergens* may safely be dismissed as unhelpful in a valuation context. It is, indeed, a quite primitive tool, built on a cash-based rather than accrual-based cash flow basis. It may at best be used (if at all) in a contract breach context in a civil law setting.

It is '… based on an anachronistic method of valuation, one that separated out *damnum emergens* and *lucrum cessans*, rather than modern financial terms. Chorzów Factory's valuation formulas reached their expiration date decades ago.'[60] It has also been described as 'economically anachronistic',[61] and discussion of the concept has recommended that 'the dichotomy of *damnum emergens* and *lucrum cessans* should be abandoned in this context'.[62]

§4.12 USING DATA OCCURRING OR COMING TO LIGHT AFTER THE EXPROPRIATORY EVENT?

When using the date of expropriation, tribunals have been faced with the query of whether they may assess data that have occurred or come to light after the event. It

58. This conclusion is also supported by the recommendations issued by the World Bank in its Guidelines on the Treatment of Foreign Direct Investment (Article 6): '(i) for a going concern with a proven record of profitability, on the basis of the discounted cash flow value; (ii) for an enterprise which, not being a proven going concern, demonstrates lack of profitability, on the basis of the liquidation value; (iii) […]'.
59. *See Sapphire International Petroleum v. National Iranian Oil Company*, 35 ILR 136 (1963); *Southern Pacific Properties (Middle East) v. Egypt* (ICSID Case No. ARB/84/3), Award of 20 May 1992; compare, in contract relations, Art. 7.4.3(2) of the Principles of International Commercial Contracts.
60. Steven E. Ratner, Compensation for Expropriations in World of Investment Treaties: Beyond the Lawful/Unlawful Distinction (2017), Law & Economics Working Papers 131, 9.
61. WQ Michael Reisman and Robert D. Sloane, Indirect Expropriation and Its Valuation in the BIT Generation (OUP 2004), 137.
62. Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (1st edn, OUP 2009).

would seem obvious that in order to arrive at the most appropriate level of 'reparation', all information available at the time of adjudication should be applied to the enquiry.

Reasons that have been given for disregarding *post factum* events are, essentially, that circumstances affecting valuation *post factum* may not have been foreseeable and that such circumstances are external to the breaching act as such. However, foreseeability is not a relevant factor affecting valuation in case of a breach. One may recall that the primary remedy under international law is restitution, and the obligation to restitute property is unaffected by what the parties may have foreseen. By the same token, the duty to pay damages remains unaffected by the foreseeability of further intervening events up to the date of the award.

However, this problem cannot arise on a proper approach to the quantification issue, putting that calculus at the time of the award. All information – irrespective of whether it pertains to events *ex ante* which have become known after the event or whether they concern subsequent, unforeseen events (they may relate to unexpected changes in the pricing of input factors, market conditions, technological development, competitive patterns, regulatory issues) – shall be used in order to arrive at the amount required to effect reparation. It is important to underscore in this regard that the expectations of the parties to the arbitration at the time of the expropriatory event are irrelevant for quantification purposes. For the same reason, one cannot attach relevance to what a willing seller and a willing buyer, acting under no compunction at the time of the expropriatory act, would accept as the fair market value of the investment as those (hypothetical) parties will not be in possession of possibly relevant *post factum* data.

Fixation of the amount of damages in as close proximity as possible to the point in time at which the amount is quantified and susceptible of enforcement must in all instances optimally fulfil the function of 'full reparation' to which the aggrieved investor is entitled.

§4.13 WHAT IF THE INVESTMENT REPRESENTS A LOWER VALUE AT THE TIME OF THE AWARD: DOES THE INVESTOR GET TO CHOOSE?

It has happened in a number of investment cases that a valuation of a business enterprise at the date of the award yields a lower monetary amount than one undertaken at the date of the breach (even disregarding any adverse economic effects inflicted on any remaining part of the business after the expropriation by the unlawful state conduct). Should this circumstance call for a departure from the principle of valuation as per the award date? In other words, should such a situation give rise to an entitlement on the part of the investor to choose the most favourable outcome (in these cases, by opting for the date of breach)?

An intuitive response to this question is that such a choice cannot reasonably be on offer. Damages following an international breach have to be quantified in terms of one monetary amount and cannot very well be represented by two different amounts. Still, in those investment cases where enterprise value has declined at the time of the award, the investor has invariably been given the right to choose the higher value that applied at the time of the expropriation.[63] Remarkably, this position has been taken for granted, and no *ratio decidiendi* has been ventured in these cases. A typical reference will read: 'The Tribunal also holds that, in the case of an unlawful expropriation, as in the present case, Claimants are entitled to select either the date of the expropriation or the date of the award as the date of valuation'.[64]

How can that be? It has been argued, for instance, that expropriation is a special case because, here, the investor would have been entitled to compensation in all circumstances (i.e., also in the event of a lawful expropriation). 'This part of the damage is, therefore, not causally linked to the valuation'.[65] But one cannot look at it in that way: in the context of a damage calculation, *all funds* awarded in a case of unlawful expropriation derive from its illegality; there are no 'spill-over' effects from the contrafactual lawful measure which is based on a different methodology.

An argument has also been raised that choice should be motivated by an interest to discourage states from engaging in overbearing conduct.[66] This is not a valid motive. While investment cases claiming damages for unlawful acts hopefully have a sobering effect on the state's conduct of its affairs, this cannot be accepted, under international law or otherwise, as a valid justification for offering the investor more than what represents reparation at the time of the award. Even if, in a given instance, this would represent a lower amount than what follows from the fair market value at the time of expropriation, it will surely be sufficient to act as a deterrent against untoward actions. And, in any event, investment tribunals are not tasked with meting out retribution in instances of untoward state conduct.

There exists no logical justification to allow the investor (or the state, for that matter) to choose between the most favourable valuation that can be achieved at the time of expropriation and the time of the award, respectively. This may produce a result where the investor is afforded damages in an amount which is less than what has followed from a lawful expropriation. However, there is nothing remarkable in that; as the methodologies to apply in respect of lawful and unlawful expropriations are quite distinct, there is nothing remarkable that they may yield different outcomes.

One can understand the spontaneous sentiment expressed in doctrine and in many investment cases that a state having attracted responsibility for an unlawful act

63. *ADC v. Hungary*, ICISD Case No. ARB/03/16, Award of 2 October 2006; *Kardassopopulos v. Georgia*, ICSID Case No. ARB/05/18, Award of 3 March 2010; *Hulley Enterprises et al v. Russia*, PCA Cases Nos 227 and 228, Award of 18 July 2014; *Unglaube v. Costa Rica*, ICSID Cases Nos ARB/08/01 and ARB/09/20, Award of 16 May 2012; *ConocoPhillips et al. v. Venezuela*, ICSID Case No. ARB/07/30, Decision on Jurisdiction and Merits (3 September 2013) and Award (8 March 2019); *Hulley* (n. 34); *Yukos* (n. 34) *v. Russia*; *Veteran Petroleum* (n. 34); *Gold Reserve v. Venezuela*, ICSID Case No. ARB(AF)/09/1, Award (22 September 2014*); Pezold and others v. Zimbabwe*, ICSID Case No. ARB/10/15, Award (28 July 2015); *Teinver et al. v. Argentina*, ICSID Case No. ARB/09/1, Award (21 July 2017); *OperaFund v. Spain* (n. 8).
64. Yukos Award, para. 1763.
65. I. Marboe, 3.332.
66. *See*, *e.g.*, Conoco award, para. 242, end: 'However, a damages award that returns the plaintiff to its economic position at the date of the injury, but leaves the defendant with a gain as a result of his action may not be appropriate and not deter future unlawful acts'.

should not be able to escape the consequences at a lower price than what would follow from a lawful act. This reaction certainly is understandable but defies logic: the approaches in the two instances are different and may certainly yield these results on a proper application. There is also a forbidding element in the proposition that the investor may pick the best outcome: The purpose is to offer reparation for a certain wrongful act, and such an amount (whether considered right or wrong) is the one that, by definition, reflects the damages sustained. It is mildly surprising that the investor's entitlement to choice has not met with some pushback in more recent case law and writings.[67]

§4.14 DIVESTITURE OF THE INVESTMENT AS A RELEVANT PARAMETER?

A reason put forward by some tribunals for a higher valuation than would otherwise follow is that the investor could have divested itself of the enterprise at some earlier time and, if so, secured a higher amount of reparation than at the time of the award. The *Yukos* tribunal – as an argument why any depreciation of the value cannot be at the expense of the investor – explained that '[…] in the absence of the expropriation the investor could have sold the asset at an earlier date at its previous higher value. […]'.[68] Generally speaking, there can be no presumption in favour of the hypothesis that an investor entertains such plans – the traditional role of the investment is to secure future income for the long haul. In order for the investor to vindicate the higher value that a hypothetical divestiture of the investment would bring, it would require compelling evidence that such a sale was consummated by the investor or at least imminent in the particular instance.

The *Unglaube* case is also interesting in that the tribunal assumed that the investor would have sold the investment just prior to the peak in real estate prices in the intervening period.[69] No allegation that the investor actually had intended to sell the investment was on the record, however.

§4.15 A MANDATE TO DETERMINE FAIR MARKET VALUE

The *Santa Elena* is sometimes quoted as the authority for the proposition that the absence of payment does not render an expropriation unlawful.[70] However, it is important to note that this arbitration was *not* based on an investment treaty but on an *ad hoc* agreement to submit to arbitration prompted by the US Helms Amendment and

67. However, a poignant critique of what has been termed as the 'Asymmetrical Approach' may be found in a recent paper by Pacôme Ziegler and Cristian Gallorini, The Case for the Ex-post Valuation of Damages under International Investment Law, Journal of Investment & Trade 24 (2023), 115-265.
68. Yukos Award, para. 1768.
69. *Unglaube et al. v. Costa Rica* (ICSID Cases Nos ARB/08/1 and ARB/09/20), Award 16 May 2012, para. 318.
70. The Tidewater Award, para. 135.

that the parties did not argue in terms of lawful/unlawful expropriation; they simply wanted to have the matter of compensation finally settled. Additionally, the Parties were in agreement that 'international law' was to apply and that the investor was entitled to 'the fair market value' of the property. The only bone of contention was the valuation date, whether at the time of the expropriation (1978) or the then 'current value' (1998).

In the *Santa Elena* case, compensation had not been paid, although many years had elapsed since the expropriation.

The *Santa Elena* case concerned an investor who acquired a property in Costa Rica with a view of developing it into a tourist resort. This happened back in 1970. In 1978, Costa Rica issued an expropriation decree in respect of the property in order to create a natural preserve in view of the region's 'dazzling variety of flora and fauna'.[71] At the time, Costa Rica offered to pay the equivalent of USD 1.9 million for the property. The offer was turned down by the investor who believed that USD 6.4 million would come closer to the truth. Thereafter, a period of twenty years ensued, during which the compensation issue remained unsettled. Finally, the US prevailed upon Costa Rica to submit the compensation issue to international arbitration before an ICSID tribunal. This was in 1995. In the arbitration, the investor upped the ante and asked for USD 41.2 million.[72]

In the event, the tribunal settled for a valuation as per the time of expropriation and identified, on this basis, an amount of USD 4.15 million. Adding to this amount (compound) interest accruing up to the date of the award, the tribunal awarded a flat amount of USD 16 million in all. This is, then, a strict application of the *Factory at Chorzow* rule of FMV at the date of the taking plus interest from that date and Article 38(1) of the ILC Articles (which, of course, deals with reparation).

In this context – i.e., when an investment tribunal is mandated to determine the fair market value of a lawful expropriation – it is worth mentioning that there are still in existence some investment treaties (essentially with China and former Soviet Union republics) which leave it to international arbitration to determine 'the amount and modalities of payment' only once a domestic court in the host state has determined that an expropriation has taken place. The value of such a treaty will be illusory to the investor – a domestic court of, e.g., a former Soviet Union republic would hardly declare that foreign-held assets (even if such were in existence) had been subject to expropriation.[73]

71. Santa Elena Award, para. 15.
72. *Ibid.*, para. 29.
73. *See*, on this topic, August Reinisch, How Narrow Are Narrow Dispute Settlement Clauses in Investment Treaties?, Journal of International Dispute Settlement 2(1) (2011), 115-174, which raises the issue 'whether it is the proper role of investment tribunals to correct the meaning of dispute clauses they qualify as use- or senseless or whether such remedial action should remain reserved to the State Parties' (p. 174).

While a majority of tribunals have recognized this limitation as regards the scope of jurisdiction,[74] a few tribunals have arrogated to themselves, nonetheless, the authority to decide whether there has been an expropriation or not.[75]

§4.16 DEPARTING FROM THE PRINCIPLE OF FULL COMPENSATION?

During the gestation process leading up to the ILC Articles, extensive discussions were conducted on whether there should be a departure from the principle of full compensation in cases of, as it was called, 'crippling compensations'. Such an accommodation did not follow from any elevated principle of sovereignty as much as making a virtue out of necessity; states simply not being able to suffer the harrowing consequences of indemnifying a larger investor collective in the context of any all-out nationalization.

Although strong sympathy was expressed for such a possibility in many quarters, in the end, it was not reflected in the ILC Articles. The ILC Articles being declaratory of the status of international law, one can, therefore, say that 'full compensation' is the invariable compensation standard in cases of lawful expropriation under international customary law.[76]

In any event, if a tribunal has to decide on the lawfulness of an expropriation, it does not have to consider this issue: If the treaty requires 'full compensation', this will constitute the relevant criterion in terms of compensation for a lawful expropriation irrespective of any view on this matter in customary international law.

§4.17 CAUSATION

Normally, the matter of causation is not an issue in expropriation cases. The expropriation has caused the demise of the business, full stop, and no further enquiry as to causation is required. However, in other cases, such an enquiry is necessary, e.g., when overbearing regulatory activity has only partially stymied the operations of the business entity. This raises the spectre of cause and effect. It is uncontroversial that not all effects of a breach – however accidental and fortuitous – shall be compensated, but only such having an adequate 'nexus' to the expropriatory act. The question is only by what means investment tribunals shall fix those limits of causal events. Tribunals have struggled with this nexus between the act and the effect by resorting to terms of

74. *Vladimir and Moise Berschader v. The Russian Federation*, SCC Case No. 080/2004, Award 21 April 2006; *RosInvestCo UK Ltd. v. The Russian Federation*, Award on Jurisdiction 2007, SCC Case No. Arb V079/2005 'does not include jurisdiction over the questions whether an expropriation occurred and was legal'. 21 (para. 114); *Austrian Airlines AG v. The Slovak Republic*, UNCITRAL Final Award, 9 October 2009.
75. *European Media Ventures SA v. Czech Republic*, Judgment of the High Court of England and Wales, 5 December 2007, (2007) EWHC 2851 (Comm); *Renta 4 S.V.S.A et al. v. Russian Federation*, Award on Preliminary Objections, 20 March 2009, SCC No. 24/2007.
76. *See*, on this topic, Martins Paparinskis, Crippling Compensation in the International Law Commission and Investor-State Arbitration (ICSID Review, 37(1-2) (2022), 289-312.

'foreseeability', 'proximate cause', 'sufficient causal link', 'too remote', 'a natural consequence' and similar.[77]

These terms are in all likelihood useful tools to arrive at a satisfactory limitation of effect that may have followed a certain breach in any specific case. There is also a theory of 'adequate causation' which may give rise to liability in cases of remoteness or absent foreseeability (only requiring that a typical consequence of the conduct that can be established with the help of all relevant expertise that can be mustered).[78] However, in the context of an unlawful expropriation, one must exclude from the range of limiting factors what the parties reasonably may (or may not) have foreseen at the time of expropriation. Even if the effect was not foreseeable, it is indemnifiable if it was adequately caused by the expropriatory act.[79]

On the subject of causation, it may be mentioned that it has been argued[80] that a more nuanced approach should be adopted by analysing the economic implications of any specific breach of the prerequisites for a lawful expropriation in the particular case. That is, if an expropriation was unlawful because of the absence of a public purpose, due process and compensation, the economic consequences should be different from a situation where unlawfulness follows from, e.g., absent compensation only: in the former case, the investor would be entitled to *restititio in integrum* (because the expropriation was not supposed to happen at all), while in the latter (where a right to expropriate was present) only the adverse consequences of absent payment would be subject to damage assessment.

Despite the seeming attractiveness of this proposition, it is not likely that it can be argued from the way in which treaties are currently structured. Having regard to the way in which the conditionalities of a lawful expropriation are structured, the absence of any single criterion renders the act unlawful – and this mere fact removes the state's act from the realm of lawfulness into a situation where the interest of full reparation has to be satisfied. A different order could certainly be envisaged where the investment treaty would provide for a mandate to tribunals to determine fair market value without prejudice to the act's lawfulness, but such a solution is not on offer in current treaty practice.

77. For an illustrative discussion of the topic of causation in the ISDS context, *see SD Myers v. Canada*, Second Partial Award of 21 October 2001 (a NAFTA arbitration under the UNCITRAL Rules), paras 140-160.
78. David Khachvani, Compensation for Unlawful Expropriation: Targeting the Illegality, ICSID Review, 32(2) (2017), 385-403 (394 & seq.).
79. *See*, *e.g.*, the S D Myers Award, para. 159.
80. Pacôme Ziegler and Cristian Gallorini, The Case for the Ex-post Valuation of Damages Under International Law, Journal of Investment & Trade 24 (2023) 115-165 DOI: 10.1163/22119000-12340286.