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We are delighted to present the latest edition of *Quantum Quarterly*, in which we provide extensive case notes on damages awards that were rendered or became public since our last edition. These awards range from a few million to several hundred million U.S. dollars, and they include one case where an investor-state tribunal notably bucked the recent widespread trend of awarding compound interest. We hope you enjoy this edition.
All the best.

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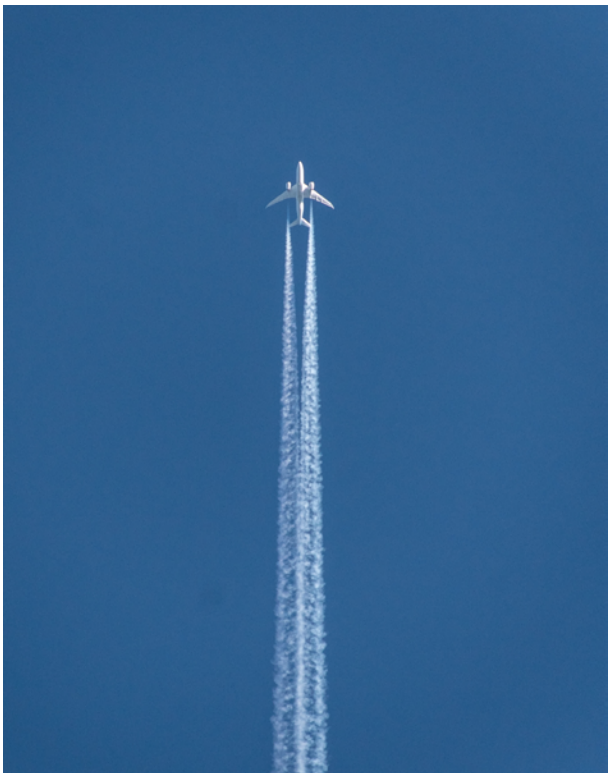


Date of the Award
September 13, 2021

The Parties
Air Canada Inc. (Claimant); Bolivarian Republic of Venezuela (Respondent)

Sector
Aviation

Applicable Treaty
Agreement between the Government of Canada and the Government of the Republic of Venezuela for the Promotion and Protection of Investments, signed in Caracas on July 1, 1996 (the bilateral investment treaty (BIT))

Members of the Tribunal
Pierre D. Tercier (president), Charles H. Poncet (Claimant's appointee) and Deva G. Villanúa (Respondent's appointee)

Background

The dispute concerned the ability of an investor to freely exchange and repatriate funds arising from its foreign investments in Venezuela. Claimant argued that it was forced to suspend its flights between Toronto and Caracas due to the unrest and challenges of conducting business in Venezuela, including its difficulties repatriating its funds from Venezuela. Specifically, the commission in charge of administering the legal exchange of currency in Venezuela failed to process Air Canada's 15 pending applications for a currency exchange to convert its bolivar-denominated returns into U.S. dollars. Claimant submitted that Respondent violated the BIT due to its failure to approve these requests, alleging breaches of protections relating to the free transfer of funds (FTF) (Article VIII of the BIT), the fair and equitable treatment (FET) standard (Article II of the BIT), and expropriation (Article VII of the BIT). Respondent denied there were any illegal restrictions on the transfer of funds. It also submitted that it treated Claimant at all times in a fair and equitable manner and that there was no expropriation.

Jurisdiction and Liability

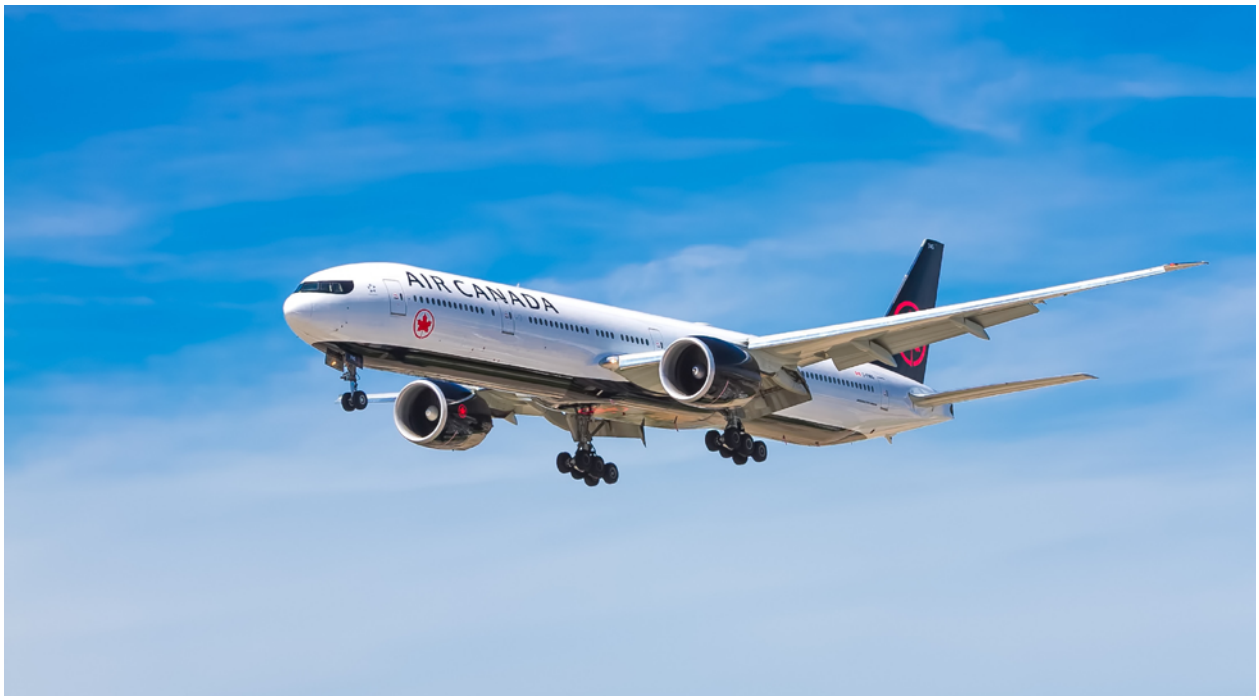
The Tribunal dismissed Respondent's jurisdiction *ratione materiae* and *ratione personae* objections. Respondent had argued that Claimant failed to establish the existence of an "asset" that constituted an "investment" under the terms of the BIT and the *Salini* test and that Claimant had failed to show how it owned or controlled the alleged investment in compliance with the laws of Venezuela. The Tribunal found that Claimant had demonstrated that it had assets within the meaning of Article I(f) of the BIT and that such assets constituted an "investment in the legal sense."[1] Claimant's capital contributions generated rights of value related to the Toronto-Caracas-Toronto route, in particular through ticket sales.[2] The fact that Respondent formally authorized the operation of Air Canada in Venezuela and certified Air Canada's status as a foreign company in Venezuela further confirmed the legality of its investment at its "inception."[3] The Tribunal found that Respondent's *ratione personae* objection equally failed under Article I(g) of the BIT since it was undisputed that Claimant was a company incorporated under the laws of Canada, which did not have Venezuelan citizenship, and the requirement of having made a protected investment in the territory of Venezuela had been established.[4]

With regard to liability, the Tribunal found two breaches of the BIT. First, the Tribunal found that Respondent violated the FTF provision found in Article VIII of the BIT. Respondent's inactions in relation to Claimant's pending requests for currency exchange deprived Claimant of the right to freely transfer its funds. Respondent's failures to act were similarly unjustified. Second, Respondent breached the FET obligation in Article II(1) of the BIT. The Tribunal considered the following three elements under this claim: (i) Claimant's legitimate expectations, (ii) Respondent's transparency and (iii) arbitrariness, inconsistency or discrimination by Respondent.[5] Here, the Tribunal determined that there existed a breach of Respondent's obligation to treat Claimant in a fair and equitable manner because Claimant's legitimate expectations were violated and because Respondent failed to treat Claimant in a transparent and nondiscriminatory manner.[6] The Tribunal held there was no evidence of direct or indirect expropriation under Article VII of the BIT.[7]

Quantum

Having found Respondent in violation of the BIT, the Tribunal proceeded to determine the damages arising from these breaches. The Tribunal set out four overarching principles to determine whether Claimant was entitled to its claimed losses:

- First, it determined that the principle of "full reparation," developed in the Permanent Court of International Justice judgment in *Chorzów Factory* and codified in the ILC draft articles, applied.
- Second, it agreed with Respondent that Claimant held the burden of proving "actual and concrete loss" as a result of Respondent's violation of Article VIII and Article II(2) of the BIT.[8]
- Third, the Tribunal found that there needed to be a "sufficient causal link between the breach and the damage caused," since causation is "not only a prerequisite for the claim for damages but also has an impact on the amount or scope of the damages to be compensated."[9] In this regard, the Tribunal explained that proof of "partial causation" only would result in a "substantial reduction" in damages.[10]



- Fourth, the Tribunal explained that the right to damages could be affected (i) "[w]hen there is a duty to mitigate damages on the part of the non-breaching party, and that party has failed to do so" and (ii) "[w]here the non-breaching party is at fault in some way and that fault contributes to the loss suffered, known as 'contributory fault.'"[11]

Applying these principles, the Tribunal considered the question of entitlement to damages based on whether Claimant suffered loss as a result of Respondent's BIT violations, and then it proceeded to the question of quantification of such losses.

A. Entitlement to Damages

Claimant sought damages for Respondent's breach of any and all of the provisions of the BIT. Specifically, Claimant requested the amount in U.S. dollars that it was unable to repatriate in respect of the 15 pending currency exchange requests it submitted to the government entity authorized to administer the legal exchange of currency in Venezuela, which were never processed. Respondent objected, arguing that Claimant failed to prove its alleged damages in a concrete and precise manner, and because it had failed to establish the required causal link between the alleged act/omission and the damages.

The Tribunal found a "sufficient nexus" existed between Respondent's actions and the harm suffered by Claimant, which it found existed whether assessed under the FTF violation or the FET violation.[12] It averred that there was no reason why Claimant's pending currency exchange requests would not have been approved, since they were properly submitted by Claimant in accordance with the applicable procedure and no deficiencies existed in Claimant's applications.[13] It also found that but for Respondent's inaction (whether intentional or not), Claimant would have been able to exchange and repatriate the returns at the exchange rate set by the government at the time or, in the alternative, reach settlement in this context. In the but-for world, Claimant "would most likely still operate and profit from its route in Venezuela."[14] The Tribunal concluded that as a result of Respondent's

breaches of the BIT, Claimant "lost the opportunity to earn its revenues in U.S. dollars, and furthermore, the opportunity to profit from that amount."[15]

The Tribunal denied Respondent's arguments with respect to mitigation and contributory fault. Respondent had argued that Claimant's damages claim should be reduced by 25 percent to 75 percent because, *inter alia*, it could have sought recourse through various administrative and judicial procedures, it could have acquired U.S. dollars through alternatives to the state-subsidized market, and Claimant allegedly aggravated its damages by initiating the arbitral proceedings in December 2016 rather than sooner.

The Tribunal found that Claimant did not fail to mitigate.[16] First, Claimant was under no obligation to pursue administrative and judicial channels given that there were no regulatory decisions it could have challenged. Second, the Tribunal found that Claimant had no other mechanisms for exchanging foreign currency with equally beneficial exchange conditions. Third, the Tribunal gave weight to Claimant's attempts to mitigate the consequences by contacting Venezuelan officials at the time. Fourth, it found that Claimant brought its claims against Venezuela under the BIT in a timely manner. Fifth, it found that Claimant's suspension of its operations in Venezuela were justified in light of the circumstances. The Tribunal relied on the same reasons in dismissing Respondent's contributory fault arguments.

B. Quantification of Damages

On quantum, Claimant sought as damages US$50,618,073.90, an amount equal to the 15 pending currency exchange requests that it could have repatriated. Respondent disputed this amount on the basis that the quantification was "fundamentally flawed."[17] Since the BIT did not indicate proper compensation for Respondent's breaches of the FTF and FET obligations, the Tribunal noted that the purpose of compensation must be to "reinstate Claimant in the same financial position it would have been in had there been no BIT breach."[18] This position was supported under Article 36 of the ILC draft articles, and the Tribunal found that it held a wide margin of discretion in applying these principles.

In assessing whether Claimant's claimed U.S. dollar amount was appropriate, the Tribunal found Claimant's expert to be "reasonable, independent and objective" and his analysis appropriate to the case.[19] The Tribunal did not find (and Respondent did not provide) any explanation as to "which or how any other economic analysis would be more appropriate."[20] It consequently rejected Respondent's arguments that Claimant relied on any improper or non-contemporaneous documents, including any alleged documentary inconsistencies that could render Claimant's expert's approach inappropriate. Due to U.S. sanctions, Respondent's quantum expert was unable to provide a second expert rebuttal report or attend the hearing. Respondent failed to support its case with the opinion of another expert who was not subject to such sanctions. The Tribunal decided that although it would not ignore Respondent's expert report, it would "take into account that its contents were not ratified or subject to cross-examination."[21]

The Tribunal next addressed Respondent's defenses that the amounts Claimant sought to repatriate through the 15 pending requests were somehow overstated and that a consideration of these factors reduced Claimant's alleged damages by more than 50 percent, to US$21,334,156.51. In this regard, the Tribunal rejected Respondent's claim that the investor inflated the prices of its ticket sold in bolivars in Venezuela, since the opposite had been confirmed by Claimant's 2013 tax return and independently also by International Air Transport Association records.[22] It also rejected Respondent's argument that the application of the 6.3 bolivars per U.S. dollar exchange rate to calculate Claimant's damages was somehow

inappropriate.[23] It found that Respondent's argument to apply a rate at the "date of transfer" under the BIT was unworkable because there was no such date in the present case.[24] Rather, to place Claimant in the financial position in which it would have been in the absence of Respondent's breach, the Tribunal believed it more appropriate to use the exchange rate applied when Respondent settled other airlines' currency exchange requests for their 2012 and 2013 returns in bolivars, i.e., the 6.3 bolivars per U.S. dollar rate.

The Tribunal accepted Respondent's defenses that the damages awarded should exclude certain amounts in selected instances. It agreed with Respondent that Claimant would not have been authorized to acquire foreign currency for the net proceeds for the "sold outside, ticketed in" trips originating from the Republic.[25] The Tribunal also accepted Respondent's objection that the damages amount should exclude interest revenue that did not qualify as proceeds from ticket sales. It agreed with Respondent that in the but-for scenario, Claimant would not have been authorized to transfer such interest revenue outside the Republic through currency exchange requests. Finally, the Tribunal determined that Claimant's damages would exclude any amounts that Respondent was entitled to receive in bolivars in March 2014.[26]

Lastly, the Tribunal addressed the issue of the equivalent bolivar amount kept by Claimant. Respondent argued that in the but-for scenario, Claimant would have had to provide bolivars in exchange for the U.S. dollars, and that to avoid overcompensation, Claimant should provide Respondent with bolivars equivalent to any damages awarded as per the applicable exchange rate as of the date of the award. Claimant rejected this claim, arguing that it should only provide Respondent with amounts it would have received in early 2014. Specifically, Claimant recalled it was owed US$50.6 million in exchange for Venezuelan bolivars (VEF) 319 million and that it should provide Respondent with VEF 319 million at current exchange rates, which would be equivalent to a few thousand U.S. dollars.[27] In contrast, Respondent ignored the historically owed US$50.6 million that was the equivalent of VEF 319 million and focused instead on the amount in U.S. dollars it would be ordered to pay under the Award, that being the amount needed to be converted into VEF as of the date of the Award.[28] The Tribunal found that both parties were partly correct and partly wrong; in the absence of a BIT breach, Claimant would have transferred the amount of U.S. dollars equivalent to VEF 319 million in March 2014 (when Venezuela announced that it would allow other airlines to repatriate their revenue). In this regard, a 10.9 exchange rate appeared to represent a common ground among the parties.[29]

Interest

The Tribunal observed that the BIT gave no indication of "applicable interest" in the context of violations other than unlawful expropriation. The Tribunal held that a normal commercial rate was the appropriate interest rate on the amounts.[30] The parties disagreed on three points in relation to such interest: (i) the timing of interest, (ii) the applicable rate of interest and (iii) whether interest should be compounded.

A. Timing of Interest

Claimant requested both pre- and post-award interest on damages. In contrast, Respondent argued that interest should begin after the date of the Award or, in the alternative, the date of the request for arbitration. The Tribunal did not identify a specific "time when the international wrongful act arose," but it considered that the award of pre-award interest on the principal amount should start running from the date on which other airlines obtained the U.S. dollars they were owed.[31]

B. Applicable Rate of Interest

The parties proposed a total of five alternative interest rates, specifically Venezuela's cost of borrowing, the short-term risk-free rate, Claimant's cost of debt, the interest rate on cash earned by Claimant and the six-month U.S. dollar London Interbank Offered Rate plus 1 percent or 2 percent. The Tribunal did not choose any of the proposed rates. Instead, it found that Canada's "effective interest rate for businesses" adequately reflected a normal commercial rate. The Tribunal awarded a business borrowing interest rate published by the Bank of Canada that represents a "weighted-average borrowing rate for new lending to non-financial businesses, estimated as a function of bank and market interest rates."[32]

C. Compound or Simple Interest

The Tribunal rejected Claimant's request for compound interest. It held that although it was true that compound interest is "appropriate" in cases where the injured party could have "used its principal by depositing it and earning interest on it," such compounding as an element of "full redress must be particularly justified."[33] In support, the Tribunal generally cited to the commentary found in the 2001 ILC draft article on Responsibility of States for Internationally Wrongful Acts. The commentaries state that the "general view" of courts and tribunals is to oppose awarding of compound interest absent "strong and quite specific" arguments to the contrary.[34] The Tribunal found that the present case did not provide such justification.[35] In light of the foregoing, the Tribunal decided that simple interest should accrue on the amount awarded at Canada's effective interest rate for businesses from May 26, 2014, until it was paid in full.

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1 *Air Canada v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB(AF)/17/1, Award, September 13, 2021 (Award), ¶ 304.

2 Award, ¶ 304.

3 Award, ¶ 305.

4 Award, ¶ 311.

5 Award, ¶ 449.

6 Award, ¶ 470.

7 Award, ¶ 533.

8 Award, ¶ 597.

9 Award, ¶ 598.

10 Award, ¶ 598.

[11] Award, ¶ 598.
[12] Award, ¶ 606.
[13] Award, ¶ 605.
[14] Award, ¶ 606.
[15] Award, ¶ 606.
[16] Award, ¶ 608.
[17] Award, ¶ 566.
[18] Award, ¶ 613.
[19] Award, ¶¶ 619, 622.
[20] Award, ¶ 622.
[21] Award, ¶ 618.
[22] Award, ¶ 625.
[23] Award, ¶ 637.
[24] Award, ¶ 636.
[25] Award, ¶ 559.
[26] Award, ¶ 650.
[27] Award, ¶ 642.
[28] Award, ¶ 642.
[29] Award, ¶ 644.
[30] Award, ¶ 694.
[31] Award, ¶ 696.
[32] Award, ¶ 699.
[33] Award, ¶ 701.
[34] 2001 Draft Articles on Responsibility of States for Internationally Wrongful Acts, With Commentaries, ¶¶ 108-109.
[35] Award, ¶ 701.

Banco Bilbao Vizcaya Argentaria S.A. v. Plurinational State of Bolivia, ICSID Case No. ARB(AF)/18/5

Date of the Award
July 12, 2022

The Parties
Banco Bilbao Vizcaya Argentaria S.A. (Claimant); Plurinational State of Bolivia (Respondent)

Sector
Finance

Applicable Treaty
Agreement for the Reciprocal Promotion and Protection of Investments between the Kingdom of Spain and the Republic of Bolivia, dated October 29, 2001 (Spain-Bolivia BIT)

Members of the Tribunal
Stanimir A. Alexandrov (president, appointed by the chair of the International Center for Settlement of Investment Disputes (ICSID) Administrative Council), Valeria Galíndez (Claimant's appointee) and Yves Derains (Respondent's appointee)

Background

In 1996, Bolivia adopted a new pension law pursuant to which individuals' pension contributions were to be administered by private entities known as administradoras de fondos de pensiones (pension fund administrators, or AFPs).[1] Spanish banks Banco Bilbao Vizcaya and Invesco-Argentaria entered the Bolivian market and incorporated subsidiary companies, which became AFPs.[2] The two Spanish companies later merged to form Banco Bilbao Vizcaya Argentina (BBVA), Claimant in this arbitration.[3]

The dispute has its origin in the nationalization of Bolivia's pension system in 2010 by means of Pension Law No. 65 (nationalization law) and the subsequent treatment of BBVA Previsión (Previsión), an AFP and Claimant's Bolivian subsidiary. The nationalization law, enacted after a constitutional reform provided that all social security services must be provided by the state, established a state entity known as the *Gestora Pública de la Seguridad Social de Largo Plazo* (Public Manager of Long-Term Social Security or *Gestora*), which would take charge of the administration of the Bolivian pension system.[14] The nationalization law required AFPs to transfer all information and documentation regarding their operations, along with all assets and liabilities of the pension funds they managed, to the *Gestora*.[5] However, as it would take time for the *Gestora* to be established, AFPs were to continue to provide their services during a transition period, at the end of which all contracts with AFPs would be deemed "resolved."[6] The law did not provide for compensation to AFPs for the termination of their contracts, or for the transfer of the information and documentation related to their operations.[7]

The years that followed the enactment of the nationalization law saw considerable delays in the establishment of the *Gestora*, which was formally created only in 2015.[8] While the Supreme Decree that created the *Gestora* provided that it was to begin operations within 18 months of its creation, Bolivia needed to extend this deadline on four occasions, most recently in September 2021.[9] There were also delays in the process of transferring data from Previsión to the state, which was not complete as of July 2021.[10] BBVA also alleged that during the transition period, Previsión was subject to

measures of harassment by Bolivia, including, *inter alia*, the imposition of a US$73 million fine[11] and the imposition of a requirement that Previsión pay an amount equal to a deficit in employer contributions to pension plans (the employer contribution deficit) before it could exit the Bolivian market.[12]

Against this backdrop, BBVA commenced arbitration against Bolivia under the Spain-Bolivia BIT before ICSID's Additional Facility on July 31, 2018.[13]

Jurisdiction and Liability

Bolivia objected to the Tribunal's jurisdiction on the basis that in the contract entered into by Previsión and the Bolivian government, the parties had excluded recourse to arbitration with respect to any questions bearing on "norms of imperative character contained in the Pension Law."[14] Bolivia argued that this carve-out applied to and encompassed BBVA's claims in the BIT arbitration.[15]

The Tribunal disagreed, finding first that there was no "clear and express" renunciation of treaty arbitration in the contract.[16] The Tribunal noted that the clause relied upon by Bolivia did not refer to the BIT or any investors' rights thereunder, and the Spain-Bolivia BIT was dated six years after the contract.[17] The Tribunal also found that the prohibition on arbitration in the contract was best interpreted as excluding only domestic arbitration under the Bolivian commercial code.[18] The Tribunal followed the annulment committee in *Vivendi v. Argentina* in emphasizing that a distinction must be drawn between treaty and contract claims,[19] and it observed that all of BBVA's claims were treaty claims.[20] The Tribunal therefore upheld its jurisdiction over BBVA's claims.[21]

On liability, BBVA argued that Bolivia had violated the fair and equitable treatment (FET) provision in Article 3(1) of the Spain-Bolivia BIT as well as Article 3(2)'s prohibition on hindering protected investments through arbitrary conduct.[22] The Tribunal found that Bolivia's 12-year delay in completing the nationalization of its pension system was unjustified, and it had subjected AFPs like Previsión to an extended "transition period" that involved considerable uncertainty.[23] In the Tribunal's view, Bolivia's conduct breached the BIT's FET standard[24] and its prohibition on arbitrary conduct.[25] In particular, the Tribunal considered that Bolivia had arbitrarily impeded BBVA's right to dispose of its investment as it saw fit, and it agreed with BBVA's claim that it had been held "hostage" by Bolivia's conduct.[26]

The Tribunal also found that Bolivia had violated the BIT's FET standard by subjecting Previsión to contradictory regulations during the extended data transfer process, creating an impermissible "roller-coaster effect" on BBVA's investment.[27] It found that Bolivia's imposition of a requirement that Previsión pay the employer contribution deficit before it could exit the Bolivian market was arbitrary and breached Articles 3(1) and 3(2),[28] though it considered BBVA's claim with regard to the US$73 million fine to be premature, as that fine was subject to ongoing judicial review in Bolivia.[29]

Quantum

BBVA first requested reparation in the form of "cessation," referring to Article 30 of the International Law Commission's (ILC) Articles on the Responsibility of States for Internationally Wrongful Acts (ILC Articles), which BBVA argued reflects customary international law that is binding on Bolivia.[30] Article 30 of the ILC Articles requires a state that has committed an internationally wrongful act — including the breach of a treaty — to cease that act if it is continuing.[31] Specifically, BBVA requested that the Tribunal order Bolivia to cease any actions related to the US$73 million fine and the requirement that Previsión pay off the employer contribution deficit and to acquire BBVA's shares in Previsión in exchange for compensation at fair market value, effectively completing the nationalization of BBVA's investment.[32]

Bolivia objected to this requested relief on the ground that the Tribunal lacked the power to grant it. It argued that an order of the nature requested by BBVA would violate Bolivia's sovereignty and that no obligation of cessation existed under public international law.[33] Bolivia also took issue with the specific orders requested by BBVA, arguing in particular that there was no basis to order Bolivia to pay any compensation for its acquisition of the Previsión shares.[34]

The Tribunal ultimately considered that it did not need to address the question of whether it was empowered to order non-compensatory forms of relief, as it concluded that the most appropriate and effective form of relief was compensation for the value of BBVA's shares in Previsión.[35] It reached this conclusion after finding that the value of BBVA's shares in Previsión had been negatively impacted by the impossibility of selling those shares as well as by uncertainty as to the precise moment when Previsión's services would be taken over by the state.[36]

With regard to the quantum of compensation, BBVA argued that compensation should reflect the fair market value (FMV) of its shares in Previsión[37] and that the valuation date should be the date of the Tribunal's award.[38] BBVA contended that the Tribunal should apply a discounted cash flow (DCF) analysis. An expert team from Compass Lexecon provided a DCF calculation that valued BBVA's shares in Previsión at US$118.5 million.

For its part, Bolivia argued that calculating compensation based on the FMV of BBVA's shareholding was inappropriate outside the context of a case involving expropriation.[39] It argued for a valuation date in 2010, as that was when the nationalization process at issue in the dispute began.[40] Bolivia and its experts from The Brattle Group (Brattle) raised several issues with BBVA's DCF calculation,[41] including that Compass Lexecon had not taken into account evidence from the parties' negotiations that BBVA was prepared to sell its shares in Previsión for US$15 million in December 2010.[42]

Prior to engaging in its own analysis of the quantum of compensation, the Tribunal noted that in the absence of Bolivia's breaches of the BIT, the result would have been the implementation of the nationalization of Previsión and the accompanying payment of

compensation to BBVA.[43] The Tribunal then took the unusual step of making its award of monetary compensation to BBVA conditional on Claimant's making available to Bolivia its shares in Previsión, citing *CMS Gas v. Argentina* as precedent for this approach.[44] The Tribunal specified that BBVA could only obtain the awarded compensation once title to the shares in question had been delivered to the state.[45]

Turning to the issue of valuation, the Tribunal rejected Bolivia's argument that an FMV-based valuation was inappropriate outside the context of an expropriation claim. It noted that numerous tribunals had found FMV to be a valid criterion to determine reparation in the context of other breaches.[46] Referring to a definition of FMV originally set forth in the case law of the Iran-U.S. Claims Tribunal and later adopted by tribunals in investment treaty cases, the Tribunal agreed with BBVA's experts at Compass Lexecon that prices from forced sales should not be used as a basis to determine FMV.[47]

This finding was particularly relevant given that Brattle (Bolivia's quantum experts) had used the figure of US$15 million — the amount at which BBVA had offered to sell its shares in Previsión to the government in December 2010 — as the starting point for its valuations.[48] The Tribunal rejected these valuations, *inter alia*, because it considered that the US$15 million starting point did not reflect the FMV of BBVA's shareholding.[49] It observed that BBVA had made its offer only 13 days after the promulgation of the nationalization law. In this context, BBVA's offer was not made in conditions like those on the open market but rather was made under pressure and constraints to sell its shares to the state.[50]

With regard to the valuation date, the Tribunal observed that the value of Previsión had increased significantly since the passage of the nationalization law in 2010.[51] It therefore agreed with BBVA that an *ex post* valuation was more appropriate and that an *ex ante* date such as that proposed by Bolivia would allow Bolivia to take advantage of its own unlawful conduct.[52] The Tribunal therefore selected September 30, 2020 — the date proposed by Compass Lexecon — as the valuation date.[53]

Turning then to the valuation methodology, the Tribunal noted that the parties' experts were in agreement that a DCF methodology would be the most appropriate way to determine the value of BBVA's shares in Previsión, and it agreed with their assessment.[54] The Tribunal then reviewed Bolivia's and Brattle's criticisms of the DCF calculation presented by Compass Lexecon. It first rejected Bolivia's argument that Compass Lexecon's calculation was flawed because it ignored the risks of additional competition in the Bolivian pension sector.[55] The Tribunal characterized this argument as "speculative" and noted that a 2002 tender to select an additional AFP had to be closed due to lack of participation.[56]

On the other hand, the Tribunal credited Brattle's criticism that Compass Lexecon had incorrectly assessed the increase in pension contributions in projecting BBVA's cash flow. Specifically, the Tribunal preferred Brattle's estimate of the increase in pension contributions, which was linked to increases in Bolivia's population, to Compass Lexecon's estimate, which was linked to Bolivia's economic growth.[57] The Tribunal also agreed with Brattle's criticisms of the risk-free rate and beta components of the discount rate applied by Compass Lexecon.[58] In particular, the Tribunal agreed with Brattle that there should be consistency between the term of the bonds used to estimate the risk-free rate and those used to estimate the market risk premium.[59] The Tribunal adopted the lower risk-free rate proposed by Brattle[60] as well as the betas proposed by Brattle.[61] Finally, the Tribunal agreed with Brattle that the country-risk premium should be based on the Emerging Market Bond Index (EMBI), as it stood close to the valuation date, rather than taking the average of the EMBI over the 12 months preceding

the valuation date and then excluding March to September 2020 due to the effects of COVID-19, as Compass Lexecon had done.[62]

Finally, the Tribunal rejected Brattle's argument that the Tribunal should deduct from its FMV calculation the value of the US$73 million fine and the amount of the employer contribution deficit. The latter was found to be a breach of the BIT,[63] while the former was still subject to pending proceedings before Bolivian courts, and its impact was uncertain.[64]

Applying adjustments to Compass Lexecon's DCF calculation to account for areas where it agreed with Brattle, the Tribunal ultimately arrived at a valuation of US$94.8 million for BBVA's shares in Previsión.[65]

Lastly, the Tribunal addressed BBVA's request that any compensation not be subject to any withholding due to taxation, as its DCF calculation already accounted for taxes. The Tribunal agreed, holding that the awarded compensation should be free from any Bolivian taxes.[66]

Interest

With regard to interest, the Tribunal held that compound interest was appropriate, noting the practice of other international tribunals, which indicated that compound interest serves to guarantee that a claimant receives full reparation.[67]

The Tribunal observed that both parties' experts were in agreement that Bolivia's sovereign cost of debt would be a reasonable interest rate, as it reflected the conditions for a loan to Bolivia. The Tribunal agreed with this assessment and noted that any lower or risk-free interest rate would disincentivize Bolivia's prompt payment of the awarded compensation.[68] The Tribunal therefore chose a rate of 6.36 percent, which had been proposed by Compass Lexecon and to which Bolivia had not objected.[69]

The Tribunal observed that the valuation date of September 30, 2020, was initially meant to coincide with the date of the award, but the award was only rendered in July 2022. Since BBVA had not been able to update its valuation, the Tribunal decided to grant pre-award interest at a rate of 6.36 percent, compounded annually, starting from October 1, 2020.[70] The Tribunal calculated that as of June 1, 2022, the amount of interest owed was US$10,217,182.61, and Bolivia was ordered to pay this amount.[71] Bolivia was also ordered to pay post-award interest at the same interest rate on both the US$94.8 million in compensation and the US$10.2 million in pre-award interest from the date of the award until the date of effective payment.[72]

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1 *Banco Bilbao Vizcaria Argentaria S.A. v. Plurinational State of Bolivia,* ICSID Case No. ARB(AF)/18/5, Award, July 12, 2022, ¶ 131.
2 Award, ¶¶ 136-137.
3 Award, ¶ 144.
4 Award, ¶¶ 146-147.
5 Award, ¶ 148.
6 Award, ¶¶ 148, 150.
7 Award, ¶ 150.
8 Award, ¶ 204.
9 Award, ¶¶ 206-210.
10 Award, ¶¶ 211-288.
11 Award, ¶ 477.
12 Award, ¶¶ 468-469.
13 Award, ¶ 9.
14 Award, ¶¶ 349-350.
15 Award, ¶ 357.
16 Award, ¶¶ 374-382.
17 Award, ¶¶ 378-379.
18 Award, ¶¶ 380-381.
19 Award, ¶ 383 (citing *Compañía de Aguas del Aconquija, S.A. & Vivendi Universal v. Argentine Republic,* ICSID Case No. ARB/97/3, Decision on Annulment, July 3, 2002, ¶ 444).
20 Award, ¶ 388.

21 Award, ¶ 389.
22 Award, ¶ 390.
23 Award, ¶¶ 554-555.
24 Award, ¶ 576
25 Award, ¶ 578.
26 Award, ¶¶ 578-579.
27 Award, ¶ 599.
28 Award, ¶ 613.
29 Award, ¶ 652.
30 Award, ¶ 658.
31 Ibid.
32 Award, ¶¶ 661-662.
33 Award, ¶ 728.
34 Award, ¶ 736.
35 Award, ¶¶ 786-787.
36 Award, ¶ 782.
37 Award, ¶ 671.
38 Award, ¶ 675.
39 Award, ¶¶ 756-758.
40 Award, ¶ 760.
41 Award, ¶¶ 762-764.
42 Award, ¶ 763.
43 Award, ¶ 788.
44 Award, ¶ 390.
45 Award, ¶¶ 554-555.
46 Award, ¶ 576.
47 Award, ¶ 578.
48 Award, ¶¶ 578-579.
49 Award, ¶ 599.
50 Award, ¶ 613.
51 Award, ¶ 652.
52 Award, ¶ 658.
53 Ibid.
54 Award, ¶¶ 661-662.
55 Award, ¶ 728.
56 Award, ¶ 736.
57 Award, ¶¶ 786-787.
58 Award, ¶ 782.
59 Award, ¶ 671.
60 Award, ¶ 675.
61 Award, ¶¶ 756-758.
62 Award, ¶ 760.
63 Award, ¶¶ 762-764.
64 Award, ¶ 763.
65 Award, ¶ 788.
65 Award, ¶ 919.
66 Award, ¶¶ 928-929.
67 Award, ¶ 922.
68 Award, ¶ 923.
69 Award, ¶ 924.
70 Award, ¶¶ 925-926.
71 Award, ¶¶ 927, 936(vi).
72 Award, ¶ 936(vii).

Bank Melli Iran and Bank Saderat Iran v. The Kingdom of Bahrain, PCA Case No. 2017-25

Date of the Award
November 9, 2021

The Parties
Bank Melli Iran and Bank Saderat Iran (Claimants); Kingdom of Bahrain (Respondent)

Sector
Finance — Banking

Applicable Treaty
Agreement on Reciprocal Promotion and Protection of Investments between the Government of the Islamic Republic of Iran and the Government of the Kingdom of Bahrain, dated October 19, 2002

Members of the Tribunal
Professor Gabrielle Kaufman-Kohler, Presiding Arbitrator (replaced Professor Rudolph Dolzer on his passing); Professor Bernard Hanotiau (Claimants' appointee, replaced Professor Emmanuel Gaillard on his passing); and the Right Honorable Lord Collins of Mapesbury (appointed by appointing authority, the Permanent Court of Arbitration)

Background

Claimants Bank Melli Iran and Bank Saderat Iran are Iranian banks that, along with Ahli United Bank, a Bahraini bank, incorporated Future Bank in Bahrain in 2004. The three banks signed a shareholders'

agreement giving each of them an equal interest in Future Bank. As a Bahraini bank, Future Bank is subject to supervision by the Central Bank of Bahrain (CBB). From the start, it maintained strong connections to Iran and Iranian businesses. This became an issue when sanctions against Iran gained ground between 2006 and 2010, with the UN Security Council (UNSC), the United States and the European Union all adopting sanctions against Iran and various Iranian entities. This ramp-up of sanctions led CBB to issue a directive in September 2010 (2010 CBB directive) requiring all Bahraini banks to "ensure that they are fully compliant with the requirements of all United Nations Security Council Resolutions imposing sanctions on the Islamic Republic of Iran" and to familiarize themselves with the sanctions imposed by the U.S. and "ensure they do not fall foul of its provisions."[1]

During the same time period, CBB periodically raised issues with Future Bank's compliance with CBB regulations, such as those related to money laundering, and with its Iran exposure. Each time, Future Bank indicated that it would put measures in place to address CBB's concerns. Then, in June 2011, CBB met with Future Bank representatives to recommend that they consider voluntary liquidation, which Respondent framed as a warning because of Future Bank's repeated violations of CBB regulations. Future Bank did not voluntarily liquidate, but over the next few years, CBB continued to note Future Bank's violations of various CBB regulations touching on its dealings with Iran. CBB also took note of Future Bank's level of Iran exposure, which it instructed it to decrease, including its exposure to its own shareholders, i.e., Claimants.

On April 30, 2015, CBB decided to place Future Bank under administration on the basis that Future Bank's continuing to offer its "services under supervision will cause harm to the production of financial services and the general interest in the Kingdom."[2] CBB issued its administration decision the same day, ordering Future Bank to "cease trading immediately" and to provide CBB's representative with full access to Future Bank's premises, records and systems, since CBB had assumed "full managerial control."[3] On May 3, 2015, CBB representatives met with representatives from Future Bank to inform them that it had decided to liquidate Future Bank. CBB again invited Future Bank to agree to voluntary liquidation. CBB published its administration decision on May 7, 2015, and Future Bank appealed the administration decision the same day. CBB dismissed the appeal on May 18, 2015, citing Future Bank's violations of CBB regulations and of international sanctions against Iran. After putting Future Bank into administration, CBB commenced an investigation of Future Bank, which led to a report (2015 CBB Report) on Future Bank's alleged violations of applicable regulations, including violations of various UNSC resolutions stemming from the provision of financial support to legal entities directly and indirectly owned by the Iranian government.

On the basis of the 2015 CBB Report, on December 22, 2016, CBB resolved to liquidate Future Bank, publishing its decision in the official gazette. In February 2017, Claimants brought this arbitration against Respondent for violations of the Bahrain-Iran bilateral investment treaty (BIT) arising out of Future Bank's forced administration.

Jurisdiction and Liability

A. Jurisdiction and Admissibility

Respondent made two preliminary objections as to the jurisdiction and admissibility of Claimants' claims: (1) that Claimants engaged in systemic illegal activities, rendering their claims inadmissible under the doctrines of clean hands and international public policy, and (2) that Claimants failed to exhaust local remedies before submitting their claims to arbitration.

i. Future Bank's Alleged Illegal Activities

The Tribunal first considered whether Future Bank's alleged illegal activities constituted a bar to jurisdiction or admissibility. It concluded that the objection was not jurisdictional, since it stemmed from activities post-dating Future Bank's establishment, as opposed to Claimants' actions in establishing their investments. However, it determined that Future Bank's illegal activities would constitute a bar to admissibility if Future Bank's illegal conduct met a two-part test, namely, if it (i) were serious and widespread and (ii) bore a close relationship to the claims at issue. In order to constitute serious violations, the Tribunal noted that an investor's wrongful conduct must relate to a fundamental rule of law. The UN sanctions met this test, as did the national (U.S.) and regional (EU) sanctions to the extent that they were co-extensive with the UN sanctions, but not to the extent that they included entities not covered by the UN sanctions. The Tribunal noted that none of the sanctions applied directly to Future Bank, meaning that Bahrain would have to give effect to those sanctions under Bahrani law. It concluded that the 2010 CBB directive gave effect to the UN sanctions but not to the U.S. or EU sanctions.

Applying the two-factor test, the Tribunal concluded that Future Bank's illegal activities did not constitute a bar to admissibility. Although Future Bank had committed several sanctions violations, the record contained "insufficient indications to establish systemic and/or severe violations of fundamental rules of law that would call for a declaration of inadmissibility as a blanket measure."[4] Moreover,

the Tribunal found that Claimants' claims did not relate to Future Bank's unlawful conduct but rather related to the measures taken by the Bahrani regulatory authorities against Future Bank. Therefore, Claimants' claims were admissible.

ii. Exhaustion of Local Remedies

The Tribunal likewise dismissed Respondent's second preliminary objection, i.e., that Claimants failed to exhaust local remedies before bringing the arbitration. It concluded that exhaustion of local remedies[5] was not required under the BIT since "neither the dispute settlement clause in Article 11 nor any other provision of the BIT require the exhaustion of local remedies" and that (with the exception of denial-of-justice claims) there was no general requirement under international law to pursue local remedies. The Tribunal also noted that the BIT's fork-in-the-road clause would preclude investors from seeking redress in an international forum if it accepted Respondent's position.

B. Liability

On the merits, the Tribunal determined that Respondent's forced administration and liquidation of Future Bank interfered with Claimants' shareholding rights in Future Bank and constituted an indirect expropriation in violation of Article 6(1) of the BIT. The Tribunal found that there was a manifest lack of reasoning for CBB's decision to place Future Bank under administration in violation of the applicable regulatory framework and that there was strong circumstantial evidence of political targeting due to Future Bank's connections to Iran. Because CBB's measures were "unreasonable, disproportionate, and politically motivated,"[6] they did not meet the requirement that expropriatory measures be taken for a public purpose. Moreover, Respondent failed to pay effective and appropriate compensation "without delay" after placing the bank under administration on April 30, 2015.[7] Thus, Respondent's actions constituted an unlawful expropriation under Article 6(1) of the BIT. In the interests of procedural economy, the Tribunal did not address Claimants' other alleged treaty violations because it would not alter or add to the remedies available to Claimants for Respondent's violation of Article 6(1).

Quantum

Claimants sought (i) payment of fair market value of their investments, including lost profits; (ii) pre-award interest to compensate for lost business opportunities following April 30, 2015; (iii) post-award interest; and (iv) moral damages for reputational harm suffered as a result of Respondent's actions. Claimants had originally requested restitution but withdrew that request at the hearing.

Respondent, by contrast, argued that Claimants were not entitled to any reparation because Future Bank's value actually increased under its administration, meaning that Claimants had suffered no loss. Respondent also asserted that any damages awarded to Claimants must account for their current debt to Future Bank in order to avoid Claimants' unjust enrichment. Finally, Respondent rejected Claimants' request for moral damages because any reputational damage was the result of Claimants' own conduct and could not be attributed to Respondent.

A. Standard of Compensation

The Tribunal began its analysis by setting out the applicable standard for compensation. The Tribunal recalled that it was a basic principle of international law that states incur responsibility for their internationally wrongful acts, with the corollary to that principle being that states must make full reparation for injury caused. It pointed to the principle of full reparation as first set forth in the "often-quoted *Chorzów Factory* case,"[8] which

requires that the state "eliminate all consequences of the internationally illicit act and restore the injured party to the situation that would have existed if the act had not been committed."[9] It also referred to International Law Commission (ILC) Articles 36(1), 31(2) and 36(2), which "are routinely applied by analogy in investor-state arbitration."[10] Noting that the BIT was silent on the standard of compensation for internationally wrongful acts, the Tribunal concluded that "[t]he standard governing compensation for unlawful expropriations is thus subject to customary international law, specifically to the principle of full reparation as articulated by the PCIJ in the *Chorzów Factory* case and later expressed in the ILC Articles."[11] The Tribunal noted that both parties' valuations relied on Future Bank's fair market value at the time of the expropriation, which it found to be consistent with the principle of full reparation insofar as it would restore Claimants to the situation that they would have been in but for Respondent's breach.

B. Claimant's Actual Scenario

Since compensation is intended to wipe out the material consequences of the state's unlawful act, the Tribunal determined that the "damage inflicted by [Respondent's] unlawful conduct is thus equal to the difference between (i) the Claimants' economic position but-for the wrongful measures (but-for scenario) and (ii) their actual economic position (actual scenario)."[12] However, it noted that it was not enough simply to compare the value of Claimants' shares at the time of the expropriation and on the date of the award, since that would ignore the *de facto* economic position of Claimants who had been permanently deprived of the benefits of their shares. That said, it took note of Respondent's representation that Claimants were entitled to the liquidation proceeds of Future Bank and the resulting possibility of their double recovery. Considering that Claimants had not received liquidation proceeds for more than six years and that Respondent had failed to provide any detailed information on their progress, the Tribunal considered the prospect of Claimants' recovery to be highly uncertain. Still, it could not rule out entirely the possibility of double recovery. To address this, it determined that if Claimants collected under the award before liquidation proceeds were paid out, "it would be up to the competent Bahraini authorities to consider the amounts at issue and avoid the materialization of the risk of double recovery."[13] If Claimants received liquidation proceeds before collecting the award, the "liquidation payment could … come in deduction of the amount of damages owed hereunder."[14] Either way, the Tribunal determined to calculate damages without discounting the alleged current value of Claimants' shares in Future Bank or Claimants' potential recovery in the liquidation proceedings.

C. Calculation of Fair Market Value

Turning to the appropriate valuation method, the Tribunal noted that both parties agreed that an asset-based approach was acceptable. However, Claimants' expert argued that an income-based approach was most suitable to capture the value of Future Bank's profits but for the expropriation. In the alternative, Claimants argued for a market-based approach, i.e., based on the value of comparable assets sold in the open market. While Respondent's expert accepted that income and market-based approaches were generally acceptable valuation methodologies, it believed they were inappropriate in the present circumstances because a hypothetical purchaser would not pay more than the asset-based valuation for Claimants' shares at the administration date.

The Tribunal noted that an income-based approach was generally considered to best reflect the fair market value of a going concern with a proven record of profitability like Future Bank. That said, it emphasized

that an income-based approach presupposed that Future Bank would continue to be equally profitable moving forward, a prospect the Tribunal considered speculative for several reasons. First, Future Bank had violated applicable laws and regulations, including by dealing with sanctioned entities. A hypothetical buyer would have discovered those irregularities and discounted the price to account for the risk of increased regulatory intervention. That would impact the prospects for Future Bank's future profitability. Second, Future Bank's business model was primarily based on its dealings with Iranian entities, and it was facing increased pressure from CBB to reduce its exposure to Iran. A hypothetical buyer would consider future profits based on this model to be too speculative to project into the future and would instead rely on the book value of Future Bank's existing assets. Notably, this analysis would also affect the market-based valuation.

The Tribunal thus decided to compute damages based on the asset-based valuation methodology. The asset-based valuation minimized the risk of compensating Claimants for their violations of applicable regulations, and it also did not assume that Future Bank would continue with the same "Iran-exposed business model with which the regulator had taken issue."[15]

As to the value of Claimants' shares under the asset-based approach, Claimants' expert had calculated their value to be Bahraini dinar (BHD) 91,386,000 (US$243 million), while Respondent's expert calculated it to be BHD 96,195,000 (US$255 million). Because Respondent's valuation was higher, the Tribunal adopted the amount put forward by Claimants' expert, setting the fair market value of Claimants' shares as of the date of the expropriation at BHD 91,368,000 (US$243 million).

D. Respondent's Setoff Request

Respondent submitted that Claimants' current debt to Future Bank amounted to BHD 136.3 million (US$363.6 million), which exceeded the value of Claimants' shares. It therefore requested the Tribunal deduct Claimants' debt from the amount awarded to Claimants to avoid the risk of unjust enrichment. Claimants opposed, arguing that the BIT did not permit counterclaims, undermining Respondent's setoff argument.

The Tribunal noted that Respondent's request could be understood either as a request to consider Claimants' debt in assessing the fair market value of their shares or as a request for a setoff. If the former, the Tribunal considered the argument lacked merit because it was not obvious why the bank's book value would be reduced because it granted a loan to its shareholders. If the latter, the Tribunal concluded it could not grant a setoff for several reasons. Respondent's claim for setoff could not be brought before the Tribunal because Claimants' debt to Future Bank arose from a contract between Claimants and Future Bank, not between Claimants and Respondent. As a tribunal established under the UN Commission on International Trade Law (UNCITRAL) Rules, the Tribunal had no jurisdiction over the claim because it did not arise out of the BIT. Second, under Article 11 of the BIT, the Tribunal lacked jurisdiction over a claim for recovery of amounts that Claimants owed to a third party, i.e., Future Bank. Third, even assuming the Tribunal had jurisdiction, neither party had addressed which law governed the setoff claim and whether the requirements for a setoff were met. Moreover, there was no basis to assume the amounts due to Future Bank would not be otherwise recovered.

E. Moral Damages

Finally, the Tribunal dismissed Claimants' request for moral or reputational damages on the basis that Claimants "failed to offer evidence [of], let alone establish, the existence of such a damage."[16]

Interest

It was undisputed that Claimants were entitled to pre-award interest from the valuation date, April 30, 2015. The parties disagreed, however, as to the appropriate rate. Claimants argued that Future Bank's weighted average cost of capital (WACC) was appropriate because it reflected the business opportunities Claimants lost after expropriation. Bahrain disagreed. The Tribunal concluded that it would be inappropriate to apply WACC given that it includes an element of reward for business risks that Claimants no longer bore after expropriation. Instead, it awarded interest on a risk-free basis, adopting U.S. Treasury bonds, as proposed by both parties' experts. The experts disagreed as to the relevant duration of the U.S. Treasury bonds, but the Tribunal agreed with Respondent's expert that five years was appropriate because the time between the valuation date and the award was closer to five years than to the 10 years proposed by Claimants' expert.[17] Because the parties and their experts did not address whether interest should be compounded or the appropriate compounding rate, the Tribunal awarded simple interest.[18]

It was also undisputed that Claimants were entitled to post-award interest.[19] Claimants had proposed the London Interbank Offered Rate plus 2 percent compounded annually, but the Tribunal saw no reason to apply a different interest rate to post-award interest than to pre-award interest, so it applied the same rate as pre-award interest, i.e., the return on five-year U.S. Treasury bonds.[20]

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1 *Bank Melli Iran and Bank Saderat Iran v. The Kingdom of Bahrain*, PCA Case No. 2017-25, Award, November 9, 2021 (Award), ¶ 228.

2 Award, ¶ 292.

3 Award, ¶ 295.

4 Award, ¶ 503.

5 Award, ¶ 518.

6 Award, ¶ 694.

7 Award, ¶ 696.

8 Award, ¶ 739.

9 Award, ¶ 739.

10 Award, ¶ 741.

11 Award, ¶ 741.

12 Award, ¶ 746.

13 Award, ¶ 752.

14 Award, ¶ 753.

15 Award, ¶ 772.

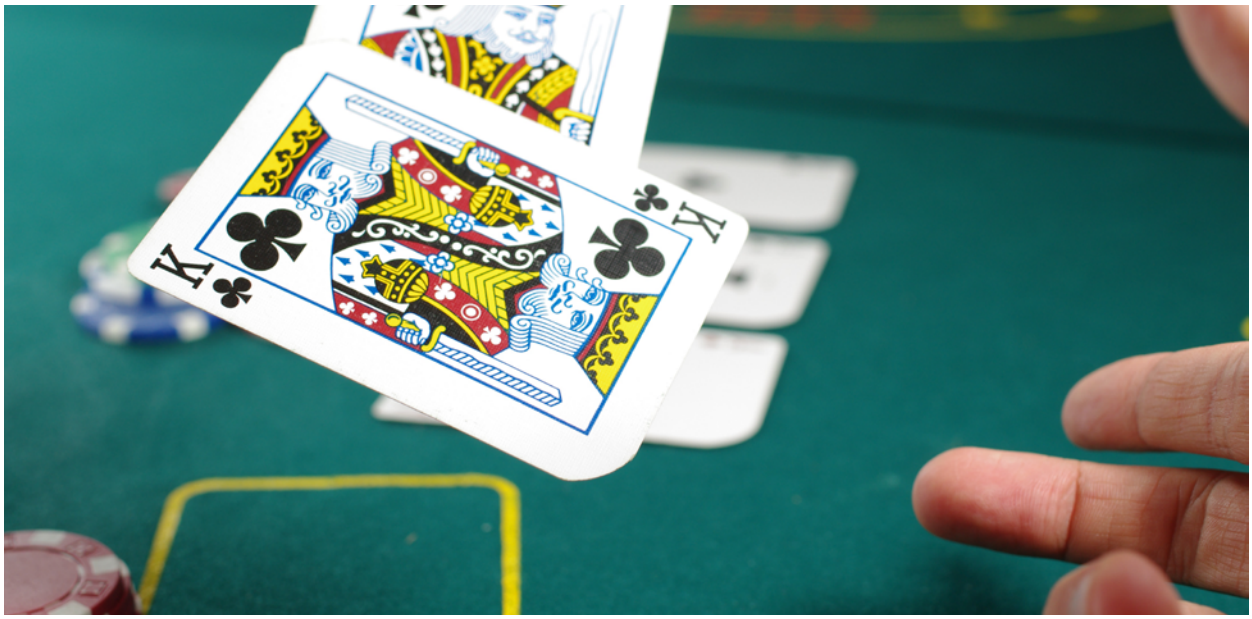
16 Award, ¶ 794.

17 Award, ¶ 802.

18 Award, ¶ 803.

19 Award, ¶ 805.

20 Award, ¶ 807.



Casinos Austria International GmbH and Casinos Austria Aktiengesellschaft v. Argentine Republic, ICSID Case No. ARB/14/32, Award, November 5, 2021

Date of the Award
November 5, 2021

The Parties
Casinos Austria International GmbH and Casinos Austria Aktiengesellschaft (Claimants); Argentine Republic (Respondent)

Sectors
Gaming and Lottery, Arts, Entertainment, Recreation

Applicable Treaty
Argentina-Austria Bilateral Investment Treaty (1992) (BIT)

Members of the Tribunal
Hans Van Houtte (president), Stephan Schill (Claimants' appointee) and Santiago Torres (Respondent's appointee)

Background

This case arose from Argentina's revocation of a 30-year exclusive license for ENJASA (which was majority owned by Claimants) to operate gaming and lottery activities in the Argentinian province of Salta. In the 1990s, Argentina sought to privatize its gaming industry. As part of those efforts to privatize the gaming sector, Respondent created the entity ENJASA. Shortly thereafter, Respondent created the regulatory entity ENREJA to regulate the gaming sector, including ENJASA. In 1999, Respondent granted ENJASA a 30-year exclusive license for gaming operations, which specified ENJASA would forfeit its license (1) if it did not follow gaming sector and anti-money laundering regulations and (2) if it performed additional gaming operations without Respondent's approval.

In September 1999, Respondent announced a tender of 90 percent of ENJASA's shares. The sole participant in this tender was a temporary business association (Unión Temporal de Empresas, or UTE), a joint venture that included Claimants. In 2000, the UTE won the public tender. The UTE's shares in ENJASA were then transferred to L&E, an Argentinian corporation formed by UTE members in proportion to their participation in the UTE. The shareholding of UTE and ENJASA changed over the years, with Claimants eventually increasing their indirect shareholding in ENJASA to 99.94 percent. ENJASA's presence in Salta grew dramatically, with holdings that included four casinos and a five-star luxury hotel.

From 2000 to 2007, Respondent made regulatory changes regarding the gaming sector and money laundering. Following the changes, Respondent sanctioned Claimants twice for minor violations. In 2008, ENJASA entered into an agreement with Respondent to renegotiate, *inter alia*, ENJASA's operating fees.

Between 2008 and 2013, Claimants were fined 13 more times and investigated three times for noncompliance with various obligations.

In August 2013, Respondent revoked ENJASA's license, leading to a series of largely unsuccessful challenges by Claimants. While participating in domestic proceedings (which did not resolve the dispute), Claimants put Respondent on notice of their claim under the BIT. Claimants then filed for arbitration before the International Center for Settlement of Investment Disputes (ICSID) in December 2014. Claimants' final domestic challenge was withdrawn in August 2018.

Jurisdiction

On June 29, 2018, the Tribunal issued its Decision on Jurisdiction. The panel split 2-1, with Respondent's nominee issuing a dissenting opinion and declaration of dissent. The majority rejected Respondent's argument that because ENJASA already held the license and other assets when Claimants acquired their shareholding, Claimants did not own the license that Respondent revoked. The majority further held that Claimants' 60 percent share was an investment under the ICSID Convention, as it satisfied the Salini criteria.[1]

The majority rejected Respondent's argument that Claimants had brought contractual but not treaty claims. Important to the majority was the fact that Claimants had argued Respondent had revoked ENJASA's license as part of a plan to remove ENJASA from its 30-year monopoly, in breach of the BIT. The majority found this to be sovereign conduct rather than purely commercial conduct. Similarly, the majority held there was prima facie evidence that Respondent had indirectly expropriated Claimants' investments, because Respondent had destroyed Claimants' share value in ENJASA. The majority also rejected Respondent's arguments that Claimants did not bring a prima facie claim for breach of Respondent's fair and equitable treatment (FET) obligations. Important to the majority was that Respondent revoked ENJASA's licenses without a hearing, and that this was a disproportionate and retroactive act.

The majority found that Claimants had not brought a prima facie claim for Respondent's breach of the BIT's national treatment clause, and so they declined jurisdiction over these claims. The majority also rejected Respondent's arguments that forum selection clauses in the contracts barred the treaty claims, since (1) the clauses did not apply to Respondent, as it was not a party to the contracts, and (2) the clauses did not cover BIT claims.

The majority also performed a detailed analysis regarding Article 8(4) of the BIT, which requires the investor to pursue local remedies for 18 months before starting arbitration. The majority held Article 8 of the

BIT meant Respondent consented to arbitration, and so these requirements regarded admissibility and not jurisdiction. This meant that Claimants could satisfy them after the arbitration had started. Based on the facts of the case, the majority concluded Claimants had satisfied these requirements.

Liability

On November 5, 2021, the majority issued its Award. The majority held that by revoking ENJASA's license, Respondent had indirectly expropriated Claimants' interests in ENJASA's shares. The majority performed a two-pronged indirect expropriation analysis, focusing on (1) whether there had been a permanent and substantial deprivation of Claimants' capacity to benefit and receive economic use from their investment and (2) "whether the host State took those measures in the exercise of its police powers or its right to regulate, which are, as numerous tribunals have emphasized, a recognized component of State sovereignty, safeguarded under both customary international law and the law of investment treaties."

First, the majority held that by revoking ENJASA's license, Respondent had substantially deprived Claimants of their enjoyment of their investments. Second, the majority held that Respondent's decision to revoke ENJASA's license was an arbitrary exercise of regulatory powers. The majority then concluded that Respondent's revocation of ENJASA's license was disproportionate to Claimants' alleged violations, and so Respondent improperly exercised its police powers. The majority did not find that Respondent's actions were a violation of due process. Still, the majority held that by revoking ENJASA's license and then transferring its operations to third parties, Respondent committed an unlawful indirect expropriation.

The majority did not decide Claimants' direct expropriation claim, because any relief granted would overlap with Claimants' indirect expropriation claim. Similarly, the majority did not decide Claimants' FET claims, because Claimants had not alleged separate damages from their indirect expropriation claim. Mr. Torres, Respondent's nominee, issued a separate dissenting opinion, rejecting the majority Award in its entirety.

Quantum

A. Full Reparation and the DCF Method

The majority held that Claimants were entitled to full reparation, which would require Claimants to "be put economically into the position they would, in all probability, have been in but for the revocation of ENJASA's license." The majority concluded that the discounted cash flow method was appropriate to establish Claimants' losses and held the date range should start the day Respondent revoked ENJASA's license.

B. Valuation Model

Regarding the proper valuation model for Claimants' ENJASA shares, the majority agreed with Claimants' expert's recommendation of "projected cash flows," which consisted of two valuation scenarios estimating the expected money to flow into and out of the business. The first scenario's forecast was based on "actual figures, excluding non-recurring costs and revenues," which included "(i) ENJASA's actual results prior to the Valuation Date, and (ii) financial projections that were prepared by ENJASA's management in the normal course of business … ." Claimants provided a second scenario, which Claimants' expert only developed to respond to Respondent's expert's concerns about using actual data from 2013. This estimate "relied less on projections and was closer to ENJASA's historical data, in particular ENJASA's audited financial statement." But Claimants' expert asserted that this second scenario was incorrect, arguing that the Tribunal should take ENJASA's

contemporaneous projections into account and thus accept scenario one.

Respondent, on the other hand, advocated a discounted dividend model, which "predict[ed] the price of a company's stock on the theory that its price at the Valuation Date is worth the sum of all of its future dividend payments, discounted back to the Valuation Date."

The Tribunal sided with Claimants' method because this method better represented the company's actual value. The majority rejected Respondent's experts' proposed discounted dividend model because there was a risk it would cause variations between net profit and income. Importantly, between 2011 and 2012, ENJASA's net profits jumped 150 percent. Using Respondent's methodology would dramatically change the valuation.

C. Relevant Cash Flow

Regarding relevant cash flow, the majority held it was proper to use ENJASA's financial statements up to the date of Respondent's revocation of ENJASA's license, despite the fact that the 2013 statements were not audited. The majority also held that it was proper to include the future cash flow stemming from slot machines from a planned acquisition in 2014.

Further, the majority accepted Claimants' argument that revenue from Claimants' hotel should be excluded. The hotel was not affected by Respondent revoking ENJASA's license, and it continued to operate afterward, although without generating a profit. Because the hotel was operating at a break-even level, the majority rejected Respondent's argument that this would cause the positive cash flow to be overstated. So, the majority excluded the hotel revenue from its calculation.

The majority also agreed with Claimants' treatment of ENJASA's working capital and its effect on the company's projected future cash flows. Respondent's expert's forecast level of working capital was based on a stable percentage of average revenues from 2009 until 2012, without any further adjustments. Claimants' expert, on the other hand, argued that the level of working capital needed to be adjusted continuously after 2013 and decreased proportionally. The majority agreed with Claimants, highlighting that Respondent's analysis did not reflect the effects of inflation on working capital, causing cash flow to be undervalued.

Finally, the majority agreed with Claimants' approach to the future cash flows from a subsidiary because the subsidiary had also suffered losses due to Respondent revoking ENJASA's license.

D. Proper Discount Rate

Regarding the proper discount rate to apply, the majority accepted Claimants' argument for a 3.39 percent risk-free rate based on the August 2013 20-year U.S. Treasury yield. Also, the parties agreed on, and thus the majority applied, a 5.46 percent equity risk premium. Considering the differences in systemic risks in different sectors of the gaming industry, the majority adopted different industry betas for each sector.[2] Finally, the majority used a 2 percent U.S. inflation rate to adjust the discount rate.

E. Exchange Rate

Regarding the exchange rate, the majority noted that the BIT was unclear, as it only stated that the exchange rate would be "determined in accordance with the framework of the respective bank system of the territory of each Contracting Party." Because the commonly applied, free and legal exchange rate in August 2013 was 8.1 Argentine pesos to 1 U.S. dollar, the majority adopted this exchange rate to calculate damages.

F. The Majority's Damages Calculation

Relying on the above, the majority held that Respondent was liable to pay Claimants US$21.66 million in compensation. Finally, the majority rejected Claimants' request for consequential damages arising from their post-revocation windup costs. While the Tribunal held that in principle such additional costs incurred after revocation could be claimed as consequential damages, it concluded that Claimants had failed to prove that these costs were not fully offset by corresponding gains from the sale of the hotel and the premises of the casino in 2017.

Interest

The majority held Respondent must pay 4 percent interest per year, compounded annually, from August 13, 2021, until Argentina made a full payment.

Finally, the majority granted Claimants' request for legal costs, in line with the principle of full reparation, in the amount of US$5,461,265. The majority then added 4 percent interest, compounding annually from the Award's date.

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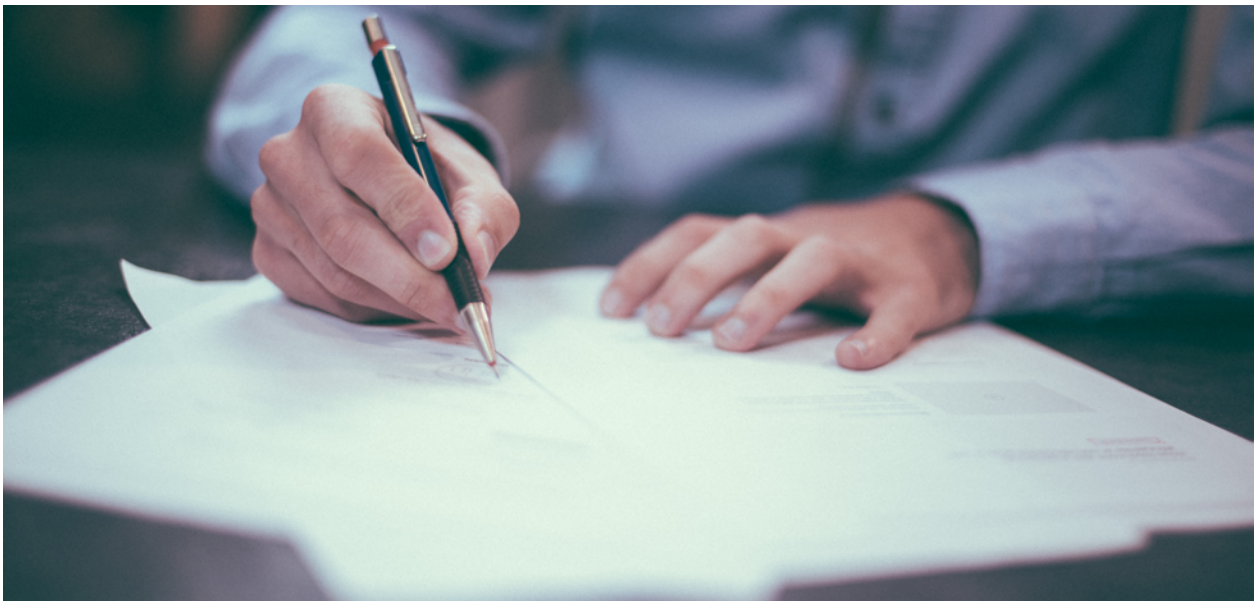
[1] The Salini test comes from the case *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, and it establishes that for there to be an "investment" under Article 25(1) of the ICSID Convention, it must have the following elements: (1) the existence of a substantial contribution by the foreign national, (2) a certain duration of the economic activity in question, (3) the assumption of risk by the foreign national and (4) the contribution of the activity to the host state's development. *Salini Costruttori SpA and Italstrade SpA v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction (July 23, 2001), ¶¶ 50-58.

[2] Industry betas are a metric that reflects the systemic risk that is similar for all businesses in a specific industry.



Lion Mexico Consolidated L.P. v. United Mexican States, ICSID Case No. ARB(AF)/15/2

Date of the Award
September 20, 2021

The Parties
Lion Mexico Consolidated L.P. (Claimant)
United Mexican States (Respondent or Mexico)

Sector
Real Estate

Applicable Treaty
North American Free Trade Agreement (NAFTA)

Members of the Tribunal
Juan Fernández-Armesto (President), David J.A. Cairns (Claimant's Appointee) and Laurence Boisson de Chazournes (Respondent's Appointee)

Background

In 2007, Claimant, a Canadian company, granted three loans to a group of Mexican companies (Debtors) to develop three separate real estate properties in Mexico's Pacific Coast and Midwest. Each loan was secured by a promissory note and a mortgage on the plots of land on which the real estate projects were to be built. By 2009, the Debtors had defaulted on the loans and started negotiations with Claimant to avoid foreclosure. The parties negotiated for years without success.

While Claimant began foreclosure actions, the Debtors engineered a complex judicial fraud in which they filed two lawsuits — one to enforce a forged settlement agreement, and another to preclude Claimant from defending its rights in Mexican courts.[1] Eventually, and without participation by Claimant in the proceedings, the Debtors obtained a judgment upholding the forged settlement agreement and canceling the mortgages on the loans.

During the next years, Claimant filed multiple actions seeking to undo the Debtors' scheme; however,

Mexican courts repeatedly rejected Claimant's efforts to annul the effects of fraud. Finally, and after asserting that any attempt to obtain relief from the Mexican judicial system would be futile, Claimant withdraw its domestic actions and instituted a NAFTA arbitration claiming denial of justice.

Jurisdiction and Liability

On July 30, 2018, the Tribunal issued its Decision on Jurisdiction. The Tribunal found that Claimant's mortgages on the real estate properties qualified as an investment made under NAFTA. Conversely, it found that the promissory notes were not protected investments under NAFTA.[2]

On September 20, 2021, the Tribunal issued its final award (Award), finding that Mexico denied justice to Claimant and failed to provide fair and equitable treatment under NAFTA's Article 1105.[3]

Quantum

A. Guiding Principles

Before discussing the specific components of Claimant's quantum damages, the Tribunal acknowledged that there is no specific standard to compensate denial-of-justice violations under NAFTA and thus the standard must be found in customary international law. The Tribunal then referred to the seminal *Chorzów Factory* decision, which establishes the principle of full reparation for the caused injury.[4]

The Tribunal explained that in order to determine Claimant's compensation, it had to follow a three-step approach. First, the Tribunal had to value Claimant's investment (i.e., the mortgages) at a specific valuation date and under the assumption that no wrong had taken place (but-for scenario). Second, the Tribunal had to determine the actual value of the investment (as-is scenario). Finally, the Tribunal had to calculate the difference between those two scenarios to determine the injury suffered by Claimant.[5]

With respect to the valuation date, the Tribunal reasoned that while the denial of justice had occurred over a long period of time, the origin of Mexico's delict could be "pinpointed" to the judgment that enforced the forged settlement agreement and the cancellation of the mortgages before the Mexican public registries.[6]

The Tribunal then divided Claimant's compensation analysis into three distinct categories: (i) impairment of the investment, (ii) legal fees arising from the withdrawal of the foreclosure proceedings and (iii) expenses incurred in the exhaustion of local remedies.[7]

B. Compensation for Impairment of the Investment

To begin, the Tribunal considered that the value of the mortgages in the but-for scenario should be equal to the market value of the properties minus transaction costs. Had it not been for Mexico's denial of justice, Claimant would have been able to foreclose on the mortgages and resell the properties to a willing third party, using the sale proceeds to set off the amounts owed under the original loans.[8] The Tribunal then recognized that in the but-for scenario, Claimant would have incurred foreclosure costs like legal fees and property taxes and that those amounts should be deducted from any award of compensation.[9]

The Tribunal then focused on the valuation of the properties, which was the main point of disagreement between the parties. While Claimant's valuation yielded US$85.9 million, Mexico proposed a valuation of US$47 million.[10] To determine the properties' market value, the Tribunal examined the economic factors affecting each property.

In the case of the first property (Nayarit Property), the Tribunal analyzed the economic impact of a public road that divided the property into two plots of land and diminished its value.[11] On this point, the Tribunal sided with Claimant, giving weight to a collaboration

agreement with the municipal government, which allowed the real estate developer to take the public road as an integral part of the property, i.e., proceed to development without division.[12] Afterward, the Tribunal analyzed the sales of comparable models submitted by the parties' experts adjusting prices downward or upward depending on multiple factors such as the differences between sales and listings and the existence of master plans, property location, beach frontage area, etc. Finally, the Tribunal ruled that the Nayarit Property value was US$42,615,487 at the valuation date minus the costs of the foreclosure procedure; the net market value of the property totaled US$40,630,184.

In the case of the second and third properties (Guadalajara Properties), which consisted of two adjacent plots of lands with different zoning rights, the Tribunal also contrasted the parties' experts' sales comparison models.[13] In the valuation of the Guadalajara Properties, the Tribunal rejected Claimant's proposition that the two plots of land could be jointly developed as a single mixed-use property, because there was not sufficient evidence that this configuration could be achieved under existing municipal legislation.[14] Thereafter, the Tribunal adjusted Claimant's and Respondent's respective comparable models to determine an average price for the sale of both plots. The Tribunal ruled that the Guadalajara Properties' value was US$28,434,075 at the valuation date minus the costs of the foreclosure procedure; the net market value of the properties was US$27,063,184.[15]

Although the Tribunal found that the market value of the properties minus transaction costs was US$67,693,368, it decided to apply a discretionary 30 percent discount[16] because of the "uncertainties" and "legal risks" arising from the foreclosing actions and the "personal characteristics of the debtors," which were willing to go to great lengths to engage in legal abuses to protect their economic interest. In the Tribunal's view, these obstructions, which were "close to a certainty" in a but-for scenario, would be unrelated to Mexico's breaches of its NAFTA obligations. Consequently, the Tribunal ruled that the investment's but-for value was US$47,000,000 (coincidentally the valuation figure that had been submitted by Mexico).[17]

C. Legal Fees Arising From the Withdrawal of the Foreclosure Proceeding

Claimant additionally sought to be compensated for the legal costs and fees of withdrawing its foreclosure proceedings, which was a condition precedent to institute NAFTA arbitration.[18] According to Claimant, the legal costs and fees caused by such withdrawal could be US$14 million.[19] Mexico, in turn, argued that Claimant had no obligation to withdraw the foreclosure proceedings to observe NAFTA's condition precedents to file for arbitration.[20]

The Tribunal sided with Claimant and ruled that the foreclosure proceedings in Mexico qualified as the type of municipal procedure that NAFTA required to be waived to access treaty arbitration.[21] In addition, the Tribunal established that but for Mexico's conduct, Claimant would not have been forced to withdraw the foreclosure proceedings and be subject to those legal costs and fees.[22]

Since the foreclosure proceedings were still ongoing, the Tribunal decided that full reparation required Mexico to assume the obligation of reimbursing Claimant for the legal costs and fees "established by the Mexican Courts and actually paid by [Claimant] to the [Debtors]."[23] The Tribunal also noted that Claimant had a duty to diligently mitigate its losses and continue to defend the legal costs and fees requested by the Debtors.[24]

D. Expenses Incurred in the Exhaustion of Local Remedies

Finally, Claimant averred that it had to be compensated for the legal costs and fees incurred for the domestic proceedings aimed at annulling the fraudulent scheme.[25] The Tribunal did not rule on Claimant's entitlement to recover its legal costs and fees because it determined that Claimant had failed to submit sufficient evidence to support its claim for the legal costs and fees incurred in domestic proceedings.[26] However, *in dicta*, the Tribunal stated that, in principle, a denial-of-justice claim requires the exhaustion of local remedies and thus, had the Mexican legal system been able to correct its wrong, Claimant would have incurred those legal costs and fees anyway.[27] The Tribunal concluded that the question about recoverability of legal costs and fees was one to be settled by municipal law.[28]

Interest

With regard to the interest rate, Claimant argued that the applicable rate must be the one provided by the Mexican Commercial Code, at 6 percent per year, compounded on a monthly basis. Alternatively, Claimant proposed the application of the 28-day Interbank Equilibrium Interest Rate, which is applied by Mexican courts when they award damages in *amparo* proceedings.[29]

Mexico disagreed and proposed to use the rate of U.S. Treasury bills if the Award were denominated in U.S. dollars, or the rate applicable to *Certificados de la Tesorería de la Federación* if the Award were denominated in Mexican pesos. Mexico also took the position that Claimant should not be rewarded with compound interest and that if it were, compounded interest should accrue annually as opposed to on a monthly basis.[30]

The Tribunal deemed both proposals inadequate. While Claimant asked that an interest rate applicable to Mexican transactions be applied to a U.S. dollar award, Mexico sought to apply a rate that is applicable to the financing of the U.S. government and not to a commercial enterprise.[31] According to the Tribunal, Article 1110(4) of NAFTA mandates the use of a "commercially reasonable rate" if payment is made in a G7 currency such as the U.S. dollar.[32] Therefore, the Tribunal ruled that the applicable rate should be the London Interbank Offered Rate plus 2 percent for six-month deposits denominated in U.S. dollars.

The Tribunal ruled that interest should accrue semiannually from the *dies a quo*, the date of the breach, until the *dies ad quem*, the date of payment to indemnify Claimant adequately.[33]

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1 According to the forged settlement agreement, Claimant consented to the cancellation of the loans and security in exchange for equity interest in one of the Debtors' companies.

2 Decision on Jurisdiction ¶ 266.

3 Award, ¶ 610. The Tribunal's determination is limited to the state courts of Jalisco, which intervened in the domestic judicial fraud, and does not extend to the entire Mexican judicial system.

4 Award, ¶¶ 621-624.

5 Award, ¶ 627.

6 Award, ¶ 631. In reaching this decision, the Tribunal rejected Claimant's proposal of a later valuation date in a scenario in which Claimant foreclosed the mortgages and sold them to third parties. The Tribunal called this proposal purely hypothetical.

7 Award, ¶ 633.

8 Award, ¶ 637. The Tribunal noted that the value of the properties was lower than the owed amount under the loans.

9 Award, ¶ 640.

10 Award, ¶ 644.

11 Award, ¶ 680.

12 Ibid.

13 Award, ¶ 721. In addition to its sales comparison model, Mexico proposed a residual value approach.

14 Award, ¶¶ 738-739.

[15] Award, ¶ 759.

[16] Award, ¶ 770.

[17] Award, ¶¶ 764-766. The Tribunal rejected two additional arguments in which Mexico sought to reduce compensation because of Claimant's equity interest in Debtors' companies (which was acquired through the forged settlement agreement) and the possibility to be compensated in criminal proceedings against the Debtors.

[18] According to NAFTA's Art. 1121, investors must waive their right to initiate or continue claims with respect to the illegal measure disputed in the treaty arbitration, except for proceedings of injunctive, declaratory or other extraordinary relief that do not involve compensation of damages.

[19] Award, ¶ 801. As quantified by the Debtors in the foreclosure proceedings.

[20] Award, ¶ 802.

[21] Award, ¶¶ 815-816.

[22] Award, ¶¶ 825-826, 837.

[23] Award, ¶ 838.

[24] Award, ¶ 839.

[25] Award, ¶ 840.

[26] Award, ¶ 847.

[27] Award, ¶ 848.

[28] Ibid.

[29] Award ¶ 860. *Amparo* proceedings essentially relate to the protection of constitutional rights and often involve granting temporary or definitive injunctions. Mexico's Supreme Court has established that the interest rate applicable to damages caused by injuctions must be equal to Mexico's 28-day Interbank Equilibrium Interest Rate, reflecting "the performance that could have been achieved by the lost amount or what any person could have obtained by depositing such amount in a banking institution."

[30] Award ¶¶ 863-865.

[31] Award ¶¶ 876-877.

[32] Award ¶ 873.

[33] Award ¶¶ 886-889.

LSF-KEB Holdings SCA and others v. Republic of Korea, ICSID Case No. ARB/12/37

Date of the Award
August 30, 2022

The Parties
LSF-KEB Holdings SCA, LSF SLF Holdings SCA, HL Holdings SCA, Kukdong Holdings I SCA, Kukdong Holdings II SCA, Star Holdings SCA, Lone Star Capital Management SPRL and Lone Star Capital Investments S.a.r.l. (jointly, Lone Star or Claimants); Republic of Korea (Respondent)

Sector
Banking

Applicable Treaty
Bilateral investment treaty (BIT) between Korea and Belgium-Luxembourg Economic Union (2011) (2011 BIT)

Members of the Tribunal
V.V. Veeder, QC (president from 2013-2020; resigned); Ian Binnie, C.C., Q.C. (president from 2020 onward); Charles N. Brower (Claimants' appointee); and Brigitte Stern (Respondent's appointee)

Background

LSF-KEB and its co-claimants are subsidiaries of a Texas-based investment fund commonly known as Lone Star. In 2003, Lone Star purchased the Korean Exchange Bank (KEB) for US$1.7 billion, with the goal of overhauling it and selling it at a profit.

In 2007, Lone Star first attempted to sell its KEB stake to the Hong Kong Shanghai Banking Corporation (HSBC) for US$6 billion, which would

have turned a profit of about US$4 billion, according to its own calculations. The sale eventually failed. According to Claimants, the sale failed because of "obstructive delaying tactics" of Korea's Financial Supervisory Commission (FSC), which was tasked with authorizing applications for merger, acquisition and transfer of businesses and management of financial institutions. Claimants argued that the FSC's "wait and see" policy to approve the pending Share Purchase Agreement (SPA) with HSBC was "a pretext to appease hostile public opinion" and exceeded its competences and the law. Respondent defended its approach and denied any responsibility for financial losses due to the failed sale.

In 2008, Lone Star was criminally convicted of stock manipulation in the acquisition of a subsidiary. The conviction triggered a statutory requirement for Lone Star to divest its KEB stake. Lone Star also lost part of its voting rights.

In 2010, Lone Star concluded an SPA to sell its

stake in KEB to Hana Financial Group Inc. and its subsidiary Hana Bank (Hana) for US$4.3 billion (original Hana SPA). In 2012, the FSC approved the sale, subject to Lone Star accepting a price reduction of US$433 million.[1] Eventually, KEB was sold for US$3.5 billion to Hana (amended Hana SPA). According to Claimants, the price reduction was covertly imposed by FSC. They considered that Respondent breached its treaty obligations, in particular its obligation to afford Claimants fair and equitable treatment (FET), including the duty of good faith. Respondent argued that the price reduction was caused by the criminal conviction and estimated that despite the price reduction, Lone Star ultimately made a 171 percent total return on its investment.

Claimants also alleged a violation of the BIT and the tax treaty due to "the unfair and unrelenting attack by the Korean National Tax Service."

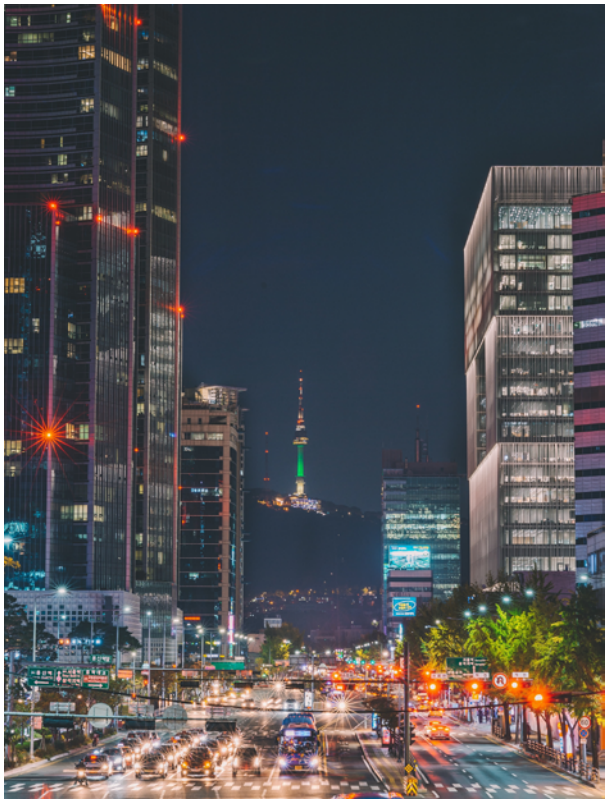
For the alleged damages, interest and tax gross-up relating to the failed stock sale to HSBC, the successful stock sale to Hana, and its tax claims, Claimants sought compensation of approximately US$4.7 billion plus interest.

Jurisdiction and Liability

On August 30, 2022, the arbitral tribunal issued its final award (Award). Claimants invoked protection under the BIT between Korea and Belgium-Luxembourg Economic Union of 1976, the 2011 BIT, and the Korea-Belgium Tax Treaty of 1977.

The Tribunal dismissed the claims that arose under the 1976 BIT because the investments made by Claimants did not fall under the protected categories enumerated in the BIT.[2] For this reason, as protection was inexistent to begin with, the Tribunal also rejected Claimants' argument that the investments were protected during the transitional period from 1976 to 2011.[3] It thereby concluded that it lacked jurisdiction over the claim relating to the planned sale to HSBC, predating March 27, 2011,[4] the date of entry in force of the 2011 BIT. However, the fact that Lone Star asserted that its alleged mistreatment began with the failed HSBC transaction did not mean that the Tribunal lacked jurisdiction over later conduct, which was decided on the basis of the 2011 BIT.

With respect to tax-related claims, the Tribunal found that it lacked jurisdiction under the 1977 Belgium-Korea tax treaty,[5] but it ruled it had jurisdiction based on the 2011 BIT to decide disputes over tax assessments imposed after 2011. Lone Star requested a US$257.4 million tax gross-up, reasoning that the Award would count as corporate income in Belgium and Korea. The Tribunal unanimously rejected this claim on the merits,[6] considering that it "is of dubious legal validity" but in any event fails due to lack of essential evidence.[7] It ruled that Claimants had not established the taxes levied on the Award,[8] since



(i) following *CSOB v. Slovakia*, taxes should not be taken into account when determining compensation,[9] (ii) Lone Star's evidence was unpersuasive,[10] (iii) Claimants' quantum expert did not have expertise on Belgian tax law and provided an "insufficient basis" for gross-up to compensate for potential taxes,[11] and (iv) a ruling from the Belgian Tax Ruling Commission forming part of Claimants' evidence was argumentative and without a transparent basis.[12]

Furthermore, the Tribunal rejected Claimants' allegation of wrongful interference by the FSC in KEB's dividend policy[13] and Claimants' claim for expropriation in relation to Respondent's interference with Claimants' disposal of its KEB shares, which it considered "ill-founded."[14]

However, the Tribunal by majority considered that Respondent was liable for not acting in good faith toward Claimants. Lone Star based its claim, among others, on Respondent's violation of its treaty obligation of FET toward investors.[15] The Tribunal agreed with this argument and found that despite Lone Star's misconduct, the FSC still had an obligation to process the application for the sale to Hana in good faith and expeditiously, but instead of doing so, it acted "entirely in (...) its own institutional self-interest."[16] Moreover, the Tribunal rejected Respondent's argument that the chain of causation had been broken by Lone Star's agreeing to the amended Hana SPA with its imposed price reduction. Nevertheless, it considered that Lone Star's criminal conviction also "exposed LSF-KEB to the orchestration of the price reduction."[17] It thus considered that the price reduction suffered by Lone Star (net price reduction of US$433 million) was caused by "separate but entangled conduct of both Lone Star and the FSC."[18] The Tribunal, by majority, found both parties liable, and on account of Lone Star's contributory fault, it reduced quantum by 50 percent (US$216.5 million).

Quantum

A. Valuation Methodology

The Tribunal considered KEB's share price "easily ascertainable," as the stock is traded on the open market in Korea. However, the Tribunal also acknowledged that Lone Star's majority shareholding was worth "much more" than its market price, due to its controlling stake in the bank.[19]

B. Valuation

Claimants supported their claims on the principle provided in the *Chorzów Factory* case, which states that "reparation must, as far as possible, wipe out all the consequences of the illegal act and reestablish the situation which would in all probability, have existed if that act had not been committed."[20] Claimants' quantum expert considered the original price of approximately US$6 billion fixed in the HSBC SPA was a fair market value of Lone Star's controlling shares in KEB at that point of time. He argued that without Respondent's interference, Lone Star would have made US$6 billion in gross proceeds resulting from that sale, which after adjusting for proceeds from the sale to Hana, taxes and interest caused Lone Star lost profits of approximately US$2.9 billion. The Tribunal rejected this starting point for the calculation of damages based on its jurisdictional finding regarding the planned HSBC transactions.[21]

The Tribunal considered that Lone Star's losses corresponded to the difference in price between the original Hana SPA (US$4.3 billion) and the amended Hana SPA (US$3.5 billion), which had been caused in part by FSC's bad faith conduct–that is, a gross reduction of US$832.2 million. It then discounted the mid-2011 dividend of US$400.2 million that Lone Star received and that it considered mitigated Lone Star's losses. As a result, the Tribunal evaluated Claimants' net loss at US$33 million, which includes interest from May 24, 2011, to September 30, 2011.[22]

C. Apportionment

In light of both parties' wrongdoing, the Tribunal considered that the loss of US$433 million is "not capable of disaggregation into bits that can be assigned to one side or other."[23] It therefore treated the loss as a lump sum and considered that both parties were equally at fault.[24] Thus, it awarded Claimants compensation in the amount of US$216.5 million.

Interests and Costs

The Tribunal held that Claimants were entitled to pre- and post-judgment interest until date of payment.[25] Claimants sought compound interest from December 3, 2011, until the date of payment at the average one-month U.S. Treasury rate.[26] Respondent considered Claimants not entitled to compound pre-award interest but made no observations regarding the rate, its source or the annual compounding period.[27] The Tribunal agreed with Claimants, considering the rate and compounding period claimed "appropriate" and "in the absence of any objection by the Respondent accepts the U.S. Treasury bill benchmark as appropriate."[28]

Finally, the Tribunal exercised its discretion in the allocation of costs and ruled that considering the "divided success," each party should bear its own costs and attorney fees.[29] The costs of the arbitration, paid in advance in equal parts by the parties, should be shared as already done.[30]

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1 The gross price reduction was US$832.2 million (the difference between the original Hana SPA for US$4.3 billion and the amended Hana SPA for US$3.5 billion). However, since Lone Star received a midyear dividend of US$400.2 million in 2011, the actual net loss due to the price reduction was US$433 million.

2 Award, ¶ 280.

3 Award, ¶ 281.

4 Award, ¶ 291.

5 Award, ¶ 296, 372.

6 Award, ¶ 296, 372.

7 Award, ¶ 909-910.

8 Award, ¶ 904.

9 Ibid.

10 Award, ¶ 905; *Ceskoslovenská Obchodní Banka, A.S. v. Slovak Republic*, ICSID Case No. ARB/97/4, Award, 29 December 2004, ¶ 367.

11 Award, ¶ 907.

12 Award, ¶ 908.

13 Award, ¶¶ 691-694, 728.

14 Award, ¶¶ 772-774.

15 Award, ¶¶ 247, 713.

16 Award, ¶ 741.

17 Award, ¶ 800.

18 Award, ¶¶ 799, 804-805.

19 Award, ¶ 7.

20 Award, ¶ 889; *Factory at Chorzów (Germany v. Poland)*, PJIJ, Judgment No. 13, 13 September 1928, p. 47.

21 Award, ¶ 892, more particularly footnote 1183.

22 Award, ¶ 892.

23 Award, ¶ 894.

24 Award, ¶¶ 856-896.

25 Award, ¶ 921.

26 Award, ¶ 911.

27 Award, ¶ 917.

28 Award, ¶ 921.

29 Award, ¶¶ 924-925.

30 Award, ¶¶ 926-927.

Niko Resources (Bangladesh) Ltd. v. Bangladesh Oil Gas and Mineral Corporation (Petrobangla), Bangladesh Petroleum Exploration and Production Company Limited (Bapex) (II), ICSID Case No. ARB/10/18

Date of the Award
September 24, 2021 (Award)

Annulment
Pending (ICSID *ad hoc* committee: Eduardo Zuleta, Claudia Annacker and Makhdoom Ali Khan)

The Parties
Niko Resources (Bangladesh) Ltd. (Niko or Claimant); Bangladesh Oil Gas and Mineral Corporation (Petrobangla) and Bangladesh Petroleum Exploration and Production Company Limited (Bapex) (jointly, Respondents)

Sector
Oil and Gas

Members of the Tribunal
Michael Schneider (president), Jan Paulsson (Claimant's appointee) and Campbell McLachlan (Respondents' appointee)

Background

This long-running dispute is one of several International Center for Settlement of Investment Disputes (ICSID) arbitrations launched by Niko and its affiliates concerning the company's operations in Bangladesh.

Claimant, a Canadian-owned oil company, entered into a joint venture agreement (JVA) with Bangladeshi state-owned oil company Bapex to develop multiple gas fields. After the joint venture began producing gas, it negotiated and executed a gas purchase and sales agreement (GPSA) with Bapex's parent company, Petrobangla.

In 2005, there were two explosions in the northern gas field that Claimant operated, causing damage to the local population and the environment.[1] A few months after the explosions, Claimant gifted a luxury car worth US$140,000 to the then-Bangladeshi energy minister and also paid for his trips to New York and Calgary. The Bangladeshi official resigned when these gifts were made public. Niko would later plead guilty to bribing the minister in a criminal probe brought by Canadian law enforcement.

After the explosions, local courts issued multiple injunctions forbidding the Bangladeshi government from making any payments to Niko, even for gas produced from fields that were not involved with the explosions.[2] The first of these court orders was issued in 2005 (2005 Injunction) and was repeatedly extended.[3] In 2007 and 2008, Niko requested payment for the outstanding amounts; Petrobangla ignored the requests.[4]

In 2010, Claimant initiated two arbitrations against Bangladesh and its state-owned oil companies. The parties selected identical tribunals to hear the parallel arbitrations. In *Niko v. Bangladesh (I)*, Claimant sought a declaration that it was not liable for the two well explosions. In *Niko v. Bangladesh (II)* — the instant case discussed below — Claimant sought its outstanding payments owed for gas delivered under the GPSA. In 2019, another Niko affiliate, Niko Exploration (Block 9), filed a third arbitration against Bangladesh for withheld payments related to another gas field.

Jurisdiction and Liability

On August 19, 2013, the Tribunal issued its Decision on Jurisdiction, affirming jurisdiction over Claimant's claims but declining jurisdiction over one of the named respondents, Bangladesh.[5] The Tribunal found the state-owned oil companies were not acting as agents for the state when signing the JVA or the GPSA, so the state could not be joined as a party to these contract disputes. The Tribunal rejected Respondents' corruption-based jurisdictional arguments. The Tribunal did not find evidence of corruption in Claimant obtaining the JVA (which was signed years before the bribes), and there was no indication the bribes influenced the GPSA, because the Bangladeshi official resigned shortly after the gifts were given, the state entities were fully aware of the actions and the state entities decided to sign the GPSA 18 months later despite those revelations.[6]

On the merits of the claim, the Tribunal issued several decisions[7] finding that the GPSA was valid and Petrobangla owed Claimant for the gas it received from November 2004 to April 2010. The Tribunal issued multiple decisions because Respondents did not comply with the Tribunal's orders, allegedly because of contradictory rulings from local courts in Bangladesh.

In 2014, the Tribunal issued its first decision, ordering Petrobangla to pay Niko for the unpaid quantities of gas.[8] In a subsequent decision, the Tribunal ordered the monies to be deposited in an escrow account — to be held in reserve as a possible offset for damages that Niko might owe Respondents for the two explosions being considered in *Niko v. Bangladesh (I)*.[9] When Respondents refused to pay any amounts into the escrow account unless the Bangladeshi courts modified the 2005 Injunction, the Tribunal issued a third decision, ordering Respondents to make a direct payment to Claimant for the money owed.[10]

In 2016, Respondents petitioned the Tribunal to revisit the state's allegations of corruption and to reconsider the Tribunal's prior decisions ordering them to pay for the gas shipments. The Tribunal reheard the corruption claims that had previously been rejected in the Tribunal's 2013 jurisdiction decision. This separate phase addressing Respondents' latest corruption allegations lasted for three years, from 2016 to 2019, and concluded when the Tribunal issued a 580-page decision finding that the JVA and GPSA were not tainted by corruption.[11]

After the rejection of Respondents' corruption claims, Niko petitioned the Tribunal for a final, binding award on the amounts payable for the gas delivered under the GPSA.

Quantum

The quantification of damages was straightforward since both parties agreed on the amount owed. The claim involved 66 unpaid invoices for the delivery of gas from November 2004 to April 2010. Claimant adopted the figures set out in Respondents' pleadings — amounting to US$25,312,747 plus Bangladeshi taka (BDT) 139,988,337 (approximately US$1.3 million).[12] These amounts were undisputed from the Tribunal's initial decision in 2014 to the final Award issued in 2021.[13]

Interest

In awarding interest, the Tribunal was guided by the law of Bangladesh and reports from the Bangladesh Export Development Fund concerning foreign currency facilities to determine what would be "a reasonable rate in the context of commercial conditions in Bangladesh."[14] In its earlier decisions, the Tribunal ordered Petrobangla to pay interest at the following rates:

(i) The six-month London Interbank Offered Rate (LIBOR) plus 2 percent for the U.S. dollar amounts

(ii) Five percent for the Bangladeshi taka amounts[15]

As of 2015, the Tribunal had ordered the interest to be compounded annually. The Tribunal confirmed these interest rates found in its prior decisions. Interest ran for each invoice starting 45 days after delivery of the invoice.

The parties agreed that the interest that had accrued on the invoices through November 19, 2020, amounted to US$13,195,703 and BDT 116,852,605 (approximately US$1.1 million).[16]

By the time of the final Award, LIBOR was being phased out, so the parties agreed to replace LIBOR with the Secured Overnight Financing Rate (SOFR).[17] Respondents agreed that SOFR reflected "commercially accepted ways in which everybody is dealing with the disappearance of LIBOR."[18]

Unpaid amounts after November 20, 2020, would be subject to the 180-day average SOFR plus 2 percent for the U.S. dollar amounts and 5 percent for the Bangladeshi taka amounts.[19]

Costs

A significant portion of the Award was related to the parties' costs. The Tribunal had to account for a complex situation where several of the arbitration's most intensive phases (like the jurisdictional phase and the rehearing of the corruption allegations) involved crosscutting issues that impacted both this arbitration and the parallel *Niko v. Bangladesh (I)* arbitration.

Claimant sought Canadian (CAD) 3.2 million (approximately US$2.3 million) plus US$224,000.[20] To single out the costs devoted to this arbitration, Claimant organized its costs into three phases and then requested either 100 percent of the phase's costs or 50 percent of the costs. The approximate figures of

Claimant's costs equated to:

(i) Jurisdiction, requesting CAD 330,000 and US$83,200, which represented *half* of the legal fees for that phase

(ii) Merits, requesting CAD 1.2 million and US$86,000, which represented *all* of the costs for that phase

(iii) Corruption claim, requesting CAD 1.6 million and US$55,000, which represented half of the costs for that phase

Respondents, in contrast, only sought US$457,000.[21] Respondents also divided their costs into a jurisdiction phase and a merits phase. Respondents similarly thought 50 percent of the costs incurred during the jurisdictional phase and 100 percent of the costs incurred during the merits phase should be attributed to this arbitration.

The Tribunal noted the significant difference in the amount of the parties' claimed costs. The Tribunal observed that Respondents only listed fees and costs for counsel before 2015 (e.g., not listing the fees and costs for Foley Hoag, which represented Respondents for more than six years).[22] Respondents did not consider the corruption claim phase (2016-2019) to be pertinent to the arbitration regarding outstanding gas payments. Respondents argued that the Tribunal should only include those costs in a final award that covered both arbitrations. The Tribunal disagreed based on its reading of Article 61(2) of the ICSID Convention, because the arbitrations costs "shall form part of the award" and the Tribunal determined it had no discretion to award partial costs for the current arbitration while reserving a portion to be awarded at a later date.[23]

A. Allocation of Costs Related to This Arbitration

The Tribunal agreed with the parties that 50 percent of the jurisdictional phase was attributable to this arbitration and 100 percent of the merits was attributable to the gas payments dispute.[24] As to the corruption claim phase (which Claimant estimated at 50 percent and for which Respondents advocated for its total exclusion), the Tribunal agreed more with Respondents, finding that the corruption claims brought by Respondents dealt primarily (though not exclusively) with the other arbitration because of the focus on the JVA. The Tribunal identified only a handful of pages exclusively dealing with the GPSA in the Tribunal's 580-page corruption claim decision, though recognizing that other sections did involve the GPSA indirectly. By its own measure, the Tribunal estimated that 15 percent of its efforts during this phase were directed toward the GPSA.[25] Without additional evidence from the parties about the allocation of their time and effort, the Tribunal determined that the costs for this phase were estimated at 15 percent of the total fees and costs incurred during this time frame.[26]

B. Evidence of Costs

Neither of the parties provided underlying documentation. Respondents provided lump-sum figures, whereas Claimant went into more detail, providing tables listing high-level information about each claimed invoice (date, amount, sender, etc.).[27] The Tribunal accepted the figures as contained in the parties' submissions.

C. Allocation of Costs Between the Parties

The Tribunal awarded costs based on the relative success of the parties on each phase of the dispute (jurisdiction, merits and corruption claims).

For the jurisdictional phase, the Tribunal determined that each party should bear its own legal costs because each side was partially successful; Claimant had ultimately succeeded, but Respondents' objection to the Tribunal's jurisdiction over Bangladesh was a significant win.[28] For the merits phase, the Tribunal awarded Claimant all of its costs.[29] The Tribunal found no reason to reduce Claimant's requested fees. The

Tribunal also found that comparing Claimant's fees with Respondents' claimed fees was not advisable because Respondents underreported their actual expended costs. For the corruption claims, the Tribunal awarded Claimant the full 15 percent of the costs attributable to this arbitration because Claimant fully prevailed on its claim.

Ultimately, the Tribunal awarded Claimants CAD 1,737,592 and US$526,258.58 in costs.

D. Interest on Costs

The Tribunal awarded post-award interest on costs because of the protracted nature of the dispute, which lasted more than a decade. The Tribunal based its decision on Article 61(2) of the ICSID Convention, finding the Tribunal not only had the power to decide who should bear those costs but also had the power to decide when the awarded costs must be paid "and the consequences if the payment is not made" in the time frame allotted.[30]

The Tribunal ordered interest at a rate of 180-day average SOFR plus 2 percent, with the interest accruing after a 45-day grace period.

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1 Award, ¶¶ 28-29.

2 Award, ¶¶ 31-33, 41-42.

3 Award, ¶ 31.

4 Award, ¶¶ 37-38.

5 Award, ¶ 51.

6 Award, ¶ 53.

7 The Tribunal styled these rulings "decisions" rather than "awards" likely because of the ongoing nature of the other concurrent arbitration, *Niko v. Bangladesh (I)*. See Award, ¶ 128.

8 Award, ¶ 71.

9 Award, ¶ 84.

10 Award, ¶¶ 86-129.

11 Award, ¶¶ 169-173.

12 Award, ¶¶ 57-58, 71. Claimant originally calculated the amounts at US$25,313,920 and BDT 139,993,479; Claimant decided the discrepancy was so small it was "not worthwhile to debate them."

13 Award, ¶¶ 71, 375

14 Award, ¶ 370.

15 Award, ¶¶ 250.

16 Award, ¶ 251.

17 Award, ¶¶ 186-187.

18 Award, ¶ 256.

19 Award, ¶ 257.

20 Award, ¶¶ 267-271.

21 Award, ¶¶ 272-276.

22 Award, ¶¶ 293, 276.

23 Award, ¶¶ 292-305.

24 Award, ¶¶ 306, 310.

25 Award, ¶ 326.

26 Award, ¶ 327.

27 Award, ¶¶ 287, 291.

28 Award, ¶¶ 346-350.

29 Award, ¶¶ 351-359.

30 Award, ¶ 371.

PACC Offshore Services Holdings Ltd. v. United Mexican States, ICSID Case No. UNCT/18/5

Date of the Award
January 11, 2022

The Parties
PACC Offshore Services Holdings Ltd. (Claimant); United Mexican States (Respondent)

Sector
Offshore Marine Services Industry, Oil and Gas, Bareboat Charter Services

Applicable Treaty
Agreement between the Government of the United Mexican States and the Government of the Republic of Singapore on the Promotion and Reciprocal Protection of Investments (signed on November 12, 2009; entered into force on April 3, 2011)

Members of the Tribunal
Dr. Andrés Rigo Sureda (president), Prof. W. Michael Reisman (Claimant's appointee) and Prof. Philippe Sands (Respondent's appointee)

Background

The dispute relates to bareboat charter services that PACC Offshore Services Holdings Ltd. (POSH or Claimant) provided to Oceanografía, S.A. de C.V. (OSA), which in turn sub-chartered them to Petróleos Mexicanos (PEMEX), a Mexican state-owned oil and gas company. Through a series of acts and omissions by authorities of the United Mexican States (Mexico or Respondent) — which included a ban on entering into public contracts, criminal investigations, seizure of OSA's assets and seizure of POSH's vessels — POSH claimed that Respondent unlawfully expropriated, failed to accord fair and equitable treatment to, and failed to provide full protection and security to its investment in Mexico. Claimant sought damages of approximately US$250 million for these alleged breaches of the Mexico-Singapore bilateral investment treaty (BIT).

According to Claimant, in 2011, PEMEX was about to engage in an expansion process that would require additional offshore support vessels. POSH, a Singaporean provider of offshore marine solutions, intended to provide such support vessels, and it engaged OSA, a Mexican provider of oil engineering services, because it needed a Mexican partner to participate in PEMEX tenders. This led to a structure in which POSH provided bareboat charter services to OSA, which in turn sub-chartered these services to PEMEX.

In August 2011, Claimant set up a joint venture in Mexico and acquired six vessels from related entities through bridge loans in the amount of US$142.75 million. In order to secure these loans, Claimant and OSA agreed to security in the form of an irrevocable trust (Irrevocable Trust), with POSH as the primary beneficiary, to receive all payments owed by PEMEX in connection with the OSA-PEMEX contracts. Between late 2011 and mid-2012, Claimant chartered four additional vessels, for a total of 10 ships.

According to Respondent, the Auditoría Superior de la Federación discovered various irregularities concerning OSA. In early 2014, Mexican authorities concluded that OSA failed to obtain mandatory insurance policies, which resulted in a ban preventing OSA from entering into new contracts with any public entity (sanction). The sanction led to further investigations, including a criminal complaint by the Mexican bank Banamex against OSA for US$400 million on account of allegedly forging work estimates

and approvals from PEMEX to obtain cash advances from the bank. This resulted in the seizure of OSA assets, termination of loans, a detention order seizing the 10 vessels that Claimant chartered to OSA, and an order blocking OSA, POSH and POSH subsidiaries from entering into new contracts with the Mexican government. By March 2014, the operation was essentially shut down, a series of criminal investigations were pursued against POSH's and OSA's managers, and Mexican authorities commenced insolvency proceedings against OSA. In this context, all payments to the Irrevocable Trust were diverted to pay OSA creditors instead of POSH. Claimant's vessels were released four to five months after their seizure in the midst of this process.

Thus, the dispute centered on Claimant's allegations that these measures attributable to the Mexican government resulted from an arbitrary campaign against OSA in violation of the BIT. Conversely, Mexico alleged that the Tribunal lacked jurisdiction over the dispute and, in the alternative, that these claims should be denied on the merits.

Jurisdiction and Liability

Respondent raised a jurisdiction challenge on the grounds that (i) Claimant failed to establish a legal causal link between its investments and the government's alleged measures; (ii) its contracts with OSA were not an investment under the BIT; and (iii) any claims were time-barred because Article 11(8) of the BIT requires that claims be initiated within three years from the date on which Claimant first became aware of the existence of the alleged measures, and because the Notice of Intent was delivered on May 4, 2017, any measures prior to May 4, 2014, would be time-barred.

Essential to the Tribunal's analysis was the relationship (or lack thereof) between POSH and OSA. Notably, the Tribunal found that OSA was not an investment or investor as defined in BIT but a contractual counterparty to POSH, and that Claimant failed to address the effect of its connection to OSA on the investment. In addition, the Tribunal noted that OSA was sanctioned for fraud in the U.S., which included a cease-and-desist order from the U.S. Securities and Exchange Commission for allegedly submitting fraudulent invoices to obtain financing from Banamex. The Tribunal thus found that Mexico was not only entitled to investigate OSA but was in fact required to take certain investigatory and other measures to protect the rule of law.

The crux of the jurisdictional case was whether Claimant was able to show "proximate causation" or a "legally significant connection" between the acts attributable to the Mexican government and its alleged losses. Citing to *Methanex v. U.S.A.*, the Tribunal acknowledged that an endless chain of consequences may flow from any government decision and that treaties cannot permit an infinite number of investment claims. Therefore, the Tribunal held that there must be "some degree of direct connection between the contested measure and the loss claimed"[1] and that Claimant is only affected indirectly through its contractual connection with OSA such that OSA's losses are not Claimant's losses.

The only claims that survived the jurisdictional challenge as having a "legally significant connection" to the acts attributable to the Mexican government were those pertaining to (i) the diversion of the Irrevocable Trust to pay OSA creditors instead of POSH, (ii) the detention of the 10 vessels and (iii) a blocking order preventing POSH's subsidiaries from entering into new contracts with the Mexican government.[2] Regarding these claims, the Tribunal held that while the cutoff date of the three-year period was May 4, 2014, the government's acts related to these three sets of claims were composite acts of a continuing character such that even though

they may have been taken before the cutoff date, their effects extended beyond the cutoff date.

Turning to the merits, the Tribunal found that Mexico was responsible for the acts and omissions of its agencies and instrumentalities under Article 4 of the International Law Commission's Articles on Responsibility of States for Internationally Wrongful Acts, and it reviewed the surviving claims in turn.

As to the first surviving claim (i.e., the diversion of the Irrevocable Trust), the Tribunal relied on *Eli Lilly & Co. v. Canada* to hold that only in "very exceptional circumstances" will the acts of a court violate international law and that a claimant must show "a 'notoriously unjust' or 'egregious' administration of justice 'which offends a sense of judicial propriety.'"[3] Here, the Tribunal found that the purpose of the Irrevocable Trust was to guarantee all of OSA's debts, not just POSH's loans, such that the Mexican courts' decisions to use the Irrevocable Trust's assets to pay OSA's creditors in bankruptcy were not "egregious or shocking."[4] Therefore, because Claimant had access to Mexican courts and those courts' decisions to assign moneys received during the pre-insolvency suspect period were reasonable, Mexico did not violate the BIT.

As to the second surviving claim (the detention of Claimant's 10 vessels), the Tribunal relied on *LG&E v. Argentina* for the proposition that expropriation must be "permanent" and "cannot have a temporary nature."[5] Here, because the detention was for a period of four to five months and there was no evidence that the deprivation was ever intended to be permanent, there was no expropriation of the vessels, which remained under POSH's title. However, precisely because the vessels were not OSA's property — which Mexico already knew or should have known, since the ownership information for the vessels is instantly available to Respondent — the Tribunal held that this order was "arbitrary, grossly unfair and unjust, and for this reason breached the applicable standard requiring the Respondent to grant the Claimant fair and equitable treatment."[6]

As to the third and last surviving claim (the order blocking POSH's subsidiaries from contracting directly with PEMEX), the Tribunal held that because all PEMEX contracts go through a public bidding process, POSH did not have an investment right to contract with PEMEX. Without written evidence of any promise ever being made to POSH that it would receive PEMEX contracts without participating in the public bidding process, Claimant failed to establish a right that could be subject to expropriation.[7]

Therefore, the Tribunal rejected all of Claimant's claims except for a period of four to five months in which Claimant's vessels were unlawfully detained by the Mexican government.

Quantum

Against the jurisdictional and substantive background above, the only damages the Tribunal had to assess were the consequences of the detention of Claimant's vessels for a period of four to five months in 2014. Claimant sought two types of damages: (i) US$11.2 million in lost charter hire for the period in which the vessels were detained and (ii) US$2.1 million in demobilization fees and repair costs of the vessels.[8] Conversely, Respondent observed that Claimant had not deducted the operating costs of the estimated lost charter hire and that there was no reason to assume that it would be able to charter 100 percent of the vessels for the totality of the detention period, so the appropriate estimate should have been US$6.7 million as opposed to US$11.2 million. In addition, Respondent observed that PEMEX had no obligation to pay for demobilization fees and repair costs, so those figures should be disregarded in their entirety.

The Tribunal first stated that there should be some "economic consequence for both the period of detainment and uncertainty surrounding the release date." As even Respondent agreed, if the Tribunal finds that the detention order was unlawful, "Respondent acknowledges that it would be responsible for any damages flowing from that detention."[10] The Tribunal agreed with Respondent's assumption that the detained vessels would be under a new contract for 80 percent of the detention period, that operating cost must be deducted, that demobilization fees and repair costs were not an obligation attributable to PEMEX, and, therefore, Claimant's total damages were US$6.7 million.[11]

Interest

While the Tribunal hints at a distinction in the treatment of interest for a case of expropriation and a case for unfair treatment,[12] the parties have not raised any such distinction in their arguments, and thus the Tribunal will apply the requisite interest "at a commercially reasonable rate" for a case of FET violation as it would to a case of expropriation. Claimant requested interest at the London Interbank Offered Rate (LIBOR) plus 12 percent or, in the alternative, 4 percent, and Mexico argued that LIBOR without added percentage points would be a commercially reasonable rate.[13] The Tribunal held that Claimant failed to show the reasonableness of adding 12 or 4 percentage points and thus concluded that LIBOR is a commercial rate.

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1 Award, ¶. 146.
2 Award, ¶ 150.
3 Award, ¶ 228.
4 Award, ¶ 243.
5 Award, ¶ 245.
6 Award, ¶ 259.
7 Award, ¶ 250.
8 Award, ¶¶ 261-263.
9 Award, ¶ 267.
10 Award, ¶ 269.
11 Award, ¶ 274.
12 Award, ¶ 275.
13 Award, ¶ 276.

RENERGY S.à.r.l. v. Kingdom of Spain, ICSID Case No. ARB/14/18

Date of the Award
May 6, 2022

The Parties
RENERGY S.à.r.l. (Claimant or RENERGY); Kingdom of Spain (Respondent or Spain)

Sector
Renewable Energy, Wind Energy, Solar Energy

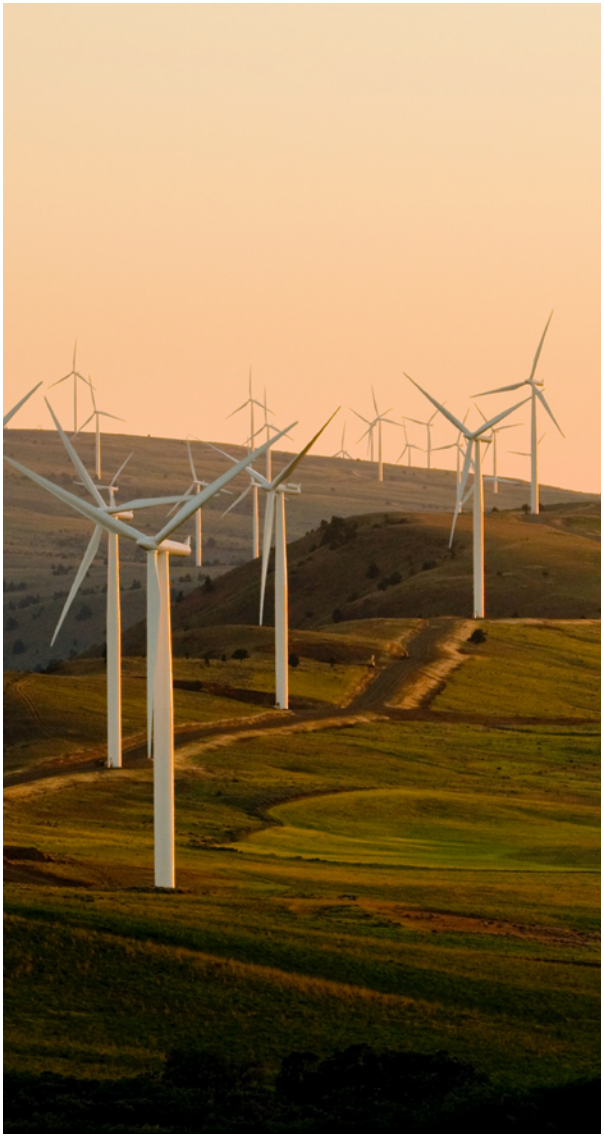
Applicable Treaty
Energy Charter Treaty (ECT)

Members of the Tribunal
Judge Bruno Simma (president), Prof. Christoph H. Schreuer (Claimant's appointee) and Prof. Philippe J. Sands (Respondent's appointee)

Background

On November 6, 2007, Claimant acquired a 50 percent indirect shareholding interest in three wind farms in Spain.[1] After indirectly owning the wind farms for more than 10 years, on December 21, 2017, Claimant transferred its indirect 50 percent equity interest in the wind farms for a price of €9 million; it contractually agreed to retain its rights to any ECT claims and actions against Spain.[2]

On November 21, 2007, Claimant purchased a 33.33 percent shareholding interest in Ibereolica Solar S.L. (Ibereolica Solar), which indirectly owned two solar photovoltaic (SPV) plants in Spain (Olivenza and Moron; together, the CSP Plants).[3] Eventually, Claimant itself came to hold an indirect shareholding in the CSP Plants of 17.92



percent.[4] On March 22, 2018, Ibereolica Solar sold its shareholding interest in the CSP Plants to a third party but again contractually agreed to retain all of its rights over any ECT claims and actions against Spain.[5] The purchase price for the CSP Plants was €11,108,812.20 for Moron and €9,802,179.21 for Olivenza, plus additional deferred payments of €2,421,055.24 for Moron and €2,487,588.45 for Olivenza.[6]

Claimant's three wind farms and the two CSP Plants qualified for feed-in tariffs under Spain's

Royal Decree 436/2004 (RD 436/2004) and Royal Decree 661/2007 (RD 661/2007) (together, the old regulatory regime, or ORR). Under RD 436/2004 and RD 661/2007, Claimant's plants also maintained the right to sell the entire amount of energy they produced, according to the market plus feed-in tariff price, which Spanish regulators updated on a quarterly basis according to domestic inflation.[7]

Starting in 2012, Spain enacted a series of legislative changes to the ORR, which modified the feed-in tariffs that Claimant's plants had qualified for under RD 436/2004 and RD 661/2007, and instead set a cap on the total amount of electricity that the plants could sell annually for the market plus tariff price.[8] The primary piece of legislation enacting these changes was Royal Decree 413/2014 (RD 413/2014).[9] Additionally, Spain promulgated a 7 percent "tax on the value of electric power generation" (referred to by its Spanish acronym TVPEE), and one of the Spanish regions in which Claimant owned wind farms, Castile and Léon, adopted a "tax on the environmental effects (TEE) caused by [...] wind farms" (together with the rest of the disputed measures, the new regulatory regime, or NRR), both of which allegedly decreased the revenue of Claimant's plants.[10] Claimant alleged that all of Spain's changes to the ORR caused it damages of €151 million.[11]

Jurisdiction and Liability

Spain advanced three objections to the Tribunal's jurisdiction over Claimant's claims. First, Spain asserted that, according to EU law and the Court of Justice of the European Union decisions in *Slovak Republic v. Achmea* and *Republic of Moldova v. Komstroy*, the Tribunal lacked jurisdiction over Claimant's claims because Claimant was an EU "citizen" investing in Spain, an EU member state.[12] The Tribunal rejected this argument. It held that Article 16 of the ECT, the treaty's conflicts provision, guaranteed Claimant access to any "more favourable" rule contained within the ECT and specifically those rules related to the "settlement of disputes."[13] Thus, the Tribunal concluded that even if it "had to resolve a conflict of laws regarding its jurisdiction, Article 16 ECT would decide that conflict in favour of Article 26 ECT," the ECT's dispute resolution provision.[14]

Second, Spain challenged the Tribunal's competence to hear Claimant's claims regarding "certain assets," namely "returns," "rights conferred by law or contract" and "interests."[15] Specifically, Spain contended that Claimant could only claim for damage resulting from the "loss of value of its indirect participation in the capital of the SPVs [owning the wind farms and CSP Plants] caused by the Disputed Measures."[16] To the contrary, Claimant argued that, according to the plain definition of "Investment" under Article 1 ECT, its investment included not just its shareholding in the local Spanish SPVs but also "subordinated debt interests" and the "returns, in the SPVs."[17] The Tribunal agreed with Claimant that Article 1(6) of the ECT offered a "non-exhaustive list of assets that the investor may own or control directly," including "tangible and intangible, and movable and immovable, property, and any property rights such as leases, mortgages, liens, and pledges," as well as "claims to money and claims to performance pursuant to contract having an economic value and associated with an "[i]nvestment" and "[r]eturns."[18] After noting that non-ECT investment tribunals had adopted "mixed" views on whether the rights of indirect investors go beyond what can be directly derived from their shareholding, the Tribunal declined to characterize Spain's argument on this point as a jurisdictional objection.[19] Instead, the Tribunal observed that Respondent had taken issue with the "question of how [RENERGY's] claims are to be characterized and computed."[20] Thus, the Tribunal dismissed Spain's second jurisdictional question and

stated that it would address the issue of which direct and indirect assets RENERGY could claim damages for in its decision on quantum.[21]

Third, and finally, Spain challenged the Tribunal's competence to decide Claimant's claim that the TVPEE and TEE had breached the ECT's fair and equitable treatment (FET) provision, Article 10(1), and claimed that, according to the ECT's tax carve-out provision, Article 21(1), the ECT "does not create any obligations with respect to taxation measures."[22] Claimant, to the contrary, asserted that under the ECT's "clawback" provision for taxation measures, Article 21(3), the Tribunal could assert jurisdiction over the alleged breaches caused by the TVPEE and the TEE because they were taxes "other than [...] on income or on capital."[23] The Tribunal agreed with Spain that the TVPEE and TEE were properly considered taxes under Article 21(1) of the ECT and that they were not subject to the treaty's clawback provision, Article 21(3).[24] Therefore, the Tribunal upheld Spain's objection to jurisdiction regarding the TVPEE and TEE and concluded it could not consider whether either of these taxation measures breached the ECT's FET clause.[25]

On liability, the majority of the Tribunal, Judge Bruno Simma (president) and Claimant's appointee, Prof. Schreuer, held that the changes Spain imposed on the ORR defied Claimant's legitimate expectations of "relative stability" in violation of the ECT's FET provision, Article 10(1).[26] The majority held that Spain "materially changed" its understanding of the reasonable rate of return originally guaranteed to Claimant's plants by the ORR according to RD 436/2004 and RD 661/2007.[27] It explained that Spain had "switched the remunerative paradigm by transforming a system in which investors were incentivized to maximise production to a system in which production level was much less important."[28] Accordingly, the majority concluded that the changes imposed by the NRR had a "severe adverse economic impact" on RENERGY's investments and were "adopted without any transitional period."[29] However, the majority denied Claimant's additional claims concerning full protection and security, non-impairment, and the umbrella clause under ECT Article 10(1) as well as the expropriation claim under ECT Article 13(1).[30]

In his dissent, Prof. Sands explained that he felt it was "misconceived for the majority, in exploring the ECT obligation, to have located its analysis solely within the framework of legitimate expectations."[31] He asserted that the majority's ruling "falls foul of the principle that it is not the function of an arbitral tribunal to make use of an investment treaty as a form of insurance policy" and that a tribunal should "carry out an objective assessment of an investor's expectations and not merely accept them as being protected under the treaty."[32] Prof. Sands concluded that he would have denied RENERGY's claim of breach of the ECT's FET standard by the NRR, since RENERGY's losses fell within "the acceptable margin of change" when analyzed in context "against the background of the economic and environmental challenges faced by Spain."[33]

Quantum

The majority of the Tribunal also split with Prof. Sands regarding quantum. The majority agreed with RENERGY that, in view of the lack of specific provisions in the ECT on the standard for compensation (except in the case of lawful expropriations), principles of customary international law should guide its assessment of quantum.[34] The majority stated that based on the International Law Commission Draft Articles on State Responsibility for Internationally Wrongful Acts, Article 36(1) and the Permanent Court of International Justice ruling in *Chorzów Factory*, the applicable principle under customary international law was that of "full reparation, wiping out the consequences of the illegal act."[35]

However, the majority did not agree with Claimant that *Chorzów* required "constructing a but-for scenario" in which the ORR would have "remained unchanged."[36] Instead, the majority took the view that since "Respondent breached the FET standard by exceeding the acceptable margin of legislative change" and thus "violat[ed] Claimant's legitimate expectation of Relative Stability," the "illegality of the Disputed Measures … is limited to that portion which exceeds the applicable margin."[37] After making this finding, the majority stated that it was "of course aware of the difficulties in attempting to precisely demarcate the outer boundary of the acceptable margin of change" but noted that the tribunal in *Eiser v. Spain*[38] (which had also found Spain liable for a breach of Article 10(1) of the ECT's FET provision due to its imposition of the NRR) had agreed that "in a case of such scope and complexity damages cannot be determined with mechanical precision."[39]

The majority nevertheless agreed with RENERGY that the discounted cash flow (DCF) methodology was the "appropriate means" of determining RENERGY's damages.[40] However, with regard to the construction of the but-for scenario, the majority explained that it needed to make some changes to Claimant's proposed framework to "reflect the foregoing finding that the Respondent shall only be liable for the damage caused by the portion of the Disputed Measures that exceeded the acceptable margin."[41] In other words, the majority accepted the DCF approach but declined to adopt Claimant's proposed DCF model, which assumed that the tariff established under the ORR would remain completely "frozen" wholesale; instead, the majority decided to adjust Claimant's DCF model such that Spain would only owe damages to RENERGY for the portion of the changes imposed by the NRR that had "materially changed" Spain's framework of relative tariff stability.[42] The majority then conducted its own quantum analysis in two major steps.

First, the majority endeavored to construct an "alternative but-for scenario" in line with its ruling on Spain's violation of its promise to RENERGY of "relative" regulatory stability.[43] Contrary to Claimant's proposed framework for the DCF, the majority concluded that the alternative but-for scenario would include Royal Decree Law 2/2013, which would enter into force only on February 1, 2013 — not with retroactive effect as of January 1, 2013, as in the "actual scenario."[44] The majority also assumed that Claimants' CSP Plants and wind farms chose the Regulated Tariff offered by Spain as of that date.[45]

The majority then noted a difference between the opinions of Claimant's and Respondent's quantum experts as to how long the Regulated Tariff should be assumed to apply in the adjusted but-for scenario. The Brattle Group (Brattle), Claimant's expert, suggested that the tariff could apply either permanently or only until July 2013, while Respondent's expert, Accuracy, argued that RDL 2/2013 should apply permanently. The majority agreed with Spain's expert that in the alternative but-for scenario, RDL 2/2013 should apply permanently, since it was "meant to isolate the damage inflicted on the Claimant by those Disputed Measures that exceeded the acceptable margin of change."[46] As a result, the majority explained, the alternative but-for scenario "must include all Disputed Measures that remained within the acceptable margin of change, which includes RDL 2/2013."[47]

Further, the majority determined that as of July 14, 2013, the day on which RDL 9/2013 came into force, "both the supplement and the penalty for reactive energy shall be eliminated [in the alternative but-for scenario]."[48] The majority explained that "[w]hile RDL 9/2013 eliminated only the supplement, the Tribunal would not find it appropriate if damages were reduced by the corresponding penalty (that RDL 9/2013 maintained)."[49] Additionally, in its alternative but-for scenario, as of June 21, 2014, the day on which Ministerial Order IET/1045/2014 entered into

force, Claimant's CSP Plants and wind farms would be subject to a limitation whereby they would not receive any feed-in tariff remuneration after 25 or 20 years of operation, respectively.[50] The majority also agreed with Spain that since it had found that the cap imposed on the annual amount of hours Claimant's CSP Plants and wind farms could be eligible for the feed-in tariff of 2,040 was reasonable and did not breach the ECT, the alternative but-for scenario would also assume that, as of 2014, all of Claimant's plants would be subject to this cap.[51]

The two final assumptions the majority adopted in its alternative but-for scenario were that (1) as of October 15, 2015 — i.e., the day on which Ministerial Order IET/1882/2014 entered into force — an annual cap of 15,000 megawatt hours would apply to the payment of the feed-in tariff for energy produced by Claimant's CSP Plants through the burning of liquefied natural gas, and (2) as of July 2013, the wind farms and the CSP Plants would be subject to a prospective internal rate of return (IRR) cap of 7 percent pre-tax and 8 percent post-tax (excluding financing).[52] The majority explained that since Spain in the ORR had suggested that a 7 percent pre-tax IRR and an 8 percent post-tax IRR were "reasonable," diligent investors "could not expect to receive, for the entire lifetime of their plants," tariff rates that lifted their IRRs above these levels.[53] Thus, the majority found it "appropriate to implement a respective cap on [IRR for investors] in its alternative but-for scenario."[54]

Second, and after introducing the changes it would make to Claimant's proposed DCF in its own alternative but-for scenario, the majority examined the contention of both Claimant's and Respondent's quantum experts that it would be "appropriate" to apply an illiquidity discount to account for the "lack of marketability" of Claimant's CSP Plants and wind farms.[55] However, the majority noted, the parties' experts disagreed as to what the illiquidity discount should be.[56] Brattle suggested the rate should be 25 percent in the actual scenario, assuming it would take 12 months to find a buyer for Claimant's shareholding in the wind farms and CSP Plants, and 12 percent in the but-for scenario, assuming three months to find a buyer.[57] Accuracy, to the contrary, calculated 16.7 percent in the actual scenario, assuming three months to find a buyer, but 35 percent in the but-for scenario, assuming 12 months to find a buyer.[58]

The majority remarked that the different calculations produced by the parties' experts regarding the illiquidity discount and the corresponding periods for finding a buyer were "explained by the fact that Accuracy looked at market illiquidity while Brattle looked at 2014, [because of] their respective valuation dates."[59] The majority further observed that "the illiquidity discount is closely related to regulatory risk," which explained why Brattle "assumes a decrease in the illiquidity discount from the actual scenario to the but-for scenario, while Accuracy takes

the opposite view."[60] Since the majority agreed with Brattle that the appropriate valuation date for the DCF was June 21, 2014 (when the primary components of the NRR came into force), the majority adopted Brattle's illiquidity discount for both the actual and alternative but-for scenarios, which was also based on a 2014 date.[61]

Applying these changes to Claimant's proposed DCF analysis, the majority of the Tribunal found that the overall damage suffered by RENERGY, as of the valuation date of June 21, 2014, totaled €32,896,240.00.[62]

Prof. Sands, who dissented from the majority on quantum as well, concluded that the majority's analysis improperly "melds" the issues of liability and quantum.[63] In his view, there was "no evidence before the Tribunal that the Respondent offered any commitment or assurance that change [to the ORR and its promised tariffs] would not exceed an 'acceptable margin' or that the Claimant placed reliance on any such commitment or assurance."[64] As to the majority's finding that the acceptable margin of regulatory change that Spain exceeded was to be valued at €32,896,240.00, Prof. Sands stated that there was "not a shred of evidence in the record … to support [such a] conclusion."[65] He accused the majority of engaging in a "finger in the air exercise" and admitting that damages cannot be "determined with acceptable precision."[66] For Prof. Sands, the majority's approach was unacceptable and "not … comprehensive" to an ordinary reader, and he would have held that Spain's "balanced approach" would not have breached any provision of the ECT.[67]

Interest

The majority of the Tribunal stated that it had "no hesitation" in concluding that the principle of full reparation under Chorzów entitled RENERGY to payment of interest.[68] It then considered that Spanish 10-year bonds, as suggested by RENERGY, would be an "appropriate benchmark."[69] Such a conclusion was also supported by the fact that Spain itself had suggested that the "bond duration should mirror the time between the valuation date [June 2014] and the award date [May 2022]," making the "10-year bonds a better approximation than the 2-3 year bonds suggested by the Respondent."[70]

On the question of post-award interest, the majority considered the arbitral jurisprudence proffered by the parties on "whether a differential should be applied on pre-award interest so as to incentivize compliance with the arbitral award."[71] It concluded that, in line with the commentary to ILC Articles 38(1) and 36, the principle of full reparation "is not concerned to punish the responsible State, nor does compensation have an expressive or exemplary character."[72] Thus, the majority concluded that the same interest rate should apply before and after award so as to avoid any suggestion of punishing the sovereign.[73] Finally, noting the lack of opposition from Respondent, the majority accepted Claimant's request that the interest be compounded monthly.[74]

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1 *RENERGY S.à.r.l. v. Kingdom of Spain*, ICSID Case No. ARB/14/18, May 6, 2022, Award (Award), ¶ 121.

2 Award, ¶ 125.

3 Award, ¶ 127.

4 Award, ¶ 132.

5 Award, ¶ 134.

6 Award, ¶ 134.

7 Award, ¶ 174.

[8] Award, ¶ 198 *et seq*.
[9] Award, ¶¶ 227-233.
[10] Award, ¶ 213.
[11] Award, ¶ 253(iii).
[12] Award, ¶ 280.
[13] Award, ¶¶ 340, 372-373.
[14] Award, ¶ 383.
[15] Award, ¶ 419.
[16] Award, ¶ 419.
[17] Award, ¶ 426.
[18] Award, ¶¶ 432-434.
[19] Award, ¶¶ 439, 442.
[20] Award, ¶ 442 (emphasis added).
[21] Award, ¶ 442.
[22] Award, ¶ 446.
[23] Award, ¶ 487.
[24] Award, ¶ 495.
[25] Award, ¶ 495.
[26] Award, ¶¶ 909-910, 1072.
[27] Award, ¶ 775.
[28] Award, ¶ 775.
[29] Award, ¶ 910(ii)-(iii).
[30] Award. ¶¶ 946, 964, 980, 1011.
[31] *RENERGY S.à.r.l. v. Kingdom of Spain,* ICSID Case No. ARB/14/18, Decision on Liability and Quantum of Prof. Philippe Sands QC, May 6, 2022 (Sands Dissent), ¶ 5.
[32] *Sands Dissent,* ¶¶ 10, 12.
[33] *Sands Dissent,* ¶¶ 23, 46.
[34] Award, ¶ 1029.
[35] Award, ¶ 1029.
[36] Award, ¶ 1030.
[37] Award, ¶ 1030 (emphasis added).
[38] *Eiser Infrastructure Ltd. and Energia Solar Luxembourg S.à.r.l. v. Kingdom of Spain,* ICSID Case No. ARB/13/36, Award, May 4, 2017.
[39] Award, ¶ 1031 (quoting *Eiser Infrastructure Ltd. and Energia Solar Luxembourg S.à.r.l. v. Kingdom of Spain,* ICSID Case No. ARB/13/36, Award, May 4, 2017, ¶ 473).
[40] Award, ¶ 1032.
[41] Award, ¶ 1032.
[42] Award, ¶ 1032.
[43] Award, ¶ 1034.
[44] Award, ¶ 1035.
[45] Award, ¶ 1035.
[46] Award, ¶ 1035.
[47] Award, ¶ 1035.
[48] Award, ¶ 1036.
[49] Award, ¶ 1036.
[50] Award, ¶ 1037.
[51] Award, ¶ 913.
[52] Award, ¶¶ 1039-1040.
[53] Award, ¶ 1040.
[54] Award, ¶ 1040.
[55] Award, ¶ 1041.
[56] Award, ¶ 1041.
[57] Award, ¶ 1041.
[58] Award, ¶ 1041.
[59] Award, ¶ 1042.
[60] Award, ¶ 1042.
[61] Award, ¶ 1043.
[62] Award, ¶ 1046.
[63] *Sands Dissent,* ¶ 37.
[64] *Sands Dissent,*¶ 37.
[65] *Sands Dissent,* ¶ 39.
[66] *Sands Dissent,* ¶¶ 39-40.
[67] *Sands Dissent,* ¶¶ 40,46.
[68] Award, ¶ 1047.
[69] Award, ¶ 1048.
[70] Award, ¶ 1048.
[71] Award, ¶ 1049.
[72] Award, ¶ 1049.
[73] Award, ¶ 1049.
[74] Award, ¶ 1050.

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