

# BELOW-MARKET INTEREST IN INTERNATIONAL CLAIMS AGAINST STATES

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## ABSTRACT

The article deals with an important but strange contradiction in international legal practice. The official doctrine provides that states must fully compensate all damage caused by an internationally wrongful act. Yet, when it comes to compensating the injured party for the delay caused by the state's failure to compensate promptly (usually awarded in the form of interest on the direct damages), international tribunals almost universally shy away from awarding the full economic measure of interest. The consequences of the systematic undercompensation of claimants in international law assume special gravity because of the long period of time that typically elapses between the injury and the award by a tribunal or claims commission. The delay commonly exceeds three years and sometimes extends to 10 or 15, during which time the value of an interest award begins to overshadow the value of the direct damages award itself. This institutionalized undercompensation of claimants occurs in every international human rights case, and more often than not elsewhere, from wrongful expropriation of property cases to breach of international contract claims. This article analyzes and attempts to explain this disconnection between doctrine and practice, and to relate it to the nature of the international decision-making process.

*Ad præsens ova, cras pullis sunt meliora.*<sup>1</sup>

## I. INTRODUCTION

Public international law imposes few obligations so widely accepted as the duty of every state to provide full reparation for any injury caused by

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<sup>1</sup> 'Today's eggs are better than tomorrow's hens.' François Rabelais, *The Histories of Gargantua and Pantagruel* (John M. Cohen trans. [1532] 1982) 395.

the state's internationally wrongful act.<sup>2</sup> In the often-repeated adage of the Permanent Court of International Justice's (PCIJ) *Factory at Chorzów* judgment, international law provides that a breach of an international legal obligation entails 'an obligation to make reparation in an adequate form'<sup>3</sup> and that such 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'.<sup>4</sup> The *Chorzów Factory* formulation recurs frequently in international judicial and arbitral decisions.<sup>5</sup> While restoring the claimant to the *status quo ante* may not always be literally possible, the tribunal is bound to attempt the closest approximation of that state ascertainable on the credible evidence.<sup>6</sup>

The duty of full reparation, sometimes called *restitutio in integrum* in a nod to its Roman ancestry,<sup>7</sup> is enshrined in customary international law as reflected in the International Law Commission's Articles on State Responsibility, several major contemporary conventions, and numerous bilateral investment treaties (BITs) and free trade agreements (FTAs). With the spread of international law into new fields of human endeavor, full reparation has become a bedrock principle in subjects as diverse as human rights, *ius in bello*, and foreign investment.<sup>8</sup>

<sup>2</sup> U.N. Int'l L. Comm'n, Articles on the Responsibility of States for Internationally Wrongful Acts art. 34 (November 2001), Off. Rec. of the G.A., 56th sess., supp. 10 (UN Doc. A/56/10), chp.IV.E.1 [hereinafter ILC Articles]; see, e.g. Armed Activities on the Territory of the Congo (*D. R. C. v Uganda*), Judgment, ICJ Reports 2005, 168, para 259 (merits).

<sup>3</sup> *Factory at Chorzów (Ger. v Poland)* (Claim for Indemnity — Jurisdiction), PCIJ Judgment No. 9, Series A, No. 9, at 21.

<sup>4</sup> *Factory at Chorzów (Ger. v Poland)* (Claim for Indemnity — Merits), PCIJ Judgment No. 13, Series A, No. 17, at 47; accord *American Mfg. & Trading Inc. v Zaire*, ICSID Case No. ARB/93/1, Award of 21 February 1997, para 6.21; *Petrobart v Kyrgyz Rep.*, Stockholm Chamber of Commerce Arb. No. 126/2003, Award of 29 March 2005, at 78.

<sup>5</sup> See, e.g. *Corfu Channel Case (U.K. v Alb.)*, 1949 I.C.J. Rep. 4, 23 (Merits); *Metalclad Corp. v Mexico*, Award of 30 August 2000, ICSID Case No. ARB(AF)/97/1, 40 I.L.M. 36, 52; *The Sapphire*, 35 I.L.R. 136, 185–6 (1963); *Norwegian Shipowners' Claims*, Award of 13 October 1922, 1 R.I.A.A. 307, 338 (1922); *Lighthouses Arbitration (Fr. v Greece)*, 23 I.L.R. 299, 300–1 (1956).

<sup>6</sup> Green Hackworth, *Digest of International Law*, vol. 5 (Washington, DC: U.S. Government Printing Office, 1985) 718–21.

<sup>7</sup> See Aaron Fellmeth and Maurice Horwitz, *Oxford Guide to Latin in International Law* (Oxford: Oxford University Press, 2009) 256. Technically, *restitutio in integrum* refers to restitution—an uncommon remedy at international law—but the term has acquired the more general denotation of full reparation.

<sup>8</sup> See, e.g. European Convention on Human Rights arts. 5(5), 41; American Convention on Human Rights art. 63(1); Convention on the Elimination of All Forms of Racial Discrimination art. 6; UN Convention Against Torture art. 14; UN Covenant on Civil and Political Rights art. 9(5); 1907 Hague Convention No. IV art. 3; Additional Protocol I to the 1949 Geneva Conventions art. 91; North American Free Trade Agreement (Can.-Mex.-U.S.) art. 1110, 17 December 1992, 32 I.L.M. 605.

Like most equitable principles formulated in streamlined prose, *restitutio in integrum* can prove challenging to apply in practice. Quantifying and assessing with precision the loss to the claimant caused by the respondent state's wrongful act often poses difficulties in the form of uncertainty about the quantum of damages and the abstract nature of the harm suffered. The compensable loss includes not only direct injuries to the claimant; damaged, expropriated, or destroyed property; and other tangible harms, but the loss of economic opportunities as well. Such opportunities may include the foregone option of earning a return on compensation that the respondent state should (at least theoretically) have paid the claimant promptly after causing the harm—interest on the compensation due. They may also include lost profits (*lucrum cessans*) that the claimant would have earned had the respondent state not wrongfully deprived the claimant of the use of the claimant's capital. The PCIJ observed in the *Factory at Chorzów* case that a tribunal applying the compensation standards of international law must

determine the monetary value, both of the object which should have been restored in kind and of the additional damage, on the basis of the estimated value of the undertaking... together with any probable profit that would have accrued to the undertaking between the date of taking possession and that of the expert opinion.<sup>9</sup>

Analyzing this celebrated judgment, the Iran–U.S. Claims Tribunal reaffirmed that '[o]ne essential consequence of this principle [of full reparation] is that the compensation 'is not necessarily limited to the value of the undertaking at the moment of dispossession' (plus interest to the day of payment).'<sup>10</sup> It is well established that the duty to compensate for the time value of injured assets is a general one, applying in breach of international contract claims as well as expropriation and other tort claims.<sup>11</sup>

<sup>9</sup> *Factory at Chorzów (Ger. v Poland)*, PCIJ Judgment No. 13, Series A, No. 17, at 52 (Claim for Indemnity — Merits).

<sup>10</sup> *Amoco Int'l Finance Corp. v Iran*, Award No. 310-56-3 (14 July 1987), 15 Iran-U.S. Claims Trib. Rep. 189, 247–9; accord *DIC of De., Inc. v Tehran Redev. Corp.*, Award No. 176-255-3 (26 April 1985), 8 Iran-U.S. Claims Trib. Rep. 144, 171; *Amoco Int'l Finance Corp.*, Award No. 310-56-3, at 299 (Brower, J., concurring) (noting that precedents in the Tribunal confirm that expected future profits must be included in the calculation of compensation.).

<sup>11</sup> See, e.g. *Lena Goldfields, Ltd. v Union of Soviet Socialist Republics*, Judgment of 2 September 1930, 5 A.D. (1929–30), reprinted in *Cornell Law Quarterly* 36 (1950) 51; *Norwegian Shipowners' Claims (Nor. v U.S.)*, Award of 13 October 1922, 1 R.I.A.A. 307, 338 (1922); see also Charles Rousseau, *Droit International Public*, vol. 5 (Paris: Sirey, 1983) 223 ('Besides the actual loss of the assets, the damages may include the injury suffered by the owner from the loss of the use or possession of said assets, so that the loss of the anticipated profits appears as an essential element of the injury for which the claimant state seeks reparation.') (my translation); Hersh Lauterpacht, *Private Law Sources and Analogies of International Law* (London: Longmans, Green and Co. Ltd., 1927) 148–9 ('[T]o maintain that international law disregards altogether compensation for *lucrum cessans* is repellent to justice and common sense, as it is out of accord with the practice of international tribunals.');

Ladislas Reitzler, *La réparation comme conséquence de l'acte illicite en droit international* (Paris: Sirey, 1938) 188

Compensation for the lost time value of assets has been a generally accepted component of damages under international law since its early development.<sup>12</sup> The practice of specifically awarding lost profits for wrongful injury to an income-producing asset has its roots in Roman civil law<sup>13</sup> and was adopted by many international tribunals in the nineteenth century on the theory that:

No compensation for an injury can be just and adequate which does not repair that injury; but he who wrongfully deprives me of a lawful profit, which I am employed in making, can not be said to afford me reparation until he has given me an equivalent for the advantages of which he has deprived me, to which advantages my right was as unquestionable as the right I had in the things from which they were to arise.<sup>14</sup>

Various distinctions between prohibited and permitted compensation for the lost time value of money were made by classical writers on mostly religious grounds,<sup>15</sup> but in modern times, the award of lost profits has become *de rigueur* in international investment cases.<sup>16</sup> Lost profits are typically awarded on damaged, expropriated, or destroyed capital assets for the period between the dispossession of the property and the award. The rationale for lost profits awards is that, in the absence of the state's wrongful act, the claimant would have used the capital to earn a return greater than that obtainable through an investment returning interest at a commercial rate.

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(‘[L]ucrum cessans has a quite clear meaning. It designates a profit, not yet earned, that could have been obtained had the wrong not occurred, in contrast to *damnum emergens*, by which is meant personal property of which the owner has been deprived.’) (my translation); Jean Personnaz, *La réparation du préjudice en droit international public* (Paris: Sirey, 1939) 182, 288; Ian Brownlie, *System of the Law of Nations* (Oxford: Oxford University Press, 1983) 225 (‘Reasonably foreseeable loss of profits (*lucrum cessans*) is regularly allowed as an aspect of compensation and this without tribunals being concerned whether such damages are ‘direct’ or not.’).

<sup>12</sup> See Hugo Grotius, *De Jure Belli ac Pacis Libri Tres*, vol. 1 (Buffalo, NY: Willaim S. Hein & Co., 1995) 431 (1625) (‘[A] person will be understood to have less, and therefore to have suffered loss, not only in the property itself, but also in the products which strictly belong to it, whether these have actually been gathered or not, if he might have gathered them...’).

<sup>13</sup> See generally Karl-Heinz Below, *Die Haftung für Lucrum Cessans im Römischen Recht* (Munich: C.H. Beck, 1964) (discussing the practice of awarding lost profits in Roman civil law).

<sup>14</sup> *The Betsy* (U.S.-Gr. Brit. 1868), John Bassett Moore (ed.), *History and Digest of International Arbitrations in Which the United States Has Participated* (Washington, DC: U.S. Gov’t Printing Off., 1898), vol. 4, 4205 [hereinafter Moore]; accord *Norwegian Shipowners’ Claims* (Nor.-U.S.), Award of 13 October 1922, 1 R.I.A.A. 307, 338 (1922); *The Cheek* (U.S.-Siam 1898), 2, Moore, this note, at 1899.

<sup>15</sup> Textor, for example, distinguished between permissible moratory interest as *lucrum cessans* (i.e. interest awarded to compensate for an injury to a creditor caused by the debtor’s delay in repayment) and forbidden lucrative usury (i.e., interest payable by prior agreement of the creditor and debtor). See Johann Wolfgang Textor, in John Pawley Bate (trans), *Synopsis of the Law of Nations* (Washington, DC: Carnegie Endowment for Int’l Peace, 1916 [1680]) 121.

<sup>16</sup> See Christine Gray, *Judicial Remedies in International Law* (Oxford: Oxford University Press, 1987) 25; see, e.g. *Sedco v Iran*, 15 Iran-U.S. Cl. Trib. Rep. 23 (1987); *Libyan Am. Oil Co. (LIAMCO) v Libya* (Award of 12 April 1977), 62 I.L.R. 139 (1982).

Interest compensates for the same general class of injury—the lost time value of an asset of which the claimant was deprived by the state’s failure to compensate the direct injury (*damnum emergens*). In the case of interest, the asset whose time value has been sacrificed is money that should have been paid in compensation of the injury. Thus, interest tends to be awarded on injuries other than those affecting income-producing assets.

The legal principle guiding the assessment of damages for the lost time-value of money has long been *qui tardius solvit, minus solvit*—whoever pays tardily, pays less. Insofar as delay in paying reparations benefits the respondent, the respondent is expected to compensate the claimant for that delay. Any other solution would reward the respondent for delaying the payment of compensation to the injured party. It would, moreover, compound the claimant’s injury by adding the loss of the use of the compensation now owed to the original injury suffered.

Religious prohibitions on usury and concerns about equity made the award of lost profits a standard practice long before international tribunals began allowing interest on damages in international claims against states,<sup>17</sup> despite the facts that both kinds of awards serve essentially the same purpose, and lost profits are generally less susceptible to proof than the loss of interest.<sup>18</sup> With changes in attitudes about economics and state sovereignty, the practice of granting interest on an award rendered in resolution of international claims has gone from rare to common in the last thirty years. Modern BITs and FTAs commonly include a provision for the payment of interest in case of expropriation or other taking.<sup>19</sup> International tribunals, formerly reluctant to assess damages against states for delays in paying compensation, now award such damages as a matter of course.

Unless the claimant and the respondent state have contractually agreed to an award or denial of interest, which is normally enforced without hesitation,<sup>20</sup> the questions of how and whether to assess interest become issues of contention. Interest may figure prominently in compensation for wrongful injuries in almost every national legal system, but it assumes heightened importance in international law practice. The long delays between the harm and the payment

<sup>17</sup> In 1939, Jean Personnaz concluded that international law does not mandate awards of interest at all. Personnaz, above n 11, at 233. Ten years later, in the *Corfu Channel* case, the court awarded no interest to the victorious claimant. *Corfu Channel Case (U.K. v Alban.)*, 1949 I.C.J. Rep. 243, 249–50 (Damages). But see *Russian Indemnities (Russ. v Turk.)*, Award of 11 November 1912, 11 R.I.A.A. 421 (finding a ‘general principle of law’ among various municipal legal systems mandating the award of some kind of interest on a delayed payment).

<sup>18</sup> Cf. W. Michael Reisman and Robert D. Sloane, ‘Indirect Expropriation and Its Valuation in the BIT Generation’, 74 *British Year Book of International Law* 115 (2003), at 139 (discussing the uncertainty inherent in hypothetical calculations of lost profits).

<sup>19</sup> See, e.g. U.S.-Argentina Bilateral Investment Treaty art. IV(1); U.K.-Panama Bilateral Investment Treaty art. 5(1); Australia-U.S. Free Trade Agreement art. 11.7(3) and (4), 1 January 2005.

<sup>20</sup> See, e.g. *Libyan American Oil Co. v Libyan Arab Rep.*, 20 I.L.M. 1, 115–16 (1981).

of compensation typical in international claims against states are in some cases so great that accumulated interest may overshadow the claimant's direct loss. In some older cases, international tribunals have imported the Roman *alterum tantum* rule into international law to limit interest awards to amounts no greater than the principal due,<sup>21</sup> but in more modern cases tribunals have adhered more closely to basic economic reasoning and awarded interest in amounts greater than the principal when appropriate.<sup>22</sup>

Although international awards and judgments now commonly include some form of interest, two factors make predictions about how international tribunals will award interest in international claims against states less reliable than predictions about awards of *damnum emergens*. First, despite long experience, there is no single, universally accepted method of assessing interest in international practice. Tribunals have varied widely in the type and quantum of interest awarded in similar cases. Second, there exists a continued disjunction between the universally acclaimed *Chorzów Factory* doctrine and actual international practice. Awards including or denying interest, while never questioning the duty to put the claimant in as good a position as it would have been in the absence of the injurious act, frequently assess interest at a level significantly below full reparations. While both of these phenomena are well known to international lawyers, little thought has been put into explaining their causes.

This article seeks to answer these questions. Section II briefly surveys international practice in awarding interest to set the stage of the discussion in Section III of the factors that may influence international tribunals to shy away from strictly economic methods of assessing interest. The three main legal variables that determine the economic effect of interest awards—the choice of interest rate (Section II.A), the question of compounding (Section II.B), and the determination of the period during which interest will run (Section II.C)—are discussed in turn. In Section III, four non-economic influences that may affect interest awards are identified and analyzed: the characterization of interest as punitive and, therefore, forbidden by international law (Section III.A); the role that the need for predictability plays in the international decision process (Section III.B); concerns about showing sufficient deference to sovereign respondents (Section III.C); and the systemic interest in effectuating a compromise to assist the parties in settling a dispute that may otherwise have destabilizing consequences

<sup>21</sup> See, e.g. Yuille, *Shortridge & Co. Case*, in Albert Lapradelle and Nicolas Politis, *Recueil des arbitrages internationaux* (Paris: Pedone, 1924), vol. 2, 79, at 108.

<sup>22</sup> See Gray, above n 16, at 29; John A. Westberg, *International Transactions and Claims Involving Government Parties: Case Law of the Iran-U.S. Claims Tribunal* (Netherlands: Kluwer Law Int'l, 1991) 254 (noting that 'interest awards doubled the principal amounts awarded' in many claims adjudicated by the U.S.-Iran Claims Tribunal). For example, in *Compañía del Desarrollo de Santa Elena, S.A. v Costa Rica*, 15 ICSID Rev. 169, 200 (2000), the tribunal awarded nearly \$12 million in interest on a claim of just over \$4 million in direct damages.

(Section III.D). Depending on the circumstances of each case, some of these factors are more persuasive than others, but each plays a greater role in international practice involving state parties than in municipal judicial practices within states.

Section IV concludes by observing that what makes the study of the variability and economic inaccuracy of historical and modern interest practices edifying and important is not the fact of systemic undercompensation of claimants in international practice so much as the insight about the dynamics of international decision making to be gained from a study of the factors that result in compensation below that which strict economic logic would dictate.

Because this article is concerned exclusively with the development of public international law, it eschews the common practice of treating decisions in purely private law disputes and those concerned with public international law as equivalent. The focus here is, accordingly, primarily on international courts, investor-state arbitral tribunals, mixed claims commissions, and international claims commissions. Domestic courts and private arbitral tribunals generally<sup>23</sup> apply principles of domestic law selected by the private parties, or the law appropriate under conflict of laws principles, as the governing rules of the transaction at issue. In contrast, the tribunals under consideration here often apply treaty rules and customary principles of public international law and, therefore, need not limit themselves to considering the law of any one specific state. This distinction is particularly important because the laws of some states allow their domestic courts to alter or supplement interest awards rendered by private commercial arbitral tribunals.<sup>24</sup>

## II. ASSESSING INTEREST IN INTERNATIONAL PRACTICE

Interest has long been granted in one form or another on damages in international arbitral and claims commission awards,<sup>25</sup> including in the practice of the U.S. Foreign Claims Settlement Commission,<sup>26</sup> International Centre for Settlement of Investment Disputes (ICSID) arbitrations,<sup>27</sup> UN

<sup>23</sup> The exception is when the parties instruct the arbitrator to decide the contentious issue based on *lex mercatoria* or *ex aequo et bono*.

<sup>24</sup> For example, the French Cour de Cassation has recently held that, although an arbitral tribunal had not awarded post-award interest in its decision, the victorious claimant could obtain such interest in an enforcement action before a French court. *Pourvoi No. 01-10269*, Cour de Cassation, 1er Chambre Civil (30 June 2004) (Fr.). Such supplements are unavailable in arbitrations conducted under public international law.

<sup>25</sup> See Lauterpacht, above n 11, at 145–6, 300; see, e.g. *Russian Indemnity Case*, Award of November 1912, in James Brown Scott, *Reports of the Permanent Court of Arbitration* (Washington, DC: Carnegie Endowment for Int'l Peace, 1916) 297, at 316.

<sup>26</sup> 22 U.S.C. § 1626 (2007).

<sup>27</sup> For example, *Asian Agricultural Prods. Ltd. v Sri Lanka*, ICSID Case No. ARB/87/3, Award of 27 June 1990, 6 ICSID Rev. 571, para 114 (1991).

Compensation Commission recommendations,<sup>28</sup> Iran–U.S. Claims Tribunal decisions and awards,<sup>29</sup> and *ad hoc* international arbitration.<sup>30</sup> The 2001 ILC Articles on State Responsibility provide for interest in Article 38:

1. Interest on any principal sum due under this chapter shall be payable when necessary in order to ensure full reparation. The interest rate and mode of calculation shall be set so as to achieve that result.
2. Interest runs from the date when the principal sum should have been paid until the date the obligation to pay is fulfilled.<sup>31</sup>

Indeed, the practice of awarding interest is so uncontroversial that by 1987 one commentator could identify but a single arbitration in which an international tribunal declined to award it expressly on a theory that interest was not allowable under international law on awards against states.<sup>32</sup>

Calculation methodologies for interest differ partly based on evidentiary issues and partly based on different assumptions about the nature of the claimant's injury. Compounding the difficulty of calculating interest reliably is the lack of any uniform state practice that might offer guidelines to international tribunals. Sections II.A and II.B will analyze whether and to what extent each methodology reflects economic reality. Section II.A focuses on the interest rate chosen by international tribunals, and Section II.B discusses the decision whether to compound the interest and, if so, at what interval.

One variable especially important to interest awards is the date from which interest runs. Technically, all interest compensates the claimant for unpaid sums owed on a loss that (counterfactually) should have been compensated immediately after the injury. In practice, international tribunals distinguish between pre-award and post-award interest, with post-award interest being the more commonly granted of the two. International practice on the circumstances under which pre-award interest will be granted is variable and

<sup>28</sup> UN Compensation Comm'n, Governing Council, Decision 16, S/AC.26/1992/16\_\*, 4 January 1993, paras 1–2; e.g. U.N. Compensation Comm'n, Report and Recommendations Made by the Panel of Commissioners Concerning the First Instalment of Claims for Departure from Iraq or Kuwait (Category 'A' Claims), 21 October 1994, UN Doc. No. S/AC.26/1994/2, para 51.

<sup>29</sup> For example, *Iran v United States of Am.*, Iran-U.S. Cl. Trib., DEC-65-A19-FT, 30 September 1987, 16 I.C.T.R. 285, 289–90 (full trib.); *Sylvania Tech. Sys. v Iran*, Iran-U.S. Cl. Trib., Award No. 180B64-1, 27 June 1985, 8 I.C.T.R. 298, 320.

<sup>30</sup> For example, Lord Nelson Claim (No. 20), Brit.-Am. Cl. Arb. Trib. (1 May 1924) ('It is a generally recognized rule of international law that interest is to be paid at the rate current in the place and at the time the principal is due.'). See generally J.G. Wetter, 'Interest as an Element of Damages in the Arbitral Process', *International Financial Law Review* 20 (1986).

<sup>31</sup> ILC Articles, art. 38.

<sup>32</sup> See Gray, above n 16, at 30. There are, of course, many awards withholding pre-award interest, but Gray's point is that such awards do not reject interest as required by international law on principle, but rather under the specific facts of the case.

reflects diverse economic and jurisprudential theories. Section II.C of this section will discuss why and how international tribunals distinguish between pre-award and post-award interest, and whether this distinction is economically sound.

## A. Measures of interest

### 1. International practice in setting interest rates

In national legal systems, courts commonly add prejudgment or postjudgment interest, or both, to awards of damages.<sup>33</sup> Interest is typically set at either a statutory rate or a commercially available rate,<sup>34</sup> except, in some jurisdictions, when the claimant can demonstrate that it has historically benefited from, or was required to borrow at, a higher rate.<sup>35</sup> Especially in common law states, courts may maintain liberty to set interest according to their sense of the equities of the case.<sup>36</sup>

International practice in awarding interest began by emulating the domestic practices of states, but the high variability of state practice provides little definite guidance on the details of the award. In the past, mixed and national claims commissions, the PCIJ and International Court of Justice, and various arbitral tribunals typically awarded default interest in cases of economic injury to a non-income-producing asset at a simple rate of 6%—a choice rarely explained or justified except by the occasional offhand reference to such a rate being ‘fair’ or commercially ‘usual’.<sup>37</sup>

<sup>33</sup> See Personnaz, above n 11, at 217; Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (Oxford: Oxford University Press, 2009) 330; see, e.g. Supreme Court Act 1981, ch. 54, § 35A (Eng.); N.Y. C.P.L.R. 5001(a) (2009); Código Civil Federal art. 2117, Diario Oficial de la Federación [D.O.] 26 May, 14 July & 31 August, 1928 (Mex.); Código de Comercio art. 362, D.O. 7 October 1889 (Mex.) .

<sup>34</sup> See Thierry SÉNÉSCHAL and John Y. Gotanda, ‘Interest as Damages’, 47 *Columbia Journal of Transnational Law* 491 (2009) at 501–2. In U.S. federal practice, that has typically been the Treasury bill rate or the prime interest rate. See, e.g. *Lam, Inc. v Johns-Manville Corp.*, 718 F.2d 1056, 1066 (Fed. Cir. 1983). U.S. states typically use some statutory rate.

<sup>35</sup> See, e.g. *Lam, Inc. v Johns-Manville Corp.*, 719 F.2d 1056, 1066 (Fed. Cir. 1983); *Micro Motion, Inc. v Exac Corp.*, 761 F. Supp. 1420, 1436 (N.D. Cal. 1991).

<sup>36</sup> See, e.g. *Gyromat Corp. v Champion Spark Plug Co.*, 735 F.2d 549, 556–7 (Fed. Cir. 1984). In the People’s Republic of China, for example, interest rates on judicial awards are reported to vary between 5% and 10%. See SÉNÉSCHAL and Gotanda, above n 34, at 503.

<sup>37</sup> See Richard B. Lillich and Gordon A. Christenson, *International Claims: Their Preparation and Presentation* (Washington, DC: PAIL Institute Publications, 1962) 86; see, e.g. *Libyan American Oil Co. v Libya*, Award of 12 April 1977, 62 I.L.R. 141, 215 (1982); *The Wimbledon Case*, PCIJ Ser. A, No. 1, at 32 (postaward interest only). In the *Factory at Chorzów* case, Germany requested pre-award interest at a simple rate of 6% per annum. *Factory at Chorzów (Merits)*, PCIJ Judgment No. 13, Series A, No. 17, at 7. In the *Alabama Claims* arbitration, the tribunal awarded \$15.5 million in gross to the United States without specifying how it arrived at this appraisal. It is only because the dissenting arbitrator disclosed that the tribunal assessed pre-award interest on the main sum at a rate of 6% that we know interest played a role in the award. See Moore, above n 14, vol. 1 at 651 (Cockburn dissenting).

Although many modern international tribunals and claims commissions continue to lean on a 6% standard,<sup>38</sup> others have sought a more nuanced or customized measure of damages, looking to the ‘prevailing’ rate of interest in a relevant market.<sup>39</sup> The relevant market rate varies according to the tribunal deciding the issue. Both international arbitral tribunals and mixed claims commissions have sometimes used the rate of interest prevailing in the respondent state,<sup>40</sup> but some have used the rate prevailing in the claimant’s state.<sup>41</sup> In many states, nominal interest rates do not accurately reflect commercial practice—for example, due to high inflation rates or because the state artificially limits private interest rates by law. International tribunals have accordingly begun to overcome their past reluctance<sup>42</sup> to disregard national rates and to award free market commercial interest rates instead.<sup>43</sup>

In practice, nominal rates awarded vary widely from 3 to 17.5%,<sup>44</sup> while real interest rates rarely exceed 10% simple interest.<sup>45</sup> Although some international tribunals have taken pains to explain their chosen rate, it remains

<sup>38</sup> For example, *Middle East Cement Shipping & Handling Co. S.A. v Egypt*, Case No. ARB/99/6, Award of 12 April 2002, 18 ICSID Rev.-FILJ 602; *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000, 40 I.L.M. 36, para 128 (2001); *Técnicas Medioambientales SA v Mexico*, Award of 29 May 2003, 19 ICSID Rev.-FILJ 159, para 197 (2004).

<sup>39</sup> For example, *Illinois Central R.R. Co. v Mexico* (Mex.-U.S. Gen. Cl. Comm’n), 6 December 1926, 4 R.I.A.A. 134, 136.

<sup>40</sup> For example, *Delagoa Bay Rwy. Co. (Port. v Gr. Brit.)*, Moore, above n 14, vol. 2 at 1865; *Orinoco Steamship Co. (U.S. v Venez.)*, Perm. Ct. Arb. Award of 25 October 1910 (fixing interest at the 3% allowed by Venezuelan law); see Gray, above n 16, at 31; Reitzer, above n 11, at 193.

<sup>41</sup> For example, *The Macedonian Case* (U.S.-Chile), Moore, above n 14, vol. 2 at 1449; see Reitzer, above n 11, at 193; John Gotanda, *Supplemental Damages in Private International Law* (Netherlands: Kluwer Law Int’l, 1997) 47–50; Jérôme Ortscheidt, *La réparation du dommage dans l’arbitrage commercial international* (Paris: Dalloz, 2001) 258–61.

<sup>42</sup> For example, *Orinoco Steamship Co. (U.S. v Venez.)*, Perm. Ct. Arb. Award of 25 October 1910 (‘[T]he Venezuelan law fixes the legal interest at 3%... under these conditions, the Tribunal, although aware of the insufficiency of this percentage, cannot allow more.’).

<sup>43</sup> For example, *Southern Pacific Props. (M.E.) Ltd. v Egypt*, Case No. ARB/84/3, 3 ICSID Rep. 189, paras 223, 237 (1992); *American Independent Oil Co. v Kuwait*, Award of 24 March 1982, 21 I.L.M. 976, paras 168–78.

<sup>44</sup> See Reitzer, above n 11, at 193; see also Ortscheidt, above n 41, at 261 (noting interest awarded at rates between 6.25 and 14%). The U.N. CISG, although concerned exclusively with private contracts, specifies that interest is payable on the debt of a defaulting party without further elaboration. Convention on Contracts for the International Sale of Goods art. 78, 11 April 1980, S. Treaty Doc. No. 98-9 (1983), 1489 U.N.T.S. 3.

<sup>45</sup> A nominal rate of interest is the face value of the interest rate. The real rate of interest is the nominal rate discounted by inflation. For example, suppose a claimant is granted nominal interest on an award at a rate of 10% for the period between the injury and the award. Suppose further that the rate of inflation on the currency in which the award is expressed was 6% during the same period. The real interest rate is 4%.

While relatively few international tribunals expressly award real interest (as opposed to nominal interest), a few tribunals have done so. See, e.g. *American Independent Oil Co. (Aminoil) v Kuwait*, Award of 24 March 1982, 21 I.L.M. 976 (1982). More often, they have accounted for past inflation by increasing the nominal interest rate in the award, which is functionally equivalent to awarding real interest.

common for tribunals to neglect to justify their interest awards except, as noted above, through a brief reference to the chosen rate being ‘reasonable’ or ‘usual’. In short, there is no consistently applied rule of international law that prescribes the standards to be used in assessing rates of pre-award or post-award interest beyond the general standard of ‘full compensation’,<sup>46</sup> either between different international tribunals or within the jurisprudence of most standing tribunals.

Even the longstanding Iran-U.S. Claims Tribunal declined to promulgate a general rule respecting when and how much interest should be awarded.<sup>47</sup> The result in that tribunal’s jurisprudence has been disparate determinations of interest rates—often without published explanation—ranging from about 8 to 12%.<sup>48</sup> In the 1985 *Sylvania Technical Systems* opinion, Chamber 1 of the Tribunal recognized the problem and determined that, if no pertinent contract stipulated an interest rate, then the Tribunal would award the interest rate that the successful claimant would have been in a position to have earned if it had been paid at the time of injury, generally the 6-month certificate of deposit rate in the United States.<sup>49</sup> This was not the ideal choice for promoting a consistent jurisprudence, as CD rates varied from bank to bank and are moreover often extremely low. In any case, Chamber 3 of the Tribunal reverted to the flexible, case-by-case approach the following year in the *McCullough* case.<sup>50</sup> The Tribunal’s most common rate was 12% uncompounded,<sup>51</sup> but significant variation continued for the life of the Tribunal.

The European Court of Human Rights jurisprudence provides another case in point. Until late 2004, the Court awarded interest based on either the rate applicable in the petitioner’s state of citizenship or a currency-based rate without further explanation (typically between 4 and 8% simple interest).<sup>52</sup> The choice of rates in one case caused considerable contention on the

<sup>46</sup> See *McCullough v Ministry of Post, Telegraph & Telephone*, 11 Iran-U.S. Claims Trib. Rep. 3, para 97 (1986).

<sup>47</sup> See Westberg, above n 22, at 257.

<sup>48</sup> *Ibid.* at 258; Marboe, above n 33, at 357.

<sup>49</sup> *Sylvania Technical Sys., Inc. v Iran*, 8 Iran-U.S. Claims Trib. Rep. 298, 320 (1985); accord *Siemens A.G. v Argentina*, Award of 4 January 2007, ICSID Case No. ARB/02/8, para 396.

<sup>50</sup> *McCullough v Ministry of Post, Telegraph & Telephone*, 11 Iran-U.S. Claims Trib. Rep. 3, para 103 (1986).

<sup>51</sup> George H. Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal* (Oxford: Clarendon Press, 1996) 475–6.

<sup>52</sup> For example, *A.D.T. v United Kingdom*, 2000 E.C.H.R. 35765/97, para 48 & Order 3(b) (awarding the applicant, a U.K. citizen, ‘the statutory rate of interest applicable in the United Kingdom at the date of adoption of the present judgment [of] 7.5% [simple interest] per annum.’); *Lustig-Prean & Becket v United Kingdom*, 31 E.H.R.R. 23, para 40 (awarding the applicants, U.K. citizens, the statutory rate of interest of 8% simple interest per annum); *Fretté v France*, 38 E.H.R.R. 21, para 59 (2004) (awarding the applicant, a French citizen, the statutory rate of interest of 4.26% simple interest per annum); *Mouta v Portugal*, 31 E.H.R.R. 47, para 43 (2001) (awarding the applicant, a Portuguese citizen, the statutory rate of interest of 7% per annum).

bench, revealing that at least some judges were aware of the problems associated with inconsistent awards.<sup>53</sup> Only in 2004 did the Strasbourg Court adopt a uniform practice of including post-award simple interest equal to the variable marginal lending rate of the European Central Bank (ECB) plus 3% when the Court awards damages in euros.<sup>54</sup>

ICSID panels seem to be moving toward a consistent practice as well. Since 1990, they have increasingly awarded interest based on a widely used market rate, such as the U.S. Treasury bill rate, the London Inter-Bank Offered Rate (LIBOR), or the European Interbank Offered Rate (EURIBOR).<sup>55</sup> The T-bill rate is the rate offered by the U.S. government on bonds having a one to sixth month maturity. The interbank offered rates are reference rates at which banks borrow unsecured funds from other banks for brief periods (from one day to one year). Interbank rates change daily and are widely used for calculating variable rate mortgages and rates on various derivative financial instruments. Each of these rate types shares three key factors: (i) a short credit term, (ii) substantial variability over time, and (iii) an extremely low risk of default on the debt and an accordingly very low interest rate. Such rates, while used in only a narrow range of private commercial lending transactions, provide an easily ascertainable base rate.

## 2. *Risk-free or customized interest rates?*

The growing reliance on T-bill and interbank offered rates—effectively ‘risk-free’ rates—is gradually creating greater consistency in international arbitration and litigation, but it has not escaped criticism. Thierry S eneschal and John Gotanda have recently argued that international tribunals award interest below commercial rates typically obtained by business firms due to ignorance of economics and financial principles.<sup>56</sup> Because multinational enterprises may invest in financial instruments carrying significantly greater risk and corresponding reward than risk-free rates, they argue, international

<sup>53</sup> *Goodwin*, [2002] E.C.H.R. 28957/95 (Fischbach, J., concurring; T urmen, J., dissenting; Greve, J., dissenting).

<sup>54</sup> See, e.g. *Salduz v Turkey*, 49 E.H.R.R. 19, para 80 (2009); *Goodwin v United Kingdom*, [2002] E.C.H.R. 28957/95, para 124; *W oditschka & Wilfling v Austria*, 41 E.H.R.R. 32, para 44 & Order 5(c) (2005); *Karner v Austria*, 38 E.H.R.R. 24, 538 para 51 (2004); *S.L. v Austria*, 37 E.H.R.R. 39, para 56 (2003). Euro awards may be converted to the applicant’s national currency on the date of payment.

<sup>55</sup> See *Marboe*, above n 33, at 350–4; *Ortscheidt*, above n 41, at 261–2; John Yukio Gotanda, *Compound Interest in International Disputes* (Oxford University Comparative Law Forum, 2004) 2 [hereinafter Gotanda, *Compound Interest*]; S eneschal and Gotanda, above n 34, at 523–4; see, e.g. *Siag v Egypt*, Award of 11 May 2009, ICSID Case No. ARB/05/15, paras 597–8; *Funnekotter v Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award of 22 April 2009, paras 143–4, 48 I.L.M. 764 (2009); *MTD Equity Sdn. Bhd. v Chile*, Award of 21 May 2004, ICSID Case No. ARB/01/7, para 250; *Maffezini v Spain*, ICSID Case No. ARB/97/7, Award of 13 November 2000, 16 ICSID Rev.-FILJ 248, and 96 (2001); *Liberian E. Timber Corp. v Liberia*, ICSID Case No. ARB/83/2, Award of 31 March 1986, 2 ICSID Rep. 343, 379 (1994).

<sup>56</sup> S eneschal and Gotanda, above n 34, at 494.

tribunals should award interest at commercially comparable rates accounting for the claimant's risk preferences.<sup>57</sup> One attraction of this approach is that, if followed, it would create a certain parity between pre-award interest and lost profits determinations. Tribunals awarding interest would perform the same kind of analysis that they currently perform in awarding lost profits. In calculating lost profits, they weigh evidence that a specific amount of profits would have been predictably earned by the lost capital at the time of the loss. In essence, S eneschal and Gotanda propose that the same consideration of the claimant's individual circumstances should inform a determination of the appropriate interest rate on an award. A few international investment arbitration panels have recently adopted a similar line of reasoning.<sup>58</sup>

Because training in economics or finance is not required of international arbitrators and judges, S eneschal and Gotanda's claim is superficially plausible. On the whole, the sparse explanations offered by international tribunals for their interest awards have rarely displayed anything approaching a thorough understanding of modern principles of finance. However, a risk-free rate may nonetheless prove economically sound upon examination. A few international tribunals, at least, have displayed considerable economic nuance in their interest awards. In * eskoslovenska Obchodnı Banka A.S. v. Slovak Republic*, for example, the claimant argued that it should be entitled to 42.53% interest on the award, because it would have invested in Slovak government bonds paying that rate. In rejecting the argument, the tribunal noted not only an absence of evidence that the claimant would have purchased such bonds, but also that the rate was a nominal one reflecting very high inflation during the period and a higher risk of default.<sup>59</sup> Greater economic sophistication is gradually becoming more common among international arbitrators, though it does not yet represent the norm.

One potential explanation for why an international tribunal might avoid commercial rates of interest is that the tribunal may perceive that a commercial rate of interest overcompensates the claimant. S eneschal and Gotanda's hypothesis posits that risk-free rates fail to compensate commercial actors adequately because such actors are not risk-averse. They are aware of the immediate objection that, if international tribunals were to award commercial interest rates in arbitral awards, the claimant would benefit from the higher rate without undertaking the corresponding risk. They answer that 'over the long run', commercial actors could in some cases prove that an investment project would earn a higher than risk-free cash flow.<sup>60</sup>

<sup>57</sup> Ibid. at 510, 523–4.

<sup>58</sup> See, e.g. *National Grid PLC v Argentine Rep.*, UNCITRAL Award of 3 November 2008, para 294; *Siemens A.G. v Argentine Rep.*, ICSID Case No. ARB/02/8, Award of 6 February 2007, paras 399–400, 44 I.L.M. 138.

<sup>59</sup> Case No. ARB/97/4, Award of 29 December 2004, 13 ICSID Rep. 181, para 332.

<sup>60</sup> S eneschal and Gotanda, above n 34, at 526–7.

This argument appears to misapprehend the economic concept of risk. There is always a correlation between risk and rate of return; risk is a probability calculation inherent in the corresponding rate of return. That a project would very likely have earned a rate of return higher than a risk-free rate does not justify discounting the risk factor that primarily explains the higher return. Long-established business ventures frequently fail to earn the expected profits or even incur losses. Future earnings are always highly speculative. Because an international tribunal cannot retroactively impose risk on the victorious claimant, a commercial interest rate could<sup>61</sup> overcompensate the claimant by awarding it an amount that includes a risk premium, when in fact the claimant was never forced to undertake any commercial risk. Consequently, it could be argued that a risk-free interest rate best approximates the claimant's actual loss in most cases.

A potential rejoinder is that, because awards of lost profits correspond to the claimant's actual loss, awards of interest should do the same. In this connection, some commentators have distinguished between 'interest on damages' versus 'interest as damages', the latter typically referring to interest awarded because the claimant incurred actual costs—usually by borrowing to mitigate damages caused by the respondent's breach of contract or other wrongful act, although the necessity of borrowing could be hypothetical.<sup>62</sup>

While appealing, the argument requires further nuance. An award of lost profits is usually calculated based on the market value of the business, including expected discounted future cash flows, at the time of the expropriation or other injury.<sup>63</sup> The value is projected rather than retrospective; it does not rely on 20–20 hindsight, but rather on the amount at which the asset's value would have been estimated at the time of loss. Although lost profits calculations should not account for *de facto* market conditions that would increase or decrease the profits that were not reasonably foreseeable at the time of loss, if determined properly, the value should include an adjustment for risk and uncertainty (as in fact often occurs).<sup>64</sup>

<sup>61</sup> 'Could', because, if the investment involves a state-sanctioned monopoly or other investment where the primary uninsured risk involves some kind of state interference or breach of contract, the investor's risk-free rate of return may be higher than the risk-free market rate. An example of such an advantage occurred in *Benvenuti et Bonfant Sarl v People's Republic of Congo*, Award of 8 August 1980, ICSID Case No. ARB/77/2, 21 I.L.M. 740 (1982), in which the government of Congo agreed to adopt *inter alia* measures to protect the foreign investor from import competition.

<sup>62</sup> See Louis Sohn and Richard Baxter, Draft Convention on the International Responsibility of States for Injuries to Aliens, Draft No. 12, § 38(1), Explanatory Note, reprinted in 55 *American Journal of International Law* 242 (1961); SÉNÉSCHAL and GOTANDA, above n 34, at 514–21.

<sup>63</sup> See John Y. Gotanda, 'Recovering Lost Profits in International Disputes', 36 *Georgetown Journal of International Law* 61 (2004) 90–2 [hereinafter Gotanda, *Recovering Lost Profits*].

<sup>64</sup> See, e.g. Final Award in Case No. 8445 of 1996, 26 Y.B. Comm. Arb. 167 (2001), at 175–77 (ICC arbitration).

The different risk profiles confronting a borrower and lender may justify varying treatment of different classes of claimants. The value of the loss of an unleveraged asset or debt-free claimant is properly measured by a risk-free rate, because the award removes any hypothetical risk to the extent that the respondent state can be relied upon to honor it (which in the case of international arbitration and litigation is very great as a rule).<sup>65</sup> The actual risk undertaken by the claimant will have been negligible in most cases. In many investment arbitrations and human rights cases, especially those involving the loss of an unleveraged asset or injury to a debt-free claimant, the lost time-value of the award is properly measured by a risk-free rate.

In contrast, the borrower rate of interest is high to reflect the possibility of the debtor's default, which a belated award of compensation by an international tribunal does not retroactively mitigate. The value of the loss of a highly leveraged asset, then, is properly calculated according to the claimant's cost of borrowing—usually well above a T-bill or interbank offered rate. Indeed, the problem of risk and uncertainty disappears in the case where the injury actually forced the claimant to borrow at a commercial rate of interest to mitigate its damages. The claimant's rate of borrowing necessarily sets the standard for an award of *restitutio in integrum*. In such cases, a risk-free interest rate will undercompensate the claimant except where the claimant was able to borrow at that rate. An invariable practice of setting interest at a risk-free rate will, consequently, result in insufficient compensation in at least some cases.

## B. The question of compounding

States differ in their domestic laws of remedies with respect to whether prejudgment or postjudgment interest may be compounded.<sup>66</sup> In early international arbitration, tribunals and claims commissions followed a fairly consistent pattern of declining to compound interest awards, so that, in 1943, Marjorie Whiteman could claim that a well settled rule of international law

<sup>65</sup> Michael Knoll has argued in a U.S. domestic context that the defendant's cost of borrowing is always the correct rate for prejudgment interest when the plaintiff is an individual, on the theory that the plaintiff 'invested in' the defendant by involuntarily loaning the defendant the compensation due to it. See Michael Knoll, 'A Primer on Prejudgment Interest', 75 Texas Law Review 293 (1996), at 308–11. This analysis does overlook that the defendant's borrowing rate is based on investment risk that the plaintiff did not in fact assume due to the fact that compensation was awarded to the plaintiff by a court of law. While, in a private law context, there is always some risk that a private defendant will become insolvent and prove unable to satisfy the judgment, sovereign states do not often become totally insolvent.

<sup>66</sup> In selective surveys of state practice, John Gotanda and Jérôme Ortscheidt have separately observed that many states generally award simple rather than compound interest, but this practice has many varied exceptions. Gotanda, *Compound Interest*, above n 55, at 2; Ortscheidt, above n 41, at 273–5.

disfavored awards of compound interest.<sup>67</sup> This practice diverged from private commercial practice, where interest on virtually all debt is compounded periodically. In the past thirty years, international arbitration and claims practice has increasingly, if unevenly, come to reflect commercial practice in favor of compound interest.

Nonetheless, international law has not yet developed a firm rule mandating the compounding of interest in claims against states, and some tribunals have remained steadfast in declining to compound interest on awards in cases involving sovereign respondents. The Iran–U.S. Claims Tribunal, for example, generally refused to compound pre-award interest based upon perceived historical practice,<sup>68</sup> and the practice of the European Court of Human Rights is consonant.<sup>69</sup> North American Free Trade Agreement panels and *ad hoc* panels, too, have often awarded simple interest in the recent past.<sup>70</sup>

The *Santa Elena* case initiated a gradual change in ICSID treatment of compound interest awards.<sup>71</sup> There, the tribunal noted the general trend against awards of compound interest in breach of contract claims, but distinguished claims for expropriation, in which compound interest was often awarded.<sup>72</sup> In the tribunal's view, the award of simple or compound interest is within the discretion of the tribunal, which must weigh issues of fairness.<sup>73</sup> However, the tribunal then noted that whenever an injury occurs in which a claimant is deprived of pre-award interest that could have been reinvested, the award should reflect 'at least in part' that loss in the form of compound interest.<sup>74</sup> Similar reasoning was deployed in *Wena Hotels Ltd. v. Egypt*,<sup>75</sup> where the tribunal justified its decision to award interest compounded

<sup>67</sup> See Marjorie Whiteman, *Damages in International Law 1997* (Washington, DC: U.S. Gov't Printing Off., 1943), vol. 3.

<sup>68</sup> See, e.g. *Anaconda-Iran, Inc. v Iran*, 13 Iran-U.S. Claims Trib. Rep. 199, 234 (1988); *R. J. Reynolds Tobacco Co. v Iran*, 7 Iran-U.S. Claims Trib. Rep. 181, 191 (1986); *Starrett Housing Corp. v Iran*, 16 Iran-U.S. Claims Trib. Rep. 112 (1987). But see *ibid.* at 252 (Holtzmann, J., dissenting) (arguing that an award of compound interest is appropriate because banks charge compound interest in their 'normal commercial practice').

<sup>69</sup> See, e.g. *Arnarsson v Iceland*, 2003 E.C.H.R. 365, 427, 39 E.H.R.R. 20 (2004) (awarding simple interest on award for period between award and settlement); *B.B. v United Kingdom*, 39 E.H.R.R. 30 (2004) (same); *A.D.T. v United Kingdom*, 2000 E.C.H.R. 35765/97, para 48 & Order 3(b) (same).

<sup>70</sup> See, e.g. *Feldman v Mexico*, NAFTA Panel, Award of 16 December 2002, 42 I.L.M. 625, para 206 (2003); *American Indep. Oil Co. (Aminoil) v Kuwait*, 21 I.L.M. 976, 1042, para 178 (1982).

<sup>71</sup> *Compañía del Desarrollo de Santa Elena, S.A. v Costa Rica*, 15 ICSID Rev. 169, 205 (2000).

<sup>72</sup> *Ibid.* paras 95–7 (citing *inter alia* *Sylvania Tech. Serv. v Iran*, 8 Iran-U.S. Claims Trib. Rep. 298 (1985)); see, e.g. *Wena Hotels Ltd. v Egypt*, 41 I.L.M. 919 (2002); *Metalclad Corp. v Mexico*, 40 I.L.M. 36 (2001); *American Indep. Oil Co. (Aminoil) v Kuwait*, 66 I.L.R. 518, 613, 21 I.L.M. 976 (1982).

<sup>73</sup> *Compañía del Desarrollo de Santa Elena*, 15 ICSID Rev. para 103.

<sup>74</sup> *Ibid.* para 104.

<sup>75</sup> 41 I.L.M. 896 (2002).

quarterly by the fact that almost all commercial and financial instruments—in which the claimant could have invested compensation received for the injury—pay compound interest.<sup>76</sup>

ICSID tribunals have increasingly followed the *Santa Elena* line of reasoning and awarded compound interest in expropriation cases.<sup>77</sup> It is now common for ICSID tribunals to award compound interest without seeing any need for justification, although these tribunals have achieved no uniformity in setting the compounding period.<sup>78</sup> ICSID tribunals have departed from *Santa Elena* in awarding compound interest in cases not involving direct expropriation, however. For example, in *Maffezini v. Spain*,<sup>79</sup> an ICSID tribunal granted an investor interest on an award rendered to compensate the investor for interference with its investment by an agency of the Spanish government. The tribunal found that the claimant (an Argentinian investor) had formed a Spanish corporation as a joint venture with a Spanish government-controlled company. After the joint venture began to experience financial difficulties, the Spanish government entity transferred funds from the claimant's personal bank account to the joint venture in the form of a loan without the claimant's consent.<sup>80</sup> After finding the respondent liable for the unauthorized transfer, the tribunal granted the claimant pre-award interest, then compounded the interest on an annual basis on the ground that 'the funds were withdrawn from [the claimant's] time-deposit account'.<sup>81</sup> The tribunal fixed the interest rate at the LIBOR rate for the Spanish peseta.<sup>82</sup> The tribunal also allowed post-award interest at a rate of 6% per annum, compounded monthly.<sup>83</sup>

<sup>76</sup> Ibid. at 919, quoting John Y. Gotanda, 'Awarding Interest in International Arbitration', 90 *American Journal of International Law* 40 (1996), at 61 [hereinafter Gotanda, *Awarding Interest*].

<sup>77</sup> See, e.g. *Funnekotter v Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award of 22 April 2009, paras 145–6, 48 I.L.M. 764 (2009); *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000, 40 I.L.M. 36, para 128 (2001); *Desert Line Projects LLC v Republic of Yemen*, ICSID Case No. ARB/05/17, Award of 6 February 2008, paras 293, 295, 48 I.L.M. 82 (2009); *Siemens A.G. v Argentine Rep.*, ICSID Case No. ARB/02/8, Award of 6 February 2007, 44 I.L.M. 138, para 399.

<sup>78</sup> Compare *Funnekotter v Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award of 22 April 2009, paras 145–6, 48 I.L.M. 764 (2009) (granting interest at 10% compounded every six months) with *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000, 40 I.L.M. 36, para 128 (2001) (granting pre-award interest at 6% compounded annually). ICSID tribunals have never to my knowledge compounded pre-award interest on less than a six-monthly basis, but post-award interest is commonly compounded on a monthly basis. See, e.g. *ADC Affiliate Ltd. v Hungary*, ICSID Case No. ARB/03/16, para 522.

<sup>79</sup> ICSID Case No. ARB/97/7, Award of 13 November 2000, 16 ICSID Rev. 212 (2002).

<sup>80</sup> Ibid. paras 72, 75–6.

<sup>81</sup> Ibid. para 96.

<sup>82</sup> Ibid.

<sup>83</sup> Ibid. para 97. See also *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, 26 Y.B. Comm. Arb. 99 (2001), at para 131.

Although no firm rule of international law has developed in favor of compounding interest, the growing preference in international investment practice for compound interest comports with economic reasoning, equity, and pragmatic considerations alike.<sup>84</sup> Because both debt and investments usually pay compound interest, awarding simple interest to a claimant effectively deprives the injured party of sums that it would have received had the injury been compensated immediately. In other words, because the claimant could have invested the compensation and, subsequently, reinvested interest received on that investment, compound interest is a necessary component of the reparations due under the *Chorzów Factory* doctrine. Alternatively, if the claimant had debts, it could have paid off debts through the award, thereby avoiding the payment of compound interest on the debt.<sup>85</sup> By extension, not awarding compound interest to the claimant confers a windfall on the respondent state. Had the respondent borrowed money from the claimant (the economic equivalent of not paying the claimant damages in a timely manner), it would have paid compound interest on the borrowed sum, because commercial debt is expected to bear compound interest.

It follows that failing to award compound interest effectively forces the claimant to loan part of the funds it would have received upon prompt compensation for the injury to the respondent itself, in effect subsidizing the very party that injured it. Such a situation would give the respondent that is earning compounded returns on its own investments, or paying compound interest to creditors, an incentive to draw out litigation through dilatory tactics, because, for the period during which the respondent resists payment, the interest payable on the respondent's debt to the claimant confers an economic benefit on the respondent. Quite aside from the inequity of depriving a party already injured of full compensation and allowing the responsible party to profit from its own delay in paying compensation (*commodum ex iniuria sua nemo habere debet*<sup>86</sup>), effectively forcing the claimant to loan money to the respondent for the period between the injury and the award (and possibly thereafter) does little to advance the international community's interest in encouraging the prompt settlement of disputes or the expeditious satisfaction of arbitral awards.

<sup>84</sup> Numerous publicists have strongly advocated the general use of compound interest in international arbitral awards, mostly on economic or equity grounds. See, e.g. F.A. Mann, 'Compound Interest as an Item of Damage', in F.A. Mann (ed.), *Further Studies in International Law* (Oxford: Oxford University Press, 1990) 378, 383; Gotanda, *Awarding Interest*, above n 76, at 61; Gotanda, *Compound Interest*, above n 55; Yves Derain, *Intérêts moratoires, dommages-intérêts compensatoires et dommages punitifs devant l'arbitre international*, in *Études offertes à Pierre Bellet* (Paris: Litec, 1991) 101, 114.

<sup>85</sup> Gotanda, *Compound Interest*, above n 55.

<sup>86</sup> See Fellmeth and Horwitz, above n 7, at 58.

### C. Timing of interest

In calculating interest, an international tribunal must decide from what date interest begins accruing, sometimes called the *dies a quo*.<sup>87</sup> National legal systems differ in the time from which interest begins to accrue—usually, either the date of the injury or the date of the award, although some states begin interest on an intermediate date, such as the date that the claimant asserted a demand for performance or compensation.<sup>88</sup> Given that any delay in compensation to an injured party inevitably aggravates the injury, the non-universality of prejudgment interest awards in municipal practice may seem surprising. The usual rationale for the denial of prejudgment interest is that, until a tribunal has fixed the amount of compensation due, or at the very least until the defendant has been presented with a demand by the plaintiff, the defendant cannot know what amount of compensation it owes to the plaintiff, or whether it is even legally liable to the plaintiff. It would be unfair, in this view, to exact interest from the defendant on an ‘unliquidated’ claim that it did not know with certainty it legally owed to the plaintiff.

Historically, international practice largely followed this reasoning and disallowed pre-award interest altogether, while often allowing post-award interest.<sup>89</sup> The 1922 U.S.-German Mixed Claims Commission,<sup>90</sup> the Mexico-U.S. General Claims Commission,<sup>91</sup> and the French-Mexican Claims Commission<sup>92</sup> all distinguished between liquidated and unliquidated claims.<sup>93</sup> In liquidated claims, interest is calculated from the date of the injury and, in unliquidated claims, from the date of the award. The PCIJ in *The Wimbledon* continued this practice, declining to grant pre-award interest on the theory that the amount owed had not become ‘fixed and the obligation to pay... established’ until the award was rendered.<sup>94</sup> Perhaps because of its antiquity and the range of authorities endorsing it, the liquidated-unliquidated paradigm has proven tenacious. Although the

<sup>87</sup> *Ibid.* at 80.

<sup>88</sup> See Georg Schwarzenberger, *International Law*, 3rd ed. (London: Stevens & Sons Ltd., 1957), vol. 1, 675; Reitzer, above n 11, at 194; SÉNÉSCHAL and GOTANDA, above n 34, at 501.

<sup>89</sup> See, e.g. *Delagoa Bay Rwy. Co. (Port. v Gr. Brit.)*, Moore, above n 14, vol. 2, at 1865; *Norwegian Claims Case (Nor. v U.S.)*, Award of 13 October 1922, 1 R.I.A.A. 309, 311 (1922) (post-award interest at 6% being provided for in the *compromis*); *Spanish Zone of Morocco Claims*, 2 Annual Digest of Public International Law 207 (1924).

<sup>90</sup> *Case Concerning Administrative Decision No. III (U.S.-Ger. Mixed Cl. Comm’n)*, 7 R.I.A.A. 64, 70 (1923).

<sup>91</sup> *Illinois Central R.R. Co. v Mexico (Mex.-U.S. Gen. Cl. Comm’n)*, 6 December 1926, 4 R.I.A.A. 134, 136.

<sup>92</sup> A.H. FELLER, *The Mexican Claims Commission* (New York: MacMillan, 1935) 309.

<sup>93</sup> See also, e.g. *The Macedonian Case (U.S.-Chile)*, Moore, above n 14, vol. 2, at 1449; *Cervetti Case (Italy-Venez.)*, 10 R.I.A.A. 492, 497 (1903).

<sup>94</sup> *The Wimbledon Case*, PCIJ Ser. A, No. 1, at 32.

practice of limiting interest to post-award periods was criticized by Salvioli as early as 1933,<sup>95</sup> it continues in many cases. It was observed as recently as 1977 by the tribunal in *Libyan American Oil Co. v. Libya*, which held that interest should not run on unpaid ‘compensation’ of unknown amount owed to the claimant, but rather should apply only to ‘damages’ awarded by the tribunal.<sup>96</sup>

As international claims practice has progressed, post-award interest has become standard,<sup>97</sup> and while pre-award interest has become more common, but it remains far from universally accepted. As one chamber of the Iran-U.S. Claims Tribunal observed, international tribunals have been markedly inconsistent in their decisions to allow pre-award or post-award interest and to fix the time whence interest will run: ‘In some cases, the starting point is fixed at the time when the damage occurred. In yet other cases, the date of the award or of its notification or a specific date after the award, is determinative.’<sup>98</sup> ICSID tribunals have begun to favor the view that interest is part of the compensation for the wrongful act and, accordingly, should run ‘from the date when the State’s international responsibility became engaged’,<sup>99</sup> usually meaning the date of injury.<sup>100</sup> But European Court of Human Rights judgments continue to omit pre-award interest, and some ICSID tribunals continue to decline to allow pre-award interest

<sup>95</sup> Gabriele Salvioli, *Les règles générales de la paix*, 46 *Receuil des Cours* 252 (1933-IV).

<sup>96</sup> Award of 12 April 1977, 62 I.L.R. 141, 215 (1982).

<sup>97</sup> See, e.g. *Arnarsson v Iceland*, 39 E.H.R.R. 20 (2004), at 427; *Compañía del Desarrollo de Santa Elena, S.A. v Costa Rica*, 15 ICSID Rev. 169, 205 (2000); *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000, 40 I.L.M. 36, para 128 (2001); *Sedco, Inc. v National Iranian Oil Co.*, 15 Iran-U.S. Claims Trib. Rep. 129, para 589 (1987).

<sup>98</sup> See *McCullough v Ministry of Post, Telegraph & Telephone*, 11 Iran-U.S. Claims Trib. Rep. 3, para. 95 (1986) (footnotes omitted); see also Schwarzenberger, above n 88, vol. 1, at 675 (noting inconsistency in the *dies a quo* interest runs in international decisions); Gray, above n 16, at 169–70 (noting a lack of consistency and precision in international administrative tribunal and European Court of Justice awards of interest).

<sup>99</sup> *Asian Agricultural Prods. v Sri Lanka*, Case No. ARB/87/3, Award of 27 June 1990, 4 ICSID Rep. 245, 294, para 114; accord *Metalclad Corp. v Mexico*, ICSID Case No. ARB(AF)/97/1, Award of 30 August 2000, 40 I.L.M. 36, para 128 (2001).

<sup>100</sup> The UN Compensation Commission (UNCC) consistently allowed pre-award interest whenever lost profits were unavailable, but special conditions made some such awards precarious. The UNCC’s Governing Council specified that both pre-award and post-award interest should be awarded at appropriate rates, but reimbursement for damages would take precedence over reimbursement for interest. UN Compensation Comm’n, Governing Council, Decision 16, S/AC.26/1992/16.\*/, 4 January 1993. If pre-award interest constituted ‘interest’ rather than ‘damages’ under its definition, many years of lost time value of the damages could be forfeited should the Commission’s fund run out. In the event, the issue never arose, because the modest awards recommended by the UNCC panels did not quickly exhaust the fund. In any case, most tribunals have considered pre-award interest to constitute part of the damages rather than a separate cause of action. See, e.g. DEC 65-A 19-FT, 16 Iran-U.S. Claims Trib. Rep. 785, para. 12 (1987). Generally, however, the distinction is of little practical consequence to the claimant under current law.

except when confirming a prior arbitral award, in which case the interest only runs from the date of the prior award.<sup>101</sup>

While the practice of refusing pre-award interest may seem logical in light of the uncertainty of the damages owed to the claimant before the tribunal issues its decision, and has indeed persuaded some commentators,<sup>102</sup> the same logic would apply to any award or judgment. The necessary implication of this course of reasoning is that the respondent state does not actually owe the claimant compensation until a tribunal has officially quantified the injury and stipulated the amount owed. The possible rationales for this approach, which seem to relate mainly to concerns of equity and avoiding punishing the respondent for failure to pay a sum not yet fixed by a legal authority, are explored in more detail in Section III. Whatever the theory underlying the denial of pre-award interest, however, it is inconsistent both with the doctrine that an international tribunal's award recognizes but does not create legal liability for a wrongful act and, more important, with basic economic theory.

### III. EXPLANATIONS FOR BELOW-MARKET INTEREST AWARDS

The preceding discussion illustrates a continuing, if gradually abating, dissonance between the jurisprudential orthodoxy of full compensation and the actual practice of international tribunals in awarding interest. The aversion to full economic measures of interest reveals itself not only in the occasional past use of the arbitrary rule of *alterum tantum*,<sup>103</sup> but in the refusal of tribunals to award both pre-award and post-award compound interest. It is also indirectly evident in the reluctance of tribunals to explain how calculations of interest figured into their awards and to justify the choice of rates.

Several authors have noted that no method of assessing damages, particularly interest, has consistently been adopted by the tribunals.<sup>104</sup> Christine Gray has hypothesized that damages awards 'may well depend not so much on the extent of the injury suffered but rather on various political considerations including the relative power of the two states.'<sup>105</sup> If the facts support Gray's thesis, they do not do so robustly. There is no discernable pattern in modern arbitral practice that consistently favors the more politically, economically, or militarily powerful state. Tribunals have tended to award direct damages tracking the evidence fairly closely. In no case was *damnum emergens* awarded in an amount representing a radical departure from the offers of evidence (at least, from the evidence recited by the tribunal in its

<sup>101</sup> For example, *Desert Line Projects LLC v Republic of Yemen*, ICSID Case No. ARB/05/17, Award of 6 February 2008, para 298, 48 I.L.M. 82 (2009).

<sup>102</sup> For example, Ortscheidt, above n 41, at 268–70.

<sup>103</sup> See Fellmeth and Horwitz, above n 7, at 27.

<sup>104</sup> See, e.g. Gray, above n 16, at 6; J. Subilia, *L'Allocation d'intérêts dans la jurisprudence internationale* (Thesis, Lausanne 1972) (on file with the author).

<sup>105</sup> Gray, above n 16, at 6.

opinion). On the other hand, political considerations relating to the position of the tribunal relative to the states may have played some role in persuading arbitrators to adopt consciously or unconsciously a conciliatory posture primarily toward states in the portion of the award least bound by firm rules and most subject to discretion and flexibility—the award of interest.

There are four rationales that might explain why international tribunals would hesitate to award full and economically precise interest against state respondents. The one with the longest pedigree posits that interest impermissibly punishes the respondent state for failing to compensate the injury. A second explanation is that continuing even a pathological remedies doctrine may serve the international community's need for stability by conforming to the community's expectations about interest awards. A third explanation is based on the deference that international authorities traditionally afford to sovereign states. Finally, it is useful to consider that the international community's expectations about the role of international tribunals focus on their ability to settle disputes effectively or expeditiously, rather than on their strict compliance with economic justice.

### A. Characterization of interest as punitive

One reason international tribunals sometimes deny interest is the assumption that interest awards are punitive. In several cases from the nineteenth and early twentieth centuries, international tribunals explicitly justified the exclusion of any interest whatsoever against a respondent state because international law forbids punishing a sovereign.<sup>106</sup> In modern cases, the theory is rarely explicit, but rather seems implicit in the tribunal's reasoning. For example, international tribunals sometimes justify a denial of pre-award interest because the respondent state had not engaged in any dilatory tactics. The Eritrea-Ethiopia Claims Commission, which was charged with ascertaining violations of international law during the 1998–2000 war between those countries and ordering compensation to successful claimants, denied interest to both parties on precisely those grounds.<sup>107</sup> The tribunal's reasoning in its final award implied that, in case of dilatory tactics, it might have awarded interest to compensate the other party, but losses caused by the delay between injury and compensation do not turn on the question of whether a

<sup>106</sup> See Personnaz, above n 11, at 232–3 and examples cited therein.

<sup>107</sup> Final Award: Eritrea's Damages Claims (Erit.-Eth.), para 44 (17 August 2009), at <http://www.pca-cpa.org>. Another basis for refusal to award interest was that, because the awards to the respective parties and the delays involved were approximately equivalent, interest awards would have canceled each other out. Of course, this is not an especially persuasive rationale given that the same is true of the damages awards themselves. Moreover, the denial or award of interest carries substantial economic significance in the event that one state party pays on its award in a timely manner but the other does not, because post-award interest will be increased through running on pre-award interest as well as the direct damages.

party has intentionally caused the delay. The injury is the same regardless of the reason for it. Evidently, the tribunal viewed the award of interest as a potential punishment for and deterrent of dilatory tactics.

Further evidence is implied in the doctrine of contributory fault. As early as the 1930s, Personnaz found it '*un principe bien établi qu'une faute du réclamant peut lui faire perdre son droit aux intérêts* [a well established principle that the claimant's misconduct can cause him to lose his right to interest]', either when the claimant's contributory act aggravated its own direct damages or when a claimant unjustifiably delayed in the filing of the claim.<sup>108</sup> The theory is evidently that the respondent state should not suffer, and the claimant should not benefit, by the claimant's own act (again, *commodum ex iniuria sua*, but this time reversing the parties). The implication is that the award of interest harms the respondent and benefits the claimant without providing any countervailing consideration.

That states are generally immune to punitive damages claims is well established customary international law,<sup>109</sup> but compound interest at a risk-free or even commercial rate cannot be characterized as 'punitive' without grossly distorting the meaning of the term.<sup>110</sup> Because they are a necessary component of full reparations and have no retributive or deterrent effect, they are properly characterized as remediation. ICSID tribunals in several cases have understood this point, expressly rejecting the argument that pre-award interest should be denied as punitive.<sup>111</sup>

As for the dilatory tactics and contributory fault theories, from a purely economic perspective, it is difficult to imagine a case in which a denial of interest would be justified. It is unlikely that many claimants voluntarily

<sup>108</sup> Personnaz, above n 11, at 230. Given the prevalence of creeping expropriation in modern foreign investment law practice, determining the date of injury, and thus the date beyond which the claimant's delay in filing a claim is unreasonable, has become more difficult than it was when Personnaz wrote. Cf. Reisman and Sloane, above n 18, at 143–7 (discussing the difficulties confronting foreign investors of determining when a claim for expropriation should be brought).

<sup>109</sup> See Schwarzenberger, above n 7, vol. 1, at 673. But see *Sedco, Inc. v National Iranian Oil Co.*, 10 Iran-U.S. Cl. Trib. Rep. 180 (1986), 25 I.L.M. 629, 648 n. 35 (Brower, J., concurring) (suggesting that punitive damages might be worth considering as a deterrent to unlawful expropriation).

<sup>110</sup> See generally Aaron Xavier Fellmeth, 'Civil and Criminal Sanctions in the Constitution and Courts', 94 Georgetown Law Journal 1 (2005) (distinguishing between remediation and punishment based on the systemic effect of the sanction to restore the victim to the *status quo ante* on one hand or to effectuate retribution or deterrence on the other, with deterrence defined as punishment to a degree that would prevent most rational persons from engaging in the sanctioned conduct).

<sup>111</sup> See, e.g. *Compañía del Desarrollo de Santa Elena v Costa Rica*, 38 I.L.M. 1317, para 104 (2000); *Middle East Cement Shipping & Handling Co. S.A. v Arab Rep. of Egypt*, ICSID Case No. ARB/99/6, Award of 12 April 2002, 18 ICSID Rev.-FILJ 602, para 175 ('It is not the purpose of compound interest to attribute blame to, or to punish, anybody for the delay in the payment made to the expropriated owner; it is a mechanism to ensure that compensation awarded to the Claimant is appropriate in the circumstances.').

delay seeking reparations. More common are cases in which the claimant delays seeking redress due to uncertainty about when his right to seek damages has ripened (as in the case of creeping expropriation<sup>112</sup>) or due to attempts to exhaust local remedies before seeking remedies in an international forum (as in the case of human rights violations). In the relatively unusual event that the claimant has unjustifiably delayed in seeking reparations, a denial of interest may carry superficial appeal, but interest neither punishes the respondent state nor rewards the claimant. Interest is merely a measure of the time value of money—in this case, the compensation due to the claimant—and, assuming the interest rate awarded by the tribunal is not excessive, one paying interest is only ‘harm’d by the necessity of paying in direct proportion to the benefit it receives from not having compensated the underlying injury. Similarly, the claimant receives no benefit from the payment of interest other than what is necessary to offset the harm of losing the time value of the compensation admittedly due to it.

The response to the contributory fault theory is comparable. Where the claimant contributed to his own damages, the proper response would be to reduce the damages awarded by an amount commensurate with the claimant’s fault. Interest on that amount will accordingly be reduced in proportion to the reduction of the principal. Whatever the claimant’s contribution to his own injury, it is logically unrelated to the delay in compensation for that injury to the extent it was caused by the respondent state.

One could object that an unjustified delay in seeking compensation constitutes a forced loan by the claimant to the respondent, and an international tribunal ought to hesitate before assisting a claimant to compel a sovereign state to assume an increased debt burden. True, it might be argued that the respondent may well have been free to compensate the claimant at any time prior to the filing of the claim. By choosing not to compensate the claimant, the respondent effectively elected to borrow from the claimant the compensation due. But the respondent may have been unaware or uncertain of the claimant’s injury or the respondent’s role in causing that injury, and the amount of the compensation due may have been unsettled.<sup>113</sup>

The problem with this rejoinder is that it continues in the erroneous assumption that interest harms the respondent state. The fact that the loan is ‘forced’ upon the respondent does not transform an award of interest into punishment. Because interest is almost always awarded at the prevailing market rate—frequently below it, as John Gotanda has pointed out<sup>114</sup>—the lapse of time between the wrongful act and the payment of compensation

<sup>112</sup> See Reisman and Sloane, above n 18. As these authors observe, pressuring investors to bring a premature claim in response to adverse host state regulation has potential negative consequences for the dispute resolution process.

<sup>113</sup> See Personnaz, above n 11, at 234.

<sup>114</sup> Gotanda, *Awarding Interest*, above n 84, *passim*.

offers no benefit to the claimant. It may arguably harm the respondent if the respondent positively wished not to assume debt, but the near universality of significant government debt<sup>115</sup> saps the force of this argument. If debt at moderate or risk-free rates were harmful to states, they could hardly be expected to assume it voluntarily on a regular basis.

## B. The roles of stability and inertia

The explanation for the preference for simple interest and lost profits at least partly appears to reflect legal inertia. Gotanda has surmised that the preference for simple interest may originate in a time when domestic courts were able to resolve cases quickly, making the difference between simple and compound interest relatively insignificant.<sup>116</sup> This may be accurate; the rejection of compound interest or indeed pre-award interest altogether may be a case of indiscriminate international borrowing from domestic sources of law.<sup>117</sup> Because economically accurate interest is rarely awarded in domestic legal practice, it should perhaps be unsurprising that international tribunals decline to award such damages as well. This hypothesis finds support in the tendency of international tribunals to refer to state domestic practices in assessing rates of interest on damages awards<sup>118</sup> and in the fact that international arbitrators nearly always have training in the practices of their domestic legal systems.

On the other hand, international tribunals sometimes observe significantly that, because international and domestic legal regimes governing damages awards developed separately, domestic practices have no necessary relevance to the question of how an international tribunal should decide a similar question of law.<sup>119</sup> Moreover, the settlement of international disputes has never been especially prompt. If the denial of compound pre-award interest borrows from municipal practice, the choice is inapposite.

Whatever the remote origin of the pattern of awarding suboptimal interest, it does not explain its longevity in an era of increasing economic sophistication. One possible explanation for its modern persistence is that, although international arbitral tribunals and courts are rarely bound by precedent, they may continue an established practice from a perceived duty to foster

<sup>115</sup> For the past ten years, almost all OECD member states have more or less continually carried government debt over 20% — and often over 40% — of their annual GDPs. See OECD.Stat Extracts, Central Government Debt, at <http://stats.oecd.org> (visited 21 May 2010). Developing countries typically have comparable or much higher debt ratios. See International Bank for Reconstruction & Development, World Development Indicators 2009, at 199–200, at <http://siteresources.worldbank.org/DATASTATISTICS/Resources/wdi09introch4.pdf> (visited 21 May 2010).

<sup>116</sup> Gotanda, *Compound Interest*, above n 55.

<sup>117</sup> See Lauterpacht, above n 11.

<sup>118</sup> See Gray, above n 16, at 6–7; Ortscheidt, above n 41, at 258–61.

<sup>119</sup> For example, *George Pinion Case (Fr. v. Mex.)*, 5 R.I.A.A. 327, 448 (1928).

stability and predictability in international decision processes.<sup>120</sup> International tribunals have in fact often relied on precedents from a time when lawyers could boast of relatively little economic sophistication, not from a conviction that economically sound interest would be bad policy, but out of concern not to upset the settled expectations of the international community. The very fact that interest may overshadow direct damages may be thought to argue for continuing past practices of refusing pre-award interest or avoiding compounding, because very high awards may specially disturb these expectations. Support for this thesis may be found in the heavy reliance on legal precedents rather than economic reasoning in the decisions of arbitral tribunals and claims commissions; early decisions commonly relied on the absence of precedent in favor of awarding compound interest to justify rejecting the claimant's request.<sup>121</sup> The Iran–U.S. Claims Tribunal similarly leaned heavily on precedent, even while recognizing that the rejection of compound interest in international practice was not totally uniform.<sup>122</sup> Some tribunals have even justified uniform treatment of interest as a desirable practice based on the pragmatic advantages to the business community of certainty and stability.<sup>123</sup>

Obviously, the value of precedent must have limits; whatever benefits a harmonious line of arbitral and judicial precedents confers on the international community, other considerations will carry greater weight from time to time. It may be that the economic significance of pre-award interest or of compounding in many cases is insufficient to outweigh the value of stability and predictability. Yet, given the unusual variation in international practice relating to awards of interest, it could hardly be argued that the *status quo* is invested with a great deal of either of these virtues.

### C. Deference to sovereignty

The position of a sovereign state as a litigant is a unique one that calls for special circumspection and political sensitivity on the part of an international

<sup>120</sup> See, e.g. *Saipem S.p.A. v Bangladesh*, ICSID Case No. ARB/05/07, Decision of 21 Mar. 2007, para 67 ('The Tribunal considers that it is not bound by previous decisions. At the same time... [i]t believes that, subject to compelling contrary grounds, it has a duty to adopt solutions established in a series of consistent cases. It also believes that, subject to the specifics of a given treaty and of the circumstances of the actual case, it has a duty to seek to contribute to the harmonious development of investment law and thereby to meet the legitimate expectations of the community of States and investors towards certainty of the rule of law.')

<sup>121</sup> For example, *British Claims in the Spanish Zone of Morocco (U.K. v Sp.)*, 2 R.I.A.A. 641 (1925); *Norwegian Shipowners' Claims (Nor. v U.S.)*, Award of 13 October 1922, 1 R.I.A.A. 307 (1922); *Christern & Co Case (Ger. v Venez.)*, 10 R.I.A.A. 363 (1903).

<sup>122</sup> See, e.g. *McCullough & Co. v Ministry of Post, Telegraph & Telephone*, 11 Iran-U.S. Claims Trib. Rep. 3, 28 (1986); *Anaconda-Iran, Inc. v Iran*, 13 Iran-U.S. Claims Trib. Rep. 199, 234 (1988); *R. J. Reynolds Tobacco Co. v Iran*, 7 Iran-U.S. Claims Trib. Rep. 181, 191 (1986); *Starrett Housing Corp. v Iran*, 16 Iran-U.S. Claims Trib. Rep. 112 (1987).

<sup>123</sup> For example, *Sylvania Tech. Sys. Inc. v Iran*. 8 Iran-U.S. Cl. Trib. Rep. 198, 321 (1985).

tribunal. Most obviously, payment on the arbitral award requires the goodwill of state parties in a way rarely required of private parties due to stronger enforcement mechanisms, such as those in the 1958 New York Convention.<sup>124</sup> Sovereign states are expected to comply voluntarily with binding international decisions; the tribunals themselves usually lack the resources and indeed authority to coerce compliance.<sup>125</sup> While there is no reason to believe that such considerations slant arbitral awards in favor of states involved in disputes with private parties, they may sometimes deter aggressive departures from established precedents in pursuit of even a clearly preferable public policy.

Concerns about treating sovereign states with insufficient deference may exert an unconscious influence on an international tribunal's exercise of discretion in general. In the *Anaconda-Iran* case, for example, a chamber of the Iran–U.S. Claims Tribunal reverted to the *alterum tantum* rule, declining to award compound interest because, due to the inevitable delay in adjudication, 'interest due could, by far, exceed the principal awards awarded'.<sup>126</sup> By the tribunal's reasoning such an award would confer a profit on the claimant rather than restitution. John Gotanda has already pointed out the economic fallacy of the chamber's reasoning.<sup>127</sup> It is certainly possible that the decision resulted from faulty knowledge of economics, but an alternative explanation is that the propensity to underestimate interest is a holdover from the exalted Westphalian view of state sovereignty ingrained in, and slowly leeching out of, the consciousness of international arbitrators and judges. International tribunals may view a refusal to compensate injuries promptly, and a decision to employ dilatory tactics of litigation, as prerogatives of sovereign states so long as they are kept within reasonable limits.

Consider that international tribunals have sometimes proven receptive to state claims of impracticability as an excuse for violating legal obligations. In *Sempra Energy International v. Argentina*, an ICSID tribunal rejected the argument that an economic crisis excuses a state from granting fair and equitable treatment to foreign investors, but did 'take into account' the crisis conditions in assessing compensation due to the investor.<sup>128</sup> In *National Grid PLC v. Argentina*, an UNCITRAL tribunal went further still. The tribunal acknowledged Argentina's breach of the Argentina–U.K. BIT

<sup>124</sup> Convention on the Recognition and Enforcement of Foreign Arbitral Awards, signed 10 June 1958, entered into force 7 June 1959, 330 U.N.T.S. 38.

<sup>125</sup> Cf. Richard B. Lillich, *International Claims: Their Adjudication by National Commissions* (Syracuse, NY: Syracuse University Press, 1962) 108–9 [hereinafter Lillich, Claims Adjudication]. There are, of course, exceptions, such as the UNCC and the Iran–U.S. Claims Tribunal, both of which had access to a dedicated compensation fund.

<sup>126</sup> *Anaconda-Iran, Inc. v Iran*, 13 Iran–U.S. Claims Trib. Rep. 199, 235 (1986).

<sup>127</sup> See Gotanda, *Compound Interest*, above n 55.

<sup>128</sup> *Sempra Energy Int'l v Argentine Rep.*, Award of 28 September 2007, paras 303–4, ICSID Case No. ARB/02/16.

by failing to afford fair and equitable treatment to the claimant, but insisted that it could not ‘be oblivious to the crisis that the Argentine Republic endured at the time. . . . What would be unfair and inequitable in normal circumstances may not be so in a situation of an economic and social crisis.’<sup>129</sup> The tribunal ultimately exonerated Argentina from liability on this ground. It is difficult to imagine an international tribunal reducing the damages awarded against a private party that breached a legal obligation based on economic distress. Much less would a tribunal exonerate a private party altogether because it was suffering economic difficulties under circumstances comparable to those in the Argentinian investment arbitrations.

The propensity to afford latitude to states rather than to hold them accountable *strictissimi iuris* may seem especially attractive in highly contentious and relatively novel (by international law standards) fields, such as investment arbitration and human rights litigation. Many important legal questions, such as the definition of indirect expropriation or ‘fair and equitable treatment’ in international investment law, or state obligations in almost any field of international human rights law, remain relatively amorphous and subject to interpretation not only at the periphery but at the very core. To hold states to the most rigorous obligation of economic compensation in highly contentious cases decided against them may be considered extreme, unfair, or counterproductive. When better settled principles of law are being applied, a forgiving standard of compensation is less appropriate.

This may explain why the gradual movement in international investment law toward more accurate measures of interest, such as the recognition that pre-award interest forms part of the overall compensation for the claimant’s injury, and the acceptance of periodic compounding, has not yet been replicated in international human rights law. The proliferation of international decisions in investment cases has resulted in the development of an increasingly sophisticated jurisprudence. International human rights jurisprudence has also developed considerably, but its greater breadth and relative paucity of authoritative tribunals means many fewer cases elaborate any specific point of law. There is no especially cogent justification for denying full compensation for the delay in reparations to the victim of a human rights violation. It could be that, given the perceived political delicacy of the human rights obligations accepted by states, and the potentially expansive interpretation of those obligations by international courts and tribunals, judges consciously or unconsciously soften the blow of an adverse judgment by mitigating the damages somewhat.

Sensitivity to these same concerns may, indeed, prove necessary to the proper functioning, and perhaps at the extreme, the continued existence, of an international dispute resolution system. A respondent state’s decision

<sup>129</sup> *National Grid P.L.C. v Argentine Rep.*, UNCITRAL Award of 3 November 2008, para 180, at <http://ita.law.uvic.ca/>.

to resort to international arbitration or claims litigation, unlike a defendant's appearance in a domestic court, always relies on an element of cooperation. While states agree to arbitrate claims for many pragmatic reasons—e.g. to attract foreign investment or maintain friendly relations with other states—states generally maintain the practical option of resisting arbitration or refusing to satisfy an award. There are, of course, undesirable consequences to such a choice, but the shadow of noncompliance always darkens the international decision process to a degree, however slight. The prospect that a dissatisfied state will opt out of the dispute resolution system entirely casts a more portentous shadow. It is possible, for example, that the tendency to view interest as punitive to the respondent state or a windfall to the claimant originates in the sense that states ultimately can deny payment and that awarding damages for the period of denial may deter the state from future cooperation. Indeed, in 2007, Bolivia reacted to a series of arbitral awards in favor of aggrieved foreign investors by becoming the first state to denounce the ICSID Convention,<sup>130</sup> followed by Ecuador for similar reasons in 2009.<sup>131</sup> Interest awards that significantly increase the compensation to injured investors may contribute to disaffection with the dispute resolution system itself.

To the extent that a respondent state senses that an international tribunal has arrived at a compromise between the respondent state's interests and those of the claimant, the respondent may be encouraged to make frequent use of the dispute resolution system. International arbitrators and commissioners must remain cognizant of the need to maintain the good will of states in order for the dispute resolution system to continue to serve the needs of the international community. Putatively excessive or unexpectedly large awards, however justifiable economically or even ethically, carry a risk of provoking dissatisfaction with, or, at an extreme, abandonment of, the system. The arbitrators themselves are subject to a similar tension—unconscious or not—with respect to their own participation in the system. The role of an arbitrator in a dispute involving a sovereign state is a prestigious and sometimes lucrative one, and an arbitrator may perceive that a conservative award is less likely to encourage challenges to the arbitrator's appointment in future cases, although one hopes that such considerations in fact exert minimal influence, if any.

The foregoing argument could perhaps be made with respect to direct damages awards generally as well as interest calculations. In fact, the pull

<sup>130</sup> Int'l Centre for the Settlement of Investment Disputes, News Release: Bolivia Submits a Notice under Article 71 of the ICSID Convention, 16 May 2007, at <http://icsid.worldbank.org/ICSID/>.

<sup>131</sup> See Int'l Centre for the Settlement of Investment Disputes, News Release: Ecuador Submits a Notice under Article 71 of the ICSID Convention, 9 July 2009, at <http://icsid.worldbank.org/ICSID/>.

toward compromise is evident in the proclivity of international tribunals, as observed by many commentators, to approximate justice by awarding damages roughly midway between the claimant's and respondent's valuations.<sup>132</sup> In the *Aminoil* case, for example, the tribunal actually awarded the mean between the divergent estimates of lost profits of the parties' accounting experts without further explanation.<sup>133</sup> Arbitrators have sometimes expressly praised the value of moderation in calculating damages in cases involving sovereign respondents.<sup>134</sup>

With respect to interest awards, the *a fortiori* argument applies. Unlike the well settled methodologies for assessing direct damages, the quantum of interest remains a relatively open question on which the tribunal maintains a certain flexibility. At the very least, the tribunal can cite numerous precedents denying pre-award or compound interest. Moreover, although calculations of direct damages are usually justified in the reported reasoning of the tribunal's award based on the evidence presented, the published award will rarely justify a decision regarding interest with more than a sentence or two. If any part of the award will be subject to tacit compromise in favor of a respondent state, the interest portion is usually the most suitable. If this hypothesis is correct, then one would expect that the more politically charged or volatile a case appears to be, the more likely the tribunal will dispense with legal or economic formalities and resort to compromise awards that are likely to be at least minimally acceptable to all parties.<sup>135</sup>

#### D. The role of the tribunal in providing political cover

A related influence might be found in the arbitrators' consciousness of their role in the political process. The arbitrators, judges, or commissioners may

<sup>132</sup> See, e.g. Gray, above n 16, at 169–70; Gotanda, *Recovering Lost Profits*, above n 63, at 61–2; Markham Ball, *Assessing Damages in Claims by Investors Against States*, 16 ICSID Rev. 408, 426 (2001); Stephen M. Schwebel, 'Compound Interest in International Law', in *Studi di Diritto Internazionale in Onore di Gaetano Arangio-Ruiz* (Naples: Editoriale Scientifica, 2004), vol. 2, 880, 882. Exemplary cases include *Payne v Iran*, 12 Iran-U.S. Claims Trib. Rep. 3, paras. 34–7 (1986), in which the Iran-U.S. Claims Tribunal valued an expropriated business using no specific valuation method but in an amount that fell between the claimant's and respondent's valuations, and *Compañía del Desarrollo de Santa Elena, SA v Costa Rica*, 15 ICSID Rev. 167, 199–200 (2000), in which the tribunal awarded lost profits for an expropriation in an amount approximately equal to the mean between the parties' requests.

<sup>133</sup> *American Indep. Oil Co. (Aminoil) v Kuwait*, 21 I.L.M. 976 (1982).

<sup>134</sup> See, e.g. Cervetti Case (*Italy v Venez.*), 10 R.I.A.A. 492, 493 (1903) ('It is indisputable that the measure of redress should be fixed in a spirit of moderation.') (opinion of Commissioner Agnoli).

<sup>135</sup> There are, of course, disadvantages to the willingness of international tribunals to bestow suboptimal interest awards. As with any award of less than full compensation, the granting or acceptance of economically inadequate damages undermines the principle of full compensation and, to some degree, of the international responsibility of states in general. Cf. Lillich, *Claims Adjudication*, above n 125, at 105–6 (arguing that in accepting lump-sum settlements in amounts smaller than actual damages for expropriation, the United States has undercut its own arguments that international law requires relief to be 'prompt, effective and adequate').

not conceive of their role as strict dispensers of justice or crafters of doctrine for the ages so much as facilitators of a politically expedient resolution to a potentially destabilizing international conflict. As Robert Hudec observed in the context of early General Agreement on Tariff and Trade dispute resolution, the award of an independent third party may temper or defuse domestic political criticism of an unpopular compromise that the state government might otherwise be reluctant to accept.<sup>136</sup> Steven Ratner has similarly noted the role that the International Court of Justice may play in assisting political elites to settle international disputes when a resolution on any terms acceptable to the other party would be unpopular with important domestic actors. Political elites navigating between the need to resolve an international dispute and domestic opposition to any likely negotiated outcome may resort to an ostensibly impartial tribunal to diffuse responsibility for the outcome. From the perspectives of these elites, Ratner observes, ‘a certain amount of doctrinal inconsistency or opacity will not really matter—the opinion need only be good enough to convince key domestic constituencies that it has treated their claims seriously’.<sup>137</sup> The preference for a relatively prompt compromise not entirely dissatisfactory to any party to the dispute over optimal or consistent doctrine may explain the tendency of tribunals to approximate nonessential elements of the award such as interest rather than rigorously calculating the full economic loss suffered by the claimant.

Consistent with this hypothesis, international tribunals hearing politically charged cases involving human rights, armed conflicts, and similarly volatile issues tend to result in awards much less exacting in their calculations of damages than more routine commercial cases such as those arising from breach of contract or expropriation.<sup>138</sup> Gray has described damages based on human rights violations awarded by the European Court of Human Rights, for example, as ‘impressionistic’ and a ‘rough approximation to “just satisfaction”’ rather than a methodical attempt to interpret and apply this international law relating to damages awards.<sup>139</sup>

More evidence for the importance of these factors comes from the occasional misapplication of the ‘abuse of right’ doctrine. As John Gotanda has noted, a few *ad hoc* international arbitral tribunals have relied on the abuse of

<sup>136</sup> Cf. Robert Hudec, *The GATT Legal System and World Trade Diplomacy* (Santa Barbara, CA: Greenwood Pub. Grp., 1975) 179.

<sup>137</sup> Steven R. Ratner, ‘Land Feuds and Their Solutions: Finding International Law Beyond the Tribunal Chamber’, 100 *American Journal of International Law* 808 (2006), at 816.

<sup>138</sup> See, e.g. Cervetti Case (*Italy v Venez.*), 10 R.I.A.A. 492, 493 (1903) (opinion of Commissioner Agnoli) (‘The fact that the adjudication of interest must aggravate the financial situation of Venezuela is worthy to be taken into consideration, and it is with this in view that the undersigned has fixed the rate at 5 per cent, which, given the usages of the country [the normal commercial rate being 12%], is very light indeed.’).

<sup>139</sup> Gray, above n 16, at 158.

right doctrine to deny a claimant's admittedly legitimate right to lost profits.<sup>140</sup> In the cases in which the abuse of right doctrine has been successfully invoked, it was used to justify denying a claimant's action for legitimate damages when the claim was being exercised unreasonably, without any interest of the claimant, and predominantly to harm the respondent.<sup>141</sup> However, the doctrine has more recently been applied by some tribunals merely to deny a legitimate and good faith claim. In one arbitration, *Himpurna California Energy v. PLN*,<sup>142</sup> the tribunal denied lost profits arising from a breach of contract by Indonesia ostensibly because the claimant had not yet fully invested in performance of its obligations and because the respondent Indonesia would not necessarily have benefitted from claimant's performance under the contractual terms.<sup>143</sup> In a similar arbitration, *Patuha Power Ltd. v. PLN*, the tribunal also invoked the abuse of right doctrine, apparently on the ground that the Indonesian economy could ill afford to pay full lost profits.<sup>144</sup> The tribunals' respective invocations of abuse of right were doctrinally inappropriate, because the claimant in each case was seeking to enforce its rights for its own admittedly legitimate benefit, not predominantly to harm the respondent.<sup>145</sup>

The role of the international tribunal in settling robust controversies is especially crucial in disputes between two or more sovereign states. For example, when a state pays a lump-sum settlement to another as compensation for harms done to the recipient state's nationals, the settlement amount generally reflects a political compromise between the two states based on a variety of factors. On the paying state's side, these may include an unwillingness or inability to admit full liability<sup>146</sup> or skepticism about the amounts claimed by the injured individual claimants or their national government. On the recipient state's side, the factors include those already mentioned as well as others, such as an inability to obtain a full settlement, a desire to avoid frustrating a friendly state by extended negotiations, a lack of certainty of the amount of damages,<sup>147</sup> or a preference for prompt and certain settlement.

<sup>140</sup> See Gotanda, *Recovering Lost Profits*, above n 63, at 97–9.

<sup>141</sup> See Bin Cheng, *General Principles of Law as Applied by International Courts and Tribunals* (Cambridge: Cambridge University Press, 1987) 134–6; Joseph M. Perillo, 'Abuse of Rights: A Pervasive Legal Concept', 27 *Pacific Law Journal* 37 (1995), 47.

<sup>142</sup> *Himpurna Cal. Energy Ltd. v PT (Persero) Perusahaan Listrik Negara*, 25 Y.B. Comm. Arb. 13 (2000).

<sup>143</sup> *Ibid.* at 90–3.

<sup>144</sup> *Patuha Power Ltd. v PT (Persero) Perusahaan Listrik Negara*, 14 Mealey's Int'l Arb. Rep. B-1 (December 1999).

<sup>145</sup> As John Gotanda has noted, the abuse of right doctrine does not turn on the mere fact that the enforcement of a claimant's legitimate right to damages might cause the respondent financial hardship. See Gotanda, *Recovering Lost Profits*, above n 63, at 100, 106.

<sup>146</sup> As Richard Lillich pointed out, if an expropriating state was willing and able to pay full compensation for the expropriated business, it is unlikely to have resorted to expropriation in the first place. See Lillich, above n 125, at 107.

<sup>147</sup> See *ibid.* at 111.

As a result, such settlements tend as a general rule to fall short of full restitution, leaving the recipient state to parcel out the settlement amount to its injured nationals, usually through a claims commission applying international law to determine the right to and amount of compensation payable.<sup>148</sup> And these commissions, in turn, necessarily award each injured citizen less than full compensation for their injuries in such cases.<sup>149</sup> When the commissions lack the funds to compensate even out-of-pocket expenses, compound interest cannot equitably be awarded to any claimant.

In the context of investor-state arbitration generally, it is significant that mandatory dispute resolution has come under a great deal of criticism, both by developing countries and liberals in developed countries, for allegedly giving more deference to the interests of wealthy corporate investors than to local needs for environmental protection, labor standards, and other host state interests.<sup>150</sup> Political elites in most states feel pressure to convince domestic constituencies that the government is pressing the national interest vigorously on the international stage. Failure to win concessions on politically volatile controversies can have negative ramifications for the government's domestic authority and credibility. Below-market interest rate awards reduce the total compensation owed and may accordingly assist the defeated government in claiming an offsetting victory, or at least minimizing the political effects of a loss.

#### IV. CONCLUSIONS

The important conclusion to be drawn from the preceding discussion is not that claimants in international litigation and arbitration are being systematically denied full economic reparations because international tribunals have forgotten the *qui tardius solvit* maxim, although that is true to a degree. Rather, it reveals how international claims against states and domestic dispute resolution within states operate under different dynamics. Whatever the reason that some states do not award both prejudgment and postjudgment compound interest as a matter of principle in all cases of wrongful injury, they are not identical to the reasons that international tribunals have tended to award below-market interest.

International tribunals are creatures of international agreement and are designed to serve the policy goals of the community that created them.

<sup>148</sup> See *ibid.* at 71–2.

<sup>149</sup> See *ibid.* at 38 and n. 131.

<sup>150</sup> See Guillermo Aguilar Alvarez and William W. Park, 'The New Face of Investment Arbitration: NAFTA Chapter 11', 28 *Yale Journal of International Law* 365 (2003), 383–6; K. Scott Gugeon, 'Valuation of Nationalized Property Under United States and Other Bilateral Investment Treaties', in Richard B. Lillich (ed.) *Valuation of Nationalized Property in International Law* (Charlottesville: University of Virginia Press, 1987) 101, 108; see, e.g. Ralph Nader et al. (eds), *The Case Against Free Trade: GATT, NAFTA, and the Globalization of Corporate Power* (San Francisco: Earth Island Press, 1994).

Whatever the charms of an internally consistent legal doctrine, strict adherence to precedents, or even the satisfaction of self-consistent logic, these may at some point interfere with the pursuit of the values that justify the tribunal and dispute resolution system in the first place. From conflicts between such values, we sometimes observe disjunction between doctrine and practice, or what legal realists have variously called ‘law in books’ versus ‘law in action’,<sup>151</sup> or the ‘myth system’ versus the ‘operational code’.<sup>152</sup> In the context of interest awards, there is quite clearly a disjunction between doctrine and practice. The formal doctrine of full reparations, which posits the injured party’s right under international law to full compensation restoring it to the *status quo ante delictum*, does not accurately describe international practice in the calculation of interest. The contradiction between doctrine and practice is, moreover, very rarely recognized in the published reasoning of international tribunals despite frequent comment by scholars.

The cause of the disjunction in any given case could include any of the four factors identified in the foregoing discussion. Indeed, the factors likely interact. The practice of following precedents, however at odds these may be with modern economic theory, does impart stability and confirms the expectations of state parties to the dispute resolution proceeding. Similarly, granting less than full reparations in a low-profile part of the award, such as interest calculations, provides both the arbitral tribunal and the respondent state with the satisfaction of feeling that a compromise has been wrought and concessions won.

The absence of any rigorous attempt to explain the contradiction between doctrine and practice in the scholarly literature may result from the professional hazard of wishing to believe that positive rules of international law rarely bow to political considerations. This may explain Lauterpacht’s insistence that the ‘cases in which an arbitral tribunal sacrifices a juridical principle for the sake of a political compromise’ are rare, and their influence ‘conspicuously small’.<sup>153</sup> Lauterpacht may have intended to refer specifically to departures from a settled juridical principle in the direction of a decision *contra legem*. But this is not the usual case; a tribunal much more often confronts conflicting norms, each arguably applicable to the facts at hand. The juridical principle that prevailed in the *Chorzów Factory* case is directly contrary to the juridical principle holding sovereign states exempt from pre-award compound interest on damages assessed against them. A departure from one or the other principle is inevitable in many cases, but under what circumstances should the full reparation norm prevail, and in what circumstances should interest awards be limited to some amount falling

<sup>151</sup> Roscoe Pound, ‘Law in Books and Law in Action’, 44 *American Law Review* 12 (1910).

<sup>152</sup> W. Michael Reisman, *Folded Lies: Bribery, Crusades and Reforms* (New York: Free Press, 1979) 1–2.

<sup>153</sup> Lauterpacht, above n 11, at 220.

short of that ideal? The forces that persuade arbitral and judicial authorities to favor one outcome or the other in any given case include doctrinal justifications such as the force of precedent, and these contribute to the stability and predictability of the legal system. But they include political and systemic considerations as well. While, in a domestic judicial decision process, succumbing to such influences is frowned upon, in an international context, sensitivity to the political consequences of a juridical decision is expected and, indeed, necessary.

To explain the divergence between doctrine and practice does not, however, necessarily justify it. The *Chorzów Factory* doctrine represents an ideal atypically susceptible to attainment as an observed norm. If adopted exactly in interest awards, the doctrine promises to deter self-serving delays in compensation to victims of internationally wrongful acts, including dilatory litigation tactics; to ensure economic justice to victims of such wrongful acts; and to increase the consistency of damages calculations. Greater consistency, in turn, reduces the uncertainty and consequently the cost of foreign investment. As international practice coalesces around economically sound interest calculations, the expectations of the international community will eventually encompass such awards as well, changing concerns about stability and predictability into a force discouraging departures from economically rational awards of interest. From the claimant's perspective, such awards hardly stand in need of justification. From the international community's perspective, it seems very likely that the advantages for dispute resolution systems will eventually be perceived to outweigh the short-term gains to respondent states that result from the current variable and often arbitrary practice.