Damnum emergens and lucrum cessans: is it relevant?

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Issues to be covered

• The doctrine of damnum emergens and lucrum cessans and its place in international law
• “Fair market value” of investment – different approach to compensation (BITs)
• Do tribunals really determine “market value”?
• The role of the certainty requirement in tribunals’ reasoning
• The upshot – the damnum/lucrum doctrine entering through the back door. Why?

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The doctrine of damnum emergens and lucrum cessans

• Roman law – two elements of loss (actual/positive damage and loss of profit)
• Adoption in international law (breach of contract):
  – 2004 UNIDROIT Principles (Article 7.4.2 “The aggrieved party is entitled to full compensation for harm [which] includes both any loss which it suffered and any gain of which it was deprived…”)
  – Arbitral jurisprudence (eg, Delagoa Bay, Sapphire v NIOC, Himpurna v PLN, Liamco v Libya, Amco v Indonesia)

• Objective – full compensation placing an aggrieved party in same pecuniary position it would have been in if the contract had been
“Market value of investment” – a different approach to compensation

• BITs’ expropriation clauses
• Value – price a willing buyer would pay to a willing seller (present worth of expected future benefits)
• Valuation methods (financial/business perspective):
  – Income-based approach (eg, DCF)
  – Market-based approach (transactions with comparable companies/assets)
  – Asset-based approach (eg, net book value of assets)
• Same facts may lead to different approaches to compensation, depending on the cause of
Jurisprudence – how have tribunals determined “value”?

• Forward-looking methods – rare (eg \textit{ADC v Hungary}, \textit{CMS v Argentina}, \textit{CME v The Czech Republic})

• Most popular approach – award of actual expenditures, including (in different cases):
  - negotiating and planning costs, capital contributions and loans, marketing costs, cost of particular assets contributed, costs of recruiting and relocating of relevant personnel, travel and accommodation expenses, insurance, consulting and even telephone costs.

• Actual expenditures \neq value

• Actual expenditures = damnum emergens

  Sometimes – award of actual expenditures + a little extra (\textit{SPP v Egypt}, \textit{Tecmed v Mexico})
“Certainty” – major legal obstacle

- Damages must be certain and non-speculative
- Future is always uncertain
- Uncertainty can be built into the forward-looking valuation
- Most arbitrators are not willing to go that route
Where does this leave us?

• Damnum ≠ value, arbitrators doing not what the law instructs them to do
• Assessing the actual (past) loss rather than valuing the investment
• Putting the investor in a position before the investment was made, rather than in a position he would have been in had the wrongful act not occurred
• The danger of double counting when awarding
Why?

- Typically, forward-looking methods yield a higher figure, while asset-based methods give a lower figure (compared to damnum).
- Damnum/lucrum approach perceived as producing "fairer", "moderate" result, better balancing interests of investors and States.
- Reverse engineering – first the "fair" outcome, then the reasoning to match that outcome.