

**Case summary**

**Wena Hotels Ltd v Arab Republic of Egypt**

**Year of the award:** 2000

**Forum:** ICSID

**Applicable investment treaty:** Egypt – United Kingdom BIT (1975)

<b>Arbitrators</b>	<b>Timeline of the dispute</b>
Mr. Monroe Leigh – President Prof. Ibrahim Fadlallah Prof. Don Wallace, Jr.	10 July 1998 – request for arbitration 18 December 1998 – arbitral tribunal constituted 29 June 1999 – decision on jurisdiction 8 December 2000 – arbitral award 28 January 2002 – decision on the application for annulment of the award (annulment declined) 31 October 2005 – decision on the application for interpretation of the award

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## **I. Executive Summary**

In 1989-1990, Wena, a British company, entered into two long-term agreements with the Egyptian Hotels Company (“EHC”), wholly owned by the Egyptian Government. Under the agreements, two hotels – Nile Hotel in Cairo and Luxor Hotel in Luxor – were leased to Wena.

Following the rent-related disputes that arose between the parties shortly thereafter, on 1 April 1991 EHC took possession of both hotels by force. As a result of domestic legal procedures, in 1992 both hotels were returned to Wena but in a damaged state. In addition, due to Government’s interference with operating licenses, Wena was effectively prevented from operating the hotels again.

Wena attempted to cover its damages through commercial arbitrations provided for in the agreements but was actually able to obtain only EGP 1.5 million (US\$435,570) for damages from the seizure of the Nile Hotel. As a side-result of these arbitrations, Wena had to surrender, and was evicted from, both hotels.

In 1998, Wena initiated ICSID arbitral proceedings against Egypt under the provisions of the Egypt-UK BIT claiming that Egypt’s actions constituted an unlawful expropriation and that Egypt had failed to accord Wena’s investments “fair and equitable treatment” and “full protection and security”. Wena claimed damages of no less than US\$ 62,820,000.

The Tribunal found merit in both substantive claims of the investor and proceeded to the award of “prompt, adequate and effective compensation” that would amount to “the market value of the investment immediately before the expropriation”, as required by the BIT. The Tribunal dismissed Wena’s claim for lost profits and lost opportunities as too speculative and estimated compensation on the basis of Wena’s actual investments. The Tribunal was not stopped by the fact that much of the investment came from affiliates of Wena rather than from Wena and that Wena did not provide conclusive evidence of its expenses because part of Wena’s financial documentation had been lost as a result of the hotels’ seizure.

The Tribunal awarded interest at a rate of 9%, compounded quarterly. It also provided for post-Award interest and compensated the Claimant for its legal costs. The total award including interest and legal costs amounted to US\$ 20.6 million.

## **II. Factual Background and Claims of the Investor**

In 1989 and 1990, Wena Hotels Ltd. (“Wena”), a British company, entered into two long-term agreements with the Egyptian Hotels Company (“EHC”), wholly owned by the Egyptian Government. The agreements concerned lease to, and development by Wena, of two hotels – Nile Hotel in Cairo (for 21.5 years) and Luxor Hotel in Luxor (for 25 years). The agreements provided that EHC would not interfere in the

management and/or operation of the hotels or interfere with the enjoyment of the leases by Wena.

Shortly after entering into the agreements, disputes arose between EHC and Wena concerning their respective obligations. Wena alleged to have received the hotels in a condition below that stipulated in the agreements and withheld part of the rent. Egypt claimed that Wena had failed to pay the rent. Having reached a stalemate in the dispute, on 1 April 1991 EHC took possession of both hotels by force.

In early 1992, the Chief Prosecutor of Egypt ruled that the seizure of the hotels had been illegal. The hotels were returned to Wena but in a damaged state, especially the Nile Hotel. In addition, due to Egypt's Ministry of Tourism interference with operating licenses for the hotels, Wena was effectively prevented from operating the hotels again.

After the return of the hotels, Wena sought compensation from Egypt. In two arbitrations that it had initiated, in 1994 Wena was awarded EGP 1.5 million for damages from the seizure of the Nile Hotel (paid by Egypt in 1997) and EGP 9.06 million for damages from the seizure of the Luxor Hotel. The latter arbitral award was subsequently nullified by the Cairo Appeal Court. The awards also required Wena to surrender the hotels to the EHC's control. Wena was evicted from the Nile Hotel in 1995 and from the Luxor Hotel in 1997.

In 1998 Wena initiated ICSID arbitral proceedings against Egypt under the provisions of the Egypt-UK BIT claiming that Egypt's actions constituted an unlawful expropriation without "prompt, adequate and effective compensation" and that Egypt had failed to accord Wena's investments "fair and equitable treatment" and "full protection and security", as required by the BIT. Wena claimed damages of no less than US\$ 62,820,000.

### **III. Findings on Merits<sup>1</sup>**

#### ***A. Applicable law***

The Tribunal affirmed the BIT as the primary source of applicable law. In accordance with Article 42(1) of the ICSID Convention, the Tribunal also held that, as beyond the BIT there was no special agreement between the parties on the applicable law, the Tribunal should subsidiarily apply both Egyptian law and "such rules of international law as may be applicable". (paras.78-79) The Tribunal did not determine the hierarchy between these two secondary sources of applicable law.<sup>2</sup>

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<sup>1</sup> Prior to its award on merits, the Tribunal issued a decision on jurisdiction of 29 June 1999 which is not covered in this summary.

<sup>2</sup> The matter of applicable law, and in particular the role of international law, was also discussed in the Decision on application for annulment of the award, dated 28 January 2002, paras.37-46. The Annulment Committee concluded that the Tribunal had not manifestly exceeded its powers by failing to apply the applicable law.

## ***B. Fair and Equitable Treatment (FET)***

The Tribunal agreed with Wena that Egypt had failed to accord Wena's investment "fair and equitable treatment" and "full protection and security" in violation of the BIT. The Tribunal stated the following reasons for this finding:

- Egypt was aware of EHC's intentions to seize the hotels and took no actions to prevent EHC from doing so;
- Once the seizures occurred, both the police and the Ministry of Tourism took no immediate action to restore the hotels promptly to Wena's control;
- Egypt never imposed substantial sanctions on EHC or its senior officials, suggesting Egypt's approval of EHC's actions. (para.84)

## ***C. Expropriation***

The Tribunal also agreed with Wena that Egypt's actions constituted an expropriation without "prompt, adequate and effective compensation" in violation of the BIT. The Tribunal reasoned that "whether or not [Egypt] authorized or participated in the actual seizures of the hotels, Egypt deprived Wena of its 'fundamental rights of ownership' by allowing EHC forcibly to seize the hotels, to possess them illegally for nearly a year, and to return the hotels stripped of much of their furniture and fixtures." (para.99) Moreover, even after the hotels were returned to Wena, Egypt failed to satisfy its obligation under the BIT, and international norms generally, by refusing to offer Wena "prompt, adequate and effective compensation" for the losses it had suffered as a result of Egypt's failure to act. (para.100)

# **IV. Findings on Damages**

## ***A. Law Applicable to the Determination of Damages***

The Tribunal applied the BIT and international law.

## ***B. Standard of Compensation***

Article 5 of the BIT provided that in the event of an expropriation, the private investor shall be entitled to "prompt, adequate and effective compensation" and "such compensation shall amount to the market value of the investment immediately before the expropriation." The Tribunal applied this standard to the determination of damages. (para.118) In the Decision on the application for annulment, the Annulment Committee added that such a standard "confers to a Tribunal a certain margin of discretion",<sup>3</sup> which apparently means that the Tribunal may choose between different methods that would allow, in the Tribunal's view, to reach this standard.

## ***C. Heads of Damages Claimed***

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<sup>3</sup> Decision on the application for annulment of the award, para.91

Wena submitted two alternative claims:

- 1) GB£ 20.4 million for lost profits, GB£ 22.8 million for lost opportunities and GB£ 2.5 million for reinstatement costs (in total, GB£ 45.7 million) plus interest and legal costs; or
- 2) US\$ 8,819,467 as the amount of its investment in the Egyptian hotel venture plus interest and legal costs.

The Tribunal considered that Wena's claims for lost profits (calculated by Wena using a discounted cash flow analysis), lost opportunities and reinstatement costs were inappropriate because an award based on such claims would be too speculative. The Tribunal referred to *Metalclad v. Mexico*, *SPP (Middle East) v. Egypt* and *American Manufacturing and Trading v. Zaire* to support its view and gave three reasons for declining that claims:

- 1) there was an insufficiently solid base on which to found any profit or for predicting the growth or expansion of the investment made by Wena (Wena had operated the Luxor hotel for less than 18 months, and had not even completed its renovations on the Nile Hotel, before they were seized);
- 2) there was some question whether Wena had sufficient finances to fund its renovation and operation of the hotels;
- 3) there was a large disparity between the requested amount (GB£ 45.7 million) and Wena's stated investment in the two hotels (approx. US\$ 8.8 million).

(paras.123-124)

The Tribunal thus dismissed the first of the two alternative claims as inappropriate and decided that the proper calculation of the "fair market value of the investment" was best arrived at, in that case, by reference to Wena's actual investment in the two hotels. (para.125)

#### ***D. Calculation of the Actual Investment***

Wena claimed US\$ 8,819,467 as the amount of its investment in the Egyptian hotel venture (particular costs and expenses constituting that amount were not specified in the Award). Egypt objected to that amount on the grounds that much of the investment came from affiliates of Wena rather than from Wena. However, the Tribunal decided that regardless of "whether the investments were made by Wena or by one of its affiliates, as long as those investments went into the Egyptian hotel venture, they should be recognized as appropriate investments." The Tribunal stated that it was persuaded that it was "a widely established practice for hotel enterprises to adopt allocation measures, which spread the profits from the group operations into various jurisdictions where there are tax advantages to the group as a whole." (para.126)<sup>4</sup>

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<sup>4</sup> The Annulment Committee agreed with this approach stating that "it was a matter of fact and evidence on the origin of the sums invested and the ultimate beneficiary of the sums awarded." The Annulment Committee also noted that "ICSID practice has been quite flexible on claims that include the interests of subsidiaries and affiliates, including on occasions entities that are nationals of States that are not contracting parties to the [ICSID] Convention." (Decision on the application for annulment of the Award, para.54).

The Tribunal diminished the said figure by US\$ 322,000 “to eliminate probably double counting in certain instances” and further deducted US\$435,570 received already by the Claimant as a result of the Egyptian arbitration award. (para.127)

### ***E. Burden of Proof and Evidence***

In the annulment proceedings, Egypt argued that Wena had not supplied any evidence of the sums it claimed to have invested in the hotels nor gave any evidence as to the losses it claimed to have suffered. Essentially, Egypt argued that Wena had not met its burden of prove the amount of damages suffered.

In its decision, the Annulment Committee emphasized that it was “the Tribunal’s discretion to make its opinion about the relevance and evaluation of the elements of proof presented by each Party. Arbitration Rule 34(1) recalls that the Tribunal is the judge of the probative value of the evidence produced. The record also shows that account had to be taken of the loss of part of Wena's financial documentation as a result of the events of April 1, 1991.” (paras.62-65)

Essentially, the Annulment Committee did not go into the discussion of whether Wena had presented sufficient evidence to prove damages but adopted a stance of deference to the Tribunal in the matter of assessing the evidence.

### ***F. Interest***

Wena claimed interest but specified neither the proposed rate of interest, nor whether the interest should be compounded. The Tribunal awarded interest at a rate of 9%, compounded quarterly. (para.128) The rate of interest was chosen with reference to long-term government bonds in Egypt, which at the time of arbitration were yielding 10%. The Tribunal did not specify the date from which interest was calculated; presumably, it was the date of seizure of the hotels (1 April 1991).<sup>5</sup>

In its application for annulment of the Award, Egypt complained that the Tribunal had awarded interest even through the applicable BIT provision (on compensation for expropriation) did not provide for the award of interest. The Annulment Committee disagreed noting that, according to the BIT, compensation must be, first, “prompt, adequate and effective” and, second “compensation shall amount to the market value of the investment expropriated immediately before the expropriation itself.” The Annulment Committee reasoned that “[a]lthough not referring to interest, the provision must be read as including a determination of interest that is compatible with those two principles. In particular, the compensation must not be eroded by the passage of time or by the diminution in the market value. The award of interest that reflects such international business practices meets these two objectives.” The Annulment Committee thus upheld the award of interest in principle. (Decision on the application for annulment of the award, paras.51-53)

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<sup>5</sup> This conclusion regarding the date was later confirmed by the Annulment Committee. See Decision on the application for annulment of the Award, para.98.

In the annulment proceedings, Egypt also complained that the Tribunal had fixed the interest rate of 9% without giving reasons. The Annulment Committee dismissed this argument, stating, *inter alia*, that “[a]s an extended practice shows, international tribunals and arbitration panels usually dispose of a large margin of discretion when fixing interest. It is normal, therefore, that very limited reasons are given for a decision which is left almost entirely to the discretion of the tribunal.”<sup>6</sup>

The Tribunal explained its choice of compound, as opposed to simple, interest as more “appropriate in most modern, commercial arbitrations.”<sup>7</sup> The Tribunal referred to Professor Gotanda’s observation that “almost all financing and investment vehicles involve compound interest... If the claimant could have received compound interest merely by placing its money in a readily available and commonly used investment vehicle, it is neither logical, nor equitable to award the claimant only simple interest.”<sup>8</sup> The Tribunal also referred to Prof. Mann’s opinion to the same effect. (para.129)

The Tribunal calculated that the total amount of compensation, including interest, was equal to US\$ 19,493,283.

The Tribunal also provided for post-Award interest, calculated on the total amount compensation including pre-Award interest and costs, at 9% compounded quarterly, starting 30 days after the date of the Award and running until the awarded amount was paid.

## **G. Costs**

The Tribunal awarded the Claimant its attorney’s fees and costs incurred in presenting the merits of the arbitration in the amount of US\$ 1,107,703 (fees and costs incurred at the jurisdictional stage were excluded because Tribunal’s decision on jurisdiction already included the apportionment of costs).

## **V. Implications/Initial Analysis**

- The **standard of compensation** does not rigidly determine the approach that would be taken by a tribunal to the calculation of damages. One and the same standard of compensation can lead to application of different approaches to determination of damages and valuation methods. As noted by the Annulment Committee, the Tribunal has a margin of discretion in this respect.
- **DCF analysis** can be used not only to estimate the value of an enterprise as a going concern but also to assess lost profits.
- **Lost profits** can be successfully claimed, and would not be considered as speculative, if (1) the investment had a sufficient history of profitable operations, (2) there were sufficient finances to continue successful operations

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<sup>6</sup> Decision on the application for annulment of the Award, paras.94-97.

<sup>7</sup> One arbitrator (Prof. Don Wallace, Jr.), while agreeing that compound interest should be awarded, was “not persuaded” that compounding should be quarterly.

<sup>8</sup> John Y. Gotanda, *Awarding Interest in International Arbitration*, 90 Amer. J. Int’l L. 40, 61 (1996).

with no major obstacles visible, and (3) the disparity between the DCF claim and the actual investment is not excessively large.

- The Tribunal adopted a liberal approach, according to which **investment expenses/costs** would be recoverable if shown that they relate to the investment project and were made by a company or person affiliated with the investor-Claimant.
- The Tribunal has broad **discretion in assessing the evidence** presented to prove the quantum of damages. A factor, such as loss of financial documentation as a result of the breach, could make the Tribunal less strict when evaluating the evidence.
- As affirmed by the Annulment Committee, **interest** may be awarded even if not expressly provided for in the BIT. The right to interest now forms part of customary international law. It is based on the understanding that “the compensation must not be eroded by the passage of time or by the diminution in the market value”.
- Tribunals have **broad discretion** when awarding **interest** and are not required to give detailed reasons.
- The Tribunal was convinced that **compound interest** was more appropriate in international arbitrations because most financing and investment vehicles (in which the claimant could have easily placed its money, if not for the breach) offered compound interest.
- Notably, the Tribunal ruled that interest should be **compounded quarterly**, not annually (without any explanation).
- **Post-Award interest** was calculated on the total amount of compensation including the pre-Award interest and costs.