

# ICESCR MINIMUM CORE OBLIGATIONS AND INVESTMENT: RECASTING THE NON-EXPROPRIATION COMPENSATION MODEL DURING FINANCIAL CRISES

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## ABSTRACT

*This Article proposes a reassessment of current methods for valuing compensation owed by host States for breaches of non-expropriation standards of investment treaties, when the host State breaches such standards in order to fulfill obligations to its citizens under the International Covenant on Economic Social and Cultural Rights (ICESCR). The ICESCR minimum core obligations continue to have binding force during financial crises, despite the latter's impairment of host States' fiscal resources and social protection capabilities. Current investment arbitral jurisprudence involving financial crises show that tribunals have not adjudged host States implementing interventionist social protection measures to be responsible for direct or indirect expropriation, but rather for violating other treaty standards such as the "fair and equitable treatment" clause.*

*Arbitral tribunals have generally determined compensation for such breaches by referring to a "fair market value" standard, more synchronous with assumptions of perfectly competitive markets. However, the process of determining compensation for breaches of non-expropriation standards is governed by the general law of international responsibility, of which compensation is only one of the forms of reparations. Under the law of international responsibility, compensation is not intended to be punitive or expressive, but is evaluated according to the objective conduct of both the injuring State and the injured State, in order to reach the most equitable outcome that redresses damage to the injured State. Investment arbitral tribunals determining compensation for a host State's non-expropriation breaches should, thus, be similarly obliged to reach for equitable outcomes, rather than automatically resorting to the flawed definition of the "fair market value" standard.*

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*This Article shows that States, in conjunction with the Committee on Economic, Social and Economic Rights (“the Committee”), jointly define the minimum core obligations particular to their respective jurisdictions in light of resource constraints, governmental capacities, and growth prospects. While minimum core obligations are not static concepts, they can nonetheless be empirically determined and institutionally verified, as shown in the settled practices of the Committee in working with State Parties to the ICESCR. The Article then synthesizes current tribunals’ approaches in valuing compensation for breaches of non-expropriation treaty standards in times of economic crises (primarily through the 2001-2002 Argentine financial crises), and reveals latent methodological defects from using a broad “fair market value” standard, without considering equitable adjustment factors and other comparable arbitral practices that focus more narrowly on past performance, rather than future earnings projections for compensation in times of emergencies. Finally, the Article suggests a valuation proposal that recasts country risk premium to factor in the host State’s obligation to fulfill the ICESCR minimum core obligations as a fixed constraint on government resources, even in times of financial or economic crisis.*

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*“Concerns have sometimes been expressed that the principle of full reparation may lead to disproportionate and even crippling requirements so far as the responsible State is concerned. The issue is whether the principle of proportionality should be articulated as an aspect of the obligation to make full reparation. In these Articles, proportionality is addressed in the context of each form of reparation, taking into account its specific character. Thus restitution is excluded if it would involve a burden out of all proportion to the benefit gained by the injured State or the other party. Compensation is limited to damage actually suffered as a result of the internationally wrongful act, and excludes damage which is indirect or remote.”<sup>1</sup>*

#### I. INTRODUCTION: THE PROSPECTS OF ICESCR-DRIVEN MITIGATION OF COMPENSATION

Compensation in international law has never been a precise science. Throughout international legal history, the determination of reparations has differed widely with regard to quantum, mode of settlement, and the means of enforcement upon States.<sup>2</sup> Compensation owed for injuries that are partly endogenously determined by a State’s acts (such as through governmental measures that result in material deprivation or injury), and partly exogenously

1. Rep. of the Int’l Law Comm’n, 53d Sess., Apr. 23–June 1, July 2–Aug. 10, 2001, at 236, art. 34 cmt. 5, U.N. Doc. A/56/10; GAOR, 56th Sess., Supp. No. 10 (2001) [hereinafter 2001 ASR] (internal citations omitted).

2. See BORZU SABAHI, COMPENSATION AND RESTITUTION IN INVESTOR-STATE ARBITRATION 7–55 (2011); Richard M. Buxbaum, *A Legal History of International Reparations*, 23 BERKELEY J. INT’L L. 314, 314 (2005) (describing modern shift in focus from state-centered to individual- and societal-centered rights and obligations in reparations).

caused by an economic emergency,<sup>3</sup> introduces another intriguing layer of complexity to an already variable regime within international law.

Compensation awards in international investment arbitrations involving host State measures taken during economic emergencies manifest these significant variances in the estimation of both the quantum and the components of compensation to injured investors. While the 2005 *CMS Gas v. Argentina* tribunal declared that the Argentine financial crisis “cannot be ignored and . . . has specific consequences on the question of reparation,”<sup>4</sup> those consequences have never been specified or explained in the arbitral awards to date that have dealt with the question of the Argentine financial crisis.<sup>5</sup> Instead, most tribunals have rejected Argentina’s extreme interpretation of the necessity defense, which calls for the outright inapplicability of an investment treaty during a situation of self-judged emergency or necessity within the host State.<sup>6</sup> Where arbitral tribunals have relied upon the necessity defense as defined under Article 25 of the International Law Commission (ILC) 2001 Articles on the Responsibility of States for Internation-

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3. For the taxonomy of economic emergencies, see CARMEN M. REINHART & KENNETH ROGOFF, *THIS TIME IS DIFFERENT: EIGHT CENTURIES OF FINANCIAL FOLLY* 3–14 (2009).

4. *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶ 406 (Apr. 25, 2005).

5. See, e.g., *LG&E Energy Corp. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability, ¶¶ 226–66 (Oct. 3, 2006); *Sempra Energy Int’l v. Argentine Republic*, ICSID Case No. ARB/02/16, Decision on Argentina’s Application for Annulment of the Award, ¶¶ 159–223 (June 29, 2010); *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶¶ 315–35, 354–94; *Enron Corp. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, ¶¶ 303–45 (May 22, 2007) (¶¶ 355–405 in the Decision on the Application for Annulment); *Cont’l Cas. Co. v. Argentine Republic*, ICSID Case No. ARB/03/9, Award, ¶¶ 107–81, 189–236 (Sept. 5, 2008); *BG Grp. PLC v. Republic of Argentina*, UNCITRAL, Final Award, ¶¶ 367, 369, 381–90, 407–12 (Dec. 24, 2007); *Nat’l Grid PLC v. Republic of Argentina*, UNCITRAL, Award, ¶¶ 250–62 (Nov. 3, 2008); *Suez v. Argentine Republic (Suez & Vivendi)*, ICSID Case No. ARB/03/19, Decision on Liability, ¶¶ 249, 257–71 (July 30, 2010); *Total SA v. Argentine Republic*, ICSID Case No. ARB/04/1, Decision on Liability, ¶¶ 482–85 (Dec. 21, 2010); *El Paso Energy Int’l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award, ¶¶ 552–670 (Oct. 27, 2011); *Impregilo SpA v. Argentine Republic*, ICSID Case No. ARB/07/17, Final Award, ¶¶ 336–60 (June 21, 2011); *Metalpar v. Argentine Republic*, ICSID Case No. ARB/03/5, Award on the Merits, ¶¶ 208–11 (June 6, 2008).

6. Treaty Concerning the Reciprocal Encouragement and Protection of Investment, U.S.-Arg., Nov. 14, 1991, S. TREATY DOC. No. 103-2 [hereinafter U.S.-Arg. BIT], provides: “This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.” For a full discussion of the interpretive issues regarding necessity clauses in international investment treaties like Article XI of the U.S.-Arg. BIT, see DIANE A. DESIERTO, *NECESSITY AND NATIONAL EMERGENCY CLAUSES: SOVEREIGNTY IN MODERN TREATY INTERPRETATION* 145–236 (2012).

ally Wrongful Acts (“2001 ASR”), Argentina was ultimately found to have failed to meet the high evidentiary threshold required to prove all the elements of this defense.<sup>7</sup> These elements are as follows:

Article 25. Necessity

1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:

(a) Is the only way for the State to safeguard an essential interest against a grave and imminent peril; and

(b) Does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.

2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:

(a) The international obligation in question excludes the possibility of invoking necessity; or

(b) The State has contributed to the situation of necessity.<sup>8</sup>

Article 27(a) of the 2001 ASR imposes the requirement that the State invoking necessity must comply with the international obligation breached as soon as the circumstance precluding wrongfulness (in this case, the state of necessity) has terminated.<sup>9</sup>

Likewise, Argentina has generally not succeeded in advancing a drastic interpretation of specific Bilateral Investment Treaty (BIT)

7. Tribunals found that the requirements of Article 25 of the 2001 ASR were not met in: *EDF Int'l SA v. Argentine Republic*, ICSID Case No. ARB/03/23, Award, ¶¶ 1169–81 (June 11, 2012); *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶¶ 315–31; *Enron Corp.*, ICSID Case No. ARB/01/3, ¶¶ 294–313; *BG Grp. PLC*, UNCITRAL, ¶¶ 388–412; *Nat'l Grid PLC*, UNCITRAL, ¶¶ 255–62; *Sempra Energy Int'l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award, ¶¶ 344–55 (Sept. 28, 2007); *Suez & Vivendi*, ICSID Case No. ARB/03/19, ¶¶ 257–65; *Total SA*, ICSID Case No. ARB/04/1, Decision on Liability, ¶ 345 (Dec. 21, 2010); *Impregilo SpA*, ICSID Case No. ARB/07/17, ¶¶ 344–59. Another instance when an arbitral tribunal rejected the customary defense of necessity under Article 25 of the 2001 ASR is *Funnekotter v. Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award, ¶¶ 105–06 (Apr. 15, 2009). On the other hand, the defense under Article 25 of the 2001 ASR was accepted in *LG&E Energy Corp.*, ICSID Case No. ARB/02/1, ¶¶ 245–59. Article 25 of the 2001 ASR was treated as a norm assisting in the interpretation of the defense of necessity under the investment treaty (Article XI of the U.S.-Argentina Bilateral Investment Treaty (BIT)) that was partly accepted in *Continental Casualty Co.*, ICSID Case No. ARB/03/9, ¶¶ 168, 192–219.

8. 2001 ASR, *supra* note 1, art. 25.

9. 2001 ASR, *supra* note 1, art. 27 states:

Article 27. Consequences of invoking a circumstance precluding wrongfulness  
The invocation of a circumstance precluding wrongfulness in accordance with this chapter is without prejudice to:

(a) Compliance with the obligation in question, if and to the extent that the circumstance precluding wrongfulness no longer exists;

(b) The question of compensation for any material loss caused by the act in question.

provisions on “measures not precluded” that involve “essential security interests” (otherwise known as “necessity clauses”). Under Argentina’s interpretation, the entire treaty no longer applies when a host State decides to implement any measure whatsoever that it deems necessary to serve its “essential security interests.”<sup>10</sup> The logical consequence of this interpretation would be that no breach can arise from an inapplicable treaty.

The foregoing interpretive theory is gainsaid by the actual textual formulations of these necessity clauses, the plain letter of which are altogether silent on the alleged effect of treaty inapplicability.<sup>11</sup> The majority of arbitral awards reported to date have rejected this theory, frequently holding Argentina liable for damages incurred by investors as a result of governmental measures taken during its 2001-2002 financial crisis.<sup>12</sup> These governmental measures were deemed to breach non-expropriation standards, such as the “fair and equitable treatment” (FET) standard, in Argentina’s investment treaties.<sup>13</sup> The purpose of the FET stan-

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10. Diane A. Desierto, *Necessity and Supplementary Means of Interpretation of Non-Precluded Measures in Bilateral Investment Treaties*, 31 U. PA. J. INT'L L. 827, 831, 850, 876, 922–23 (2010) [hereinafter Desierto, *Necessity and Supplementary Means*]; see also DESIERTO, *supra* note 6, at 173–74 (citing *Sempra Energy Int'l*, ICSID Case No. ARB/02/16; *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8; *LG&E Energy Corp.*, ICSID Case No. ARB/02/1; *Enron Corp.*, ICSID Case No. ARB/01/3; *Total SA*, ICSID Case No. ARB/04/1; *Suez & Vivendi*, ICSID Case No. ARB/03/19; *Impregilo SpA*, ICSID Case No. ARB/07/17).

11. Article XI of the U.S.-Arg. BIT provides: “This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of its own essential security interests.” See Desierto, *Necessity and Supplementary Means*, *supra* note 10, at 879, 928.

12. Argentina’s interpretation (e.g., the effect of treaty inapplicability for non-precluded measures) has been rejected in: *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶¶ 353–73, 389–92; *Enron Corp.*, ICSID Case No. ARB/01/3, ¶¶ 331–39; *El Paso Energy Int'l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, ¶¶ 613–15 (Oct. 27, 2011); *Sempra Energy Int'l*, ICSID Case No. ARB/02/16, Award, ¶¶ 364–97; *Nat'l Grid PLC*, UNCITRAL, ¶¶ 250–53; *Impregilo SpA*, ICSID Case No. ARB/07/17, ¶¶ 337–43. Significantly, in the 2012 award in *EDF Int'l SA*, ICSID Case No. ARB/03/23, ¶¶ 1153–54, Argentina did not argue the effect of treaty inapplicability: “Article 5(3) comprises a general exception for acts which occurred during extraordinary circumstances that would otherwise be contrary to the State’s obligations under the BIT. Under such circumstances, the BIT would, according to Respondent, oblige the State *only* to provide national treatment and most favorable treatment to foreign investors.”

13. See, e.g., *Suez v. Argentine Republic (Suez & Interagua)*, ICSID Case No. ARB/03/17, Decision on Liability, ¶¶ 174–228 (citing Articles 3 and 5(1) of the Argentina-France BIT and Article IV(1) of the Argentina-Spain BIT); *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶¶ 326–519 (citing Art. II(2)(a) of the 1991 Argentina-United States BIT); *Azurix Corp. v. Argentine Republic*, ICSID Case No. ARB/01/12, Award, ¶¶ 324–77 (June 23, 2006) (citing Art. II(2)(a) of the 1991 Argentina-United States BIT); *Compania de Aguas del Aconquija SA v. Argentina*, ICSID Case No. ARB/97/3, Award, ¶¶ 7.4.1–7.4.12 (Aug. 20, 2007) (citing Art. 3 of 1993 Argentina-France BIT); *Total SA*, ICSID Case No.

dard, as originally used in BIT practice, “is to fill gaps that may be left by the more specific standards, in order to obtain the level of investor protection intended by the treaties . . . The systematic location and operation of the clauses in existing investment treaties is reminiscent of general codes in civil law countries that set forth a number of specific rules and complement these with a general clause of good faith as an overarching principle that fills gaps and informs the understanding of specific clauses.”<sup>14</sup>

The arbitral awards in *El Paso, LG&E, Impregilo, Sempra, Azurix, Enron, CMS, BG Group, Suez, and Total* held that the measures Argentina implemented during its 2001-2002 financial crisis breached the FET standard in the BITs at issue in each case, and adjudged compensation as the appropriate form of reparations under the general law of reparations codified in Articles 36 et seq. in the 2001 ASR.<sup>15</sup> The same awards rejected the claims against Argentina for alleged violations of the direct or indirect expropriation provisions of the investment treaties in these cases.<sup>16</sup> While the expropriation provisions in the treaties often contained an explicit requirement of payment of prompt, adequate, and effective compensation, the treaties’ provisions on the FET standard did not provide a similar requirement of payment of compensation upon breach.<sup>17</sup>

The award in *Compañía de Aguas del Aconquija SA and Vivendi Universal SA* found that Argentina violated the FET standard, the full protection and security standard, and the BIT provision on expropriation, and thus applied methods of compensation arising from both general international law (for breaches of FET and full pro-

ARB/04/1, ¶¶ 125–27 (citing Art. 3 of the 1993 Argentina-France BIT); *Impregilo SpA*, ICSID Case No. ARB/07/17, ¶¶ 284–331 (citing Art. 2(2) of the Argentina-Italy BIT).

14. RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 122 (2008).

15. See, e.g., *El Paso Energy Int’l Co.*, ICSID Case No. ARB/03/15, ¶ 752; *LG&E Energy Corp. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability, ¶ 267 (Oct. 3, 2006); *Impregilo SpA*, ICSID Case No. ARB/07/17, pt. VI; *Sempra Energy Int’l*, ICSID Case No. ARB/02/16, Award, ¶ 486; *Azurix Corp.*, ICSID Case No. ARB/01/12, ¶ 442; *Enron Corp.*, ICSID Case No. ARB/01/3, ¶ 453; *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶ 472; *Nat’l Grid PLC*, UNCITRAL, ¶ 296; *BG Grp. PLC*, UNCITRAL, ¶¶ 413–18; *Suez*, ICSID Case No. ARB/03/117, ¶ 248; *Total SA*, ICSID Case No. ARB/04/1, ¶ 485.

16. *El Paso Energy Int’l Co.*, ICSID Case No. ARB/03/15, ¶¶ 265–80; *LG&E Energy Corp.*, ICSID Case No. ARB/02/1, ¶¶ 185–200; *Impregilo SpA*, ICSID Case No. ARB/07/17, ¶¶ 268–83; *Sempra Energy Int’l*, ICSID Case No. ARB/02/16, Award, ¶¶ 280–86; *Azurix Corp.*, ICSID Case No. ARB/01/12, ¶¶ 314–22; *Enron Corp.*, ICSID Case No. ARB/01/3, ¶¶ 234–350; *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶¶ 252–64; *Nat’l Grid PLC*, UNCITRAL, ¶ 296; *BG Grp. PLC*, UNCITRAL, ¶¶ 144–55, 244–72; *Suez & Interagua*, ICSID Case No. ARB/03/17, ¶¶ 117–51; *Total SA*, ICSID Case No. ARB/04/1, ¶¶ 191–99.

17. U.S.-Arg. BIT, *supra* note 6, art. VI.

tection and security) and the BIT (for violation of the expropriation provision).<sup>18</sup> Arbitral tribunals uniformly refer to compensation as a form of reparations embraced by the *Chorzów* standard, under which the injured party is to be returned to its position had the injury not occurred.<sup>19</sup> Nonetheless, their valuation methods exhibit marked differences owing to the broad margin of arbitrator discretion in determining “financially assessable damage” within the purview of Article 36 of the 2001 ASR.

Argentina did not seek mitigation of damages or reduced liability by arguing that its measures were taken to ensure continued compliance with international social and economic rights.<sup>20</sup> Rather, the *amicus curiae* brief in the *Suez v. Argentina* case, submitted by five non-governmental organizations in 2007, first advanced this position by proposing a method of interpretation of fundamental social and economic rights in relation to a BIT.<sup>21</sup> The thirty-page *amicus* brief in *Suez*<sup>22</sup> identified the applicable human rights involved to be the right to water, right to life, and related rights.<sup>23</sup> The *Suez amici* argued that these human rights are included in the relevant applicable law to the dispute as “rules of international law” under Article 42(1) of the International Centre for Settlement of Investment Disputes (ICSID) Convention,<sup>24</sup> and as such, could be read to assist in the interpretation of the “FET standard and the “indirect expropriation” standard in the BIT.<sup>25</sup> The bulk of the analysis in the *Suez* brief was devoted to this novel reinterpretation of the FET and indirect expropriation.<sup>26</sup> Towards the end of its argument, the *amici* briefly mentioned that:

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18. *Compania de Aguas del Aconquija SA*, ICSID Case No. ARB/97/3, ¶¶ 11, 11.1.

19. *Factory at Chorzów (Ger. v. Pol.)*, 1927 P.C.I.J. (ser. A) No. 9, at 47 (Sept. 13) (“The essential principle contained in the actual notion of an illegal act—a principle which seems to be established by international practice and in particular by the decisions of arbitral tribunals—is that reparation must, as far as possible, wipe-out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed. Restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear; the award, if need be, of damages for loss sustained which would not be covered by restitution in kind or payment in place of it—such are the principles which should serve to determine the amount of compensation due for an act contrary to international law.”).

20. *See Suez & Vivendi*, ICSID Case No. ARB/03/19.

21. *Id.* ¶ 256.

22. *See* Brief for Centro de Estudios Legales y Sociales et al. as Amici Curiae, *Suez & Vivendi*, ICSID Case No. ARB/03/19 (July 30, 2010) [hereinafter Brief for Centro de Estudios Legales y Sociales].

23. *Id.* at 12.

24. *Id.* at 13–14.

25. *Id.* at 15–16, 21.

26. *Id.* at 19, 21, 23, 24.



Human rights law could displace investment law in a conflict of norms situation. . . [which] could arise if the Tribunal were to find, for example, that the backdrop of a severe economic crisis, the guarantees offered to foreign investors with respect to the concession's economic equilibrium were incompatible with the government's duty to ensure access to water to the population.<sup>27</sup>

The *amici* chose not to develop this argument further, however, finding that it was not necessary for the adjudication of the case.<sup>28</sup>

This Article builds its analysis from key pronouncements in the 2010 *Suez* award and the 2005 *CMS* award. First, the *Suez* tribunal acknowledged that in a time of emergency, a host State remains bound to observe *both* its international human rights obligations as well as its investment treaty obligations.<sup>29</sup> The tribunal did not elucidate this point further, as it found that on the facts of the case Argentina had not shown its inability to fulfill both sets of obligations at the time of the 2001–2002 financial crisis.<sup>30</sup> Second, while the *CMS* tribunal acknowledged that the 2001–2002 Argentine financial crisis would have “specific consequences on the question of reparation,”<sup>31</sup> the ultimate award of compensation did not specify those consequences. These developments in tribunal reasoning spur this Article's proposal that a host State's good faith compliance with the minimum core obligations under the International Covenant on Economic Social and Cultural Rights (ICESCR) during economic emergencies can, and indeed should, be taken into account in the process of valuing the compensation attributable to the same host State for injury caused to investor rights.

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27. *Id.* at 26.

28. *Id.*

29. *Suez & Vivendi*, ICSID Case No. ARB/03/19, ¶ 262 reads as follows:

*The third condition for the defense of necessity: Treaty obligation does not exclude the necessity defense.* The texts of the three BITs in question do not specifically exclude or allow the admissibility of a defense of necessity. . . Argentina and the *amicus curiae* submissions received by the Tribunal suggest that Argentina's human rights obligations to assure its population the right to water somehow trumps its obligations under the BITs and that the existence of the human right to water also implicitly gives Argentina the authority to take actions in disregard of its BIT obligations. The Tribunal does not find a basis for such a conclusion either in the BITs or international law. *Argentina is subject to both international obligations, i.e., human rights and treaty obligation, and must respect both of them equally. Under the circumstances of these cases, Argentina's human rights obligations and its investment treaty obligations are not inconsistent, contradictory, or mutually exclusive. Thus, as discussed above, Argentina could have respected both types of obligations.* Viewing each treaty as a whole, the Tribunal does not find that any of them excluded the defense of necessity. Therefore Argentina must be deemed to have satisfied the third condition for the defense of necessity.

*Id.* (emphasis added).

30. *Id.* ¶ 262.

31. *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶ 406 (Apr. 25, 2005).

Part II of this Article describes the State—driven consultative process of determining a state's minimum core obligations under the ICESCR as the obligatory baseline after a State joins the ICESCR. While this baseline may be empirically dynamic over time, it is nevertheless still capable of broad-based identification through the established monitoring practices and reportage process facilitated by the Committee on Economic, Social, and Cultural Rights (the Committee) together with ICESCR Member States, specialized agencies of the United Nations, as well as non-governmental organizations, considered in conjunction with the substantive content of such minimum core obligations as developed by the Committee over the years in its General Comments.<sup>32</sup> During economic crises, the Committee can exercise its mandate from the United Nations Economic and Social Council to continuously consult with, and elicit information from, the aforementioned constituencies and States parties to the ICESCR, in order to determine the scope and mode of observance of such applicable minimum core obligations by States.

Part III then shows that most arbitral tribunals confronted with breaches of non-expropriation standards in investment treaties during financial crises or emergencies tend circuitously to refer to the "fair market value" standard defined in the treaty for compensation of expropriation. This Article argues that tribunals awarding compensation on the basis of the "fair market value" standard do not adequately consider other salient factors for determining what ought to be merely "financially assessable damage" as the standard of compensation under Article 36 of the 2001 ASR. This Article draws particular attention to the concepts of "mitigation" of compensation arising from the equitable conduct of the parties, as well as other tribunals' use of "past performance" yardsticks<sup>33</sup> in compensating losses arising from emergencies. In line with these concepts, this Article submits that a host State's good faith compli-

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32. See Comm. on Econ., Soc. & Cultural Rights, Rep. on the 5th Sess., Nov. 26–Dec. 14, 1990, at 83, ¶ 2, U.N. Doc. E/C.12/1990/8, Annex III; ESCOR, Supp. No. 3 (1991) [hereinafter General Comment 3]; see also Comm. on Econ., Soc. & Cultural Rights, Substantive Issues Arising in the Implementation of the International Covenant on Economic, Social and Cultural Rights: General Comment 12, ¶ 17, U.N. Doc. E/C.12/1999/5 (May 12, 1999) [hereinafter General Comment 12]; Comm. on Econ., Soc. & Cultural Rights, Substantive Issues Arising in the Implementation of the International Covenant on Economic, Social and Cultural Rights: General Comment 14, ¶ 43, U.N. Doc. E/C.12/2000/4 (Aug. 11, 2000) [hereinafter General Comment 14]; Comm. on Econ., Soc. & Cultural Rights, General Comment 19: The Right to Social Security (Art. 9), ¶ 59, U.N. Doc. E/C.12/GC/19 (Feb. 4, 2008) [hereinafter General Comment 19].

33. Instead of "lost profits or *lucrum cessans*."

ance with the ICESCR minimum core obligations during an economic emergency should be deemed an acceptable ground within the general law of reparations for equitably reducing the quantum of investment compensation awards.

Part IV suggests that the discount rate predominantly used should also capture the host State's duty to fulfill ICESCR minimum core obligations as a fixed constraint on government resources in times of financial crises. This can be done in two ways: first, through the estimation of the investment beta (which tracks the sensitivity of the investment's returns relative to overall market returns), and second, through the estimation of the country risk premium (which refers to the additional risk associated with investing in a particular country). Both the investment beta coefficient and the country risk premium should be adjusted upwards, in order to reflect the inherent uncertainty of the range of government policies that may be adopted to fulfill the ICESCR minimum core obligations during economic crises.<sup>34</sup> The upward adjustment of the investment beta and the country risk premium will result in a more realistic discount rate, and ultimately a less bloated assessment of the value of an investment at the time the host State imposes governmental measures to fulfill its ICESCR obligations.

In Part V, the Article submits that the proportionality requirement built into the structure of the law of reparations must be restored in the award of compensation in investment arbitrations involving host State measures taken in a time of financial or economic crises. The fair market value standard, as defined under assumptions of perfect competition in the International Glossary of Business Valuation Terms, cannot be treated as the default measure under the general law of international responsibility, which only refers to "financially assessable damage" in Article 36 of the 2001 ASR. The determination of compensation under this Article is intended to produce the "equitable outcome" for both the injured State and the injuring State—the same requirement should not be overlooked when the injured party is an individual or institutional investor. While the ICESCR minimum core obligations likewise require estimation and verification, arbitral tribunals can invite the Committee to extend *amicus* expertise in particular cases when a State asserts that its injurious acts to investors were committed to fulfill its ICESCR minimum core obligations in good faith during an economic emergency. Host States still retain the *onus*

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34. See Lubos Pastor & Pietro Veronesi, *Uncertainty About Government Policy and Stock Prices*, 67 J. FIN. 1219, 1252–55 (2012).

*probandum* to show that their invocation of ICESCR compliance is not made simply as a pretextual afterthought to avoid international responsibility elsewhere.

## II. ICESCR MINIMUM CORE OBLIGATIONS DURING ECONOMIC EMERGENCIES

### A. *Shifting between Paradigms of Justiciability and Treaty Monitoring*

Admittedly, while ICESCR rights have been more prevalent objects of domestic judicial enforcement,<sup>35</sup> they have not yet been tested as decisive *lis mota* in contentious cases before the International Court of Justice (ICJ). The ICJ has explicitly articulated some aspects of the nature of ICESCR rights and a State's likely breach of such rights only through an advisory opinion.<sup>36</sup> In the *Advisory Opinion on the Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory*, the ICJ declared that Israel, as the Occupying Power, "is bound by the provisions of the International Covenant on Economic, Social and Cultural Rights. Furthermore, it is under an obligation not to raise any obstacle to the exercise of such rights in those fields where competence has been transferred to Palestinian authorities."<sup>37</sup>

The ICJ also considered the relevance of international human rights obligations, including several ICESCR provisions on: (1) the right to work, protection, and assistance accorded to the family and to children and young persons, (2) the right to an adequate standard of living, (3) the right to be free from hunger, (4) the right to health, and (5) the right to education,<sup>38</sup> ultimately finding that the construction of the wall impeded the exercise of such ICESCR rights.<sup>39</sup> Other than this advisory opinion, the ICJ has not had the direct opportunity to adjudicate legal issues arising from ICESCR rights. By contrast, regional human rights systems have demonstrated more normative developments on economic, social and cultural rights (such as the African Charter on Human and Peoples'

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35. See INT'L COMM'N OF JURISTS, COURTS AND THE LEGAL ENFORCEMENT OF ECONOMIC, SOCIAL AND CULTURAL RIGHTS: COMPARATIVE EXPERIENCES OF JUSTICIABILITY 23-64 (2008), available at <http://www.unhcr.org/refworld/docid/4a7840562.html> (defining the content, scope, justiciability, and interpretations of ESC rights in domestic courts through principles and case law examples).

36. *Legal Consequences of the Construction of a Wall in the Occupied Palestinian Territory*, Advisory Opinion, 2004 I.C.J. 136, 180-81 (July 9).

37. *Id.* ¶ 112.

38. *Id.* ¶ 130.

39. *Id.* ¶ 133-34.

Rights,<sup>40</sup> the 1948 Charter of the Organization of American States,<sup>41</sup> the 1969 American Convention of Human Rights,<sup>42</sup> the 1988 Additional Protocol on Economic, Social and Cultural Rights,<sup>43</sup> and the revised European Social Charter).<sup>44</sup> These latter instruments enforce economic, social, and cultural rights according to procedures and mechanisms specifically defined under each regional treaty regime.<sup>45</sup>

International remedies for ICESCR violations thus partake more of the nature of individual complaints mechanisms, rather than traditionally litigated inter-State disputes. It was not until December 2008 that the landmark individual complaints procedure for the Committee was initiated through the Optional Protocol to the International Covenant on Economic, Social and Cultural Rights (“Optional Protocol to the ICESCR”).<sup>46</sup> As of this writing, the Optional Protocol to the ICESCR will enter into force after three more State ratifications or accessions; to date only eight State Parties (Argentina, Bolivia, Bosnia and Herzegovina, Ecuador, El Salvador, Mongolia, Spain, and Slovakia) have completed ratification and/or accession procedures out of the thirty-nine signatory States.<sup>47</sup> The Optional Protocol to the ICESCR empowers the Committee to request urgent interim measures from a State Party “as may be necessary in exceptional circumstances to avoid possible irreparable damage to the victim or victims of the alleged violations.”<sup>48</sup> After examination of the individual communication, the

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40. African Charter on Human and Peoples’ Rights, June 27, 1981, 1520 U.N.T.S. 217, 245.

41. Charter of the Organization of American States, Apr. 30, 1948, O.A.S.T.S. No. 1-C.

42. American Convention on Human Rights, Nov. 21, 1969, 1144 U.N.T.S. 143.

43. Additional Protocol to the American Convention on Human Rights in the Area of Economic, Social, and Cultural Rights, Nov. 17, 1988, O.A.S.T.S. No. 69.

44. European Social Charter (Revised), May 3, 1996, 2151 U.N.T.S. 277 (2001).

45. See Mashood A. Baderin, *The African Commission on Human and Peoples’ Rights and the Implementation of Economic, Social and Cultural Rights in Africa*, in ECONOMIC, SOCIAL, AND CULTURAL RIGHTS IN ACTION 139, 140 (Mashood A. Baderin & Robert McCorquodale eds., 2007) [hereinafter RIGHTS IN ACTION]; Veronica Gomez, *Economic, Social, and Cultural Rights in the Inter-American System*, in RIGHTS IN ACTION, *supra*, at 167, 167–68; Robin R. Churchill & Urfan Khaliq, *Violations of Economic, Social, and Cultural Rights: The Current Use and Future Potential of the Collective Complaints Mechanism of the European Social Charter*, in RIGHTS IN ACTION, *supra*, at 195, 196.

46. Optional Protocol to the International Covenant on Economic, Social and Cultural Rights arts. 1–2, G.A. Res. 63/117, U.N. Doc. A/RES/63/117, Annex, at 2 (Mar. 5, 2009) [hereinafter Optional Protocol to ICESCR].

47. See Status of the Optional Protocol to ICESCR, U.N. TREATY COLLECTION, [http://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsg\\_no=IV-3-a&chapter=4&lang=en](http://treaties.un.org/Pages/ViewDetails.aspx?src=TREATY&mtdsg_no=IV-3-a&chapter=4&lang=en) (last updated Oct. 20, 2012).

48. Optional Protocol to ICESCR, *supra* note 46, art. 5.

Committee transmits its views to the State Party concerned for that State Party's consideration and action.<sup>49</sup> The Optional Protocol confers authority to the Committee to conduct confidential inquiries on alleged grave or systematic violations by a State Party of ICESCR rights, and thereafter to transmit findings and recommendations to the State Party concerned.<sup>50</sup> The Optional Protocol also enables an inter-State communications procedure, culminating with the issuance of a Committee report on the disputed matter.<sup>51</sup>

### B. *Minimum Core Obligations as the Raison d'être of the ICESCR*

Article 2(1) of the ICESCR contains the core obligation of States in the form of the "undertaking to take steps" to realize ICESCR rights.<sup>52</sup> The tenor of the obligation is purposely evolutionary ("to the maximum of available resources") and dynamic ("with a view to progressively achieving the full realization of the rights recognized in the present Covenant by appropriate means"), in contrast with the discrete and readily-determinable obligation "to respect and to ensure" civil and political rights under Article 2(1) of the International Covenant on Civil and Political Rights (ICCPR).<sup>53</sup> The Committee explains the obligation "to take steps" as one that should be "deliberate, concrete, and targeted as clearly as possible towards meeting the obligations recognized in the Covenant,"<sup>54</sup> with the means to be used to fulfill the obligation to take steps being "all appropriate means, including particularly the adoption of legislative measures."<sup>55</sup> Other possible appropriate measures may include, and are not limited to, "administrative, financial, educational and social measures."<sup>56</sup> Most importantly, the Committee stresses that the "principal obligation of result reflected in article

49. *Id.* arts. 7-8.

50. *Id.* art. 11.

51. *Id.* art. 10.

52. International Covenant on Economic, Social and Cultural Rights art. 2(1), Dec. 16, 1966, S. TREATY DOC. NO. 95-19, 993 U.N.T.S. 3 [hereinafter ICESCR] ("Each State Party to the present Covenant undertakes to take steps, individually and through international assistance and co-operation, especially economic and technical, to the maximum of its available resources, with a view to achieving progressively the full realization of the rights recognized in the present Covenant by all appropriate means, including particularly the adoption of legislative measures.").

53. International Covenant on Civil and Political Rights art. 2(1), Dec. 16, 1966, S. TREATY DOC. NO. 95-20, 999 U.N.T.S. 171 ("Each State Party to the present Covenant undertakes to respect and to ensure to all individuals within its territory and subject to its jurisdiction rights recognized in the present Covenant . . .").

54. General Comment 3, *supra* note 32, ¶ 2.

55. *Id.* ¶ 3.

56. *Id.* ¶ 7.

2(1) is to take steps ‘with a view to achieving progressively the full realization of the rights recognized’ in the Covenant.”<sup>57</sup> The Committee posits that “progressive realization” entails necessary flexibility but does not deprive the ICESCR of its *raison d’être*.<sup>58</sup> As such, States Parties to the ICESCR are obligated to “move as expeditiously and effectively as possible” towards realizing ICESCR rights, and must fully justify any “deliberately retrogressive measures” before such measures are introduced.<sup>59</sup>

The central concept behind the general obligation under ICESCR Article 2(1) is for States to observe the irreducible *minimum core obligations* that exists as the *raison d’être* of the ICESCR. After examining years of State reports and practices, the Committee took the position in its 1990 General Comment 3 that there exists a “minimum core obligation to ensure the satisfaction of, at the very least, minimum essential levels of each of the rights,” even when resource constraints are taken into account.<sup>60</sup> A State Party can only justify its failure to meet the ICESCR minimum core obligation due to a lack of available resources if it shows that “every effort has been made to use all resources that are at its disposition in an effort to satisfy, as a matter of priority, those minimum obligations.”<sup>61</sup> The Committee was explicit in requiring the observance of the ICESCR minimum core obligations even in times of “economic recession,” where “the vulnerable members of society can and indeed must be protected by the adoption of relatively low-cost targeted programmes.”<sup>62</sup> In a document called “16 May 2011 Letter to States Parties,” the Committee Chairperson reminded States that austerity programs imposed in response to financial crises must not deviate from the minimum core content of ICESCR obligations:

Economic and financial crises, and a lack of growth, impede the progressive realization of economic, social and cultural rights and can lead to retrogression in the enjoyment of those rights. The Committee realizes that some adjustments in the implementation of some of these Covenant rights are at times inevitable. States Parties, however, should not act in breach of their obligations under the Covenant.

In such cases, the Committee emphasizes that any proposed policy change or adjustment that has to meet the following

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57. *Id.* ¶ 9.

58. *Id.*

59. *Id.*

60. *Id.* ¶ 10.

61. *Id.*

62. *Id.* ¶ 12.

requirements: first, the policy is a temporary measure covering only the period of crisis; second, the policy is necessary and proportionate, in the sense that the adoption of any other policy, or a failure to act, would be more detrimental to economic, social and cultural rights; third, the policy is not discriminatory and comprises all possible measures, including tax measures, to support social transfers to mitigate inequalities that can grow in times of crisis and to ensure the rights of the disadvantaged and marginalized individuals and groups are not disproportionately affected; *fourth, the policy identifies the minimum core content of rights, or a social protection floor, as developed by the International Labour Organization and ensures the protection of this core content at all times.*<sup>63</sup>

The ICESCR minimum core obligation takes into account not just the State's available resources, but also those resources over which the State exercises *jus disponendi* (right to dispose). Identifying the exact content of the minimum core obligations in each and every case is not a static process, but rather, is one that purposely accepts evolution according to need, scientific and technological advancement, and other factors.<sup>64</sup> Nonetheless, the legal parameters of "essential levels" or "core content" of ICESCR obligations are determinable. A minimum core obligation refers to the essential level of each ICESCR right, "without which a right loses its substantive significance as a human right."<sup>65</sup> Manisuli Ssenyonjo describes the minimum core obligation as an "absolute international minimum," applicable "whatever the State's level of development and available resources" since the ICESCR minimum core obligation entails "a basic level of subsistence necessary to live in dignity . . . the base-line below which all States must not fall; and should endeavor to rise above."<sup>66</sup>

It is from this baseline that States can move progressively towards the full realization of ICESCR rights. Before a State may attribute its failure to meet minimum core obligations to a lack of available resources, the Committee explained that the State "must demonstrate that every effort has been made to use all resources that are

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63. Letter from Ariranga G. Pillay, Chairperson, Comm. on Econ., Soc. & Cultural Rights, to All States Parties to the ICESCR (May 16, 2011) (emphasis added), *available at* <http://www2.ohchr.org/english/bodies/cescr/docs/LetterCESCRtoSP16.05.12.pdf>.

64. INT'L COMM'N OF JURISTS, *supra* note 35, at 23.

65. MAGDALENA SEPÚLVEDA, THE NATURE OF THE OBLIGATIONS UNDER THE INTERNATIONAL COVENANT ON ECONOMIC, SOCIAL AND CULTURAL RIGHTS 366 (2003).

66. MANISULI SSENYONJO, ECONOMIC, SOCIAL AND CULTURAL RIGHTS IN INTERNATIONAL LAW 66-67 (2009).



at its disposition in an effort to satisfy, as a matter of priority, those minimum obligations.”<sup>67</sup>

### C. Identifying and Measuring Minimum Core Obligations

While it may thus appear that ICESCR minimum core obligations are a constantly evolving, and rather imprecise, conceptual *bricolage*, the process of identifying the ICESCR minimum core obligations is not too far removed from the usual methods of proportionality analysis in judicial reasoning.<sup>68</sup> Apart from requiring States themselves to identify their core minimum entitlements to ICESCR rights that apply to them and to periodically collect data on this ICESCR baseline,<sup>69</sup> the Committee itself has issued General Comments specifying the minimum core content of several rights including the right to food,<sup>70</sup> the right to health,<sup>71</sup> the right to social security,<sup>72</sup> and the right to water.<sup>73</sup> These Comments pro-

67. General Comment 3, *supra* note 32, ¶ 10.

68. See generally AHARON BARAK, PROPORTIONALITY: CONSTITUTIONAL RIGHTS AND THEIR LIMITATIONS 202–10 (2012) (on proportionality and international and national human rights law); *id.* at 422–34 (on proportionality and positive constitutional rights).

69. Philip Alston, *Out of the Abyss: The Challenges Confronting the New U.N. Committee on Economic, Social and Cultural Rights*, 9 HUM. RTS. Q. 332, 353 (1987) (“Each right must therefore give rise to an absolute minimum entitlement, in the absence of which a state party is to be considered to be in violation of its obligations. The question for the Committee is how to go about identifying the core entitlement flowing from each right recognized in the Covenant. In the first instance, of course, the responsibility rests with the states parties themselves.”); see Comm. on Econ., Soc. & Cultural Rights, Concluding Observations of the Committee on Economic, Social and Cultural Rights: Sweden, ¶ 40, U.N. Doc. E/C.12/1/Add.70 (Nov. 30, 2001); Comm. on Econ., Soc. & Cultural Rights, Concluding Observations of the Committee on Economic, Social and Cultural Rights: Suriname, ¶¶ 9, 18, U.N. Doc. E/C.12/1995/6 (June 7, 1995); Comm. on Econ., Soc. & Cultural Rights, Concluding Observations of the Committee on Economic, Social and Cultural Rights: Australia, ¶ 33, U.N. Doc. E/C.12/1/Add.50 (Sept. 11, 2000); see also CONCLUDING OBSERVATIONS OF THE U.N. COMMITTEE ON ECONOMIC, SOCIAL AND CULTURAL RIGHTS 20–26 (Leif Holmström ed., 2003) (Argentina); *id.* at 289–98 (Iraq); *id.* at 307–20 (Israel).

70. General Comment 12, *supra* note 32, ¶ 6–15, 17; see also Rolf Kunnemann, *The Right to Adequate Food: Violations Related to Its Minimum Core Content*, in CORE OBLIGATIONS: BUILDING A FRAMEWORK FOR ECONOMIC, SOCIAL AND CULTURAL RIGHTS 161, 161–83 (Audrey Chapman & Sage Russell eds., 2002) [hereinafter CORE OBLIGATIONS] (explaining the Covenant’s treatment of the right to food).

71. General Comment 14, *supra* note 32, ¶ 43; see also Audrey R. Chapman, *Core Obligations Related to the Right to Health*, in CORE OBLIGATIONS, *supra* note 70, at 185, 185–215 (explaining the Covenant’s treatment of the right to the highest attainable standard of health).

72. General Comment 19, *supra* note 32, ¶ 59; see also Lucie Lamarche, *The Right to Social Security in the International Covenant on Economic, Social and Cultural Rights*, in CORE OBLIGATIONS, *supra* note 70, at 87, 87–114 (explaining the Covenant’s treatment of the right to social security).

73. Comm. on Econ., Soc. & Cultural Rights, Substantive Issues Arising in the Implementation of the International Covenant on Economic, Social and Cultural Rights: Gen-

vide useful guidelines and benchmarks for States not just in their country reporting duties to the Committee, but also for undertaking their ongoing and regular national assessments of the “minimum core content” of ICESCR protection. The Limburg Principles on the Implementation of the ICESCR, formulated in 1986 by a distinguished group of international law experts and representatives of the United Nations Centre for Human Rights, the International Labour Organisation, the United Nations Educational, Scientific and Cultural Organization (UNESCO), the World Health Organization (WHO), and the United Nations Economic and Social Council, emphasize the “subsistence” quality of the minimum core obligations under the ICESCR: “States Parties are obligated, regardless of the level of economic development, to ensure respect for minimum subsistence rights for all.”<sup>74</sup> The implication of the ICESCR minimum core obligations, according to Robert E. Robertson, is that the State has the obligation:

[T]o intrude without limit into both private and state resources previously used for other purposes, in order to ensure that its population receives “core” entitlements. In other words, there is an assumption, though a rebuttable one in the eyes of the Committee, that every state possesses sufficient resources for subsistence purposes if they define resources broadly enough and are sufficiently aggressive in resource acquisition.<sup>75</sup>

Robertson proposes examining different types of resources—human resources, technological resources, information resources, natural resources, and financial resources—in order to empirically measure a State’s compliance with ICESCR obligations.<sup>76</sup> The UN Commission on Human Rights has also urged States to “consider identifying specific national benchmarks designed to give effect to the minimum core obligation to ensure the satisfaction of minimum essential levels of each of the [ICESCR] rights . . . .”<sup>77</sup> Academic literature has since developed helpful guidance on quantitative measurements, analytical indicators, and empirical methodologies to determine the “minimum core obligation” of

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eral Comment No. 15 (2002), ¶ 37, U.N. Doc. E/C.12/2002/11 (Jan. 20, 2003) [hereinafter General Comment 15].

74. Comm’n on Human Rights, Note Verbale Dated 5 December 1986 from the Permanent Mission of the Netherlands to the United Nations Office at Geneva Addressed to the Centre for Human Rights, ¶ 25, U.N. Doc. E/CN.4/1987/17 (Jan. 8, 1987).

75. Robert E. Robertson, *Measuring State Compliance with the Obligation to Devote the ‘Maximum Available Resources’ to Realizing Economic, Social, and Cultural Rights*, 16 HUM. RTS. Q. 693, 702 (1994).

76. *Id.* at 702–13.

77. Comm’n on Human Rights Res. 1993/14, Rep. on the 49th Sess., Feb. 1–Mar. 12, 1993, ESCOR, Supp. No. 3, E/CN.4/1993/122, at 88, ¶ 7 (Feb. 26, 1993).

ICESCR rights, considering the peculiar resource constraints, governmental capabilities, and population needs unique to various States Parties.<sup>78</sup> While ICESCR minimum core obligations are inherently dynamic as defined by States in conjunction and consultation with the Committee, these core entitlements remain determinable precisely due to the periodic dialogic processes between the ICESCR State Parties and the Committee.

Furthermore, some domestic constitutional court practices already reflect gainful acceptance of the ICESCR minimum core obligations. In its landmark judgment in *Government of South Africa v. Grootboom*, the South African Constitutional Court defined minimum core obligations as “determined generally by having regard to the needs of the most vulnerable group that is entitled to the protection of the right in question.”<sup>79</sup> The South African Constitutional Court noted that for purposes of the particular case, it did not yet have the comparable information—income, unemployment, availability of land, poverty, differences between city and rural communities, economic and social circumstances, and history of a country—at its disposal to determine the minimum core content of the right to housing as recognized in South Africa.<sup>80</sup> The German Constitutional Court tied the concept of a “minimum level of existence” (Existenzminimum) to the fundamental constitutional duty of the State to “ensure persons the minimum conditions for a dignified existence.”<sup>81</sup> Admittedly, these are distinct practices of both the German and South African Constitutional Courts that have developed according to their own legal traditions and receptivity to international law. Some scholars validly raise the

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78. See generally George S. McGraw, *Defining and Defending the Right to Water and Its Minimum Core: Legal Construction and the Role of National Jurisprudence*, 8 LOY. U. CHI. INT'L L. REV. 127 (2011) (arguing for a “minimum core” standard and reviewing a variety of domestic examples of its implementation); Sital Kalantry, Joyceln E. Getgen, & Steven Arrigg Koh, *Enhancing Enforcement of Economic, Social, and Cultural Rights Using Indicators: A Focus on the Right to Education in the ICESCR*, 32 HUM. RTS. Q. 253 (2010) (proposing the development of “analytic indicators” in a structure-process-outcome framework to define state obligations and to measure compliance, focusing on the right to education); EDWARD ANDERSON, USING QUANTITATIVE METHODS TO MONITOR GOVERNMENT OBLIGATIONS IN TERMS OF THE RIGHTS TO HEALTH AND EDUCATION (Nov. 2008), available at <http://www.cesr.org/downloads/Quantitative%20Methods%20for%20Measuring%20ESCR.pdf>; Eitan Felner, *A New Frontier in Economic and Social Rights Advocacy? Turning Quantitative Data into a Tool for Human Rights Accountability*, 9 SUR INT'L J. HUM. RTS. 109 (2008). On auditing national government policies in light of the ICESCR, see the methodology developed in Radhika Balakrishnan & Diane Elson, *Auditing Economic Policy in the Light of Obligations on Economic and Social Rights*, 5 ESSEX HUM. RTS. REV. 1, 1–19 (2008).

79. *Gov. of South Africa v. Grootboom*, 2001 (1) SA 46 (CC), ¶ 31.

80. *Id.* ¶¶ 31–32.

81. INT'L COMM'N OF JURISTS, *supra* note 35, at 24 (citing BVERFGE 40, 121 (133)).

concern that “in general, the direct effect of [ICESCR and similar] treaties is marginal to social and economic rights litigation in the courts examined: courts rarely relied on or even cited international or regional treaty instruments in their written opinions.”<sup>82</sup>

The presence of indeterminacy admittedly generates some complexity in the process of identifying the ICESCR minimum core obligations at any given point in time.<sup>83</sup> Host States confronted with conflicting fiscal priorities between socioeconomic protection and investor compensation during economic emergencies will inevitably have to establish that prioritization of public funds is indeed for the purpose of maintaining the minimum essential levels mandated by the ICESCR minimum core obligation. This analysis will require proof of the actual content of the ICESCR minimum core obligations in a given factual setting.

A host State advancing this preliminary argument need not be overburdened by the *onus probandi*. As gleaned from the foregoing benchmarks provided by the Committee and the comparative domestic jurisprudence interpreting the ICESCR minimum core obligations, it is indeed possible to determine the “essential levels” of each ICESCR right. This may be achieved by referring to the following: (1) the State’s available resources for its disposal at the time of the economic emergency, (2) the nature and needs of vulnerable domestic groups during the economic emergency, (3) the insufficiency of present government efforts to satisfy the ICESCR minimum core obligation and a demonstrable need for more fiscal intervention to directly provide such “essential levels,” and (4) the clear intent of the government to provide for the public interest, and not merely to use the ICESCR core minimum obligation as a subterfuge or pretext to avoid payment of investor compensation. The ICESCR General Comments can also provide guidance to States as they make ICESCR-compliant calibrations of socio-economic protections within their jurisdictions. A host State that is a party to the ICESCR has also itself (presumably) submitted the mandatory initial report to the Committee, setting out the ICESCR minimum core obligations applicable within its jurisdiction.<sup>84</sup> The

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82. Varun Gauri & Daniel M. Brinks, *Introduction to Courting Social Justice: Judicial Enforcement of Social and Economic Rights in the Developing World* 1, 33 (Varun Gauri & Daniel M. Brinks eds., 2008).

83. See Katharine G. Young, *The Minimum Core of Economic and Social Rights: A Concept in Search of Content*, 33 *YALE J. INT'L L.* 113, 164–73 (2008).

84. See ICESCR, *supra* note 52, arts. 16, 17; Comm. on Econ., Soc. & Cultural Rights, Rules of Procedure of the Committee, r. 58–65, U.N. Doc. E/C.12/1990/4/Rev. 1 (Sept. 1, 1993).

Committee's Annual Reports to the UN Economic and Social Council under the 1503 Reporting Procedure also independently examine situations in countries that have not submitted such initial reports.<sup>85</sup> The Committee can also cross-reference State reported data with quantitative indicators and primary data collected by other specialized agencies of the United Nations, such as the WHO, the International Labour Organization, the Food and Agriculture Organization, and UNESCO.<sup>86</sup>

D. *Applicability of ICESCR Minimum Core Obligations to Emergencies*

A final preliminary consideration for host States advancing the ICESCR minimum core obligations is that the minimum floor or obligatory baseline of socioeconomic protection applies both in times of stability and emergency. Unlike the ICCPR, the ICESCR does not have a specific derogation or public emergency provision. ICESCR Article 4 merely operates to permit narrow limitations to ICESCR rights as "determined by law only in so far as this may be compatible with the nature of these rights and solely for the purpose of promoting the general welfare in a democratic society."<sup>87</sup> The Office of the UN High Commissioner of Human Rights interprets this limitation to mean that "[t]here is no express permission under human rights law for States to derogate from their obligations in relation to economic, social and cultural rights during emergencies, disasters or armed conflicts."<sup>88</sup> According to the Committee, "because core obligations are non-derogable, they continue to exist in situations of conflict, emergency, and natural disaster."<sup>89</sup> Consequently, the Committee finds that "[w]hen grouped together, the core obligations establish an international minimum threshold that all developmental policies should be designed to respect . . . . If a national or international anti-poverty strategy does not reflect this minimum threshold, it is inconsistent with the

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85. See *International Norms and Standards Relating to Disability: § 3.2 1503 Procedure of the Economic and Social Council*, U.N. ENABLE, <http://www.un.org/esa/socdev/enable/comp203.htm#3.2> (last visited Oct. 22, 2012).

86. Manuli Ssenyonjo, *Economic, Social and Cultural Rights: An Examination of State Obligations*, in RESEARCH HANDBOOK ON INTERNATIONAL HUMAN RIGHTS LAW 36-70 (Sarah Joseph & Adam McBeth eds., 2010).

87. ICESCR, *supra* note 52, art. 4.

88. OFF. OF U.N. HIGH COMM'R FOR HUMAN RIGHTS, FREQUENTLY ASKED QUESTIONS ON ECONOMIC, SOCIAL, AND CULTURAL RIGHTS: FACT SHEET No. 33, at 25, U.N. Sales No. E.08-44591 (2008).

89. Comm. on Econ., Soc. & Cultural Rights, Poverty and the International Covenant on Economic, Social, and Cultural Rights, ¶ 18, U.N. Doc. E/C.12/2001/10 (May 10, 2001).

legally binding obligations of the State party.”<sup>90</sup> The ICESCR minimum core obligation thus remains applicable even when the State’s fiscal resources are strained to the hilt by economic emergencies, precisely since this is the key *raison d’être* of the ICESCR.<sup>91</sup>

### III. COMPENSATION FOR NON-EXPROPRIATION BREACHES: LESS SCIENCE, MORE ART

In determining compensation for breaches of non-expropriation standards in investment treaties, it should be recalled that “valuation, although employing broad principles of economics, is as much an art as it is a science. Each approach may yield a different result and which approach offers the best or better framework is a determination made in the light of the facts of a case.”<sup>92</sup>

Although arbitral tribunals refer to the general law of international responsibility to determine compensation for breaches of non-expropriation standards in investment treaties, such as the FET standard, the valuation process has been inconsistent, especially when an economic emergency is at issue.

#### A. “Fair Market Value” as the Default Standard

Since the origin of the basis for compensation for breaches of non-expropriation standards is the law of state responsibility, which merely refers to “financially assessable damage” under Article 36 of the 2001 ASR,<sup>93</sup> it is reasonable to assume that the latter would not always require equivalence with “fair market value.” The first reported investment award, *Asian Agricultural Products Ltd. (AAPL) v. Sri Lanka*, involved an armed conflict that destroyed the physical assets of the joint venture company in which the investor held shareholdings.<sup>94</sup> In that case, the claimant investor argued that the attack on the property exceeded the requirements of military

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90. *Id.* ¶ 17.

91. Manisuli Ssenyonjo, *Economic, Social and Cultural Rights, in* INTERNATIONAL HUMAN RIGHTS LAW: SIX DECADES AFTER THE UDHR AND BEYOND 49, 78 (Mashood A. Baderin & Manisuli Ssenyonjo eds., 2010) (“Given the nature of the rights protected under the ICESCR, the existence of a general limitations clause in Article 4, and the fact that states are not required to do more than what the maximum available resources permit, derogations from the ICESCR in situations of conflict, war, emergency and natural disaster would appear to be unnecessary.”)

92. MARK KANTOR, VALUATION FOR ARBITRATION: COMPENSATION STANDARDS, VALUATION METHODS, AND EXPERT EVIDENCE 14 (2008) (citing *In re* Winstar Communications Inc., 348 B.R. 234, 274 (Bankr. D. Del. 2005)).

93. 2001 ASR, *supra* note 1, art. 36.

94. *Asian Agric. Prods. Ltd. v. Sri Lanka*, ICSID Case No. ARB/87/3, Final Award on Merits and Damages, ¶ 3 (June 21, 1990).

necessity, while Sri Lanka argued that the investor knowingly assumed the risk by investing in an area already endangered by the presence of a separatist movement.<sup>95</sup> The *AAPL* tribunal held that Sri Lanka breached the treaty standard requiring “full protection and security” of investment by failing to exercise due diligence to communicate with the staff on the ground to minimize the risk of destruction.<sup>96</sup> The *AAPL* tribunal limited the compensation award to the actual value of the claimant investor’s shareholding in the joint venture company, noting that lost profits or future earnings (*lucrum cessans*) were not appropriate and should not be awarded since the case did not involve unlawful expropriation claims or liability for the unilateral termination of a State contract.<sup>97</sup>

In contrast, the reported arbitral awards involving the 2001-2002 Argentine financial crisis demonstrate a trend favoring the “fair market value” standard as the standard of compensation for reparations owed by Argentina to investors for the breach of non-expropriation standards (e.g., the FET standard, full protection and security standard, and national treatment). The awards in *El Paso*, *LG&E*, *Impregilo*, *Sempra*, *Azurix*, *Enron*, *CMS*, *BG Group*, *Suez*, and *Total* determined compensation for breaches of non-expropriation standards according to the “fair market value” standard of compensation defined in the provision on expropriation in the investment treaty.<sup>98</sup> The award in *Compañía de Aguas del Aconquija SA and Vivendi Universal SA* effectively applied the “fair market value” standard as a method of compensation for expropriation as well as breaches of non-expropriation standards.<sup>99</sup>

The reference to “fair market value” as the default standard arises mainly from the broad scope of arbitrator discretion over the constituent elements of “compensation” under the general law of reparations in the 2001 ASR. In the 2011 award in *El Paso Energy*

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95. *Id.* ¶¶ 28, 32.

96. *Id.* ¶ 85(B).

97. *Id.* ¶¶ 102–06.

98. *See, e.g.*, *El Paso Energy Int’l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award, ¶ 752 (Oct. 27, 2011); *Impregilo SpA v. Argentine Republic*, ICSID Case No. ARB/07/17, Final Award, ¶¶ 378, 381 (June 21, 2011); *Sempra Energy Int’l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award, ¶¶ 402–04 (Sept. 28, 2010); *Azurix Corp. v. Argentine Republic*, ICSID Case No. ARB/01/12, Award, ¶¶ 424, 442 (June 23, 2006); *Enron Corp. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, ¶ 453 (May 22, 2007); *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶ 410 (Apr. 25, 2005); *Nat’l Grid PLC v. Republic of Argentina*, UNCITRAL, Award, ¶¶ 263, 275 (Nov. 3, 2008); *BG Grp. PLC v. Republic of Argentina*, UNCITRAL, Final Award, ¶ 422 (Dec. 24, 2007).

99. *Compañía de Aguas del Aconquija SA v. Argentina*, ICSID Case No. ARB/97/3, Award, ¶¶ 8.2.8–8.2.11 (Aug. 20, 2007).

*International Company v. Argentina*,<sup>100</sup> the arbitral tribunal concurred with the tribunal's view in *SD Myers v. Canada*<sup>101</sup> that:

[T]he silence of the treaty indicates the intention of the drafters "to leave it open to tribunals to determine a measure of compensation appropriate to the specific circumstances of the case," adding that "whatever precise approach is taken, it should reflect the general principle of international law that compensation should undo the material harm inflicted by a breach of an international obligation."<sup>102</sup>

As a result, arbitral tribunals dealing with the 2001-2002 Argentine financial crisis awarded compensation invoking the definition of the "fair market value" in the International Glossary of Business Valuation Terms:

The price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.<sup>103</sup>

The above definition ideally assumes perfectly competitive markets and information between market players to arrive at the optimal arm's length price. The objectivity of this value is based on available market data and the exercise of professional judgment.<sup>104</sup> While the above definition has been widely adhered to by arbitral tribunals that dealt with the Argentine financial crisis,<sup>105</sup> the awards themselves demonstrate uneven constructions of elements that constitute "fair market value."<sup>106</sup> This broad "fair market value" standard is not synonymous with the prescribed definition of compensation under Article 36 of the 2001 ASR, which only refers to "financially assessable damage, including loss of profits

100. *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶¶ 698-742.

101. *S.D. Myers Inc. v. Canada*, UNCITRAL (NAFTA), First Partial Award, ¶¶ 309, 315 (Nov. 13, 2000).

102. *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶ 701.

103. AM. SOC'Y OF APPRAISERS, ASA BUSINESS VALUATION STANDARDS 27 (2009).

104. SABAH, *supra* note 2, at 103-04.

105. *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶ 402 (Apr. 25, 2005); *Nat'l Grid PLC v. Republic of Argentina*, UNCITRAL, Award, ¶ 263 n.99 (Nov. 3, 2008); *Sempra Energy Int'l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award, ¶ 405 n.160 (Sept. 28, 2007); *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶ 702 n.678; *Azurix Corp. v. Argentine Republic*, ICSID Case No. ARB/01/12, Award, ¶ 424 n.354 (June 23, 2006).

106. *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶ 422, 428, 430-31; *Nat'l Grid PLC*, UNCITRAL, ¶ 275; *Sempra Energy Int'l*, ICSID Case No. ARB/02/16, ¶¶ 411-12, 415; *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶ 712; *Azurix Corp.*, ICSID Case No. ARB/01/12, ¶¶ 425-33.



insofar as it is established.”<sup>107</sup> The ILC views this type of compensation as intended solely to “address the actual losses incurred as a result of the internationally wrongful act . . . . It is not concerned to punish the responsible State, nor does compensation have an expressive or exemplary character.”<sup>108</sup> The arbitral awards and international decisions surveyed by the ILC likewise did not advocate an all-encompassing “fair market value” standard to determine compensation.<sup>109</sup> The International Tribunal on the Law of the Sea in *M/V Saiga (No. 2)*, for example, excluded certain items from compensation, such as expenses incurred due to compliance with procedures “*in the exercise of the normal functions* of a flag State.”<sup>110</sup>

### B. Valuation Methods and Components of “Fair Market Value”

Using the broad definition of “fair market value” as the default standard of compensation thus admits some inherent uncertainty as to the tribunal’s choice of a valuation method and the components that it would accept for estimating “fair market value.” The arbitral awards that dealt with the asr-2002 Argentine crisis reflect the uncertain methodologies adopted by the tribunals.<sup>111</sup> While the *Sempra* tribunal initially clarified that compensation was unnecessary if the host State and claimant investor could agree on other modes of redress,<sup>112</sup> it ultimately imposed the fair market value standard<sup>113</sup> (the standard of compensation traditionally used for non-expropriation breaches of the BIT) as the level of compensation presumably required by the BIT for direct or indirect expropriations.<sup>114</sup> The *Sempra* tribunal simply determined the level of compensation from the difference between the value of the firm without the Argentine governmental measures, and the value of the firm after the imposition of such measures, thereafter adding

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107. 2001 ASR, *supra* note 1, art. 36.

108. *Id.* at 245, art. 36 cmt. 4.

109. *See id.* art. 36.

110. *Id.* at 249, art. 36 cmt. 10 (emphasis added).

111. *See generally* Siemens AG v. Argentine Republic, ICSID Case No. ARB/02/8, Award and Separate Opinion (Feb. 6, 2007) (illustrating one case did not even distinguish between compensation owed for expropriation and compensation owed for breach of non-expropriation standards such as the fair and equitable treatment standard). Arbitrator Professor Domingo Bello Janeiro observed in his Separate Opinion that the tribunal should have appointed an independent expert to quantify the amount of damages to be awarded due to the complexity of the valuation and financial issues. *See id.*

112. *See Sempra Energy Int’l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award, ¶ 400 (Sept. 28, 2007).

113. *Id.* ¶ 404.

114. *Id.* ¶ 403.

historical damages to the resulting differential.<sup>115</sup> The 2007 *Enron* tribunal followed suit and also adopted this valuation method,<sup>116</sup> rejecting Argentina's argument that the claimant had received historically higher returns on its investment, as "[n]either historic nor estimated returns have been retained as a valid ground to oppose compensation under international law."<sup>117</sup> Despite its disinclination to import the "fair market value" standard, the 2007 *BG Group* tribunal ultimately held that compensation under the "fair market value" measure was an established practice in the assessment of damages under customary international law.<sup>118</sup>

At times, the "fair market value" of an investment has been deemed to include not only the principal capital contribution, but also all other costs presumably incurred to improve the productivity of an investment. The 2006 *Azurix* award included the investor's claim for "enhanced compensation," which, due to alleged cumulative breaches of other provisions of the BIT, extended well beyond the BIT provision defining compensation for expropriation.<sup>119</sup> Adopting the positions taken by the tribunal in *CMS v. Argentina*, and the NAFTA tribunals in the *S.D. Myers, Pope & Talbot*, and *Feldman* cases, the *Azurix* tribunal held that it was "appropriate" to use compensation based on the fair market value of the concession (investment), as there were cumulative breaches in this case that extended beyond creeping or indirect expropriation covered in a specific BIT provision.<sup>120</sup> The tribunal thereafter adopted "actual investment" (and not standard "book value" or the value at which an asset is pegged in a company balance sheet) as the valuation methodology.<sup>121</sup> Applying this method, the ultimate compensation awarded by the *Azurix* tribunal included the concession price, additional capital contributions for the concession, and actual litigation costs, but the tribunal rejected *Azurix's* claims for consequential damages, as well as its theory of restitution for "unjust enrichment."<sup>122</sup>

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115. *Id.* ¶¶ 412, 415.

116. *Enron Corp. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, ¶¶ 363, 388–89 (May 22, 2007).

117. *Id.* ¶ 370.

118. *BG Grp. PLC v. Republic of Argentina*, UNCITRAL, Final Award, ¶¶ 422–99 (Dec. 24, 2007).

119. *Azurix Corp. v. Argentine Republic*, ICSID Case No. ARB/01/12, Award, ¶ 409 (June 23, 2006).

120. *See id.* ¶¶ 419–24.

121. *Id.* ¶ 425.

122. *Id.* ¶¶ 428–32, 438.

Among the Argentine awards that dealt with the issue of reparations for breaches of the BIT beyond expropriation, the 2005 *CMS* award is demonstrably the most illuminating on the alternative resort to compensation as a form of reparations under general international law.<sup>123</sup> At the outset, the *CMS* tribunal reiterated that compensation “is only called for when the damage is not made good by restitution,” and that there are a plethora of methods for financially assessing damage, such as the “asset value” or “replacement cost” approach, the “comparable transaction” approach, the “option” approach, and the discounted cash flow (DCF) approach.<sup>124</sup> While declaring that “[r]estitution is by far the most reliable choice to make the injured party whole,” the *CMS* tribunal explicitly acknowledged that the Argentine “crisis cannot be ignored and it has specific consequences on the question of reparation.”<sup>125</sup> The tribunal did not explain what these consequences were, but rather went on to acknowledge that in the absence of a compensation provision for non-expropriation breaches of the BIT, “the cumulative nature of the breaches . . . is best dealt with by resorting to the standard of fair market value.”<sup>126</sup>

Notably, the arbitral tribunal in *National Grid PLC v. Argentina*<sup>127</sup> attempted to distinguish between the effect of governmental measures per se on the loss of investment value, and the independent impact of economic crisis on the value of an investment; however, the tribunal’s differentiation appears methodologically idiosyncratic.<sup>128</sup> While the *National Grid* tribunal applied the DCF method

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123. *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶¶ 399–469 (Apr. 25, 2005).

124. *Id.* ¶¶ 401, 403. The “replacement cost” approach looks at the cost of replacing the asset or investment, while the “comparable transaction” approach looks at how an investment or asset is priced in similarly situated transactions. *Id.* ¶ 403. The “option” approach looks at alternative uses of an asset, and the net price of the asset given the costs and benefits of such alternative uses. *Id.* The discounted cash flow (DCF) approach adjusts the acquisition cost of an asset or investment using a discount rate applied to the anticipated duration or maturity of an investment. *Id.* For a more detailed explanation of these methods, see KANTOR, *supra* note 92, at 7–26; Anthony Charlton, *Valuation Approaches and the Financial Crisis*, KLUWER ARBITRATION BLOG (Nov. 29, 2011), <http://kluwerarbitrationblog.com/blog/2011/11/29/valuation-approaches-and-the-financial-crisis-part-1—market-methods/>.

125. *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶ 406.

126. *Id.* ¶ 410.

127. *Nat’l Grid PLC v. Republic of Argentina*, UNCITRAL, Award, ¶ 274 (Nov. 3, 2008).

128. *Id.* (“The Tribunal turns now to the task of assessing the quantum of compensation for breach of Respondent’s obligations under the Treaty to provide ‘fair and equitable treatment’ as well as ‘protection and constant security.’ According to the compensatory principles set forth above, the compensation should reflect the loss of value of the Claim-

as the method to determine the loss of fair market value of an operating business entity, it recognized that the 2001-2002 Argentine economic crisis should be considered in ascertaining the appropriate discount rate.<sup>129</sup> The tribunal thereafter employed a comparable transactions analysis, to arrive at a proxy value of National Grid's shares at the time of the Argentine governmental measures as well as the economic crisis, in order to justify its choice of a much lower base value to be discounted (\$52.8 million) than that proposed by the Claimant's expert (\$320.8 million),<sup>130</sup> as well as a discount rate (12%) that was significantly higher than that used by the Claimant's expert.<sup>131</sup> The result was indeed a much lower compensation award (\$53.59 million) than the amount sought by the investor (\$112.4 million),<sup>132</sup> but the viability of this approach depended considerably upon the similarity or substitutability between the proxy transaction and the actual investment subject of the case. The tribunal acknowledged the imperfections of this approach but maintained that its method at least "appropriately reflects the impact of the [Argentine government's] Measures, while still recognizing that, because of the economic and social crisis, the situation of the Argentine economy was definitely not 'business as usual.'"<sup>133</sup>

In contrast, the 2011 *Impregilo* award did not refer to the fair market value standard at all but rather awarded compensation limited solely to the actual principal or capital contributions of the claimant investor.<sup>134</sup> The *Impregilo* tribunal agreed with the *Chorzów* standard and understood that "Impregilo should in principle be placed in the same position as it would have been, had Argentina's unfair and inequitable treatment of Impregilo's investment not occurred."<sup>135</sup> The tribunal was quick to acknowledge, however, that this *ex ante* restitution was in no way a precise or definitive process: "it would be unreasonable to require precise proof of the

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ant's shares in Transener as a result of the Measures and other actions taken by the government of the Argentine Republic. As indicated above, the Tribunal recognizes that the Measures were taken at a time of economic crisis and that it is part of the task of the Tribunal, in calculating the quantum of compensation, to assess the effect of such crisis, irrespective of the Measures, on the application of the Regulatory Framework.").

129. *Id.* ¶¶ 275, 282.

130. *Id.* ¶¶ 279, 287-88.

131. *Id.* ¶ 289.

132. *Id.* ¶¶ 265, 296.

133. *Id.* ¶ 290.

134. *Impregilo SpA v. Argentine Republic*, ICSID Case No. ARB/07/17, Final Award, ¶¶ 380-81 (June 21, 2011).

135. *Id.* ¶ 361.

extent of the damage sustained by Impregilo. Instead, reasonable probabilities and estimates have to suffice as a basis for claims for compensation.”<sup>136</sup> The *Impregilo* tribunal then conducted a fact-intensive analysis, reaching the conclusion that the failure of the concession (the investment subject of this case) was attributable in part to the claimant investor, as well as to the acts or failures of Argentina in implementing measures during its 2001-2002 economic crisis.<sup>137</sup> Due to the “shared responsibility for the failure of the concession,” the *Impregilo* tribunal deemed it “inappropriate to calculate damages on the basis of customary economic parameters such as a cost or asset based method or an income method. Instead, the damages to be paid by the Argentine Republic to compensate for unfair and inequitable treatment should be determined on the basis of a reasonable estimate of the loss that may have been caused to Impregilo.”<sup>138</sup> Compensation was awarded only according to the actual capital contribution of Impregilo, and not for any potential gains from the concession.<sup>139</sup>

Finally, it should be noted that the breadth of the “fair market value” standard has been recently criticized. The 2011 *El Paso v. Argentina* award shows a telling divide between the majority’s use of the broad “fair market value” standard, and the narrower definition preferred by dissenting arbitrator Brigitte Stern.<sup>140</sup> Stern’s dissent argued that the tribunal “should only take into account what a willing buyer and a willing seller could foresee at the time of the interference with the investor’s rights.”<sup>141</sup> Relying on the *Chorzów* standard,<sup>142</sup> the *El Paso* majority rejected this narrower view of compensation.<sup>143</sup> Instead, the *El Paso* majority used an Income-Based Approach in the form of the DCF method of valuation, an approach in line with the Expert’s Reports and the practice of other arbitral tribunals in cases involving Argentine emergency measures in *CMS*, *Enron*, and *Sempra*.<sup>144</sup>

As may be seen in the above approaches taken in different arbitrations arising from Argentina’s governmental measures during its

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136. *Id.* ¶ 371.

137. *See id.* ¶¶ 362–70.

138. *Id.* ¶¶ 376–78.

139. *Id.* ¶¶ 379–81.

140. *See El Paso Energy Int’l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award (Oct. 27, 2011).

141. *Id.* ¶¶ 702–03.

142. *Id.* ¶ 705.

143. *Id.* ¶¶ 705–12.

144. *Id.* ¶¶ 711–12.

2001-2002 financial crisis, regardless of the valuation method used, arbitral tribunals eventually refer to the “fair market value” standard to determine the quantum of compensation.<sup>145</sup> In reaching for the “fair market value” of an investment as the level of compensation, arbitral tribunals (with the exception of the *National Grid* tribunal) did not manifestly differentiate between price effects that were endogenously caused by the Argentine governmental measures and price effects that could have been exogenously caused by the systemic financial crisis as a whole.<sup>146</sup>

Under the *Chorzów* standard, the injured party is to be returned to its position had the injury not occurred.<sup>147</sup> By equating the broad “fair market value” standard with the expectancy interest underlying compensation in the law of international responsibility, arbitral tribunals ultimately ascertain the quantum of compensation under considerably elastic parameters. When the tribunals rejected Argentina’s unique version of the necessity defense (which sought the full inapplicability of the entire investment treaty in self-judged emergency situations), they did not take into account the possible independent and exogenous effect of the 2001-2002 financial crisis in determining ultimate value of investment loss or damage.<sup>148</sup> None of the tribunals also had the opportunity to consider the possible weight of good faith compliance with ICESCR minimum core obligations at the time of the 2001-2002 crisis, since Argentina tailored its defenses according to a sweeping necessity argument.<sup>149</sup> The result was that the damages assessed by several tribunals under the “but for the measures” method (e.g., by subtracting the “with measures” investment value from the “without measures” investment value), impliedly attributed damage to the investment entirely to Argentina’s governmen-

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145. See *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/8, Award, ¶ 402 (Apr. 25, 2005); *Nat'l Grid PLC v. Republic of Argentina*, UNCITRAL, Award, ¶ 263 n.99 (Nov. 3, 2008); *Sempra Energy Int'l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award, ¶ 405 (Sept. 28, 2007); *El Paso Energy Int'l Co.*, ICSID Case No. ARB/03/15, ¶ 702; *Azurix Corp. v. Argentine Republic*, ICSID Case No. ARB/01/12, Award, ¶ 424 (June 23, 2006).

146. See *Enron Corp. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, ¶¶ 363, 370, 388–89 (May 22, 2007); *Azurix Corp.*, ICSID Case No. ARB/01/12, ¶¶ 409, 419–24; *CMS Gas Transmission Co.*, ICSID Case No. ARB/01/8, ¶¶ 401, 403.

147. Andrea Saldarriaga & Mark Kantor, *Calculating Damages: Arbitrators, Counsel, and Experts Can Do Better than They Have in the Past*, in *INVESTING WITH CONFIDENCE: UNDERSTANDING POLITICAL RISK MANAGEMENT IN THE 21ST CENTURY* 196, 222 (Kevin W. Lu, Gero Verheyen & Srilal M. Perera eds., 2009).

148. DESIERTO, *supra* note 6, at 145–236.

149. See, e.g., *EDF Int'l S.A. v. Argentine Republic*, ICSID Case No. ARB/03/23, ¶¶ 1153, 1161, 1163 (June 11, 2012).

tal measures, without consideration for exogenous causes such as market volatility.<sup>150</sup> In such cases where a tribunal finds that the host State did not commit a direct or indirect expropriation, but only a breach of a non-expropriation standard such as the FET standard, it strains credulity that the very *same* treaty standard of compensation (“fair market value”) would be immediately transposed into situations that do not involve State-sanctioned property takings.<sup>151</sup> The 2001 ASR did not provide for an automatic equivalence between “fair market value” and compensation.<sup>152</sup>

C. *Mitigation of Compensation under the General International Law of Reparations*

Tribunals that have dealt with economic emergencies such as the 2001-2002 Argentine financial crisis have been silent on the issue of mitigation of compensation arising from investor conduct. Compensation under Article 36 of the 2001 ASR assesses damage from the perspective of the injured State, but also reaches valuation determinations with the intent of reaching an “equitable” outcome between the injuring and injured State.<sup>153</sup> The ILC acknowledges that the scope of reparations may be affected by the degree to which the party injured by a breach of an international obligation exercises prudence to mitigate damages occasioned by the injury:

A further element affecting the scope of reparation is the question of mitigation of damage. Even the wholly innocent victim of wrongful conduct is expected to act reasonably when confronted by the injury. Although often expressed in terms of a “duty to ‘mitigate’”, this is not a legal obligation which itself gives rise to responsibility. It is rather that a failure to mitigate by the injured party may preclude recovery to that extent.<sup>154</sup>

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150. See, e.g., *id.* ¶¶ 1182–85.

151. See WORLD BANK, GUIDELINES ON THE TREATMENT OF FOREIGN DIRECT INVESTMENT, at III(1)–(10), available at <http://italaw.com/documents/WorldBank.pdf>; Ligia Catherine Arias Barrera, *Lack of Definition of Compensation in International Investment Disputes for Non-Expropriation Claims: Is There an Appropriate Mechanism to Determine It?*, 10 REVISTA MERCATORIA 75, 113 (2011).

152. See 2001 ASR, *supra* note 1, art. 36.

153. *Id.* at 247–48, art. 36 cmt. 7 (“As to the appropriate heads of compensable damage and the principles of assessment to be applied in quantification, these will vary, depending upon the content of particular primary obligations, an evaluation of the respective [behavior] of the parties and, more generally, a concern to reach an equitable and acceptable outcome.”) (emphasis added).

154. *Id.* at 228–29, art. 31 cmt. 11.

Several investment arbitral tribunals have applied a similar concept of mitigation of losses.<sup>155</sup> The arbitral tribunal in *Middle East Cement v. Egypt* treated the duty to mitigate as a “general principle of law” that formed part of the applicable rules of international law to the dispute,<sup>156</sup> a position also accepted by the arbitral tribunal in *CME Czech Republic BV v. Czech Republic*.<sup>157</sup>

Applying the concept of mitigation to economic emergencies, it should be material for the host State to present evidence, not just to dispute the investors’ financial assessment of their losses, but also to establish its actual fiscal predicament in view of its continuing obligations to provide the “essential levels” of the ICESCR minimum core obligations. To the extent that compliance with the ICESCR minimum core obligations was duly disclosed to the investor at the time of the establishment of the investment in the form of specific assurances<sup>158</sup> or as a central part of its regulatory fabric,<sup>159</sup> and the host State acted in good faith to comply with such obligations,<sup>160</sup> investors can rightfully be presumed to have expected that the host State would and could not depart from these obligations during an economic emergency. On the basis of these expectations, arbitral tribunals should thus consider whether the investor acted to mitigate his losses in anticipation of the host State’s reasonable implementation of the ICESCR minimum core obligations during the economic emergency.

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155. SERGEY RIPINSKY & KEVIN WILLIAMS, DAMAGES IN INTERNATIONAL INVESTMENT LAW 322–25 (2008); IRMGARD MARBOE, CALCULATION OF COMPENSATION AND DAMAGES IN INTERNATIONAL INVESTMENT LAW 122–26 (2009).

156. *Middle E. Cement Shipping & Handling Co. S.A. v. Egypt*, ICSID Case No. ARB/99/6, Award, ¶ 167 (Apr. 12, 2002).

157. *CME Czech BV v. Czech Republic*, UNCITRAL, Partial Award, ¶ 482 (Sept. 13, 2001).

158. See *Glamis Gold Ltd. v. United States*, UNCITRAL, Award, ¶ 24 (June 8, 2009).

159. See *Anderson v. Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, ¶¶ 55–59 (May 19, 2010) (where the tribunal accepted that Costa Rica had established the centrality of its banking and administrative regulations as part of the regulatory fabric to which the investment was subject).

160. See *Saluka Investments BV (Neth.) v. Czech Republic* at ¶ 307 (Perm. Ct. Arb. 2006) (“A foreign investor protected by the Treaty may in any case properly expect that the Czech Republic implements its policies *bona fide* by conduct that is, as far as it affects the investors’ investment, reasonably justifiable by public policies and that such conduct does not manifestly violate the requirements of consistency, transparency, even-handedness and non-discrimination.”).



D. *Other Interpretations of “Compensation” under General International Law*

Other institutions, also dealing with emergencies and “compensation” under the law of international responsibility, have not resorted to the broad “fair market value” standard frequently used by tribunals that have dealt with the 2001-2002 Argentine financial crisis. As seen below, “financially assessable damage” as the measure of compensation under the general law of reparations need not be as expansive as the International Glossary of Business Terms’ definition of “fair market value.”

1. “Past Performance” Measure in the UN Compensation Commission

The UN Compensation Commission (UNCC) was established in 1991 by the UN Security Council to establish a procedure for payment of claims and compensation for losses and damage suffered from Iraq’s illegal invasion of Kuwait.<sup>161</sup> In its Decision, “Propositions and Conclusions on Compensation for Business Losses,” the UNCC held that “compensation may only be claimed for the loss suffered during the relevant period [of loss resulting from Iraqi invasion and occupation of Kuwait]. . . . . The method of valuation should therefore be one that focuses on past performance rather than on forecasts and projections into the future.”<sup>162</sup> The relevant Security Council resolutions establish the international responsibility of Iraq as expressly accepted by the Iraqi Government, and set up the UNCC to process claims of losses and damages arising from the Iraqi invasion of Kuwait.<sup>163</sup>

The UNCC method of valuation is relevant to the assessment of compensation for breaches of non-expropriation investment treaty standards (such as the FET standard), precisely because compensation paid in the UNCC claims was for actual losses or damages incurred in the context of an emergency resulting from interna-

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161. See S.C. Res. 661, U.N. Doc. S/RES/661 (Aug. 6, 1990); S.C. Res. 687, U.N. Doc. S/RES/687 (Apr. 3, 1991); S.C. Res. 692, U.N. Doc. S/RES/692 (May 20, 1991); S.C. Res. 705, U.N. Doc. S/RES/705 (Aug. 15, 1991); S.C. Res. 706, U.N. Doc. S/RES/706 (Aug. 15, 1991); S.C. Res. 778, U.N. Doc. S/RES/778 (Oct. 2, 1992); S.C. Res. 986, U.N. Doc. S/RES/986 (Apr. 14, 1995).

162. U.N. Compensation Commission, Decision Taken by the Governing Council of the United Nations Compensation Commission During the Resumed Fourth Session, at the 23rd Meeting, Held on 6th March 1992, ¶¶ 17, 19, U.N. Doc. S/AC.26/1992/9 (Mar. 6, 1992).

163. S.C. Res. 687, *supra* note 161; S.C. Res. 692, *supra* note 161; S.C. Res. 986, *supra* note 161; S.C. Res. 1483, U.N. Doc. S/RES/1483 (May 22, 2003).

tionally wrongful acts committed by a foreign State that were not in the nature of direct or indirect expropriatory takings.<sup>164</sup> The compensation paid by the UNCC was issued for damage or loss of property from a State's internationally wrongful acts, not necessarily in the nature of expropriation or regulatory takings.<sup>165</sup> While there is a substantial amount of international practice that equates compensation valuation with "fair market value," this standard is frequently derived from expropriation cases, not cases involving losses not attributable to a State's expropriatory acts.<sup>166</sup>

Notably, the ICJ has not yet adopted or imposed a broad "fair market value" standard to determine the quantum of compensation owed by States for damage caused by their internationally wrongful acts. In the 1949 *Corfu Channel case*, despite Albania's non-participation, the ICJ considered Albania to be in default and received evidence from the United Kingdom's technical experts.<sup>167</sup> The ICJ ultimately awarded compensation to the United Kingdom based on the actual replacement cost of damaged or destroyed British ships, and the actual cost of pensions, medical expenses, and grants made to victims or their dependents.<sup>168</sup> When confronted with the non-participation of the United States on the issue of Nicaragua's request for compensation in *Military and Paramilitary Activities in and against Nicaragua*, the ICJ held that it would "refrain from any unnecessary act which might prove an obstacle to a negotiated settlement."<sup>169</sup> The ICJ again referred parties to settlement in the 1997 *Gabèikovo-Nagymaros* case, holding that both Hungary and Slovakia were under obligations to pay to, and receive compensation from, the other, and due to the "intersecting wrongs by both Parties[,] . . . the issue of compensation could satisfactorily be resolved in the framework of an overall settlement."<sup>170</sup> The evidentiary process for determining the quantum of compensation is an open process that examines all relevant facts and cir-

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164. *El Paso Energy Int'l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award, ¶¶ 704–05 (Oct. 27, 2011).

165. *Id.*

166. JAMES S. CRAWFORD, *THE INTERNATIONAL LAW COMMISSION'S 2001 ARTICLES ON STATE RESPONSIBILITY* 225–27 (2002).

167. *Corfu Channel Case*, Judgment of December 15th, 1949, 1949 I.C.J. 244, 248–49 (Dec. 15).

168. *Id.* at 248–50.

169. *Military and Paramilitary Activities in and Against Nicaragua (Nicar. v. U.S.)*, 1986 I.C.J. 14, ¶¶ 283–85 (June 27).

170. *Gabèikovo-Nagymaros Project (Hung./Slovk.)*, 1997 I.C.J. 7, ¶¶ 152, 153 (Sept. 25).

cumstances, as stressed by the ICJ in the 1974 *Fisheries Jurisdiction* case:

In order to award compensation the Court can only act with reference to a concrete submission as to the existence and the amount of each head of damage. Such an award must be based on precise grounds and detailed evidence concerning those acts which have been committed, taking into account all relevant facts of each incident and their consequences in the circumstances of the case.<sup>171</sup>

The silence of the ICJ on the “fair market value” standard further militates against its use to determine the quantum of compensation, in the form of reparations for damages caused by a State’s internationally wrongful acts under the general law of international responsibility. As shown by the UNCC, “past performance” may also be a sufficient standard to approximate “financially assessable damage” within the ambit of compensation as defined in Article 36 of the 2001 ASR.<sup>172</sup>

2. The *Oscar Chinn Case*: Compensation as an “Act of Grace,”  
Rather than a Vested Right, When Losses are Incurred  
Solely due to Changes in General Economic  
Conditions

Compensation may also be offered by a State as an “act of grace”, rather than as a matter of vested right. In the 1934 *Oscar Chinn case*, the Permanent Court of International Justice (PCIJ) declined to characterize voluntary refunds by the Belgian Government as a form of compensation awarded through legal entitlement.<sup>173</sup> In this case, the PCIJ declared that the Belgian Government did not violate the provisions of the Convention of Saint-Germain-en-Laye (the Convention) when the Belgian Minister for the Colonies issued a 1931 communication to various transport companies (including Oscar Chinn’s transport company) ordering the temporary reduction of transport tariffs for certain traded goods in the Belgian Congo, due to the collapse of prices for such produce during the worldwide economic crisis of the Great Depression.<sup>174</sup> The communication also provided that the Belgian Colonial Administration would reimburse the transport companies for costs or losses

171. *Fisheries Jurisdiction (Ger. v. Ice.)*, 1974 I.C.J. 175, ¶ 76 (July 25).

172. See 2001 ASR, *supra* note 1, art. 36 cmt. 26 n.559; U.N. Compensation Comm’n Governing Council, Propositions and Conclusions on Compensation for Business Losses: Types of Damages and Their Valuation, ¶ 19, U.N. Doc. S/AC.26/1992/9 (Mar. 6, 1992).

173. *The Oscar Chinn Case (U.K. v. Belg.)*, 1934 P.C.I.J. (ser. A/B) No. 63, at 88 (Dec. 12).

174. *Id.* at 71, 85–86.

arising from the rate reductions when their statement of accounts reflected a deficit.<sup>175</sup> The Belgian Colonial Administration would thereafter recover the reimbursements when the global economic situation would permit the restoration of the transport tariffs to their original levels.<sup>176</sup> Under this arrangement, Union nationale des Transports fluviaux (Unatra), a transport company in which the Belgian Government held substantial shareholdings, received refunds for the transport tariff reductions imposed by Belgium pursuant to the 1931 communication.<sup>177</sup>

Oscar Chinn, a British national who also ran his own transport company in the Belgian Congo, argued that the 1931 communication reduced his business to ruin due to transport tariff reductions and refunds offered to his competitors and not to all transport operators, which made the costs of his own transport company too prohibitive against further operations.<sup>178</sup> Transport companies not included in the refund scheme in the 1931 communication also requested the Minister of the Belgian Colonies for compensation for the losses they incurred.<sup>179</sup> The Minister declined such requests, saying that governmental assistance in the form of compensation was limited to transport companies over whose rates the Belgian Government had a right of supervision.<sup>180</sup> In 1932, however, the Minister issued a notice, granting to all private transporters "as an advance" the refund of losses suffered as a result of transporting products whose downstream rates were reduced.<sup>181</sup>

The United Kingdom argued that Belgium's reduction of tariffs in favor of Unatra in return for temporary monetary compensation "made it impossible for the other fluvial transporters, including Chinn, to retain their customers," thus enabling Unatra to exercise a de facto monopoly incompatible with the obligation to maintain commercial freedom and equality under the Convention.<sup>182</sup> The United Kingdom also accused Belgium of engaging in discriminatory conduct contrary to the principle of equality of treatment under the Convention and of violating Chinn's vested rights by

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175. *Id.* at 73-74.

176. *Id.* at 74.

177. *Id.* at 70, 74.

178. *Id.* at 75.

179. *Id.*

180. *Id.* at 43.

181. *Id.* at 44.

182. *Id.* at 20.

making it commercially impossible for him to continue with his business.<sup>183</sup>

The PCIJ held that Belgium did not breach the guarantees of freedom of trade, equality, and non-discrimination under the Convention with the treatment afforded by the 1931 communication to transport companies whose rates were subject to the Belgian Government's supervision.<sup>184</sup> As a transport company under the particular supervision of the Belgian Government, Unatra already posed different terms of competition known to Chinn at the time he joined the river transport business.<sup>185</sup> The Court held that the competitive situation ensuing from State supervision over Unatra was a "possible effect of commercial competition" but did not breach the freedom of trade and navigation.<sup>186</sup> In view of the Great Depression, the Belgian Government adopted temporary measures through the 1931 communication to publicly-regulated companies such as Unatra.<sup>187</sup> These measures could not be deemed to breach freedom of trade and navigation. Neither did Belgium violate the principle of discrimination, since:

[T]he treatment accorded to Unatra was based on the special position of that Company, as a Company under the supervision of the Belgian Government. The special advantages and conditions resulting from the measures . . . were bound up with the position of Unatra as a Company under State supervision and not with its character as a Belgian Company. These measures, as decreed, would have been inapplicable to concerns not under government supervision, whether of Belgian or foreign nationality.<sup>188</sup>

Finally, the Court denied that Chinn had any vested right to compensation arising from the 1932 notice of the Belgian Minister to private transporters.<sup>189</sup> The Court noted that the State could not be liable for a business loss resulting from deteriorating general economic conditions:

No enterprise – least of all a commercial or transport enterprise, the success of which is dependent on the fluctuating level of prices and rates – can escape from the chances and hazards resulting from general economic conditions. Some industries may be able to make large profits during a period of general prosperity, or else by taking advantage of a treaty of commerce

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183. *See id.* at 24.

184. *See id.* at 21.

185. *Id.* at 26.

186. *Id.* at 24.

187. *See id.* at 25.

188. *Id.* at 26.

189. *Id.* at 27.

or of an alteration in customs duties; but they are also exposed to the danger of ruin or extinction if circumstances change. Where this is the case, no vested rights are violated by a State.<sup>190</sup>

The advances granted by the Belgian Government to private transporters in 1932 was "ascribed to the desire of every government to show consideration for different business interests, and to offer them some compensation, when possible. The action of the Government appears to have been rather in the nature of an act of grace."<sup>191</sup>

The *Oscar Chinn* case is a unique case involving losses to a private party that were attributed by the Court to the price effects of an economic crisis such as the Great Depression.<sup>192</sup> The Court did not find a sufficient nexus of causation between the business losses suffered by Chinn and the more favorable regulatory climate faced by his competitors such as Unatra, other than the reinforcement of pre-existing terms of competition between Unatra and all other transport companies.<sup>193</sup> The Court's discussion latched on to the failure of Chinn (or the United Kingdom) to show that the regulatory differentiation between State-supervised transport companies and private transport companies was a mode of discrimination prohibited by the Convention or applicable international laws.<sup>194</sup> Since the Court found that it was the general economic conditions of the Great Depression that caused Chinn's business losses and not any regulatory measure of Belgium, there was no international responsibility from which the duty to pay compensation would arise.<sup>195</sup> In the absence of competition laws expressly imposing a duty upon Belgium to act (e.g., such as to exercise its governmental powers to ensure the preservation, and prevent the exacerbation, of terms of competition faced by private transporters such as Chinn), Chinn's loss of capital and profits, arising exclusively from prevailing market conditions and the impact of the Great Depression on transport prices, could not be redressed by compensation under international law.

As this Article has shown, compensation under the general law of reparations for breaches of international law that are not

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190. *Id.*

191. *Id.*

192. *Id.* at 87-88; see MOHAMED BEDJAOU, *THE NEW WORLD ORDER AND THE SECURITY COUNCIL: TESTING THE LEGALITY OF ITS ACTS* 497 (1994) (noting remarks of Professor Andre Gros that dissenting Judge Anzilotti considered the fact of the economic crisis at the time as a possible).

193. *Oscar Chinn*, 1934 P.C.I.J. (ser. A/B) at 87-88.

194. *Id.* at 85-88.

195. *Id.* at 84-89.

equivalent to expropriation need not always be assessed according to the broad “fair market value” standard. When investment tribunals use this standard to compensate breaches of non-expropriation treaty standards, they problematically assume a conceptual equivalence between the qualitative effects of an expropriation (and the specific intent of the States Parties in providing for “prompt, adequate, and effective” compensation in these cases), and all other breaches of provisions in the investment treaty. This method neglects the actual function of compensation under the general law of international responsibility, which is to reach for an “equitable outcome” for both the injured and injuring State.<sup>196</sup> As a matter of equity, it would not be unreasonable for the arbitral tribunal to adjust the quantum of compensation, in view of the host State’s simultaneous observance of the ICESCR minimum core obligation during an economic emergency. Several arbitral tribunals have relied on “equitable considerations”<sup>197</sup> to adjust the quantum of compensation taking into account the peculiarity of fact-patterns on a case-by-case basis:

Because of difficulties involved in the precise assessment of damages, subjective elements present in many assessment methodologies and the need for approximations, tribunals are almost inevitably, although to varying degrees, guided by equitable considerations . . . . The notion of equity is inherently subjective . . . much depends on the personal and collective views and beliefs of the members of the arbitral tribunal and their reading of the facts of the case. Generally, however, in the context of an investment dispute, equitable considerations can well serve as a basis for finding a just balance between private interests of the foreign investor and public interests of the respondent State.<sup>198</sup>

Equitable considerations are suited to situations where adjudication inimitably involves some discretionary ambiguity.<sup>199</sup> Arbitral tribunals seeking to apply compensation under Article 36 of the 2001 ASR to non-expropriation breaches of a BIT should acknowledge that this exercise is largely discretionary. However, most of the investment tribunals (save for *National Grid*) that held Argen-

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196. See 2001 ASR, *supra* note 1, at 247–48; Diane A. Desierto, *Calibrating Human Rights and Investment in Economic Emergencies: Prospects of Treaty and Valuation Defenses*, 9 MANCHESTER J. INT’L ECON. L. at 29 (forthcoming Sept. 2012) [hereinafter Desierto, *Calibrating Human Rights*].

197. See Desierto, *Calibrating Human Rights*, *supra* note 196, at 30 n.109 (listing six arbitral awards relying on principles of equity).

198. See RIPINSKY & WILLIAMS, *supra* note 155, at 124–26.

199. See Mark Weston Janis, *The Ambiguity of Equity in International Law*, 9 BROOKLYN J. INT’L L. 7, 25–26 (1983) (restating Lauterpacht’s acceptance of the use of equity in discretionary situations).

tina liable for breach of the FET standard tended to impose the “fair market value” standard as the standard of compensation, without making equitable adjustments on account of possible exogenous effects of overall market crises on the deteriorating value of an investment.<sup>200</sup>

As seen in the practices of the UNCC, valuation could be limited solely to a business’ “past performance” and not necessarily “lost profits” or expected earnings, when emergencies of a scale such as the Iraqi invasion of Kuwait could also have systemic ripple effects, environmental consequences, and other exogenous hazards that make it difficult to ascertain the future projections of profitability of a business.<sup>201</sup> The *Oscar Chinn* case is the extreme example of a situation where the Court attributed one transport owner’s business loss to exogenously-determined causes, such as the worldwide Great Depression’s effects on transport prices.<sup>202</sup> It might well have been that the volume of transactions of Chinn’s business was too insignificant relative to the market dominance of Unatra in the overall transport market of the Belgian Congo, thus making his business more price-sensitive to economic downturns such as the Great Depression. Had there been competition laws in place already binding Belgium to intervene to protect smaller firms such as Chinn’s from monopolistic behavior during economic emergencies, Chinn’s transport business would probably not have been as price-sensitive to exogenously-determined shocks such as the Great Depression.

Government policies taken during an economic emergency clearly will have an impact on the ultimate price or value of an investment or business as a going concern. As will be seen below, when a host State seeks to implement government policies that ensure continued observance of the ICESCR minimum core obligations in a time of economic emergency or financial crisis but collaterally injures investors by altering the expected regulatory environment, there is a need to reassess the “financially assessable damage” that should be compensable.<sup>203</sup> For example, the minimum core obligations on the right to water, as discussed by the

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200. See *supra* note 98 (citing, *inter alia*, LG&E Energy Corp. v. Argentine Republic, ICSID Case No. ARB/02/1, Decision on Liability, ¶ 227 (Oct. 3, 2006); Sempra Energy Int’l v. Argentine Republic, ICSID Case No. ARB/02/16, Award, ¶ 486 (Sept. 28, 2007); Azurix Corp. v. Argentine Republic, ICSID Case No. ARB/01/12, Award, ¶ 442 (June 23, 2006)).

201. U.N. Compensation Comm’n Governing Council, *supra* note 172, ¶¶ 17, 19.

202. Oscar Chinn (U.K. v. Belg.), 1934 P.C.I.J. (ser. A/B) No. 63, at 86–89 (Dec. 12).

203. See *infra* Part IV.



Committee on Economic, Social, and Cultural Rights includes State obligations to “ensure access to the minimum essential amount of water that is sufficient and safe for personal and domestic uses to prevent disease” as well as to “ensure the right of access to water and water facilities and services on a non-discriminatory basis, especially for disadvantaged or marginalized groups.”<sup>204</sup> A State acting to fulfill these obligations in a manner that ultimately interferes with the expected returns on investment of an investor—well short of a direct or indirect expropriation (and thus only breaching a non-expropriation standard in an investment treaty)—should not be held to the same broad “fair market value” standard for valuing compensation.

#### IV. A READJUSTMENT PROPOSAL: RECASTING THE INVESTMENT BETA AND THE COUNTRY RISK PREMIUM IN THE DISCOUNT RATE

Part III showed that, apart from the rather unrealistic definition of the broad “fair market value” standard under perfectly competitive market conditions, the same standard cannot be easily or legitimately equated to compensation as designed under the general international law of reparations in Article 36 of the 2001 ASR.<sup>205</sup> For such “compensation” for breaches of non-expropriation standards (such as the FET standard) to approximate the function of compensation under Article 36 of the 2001 ASR, the quantum of compensation must reflect a consideration of the behavior of both the injured party as well as the injuring party, in order to be justly regarded as an “equitable outcome.” This Part proposes to follow this principle in the assessment of the discount rate applied to an investment, by taking into consideration the host State’s obligations to continue observing the ICESCR minimum core obligations during economic emergencies.

##### A. *Unpacking the Components of the Discount Rate*

To recall, the discount rate is the “expected total rate of return [that] the investor requires to commit funds to the particular investment. It is market-driven in that it represents the expected rates of return available in the market on other investments that are comparable in terms of risk.”<sup>206</sup> The discount rate is applied under a DCF valuation method, which “calculate[es] the com-

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204. General Comment 15, *supra* note 73, ¶ 37(a), (b).

205. *See supra* Part III.

206. KANTOR, *supra* note 92, at 140.

pany's anticipated future stream of net cash flow over a specific future period of time, and then discounting that gross amount back to a present-value lump sum."<sup>207</sup> The higher the discount rate that is used, the lower the ultimate present-value lump sum of an investment, and vice versa. It is thus unsurprising that the discount rate (which was frequently used in the valuation methodologies in the arbitral awards that dealt with the 2001-2002 Argentine financial crisis) is one of the most heatedly contested issues in international investment arbitration, with claimant investors seeking lower discount rates (thus higher present values of their investment) and respondent States seeking higher discount rates (lower present values of investment to be compensated).<sup>208</sup>

The Capital Asset Pricing Model pioneered by Nobel Laureate William Sharpe presents the standard formula to determine the discount rate<sup>209</sup>:

$$\bar{r}_a = r_f + \beta_a(\bar{r}_m - r_f)$$

where:

$r_f$  = Risk free rate

$\beta_a$  = Beta of the security

$\bar{r}_m$  = Expected market return

$(\bar{r}_m - r_f)$  = Equity market premium

The investment beta is intended to measure the "sensitivity (volatility) of the rate of return on an individual security (or a portfolio of securities) to general rates of return in the public stock markets."<sup>210</sup> The higher the investment beta, the more sensitive the value of the investment is to the price fluctuations of the overall market. An investment beta higher than 1.0 reflects greater uncertainty, causing the discount rate to increase, and ultimately decreases the present value of an investment.<sup>211</sup> The equity market premium, on the other hand, "measure[s] the additional return the investor will require before investing in a portfolio that contains such an investment, as compared with the risk-free investment."<sup>212</sup> Variables that determine the equity risk premium have

207. *Id.*

208. *See id.* at 141. On the selection of discount rates, see Vidya Rajarao, *Determining Damages in Cross-Border Disputes*, TRANSNAT'L DISPUTE MGMT., Nov. 2007, at 1, 5.

209. *See* WILLIAM F. SHARPE, INVESTORS AND MARKETS: PORTFOLIO CHOICES, ASSET PRICES, AND INVESTMENT ADVICE 96 (2006). Formula image taken from *The Capital Asset Pricing Model: An Overview*, INVESTOPEDIA (Nov. 24, 2010), <http://www.investopedia.com/articles/06/capm.asp#axzz1uIvuuDmr>.

210. KANTOR, *supra* note 92, at 164.

211. *Id.* at 165.

212. *Id.*

been identified to include: (1) investor risk aversion and consumption preferences, (2) the health and predictability of the overall economy, (3) information about firm earnings and cash flows, (4) illiquidity costs (or the costs of trading the asset), (5) catastrophic risk (e.g., “events that occur infrequently but can cause dramatic drops in wealth”), and (6) government policy, where uncertainty about government policy can translate into higher equity risk premiums.<sup>213</sup>

An investor seeking to invest in a host State that is a party to the ICESCR should expect that State to continue fulfilling its minimum core obligations during economic emergencies or financial crises. As established above, these minimum core obligations have to be determined dynamically over time, with particular regard to the resource constraints of the State, the needs of its vulnerable populations, and the Committee guidelines in the General Comments for identifying what subsistence levels are sufficient at a given point in time under a specific State Party context.<sup>214</sup> The precise shape or contour of the government policies taken to observe the ICESCR minimum core obligations during an economic crisis can vary over time. The result is that more uncertainty as to government policy should be considered when the prospective host State for an investment is also a party to the ICESCR. The increased uncertainty will be reflected through upward estimations of both the investment beta (the sensitivity of the investment to the overall fluctuations of the market) and the equity risk premium (the additional return sought by the investor to invest in the asset, business, or project, rather than simply purchasing a risk-free security such as United States Treasury Bills).<sup>215</sup>

*B. Adjusting the Investment Beta and the Equity Risk Premium for Increased Uncertainty from ICESCR-Sensitive Government Policies*

The investment beta is usually estimated using Ordinary Least Squares regression, typified by a covariance function reflecting market risk and investment-specific risk.<sup>216</sup> Investment betas change over time, and may not always be stable predictors of mar-

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213. See Aswath Damodaran, *Equity Risk Premiums (ERP): Determinants, Estimation and Implications – The 2012 Edition 6–13* (Mar. 14, 2012) (unpublished manuscript), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2027211](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2027211).

214. See *supra* Part II.

215. See AVINASH K. DIXIT & ROBERT S. PINDYCK, *INVESTMENT UNDER UNCERTAINTY* 175–212 (1994).

216. D. Bradfield, *Investment Basics XLVI. On Estimating the Beta Coefficient*, 57 *INVESTMENT ANALYSTS J.* 47, 47 (2003).

ket risk vis-à-vis investment-specific risk.<sup>217</sup> The investment beta is determined by two sets of parameters: “1) the degree of uncertainty attached to various categories of economic events (the proportional contributions of the events to market variance), and 2) the response of the security returns to these events (relative response coefficients).”<sup>218</sup> Where governmental policies are expected to be taken to fulfill ICESCR minimum core obligations during a given economic emergency, the investment beta must reflect the increased uncertainty arising from the State’s obligation to fulfill such ICESCR minimum core obligations.

Government policies to maintain observance of the ICESCR minimum core obligations during economic emergencies can be expected to have some distributional consequences, such as: realigning fiscal priorities to guarantee subsistence levels of social and economic goods for vulnerable civilian populations, altering competition regulations or regulatory frameworks to better enable access of vulnerable civilian populations to key social and economic goods (e.g., water and other utilities), or providing incentives and subsidies to other market players to produce essential social and economic goods (such as medicine) at prices lower than arm’s length market prices. These changes of government policy are difficult to forecast until the actual economic emergency has occurred and the State duty to fulfill the ICESCR minimum core obligations is defined in relation to the effect of such emergency on the enjoyment of subsistence levels of ICESCR rights by the State’s citizens. The data used to approximate the market rate of return, for example, might also need adjustment in view of potential market segmentations (e.g., a government policy may introduce price discriminations in favor of historically vulnerable economic groups such as the elderly, children, and women, lower income groups or the unemployed, larger households in depressed areas that require more welfare assistance during economic crises, etc.). The frequency of price-distorting government intervention for social protection during economic crises can also be scrutinized as part of the historical data for estimating market returns and overall volatility. Finally, country-specific risk can additionally be taken into account when resource constraints, geographic endow-

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217. See Chris Tofallis, *Investment Volatility: A Critique of Standard Beta Estimation and a Simple Way Forward*, 187 EUR. J. OPERATIONAL RES. 1358, 1360–61 (2008) (discussing a relatively recent critique against using the investment beta to split up the notion of total risk into “market risk” and “investment-specific risk”).

218. BARR ROSENBERG & JAMES GUY, *Prediction of Beta from Investment Fundamentals: Part One, Prediction Criteria*, 32 FIN. ANALYSTS J. 60, 64 (1976).

ments, demographic characteristics, and other exogenous factors outside the control of a State can end up magnifying the subsistence levels actually required to meet the ICESCR minimum core obligations.<sup>219</sup> The ultimate effect of the increased uncertainty generated from less predictable government policies of a State party to the ICESCR should be an upward adjustment of the investment beta.

Similar reasoning regarding increased uncertainty from government policies can be applied to the equity risk premium. A 2011 study by Lubos Pastor and Pietro Veronesi from the University of Chicago found that apart from economic shocks and capital impact shocks, political shocks also contribute significantly to the risk premium, “despite being unrelated to the economic fundamentals Investors demand compensation for uncertainty about the outcomes of purely political events, such as debates and negotiations. Those events matter to investors because they affect the investors’ beliefs about which policy the government might adopt in the future.”<sup>220</sup> Political uncertainty arising from changes in government policies is expected to increase the equity risk premium as well as volatilities and correlations of stock returns.<sup>221</sup> During an economic emergency in which a State party to the ICESCR is expected to continue to observe minimum core obligations, the governmental policy changes necessitated in these circumstances should thus be foreseen to contribute to increased uncertainty, and ultimately, a higher equity risk premium.

As this Part has shown, upward adjustments in the investment beta and the equity risk premium result in higher discount rates, thus lowering present values of compensable investment.<sup>222</sup> This is more aligned with the “equitable outcome” envisaged for compensation under the general law of reparations, which ought to apply to the method of deriving compensation for breaches of non-expropriation standards of investment treaties. When a host State is able to show that it acted in good faith to observe its ICESCR obligations during an economic emergency or financial crisis and

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219. See generally Turan G. Bali & Nusret Cakici, World Market Risk, Country-Specific Risk and Expected Returns in International Stock Markets (Oct. 14, 2009) (unpublished manuscript), available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1489159](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1489159).

220. Political shocks “arise due to learning about the political costs associated with the potential new policies of a government.” Lubos Pastor & Pietro Veronesi, *Political Uncertainty and Risk Premia* 1, 2 (Sept. 7, 2001) (unpublished manuscript), available at <http://www.bus.wisc.edu/finance/workshops/documents/SSRN-id1932420.pdf>.

221. See *id.* at 24–25.

222. See *supra* Part IV.A.

only collaterally injured the investment, the actual level of compensable damage attributed to the host State for the investor's loss should reflect this distinction.

#### V. CONCLUSION: RESTORING PROPORTIONAL COMPENSATION IN INTERNATIONAL INVESTMENT LAW

Proportionality in international investment law is frequently sought in the interpretation of substantive standards of investment protection,<sup>223</sup> but proportionality also has a significant role to play in the more pragmatic issue of valuing compensation owed by a host State. Proportionality nuances are never more urgent than in the process of valuing compensation for losses incurred during times of economic emergencies. The market price of an investment is a function of both endogenous variables (such as firm-specific characteristics and the firm's dominance of the market relative to its overall size) as well as exogenous variables (such as systemic risk, adaptive regulatory changes, and external competition). In an economic emergency or financial crisis, the influence of exogenous variables on the market price of an investment will indeed be significant. At times, however, such adverse impacts on investment price and rate of return could be explained by good faith compliance by a State with other international obligations that incidentally distort the investment price and rate of return. A State Party to the ICESCR would (and should) continue to observe minimum core obligations towards its citizens during economic emergencies, even if the form of its observance would call for uncertain regulatory changes. When a State Party finds itself breaching its investment treaty's non-expropriation standards (such as the notoriously ambiguous FET standard), due to its good faith observance of the ICESCR, it should not be penalized by an arbitral tribunal that automatically transposes the Hull formula of

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223. See Xiuli Han, *The Application of the Principle of Proportionality in Tecmed v. Mexico*, 6 CHINESE J. INT'L L. 635, 637 (2007) ("In EU law, the principle of proportionality is becoming a constitutional principle of Europe. The principle of proportionality also exists in international law and is spreading to various branches of it."); Alec Stone Sweet, *Investor-State Arbitration: Proportionality's New Frontier*, 4 L. & ETHICS HUM. RTS. 47, 61–62 (2010) ("[An] indicator of judicialization—or, the gradual entrenchment of investment arbitration as a stable system of governance in the field of foreign direct investment—is the deployment, by arbitrators, of modes of reasoning and doctrinal frameworks developed by courts. Most dramatically, tribunals are in the process of embracing balancing and proportionality."); Benedict Kingsbury & Stephan W. Schill, *Public Law Concepts to Balance Investors' Rights with State Regulatory Actions in the Public Interest – The Concept of Proportionality*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 75, 79–80 (Stephan W. Schill ed., 2010).

“prompt, adequate, and effective” compensation for direct or indirect expropriations as an overly expansive proxy of “financially assessable damage” for compensation under the general international law of reparations. As this Article has shown, there are ways to equitably adjust the compensation valuation process in view of a host State’s good faith fulfillment of its minimum core obligations under the ICESCR.

A recently observed trend in awards in the ICSID shows that some tribunals are starting to issue more narrow compensation awards in order to protect “reliance interests,”<sup>224</sup> or economic harms suffered by a party who depends on a party’s *foreseeable* compliance with its obligation.<sup>225</sup> Rather than reaching for expansive “expectancy interest” protection, which would attempt to restore a party as close as possible to the situation before contract breach and which usually includes projecting lost profits, arbitral tribunals such as those in *Impregilo v. Argentina* and *National Grid PLC v. Argentina* demonstrate incipient attempts to account for the shared impact of economic crises on both the host State as well as the investor.<sup>226</sup> These attempts reflect the earlier sensibilities expressed in *CMS Gas* that the impact of a financial crisis should also have “some consequences on the question of reparation,” as well as the position taken by dissenting Arbitrator Brigitte Stern in *El Paso* that the value of an investment should be assessed at its most “foreseeable” price.<sup>227</sup>

While investment arbitration tribunals to date have not fully adopted scientifically consistent methods for valuing investment losses suffered as a result of governmental social protection measures *as well as* systemic economic crises, the analysis must begin somewhere. This Article offers one way to distinctively adjust the valuation model for breaches of non-expropriation treaty standards, when a host State obligated to observe the ICESCR minimum core obligations during the emergency must make the political decision to impose ICESCR-compliant governmental measures that injure investor interests. By adjusting the discount rate upwards to reflect the higher risk premium ensuing from the

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224. David Collins, An Economic Justification for Reliance Remedies at ICSID (Mar. 2008) (unpublished manuscript), available at [http://works.bepress.com/david\\_collins/1](http://works.bepress.com/david_collins/1).

225. See Robert Birmingham, *Notes on the Reliance Interest*, 60 WASH. L. REV. 217, 221 (1985).

226. *Impregilo SpA v. Argentine Republic*, ICSID Case No. ARB/07/17, Final Award, ¶¶ 49–86 (June 21, 2011).

227. *El Paso Energy Int’l Co. v. Argentine Republic*, ICSID Case No. ARB/03/15, Award, ¶¶ 678–79 (Oct. 27, 2011).

uncertainty of inevitable governmental policy changes to meet the ICESCR minimum core obligations during economic emergencies, arbitral tribunals can reach a more realistic assessment of the present value of an investment that also factors in the independent price impacts of the uncertainty of government behavior in response to market volatility during these emergencies.

A host State that establishes its good faith compliance with the ICESCR minimum core obligations during an economic emergency, and who does not invoke the ICESCR as a belated pretext to escape investor liability, should be given the benefit of equitably adjusted compensation. This would not only be consonant with the original intent of proportionality underlying the schema of reparations under the law of international responsibility,<sup>228</sup> but it would also confirm the fundamental centrality of the ICESCR to the regulatory fabric assumed by investors making the initial decision to invest in a State who is also a party to the ICESCR. In a time of economic crisis, no investor can expect a host State to disavow its ICESCR minimum core obligations to civilian populations. Thus, when the host State's political choice to deliberately breach a non-expropriation standard in the investment treaty arises from this sense of good faith compliance with the ICESCR—there being no other way to perform obligations in both treaty regimes compatibly within the terms of Article 30(4) of the Vienna Convention on the Law of Treaties<sup>229</sup>—the quantum of compensation should be assessed from the narrowest proportional extent to protect the “reliance interest” of the injured investor.

Precisely since the ILC emphasizes the intrinsic importance of the proportionality requirement to the law of reparations,<sup>230</sup> it would be contrary to the public function and just purposes of reparations to require “expectancy interest” compensation levels that beggar, punish, and extort from host States pursuing social protection measures under the ICESCR in good faith.

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228. 2001 ASR, *supra* note 1.

229. Vienna Convention on the Law of Treaties art. 30(4), May 23, 1969, 1155 U.N.T.S. 331.

230. 2001 ASR, *supra* note 1.