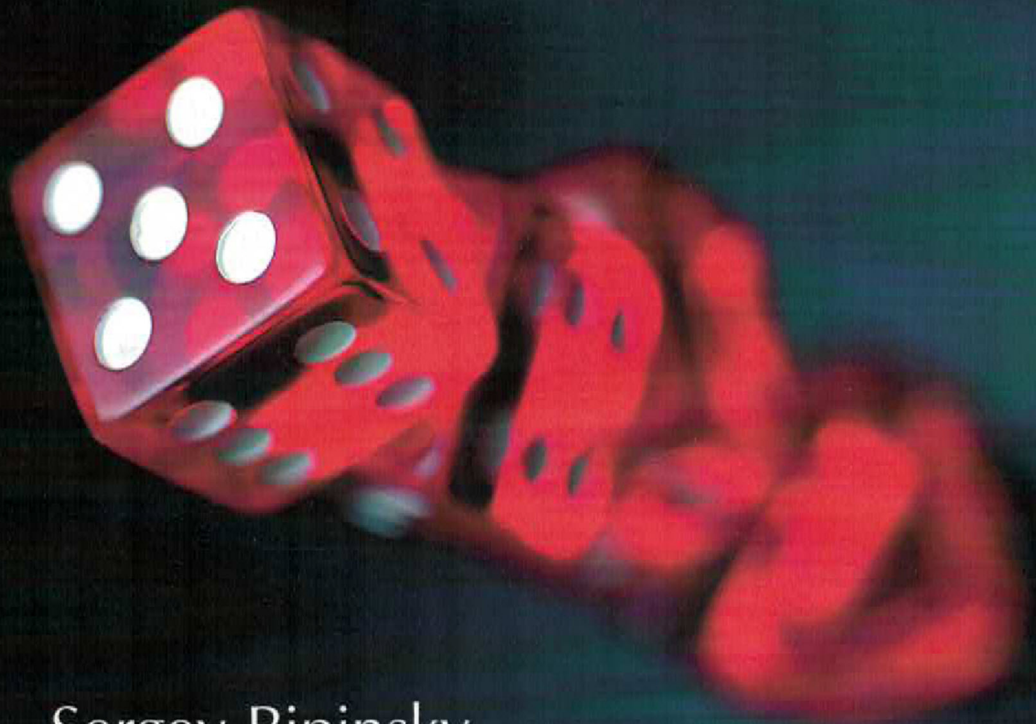
Damages in International Investment Law



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CA381-001

Some tribunals have denied compensation for lost profits where a business had *some* history of profitable operations but it was considered *insufficient*. For example, in *Tecmed v Mexico*, the Tribunal considered that two years of business operation was an insufficient historical period for deriving reliable cash flow projections for future 15 years.[109] Equally, in *SPP v Egypt*, the Tribunal noted the 'fragility of a calculation which depends on forecasting cash flows almost twenty years into the future on the basis of revenues generated over a period of little more than a year.'[110]

When deciding claims based on investments that have not had a long history of past earnings, the Iran–US Claims Tribunal has shown a similar disinclination to accept lost profits claims. For example, in *AIG v Iran*, the Tribunal noted that the 'company had been conducting its business only for little more than four and a half years, and such a short period must be deemed to provide an insufficient basis for projecting future profits', despite the Tribunal's finding that the expropriated company was a going concern at the time of the taking.[111] However, this case appears to be an outlier; normally, four and half years of successful business operations would provide sufficient evidence for the recovery of lost profits unless there are other reasons to disallow the claim, as was indeed the case in *AIG v Iran*.[112]

Past profitability in itself is not a sufficient condition

Although the past record of profitable operations provides a strong evidence of lost profits, other circumstances may nevertheless preclude compensation of lost profits. The practice of the Iran–US Claims Tribunal offers pertinent examples. The Tribunal rejected claims for lost profits where it believed that, due to the general effects of the Iranian Revolution (distinct from the conduct of the Iranian Government), the business in question was unlikely to continue to be profitable after the taking. Thus, in *Phelps Dodge v Iran*, the Tribunal stated that it:

> could not properly ignore the obvious and significant negative effects of the Iranian Revolution on SICAB's [an Iranian entity, in which the claimant held an equity interest] business prospects, at least in the short and medium term. ... SICAB's short-term prospects would certainly have been seen in November 1980 [date of the taking] as sufficiently uncertain to require a considerable discounting of the anticipated long-term profits.[113]

[109] *Tecmed v Mexico*, Award of 29 May 2003, para 186.
[110] *SPP v Egypt*, Award of 20 May 1992, para 187.
[111] *AIG v Iran*, Award of 19 December 1983, 4 Iran–US CTR 96, 108.
[112] See ibid 107–8.
[113] *Phelps Dodge v Iran*, Award of 19 March 1986, 10 Iran–US CTR 121, para 30.

For this reason, the Tribunal in *Phelps Dodge* limited its award to the amount of the claimant's initial investment. *Sola Tiles v Iran* presents another example. The case concerned an expropriation of an Iranian tile-importing company ('Simat') owned by the claimant. The Tribunal offered the following analysis:

> In 1978, ... the prospects for Simat's business were clearly favourable. Different elements had come into play by the time of the expropriation [late 1979], however. Simat's trade consisted largely of selling specialised luxury tiles, the market for which depended in large measure on the continued construction of luxury houses and apartments. ... [T]he market for items such as those imported by Simat would have suffered a severe diminution as a result of the sweeping social changes brought about by the Islamic Revolution.[114]

On this basis, the Tribunal refused to assign any value to the 'goodwill element' of Simat's business or to 'future lost profits'.[115] Without entering into the discussion of whether the distinction between 'goodwill' and 'lost profits' is a valid one,[116] the point is that the Tribunal considered that, in light of the prevailing circumstances and despite the previous successful performance record, future profits were uncertain.[117]

7.3.2(b) Start-up businesses and lost profits

The approach of rejecting lost profits in respect of enterprises which at the time of breach were not going concerns with a profitable record has been criticized as leaving the injured party less than whole and failing to achieve the goal of full compensation.[118] Consider a situation where an investor obtains a concession for the exploration and exploitation of oil: the investor will carry a risk of not discovering oil and thus losing the totality of its investment. At the same time, once the exploration campaign proves successful, the major risk of the investment is gone, and one should be able to predict with reasonable certainty the range of revenues that the concession will generate, even without a prior record of profitable operations. Perhaps with such situations in mind, it has been suggested that lost profits

[114] *Sola Tiles v Iran*, Award of 22 April 1987, 14 Iran–US CTR 223, paras 62–64.
[115] ibid para 64.
[116] On the notion of 'goodwill', see p 219, note 154.
[117] Note also that the Tribunal emphasized that Simat had had the 'briefest past record profitability, having shown a loss in 1976, its first year of trading, and a small profit the next year' (*Sola Tiles v Iran*, Award of 22 April 1987, 14 Iran–US CTR 223, para 64).
[118] J Gotanda, 'Recovering Lost Profits in International Disputes' (2004) 36 *Georgetown Journal of International Law* 61, 99–100. Gotanda argues that this approach is contrary to the rules and laws of many countries concerning remedies for breach of contract and incorrect from a policy standpoint.

CA381-003