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DOUBLE RECOVERY OR DOUBLE DIPPING: REPARATIONS TO PERSONS BELONGING TO THE SAME CORPORATE GROUP IN INVESTMENT ARBITRATION

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1. Introduction

Investment arbitration tribunals have constantly awarded reparations to shareholders based on violations of bilateral investment treaties (BITs) which include shares and other forms of participation as covered investments.[1] The first case brought by a shareholder, surprisingly also the first dispute brought under a BIT, was *AAPL v. Sri Lanka*[2]. In this case, the tribunal found that the amount of compensation due had to be calculated in a manner that adequately reflects the full value of the claimant's shareholding in Serendib.[3] The tribunal concluded that the treaty protected the shares not the assets of the company.

> The undisputed "investments" effected since 1985 by AAPL in Sri Lanka are in the form of acquiring shares in Serendib Company, which has been incorporated in Sri Lanka under the domestic Companies Law. Accordingly, the Treaty protection provides no direct coverage with

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[1] *Antoine Goetz and others v. Republic of Burundi* (ICSID Case No. ARB/95/3) Award embodying the parties' settlement agreement of February 10, 1999, [French original] 15 *ICSID Rev.—FILJ* 457 (2000); [hereinafter: *Goetz v. Burundi*] at § 89; *Emilio Agustín Maffezini v. Kingdom of Spain* (ICSID Case No. ARB/97/7) Decision on Objections to Jurisdiction of January 25, 2000, 5 *ICSID Rep.* 396 (2002); 124 *I.L.R.* 9 (2003) [hereinafter: *Maffezini* Jurisdiction] at § 68/70; *Compañía de Aguas del Aconquija SA and Vivendi Universal SA v Argentina,* Decision on jurisdiction, (ICSID Case No ARB/97/3) November 14, 2005, http://ita.law.uvic.ca/documents/AguasVivendijurisdictiondecision.pdf [hereinafter: *Vivendi* Jurisdiction], *Azurix Corp. v. Argentine Republic* (ICSID Case No. ARB/01/12) Decision on Jurisdiction of December 8, 2003, 43 *I.L.M.* 262 (2004); [hereinafter: *Azurix* Jurisdiction] at § 72-76; *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Argentine Republic* (ICSID Case No. ARB/02/1) Decision of the Arbitral Tribunal on Objections to Jurisdiction of April 30, 2004, [English original] 21 *ICSID Rev.—FILJ* 155 (2006); [hereinafter: *LG&E* Jurisdiction] at § 50 and in the Decision on Liability of October 03, 2006, 21 *ICSID Rev.—FILJ* 203 (2006); [hereinafter: *LG&E* Award] at § 177; *Asian Agricultural Products Limited v. Democratic Socialist Republic of Sri Lanka* (ICSID Case No. ARB/87/3). Award and Dissenting Opinion of June 27, 1990, 4 *ICSID Rep.* 246 (1997) [hereinafter: AAPL v. Sri Lanka]; *Camuzzi International S.A. v. Argentine Republic* (ICSID Case No. ARB/03/2) Decision on Objections to Jurisdiction, May 11, 2005, available at http://icsid.worldbank.org/ICSID/FrontServlet [hereinafter: *Camuzzi* Jurisdiction] at § 47; Gas *Natural SDG, S.A. v. Argentine Republic* (ICSID Case No. ARB/03/10) An electronic text of the Decision of the Tribunal on Preliminary Questions on Jurisdiction of June 17, 2005, is provided by International Law in Brief at http://www.asil.org/pdfs/GasNat.v.Argentina.pdf [hereinafter: *Gas Natural* Jurisdiction] at §35; to mention a few.

[2] *AAPL v. Sri Lanka,* supra footnote 1.

[3] Ibid.

> regard to Serendib's physical assets as such ("farm structures and equipment", "shrimp stock in ponds", cost of "training the technical staff", etc..), or to the intangible assets of Serendib if any ("good will", "future profitability", etc…). The scope of the international law protection granted to the foreign investor in the present case is limited to a single item: the value of his share-holding in the joint-venture entity (Serendib Company). [4]

Consequently, the tribunal considered the damage of the shareholder to be different from that of the company since the damaged assets in one case and the damaged assets on the other are different; e.g. the license, contracts or buildings in the case of the local company and the shares in the case of the shareholder. Still, whatever method is applied to determine the damage to the shares, the value of the shares will still depend to a certain extent on the value of the company which will depend, amongst other, on its assets.[5] Thus, measures directed at the company which detriments its assets, such as contracts or other non-current assets would affect the company's income producing potential probably provoking at the same time a decline in the share's price, and thus damage to the shareholder.

This *indirect* nature of the damage, this is, produced incidentally (considered in the causal nexus between the measures and the damage) by injurious measures directed at the local company, has not prevented investment arbitration tribunals to award damages to shareholders. This was the case in the in the overwhelming number of cases brought against Argentina after the 2002 economic crisis. In these cases tribunals found violations of BITs produced by regulatory action, in particular the Emergency Law No. 25.561[6] which affected the profitability of licenses and concessions of the locally established subsidiaries in the first place. [7]

In domestic law and general international law, the shareholder is not allowed to claim for indirect damages because he is already protected indirectly through the company's action.[8] However, this is the effect of BITs; to give an additional protection to the investor. [9] Given this additional character of the treaty protection of the shareholder, the exercise of the local company's rights does not affect the exercise of the shareholder treaty rights and vice versa. Hence, the shareholder would receive indirect protection through the exercise of the rights of the company and direct protection through investment arbitration. Consequently, a risk of double recovery of the foreign shareholder of a locally incorporated company arises.

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[4] Ibid § 94-95; see also Sornarajah, *The International Law on Foreign Investment*, 2nd ed. (2004), at 231.

[5] Bottini, 'Indirect claims under the ICSID convention', 29 *University of Pennsylvania Journal of International Law* (2007), at 638.

[6] Ley de Emergencia Pública y Reforma del Régimen Cambiario No. 25.561, Approved by decree No. 30/2002, 6 January 2002, Argentina, available at http://www.portaldeabogados.com.ar/noticias/020104.htm

[7] E.g., *Siemens* Award and Separate Opinion, February 6th, 2007, available at: *www.investmentclaims.com* [hereinafter: *Siemens* Award] § 308; *LG&E* Award § 123/139, supra footnote 1; *CMS* Award of May 12, 2005; 44 *I.L.M.* 1205 (2005) available at http://icsid.worldbank.org/ICSID/FrontServlet [hereinafter: *CMS* Award] § 164, 264/269; *Azurix* Award July 14, 2006, available at http://icsid.worldbank.org/ICSID/FrontServlet [hereinafter: *Azurix* Award] at § 374/377.

[8] E.g. when the company seizes a local court based on tort or contract law

[9] Cremades, "Contract and treaty claims and the choice of forum in foreign investment disputes," in *ICC Institute of World Business Law, 24th Annual meeting* (2004), 20.

In addition, according to investment arbitral awards[10] investments by intermediate companies do not deprive the shareholder of the ability to pursue claims against the violation of BITs.[11] Therefore, both a direct shareholder and an indirect shareholder could be protected for the damage indirectly produced to their shares by measures directed at the local company. This further exacerbates the risk of double recovery because the indirect shareholder would be protected multiple times: directly through the BIT and indirectly though the actions of the companies in which the shareholder hold shares; i.e. the company which is the direct investor (shareholder of the locally incorporated subsidiary) and the locally incorporated subsidiary.

These concerns are the subject of this article. The first part will analyze reparations to both the shareholders and the local company, and the second part will analyze reparations to shareholders belonging to the same corporate structure.

2. Reparations to shareholders and to the local company

The jeopardy of double recovery has been highlighted by numerous investment arbitration tribunals. In *Enron*[12] the tribunal declared that: "if these (CIESA and TGS) were separately compensated, is correct, and if such eventual compensations were to be accumulated they would result in a "double-dipping" or double recovery."[13]

In a subsequent passage, the tribunal offered no solution. Later, while dealing with the argument of Argentina that if tariffs were increased, then consumers would end up paying twice for the same interest, it left it to the government to negotiate and regulate.[14]

This was further highlighted in *Sempra* where the tribunal stated that "international law and decisions offer numerous mechanisms for preventing the possibility of double recovery", yet it refers to none and considered that double recovery "was not likely".[15] In *Suez*, the tribunal noted that "any eventual award in this case could be fashioned in such a way as to prevent double recovery"[16], but then referred to no such solutions.

It seems that tribunals have underestimated the problem. At the hypothetical level, one may distinguish two situations.

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[10] *Wena Hotels Limited v. Arab Republic of Egypt* (ICSID Case No. ARB/98/4) Decision on Jurisdiction of June 29, 1999, 41 *I.L.M.* 881 (2002); 6 *ICSID Rep.* 74 (2004) [hereinafter: *Wena Hotels* Jurisdiction] at § 45-46; *Sempra* Jurisdiction, supra footnote 1, § 90/91; *Camuzzi* Jurisdiction, supra footnote 1, § 63; *Gas Natural* Jurisdiction, supra footnote 1, § 33/35.

[11] Schreuer, " Shareholder's protection in international investment law," (2005), http://www.univie.ac.at/intlaw/pdf/csunpublpaper_2.pdf ; Dimsey, *The Resolution of International Investment Disputes: Challenges and Solutions* (2008), at 69; Rubins, 'The Notion of 'Investment' in International Investment Arbitration', in S.K. N. Horn (ed), *Arbitrating Foreign Investment Disputes Procedural and Substantive Legal Aspects* (2004) 283 - 324, at 313 et seq.

[12] *Enron Creditors Recovery Corporation (formerly Enron Corporation) and Ponderosa Assets, L.P. v. Argentine Republic* (ICSID Case No. ARB/01/3) Award, May 15, 2007, available at www.investmentclaims.com [hereinafter: *Enron* Award].

[13] Ibid § 167.

[14] "In respect of another argument concerning double recovery, it can only express the certainty that if the situation arises or its consequences would end up affecting the tariffs, able government negotiators or regulators would make sure that no such double recovery or effects occur." Ibid § 212.

[15] *Sempra Energy International v. Argentine Republic* (ICSID Case No. ARB/02/16) Award, September 28, 2007, available at www.investmentclaims.com [hereinafter: *Sempra* Award] 395.

[16] *Suez* supra footnote 1, § 51.

In the first situation, if reparations are awarded to the company before they are awarded to the investor, then the compensation received by the local company would positively affect the value of the share. Thus, in principle there would be no problem, since there would be no damage to the shareholder. However, the question arises whether, a shareholder can recover reparations which are in addition to those received by the local company, if an international tribunal considers that the local court has awarded the shareholder insufficient reparations.

In the second situation, if the shareholder is awarded reparations for the total of the damage to the value of its shares, this compensation would not be reflected in the assets of the company. As a matter of justice, the State may want to have a proportional reduction of the amount of reparations in the amount it has to pay to the local company because it has already paid. Could the reparations made to the shareholder be discounted from the reparations to be paid to the company? What about the local shareholders? And creditors?

These hot issues have been highlighted by the tribunal in the *GAMI* case[17]. GAMI claimed for damages against the expropriation of sugar mills belonging to GAM. GAM, the local company, had initiated local proceedings against Mexico and had obtained compensation for some of the expropriated mills. The arbitral tribunal stated:

> "A consequence of GAMI's independent right of action under NAFTA may be illustrated by a hypothetical example. The notional compensation of GAM by Mexico in an amount representing M$ 100 per share would not in principle disentitle GAMI from asking the NAFTA Tribunal for an additional amount representing and additional M$ 50 per share. But the theory gives rise to a number of practical difficulties. One might imagine a perfect world in which a national court of last recourse sits down with a NAFTA tribunal incapable of reviewable error to discharge their respective responsibilities. This could be done quite logically. The Mexican court could order payment to GAM based on an evaluation of the five expropriated mills. As a matter of mathematics that evaluation might represent M$ 100 per share of all shares of GAM. At the same time the NAFTA tribunal might find that a higher level of compensation was mandated and thus order a top-up to GAMI of M$ 50 per share"[18]

The tribunal then concluded that "this scenario is of course fantasy" since it lacked legal foundation and legal credibility.[19] On what reasonable ground could the payment to GAMI be reduced to account for the payment of GAM given that GAM had never paid dividends to its shareholders?[20] Further, "why should GAMI's recovery be debited on account of a payment to GAM which is perhaps utterly unlikely to find its way to the pockets of its shareholders?"[21] "The overwhelming implausibility of a simultaneous resolution of the problem by national and international jurisdictions impels consideration of the practically certain scenario unsynchronised resolution".[22]

Then explaining a situation where the shareholder was awarded damages before the Mexican courts, it said:

> "It is sufficient to consider the hypothesis that a NAFTA tribunal were to order payment to GAMI before the Mexican courts render their final decision. One might adapt the hypothetical example given in paragraph 116 above. GAMI would thus have received M$ 150 per share (there

[17] *GAMI,* supra footnote 1.
[18] Ibid § 116.
[19] Ibid § 117 /118.
[20] Ibid § 118.
[21] Ibid.
[22] Ibid § 119.

> would have been no prior offsetting Mexican recovery). What effect should the Mexican courts now give to the NAFTA award? How could GAM's recovery be reduced because of the payment to GAMI? GAM is the owner of the expropriated assets. It has never paid dividends. It would have been most unlikely to distribute revenues in the amount recovered by GAMI. At any rate such a decision would have required due deliberation of GAM's corporate organs. Creditors would come first. And other shareholders would have an equal right to the distribution. GAM would obviously say that it is the expropriated owner and that its compensatable *[sic]* loss under Mexican law could not be diminished by the amount paid to one of its shareholders"[23]

Finally, it stated that these statements "can quickly transport the analysis onto a fragile limb"[24] and continued to analyse the claim as an independent one[25]. GAMI was not awarded damages because none of the claims of GAMI violated NAFTA; however if the tribunal had found a violation and a damage it would have awarded damages independently.

Let us return to our first situation, that is, the company receiving compensation prior to the shareholder. Could the shareholder receive an additional relief? Yes, based on the treaty, which creates an independent system of protection[26]. Would this relief be "conditional" to the one received by the local company? No. The question is not to reduce the shareholders' reparation based on reparations received by the local company, but to determine the loss suffered in the value of the shares. Undoubtedly, reparations received by the local company will affect the value of the share but the shareholder would be receiving full compensation. Would this put local shareholders in a disadvantaged position? Of course. But there is nothing wrong with that, since the rights of the company, or of other shareholders or creditors, would not be affected. That is the idea of treaty investment arbitration to give *special* treatment and additional warranties to foreign investors as an investment promotion policy.

As to the second situation, that is, if the shareholder was awarded damages prior to the company, could the *quantum* of reparations of the company be reduced because the State has previously already paid the foreign shareholder? This would put at stake the basic principles of corporate law and stability of economic relations. If the *quantum* of reparations to be awarded to the local company were to be reduced in the amount paid to the shareholder, this would, first, affect the rights of the company (and indirectly the local shareholders) since the company would have its municipal right to compensation taken (a treaty right should be interpreted in a way that gives "more" rather than removing what the local subjects already had according to domestic law). Second, the rights of creditors of the company would be jeopardized since only the shareholders' creditors would have access to the compensation. Third, for what reason would the shareholder receive those benefits of the company? Could it be seen as an anticipation of capital, extraordinary dividends? This would require in any case a corporate decision. Fourth, treaty rights are additional and independent of domestic rights. For all these reasons, the State should pay twice. A different solution would produce a state of insecurity in economic relations apart from being less equitable to creditors and other shareholders.

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[23] Ibid § 120.
[24] Ibid § 121.
[25] Ibid § 133.
[26] Cremades, "Contract and treaty claims and the choice of forum in foreign investment disputes," 20.

Arguably, it would be different in a case where the local company is a mere instrument of the foreign shareholder. In such a case, both subjects would be considered a unity. Still, the practicability of this hypothesis is still too problematic. What about creditors of the local company? Could they also consider both entities as a single unit?

3. Reparations to different shareholders of the local company

In the situation of shareholders at the same level of ownership receiving reparations altogether, there would be no problem of double recovery since the reparations would be proportional to their shares. Conversely, if shareholders at different levels of ownership were to receive reparations the risk of double recovery emerges.

There are no instances where the question of damages between different shareholders of the same group at different levels of ownership has been considered. On the hypothetical plane, one may ask which shareholder is entitled to reparations? The direct or the indirect one? Judges Tanaka and Jessup in their separate opinions in the *Barcelona Traction* case proposed as a solution the first come, first served approach. [27] Arguably, even if the approach could seem at first sight, to be a good option, it is difficult to see how to coordinate the assessment of damages amongst different independent tribunals.

Moreover, there are no instances where compensation has been reduced in cases involving parent companies and subsidiaries. The problem stems from the fact that reparation would be awarded to two different legal entities based on different rights regarding different assets (the assets of the company and the shares of the shareholder).[28] Hence, can reparation be considered to have been awarded more than once in respect of the same injury? Is it the same injury? Does it result in unjust enrichment of the claimant? Is it the same claimant? Since the parties are different the stringent criteria of the piercing of the corporate veil shall be met. Due to these concerns, Thomas Wälde explains: "[o]n considerations of all aspects it seems correct to apply rather a standardised approach of "economic identity" and to presume, without detailed counter-proof, that the subsidiary's harm is economically equivalent to the harm suffered, and to be compensated, by the foreign owner pro rata commensurate with its share ownership.[29]

In any case this leads to the very basic question of why the indirect investor should be protected. Is it because he is the "real investor" or because all shareholders of the same group, or at least some of them, shall be protected? If it were because he is the real investor, then such a determination should be made carefully in order to avoid the existence of multiple claims of investors at competing levels. If the idea is to grant

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[27] *Barcelona Traction*, Judge Tanaka Separate Opinion at 130 et seq. See also Prof. Caflisch who considers it is an inadequate method as it was suggested by the I.C.J. in the Reparations Case. Caflisch, 'The Protection of Corporate Investments Abroad in the Light of the Barcelona Traction Case', *Zeitschrift für ausländisches öffentliches recht und völkerrecht* (1971) 162-196, at 192.

[28] The problem of assessing the damages of parent and subsidiary companies arose in the *Chorzów Factory* case, PCIJ *Collection of Judgements,* Series A, No. 17, at 48. See also the Advisory Opinion in *Reparation for injuries suffered in the service of the United Nations,* in which the ICJ stated that the defendant State cannot "be compelled to pay the reparation due in respect of the damage twice over". *I.C.J. Reports* 1949, at 186.

[29] Wälde, 'Compensation, Damages and Valuation in International Investment Law', 4, (6) *Transnational Dispute Management* (2007), at 43.

protection to all of them, the risk is evident: there would be an unnecessary multiple protections leading to double recovery and abuse of investors rights. Arguably, the more indirect the shareholder gets the more remote the damage will be. Logically, at one point the causal link between the measures and the damage will disappear. This lead Thomas Wälde, one of the few to have studied the issue of damages in investment arbitration and the risk of double-dipping in the case of companies of the same group, to suggest that the solution was to set a cut-off (ownership) point and require a sufficient direct relationship with the damage.[30]

4. Conclusion

Shareholders benefiting from the protection of an international investment agreement have a direct action to claim for both direct and indirect damage in investor-State arbitration. Since shareholders are protected indirectly through the company's actions there is a risk of double recovery. Nevertheless, since the protection in investment treaties is additional and not conditional to the reparations obtained by the local company, the State should pay twice.

Since indirect shareholdings are protected in investment treaties in addition to direct shareholdings there is a multiplication of claimants and of possible reparations to be awarded to investors of the same corporate group regarding the same measures and the same investment.

[30] Ibid., at 42.