

MEXICO CITY: Recovery of damages and loss of income

WEDNESDAY, 16 NOVEMBER 2011

A conference organised by Wöss & Partners SC and the Institute of Juridical Investigations at the National Autonomous University of Mexico considered approaches to damages and loss of income claims. **Adriana San Román**, partner and financial analyst at the Mexican firm, reports.



Herfried Wöss began with an overview of the principles of damages and loss of income claims for the violation of long-term contracts, with reference to his experience as arbitrator and party counsel in international arbitrations. He considered the issues a claimant will face - such as burden of proof, choosing the right financial expert, building a damages claim on the underlying legal principles, and selecting the right valuation method - including the applicable discount rate under the discounted cash flow method.

Wöss highlighted the problem of double counting arising from the confusion of concepts such as *damnum emergens* (material damage) and *lucrum cessans* (lost profits) and the

more apt approach of using the expectation or positive interest model (a differential model created by German scholar Theodor Friedrich Mommsen in the 19th century) to cope with the double counting issue.

Wöss also referred to the problem of arbitral tribunals misinterpreting Richard Posner's theory of "efficient breach" (as set out in *The Economic Analysis of Law*); and new tendencies such as Jan Paulsson's expectation theory as opposed to a rescission doctrine. In particular, Wöss underlined the importance of the leading principles such as *pacta sunt servanda* and full compensation using subjective valuation in a contractual environment, which is different from an objective determination of a fair market value in an expropriation scenario. The damages and loss of income caused by a breach of a joint venture agreement are different from the value of the company, he explained.

Craig Miles, a partner at King & Spalding in Houston, discussed, among other things, the distinction between lawful and unlawful expropriation; the date of breach versus date of expectations for measuring damages; the standard of compensation for non-expropriation violations of investment treaties; and the problem of measuring damage to a shareholder when there is debt at the level of the holding company or operating company.

Regarding lawful versus unlawful expropriation, Miles said that arbitrators could avoid the academic discussion about the distinction (if any) between the two by measuring damages from the date of breach but using an interest rate from that date forward that reflects the arbitrators' perception of the lawful or unlawful nature of the measures at issue. Regarding the problem of debt, Miles suggested that arbitrators should look at the investment holistically from the perspective of the shareholder's overall equity stake in the damaged operating company, and not limit damages to the debt-diluted value of the shareholder's equity on the date of breach.

Mark Kantor's presentation addressed the scope of responsibilities of a damages expert in an international arbitration, and in particular whether the damages expert is entitled to be an advocate on behalf of the party who engaged the expert or must present objective and unbiased evidence. Arbitration laws and rules are silent concerning whether party-appointed expert damages witnesses are subject to ethics duties such as impartiality and objectivity. National court systems offer three approaches:

many civil law systems rely on tribunal-appointed experts rather than party-appointed expert witnesses;

- the English courts require a party-appointed damages expert to offer objective and unbiased evidence and not to serve as an advocate for the party; and
- the US courts accept that a party-appointed expert may be partisan, but require the court to act as a gatekeeper to assure that the evidence is reliable and based on scientific methods and methodology.

The 2010 revised IBA Rules on the Taking of Evidence in International Arbitration move towards the English approach, requiring party-appointed experts to certify their independence from the party, legal advisers and the arbitral tribunal. The experts' own professional bodies also impose ethics responsibilities on their members when acting as

witnesses in disputes.

In addition, the codes of professional responsibility of the main professional bodies in the US to which many damages experts belong impose a duty of objectivity and impartiality on their members when acting as witnesses, and prohibit advocacy. No similar code of conduct exists, however, for commercial or investment bankers or academics. Arbitrators can establish practical parameters for the conduct of party-appointed experts such as a duty to disclose material relationships; a duty to include in any written and oral evidence all material information, whether supportive or adverse; and a duty to professionally assess the reasonableness of assumptions on which that expert relies in the expert evidence.

As the only economist on the panel, Santiago Dellepiane, a vice president with Compass Lexecon in New York, discussed key aspects of damages analysis. In particular, Dellepiane explained some of the main characteristics that distinguish valuation work for arbitration from valuation work in other settings that do not involve disputes. He focused on the importance of evidence relied on by experts which helps provide panels with additional comfort on the expert's submission, and discussed specific examples.

Speaking from the perspective of someone who has prepared expert reports as well as experts for hearings and trials for many years, he provided the audience with recommendations on things to consider when retaining experts, in particular: stay away from experts who bring 'canned' approaches, encourage the use of multiple valuation methods, and be prepared to understand the differences between an expert's damages assessment and other valuations.

Noiana Marigo, of Freshfields Bruckhaus Deringer in New York, spoke on moral damages in the context of investment arbitration. While more than a dozen investment treaty cases have discussed the appropriateness of awarding moral damages, the guidance provided by these tribunals to date has been rather limited, Marigo observed. The increase in such claims following the *Desert Line v Yemen* decision in 2008 demands a deeper analysis of the complex legal questions common to claims for moral damages in investment arbitration.

Open questions include whether tribunals have jurisdiction to hear such claims, whether legal persons may request moral damages suffered personally or by company executives, whether states may demand moral damages when faced with fraudulent claims and, in general, the circumstances under which an award for moral damages is justified.

Derrick Carson, partner at Locke Lord Bissell & Liddell in Houston, spoke about advocacy techniques in presenting damages evidence in international arbitration. He discussed the need to include damages in a cohesive theory of the case and gave a series of examples from his litigation experience. He also explained practical aspects of preparing experts for hearing and techniques for persuasive presentation of damages evidence.

The conference ended with a cocktail reception opened by **Ann Ryan Robertson**, the chair of the Chartered Institute of Arbitrators' North American branch.

The panel moderators were **Francisco González de Cossío** of González Cossío Abogados; **Paul Marquéz** of the Instituto de Investigaciones Jurídicas; **Alejandro Faya Rodríguez**, director general for foreign investment at the Ministry of Economy and consultant to UNCTAD for investment arbitration; **Adriana San Román** of Wöss & Partners; and **Sofía Gómez Ruano** of Azar, Ortega y Gómez Ruano.

Speaking after the event, the general counsel of power and automation group ABB Mexico, **Alejandro Rodríguez**, described it as “a very solution-oriented and high-level seminar”. Mark Kantor added, “The success of a conference can be measured by the questions from the floor. By that measure, this conference was clearly a success, with many challenging and informed questions leading to valuable give-and-take between the speakers and the members of the audience.”