

Daniel W. Kappes & Kappes, Cassiday & Associates

CLAIMANTS

and

Republic of Guatemala

RESPONDENT

ICSID Case No. ARB/18/43

**PARTIAL DISSENTING OPINION OF
PROF. ZACHARY DOUGLAS QC**

1. It is perhaps unusual to commence a dissenting opinion by paying tribute to the majority's decision; but it is appropriate to record that, on the critical issue that divides us, the majority has carefully considered the arguments for and against its position in a spirit of fairness and transparency. The majority has not, as is unfortunately all too common in this field, belittled the complexity of the problem or ignored the competing arguments in justifying its conclusion.
2. As a result my dissent can be expressed succinctly. I disagree with the majority's ultimate conclusion that a controlling shareholder of a company has a free hand in choosing whether to bring a claim for reflective loss in its own name or whether to bring a claim on behalf of the company for its direct loss under Article 10.16.1 of DR-CAFTA. Article 10.16.1 reads:
 1. In the event that a disputing party considers that an investment dispute cannot be settled by consultation and negotiation:
 - (a) the claimant, on its own behalf, may submit to arbitration under this Section a claim
 - (i) that the respondent has breached

- (A) an obligation under Section A,
- (B) an investment authorization, or
- (C) an investment agreement;

and

- (ii) that the claimant has incurred loss or damage by reason of, or arising out of, that breach; and

(b) the claimant, on behalf of an enterprise of the respondent that is a juridical person that the claimant owns or controls directly or indirectly, may submit to arbitration under this Section a claim

- (i) that the respondent has breached

- (A) an obligation under Section A,
- (B) an investment authorization, or
- (C) an investment agreement; and

- (ii) that the enterprise has incurred loss or damage by reason of, or arising out of, that breach.

3. The Claimants' primary submission on the ordinary meaning of the words of Article 10.16.1 is that the use of the word "*may*" (i.e. the "*claimant... may submit to arbitration*") rather than "*shall*" indicates that a claimant has complete discretion as to whether to pursue a claim under either limb of Article 10.16.1.¹ But that argument is fallacious: claimants cannot be mandated to submit their claims to arbitration—their consent is always required—and hence the word "*shall*" could not have been used in this context. The majority of the Tribunal does not itself rely on this argument and their analysis of the ordinary meaning of the words leads them to the conclusion that it is not dispositive one way or another on the issue. With this I agree.
4. Once, however, the other provisions of Chapter 10 of DR-CAFTA are factored into the interpretation of Article 10.16.1 as the relevant "*context*" in accordance with Article 31 of the Vienna Convention, to my mind the proper conclusion comes into sharp focus.
5. Article 10.18, which is entitled "*Conditions and Limitations on Consent of Each Party*", sets out a sophisticated mechanism to ensure that there will be no multiplicity of claims in domestic and international fora. A claimant must provide, with its notice of arbitration, a written waiver "*of any right to initiate or continue before any administrative*

¹ E.g. Claimants' Counter-Memorial on Preliminary Objections, §21.

tribunal or court under the law of any Party, or other dispute settlement procedures, any proceeding with respect to any measure alleged to constitute a breach referred to in Article 10.16.” If the controlling shareholder brings a claim under Article 10.16.1(b) on behalf of its company, then it has to provide a waiver both for itself and the company (Article 10.18.2(b)(ii)). The result is that the controlling shareholder and the company cannot pursue remedies in different fora in respect of the same alleged prejudice.

6. Article 10.26 then extends the logical consequences of this waiver requirement in Article 10.18. If a claim is brought on behalf of the company pursuant to Article 10.16.1(b), then Article 10.26.2(b) directs that any damages awarded must be paid to the company and not to the controlling shareholder. There is then no risk of double recovery because the controlling shareholder and the company would have previously waived the pursuit of any other remedy in respect of the same prejudice. Article 10.26.2(c) then states that “*the award shall provide that it is made without prejudice to any right that any person may have in the relief under applicable domestic law*”. This provision evidences a clear concern with the protection of the rights of any creditors of the company (secured and unsecured commercial creditors, involuntary creditors such as tort victims of the company’s activities, the tax authorities, and so on).
7. The question is then whether these provisions, and the obvious mischief that they seek to prevent, can be bypassed simply by the controlling shareholder bringing a claim for reflective loss instead under Article 10.16.1(a)? (No requirement of a waiver by the company or payment of damages to the company or a provision for the protection of the company’s creditors is contemplated for claims under Article 10.16.1(a).)
8. The question can be tied to the facts of the present case: is it permissible for Mr Kappes and KCA, as the controlling shareholders of Exmingua, to bring a claim before this Tribunal for reflective loss in respect of alleged prejudice to Exmingua, and at the same time for Exmingua to maintain its claim in respect of the same prejudice before the Constitutional Court of Guatemala? Can the risk of double recovery be countenanced? And if Mr Kappes and KCA are ultimately successful on the merits, can they avoid satisfying the legitimate claims of the creditors of Exmingua by recovering damages directly rather than through the company?

9. If these questions are answered affirmatively, as the majority has decided, then the specific objectives underlying Articles 10.18 and 10.26—the prevention of multiple claims in respect of the same prejudice, the avoidance of double recovery and the protection of the company’s creditors—can be defeated by the simple election of the claimant under Article 10.16.1.
10. This is where I respectfully depart from the majority’s reasoning. They have considered the *effet utile* principle in relation to Article 10.16.1(b) in isolation of the context provided by Articles 10.18 and 10.26. The *effet utile* principle, however, must be applied to all the express provisions of Chapter 10 of DR-CAFTA. If a particular interpretation of Article 10.16.1 fatally undermines Articles 10.18 and 10.26, then the obvious inference to be drawn is that that interpretation is wrong.
11. Consider Article 10.18.4, for instance, which provides:

No claim may be submitted to arbitration:

(a) for breach of an investment authorization under Article 10.16.1(a)(i)(B) or Article 10.16.1(b)(i)(B), or

(b) for breach of an investment agreement under Article 10.16.1(a)(i)(C) or Article 10.16.1(b)(i)(C),

if the claimant (for claims brought under Article 10.16.1(a)) or the claimant or the enterprise (for claims brought under Article 10.16.1(b)) has previously submitted the same alleged breach to an administrative tribunal or court of the respondent, or to any other binding dispute settlement procedure, for adjudication or resolution.

12. If the majority is correct, then it would appear to follow that a company can bring a claim for breach of an investment agreement pursuant to the arbitration clause in that agreement, and, if it is unsuccessful, its controlling shareholder can then bring the same claim to arbitration under Article 10.16.1(a) of DR-CAFTA. Article 10.8.4, which is obviously designed to avoid the multiplicity of claims relating to the same prejudice, is thereby emptied of practical utility.
13. In isolating Article 10.16.1 from the other provisions of Chapter 10 of DR-CAFTA in this way, the majority has also, in my respectful opinion, asked the wrong question. They have asked whether Article 10.16.1(b) would be deprived of an *effet utile* from the perspective of the putative claimants, who are obviously not parties to the treaty

and had no hand in drafting its provisions. They have answered that question by pointing to certain (hypothetical) advantages to claimants in pursuing claims on behalf of the company under Article 10.16.1(b) rather than claims for reflective loss under Article 10.16.1(a). In other words, if a rational claimant acting in its self-interest might go down the route of Article 10.16.1(b), for reasons subjective to that claimant, then for the majority an *effet utile* is established for that provision.²

14. Formulating the question in this way assumes what needs to be proven by reference to the context to be established in accordance with Article 31 of the Vienna Convention. The assumption is that the idea animating the State Parties in drafting Article 10.16.1 was to confer the broadest possible flexibility to controlling shareholders in advancing their claims against the respondent States. There is no basis for that assumption in the treaty itself. To the contrary, what is expressed in the treaty is that the State Parties were motivated to ensure that controlling shareholders could not bring a claim in their own right and at the same time direct their company to pursue other remedies in different fora (Article 10.18). What is also expressed in the treaty is that the State Parties were motivated to ensure that there would be no risk of double recovery and that the rights of creditors of the company would not be undermined or extinguished as result of paying damages directly to shareholders rather than through the company (Article 10.26). This is the relevant and permissible context to take into account pursuant to Article 31 of the Vienna Convention: it is derived from an analysis of the express terms of the treaty.
15. If that context is taken into account, then Article 10.16.1 must be interpreted as directing controlling shareholders to channel claims relating to prejudice to companies through the bespoke mechanism of Article 10.16.1(b).
16. Although it is by no means conclusive, the fact that all three State Parties to NAFTA have taken the same view in respect of the substantially similar provisions in Articles

² The majority considers that they are justified in asking this question because that is how the case was put (FN 149). There is no harm in asking this question to test the reasonableness or otherwise of a particular interpretation of Article 10.16.1 arrived at by applying Article 31 of the Vienna Convention. But it cannot be the legitimate question to ask for the purposes of arriving at that interpretation in the first place consistently with Article 31: the subjective preferences of non-parties to DR-CAFTA are not an element that can be taken into account unless it can be demonstrated that the State Parties drafted Article 10.16.1 to give effect to those subjective preferences. The context provides no evidence for that assumption but instead positively refutes it (see Articles 10.18 and 10.26).

1116 and 1117 confirms this interpretation.³ The following was the US Government's understanding of what it had just signed when NAFTA was sent to Congress:

Articles 1116 and 1117 set forth the kinds of claims that may be submitted to arbitration: respectively, allegations of direct injury to an investor, and allegations of indirect injury to an investor caused by injury to a firm in the host country that is owned or controlled by the investor.⁴

17. In one of the early NAFTA cases, the tribunal in *Mondev v USA* highlighted the importance of the distinction between Articles 1116 and 1117:

Having regard to the distinctions drawn between claims brought under Articles 1116 and 1117, a NAFTA tribunal should be careful not to allow any recovery, in a claim that should have been brought under Article 1117, to be paid directly to the investor.⁵

18. The distinction was considered more recently by the tribunal in *Clayton v Canada*:

[...] The terms of Article 1116 do not make clear whether they are limited to direct loss or they can include indirect loss that is, reflective loss.

However, if the words of Article 1116 are to be read “in their context” then Article 1117 has to be considered. This provision allows an investor to claim for loss to an enterprise thus providing for the recovery of reflective loss. As a result, to permit reflective loss to be recovered under Article 1116 would raise questions about the relationship between the two provisions perhaps rendering Article 1117 inutile. This is the point made by the Respondent. The Investors argue that the potential for conflict only arises when claims are brought under both Article 1116 and

³ USA: *Pope & Talbot Inc. v Government of Canada*, Seventh Submission from the United States of America, 6 November 2001, §§3-5, RL-0071; *GAMI v Mexico*, Submission of the United States of America, 30 June 2003, §14, RL-0072; *William Ralph Clayton, & Bilcon of Delaware Inc. et al. v. Government of Canada*, PCA Case No. 2009-04, Submission of the United States of America, 29 December 2017, §12, RL-0008.

Canada: *Clayton v Canada*, Government of Canada Counter-Memorial on Damages, 9 June 2017, §28, RL-0017; S.D. Myers, Counter-Memorial (Damages Phase), 7 June 2001, §§108-109, RL-0075.

Mexico: *GAMI v Mexico*, Statement of Defense, 24 November 2003, §§167(e) and (h), RL-0076.

⁴ US Government, The NAFTA Implementation Act, Statement of Administrative Action, p. 146, RL-0070.

⁵ *Mondev v USA*, Award, 11 October 2002, (Sir Ninian Stephens, Prof. James Crawford, Judge Stephen Schwebel), §86, RL-018.

Article 1117, but this only reinforces the question of why Article 1117 was included into NAFTA if claims can be brought for reflective loss under Article 1116.

Both the Respondent and the United States in their submissions argue that the inclusion of separate provisions in Article 1116 and Article 1117 was deliberate. Article 1116 gave effect to the traditional rule of customary international law that a party can sue for its losses arising out of the breach of an international obligation. Article 1117 was designed to permit claims by an investor on behalf of its investment, thus permitting a claim for reflective loss. In the absence of that provision a claim for reflective loss would otherwise be barred under customary international law by virtue of the ICJ judgment in *Barcelona Traction*, which rejected the right of shareholders to bring claims in place of the corporation.

The Tribunal finds this to be a plausible explanation for the existence of the two separate provisions in NAFTA Chapter Eleven, which would argue against overlap between them and would mean that reflective loss could not be recovered under Article 1116.⁶

19. Returning to the majority's reasoning in this case, even if it were permissible to interpret Article 10.16.1 through the eyes of putative claimants in a manner that defeats the utility of other express provisions of the treaty, I am not persuaded that the suggested reasons why a rational claimant might elect to pursue a claim under Article 10.16.1(b) rather than Article 10.16.1(a) are particularly good ones.
20. The only such reason advanced by the Claimants in this case is that there may be tax or currency conversion advantages in bringing a claim on behalf of the company rather than as a shareholder's claim for reflective loss.⁷ But did the State Parties really draft Article 10.16.1 with the objective of allowing claimants to minimize their tax burden or currency exchange costs in mind? That seems rather unlikely and there is of course no evidence for that hypothesis.
21. The majority postulates instead that a controlling shareholder, who nevertheless does not hold all of the shares, might elect to pursue a claim on behalf of the company so that potentially greater damages covering the company's entire loss can

⁶ *Clayton v Canada*, Award on Damages, 10 January 2019 (Judge Bruno Simma, Prof. Don McCrae, Prof. Bryan Schwartz), §§371-4, CL-0070.

⁷ Transcript of 16 December 2019 Hearing, pp. 101, 204.

be recovered, thereby restoring the company to full health. It is true that a controlling shareholder might do that even if we know empirically that precious few have gone down that route when it has been available (e.g. when the mechanism under Article 25(2)(b) of the ICSID Convention applies). But the critical point is that we cannot look at this exclusively from the vantage point of putative claimants. Are the serious policy objectives underlying Articles 10.18 and 10.26 intended to be contingent upon the benevolence of the claimant in electing to restore the company to its full health rather than bypassing the company (and its creditors) and recovering directly? It seems highly improbable that the State Parties would attempt to erect a bulwark against the familiar problems associated with reflective loss claims (multiplicity of proceedings, risk of double recovery, evisceration of creditors' rights) and at the same time provide claimants with the means to run straight through it.

22. The majority finally cites the complexities of proving causation and quantum when a shareholder claims that a loss to the company has resulted in a loss to the value of its shares. They argue that a controlling shareholder may thus elect to bring a claim on behalf of the company to avoid these potential hurdles.
23. There is a certain irony to this point. One of the reasons that systems of municipal law and the other branches of international law do not allow unrestricted reflective loss claims is precisely because their quantification is fraught with conceptual difficulties. What happens, to take a few banal examples, if shares in a going concern increase in value after the alleged breach or after the award? Or if the company has a policy of reinvesting profits rather than paying dividends? Or has a substantial debt that must be serviced to third parties before dividends can be paid? Until recently, tribunals in investment treaty cases were content to ignore these difficulties altogether and simply award a shareholder a percentage of the value of the company at the date of the breach commensurate with the size of its shareholding. Perhaps an outlier in the early days of the jurisprudence was the award in *Nykomb v Latvia* (as cited by the majority) where it was recognized that things were not quite that simple. But the concession to complexity in that award did not translate into a sophisticated solution: after recognizing that there is no 1:1 relationship between income to a company and income to a 100% shareholder, the tribunal simply divided the company's income by a factor of 3 to quantify the shareholder's reflective loss. No justification was given for that figure. It was plucked straight from the stratosphere.

24. It is true, as the majority suggests, that things have evolved and now the complexities attending the quantification of reflective loss claims are more likely to be taken into account by a tribunal. But did the State Parties in drafting Article 10.16.1 really: (i) envisage that reflective loss claims on an unrestricted basis would be permitted by investment tribunals as a matter of principle given that customary international law rejects this, international human rights law rejects this and municipal systems of law recognizing the institution of a limited liability company reject this and (ii) contemplate that the same early decisions of investment tribunals permitting reflective loss claims would later be discredited in respect of their approach to the quantification of damages such that (iii) it was prudent to allow controlling shareholders to avoid the hurdles imposed by the recent, more robust approach to quantification of damages for reflective loss claims by opening up a route to claim on behalf of the company?⁸
25. Or did the State Parties simply intend that claims relating to a loss to a company be brought on behalf of the company?
26. The majority recognizes that multiplicity of claims, the risk of double recovery and the evisceration of creditors' rights are serious problems attending the pursuit of reflective loss claims. But the majority ultimately concludes that these are policy considerations that are not for a tribunal to grapple with in the interpretation of Article 10.16.1. This is nub of my disagreement. These policy considerations are manifest in the express provisions of the same Chapter 10 of DR-CAFTA in which Article 10.16.1 is embedded. The choice ultimately boils down to interpreting Article 10.16.1 to operate consistently with Articles 10.18 and 10.26 and the policies they promote, or interpreting Article 10.16.1 to render Articles 10.18 and 10.26 moot

⁸ I do not agree with the majority that a more careful approach to quantifying a reflective loss claim entails that creditors' rights are thereby preserved "*because shareholders in these circumstances do not recover any proceeds that properly were due to creditors*" (FN 176). There is a massive difference between (i) creditors actually getting paid because compensation for prejudice to the company passes through the company (creditors would have preference over the shareholders in this scenario) and (ii) funds due to creditors not being included in the mathematical calculation of reflective loss to a controlling shareholder. The reality in the vast majority of cases is surely that if a company suffers substantial prejudice on account of measures attributable to the host State and damages are awarded to the controlling shareholder directly rather than through the company, then that company is unlikely to be able to trade out of difficulties and pay the amounts owing to creditors when they fall due. The rights of creditors become illusory as a practical matter if a controlling shareholder has the option of bypassing the company. This is precisely one of the reasons that no other branch of the law allows unrestricted claims for reflective loss by shareholders.

for all practical purposes. I consider that Article 31 of the Vienna Convention and the principle of *effet utile* mandate the former approach.

27. I finally note that the Claimants in this case have offered no explanation as to why they did not simply file a claim on behalf of their company, Exmingua, under Article 10.16.1(b). Nor have they suggested that there was any impediment to do so. In this case there will, therefore, be multiple proceedings, a risk of double recovery and the possibility that Exmingua's creditors will be left out of pocket in respect of their legitimate claims—in order to satisfy an unarticulated preference of Exmingua's shareholders to seek compensation directly.
28. My dissent is partial in several respects. First, even on my reading of Article 10.16.1, the Claimants would not be prevented from pursuing their claim for the expropriation of their shares in Exmingua because such a claim is cognizable under Article 10.16.1(a)—it is a claim to vindicate their legal rights as shareholders rather than their mere economic interest in the value of Exmingua's shares. Second, I join the majority without reservation in the Tribunal's decisions on the Respondent's second and third objections on the premise that the majority prevails in respect of its disposal of the first objection.



Zachary Douglas