CRA Insights:
International Arbitration

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The importance of interest in arbitral awards

Interest has a significant impact on arbitral awards. Pre-award interest has added approximately 50% on average to awarded damages across non-annulled ICSID awards since 2000.

The interest rate is crucial to compensation. If all these cases awarded interest at LIBOR+2%, interest would have added 43% on average to awarded damages. On the other hand, if these cases used US T-Bill rates to calculate interest, interest would have added only 22% on average. On a hypothetical $100 million award before interest, this represents a difference of approximately $20 million in interest just due to a choice of rate. Naturally, the interest rate is frequently set contractually or by legal instruction.

Since 2015, tribunals' most common choice of pre-award interest rate has been LIBOR plus an increment whereas rates based on T-Bills or on LIBOR without an increment have become less prevalent. 2% is the most popular increment on LIBOR.

The data

We consider the universe of cases listed on ICSID as of December 31, 2021 and find **53 cases** with a non-annulled award of damages and pre-award interest. Table 1 details the steps followed to identify awards included in our analysis.

Table 1: Awards reviewed and included in analysis

Criteria	Count
Number of cases in ICSID and UNCTAD	1,320
Number of cases containing an award document[1]	223
Number of cases with an award on damages[2]	71
Number of cases with pre-award interest rate information	**63**
Number of cases with damages awarded since 2000	60
Number of cases with interest not applied as a penalty[3]	57
Number of cases based on LIBOR, US Treasury Yields, Prime Rate, a Fixed Percentage, a Fixed Amount[4]	56
Number of cases without annulment after award date	**53**

[1] These cases have available award documents listed under the title "Award" or "Award of the Tribunal."
[2] Award documents don't necessarily contain an award of damages, some simply state assigned legal fees and costs to be paid.
[3] Three cases included interest rate information, but interest applied as a penalty only if compensation of the award was not paid on time.
[4] The interest rate for the one case excluded was based on EURIBOR.

Pre-award interest was based on LIBOR in 36% of the cases, on fixed percentage rates[5] in 42% of the cases, and on T-Bills in 8% of the cases. 13% of the cases involved an interest amount stated in dollar terms.[6]

However, these proportions have changed through time. As shown in Figure 1, tribunals have been setting pre-award LIBOR plus an increment more often after 2015 than before. Half of the decisions since 2015 have had interest based on LIBOR plus an increment, as compared to 22% before 2015. Pre-award interest based on a fixed percentage rate, T-Bills or LIBOR without an increment have been chosen less since 2015.

Figure 1: Pre-award rates before and since 2015[7]

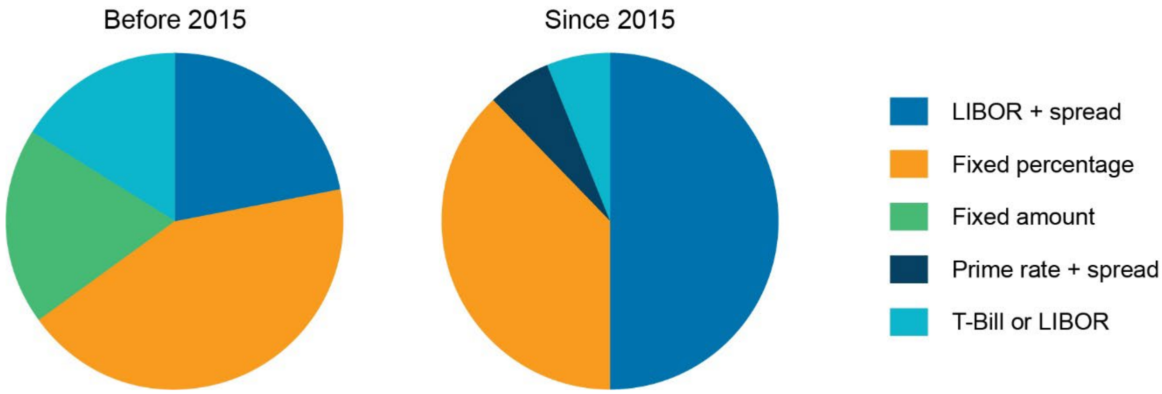
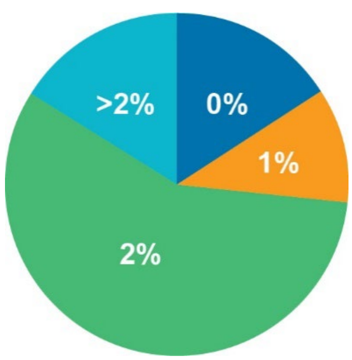


Figure 2 shows the most common increments on LIBOR. More than half of the LIBOR awards employed a LIBOR+2% rate. Figure 3 shows that 6% to 8% were the most common of the fixed interest rates awarded.

Figure 2: Distribution of increments on LIBOR



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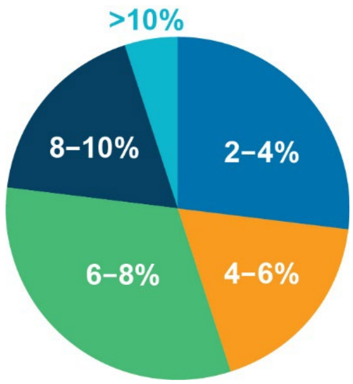
5 These are stated in the award documents as fixed percentages, e.g., 3% or 4%.

6 A lump sum interest amount is awarded without any dependency on an interest rate.

7 Prime Rate + spread was not used before 2015. Fixed amount was not used since 2015.

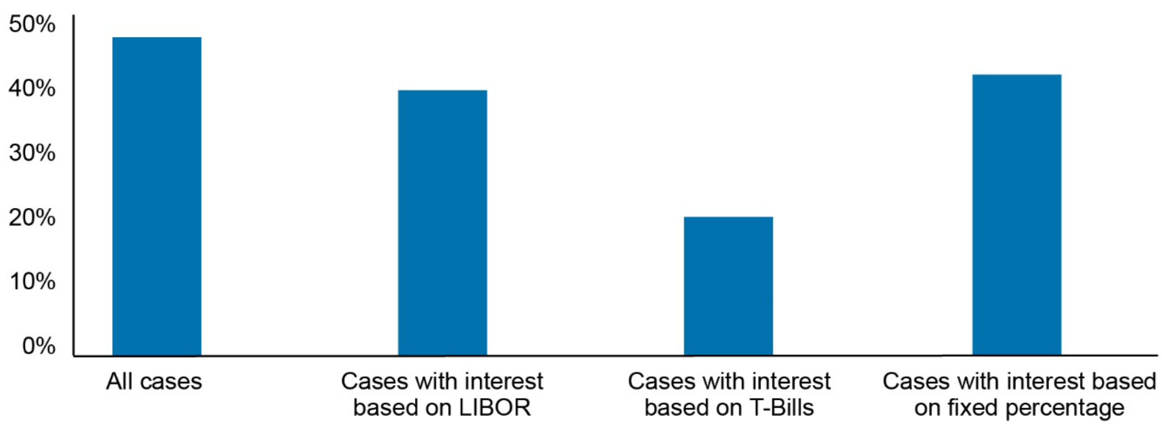
Figure 3: Distribution of interest based on fixed percentages



Increase in award due to pre-award interest

Figure 4 shows that pre-award interest added an average 47% to the awarded damages; the respective median is 33%.[8] In particular, interest increased compensation by over 50% in more than 30% of the cases (Figure 5). Further, interest increased compensation by at least $10 million in over 40% of the cases (Figure 6).

Figure 4: Increase in average compensation due to pre-award interest



[8] Our analysis assumes a 12-month tenor when the tenor of the pre-award interest is unspecified. We assume annual compounding frequency for awards without compounding frequency indicated.

Figure 5: Distribution of increase in compensation due to pre-award interest (%)

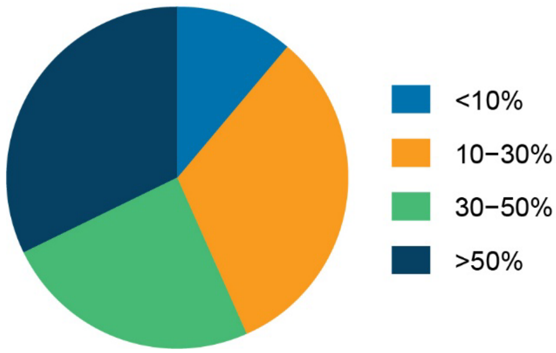
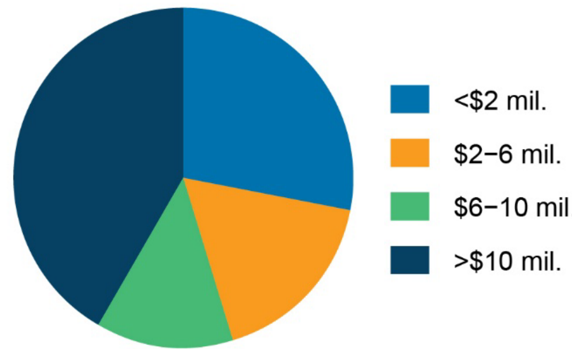


Figure 6: Distribution of increase in compensation due to pre-award interest ($)



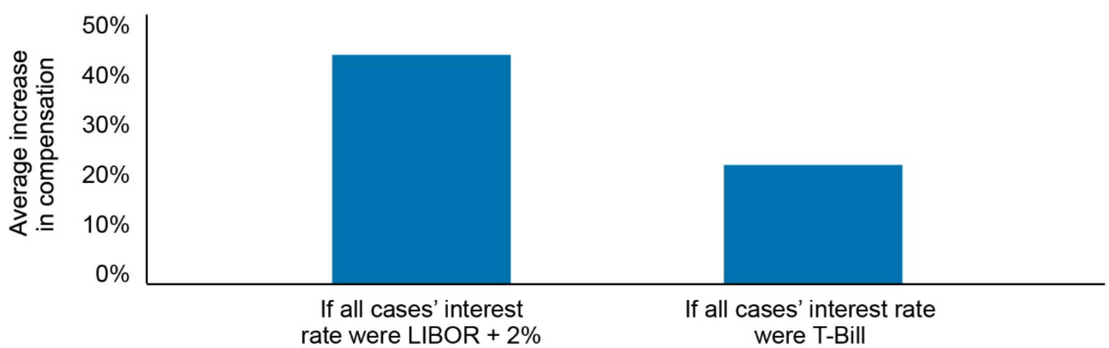
The effect of choice of rate on compensation

Next, we examine the impact of the choice of rate on awards. To illustrate the relevance of the tribunal's decision on the rate of pre-award interest, we examined what the increase in compensation would be had pre-award interest for all cases been either LIBOR+2% or the US T-Bill rate.

If tribunals had selected T-Bill rates, pre-award interest would have added 22% to the awarded damages on average (Figure 7). But if tribunals had selected LIBOR + 2% in all cases, pre-award interest would have added 43% to the awarded damages on average.

This is an average difference of 20 percentage points. On an award of $100 million before interest, it would represent a difference of approximately $20 million in interest. Few tribunal decisions among quantum experts' opinions are near this impact on compensation.

Figure 7: Average increase in compensation: hypothetical rates



There isn't an observable relation between the size of an award and the tribunal's choice of pre-award interest rate (expressed as a % of the award excluding interest).

Take-aways

Interest is a significant component of damage awards and so is the choice of interest rate. For example, if a case were to be awarded now for a breach five years ago, the difference between awarding LIBOR+2% vs. T-Bill rates would be 16% of the award before interest.[9]

About CRA's International Arbitration experience

CRA experts have extensive experience in commercial and investment treaty arbitrations and have provided testimony in all the major international arbitration forums, including ICSID, PCA, ICC, LCIA, SIAC, HKIAC, SCC, and under UNCITRAL rules. With the highest average claim among top-10 expert firms, we have been engaged in some of the most complex and high-profile disputes of recent years. We combine finance and quantum expertise with industry expertise from energy, oil and gas, metals and materials, mining, pharmaceuticals and life sciences, banking, financial services, and various other industries to offer a one-stop solution for clients in disputes that might otherwise require several firms.

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[9] 12M USD LIBOR from Bloomberg and 1-Year T-Bill Rate from fred.stlouisfed.org.