Chapter 2

Compensatory Interest

§ 2.1 Introduction

The issue of whether compensatory interest should be paid on outstanding monetary claims arises in almost every dispute between transnational parties. In fact, it is not uncommon for interest claims to amount to millions of dollars and, because a lengthy period may elapse between the origin of the dispute and the final award, whether a tribunal awards interest may be as significant, from a monetary standpoint, as the principal claim itself. Claims for interest typically raise three issues: (1) whether interest is permitted, (2) if so, what is the period of time for which interest accrues, and (3) at what rate interest is to be awarded.

Most countries permit awards of compensatory interest as compensation for the use or detention of money. A few countries prohibit the payment of interest, primarily because it is inconsistent with their religious beliefs. However, even some countries whose religious beliefs generally prohibit the payment of interest have allowed it in certain commercial transactions. Indeed, the practice has become so widespread, it can be said that the liability to pay interest as part of an award of damages is an accepted international legal principle.

With respect to the period for which interest is allowed, the laws of most countries provide that interest starts to accrue from the date of default or the date when the cause of action accrues. Exactly what constitutes a default, however, varies from jurisdiction to jurisdiction. The consensus appears to be that, if there exists an agreement that provides a breach of contract will occur if the respondent fails to fulfill its obligations by a certain time and the respondent does not perform by that date, then interest will automatically start to accrue. If there exists an agreement between the parties but it does not specify such a date, the prevailing view is that interest begins to accrue only after the claimant provides the respondent with a demand for performance.

With respect to the rate at which interest accrues, the laws of most countries provide for payment at the rate set forth in the parties' agreement. When the contract does not specify the rate, statutory provisions usually apply. Unfortunately, these statutory interest rates tend to be lower than market rates and often remain unchanged for years. Further, they vary significantly from country to country, ranging from 4% to 16%.

interest. The latter, known as the UNIDROIT Principles, contains detailed provisions stating that interest should generally be paid from the time of non performance and should accrue at a rate equivalent to the average bank short term lending rate to prime borrowers prevailing for the currency of payment at the place of payment.

Among international tribunals, there exists no uniform approach for awarding interest. As a result, interest awards have varied greatly. There has been little agreement on the circumstances warranting the payment of interest,\(^6\) and the rates at which interest has been awarded have ranged from 3% to 20%.\(^7\)

This chapter is derived from John Y. Gotanda, *Awarding Interest in International Arbitration*, 90 Am. J. Int'l L. 40 (1996)\(^1\)

This chapter specifically addresses issues concerning the awarding of compensatory or pre award interest, which is interest as part of an award. Moratory interest, which is interest on an award, is discussed in Chapter 3.


\(^3\) See, e.g., American Bell, 12 Iran U.S. Cl. Trib. Rep. at 229 (awarding in addition to damages of $15 million, interest at a rate of 10% for seven years); Telecommunications Co. of Iran v. United States, 23 Iran U.S. Cl. Trib. Rep. 320, 337 (1989) (awarding, in addition to damages of $1.2 million, 10% interest for approximately 10 years).

\(^4\) See, e.g., KCA Drilling Ltd. v Sonatrach, ICC No. 5651 (awarding $23 million in damages and $26 million in interest), summarized in pertinent part in David J. Branson & Richard E. Wallace, Jr., *Awarding Interest in International Commercial Arbitration: Establishing a Uniform Approach*, 28 VA. J. INT'L L. 919, 920 (1988); Aminoil, 21 I.L.M. at 1042 (awarding $83 million in damages and $96 million in interest). If, for example, simple interest accumulates at a rate of 10% per annum, the amount owed will be doubled in 10 years. By contrast, if interest on the amount owed is compounded, it will be doubled in 7.3 years.


\(^6\) Compare Grove Skansa v. Lockheed Aircraft Int'l AG, Award No. 3903 (ICC 1981), summarized in pertinent part in Branson & Wallace, supra note 4, at 933 37 (refusing to apply New York statutes regarding interest even though the parties explicitly stated that New York law would govern all contract disputes) with Final Award No. 5946 (ICC 1990), reprinted in 16 Y.B. COM. ARB. 97 (1991) (holding that the parties' disputes concerning interest would be resolved under the New York statutes as provided in the agreement).

\(^7\) See McCollough & Co., Inc. v. Ministry of Post, Tel. & Tel., 11 Iran-U.S. Cl. Trib. Rep. 3, 28 n.21 (1986) (citing cases); 3 MAJORIE M. WHITEMAN, DAMAGES IN INTERNATIONAL LAW, 1924, 1975 86 (1953) (discussing cases); JACKSON H. RALSTON, THE LAW AND PROCEDURE OF INTERNATIONAL TRIBUNALS 130 (1926) (discussing cases).

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**Referring Principles:**

- VII.6 - Duty to pay interest