INTERNATIONAL CENTRE FOR THE SETTLEMENT OF INVESTMENT DISPUTES

CASE NUMBER ARB/05/10

BETWEEN

MALAYSIAN HISTORICAL SALVORS SDN BHD ... Claimant

AND

THE GOVERNMENT OF MALAYSIA ... Respondent

RESPONDENT'S REPLY MEMORIAL ON OBJECTIONS TO JURISDICTION

The Arbitrator: Mr. Michael Hwang, SC

Secretary to the Tribunal: Mr. Ucheora Onwuamaegbu

Representing the Claimant

The Eren Law Firm
2555 Pennsylvania Avenue
Suite 1005
Washington DC, 20037-1651

Representing the Respondent

Attorney General's Chambers Malaysia
Level 8, Block C3
Federal Government Administrative Centre
62512 Putrajaya, Malaysia

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A. PRELIMINARIES

1. The Respondent wishes to record its concern and objections over the use of disparaging and scurrilous language in the Claimant's Memorial on Jurisdiction dated 15.3.2006. Frequently the Claimant makes sweeping statements and draws dubious conclusions from documents that are not only incomplete in itself, but questionable. Irrelevant and out of context incidents are cited.

2. For ease of reference the Respondent has prepared an index to the Claimant's exhibits [**Index to Claimant's Exhibits**].[1] Specific remarks concerning certain exhibits are included in that Index. But generally, the Respondent wishes to also put on record that there are documents exhibited by the Claimant which are wholly irrelevant to the proceedings before this Arbitral Tribunal particularly **Exhibits G, H, I, J, K and N**. These documents ought to be disregarded.

3. Where appropriate the Respondent will deal with some of the documents exhibited specifically.

4. Further, the Respondent states that it intends to rely on the submissions made in the Respondent's Memorial on Objection to Jurisdiction dated 11.03.2006 in its entirety in reply to the Claimant's Memorial on Jurisdiction. In addition the following Reply is made.

[1] Annex 83

B. INTRODUCTION

5. The Respondent's Reply Memorial is filed in response to the Claimant's Memorial on Jurisdiction dated 15.3.2006.

6. At **page 5** of that Memorial the Claimant asserts the following -

> "(i) the Government of Malaysia has unlawfully taken MHS's money and violated MHS's rights to money;
>
> (ii) Malaysia's arbitral tribunal, courts and other institutions have been complicit in that process by denying required due process of law to MHS; and that
>
> (iii) the Government of Malaysia has not afforded MHS and MHS's investment in Malaysia fair and equitable treatment as Malaysia is obligated to do."

7. According to the Claimant's Memorial [**page 26**] it is alleged that -

> "(1) the UK/Malaysia BIT protects MHS's investment in Malaysia;
>
> (2) Malaysia has breached its obligation to MHS under the UK/Malaysia BIT and under general international law; and
>
> (3) MHS has suffered loss and damage by reason of Malaysia's breaches."

8. The Claimant further alleges that the Respondent has violated -

> "(i) Articles 2 (2) (Protection of Investment, Fair and Equitable Treatment, Unreasonable and Discriminatory Measures, Observance of Obligations), 4(1) (Expropriation), and 5 (Repatriation of Investment) of the UK/Malaysia BIT;
>
> (ii) international law."

9. However the Respondent states that this Arbitral Tribunal cannot decide on those assertions and allegations because it does not have the requisite and relevant jurisdiction and competence to do so.

C. GROUNDS IN SUPPORT OF OBJECTION TO JURISDICTION AND COMPETENCE OF THE ARBITRAL TRIBUNAL AS RAISED IN THE RESPONDENT'S MEMORIAL

10. At **page 2 of the Respondent's Memorial on Objections to Jurisdiction** dated 11.3.2006 two grounds in support of its objections against the jurisdiction and competence of the Arbitral Tribunal were raised -

> "(a) The Claimant and the claim do not fall within the scope of Article 25 of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (ICSID Convention) and Article 7 of the Agreement Between the Government of the United Kingdom of Great Britain

and Northern Ireland and the Government of Malaysia for the Promotion and Protection of Investments (IGA).

(b) The Claimant's claim is not an "investment "under Article 1 of the IGA."

11. Six issues were identified at **page 2 of the Respondent's Memorial on Objections to Jurisdiction** as relevant in the consideration of the two grounds raised, namely -

(i) Whether the Claimant has the *locus standi* to institute proceedings before the ICSID Tribunal?

(ii) Whether the Claimant's claim is an "investment" within the meaning of Article 25(1) of the ICSID Convention?

(iii) Whether the Claimant's claim is an "approved project" pursuant to Article 1 (1) (b) of the IGA?

(iv) Whether the Arbitral Tribunal has jurisdiction to determine a pure contractual claim?

(v) Whether the Claimant has been denied access to justice in the Malaysian Courts?

(vi) Whether the Claimant has exhausted all domestic remedies prior to instituting the request for arbitration before ICSID?

12. On a perusal of the Claimant's Memorial on Jurisdiction it can safely be said that the Claimant **agrees** with the Respondent that **this Arbitral Tribunal's jurisdiction and**

competence is entirely dependent on the interpretation and application of Article 25 of the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (ICSID Convention) and Articles 1 and 7 of the Agreement Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Malaysia for the Promotion and Protection of Investments (IGA).

13. This can be gleaned from **pages 23 to 24 of the Claimant's Memorial** where it is stated –

> "1. MHS must allege claims or disputes which are justiciable under the UK/Malaysia BIT,
> 2. the legal claims or disputes mentioned above must arise directly out of an investment,
> 3. the investment must be between Malaysia or the Government of Malaysia and a national or company of the United Kingdom,
> 4. the parties to the dispute, MHS and the Government of Malaysia, must consent in writing to submit the dispute to the Centre,
> 5. the investment at issue has to fall within the definition of the term "investment" set forth in the UK/Malaysia BIT,
> 6. the qualifying investment must be approved by the Government of Malaysia, and
> 7. the parties in dispute, viz. MHS and the Government of Malaysia, must have attempted to resolve their dispute within three months through the pursuit of remedies in Malaysia or otherwise prior to instituting arbitration proceedings under the ICSID Convention."

14. From the above it can also be safely concluded that in determining the issue of jurisdiction and competence the 6 issues set out in paragraph 11 above are substantially the same as those mentioned by the Claimant.

D. REPLIES TO THE CLAIMANT'S SUBMISSION

15. First, the Respondent submits that the Respondent has already comprehensively dealt with all the matters raised by the Claimant in the **Respondent's Memorial on Objections to Jurisdiction**.

16. However, for the sake of completeness the Respondent will address the issues once more taking into account the submissions of the Claimant.

(i) *Locus Standi*

17. The Claimant says that it has *locus standi* to institute this claim under the IGA read together with the ICSID Convention – **pages 28, 32 and 33 of the Claimant's Memorial**.

18. The Respondent denies this for the reasons already explained in the **Respondent's Memorial on Objections to Jurisdiction: pages 29 to 31**.

(ii) "Investment" and Article 25(1) of the ICSID Convention

19. According to the Claimant the Salvage Contract is an investment under Article 25 of the ISCID Convention and Article 1 of the IGA. The Claimant's assertion is premised on performance:

    (a) The Claimant's performance of the Salvage Contract is the quintessence of investment under Article 25 of the ISCID Convention – **pages 27 and 28 of the Claimant's Memorial**;

    (b) The Claimant's performance of the Salvage Contract is the quintessence of investment under Article 1 of the IGA – **pages 34 to 38 of the Claimant's Memorial**;

    (c) The Salvage Contract is an approved project – **pages 38 to 48 of the Claimant's Memorial**.

20. The Respondent denies this for the reasons already explained in the **Respondent's Memorial on Objections to Jurisdiction – pages 31 to 39**.

21. The Respondent further submits that the Salvage Contract and its terms need to be examined in their proper context in order to understand their application and significance.

22. The purpose and intention between the Claimant and the Respondent at the time of the execution of the Salvage Contract is clearly set out in the preamble to the Salvage Contract. It reads as follows -

"THIS CONTRACT is made this 3rd day of August 1991 between the GOVERNMENT OF MALAYSIA (hereinafter referred to as the 'GOVERNMENT') of the one part and the MALAYSIAN HISTORICAL SALVORS SDN BHD, a company incorporated in Malaysia and having its registered office at c/o IPCO SDN BHD, 26th FLOOR, MENARA PROMET, JALAN SULTAN ISMAIL, 50250 KUALA LUMPUR (hereinafter referred to as the 'SALVOR') of the other part.

Whereas the GOVERNMENT hereby enters into the Agreement with the SALVOR and the SALVOR agrees to survey, identify, classify, research, restore, preserve, appraise, market, sell/auction and carry out a scientific survey and salvage of the wreck and contents (hereinafter to be referred as the 'Works') believed to be the Wreck "DIANA" located approximately at a position LAT. 02 Deg 14.0 Min. North and Long. 102 Deg. 06.0 Min East (hereinafter to be referred to as the 'Wreck').

Whereas the Works is for the sole purpose of archeological interest and the study of historical heritage."

23. Clauses 2 and 4 of the Salvage Contract read as follows -

"CLAUSE 2 – SCOPE OF CONTRACT

2.1 **The SALVOR shall carry out and complete all Works in accordance to the terms and**

conditions of this Contract, the instruction of the survey and salvage as issued by the Principal Receiver of Wrecks, the Instructions for the scientific excavation, restoration and preservations as issued by the Director General of Museums and as directed by the Supervision Team.

2.2 The Contract shall be on 'No Finds No Pay' basis and all expenses incurred shall be on the account of the SALVOR.

CLAUSE 4 – SERVICE FEE

4.1 In Consideration of the Works done by the Salvor, the Government shall pay the Salvor a fee equivalent to the following: -

4.1.1 For the sum of appraised value (for Finds not Sold/Auctioned) and the Sale/Auction Value (for Finds Sold/Auctioned) or Finds under and including US Dollars Ten (10) Million, a seventy percent (70%) share of the proceeds.

4.1.2 For the sum of appraised value (for Finds not Sold/Auctioned) and the Sale/Auction Value (for Finds Sold/Auctioned) or Finds above US Dollars Ten (10) Million and up to US Dollars Twenty (20) Millions, a sixty percent (60%) share of the proceeds.

4.1.3 For the sum of appraised value (for Finds not Sold/Auctioned) and the Sale/Auction Value (for

Finds Sold/Auctioned) or Finds above US Dollars Twenty (20) Million, a fifty percent (50%) share of the proceeds."

24. The Salvage Contract was for a period of only eighteen (18) months.

25. While the Salvage Contract may be suggested to be an investment in the ordinary sense of the term "investment" where there is financial value for performance, this is overly simplistic. A contract, in particular this Salvage Contract, cannot be transformed by the mere fact of financial value for performance into an "investment" giving rise to an international law obligation under the IGA.

26. Even if for argument's sake, which is denied, the Salvage Contract is to be considered as an investment it has first of all to be classified by the appropriate Ministry in Malaysia i.e. the Ministry of International Trade and Industry as an investment in an "approved project" within the ambit of Article 1 of the IGA.

27. Yet another relevant factor to be considered is that the term "Government" used in the Salvage Contract is defined in Clause 1.5 of the Salvage Contract as "where appropriate the Secretary General, Ministry of Finance, the Secretary General, Ministry of Transport, the Secretary General, Ministry of Culture and Tourism, the Director General of Museums and the Director of Marine, Peninsular Malaysia or their representatives". The Ministry of International Trade and Industry which is charged with the responsibility of classifying "approved projects" is not included in the definition of "Government" in the Salvage Contract.

28. Whilst it is not in dispute that a Committee was set up to formulate guidelines and procedures concerning salvage contracts including this Salvage Contract the Respondent submits that nothing turns on this.

29. At **page 9 of the Claimant's Memorial** the Claimant has made reference to the Chairman of that Committee "left the Salvage Committee after being accused of criminal breach of trust."

30. The Respondent denies that and states that the charge against the Chairman on 11.11.2005 for an offence under section 409 of the Penal Code[2] read together with sections 109 and 34 of the Penal Code is totally unrelated to this matter. The Chairman was actually charged for abetting another person in committing a criminal breach of trust committed between 27.4.1999 to 31.7.1999.[3] During that period not only was there no longer any Committee in existence but the arbitration relating to this Salvage Contract had already been completed. Such references in **Exhibit B** as mentioned in **page 9 of the Claimant's Memorial** are therefore irrelevant, out of context and in fact mischievous. Such references must therefore be disregarded.

31. For the abovementioned reasons, the Respondent submits that the Salvage Contract was in fact an ordinary service contract and not an investment under the IGA. It was not and was never within the contemplation of the parties that the Salvage Contract was to be construed as an investment.

[2] Annex 84
[3] Annex 85

32. Since as shown in the Respondent's Memorial concerning *locus standi* that the Claimant was at the material time not a majority British owned company, the requirements of Article 25 of the ICSID Convention have not been satisfied.

(iii) Salvage Contract not an "approved project"

33. The Claimant says that the Salvage Contract is an "approved project" within Article 1(1) (b) (ii) of the IGA for two reasons:

(a) classification as an "approved project" is not required - **page 39 of the Claimant's Memorial**;

(b) in any event, there is classification as an "approved project" - **page 39 of the Claimant's Memorial**.

34. In the Claimant's view classification as an "approved project" is not required because the Salvage Contract is made with the Respondent. Even if it were required, "the Contract and the assent to the Contract manifested by the Government of Malaysia and its ministries and departments at the time of its execution and throughout the period of MHS's performance under the Contract meets any requirement for the classification of the salvage project by the appropriate ministry in Malaysia as an "approved project" in accordance with the relevant ministry's legislation and administrative practice." - **pages 39 and 41 to 48 of the Claimant's Memorial**.

35. In reply the Respondent refers to **pages 39 to 44 of the Respondent's Memorial on Objections to Jurisdiction** and to **paragraph 23 in this Reply Memorial on Objections to Jurisdiction**.

36. There should be no undue emphasis on the execution of the Salvage Contract by the Marine Department on behalf of the Respondents as all contracts entered into by the Respondent have to be signed by authorized persons pursuant to the Government Contracts Act 1949 [Act 120][4]. Section 2 thereof states –

> "All contracts made in Malaysia on behalf of the Government shall, if reduced to writing, be made in the name of the Government of Malaysia and may be signed by a Minister, or by any public officer duly authorized in writing by a Minister either specially in any particular case, or generally for all contracts below a certain value in his department or otherwise as may be specified in the authorization."

37. As mentioned in paragraph 23, clause 1.5 of the Salvage Contract identifies the entities that fall within the meaning of the term "Government".

38. The absence of Ministry of International Trade and Industry from that definition further fortifies the Respondent's assertion that the Salvage Contract was not an "approved project" within the meaning of the IGA.

[4] Annex 86

39. The decision in **Philippe Gruslin v Malaysia ICSID Case No. ARB/99/3**[5] is on all fours with the instant case. A copy of the Award is annexed hereto. It is also available at http://ita.law.uvic.ca[6] while excerpts of the same are available at http://www.worldbank.org/icsid.[7]

40. Gruslin, a national of Belgium invested in Malaysian securities using a Luxembourg mutual fund. Subsequent exchange controls imposed by Malaysia allegedly destroyed the entire value of those securities. The bilateral investment treaty between Malaysia and Belgium defined investment broadly, including **"shares and other types of holding." However the definition was qualified by a proviso, that such assets would only constitute investments "provided that such assets when invested … are invested in a project classified as an 'approved project' by the appropriate Ministry in Malaysia …"** [8]

41. The Respondent argued that the additional condition of "approved project" was intended to limit the encouragement and protection of foreign investment made in Malaysia to investments in projects that contributed to the manufacturing and industrial capacity of Malaysia. Investments in Malaysian securities did not fall within that definition. Gruslin did not apply for characterization as an approved project. Evidence of interpretation and consistent application of that IGA similar to what is presented here was led. It was also argued that it would amount to a radical departure and derogation of the explicit requirements of that entire IGA.

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[5] Annex 87
[6] Annex 88
[7] Annex 89
[8] Annex 46 in Respondent's Memorial

42. The Tribunal agreed that it lacked jurisdiction for the reasons submitted. Regulatory approval of a project and not mere approval at some time of the general business activities of a corporation was required.

43. The above decision in **Philippe Gruslin** has often been cited by writers when discussing the definition of "investment" in IGAs. Writers[9] recognize the presence of limitations on this term. **M.Sornarajah[10]** in his book "**The International Law on Foreign Investment"** at **page 225** –

> "4.2.2 Limitation on the definition of investment
>
> Though investments are defined as widely as possible, many bilateral investment treaties confine the benefits of the treaty only to investments approved by the state parties to the treaty. **This limitation, at once, creates two categories of foreign investment originating from the same state party, one which is protected by the treaty because it is approved by the state party which receives the investment, and one which is not because it lacks such approval. Discrimination between investments is inherent in this situation**."

44. Malaysia is not the only country that confines the benefits of an IGA to only investments approved by the state parties to the treaty. According to **M. Sornarajah**[11] -

[9] Annex 90 - Noah Rubins & N. Stephen Kinsella in "International Investment, Political Risk and Dispute Resolution" – A Practitioner's Guide, Oceana Publications @ page 306
[10] Annex 55 in Respondent's Memorial
[11] ibid

> "This limitation is to be found in the treaties made by south-east Asian states. The treaties of Singapore and Malaysia contain the requirement that the investment must be approved for the purposes of I nvestment".

45. This is illustrated in the case of **Yaung Chi Oo Trading Pte Ltd v Government of the Union of Myanmar (2003) 42 ILM 540**.[12]

46. Under Article II (3) of the 1987 ASEAN Agreement the investment must be "specifically approved in writing and registered by the host country and upon such conditions as it deems fit for the purpose of this Agreement" before protection under the 1987 Agreement was available. The lack of such approval led to the arbitral tribunal similarly refusing jurisdiction.

47. For the reasons explained in the Respondent's Memorial on Objections to Jurisdiction the mandatory requirement in Article 1 (1) (b) (ii) of the IGA must be fulfilled. Since the Salvage Contract undertaken was not an approved project within the meaning of that Article the protection under the IGA is not available to the Claimant.

(iv) Pure Contractual Claim

48. The Claimant likens its claim to one within Article 2 (2) of the IGA [**pages 24 and 25 of the Claimant's Memorial**]. The Claimant asserts that Article 2 (2) contains an "umbrella clause" where breaches of the Salvage Contract

[12] Annex 91

can amount to treaty violations for which the Arbitral Tribunal can take jurisdiction. However, no justification for such proposition is offered by the Claimant.

49. The Respondent denies this and relies on the submissions set out at **pages 44 to 50 of the Respondent's Memorial on Objections to Jurisdiction**.

50. The Respondent submits that this proposition need not be considered because the Claimant has failed to fulfill the threshold requirements concerning "investments" and "approved projects" earlier discussed.

51. Article 2 of the IGA cannot be resorted to, to elevate a pure contractual claim into a treaty claim. Article 2 of the IGA reads as follows -

> "Article 2
> Promotion and Protection of Investment
>
> (2) Each Contracting Party shall encourage and create favourable conditions for nationals or companies of the other Contracting Party to invest capital in its territory, and, subject to its rights to exercise powers conferred by its laws, shall admit such capital.
>
> (3) Investments of national or companies of either Contracting Party shall at all times be accorded fair and equitable treatment and shall enjoy protection and security in the territory of the other Contracting Party. Neither Contracting Party shall in any way

> impair by unreasonable or discriminatory measure the management, maintenance, use, enjoyment or disposal of investments in its territory of nationals or companies of the other Contracting Party. **Each Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party**."

52. The Claimant is alleging that it is entitled to protection by virtue of Article 2(2) of the IGA in light of the express provision that –

> **"Each Contracting Party shall observe any obligation it may have entered into with regard to investments of nationals or companies of the other Contracting Party."**

53. The Claimant submits that the abovementioned provision amounts to an "umbrella clause".

54. The Respondent submits that generally, coverage of such a clause varies both in terms of the type of undertaking guaranteed and the relationship of that guarantee to investors and investments. The effect of an umbrella clause depends on the nature of the contractual rights in question and the text of the particular applicable clause. Some umbrella clauses are broad whilst others impose certain limitations.

55. The Respondent submits that in construing Article 2(2) of the IGA its plain meaning must be examined.

56. In **SGS Société Générale de Surveillance v Islamic Republic of Pakistan ICSID Case No. ARB01/03**[13] the Arbitral Tribunal was asked to consider the issue of umbrella clauses in the context of the Bilateral Investment Treaty between Pakistan and Switzerland (Swiss-Pakistan BIT) by virtue of the breach of the Pre-Shipment Inspection Agreement (PSI Agreement).

57. The "umbrella clause" in Article 11 of the Swiss-Pakistan BIT provided as follows -

> "Either Contracting Party shall constantly guarantee the observance of **the commitments it has entered into with respect to the investments** of the investors of the other Contracting Party."

58. The claimant [SGS] argued that the inclusion of an "umbrella clause" such as the Swiss-Pakistan BIT's Article 11 had the effect of elevating a simple breach of contract to a treaty claim under international law.

59. The Arbitral Tribunal held at paragraph 168 that –

> "168. The consequences of accepting the Claimant's reading of Article 11 of the BIT should be spelled out in some detail. Firstly, Article 11 would amount to incorporating by reference an unlimited number of State contracts, as well as other municipal law instruments setting out State

[13] Annex 56 in Respondent's Memorial

commitments including unilateral commitments to an investor of the other Contracting Party. Any alleged violation of those contracts and other instruments would be treated as a breach of the BIT. Secondly, the Claimant's view of Article 11 tends to make Article 3 to 7 of the BIT substantially superfluous. There would be no real need to demonstrate a violation of those substantive treaty standards if a simple breach of contract, or of municipal statute or regulation, by itself, would suffice to constitute a treaty violation on the part of a Contracting Party and engage the international responsibility of the Party. A third consequence would be that an investor may, at will, nullify any freely negotiated dispute settlement clause in a State contract. On the reading of Article 11 urged by the Claimant, the benefits of the dispute settlement provisions of a contract with a State also a party to a BIT, would flow only to the investor. For that investor could always defeat the State's invocation of the contractually specified forum, and render any mutually agreed procedure of dispute settlement, other than BIT-specified ICSID arbitration, a dead-letter, at the investor's choice. The investor would remain free to go to arbitration either under the contract or under the BIT. But the State party to the contract would be effectively precluded from proceeding to the arbitral forum specified in

> the contract unless the investor was minded to agree. The Tribunal considers that Article 11 of the BIT should be read in such a way as to enhance mutuality and balance of benefits in the inter-relation of different agreements located in differing legal orders."

60. In **SGS Société Générale de Surveillance S.A. v The Republic of the Philippines ICSID Case No. ARB02/06**[14] questions concerning an umbrella clause under the Swiss-Philippines BIT were raised. Article X(2) of the Swiss-Philippines BIT reads -

> "Each Contracting Party shall observe **any obligation it has assumed with regard to specific investments** in its territory by investors of the other Contracting Party."

61. It is critical to note that the arbitral tribunal in both cases mentioned above recognized that the subject matter of the contract constituted a form of "investment". For example in the latter case, the Arbitral Tribunal stated at **paragraph 29** –

> "...It is not disputed that SGS is potentially an investor of the other Contracting Party under the BIT: no issue of SGS's nationality or effective control is raised. Furthermore it is not denied by the Respondent that the services provided by SGS, itself or through its wholly-owned Swiss affiliates, and the resulting rights to payment are

[14] Annex 92

capable of constituting an investment. Under Article I(2) of the BIT, **the term "investments" is defined to include "**every kind of asset" including "(c) claims to money or to any performance **having an economic value"**."

62. In adopting a broad interpretation of umbrella clauses, the Arbitral Tribunal in **SGS v Philippines** stated that –

> "119. This provisional conclusion – that Article X(2) means what it says – is however contradicted by the decision of the Tribunal in SGS v. Pakistan, the only ICSID case which has so far directly ruled on the question. It should be noted that the "umbrella clause" in the Swiss-Pakistan BIT was formulated in different and rather vaguer terms than Article X(2) of the Swiss-Philippines BIT.
>
> ...
>
> Apart from the phrase "shall constantly guarantee" (what could an inconstant guarantee amount to?), the phrase "the commitments it has entered into with respect to the investments" is likewise less clear and categorical than the phrase "any obligation it has assumed with regard to specific investments in its territory" in Article X(2) of the Swiss-Philippines BIT."

63. Although the Arbitral Tribunal in **SGS v Philippines** found that the relevant umbrella clause made the breach a treaty breach nevertheless there was due regard given to obligations assumed by the host State to foreign investors for "specific investments" in connection with such contractual commitments. In **paragraphs 126 and 127**, the Tribunal stated as follows –

> "126. Moreover the SGS v. Pakistan Tribunal appears to have thought that the broad interpretation which it rejected would involve a full-scale internationalisation of domestic contracts—in effect, that it would convert investment contracts into treaties by way of what the Tribunal termed "instant transubstantiation". But this is not what Article X(2) of the Swiss-Philippines Treaty says. It does not convert non-binding domestic blandishments into binding international obligations. It does not convert questions of contract law into questions of treaty law. In particular it does not change the proper law of the CISS Agreement from the law of the Philippines to international law. Article X(2) addresses not the scope of the commitments entered into with regard to specific investments but the performance of these obligations, once they are ascertained. It is a conceivable function of a provision such as Article X(2) of the Swiss-Philippines BIT to provide assurances to foreign investors with regard to the performance of obligations assumed

by the host State under its own law with regard to specific investments—in effect, to help secure the rule of law in relation to investment protection. In the Tribunal's view, this is the proper interpretation of Article X(2).

127. To summarize, for present purposes Article X(2) includes commitments or obligations arising under contracts entered into by the host State. The basic obligation on the State in this case is the obligation to pay what is due under the contract, which is an obligation assumed with regard to the specific investment (the performance of services under the CISS Agreement). But this obligation does not mean that the determination of how much money the Philippines is obliged to pay becomes a treaty matter. The extent of the obligation is still governed by the contract, and it can only be determined by reference to the terms of the contract."

64. In **Joy Mining Machinery Limited v The Arab Republic of Egypt**[15] the Arbitral Tribunal stated in paragraphs 77 to 81 that -

"77. In *SGS v. Pakistan*, the Tribunal came to the conclusion that it did not have jurisdiction over contract claims "which do not also constitute or amount to breaches of

[15] Annex 54

the substantive standards of the BIT". In *SGS v The Philippines,* where contractual claim were more easily distinguishable from treaty claim, the Tribunal referred certain aspects of contractual claim to local jurisdiction while retaining jurisdiction over treaty-based claims. A further feature noted by the tribunals in these last two cases was that both treaties contained a broadly defined "umbrella clause".

78. In the present case the situation is rendered somewhat simpler by the fact that a bank guarantee is clearly a commercial element of the Contract. The Claimant's arguments to the effect that the non-release of the guarantee constitutes a violation of the Treaty are difficult to accept. In fact, the argument is not sustainable that a nationalization has taken place or that measures equivalent to an expropriation have been adopted by the Egyptian Government. Not only is there no taking of property involved in this matter, either directly or indirectly, but the guarantee is to be released as soon as the disputed performance under the Contract is settled. It is hardly possible to expropriate a contingent liability. Although normally a specific finding to this effect would pertain the merits, in this case not even the prima facie test would be met. The same holds true in respect of the argument concerning

the free transfer of funds and fair and equitable treatment and full protection and security.

79. **Disputes about the release of bank guarantees are a common occurrence in many jurisdictions and the fact that a State agency might be a party to the Contract involving a commercial transaction of this kind does not change its nature. It is still a commercial and contractual dispute to be settled as agreed to in the Contract, including the resort to arbitration if and when available. It is not transformed into an investment or an investment dispute.**"

80. There has been much argument regarding recent cases, notably SGS v. Pakistan and SGS v. Philippines. However, this Tribunal is not called upon the sit in judgment on the views of other tribunals. It is only called to decide this dispute in the light of its specific facts and the law, beginning with the jurisdictional objections.

81. In this context, **it could not be held that an umbrella clause inserted in the Treaty, and not very prominently, could have the effect of transforming all contract disputes into investment disputes under the Treaty, unless of course there would be a clear violation of the Treaty rights**

> **and obligations or a violation of contract rights of such a magnitude as to trigger the Treaty protection, which is not the case. The connection between the Contract and the Treaty is the missing link that prevents any such effect. <u>This might be perfectly different in other cases where that link is found to exist, but certainly it is not the case here</u>.**"

65. Notwithstanding the restrictive and broad interpretations of the umbrella clauses in the **SGS v Pakistan** and **SGS v Philippines**, this Arbitral Tribunal should interpret Article 2(2) of the IGA in the context of specific facts, language and provisions of the IGA. Article 2(2) of the IGA cannot be construed to automatically transform all contract disputes into investment disputes because it is in the nature of an "umbrella clause".

66. Superficially, the investment appears to fall under Article 1(1) (a) (iii) of the IGA as "claims to money or performance under contract having financial value". However, the term "investment" is restricted under Article 1(1) (b) (ii) to 'all investments made in projects classified by the appropriate Ministry of Malaysia in accordance with its legislation and administrative practice as an "approved project"'.

67. The Respondent maintains that the requisite "approved project" status has never been attained by the Claimant. This issue has been addressed in **paragraphs 64 to 90 of the Respondent's Memorial on Objections to Jurisdiction** and the Respondent repeats and adopts the submissions therein with regard to the conditions and

procedure for an “investment” to qualify as an “approved project” within the ambit of the IGA.

68. The Respondent submits that the Salvage Contract in dispute is a common service and contractual transaction in which a government entity is a party to. The fact that the Respondent is a party to a contract of this kind does not change the nature of the contract and will not transform the contract into an investment or an investment dispute.

69. As stated in **Joy Mining** the Claimant must also establish a link between the alleged breach of the Salvage Contract and the purported breach of the IGA. As a matter of law, a breach of the Salvage Contract does not amount to a breach of the IGA as one is subject to domestic law and the other international law.

70. The Respondent submits that the Tribunal should not undertake the responsibility of resolving a purely contractual dispute arising from a plain Salvage Contract that is not recognized by the host State as an investment under its domestic law and administrative practice. Indeed, the Tribunal must duly reflect on the intention of the parties at the time of the conclusion of the Salvage Contract. The intention clearly was to conclude an ordinary service contract. The parties did not set out to regard such a contract or arrangement to be an investment within the meaning of the IGA.

71. The Salvage Contract is ordinary and definitely falls short of an investment within the meaning of the IGA. The terms of this IGA cannot elevate all contractual claims to treaty claims under international law where such contractual

claims are beyond the spheres of domestic courts and tribunals.

72. The present dispute does not amount to a treaty-based breach. Rather it concerns a claim for breach of a simple service contract. In any event the Claimant has admitted that the Salvage Contract is a "Commercial Contract between "Government" and "Salvor" " – see Claimant's letter dated 18.7.1994 in **Exhibit P in Claimant's Memorial**.

73. Accordingly it is submitted that the Claimant's allegation that Article 2 (2) of the IGA elevates a mere contractual obligation to an international law obligation justiciable under the IGA is unfounded.

(v) Denial of Justice

74. First, the Respondent objects to the general, gratuitous and scandalous remarks made (**pages 15 to 20 of the Claimant's Memorial** and the accompanying exhibits, **Exhibit F in the Claimant's Request dated 30.9.2004** and **Annex 23 in the Respondent's Memorial on Objections to Jurisdiction**) and the aspersions cast on the Judiciary and the judicial system of Malaysia. Such remarks are furthermore irrelevant. Winning and losing claims before any court of law is common place and is never a reflection of the integrity of any legal system, including that of Malaysia's.

75. Specifically the Respondent refers to **footnote 4 at page 19 of the Claimant's Memorial**. The Claimant says that the then Minister of Legal Affairs "admitted the many

shortcomings of the legal system" - **Exhibit I in the Claimant's Memorial**, a copy of a keynote address by the said Minister at the Inaugural International Conference on Arbitration on 28.2.2003 was used in support. The Respondent disputes this. **Pages 6 and 7 of Exhibit I** touches on the general issue of misconduct of arbitrators, a problem not in the least peculiar to any country. The Minister's references to decisions of the Malaysian courts illustrate the vigilance and significant role played by the Malaysian courts in the Respondent's legal system in checking misconduct of arbitrators. This clearly disproves the Claimant's allegations against the Malaysian legal system.

76. In the Introduction and the Summary of Relevant Background Facts [**pages 3 to 26 of the Claimant's Memorial**] the Claimant seeks to lay out the facts and reasoning on the allegation of denial of justice.

77. The Respondent denies that there has ever been any denial of justice. The Respondent relies on **Pages 51 – 75 of the Respondent's Memorial on Objections to Jurisdiction** in reply to this.

78. Nevertheless, for completeness, the Claimant's allegations relating to the deficiencies of the arbitration proceedings shall be addressed below.

- ***Arbitration under the KLRCA***

79. Clause 32 of the Salvage Contract provides for a dispute resolution mechanism in order to resolve differences between the parties by way of arbitration. On 27.5.1996, by

a **CONSENT ORDER** and not an *ex parte* order, the Claimant and the Respondent entered into a "new" adhoc Arbitration Agreement wherein it was agreed that the arbitration would be conducted in accordance with the Rules of the Kuala Lumpur Regional Centre for Arbitration (KLRCA) and the UNCITRAL Arbitration Rules 1976.

80. When the Claimant elected to arbitrate under the Rules of KLRCA and the UNCITRAL Arbitration Rules 1976 it was an independent and voluntary decision on its part with the benefit of legal advice from its Malaysian solicitors.

- ***Appointment of Mr. Justice (Rtd) Richard Talalla***

81. The Consent Order dated 27.5.1996 vested power in the Director of the KLRCA to appoint the sole arbitrator. The Director of the KLRCA then appointed Mr. Justice (Rtd) Richard Talalla as the sole arbitrator.

82. It should be noted that the Claimant did not object to the appointment of Mr. Justice (Rtd) Richard Talalla as the sole arbitrator at that time. It was only after the Claimant failed in its claim that he questioned the competence of Mr. Justice (Rtd) Richard Talalla as an arbitrator.

83. In the light of the above, the Respondent submits that -

(a) The variation of the agreement to arbitrate was premised on the legal advice rendered by the Claimant's solicitors. The Claimant elected to adopt this advice and cannot now blame the Respondent

and/or the Malaysian judiciary for its subsequent failure to succeed in the arbitration proceedings;

(b) The appointment of Mr. Justice (Rtd) Richard Talalla was made in accordance with the terms of the Consent Order dated 27.5.1996. The Director of the KLRCA was vested with the power to appoint the said arbitrator. This was not a decision made on an *ex parte* basis by the Director of the KLRCA;

(c) The KLRCA is not an organ of the Respondent. It is an entirely independent body;

(d) The Claimant did not challenge the appointment of Mr. Justice (Rtd) Richard Talalla from the outset.

- ***The Arbitration Award***

84. The Claimant submits that the Arbitration Award handed down by Mr. Justice (Rtd) Richard Talalla was defective, as the Arbitrator did not give reasons for his decision.

85. It is an undisputed fact that the Claimant despite having had the benefit of legal advice chose not to apply for a correction of the Arbitration Award pursuant to Article 37 of the Rules of KLRCA.

86. Article 37 of the Rules of the KLRCA expressly provides that -

"**Additional Award**
Article 37

1. Within thirty days after the receipt of the award, either party, with notice to the other party, may request the arbitral tribunal to make an additional award as to claims presented in the arbitral proceedings but omitted from the award.

2. If the arbitral tribunal considers the request for an additional award to be justified and considers that the omission can be rectified without any further hearings or evidence, it shall complete its award within sixty days after the receipt of the request.

3. When an additional award is made, the provisions of Article 32, para 2 to 7, shall apply."

87. The failure on the part of the Claimant to seek to remedy this purported defect in the Arbitral Award cannot now be remedied by seeking to re-litigate this matter before this Arbitral Tribunal.

88. The simple fact of the matter is that the Claimant had various legal remedies available to it in Malaysia, but the Claimant chose not to exercise such remedies.

89. The Respondent ought not to be blamed for the Claimant and/or its legal adviser's failings as stated in the Respondent's Memorial on Objections to Jurisdiction.

- ***Review of the Award by the KLRCA***

90. The Director of the KLRCA has no power to review the Arbitration Award under the Rules of the KLRCA. This is evidenced by -

    (a) The lack of an express power to review within the provisions of the Rules of the KLRCA; and

    (b) The letters from the Director of the KLRCA to the Claimant dated 6.7.1999 and 16.7.1999 **[See Claimant's Exhibit F]**.

91. By letter dated 16.7.1999 the Director of the KLRCA expressly informed the Claimant the following:

> "**You have acknowledged that I do not have the authority to overturn the Award. Neither do I have the authority to initiate as Director a formal investigation of the Award and to answer each of your criticisms as you request. The Rules do not empower me to do so, and I cannot go out of my way to act otherwise**.
>
> In every arbitration there is a winner and a loser. As an aggrieved party you took such legal measures as were available to you to set aside the Award and they were unsuccessful. **The Centre cannot be arrogating to itself the functions of the Court to investigate the merits of the Award, which I would be doing if I were to answer each of your criticisms. You have also lodged your complaints with the CIARB in London and you**

> **now seek to involve the Centre as well in your quest to attack the arbitrator. The Centre cannot be a party to this, or act in any way which will put its neutrality at risk**."

92. As such, the KLRCA had no power to review the Arbitration Award. The only recourse available to the Claimant was to seek to set-aside the Arbitration Award before the High Court, provided the Claimant satisfied the requirements of sections 23 and 24 of the Arbitration Act 1952.

- ***Conduct of Proceedings before the High Court***

93. At **page 16 of the Claimant's Memorial on Jurisdiction** the Claimant asserts that it was not given a fair hearing by Mr. Justice Dato' Abdul Azmel bin Haji Ma'amor. The Respondent submits that such an allegation is entirely baseless and devoid of merit.

94. This reasoning is premised on the conduct of proceedings before the High Court, which has been set out in full at **paragraph 31 of the Respondent's Memorial on its Objection to Jurisdiction**.

95. Despite the prejudicial language of the Claimant relating to the Court proceedings, from the records furnished this Arbitral Tribunal will see that actually the Court had the benefit of extensive written submissions from **all parties** before it came to a decision.

96. For completeness, the material events are reproduced below -

(a) On **11.8.1998** the Claimant filed an application in the Kuala Lumpur High Court to set aside the Award or to remit the matter back to the Arbitrator pursuant to the provisions of the Malaysian Arbitration Act 1952;

(b) On **7.9.1998** the Respondent filed its affidavit in reply;

(c) On **23.9.1998** Court proceedings were adjourned as the Claimant changed solicitors from Messrs Azman Davidson & Co to Messrs Karpal Singh & Co;

(d) On **23.9.1998** the Court directed that -

- The Claimant to file written submissions within 3 weeks from the said date;
- The Respondent file its written submission in reply within 3 weeks thereafter;
- The Claimant file its written submission in reply within 1 week thereafter.

(e) On **29.10.1998** the Claimant wrote to the Court and requested a further 2 weeks to file its written submissions;

(f) On **2.11.1998** the Court granted the Claimant's request;

(g) On **18.11.1998**, the Claimant filed its written submission;

(h) On **22.12.1998**, the Respondent filed its written submission in reply;

(i) On **4.2.1999**, the Learned Judge having considered the written submissions before it ordered that the Claimant's application be dismissed with costs.

97. Insofar as the Claimant's allegation that Mr. Francis Ball was not permitted to be heard, it is submitted that as a matter of court procedure in Malaysia and for that matter anywhere in the common law world, once a litigant has a legal representative appearing in the court, the litigant is generally not permitted to address the court. The rights of audience are further generally restricted to the advocates and solicitors of the Malaysian Bar. In this instance, Mr. Gobind Singh Deo represented the Claimant and as Counsel for the Claimant only he had a right of audience.

98. In the light of the above, the Claimant is wrong in alleging that it was not given a fair hearing.

99. The learned Judge gave an oral decision and would have to give his written grounds of judgment if the Claimant had appealed to the Court of Appeal, or if a request for one had been made.

100. The Respondent has clearly shown that there has been nothing close to what may be said to be a denial of justice. The records of the various proceedings before the Sole Arbitrator as well as the Malaysian Courts speak for themselves.

101. Once again the Respondent submits that the purpose of ICSID arbitrations including the current case surely cannot be to relitigate a settled dispute. ICSID Arbitration is not a plenary appellate forum to review decisions of national courts of States. That would certainly run foul of the spirit of the ICSID Convention.

(vi) Exhaustion of Domestic Remedies

- **The Pursuit of Local Remedies through the Claimant's complaints to the various Ministers of the Respondent, Ambassadors, High Commissioners, the Queen of England and other persons**

102. At **pages 16 to 20 of the Claimant's Memorial on Jurisdiction** the Claimant states that it has exhausted its domestic remedies by virtue of the following -

(a) A meeting with the Minister of Culture and Tourism on 17.3.1999;

(b) A letter of complaint to the then Prime Minister of Malaysia dated 15.12.1998;

(c) A letter of complaint to Datin Seri Dr. Siti Hasmah, the wife to the then Prime Minister of Malaysia dated 20.11.1998;

(d) A letter of complaint to the Minister of Special Functions dated 19.11.1998;

(e) A letter of complaint to the Malaysian International Chamber of Commerce 22.6.1999;

(f) Voiced its dissatisfaction with the Minister of Law;

(g) A letter of complaint to the US-ASEAN Business Council in Washington D.C., USA dated 22.6.1999;

(h) A letter of complaint to Queen Elizabeth II dated 16.8.1998;

(i) A letter of complaint to the British High Commissioner to Malaysia dated 16.8.1998.

[See Claimant's Exhibits G, H and J]

103. The fact that the Respondent's Ministers did not accede to the Claimant's request to interfere in the affairs of the Malaysian Judiciary is evidence of the fact that the Malaysian Judiciary is an independent body, separate and distinct from the Executive. The doctrine of separation of powers operates and is very much alive in Malaysia.

104. The Respondent submits that the details surrounding the attempts to refer this dispute to the Cabinet Ministers, diplomats and even the Queen of England are not relevant to the Claimant's assertion that it has –

(a) been denied justice; and
(b) exhausted its domestic remedies within Malaysia.

- ***Conduct of Disciplinary Proceedings by the Chartered Institute of Arbitrators (CIARB)***

105. At **pages 20 and 21 of the Claimant's Memorial on Jurisdiction**, the Claimant refers to the referral of Mr. Justice (Rtd) Richard Talalla to the CIARB for an internal review to be held in relation to the arbitrator's conduct during the arbitration proceedings in Malaysia "In its further search for some semblance of justice, due process, and fairness in Malaysia".

106. The Claimant submits that as a result of the findings of the CIARB that Mr. Justice (Rtd) Richard Talalla had not misconducted himself during the course of the arbitration proceedings, "this proceeding exhausted viable legal and other remedies available to MHS in Malaysia".

107. At this point the Respondent specifically refers to the **Claimant's Bundle of Documents Vol. 1 at Exhibit J**. There are actually 4 separate documents in this exhibit. The latter two of these documents are incomplete whilst the authenticity of the last purported 'handwritten note' is also questioned. Opportunity must be afforded to the Respondent to address these documents in the event the complete text is made available. In any event the Respondent submits that the last document should be disregarded.

108. This issue has been addressed in **paragraphs 182 to 194 of the Respondent's Memorial on Objection to Jurisdiction**. The Respondent intends to repeat and adopt the submissions therein in reply to the Claimant's arguments herein.

109. The Respondent further submits that the Claimant's arguments herein are flawed. This reasoning is premised on the following grounds:

(a) CIARB informed the Claimant by letter dated 10.1.2001 that the Disciplinary Tribunal of the CIARB found that the charges brought against Mr. Justice (Rtd) Richard Talalla were not proved and accordingly dismissed the matter.

(b) CIARB's subsequent letter dated 18.6.2002 to the Claimant [**See Claimant's Bundle of Documents Vol. 1 at Exhibit J]*** stated -

> "2. **The Institute made it entirely clear to you at the outset, and upon receipt of your complaint, that by investigating your complaint against Mr. Talalla it was not capable of changing the outcome of the final award or otherwise interfering with the consequences of the award. Only a court of law is capable of opening up an arbitral award**. The Institute was however capable of investigating your complaint against Mr. Talalla in the light of its powers set out in the Charter, the Bye-laws and the Schedule to the Bye-laws, in accordance with the definition of professional misconduct (Bye-law 15). **The Professional Conduct Committee was only able to investigate whether Mr. Talalla, by virtue of his**

membership of the Institute had misconducted himself."

[* The Respondent observes that this letter is incomplete]

(c) The Claimant failed and/or neglected to exercise its right of appeal to the Court of Appeal against the decision of Mr. Justice Dato' Abdul Azmel bin Haji Ma'amor in dismissing the Claimant's application to set aside the Arbitration Award; and

(d) The referral of Mr. Justice (Rtd) Richard Talalla to the CIARB and its Disciplinary Tribunal does not amount to an exhaustion of internal remedies.

110. The Respondent submits that such conduct on the part of the Claimant in no way amounts to an exhaustion of domestic remedies. The final conclusive remedy available was to pursue an appeal to the Court of Appeal and ultimately to the Federal Court of Malaysia and the Claimant failed to exhaust them.

Ancillary Issues

- **"Fork-in-the-Road" Argument**

111. In the submissions on the several issues as identified by the Respondent, the Claimant has contended that its right to litigate a claim under the IGA can be exercised independently of any rights asserted under the Salvage Contract. This is commonly known as the "fork-in-the-road" argument.

112. The Claimant has sought to rely on two decisions, namely -

(a) **Azurix Corp v The Argentine Republic ICSID Case No. ARB/01/12**[16]; and

(b) **Salini Costruttori S.P.A. and Italstrade S.P.A. v Kingdom of Morocco ICSID Case No. ARB/00/4**.[17]

113. The Respondent submits that these two decisions do not support the Claimant's case.

114. In **Azurix Corp v The Argentine Republic** the Province of Buenos Aires (Province) commenced the privatization of the services of Administracion General de Obras Sanitarias de la Provincia de Buenos Aires (AGOSBA) in 1996. The AGOSBA was responsible for the provision of potable water and sewerage service in the Province. The Province passed Law 11.820 to create a regulatory framework for the privatization of the AGOSBA's services. As part of this regulatory framework, the future operator of the water services would be regulated by a new regulatory body known as Organismo Regulador de Aguas Bonaerense (ORAB).

115. The bid offer was made by two companies of the Azurix Group of Companies established for this specific purpose, i.e., Azurix AGOSBA S.R.L. (AAS) and Operadora de Buenos Aires S.R.L. (OBA). AAS and OBA are indirect subsidiary companies of Azurix. AAS was registered in Argentina and is 0.1% owned by Azurix Argentina Holdings

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Inc., which in turn was 100% owned by Azurix. OBA, was also registered in Argentina and was 100% owned by Azurix Agosba Limited, which in turn was 100% owned by Azurix Agosba Holdings Limited. Azurix owns a 100% of the shares in Azurix Agosba Holdings Limited.

116. Both AAS and OBA succeeded in securing the contract to manage the water services in the Province. On 19.9.2001, Azurix filed its request for arbitration before ICSID on the grounds that The Argentine Republic had breached the terms of the 1991 Treaty Concerning the Reciprocal Encouragement and Protection of Investment between the Argentine Republic and the United States of America.

117. The Argentine Republic took out two procedural objections, the second of which bears consideration. The Argentine Republic argued that the ICSID Tribunal had no jurisdiction premised on the "fork-in-the-road" argument as the alter ego of Azurix, i.e. ABA had elected under the relevant provisions of the 1991 Treaty Concerning the Reciprocal Encouragement and Protection of Investment between the Argentine Republic and the United States of America to submit the dispute between parties to the jurisdiction of the local court of the Argentine Republic by proceedings with judicial review and legal proceedings in the Argentine Republic. The Arbitral Tribunal dismissed the Argentine Republic's objection to jurisdiction.

118. In reaching its decision, the Arbitral Tribunal reasoned that –

(a) The parties to the proceedings in Argentina were different from those present before the Arbitral

Tribunal. ABA had filed an action against the Province, whilst the parties before the Arbitral Tribunal were Azurix and the Argentine Republic; and

(b) ORAB is not equivalent to an administrative tribunal for the purposes of the 1991 Treaty Concerning the Reciprocal Encouragement and Protection of Investment between the Argentine Republic and the United States of America.

119. The Respondent submits that the facts and the reasoning of the Arbitral Tribunal in **Azurix Corp v The Argentine Republic** are inapplicable in this instance for the following reasons –

(a) There is no party identity crisis as the parties before this Arbitral Tribunal are identical to the parties before the arbitration proceedings and the court proceedings in Malaysia;

(b) Unlike the ORAB, the High Court of Malaya does have the independence required of a tribunal and does have a judicial function to settle conflicts; and

(c) Unlike the ORAB, the High Court of Malaya is a judicial organ of the Malaysian Judiciary.

120. In fact, the decision of the Arbitral Tribunal in **Azurix Corp v The Argentine Republic** assists the Respondent in that it has narrowed the preclusive effect of the “fork-in-the-road” doctrine.

121. The effect of this decision is that the Claimant cannot simply elect to rely on remedies available under international law where –

(a) the parties are the same;
(b) the subject matter of the dispute is the same; and
(c) legal proceedings have been instituted in the local court,

122. In respect of the **Salini Costruttori S.P.A. and Italstrade S.P.A. v Kingdom of Morocco** this decision can be distinguished on the basis of the terms of the applicable IGA.

123. Article 8 in the Bilateral Treaty between Italy and Morocco provides as follows:

> ”1) All disputes or differences, including disputes related to the amount of compensation due in the event of expropriation, nationalization, or similar measures, between a Contracting Party and an investor of the other Contracting Party concerning an investment of the said investor on the territory of the first Contracting Party should, if possible, be resolved amicably.
>
> 2) If the disputes cannot be resolved in an amicable manner within six months of the date of the request, presented in writing, the investor in question may submit the dispute either:
>
> a. to the competent court of the Contracting Party concerned;

b. to an ad hoc tribunal in accordance with the Arbitration Rules of the UN Commission on International Trade Law;

c. to the International Centre for Settlement of Investment Disputes (ICSID), for the application of the arbitration procedures provided by the Washington Convention of March 18, 1965 on the settlement of investment disputes between States and nationals of other States.

3) The two Contracting Parties shall refrain from handling, through diplomatic channels, all questions pertaining to an arbitration or to pending legal proceedings, as long as these proceedings have not come to an end and that one of the said Parties has not complied with the judgment of the arbitral tribunal or the designated ordinary court, within the term for enforcement fixed by the judgment or to be otherwise established, on the basis of the rules of international or national law applicable in the case."

124. The IGA entered into between the United Kingdom and Malaysia does not have a provision similar to Article 8 of the BIT entered into between Italy and Morocco. The provision of Article 8 in the **Salini Costruttori S.P.A. and Italstrade S.P.A. v Kingdom of Morocco** case gives the Claimant a choice as to whether the Claimant wishes to submit the dispute to the competent court of the contracting party or to an ICSID arbitration.

125. There is no equivalent provision in the IGA. It is therefore submitted that the Claimant must, in the circumstances, exhaust the legal remedies by filing an appeal to the Malaysian Court of Appeal from the decision of the High Court.

126. It is therefore submitted that the decision in **Salini Costruttori S.P.A. and Italstrade S.P.A. v Kingdom of Morocco** does not in any way assist the Claimant in its arguments.

127. Due consideration should also be given to the views of **Jan Paulsson** in his book **Denial of Justice in International Law**[18] at **page 129** wherein he states that -

> "**Claims properly initiated before a national court or an arbitral tribunal established by contract fall to be decided by that court or tribunal. Whatever international jurisdiction that may be available under a treaty would not, absent unusual circumstances, be in a position to hear such claims. They include claims of denial of justice provided that their 'essential basis' has been set forth as part of the cause of action.**
>
> But that will not be so in the more likely case that the alleged denial of justice takes place in the course of the action before such a court or

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contractually stipulated arbitral tribunal. The claimant was by definition ignorant of a wrong which had not occurred at the time the complaint was formulated."

128. For the reasons mentioned above, it is submitted that the Claimant is wrong in law and on the facts to rely on the "fork-in-the-road" argument in arguing that this Arbitral Tribunal has jurisdiction. It is an undisputed fact that the Claimant chose to exercise the domestic remedies available to it in Malaysia but failed to exhaust those remedies. Moreover, the Claimant has failed to establish that there is a systemic failure within the Malaysian legal system in exercising justice. On the other hand, the Respondent has shown the contrary to be the correct position.

- **Expropriation**

129. Article 4 of the IGA which is relevant in this regard reads as follows:

"**Article 4**
Expropriation

(1) Investments of nationals or companies of either Contracting Party should not be nationalized, expropriated or subjected to measures having effect equivalent to nationalization or expropriation in the territory of the other Contracting Party except for a public purpose related to the internal needs of the expropriating Party and against prompt, adequate and effective

compensation. Such compensation shall amount to the value of the investment expropriated immediately before the expropriation or impending expropriation became public knowledge and shall be freely transferable. The legality of any such expropriation and the amount of compensation shall be determined by due process of law in the territory of the Contracting Party in which the investment has been expropriated.

(2) Where a Contracting Party expropriates the assets of a company which is incorporated or constituted under the law in force in any part of its own territory, and in which nationals or companies of the other Contracting Party own shares, it shall ensure that the provisions of paragraph (1) of this Article are applied to the extent necessary in respect of the shareholders of such a company."

130. In international law, the term "expropriation" is commonly defined as "the taking by a host state of property owned by a foreign investor and located in the host State".[19]

131. Expropriation may accompany a breach of a State contract wherein the State not only openly and deliberately takes property by way of outright seizure or formal or obligatory transfer of title in favour of the host State but also by covet or incidental interference with the use of the property. Such taking of property has the effect of depriving the owner of

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the said property the use or any economic benefit of the property. However, the concept of a breach of contract and the issue of expropriation are distinct.

132. In **Waste Management Inc v United Mexican States ICSID Case No. ARB (AF) 00/3**[20] the Arbitral Tribunal had occasion to examine the question of whether there was conduct amounting to an expropriation of the claimant's contract rights.

133. In addressing this question the arbitral tribunal held -

> "174. Thirdly, there is the much smaller group of cases where the only right affected is incorporeal; these come closest to the present claim of contractual non-performance [...]. In such cases, simply to assert that "property rights are created under and by virtue of the contract "is not sufficient. **There mere non-performance of contractual obligation is not to be equated with a taking of property, nor (unless accompanied by other elements) is it tantamount to expropriation. Any private party can fail to perform its contracts, whereas nationalisation and expropriation are inherently governmental acts, as is envisaged by the use of term "measure" in Article 1110(1). It is true that, having regard to the inclusive definition of "measure", one could envisage conduct tantamount to an expropriation which consisted of acts and omissions not specifically or exclusively governmental. All the same, the**

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normal response by an investor faced with a breach of contract by its governmental counter-party (the breach not taking the form of an exercise of governmental prerogative, such as a legislative decree) is to sue in the appropriate court to remedy the breach. It is only where such access is legally or practically foreclosed that the breach could amount to a definitive denial of the right (i.e. the effective taking of the chose in action) and the protection of Article 1110 be called into play.

175. The Tribunal concludes that it is one thing to expropriate a right under a contract and another to fail to comply with the contract. **Non-compliance by a government with contractual obligation is not the same thing as, or equivalent or tantamount to, an expropriation. In the present case the Claimant did not lose its contractual rights, which it was free to pursue before the contractually chosen forum. The law of breach of contract is not secreted in the interstices of Article 1110 of NAFTA. Rather it is necessary to show an effective repudiation of the right, unredressed by any remedies available to the Claimant, which has the effect of preventing its exercise entirely or to a substantial extent**."

134. Similarly, in **Impregilo S.p.A. v Islamic Republic of Pakistan ICSID Case No. ARB/03/3**[21]. In addressing the Impregilo S.p.A's claim that the Islamic Republic of Pakistan had committed acts equivalent to expropriation

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under Article 5(2) of the BIT between Pakistan and Italy the Arbitral Tribunal held -

> "278. The tribunal observes that in those two cases, the measures in question had a unilateral character and were taken by a State or a Province acting in the exercise of its sovereign authority ("puissance publique") and not as a contracting party. Indeed, all the key decisions relating to indirect expropriation mention the "interference" of the Host State in the normal exercise, by the investor, of its economic rights. **However, a Host State acting as a contracting party does not "interfere" with a contract; it "performs" it. If it performs the contract badly, this will not result in a breach of the provisions of the Treaty relating to the expropriation or nationalisation, unless it be proved that the State or its emanation has gone beyond its role as a mere party to the contract, and has exercised the specific functions of a sovereign authority.**
>
> 279. **Moreover, the effect of the measures taken must be of such importance that those measures can be considered as having an effect equivalent to expropriation.**
>
> 280. In the present case, Impregilo complains that Pakistan's conduct throughout the duration of the Project constituted an effective

expropriation of its investment, including its rights under the Contracts. It alleges that the actions of Pakistan and WAPDA frustrated its ability to carry out and complete the work in a timely fashion, thereby preventing the realisation of the benefit of the investment. Further it alleges that WAPDA and Pakistan frustrated the contractual dispute resolution mechanism and Impregilo's right to an impartial hearing and settlement of its claims, thereby again preventing the realisation of the value of the investment. According to Impregilo, Article 5 of the BIT has therefore been violated by Pakistan.

281. **Following the analysis above, it is the Tribunal's view that only measures taken by Pakistan in the exercise of its sovereign power ("puissance publique"), and not decision taken in the implementation or performance of the Contracts, may be considered as having an effect equivalent to expropriation. Therefore, the Tribunal has jurisdiction only to consider the former, and not the latter, for the purpose of Article 5 of the BIT**."

135. The Respondent submits that the conclusions of the Tribunals mentioned above are applicable in this instance. This is premised on the following grounds:

a. The Salvage Contract by construction is a service contract, wherein the Claimant is paid for service rendered, that is, salvaging the “DIANA” wreck;

b. Pursuant to Clause 4 of the Salvage Contract, as part of its payment, the Claimant is entitled to a fee from the auction of certain valuable findings;

c. Pursuant to Clause 17 of the Salvage Contract, the Claimant is **NOT** entitled to actual possession of the finds from the “DIANA” wreck as the finds are the property of the Respondent; and

d. The Claimant has failed to show any instances where the Respondent expropriated the Claimant’s “investment”. The Respondent in carrying out its obligations under the Salvage Contract acted in its capacity as a contracting party and not as a sovereign authority taking **unilateral measures** amounting to expropriation.

136. The Respondent further submits that this is purely an attempt on the part of the Claimant to transform what is in essence a pure contractual claim to a treaty claim falling within the IGA.

137. In the light of the above, the Respondent submits that the Claimant's allegation and argument that there has been an expropriation of the Claimant's funds is totally unfounded and misplaced. The Arbitral Tribunal is urged to disregard this argument.

- **Legal Dispute**

138. The Claimant raises this at **page 27 of the Claimant's Memorial on Jurisdiction**.

139. The Respondent has at all times submitted that in order for the Arbitral Tribunal to take jurisdiction and be competent to hear this claim the conditions prescribed under Article 25 of the ICSID Convention and Articles 1 and 7 of the IGA must be satisfied.

140. Allegations neither confer jurisdiction nor competence. A claim is only justiciable as a legal dispute if it arises directly out of an investment within the meaning within the ambit of the ICSID Convention and the IGA. This legal dispute, which is denied, does not arise out of an investment in an "approved project" for the multitude of reasons already discussed above and in the Respondent's Memorial on Objections to Jurisdiction.

D. CONCLUSION

141. The **Claimant's Memorial on Jurisdiction** has not raised any viable doubts or responses to any of the issues identified in support of the grounds of objections against the Arbitral Tribunal's jurisdiction and competence.

142. On the contrary the Respondent submits that the Claimant's Memorial to Objections supports and fortifies those objections of the Respondent.

143. Over and above the submissions earlier set out above and in the Respondent's Memorial on Objections to Jurisdiction the Respondent submits –

(a) The Salvage Contract is a service contract and does not amount to an "investment" within the meaning of Article 1 of the IGA. Even if it amounts to an "investment" (which is denied) it is not an "approved project";

(b) Article 2(2) of the IGA is not an umbrella clause;

(c) In any event the Claimant's arguments on "umbrella clause" must fall because the investment in the Salvage Contract is not an investment in an approved project. There is no requisite link between the alleged breach of the Salvage Contract with the purported breach of the IGA. Applying a broad interpretation will only bring serious and disastrous consequences;

(c) The Respondent has not expropriated the Claimant's monies and/or breached the provisions of Article 4 of the IGA;

(d) The Claimant has not exhausted all domestic or local remedies available to it in Malaysia in respect of the conduct of the arbitration proceedings and/or the proceedings before the Malaysian Courts;

(e) The Claimant has failed to disclose any evidence of a systemic trend of denial of justice in Malaysia;

(f) The references to the various Cabinet Ministers, diplomats and other organizations do not amount to –

- evidence of a systemic denial of justice prevalent within the Malaysian Courts; and
- the exhaustion of the legal remedies available to the Claimant in Malaysia;

(g) The "fork-in-the-road" argument does not apply as the Claimant elected not to exercise the remedies available to it domestically;

(h) The Claimant's documents in fact show a systemic and persistent intent of nothing else but rearbitrating a claim which has already been finally settled – see letter dated 19.11.1998 in **Exhibit G**; seven letters dated 6.2.2001, 28.11.2002, 15.3.2000, 20.9.2001 (to the Prime Minister of Malaysia), 15.9.2001, 20.9.2001

(to the Chief Justice of the Federal Court, Malaysia), 20.9.2001 (to the Minister in the Prime Minister's Department) all in **Exhibit H in the Claimant's Memorial**.

144. The Respondent reiterates that -

i. The Claimant has **NO** *locus standi* to institute arbitral proceedings under the ICSID Convention and/or IGA;

ii. The Salvage Contract between the Claimant and the Respondent **DOES NOT AMOUNT TO AN "INVESTMENT"** within the meaning of Article 1 and Article 7 of the IGA read together with Article 25(1) of the ICSID Convention;

iii. The Salvage Contract is **NOT AN "APPROVED PROJECT**";

iv. The dispute between parties is **PURELY CONTRACTUAL** and **NOT WITHIN** the jurisdiction of the Arbitral Tribunal;

v. The Claimant's allegation that it has been denied justice is baseless;

vi. The Claimant **DID NOT EXHAUST** all domestic or local remedies available to it in Malaysia.

145. Accordingly, this Arbitral Tribunal has **NO** jurisdiction or competence to determine this dispute.

146. Wherefore, the Respondent requests that the Arbitral Tribunal:

(a) Declare that the Claimant's claim does not fall within the jurisdiction and competence of ICSID or of the Arbitral Tribunal; and

(b) Order the Claimant to pay the Respondent all costs reasonably incurred in by the latter in connection with these proceedings.

Dated the 19th day of April 2006

COUNSEL FOR THE RESPONDENT

TAN SRI ABDUL GANI BIN PATAIL
ATTORNEY GENERAL, MALAYSIA

(With him: Dato' Umi Kalthum Bte Abdul Majid
Dato' Mary Lim Thiam Suan
Mr. Kamaludin Bin Md. Said
Dato' K.C. Vohrah
Dato' Cecil Abraham
Mrs. Mahiran Bte Md. Isa
Mrs. Aliza Bte Sulaiman
Mr. Mohammad Al-Saifi Bin Haji Hashim
Mrs. Chandra Devi Letchumanan
Mr. Mohd. Taufik Bin Mohd. Yusoff)

The **Respondent's Reply Memorial on Objections to Jurisdiction** is filed by the Attorney General's Chambers of Malaysia, Solicitors for the Respondent, whose address for service is at the Civil Division, Level 3, Block C3, Federal Government Administrative Centre, 62512 Putrajaya, Malaysia.

[Ref: JPN(S) 152/185/113 Tel: 03-88855000 Fax: 03-88889369]