APPENDIX D

BEFORE THE INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

ICSID Case No. ARB/98/8

TANZANIA ELECTRIC SUPPLY COMPANY LIMITED

Claimant

-and-

INDEPENDENT POWER TANZANIA LIMITED

Respondent

DECISION ON ALL FURTHER REMAINING ISSUES

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1. In our Decision on Tariff and other Remaining Issues dated 9 February 2001, which followed the submission of detailed written Memorials and oral submissions from both parties, the Tribunal considered and determined a number of issues, including, in particular:

   What, if any, adjustments should be made to the Reference Tariff stated in the PPA?

2. We considered this issue in Part 11 (paragraphs 164 to 166), in which we recorded our understanding that, by the time of the last exchanges between the parties, they were confident that, armed with the appropriate adjustments to take account of the specific matters referred to us, they would be able to agree on the application of the financial model and the tariff which should be derived as a consequence. However, although our Decision was intended and expressed to be final in relation to those issues with which we had dealt, we gave the parties the opportunity to make further application to the Tribunal if such agreement was not reached.

3. Following the publication of our Decision, TANESCO raised a number of further matters going to the calculation of the Reference Tariff.

4. Further, in Part 12 of our Decision (paragraphs 167 to 168), the Tribunal recorded its understanding that both parties were agreed that, once the appropriate figures to be fed into the financial model had been ascertained so that the initial Reference Tariff could be calculated, steps should be taken to bring about the commencement of commercial operations. We noted that neither party had addressed the question of how much time would be required for this purpose, and therefore restricted ourselves at that stage to ordering the parties to co-operate in taking whatever steps would be necessary to achieve the commencement of commercial operations as soon as reasonably practicable.

5. Following the publication of our Decision, IPTL invited the Tribunal to fix a date by which the commencement of commercial operations should be achieved.

6. Written Memorials and Reply Memorials were then submitted sequentially on behalf of the parties as follows:

TANESECO's "Memorial Regarding Remaining Tariff Issues" dated 26 March 2001;

IPTL's "Memorial Regarding Remaining Tariff Issues" dated 2 April 2001;

TANESCO's "Reply Memorial Regarding Remaining Tariff Issues" dated 16 April 2001;

IPTL's "Reply Regarding Remaining Tariff Issues" dated 20 April 2001.

TANESCO submitted further evidence in the form of the Sixth and Seventh Witness Statements of Dr Martin C Swales and the Second Witness Statement of Mr Miles S. Connell.

7. The following remaining issues were referred to the Tribunal for decision:

(1) How the Construction Contingency Reserve should be dealt with.

(2) What, if any, adjustment should be made to the figure for Sovereign Risk and other insurances?

(3) What, if any, adjustment should be made to the Lenders' Participation Fee portion of "Financing and Agency" fees in consequence of the Tribunal's conclusions as to the deductions to be made from the claimed Project Costs.

(4) What, if any, adjustment should be made to the Reference Tariff by reason of the alleged reduction in IPTL's deemed equity in the project?

(5) What, if any, further orders should be made in relation to the Commencement of Commercial Operations?

8. The Tribunal was also asked to note and incorporate in its Decision and thereafter in its final Award a formal stipulation as to the agreement between the parties concluded since the last hearing concerning the Cost of Gas Conversion, to which the Tribunal had referred briefly in paragraph 144 of its Decision of 9 February 2001.

9. At the request of TANESCO, a further oral hearing before the Tribunal was held on Sunday 29 April 2001 at the offices of the World Bank in Washington DC, United

States of America, at which TANESCO was represented by Mr Robert W Hawkins and Mr John Jay Range of Hunton & Williams and IPTL was represented by Mr Robert Sentner of Nixon Peabody LLP. Dr Swales and Mr Connell were in attendance, but were not questioned in relation to their statements.

10. At the hearing, the Tribunal was informed that the parties had reached agreement on remaining issues (2) and (3) as summarised in paragraph 7 above. The Tribunal invited the parties to reduce the terms of their agreement to writing and to submit the same to the Tribunal for incorporation into this Decision and, by reference, our final Award. The terms of the agreed stipulations relating to these issues were communicated to the Tribunal under cover of a letter from Hunton & Williams to ICSID dated 14 May 2001, confirmed by Nixon Peabody LLP on the same day.

11. We therefore set out first, as part of this Decision, the terms of the agreed stipulations made between the parties in relation to: (1) the Cost of Gas Conversion; (2) Financing and Agency Fees; and (3) Sovereign Risk and other insurances, as follows:

(1) **Gas Conversion**:

> "Pursuant to Section 7.1 of the Power Purchase Agreement ("PPA") dated 26 May 1995, between Tanzania Electric Supply Company Limited ("TANESCO") and Independent Power Tanzania Limited ("IPTL"), IPTL is required to convert the Tegeta facility to operate on Natural Gas upon the occurrence of certain conditions precedent.
>
> Accordingly, the Engineering Procurement and Construction Agreement (the "EPC Contract"), dated February 1997, between IPTL and Stork-Wartsila Diesel B.V. ("Wartsila") contains provisions pursuant to which Wartsila shall convert the facility to Natural Gas operation for a fixed price of US$11,583,000.
>
> TANESCO hereby agrees that upon fulfilment of the conditions precedent contained in Section 7.1 of the PPA, TANESCO will fully fund the costs of

conversion at the fixed price and under the payment terms contained in the EPC Contract."

(2) **Financing and Agency Fees**:

"1. In paragraph 9(E) of the Loan Facility Agreement, the Lender's Participation Fee portion of the Financing and Agency Fees for the Tegeta Power Plant was set at two percent (2%) of the Project loan amount of $105,000,000, which loan amount was fixed at 70% of Project Cost of $150,000,000.

2. In its February 9, 2001 Decision, the Tribunal reduced the amount of certain claimed expenses that may be included in the total Project Cost for purposes of tariff calculation. The final Project Cost (and the corresponding final loan amount) that may be included in the calculation of the tariff cannot be determined until resolution of all remaining disputes concerning Project Cost.

3. The parties stipulate and agree that the amount to be included as a Project Cost for the Lender's Participation Fee portion of financing and agency fees will be 2% of loan amount, calculated as [70% or 73.51%] of the reduced Project Cost resulting from the Award of this Tribunal, subject to adjustment upward or downward by the Award of a subsequent Tribunal, if any, that finally determines the amounts allowable for the Construction Contingency portion of the Project Cost."

(3) **Sovereign Risk and other Insurances:**

"1. The insurance expenses claimed by IPTL as a Project Cost in the financial model, and referenced in a letter dated July 21, 1997 from Johnson & Higgins to Mechmar bearing document nos. I00014 through I00018, at Joint Appendix 302, are the following: $1,879,802 for Construction Cover, $2,052,000 for CEND Cover, $393,750 for War Risk Cover, and $450,000 for Currency Inconvertibility Cover. The premium on CEND Cover was calculated on an insured value of $150,000,000 (i.e., 100% of claimed Project Cost) at a rate of 1.368%. The premium on War Risk Cover was calculated on an insured value of $105,000,000 (i.e., the debt portion of claimed Project Cost) at a rate of .375%. The premium on Currency Inconvertibility Cover was calculated on an insured value of $30,000,000 at a rate of 1.5%.

2. In its February 9, 2001 Decision, the Tribunal reduced the amount of certain claimed expenses that may be included in the total Project Cost for purposes of tariff calculation. The final Project Cost that will be included in the calculation of the tariff cannot be determined until resolution of all remaining disputes concerning Project Cost. The parties have reached an agreement that, when all remaining issues are ultimately resolved, the amount to be used as the insured value of Construction, CEND and War Risk Cover for purposes of calculating insurance premiums included as a Project Cost should be reduced based on the amount of total Project Cost allowed by the Tribunal.

3. The parties therefore stipulate and agree that the amount to be used as the insured value of Construction, CEND and War Risk Cover for purposes of calculating premiums to be included as a Project Cost will be reduced in proportion to the reduction in claimed Project Cost resulting from the Award of this Tribunal, subject to adjustment upward or downward by the Award of a subsequent Tribunal, if any, that finally determines the amounts allowable for the Construction Contingency portion of the Project Cost. The insured value of Currency Inconvertibility Cover will remain at $30,000,000, and the resulting premium of $450,000 will not be proportionately reduced.

4. For purposes of determining and modelling the insurance portion of fixed operations and maintenance cost, a 20-year straight line depreciation schedule will be adopted to reduce the insured value of CEND and War Risk Cover that may be included in the financial model ear year of the PPA. The initial value used in the depreciation schedule will be the value determined from the proportionate reduction in Project Cost resulting from the award or awards referenced above. Each year thereafter, the value for which the Project may be insured for purposes of the tariff calculation will be reduced by five percent (5%) per annum such that the value of the Project in the year 20 is only 5% of its value in year 1. The amount of CEND Cover that may be included each year to calculate the fixed operations and maintenance cost will be established according to the depreciation schedule referenced in this paragraph. The amount of War Risk Cover that may be included each year to calculate operations and maintenance cost will be fixed at [70% or 73.51%] of the depreciated value of the Project as determined from the depreciation schedule referenced in this paragraph. The parties have agreed, for purposes of modelling future operating expenses only, that $30,000,000 will continue to be used as the maximum insured value of Currency Inconvertibility Cover. If future operating experience indicates less than $30,000,000 needs to be converted from Tanzanian shillings to U.S. dollars, TANESCO may request IPTL to reduce the amount of Currency Inconvertibility Cover. Should the parties not reach mutual agreement, TANESCO reserves the right to challenge whether $30,000,000 is an excessive amount of Currency Inconvertibility Cover.

5. The intial rates used in the financial model to calculate premiums for operating expenses will be the rates set out in the Premium Schedules provided by IPTL on April 24, 2001. The rate for CEND Cover will be 1.368%. The rate for War Risk Cover will be .2625%. The rate for Currency Inconvertibility Cover will be 1.25% until IPTL obtains a current quotation for such Cover, which quotation will then be used in the model.

6. The sovereign risk insurance portions of fixed operations and maintenance cost for the entire 20 year term of the PPA will initially be calculated using the depreciation schedule referenced in paragraph 4 above and the rates referenced in paragraph 5 above. Each year thereafter, rates will be adjusted to the extent that CEND, War Risk or Currency Inconvertibility Cover is renewed at a different market rate.

7. IPTL stipulates and agrees that with respect to insurance costs that will be passed through the tariff to TANESCO, it has an obligation to act in a commercially reasonably and prudent manner and otherwise in accordance with the requirements of the PPA in procuring the insurance."

12. We now turn to the remaining issues upon which the parties were not agreed and which we deal with in the order as above.

The Construction Contingency Reserve:

13. Although it was submitted on behalf of IPTL that TANESCO should be precluded from re-opening this issue, which they contended had been the subject of an earlier agreement, the Tribunal concluded that no such binding agreement had been made.

14. TANESCO's submission, in brief summary, was as follows:

(1) No part of the Construction Contingency Reserve of US$5,709,000 had been utilised before IPTL had informed TANESCO in September 1998 that the plant was ready for the commencement of commercial operations, as certified by an Independent Engineer.

(2) No part of the Construction Contingency Reserve had been utilised since.

(3) The Reserve could only properly be utilised for payment of the cost of variation orders under the EPC Contract, and no such variation order had been issued or was likely to be issued.

(4) The only suggestion made on behalf of IPTL as to the possibility of any variation order being issued before the commencement of commercial operations related to possible further work or changes due to the plant having remained idle for 2½ years, in circumstances in which the Tribunal had held that IPTL was to be responsible for all such delay.

(5) For these reasons, the Construction Contingency Reserve should now be set at zero for the purposes of the calculation of the initial Reference Tariff.

15. IPTL, for its part, accepted the first three propositions, but challenged the fourth, as well as TANESCO's conclusion. There were, it was contended, two separate but associated questions, namely:

(1) Whether any part of the Construction Contingency Reserve was or would be used?

(2) To the extent to which it was not used, when should it be released?

16. As to the first of these questions, the Construction Contingency Reserve was, according to IPTL, to be available for any legitimate extra work or variation up to the time of commencement of commercial operations. While no part of it had been used thus far, it was impossible to say at this stage that no circumstances could arise under which it would be used. Apart from the fact that the plant had remained idle for 2½ years,

testing had not yet taken place. Furthermore, the Tribunal had not concluded that any and all consequences of delay were to be for IPTL's account, but merely that, since IPTL was at least in part responsible for the long-standing impasse between the parties, it could not recover damages from TANESCO for the latter's alleged breach in failing to do its part to fulfil conditions precedent to commercial operation commencing.

17. As to the second question, IPTL submitted that, although the loan documentation provided for the release of any unused part of the Construction Contingency Reserve at the end of eight years, TANESCO, through Dr Swales, had challenged the reasonableness of this provision. In his proposed financial model put forward on behalf of TANESCO on 11 July 2000, Dr Swales had modelled the release of the funds during the first operating year, and being applied to fund the debt service and maintenance reserves. The Reserve was included as a proper cost for tariff calculation purposes over the first year after the commencement of commercial operations. IPTL stated in its Post-Hearing Memorial that it accepted that proposal.

18. TANESCO pointed out that, in Mr Willy Lim's Witness Statement of 11 July 2000, he had conceded that, since it was not expected that any part of the Construction Contingency Reserve would be utilised, the total project cost would be reduced accordingly at the date of commercial operation: Dr Swales' "proposal" was therefore not open for acceptance.

19. The Tribunal concludes that, in the above circumstances, it cannot and should not determine finally at this stage that the amount of the Construction Contingency Reserve to be fed into the financial model should be set at zero. If, before commercial operations commence, any extra work or variation is required, which IPTL claims

should be funded out of the Construction Contingency Reserve, then, if TANESCO disagrees, there will be a further dispute which will have to be resolved. The Tribunal also concludes that there is no binding agreement between the parties as to when any unused portion of the Construction Contingency Reserve should be released. It would have been inclined to accede to Dr Swales' uncontroverted opinion on this point, but IPTL has offered to be more generous and to agree that any part of the fund which has not been utilised by the time commercial operations commence shall be released forthwith with the result that, in effect, there will have to be a further adjustment at that time to the Reference Tariff ab initio.

20. Accordingly, the Tribunal concludes that for present purposes the financial model must be calculated on the basis that the Construction Contingency Reserve is included as part of the Project Cost, but shall be released at the date when commercial operations commence with a consequent adjustment to the Project Cost and the Reference Tariff, save to the extent to which any extra work or variation is required before the commencement of commercial operations which IPTL contends should be funded out of the Construction Contingency Reserve. The parties agreed at the hearing that any dispute as to whether and to what extent the Construction Contingency Reserve should be utilised for this purpose shall be referred to the present Tribunal for subsequent decision and Award as necessary. The parties have undertaken to provide such agreement in writing for incorporation by the Tribunal into its prospective Final Award.

The Alleged Reduction in IPTL's Deemed Equity Contribution:

21. It will be recalled that one of the assumptions contained within the 31 May 1995 letter was that the ratio between what was described as "Senior Debt" and "Equity" should be 70%/30%.

22. TANESCO contends that, in consequence of the Tribunal's Decision which disallowed a number of items of alleged expenditure, which were claimed to have constituted part of the overall Project Costs and which were said to have been funded by IPTL as part of its equity contribution (totalling US$5,027,410.35), IPTL's equity contribution was in fact reduced to 26.49%; that accordingly, IPTL's return on its actual equity, if unadjusted, would be higher than the agreed adjusted IRR of 22.31%; and that there should therefore be an appropriate further adjustment to the Reference Tariff pursuant to Addendum No. 1.

23. On behalf of IPTL, it was first of all submitted that this is a new point, which should have been raised (if at all) as part of the disputed tariff calculation issues which were the subject of the Tribunal's Decision of 9 February 2001. IPTL goes further and contends that, not only was the point not taken but, through Dr Swales, TANESCO conceded that the 70%/30% debt/equity ratio remained. The proposed financial model which Dr Swales put forward was calculated on that ratio, and in his Fifth Witness Statement submitted for the purposes of the tariff calculation phase of the proceedings, he listed, in paragraph 3, those of the assumptions which had not changed as including "Senior Debt: 70%" and "Equity: 30%" (although he added a footnote to the effect that he was unable to verify from the documents produced by IPTL that it did in fact contribute equity equal to 30% of the claimed project costs). One thing is clear – it was not suggested on behalf of TANESCO at that stage that the 70%/30% ratio would have to be adjusted to take account of any part of the claimed project costs which the

Tribunal determined should be disallowed, depending on the source of the relevant funds.

24. Mr Hawkins for TANESCO fairly conceded that the point had not been raised, but suggested that TANESCO had not been in a position to raise it until after the Tribunal made its decision on the various items of claimed costs which were challenged. We do not accept that argument. The adjustment might not have been quantifiable at that stage, but the point could certainly have been raised, argued in principle and determined. It was not the intention of the Tribunal to give the parties a further opportunity to raise wholly new points after publication of its Decision.

25. However, Mr Sentner for IPTL also invited us to dismiss the point on its merits, insofar as he contended that TANESCO had failed to make out its case on the facts. TANESCO relied in particular on the documents relating to the 9th and last drawdown, which showed a total drawdown figure of US$119,296,000, comprising a contribution from the agent bank of US$84,000,000 (being 70%) and an equity portion of US$35,296,000 (being precisely 30%). TANESCO's claim for adjustment depended on the assumption that certain of the items which we had disallowed, and in particular: Development Cost of US$3,202,869; Cost of Raising Equity of US$715,486.35; KTA Tenaga Fees of US$809,055; and payment to Omni Management Services of US$300,000, were claimed as being part of IPTL's equity contribution. However, IPTL contended that one should not assume for these purposes that these items of claimed expenditure were to be identified as having been funded by or attributed to IPTL's equity contribution, and others as being the product of the bank loans. Both aspects of the money contributed went into one notional "pot" from which expenditure was made.

26. The Tribunal respectfully agrees that, even if this claim for adjustment were not to be dismissed on the "technical" ground that it was raised too late, one result of it being submitted without the opportunity of investigating precisely what contribution was in fact made by the banks on the one hand or by IPTL on the other in relation to each item of claimed cost which the Tribunal rejected or reduced was that the exercise could not now be carried out. Although the Tribunal was not persuaded by every aspect of Dr Swales' evidence, it shares his inability to verify from the evidence presented precisely what were the respective debt and equity proportions of the claimed Project Costs.

27. Furthermore, as it seems to the Tribunal, if one were to reduce IPTL's equity contribution by reference to these specific costs which were disallowed, one should do a similar exercise in relation to the debt contribution. TANESCO's figures did not (for instance) appear to include in the equation the substantial deduction which the Tribunal concluded was to be made from the EPC Contract Price, and thus the Project Costs, for the purposes of calculating the Reference Tariff. In order to determine the "true" debt/equity contribution, the question arises whether this should be deducted from debt or equity, or remain deemed to have been contributed on the assumed 70%/30% ratio. Despite Mr Hawkins' admirable persistence, the Tribunal was not persuaded that in the calculation which it presented TANESCO had been comparing like with like.

28. Finally, the Tribunal is of the view that different considerations might in any event have applied, depending on the reason why the sums claimed were disallowed in whole or in part – whether the Tribunal was not satisfied that the money was spent at all; or whether the Tribunal was not satisfied that it was spent in connection with this project; or whether the Tribunal merely concluded that the expenditure was not reasonably or

prudently incurred. Since only the latter had been in issue before us in the proceedings leading to our Decision, we saw no need to differentiate, and had not done so.

29. Accordingly, and for these reasons, the Tribunal concludes that further adjustments should not be made to the financial model on this ground.

The Commencement of Commercial Operations:

30. The Tribunal has already referred above to paragraph 168 of its Decision of 9 February 2001.

31. For IPTL, Mr Sentner at one stage seems to be asking the Tribunal for an order that commercial operations should commence by 31 July 2001. However, he conceded that IPTL would need a period which he estimated as 90 days from the publication of our Final Award in order to complete all necessary preliminary steps, and in particular to arrange for the provision of the necessary finance from the lenders. Whilst the Tribunal undertook to use its best endeavours to produce its Final Award as soon as possible, it was acknowledged that, after the communication of this Decision to the parties, final adjustments would have to be made to the financial model, which the parties agreed should then be incorporated by reference into our Final Award.

32. In these circumstances, and also in view of the fact that no-one could be sure what, if any, problems would be revealed during commissioning and testing, and what, if any, further physical work needs to be done, the Tribunal considers that it would not be helpful to the parties for us to make an order which may not be achievable despite the good faith efforts of the parties.

33. Accordingly, the Tribunal amends and refines the order which we indicated we were minded to make in paragraph 168 of our Decision of 9 February 2001, and hereby orders that the parties shall comply with their respective obligations under the PPA, and shall use their best endeavours and co-operate together to achieve the commencement of commercial operations as soon as practicable and with a view to commercial operations commencing within 90 days of the publication of our Final Award.

Dated this 24th day of May. 2001.

The Honorable Charles N. Brower

Charles N. Brower

The Honourable Andrew Rogers QC

Andrew Rogers

Kenneth Rokison QC