APPENDIX C

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 TARIFF AND OTHER REMAINING ISSUES

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DECISION ON TARIFF AND OTHER REMAINING ISSUES

1. Introduction

A. The Parties:

1. The Claimant, Tanzania Electric Supply Company Limited ("TANESCO"), is a Tanzanian corporation, being a public utility wholly owned by the United Republic of Tanzania, and charged with responsibility for the generation, supply and transmission of electric power throughout the country.

2. The Respondent, Independent Power Tanzania Limited ("IPTL"), is similarly a corporation incorporated in Tanzania. It was formed as a "joint venture" company between VIP Engineering & Marketing Limited, a Tanzanian engineering company, and Mechmar Corporation (Malaysia) Berhard, a Malaysian corporation.

B. The Contract:

3. This arbitration arises out of a Power Purchase Agreement ("PPA") dated "as of" 26 May 1995 between TANESCO and IPTL, whereby IPTL agreed to design, construct, own, operate and maintain an electricity generating facility with a nominal net capacity of 100 megawatts, to be located in Tegeta, Tanzania (approximately 25 kilometres north of Dar es Salaam) (the "Facility"), and to operate the Facility and deliver electricity generated thereby to TANESCO for an initial period of 20 years, subject to extension for further periods as therein provided. We refer to the project as "the Tegeta Project".

4. Under Article V of the PPA, the price to be paid after the Initial Operations Date of the first unit comprised three basic elements, namely:

   (1) A "Capacity Payment";

   (2) An "Energy Payment";

   (3) A "Test Energy Payment", to be applied before the applicable Commercial Operations Date.

5. Under Appendix B, a "Reference Tariff" was to be established, comprising a "Capacity Purchase Price" (which in turn consisted of two elements, namely a "Capital Component" and a "Debt Component"), and an "Energy Purchase Price" (also consisting of two elements, namely a "Fuel Cost Component", and a "Variable Operations and Maintenance Costs Component"), which was subject to

escalation/variation in accordance with the detailed provisions of Appendix B so as to arrive at the actual price or tariff to be payable.

6. Under Article IV it was a condition precedent to the obligation of TANESCO to purchase electrical energy and capacity from IPTL that IPTL should have fulfilled certain conditions, including in particular under Article 4.1(b) the submission, not less than 30 days prior to the Commencement Date of a certificate from the Independent Engineer stating that the Facility, when constructed in accordance with the general layout drawings submitted therewith would (inter alia) conform with the Description of the Facility; and under Article 4.1(c) the provision, as soon as available but in any event prior to the Initial Operations Date of each unit, of a certificate from the Independent Engineer stating that the Facility has been designed and constructed (inter alia) in all material respects in accordance with the terms of the Agreement and the general layout drawings.

7. Addendum No. 1 to the PPA, dated 9 June 1995, provided (inter alia):

> "Before commencement of commercial operations the Reference Tariff mentioned in Table I of Appendix B will be adjusted upwards or downwards depending on the effect of changes that will have taken place on any or all the underlying assumptions stated in the Power Purchase Agreement".

C. Ancillary Agreements:

8. On 8 June 1995, an Implementation Agreement and a Guarantee Agreement were entered into between the Government of the United Republic of Tanzania and IPTL.

D. The Commercial Background:

9. The above contractual relationship was entered into against the background of a severe shortage of electric power within Tanzania, which was apparently due in part to developments in the economy which stimulated significant growth in the demand for electricity, coupled with problems experienced within Tanzania's existing hydro-generated power system. A firm of international consultants, Acres International Limited ("Acres"), had been involved in advising the Government of Tanzania and TANESCO on a continuing basis since the late 1970's. By 1995, the need for further generating capacity was regarded as urgent.

E. Jurisdiction and the Establishment of the Arbitral Tribunal:

10. Article XVIII of the PPA provided (inter alia) agreed machinery for the resolution of disputes. By Article 18.3, it was agreed that any dispute arising out of or in connection with the PPA should be settled by arbitration in accordance with the Rules of Procedures for Arbitration Proceedings of the International Centre for the Settlement of Investment Disputes (the "ICSID Arbitration Rules") established by the Convention on the Settlement Investment of Disputes between States and Nationals of other States (the "ICSID Convention"), and that for the purposes of consenting to the jurisdiction of the Convention it was agreed that IPTL was a foreign-controlled entity, unless the amount of the voting stock in IPTL held by non-Tanzanian investors should decrease to less than fifty per cent of its voting stock. Such arbitration was to be conducted in London, England and, unless otherwise agreed by the parties, before a tribunal of three arbitrators - one to be nominated by TANESCO, one to be nominated by IPTL, and the third to be nominated by the party - nominated arbitrators or failing

their agreement by the High Court of England and Wales.

11. Disputes did arise between the parties, as hereinafter more particularly defined, which were duly referred to arbitration pursuant to the aforesaid contractual provision - the Request for Arbitration being lodged with ICSID on 25 November 1998, and formally registered by the Secretary General on 7 December 1998.

12. TANESCO and IPTL nominated the Honorable Charles N Brower of Messrs White & Case LLP, 601 Thirteenth Street, NW, Suite 600 South, Washington, DC, United States of America, and the Honourable Andrew Rogers QC of 233 Macquarie Street, Level 7, Sydney NSW 2000, Australia respectively as arbitrators, and the two arbitrators so nominated agreed to the appointment of Kenneth Rokison QC of 20 Essex Street, London WC2R 3AL, United Kingdom to be third arbitrator and President of the Tribunal. The Tribunal was fully constituted on 24 March 1999.

13. The arbitral proceedings have been conducted throughout in accordance with the ICSID Convention and the ICSID Arbitration Rules, under the auspices and administration of the Centre in Washington, DC. Jurisdiction in this case has at no time been contested by either party. TANESCO was designated by Tanzania as an agency of that state pursuant to Article 25(1) of the Convention on 24 September 1998, and TANESCO's consent to arbitrate disputes with IPTL in accordance with the ICSID Arbitration Rules as provided by Article XVIII of the PPA was expressly approved by the Government of Tanzania by Article 21.2 of the Implementation Agreement. IPTL, although a Tanzanian corporation, has at all material times been

owned and controlled to the extent of at least 70% by nationals of Malaysia. Both Tanzania and Malaysia are parties to the ICSID Convention.

F. Events Leading to the Development of the Disputes and the Arbitration:

14. In due course, on 4 February 1997, an Engineering, Procurement and Construction Contract (the "EPC Contract") was concluded between IPTL and Stork-Wartsila Diesel B.V. ("Stork-Wartsila"), a company established in The Netherlands, for the purpose of constructing the generation plant required to perform the PPA. In addition, on 21 May 1997, IPTL entered into a Fuel Supply Agreement (the "FSA") with Galana Petroleum Limited ("Galana") and Total International Limited ("Total") for an initial term of 5 years to supply the fuel necessary to operation of the Facility.

15. As the Facility was being constructed and the prospect of commencing commercial operations came nearer, the disagreements between the parties which ultimately led to this arbitration developed. In particular, TANESCO took issue with the fact that the EPC Contract with Stork-Wartsila called for the provision of ten 10 MW medium speed diesel engines, instead of the five 20 MW slow speed diesels originally stated in the PPA. Further, it was becoming necessary for the parties to discuss adjustment of the Capacity Purchase Price as foreseen in Addendum No. 1 to the PPA.

16. These events took place against the background of apparent controversy within Tanzania regarding a competing project, known as the SONGO-SONGO Gas-to-Electricity or "SONGAS" Project, in respect of which agreements had been initialled on 23 March 1997 between (inter alia) the Government of Tanzania, TANESCO, and

two Canadian companies, Ocelot Energy Inc. ("Ocelot") and TransCanada Pipelines Limited. This rival project was to be built by Canadian interests and financed by the International Bank for Reconstruction and Development. There was evidence in the arbitration that, notwithstanding the urgency with which the PPA had been concluded in 1995,pressures were thereafter exerted both on and within the Government of Tanzania and TANESCO to defer it, if not eliminate it, in favour of the SONGAS Project.

17. On 9 April 1998, on the eve of scheduled discussions between TANESCO and IPTL on the adjustment of the tariff for the Capacity Purchase Price, TANESCO served on IPTL a Notice of Default asserting that IPTL was "in default on its obligation to supply and install slow speed diesel generating sets in accordance with Section 1.1 of Appendix A to the PPA" and calling upon IPTL to cure such default within 90 days as required under Article 16.3 of the PPA

18. Negotiations proceeded somewhat sporadically during the course of the summer and early autumn of 1998 with the participation of the Tanzanian Government, TANESCO, and its legal and technical advisers, Hunton & Williams and Acres respectively, together with IPTL. However the parties remained at loggerheads regarding both adjustment of the Capacity Purchase Price and the substitution of medium speed diesels for slow speed diesels.

19. On 25 November 1998 the Request for Arbitration was lodged on behalf of TANESCO, asserting two claims:

(1) That medium speed diesel engines had been substituted for the required slow speed diesels without obtaining the prior written consent of TANESCO, thus entitling TANESCO to terminate the PPA; alternatively

(2) That, pursuant to Addendum No. 1 the Capacity Purchase Price was to be "cost based", but IPTL was refusing to share relevant information with TANESCO and the cost seemed excessive, so that in the event that the PPA could not be terminated the tariff should be adjusted.

G. Subsequent Developments:

20. On 14 December 1998, TANESCO gave to IPTL Notice of Intent to Terminate pursuant to Article 16.3(a) of the PPA, which was copied to IPTL's lenders, stating that, barring consensual resolution of the matter, TANESCO reserved its right to terminate the PPA pursuant to Article 16.3(c).

21. Meanwhile on 30 November 1998, five days after lodging of the Request for Arbitration with the Centre, IPTL filed a petition in the High Court of Tanzania in Dar es Salaam, directed against TANESCO and three officials of the Government of Tanzania, seeking both a declaration that commercial operations of IPTL's facility should be deemed as having commenced 15 September 1998 and an order for payment to IPTL by TANESCO of a "Capacity Payment" in the amount of $3,623,000 monthly beginning on that date.

22. On 7 December 1998, being the same day the Request for Arbitration was registered

by the Secretary General, TANESCO petitioned the Tanzanian High Court to stay the proceedings recently commenced against it.

23. On the following day, 8 December 1998, IPTL submitted to the same Court a "Notice of Objection on a Preliminary Point of Law" asserting in effect that TANESCO had waived its right to pursue this arbitration.

24. On 5 March 1999 the High Court of Tanzania sustained the preliminary objections of IPTL and proceeded immediately to grant the relief requested by IPTL in its original petition. Leave was given to TANESCO to appeal and it sought a stay of execution pending such appeal.

25. In response, on 7 April 1999, IPTL applied for an order of execution in the amount of $23,670,266.67, that being the accumulated sum of the monthly "Capacity Payments" due pursuant to the High Court's Order up to 1 April 1999. Thereafter IPTL agreed that it would not execute for a limited period of time.

26. When the Tribunal convened its initial session with the parties on 14 June 1999, TANESCO had already issued a request for an order of provisional measures from the Tribunal directed at a cessation of all the above proceedings in the Courts of Tanzania.

27. In the course of that session, it was clarified that IPTL was willing further to stay its hand in relation to the proceedings in Tanzania, but that it would itself seek

provisional measures from this Tribunal substantially to the same effect as it had obtained from the High Court of Tanzania.

28. Thereafter, on 28 June 1999, IPTL filed with the Tribunal a request for the following provisional measures:

(1) Permitting commercial operations of the Facility to commence;

(2) Requiring TANESCO to make monthly Capacity Payments in the amount of $3,623,000, or, in the alternative, in the amount of $3,400,000 (an interim monthly payment which TANESCO previously had agreed with IPTL, subject however to approval of the Government of Tanzania, which had not been forthcoming); and

(3) Requiring Tanzania to pay forthwith a lump sum of $32,607,000, being the accumulated monthly Capacity Payments due from 15 September 1998 to May 1999 in accordance with the order of the High Court of Tanzania.

29. On 18 October 1999 the Tribunal convened to hear both parties' applications for provisional measures. In the meantime, on 8 July 1999, the order of the High Court of Tanzania had been stayed by a single Justice of the Court of Appeal of Tanzania, pending determination of the appeal thereof, and the parties then requested the Tribunal to defer consideration of TANESCO's request for provisional measures directed at the Tanzanian court proceedings.

30. At this hearing IPTL revised its request by (1) withdrawing its demand for a lump sum payment of the alleged "arrears" accumulated in respect of the order of the High Court of Tanzania, and (2) requesting that the requested order permitting commercial operations also enjoin TANESCO to co-operate with IPTL, including conducting operational tests and connecting the Facility to the Tanzanian power grid. The demand for a monthly Capacity Payment remained.

31. On 20 December 1999 the Tribunal issued its Decision On The Respondent's Request For Provisional Measures, a copy of which is attached hereto as Appendix A and which is incorporated herein by reference. The relief that had been requested by IPTL was denied by the Tribunal on the ground that it would change rather than maintain the status quo by ordering performance of the PPA, and thus was outside the scope of Arbitration Rule 39, and that there was insufficient demonstration of urgency in that IPTL, should it prevail on the merits, would in any event receive tariff payments over 20 years as foreseen by the PPA and would lose only the interim use of funds, for which an award of damages would on the face of it be an adequate remedy.

32. By the time of the hearing resulting in that Decision it had become clear that it would be appropriate to determine as a preliminary matter certain issues of construction of the PPA and law. It was ordered, therefore, that the parties should make written submissions with respect to the following preliminary issues:

    1. Was or is TANESCO entitled to terminate the PPA?

    2. If not, what are the effects (if any) on the parties' respective rights and obligations under the PPA of:

(a) the change from low speed to medium speed diesel engines; and/or

(b) any other alleged differences between the Facility as built and that provided for in the PPA and/or any other agreements between the parties?

3. How is the final Reference Tariff to be calculated, in the light of the said change and any other differences which may be established?

4. What was the effect on the parties' respective rights and obligations of Addendum No. 1 dated 9 June 1995, and, in particular, did Addendum No. 1 on its true construction have the effect that the final Reference Tariff was to be calculated by reference to the reasonable and prudently incurred cost of the Facility as built; and what were "the underlying assumptions stated in the PPA"?

33. A hearing was held 13, 14, 15 and 16 March 2000 on these preliminary issues, and on 22 May 2000 the Tribunal issued its Decision On Preliminary Issues of Construction/Law, a copy of which is attached hereto as Appendix B and which is incorporated herein by reference. As set forth in paragraph 19 of that Decision, the "Conclusions" of the Tribunal on the Preliminary Issues were as follows:

(1) That the PPA was not subject to an unsatisfied condition precedent as alleged or at all, and was not void for uncertainty; and accordingly was a valid and effective contract between the parties;

(2) That TANESCO was not entitled to serve Notice of Default and was and is not entitled to give notice of termination pursuant thereto;

(3) That the Reference Tariff should be adjusted in accordance with Addendum No. 1 by reference to changes that had taken place, before commercial operations would have commenced but for TANESCO's purported Notice of Default, in any of the assumptions listed in Mr Rugemalira's letter to the Principal Secretary of the Ministry of Water, Energy and Minerals dated 31 May 1995, with the following qualifications, namely:-

(i) that the figure of 23% for "IRR" should be amended to read "22.31%";

(ii) that it is open to TANESCO to prove that any costs incurred by IPTL relating to any of the listed assumptions were not reasonably and prudently so incurred.

The Tribunal went on to answer the Preliminary Issues listed in paragraph 32 above as follows:

(1) Not on any grounds argued and dealt with in this decision.

(2) None, save that there may be consequences on the cost of the Facility and therefore on the adjustment to the Reference Tariff to be carried out pursuant to Addendum No. 1 to the PPA.

(3) & (4) The "underlying assumptions stated in the PPA" were those listed in Mr Rugemalira's letter to the Principal Secretary of the Ministry of Water, Energy and Minerals dated 31 May 1995, and the effect of Addendum No. 1 dated 9 June 1995 was as summarised in sub-paragraph (3) above."

34. At the time of the hearing on Preliminary Issues, and at the date of our Decision on those issues, a date had already been fixed for what was hoped would be the final hearing in this matter, to consider remaining issues in relation to the fixing of the tariff, to take place during the last week in July 2000.

35. Between the date of the hearing on Preliminary Issues and the date of our Decision, on 20 April 2000 TANESCO submitted a request to the Tribunal for an order for discovery concerning alleged payments and/or gifts made or given, offered or promised by agents of IPTL to officials of the Government of the Republic of Tanzania or TANESCO, including the provision of Answers to Interrogatories and a Request for Admissions in relation to such payments or gifts.

36. Reference to allegations of bribery or attempted bribery had been made earlier in the course of the proceedings, but TANESCO had never formally pleaded such allegations or sought to raise them by way of claim or defence.

37. The request was supported by the unsworn statements of Mr Patrick Rutabanzibwa, the Permanent Secretary of the Ministry of Energy and Minerals of the Republic of Tanzania and formerly the Commissioner for Energy and Petroleum Affairs in that Ministry, Mr Prosper A.M. Victus, the Assistant Commissioner for Energy (Petroleum and Gas); and Mrs Esther Masunzu, the Assistant Commissioner for Energy (Electricity).

38. The Tribunal declined to make any of the orders requested, on the ground that no allegation of bribery had been pleaded, and that it would in any event not be right to order the answering of questions on oath when the only basis for the allegations upon which the questions were based was unsworn statements.

39. The request was renewed on 26 May 2000, when TANESCO submitted its Reply on the Merits, in which it pleaded for the first time a claim to be entitled to rescind the PPA on the basis of its allegations of bribery, which it purported to raise as an "Ancillary Claim" pursuant to Rule 40 of the ICSID Arbitration Rules (which by its paragraph (2) must be presented not later than in the Reply). The renewed application was supported by the Statutory Declaration of Mr Victus, and sworn statements of Mrs Masunzu and Mr Rutabanzibwa.

40. On 6 June 2000 IPTL raised objection to the assertion of the bribery claim and the renewed request for discovery, on the grounds (inter alia):

(1) That it was not an "ancillary" claim, but was a claim which should have been asserted, if at all, in TANESCO's Memorial on the Merits in January 2000;

(2) That, even assuming the truth of the facts alleged in the witness statements, TANESCO had failed to make out a prima facie case for rescission of the PPA; and

(3) That if the plea were to be allowed, it would jeopardise the July hearing date.

Alternatively, in the event that the Tribunal was minded to permit TANESCO to proceed with its plea of bribery, IPTL sought an order for immediate production by TANESCO of all documents relevant to the plea.

41. On 12 June 2000 the Tribunal informed the parties of its decision that it would permit TANESCO to raise the bribery issue pursuant to Rule 40 of the ICSID Arbitration Rules, and ordered both parties to produce any documents in their possession, custody or power relating to that issue. But it declined to order the wide-ranging Interrogatories or the Request for Admissions proposed, which sought the answers to questions concerning possible bribery and attempts at bribery by employees and agents of IPTL generally, on the ground that no allegations of bribery or attempted bribery had been made against any representatives of IPTL except Mr Rugemalira.

The Tribunal made it clear that the addition of the bribery allegations would not be permitted to delay the July hearing, which had been scheduled for some time.

42. On 27 June 2000 the Tribunal ruled that TANESCO should produce relevant documents in the files of its counsel emanating from the Government of Tanzania, even though the original documents had never been in the possession, custody or power of TANESCO itself.

43. These documents were produced by TANESCO's Counsel, Hunton & Williams, under cover of a letter dated 5 July 2000, on the basis of an express agreement as to their confidentiality (which in the view of the Tribunal would have applied in any event). In the penultimate paragraph of its letter, Hunton & Williams stated:

> The investigation in Tanzania is not complete. In the light of this fact, we have been instructed to advise that TANESCO will not proceed further at this time with respect to its bribery allegations but will make oral application at the hearing later this month for an extension of time to present its case with respect to the bribery claims.

TANESCO further purported to "reserve all rights regarding its bribery claim" under the ICSID Convention and Arbitration Rules and under Tanzanian law.

44. Meanwhile, on 29 June 2000 IPTL served its Reply Counter Memorial (or "Rejoinder") on the Merits and on 10 July 2000 served its Memorial on the Calculation of the Tariff. On 11 July 2000 TANESCO served its Memorial on the Calculation of the Tariff.

45. An oral hearing took place before the Tribunal at the International Dispute Resolution Centre, 8 Breams Buildings, London on 21, 21, 24, 25 and 26 July 2000, at which TANESCO was represented by Mr Robert W. Hawkins, Mr John Jay Range and Mr Brett A. Bakke of Hunton & Williams, and IPTL was represented by Mr Robert Sentner and Mr Chris Paparella of Nixon Peabody LLP.

46. Oral evidence was given by Mr William Matthews, Mr Alfred Lippert, Dr Martin Swales, Mr B.E.A.T. Luhanga, Mr Donald Wessel, Mr James Rugemalira, Datuk Majid, Mr Willy Lim and Mr Donald Chambless.

47. After the close of the oral hearing, and pursuant to the invitation of the Tribunal, IPTL filed a written submission dated 18 August 2000 on its claim for Damages for Breach of Contract, and each party filed a Post-Hearing Memorial dated 12 September 2000. Thereafter, on 2 October 2000, each party filed a written submission on the Award of Arbitration Costs.

48. At the start of the July hearing and upon the application of TANESCO, the Tribunal received "information" from Mr Rutabanzibwa (although he was not formally called as a witness) as to the progress of the investigation in Tanzania of the allegations of bribery, which had apparently started in late 1997, had thereafter proceeded somewhat sporadically, but which was said to be continuing. On the basis of this information, Counsel for TANESCO asked for an extension of time of 3 months to make additional filings in relation to these issues.

49. Mr Hawkins declined the invitation of the Tribunal to apply to withdraw the allegation, and, after considering the application, the Tribunal refused to grant the extension requested, and indicated that since the allegation remained on the record, it must be dealt with on its merits on the basis of the material put before it.

2. The Remaining Issues:

50. The issues which were canvassed before the Tribunal and which we are called upon to determine include the following:

(1) The issue of alleged bribery;

(2) Did IPTL and/or the parties fail to perform conditions precedent to Commercial Operations, including:

(1) Failing to provide a certificate from the Independent Engineer stating that the Facility when constructed would conform with the Description of the Facility, or that the Facility had been designed and constructed in all material respects within the terms of the PPA and the general layout drawings?

(2) Failing to agree the Reference Tariff?

(3) Was TANESCO in breach of its obligation to act in good faith in relation to the negotiations concerning the fixing of the tariff, and if so what are the

consequences?

(4) Was IPTL in breach of its obligation to act in good faith in relation to the negotiations and in particular to the disclosure of relevant documents and information, and if so what are the consequences?

(5) Did IPTL and Stork-Wartsila conspire together falsely to inflate the EPC price?

(6) Was IPTL in breach of its obligation to act reasonably and prudently in relation to any costs and expenses which it would have input into the amount prima facie payable by TANESCO as the Capacity Payment element of the tariff, and in particular in relation to the procurement of the EPC Contract?

(7) Was IPTL in breach of its implied obligation to act reasonably and prudently in relation to the procurement of the FSA, and if so what consequences flow?

(8) Were any breaches on the part of either party waived, or is any complaint or remedy barred by estoppel?

(9) What adjustment should be made to the Reference Tariff stated in the PPA?

(10) What if any further orders should be made?

(11) What if any order should be made in respect of the costs of the arbitration (including the fees and expenses of the Tribunal), and/or the legal and other costs of the parties?

51. The Tribunal considers these issues in the above order as follows. In so doing, it makes the following observations.

(1) The Tribunal will not repeat at length any of the arguments which were canvassed or the decisions made in the course of earlier stages in the proceedings culminating in the Decision on the Respondent's Request for Provisional Measures and the Decision on Preliminary Issues of Construction/Law, both of which are appended hereto and incorporated herein;

(2) Insofar as any issue depends on an application of principles of law, the Tribunal has sought to apply the law of the Republic of Tanzania, as it has sought to do throughout this arbitration, including the Decisions referred to in paragraph 51(1) above, that being the governing law of the contract expressly designated by the parties by Article 19.4 of the PPA.

3. The Issue of Bribery:

52. In the light of TANESCO's having pleaded this issue in its Reply on the Merits, and in the light of TANESCO's having declined the invitation of the Tribunal to withdraw the allegation, we must consider it on its merits and on the basis of the material before

us.

53. The Tribunal concludes that the allegation fails and must be dismissed. Even if the evidence presented on behalf of TANESCO were to be accepted (and we emphasise that it was very much disputed on behalf of IPTL and had at all times been vigorously denied by Mr Rugemalira), we conclude that it would have been insufficient to establish the plea.

54. In its Reply on the Merits of 26 May 2000, TANESCO invoked Sections 19, 23 and 24 of the Tanzanian Law of Contract Ordinance. It is first of all contended that part of the "consideration" for the PPA (said to be "bribes given by IPTL'S agents........to induce the PPA's execution") was unlawful, and the PPA is therefore void. Alternatively, it is contended that the PPA is voidable on the ground that consent was "procured by coercion".

55. The Tribunal notes that it has not been suggested that any unlawful payment was made to TANESCO, being the party with whom IPTL concluded the PPA. Further, as we read the evidence, the only sum said to have been paid by Mr Rugemalira and not rejected was the sum of 100,000 Tanzanian shillings (the then equivalent of less than US$200) said to have been contained in a "holiday gift package" given to Mrs Masunzu during the Christmas season of 1994. According to the notes of her interview before those investigating the allegations in Tanzania, which she adopted for the purposes of her evidence, she was twice offered $20,000 - in 1994 and again in 1996 - but refused on both occasions. Although Mrs Masunzu is said to have

admitted that, by her taking the 100,000 Tanzanian shillings, "Mr Rugemalira succeeded in getting her assistance in direct support of the IPTL project", there is no evidence to suggest either (i) that, but for the alleged bribe, she would have cast any vote or used any influence against the IPTL project, or (ii) that her support was crucial or indeed made any difference.

56. The evidence of Mr Rutabanzibwa and Mr Victus only alleges attempts at bribery, which were rejected. There is no suggestion that these alleged attempts caused either Mr Rutabanzibwa or Mr Victus to favour IPTL's cause. Indeed, one might have thought that, as men of honour, as they purport to be, the attempted bribes would have had the very opposite effect.

57. In these circumstances, the Tribunal repeats its conclusion stated in paragraph 119(1) of its Decision of 22 May 2000 to the effect that the PPA was an effective contract between the parties.

4. Did IPTL fail to perform a condition precedent to commercial operation by its failure to procure an Independent Engineer's Certificate that the Facility when constructed would conform to the contractual description, or that the Facility had been designed and constructed in all material respects within the terms of the PPA and the general layout drawings?

58. The Tribunal has already effectively dealt with this allegation in its Decision on Preliminary Issues of Construction/Law, and in particular paragraphs 77 and 78 thereof, in which it was concluded that the Certificate of the Independent Engineer which IPTL provided clearly satisfied the requirements of Article 4.1(b) of the PPA in all respects save one, namely that it stated that the plant when constructed in

accordance with the general layout drawings and technical specifications "meets generally with the Description of the Facility", rather than that it "will conform".

59. The Tribunal concluded that the difference was not a serious , let alone a material one, and accordingly, on the face of it, Article 4.1(b) was substantially satisfied. Furthermore, we observed that the response of TANESCO's Managing Director to the Certificate provided was simply to note the Independent Engineer's certification of the Facility "conforming to the requirements of the PPA's Article IV Clause 4.1(b)", from which it appears that, at the relevant time, TANESCO shared the conclusion which the Tribunal reached.

60. So far as the obligation under Article 4.1(c) is concerned, it will be observed that the PPA itself introduces a degree of flexibility, insofar as the Certificate relating to the Facility "as built" is only required to confirm the Facility's compliance with the agreement "in all material respects". In the light of our earlier conclusions expressed in our Decision on Preliminary Issues of Construction/Law, this provision presents no problems to IPTL.

61. The Tribunal concludes that there is nothing in this point, which was only canvassed briefly in TANESCO's Memorial and does not seem to feature in its Post-Hearing Memorial.

5. **Did either party fail to perform a condition precedent to commercial operation, namely to agree on the Reference tariff?**

62. TANESCO relies on the wording of Addendum No. 1, which provides that "Before the commencement of commercial operations, the Reference Tariff...... will be adjusted upwards or downwards depending on the effect of changes that will have taken place in any or all the underlying assumptions stated in the PPA". The Tribunal has concluded that the "underlying assumptions" referred to are those set out in IPTL's letter of 30 May 1995.

63. The PPA makes no provision for the agreement of the parties to such adjustment, and no provision as to what is to happen if the parties are unable to reach agreement on the adjustment to be made. TANESCO contends that, absent such provision, there is no room for an implication by necessity. If the parties are ultimately unable to agree, the arbitration clause provides machinery for resolving the parties' dispute; meanwhile, nothing further can happen.

64. IPTL challenges the assertion that Addendum No. 1 should be read as a condition precedent, providing, in effect, that the appropriate adjustment to the Reference Tariff must be agreed before commercial operations can commence. That is not what Addendum No. 1 says: rather, it provides that there shall be the appropriate adjustment. This is a mutual obligation of the parties. If agreement cannot be reached on the amount of any such adjustment before the commencement of operations, it can always be adjusted with retroactive effect once an agreement or, absent agreement, an arbitral award is made.

65. It is true that a retrospective adjustment would be possible. But that is not what Addendum No. 1 contemplates. What should be the amount of any provisional payment in the meantime? Should it be the unadjusted amount? Or the minimum amount conceded by TANESCO? Despite the immediate and instinctive feeling expressed by the Tribunal that it cannot have been the mutual intention that the Facility should stand idle while any dispute concerning the appropriate adjustment was finally settled by agreement or arbitration, it is not easy to identify the precise scope of any term which business efficacy requires to be implied.

66. The Tribunal is reluctantly driven to the conclusion that there is no basis for implying a term to the effect that commercial operations should begin notwithstanding the lack of agreement on the adjusted Reference Tariff. Similarly, the Tribunal is unable to conclude that there is was any implied term requiring the parties to proceed on the basis of a provisional or interim tariff pending agreement between the parties or a decision by the relevant tribunal charged with the resolution of any dispute.

67. However, now that the Tribunal is charged with that task, there is no reason why we should not decide what if any adjustment is appropriate and for commercial operation to commence in accordance with our decision. Indeed, the Tribunal notes that each party in its Post-Hearing Memorial seeks an order for the commencement of commercial operations at an appropriate date.

6. Was TANESCO in breach of its obligation to act in good faith in relation to any negotiations concerning the fixing of the tariff, and if so what are the consequences?

Was IPTL in breach of its obligation to act in good faith in relation to such negotiations and in particular the disclosure of relevant documents and information, and if so what are the consequences?

68. Lengthy delay in the commencement of commercial operations was clearly not in the interest of either party, and the Tribunal concludes that business efficacy requires the implication of a term that the parties shall negotiate in good faith in an endeavour to agree the appropriate adjustment with the minimum of delay. Each party accuses the other of a lack of good faith in this respect. TANESCO asserts that the primary reason for the failure to achieve any progress in the tariff negotiations which took place between about April and September 1998 was the refusal by IPTL to accept that it was under any obligation to incur project costs reasonably and prudently, or to provide TANESCO with documents and other information necessary to demonstrate that project costs (a) had actually been incurred and (b) had been incurred reasonably and prudently. IPTL, on the other hand, asserts that TANESCO was not prepared to embark upon negotiations in good faith at all, in circumstances where it was alleging that, by reason of the substitution of medium speed for low speed diesel engines, the Facility had not been built in accordance with the contractual description and IPTL was thereby in default. Once the Notice of Default had been served on 9 April 1998, IPTL was met at the purported tariff negotiations by Acres as well as representatives from TANESCO's lawyers, Hunton & Williams. According to IPTL, it did supply substantial documentation, including giving access to its current electronic financial model, and proposed the appointment of an independent engineer to assess the

reasonableness of the project costs and agreed to be bound by his decision - but TANESCO would not agree.

69. It is the view of the Tribunal that, in the negotiations which took place from April to September 1998, both parties were guilty of a degree of posturing, and, as we have concluded in our Decision on Preliminary Issues of Construction/Law and hereinafter in this Decision, neither was adopting a stance which we consider to have been wholly justified. The contemporaneous record shows that, once the Notice of Default had been served, it was IPTL who, at the meeting between the parties' representatives on 14 April 1998, initially refused to engage in any discussions on the final tariff until the disagreement over the issue of alleged default had been resolved (a stance repeated in IPTL's letter the following day), while TANESCO and the Government of Tanzania expressed themselves as willing for discussions to move forward "on a parallel basis" and urged IPTL to participate. True, IPTL soon changed its stance, and in a letter dated 24 April 1998 expressed its willingness to start final tariff negotiations even if the Notice of Default were not withdrawn, and negotiations continued thereafter. However, progress was undoubtedly hampered by the fact that IPTL said that neither it nor its advisers were able to provide documentation relating to the bidding process for the EPC Contract, being the biggest single item of expenditure. Further, although TANESCO did not withdraw its Notice of Default (which the Tribunal held in its previous Decision was not justified in the circumstances), it did not use this as a ground for not continuing the negotiation process. Indeed, the parties reached agreement at a meeting on 29 October 1998 on the tariff to be applied during the interim period while the disputes between the parties were being reviewed and

resolved through the dispute resolution mechanism, but the agreement reached was made subject to the approval of the Government of Tanzania, which was unfortunately not forthcoming. However, in any event, as we have concluded, there was no obligation to agree upon an interim tariff. It was against this background that IPTL launched proceedings in the Tanzanian Courts for interim mandatory orders requiring TANESCO to make monthly capacity payments. The positions of the parties were then "polarised", and remained so during the course of the arbitration.

70. Accordingly, the Tribunal concludes that IPTL's allegation that TANESCO failed and refused to negotiate in good faith after April 1998 is not made out, and that, at all events, such failure and/or refusal was not the sole or effective cause of the fact that a tariff was not agreed with the result that commercial operations did not commence. Accordingly, the Tribunal concludes that IPTL's claim to damages fails, and that it is therefore unnecessary to consider the details of the quantum of its claim.

71. So far as the counter-allegation by TANESCO is concerned, the Tribunal concludes that its complaint as to IPTL's reluctance to provide relevant documents and other information, so as to enable TANESCO to assess the reasonableness and prudence of its conduct, is made out, even though IPTL might reasonably have concluded that the provision of further documents and information at that stage would have been unlikely to bear fruit. But in the event, since TANESCO claims no damages for IPTL's breach in this respect, the point is academic.

7. Did IPTL and Stork-Wartsila conspire to inflate the EPC Contract price?

72. In our Decision of May 2000 (paragraph 69), we mention the suggestion that there was what had been described as an "unholy alliance" between IPTL and Wartsila which resulted in a falsely inflated EPC Contract price. TANESCO suggests that this was motivated by a decision to maximise the project cost so as to increase IPTL's gross return, which had been fixed as a percentage of its equity contribution; or some other ulterior motive.

73. This was plainly an allegation of dishonesty, and accordingly carries with it a correspondingly heavy burden of proof, especially as the allegation, if true, would have had to have involved a very well-known and well-respected international engineering corporation. Apart from relying on the fact that the Stork-Wartsila final bid price in January 1996, which was accepted, was higher than the rival Hyundai bid and higher than the price which Stork-Wartsila had bid in September 1995, TANESCO relies on what are described as secret "tête-à-tête" meetings between IPTL's agents, Mechmar, and Stork-Wartsila in August and September 1995, when Stork-Wartsila and Mechmar were discussing a form of joint venture or "Construction Consortium", under which performance of part of the EPC Contract (including in particular all tanks, oil-fired boilers, civil works of the power plant, staff housing and access road and water pipeline) was to be sub-contracted to Mechmar Energy.

74. In the view of the Tribunal there was nothing even prima facie sinister about the joint venture proposal, which, as the evidence put before us concerning other projects and their costs demonstrates, was by no means extraordinary. Furthermore, despite the

plea in TANESCO's closing written submissions that the evidence of bad faith by Mechmar/ IPTL is "overwhelming", as TANESCO itself was at pains to point out, at the time the parties to the proposed joint venture were discussing the prices in the latter part of September 1995, the price for that part of the work which was to be carried out by Stork-Wartsila appears to have been very much in line with its proposal of 7 July 1995, which in turn was "comparable" with its earlier proposal of 23 March 1995, with an appropriate adjustment to take account of changes in the ("Dfl")(Dutch Guilder)/US$ exchange rate.

75. In any event, we do not consider that the allegation really advances TANESCO's case. If we were to conclude that the award of the EPC Contract to Stork-Wartsila at the price agreed in January 1996 was unreasonable in the circumstances, especially bearing in mind the lower rival Hyundai bid at the same time, IPTL's motive does not matter. IPTL will in those circumstances have been in breach of the term which the Tribunal has concluded should be implied, namely that IPTL must have acted reasonably and prudently in the procurement of the EPC Contract and other contracts, and the damages to which TANESCO would prima facie be entitled would be such as to put it in the financial position in which it would have been had IPTL and its agents acted reasonably and prudently. So, if the Tribunal concludes that the EPC Contract should have been procured at a lower price (either from Stork-Wartsila or Hyundai), the tariff must, in the result, be calculated on the hypothesis that such lower price had been agreed.

8. Was IPTL in breach of its obligation to act reasonably and prudently in relation to any costs and expenses which would have an impact on the amount prima facie payable by TANESCO as the Capacity Payment element of the Reference Tariff, and in particular in relation to the procurement of the EPC Contract?

76. As the Tribunal concluded in its Decision on Preliminary Issues of Construction/Law, the Capacity Purchase Price element of the Reference Tariff fell to be adjusted by reference to any changes in the assumptions listed in Mr Rugemalira's letter of 31 May 1995.

77. We further concluded that it was for IPTL to establish what costs and expenses were incurred under each head, and that TANESCO then had the burden of establishing, if it could, that any part of such costs or expenses was unreasonably or imprudently incurred, on the basis of the information and in particular the documents which IPTL was obliged to furnish.

78. An analysis of TANESCO's attack on the amounts claimed by IPTL to have been incurred by way of costs and expenses shows that they fell into two categories, namely:

(1) A challenge to the assertion that costs or expenses had been incurred at all, and if incurred, whether for the purposes of the Tegeta Project; and

(2) A challenge as to the reasonableness of the cost or expense, and thus the reasonableness and prudence of IPTL's conduct.

A. The EPC Contract:

79. This was the subject of TANESCO's principal attack, and occupied a substantial proportion of the parties' submissions and evidence. A lot of money turns on this item, and we therefore think it right to deal with it in some detail. The main evidence presented was of two kinds, namely:

(1) Evidence of the cost of other projects around the world which were said by one party or the other to be "comparable" or at least to afford some guidance (with adjustments where appropriate), backed up by the opinions of experts;

(2) Evidence of the process whereby the EPC Contract came to be awarded to Stork-Wartsila at the agreed price.

There was also evidence presented through Mr Chambless based on published data of prices in the North American market, which we will mention hereafter, but which we regarded as not particularly helpful.

80. In relation to the costs of other projects, a degree of caution is clearly necessary, since every project is different, and quite apart from differences in specification, including the required fuel type and basic technology involved, allowance may have to be made for such matters as the country in which the project is located and the associated political risk, the accessibility of the site, the location in relation to the sourcing and price of labour, equipment and materials, inflation over time, and currency fluctuations. One must also bear in mind the relative market situation in terms of

supply and demand, including individual companies' order books and backlogs. Further, even if, looked at objectively in comparison with other projects at other places and at other times, the price of a project might appear to be high, market forces may still dominate, and provided that the would-be purchaser adopts an appropriate bidding strategy and gives an opportunity of bidding to a sufficient number of likely interested suppliers, and thereafter negotiates in a proper manner, he will prima facie have acted reasonably and prudently.

81. The Tribunal does not think it helpful to attempt a detailed analysis of the considerable amount of material put before us on both sides relating to allegedly "comparable" projects - an exercise which has helpfully been reviewed by both parties in their Post-Hearing Memorials following detailed presentations in their earlier written submissions on which the witnesses elaborated at the hearing. We do think it worthwhile, however, to make the following points regarding this evidence.

82. Nowhere are the problems associated with an analysis of "comparable" projects more clearly illustrated than in the parties' evidence regarding the 74 MW Kipevu II project in Kenya. Understandably, both parties addressed Kipevu II as the project geographically nearest to the Tegeta Project and by virtue of this basic fact alone arguably comparable. Moreover, it appears also to be a Stork-Wartsila project using diesel engines identical to those installed at Tegeta.

83. In the first affidavit submitted on this subject by IPTL, Mr Fred W. Campbell, a project manager in the Energy Division of Burns & McDonnell Engineering Company

of Kansas City, Missouri, USA, sought to justify Stork-Wartsila's EPC price by reference, inter alia, to the $85 million price tag which the parties accept as published by the World Bank in respect of Kipevu II. Although it is clear from the World Bank documents that, as Mr Campbell stated, "the cost of the Kipevu II *project* is $1135/KW" ($85 million ÷ 74 MW = $1,135/KW), it does not follow that this is, as Mr Campbell went on to say, "virtually the same as the $1,140/KW of the Tegeta Project," since this latter figure represents only the *EPC cost* of Tegeta ($114,000,000 ÷ 100 MW = $1,140/KW), and not the *overall project* cost. (Emphasis added). Such an obviously faulty analysis could not possibly justify the conclusion, made by Mr Campbell on the basis of Kipevu II (as well as other projects), that "the EPC price of the Tegeta Project is within international norms". On the other hand, it is evident that there are significant aspects of Kipevu II that suggest the possibility that it may entail less EPC work than Tegeta, whose per-KW cost then could naturally be higher. Thus, Kipevu II was to be located on land already cleared and adjacent to Kipevu I, an earlier (and similar) state-owned project, as well as to an even older state-owned steam power plant known simply as Kipevu and a new barge-mounted gas turbine independent power project fired on condensate (known as Westmont Power). TANESCO's expert Mr Alfred Lippert, a Chief Mechanical Engineer with Lahmeyer International GmbH of Bad Vilbel, Germany, when examined at the hearing, quite understandably could not express an opinion whether in the circumstances the Kipevu II EPC costs would have included, for example, construction of any access roads, interconnection to the Kenyan power grid, substation upgrades, housing, or two years' supply of spare parts, all of which were required in Stork-Wartsila's EPC contract for Tegeta. Mr Lippert agreed that "it was reasonable" for Hyundai to have bid about $8

million for such "provisional items" required in the Tegeta EPC Contract. In addition, he acknowledged that Stork-Wartsila was required to level and clear the Tegeta site, whereas the Kipevu II site had already been prepared. As Mr Lippert also acknowledged, the Kipevu II site is such that fuel delivery can be accomplished simply by constructing a 50-metre spur into the existing pipeline already serving nearby generating plants, thereby obviating the trucking and associated facilities required at Tegeta.

84. Even had Kipevu II and Tegeta involved identical requirements in all respects, however, it was demonstrated to the Tribunal's satisfaction that because of currency fluctuations the period of time separating the two EPC price agreements could render them wholly incomparable. While the Stork-Wartsila EPC price of $114,188,560 for Tegeta was fixed on 22 January 1996, the PPA for Kipevu II was signed only in November 1998. Neither party could provide a date as of which an EPC price had been fixed with respect to Kipevu II, and the evidence was that at least as of 13 January 2000 no construction work had taken place there. As IPTL pointed out, at the time Stork-Wartsila had fixed the Tegeta *EPC price* of $114,188,560, that sum (rounded to $114 million) represented Dfl. (Dutch guilders) 190,254,601, but as of 29 June 2000 that same guilder sum equalled $81,415,166, or several million dollars *less than the entire project cost* of Kipevu II, which is three-quarters the size of Tegeta. (Emphasis added). While Stork-Wartsila doubtless procured much in dollars, or in other non-guilder currencies, the point remains: clearly comparisons unadjusted for such factors are of little value, if any.

85. The difficulties in analyzing "comparable" projects thus illustrated necessarily increase the further away one gets from a presumptively somewhat similar situation as is presented by Kipevu II. Thus, the Tribunal finds it can draw but limited comfort from Mr Lippert's reliance on three other projects also using Stork-Wartsila engines identical to those installed at Tegeta, namely: Tapal, in Karachi, Pakistan; Zamboango, in the Philippines; and Lufussa, in Honduras. Still less can one be materially influenced by any of the seven additional projects on which TANESCO relies, all of which use Stork-Wartsila's "next largest engine", the 18 V46, and which are located variously in Bangladesh (Haripur); India (Tamil); Jamaica (Old Harbour); Pakistan (Karachi and Kohinoor); the Philippines (Luzon); and Vietnam (Ba Ria-Vung). It is noteworthy nonetheless that one of these, Old Harbour in Jamaica, is asserted to cost overall $1,353/KW (as compared to Tegeta's $1,500/KW). Moreover, as to a great number of the projects on which Mr Lippert gave evidence, the only information available apparently consisted exclusively of news reports from wire services and the like.

86. It is thus hardly surprising that in these proceedings IPTL vigorously questioned the usefulness of such evidence laid before us by TANESCO, and, apart from the early affidavit of Mr Campbell, itself abjured resort to such sources. The Tribunal is constrained to conclude, however, that IPTL's evidence in response, consisting of an expert estimate of the actual cost of building the project in issue, is equally flawed, both in concept and in execution.

87. TANESCO rightly points out that the best evidence of actual costs would presumably be found in Stork-Wartsila's own EPC construction records. Although Stork-Wartsila is not a party to this arbitration, the fact that, as IPTL has advised us, Stork-Wartsila is still owed in excess of $28 million in EPC Contract payments (including claimed interest), has previously collaborated with IPTL's parent company as a potential joint venturer on the project, and apparently had made some documents available to IPTL for use in this arbitration (including for the use of its cost estimation expert, Mr Chambless) at least raises a question as to why its construction cost documentation was not supplied to the Tribunal. The Tribunal does not go so far, however, on the record before it, as to draw any inferences in this regard, for which TANESCO in any event has not specifically asked. The fact remains, nonetheless, that the evidence presented by IPTL is essentially of an expert nature.

88. That evidence consists of three affidavits, supplemented by testimony at the hearing, from Mr Donald L Chambless of R.W. Beck International Ltd. ("R.W. Beck"). Essentially, Mr Chambless led a team, other members of which visited the site at Tegeta, that gathered various data on the basis of which it concluded that Stork-Wartsila's EPC price of about $114 million was a "fair price" and "reasonable". It is notable, however, that in pricing all construction items, apart from "historical data" and "our experience in estimating projects of this type for over forty years", the team relied on reference works such as R.S. Means Construction Cost Data and Richardson Engineering Service Inc.'s Process Plant Construction Estimating Standards, which it was agreed are sourced only from United States experience and information. The relevance of those reference works to a project in Tanzania is debatable, and indeed

has been vigorously contested. The fact that R.W. Beck has relied on these same authorities in evaluating 40 or so projects outside the United States for prospective lenders poses questions as to the identity and nationality of the lenders, the extent to which the projects evaluated were sourced in the United States and how linked the projects otherwise were to the United States. Regardless of the answers to those questions, such reference works alone cannot be authoritative as regards the Stork-Wartsila EPC contract for Tegeta. The force of this testimony was further reduced by a few admitted mistakes, and in particular, the admitted reliance on multiple hearsay for the price of the turbines, the largest single element of the EPC.

89. After detailed cross-examination of the respective experts concerning the projects upon which they relied, on the one hand, and their estimates, on the other, it appeared that many apparent marked differences among projects could be explained by the sorts of factors outlined in paragraph 80 above. The broad conclusion of the Tribunal is to the effect that, generally speaking, medium speed diesel engine facilities tend to be less expensive than low speed diesel engine facilities, and that the EPC Contract price agreed between IPTL's agents and Stork-Wartsila, while not wholly out of line with other projects, when appropriate adjustments had been made, looked to be "on the high side".

90. Turning to what we regard as the more relevant evidence as to the process whereby the EPC Contract came to be awarded to Stork-Wartsila at the price agreed, IPTL employed KTA Tenaga to prepare the project specifications, and to prepare and review tender and bid documents.

91. KTA Tenaga submitted preliminary tender documents to a number of potential bidders in October 1994, as a result of which preliminary price quotations were received from Stork-Wartsila, Hyundai and MAN B & W. Stork-Wartsila quoted US$53,058,000 for the supply of 11 x SW 38 medium speed diesel engines only. MAN B & W quoted DM154,175,000 (approximately US$102 million) for a plant using 9 x 92 58/64 medium speed diesel engines. Hyundai quoted US$99,705,000 for a plant using 5 x Hyundai - MAN B & W low speed engines, or alternatively US$91,099,000 for 8 x medium speed engines (a difference of approximately US$8.6 million).

92. Further revised tender documents were submitted to a number of potential bidders in June 1995. It was not suggested that the list of addressees was insufficient or that there was any obvious omission from it. Stork-Wartsila, Hyundai and MAN B & W again submitted bids. According to the bid documents, the Stork-Wartsila bid was for a total price of US$124,078,200, including a provisional sum of US$17,000,000 for conversion to natural gas firing. Hyundai's bid was for a total price of US$141,472,350, which included US$29,071,800 for gas conversion. MAN B & W's bid, which was now for 6 x 48/60 series engines, was for a total price of US$114,306,671 including US$7,857,000 for gas conversion. Some of the figures quoted in KTA Tenaga's Tender Summary Sheet are slightly different, but the differences are not significant. It should be mentioned that Stork-Wartsila's bid provided for completion in 14 months, whereas Hyundai's bid was for completion in 22 months.

93. It was appreciated that the time factor and cost of gas conversion made the Hyundai bid uncompetitive, and in August 1995 Hyundai wrote putting forward an alternative proposal to use dual fuel engines. On 14 September 1995 Stork-Wartsila submitted a revised price schedule, in which it was said that the price for gas conversion had been reduced to US$11.5 million, and that it generally reflected a reduction in price of about 5%. This revised price schedule was presented at a meeting in Kuala Lumpur, at which the possible joint venture or "Construction Consortium" division of work between Stork-Wartsila and Mechmar was discussed. The total price then proposed was Dfl.170, 221,875, being the equivalent of US$104,430,280, of which Stork-Wartsila's share of the works totalled Dfl.148,123,793.

94. In December 1995 KTA Tenaga produced a detailed "Tender Adjudication Report", the version in the arbitration file being dated 29 December 1995, which summarised what were described as the final tender prices, in US dollars, as follows:

Stork-Wartsila	US$103,470,000 (without gas conversion) US$114,990,000 (including gas conversion)
Hyundai	US$117,566,100 (without gas conversion) US$126,788,900 (including gas conversion)
MAN B & W	US$106,449,671 (without gas conversion) US$114,306,371 (including gas conversion)

KTA Tenaga made a Preliminary Evaluation of the three tenders, in which points were allocated for technical compliance with the tender documents, commercial terms, completion time, experience and power track record, price, guarantees and O&M proposal. Of a possible 120 points, Hyundai "scored" 104, Stork-Wartsila 91

and MAN B & W only 55. In the Technical Evaluation, KTA Tenaga noted that Hyundai had offered slow speed diesel engines, which they observed should mean less maintenance demand, while the medium speed engines offered by Stork-Wartsila were said to have a higher fuel consumption. The time for completion quoted by Hyundai was said to be 19 months, with the first engine to be commissioned in 16 months from the date of the award of the contract, as against 15 months for Stork-Wartsila, with the first three units ready within 10 months from the award of contract, and the export of power commencing after 13 months. Under the heading of "Experience", KTA Tenaga commented that the W38 medium speed diesel engines offered by Stork-Wartsila were relatively new and that no W38 engine had been operated on natural gas. Despite taking account of the fact that Hyundai did not seem to have had adequate experience of working in Tanzania, under the general heading of "Experience" Hyundai was rated marginally higher.

95. KTA Tenaga's "Conclusions" include the observation:

> ...It is apparent that [Hyundai] has given the most attractive techno commercial offer....

With regard to the slow speed engines offered by Hyundai, KTA Tenaga observed that, because of their lower running speed, the wear and tear on the engines and parts should be lower, leading to a more lasting engine, and that the level of sophistication of the slow speed engine was much lower than that of the medium speed engine, thus leading to lower maintenance and a lower level of technical skills to maintain the

engine - an important consideration in a developing country like Tanzania. Its final "verdict" was encapsulated in a passage on the penultimate page:

> This is the case of purchasing a cheaper plant against a technically better plant that is likely to perform reliably in the long run.

96. Thus far, there would seem to be no basis for criticising the conduct of IPTL or its agents, although, against this background, it may be thought odd that on 29 December 1995, Mechmar wrote a "STRICTLY PRIVATE AND CONFIDENTIAL" letter to Stork-Wartsila expressing Mechmar's interest to work with Stork-Wartsila for the Tegeta project. But it was made clear in the letter that there was no legally binding commitment.

97. It was the developments in the last stage of the evaluation of the bids and the award of the contract which were particularly criticised by TANESCO. KTA Tenaga met with Hyundai on 15 and 16 January 1996, following which Hyundai submitted a revised tender on 22 January, reducing its price, including gas conversion, by approximately US$10million to US$116,610,400. On 17 January 1996, KTA Tenaga also met with Stork-Wartsila, which on 22 January 1996 submitted a revised tender in the sum of US$114,188,500 (excluding gas conversion of US$11,543,000), and a total including gas conversion of US$125,731,500. Thus, on pricing, the relative position as between Stork-Wartsila and Hyundai had been suddenly and dramatically reversed. As a result of Hyundai's reduction in price of approximately US$10million and Stork-Wartsila's increase of approximately US$10.7million, the Hyundai bid was now approximately US$9million cheaper.

98. KTA Tenaga produced a further "Tender Adjudication Report" in January 1996, which largely reproduced its December Report, but which omitted much of the detailed discussion in the "Conclusions" to which we have referred, and simply concluded "From the technical evaluation both of the offers are equivalent". Significantly it omitted all discussion of price. On the second page of the Introduction, it is stated:

> This report concerns the technical aspects of the two submission [sic] and clarification but does not include the economic/financial aspects which Mechmar Corporation has instructed that they are conducted by Fieldstone Private Capital Group.
>
> As such, this Report cannot make a complete recommendation for Contract Award which is the responsibility of Mechmar Corporation to combine the technical and financial reports before deciding on the Award.

There is no document in the file containing Fieldstone's economic/financial analysis, and in his oral evidence, in answer to questions from the Tribunal, Mr Willy Lim, the Managing Director of Fieldstone, confirmed that Fieldstone had not been asked to review the financial aspects of the January bids from Stork-Wartsila and Hyundai, and played no part in the financial negotiations. Further, there is no document in the file reflecting Mechmar's decision or recommendation to IPTL.

99. It is the view of the Tribunal that, against the background that in December 1995 IPTL's technical consultants, KTA Tenaga, had advised that the Hyundai proposal was "a technically better plant that is likely to perform reliably in the long run", the undocumented decision to award the EPC contract to Stork-Wartsila at a significantly

higher price seems illogical, and raises very serious questions as to whether IPTL acted reasonably or prudently in taking the decision it did.

100. In his second witness statement, Datuk Majid, the Chairman of IPTL, put forward a number of reasons why IPTL decided to award the EPC contract to Stork-Wartsila rather than Hyundai. The Tribunal accepts that in accordance with the Stork-Wartsila bid, the engines would be "on line" a little earlier, but many of the other reasons put forward seem to us to be spurious. KTA Tenaga had carried out a detailed technical evaluation of the two bids, and even if one accepts the rather "watered down" statement in the January 1996 Report, and ignores the more detailed comparison in the December 1995 Report, it had concluded that the bids were technically "equivalent". The suggestion that the Hyundai revised bid was less credible because it had dropped its price by a substantial amount at the last minute is itself incredible to the Tribunal. It is readily understandable, that in the course of a competitive bidding process, especially if the competitors are aware of what others are bidding (which may or may not have been the case here), a would-be contractor will be willing to drop his price in order to secure the contract. On the other hand, one would have thought that a last minute *increase* of US$10 million in the bid price would have given more cause for concern, and would not only have raised serious questions about the reliability of Stork-Wartsila's pricing methods, but would or should have met with a considerable resistance. There is no other evidence to support the suggestion that Fieldstone had advised that the Hyundai engines would not be financeable on a limited recourse basis, and the suggestion that IPTL did not feel that it could reasonably proceed on the basis of Hyundai's dual-fuel engine proposal is simply contrary to the evidence. That

was the proposal which had been evaluated by KTA Tenaga in December 1995. The "relatively small difference in price" to which Datuk Majid refers in paragraph 16 of his second witness statement was US$9 million, which even in percentage terms cannot sensibly be described as "small". It was suggested on behalf of IPTL that the, or at least a major, consideration was that the Hyundai revised proposal of January 1996 was expressed to be only valid up to 21 February 1996 "unless otherwise mutually agreed", whereas the contract could not have been concluded until financial close; Stork-Wartsila , on the other hand, maintained its price until the EPC Contract was eventually signed in February 1997. But Datuk Majid did not identify this in his statement as one of the reasons which had motivated IPTL at the time, and there is no evidence that IPTL or Mechmar ever went back to Hyundai to ask for its revised bid to remain open for longer. In IPTL's Post-Hearing Memorial, it is said, in paragraph 100:

> IPTL was unable to produce documentation which established that this $10 million increase was based on locking the price in. IPTL submits that this lack of documentation reflects bad record-keeping on this point and nothing else.

101. There is no contemporaneous document containing any explanation for the increase, nor any record of discussion either between IPTL and its advisers, or between IPTL or its advisers and Stork-Wartsila. The Tribunal does not accept that IPTL has demonstrated any sufficient reason for choosing the Stork-Wartsila bid. It is said that the lenders and lenders' engineers accepted the price as reasonable for the project and lent money on the basis of the US$114 million contract price. But there is no evidence that they were made aware of the fact that:

(1) Stork-Wartsila's price had been revised upwards by US$10 million, apparently without explanation, at the last minute; or

(2) That the Stork-Wartsila price was then US$9 million higher than the competitive bid from Hyundai, which IPTL's technical advisers had concluded only one month previously to be technically superior.

102. The Tribunal does not consider that on this point it was assisted by expert opinion as to whether or not the final Stork-Wartsila bid price was reasonable or unreasonable in an objective sense or, for example, as to whether or not the gas conversion process for the medium speed engines would have been more or less difficult than for the dual fuel slow speed engines offered by Hyundai. We are concerned essentially with determining whether IPTL acted reasonably and prudently in opting for Stork-Wartsila after the revised bids in January 1996. The Tribunal concludes that it did not. This constituted a breach of the term which we have held must be implied into the PPA and Addendum No. 1. It is not possible to reach any firm conclusion as to whether, if IPTL had acted reasonably and prudently, it would have accepted the Hyundai revised bid, or instead would have successfully resisted (at least substantially) Stork-Wartsila's last minute price increase. Either course would probably have passed the reasonableness and prudence test. The Tribunal must therefore adopt a "broad brush" approach, and concludes that, in order to compensate TANESCO for the breach, for the purposes of the adjustment of the Reference Tariff under Addendum No. 1, the EPC Contract price should be reduced by US$10 million.

B. Other issues concerning the adjustment of the Capacity Payment Element of the Reference Tariff

(1) The Cost of Housing:

103. In relation to the EPC Contract with Wartsila, TANESCO raises the further specific point that IPTL was in breach of its duty to act reasonably and prudently by failing to take any steps to procure a reduction in price based on the reduced scope of housing built. In doing so, it relies on the following facts:

The housing specification required the EPC contractor to build at least a total of 37 units, including 6 single storey semi-detached houses, 30 units of single storey houses and one unit 1½-storey clubhouse and facilities. This did not change. Item 26 of Wartsila's Final Tender Price of 22 January1996 provided the basis for the EPC Contract and included the sum of US$7,566,000 for "Provisional Items as specified in Section 3.7.16. Staff Housing for Residential Staff and Executive Staff". However, the EPC Contract signed on 4 February 1997 provided that the housing scheme should consist of only 6 units of single-storey semi-detached houses, and 4 units of single-storey bungalows. According to the evidence of Mr Lippert, the value of the houses actually built was only approximately US$780,000;0 IPTL puts the value at approximately US$1.7 million.

104. In IPTL's Counter-Memorial it was said that IPTL determined that the cost associated with the housing project was too high and therefore decided to limit the size of the project. But if that were done before the specification was changed in the EPC Contract of 4 February 1997, as it seems it must have been, one asks rhetorically:

Why was the price not changed? In his oral evidence, Datuk Majid emphasised that this was just a provisional sum, and that the housing was never completed because of TANESCO's Notice of Default. But this appears not to have been the case. The limited number of houses specified in the 4 February 1997 EPC Contract were built. But even if Datuk Majid's evidence was correct, then the provisional sum stated in the Tender and included in the contract price should be correspondingly reduced. The Tribunal concludes that, for the purpose of the adjustment under Addendum No. 1, the EPC Contract price should be reduced by a further sum of US$6 million.

(2) Development Costs:

(a) Staff and Management Costs:

105. IPTL claims to have incurred US$6,238,000 as "Development Costs", compared with the US$4,800,000 estimated in May 1995, and which included US$5,385,000, stated to be "Staff and Management Costs". In response to TANESCO's enquiry, these were said to be the costs charged by Mechmar to IPTL for four years of work performed by Mechmar's directors and employees. When asked for a breakdown by reference to the individuals concerned, the nature of their work and the amounts billed in respect of each individual, IPTL claimed to have been unable to provide any such breakdown.

106. The loan drawdown documents which were produced by IPTL show two payments made respectively to "Omni Technical Management Establishment" ("OTME") and "Prime Consolidated Establishment" ("PCE") which together totalled US$5,350,000. Mechmar's accountant had submitted a letter to the lenders in support of a drawdown payment in July 1997, stating that the payments were supported by a Sale and

Purchase Agreement between IPTL and OTME for project development services, and a further agreement between IPTL and Aeromore Corporation (M) Sdn Bhd. ("ACMSB") and a further agreement between ACMSB and PCE, for the provision of financial services. TANESCO asked for copies of these agreements and was eventually informed by counsel for IPTL on 9 December 1999:

> The payments to OMNI Technical Management and Prime Consolidated Management were not payments pursuant to contracts or invoices. Rather, they were inter-company transfers and funds between Mechmar and its subsidiaries. The transfers had no relevance to the IPTL project, and neither OME nor PCE were involved with the IPTL project.

In the course of the hearings in March 2000, Counsel for IPTL confirmed that, according to his instructions and despite the statement of Mechmar's accountants referred to above, there were no documents and no agreements. A statement from Mechmar's Chairman, Mr Tan Kean Wan, dated 27 March 2000, explained that amounts paid by Mechmar to its management and staff as well as to "consultants and vendors" were financed by borrowings from OMTE and PCE pursuant to the agreement referred to in the accountant's letter. His statement refers to staff and management costs totalling 13,676,845 Malaysian Ringgits (which appears to be a precisely calculated figure), but no documents have been provided in support.

107. TANESCO suggests that the figures claimed were simply invented, and the alleged agreements fabricated. It further contends that the amount of staff and management costs claimed is so large as to "bend credulity". Based on the evidence of TANESCO's "expert" Dr Swales, it is suggested that a reasonable amount to allow,

using the rates which Mechmar is said to have charged for its management and staff, being 250 Malaysian Ringgits (US$100) per man-hour for director level and 150 Ringgits Malaysian (US$60) per hour for associate and analyst level, would be US$1,280,000.

108. It is worth mentioning at this stage that Dr Swales of Acres was presented to the Tribunal as an expert witness. He is no doubt a great expert in his field, with considerable experience of international projects of this kind. But he was very much involved with this project at the material time as consultant to TANESCO and the Government of Tanzania. He was not favourably disposed to the IPTL project, considering it to be unnecessary and undesirable in the light of the rival SONGAS project, and he represented TANESCO in negotiations which took place in 1998. It could not be suggested that he was an independent or disinterested expert. Indeed, he was clearly a partisan witness who viewed matters through "TANESCO-coloured spectacles", and whilst the Tribunal pays due regard to his opinions, clearly in these circumstances they have to be weighed with some caution. As he frankly conceded in cross-examination, he was doing his best to support his client's case.

109. IPTL submits that Mr Tan's explanation concerning the involvement of OTME and PCE should be accepted, especially since he was present during each day of the hearings but no request was made to cross-examine him on this point; that the development costs claimed are in line with industry norms; and that since the lenders accepted the claimed development costs as part of the project cost, TANESCO should do likewise.

110. This last submission of course misses the point that the payment by the lenders was itself based on the accountant's statement to which we have referred. The fact is that no documents have been produced to support the figure claimed. The burden must be on IPTL to establish that the development costs which it claims to have incurred and which were greater than those estimated at the time the PPA was concluded were in fact incurred. The burden of proof may then shift to TANESCO to establish on the basis of the documents and other evidence, including expert opinion, that they were not incurred reasonably or prudently. It was pointed out by Dr Swales in cross-examination that the "Development Costs" in relation to the neighbouring Kipevu II project, which TANESCO relied on in its extensive study of comparable projects for purposes of trying to establish the unreasonableness of the EPC Contract, were US$6.1 million, which is very much in line with the sum claimed in this case. But as Dr Swales also pointed out, "Development Costs" may vary considerably from one project to another, depending, amongst other things, on how much work is done "in-house".

111. Taking all these considerations into account, the Tribunal concludes that a reasonable figure for staff and management costs is US$2.5 million.

(b) Interest Charges and Related Legal Fees:

112. The sum of US$294,525.28 is said by IPTL to have been incurred as interest charges, being part of its Development Costs; and a further US$59,157.25, out of total legal fees of US$129,519.68, were claimed as legal fees in connection with various bank loans.

6238
2.5
3733

113. TANESCO challenges these figures on the basis that there is no evidence to link the loans or the interest or legal charges to the IPTL project, other than from Kassim Chan, the accounting firm who confirmed the payments to OTME and PCE, which we have dealt with above. TANESCO further poses the question: If Mechmar borrowed US$5,385,000 from OTME and PCE (as was claimed), why did it need to borrow from banks?

114. In relation to the interest charges, IPTL conceded in its Post-Hearing Memorial that, since it was deriving a return from the equity, interest charges relating to the raising of that equity should be for its account, and agreed to omit this figure from the final financial model. Logically, the legal fees in connection with the loans must also be omitted, bringing the legal fees down to US$70,362.20. This reduced figure is, as we understand it, accepted by TANESCO as part of legitimate "Development Costs", as is the cost of technical and financial advisers, being US$135,741.74 and US$45,472.44 respectively, lenders' "due diligence" in the sum of US$122,382, and "Miscellaneous" of US$12,105.91.

(c) Travel Costs

115. The last point on which TANESCO takes issue in relation to the claimed "Development Costs" is the sum of US$169,209 claimed as travel reimbursement. Again, no underlying invoices or vouchers have been made available to TANESCO, or indeed to the Tribunal. TANESCO contends that in these circumstances these costs should be wholly disallowed. IPTL points out that the project was an international one, being developed between Tanzania and Malaysia with the main

contractor located in The Netherlands. A considerable amount of travel was clearly involved, and it is not suggested that the sum claimed (which was accepted by the auditors) was unreasonably incurred. In addition to the general point, TANESCO contends that a small portion of the travel cost claimed, amounting in total to US$12,913, related to travel to India, Burma, Thailand and Uganda, and would appear to have nothing whatever to do with the IPTL project. IPTL contends that these reflected part of the project development efforts. It is a small sum, and taking account of this, and in the absence of detailed evidence, the Tribunal allows US$150,000.

(d) Summary

116. In these circumstances, the total to be allowed in respect of Development Costs is as follows:

	US$
Staff and Management Costs	2,500,000.00
Interest	Nil
Legal fees	70,362.20
Technical advisers	135,741.74
Financial Advisers	45,472.44
Lenders "Due Diligence"	122,382.00
Travel Reimbursement	150,000.00
Miscellaneous	12,105.91
Total	US$3,036,064.29

Thus, in respect of this aspect of the cost, the 1998 figure of US$6,238,000 put forward by IPTL falls to be adjusted downwards by approximately US$3.2 million,

and in consequence the May 1995 figure falls to be adjusted downwards by approximately US$1.8 million.

(3) The Cost of Raising Equity:

117. This item comprises sums paid to consultants, banks and legal advisers by way of fees in relation to the raising of the necessary finance for its 30% equity contribution through a term loan and "rights" issue. As Dr Swales pointed out, under the PPA, IPTL was obliged to fund and maintain a 30% equity participation in the project, which suggests that the costs of and associated with the raising of that equity contribution should not be regarded as part of the project costs.

118. IPTL's response is that the agreed internal rate of return ("IRR") of 22.31% was to be a "net" return, so that if IPTL had to raise funds to finance its equity contribution and to pay fees and expenses in relation to such financing, these should be taken into account.

119. The Tribunal considers that in respect of this item, IPTL's contention is wrong in principle. The PPA required IPTL to finance the project as to 30% with its own equity "contribution", the remaining 70% being by way of loans. The underlying assumption was that the 30% would be contributed by IPTL. Whether it did so by using its own capital or by way of a "rights" issue or bank loan is not in the view of the Tribunal properly to be regarded as part of the project cost to be taken into account for the purposes of arriving at the agreed IRR.

120. TANESCO is, properly in our view, prepared to allow project advisors' fees, such as an invoice from Long & Co relating to legal advice and project documentation, as well as the fees paid to Fieldstone, which was agreed at 1% of the project debt. According to IPTL, the financial model for determining the Reference Tariff is geared to adjust the amount of Fieldstone's fee automatically, depending on the Tribunal's decision on the amount of reasonably-incurred total project cost.

(4) KTA Tenaga's Costs:

121. IPTL has claimed that it paid KTA Tenaga the equivalent of a total of US$2,559,055 for "consultancy services" during the project-implementation stage from July 1997 to June 1998. It is not disputed that IPTL had a commitment to pay this sum (as to 25% on appointment and the balance over 12 instalments) nor that it was in fact paid. But TANESCO, again relying on the opinion evidence of Dr Swales, suggests that the sum is "exorbitant". Dr Swales would only be prepared to allow US$610,000 as a reasonable sum.

122. TANESCO points to the fact that Stork-Wartsila was engaged as the EPC contractor, and that, as such, Wartsila's tasks would have included the design, engineering, procurement, construction, installation, testing and commissioning of the power station. Furthermore, KTA Tenaga was apparently paid the sum of US$124,016 in 1995, plus travel expenses of US$11,726, for its involvement in the initial feasibility study and the obtaining of approvals. Finally, it was pointed out that IPTL paid US$84,791 to Messrs Burns & McDonnell as engineering consultants to the lenders,

for "construction progress review", and claims to have paid a further US$354,177 to KTA Tenaga for the services of engineers, resident site staff and related expenses.

123. IPTL responded to these points quite briefly, contending that KTA Tenaga's fees of less than 3% of the contract price were "within industry norms", and criticising Dr Swales for providing no basis for his opinion that their fees should have been lower.

124. Again, the Tribunal is faced with the problem of a "yawning" gap between the parties' respective positions, with a lack of sufficient documentation to assist in resolving the conflict. In particular, two letters which are specifically referred to in KTA Tenaga's invoice cannot apparently be located.

125. This may be another example of where IPTL must take the consequences of its apparently inadequate system of collecting and retaining documents. It appreciated and indeed acknowledged that at the end of the day it would have to justify its costs and expenses as not only having been incurred, but as having been incurred reasonably and prudently. However, again the Tribunal considers that Dr Swales' notional figures for "reasonable and prudent costs" seem too low, and thinks it appropriate to reduce IPTL's claim to US$1.75 million.

(5) Land Costs:

126. IPTL has claimed the "round" figure of US$1 million in respect of its expenditure in the acquisition of land. It claims to have provided documentary evidence to TANESCO of expenditures totalling 389,284,647 Tanzanian Shillings (the equivalent,

at the exchange rate of 600 Tsh = 1 US$, of US$648,807), and to have provided evidence to substantiate its claim that it has been required to reserve a further 2,978,571 Tanzanian Shillings (said to be the equivalent of US$276,666) in respect of disputes and court proceedings with landowners. A list of the payments made appears in the documents but it is said it was thought prudent to reserve a further 100 million Tanzanian Shillings (the equivalent of US$166,666) against potential further litigation. All this is said to total US$1,092,139.

127. However, the Tribunal finds it difficult to follow IPTL's submissions and calculations in relation to the relevant document at page I 0785-6 (JA 323). The 389,284,647 Tanzanian Shillings expended seems clear. But the further sum of 2,978,571 Tanzanian Shillings does not appear to be described as a reserve at all, but rather the total of sums which have been paid to the Ministry of Land. Furthermore, at the exchange rate of 600 Tsh = 1 US$, this would amount to only about US$5,000. The sum for "contingent liabilities" is said to be 166,000,000 Tanzanian Shillings (which at the same exchange rate would amount to US$276,666) which does not appear in IPTL's calculations on page 91 of its Post-Hearing Memorial. The total figure stated in the relevant document said to reflect "Payments made by IPTL in connection with Project Site Land Compensation, Right of Way etc" is 655,284,649 Tanzanian Shillings, which reflects the US$1,092,140-odd claimed.

128. Dr Swales, in this case as in others, seeming to adopt the position of advocate rather than expert, states that the documents do not support a total expenditure of US$1,000,000. According to him, 266,000,000 Tanzanian Shillings of the money

allocated to land acquisition was not spent, and accordingly he reduces the land acquisition cost to US$594,000. The difference between this and the sum of US$648,807 may be due in whole or in part to the fact that Dr Swales employs a different exchange rate.

129. A total of this item is not dealt with specifically either in TANESCO's Memorial on the Calculation of the Tariff or in its Post-Hearing Memorial, which suggests that it does not set much store by it. In any event, the Tribunal is not persuaded that there is any basis on the evidence to reduce the figure of US$1 million.

(6) US$300,000 Transferred to Omni Management Services Esp:

130. IPTL claimed an equity contribution in relation to this payment, made by transfer to a bank account in Liechtenstein. TANESCO points out that it is wholly unsupported by any invoice or any documentation linking it to the IPTL project. IPTL concedes the point and has agreed to make an appropriate deduction in the final financial model for determining the Reference Tariff.

(7) Insurance:

131. According to TANESCO, there is a dispute concerning "Lenders' Risk" insurance, which IPTL's lenders required IPTL to maintain until the final 24 months before the loan was repaid. It was common ground that the PPA requires TANESCO to pay for risk insurance obligations imposed on IPTL by its lenders. According to Dr Swales, the IPTL financial model reflects a declining cost for this insurance over the 5 years of cover, being the maximum duration for which it would be quoted. Thereafter, it

assumes that the premium remains fixed for the rest of the project. Dr Swales, supported in this aspect of his evidence by Mr Matthews, contends that the obligation should end at the end of the sixth year when the obligations imposed by the lenders come to an end. Mr Willy Lim of Fieldstone contends that these "sovereign risk" insurance premiums properly apply to both the debt and equity financing of the project, since it is required not only by the lenders but also by the equity investors. He contends that insurance is reasonable and customary for the cost to be included as part of the project costs for the duration of the project for tariff calculation purposes.

132. This issue will not affect the tariff for the first few years, but in the view of the Tribunal Mr Lim is probably correct and the appropriate premiums should be taken into account. Dr Swales does make what seems to us to be a valid point that when the seventh year is reached, that part of the financing covered by the loans will have been repaid and need not be covered by insurance. Furthermore, the premiums might properly take account of the declining value of the plant. The Tribunal makes no deduction in respect of this item, but expects the parties to take these observations into account in due course.

(8) Exchange Rates:

133. TANESCO asserts that for the purposes of calculating its equity in the project, IPTL has used a constant exchange rate of 2.54 Malaysian Ringgits to the US Dollar, whereas the actual exchange rate on the date for each of the nine drawdowns on the project loan was greater than 2.54. This is said to have resulted in an overstatement of IPTL's equity contribution by US$1,373,117.

134. IPTL contends that TANESCO's assertion is misconceived, and denies having used the wrong exchange rates. The bulk of the equity contributions in dispute relate to the disbursement of development expenses and other project expenses prior to the financial closing of the project. From the first quarter of 1994 to the second quarter of 1997, Dollar/Ringgit exchange rates fluctuated very little (being in the range 2.4373 to 2.6885). The lenders and the auditors accepted a flat rate over the period of 2.54, being an approximate average of these rates.

135. On this point, the Tribunal concludes that IPTL is right in principle, and that TANESCO's complaint is not justified.

(9) Mobilisation:

136. Dr Swales contended that, although the figure for mobilisation costs of US$1.394 million (or US$1.4 million in round terms) should be allowable, it should be fed into the financial model as having been incurred in the 5 months before the start of commercial operations as specified in the O&M Agreement.

137. IPTL concedes this point, and has agreed to adjust the financial model accordingly.

(10) Fuel Oil Reserve:

138. Dr Swales contends that the amount taken for the fuel oil reserve, namely US$3,249,000 is excessive and unnecessary, being based on the assumption that all the fuel oil tanks at the site were or would be full. Dr Swales suggests that when the power station is operating, TANESCO will continue to generate its "base-load" energy

requirements by means of its hydro power capacity, and that the Tegeta plant will be used in its early years, if at all, to meet short term "peak" demand. As a result, to assume that all three 5,000 metric tonne tanks will be filled to capacity, which would provide 30 days operation at 100% capacity, is unrealistic and unreasonable. Dr Swales considers that it would be sufficient to keep only one of the three tanks full, and to transport additional fuel as and when necessary from the additional 15,000 metric tonnes which IPTL is required to keep available at Dar-es-Salaam.

139. Dr Swales also disputes the amount of US$556,000 allowed in the model for industrial diesel oil - a type of fuel which, according to Dr Swales, TANESCO was never advised was needed at the plant.

140. IPTL contends that, under the PPA, IPTL is obliged to maintain the capacity to utilise the plant fully if called upon by TANESCO to do so. Unless and until that requirement is amended, a reserve of 30 days fuel at full capacity is reasonable. Dr Swales' speculation as to the extent to which TANESCO will make use of the available power is irrelevant. The Tribunal tends to agree. With regard to the industrial diesel oil, IPTL contends that the reserve included is a manufacturers' recommendation. On this point, too, TANESCO fails.

(11) Maintenance Reserve:

141. In its Post-Hearing Memorial, IPTL states that it agrees with Dr Swales' comments relating to this issue, and that the financial model has been adjusted to take account of

that agreement. In these circumstances, it appears to be unnecessary for the Tribunal to deal with this matter further.

(12) Gas Conversion:

142. In its Memorial on the Calculation of the Tariff, TANESCO complained that ITL, in its 1998 financial model, had departed from the agreement made in May 1995 that the assumed cost of gas conversion (US$11,543,000) was to be financed as to 70% by debt and 30% by equity, and unilaterally established a Gas Equipment Reserve to be funded through the tariff from the outset.

143. TANESCO contends that the cost of gas conversion should not be included in the tariff unless and until conversion takes place, and that, if and when such conversion occurs, IPTL is obliged to fund the conversion cost in the proportions set out above.

144. In its Post-Hearing Memorial, IPTL states that the parties have agreed on a mechanism with respect to the funding of gas conversion, which is reflected in the agreed-upon financial model. Again, it seems that no further action from the Tribunal is called for.

9. Was IPTL in breach of an implied obligation to act reasonably and prudently in relation to the procurement of the Fuel Supply Agreement ("FSA"), and if so, what are the consequences?

145. As the Tribunal has already explained in outline above, one of the elements in the purchase price and therefore the tariff in respect of power supplied pursuant to the

PPA was the Energy Purchase Price, which included a Fuel Cost Component, which was subject to escalation under Appendix B, Clause 9.1(a) of the PPA on the basis of changes in fuel prices.

146. In the light of these provisions, and insofar as IPTL was responsible for making the necessary contractual arrangements to obtain fuel, the price of which would be reflected in any such escalation, TANESCO contended that IPTL was under an implied obligation to act reasonably and prudently in performing that function. By parity of reasoning to that adopted in relation to the interpretation of Addendum No. 1, considered as part of its Decision on Preliminary Issues of Construction/Law, the Tribunal accepts this submission.

147. The contest between the parties therefore involved a determination whether the arrangements made by IPTL satisfied these requirements.

148. In its Memorial and Submissions on Preliminary Issues of Construction/Law TANESCO submitted that by reason of the alleged breach of IPTL's obligations in this regard, the Tribunal should declare "that IPTL is not entitled to base the Fuel Cost Component of the final Reference Tariff on the contract obtained by it for the supply of fuel". The Tribunal was also invited to declare that IPTL may not "pass-on" any damages for its breach.

149. In its Post-Hearing Memorial TANESCO appeared to change its position somewhat by seeking instead damages. The measure of damages it has submitted should be the

difference expressed in dollars per tonne between the reasonable price and the price specified in the fuel contract - "TANESCO should receive a reduction in its monthly tariff".

150. IPTL, as buyer, entered into the FSA bearing the date 21 May 1997, with Galana Petroleum Limited ("Galana") and Total International Limited ("Total") as sellers. The FSA provided for an initial term of 5 years, with an option for a further 5 years on the same terms and conditions and, thereafter the parties were required to negotiate in good faith for any further period.

151. The complaints of TANESCO in relation to the provisions of the FSA were threefold. First, the process whereby the successful contractor was identified was flawed. Second, the cost of fuel was based on the Singapore rather than the Arab Gulf spot market. Third, the charges for freight, depot throughput, storage and trucking were excessive.

152. TANESCO's case rested on the evidence of Mr William Matthews, an energy consultant. Mr Matthews of course was not involved in the negotiation of the FSA.

153. The criticism that TANESCO levelled against the commercial reasonableness of the FSA was blunted by two factors. First, Mr Matthews was unable to point to any independent power project in Africa which was obtaining fuel under a long term contract on better terms and conditions than those provided under the FSA. Second, not only was there no evidence that anyone else was willing and available to supply

the fuel at a better price and on better conditions than Galana and Total, but, on the contrary, on the unchallenged factual evidence, TANESCO had sought tenders from all the recognised major fuel suppliers in the region, none of whom, with the exception of Galana and Total, was interested enough to tender for the FSA.

154. IPTL, for its part, relied largely on the evidence of Mr Donald Wessel who also was not involved in the negotiation of the FSA. Mr Wessel gave a number of persuasive explanations for the lack of interest by potential suppliers, which can be summarised as follows:.

(1) TANESCO was not required by the PPA to purchase any electricity at all. For this reason, the project would have been viewed as having a low probability of success and the contract as a "high risk" one.

(2) The FSA gave a fuel supplier no assurance that it would be called upon to supply a single barrel of fuel oil to the project but it does obligate the supplier to provide fuel oil if and when called upon by IPTL under a set of terms and conditions including a rigid price formula over a 5 year period regardless of any future developments in the market place.

(3) The PPA contemplated that the project might change to natural gas at any time at the option of TANESCO, at which point the FSA would have been have been of no value to the supplier.

155. There is no doubt that the price provided for the fuel, the cost of freight and other charges under the FSA are higher than those quoted on the spot market at the time, as demonstrated by Mr Matthews' evidence. The difficulty with his argument, however, is that reliance upon the spot market, by way of comparison to a long term supply contract, was simply commercially unrealistic. The Tribunal concludes that, although the apparent reasonableness or otherwise of the terms of the FSA may be highly relevant as evidence of the extent to which IPTL acted reasonably and prudently in procuring the FSA on the terms it did, the question at the end of the day remains whether, with greater efforts, it could have procured the supply of fuel on better terms. We conclude that IPTL was obliged to accept the terms of the one and only supplier willing to tender for a long term supply contract.

156. TANESCO submitted that in the absence of full disclosure of all relevant documents it was impossible to form a conclusion that the FSA was the only or the best deal available. It was pointed out that none of the representatives of KTA Tenaga, Fieldstone or Long & Co., who were charged with the responsibility for negotiating with the suppliers, testified that Galana and Total were the only parties interested in bidding on the FSA. The Tribunal has carefully considered the argument that in the absence of further material no conclusion could be formed that the FSA was indeed a contract that a reasonable and prudent purchaser would have entered into. However in the absence of any evidence whatsoever of the availability of any other potential long term supplier the Tribunal rejects the claim by TANESCO that IPTL had breached its implied duty.

157. The Tribunal has noted that under Article 2.4 of the FSA, the agreement was to lapse if notice for the first delivery thereunder were not given within 3 years from the date of the agreement, or such other date as may be agreed. We do not know what if any further agreement or discussions may have taken place between IPTL and Galana and Total, but it may be that TANESCO's complaints regarding the terms of the FSA may have become academic.

10. Waiver/estoppel.

158. IPTL contends that TANESCO waived or should be estopped from exercising any right to question the reasonableness or prudence of its conduct in relation to the costs of the project. As we understand it, the point is put in three ways. First, if there is an implied obligation on the part of IPTL to act reasonably and prudently in relation to the contract awarded and costs incurred (as the Tribunal has held), there must be a concomitant obligation on the part of TANESCO to exercise its right to object within such time as IPTL could reasonably have acted upon such objection. Second, TANESCO "elected" to accept the EPC Contract price by not objecting to the cost and through the confirmation by the Government of Tanzania of its support for the project provided the tariff would be around 10 US cents per kWh. Third, TANESCO should be estopped by acquiescence and/or convention because, with full knowledge of the EPC Contract price, it stood by without comment or protest as IPTL formally entered into the EPC contract with Wartsila and procured the building of the power station.

159. IPTL was no doubt encouraged to raise these pleas by the fact that, in our Decision on Preliminary Issues of Construction Law, the Tribunal indicated that on the material

then available it would have been inclined to the view that TANESCO would have been precluded, by estoppel by convention or acquiescence from raising objection to the change from low speed to medium speed diesel engines.

160. But in the view of the Tribunal, there are crucial differences between the issue addressed in that Decision and the issues now falling to be determined. It is "hornbook" law that it is a pre-requisite to the operation of doctrines of election, waiver or estoppel that the party said to have elected or waived or to be estopped had full relevant knowledge at the material time. If the complaint were that the EPC Contract price was unreasonable per se, then one could see some force in the argument. But the implied term as found by us and which is said to have been broken by IPTL was an obligation to act reasonably and prudently in relation to any agreement with a third party which would have had an effect on the extent of TANESCO's obligation to reimburse IPTL through the tariff payment. Although IPTL challenges TANESCO's assertion that it deliberately withheld relevant documentation, it cannot be suggested that TANESCO possessed full knowledge of all the details of the bidding process which the Tribunal has sought to analyse in its consideration of the reasonableness or otherwise of the decision to award the EPC Contract to Wartsila at the price agreed. Indeed, much of the detail emerged for the first time in the course of the arbitration.

161. Furthermore, insofar as IPTL seeks to rely on the support given to the project by the Government of Tanzania, we do not consider for these purposes the Government and TANESCO should be identified the one with the other. In any event, the Government

of Tanzania was in no better position than was TANESCO to form a judgment. Its relevant knowledge was no greater.

162. Finally, as TANESCO points out, despite its lack of detailed knowledge, concern was expressed from time to time within Tanzania about the cost of the project, and IPTL acknowledged more than once that the appropriate time for discussing the propriety of its expenditure would be when the discussions over the adjustment of the Reference Tariff pursuant to Addendum No. 1 took place. TANESCO places particular reliance on a document published by IPTL and apparently written by Mr Rugemalira in August 1996, entitled "The Truth about the IPTL Project", in which it was stated:

> Obviously IPTL will have to show and if necessary justify that the actual costs that will be used to adjust the reference tariff in order to arrive at the initial tariff were incurred in the most efficient and competitive manner.

163. Accordingly, the Tribunal concludes that there was no relevant election, waiver or estoppel.

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

164. In the paragraphs above, the Tribunal has considered the numerous points raised by TANESCO in response to the figures put forward by IPTL as the appropriate figures to be fed into the "financial model" produced by Mr Lim (which we understand has now been adjusted so as to be in a form acceptable to both parties).

165. In relation to the Energy Payment, we have rejected TANESCO's complaint in relation to the terms of the FSA, so that no adjustment falls to be made by reason of

IPTL's alleged unreasonableness or imprudence.

166. It was the understanding of the Tribunal that, by the time of their last exchanges, the parties were confident that, armed with the appropriate adjustments, they would be able to agree on the application of the financial model and the tariff which should be derived as a consequence. If this is not the case, or if either party wishes to have an Award which sets out the relevant calculated figure, further application must be made to the Tribunal.

12 What further orders should be made?

167. According to the understanding of the Tribunal, both parties were agreed that, once the appropriate figures to be fed into the 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.

168. Neither party addressed the question of how much time would be required for this purpose, and in these circumstances, the Tribunal considers it appropriate to order that the parties should co-operate in taking whatever steps are necessary to achieve the commencement of commercial operation as soon as reasonably practicable.

13. Costs:

169. The Tribunal received detailed submissions from the parties in relation to the apportionment of costs and the amount which should be allowed. We appreciate that, so far as the party and party costs are concerned, which reflect the very substantial amount of work done by the parties' legal representatives, as well as the substantial

cost of expert and other evidence, the sums expended by the parties are considerable. The costs of the arbitration, including the fees and expenses of the Tribunal and of ICSID, are fortunately, somewhat more modest.

170. The Tribunal has considered the apportionment of costs on the basis of the approach, which appeared to be common ground between the parties, that costs should follow the event. However, in this case, there was and is no one simple "event". The parties have each had a share of success and of failure - TANESCO being successful in resisting IPTL's application for provisional measures; IPTL being largely successful on the Preliminary Issues of Construction/Law, and in particular the principal question of the validity of the Notice of Default and therefore the continuing existence of the PPA; and on the issue of bribery, which TANESCO chose to introduce at a very late stage; and TANESCO having enjoyed a substantial degree of success in relation to the tariff issues, and in particular the question of the reasonableness and/or prudence of IPTL's conduct in relation to the award of the EPC Contract.

171. We do not think that it is appropriate to make any apportionment on an "issue-by-issue" basis. This would require lengthy and detailed analysis which would itself be expensive, and indeed would not be possible on the material we have before us.

172. Taking these factors into account, the Tribunal concludes that it would be fair to order that each party should bear its own legal and other costs, and that the costs of the arbitration should be borne as to 50% by each party.

14. Acknowledgement:

173. Finally, the Tribunal wishes to extend its appreciation to the legal representatives on each side for their considerable industry and assistance; and to The Centre in Washington D.C. for its efficient and very helpful administration of the arbitration.

Dated this 9th day of February 2001.

The Honorable Charles N. Brower

Charles N. Brower

The Honourable Andrew Rogers QC

Andrew Rogers

Kenneth Rokison QC

[signature]