INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
WASHINGTON, D.C.

In the arbitration proceeding between

MOBIL EXPLORATION AND DEVELOPMENT ARGENTINA INC. SUC. ARGENTINA AND MOBIL ARGENTINA SOCIEDAD ANÓNIMA

Claimants

and

THE ARGENTINE REPUBLIC

Respondent

ICSID Case No. ARB/04/16

Decision on Jurisdiction and Liability

Members of the Tribunal
Justice Gustaf Möller, President
Professor Piero Bernardini, Arbitrator
Professor Antonio Remiro Brotóns, Arbitrator

Secretary of the Tribunal
Natalí Sequeira

Date of dispatch to the Parties: April 10, 2013

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I. REPRESENTATION OF THE PARTIES

Representing Mobil Exploration and Development Argentina Inc. Suc. Argentina and Mobil Argentina Sociedad Anónima:

Mr. R. Doak Bishop
Mr. Guillermo Aguilar-Alvarez
Mr. Craig S. Miles
Ms. Silvia M. Marchili
Mr. David H. Weiss
King & Spalding
1100 Louisiana St, Suite 4000
Houston, Texas
United States of America

Mr. José A. Martínez de Hoz (Jr.)
Ms. Jimena Vega Olmos
Ms. María Florencia Villaggi
Mr. Alex Maculus
Pérez Alati, Grondona, Benites,
Arntsen & Martínez de Hoz (Jr.)

Mr. Eugene J. Silva II
Ms. Gwendolyn Dawson
Exxon Mobil Corporation

Representing the Argentine Republic:

Dra. Angelina María Ester Abbona
Procuradora del Tesoro de la Nación
Procuración del Tesoro de la Nación
Posadas 1641
CP 1112 Buenos Aires
Argentina

II. INTRODUCTION AND THE PARTIES

1. The Claimants are Mobil Exploration and Development Argentina Inc. Suc. Argentina ("**MEDA**") and Mobil Argentina Sociedad Anónima ("**MASA**") collectively referred to as the "Claimants."

2. The Respondent is the Argentine Republic and is hereinafter referred to as "**GOA**", the "**Government of Argentina**", "**Argentina**" or the "**Respondent**."

3. The Claimant and the Respondent are hereinafter collectively referred to as the"**Parties**."

III. PROCEDURAL HISTORY

4. On 19 December 2003, the Claimants filed a Request for Arbitration (the "**Request**" or "**RFA**") against the Argentine Republic with the International Centre for Settlement of Investment Disputes ("**ICSID**" or the "**Centre**"). The Request was filed pursuant to the Treaty Concerning the Reciprocal Encouragement and Protection of Investment between Argentina and the United States of America (the "**BIT**") and pursuant to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, dated 14 October 1966 ("**ICSID Convention**").

5. According to the Request, the dispute arose from the Claimant's alleged investment in Argentina. The Claimant alleges that Argentina has failed to comply with the rights and guarantees granted to investors by the terms of the BIT, international law and the local laws.

6. On 5 August 2004, the Secretary-General registered the Request for Arbitration. The Claimants further filed two ancillary claims, a first ancillary claim on 14 February 2006 ("**First Ancillary Claim**") and a second ancillary claim on 23 October 2007 "**Second Ancillary Claim**").

7. On 27 July 2005, the Claimants appointed Professor. Piero Bernardini, an Italiannational, as arbitrator. On 17 August 2005, the Argentine Republic appointed Professor. Alain Pellet, a national of France, as arbitrator. Prof. Pellet subsequently resigned. On 31 August 2006 the Argentine Republic appointed Prof. Antonio Remiro Brotóns, a national of Spain, as arbitrator. On 31 July 2008, in accordance with Rule 4 of the Rules of Procedure for Arbitration Proceedings (the "**Arbitration Rules**"), the Chairman of the Administrative Council of ICSID appointed Justice Gustaf Möller, a Finnish national, as President of the Tribunal. On August 14, 2008, the DeputySecretary-General of ICSID informed the Parties that all Members of the Tribunal had accepted their appointments and that, in accordance with Arbitration Rule 6(1), the Tribunal was deemed to have been constituted on that same day.

8. On 3 October 2008, the Tribunal held its first session by telephone conference. During the first session the Parties confirmed that the Tribunal had been properly constituted in accordance with the ICSID Convention and the applicable ICSID Arbitration Rules. Additionally the Tribunal and the Parties agreed on the procedural calendar.

9. The Claimants filed a Memorial on the Merits on 16 February 2009. On 14 May 2009 the Respondent filed a Memorial on Jurisdiction. The Claimants filed a Counter-memorial on Jurisdiction on 31 July 2009. On 7 December 2009 theRespondent filed a Counter-Memorial on the Merits. On 27 April 2010 Claimants filed a Reply on the Merits. Respondent filed a Rejoinder on the Merits on 6 September 2010.

10. The hearing on jurisdiction and merits was held from 1 April 2011 through 13 April 2011 at the seat of the Centre in Washington D.C. Present at the hearing were:

Members of the Tribunal:

Justice Gustaf Möller, President of the Tribunal
Professor Piero Bernardini, Arbitrator
Professor Antonio Remiro Brotóns, Arbitrator

ICSID Secretariat

Ms. Natalí Sequeira	Secretary of the Tribunal

Assistant to Prof. Remiro Brotóns

Professor Irene Blásquez Navarro

On behalf of the Claimants:

Ms. Kimberly Pilcher	ExxonMobil Corp.
Mr. Gene Silva	ExxonMobil Corp.
Mr. Mariano Vivas de Lorenzi	ExxonMobil Corp
Mr. R. Doak Bishop	King & Spalding LLP
Mr. Craig S. Miles	King & Spalding LLP
Mr. Guillermo Aguilar Alvarez	King & Spalding LLP
Mr. José A. Martínez de Hoz	Pérez Alati, Grondona, Benites, Arnsten & Martínez de Hoz (PAGBAM)
Ms. Valeria Macchia	PAGBAM
Ms. Silvia Marchili	King & Spalding LLP
Mr. David Weiss King & Spalding LLP	
Mr. Gustavo Topalián	PAGBAM
Ms. Jimena Vega Olmos	PAGBAM
Ms. María Florencia Villaggi	PAGBAM
Mr. Alex Maculus	PAGBAM
Ms. Adriana Forno	PAGBAM
Mr. Tim Kistner King & Spalding LLP	
Ms. Carol D. Tamez	King & Spalding LLP

Claimants' Witnesses

Ms. Norma Valle ExxonMobil Corp.	
Mr. Dub Crook III	ExxonMobil Corp.

Claimants' Experts

Prof. Michael Reisman	Yale Law School
Prof. José Alvarez	New York University Law School
Prof. Sebastian Edwards, Ph.D.	University of California, Los Angeles
Mr. Rudolf DolzerDirector	German Society of Foreign Policy Berlin
Mr. Keith McLeod	Sproule

Ms. Nora T. Stewart	Sproule
Phillip W. Pantella	Sproule
Mr. Pablo Spiller	LECG
Mr. Manuel Abdala	LECG
Mr. Diego Bondorevsky	LECG
Mr. Miguel Nakhle	LECG
Ms. Maria Lombardi	LECG
Mr. Ariel Medvedeff	LECG
Mr. Alberto B. Bianchi	Estudio Bianchi & Galarce
Mr. Julio César Rivera	Julio César Rivera Abogados
Mr. Guillermo O. Teijeiro	Negri & Teijeiro, Abogados
Mr. Carlos Manuel Bastos	Independent Consultant
Mr. Hugo Martelli	Martelli Abogados

On behalf of the Respondent:

Dirección Nacional de Asuntos y Controversias Internacionales
Procuración del Tesoro de la Nación

Dr. Horacio Pedro Diez	Subprocurador del Tesoro de la Nación
Dr. Gabriel Bottini	Director
Dra. Adriana Busto	Subdirector
Dra. Gisela Makowski	Procuración del Tesoro de la Nación
Dr. Tomás Braceras	Procuración del Tesoro de la Nación
Dr. Rodrigo Ruiz Esquide	Procuración del Tesoro de la
NaciónDra. Viviana Kluger	Procuración del Tesoro de la Nación
Dr. Matías Bietti	Procuración del Tesoro de la Nación
Dra. Verónica Lavista	Procuración del Tesoro de la Nación
Dr. Ignacio Torterola	Procuración del Tesoro de la Nación
Dr. Ignacio Pérez Cortés	Procuración del Tesoro de la Nación
Lic. Nicolás Grosse	Procuración del Tesoro de la Nación
Lic. Patricio Arnedo Barreiroq	Procuración del Tesoro de la Nación
Dr. Diego Gosis	Procuración del Tesoro de la Nación
Mr. Nicolás Duhalde	Procuración del Tesoro de la Nación
Mr. Julián Santiago Negro	Procuración del Tesoro de la Nación
Ms. M. Soledad Romero Caporale	Procuración del Tesoro de la Nación

Secretaría de Energía de la Nación

Dr. Carlos Bernardo Walter Kunz	Asesor legal
Lic. Charles Massano	Asesor

Respondent's Witnesses:

Mr. Eduardo Ratti
Mr. Daniel Cameron
Mr. Diego Guichón

Respondent's Experts:

Mr. Ismael Mata	
Mr. Norberto E. Noblía	
Mr. Guillermo Rodríguez Usé	
Mr. Esteban Greco	
Mr. Ernesto Schargrodsky	Universidad Torcuato Di Tella
Mr. Guido Sandleris	Universidad Torcuato Di Tella
Mr. Nicolás Gadano	Universidad Torcuato Di Tella
Ms. Julieta Serna	Universidad Torcuato Di Tella
Mr. Sebastián González	
Mr. Francisco Gulisano	Diamondstar S.R.L.
Mr. César Garrasino	Diamondstar S.R.L.
Mr. Benedict Kingsbury	
Mr. Barry Eichengreen	
Mr. Roberto Frenkel	
Mr. Mario E. Damill	
Mr. Nouriel Roubini	
Ms. Liliana de Riz	
Ms. Mónica Pinto	

11. As instructed by the Tribunal the last day of the hearing, the Parties submitted on 23 May 2011, corrections to the transcripts. On 13 June 2011 the Parties filed simultaneous post-hearing briefs. On 12 July 2011 the Tribunal received the parties' statements of costs.

12. On 4 May 2012, the parties were informed that the Tribunal had decided to bifurcate the proceedings by first issuing a decision on liability and postponing the quantification of damages to a separate quantum phase.

IV. THE INVESTMENT PROTECTION TREATY

13. The BIT was signed on 14 November 1991 and entered into force on 13 October 1993. It is drafted in English and Spanish and contains, *inter alia* the following provisions:

> "ARTICLE I
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> 1. For the purposes of this Treaty,
>
> a) "investment" means every kind of investment in the territory of one Party owned or controlled directly or indirectly by nationals or companies of the other Party, such as equity, debt, and service and investment contracts; and includes without limitation:
>
> (i) tangible and intangible property, including rights, such as mortgages, liens and pledges;
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> (ii) a company or shares of stock or other interests in a company or interests in the assets thereof;
>
> (iii) a claim to money or a claim to performance having economic value and directly related to an investment;
>
> (iv) intellectual property which includes, inter alia, rights relating to: literary and artistic works, including sound recordings, inventions in all fields of human endeavor, industrial designs, semiconductor mask works, trade secrets, know-how, and confidential business information, and trademarks, service marks, and trade names; and
>
> (v) any right conferred by law or contract, and any licenses and permits pursuant to law;
>
> b) "company" of a Party means any kind of corporation, company, association, state enterprise, or other organization, legally constituted under the laws and regulations of a Party or a political subdivision thereof whether or not organized for pecuniary gain, and whether privately or governmentally owned;
>
> c) "national" of a Party means a natural person who is a national of a Party under its applicable law;

d) “return” means an amount derived from or associated with an investment, including profit; dividend; interest; capita gain; royalty payment; management, technical assistance or other fee; or returns in kind;

e) “associated activities” include the organization, control, operation, maintenance and disposition of companies, branches, agencies, offices, factories or other facilities for the conduct of business; the making, performance and enforcement of contracts; the acquisition, use, protection and disposition of property of all kinds including intellectual and industrial property rights; and the borrowing of funds, the purchase, issuance, and sale of equity shares and other securities, and the purchase of foreign exchange for imports.

f) “territory” means the territory of the United States or the Argentine Republic, including the territorial sea established in accordance with international law as reflected in the 1982 United Nations Convention on the Law of the Sea. This Treaty also applies in the seas and seabed adjacent to the territorial sea in which the United States or the Argentine Republic has sovereign rights or jurisdiction in accordance with international law as reflected in the 1982 United Nations Convention on the Law of the Sea.

(…)

3. Any alteration of the form in which assets are invested or reinvested shall not affect their character as investment.

ARTICLE II

1. Each Party shall permit and treat investment, and activities associated therewith, on a basis no less favorable than that accorded in like situations to investment or associated activities of its own nationals or companies, or of nationals or companies of any third country, whichever is the more favorable, subject to the right of each Party to make or maintain exceptions falling within one of the sectors or matters listed in the Protocol to this Treaty.

2. a) Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law.

b) Neither Party shall in any way impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments. For the purposes of dispute resolution under Articles VII and VIII, a measure may be arbitrary or discriminatory notwithstanding the opportunity to review such measure in the courts or administrative tribunals of a Party.

c) Each Party shall observe any obligation it may have entered into with regard to investments.

(…)

6. Each Party shall provide effective means of asserting claims and enforcing rights with respect to investments, investment agreements, and investment authorizations.

(…)

ARTICLE IV

1. Investments shall not be expropriated or nationalized through measures tantamount to expropriation or nationalization ('expropriation') except for a public purpose; in a non-discriminatory manner; upon payment of prompt, adequate and effective compensation; and in accordance with due process of law and the general principles of treatment provided for in Article II (2) Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriatory action was taken or became known, whichever is earlier; be paid without delay; include interest at a commercially reasonable rate from the date of expropriation; be fully realizable; and be freely transferable at the prevailing market rate of exchange on the date of expropriation.

2. A national or company of either Party that asserts that all or part of its investment has been expropriated shall have a right to prompt review by the appropriate judicial or administrative authorities of the other Party to determine whether any such expropriation has occurred and, if so, whether such expropriation, and any compensation therefore, conforms to the provisions of this Treaty and the principles of international law.

3. Nationals or companies of either Party whose investments suffer losses in the territory of the other Party owing to war or other armed conflict, revolution, state of national emergency, insurrection, civil disturbance or other similar events shall be accorded treatment by such other Party no less favorable than that accorded to its own nationals or companies or to nationals or companies of any third country, whichever is the more favorable treatment, as regards any measures it adopts in relation to such losses

(…)

ARTICLE VII

1. For purposes of this Article, an investment dispute is a dispute between a Party and a national or company of the other Party arising out of or relating to (a) an investment agreement between that Party and such national or company; (b) an investment authorization granted by that Party's foreign investment authority (if any such authorization exists) to such national or company; or (c) an alleged breach of any right conferred or created by this Treaty with respect to an investment.

2. In the event of an investment dispute, the parties to the dispute should initially seek a resolution through consultation and negotiation. If the dispute cannot be settled amicably, the national or company concerned may choose to submit the dispute for resolution:

(a) to the courts or administrative tribunals of the Party that is a party to the dispute; or

(b) in accordance with any applicable, previously agreed dispute-settlement procedures; or

(c) in accordance with the terms of paragraph 3.

3. (a) Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b) and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration:

(i) to the International Centre for the Settlement of Investment Disputes ("Centre") established by the Convention on the Settlement of Investment Disputes between States and Nationals of other States, done at Washington, March 18, 1965 ("ICSID Convention"), provided that the Party is a party to such convention: or

(ii) to the Additional Facility of the Centre, if the Centre is not available; or

(iii) in accordance with the Arbitration Rules of the United Nations Commission on International Trade Law (UNICTRAL): or

(iv) to any other arbitration institution, or in accordance with any other arbitration rules, as may be mutually agreed between the parties to the dispute.

(b) Once the national or company concerned has so consented, either party to the dispute may initiate arbitration in accordance with the choice so specified in the consent

4. Each Party hereby consents to the submission of any investment dispute for settlement by binding arbitration in accordance with the choice specified in the written consent of the national or company under paragraph 3. Such consent, together with the written consent of the national or company when given under paragraph 3 shall satisfy the requirement for

(a) written consent of the parties to the dispute for purposes of Chapter II of the ICSID Convention (Jurisdiction of the Centre) and for purposes of the Additional Facility Rules; and

(b) an “agreement in writing” for purposes of Article II of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards, done at New York, June 10, 1958 (“New York Convention”).

5. Any arbitration under paragraph 3(a) (ii), (iii)) or (iv) of this Article shall be held in a state that is a party to the New York Convention.

6. Any arbitral award rendered pursuant to this Article shall be final and binding on the parties to the dispute. Each Party undertakes to carry out without delay the provisions of any such award and to provide in its territory for its enforcement

7. In any proceeding involving an investment dispute, a Party shall not assert, as a defense, counterclaim, right of set-off or otherwise, that the national or company concerned has received or will receive, pursuant to an insurance or guarantee contract, indemnification or other compensation for all or part of its alleged damage.

8. For purposes of an arbitration held under paragraph 3 of this Article, any company legally constituted under the applicable laws and regulations of a Party or a political subdivision thereof but that, immediately before the occurrence of the event or events giving rise to the dispute, was an investment of nationals or companies of the other Party, shall be treated as a national or company of such other Party in accordance with Article 25(2) (b) of the ICSID Convention.

ARTICLE XI

This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests.

ARTICLE XII

1. With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party.

2. Nevertheless, the provisions of this Treaty, and in particular Article VII and VIII, shall apply to matters of taxation only with respect to the following:

(a) expropriation, pursuant to Article IV;

(b) transfers, pursuant to Article V; or

(c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VII(l)(a) or (b),

to the extent they are not subject to the dispute settlement provisions of a Convention for the avoidance of double taxation between the two Parties, or have been raised under such settlement provisions and are not resolved within a reasonable period of time.

ARTICLE XIII

This Treaty shall apply to the political subdivisions of the Parties."

V. FACTUAL BACKGROUND

A. The Origins of the Dispute

14. The Argentine economy entering the 1990s was facing serious problems. Therefore Argentina needed to implement a dramatic change. First, in an effort to end currency instability that hindered Argentina's chances of attracting foreign investment,

Argentina enacted Law 23,928 (together with its implementing Decree 529/91, (the "**Convertibility Law"**) in 1991.[1] Pursuant to the Convertibility Law, Argentina pegged the local currency (the **"Peso"**) to US Dollar at a fixed rate of 1:1.

15. Second, Law 23,696 (the **"State Reform Law"**) provided for the unbundling and eventual privatization of public assets.[2] A main purpose of the State Reform Law was to promote foreign investment in the hydrocarbon industry, thereby stimulating oil and gas drilling, increasing reserve, and transforming Argentina from a net importer to a net exporter of hydrocarbons.[3] Revamped laws and decrees relating to investment – especially Decree 1853/93 – constituted another pillar of economic reform.[4]

16. By the 1980s, the GOA almost completely owned, and to a substantial extent operated, the entire energy sector. In the case of the Argentine oil and gas industry, the public sector dominated the exploration, production, development, transportation, refining, and distribution of hydrocarbons. The private sector played only a secondary role, restricted to activities and service contracts with Yacimientos Petrolíferos Fiscales S.E. (**"YPF**"), the former state-owned oil company, and with Gas del Estado Sociedad del Estado (**"Gas del Estado"**), which owned and operated the gas transportation and distribution system. Oil and gas exploration and development activities were in critical decline.

17. During the mid-1980s, Argentina attempted to attract foreign investment to the oil and gas industry. It launched a program named the "Houston Plan" with a view to concluding service contracts between YPF and foreign companies. The main purpose

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[1] Law 23,928 (Exhibit C-12). Decree 529/91 (Exhibit C-18).
[2] Law 23,696 (Exhibit C-10). See also Law 23,697 (Exhibit C-11).
[3] Message sent by the Federal Executive Branch to Congress introducing the bill that later became State Reform Law 23,696, quoted in José R. Dromi, *Reforma del Estado y Privatizaciones*, Ed. Astrea, 1991 (Exhibit C-165).
[4] Decree 1893/93 (Exhibit C-33).

of this project was to increase Argentina's oil and gas reserves and achieve energy surpluses by increasing oil and gas exploration.[5]

18. Under this new regime, the foreign companies had to assume all risks regarding the exploration programs even though they would not own the oil and gas eventually produced. The Houston plan turned out to be a failure; no significant investments or discoveries were made.

19. In the early 1990s, given the failure of the Houston Plan to alleviate the energy sector's critical condition, the GOA decided to deregulate the hydrocarbon industry and to privatize its utilities. Moreover, the GOA enacted a new energy legal framework for the energy sector. To induce foreign investment, the GOA then launched road shows in which it presented its new model to foreign investors, principally from the United States of America and Europe.

20. The GOA instituted a "Legal Framework" that included: (i) the Deregulation Decrees, which deregulated the hydrocarbon sector; (ii) the Gas Law, which privatized Gas del Estado and provided for freely-negotiated gas wellhead prices; (iii) Plan Argentina, which set out the bidding terms and conditions for new exploration areas; (iv) the Conversion Decree, which invited service contractors with YPF (the State-owned oil company) to transform their contracts into exploration permits or exploitation concessions; and (v) the signing of the Substitute Protocol for Protocol No. 2 to the Agreement on Economic Cooperation No. 16 with Chile (the **"Chile-Argentina Energy Treaty"**). The Protocol was designed to integrate the Argentine and Chilean gas markets and which reinforced the deregulation of the natural gas industry through international commitments to Chile.

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[5] Decree 1443/85, Third, Fourth and Fifth Recitals (Exhibit C-9).

21. The program for privatization of YPF, the state-owned oil company, included several stages prior to the privatization of YPF itself. YPF issued several calls for bids inviting private companies to enter into joint venture agreements relating to large producing fields.

22. Tecpetrol, MASA (formerly Ampolex Argentina S.A.), Compañía General de Combustibles S.A. (**"CGC"**), and Petrobras Argentina S.A. (formerly Petrobras Internacional S.A.) executed an agreement with YPF to form an Unión Transitoria de Empresas ("**UTE**"), which was then approved in December 1992 by Decree 2446/92 (the "**Aguaragüe Contract**").[6] Thus MASA acquired interests in Aguaragüe. This area is located in the Northwestern Basin in the Province of Salta, and includes various fields.

23. The Aguaragüe Contract grants the joint venture participants the right to explore and exploit the hydrocarbon reserves in the Aguaragüe field. It also contains a production sharing arrangement that grants each of the joint venture partners a share in the production of the Aguaragüe field. The Aguaragüe Contract was agreed for a 25-year term, with an option to renew it for 10 years. MASA contends that it currently owns a 23% working interest in the Aguaragüe Contract and its hydrocarbon production.[7] As a result of the exploration activities in the Aguaragüe Area, the UTE found gas in the San Antonio Sur Block. Consequently, in February 1998, the GOA granted a Concession for the exploitation of that block (the "**San Antonio Sur Concession**").[8]

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[6] Decree 2446/92 (Exhibit C-96). The Unión Transitoria de Empresas or UTE is a type of statutory joint venture agreement. In this case, the UTE was concluded with YPF S.A. – which at that time was the state-owned energy company – and other partners and contains a production sharing agreement.
[7] MASA (formerly named Ampolex Argentina S.A.) has been the holder of a 23 % working interest in the Aguaragüe joint venture or Aguarague Contract, since the issuance of Decree 2446/92 C-97. The change of Ampolex's corporate name is acknowledged in the recitals of Administrative Decision 424/99 of 10 November 1999 (Exhibit C-38).
[8] Administrative Decision 81/98 (Exhibit C-99).

24. Since the San Antonio Sur Concession is located within the Aguaragüe Area and is subject to the Aguaragüe Contract, all the rights and guarantees arising from Decrees 305/92 and 2446/92 are fully applicable to it. Furthermore, the San Antonio Sur Concession reaffirmed the right to market the hydrocarbons produced freely, in accordance with the Deregulation Decrees "the terms of which are incorporated into the title of the Concession."[9]

25. On 18 September 1996, MEDA and Mobil Oil Exploration and Production Southeast Inc. executed a Sale and Purchase Agreement (the "**BHP Assignment Agreement**") with BHP Petroleum (Argentina) S.A., BHP Petroleum (Argentina) Inc., BHP (Americas) Inc. and BHP Petroleum (GOM) Inc., through which BHP Petroleum (Argentina) S.A. assigned MEDA 90% of its working interest (a 27.99819% interest) in the title to the Sierra Chata Concession. Subsequently, BHP Petroleum (Argentina) S.A. and BHP Petroleum (Argentina) Inc. assigned their remaining working interest in the title to Sierra Chata (3.11091%) to MEDA.

26. As a result of reorganization by Mobil Corporation of its affiliates' holdings, effective on 9 December 1998, Mobil Argentina Ltd ("**MAL**") (previously named Monumentum Exploration Ltd) assigned all of its assets and liabilities, including its working interest in the Sierra Chata Concession (19.8865%), to MEDA.

27. Chihuidos is located in the Neuquén Basin, in the Province of Neuquén, and includes the Sierra Chata field. This area is located close to Chile, which does not produce gas, and was eager to increase its gas imports for power generation, residential use, and petrochemical purposes.

[9] *Ibid*, Art. 3 (Exhibit C-99).

28. One of the contracts that resulted from the Houston Plan under which companies would not own the hydrocarbons produced[10] was a service contract for the Chihuidos Area in the western Province of Neuquén. Several years later in 1991, through the Conversion Decree, the GOA provided parties to contracts, *inter alia*, under the Houston Plan the possibility of converting their contracts into new exploration permits and exploitation concessions in accordance with the Legal Framework.

29. The Chihuidos Area was included in the Conversion program, and in September 1993, Argentina issued Decree 1969/93, which granted an exploration permit in the area to YPF, Petrolera Santa Fe, International Finance Corporation, SIPSA, CGC, and BHP. Decree 1969/93 provides that these companies shall:

- own the hydrocarbons produced;[11]
- have the right to freely market that gas in accordance with the Deregulation Decrees;[12]
- receive at least the compensation set forth in the Deregulation Decrees, in case of any restriction on their right to freely market hydrocarbons, for as long as the restriction is in force;[13]
- pay up to 12% in royalties, which can only be calculated on the basis of the prices effectively collected, with applicable deductions;[14]
- be protected from discriminatory taxes;[15]

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[10] Decree 443/85, Art. 3 (Exhibit C-9).
[11] Decree 1969/93, Art. 3 (Exhibit C-94).
[12] *Ibid*.
[13] *Ibid*, Art. 5.
[14] *Ibid*, Art. 7.

- freely dispose of 70% of foreign exchange sale proceeds in accordance with the Deregulation Decrees, unless another provision entitles them to a higher percentage or eliminates the requirement.

30. Decree 1969/93 also granted those companies the right to obtain an exploitation concession that would include the rights granted under the Deregulation Decrees and the Conversion Decree. [16]

31. In June 1995, the GOA granted a concession for the exploitation of the Sierra Chata block in the Chihuidos area to Petrolera Santa Fe, Santa Fe Energy, BHP, Sociedad International Petrolera, CGC, Monument, and Gassur.[17]

32. In September 1996, Argentina issued Resolution 140/96 of the Secretary of Public Works and Services, which grants a gas export permit for the Sierra Chata Concession authorising the concession holders to export up to 2.5 million m3/day to Chile for a maximum term of 15 years or until the depletion of the remaining certified reserves, whichever occurs earlier.[18]

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[15] *Ibid*, Art. 6.

[16] Decree 1969/93, Arts. 2, 16 (Exhibit C-94).

[17] Decree 824/95 (Exhibit C-95). See also the Conversion Decree, Art. 5 (Exhibit C-28).

[18] Resolution SPWS 140/96, Arts. 1-2 (Exhibit C-81). Resolution SPWS 140/96 of the Secretariat of Public Works and Services was amended by Resolution 460/99, Exhibit C-82, and Resolution EMS 371/01 of the Secretary of Energy and Mining (Exhibit C-83). Resolution 460/99 incorporated Sipetrol Argentina S.A. and its share in the production of Sierra Chata Concession into the Sierra Chata Gas Export Permit. Resolution EMS 371/01 of the Secretary of Energy and Mining took notice of the assignment by Sipetrol Argentina S.A. of all its rights under the Sierra Chata Gas Export Permit and the underlying natural gas export contracts to Canadian Hunter Argentina S.A.

33. In granting the permit, the GOA expressly considered the provisions of the Chile-Argentina Energy Treaty and emphasized the importance of the regional integration of the gas market.[19]

34. The Sierra Chata Gas Export Permit provides for firm export rights that could not be interrupted without compensation.[20] Also Excess Gas could be exported under certain conditions.

35. On 6 January 2002 the "State of Public Emergency and Reform of Exchange Regulation Law "25,561 (the "**Emergency Law**") was enacted.[21]

36. Under Law 25,561 and Decree 214/02, the GOA unilaterally changed the provisions of private contracts between the Claimants and their domestic customers. These measures unilaterally converted Dollar-denominated obligations and receivables owed to the Claimants under gas supply contracts into Peso-denominated obligations at an exchange rate of US$ 1: AR$ 1.[22] This was done at the same time that the GOA abrogated the Convertibility Law and devalued the Argentine Peso through Law 25,561.[23] By the end of May 2002, the exchange rate had reached US$ 1: AR$ 3.60, and was in February 2009 approximately US$ 1: AR$ 3.50.

37. Moreover, the GOA effectively prevented power generators and gas distributors from passing through any price increase to their own customers.[24]

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[19] Resolution SPWS 140/96, Fourth Recital (Exhibit C-81).
[20] *Ibid*, Art. 1 (Exhibit C-81).
[21] Law 25,561 (Exhibit C-41).
[22] Law 25,561 (Exhibit C-41) and Decree 214/02 (Exhibit C-42). This mandatory conversion applied to gas supply contracts existing as of 6 January 2002. See also *Damage Valuation of MASA's and MEDA's Investments in Argentina by Manuel A. Abdala and Paolo E. Spiller* of 15 February, 2009 [hereinafter,"*LECG Report"*] ¶¶ 31 (a) and 34 (Exhibit C-2).
[23] Law 25,561 (Exhibit C-41).
[24] LECG Report, *supra* (n 22) ¶¶ 31(b), 35, 36 (Exhibit C-2).

38. On 2 April 2004, many gas producers (but not the Claimants), signed an agreement with the GOA (the "**First Gas Agreement**").[25] Through the First Gas Agreement, the GOA imposed on producers the duty to deliver certain volumes of gas to the different categories of consumers. In doing so, the GOA demanded that producers accept an obligation to supply the domestic market.

39. The First Gas Agreement established a "price path" for the upward adjustment of gas prices at the wellhead for large industrial consumers and electricity generators from 1 May 2004 to 31 July 2005.

40. On 17 May 2004, the Secretary of Energy began ordering producers – including those that did not sign the First Gas Agreement – to "re-route" and deliver all the volumes to certain domestic consumers, regardless of whether the producers had contractual relationships with those consumers.[26] The stated reason for this re-routing of gas volumes was the delay in the renegotiations the GOA imposed on gas distributors, producers, and industrial customers under the terms of the First Gas Agreement.

41. On 26 May 2004, the Secretary of Energy issued Resolution SE 503/04, which authorised the Undersecretary of Fuels to re-route" the Claimants' gas production on a daily basis to gas distribution companies.[27]

42. Soon after issuing Resolution SE 503/04, the Secretary of Energy issued Resolution SE 606/04, which enabled users that had purchased gas from gas distributors (or that had contracted exclusively for transportation and distribution services) to resell all or part of the gas to other users or distributors at freely-negotiated prices.[28]

[25] First Gas Agreement approved by Resolution MFP 208704 (Exhibit C-54).
[26] Letter of the Secretary of Energy dated 17 May 2004 (Exhibit C-125).
[27] Resolution 503/04 (Exhibit C-57).
[28] Resolution SE 606/04, Arts. 1, 9 (Exhibit C-59).

43. In April 2004, through the issuance of Resolution SE 265/04, Argentina began to restrict the gas exports of Argentine producers and sellers, including the Claimants, as a means of addressing the shortages in the domestic market.[29]

44. In compliance with an instruction contained in Resolution SE 265/04, the Undersecretariat of Fuels temporarily approved a Curtailment Program for Gas Exports and Use of Transportation Capacity (the "**Curtailment Program**").[30] The Curtailment Program provided for restrictions on: (i) all gas exports to the extent necessary to meet the domestic demand; and (ii) all gas transportation services related to exports if required to meet domestic demand. Through the Curtailment Program, the Secretary of Energy imposed restrictions on the Claimants' exports to Chile. In turn, these export restrictions prevented the Claimants from exporting gas volumes even though they were previously committed under deliver-or-pay gas export sales contracts.[31]

45. According to Resolution SE 265/04, these measures would remain in effect until the Secretary of Energy "decides that the available quantities of gas at the injection points of the Argentine transportation system are sufficient to meet domestic demand."[32] The Claimants contend that the GOA's actions artificially depress gas prices and drive up domestic demand, and therefore the resolution has effectively ensured that the GOA will continue imposing export restrictions indefinitely.

[29] Resolution SE 265/04 (Exhibit C-55); Decision of the Undersecretariat of Fuels 27/04 (Exhibit C-56); and Resolution SE 659/04 (Exhibit C-61). The measures imposing restrictions on gas exports and other gas price interferencearise from Decrees 180/04 and 181/04, which are based on the authority granted by Law 25,561 that is the same law that authorized the creation of gas Export Withholdings.
[30] Decision SSC 27/04 (Exhibit C-56).
[31] See notes sent by the Secretary of Energy imposing the curtailment of export volumes and the re-routing of such volumes to the domestic market in (Exhibit C-132 and Exhibit C-133). Claimants' gas sales export contracts (with Metrogas and Gener) were backed by the Sierra Chata Gas Export Permit.
[32] Resolution SE 265/04, Art. 1 (Exhibit C-55).

46. In June 2004, the Secretary of Energy issued Resolution SE 659/04, which amended the Curtailment Program.[33] Through this Resolution, the GOA instructed the Claimants to supply additional gas volumes to the local market, which according to the Claimants resulted in a significant curtailment of gas exports.[34]

47. Resolution SE 659/04 entitled gas producers affected by the export curtailments to sales prices that were equivalent to the prices established for each basin in the First Gas Agreement. The Claimants contend that as a consequence, gas producers received a much lower price than the price to which they were entitled under their natural gas export agreements.

48. Through Resolutions SE 752/05, 925/05, 1886/06, and 599/07, the GOA enacted additional measures that, according to the Claimants, reaffirmed the GOA's decision to continue abrogating legal and contractual rights established in the Legal Framework, the Hydrocarbon Concessions and Contracts, and the Chile-Argentina Energy Treaty.[35] These resolutions set forth a new mandatory mechanism for the purchase and sale of gas in the domestic market: they allow certain large users of gas, power generators, and CNG (compressed natural gas) stations to place "irrevocable offers" to purchase gas directly from gas producers at regulated prices.[36]

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[33] Resolution SE 659/04 (Exhibit C-61).

[34] See Witness Statement of Norma Valle (not dated) [hereinafter "*Valle Witness Statement*"] ¶ 45 (Exhibit C-4). See also notes sent by the Secretary of Energy imposing the curtailment of export volumes and the re-routing of such volumes to the domestic market pursuant to the Curtailment Program (Exhibit C-132 and Exhibit C-133). In the case of natural gas coming from the Northwestern Basin, exports could not exceed the exported volume during the 90 days prior to the execution of the Temporary Gas Sales Agreement between Argentina and Bolivia signed on 21 April 2004 (Exhibit C-92).

[35] Resolution SE 752/05 (Exhibit C-64); Resolution SE 925/05 (Exhibit C-65); Resolution SE 1886/06 (Exhibit C-73); and Resolution SE 599/07 (Exhibit C-75).

[36] LECG Report, *supra* (n 22) Report ¶¶ 41-42.

49. The First Gas Agreement expired in December 2006. Resolution SE 599/07 approved the terms and conditions of the Second Gas Agreement.[37] According to the Claimants, the Secretary of Energy issued that Resolution as an instrument to "persuade" gas producers to sign the Second Gas Agreement since the treatment granted to signing producers (the "**Signing Producers**") was more favourable than that granted to non-signing producers (the "**Non-Signing Producers**").

50. In the case of gas supply shortages in the domestic market, Resolution SE 599/07 provides that the GOA will "re-route" and curtail the exports and domestic sales of Signing Producers only after curtailing and "re-routing" the exports and domestic sales of Non-Signing Producers.[38]

51. Decree 1589/89, one of the Deregulation Decrees, provided that the export and import of hydrocarbons and their byproducts would be exempt from any present or *future* tariffs, duties, or withholdings.[39] In addition, the GOA granted safeguards against discriminatory or specific taxes.[40] Through Decree 1969/93, the GOA included both of these protections in the Sierra Chata Concession.[41]

52. In May 2004, through Decree 645/04, Argentina imposed a 20% Export Withholding on the Claimants' gas exports, among other gaseous hydrocarbons.[42] In addition, it authorized the Ministry of Economy to modify the Export Withholding rate.[43] At that

[37] Resolution SE 599/07 (Exhibit C-75).
[38] Resolution SE 599/07, Arts. 9 and 10 (Exhibit C-75).
[39] Decree 1589/89, Art. 3 (Exhibit C-15); Conversion Decree, Art. 9 (Exhibit C-28).
[40] Plan Argentina Art. 8 (Exhibit C-27). See Conversion Decree, Art. 9 (Exhibit C-28).
[41] Decree 1969/93, Arts. 1, 6 (Exhibit C-94).
[42] Decree 645/04 (Exhibit C-60).
[43] Decree 645/04, Art. 2 (Exhibit C-60).

time, the alleged purpose of Export Withholdings on gas was to align the tax treatment of gas with crude oil and byproducts.[44]

53. In June 2006, Argentina and Bolivia entered into the Framework Agreement for the Sale of Gas and the Execution of Projects Concerning Energy Integration (the "Framework Agreement").[45] Under that Agreement, Argentina agreed to buy gas from Bolivia at US$ 5/MMBTU. This entailed a significant increase over the price Argentina had paid under a previous agreement with Bolivia (*i.e.*, US$ 3.18/MMBTU) and it was much higher than US$ 1.20/MMBTU, the average regulated price then paid to MASA and other Argentine producers.

54. The GOA decided to finance the import of the higher-priced Bolivian gas by further increasing the Export Withholding rate on domestic gas. In July 2006, the GOA: (i) increased the Export Withholding rate for gas from 20% to 45%;[46] and (ii) modified the basis for calculating Export Withholdings; instead of calculating Export Withholdings based on the price that Argentine producers actually received (*i.e.*, approximately US$ 1.65/MMBTU), Argentina began calculating the withholdings on the price at which it agreed to import gas from Bolivia (initially, US$ 5/MMBTU).[47]

55. These measures effectively increased Export Withholdings on gas to a flat rate of US$ 2.25/MMBTU (45% of US$ 5/MMBTU) and raised the effective Export Withholding rate more than 67,5%, which exceeded the average export price that Argentine gas exporters received from foreign customers by approximately 40%. This amounts to

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[44] Preamble of Decree 645/04 (Exhibit C-60).
[45] *Convenio Marco entre Bolivia y Argentina para la Venta de Ga Natural y la Realización de Proyectos de Integración Energética* of 29 June 2006 (Exhibit C-122).
[46] Decree 643/04 (Exhibit C-60). See also Resolution MEP 534/06, Art. 1 (Exhibit C-71).
[47] Resolution MEP 534/06, Art. 1 (Exhibit C-71).

113% of the export price that the Claimants received and renders exporting gas unprofitable since all of the profit (and more) is taken by the GOA.[48]

56. Through Resolution MEP 127/08, the GOA, once again: (i) increased the applicable Export Withholding rate on gas (from 45% to 100%); and (ii) altered the basis on which it calculates Export Withholdings, disregarding the much lower export prices actually received by exporters such as MASA.[49] Under Resolution MEP 534/06, the GOA calculated Export Withholdings based on the price at which it imports gas from Bolivia (currently US$ 10.30/MMBTU). Since early 2008, the GOA has calculated Export Withholdings on the highest prevailing rate for gas imports (during the winter of 2008, between US$ 14.5-17/MMBTU due to the import of LNG).[50]

57. Thus, Resolution MEP 127/08 entails a further increase of approximately 650% in the applicable Export Withholding rate. As a result, during the winter of 2008, export withholdings on gas exports in Argentina were approximately between US$ 14.5 and 17/MMBTU, that is between seven and eight times higher than the actual average export price they received by Argentine producers (around US$ 1.90/MMBTU).

58. The Export Withholdings were initially designed to last five years.[51] By virtue of Law 26,217, the GOA extended the period for imposing Export Withholdings through 2012.[52] The GOA has now extended the period for imposing Export Withholdings to ten years.

[48] LECG Report, *supra* (n 22) ¶ 62.
[49] Resolution MEP 127708 (Exhibit C-77) See also LECG Report, *supra* (n 22) ¶ 63 (Exhibit C-2).
[50] Resolution MEP 127/08, Art. 1 (Exhibit C-777). The highest natural gas import price prevailing at each time is to be informed regularly to the General Customs Office by the Undersecretariat of Fuels. *See also* LECG Report, *supra* (n 22) ¶ 63 (Exhibit C-2).
[51] Law 25,561, Art. 6 (Exhibit C-41).
[52] Law 26,217 (Exhibit C-69).

59. The Legal Framework provides that the highest royalty rate that could be imposed on gas producers is 12%.[53] The Hydrocarbon Concessions and Contracts provide further guarantees to the Claimants in this respect. The Sierra Chata Concession provides that the highest royalty rate that could be imposed on the Claimants is 12%, and that it can only be calculated on the prices effectively collected.

1. Summary of the Parties' Positions

a. The Claimants' position

60. The Claimants contend that MEDA between September 1996 and November 1997 acquired different portions of its current interest in the concession for the exploitation of the Sierra Chata block in the Chihuidos area, which interest was transferred to MASA effective 2005. Claimants assert that MASA owns a 50.99% working interest in the Chihuidos area and the Sierra Chata Concession.[54]

61. The GOA's measures to unilaterally convert Dollar-denominated obligations and receivables owed to the Claimants by their domestic customers under gas supply contracts into Peso-denominated obligations at an exchange rate of US $ 1:ARS$ 1 as well as to prevent power generators and gas distributors — the Claimants' primary domestic customers — from passing through any price increase to their own customers, say the Claimants, violate the GOA's guarantees under the Legal Framework and the contracts and licenses entered into by the GOA. Those measures also effectively eliminated any chance of renegotiating the Claimants' gas supply

[53] Hydrocarbons Law, Arts. 59, 62 (Exhibit C-8). See also Conversion Decree, Art. 10 (Exhibit C-28). This protection was also incorporated into the Hydrocarbon Concessions and Contracts. See Decree 305/92, Art. 8 (Exhibit C-96), Decree 1969/93, Art. 7 (Exhibit C-94); Chihuidos Memorandum of Understanding, Art. 13 (Exhibit C-93); and Decree 824/95, Art. 10 (Exhibit C-95).

[54] The Claimants' interests in the Chihuidos exploration permit and the Sierra Chata Concession were acquired from BHP Petroleum (Argentina) Inc. and BHP Petroleum (Argentina) S.A., on the one hand, and Mobil Argentina Limited (previously named Monumentum Exploration Limited) on the other.

contracts, and therefore, constituted an unlawful interference with their freely-agreed terms.

62. Further, the Claimants assert that pursuant to Article 8 of Decree 214/02, the Argentine Government instructed courts with jurisdiction over controversies relating to these matters to maintain and preserve existing contracts in Peso terms. In practice, this measure, the Claimants contend, precluded parties from terminating contracts prior to their expiration due to the GOA's alteration of the contract price or contract price-fixing mechanism.

63. According to the Claimants the renegotiation of public service contracts between the GOA and gas and power distribution companies, a process provided for in Law 25,561,[55] has been a massive failure. To renegotiate these contracts, the GOA demands that public utility companies waive their rights—as well as those of their foreign shareholders—to initiate or continue international arbitration proceedings against the GOA based on the GOA's measures.[56]

64. In sum, the Claimants contend that a *de facto* price freeze on natural gas resulted from (i) the mandatory currency conversion of the prices the Claimants' local customers paid to the Claimants, (ii) the price freeze imposed on gas distributors and power generators, (iii) the obstacles the GOA imposed to prevent the Claimants and their

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[55] Law 25,561, Art. 9 (Exhibit C-41).

[56] The UNIREN (the commission in charge of the renegotiation of public utility contracts) has provided model drafts of the agreements to be entered with public utility companies that expressly include a waiver of bilateral investment treaty claims as a requirement to renegotiate such service concessions and licenses. To renegotiate with the Government, companies are required to surrender their most important protections and get virtually nothing in return. See also Draft memorandums of understanding regarding the renegotiation of the public utility agreements with Camuzzi Gas Pampean and Camuzzi Gas del Sur S.A. (January 12 2005); Gas Natural Ban S.A (11 April 2005); Transportadora de Gas del Norte (7 July 2004); Transportadora de Gas del Sur (7 July 2004) and Transcomahue S.A. (28 March 2005) (Exhibit C-123). See also "*Demandas ante el CIADI traban los aumentos en la tarifa de gas*", EL CRONISTA, 9 Septembre 2008 (Exhibit C-155).

customers from terminating their contracts, and (iv) the protracted renegotiation process between the Claimants' main customers and the GOA

65. Through the First Gas Agreement, GOA imposed on producers the duty to deliver certain volumes of gas to different categories of consumers. In doing so the GOA demanded that producers accept an individual obligation to supply the domestic market, even though no such obligation existed in the Legal Framework.

66. While the price path established by the First Gas Agreement provided for the gradual normalisation of gas prices for large industrial consumers, CNG stations and power generators, the First Gas Agreement maintained frozen prices for residential consumers, which represent approximately 22% of the demand.[57]

67. Moreover, the pesification of gas supply contracts – and particularly the GOA's additional measures that locked gas producers into frozen gas wellhead prices and depressed domestic energy prices – caused an increase in the demand for gas. At the same time, these measures, say the Claimants, discouraged investors from making the investments needed to drill new wells, increase reserves, and meet that increased demand.

68. According to the Claimants the result of these and other measures has been the lack of new private investment in power generation and oil and gas drilling in Argentina. Beginning in 2004, the GOA invoked the gas shortage as a justification for additional measures targeted at the Claimants' business.

69. Resolution SE 606/04, which enabled users that had purchased gas from gas distributors (or that had contracted exclusively for transportation and distribution

[57] Report of Carlos Bastos of 13 February 2009 [hereinafter "*Bastos Report*"], ¶ 103 (Exhibit C-1). See also LECG Report, *supra* (n 22) ¶ 39 (Exhibit C-2).

services) to resell all or part of the gas to other users or distributors at freely-negotiated prices, resulted in flagrant discrimination against the Claimants because the GOA forced them to accept a substantially lower price for their domestic gas sales, while industrial users were allowed to obtain substantial profits by reselling at higher prices.[58]

70. By restricting the gas export of Argentine producers and sellers, including the Claimants, the GOA disregarded Claimants' right to freely market the gas they produce, as well as Claimants' firm export rights under the Sierra Chata Export Permit.

71. The export restrictions and the orders to re-route and deliver to certain domestic customers regardless of the producers had contractual relationships with those customers violated the Claimants' rights and resulted (and continue to result) in a taking of revenues because they force the Claimants to deliver these export volumes to domestic users at prices that are substantially lower than those agreed in their export contracts.[59] Despite this taking of revenues, the GOA breached its commitment to compensate the Claimants for export restrictions at the rate of at least 35% of the international price of the Arabian Light crude oil of 34° API for 1,000m³ of 9,300 KCal.[60]

72. Those measures also required the Claimants to ignore their existing contractual commitments, and instead, deliver their gas production to large domestic users, power plants and CNG stations.

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[58] Decree 181/04 (Exhibit C-53).
[59] LECG Report, *supra* (n 22) ¶¶ 55, 58 and 61 (Exhibit C-2).
[60] Art. 6 of Decree 1589/89, Exhibit C-15. This guarantee was also specifically incorporated into the Hydrocarbon Concessions and Contracts. See Art. 5 of Decree 1969/93 with respect to Sierra Chata.

73. Resolution SE 752/05, which allowed certain domestic customers to make irrevocable offers, put the Claimants in a no-win situation. If the Claimants do not "agree" to an irrevocable offer, then the Secretary of Energy requires them to supply gas to the domestic market at a price that is significantly lower than the price they would have received had they agreed to the irrevocable offer.[61] But if the Claimants yield to the GOA's pressure and "agree" to the irrevocable offer, they would be prevented from meeting their export commitments in their contracts with export customers.

74. The Claimants contend that Argentina forces Non-Signing Producers such as the Claimants to "re-route" gas shipments from customers paying the highest prices to consumers paying the lowest ones. These restrictions not only preclude MASA from complying with its existing export commitments, but also obligate it to supply gas to domestic consumers with which it has no contractual relationships at substantially lower prices than the ones agreed under its export agreements.

75. Although domestic consumers pay Signing Producers in accordance with the price formulas established in the Second Gas Agreement (which are also capped prices), domestic consumers pay Non-Signing Producers much lower prices for the same volumes. Consequently, the prices that MASA receives for its re-routed gas are not only substantially lower than those agreed in the contracts with its export customers, but they are also lower than the prices that the Signing Producers receive for their "re-routed" volumes.

76. Even though MASA ultimately chose not to sign the Second Gas Agreement, the Claimants assert that Resolution SE 599/07 presented MASA with two choices, both of which entailed bad outcomes: (i) to sign the Second Gas Agreement and consequently assume domestic supply commitments that it could not possibly fulfil

[61] Resolution SE 752/05, Art. 20 (Exhibit C-64).

without interrupting supplies under existing export contracts, or (ii) to become a Non-Signing Producer, and therefore, be the first to suffer from export curtailments and re-routing to domestic consumers at depressed, regulated, and discriminatory prices

77. By enacting Law 25,561, which authorised the Executive Branch to impose export withholdings on hydrocarbons and authorised the Executive Branch to establish the respective applicable rates,[62] the GOA completely disregarded the guarantees, provided for by Decree 1589/89,[63] that export and import of hydrocarbons and their byproducts would be exempt from any present or future tariffs, duties, or withholdings and the safeguards against discriminatory and specific taxes.

78. As mentioned above, the Legal Framework provides that the highest royalty rate that could be imposed on gas producers is 12%.[64] Under Law 25,561, however, the GOA prohibited the Claimants from deducting Export Withholdings payments when calculating royalties. This prohibition forced the Claimants to pay royalties on their gas export sales based on prices higher than they received *(i.e.*, without deducting Export Withholdings).

b. The Respondent's position

79. Argentina first raises a number of objections relating to the jurisdiction of the Centre and of the competence of the Tribunal as well as objections relating to the admissibility of the Claimants' claims. On those grounds, Argentina requests the Tribunal to declare that this dispute does not fall within the jurisdiction of the Centre or the competence of the Tribunal as well as that the claim is inadmissible. Those objections are dealt with below at VI.

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[62] Law 25,561, Art. 6 (Exhibit C-41).
[63] Decree 1589/89 (Exhibit C-28).
[64] *Supra* ¶ 59.

80. Argentina contends that there are three main reasons why this claim, in its entirety, manifestly lacks any merit: (i) with respect to the regulatory measures for the pesification of contracts, there are no longer any serious doubts as to the fact that this was a necessary measure for the protection of public order and essential security interests, expressly authorized by Article XI of the BIT and which, therefore, does not breach the Treaty; (ii) with regard to the export duties, as they are "matters of taxation" in the terms of Article XII of the BIT, they fall outside the jurisdiction of this Tribunal, except where there is expropriation or an investment agreement, which is clearly not the case here; and (iii) in relation to the requests for additional injection, as the Claimants decided to (successfully) submit the dispute to the Argentine courts, the Tribunal also lacks jurisdiction over that measure in pursuance of the provisions of Article VII.3(a) of the BIT (choice of forum). According to Argentina, these three fundamental reasons are enough for the Tribunal to reject the claim in whole. However, there are also significant additional reasons why the Claimants' claims must be rejected by the Tribunal.

81. The measures adopted by the Argentine Government in order to deal with the most serious crisis in its entire history, as well as to defuse the gas crisis are expressly authorised under Article XI of the BIT.

82. As a result, those measures could never amount to a violation of the BIT or give rise to the Argentine State's international responsibility. Article XI of the BIT is a primary rule which defines the scope of the substantial obligations under the BIT.

83. Argentina contends that the intention of the Contracting Parties to the BIT was that each Contracting party has the exclusive right to judge whether the measures taken under Article XI of the BIT were necessary to maintain public order or protect essential security interest, subject only to the principle of good faith. This should be taken into account by the Tribunal.

84. According to Argentina, Article XI applies to any situation where the State must adopt measures in order to maintain public order or protect its own essential security interests, since that provision contains no limitation in that respect.

85. The pesification of the economy was a necessary measure in order to maintain public order, as well as, to protect essential security interests. Furthermore, the export duties and the requests for additional injection of gas volumes were also necessary in order to guarantee domestic supply and maintain public order.

86. The imposition of export duties was and still is a necessary measure. Export duties are necessary, since they provide means for paying the costs required by the emergency situation and for dealing with energy problems existing in the country.

87. The requests for additional injection were and are still necessary solutions to the delicate situation regarding energy. The supply of the domestic market is the main objective and priority of all hydrocarbon activities in Argentina and is confirmed by the Hydrocarbons Law.

88. Since the application of Article XI means that the measures adopted in accordance therewith are lawful and thus do not amount to a violation of the BIT, there is no obligation to compensate for the consequences derived from such measures.

89. Moreover, the Argentine Republic acted in accordance with Article IV.3. of the BIT. On the one hand, the measures taken by the Argentine Government and challenged by the Claimants responded to a state of national emergency. The State was forced to adopt the measures at issue to avoid the dangers deriving from such state of emergency. On the other hand, the measures adopted in response to the state of national emergency were of a general nature and impacted the Argentine economy as a whole

90. In conclusion, in cases of "state of national emergency" or "other similar events," if foreign investors suffer losses, the only obligation of that State under the BIT pursuant to Article IV.3 is not to discriminate if it decides to take measures in relation to such losses. The Argentine Republic fully complied with the special regime under the BIT for emergency situations, and, therefore, it does not violate any of the BIT provisions.

91. Pursuant to Article XII of the BIT, the tax related arbitral claims are limited to cases of expropriation, transfers or investments agreements. The tax measures adopted by Argentina are not expropriatory in nature and they have not breached any investment agreement between the Claimants and Argentina. In addition, Article XII of the BIT expressly excludes the possibility that export duties and royalties may be held to be contrary to the standard of fair and equitable treatment, the standard of protection and security, the provision on arbitrariness and discrimination and the umbrella clause.

B. The Final Submissions of the Parties

92. Paragraph 229 of the Claimants' Post Hearing Brief reads as follows:

> "For the reasons stated herein, the Claimants respectfully request an award granting the following relief:
>
> A decision rejecting Argentina's objections to jurisdiction of the Tribunal and the admissibility of the claims;
>
> A finding and declaration that Argentina has violated various provisions of the BIT and international law;
>
> An order that Argentina compensate the Claimants for all damages they have suffered;
>
> An order that the Argentine Republic pay the costs of these proceedings, including the Tribunal's fees and expenses, and the costs of the Claimants' legal representation and other costs;

> An award of pre- and post-award interest on all amounts awarded, compounded quarterly until the date of payment; and
>
> A gross-up of any taxes that may be imposed by the Argentine tax authorities; and
>
> Such other relief as may be appropriate under the BIT or may otherwise be just and proper."

93. Paragraph 223 of Argentina's post-hearing submissions states the following:

> "In view of the foregoing, the Argentine Republic, respectfully requests the Tribunal:
>
> to declare the Centre's absence of jurisdiction and the Tribunal's absence of competence over the Claimants' claim;
>
> alternatively, to dismiss each and all of the claims put forward by the Claimants; and
>
> to order the Claimants to pay for all costs and expenses arising from these arbitration proceedings, plus any applicable interest."

VI. ISSUES OF JURISDICTION

A. General Observations

94. Article 25 of the ICSID Convention lays down the general parameters for ICSID's activity and deals with the substantive questions of jurisdiction of the Centre. Article 41 of the Convention makes the arbitral tribunal the judges of their own competence.

95. Article 25 of the Convention contains requirements relating to the nature of the dispute (*ratione materiae*) and to the parties (*ratione personae*). In addition the parties must give their consent. The requirements relating to the nature of the dispute are that it must arise directly from an investment and that it must be of a legal nature. Those relating to the parties specify that one side must be a Contracting State and the other a national of another Contracting State. All other parts of Article 25 either define or otherwise specify these essential requirements.

96. Articles VII (4) of the BIT provides that each party to the Treaty consents to the submission of any investment dispute for settlement by binding arbitration in accordance with the choice specified in the written consent of the national or company under paragraph 3 of the same article. This paragraph provides that the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration *inter alia* to the International Centre for the Settlement of Investment Disputes **("Centre")**, provided that it has not submitted the dispute for resolution to the courts or administrative tribunals of the Party that is a party to the dispute or in accordance with any applicable, previously agreed dispute-settlement procedures and that six months has elapsed from the date on which the dispute arose.

97. The Claimants contend that the dispute between the Claimants and Argentina is a legal dispute over the injuries suffered by MEDA and MASA under the BIT and international law and that the dispute arises directly out of MEDA's and MASA's investments, namely: (i) legal and contractual rights arising under the Legal Framework, the Hydrocarbon Concessions and Contracts. and the Sierra Chata Gas Export Permit; (ii) rights arising out of export and domestic gas contracts; (iii) US$ 523 million invested by the Claimants in Argentina; and (iv) claims to money and performance having economic value under the Claimants' contract and legal rights.

98. The dispute is between Argentina, which became a Contracting State to the ICSID Convention on 18 November 1994, and MEDA, a company incorporated in Delaware and a national of the United States, which became a Contracting State on 14 October 1966 and MASA, an Argentine corporation, that the Claimants contend is controlled by US corporations.

99. According to the Claimants, the dispute arose with the Emergency Law No. 25,561, which was enacted and partially promulgated on 6 January 2002 and it was published in the Argentine Official Gazette on 7 January 2002.

100. Pursuant to Article 25 (2) (b) of the ICSID Convention "National of another Contracting State" means any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to arbitration and any juridical person which had the nationality of the Contracting State, party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as national of another Contracting State for the purposes of the ICSID Convention.

101. Article VII (8) of the BIT provides that for purposes of an arbitration held under paragraph 3 of the same Article, any company legally constituted under the applicable laws and regulations of a Party, or a political subdivision thereof but that, immediately before the occurrence of the event or events giving rise to the dispute, was an investment of nationals or companies of the other Party, shall be treated as a national or company of such other Party in accordance with Article 25 (2) (b) of the ICSID Convention.

102. The Claimants contend that MASA, despite being an Argentine corporation, should be treated as a U.S. Company for the purposes of this arbitration proceeding, because on the date MASA consented to submit this dispute to ICSID arbitration – 19 December 2003 – and immediately before the event or events giving rise to this dispute – 6 January 2002 –, MASA was indirectly controlled by Exxon Mobil Corporation, a company incorporated under the laws of the State of New Jersey in the United States of America.

103. Argentina and the Claimants have consented in writing to submit the dispute to ICSID arbitration; Argentina's consent is contained in Article VII(4) of the BIT; MEDA and MASA notified Argentina of their consent as required by Article VII(3)(a)(i) of the BIT, through a letter on 19 December 2003.

B. Argentina's objections to the jurisdiction of the Centre, the competence of the Tribunal and the admissibility of the Claim

1. General Observations

104. Argentina requests the Tribunal to declare that this dispute does not fall within the jurisdiction of the Centre or the competence of the Tribunal and that it is inadmissible. Although the title of the document in which this request is made is entitled "MEMORIAL OF THE ARGENTINE REPUBLIC ON OBJECTIONS TO THE JURISDICTION OF THE CENTRE, THE COMPETENCE OF THE TRIBUNAL AND THE ADMISSIBILITY OF THE CLAIM", all the seven objections included in the document are under the heading "Objections to Jurisdiction".

105. Of those seven objections, the following are objections to ICSID jurisdiction and to the competence of the Tribunal:

1) The Claimants have not proven that MEDA had acquired the investment it invokes before the 19 December 2003, when the Request for Arbitration was made;

2) Neither MEDA – directly or indirectly – nor MASA – directly are entitled to pursue claims in relation to the Exploration Permit, the Exploitation Concession and the Transportation Concession in the Chihuidos Block for measures adopted after the transfer of going concern from MEDA to MASA;

3) There is no evidence that MASA, which is an Argentine corporation, on 19 December 2003 (i.e. on the date on which the Claimants consented to submit the dispute to the jurisdiction of ICSID) was subjected to foreign control;

4) ICSID has no jurisdiction and this Tribunal has no competence in the matters of taxation raised in this case, since pursuant to Article XII of the

BIT the provisions of the BIT shall apply to matters of taxation *only* with respect to cases envisaged in that Article.

106. In addition to those four objections to ICSID jurisdiction and to the competence of this Tribunal, Argentina raises three more objections based on the admissibility of the Claim:

1) The two successive Ancillary Claims the Claimant submitted after filing and registration of the Request for Arbitration are not admissible, since they do not arise directly out of the subject-matter of the dispute raised in the Request for Arbitration and are not closely connected with that dispute, in the sense of Article 46 of the ICSID Convention and Rule 40 of the Arbitration Rules.

2) The Claimant's claims in relation to restrictions on natural gas exports and the rerouting of natural gas volumes to the domestic market are not admissible, given that MEDA and MASA submitted those issues to Argentine courts before submitting them to the Centre.

3) The claim regarding the obligation to pay royalties on gas exports, without deducting Export Withholdings has become moot.

107. When analyzing the objections raised by Argentina, the Tribunal will follow the same order in which they have been submitted by Argentina without any distinction between the objections relating to jurisdiction *strictu senso* and objections relating to the admissibility of the Claim.

108. The order in which the objections were presented is as follows: *First*, The Claimants' First Ancillary and their Second Ancillary Claim, which were filed on 10 February 2006 and 15 October 2007 respectively, i.e. after the filing and registration of the

Request for Arbitration in this case on 19 December 2003 and 5 August 2004 respectively, do not arise directly out of the subject-matter of the dispute raised in the Request for Arbitration and thus do not satisfy the requirements of Article 46 of the ICSID Convention and of Arbitration Rule 40. *Second*, the Tribunal lacks competence with respect to the Claimants' claims in relation to the restrictions on natural gas exports and the rerouting of natural gas volumes to the domestic market, given that MEDA and MASA submitted those issues to the Argentine courts before submitting them to the Centre. *Third*, the claim regarding the obligation to pay royalties on gas exports without deducting the Export Withholdings has become moot. *Fourth*, the Tribunal lacks jurisdiction over the Claimants' taxation claims under Article XII of the BIT, since that article only allows tax claims for expropriation, failure to observe the terms of either an investment agreement or an investment authorization or with respect to transfer of funds. *Fifth*, there is no evidence of MEDA's alleged investment. *Sixth*, MEDA has not proven to have validly assigned its alleged interests to MASA. *Seventh*, the Claimants have not proven that MASA, despite being an Argentine corporation, should be treated as a U.S. investor under Article 25(2)(b) of the ICSID Convention and Article VI (8) of the BIT for the purposes of this arbitration, i.e. that MASA on the date they consented to submit this dispute to the jurisdiction of ICSID – 19 December 2003 – and immediately before the occurrence of the event or events giving rise to this dispute was indirectly controlled by Exxon Mobil Corporation, a company under the laws of the State of New Jersey in the United States of America

109. At the outset, before analyzing the particular issues raised by Argentina, it is vital to emphasize the scope and standard of review that shall be applied to each jurisdictional objection. In international adjudication and arbitration, it is axiomatic that the standard of review at the jurisdictional threshold is whether the factual allegations, *if* true, *could* constitute a violation within the Tribunal's jurisdiction. If the answer to this inquiry is in the affirmative, jurisdiction should be sustained. Thus the Claimants

need not establish either that the facts alleged are true or that such facts, if proved, would necessarily violate the BIT.

2. *First objection: The Tribunal has no jurisdiction over the Claimants First and Second Ancillary Claim*

a. <u>The Parties' Positions</u>

i. The Respondent

110. Argentina contends that the Claimants' First Ancillary Claim and their Second Ancillary Claim are not admissible on the ground that those claims do not arise directly out of the subject-matter of the dispute in the Request for Arbitration.

111. Argentina asserts that those ancillary claims do not satisfy the requirement in Article 46 of the ICSID Convention and Rule 40 (1) of the ICSID Arbitration Rules, pursuant to which the ancillary claim must arise directly out of the subject-matter of the dispute. For any ancillary claim to be admissible, Argentina argues that there must be a direct and very close connection between such claim and the subject-matter of the primary claim, such that they cannot be separated from each other and that the main claim cannot be settled if the ancillary claim is not adjudicated.

112. The subject-matter of the dispute raised in the Request for Arbitration, dated 19 December 2003, was the alleged violation by the Argentine Republic of the BIT to the detriment of MEDA and MASA, as a result of the adoption of Law No. 25,561 and Presidential Decree No. 214/2002, the pesification of natural gas and natural gas liquids supply contracts, and the elimination of adjustment and indexation clauses contained in public utility contracts, including tariffs for natural gas distribution.

113. However, in their First Ancillary Claim dated 10 February 2006, the Claimants mentioned complaints completely different to those included in the Request for

Arbitration. Such complaints related to the restrictions and rerouting of gas exports, as well as to the imposition of export duties by the Argentine Republic.

114. On 15 October 2007, the Claimants filed a Second Ancillary Claim, where they insisted on their ancillary claims regarding the restrictions on the rerouting of exports indicated in their First Ancillary Claim.

115. In light of the above, neither the First Ancillary Claim nor the Second Ancillary Claim arises directly out of the subject-matter of the dispute raised by the Claimants in their Request for Arbitration. The Request for Arbitration refers to a measure of general regulation, known as "pesification," which regulated the currency of hundreds of thousands of contracts of very different nature — from lease agreements between two individuals involving insignificant amounts to public utility contracts —and to the elimination in public utility contracts of indexation clauses based on price indexes from other countries. Conversely, the First and Second Ancillary Claims refer to restrictions on gas trade, which measures exclusively refer to the hydrocarbons sector, and to the imposition of export duties on natural gas.

116. The Ancillary Claims challenge measures different to those challenged in the Request for Arbitration, they involve different legal issues and different elements, and the scope and nature of the dispute raised in the Ancillary Claims are different to those raised in the Request for Arbitration

ii. The Claimants

117. In the Claimants view their ancillary claims comply with Article 46 of the ICSID Convention and Rule 40 of the Arbitration Rules, since they arise directly out of the subject-matter of the dispute, fall within the scope of the parties' consent to ICSID arbitration and are otherwise within the Tribunal's jurisdiction. Even if the Tribunal were to accept Argentina's objection on ancillary claims, that conclusion would not dispose of any jurisdictional issues since the Claimants would maintain standing to

bring their ancillary claims in a separate ICSID proceeding. The practical consequence of accepting Argentina's argument would entail a risk of inconsistent decisions under the BIT regarding Argentina's measures toward the Claimants' investment and would conflict with the goals of judicial economy that the drafters of the ICSID Convention sought to achieve.

b. The Tribunal's analysis

118. The question to be addressed by the Tribunal is whether the First Ancillary Claim and the Second Ancillary Claim are "incidental or additional claims arising directly out of the subject-matter of the dispute." As Argentina points out Note B to Arbitration Rule 40 in the explanatory note adds the following explanation:

> "The test to satisfy this condition is whether the factual connection between the original and the ancillary claim is so close as to require the adjudication of the latter to achieve the final settlement of the dispute, the object being to dispose of all the grounds of dispute arising out of the same subject-matter."[65]

119. The quotation above from Note B (a) to Arbitration Rule 40 may seem to be a somewhat narrower description of the standard which, of course, is to be found in the authentic languages of Article 46 and Rule 40. But, the phrase "to require adjudication of the latter in order to achieve the final settlement of the dispute" is clearly not equivalent to, as Argentina suggests, to a requirement that ancillary claims be adjudicated if, and only if, the initial claims *cannot* be resolved without the ancillary claims. That is not what Article 46 and Rule 40 say.

[65] ICSID Rules of Procedure for Arbitration Proceedings (Arbitration Rules) with explanatory notes prepared by the ICSID Secretariat, January 1968, note to Arbitration Rule 40, 1 ICSID REPORTS 63,100 (1993)(Exhibit LA AR-1).

120. Thus the Tribunal must reach a determination on the subject-matter of the dispute and decide whether the ancillary claims arise directly out of that subject-matter.

121. In their Request for Arbitration dated 19 December 2003, the Claimants submit at page 22 under the heading "The Dispute" as follows:

> "In breach of the above undertakings and the guarantees and protections established in the BIT, international law, the Hydrocarbon Regulatory Framework, the Hydrocarbon concessions and Contracts and other legal and contractual rights of the Claimants, Argentina has unilaterally taken certain measures including, but not limited to, the enactment, issuance and/or approval of Law 25.561 AND Decree No 214/2002, as amended. Wide ranging and damaging changes have been introduced, including the repeal of certain key provisions of the Hydrocarbon Regulatory Framework, which directly impacted and significantly injured Claimants' investments in Argentina."

122. In the light of this broad language and since the claim raised in the Request for Arbitration and the ancillary claims involve the same contracts, concessions and permits and legal framework and arise of the sovereign measures which directly affected the Claimants' legal and contractual rights and their natural gas business, the Tribunal is of the view that in the instant case the subject-matter of the dispute are the alleged damages caused, it is argued, by Argentina's violation of its obligations owed to the Claimants under the BIT. The measures giving rise to the claim raised in the Request for Arbitration and the ancillary claims form a unified sequence of sovereign acts. The GOA enacted the measures that form the basis of the ancillary claim in reaction to the macroeconomic effects of the measures at the heart of the claim raised in the Request for Arbitration. Those measures constitute an aggravation of the initial restrictions on the Claimants' right to freely market and price their natural gas production.

123. Moreover, as the Claimants argue, consideration of the original claim in isolation would not fully resolve the dispute over price interference, which includes measures giving rise to the ancillary claims. Even if Argentina's objection on ancillary claims were accepted that conclusion would, as the Claimants argue, not dispose of any

jurisdictional issues since this would not affect the Claimants standing to bring their ancillary claims in a separate ICSID proceeding. Thus also procedural efficiency and the interest to avoid inconsistent decisions speak against Argentina's objection. Resolving the original and ancillary claims in the same arbitration will ensure a more consistent and efficient outcome. Argentina will suffer no prejudice by the consolidation of the Claimants' original and ancillary claims, since the ancillary claims were filed well in advance of the Tribunals constitution, and Argentina and ICSID were aware of those claims when making their decisions of whom to appoint and whether to accept appointments to the Tribunal. The objection is accordingly dismissed.

3. Second objection to jurisdiction – Fork in the road

a. The Parties' Positions

i. The Respondent

124. Second, Argentina contends that the Tribunal lacks competence with respect to the Claimants' claims in relation to the restrictions on natural gas exports and rerouting of natural gas volumes to the domestic market, given that MEDA and MASA submitted those issues to the Argentine courts approximately two years before submitting them to the Centre. This, it is alleged, amounts to the choice of local courts under the BIT and hence the "fork in the road" provision has been triggered and the jurisdiction of an ICSID tribunal would thus be precluded.

125. Article VII of the BIT sets forth *inter alia*:

> "2. In the event of an investment dispute, the parties to the dispute should initially seek a resolution through consultation and negotiation. If the dispute cannot be settled amicably, the national or company concerned may choose to submit the dispute for resolution:
>
> a) to the courts or administrative tribunals of the Party that is a party to the dispute; or

> b) in accordance with any applicable, previously agreed dispute-settlement procedures; or
>
> c) in accordance with the terms of paragraph 3.
>
> 3. (a) Provided that the national or company concerned has not submitted the dispute for resolution under paragraph 2 (a) or (b) and that six months have elapsed from the date on which the dispute arose, the national or company concerned may choose to consent in writing to the submission of the dispute for settlement by binding arbitration:
>
> i) to the International Centre for the Settlement of Investment Disputes("Centre") established by the Convention on the Settlement of Investment Disputes between States and Nationals of other States, done at Washington, March 18, 1965 ("ICSID Convention"), provided that the Party is a party to such Convention;..."

126. MASA and MEDA filed with the federal courts of the provinces of Salta and Neuquén, respectively, two *amparo* actions asking that the measures taken by the GOA in relation to natural gas exports and rerouting of natural gas volumes to the domestic market be set aside on grounds of illegitimacy and manifest arbitrariness. In such actions filed by MEDA and MASA with the Argentine federal courts, the Claimants complained about the same resolutions, decisions and notes issued by the Argentine authorities as the one they complained about before ICSID and this Tribunal in their ancillary claims.

127. MASA filed before the local courts a claim on the grounds of the illegality and arbitrariness of "Resolution No. 265 of the Secretariat of Energy, of Decision No. 27/04 of the Under-Secretariat of Fuels," and of "Resolution No. 659/2004 of the Secretariat of Energy, amending Decision No. 27/04 of the Under-Secretariat of Fuels." Furthermore, in its financial statements, MASA reported that it had challenged the rules related to gas rerouting and Resolution No. 810/07 of the Secretariat of Energy, suspending the permit to export from Aguaragüe.

128. MEDA also filed claims before the local courts, asking that the following regulations be set aside on grounds of illegality and manifest arbitrariness:

> "(a) article 31 of Presidential Decree No. 180/04, article 1(c) of Resolution No. 265/04 of the Secretariat of Energy and Decision No. 27/04 of the Under-Secretariat of Fuels;
>
> (b) Notes No. 1261 and 1269 of the Under-Secretariat of Fuels and Resolution No. 503/04 of the Secretariat of Energy;
>
> (c) Resolution No. 659/04 of the Secretariat of Energy;
>
> (d) Notes No. 1871, 2016, 2054, 2132 and 2155 of the Under-Secretariat of Fuels, Resolutions No. 807/04, 909/04 and 715/04 of the Secretariat of Energy and Presidential Decree No. 741/04; Marketing Office, and Resolution No. 752/05 of the Secretariat of Energy;
>
> (l) Notes No. 1414 and 1451 of the Argentine Hydrocarbons Office; and
>
> (m) Resolutions No. 925/05 and 930/05 of the Secretariat of Energy."

129. In the Respondent's view, it is clear that MEDA's and MASA's claims filed with the Argentine courts are substantially the same as their claims subsequently filed with ICSID.

130. In order for the fork-in-the-road provision to apply, it is not necessary for the claims filed with the local courts to be exactly identical to the claims filed with international tribunals, but it is enough for the claims to be substantially the same.

131. Finally, the Respondent emphasises that MEDA and MASA's claims submitted to the Argentine courts are based on the same measures and grounds as their claims before this Tribunal. The Claimants made their choice and decided to submit the issues related to restrictions on natural gas exports and rerouting of natural gas volumes to the domestic market to Argentine courts, which is why they have forfeited the possibility of raising such issues before ICSID and this Tribunal, pursuant to Article VII(3)(a) of the BIT. Consequently, the Tribunal has no jurisdiction with respect to those issues.

ii. The Claimants

132. The Claimants are of the opinion that to trigger the fork-in-the road provision the *amparo* actions must have involved an investment dispute as defined in the BIT, as well as a purpose and a cause of action identical to that before the Tribunal in this arbitration. The disputes to which the fork-in-the road provision in the BIT applies are "investment disputes", as defined in Article VII (1) of the BIT, which provides:

> "For purposes of this Article, an investment dispute is a dispute between a Party and a national or company of the other Party arising out of or relating to (a) an investment agreement between that Party and such national or company; (b) an investment authorization granted by that Party's foreign investment authority (if any such authorization exists) to such national or company; or (c) an alleged breach of any right conferred or created by this Treaty with respect to an investment."

133. In the Claimant's view the *amparo* actions instituted in Argentine courts are not such disputes. Those actions did not involve any claims that Argentina violated the BIT. The sole purpose of the *amparo* actions was to declare Argentina's export restrictions and re-routing measures as unconstitutional and void under Argentine law. The object of this BIT arbitration is to determine whether Argentina has violated the treaty provision of the BIT, and if so, what damages those violations yield. The decisions in the *amparo* actions could not resolve these questions.

134. Accordingly, the Claimants' *amparo* actions were aimed at the restoration of legal and constitutional rights under Argentine laws and there was no jurisdiction other than the Argentine courts to deal with the constitutionality of the measures in Argentina or for the Claimants to defend their rights under Argentine law. However, damage claims are not admissible in *amparo* actions.

135. Had the Claimants not been able to lodge the *amparo* actions, they would have been forced to passively watch their investment further deteriorate and would have suffered potential legal prejudice in their relationships with Chilean export customers who expected the Claimants to diligently defend their right to export the gas quantities

needed to perform their gas sales contracts. Moreover, had the Claimants not taken legal action, Argentina likely would have misconstrued that decision as acquiescence, as it has argued in several other ICSID proceedings.

136. The Claimants conclude that the fork-in-the -road clause in the light of the decisions of many ICSID tribunals, only excludes disputes before international tribunals that have been previously brought before local courts when those disputes involve the same purpose and the same cause of action – namely an investment dispute under the BIT. Thus the Claimants are of the view that Argentina's fork-in-the-road objection lacks merit and request that it be rejected.

b. The Tribunal's analysis

137. This objection to the admissibility of the claims only concerns the claims in relation to export restrictions and rerouting of volumes of natural gas to the domestic markets.

138. According to a note of MEDA and MASA of 13 July 2008 addressed to the Secretary of Energy, MEDA and MASA relinquish their rights to claim and/or begin or follow any action, national or international, arising out of or having their origin in the restrictions to the export of natural gas resulting from the application of several resolutions *inter alia* Resolution 810/07.[66] Taking into account this note and the motion filed by MASA on 21 December 2009 relinquishing the *amparo* action and the supplementary *amparo* petitions filed with the Federal Court of Salta (concerning the Aguaragüe exploitation),[67] the objection is limited to the *amparo* action brought before the Federal Court of Neuquén in 2004 (concerning the exploitation in the

[66] See Claimants' letter to the Arbitral Tribunal dated 7 August 2009 with attachments (Exhibit L-15).
[67] See Motion filed on 21 December 2009 by María Celeste Godoy and Héctor Cornejo D'Andrea, in the case captioned "*Tecpetrol S.A. and Mobil Argentina S.A. v. Argentine Government on Action for the Constitutional Rights*" (Exhibit AR-315).

Chihuidos area). This *amparo* action has been decided through the first instance ruling by the Federal Court of Neuquén dated 30 June 2010, in which the Claimants' claim was allowed.[68]

139. As stated by the Claimants, the fork-in-the -road clause, in the light of the decisions of many ICSID tribunals[69], only excludes disputes before international tribunals that have been previously brought before local courts when those disputes are between the same parties and involve the same purpose as well as the same cause of action.

140. Article 43 of the Argentine Constitution provides:

> "Any person may file an expedited and prompt amparo action, if there is no other suitable judicial remedy, against any act or omission on the part of public authorities or any private party that impairs, threatens to impair, restricts or in any other way affects rights and guarantees protected by this Constitution, a treaty or a law in an overtly arbitrary or illegal manner In this case the judge may declare the unconstitutional nature of the standard on which the act or omission is founded."

141. The Tribunal finds, in particular in the light of the legal opinion by Dr. Bianchi, which it regards reliable, that under Argentine law, the sole purpose of "*amparo* actions" is to guarantee the protection of constitutional rights upon violations caused by overtly illegal or arbitrary acts on the part of public authorities or private parties.[70] The *amparo* is a strictly summary trial, very brief, with limited proof, where the purpose is to obtain the statement of unconstitutionality or illegality of norms or a regulation, and it has no other purpose. The deadline of an *amparo* is very brief i.e. 15

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[68] Exhibit AR-334.

[69] See e.g. *CMS Gas Transmission Company v Argentine Republic*, ICSID Case No ARB/01/8, Decision on Jurisdiction (17 July 2003) [hereinafter "*CMS Decision on Jurisdiction*"] ¶80, 90-92 and *Azurix Corp v Argentine Republic, ICSID* Case No ARB/01/12, Decision on Jurisdiction (8 December 2003) [hereinafter "*Azurix Decision on Jurisdiction*"] ¶ 89-90.

[70] See Supplementary Legal opinion prepared by Alberto B. Bianchi of 30 July 2009 [hereinafter, "*Bianchi First Supplementary Opinion*"] ¶ 35.

working days. The deadline starts when the administrative action is notified, if this is an administrative action, at the very moment when the law or regulation is published in the Official Gazette, or else at the moment when the material conduct, is informed to the person concerned, and the person concerned can say that it has had the truthful knowledge. If these fifteen days lapse without a claim brought under the *amparo*, the right for an *amparo* claim will be lost.[71] The *amparo* actions are not admissible if the disputed matters require a broader investigation and production of evidence.[72]

142. Thus, an *amparo* action constitutes an alternative remedy to ordinary proceedings. This also follows from the fact that *amparo* actions are devised as summary actions with very short procedural terms that do not allow for extended debate or the production of much evidence, which is consistent with their purpose: To order that the violation of constitutional rights and guarantees cease immediately.

143. *Amparo* actions are not a proper means to seek damages. A*mparo* actions are extraordinary and their purpose is exhausted once the court orders the immediate cessation of the overtly illegal governmental conduct. Thus *amparo a*ctions are not available to seek damages.[73] This is obvious also in the light of the decisions of the Argentine Supreme Court referred to in Dr. Bianchis' report.[74]

144. The *amparo* actions that the Claimants filed with Argentine courts are not based on violations of the US-Argentina BIT. Rather, they only invoke provisions of the Argentine Constitution (the right to equality, property rights and the due process of

[71] Hearing on Jurisdiction and the Merits, 1 through 13 April 2011 [hereinafter, *"Hearing Transcript in English"]*, Day 2, Bianchi, *supra* (n 70) p. 282-284.
[72] See Bianchi First Supplemental Opinion, *supra* (n 70) ¶¶ 11-15 and 35.
[73] See Bianchi First Supplemental Opinion, *supra* (n 70) ¶¶ 21-29.
[74] See *e.g. Sargenti c/Instituto Nacional de Obras Sociales*, Fallos 322-2220 (1999) and *Gómez c/ Dirección de Bienestar de la Armada*, Fallos 327-5270 (2004), concurring vote of Justices Petracchi and Fayt. See also Bianchi First Supplemental Opinion, *supra* (n 70) ¶ 23.

law) and the Substitute Protocol No. 2 of ACE 16 executed in Buenos Aires on 7 July 1995.

145. The Tribunal finds it obvious that the sole purpose of the *amparo* actions was to declare Argentina's export restrictions and re-routing measures as unconstitutional and void under Argentine law. The purpose of an *amparo* is the restoration of the legal and constitutional rights restricted through acts that are manifestly illegal or arbitrary. As explained by Professor Reisman in his expert opinion, the *amparo* actions were defensive actions that the Claimants were compelled to file to avoid defaulting on their legal obligations to third parties in Chile.[75] An ICSID arbitral tribunal has not the power to declare an Argentine law unconstitutional or to grant an amparo. The Claimants instituted the *amparo* actions in order not to lose the rights they contend they have and not in order to seek damages. On the other hand, the purpose of the ICSID arbitration is to establish whether damages are owed by Argentina for violation of the BIT standards. *Amparo* is not a precondition to claim damages. Thus the *amparo* actions have a different cause of action and a different purpose and object than this ICSID arbitration. This is so even if decisions rendered in *amparo* proceedings become *res judicata* in relation to any subsequent claims for damages in the event that a measure is held to be unlawful.

146. To conclude, this Tribunal has no jurisdiction to set aside *any* of the laws or regulations envisaged in the *amparo* actions or declare them void under Argentine law. Conversely, the local courts of Argentina, in an *amparo* action, had, and have, no authority to adjudicate the legal claims brought in this investment arbitration; that is, they have no jurisdiction to determine whether the foregoing measures, and other measures enumerated in the Request and Ancillary Claims, violated the provisions of the BIT.

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[75] See Opinion of W. Michael Reisman on Jurisdiction of 27 July 2009 ¶ 45.

147. For the reasons mentioned above, the Tribunal finds the Respondent's objection that the Tribunal lacks competence with respect to the Claimants' claims in relation to the restrictions on natural gas export and the rerouting of natural gas volumes to the domestic market unfounded. The objection is accordingly dismissed.

4. *Third objection to jurisdiction – the claim regarding the obligation to pay royalties on gas exports without deducting the Export Withholdings has become moot*

a. <u>The Parties Positions</u>

i. The Respondent

148. Argentina contends that the Claimants' claim regarding the obligation to pay royalties on gas exports without deducting the Export Withholdings, which the Claimants allege that Argentina through Law No.25.561 (the Emergency Law) had imposed, has become moot since on 5 June 2007 (prior to the date the second ancillary claim was filed), the Supreme Court of Justice of the Argentine Republic ordered the Province of Neuquén to refrain from requiring MASA the payment of the difference for royalties resulting from the application of Decrees Nº 225 and 226 of 2006 of the Provincial Executive Branch, until a final judgment was rendered.

149. On 29 November 2007, the Executive Branch of the Province of Neuquén repealed these Decrees by issuing Decree Nº 2200/07. On 12 August 2008, the Supreme Court of Justice of the Argentine Republic declared terminated the judicial proceeding on the grounds that the Province of Neuquén and MASA had claimed the court to declare that the issue had become moot.

ii. The Claimants

150. The Claimants assert that Argentina's objection that the Claimants' claims with respect to the Province of Neuquén's practice of charging excess royalties on natural

gas exports are moot is irrelevant. Provincial Decrees 225 and 226 of 2006 concern royalties on *domestic* sales of hydrocarbons; Law 25,561 remains in effect and continues to apply to natural gas exports.

b. The Tribunal's analysis

151. The Claimants' assertion, according to which Provincial Decree 225 and 226 of 2006 concern royalties on *domestic* sales of hydrocarbons and that Law 25,561 remains in effect and continues to apply to natural gas exports, has not been rebutted by Argentina. Argentina's Counsel remarked that this claim is closely linked to the merits and that this objection will be dealt with at the merits phase[76], but this did not finally occur. Consequently, the objection is unfounded. The objection is accordingly dismissed.

5. Fourth objection to jurisdiction – the tax matters are inadmissible pursuant to the BIT

a. The Parties Positions

i. The Respondent

152. Fourth, Argentina emphasizes that pursuant to the treaty, tax matters can *only* be submitted to investment dispute resolution mechanisms contemplated in the BIT if the following is alleged: (a) that there has been an expropriation; (b) that transfers related to an investment have not been permitted; or (c) that an investment agreement or authorization has been violated.

153. Article XII of the BIT sets forth that:

[76] Transcript in English, Day 1 p. 207, 10-14.

> "1. With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party.
>
> 2. Nevertheless, the provisions of this Treaty and in particular Article VII and VIII, shall apply to matters of taxation only with respect to the following:
>
> a) expropriation, pursuant to Article IV;
>
> b) transfers, pursuant to Article V; or
>
> c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VII (l) (a) or (b),
>
> to the extent they are not subject to the dispute settlement provisions of a Convention for the avoidance of double taxation between the two Parties, or have been raised under such settlement provisions and are not resolved within a reasonable period of time."

154. Articles VII and VIII of the Treaty mentioned in Article XII establish systems for the resolution of investor-host State disputes and of disputes between signatory member States, respectively.

155. Argentina asserts that this case does not involve any of the above referred three issues. First, the imposition of export withholdings did not cause the expropriation of the Claimants' legal and contractual rights, since the Claimants transferred those export duties on to their Chilean customers. Second, there is no investment agreement or authorisation between the Claimants and the Argentine Republic. Finally, in connection with the question of transfers (item b), MEDA and MASA have not filed any complaint about this issue.

156. Although the first paragraph of Article XII of the BIT states that "[w]ith respect to its tax policies, [the State] should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party", Argentina argues that, despite that "lax duty of acting with fairness and equity in connection with tax

policies,"[77] Article XII provides that only the above mentioned three issues authorize the use of the mechanisms contemplated in Articles VII and VIII of the BIT.

157. The Claimants cannot, says Argentina, even claim that their alleged investments were not accorded fair and equal treatment. The text of Article XII is clear as regards two aspects. First, that in the case of tax matters the "duty to give a fair and equal treatment" is merely "an effort." Second, it is also clear that "notwithstanding" that "effort," the BIT dispute resolution mechanisms are "only available" for a series of issues not including the allegation of "unfair and inequitable treatment."

158. Moreover, Argentina asserts that for an investment agreement to exist, it must contain an international element. In investment agreements, the parties agree upon a special regime for the treatment of the foreign investment with one or several elements that "internationalise" that agreement.

159. On the one hand, the concessions invoked by the Claimants have no international element. The law applicable to those concessions is Argentine law. It was established that any dispute arising out of those concessions would be submitted to the local courts. Therefore, they may not be considered investment agreements. On the other hand, Claimants have not proved that, at the time they submitted their claim, there was any agreement or instrument between Argentina and MEDA.

160. The Sierra Chata Concession is not an investment agreement. The Sierra Chata Concession as well as other hydrocarbons concessions are contracts governed by the Argentine legislation without any international element that might turn them into an investment agreement.

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[77] *Memorial of the Argentine Republic on Objections to the Jurisdiction of the Centre and the Competence of the Tribunal and the Admissibility of the Claim*, ¶ 69.

ii. The Claimants

161. The Claimants contend that their claim regarding Export Withholdings and excess royalties involves: (i) Argentina's expropriation of specific legal and contractual rights and revenues; (ii) Argentina's failure to observe and comply with investment agreements (such as the Hydrocarbon Concessions and Contracts); and (iii) Argentina's unfair and inequitable treatment of the Claimants' investment.

162. *First*, Argentina's decision to establish Export Withholdings, either by itself or in conjunction with other measures, can constitute a measure "tantamount to expropriation" under the BIT.

163. *Second*, the Claimants argue that it is not correct that the first paragraph of Article XII of the US-Argentina BIT ("each Party should strive to accord fairness and equity in the treatment of taxation") eliminates the "fair and equitable treatment" standard set forth by Article II of the BIT. Even though it may be a soft obligation, it is nevertheless an enforceable obligation under international law like the obligation to negotiate in good faith. Argentina failed to provide fair and equitable treatment to the Claimants' investment in Argentina by withholding commitments expressly exempting the Claimants from Export Withholdings and violating commitments to charge a maximum royalty rate of 12 % on natural exports.

164. Moreover, the Claimants argue that Argentina imposed the Export Withholdings and excess royalties in an inequitable and discriminatory manner against the Claimants. In addition to the taking of the Claimants' legal and contractual rights by imposing the Export Withholdings and excess royalties on exports, Argentina's treatment of the Claimants' investment in relation to the Export Withholdings has been discriminatory, because the taxes: (i) were designed to compensate the banking sector for losses caused by other government measures; and (ii) targeted businesses of a specific nature, which is precisely the standard that the Legal Framework and the

Hydrocarbon Concessions and Contracts used for excluding the applicability "of discriminatory taxes."

165. In the Claimants' view Article XII of the BIT does not deprive the Claimants of their right to bring a claim under Article VII for Argentina's violation of the standards provided by Articles II and IV of the BIT. The provision on expropriation in Article IV is made directly relevant by the terms of Article XII (2), which expressly refers to Article IV. Article IV, in turn, provides that one of the conditions for a legal expropriation is compliance with the provisions of Article II (2) which include fair and equitable treatment. The Claimants' claim regarding the imposition of Export Withholdings and excess royalties on export constitutes an expropriation claim.

166. *Third*, the Claimants assert that the imposition of the Export Withholdings and excess royalties on exports resulted in the violation of commitments undertaken by Argentina under the BIT. As Argentina itself acknowledges, ICSID jurisdiction is available, and the provisions of the BIT apply (including those related to dispute resolutions mechanisms) if the dispute concerns an expropriation. Claimants' claim regarding the imposition of Export. Withholdings and excess royalties on exports constitute an expropriation claim.

167. The Claimants contend that the mere assertion of an expropriation is enough for the Tribunal to find jurisdiction in this case. Whether an expropriation of specific legal and contractual rights and revenues has occurred is not an issue for the Tribunal to decide at his stage of the proceedings, but should instead be decided at the merits phase. As for jurisdictional objections, ICSID tribunals must consider the claims as alleged by the Claimants in their Memorial, and jurisdiction exists to consider the dispute included in the Claimants' Memorial since the Claimants have *prima facie* shown that they have an expropriation claim. The dispute relates to an expropriation of legal and contractual rights and revenues, and consequently, falls within the scope of Article XII (2) (a) of the BIT.

168. *Fourth*, the Claimants assert that the Hydrocarbon Concessions and Contracts are a relevant part of the Claimants' dispute and constitute investment agreements under the BIT for purposes of the tax-related claims under Article XII of the BIT. Nowhere in the BIT is the term "investment agreement" defined. It was not used as a special term with a special meaning or as a term of art. The purpose is simply by using the term "investment agreement" to exclude ordinary commercial contracts that are not related to an investment.

169. The Claimants were granted rights to natural resources owned by the Federal or Provincial States. The Claimants' rights were conferred by virtue of a sovereign power which, of course, takes them out of the realm of ordinary commercial Concession Contracts. Thus the Claimant's Permits and concessions establish a legal relationship between them and the Argentine State.

170. Contrary to Argentina's assertion, no "international" element is required for the Hydrocarbon Concessions and Contracts to qualify as an investment agreement. There is no language in the BIT that requires any international element for an investment agreement. Even if an international element were necessary, it is present in this case. MEDA and MASA qualify as United States nationals under the BIT, and thus imbue the Hydrocarbon Concessions and Contracts with an international character. Moreover, other foreign companies and their subsidiaries were and are parties to the Hydrocarbon Concessions and Contracts. In addition, Argentina granted the Hydrocarbon Concession and Contracts as part of a movement to attract foreign companies to invest in Argentine hydrocarbon fields.

171. Thus, and "without prejudice to the fact that jurisdiction can also be affirmed on other grounds" as respects Article XII of the BIT, the failure to observe the commitments undertaken by Argentina in those "investment agreements" with respect to tax issues constitutes a *prima facie* violation of the standards of protection established by the BIT, which gives this Tribunal jurisdiction under the BIT.

b. <u>The Tribunal's analysis</u>

172. Article XII (2) of the BIT provides as follows:

> "Nevertheless, the provisions of this Treaty, and in particular Article VII and VIII, shall apply to matters of taxation only with respect to the following:
>
> (a) expropriation, pursuant to Article IV,
>
> (b) transfers, pursuant to Article V; or
>
> (c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VII (1) (a) or (b),
>
> to the extent they are not subject to the dispute settlement of a Convention for the avoidance of double taxation between the two parties, or have been raised under such settlement provisions and are not resolved within a reasonable period of time."

173. Thus, the Tribunal has no jurisdiction for tax matters except in the three situations referred to in Article XII (2) (a-c). The Claimants' have not filed any complaint about the question of transfers (item b).

174. The Claimants have made out a *prima facie* case that the GOA measures may have resulted in an expropriation of the Claimants' investment or that there may be an investment agreement as that notion may be generally understood – the notion in question is not defined by the BIT. Accordingly, to establish the Tribunal's jurisdiction, the Claimants can rely on the exceptions stated in Article XII (2).

175. Nevertheless, the question whether the Claimants' claim regarding Export Withholdings and excess royalties is an expropriation pursuant to Article IV of the BIT is inextricably linked to the merits. In the Tribunal's view, the imposition of Export Withholdings or excess royalties may *prima facie* amount to an expropriation of specific legal and contractual rights and revenues. Whether such expropriation has

occurred is not an issue for the Tribunal to decide now. The Tribunal cannot decide at this point on its jurisdiction on these issue

176. At this stage, the scope of inquiry is limited to whether the Claimants' allegations, if true, could constitute an expropriation. The Claimants need not establish at that stage either that the facts alleged are true or that such facts, if proved, would necessarily violate the BIT. Conversely, only in case that the Claimants' allegations are clearly untrue or, even if true, the Claimants' allegation that their claims regarding Export Withholdings and excess royalties would be manifestly unfounded, the Tribunal would adopt a decision on its jurisdiction (see *infra* ¶864).

177. Also, the question whether the Hydrocarbon Concessions and Contracts constitute investment agreements under the BIT for purposes of the tax-related – claims under Article XII of the BIT, is inextricably linked to the merits. Confronted with the opposing views of the parties, this Tribunal points out that what matters at the jurisdictional stage is whether the claims submitted, if they were to prove well founded, would fit into the jurisdictional parameters of the BIT. Therefore we must consider the merits to solve these issues of jurisdiction.

6. Fifth objection to jurisdiction – Absence of Evidence of MEDA's Alleged Investment

a. The Parties' Positions

i. The Respondent

178. Argentina contends that the relevant law to determine the acquisition of the rights invoked as investment is the law of the host State. Thus, the exact nature of the rights invoked by the investor is to be determined according to the law of the host State and then it must be analyzed whether those rights are included in the definition of investment established in the relevant investment treaty. Therefore, the applicable law

to determine MEDA's acquisition of the rights it invokes as investment in Sierra Chata is Argentine law.

179. Argentina submits that MEDA claims that it acquired its interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession through assignments in 1996 and 1997 from BHP Petroleum (Argentina) S.A. and Mobil Argentina Limited ("MAL", previously named Monument Exploration Limited). However, the assignment from BHP Petroleum (Argentina) S.A. to MEDA was authorised by the Executive Branch only in 2005, and the assignment from MAL to MEDA has not yet been authorised by the Executive Branch.

180. According to MEDA the BHP-MEDA Purchase and Sale Agreement is one of the documents evidencing the acquisition of its interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession. By means of this agreement, the parties agreed that BHP Petroleum (Argentina) S.A. would transfer 90% of its 31.1091% interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession to MEDA.

181. Argentina contends that in accordance with Argentine law, such permits and concessions may only be assigned upon prior authorisation of the federal or provincial Executive Branch. Indeed, Law No. 17,319 (hereinafter **"Hydrocarbons Law"**) establishes that "[p]ermits and concessions awarded under the provisions of this law may be assigned, *with a prior authorisation of the Executive Branch*, to such persons who possess the qualifications and comply with the conditions and requirements established for permit or concession holders, as the case may be." [Emphasis added]. In addition, Law No. 26,197 of 3 January 2007 provides that, as from the enactment of that law, the provinces will become counterparties to the exploration permits and the hydrocarbon exploitation and transportation concessions.

182. However, the assignment from BHP Petroleum (Argentina) S.A. to MEDA was only authorised by Administrative Decision No. 459/2005, which was published in the Argentine Official Gazette on 9 August 2005. In addition, MEDA has not produced in this arbitration the instruments which would prove that it is the holder of the Exploration Permit, the Exploitation Concession and the Transportation Concession, to wit: the final notarial deeds of assignment, which had to be submitted to the enforcement authority pursuant to Administrative Decision No 459/2005.

183. Moreover, Argentina submits that the Claimants also invoke an assignment from MAL to MEDA as source of the acquisition of their interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession. Argentina also contends that this assignment is subject to authorisation of the Executive Branch, which authorisation has not yet been granted.

184. Argentina concludes that the documents presented by the Claimants in response to the request for evidence by the Argentine Republic fail to show that MEDA had acquired its alleged interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession by the date the Request for Arbitration was filed - 19 December 2003. It is clear from the documents presented by the Claimants that the assignments invoked by them were subject to the authorisation of the Federal Executive Branch. One of the assignments alleged by the Claimants — the assignment from BHP Petroleum (Argentina) S.A. to MEDA — was authorized in 2005 and the final notarial deeds of assignment have not yet been submitted. The other assignment invoked by — the assignment from MAL to MEDA — has not yet been authorised by the Executive Branch.

185. Jurisdiction must be established at the time of filing of the claim. Therefore, since the Tribunal had no jurisdiction over MEDA's claim at the time the Request for Arbitration was filed in 2003 – as it has not been proven that MEDA had acquired its alleged investment by that date – the Tribunal has no jurisdiction to entertain

MEDA’s claims for acts or omissions of the Argentine Republic occurring prior to MEDA’s acquisition of its alleged investment. Thus the Tribunal has no jurisdiction over any of MEDA's claims.

ii. The Claimants

186. The Claimants contend that the GOA has consistently recognised (and continues to recognise) the Claimants as the rightful holders of a 50.9956% working interest in the Sierra Chata Concession. For Argentina now to attempt to deny the Claimants, ownership interests in their investments constitutes an abuse of rights (*abus de droit*) and violates the principles of good faith, estoppel and *venire contra factum proprium non valet* under both international and Argentine law.

187. MEDA acquired its working interest in the title to Sierra Chata through two transactions. First, it acquired 31.1091% from BHP Petroleum (Argentina) S.A. in 1996 and 1997 (the **“BHP Assignment”**). Second, it acquired 19.8865% in 1998 from MAL as a result of a bulk transfer of assets within Mobil Corporation (the **“MAL Transfer”**).

188. On 18 September 1996, MEDA and Mobil Oil Exploration and Production Southeast Inc. executed a Sale and Purchase Agreement (the **“BHP Assignment Agreement”**) with BHP Petroleum (Argentina) S.A., BHP Petroleum (Argentina) Inc., BHP (Americas) Inc. and BHP Petroleum (GOM) Inc., through which BHP Petroleum (Argentina) S.A. assigned MEDA 90% of its working interest (a 27.99819% interest) in the title to the Sierra Chata Concession. Subsequently, BHP Petroleum (Argentina) S.A. and BHP Petroleum (Argentina) Inc. assigned their remaining working interest in the title to Sierra Chata (3.11091%) to MEDA.

189. MEDA complied with all technical and financial conditions required by law to hold its working interest in the title to the Sierra Chata Concession, but Argentina delayed issuing an authorization of the assignment for more than eight years, despite

acknowledging in 2000 that: (i) MEDA was duly registered in the Registry of Oil Companies, thus meeting the technical conditions required by the applicable regulations to hold hydrocarbon working interests; and (ii) MEDA complied with the required business solvency parameters and had a satisfactory economic and financial condition. A failure to meet these conditions constitutes the only valid reason for the Argentine Government to delay or refuse to issue an authorization.

190. In 2005, through Administrative Decision 459/05, Argentina finally issued the formal approval of the BHP-MEDA Transfer that MEDA had applied for in 1996 and 1997. Administrative Decision 459/05 confirmed that MEDA met the statutory conditions required under Article 72 of the Hydrocarbons Law to hold an interest in Sierra Chata. It also authorized BHP Petroleum (Argentina) Inc. and BHP Petroleum (Argentina) S.A. to assign 100% of their working interest in the Sierra Chata Concession (31.1091%) to MEDA. Under Article 2 of that regulation, the parties had 60 business days to submit the public deed implementing the assignment.

191. To execute a public deed, however, Article 74 of the Hydrocarbons Law requires the submission of a certificate showing that no taxes in connection with the assigned working interests remain unpaid. Although the Claimants have diligently requested this certificate, the Province of Neuquén has arbitrarily refused to issue it due to a dispute over the Province's unreasonable and arbitrary calculation of royalties that also involves most of the oil and gas companies operating in Neuquén.

192. Through a letter to the Secretary of Energy on 21 October 2005, MEDA informed the Argentine Government of the Province of Neuquén's refusal to issue the tax certificates required to obtain a public deed showing MEDA's title in Sierra Chata. In that letter, MEDA also requested an extension of the 60-day term to obtain the tax certificates from the Province of Neuquén. MEDA reiterated its request on 21 December 2005, but the Argentine Government failed to respond whatsoever to MEDA's requests.

193. The Province of Neuquén has challenged royalty payment calculations made not only by MEDA and MASA, but also by almost all companies operating in the Province. As a result, MEDA and MASA have been unable to register the deeds for their title in Sierra Chata.

194. As a result of reorganization by Mobil Corporation of its affiliates' holdings, effective on 9 December 1998, MAL assigned all of its assets and liabilities, including its working interest in the Sierra Chata Concession (19.8865%), to MEDA.

195. On 10 December 1998, MAL and MEDA informed the Argentine Government of this assignment in accordance with the provisions of Article 15 of Decree 1969/93, through which the Argentine Government granted the Chihuidos Exploration Permit.

196. As a result of another corporate reorganization in 2004, MEDA assigned to MASA its assets and liabilities, including its 50.9956% interest in Sierra Chata. In accordance with the rules set under Article 15 of Decree 1969/93, the Claimants notified the Argentine Government of this assignment on 22 December 2004.

197. It is notable that inter-affiliate transfers, such as the MAL Transfer and the MEDA-MASA Transfer, do not require authorization from the Argentine Government. Article 15 of Decree 1969/93 provides that parties may assign portions of their interest to company affiliates simply by notifying the competent authority, which the parties promptly did upon completing the transfer. Because no formal authorization of the transfer by the Argentine Government is required, Argentina's allegations that the Executive Branch did not authorise those transfers are not relevant to the lawfulness of the transfers under Argentine law.

198. In addition to showing that assignments between affiliates do not require government approval, Article 15 of Decree 1969/93 establishes that the Energy Secretariat merely takes note of inter-affiliate assignments (rather than formally authorizing them) and that the assignor remains jointly liable with its assignee affiliate for the assigned

interest in question. Thus, when making an inter-affiliate assignment, it is not necessary to request approval from the government; but if the parties want to dispense with joint liability, then they need to seek government approval exclusively for that purpose.

199. Even if Argentina were correct that executive authorization had been required for the validity of the transfers, and not simply to enable the parties to waive joint liability, the Argentine Government, and with the enactment of Law 26,197. which transferred the eminent domain of the hydrocarbon reserves to the Provinces and, as a result, all concessions granted by the Federal Government were also transferred to the provincial authorities, the Province of Neuquén, have delayed granting authorizations for these transfers. They failed to authorise these transfers despite the fact that both MEDA and MASA have been duly registered with the Argentine Registry of Oil Companies and have complied with all technical and financial conditions required by law to hold a working interest in the Sierra Chata Concession.

200. Argentina's objection that the Claimants' investment does not accord with the formalities of Argentine law must fail for at least three reasons. *First*, for more than ten years, the Argentine Government has repeatedly acknowledged that the Claimants own a working interest in Sierra Chata; consequently, Argentina is estopped from denying the lawfulness of the Claimants' investment. *Second*, any failure to register formal title of the Claimants' interest in Sierra Chata lies entirely with the Argentine Government. Argentina cannot now benefit from its own wrong in order to deny the Claimants' standing to claim for damage to their investment under the BIT. *Third*, the Claimants complied with all statutory conditions to obtain the title. Thus, the Government's failure to grant the authorizations and tax certificates in question and its current challenge of the Claimants' standing in Sierra Chata on the grounds that the Claimants have allegedly failed to comply with the requirements of the Hydrocarbons Law, a charge that first arose in the context of this proceeding, constitute an abuse of rights (*abus de droit*) under Argentine and international law.

201. The principle of estoppel bars Argentina from challenging the Claimants' standing to claim for their interest in the Sierra Chata concession. Although the governing law of this dispute stems from the BIT and international law, it is notable that Argentine law also recognizes the doctrine of *venire contra factum proprium*, which is similar to the principle of estoppel under international law.

202. The Argentine Government has consistently and publicly recognised the Claimants as the rightful owners of a working interest in Sierra Chata. In a 2004 report to the House of Representatives, the Chief of Cabinet stated that "MASA is a corporation indirectly owned by Exxon Mobil Corporation. MEDA and MASA are natural gas producers. They hold a hydrocarbon production concession in Sierra Chata, Chihuidos, the Province of Neuquén (in accordance with the Hydrocarbons Law and Decrees 1969/93 and 824/95)...." That the Chief of Cabinet has expressly recognised the Claimants' interest in Sierra Chata is significant since it was the Chief of Cabinet who was empowered to issue hydrocarbon permits and concessions and to authorise assignments.

203. Argentina has also addressed re-routing orders in the Neuquina Basin to the Claimants. The Claimants' only concession holding in the Neuquina Basin is their 50.9956% interest in Sierra Chata; thus, Argentina necessarily directed its re-routing orders to the Claimants' interest in Sierra Chata, the same interest it now purports to deny.

204. Through Note SE 1114/04, the Secretary of Energy requested certain information from the operator of the Sierra Chata Concession. The note specified that the Secretary of Energy was sending a copy of the information request to the "other holders" of the Sierra Chat Concession. In recognition of MEDA as one of the "other holders" of the Sierra Chata Concession, the Secretary of Energy sent MEDA a copy of Note SE 1114/04.

205. The Argentine Government also recognised the Claimants' interest in Sierra Chata through Resolution SE 599/07, which approved the terms of the Second Gas Agreement that Argentina sought to have producers sign. Annex I of the Second Gas Agreement, which establishes the natural gas volumes that the Argentine Government expected to receive per basin from each natural gas producer, included MASA as a producer in both the Northwestern Basin and the Neuquina Basin. MASA does not hold any interests in the Neuquina Basin aside from its interest in Sierra Chata. Therefore, Annex I confirms that Argentina recognised MASA as a concessionaire in Sierra Chata.

206. Even the Argentine Supreme Court of Justice has recently recognised MASA as holder of the Chihuidos/Sierra Chata title. In *Mobil Argentina S.A. v. Neuquén Provincia del y otro (Estado Nacional)*, MASA requested injunctive measures against the Province of Neuquén regarding the Province's calculation of royalty payments. On 5 June 2007, the Supreme Court admitted MASA's motion and implemented the requested injunctive measures against the Province of Neuquén. In that ruling, the Supreme Court expressly recognized MASA "as co-holder of the production concession of the Sierra Chata area located in the Province of Neuquén."

207. The Province of Neuquén has also recognised the Claimants as interest holders in Sierra Chata in the following ways: (i) since executing the assignments, MEDA and MASA have paid royalties on their production from the Sierra Chata block and taxes to the provincial government; (ii) in a letter that the Province of Neuquén sent to MEDA on 24 August 2005, the Province refers to MEDA as the "Concessionaire" (iii) the Province of Neuquén has held meetings with MASA regarding the Sierra Chata Concession; (iv) the Neuquén Secretariat of Natural Resources issued Resolution 54/09, Article 10 of which provides for the notification of the Resolution to "all permit and concession holders acting in the Province," and MASA received notice of this Resolution in March 2009. The Province has accepted those payments and not

challenged the fact that they are calculated on the basis of the Claimants' entire interest in the Sierra Chata Concession.

208. These non-exhaustive examples show that the Argentine Government has consistently acknowledged the Claimants' status as title holders in Sierra Chata for more than a decade.

209. A State may not rely on its own wrongful actions or omissions as a defence to internationally wrongful conduct. Thus, Argentina's own acts and omissions prevent it from challenging the lawfulness of the Claimants' investment in Sierra Chata. The Claimants took every step and fulfilled every requirement necessary to obtain authorization and formal title to their investment in Sierra Chata. Over a period of more than ten years, however, Argentina repeatedly ignored the Claimants' requests to complete these and other administrative formalities, and due to its own incompetence in processing authorization requests, failed to process the Claimants' authorization requests in a timely manner, resulting in an undue delay that is unfortunately far too common in the Argentine Government's assignment authorization process. Argentina cannot now rely on its incompetence to deny the Claimants' standing in this proceeding. Its attempt to do so constitutes an effort to benefit from its own negligent behaviour in enforcing its legal and administrative rules.

210. In addition, to relying on its own delay in granting assignment authorizations, Argentina's reliance on the Province of Neuquén's failure to grant the Claimants a tax certificate to contest the validity of the BHP-MEDA Transfer is particularly egregious. After the Argentine Government issued Administrative Decision 459/05 approving the BHP-MEDA Transfer, BHP and MEDA unsuccessfully sought to obtain a written certificate showing that there were no outstanding tax liabilities with respect to MEDA's assigned working interest in Sierra Chata. The Province of Neuquén, however, arbitrarily refused to issue the required certificate based on

interpretive disagreements regarding royalty calculations. Although MEDA promptly informed the Secretary of Energy of these circumstances and requested an extension of the deadline for executing the deed formalizing the assignment, the Secretary of Energy failed to respond in any way.

211. Since 2002, the Province of Neuquén has systematically calculated royalties for all hydrocarbon producers, including the Claimants, in excess of the 12% statutory maximum under Argentine law. As a result, the Province is involved in several legal proceedings with the majority of hydrocarbon producers in the Province's territory. In an attempt to coerce hydrocarbon producers (including the Claimants) to comply with the Province's unlawful royalty calculations (which in many cases involve calculating royalties on the basis of prices that exceed the actual sale prices as required by the Hydrocarbons Law), the Province of Neuquén refused to issue the tax certificates necessary to formally register the assignment of working interests, concessions and permits.

212. Had the Province of Neuquén issued the tax certificates, it still would have had the right to pursue its royalty claims against producers. The tax compliance certificates issued by the federal tax authority, the *Administración Federal de Ingresos Públicos* ("**AFIP"**), expressly clarify that such certificates "do not affect the AFIP's surveillance and tax determination powers." As a consequence, the issuance of a tax certificate does not imply that the agency issuing the certificate waives its right to take legal action against the certificate holder to claim for unpaid taxes. In any event, Argentina's decision to withhold a tax certificate due to its unreasonable royalty calculations has become particularly arbitrary since the Supreme Court in December 2007 ruled that royalties were not taxes.

213. In summary, the substantial delays that affected the Claimants' assignment authorization proceedings are entirely attributable to the federal and provincial governments' bureaucracy, negligence, and misuse of authority in handling those

proceedings. Thus, Argentina may not challenge the Claimants' standing in this proceeding by arguing that the difficulties created by its own agencies and political subdivisions are attributable to the Claimants.

214. Another reason to reject Argentina's attempt to contest the Claimants' standing to claim for damages to their investment in Sierra Chata is that Argentina's position constitutes an abuse of rights (*abus de droit*) under Argentine and international law. In this case, the Argentine Government has used its otherwise legitimate authority to approve assignments as a tool to achieve goals unrelated to the legitimate purpose of that authority.

215. *First*, the Argentine Government has abused its limited discretion by failing to grant the Claimants the assignment authorisations they sought for over ten years, even though the Claimants complied with the technical and financial conditions for obtaining authorisations. *Second*, in order to gain leverage in its attempt to force producers to pay unlawfully excessive royalty payments, the Province of Neuquén has arbitrarily refused to issue the tax compliance certificate. The Claimants need to notarize title to their investment. *Third*, Argentina has violated the abuse of rights doctrine by attempting to invoke a purported failure to comply with the formalities of its internal law to undermine the Claimants right to pursue its claims under the BIT and the ICSID Convention.

216. Accordingly, Argentina's attempt to deny treaty protections to the Claimants' investment in Sierra Chata constitutes an abuse of Argentina's otherwise reasonable right to expect that investors will comply with formalities of host state laws.

b. <u>The Tribunal's analysis</u>

217. Even though the BHP-MEDA transfer was not approved until more than two years after the request for arbitration was filed by the Claimants, Argentina performed

several acts that implied acknowledgement of MEDA's and MASA's concessionaire status.

218. *First*, the fact that the Government has uninterruptedly collected taxes and royalties arising from a certain legal relationship constitutes a clear admission on the part of the Government of that legal relationship with the taxpayer. Accordingly, the fact that MEDA and MASA have paid, export withholdings, income taxes and royalties since 1998 in relation to the Sierra Chata Block, without the Federal Government or the Province of Neuquén ever objecting to their standing to do so, implies an acknowledgment of their status as concessionaires over that block.

219. *Second*, Argentina has given numerous orders to MEDA and MASA in order to implement its natural gas export curtailment measures and the routing of the so-curtailed volumes to the domestic market, the so-called “re-routings”.[78] Such a decision implies an admission by Argentina of the Claimants’ status as concessionaires; otherwise Argentina would have lacked jurisdiction and the orders would not have reflected the actual state of affairs.

220. However, Argentina imparted such orders, thus reinforcing MEDA and MASA’s good faith belief that they would be afforded a treatment consistent with their status as concessionaires.

221. *Third*, through Note 1114/04 sent to MEDA on 21 September 2004, the Secretariat of Energy impliedly considered MEDA as one of the “titleholders” of the Sierra Chata Block concession.[79] In fact, this note was aimed at demanding certain information.

[78] See Natural Gas Re-Routing and Permanent Additional Injection Orders sent to MEDA and MASA by the GOA (Exhibit C-132 and C-133),
[79] See Note 1114/04 of the Energy Secretariat, dated 21 September 2004 (Exhibit C-390).

222. *Fourth*, in the numerous reports submitted to Congress between the years 2004 and 2007, the Cabinet Chief of the Federal Executive repeatedly stated that:

> "MASA and MEDA are natural gas producers. They hold a hydrocarbon exploitation concession in "Sierra Chata", Chihuidos, Province of Neuquén (pursuant to the Hydrocarbons Law and Decrees Nos. 1969/93 and 824/95); and an exploitation contract in the Aguaragüe Area Province of Salta (Decree No. 2446/92)"[80]

223. This goes to confirm that the Argentine Government has recognised the Claimants' ownership of the relevant investments over a decade and has shown, by specific actions, that they effectively held the status of *concessionaires* of the exploration, exploitation and transportation of hydrocarbons in the "Sierra Chata" Block. Moreover, in this case, unlike other acts mentioned above, the admission of the Concessionaires' status was not privy to the State and the Claimants only, but was instead effected in a public act before the Argentine Congress.

224. The question before this Tribunal is first, whether the acts described above constitute a series of prior actions, which pursuant to the principle of good faith together with the doctrine of *venire contra factum proprium non valet*, also recognised by Argentine law, cannot be contradicted by a later act denying MEDA and MASA's status as concessionaires of the "Sierra Chata" Block. If this question is answered in the affirmative Argentina's fifth objection must already on that ground be rejected.

225. The Tribunal agrees with Argentina that investments, as defined in the BIT, must be made and carried out in accordance with the law of the host state. Ordinarily, then, foreign investors must comply with any procedures or formalities prescribed by the

[80] See Report of the Chief of Cabinet to the House of Representatives, Report 62, July 2004 (Exhibit C-387), Report of the Chief of Cabinet to the House of Representatives, Report 64, March 2005 (Exhibit C-394) and Report of the Chief of Cabinet to the House of Representatives, Report 62, July 2004 (Exhibit C-401).

host state's laws for assignments, transfers, acquisitions, and so forth. The principal such formality on which Argentina predicates its jurisdictional objection in this investment arbitration is the internal-law requirement that acquisitions and assignments receive the prior authorization of the Executive Branch authorities, provincial or federal, as the case may be.

226. Because the Claimants allegedly did not comply with this requirement as to the relevant acquisitions and assignments, they cannot, according to Argentina, under the BIT assert rights relative to concessions, contracts, export permits and other investments they made, which form the subject-matter of this arbitration.

227. However, a host state may under international law not invoke its own failure or non-feasance to defeat rights under the BIT, *a fortiori* if it has not acted in good faith. According to the Claimants' allegations, as to which sufficient evidence has been given by them, Argentina's federal and provincial authorities repeatedly and negligently failed to complete, or delayed for years, certain formalities and administrative actions required by Argentina's own law, for example, approval by Executive Branch authorities or instrumentation of public deeds.

228. The Tribunal finds that the principle of good faith and the doctrine of *venire contra factum proprium* prevent Argentina from denying the validity of the Claimants' acquisition or ownership of the above interests and others constituting its investment. Argentina has consistently and repeatedly, for about a decade recognised and acted on the basis of the validity of the Claimants' title. By its own actions and those of its provincial authorities, for which it clearly bears responsibility under international law, it has shown that it regards the Claimants as the rightful holders of title. The conduct of any State organ shall be considered an act of that State under international law, whether the organ exercises legislative, executive, judicial or any other functions, whatever position it holds in the organization of the State, and whatever its character

as an organ of the central Government or of a territorial unit of the State.[81] Argentina cannot now be heard to deny that title.

229. The Tribunal finds that inter-affiliate transfers, such as the MAL-MEDA Transfer and the MEDA-MASA Transfer, do not require authorisation from the Argentine Government, since Article 15 of Decree 1969/93 provides that parties may assign portions of their interest to company affiliates simply by notifying the competent authority, which the parties promptly did upon completing the transfer.[82] Because no formal authorisation of the transfer by the Argentine Government is required, Argentina's allegations that the Executive Branch did not authorise these transfers are not relevant to the lawfulness of the transfers under Argentine law. In addition to showing that assignments between affiliates do not require government approval, Article 15 of Decree 1969/93 establishes that the Energy Secretariat merely takes note of inter-affiliate assignments (rather than formally authorizing them) and that the assignor remains jointly liable with its assignee affiliate for the assigned interest in question. Thus, when making an inter-affiliate assignment, it is not necessary to request approval from the government; but if the parties want to dispense with joint liability, then they need to seek government approval exclusively for that purpose.

230. For the reasons mentioned above the Tribunal finds Argentina's fifth objection unfounded. The objection is accordingly dismissed.

[81] See *Articles on the Responsibility of States for Internationally Wrongful Acts*, Art. 4, *in* Report of the International Law Commission on the Work of its Fifty third Session, U.N. GAOR, 56th Sess, Supp. No. 10, at 43, U.N. Doc. A/56/10 (2001), annexed to G.A. Res. 56/83 (12 December 2001).
[82] Exhibit C-94.

7. Sixth objection to jurisdiction: – Transfer of interest from MEDA to MASA

231. On 21 December 2004, MEDA and MASA entered into a Transfer of Going Concern Agreement (hereinafter **"MEDA-MASA Transfer Agreement"**) by which MEDA agreed to transfer to MASA all of the assets and liabilities of its Argentine Branch, including its interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession in the Chihuidos Block. Pursuant to the MEDA-MASA Transfer Agreement the transfer and reorganization to be carried out thereunder became effective from 31 December 2004.[83]

a. <u>The Parties' Positions</u>

i. The Respondent

232. Argentina contends that like the assignments referred to in their fifth objection; the assignment from MEDA to MASA is subject to the prior authorisation of the Executive Branch. In this regard, in the MEDA-MASA Transfer Agreement MEDA undertook to request authorisation from the Executive Branch to carry out the assignment of the Exploration Permit, the Exploitation Concession and the Transportation Concession. Moreover, such agreement provided that if the Executive Branch refused to grant the requested authorisation, MEDA would resume in its own name the exercise of the rights and obligations derived from its interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession. Furthermore, MEDA's 2005 to 2008 financial statements informed that the assignment was pending approval from the Secretariat of Energy. However, the

[83] The MEDA-MASA Transfer Agreement (Exhibit C-179) says: "The transfer and reorganization to be carried out hereunder shall be effective from 31 December, 2004."

Claimants have not produced the letter-requesting authorisation from the Executive Branch to carry out the aforesaid assignment.

233. If MEDA had acquired prior to the filing of the Request for Arbitration the interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession it alleges as investment and had then validly assigned those interests to MASA, it would not be entitled to pursue any claim as regards those interests for measures adopted after such interests were transferred to MASA. MEDA has not either proven to have validly assigned its alleged interest to MASA.

234. The Claimants state to have excluded the ICSID claim from the transfer. However, even if MEDA were entitled to claim for measures adopted before the transfer of its alleged investment, it would not be entitled to claim for measures adopted after such transfer. Indeed a tribunal has no jurisdiction over a bilateral investment treaty claim for acts or omissions occurring after the transfer of the relevant investment. As stated by MEDA itself, since the transfer to MASA the Argentine Branch "has not performed any operation," "does not have any assets, liabilities or income" and "it is also the intention of the Head Office that the Branch do not operate in the foreseeable future." Therefore, MEDA is not entitled to pursue any claim for measures adopted after the transfer of its alleged investment.

235. MASA is not entitled either to pursue claims in relation to the Exploration Permit, the Exploitation Concession or the Transportation Concession in the Chihuidos Block. In the first place, MASA may not invoke an investment other than the investment alleged when it filed its claim. This means that MASA may not invoke as investment its alleged interests in the Chihuidos Block because when it filed its claim it invoked as investment its interests in the Aguaragüe Block. Secondly, MASA has not proven to have acquired its alleged interests in the above-mentioned permit and concessions. Finally, even if MASA had acquired such interests, this would have occurred after the

filing of the Request for Arbitration, which means that the Tribunal would nonetheless have no jurisdiction over MASA's claims as regards those interests.

236. In return for the transfer of the going concern, MEDA acquired a 54.61% shareholding in MASA. This shareholding does not entitle MEDA to pursue derivative or indirect claims for measures adopted after the transfer in relation to the alleged interests of MASA in the Exploration Permit, the Exploitation Concession and the Transportation Concession in the Chihuidos Block.

237. Firstly, MEDA may not invoke an investment other than the investment alleged when it filed its claim. This means that MEDA may not invoke as investment its shareholding in MASA, because when it filed its claim it invoked as investment its alleged interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession in the Chihuidos Block. Secondly, MEDA may not pursue a claim for rights that its subsidiary has not proven to have acquired. In this regard, MASA has not proven to have acquired its alleged interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession and, even if it had acquired such interests, this would have occurred after the filing of the Request for Arbitration. Finally, MEDA is not entitled to claim for rights, which do not belong to it. That is to say, if the transfer of MEDA's alleged interests in the Exploration Permit, the Exploitation Concession and the Transportation Concession to MASA were valid, after such transfer the invoked rights would belong to MASA and not to MEDA.

238. As regards this last issue, an investment in shares is protected by the Treaty but the shareholder has only a valid claim under the Treaty to the extent that its rights as shareholder are affected by measures of the Government. There is no definition in international law of the rights of a shareholder.

239. Therefore, it is necessary to refer to the rules of municipal law to establish the rights that a shareholder acquires through an investment in shares. In the *Barcelona Traction* case, the International Court of Justice ("**ICJ**") specifically dealt with this issue.[84]

240. A key issue that the ICJ had to consider in that case was how to transplant the legal concept of shareholder in a corporation from domestic law to international law. The answer provided by the Court was that the essential characteristics of that concept must be preserved when it forms part of an international claim. Investment treaty tribunals must provide the exact same answer.

241. The usual reference to *shares* as a form of protected investment in the first article of investment treaties solves the question of whether a shareholder in a local company has standing to file a claim under an investment treaty. This reference to *shares* says nothing with respect to the substantial rights related to the shares in a company. This question may only be solved by the *lex societatis*. Neither investment treaties nor international law regulates the rights of shareholders.

242. In municipal legal systems, "the fiction of corporate personality" is taken rather seriously. Indeed, it is only ignored when it is found to be an instrument of fraud.

243. Every legal system that recognises limited liability company structures necessarily draws a distinction between the company and its shareholders. A shareholder cannot, for instance, seize a physical asset of the company in return for relinquishing its share with an equivalent value. This would amount to misappropriation or theft. Shareholders have no rights *in rem* over the assets of the company. The company holds the assets for its own account and in its own name. A company does not hold

[84] *Barcelona Traction, Light and Power Company, Limited (Belgium v. Spain),* ICJ 3, 37 (5 February 1970) (Exhibit LA AR-62).

assets as an agent or trustee of its shareholders. If a third party seizes an asset of the company, it is not the shareholder who is the victim of theft but the company.

244. As regards the derivative or indirect claim that MEDA seeks to pursue in this arbitration proceeding, it is also worth remembering the conclusive words of the ICSID Tribunal in the *Consorzio Groupement L.E.S.I. – DIPENTA v. Algeria* case

> "Il est évident pour le Tribunal arbitral qu'il ne peut entrer en matière sur une réclamation si celle-ci lui est soumise par un sujet de droit qui n'est pas lié par le contrat sur lequel elle repose. L'affirmation est si essentielle qu'elle n'a pas besoin d'être spécialement documentée. Peu importent les liens économiques qui peuvent exister entre les entreprises; ainsi, la société-mère ne pourrait réclamer des prestations revenant contractuellement à sa société fille, même si celle-ci dépend totalement d'elle, à moins de circonstances très particulières qui ne sont pas alléguées en l'espèce. Ce sont ces parties qui ont choisi de recourir pour des motifs qui leur appartiennent à des structures juridiques différentes; elles ne peuvent ensuite demander à l'autre partie d'en faire purement et simplement abstraction."

245. To conclude, neither MEDA – directly or indirectly – nor MASA - directly are entitled to pursue claims in relation to the Exploration Permit, the Exploitation Concession and the Transportation Concession in the Chihuidos Block for measures adopted after the transfer of the going concern from MEDA to MASA. The Tribunal has no jurisdiction to entertain such claims.

ii. The Claimants

246. The Claimants argue that the MEDA-MASA transfer on 31 December 2004 merely altered the form in which the Claimants held their investment in Argentina through changes in asset ownership and shareholding of two whole-owned subsidiaries of Exxon Mobil Corporation.

247. The Claimants contend that the BIT is particularly clear in providing in Article I (3) that "[a]ny alteration of the form in which assets are invested or reinvested shall not affect their character as investment." Moreover, no issue of jurisdiction under the

ICSID Convention arises from a transfer between original claimants for reasons unconnected with the claim, even if the measures forming the basis of the claim accrue after the transfer. It follows that the alteration of the form of MEDA's investment from a direct ownership of the underlying assets to an indirect ownership through its stake in MASA's capital stock does not affect MEDA's standing to claim for damages to that investment. This also applies to MASA. That MASA, an original claimant in these proceedings, received its interest in Sierra Chata, an investment present since the commencement of these proceedings, through a bulk transfer in the form of universal succession does not preclude MASA from pursuing its claim with respect to the "inherited assets."

248. In short, a company's decision to restructure its assets and shareholding structure does not generally deprive that company or its subsidiaries of their rights under the BIT. Three consequences follow from this conclusion: (A) MEDA may claim for damage caused by Argentina's measures taken toward its investment before the MEDA-MASA Transfer; (B) from December 31, 2004, forward, MASA may claim for damage caused by Argentina's measures toward the portion of the investment it obtained from MEDA in 2004; and (C) MEDA, without duplication, may claim as a shareholder of MASA for damage caused by measures that affected MASA's investments after the MEDA-MASA Transfer.

249. It follows under investment treaty law that investors may retain standing under a bilateral investment treaty when they have transferred sold, or assigned their investment after commencing international proceedings. It is generally recognised that there is jurisdiction under the ICSID Convention if the Claimant was an investor at the time of instituting ICSID proceedings. Any assignments or transfers after that time will not affect the investor's standing to claim under the ICSID Convention.

250. In this case, MEDA directly owned its investment in Sierra Chata as of the date of initiating proceedings, and MEDA continued to directly own that interest until the

MEDA-MASA Transfer in 2004. When making the MEDA-MASA Transfer, MEDA specifically reserved its BIT claims for measures preceding that transfer. The express exclusion of MEDA's BIT claims from the MEDA-MASA Transfer was intended to preserve MEDA's right to pursue the claims up to the date of the Transfer and to demonstrate that the Claimants were not attempting to duplicate their claim for damages. MEDA's direct ownership interest imbues it with standing to claim damage caused to its investment in Sierra Chata prior to 31 December 2004.

251. Argentina's argument that MASA cannot claim for the interest in Sierra Chata that it inherited from MEDA fails to reference any legal authority for support. MASA is MEDA's successor in interest under Argentine law, and as such, may assume MEDA's standing in this arbitration. The BIT expressly applies to claims for acquired investments, and ICSID tribunals have only precluded assignees from claiming when assignments were made to obtain ICSID jurisdiction where there was none, which is not the case here. That the transfer in question was made after the date of registering the original claim has no bearing on this conclusion, since it does not introduce a new investment, a new claim, or a new claimant to this proceeding. Moreover, even if the MEDA-MASA Transfer were not valid – as Argentina alleges—the issues surrounding MASA's standing would be moot since MEDA would still own its direct interest in Sierra Chata and could continue to claim for that interest through the present date.

252. Through the 2004 bulk transfer, MASA became the owner of the Sierra Chata Assets by way of "universal succession." Under Argentine law, a transfer of a going concern involves a "universal succession" as opposed to a simple assignment of assets or transfer *uti singuli*. The existence of "universal succession" is not affected by a partial exclusion from the transfer of certain assets or liabilities.

253. It follows that, in addition to its standing to claim for all damages sustained in relation to its investment in Aguaragüe, MASA may claim for damages to the portion of the

investment received from MEDA accruing after 31 December 2004 (*i.e.*, the effective date of the MEDA-MASA Transfer).

254. While the existence and validity of the MEDA-MASA Transfer is governed by domestic law, its consequences for the current proceeding constitute a matter of international law. Article I (3) of the BIT is explicitly flexible with how investors choose to structure their investments, stating that: "Any alteration of the form in which assets are invested or reinvested shall not affect their character as investment." Likewise, the ICSID Convention contains no provision that would prohibit successors in interest, such as MASA, from continuing a claim in place of their predecessor. ICSID tribunals have consistently held that transfers and assignments of investments from one BIT-protected investor to another, such as that in the MEDA-MASA Transfer, are valid and do not raise issues of jurisdiction.

255. The corporate restructuring in this case did not involve any transfers between third parties, but rather a restructuring of assets solely between two wholly-owned ExxonMobil subsidiaries, MEDA and MASA, both of which have been claimants since the commencement of the arbitration. The Claimants introduced no new parties, investments, or claims to the proceeding as a consequence of the transfer.

256. In this case, MEDA had standing to claim for damage to the Sierra Chata assets, and transferred that interest and standing through a universal succession to an affiliate, MASA, at a time when MASA was already a Claimant in the arbitration. MEDA and MASA are US nationals for the purposes of the BIT, and they made the Transfer as part of a corporate restructuring within a group of affiliated companies, not to create ICSID jurisdiction where none existed. Thus, the Transfer complies with the nationality requirements of the ICSID Convention, and ICSID jurisdiction should be upheld.

257. Argentina's argument that "MASA may not invoke an investment other than the investment alleged when it filed its claim" is, at best, procedural in nature and has no basis in the jurisdictional requirements of either the BIT or the ICSID Convention. Simply because ICSID jurisdiction is established at the date of registering the arbitration does not mandate that a successor in interest to an investment forming part of the original claim may not continue to claim in place of the original claimant, especially when the successor in interest is already a party to the arbitration.

258. Because Argentina's objection is a procedural (rather than jurisdictional) in nature, MASA could always bring the claim in another proceeding if the Tribunal were to not admit it in this proceeding. Such a result would create inefficiencies and risk an adjudicated outcome inconsistent with the Tribunal's decision about the same measures and the same investment in this proceeding. Moreover, a decision to exclude the portion of the claim for damage to the Claimants' interest in Sierra Chata after 31 December 2004 would be inconsistent with the goal of Article 46 of the ICSID Convention and Rule 40 of the ICSID Arbitration Rules to finally resolve the dispute in one proceeding.

259. In summary, MASA is MEDA's successor in interest and may continue in MEDA's place in this proceeding to claim for the investment in Sierra Chata. This conclusion is supported by the fact that the MEDA-MASA Transfer has no bearing on the Claimants' standing under the BIT or the ICSID Convention. The dispute involves the same claimants, the same investments and the same claims; thus, the inter-affiliate restructuring between MEDA and MASA in no way prejudices Argentina. In consideration of these facts and the analysis above, the Claimants ask that the Tribunal reject Argentina's objections on this point and affirm MASA's standing to claim as MEDA's successor in interest.

260. Article I (3) of the BIT provides that "[a]ny alteration of the form in which assets are invested or reinvested shall not affect their character as investment." This provision

reflects the BIT's policy to protect investment while maintaining the investor's autonomy to structure its investment.

261. The restructuring of MEDA and MASA's investments created no jurisdiction here because ICSID jurisdiction over their claims already existed. Until the MEDA-MASA Transfer, MEDA undoubtedly fell within the personal jurisdiction of the BIT and the ICSID Convention as a United States company with an investment in Argentina. That MEDA now holds its investment indirectly does not change this fact. To deprive MEDA of ICSID's jurisdiction because of the restructuring of its interest in Sierra Chata would contradict the clear policy goal in Article I (3) of the BIT to allow investors to restructure their investment through the form they see fit.

262. With respect to MEDA's continued claim for damages to its investment in Sierra Chata as shareholder of MASA, The Claimants note that they do not seek double-recovery. Rather, the Claimants simply wish to affirm MEDA's continued standing to claim despite changing the form through which it holds its investment in Sierra Chata.

263. Argentina's attempt to deny the advantages of the BIT to a US shareholder in a local company is at odds with express provisions of the BIT. The inclusion of shareholders is confirmed by Article I (1) of the BIT, which defines "investment" as "every kind of investment in the territory of one Party owned or controlled directly or indirectly by nationals or companies of the other Party, such as equity, debt, and service and investment contracts; and includes without limitation: a company or shares of stock or other interests in a company or interests in the assets thereof" and "any right conferred by law or contract, and any licenses and permits pursuant to law."

264. Through the BITs' definition of "investments" as including companies and shares of stock, "the participation" in the locally incorporated company becomes the investment. Even if the local company is unable or unwilling to pursue the claim internationally, the foreign shareholder in the local company may pursue the claim in

his own name. The shareholder may then pursue claims for adverse action by the host State against the local company that affects its value and profitability.

265. Thus, contrary to Argentina's assertions, MEDA is not pursuing the rights of MASA. MEDA's claim is brought on its own behalf as a US investor with qualifying investments under the BIT. MEDA's shareholding in MASA and its indirect ownership of investments owned by MASA, including the concessions, contracts, and permits, is a covered investment that provides MEDA with standing under the ICSID Convention and the BIT. Claims by shareholders are well recognised in ICSID case law, Shareholders like MEDA have a direct right of action for such "derivative" claims.

b. <u>The Tribunal's analysis</u>

266. Argentina argues that the Claimants have lost standing to claim for the portion of MEDA's investment that MASA has obtained as MEDA's successor in interest through the MEDA-MASA transfer which became effective on 31 December 2004.

267. Pursuant to Article 25(2) of the ICSID Convention jurisdiction is established on the dates of consent and registration of the dispute. As a result, subsequent events do not affect jurisdiction. Thus a disposal or transfer of assets that form the basis of an investment claim, subsequent to the institution of the proceedings, such as the transfer from MEDA to MASA, does not affect the standing of the original claimant. Thus, MEDA may claim for damages caused by Argentina's measures affecting its investments before the MEDA-MASA transfer became effective on 31 December 2004.

268. The Tribunal agrees with the Claimants that the MEDA-MASA transfer merely altered the form in which the Claimants held their investments in Argentina through changes in asset ownership and shareholding of two wholly-owned subsidiaries of Exxon-Mobil Corporation.

269. Article 1(3) of the BIT provides that "[a]ny alteration of the form in which assets are invested or reinvested shall not affect their character as investment." As the Claimants submit, no issue of jurisdiction under the ICSID Convention arises from a transfer between original claimants for reasons unconnected with the claim, even if the measures forming the basis of the claim accrue after the transfer. It follows that, although MASA, an original claimant in these proceedings, received its interest in Sierra Chata, an investment present since the commencement of these proceedings, through a bulk transfer in the form of universal succession, this does not preclude MASA from pursuing its claim with respect to those assets.

270. MEDA-MASA transfer has no bearing on the Claimants' standing under the BIT or the ICSID Convention, although the transfer was made after the date of registering the Request for Arbitration. The dispute involves the same Claimants, the same investments and the same claims; thus the inter-affiliate restructuring between MEDA and MASA in no way prejudices Argentina.

271. Thus, MASA may from 31 December 2004, which is the date on which the transfer pursuant to the transfer agreement became effective, onwards claim for possible damage or harm suffered after that date because of Argentina's measures affecting the investments it obtained from MEDA.

272. On the other hand, the Tribunal finds that the transfer from MEDA to MASA had the effect that MEDA lost its standing to claim for possible damage or harm affecting the investment it transferred to MASA suffered after the transfer of assets from MEDA to MASA became effective on 31 December 2004. Being a shareholder of MASA does not give MEDA standing to pursue a claim concerning MASA's rights, which do not specifically belong to MASA's shareholders.

273. For the reasons mentioned above, the Tribunal finds Argentina's objection concerning MEDA's standing, in its capacity as shareholder of MASA, to claim for possible

damage or harm suffered after the transfer of assets from MEDA to MASA became effective on 31 December 2004 justified. In all other respects, the Tribunal finds Argentina's sixth objection unfounded. The objection is accordingly accepted as far as it concerns MEDA's standing in its capacity as shareholder of MASA but in all other respects dismissed.

8. Seventh objection to jurisdiction: – Absence of any Evidence that MASA should be treated as a US company

a. <u>The Parties' Positions</u>

i. The Respondent

274. Argentina contends that the Claimants have not proven that MASA should be treated as a US company for the purposes of Article 25(2) (b) of the ICSID Convention and Article VII (8) of the BIT. In the absence of such evidence, says Argentina, the Tribunal has no jurisdiction to entertain MASA's claim. The only evidence produced by the Claimants to try to prove the existence of control was a certificate issued by an employee of Exxon Mobile Corporation, which stated that from 1 December 2001 up to the date of issue of the certificate – 21 January 2009 – MASA had been and continued to be "an indirect wholly-owned subsidiary of Exxon Mobile Corporation." This is not sufficient to prove that Exxon Mobil controlled MASA.

ii. Claimants

275. Claimants contend that since MASA has been incorporated in Argentina at all relevant dates for determining jurisdiction, including on the date that the parties consented to submit this dispute to ICSID arbitration, it is only necessary that: (i) the parties have agreed that MASA should be treated as a national of that other Contracting State for purposes of the ICSID Convention; and (ii) MASA is controlled by shareholders of a Contracting State to the ICSID Convention other than Argentina.

276. Through Article VII (8) of the BIT, Argentina agreed to treat MASA as a US company. Argentina cannot credibly deny that MASA is an investment of Exxon Mobil Corporation, a company incorporated in New Jersey that indirectly holds 100% of MASA's shares, particularly when the Chief of Cabinet himself, in a report to the House of Representatives, expressly recognised that "MASA is a corporation indirectly owned by Exxon Mobil Corporation." The Chief of Cabinet's statement is particularly relevant because he cites information provided by the *Procuración del Tesoro de la Nación*, representing Argentina in this case, as the source of its statement.

277. That Exxon Mobil Corporation has a 100% indirect shareholding interest in MASA fortifies the reasonableness of the parties' agreement to treat MASA as a US company for purposes of the BIT and the ICSID Convention.

b. The Tribunal's analysis

278. Article 25(2)(b) of the ICSID Convention states:

> "National of another Contracting State" means:
>
> (a) any juridical person which had the nationality of a Contracting State other than the State party to the dispute on the date on which the parties consented to submit such dispute to conciliation or arbitration and any juridical person which had the nationality of the Contracting State party to the dispute on that date and which, because of foreign control, the parties have agreed should be treated as a national of another Contracting State for the purpose of this Convention."

279. MASA has been incorporated in Argentina at all relevant dates for determining jurisdiction. Therefore, it is only necessary that: (i) the parties have agreed that MASA should be treated as a national of the other Contracting State for purposes of the ICSID Convention; (ii) MASA is controlled by shareholders of a Contracting State other than Argentina.

280. Article VII (8) of the BIT states:

> "For purposes of an arbitration held under paragraph 3 of this Article, any company legally constituted under the applicable laws and regulations of a Party or a political subdivision thereof but that, immediately before the occurrence of the event or events giving rise to the dispute, was an investment of nationals or companies of the other Party, shall be treated as a national or company of such other Party in accordance with Article 25(2) (b) of the ICSID Convention."

281. Thus, in case MASA is an investment of nationals or companies of the United States of America and is under "foreign control", Argentina has agreed to treat MASA as a US company.

282. The Chief of Cabinet has in a report the House of Representatives expressly recognised that "MASA is a corporation indirectly owned by Exxon Mobil Corporation."[85] Therefore, and in the light of the full corporate charts with references to supporting stock ledger submitted by Claimants,[86] it has been established that Exxon Mobil Corporation, a company incorporated in New Jersey, indirectly holds 100 % of MASA's shares.

283. Having regard to this ownership the Tribunal finds it established that MASA also is under foreign control and that Argentina and the United States have agreed in the BIT that MASA shall be treated as a national of the United States for the purposes of the ICSID Convention. Argentina's objection is accordingly dismissed.

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[85] See Report of the Chief of Cabinet to the House of Representatives, Report 62, July 2004 (Exhibit C-387), Report of the Chief of Cabinet to the House of Representatives, Report 64, March 2005 (Exhibit C-394) and Report of the Chief of Cabinet to the House of Representatives, Report 62, July 2004 (Exhibit C-401).

[86] See Stock Ledgers and other corporate documents (Exhibit C-408).

C. Conclusions

284. The objections to the jurisdiction of the ICSID, the competence of the Arbitral Tribunal and of the admissibility of the claims raised by the Argentine Republic must be rejected. However, MEDA lacks *locus standi* in order to file a claim against the Argentine Republic: a) for damages allegedly attributable to the Respondent stemming from measures applied in the area of Aguaragüe; b) for damages occurring as of 31 December 2004 allegedly attributable to the Respondent, including damages resulting from the application of measures concerning export restrictions, re-routing, Export Withholdings and royalties in the area of Chihuidos all of which were adopted after the 31 December 2004, i.e. the date when the transfer from MEDA to MASA became effective.

285. Thus MEDA is entitled to claim for damage which occurred before 31 December 2004 allegedly attributable to the Respondent stemming from the measures applied in the Chihuidos area. MASA, for its part is entitled to claim for damages allegedly attributable to the Respondent stemming from measures applied in the area of Aguaragüe as well as for damages allegedly attributable to Respondent, which occurred as of 31 December 2004, stemming from the measures applied in the Chihuidos area, including damages resulting from the application of export restrictions, re-routing, Export Withholdings and royalties referred to in the ancillary claims.

VII. APPLICABLE LAW

286. Before proceeding to examine the facts and the parties' allegations, the Tribunal will make the following preliminary observations concerning the law applicable to the merits of the dispute.

287. Article 42 (1) of the ICSID Convention provides:

> "1. The Tribunal shall decide a dispute in accordance with such rules of law as may be agreed by the parties. In the absence of such agreement, the Tribunal shall apply the law of the Contracting State party to the dispute (including its rules on the conflict of laws) and such rules of international law as may be applicable".

A. The Parties' Positions

288. The Claimant argues that Article 42 of the ICSID Convention, in its first sentence, directs the Tribunal to look first to the rules of law agreed by the parties, and in the absence of any such agreement, the Tribunal should look to (1) the law of the Contracting State, and (2) such rules of international law as may be applicable.

289. International law applies in this case because the BIT (which is part of Argentine law) is itself the governing law as the *lex specialis* between the parties, and it expressly requires Argentina to comply with international law. In addition, international law applies under the second sentence of Article 42(1) regardless of the application of Argentine law because that sentence makes international law applicable in every ICSID arbitration in which the parties have not agreed on a choice of law to the contrary. Thus, the decision to apply international law is not optional; the Tribunal has a mandatory duty to apply applicable international law, regardless of the role of domestic law. The Claimant argues that Article 42 of the ICSID Convention, in its first sentence, directs the Tribunal to look first to the rules of law agreed by the parties, and in the absence of any such agreement, the Tribunal should look to (1) the law of the Contracting State, and (2) such rules of international law as may be applicable.

290. In any event, Argentina has incorporated international law into its domestic law and treaties prevail over domestic law. Thus international law applies in this case. The BIT expressly requires Argentina to comply with international law, and the BIT and international law have been incorporated by Argentina in its domestic law.

291. According to the Claimant, the BIT requires "the Argentine Republic to afford U.S. investors like MEDA and MASA treatment no less favourable than that required by international law, both with respect to investment generally and in particular with respect to expropriations or measures tantamount to expropriation of an investment."

292. The Claimant quote, among others, Professor Weil who says:

> "However complex and multifaceted, these attempts [to delineate the respective roles of domestic and international law] are actually futile, for no matter how domestic law and international law are combined, under the second sentence of Article 42(1), international law always gains the upper hand and ultimately prevails. It prevails indirectly through the application of domestic law where the latter is deemed consistent with international law or incorporates it. It prevails directly where domestic law is deemed deficient or contrary to international law. Thus, under the second sentence of Article 42(1), international law has the last word in all circumstances: "international law is fully applicable and to classify its role as 'only' 'supplemental and corrective' seems a distinction without a difference."[87]

293. The Claimants also rely on the statement of the ICSID Tribunal in *Santa Elena*. In that case the Tribunal concluded that Costa Rican law was "generally consistent with the accepted principles of public international law on the same subject." The Tribunal noted, however. that

> "[t]o the extent that there may be any inconsistency between the two bodies of law, the rules of public international law must prevail. Were this not so in relation to takings of property, the protection of international law would be denied to the foreign investor and the purpose of the ICSID Convention would, in this respect, be frustrated."[88]

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[87] *P. Weil, The State of the Foreign Investor and International Law: To No Longer Stormy Relationship of a Ménage Á Trois*, 15(2) ICSID REV – F.I.L.J.J. 401, 409 (2000) [*hereinafter "P. Weil"*] (Exhibit C-325).

[88] Compañía del Desarrollo de Santa Elena, SA v Republic of Costa Rica, ICSID Case No ARB/96/1, Award (17 February 2000) 39 I.L.M. 1317, 1328 (2000) [hereinafter "*Santa Elena Award*"] (Exhibit C-231).

294. Moreover, the Claimants rely, *inter alia*, on the Annulment Committee in *Vivendi II* on the law applicable to the determination of whether a breach of the BIT has occurred. It held

> "[T]he inquiry which the ICSID tribunal is required to undertake is one governed by the ICSID Convention, by the BIT and by applicable international law. Such an inquiry is neither in principle determined, nor precluded, by any issue of municipal law, including any municipal law agreement of the parties."[89]

295. In support of their contention that that international law also applies under the second sentence of Article 42(1) of the ICSID Convention, the Claimants rely here again on the authority of Professor Weil, who with regard to tribunal's choice of law analysis under the second sentence of Article 42(1), holds: "These attempts [to delineate the respective roles of domestic and international law] are actually futile, for no matter how domestic law and international law are combined, under the second sentence of Article 42(1) international law always gains the upper hand and ultimately prevails."[90]

296. The Claimants conclude that although the Tribunal is required to apply both the law of the Contracting State and applicable international law under the second sentence of Article 42(1), international law inevitably prevails when domestic and international law conflict. Any other interpretation would allow governments to enact and interpret laws in order to evade their international obligations, thereby frustrating the purpose of the ICSID Convention and the protections of the BIT.

297. The Respondent draws a different conclusion from the fact that the parties have not agreed on the applicable law. The Respondent submits that the second sentence of

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[89] *Compañía de Aguas del Aconquija SA and Vivendi Universal (formerly Compagnie Générale des Eaux) v Argentine Republic*, ICSID Case No ARB/97/3, Decision on Annulment (3 July 2002) [hereinafter "*Vivendi Decision on Annulment*"] ¶ 102, (Exhibit C-454).
[90] *P. Weil, supra* (n 87) p. 409.

Article 42(1) of the ICSID Convention must be applied. Hence, in accordance with Article 42(1) of the ICSID Convention, the law governing the present dispute consists of the provisions of the applicable BIT and other applicable rules of international law, as well as the Rules of Argentine law.

298. Moreover, the Respondent submits that in the instant dispute, the definition of rights allegedly acquired by the Claimants is defined by Argentine law. The existence of such rights, as well as their scope, manner of acquisition and conditions for their transfer are determined by Argentine law. Neither the BIT nor general international law contains any definition of these concepts. The Respondent quotes Judge Rosalyn Higgins, who states as follows:

> "So far as the concept of property itself is concerned, it is as if we international lawyers say: property has been defined for us by municipal legal systems; and in any event, we "know" property when we see it. But how can we know if an individual has lost property rights unless we really understand what property "is?"[91]

299. Therefore, in order to know whether the Argentine Republic is internationally responsible under the BIT, the Respondent asserts it must be determined, in the first place, which the rights allegedly acquired by Claimants under Argentine law are and how those alleged rights evolved under Argentine law.

300. The Respondent refers to the case *EnCana Corporation v. Ecuador*, in which, the Respondent contends, this has been upheld in the following terms: "[F]or there to have been an expropriation of an investment or return (in a situation involving legal

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[91] Rosalyn Higgins, *The Taking of Property by the State: Recent Developments in International Law*, RECUEIL DES COURS DE L'ACADEMIE DE DROIT INTERNATIONAL 259, 268 (1982-III) (Exhibit LA AR-90).

rights or claims as distinct from the seizure of physical assets) the rights affected must exist under the law which creates them."[92]

301. Moreover, the Respondent refers to Sacerdoti, who states "[f]oreign investments are subject in the first place to general legislation and to any specific applicable law and regulation of the host state."[93]

302. Therefore, the Respondent contends, Argentine law is one of the sources of law that must be applied in order to determine whether the Treaty standards for the protection of investments have been complied within in this particular case.

303. In conclusion, the Respondent asserts that Argentine law determines the existence and scope of the rights allegedly acquired by the Claimants and is part of the applicable law to be used for determining whether the Treaty provisions have been complied with.

304. Finally, Argentina contends that the human rights obligations of the State must be borne in mind in interpreting and delimiting the scope of the applicable BIT provisions, given that the emergency measures challenged by the Claimants must be analyzed in the light of all the relevant rules, including the paramount obligation of the State to guarantee fundamental human rights.

305. In their Reply, the Claimants contend that Argentine law is irrelevant to the issue of Argentina's international responsibility; it is only relevant as a fact to add context to Argentine Government's measures and conduct at issue, which the Tribunal must analyze through the lens of the BIT and international law.

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[92] *EnCana Corporation v Republic of Ecuador* UNCITRAL Arbitration, Award (3 February 2006) [hereinafter "*EnCana Award*"] ¶ 184 (Exhibit LA AR-30).
[93] Giorgio Sacerdoti, *Bilateral Treaties and Multilateral Investments*, 269 RECUEIL DES COURS DE L'ACADEMIE DE DROIT INTERNATIONAL 251, 369 (1997) (LA AR-91).

306. Moreover, the Claimants contend that Argentina's interpretation of *EnCana* is confused and inaccurate. In that case, the claimant argued that Ecuador wrongfully denied rights to refunds owed to EnCana's subsidiaries under *Ecuadorian law*. The Tribunal thus looked at Ecuadorian law to determine the content of the commitment to VAT refunds made by Ecuador. But Ecuadorian law was not employed to determine the standard of international responsibility, as Argentina implies. Nor does the *EnCana* decision imply that the Tribunal would not have looked to sources other than Ecuadorian law for the VAT refund obligation at issue (*e.g.*, assurances from State officials, legal or contractual commitments, the BIT, etc.) had the claimant alleged such additional source.

307. In addition, the Claimants rely on the statements by the Tribunal in the *CME* case and the *Tecmed* case. In the *CME* case the Tribunal stated: "The State may not invoke its own legislation to detract from [its BIT] obligation[s]."[94] In the *Tecmed* case the Tribunal held: "That the actions of the Respondent are legitimate or lawful from the standpoint of the Respondent's domestic laws does not mean that they conform to the Agreement or to international law."[95]

308. In its reply, the Claimants finally contends that in maintaining that its measures were necessary to preserve fundamental human rights in the time of the crisis, Argentina establishes no direct link between the measures at issue and its human rights obligations. In support of that Claimants refer to the *Siemens* case in which the Tribunal remarked:

> "[T]he Tribunal notes the reference made by Argentina to international human rights law ranking at the level of the Constitution after the 1994

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[94] CME Czech Republic BV v Czech Republic [hereinafter "*CME Partial Award*"], UNCITRAL, Partial Award (13 September 2001) ¶¶ 159-60 (Exhibit C-237).
[95] *Técnicas Medioambientales Tecmed SA v United Mexican States*, ICSID Case No ARB (AF) 00/2), Award (29 May 2003) [hereinafter "*Tecmed Award*"], ¶ 120 (citing *ELSI* at 73) (Exhibit C-244).

> constitutional reform and implying that property rights claimed in this arbitration, if upheld, would constitute a breach of international human rights law. This argument has not been developed by Argentina. The Tribunal considers that, without the benefit of further elaboration and substantiation by the parties, it is not an argument that, *prima facie*, bears any relationship to the merits of this case."[96]

309. Furthermore, the Claimants contend that similarly, the tribunals in *Azurix* and *CMS* held that Argentina failed to establish the incompatibility of its human rights and investment treaty obligations within the precise context of those cases.[97]

310. In its Rejoinder, Argentina reaffirms its considerations in the Counter-Memorial that, the parties have not expressly agreed on the applicable law in the BIT and, therefore, Article 42(1) of the ICSID Convention, second sentence, establishes the applicable law, which includes Argentine law, the applicable BIT provisions and other international law, for instance human rights provisions. Thus the Tribunal must apply the BIT, Argentine law and other relevant international laws in a harmonious manner so that there are no contradictions between them since the second sentence of Article 42(1) of the ICSID Convention sets forth the application of all those sources of law, without giving precedence. Argentina quotes, among others, Sacerdoti who explains:

> "[t]his construction of the relationship between domestic law and BIT's obligations indicated that the freedom of the host state to enact or change its law and regulations in the furtherance of general or specific policies (e.g. in the respect of in the environment labour and consumer

[96] *Siemens AG v Argentine Republic*, ICSID Case No ARB/02/8, Award (6 February, 2007) [hereinafter *"Siemens Award"*] ¶ 79 (Exhibit C-266).

[97] See Azurix Corp v Argentine Republic, ICSID Case No ARB/01/12, Award (14 July 2006) [hereinafter *"Azurix Award"*] (failing "to understand the incompatibility in the specifics of the instant case"), C-261; CMS Gas Transmission Co v Argentine Republic, ICSID Case No ARB/01/8, Award (12 May 2005) [hereinafter *"CMS Award"*] ¶ 121 ("there is no question of affecting fundamental human rights when considering the issues disputed by the parties") (Exhibit C-256).

protection, technological research, industrial development) is basically unaffected by BIT's".[98]

311. Moreover, Argentina relies in support of its contention that domestic law is frequently relevant to determine whether there was a breach of the international instrument, *inter alia*, on the fact that the *Ad Hoc Committee* in the Decision on Annulment in the *Vivendi case* held that "at most, it might be relevant—as municipal law will often be relevant—in assessing whether there has been a breach of the treaty."[99]

312. In its Rejoinder, Argentina emphasizes that it requests the Tribunal to take into consideration the international law of human rights when analyzing whether the Argentine Republic breached any provision under the Treaty. For instance, the fact that a measure was adopted to protect certain fundamental human rights Argentina was (and is) subject to by international laws of the highest level becomes relevant to determine if the measure that ruled certain rights of foreign investors was fair and equitable. Argentina holds that there is no conflict whatsoever between the rules on investment and on human rights and reasserts that the measures that the Claimants challenge were legitimately adopted and necessary for the protection of fundamental human rights.

B. The Tribunal's Analysis

313. The Claimants consider that the first sentence of Article 42 (1) of the ICSID Convention applies in this case since the BIT is itself the governing law as the *lex specialis* between the parties, and it expressly requires Argentina to comply with international law.

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[98] Giorgio Sacerdoti, Bilateral Treaties and Multilateral Investments, 269 RECUEIL DES COURS DE L'ACADEMIE DE DROIT INTERNATIONAL 251, ¶ 371 (Exhibit LA AR-382).
[99] *Vivendi Decision on Annulment* (n 89) ¶ 101 (Exhibit LA AR-82).

314. There is no express agreement between the Claimants and Argentina on the applicable law. Neither does the BIT contain any express clause on applicable law. Thus, the Tribunal agrees with Argentina that the second sentence of Article 42 (1) of the ICSID Convention applies in the instant case.

315. The Tribunal notes that the parties agree that the BIT is the point of reference for judging the merits of MEDA's and MASA's claim. The Tribunal further notes that, according to the Argentine Constitution, the Constitution and treaties entered into with other States have primacy over domestic laws.[100]

316. Article 42(1) of the ICSID Convention has been the subject of controversy on the respective roles of municipal law and international law. It is clear from the second sentence of Article 42(1) that both legal orders have a role to play, which role will depend on the nature of the dispute and may vary depending on which element of the dispute is considered.

317. MEDA's and MASA's claim has been advanced under the BIT and, as stated by the Annulment Committee in *Vivendi*[101] and later by the *Azurix* Tribunal[102], the Tribunal's inquiry is governed by the ICSID Convention, by the BIT and by applicable international law. While the Tribunal's inquiry will be guided by this statement, this does not mean that the law of Argentina should be disregarded. On the contrary, the law of Argentina should be helpful in the carrying out of the Tribunal's inquiry into the alleged breaches of the concessions and permits to which Argentina's law applies, but it is only an element of the inquiry because of the treaty nature of the claims under consideration.

[100] Section 31 and Section 75 (22). See Legal Opinion of Dr. Alberto B. Bianchi of 13 February, 2009 [hereinafter "*Bianchi Report*"] 54, 303 and 305 (Exhibit C-3).
[101] *Vivendi Decision on Annulment* (n 89) ¶ 102 (Exhibit C-454).
[102] *Azurix Award, supra* (n 97) ¶ 67 (Exhibit C- 261).

VIII. APPLICABLE REGULATORY FRAMEWORK

318. Argentina deregulated in 1994 natural gas wellhead prices and marketing by producers as from 1 January 1994 by Decree 2731/93. The disagreement between the parties concerns above all the significance of the Hydrocarbons Law (no. 17,319) of 1967.

A. The Parties' Positions

1. The Claimants' position

319. The Claimants assert that "Article 6 of Hydrocarbons Law provides the Government with the power to regulate only the prices of liquid hydrocarbons, not natural gas." They contend that Article 6 of the Hydrocarbons Law has not governed gas exports since the Argentine Government modified the regime governing gas exports through the Gas Law and its implementing regulations, the Chile-Argentina Energy Treaty, the Deregulation Decrees, and other government measures.

320. Even if *quod non* the Hydrocarbons Law did govern the regulation of gas prices, the Deregulation Decrees enjoy legislative status, and Articles 14 and 15 of Decree 1055/89 would prevail over the Hydrocarbons Law on the specific issues of gas prices and gas marketing. The legislative status of the Deregulation Decrees under Argentine law is widely accepted and has been upheld by Supreme Court decisions, however, Argentina fails to identify any ministerial resolutions that have purportedly repealed those decrees:

321. Articles 14 and 15 of Decree 1055/89 provide:

> "**Article 14.** — FREE DISPOSITION OF HYDROCARBONS. Hydrocarbons obtained as a result of the concessions governed by the Argentine Mining Code may be freely disposed of once 180 days have elapsed from the effective date hereof.

> **Article 15.** — The free disposition of hydrocarbons referred to in Sections 5(d), 13 and 14 hereof shall be governed by these rules:
>
> a) Hydrocarbons may be sold without restrictions in the domestic and foreign market pursuant to the legal framework in force.
>
> b) Companies shall have access to treatment, movement, storage and dispatch systems or means at rates consistent with international values.
>
> c) The payment of royalties for freely disposable hydrocarbons must be made by the companies in accordance with the regulations fixed by the SECRETARIAT OF ENERGY."

322. Decree 2446/92 [103] which approved the Aguaragüe Contract, provides in Article 4 that the parties shall own and be free to dispose of the hydrocarbons extracted from the Aguaragüe area (Northwestern Basin), *pro rata* their respective shares in the Agreement as approved in Article 1, in accordance with provisions set forth in Article 6 of Law No. 17,319, Articles 13 and 15 of Decree No. 1055, dated October 10, 1989, Articles 5 and 6 of Decree No. 1589, dated December 27, 1989, and Article 5 of Decree No. 305, dated February 12, 1992.

323. The Sierra Chata Decree 1969/93[104] Article 3, provides that the Permit holder shall own and be entitled to freely dispose of the hydrocarbons produced in the Area of the Exploration Permit, in accordance with Article 6 of Law No. 17,319, Article 15 of Decree No. 1055, dated October 10, 1989, Article 4 of Decree No. 1212, dated November 8, 1989, Articles 5 and 6 of Decree No. 1589, dated December 27, 1989, and Article 5 of Decree No. 2411, dated November 12, 1991, whose terms in force as of the signing date of the Memorandum of Understanding approved in Article 1 hereof shall be incorporated to the Exploration Permit during its effective term.

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[103] Decree 2446/92 (Exhibit C-97).
[104] Decree 1969/93 (Exhibit C-94).

324. Thus, Argentina assumed the commitment to give the Claimants a right to freely dispose of their natural gas production in the domestic and external markets not only through general legislation but through specific promises made in the Sierra Chata Concession and the Aguaragüe Contract.

325. The existence of this right was acknowledged by the current Secretary of Energy Cameron in both internal memoranda[105] and during his testimony at the hearing.[106] As stated by Decree 867/2002, the "essence of the right to freely dispose of production" is the "right of producers to dispose of the product at freely agreed prices." The minimum price guaranteed by Article 6 of Decree 1589/89140 was also specifically incorporated into the Claimants' Hydrocarbon Concessions and Contracts.

2. Argentina's position

326. Argentina contends that among the rules specifically governing the exploration, exploitation and marketing of hydrocarbons in the Argentine Republic, the Hydrocarbons Law is the highest applicable law. Nonetheless, there are certain laws enacted by the Congress which rank *pari passu* in hierarchy with the Hydrocarbons Law and govern specific aspects of hydrocarbons, such as hydrocarbon exports.

327. With regard to natural gas, the Hydrocarbons Law contains the general principles and the legal system applicable to its exploration, exploitation and industrialization, whereas the Gas Law provides for the transportation and marketing thereof.

328. Agreeing domestic prices to cover operation costs and enable the obtention of reasonable revenues is a Policy of State perfectly consistent with the power of the

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[105] Exhibit C-1058 and Exhibit C- 1031.
[106] Hearing Transcript in English, Day 4, pp. 883:13-20.

Executive Branch to regulate domestic prices set forth by the Hydrocarbons Law article 6.

329. Article 6 of the Hydrocarbons law provides:

> "Permit holders and concessionaires shall be the owners of any hydrocarbons extracted by them and, as a result, they may transport, sell and industrialize them, as well as sell their by-products, in accordance with the regulations enacted by the Executive Branch, based on reasonable technical and economic considerations which shall bear in mind the best interest of the domestic market and attempt to promote the exploration and exploitation of hydrocarbons.
>
> During periods in which the national production of liquid hydrocarbons is not enough to meet domestic needs, the use in the country of all available hydrocarbons of national origin shall be mandatory, except in cases where it is not convenient due to sufficient technical reasons. As a result, the new refineries or extensions shall adapt to the rational use of national oils.
>
> If during such a period the Executive Branch sets the prices for selling crude oil in the domestic market, such prices shall be equal to those set for the relevant state-owned company, but not lower than the price levels for imported oils of similar characteristics. Where the prices of imported oils significantly increase due to special circumstances, they shall not be taken into consideration when fixing the sales price in the domestic market and, in that case, they may beset on the basis of the actual exploitation costs of the state-owned company, such amortizations may be technically appropriate, and a reasonable interest rate on the updated and depreciated investments made by such state-owned company. If the executive sets the prices for by-products, they shall be consistent with the oil prices calculated on the basis of the above criteria.
>
> The Executive Branch shall allow the export of hydrocarbons or by-products which are not required for properly satisfying domestic needs, provided that such exports are carried out at reasonable commercial prices. In such case, it may establish the criteria that shall govern transactions in the domestic market, in order to allow all of the country's producers to participate in it in a reasonable and equitable manner.
>
> The natural gas produced may be used, first, to satisfy the needs characteristic of the exploitation of the fields from which it is extracted and of other fields in the area, whether or not they belong to the concessionaire and in pursuance of the provisions of section 31. Any state owned company providing public gas distribution services shall

> be given preference in the acquisition, within acceptable terms, of the amounts remaining after the abovementioned use at agreed-upon prices which may ensure a fair return on the relevant investment, bearing in mind the specific characteristics and conditions of the field.
>
> With the approval of the enforcement authority, the concessionaire may decide on the destination and terms of use of the gas not employed in the manner indicated above.
>
> The sale and distribution of gaseous hydrocarbons shall be subject to the regulations enacted by the Argentine Executive Branch."

330. Argentina contends that the Hydrocarbons Law passed in 1967 remains in full force and effect also after the GOA modified the regime governing gas exports through the Gas Law and its implementing regulations, the Chile-Argentine Treaty, the Deregulation Decrees, and other government measures. It is the highest-ranking statute regulating the hydrocarbons exploration and exploitation in Argentina. The Chihuidos Permit expressly establishes the right to freely dispose of hydrocarbons in accordance with Section 6 of the Hydrocarbons Law, the Deregulation Decrees and the Conversion Decree. It should be noted that Section 6 of the Hydrocarbons Law has a higher rank than the Deregulation Decrees and the Conversion Decree, and grants broad powers to the Argentine Executive Branch to impose restrictions, quotas, domestic prices, etc. The Gas Law only governs procedural aspects of exports and imports of natural gas and, as mentioned by the Secretary of Energy Cameron, "the ruling principles were still those established by Section 6 of Law 17,319, which remained fully effective."[107]

331. Section 1 of the Gas Law sets forth expressly that "[it] shall govern the transportation and distribution of natural gas [only]" whereas "[hydrocarbons] production,

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[107] Daniel Cameron Witness Statement dated 3 September 2010, [hereinafter "*Cameron Winess Statement*"] ¶ 15.

collection, and treatment shall [continue] be[ing] regulated by Argentine Law No. 17,319."

332. Furthermore, when defining the persons actively engaged in the natural gas industry, Section 9 of the Gas Law established expressly that it is only "natural gas transporters, distributors, brokers, storage operators or consumers" who are fully bound by the rights and obligations deriving from natural gas. Instead, hydrocarbons producers (such as MEDA and MASA), who are also considered "persons" engaged in the natural gas industry, carry out a general interest activity and are to abide by the Hydrocarbons Law.

333. In other words, the fact that the scope of Law No. 24,076 is narrowed down to the transportation and distribution of natural gas is unequivocal. Consequently, the activities carried out by MEDA any MASA continue being governed by the Hydrocarbons Law as stated by their respective hydrocarbon concessions.

334. Moreover, it is incorrect to maintain that paragraph 2 of Section 6 of the Hydrocarbons Law does not apply to gaseous hydrocarbons, for said Section applied to both liquid and gaseous hydrocarbons.

335. Proof of the foregoing is that paragraph 1 of Section 6 sets forth:

> "Permit holders and concessionaires shall be the owners of any hydrocarbons extracted by them and, as a result, they may transport, sell and industrialize them, as well as sell their by-products, in accordance with the regulations enacted by the Executive Branch, based on reasonable technical and economic considerations which shall bear in mind the best interest of the domestic market and attempt to promote the exploration and exploitation of hydrocarbons."

B. The Tribunal's Analysis

336. Article 3 of Decree 1969/93[108] and Article 4 of Decree 2446/92[109] make the free disposal of hydrocarbons subject to Article 6 of the Hydrocarbons Law No. 17,319[110]. Pursuant to Article 6 of the Hydrocarbons Law the holders of permits, concessionaires, and other holders of exploitation rights may transport, commercialize and industrialize the hydrocarbons obtained and market its by-products, subject to such regulatory provisions issued by the Executive Power on reasonable technical and economic bases, for the benefit of the domestic market, and stimulating the exploration and exploitation of hydrocarbons. The reference to the Hydrocarbons Law in the Claimants' Hydrocarbon concessions and contracts is due to the fact, that the Hydrocarbons Law governs specifically the rights and obligations related to exploration and production. This does not make the Hydrocarbons Law applicable to gas marketing and gas export.

337. On these grounds, the Tribunal finds that the reference to the Hydrocarbons Law in the Claimants' concessions does not exclude the application of the Gas Law since the mining titles, i.e. permits and concessions are in any case subject to Argentinean law and the Gas Law is part of the laws of Argentina.

338. The question is thus to which extent the Gas Law takes precedence over the Hydrocarbons Law. To reply to this question an analysis has to be made of the scope of application of the Gas Law.

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[108] Decree 1969/93 (Exhibit C-94).
[109] Decree 2446/92 (Exhibit C-97).
[110] Law 17319 (Exhibit C-8).

339. Article 1 (1) of the Gas Law provides:

> "This law governs the transportation and distribution of natural gas which constitute a national public service, the production, gathering and treatment thereof being regulated by law 17,319."[111]

340. Thus, according to this provision, the Gas Law governs the transportation and the distribution of natural gas, while the production, gathering and treatment thereof are regulated by Law 17,319 (the Hydrocarbons Law). However, Article 1 of the Gas law does not say which of those two laws regulates marketing of natural gas.

341. Article 96 of the Gas Law provides:

> "In the event of a conflict with this Law and other Laws, this Law shall prevail"

342. Thus in the event of any conflict between the Gas Law and other laws, the Gas Law prevails. Consequently, the Gas Law prevails in case of conflict with the Hydrocarbons Law.

343. A number of provisions of the Gas Law and its implementing regulations suggest that to the extent to which such provisions apply the Gas Law regulates also the marketing of natural gas.

344. Thus Article 13 of the Gas Law provides that:

> "Without prejudice to the rights of distributors arising from their entitlements, any consumer shall be entitled to purchase natural gas directly from producers or marketers, freely arranging with them the terms and conditions of the transaction."

345. Article 38 (c) of the Gas Law provides for ENARGAS power to interfere with gas prices only to ensure competitive conditions.

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[111] Law 24,076 (Exhibit C-31).

346. Article 83 of the Gas Law provides as follows:

> "A period of one year as from the effective date of this law is hereby set, which may be extended by a decree of the Executive Power for one extra year, during which the diversification of the supply of gas shall be defined as the goal of the energy policy. The National Executive Power may reduce the above period if the goal is achieved before such time.
>
> During such period, the Minister of Economy and Public Works and Services shall fix, for the domestic market, the maximum prices of gas at the point of entrance to the transportation system to be collected by the producers.
>
> At the expiration of such period, the prices of gas at the point of entrance to the transportation system shall be deregulated and transactions for the demand and supply of gas shall be free within the industry's guidelines and pursuant to the Regulatory Framework."

347. Decree 2731/1993, implementing Article 83 of the Gas Law, provides:

> "From January 1, 1994, be the price of natural gas deregulated. All gas supply and demand shall be freely agreed upon form such date, pursuant to this Decree and the supplementary rules issued by the ENERGY SECRETARIAT."

348. The expert Dr. Martelli said at the oral examination before the Tribunal that, "when the Gas Law was finally approved Hydrocarbons Law was limited to the mining aspects in Exploration and Production by means of Exploration permits and exploitation concessions---- Hydrocarbons Law deals with mining aspects of production of gas and petroleum, and the Gas Law deals… two aspects of gas, marketing and gas exports."[112] The same opinion was also expressed by former Secretary of Energy Mr. Bastos.[113] Argentina's expert witnesses did not submit anything that would rebut this evidence.

[112] Hearing Transcript in English, Day 5 pp. 909-910.
[113] Hearing Transcript in English, Day 5 p.1020.

349. On these grounds the Tribunal concludes that the Gas Law, and not the Hydrocarbon Law, also regulates the marketing and the export of natural gas

350. According to the Claimants, the Deregulation Decrees enjoy legislative status and prevail over the Hydrocarbons Law on the specific issues of gas prices and gas marketing, whereas according to Argentina the Hydrocarbons Law passed in 1967 is the highest-ranking statute regulating the hydrocarbons exploration and exploitation in Argentina, and that it therefore remains in full force and effect also after the GOA modified the regime governing gas exports through the Gas Law and its implementing regulations, the Chile-Argentine Treaty, the Deregulation Decrees, and other government measures.

351. The Decree 2446/92, which approved the Aguaragüe Contract, and Decree 1969/93 concerning the Sierra Chata Permit, expressly establish the right to freely dispose of hydrocarbons in accordance with Section 6 of the Hydrocarbons Law and the Deregulation Decrees. Decree 2446/92 refers in addition to the Conversion Decree.

352. According to the Legal Opinion of Dr. Alberto Bianchi dated 13 February 2009. Regulations issued by the Executive Branch are called "decrees"[114] and decrees issued to fill gaps in the general text of a law may be either "delegated" or executive decrees."[115] Those two types of decrees have the same purpose to fill the gaps in the general contents of law. [116] According to the same legal opinion Argentine law acknowledges that the Public Administration is vested with the power to complete the general text of a law, which may be achieved through two types of decrees, although no clear and specific distinction may be drawn between them.[117] Thus, Argentine law

[114] Bianchi Report, *supra* (n 100) ¶ 75.
[115] *Ibid*, ¶ 76.
[116] *Ibid*, ¶ 77.
[117] *Ibid*, ¶ 82.

allows for regulations to complete and become an integral part of laws and, if valid, the deregulated regulation becomes an integral part of the law, thus acquiring the same hierarchy and binding force as law. In other words, it becomes an integral part of the law as if it were law itself.

353. The Tribunal finds that the Executive Branch (the "**Argentine President**") regulated the Hydrocarbons Law and Law 23,696 (the **"State Reform Law"**),[118] which provided for the unbundling and eventual privatisation of public assets, through the Deregulation Decrees. Article 1 of Decree No. 1055/89 expressly states so and specifies the articles of the Laws above that are regulated; Decree No. 1212/89 mentions Law No. 23,696 and Decree No. 1055/89 in its recitals; and Decree No. 1589/89, in turn, refers to the Hydrocarbons Law and the two Decrees above. Decree No. 2411/91 not only refers to Laws Nos. 17,319 and 23,696 in its recitals, but also explains in detail the purpose of regulating and implementing the policies set out in Law No. 23,696.

354. The Hydrocarbons Law provides for a wide range of delegations to the Executive Branch. Article 2 provides that hydrocarbon activities shall be conducted "in accordance with the provisions hereof and such regulations as may be issued by the Executive Branch." Article 3 provides that the Executive Branch shall determine the national hydrocarbon policy. Articles 4 and 6 authorise the Executive Branch to grant permits and concessions and to regulate the activity of permit holders and concessionaires. Article 7 provides that the Executive Branch shall establish the rules applicable to the import of hydrocarbons and by-products, ensuring the attainment of the goal set forth herein. As stated by Dr. Bianchi the Hydrocarbons Law "is based on

[118] Law 23,696 (Exhibit C-10).

the power delegated to the Executive Branch to regulate the application of the law."[119]

355. The privatization of state-owned companies and their business implemented in Argentina during the 1990s was structured on the basis of the State Reform Law. To this end, extensive powers were delegated to the Executive Branch.[120] As to hydrocarbons, the State Reform Law authorised the Executive Branch to convert the state-owned hydrocarbon company Yacimientos Petrolíferos Fiscales ("**Y.P.F.**") and to award its areas in concessions or joint ventures, or execute lease contracts for the exploration and exploitation of certain areas.

356. The Tribunal finds that in exercising its power based on the power delegated to the Executive Branch to regulate the application of the Hydrocarbons Law, the Executive Power regulated the Hydrocarbons Law through the Decrees referred to above within the general framework of the principles of privatisation and deregulation of hydrocarbon activities under the State Reform Law. As stated by Dr. Bianchi, within the context of this policy, and to support and ensure the feasibility of the project, the Executive Branch issued the Deregulation Decrees, which, among other provisions, established the right to freely dispose of hydrocarbons, the right to freely trade hydrocarbons in the domestic and international markets, the prohibition of withholding taxes on present or future exports or discriminatory taxes, and the right to export hydrocarbons freely.[121]

357. Moreover, the Tribunal concludes that the Decrees conform to the legislative policy established in the Hydrocarbons Law and the State Reform Law. As delegated law, the Decrees referred to above are an integral part of the Hydrocarbons Law and the

[119] Bianchi Report, *supra* (n 100) ¶ 106.
[120] See in particular Arts. 8 to 20 of the State Reform Law.
[121] Bianchi Report, *supra* (n 100) ¶ 110.

State Reform Law and have the same legal status as those laws. They thus prevail over the Hydrocarbons Law of 1967 on the specific issues of gas prices and gas marketing. As can be seen from Dr. Bianchi's report, the Supreme Court has held that such regulatory provisions have the same force and effects as laws.[122]

358. Finally, as shown in the Bianchi Report, the Deregulation Decrees constitute delegated legislation contemplated in Temporary Provision Eight of the Argentine Constitution. Those Decrees were subsequently ratified by Laws No. 25,148, 25,645, 25,918, and 26,135. Laws No. 25,148, 25,645, 25,918, and 26,135 also ratified the legislative status of the Deregulation Decrees.[123]

IX. THE MEASURES CHALLENGED BY CLAIMANTS

359. Before the Tribunal considers the meaning of each of the standards allegedly breached by the Argentina, and because this discussion is closely related to the conflicting views of the parties on the facts of the dispute and their implications, the Tribunal will now consider at length the facts and the measures challenged by the Claimants and then each of the standards of treatment of the BIT supposedly breached by the Respondent. The Tribunal will follow the order in which the facts have been presented in the Claimants Memorial on the Merits taking into account the witness statements, the documentation submitted, expert opinions and the written and oral arguments made by the parties.

[122] *Ibid*, ¶¶ 120-121.
[123] Bianchi Report, *supra* (n 100) ¶¶ 122-141.

A. Pesification and other price interference

1. Introduction

a. <u>The Claimants' position</u>

360. The Claimants contend that Argentina interfered heavily with the Claimants' contracts and prices in violation of the Legal Framework and their vested rights, mainly by:

(a) Pesifying domestic gas supply contracts (*i.e.*, the mandatory conversion to Pesos of the dollar denominated gas sales prices at an artificial rate of US$1 to AR$1);

(b) Preventing gas distribution companies and power generators from passing through to their gas distribution tariffs and energy variable production costs any increase in the wellhead price of natural gas purchased from producers;

(c) Freezing the price of natural gas for all categories of users until 2004, and in the case of residential users and small commercial users, until December 2008; and

(d) Preventing gas producers from freely agreeing on the price of natural gas with their customers, as guaranteed by the Gas Law and the Claimants' Hydrocarbon Concessions and Contracts, and imposing low regulated prices.

b. <u>Argentina's position</u>

361. Argentina asserts that the Claimants, allegation that the pesification of contracts provided for by the Emergency Law and Decree No. 214/02 violated their right to freely agree on hydrocarbon prices in accordance with the statutory framework and hydrocarbon concessions and contracts is flawed.

362. The crisis of late 2001 and 2002 was the worst economic, social and institutional crisis that ever hit the country and affected all its inhabitants and sectors.

Consequently, as pointed out by Mr. Cameron, Secretary of Energy, it "also affected the energy activity in general, as well as the hydrocarbon activity in particular."[124] To endeavour to isolate from the crisis, as the Claimants attempt to do, is absurd.

363. Argentina argues that neither MEDA nor MASA have any legal standing to claim as far as gas distribution companies and power generators were prevented from passing through to their gas distribution tariffs and energy variable production costs in the well-head price of natural gas purchased from the producer. Bearing in mind the Argentine crisis of 2001-2002, the measures taken by ENARGAS and the Secretary of Energy in this respect were legitimate, reasonable and in accordance with the regulatory frameworks of natural gas and electricity

364. Moreover, Argentina contends that there have been substantial increases in gas wellhead prices, and as stated by expert Greco "market prices for most part of the domestic demand are currently well above the level prior to 2002 and exceed the maximum projected values for the long-term contracts entered into in the late 1990s."[125]

365. Further, Argentina argues that all the natural gas sales contracts entered into for export purposes were excluded from the *pesification*. Therefore, a substantial portion of the natural gas volume produced by the Claimants was not affected by the crisis at all. On the contrary, the decline in the production costs allowed the Claimants to benefit from the crisis.

366. Argentina contends that the Hydrocarbons Law expressly provides for the possibility that the State may regulate natural gas pricing.[126] Likewise, the Deregulations,

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[124] Cameron Witness Statement, *supra* (n 107) ¶ 45
[125] Report by Esteban Greco, dated 1 December, 2009 [hereinafter *Greco Report*] ¶ 119.
[126] Hydrocarbons law, Sections 3 and 6 (Exhibit AR-1).

invoked by the Claimants, do not provide for any right to set of the price of natural gas at will. On the contrary, the only reference made to natural gas prices sets forth exactly the opposite; gas prices are to be fixed by the Argentine State. Indeed, Presidential Decree No. 1212/89 established that "natural gas prices for users and producers shall be fixed on a monthly basis by the Ministry of Public Works and Services, through the Secretariat of Energy, until the market conditions include multiple suppliers." [127]

367. Moreover, Argentina argues that the Aguaragüe and Sierra Chata concessions specifically refer to the Hydrocarbon Law and to the Deregulation Decrees, which provide for the regulation of natural gas by the State.[128]

368. In sum, Argentina concludes that there is no rule that sets forth a right to set natural gas wellhead prices at will and there is no commitment in this respect in the hydrocarbon exploitation concessions either.

2. *Pesification*

a. The Claimants' position

369. As mentioned above, the Claimants assert that the pesification of domestic gas supply contracts interfered heavily with the Claimants' contracts and prices in violation of the Legal Framework and their vested rights.

370. Under Law 25,561 and Decree 214/02, the GOA unilaterally changed the provisions of private contracts between the Claimants and their domestic customers. These measures unilaterally converted Dollar-denominated obligations and receivables owed

[127] Presidential Decree No. 1212/89 section 10 (Exhibit AR-62).
[128] Presidential Decree No. 2446/92, section 4 (Exhibit AR-72).

to the Claimants under gas supply contracts into Peso-denominated obligations at an artificial exchange rate of US$ 1: AR$ 1.

371. This was done at the same time that the GOA abrogated the Convertibility Law and devalued the Argentine Peso through Law 25,561. By the end of May 2002, the exchange rate had reached US$1:AR$3.60, and currently is approximately US$1:AR$3.50. Thus, the GOA unilaterally changed private contracts so that the Claimants received only about 30% of the express contract price; this conduct flagrantly violated the Claimants' right to freely agree on the prices of hydrocarbons and their byproducts.

b. Argentina's position

372. According to Argentina, the Claimants' allegation that the pesification of contracts provided for by the Emergency Law and Decree No. 214/02 violated their right to freely agree on hydrocarbon prices in accordance with the statutory framework and hydrocarbon concessions and contracts is flawed.

373. On the one hand, the Emergency Law sets forth the abandonment of the fixed exchange rate system which had been established by the Convertibility Law, yet devaluation had already taken place. Indeed, the devaluation was not a measure adopted by the Argentine government but the Government took certain measures to face the devaluation which occurred in the market – which then turned into an exchange rate overshooting. On the other hand, the whole Argentine economy was *pesified* and the parties were forced to restructure their mutual obligations, sharing the effects of the exchange rate modification in an equitable manner.

374. However, it is clear that not only the pesification did not violate any bilateral investment treaty, but did not contradict any statutory framework or hydrocarbon concessions or contracts either. On the contrary, several Argentine courts have

acknowledged the constitutionality of the *pesification* of contracts between private parties and the provision compelling parties to freely adapt agreed upon rules. [129]

375. Furthermore, the reality demonstrates that contracts between private parties, which were governed by Argentine laws and affected by the *pesification*, were voluntarily adapted by the parties or, in the event of disagreement, by Argentine judges, posing no obstacle to the development of business in the country. Like any other contract between private parties, the contracts expressed in US Dollars to which the Claimants' challenges refer were affected by the Emergency Law. This was true not only for such contracts as were executed by the Claimants as debtors but to those executed as creditors as well.

376. However, natural gas purchase and sale agreements for export purposes were not affected by the pesification. Therefore, a substantial portion of the natural gas volume produced by the Claimants was not affected by the Emergency Law.

377. The *pesification* of the whole Argentine economy affected the contracts invoked by the Claimants, as well as any other contract subject to Argentine jurisdiction. This general measure in principle established a 180-day term for the parties to negotiate the restructuring of their reciprocal liabilities, trying to share in a fair way the effects of the modification in the exchange ratio resulting from the *pesification*. [130]Then, relevant to this specific case, Decree 214/2002 established the adaptation of those contracts due to local inflation for the benefit of the creditor, the possibility of the parties' renegotiation of the terms of the contracts if the pesification had given rise to any unfair circumstance, and the right of the parties to resort to court to request an equitable adjustment if renegotiation between the parties were unsuccessful

[129] Report by Augusto César Belluscio; November, 2009 ¶110. See also Report by Ismael Mata of 1 December 2009 [hereianfter "*Mata Report*"] ¶ 228-230.
[130] Emergency Law, Art. 11.2 (Exhibit RA-3).

c. The Tribunal's Analysis

378. Pesification was introduced by Law 25.651 and Decree 214/02 by which the Convertibility Laws was amended and the US Dollar-denominated obligations and receivables under domestic gas supply contracts were as of 6 January 2002 unilaterally converted into Peso denominated obligations at an artificial exchange rate of US $1 = AR $1. Pesification did not affect export contracts, which continued to be denominated in US Dollars.[131]

379. The Claimants do not claim damages for the Government's pesification of the economy as a general measure. What Argentina must defend are its measures that interfered with natural gas prices. The Claimants assert that they had specific commitments from the Government that they would benefit from deregulated prices and that they could freely agree to the terms of their natural gas supply agreements at the prices and currency of their choice. The Claimants contend, that therefore they were in a substantially different situation than the rest of "the whole Argentine economy" and therefore Argentina's observation that the effects of pesification reached the "whole economy" is irrelevant to this case.

380. Argentina contends that there is no specific commitment to MEDA and MASA regarding the "pesification." The purported commitment of deregulated prices is a sectoral matter and has nothing to do with a general, an "across the board" measure, such as pesification. Both are independent from each other. Pesification only deals with the currency denomination of all domestic contractual obligations. All contracts denominated in US dollars or otherwise related to a foreign currency governed by Argentine law were affected by pesification.

381. Article 3 of Decree 1969/93 concerning the Sierra Chata Permit provides:

[131] See Law 25,561 (Exhibit C-41) and Decree 214/02 (Exhibit C-42).

> "The Permit holder shall own and be entitled to freely dispose of the hydrocarbons produced in the Area of the Exploration permit, in accordance with Law 17,319, Article 15 of Decree No.1055 dated October 10, 1989, Article 4 of Decree no.1212, dated November 8,1989, Articles 5 and 6 of Decree No. 1589, dated December 27, 1989, and Article 5 of Decree No. 2411, dated November 12,1991, whose terms are in force as of the signing date of the Memorandum of Understanding approved in Article 1 hereof shall be incorporated to the Exploration Permit during its effective term."

382. Article 5 of Decree 1969/93 provides

> "Every restriction to the free disposition referred to in Article 3 of this Decree shall entitle the Permit holder to receive during the period such a restriction is applied, an amount not lower than set in Article 6 of Decree No. 1589, dated. December 27, 1989."

383. Article 4 of Decree 2446/92, which approved the Aguaragüe Contract provides:

> "Y.P.F. SOCIEDAD ANÓNIMA,TECPEETROL SOCIEDAD AÓNIMA, AMPOLEX ARGENTINA S.A. AND PETROBAS INTERNACIONAL S.A. –BRASPETRO- shall own and be free to dispose of the Hydrocarbons extracted from the Aguaragüe area (Northwestern Basin), *pro rata* their respective shares in the Agreement as approved in Article 1, in accordance with provisions set forth in Article 6 of Law 17,319, Articles 13 and 15 of Decree No. 1055, dated October 10, 1989, Articles 5 and 6 of Decree No. 1589, dated December 27, 1989 and Article 5 of Decree No. 305, dated February 12, 1992".

384. Article 6 of Decree 2446/92 provides:

> "Any restriction to the free availability of hydrocarbons referred to in Article 4 above, shall entitle the parties to the Agreement to receive, over the term of the restriction, an amount, which may not be lower than that specified in Article 6 of Decree 1589, dated December 27, 1989, unless a higher percentage is otherwise provided for by any other rule."

385. The 1989 Deregulation Decrees established that hydrocarbon producers would enjoy the right to freely market their production, both in the domestic market and abroad (Decree 1055/89, Art. 15, Decree 1212/89 Art.9. Decree 1589/89). Moreover, those Deregulation Decrees guaranteed that in the event the rights to freely market gas were

restricted, producers would be entitled to a minimum price linked to international hydrocarbon prices (Decree 1589/89, Art. 6). Thus those rights have by Decree 1969/93 and Decree 2446/92 been incorporated in the Sierra Chata Concession and in the Aguaragüe Agreement.

386. As mentioned above the Claimants' claims are not about pesification *per se* as a general measure, but rather on the compounded impact of interfering with freely negotiated contracts and prices and subsequently taking measures that impeded any price negotiations. Since the pesification interfered with freely agreed contract prices, the Claimants claim to have received only about 30 per cent of the agreed contract price as a result of pesification. Therefore, the Claimants claim damages for the effect of pesification on their private contracts for January-February 2002.

387. The Claimants' right to freely market gas, both in the domestic market and abroad as well as the Claimants right to minimum price in the event of restriction have, as mentioned above, been incorporated in both the Sierra Chata Concession and the Aguaragüe Contract and are consequently also contractual rights. Therefore, the Tribunal finds that pesification was in breach of the Claimants' contractual rights as far as it interfered with the Claimants' freely negotiated contracts for January-February 2002.

3. Interference in Prices paid by Distributors and Power Generators

a. The Claimants' position

388. The Claimants contend that the GOA effectively prevented power generators and gas distributors — the Claimants' primary domestic customers — from passing through any price increase to their own customers. Consequently, the Claimants and other producers were unable to renegotiate price increases with their main customers, with

the result that the price of gas at the wellhead remained frozen for years, because the GOA:

- prevented the **gas distribution companies** from passing through any price increase of gas at the wellhead (even in Peso terms) to their customers, in violation of the terms of the gas distribution licenses; and

- prevented **power generators** from including any price of gas in excess of the Price in Pesos allowed by ENARGAS in their declaration of variable costs for purposes of CAMMESA's determination of the energy spot price.

389. These measures violated the GOA's guarantees under the Legal Framework and the contracts and licenses entered into by the GOA. They also effectively eliminated any chance of renegotiating the Claimants' gas supply contracts, and therefore, constituted an unlawful interference with their freely-agreed terms.

390. Pursuant to Article 8 of Decree 214/02, the GOA instructed courts with jurisdiction over controversies relating to these matters to maintain and preserve existing contracts in Peso terms. In practice, this measure precluded parties from terminating contracts prior to their expiration due to the GOA's alteration of the contract price or contract price-fixing mechanism.

391. The renegotiation of public service contracts between the GOA and gas and power distribution companies, a process provided for in Law 25,561 has been a massive failure. To renegotiate these contracts, the GOA demands that public utility companies waive their rights—as well as those of their foreign shareholders—to initiate or continue international arbitration proceedings against the GOA based on the GOA measures.

392. Although the GOA initially declared that it would conclude these negotiations within 120 days it passed various laws, decrees, and resolutions that have delayed the tariff renegotiations for more than seven years.

393. Argentina's attempts to justify the measures that ENARGAS (the natural gas regulator) took to restrict the pass-through of price increases to natural gas distribution tariffs constitutes another admission that the Government took measures to manipulate gas prices.

394. Argentina alleges that Article 38(c) of the Gas Law and Decree 1411/94 provided ENARGAS with the power to interfere in natural gas prices by regulating gas distribution tariffs. However, the regulations Argentina invokes apply in a completely different context and do not authorize ENARGAS to absolutely prohibit gas distributors from passing through price increases to natural gas distribution tariffs.

395. Decree 1411/94 and the other regulations that Argentina cites were designed to operate in the context of the semi-annual price-adjustment contemplated in the Gas Law and the gas distribution licenses, as well as certain other limited situations. In this context, Decree 1411/94 granted ENARGAS the authority to monitor gas prices in order to ensure that the prices that gas distribution companies reported were negotiated in a competitive environment and on an arm's length basis. In other words, the scope of ENARGAS's authority to regulate gas distribution tariffs was limited to protecting consumers from market collusion and price-fixing.

396. ENARGAS's power to ensure market competition did not encompass the authority to prohibit the pass-through of any increases of gas wellhead prices in order to suppress gas prices at artificially low levels, as ENARGAS did in this case. To the contrary, Article 38(c) of the Gas Law expressly confined ENARGAS's ability to regulate the pass-through of gas prices to cases in which the price agreed between the producer

and the distribution company exceeds the prices agreed by other distribution companies in similar situations.

397. Consistent with the Gas Law's limitation on ENARGAS's ability to regulate gas distribution tariffs, Decree 1411/94 requires that ENARGAS verify whether the prices agreed by distribution companies result from a transparent, open, and competitive process, as well as from the distribution company's reasonable efforts to obtain the best available prices and conditions. If ENARGAS is unable to establish that a price increase reported by a particular distributor fails to meet these requirements, then it may not limit the pass-through of that price increase.

398. The limitations that Argentine regulations placed on ENARGAS's ability to regulate gas distribution tariffs reflect ENARGAS's mission to align the prices reported by a given distributor with market prices and to prevent market collusion and price-fixing. As LECG explains with reference to this process:

> "This is a benchmarking exercise that the ENARGAS ought to implement in each season to verify that distributors are getting the best prices possible in comparison to prices observed in the marketplace. If ENARGAS considered that a distributor was contracting natural gas at prices that were out of line with market prices contracted out by other buyers, then ENARGAS could limit the pass-through to end-user tariffs to benchmark contract prices, as opposed to the distributor's own contract prices."[132]

399. In this manner, ENARGAS's mission to ensure that market prices prevail was completely consistent with the Claimants' right to freely agree on prices with their customers.

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[132] Damage Valuation of MEDA's and MASA's Investments in Argentina Supplemental Report by Manuel A. Abdala and Pabolo T. Spiller of 26 April 2010 [hereinafter "*LECG Updated Report*"] ¶ 21 (Exhibit C-510).

400. It follows from this discussion that ENARGAS's authority to regulate gas distribution tariffs has no relationship whatsoever with the measures that the Argentine Government imposed to regulate gas prices. Argentina's price interference measures went far beyond that scope of authority by:

(i) absolutely prohibiting all natural gas distribution companies from passing through to their tariffs any price increase (even in pesos) agreed with producers, a prohibition that effectively destroyed producers' ability to freely agree (or renegotiate) their agreements as guaranteed by the Legal Framework and their Hydrocarbon Concessions and Contracts;

(ii) freezing and interfering with gas wellhead prices paid by other categories of consumers (e.g., power plants and industrial clients) that were outside the scope of Decree 1411/94 and the other regulations cited by Argentina; and

(iii) establishing price paths for different categories of consumers since 2004.

401. Accordingly, Argentina's reliance on ENARGAS's ability to regulate gas distribution tariffs constitutes little more than a disguised attempt to focus on issues that are irrelevant to the resolution of this investment dispute and confuse the Tribunal.

402. Like ENARGAS, the Secretary of Energy exceeded the scope of its authority by preventing power generators from factoring gas price increases into their calculation of electricity spot prices. Under the Electricity Law 24,065, power generators were to receive a uniform spot price based on the short-term marginal cost of the system. When declaring their production costs in order for the grid administrator to fix electricity spot prices, generators were required to report their variable costs of production in dollars, a calculation that primarily included the cost of natural gas, which is the most common fuel used in Argentina by thermal generators. By not allowing generators to include the actual market cost of gas in their declaration of

costs, the Secretary of Energy created spot prices that no longer reflected the economic cost of the system, an act that exceeded its powers under the regime provided by the Electricity Law 24,065**.**

b. Argentina's position

403. As mentioned above, Argentina contends that neither MEDA nor MASA have any legal standing to claim the pesification of public utility contracts and licences ordered by the Emergency law (a required measure in the context of emergency prevailing in 2002). It is essential that they have no standing to claim over regulatory measures regarding contracts to which they are not parties. If anyone could claim for the indirect effects of a measure, the number of claims would be endless. Therefore, the resulting discussion is *ex abundante cautela*. However, a fundamental aspect at issue is: the Claimants have no legal standing to claim for regulation measures regarding contracts to which they are not parties.

404. They are different companies, regulated by different rules and whose situations at the outset of the worst-ever economic, social and institutional crisis in Argentina were different. Furthermore, the Emergency Law established simultaneously the renegotiation of the contracts for public utilities, *inter alia*, contracts for the transportation and distribution of electric power and the licences of transportation and distribution of natural gas to adapt the public utilities rates to the new context.

405. The agreements were progressive and individual to each company, and did not involve companies in the gas and electricity sectors only, as alleged by the Claimants; it also involved all public services (trains, road accesses, ports, water and sewage services roads and highways, telecommunications, airports etc.) Despite the manifest complexity of the questions, final and temporary agreements were reached with all companies.

406. Evidently, MEDA and MASA are foreign to the process of renegotiating public services contracts and licences between the Argentine Executive Branch (as Grantor) and the different companies and to the resulting agreements merely because, as explained above, they are also foreign to the renegotiated contracts.

407. ENARGAS has always been empowered to intervene in the contracts for natural gas supply between producers (such as MEDA and MASA) and distributors to guarantee users the lowest cost of natural gas as possible. The interpretation of the Claimants and their expert, Mr. Bastos,[133] is not consistent with the rules, regulations and mechanisms used by ENARGAS (as regulatory authority) which show that the Government has always had an active role in the natural gas market in Argentina.

408. Before the crisis, a few measures had been taken that were the expression of the powers of the Executive to intervene in the natural gas market when it considered it necessary.

409. Even before the privatization of Gas del Estado, one of the Deregulation Decrees established the following on the price of natural gas:

> "NATURAL GAS PRICES. After the transition period, natural gas prices for users and producers shall be fixed on a monthly basis by the MINISTRY OF PUBLIC WORKS AND SERVICES, through the SECRETARIAT OF ENERGY, *until the market conditions include multiple suppliers*."[134]

410. In other words, it was established that the Argentine Government was going to regulate the fixation of natural gas prices until market conditions include multiple suppliers.

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[133] Supplementary Expert Report by Carlos M. Bastos of 23 April 2010 [hereinafter "*Bastos Supplementary Report*"] ¶¶ 22, 30-35.
[134] Presidential Decree No. 1212/89 (emphasis added) (Exhibit AR-62).

411. However, experts Sandleris and Schardgrodsky point out: “The lack of competition conditions that are indispensable for a decentralised pricing mechanism to work properly led the gas regulator (ENARGAS) to set a limit to the prices of gas paid by distribution companies systematically.[135]

412. In this regard, Guichón explains that “Since the commencement of the privatization process, there was serious concern about the high concentration of the natural gas supply in the Argentine Republic”.[136] For example, Presidential Decree No. 1020/95 established a promotion regime for gas distributors to manage natural gas purchase efficiently.[137] In a non-competitive market and, accordingly, lacking in multiple suppliers of natural gas, ENARGAS (as regulatory authority) has always intervened in the price of natural gas because it was essential for consumers’ protection in the face of potential abuse by the leading natural gas producers.

413. Therefore, if under normal conditions, there have always been mechanisms to intervene in natural gas prices, it is both logical and reasonable that – amidst a serious economic, social and institutional crisis such as the one prevailing in Argentina as from 2002 – there are reasonable grounds for the Government to intervene further in the natural gas market. In 2010, and after the events in the last two years that followed the international economic crisis, no person can argue against the need for the State to have a more active intervention in the economy in a systemic crisis scenario.

414. Moreover, the measures relating to the price of natural gas taken after the crisis in 2002 are not so different from the measures taken by other countries going through similar situations. As highlighted by the Secretary of Energy, Mr. Cameron:

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[135] Supplementary Report by Guido Sandleris and Ernesto Schargrodsky of 31 August 2010 [hereinafter “*UTDT Second Report”*] ¶ 76.
[136] Supplementary Statement by witness Diego F. Guichón of 24 August 2010 [hereinafter “*Guichón Suplementary Witness Statement”*] ¶ 37.
[137] Presidential Decree No. 1020795 (Exhibit AR-282).

> "The policy Argentina has followed is not far from that adopted by other countries under similar circumstances. Thus, during the dramatic increases that generated the 1973 petrol crisis, the United States of America established that the prices in natural gas would be restructured gradually, in a segmented way, and throughout a long period of years."[138]

415. Indeed, in the 1970's – in the face of serious problems in the natural gas supply – the United States passed the Natural Gas Policy Act ("**NGPA**"), which determined the prices of natural gas and, in turn, fixed caps for the sales of the different categories. That is to say, something very similar to the agreements and understandings with gas producers under the First and Second Natural Gas Agreement.

416. About the experience in the United States, in his expert report, Mr. Greco highlighted that "in order to respond to the gas crisis, the United States introduced measures entailing strong state intervention, with a long-term gradual deregulation schedule, and that this led to a dramatic increase in gas supply."[139]

417. It is not correct, as the Claimants allege, that "the Secretary of Energy exceeded the scope of its authority by preventing power generators from factoring gas price increases into their calculation of electricity spot prices."

418. The system of *governance* of the Argentine electricity market vests the Secretary of Energy with broad powers to introduce amendments to the dispatch rules. In this regard, in the electricity regulatory framework there are remarkable differences between the regulated sectors (transportation and distribution) and the competitive segment of power generation.

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[138] Cameron Witness Statement, *supra* (n 107) ¶ 64.
[139] Second Report by Esteban Greco of 30 August 2010 [hereinafter "*Greco Second Report*"] ¶ 101.

419. The initial functioning rules of the sector were laid down by SE Resolution No. 61/92. There, the Procedures (hereinafter, "**the Procedures**") for Operation, Dispatch and Price Calculation were established.

420. Such set of provisions included the initial rules for the functioning of the wholesale electricity market. By late 2001, when the crisis struck the country, the Procedures had been modified by several resolutions issued by the Secretary of Energy on 131 occasions. That is, the variability of the dispatch rules has been a constant in the functioning of the Argentine electricity market rather than an isolated, crisis-related fact.

421. Although the variability of the dispatch rules has been a constant in the functioning of the Argentine electricity market, some rules did not vary at all. In particular, the substantial aspects of the procedures aimed at determining payments for energy —spot prices— were not significantly changed after the crisis. They kept being based on cost statements from generators —this being subject to a maximum benchmark value— and a price based on the most expensive generator dispatched.

422. Cost statements from generators were always subject to a maximum limit fixed by the Secretary of Energy. Specific mechanisms were established after the crisis to adapt such functioning to the prevailing uncertainty. Such changes included the power of the Secretariat of Energy to audit the costs declared, increase the frequency by which the statement had to be filed (fortnightly instead of semi-annually), break down the components of the variable costs into fuels, maintenance and miscellaneous, and declare the impact of exchange rate on variable costs, etc.

423. The limits to the cost statements have been constant in the functioning of the electricity market in Argentina. In other words, there was no change or amendment to the rules of the game, only adjustments to the benchmark values provided for in the regulations in force.

424. Furthermore, fixing a maximum cap for the spot price relies on the economic justification and is a part of the ordinary functioning of the generation competitive markets. The particular features of such functioning are to be achieved through centralized rules, which do not arise from the free interaction of the actors in the market.

425. In summary, bearing in mind the Argentine crisis of 2001-2002, the measures taken by ENARGAS and the Secretary of Energy were legitimate, reasonable and in accordance with the regulatory frameworks of natural gas and electricity.

426. It is not true that the process of renegotiation of public service contracts between the Argentine Government and the gas and power distribution companies provided for by the Emergency Law was a failure.

427. The GOA reached agreements with all the national public transportation and power distribution services concessionaires. With respect to the natural gas industry, final agreements were reached with most of the licensees. Although no final agreements were reached with the gas distributor Metrogas and with the transportation companies TGN and TGS, provisional memoranda of understanding were subscribed, by means of which attempts were made to adjust gas licenses to the new economic, financial, political and social context.

428. Argentina did not demand public utility companies and their foreign shareholders to waive their rights to initiate or continue international arbitration proceedings to be able to take part in the renegotiation process. The continuity of arbitration proceedings by minority shareholders of a company after such company agreed a renegotiation and accepted the enforceability of actions herein objected proves the falsehood of that assertion.

429. Notwithstanding the foregoing, it is true that, when minority shareholders proceed with their arbitration proceedings while the major shareholder is reaching an

agreement with the government, serious inconveniences and delays in the renegotiation process take place. The Argentine Republic cannot, without any precaution, enter into agreements with public utility concessionaires and licensees that anticipate tariff increases, and then have also to pay compensation to the minority shareholder based on (and assessed) future revenues from the company with whom it renegotiated the contract. Otherwise, we would be faced with the legal contradiction of having to pay compensation with respect to a measure the same company whose rights were regulated had accepted as legitimate. It can be also concluded that Argentina's inhabitants pay twice for the same reason: as taxpayers when the country has to pay the award as users of the service when they have to pay the tariff increase.

430. Moreover, there has even been cases in which major shareholders had the intention to reach an agreement with the Argentine Republic, but had to face serious inconveniences with their minority shareholders.

431. Without prejudice to the foregoing, the Argentine Republic just requires the suspension of actions on the part of the concessionaire and the licensee, and not of their shareholders, to take part in the renegotiation process, and in case a final agreement is reached, if required, the dismissal of any other claim beyond the executed agreement and/or an indemnity commitment by the company favoured by the agreement in connection with their shareholders' claims related to the renegotiated contract.

c. The Tribunal's Analysis

432. The Claimants assert that the measures adopted by Argentina prevented gas distributors and power generators from passing through to their customers any increase to the cost of natural gas and this took away the Claimants' vested rights to negotiate prices freely. According to the Claimants the gas distributors and power generators represented 78% of the Claimants' domestic market. This has not been

disputed by Argentina. Moreover, the Claimants contend that their customers simply refused to agree on any price increase that they were not able to pass through to their own customers. This is also confirmed by the witness statement of Mrs. Valle.[140]

433. Thus, the Tribunal finds that the Claimants' are bringing their own claim and are asserting their own right and not relying on third party rights.

434. According to the legal opinion of Dr. Martelli:

> "The Argentine Government, acting through the Executive and/or the Energy Secretariat, is not legally authorized to interfere with the wellhead prices of natural gas or to prevent the pass through of the wellhead prices to the distribution tariffs, except in specific cases in which the contractually agreed-upon price entails a violation of market transparency and competitiveness. Nor is the Argentine Government legally authorized to prevent the spot price of electricity paid to power generators from being fixed pursuant to the actual cost of gas, which was the main variable production cost for those generators. Moreover, this guarantee for power generators also implied a guarantee to gas producers that they would be paid the actual cost of gas sold to generators."[141]

435. Also former Secretary of Energy Mr. Bastos's says in his Supplementary Report:

> "In this context, the reference by the Argentine Republic and its experts to Article 6 of the Hydrocarbons Law to justify the regulation of natural gas prices is untenable. The purpose of the Government was to provide clear rules for the operation of the sector. Relying upon a previous rule to neutralize the price deregulation that was implemented does not seem to be consistent with that purpose. In any event, the Gas Law — in certain cases, jointly with the Deregulation Decrees — prevails over the Hydrocarbons Law in all matters related to natural gas marketing and exports because the Gas Law provides a subsequent rule that regulates those matters specifically."[142]

[140] Hearing Transcript in English, Day 4 p. 784-785 and 791-792.
[141] Legal Report of Dr. Hugo Martelli of 23 April 2010 [hereinafter "*Martellli Legal Opinion*"] p. 14 and p. 20 (Exhibit C-508). See also Hearing Transcript in English, Day 5 p. 910.
[142] Bastos Supplementary Report, *supra* (n 133) ¶ 24. Hearing Transcript in English, Day 5 p. 1016.

436. The Tribunal finds on the basis of these statements established that ENARGAS powers under Decree 1411/94 are constrained to monitoring the competiveness of natural gas transactions between gas producers and distributors and that ENARGAS is only authorized to intervene when prices passed through to tariffs exceed certain market levels. This is also supported by Article 1 of Decree 1411/94 which refers to these powers of ENARGAS under Article 38 (c) of the Gas Law, confirming the application of the Gas Law regarding natural gas prices and by a Memorandum of the Team of Natural Gas Advisors to the Undersecretary of Fuels of 16 January 2004 indicating that

> "Moreover, gas production is governed by Law No. 17,319 and its regulations both with regard to access to gas and the conditions of its exploitation and sale. Until December 2001, prices charged for the sale of natural gas in the points of entry to the network transportation system were not subject to regulation; only ENARGAS, as part of its functions, reviewed the degree of competitiveness in which the providers of regulated gas network distribution and sale had entered into contracts, in order to deduct, when appropriate, the cost of gas purchased from the final tariffs paid by the users of these services. Those functions were performed by ENARGAS pursuant to the provisions laid down in Chapter 9 of the network gas Distribution Licenses, the model of which was approved under Decree No. 2255/1992."[143]

437. Although Argentina's expert Mr. Greco says that the fact gas prices were not competitive was just one of the reasons because of which ENARGAS could limit the transfer of prices which were negotiated by distributors with gas producers within the context of the biannual review of tariffs, he was when examined at the hearing not able to identify a single example of ENARGAS' intervention other than within its limits to protect competition.[144] He also admitted that he thought he had not in his report even analyzed the price freeze measures since 2002. [145] Thus Mr. Greco's

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[143] SSC Gas Advisors Memo p. 408 (Exhibit C-1030).
[144] Hearing Transcript in English, Day 7 pp. 1622-1624.
[145] Hearing Transcript in English, Day 7 p. 1624.

report and testimony does not rebut the evidence above Thus the Tribunal finds that ENARGAS exceeded the scope of its authority by preventing power distributors from factoring gas price increases into their calculation of electricity spot prices.

438. Under Article 36 of the Electricity Law 24,065 power generators were to receive a uniform spot price based on short-term marginal cost of the system.[146] Under the CAMMESA Proceedings, Annex 13, Items 1 and 2 (2000)[147] generators were, when declaring their production costs in order for the grid administrator to fix electricity prices, required to report their variable costs of production in dollars, a calculation that primarily included the cost of natural gas, which is the most common fuel used in Argentina by thermal generators. On these grounds and taking also into account Mr. Bastos's witness statement,[148] the Tribunal finds that the Secretary of Energy exceeded the scope of its authority by preventing power generators from factoring gas price increases into their calculation of electricity spot prices.

4. *Other Measures Preventing the Claimants from Marketing Their Production at Freely-Agreed Prices*

a. The Claimants' position

439. A *de facto* price freeze on natural gas resulted not only from the mandatory currency conversion of the prices the Claimants' local customers paid to the Claimants, and the price freeze imposed on gas distributors and power generators, but also from the obstacles the GOA imposed to prevent the Claimants and their customers from terminating their contracts, and the protracted renegotiation process between the Claimants' main customers and the GOA.

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[146] Martelli Legal Opinion, *supra* (n 141), ¶¶ 64-65, C-508. See also Bastos Report, *supra* (n 57) ¶¶ 95-100.
[147] Exhibit C-183.
[148] Bastos Report, *supra* (n 57) ¶ 42.

440. Argentina's argument that, through a renegotiation process between producers and direct industrial users, the Claimants were able to freely agree on prices with respect to most of their contracts existing as of 2002, is misleading. As a preliminary matter, providing the Claimants with the mere possibility of renegotiations does not detract from the fact that the Argentine Government unlawfully interfered in their contracts in the first place. That point aside, Argentina's allegation that the renegotiation process was feasible requires the following two assumptions, neither one of which is true: (i) that most of the Claimants' gas sales in 2002 were based on contracts entered into with categories of users other than power generators or gas distribution companies; and (ii) that renegotiations with industrial users would have been possible.

441. First, by February 2002, the Claimants had as many natural gas sales agreements with power generators and gas distributors (three) as they did with other categories of domestic users. In addition, the aggregate volume under the Claimants' gas supply agreements with power generators and gas distributors was more than twice the aggregate volume under the gas supply agreements with other categories of domestic users, and two of the gas supply agreements with consumers other than power generators and gas distributors expired in April and December 2002. Thus power generators and gas distribution companies had become the Claimants' main customers by 2002. By limiting the ability of power generators and gas distributors to passing through any increase in the cost of gas at the wellhead, Argentina rendered null any prospects of renegotiating with those customers.

442. Second, Argentina is incorrect that renegotiation with industrial users, the small remainder of the Claimants' customers by 2002, would have been possible. Under Law 25,561 and Decree 214/02, parties to pesified natural gas sales contracts had no obligation to reach an agreement within the 180-day renegotiation period that those measures created. Rather, their only obligation was to "renegotiate," which in practice consisted of a requirement that producers wait for the expiration of the 180-day

renegotiation period before starting mediation proceedings that constituted a prerequisite for filing legal actions against their customers.

443. Real renegotiations with gas purchasers were not feasible because, along the Argentine Government's so-called "instruction to renegotiate," the Government reduced in Dollar terms the Dollar-denominated sales price in producers' contracts with industrial users by one-third of the original price and barred producers from terminating those contracts. As a result, industrial users had no incentive to renegotiate those contracts, and sellers were left with no leverage.

444. In addition, when asked to renegotiate, industrial customers threatened to switch their purchases from the Claimants to natural gas distribution companies from which they could buy natural gas at pesified and depressed regulated prices, which critically reduced the Claimants' bargaining power to negotiate price increases with those customers.

445. With domestic gas prices frozen at artificially-depressed prices, on 2 April 2004, many gas producers (but not the Claimants), signed an agreement with the GOA (the **"First Gas Agreement"**).

446. Through the First Gas Agreement, the GOA imposed on producers the duty to deliver certain volumes of gas to the different categories of consumers. In doing so, the GOA demanded that producers accept an individual obligation to supply the domestic market, even though no such obligation existed in the Legal Framework.

447. The First Gas Agreement established a "price path" for the upward adjustment of gas prices at the wellhead for large industrial consumers and electricity generators from 1 May 2004 to 31 July 2005. While the price path provided for the gradual normalization of gas prices for large industrial consumers, CNG stations, and power generators, the First Gas Agreement maintained frozen prices for residential

consumers, which represent approximately 22% of the demand. Further, even these "new" prices were regulated prices in violation of the Legal Framework.

448. Since 2004, Argentina has undermined producers' ability to bargain for higher gas prices through the renegotiation of existing contracts or entering into new contracts by implementing a price-path through the First Gas Agreement and numerous other measures. Thus, producers were unable to renegotiate new prices for those segments of demand that continued to be regulated. With respect to industrial users and power generators, the First Gas Agreement also limited producers' bargaining power by operating as a limitative price signal. Even today, Argentina cannot credibly contend that the Claimants have been able to renegotiate their existing agreements or freely agree to the terms of their gas supply agreements. The ability to renegotiate has proved illusory because of the Government's various measures undermining it.

449. In addition, the GOA rendered the price adjustment ineffective to a significant extent by delaying the pass-through of the price increases to the distribution tariffs. Similarly, Resolution SE 925/05 restricted the ability of power generators to consider deregulated gas prices at the wellhead as variable costs of production when determining electricity spot prices. The GOA also failed to honour the other price adjustments established in the First Gas Agreement. For almost seven years after the issuance of Law 25,561 and Decree 214/02, the GOA froze the gas prices and tariffs for residential consumers and small commercial users.

450. Although the Claimants did not sign the First Gas Agreement, they still suffered the consequences of the depressed prices that this arrangement caused. The Claimants did not sign the agreement because it constituted a veiled attempt by the GOA to gas producers to accept the disintegration of the Legal Framework.

451. The GOA's measures described above violated the following legal and contractual rights and guarantees:

- the rights to freely market hydrocarbons at deregulated prices at the wellhead and

- the guarantee that gas distributors would pay market prices for their gas purchases, since they had the right to pass their costs through to their tariffs (calculated in Dollars and adjustable in accordance with the US PPI).

452. The resulting regime is in sharp contrast to the one that MEDA and MASA relied on when investing in Argentina, a regime under which the GOA guaranteed that “the sale of gas between producers, distributors, and large users [would] be freely agreed between them.”

453. Beginning in 2004, the GOA invoked the gas shortages that its own policies had caused as a justification for adopting additional measures targeted at the Claimants' business.

454. On 17 May 2004, the Secretary of Energy began ordering producers – including those that did not sign the First Gas Agreement — to “re-route” and deliver all the volumes arbitrarily allocated in the First Gas Agreement to certain domestic consumers, regardless of whether the producers had contractual relationships with those consumers. The stated reason for this forced re-routing of gas volumes was the delay in the renegotiations the GOA imposed on gas distributors, producers, and industrial customers under the terms of the First Gas Agreement.

455. Because the Claimants did not sign the First Gas Agreement, the GOA had no legal basis to impose its provisions on the Claimants. By applying this measure to the Claimants, the GOA violated the Claimants’ right to freely sell their production and interfered with the Claimants’ contractual obligations to deliver gas to domestic customers that were not benefited by the “rerouting.”

456. In reaction to a gas shortage of its own making, the GOA forced the Claimants to terminate deliveries under their contracts with foreign and domestic customers in favour of deliveries to certain low-paying domestic consumers unilaterally selected by the Government. On 26 May 2004, the Secretary of Energy issued Resolution SE 503/04, which authorized the Undersecretariat of Fuels to "re-route" the Claimants' gas production on a daily basis to gas distribution companies.

457. These re-routing measures resulted in a loss of revenues for the Claimants, since the prices they would have received under their gas sales agreements were much higher than the prices they actually received for their volumes re-routed to third parties such as distribution companies.

458. Soon after issuing Resolution SE 503/04, the Secretary of Energy issued Resolution SE 606/04, which enabled users that had purchased gas from gas distributors (or that had contracted exclusively for transportation and distribution services) to resell all or part of the gas to other users or distributors at freely-negotiated prices. Resolution SE 606/04 resulted in flagrant discrimination against the Claimants because the GOA forced them to accept a substantially lower price for their domestic gas sales, while industrial users were allowed to obtain substantial profits by reselling the gas at higher prices.

459. The Claimants argue that Argentina in an attempt to defend its natural gas pricing policies asserts that there have been substantial increases in gas wellhead prices, but fails to mention that it froze natural gas prices completely for all segments of natural gas demand until the execution of the First Gas Agreement in July 2004. In addition, Argentina acknowledges that it kept gas prices absolutely frozen for residential users and small commercial users until the execution of the Supplementary Gas Agreement in September 2008. Most importantly, Argentina acknowledges that it continues to systematically manipulate gas prices, a practice that violates its commitments to the Claimants and the rules established under the Deregulation Decrees and the Gas Law.

460. Further, Argentina's argument, that its alleged price increases have resulted in gas prices that are currently above the price levels existing prior to its pesification of the Claimants' contracts, is highly misleading because Argentina is comparing 2010 gas prices for some segments of users to those just prior to 2002. In any case, Argentine gas prices remain substantially lower than the prices of alternative fuels in Argentina and the prices of natural gas imported from Bolivia, which have increased at a much quicker (and more natural) pace. Had Argentina not interfered with gas prices in the first place, the Claimants could have expected substantial increases in gas prices that aligned more closely with price increases for those alternative fuel sources, even though the prices for alternatives to Argentine gas would have remained higher. Notably, domestic gas prices in Argentina are the lowest in the region, in spite of the fact that, at the time of the Claimants' investment, the Argentine Government had strived for a uniform regional gas price through deregulation and regional integration.

461. In addition, Mr. Greco, one of Argentina's experts presents the current price levels in a misleading way, because he fails to consider both that Argentina has forcibly reduced the Claimants' exports to a minimum (*i.e.*, they have only marginally collected export prices since 2007) and that the Claimants' gas sales are not limited to industrial customers and power plants, especially given the Government's re-routing measures. In fact, the Claimants sell a substantial portion of their gas to distributors for residential consumption, meaning that the Claimants receive the lowest regulated price for that portion of their sales (approximately US$ 0.60/MMBTU). Thus, the Claimants' weighted average sale price between 2007 and 2009 has been lower than US$ 1.10/MMBTU, which is significantly lower than the prices stated by Argentina's expert.

462. The above analysis demonstrates that Argentina's arguments regarding gas price increases are misleading. When put in their proper context, Argentina's alleged price increases can only be seen as "increases" if measured against the frozen gas prices that Argentina artificially created in 2002; they have been insufficient to mitigate the

Claimants' losses. The analysis below further demonstrates that Argentina's alleged price increases were late, partial and insufficient, or non-existent.

463. The Respondent's expert Greco states that Decree 689/02 provided for the dollarization of export prices "which entailed a growth in excess of 249% in export prices measured in local currency at the exchange rate as of December 2002."This is completely wrong because it implies that Argentina converted prices in one currency (Pesos) to US dollars. But Decree 689/02 did not dollarize export prices; rather it clarified that export contracts were excluded from the effects of pesification. As a consequence, the prices in natural gas export agreements did not increase.

464. Greco derives his conclusion that export prices "grew" from the fact that, after the devaluation of the Argentine currency, gas export prices (which were dollar denominated) represented a larger figure in pesos. The fact, however, is that export prices did not increase (and had no impact on the domestic prices or domestic consumers). Notably, export prices were affected due to Argentina's measures, because they were linked to domestic basin prices that the Government had frozen at pesified levels in 2002. Thus, Greco's argument aims to mislead by manipulating the facts.

465. Through another sleight of hand, Greco alleges that, through the maintenance of gas prices (measured in pesos) that corresponded to gas prices in the winter of 2001, the Government increased the natural gas price component of distribution tariffs in 2002. Greco bases this conclusion on the fact that gas prices are higher in winter periods. Thus, because the country maintained gas prices during the first part of the winter of 2002 (May-June) that corresponded to the prices charged in the winter of 2001, Greco concludes that the price of natural gas included in tariffs increased by 10% compared to the gas prices (in pesos) included in tariffs between October 2001-April 2002.

466. Greco's analysis is flawed for two reasons. First, the regulations regarding the seasonal semi-annual distribution tariff adjustment did not affect the prices that distributors paid to gas producers; those prices had been pesified and remained frozen. Second, contrary to Greco's assertion, the maintenance of the 2001 winter prices for the first part of the winter of 2002 confirms: (i) that gas prices did not increase (even in pesos) since the level of gas prices passed through to the distributors during the winter of 2001 was maintained for the winter of 2002 and (ii) that the Argentine Government froze distribution tariffs and undermined producers' ability to renegotiate their supply agreements with gas distributors.

467. The price increases included in the First Gas Agreement and the Supplementary Gas Agreement were partial, insufficient and late, and sometimes non-existent. In many cases, the Argentine Government either delayed the price increases to which it committed, took action to limit the effect of those commitments, or failed to fulfil those commitments altogether.

468. This occurred under the First Gas Agreement for several reasons. First, that agreement did not provide any compensation for the price freeze that persisted until the signing of the agreement in April 2004. Second, despite its promises in the First Gas Agreement, the Government continued regulating prices for those categories of consumers for which price increases were authorized. Third, the price increases envisioned in that agreement maintained Argentine gas prices at levels significantly below the regional gas prices and were clearly insufficient to avoid the looming energy crisis. Fourth, the Government failed to comply with its commitment that, by December 2006, residential consumers would pay the same level of prices applicable to the other categories of consumers as of July 2005. Fifth, the Government delayed the pass-through to distribution tariffs of the price increases established for industrial consumers, power generators, and CNG stations.

469. The Claimants did not sign the First Gas Agreement for at least two reasons. First, the Argentine Government required producers to waive their right to bring any claims against distribution and power generators in connection with price interference measures (a requirement that in itself constitutes an effective admission of liability for producers' rights to freely-agreed prices). At that time, the Claimants were in no position to give that right up in exchange for some partial and insufficient relief from a party that had shown no respect for its commitments or the gas market's need for clear and consistent regulation. Second, the Claimants did not want to take any action that could be construed as consent to the measures that were in violation of its rights and guarantees under the Legal Framework.

470. When the First Gas Agreement expired in December 2006, the GOA began pressing gas producers like the Claimants to enter into a more drastic version of the agreement (the "**Second Gas Agreement**"). Resolution SE 599/07 approved the terms and conditions of the Second Gas Agreement. The Secretary issued that Resolution as an instrument to "persuade" gas producers to sign the Second Gas Agreement since the treatment granted to signing producers was more favourable than that granted to non-signing producers.

471. With respect to the Supplementary Gas Agreement, Greco fails to consider several drawbacks in that agreement that left much of the damage caused by Argentina's price interference measures without remedy.

472. First, despite this agreement, the Argentine Government continued regulating prices for those categories of consumers for which price increases were authorized (*i.e.*, residential and small commercial users and GNC users). Second, the price increases contained in the agreement did not provide any compensation for the price freeze for residential and small business customers that remained in effect until the agreement was signed in late 2008; nearly seven years after the Government first froze gas prices. Third, producers never collected any portion of the price increases authorized

under this “agreement,” since the Government assigned all amounts collected due to authorized price increases to a fiduciary fund that it created to subsidize the consumption of liquid petroleum gas by low-income households. Thus, despite signing the Supplementary Gas Agreement as a mitigation mechanism, the Claimants never benefitted from the price increases to which the Government committed in that agreement.

473. None of the Government’s so-called gas “agreements” arose from an arm’s length transaction between natural gas producers and their customers. Rather, the Government used its sovereign power to impose the terms of those agreements on producers, a group that was legally entitled to much more than the agreements provided. The Energy Secretariat’s role in the execution of those “agreements” (acting as the sole counterparty) shows that the prices imposed on producers were regulated prices that violated the Claimants’ right to freely-agreed prices, as well as their legitimate expectation that the Government would not unilaterally interfere in the price terms of their private contracts.

474. Argentina also references the creation of the Gas Plus Program, which provides that the prices of natural gas produced in qualifying fields are not subject to the price guidelines of the Second Gas Agreement, and as a result, are likely to increase. This program allows producers to charge higher prices for gas produced under certain conditions, including gas from unexploited areas, blocks with special geological characteristics (*e.g.*, tight gas), and blocks which have been out of production since 2004.

475. Argentina’s invocation of the Gas Plus Program to justify its conduct in this case is misleading and irrelevant. The Argentine Government enacted the Gas Plus Program in 2008, more than six years after pesifying natural gas contracts and freezing the price of natural gas at the wellhead. Moreover, the Government did not extend the program’s application to producers such as the Claimants who did not sign the

coercive Second Gas Agreement until 2010. This means that as of January 2010 the Claimants have the ability to start taking part in the Gas Plus program. In addition, the prices received for sales not made under the program will continue to be regulated prices in violation of the Legal Framework and the Claimants' Hydrocarbon Concessions and Contracts.

476. Although Argentina has taken the position in this arbitration that, the regulated prices it established through its price interference measures are reasonable, it has publicly recognised over the years that the natural gas prices its policies created are insufficient to ensure the sustainability of the gas production sector. For example, as explained by Guichón, one of Argentina's witnesses, Secretary of Energy Cameron recognised in 2003 that the frozen prices the Government created were insufficient to sustain gas production:

> "One of Cameron's ideas, which was shared by the Under Secretary of Fuels, Cristian Folgar, was that once the widespread uncertainty as to the evolution of the exchange rate and domestic prices was eliminated and a relatively stable macroeconomic context was reached, it was necessary to start immediately to study the restructuring of energy sector prices which would cause the sector to become sustainable."[149]

477. Thus, Secretary Cameron recommended that the Government raise natural gas prices to make the energy industry sustainable.

478. As a result of Secretary Cameron's recommendation the GOA requested the preparation of a report on natural gas exploration and production costs. This report clearly explains that, following the pesification of natural gas wellhead prices, the gas sector was unable to carry out exploration activities

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[149] Witness Statement by Diego F. Guichón of 13 November 2009 [hereinafter "*Guichón First Witness Statement*"] ¶ 103.

> "Natural gas production showed a reasonable development. Since the pesification of [natural gas supply] contracts it [the gas production sector] is no longer able to: – Replace reserves (except those linked to the exploration of crude oil). – Develop new reserves."[150]

479. This assessment, made in August 2003, comports with the conclusions of numerous analysts that Argentina's interference in gas prices stifled further investment in exploration and production.

480. In 2004, through the recitals of Decree 181/04, the Argentine Government again acknowledged the insufficiency of pesified and frozen prices to sustain the gas sector and recognized the need to "provide reasonable economic signals to ensure the normal supply of natural gas and promote investments in exploration and production." More recently, in January 2010, the current Secretary of Energy emphasized the need to increase energy prices and stated that a "normal" country needs to pay "the real value" of energy.[151]

481. These statements from Argentine Government officials clearly contradict Argentina's assertions in this case that the Government priced natural gas in a fair and sustainable manner. In addition, the Government's many acknowledgments that its measures kept gas prices artificially low dispels any notion that it has honoured the right of gas producers to freely agree on prices or that the Claimants were to blame for the damages they suffered from price interference measures. To the contrary, these statements show that the Government was very much aware that its price interference measures would have the effect of depriving producers like the Claimants of their right to freely-agreed prices, and that by doing so, those measures would disincentive investment and lead to decreased exploration and production levels throughout the

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[150] L. Grieco, J González Naya, f. Kohldorfer, *Estimación del Costo del Gas en cabecera del Gasoducto Troncal*, August 2003 (Exhibit AR-169).
[151] See Daniel Cameron, "Energía: Gobierno insiste en que debe subir las tarifas", Ámbito Financiero (4 January 2012) (Exhibit C-571).

country." Despite this awareness, the Government maintained its course and now attempts to blame on the Claimants for what it once openly acknowledged as a foreseeable consequence of its price interference measures.

b. Argentina's position

482. Argentina contends that there have been substantial increases in gas wellhead prices, and as stated by expert Greco "market prices for most part of the domestic demand are currently well above the level prior to 2002 and exceed the maximum projected values for the long-term contracts entered into in the late 1990s."[152]

483. All the natural gas sales contracts entered into for export purposes were excluded from the *pesification*. One of the first measures taken by Argentina during the crisis was passing Presidential Decree No. 689/02, whereby contracts for exporting natural gas were excluded from pesification. As a significant part of their hydrocarbons production was earmarked for exporting, MEDA and MASA had an excellent economic performance in 2002. Therefore, Argentina argues, a substantial portion of the natural gas volume produced by the Claimants was not affected by the crisis at all. On the contrary, the decline in the production costs allowed the Claimants to benefit from the crisis.

484. MEDA and MASA attempt to ignore the crisis that hit Argentina in late 2001 and in 2002, its consequences and effects and the gradual and progressive increases of the hydrocarbons producers since 2004.

485. It is important to distinguish between the gas wellhead price received by producers (such as MEDA and MASA) and the final rates paid by the users of natural gas and

[152] Greco Report, *supra* (n 125) ¶ 119.

electricity. The wellhead price received by all producers "recorded significantly higher increases than the transportation and distribution tariffs."[153]

486. It is not true that natural gas producers were subjected to the artificial depression and freeze of prices. On the contrary, natural gas prices at the wellhead are freely agreed between producers and purchasers.

487. Actually, upon the enactment of the Emergency Law, prices of natural gas at the wellhead continued to be freely agreed between the parties and, contrary to the Claimants' assertion, they rose significantly. As explained by expert Greco "the wellhead price charged by the Claimants recorded significantly higher increases than the transportation and distribution tariffs."[154]

488. One of the measures adopted by Argentina during the crisis was the conduct of an assessment of the cost of natural gas exploration and production. Afterwards, and on the basis of this cost assessment, the First Gas Agreement was implemented, which enabled producers to obtain very reasonable rates of return.

489. In connection with natural gas sales contracts between natural gas producers and natural gas distribution companies and power generators, the Executive Branch subscribed the Agreement for the Normalization of Natural Gas Prices, which was signed by most of natural gas producers i.e. the First Gas Agreement.[155]

490. In that sense, experts Sandleris and Schargrodsky state the following: "[T]he "First Gas Agreement" was signed by most gas producers (Repsol YPF, Total Austral, Pluspetrol, Wintershall, Pan American Energy and Petrobras Energía), and guaranteed

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[153] Greco Report, *supra* (n 125) ¶ 100.
[154] *Ibid.*
[155] First Gas Agreement (Exhibit AR-190).

around 78.5 million m3/day (68.1 million m3/day for distributors) to satisfy domestic demand. The agreement remained in effect from April 2004 until December 2006."[156]

491. Apart from guaranteeing certain volumes of natural gas, the First Gas Agreement established significant increases in natural gas wellhead prices for around 80% of demand. As pointed out by the Secretary of Energy, Mr. Cameron, "It provided for a gradual increase in prices, until reaching the value estimated as a reasonable compensation for gas producers in the drafting of Presidential Decrees No. 180 and181/2004."[157] However, MEDA and MASA could not benefit from such Agreement because they refused to sign it.

492. This Agreement implied a process of recomposition of prices of gas at the wellhead. Thus, there were price increases of about 120 per cent for industrial users.[158] In spite of that, MEDA and MASA did not sign the agreement.

493. The Claimants argue that by means of the First Gas Agreement, the Argentine Republic "demanded that producers accept an *individual* obligation to supply the domestic market, even though no such obligation existed in the Legal Framework." That is not true for two reasons. First, because it was an agreement freely subscribed by most gas producers, who committed to supply certain volumes of gas to the domestic market, but in a merely *jointly* way, and second, because the main goal of the regulation set forth in the legal framework was the supply of the domestic market.

494. On the one hand, the Claimants admit that under the First Gas Agreement, prices of natural gas at the wellhead increased gradually for around 80% of natural gas

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[156] *Analysis of the Valuation of the Damages to Claimants' Investments by Guido Sandleris and Ernesto Scadgrodsky* of 3 Decemeber 2009 [hereinafter "*UTDT Report*"] ¶ 100.
[157] Cameron Witness Statement, *supra* (n 107) ¶ 56.
[158] UTDT Report, *supra* (n 156) ¶ 103.

demand. On the other hand, they argue that these "new prices were regulated prices in violation of the Legal Framework."

495. However, agreeing domestic prices to cover operation costs and enable the obtention of reasonable revenues is a Policy of State perfectly consistent with the power of the Executive Branch to regulate domestic prices set forth by the Hydrocarbons Law.

496. In August 2007, a Second Gas Agreement was executed,[159] subscribed again by most gas producers, including, but not limited to, YPF, Total Austral, Pluspetrol, Wintershall, Pan American Energy and Petrobras Energía. As explained by expert Greco, the Second Gas Agreement "extende[d] the supply commitments to the domestic market until 2011 and establishe[d] price increase guidelines."[160]In spite of that, the Claimants did not sign the Second Gas Agreement either.

497. Regarding the prices of gas for residential consumers, in November 2008 a Supplementary Agreement was executed with gas producers, whereby gradual increases in prices of natural gas for higher-consumption residential users, commercial users, CNG and thermal generators were established.[161] MASA adhered to that agreement. MASA admits that it received a price increase at the wellhead for residential users.

498. Furthermore, given the substantial decline in the amount of natural gas reserves, the Secretary of Energy created also in 2008 a program called "Gas Plus"[162], to foster exploration and production of new gas fields, which will not be subject to the prices guidelines under the Second Gas Agreement, estimating significant increases in the

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[159] Resolution SE 599/07 (Exhibit AR-232).
[160] Greco Report, *supra* (n 125) ¶ 118.
[161] Resolution SE 1070/08 (Exhibit AR-240).
[162] Resolution SE 24/08 (Exhibit AR-221).

prices of natural gas of such fields. The "Gas Plus" program was implemented through Resolution SE 24/08.[163]

499. Through this program, a mechanism was created for encouraging investments required for increasing gas production in Argentina. In this regard, companies making new discoveries or having areas under exploitation with particular geological characteristics (Tight Gas), or having areas that have not been producing since 2004 or areas that are producing and to which new fields are added, are not subject to the price conditions reached by the 2007-2011 Agreement with Natural Gas Producers and are thus able to sell gas at unregulated prices. This category includes, for example, the companies Arpetrol Argentina S.A., Petróleos Sudamericanos S.A., Necon S.A. YPF S.A., Apache Energía Argentina S.R.L.; Tecpetrol S.A. – a partner of the Claimants in the Aguaragüe area – ; Gran Tierra Energy Argentina S.A. and Occidental Argentina Exploration and Production, Inc. Sucursal Argentina, among others.

500. In short, there have been substantial increases in gas wellhead prices, and as stated by expert Greco "market prices for most part of the domestic demand are currently well above the level prior to 2002 and exceed the maximum projected values for the long-term contracts entered into in the late 1990s."[164]

501. The Claimants disregard the results of the First Gas Agreement, which entailed a path of restructuring of gas wellhead prices and gave rise to increases in the order of 20% for industrial users.

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[163] Exhibit AR-221.
[164] Greco Report, *supra* (n 125) ¶ 119.

502. In spite of being an extremely complex process, the Argentine Government reached agreements with all the national public transportation and power distribution services concessionaires.

503. With respect to the natural gas industry, final agreements were reached with most of the licencees. In that connection, Gas Natural Ban, Gasnor, Litoral Gas, Distribuidora Gas del Centro, Distribuidora de Gas Cuyana, Gas Nea, Camuzzi Gas Pampeana, and Camuzzi Gas del Sur executed the memoranda of understanding with the GOA. Although no final agreements were reached with the gas distributor Metrogas and with the transportation companies TGN and TGS, provisional memoranda of understanding were subscribed, by means of which attempts were made to adjust gas licenses to the new economic, financial, political and social context.

504. Through Resolution No. 752/05[165], the Secretariat of Energy established that large users were required to acquire natural gas directly from hydrocarbon producers (and not through distributors) and, therefore, prices were freely agreed upon and gradually began to converge with export prices. That is to say, substantial increases for these new direct users of producers began to occur.

505. As a result of the signature of the agreements and the programmes implemented in the Secretariat of Energy, gas at the wellhead presents prices higher than pre-crisis levels and in some cases even surpass the projections of long-term contracts signed in the 90's.[166] Even with the State's regulation of natural gas prices, experts Sandleris and Schargrosky point out that the prices received by the Claimants do not differ substantially from their projections and further explain that

[165] Exhibit AR-205.
[166] Greco Report, *supra* (n 125) ¶ 118.

> "According to the data provided by the Claimants, the mean price charged between 2002 and 2009 was USD 1.08 per million BTU, which is not very different from the price projected in their original investment plan. Moreover, the sharp devaluation of the local currency must have reduced their production costs in US dollars."[167]

506. In conclusion, in view of the circumstances experienced in Argentina due to the 2002 crisis, the measures adopted by Argentina aimed at restoring the natural gas price in a gradual and progressive manner are lawful and reasonable.

c. The Tribunal's analysis

507. It is uncontested that prices for all users remained frozen until 2004 and for residential and small commercial users until December 2008. Industrial users had no incentive to renegotiate because the GOA had reduced to 1/3 the original price in USD and barred producers from terminating these contracts. Moreover, it is uncontested that the prices received by the Claimants following the First and Second Gas Agreements, which the Claimants did not sign, were regulated, a process to which the Claimants had not agreed. At the hearing the Secretary of Energy Mr. Daniel Cameron said that those agreements included 92 % of the production and signing producers represented 24% of the producers operating in Argentina.[168] The Claimants' witness Ms. Norma Valle said at the hearing that the Claimants were the first to suffer the re-routing of their export volumes to the domestic market, and their natural gas was redirected to users who paid the lowest prices in the market.[169]

508. The rerouting measures issued by the Secretary of Energy of 21 May 2004[170] in reaction to a gas shortage resulted in a loss of revenue for Claimants equal to the

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[167] UTDT Second Report, *supra* (n 135) ¶ 146.
[168] Hearing Transcript in English, Day 4 p. 888.
[169] Hearing Transcript in English, Day 4, p. 736.
[170] Resolution SE 503/04 (Exhibit C-57).

difference between the price they would have received under their gas sale agreements and the much lower prices received for volumes routed to third parties. Since Claimants refused to sign the First and Second Gas Agreements their gas production was re-directed to buyers, which paid the lowest price on the market. This notwithstanding the fact that Claimants were entitled to refuse to sign both the First and the Second Gas Agreement. The difference in price was never recovered by Claimants and is claimed in this arbitration.

509. Based on the above the Tribunal finds that prices for all users remained frozen until 2004, and for residential and small commercial users until December 2008 and that gas producers were prevented from freely agreeing on the price of natural gas with their customers, as guaranteed by the Gas Law and the Claimants' Hydrocarbon Concession and Contracts and that low regulated prices were imposed by Argentina. Moreover the Tribunal concludes that it has not been shown that there was any price recovery for the Claimants.

B. Gas Export Prices

1. The Claimants' position

510. Argentina's depression of gas wellhead prices also affected gas producers' export revenues, since the price formulas contained in the export contracts were in many cases linked to reference domestic prices. The rationale of this linkage was to avoid any discrimination between domestic and foreign customers in the context of the regional energy integration that the Government promoted. This was the case of the Claimants' export contracts with Metrogas and Gener, under which the applicable sales price would be determined in accordance with the domestic basin prices calculated and published from time to time by the ENARGAS.

511. The price-adjustment formulas in those export contracts link the determination of the minimum and maximum prices to the basin price in the Neuquina Basin published

periodically by ENARGAS. Prior to the Argentine Government's price interference measures, the gas industry considered Argentine basin prices to constitute an adequate reference price for gas, since it reflected the average price of long-term gas sales agreements in the basin in question. Since no international gas price index existed and the Southern Cone was increasingly regionalizing, it was a well-known industry practice to use basin prices as a reasonable reflection of regional prices and thus a reference price for gas export contracts. As the Argentine Government recognised when it exempted export contracts from pesification:

> "II]t is necessary to consider the features of the natural gas regional market, in which, under other economic circumstances, it was usual practice to include in the export contracts the prices of natural gas in the different basins of the Argentine Republic as a reference to establish the price of the exported natural gas and/or the range within which such prices may vary."[171]

512. Thus, the GOA's policy of freezing and depressing gas prices directly impacted the prices that some of the Claimants' foreign customers paid, with the result of reducing the Claimants' export revenues significantly.

513. By publishing basin prices on a regular basis, the Government implicitly encouraged this practice. The Government also explicitly promoted the practice of linking gas prices in international contracts to Argentine basin prices as part of its movement toward regional integration of the gas industry.

514. Like many gas producers in the 1990s, the Claimants incorporated basin prices into context of regional integration, but also in reliance on their legitimate expectations about the stability of the Legal Framework and the specific guarantees of freely-agreed prices contained in that framework and the Sierra Chata Concession. As long as the Argentine Government kept its commitment to allow producers to freely agree

[171] Decree 689/02 (Exhibit AR-142).

on gas prices, the Claimants and the industry in general understood that the basin price published by ENARGAS would adequately reflect regional gas prices and thus provide a reasonable benchmark for its gas export contracts. Indeed, that so many industry companies used basin prices as references in their international contracts underscores the depth of Argentina's commitment to freely-agreed prices for gas.

515. When Argentina dismantled the Legal Framework and destroyed the market pricing system that formed the basis of both basin prices and the specific guarantees granted to the Claimants, it severely undermined the price foundation of the Claimants' export contracts with Metrogas and Gener. The Government discontinued publishing basin prices altogether in 2002. As a result, no reference price existed to factor into the price-adjustment formulas of the Claimants' export contracts with Metrogas and Gener.

516. To respond to this situation, the Claimants sought to rely on a clause in an addendum to their contracts that provided that the parties would "use their reasonable commercial efforts" to resolve any distortions in the Neuquina basin price.[172] The Claimants entered into renegotiations with their customers under a cloud of uncertainty. Through Article 9 of Resolution SE 299/98, the Government had provided that exporters needed a new export permit in order to change the gas prices in their export contracts.[173] Given the Government's increasing propensity toward abrogating its commitments to the Claimants, they could not risk losing their export permit and thus had to renegotiate transitory prices with their export customers, which the Claimants were finally able to achieve in late 2003. But once the Government initiated export curtailments in 2004, the Claimants' customers no longer considered

[172] Clause 2 of Addendum No 2 to the Agreements entered into by and between certain gas producers, including the Claimants as sellers and Metrogas and Chilenger (now AES Gener) as purchasers (Exhibit C-100).
[173] Resolution SE 299/98 (Exhibit C-36).

the Claimants reliable suppliers, thus severely undermining the Claimants' ability to negotiate transitory prices that were at or near the prices the Claimants would have received but for Argentina's measures.

517. Despite this unfortunate sequence of events, Argentina now alleges that the Claimants' losses from the Government's interference in prices are due to the Claimants' imprudent business decisions. Here, Argentina misapprehends the concept of business risk as opposed to sovereign risk. In setting Argentine basin prices as the reference price for their export contracts, the Claimants took on the business risk of natural fluctuations in those prices, as the gas market (like any market) fluctuates periodically. However, the Claimants did not take on the risk that the Argentine Government would unilaterally abrogate those commitments and then force the Claimants to submit their export permits to government review simply to have the ability to exercise a price equilibrium clause in their private contracts. That risk was a regulatory and sovereign risk, and it was accounted for in the Argentine Government's commitments under the Sierra Chata Concession, the Legal Framework, and the BIT.

2. Argentina's position

518. The pesification of the whole Argentine economy had not affected the exports of hydrocarbons, and, in particular, natural gas purchase and transportation agreements. Among them, the contracts with the Claimants.

519. As pointed out by the Secretary of Energy, Mr. Cameron:

> "One of the measures to be highlighted from year 2002, promoted by my predecessors, was the issue of Presidential Decree No. 689/2002, which established that natural gas contracts and transport services agreements related to them were not to be affected by the pesification.

> Due to this measure, exporters of natural gas enjoyed an exceptional year in 2002, very different from the one experienced by natural gas producers wholly devoted to the domestic market and the rest of the population."[174]

520. The Claimants fall within the natural gas producers who most benefited from Presidential Decree No. 1689/02 as most of its natural gas purchase agreements were intended for export to Chile.

521. As to the Claimants contention that the "alleged" decline in gas wellhead prices also impacted on export revenues, since the price formulas contained in the export contracts were linked to reference domestic prices, Argentina argues that the Claimants themselves were the ones who agreed privately on prices in the contracts they freely subscribed. An attempt to hold Argentina liable for business decisions taken by the Claimants themselves is inadmissible.

522. The Claimants allege that "the price-adjustment formulas in [their] export contracts with Metrogas and Gener link the determination of the minimum and maximum prices to the basin price in the Neuquina Basin published periodically by ENARGAS" and that the alleged "destruction" of domestic market prices "severely undermined the price foundation of Claimants' export contracts."

523. Furthermore, Norma Valle, witness for the Claimants, points out that "relying on the basin price to calculate the price in export contracts was a common practice before the measures" and that "the Government supported that practice as a means to align domestic and export prices." [175]These claims are incorrect for various reasons.

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[174] Cameron Witness Statement, *supra* (n 107) ¶ 53.

[175] Supplementary Witness Statement by Norma Valle [hereinafter *"Valle Second Witness Statement"*] ¶ 20 (Exhibit C-512).

524. To begin with, Presidential Decree No. 689/02 detached natural gas export agreement prices from the domestic prices of each basin so that the pesification provided for in the Emergency Law and Presidential Decree No. 214/02 did not affect the exports of local producers like MEDA and MASA.

525. Indeed, Section 4 provided that "the price under natural gas purchase agreements for export, agreed upon in US dollars, shall be invoiced and must be paid in such currency and shall be adjusted in the manner provided for in the respective agreements."[176]

526. In other words, through Presidential Decree No. 689/02, MEDA and MASA were able to renegotiate natural gas prices under their export agreements with AES Gener and Metrogas in more advantageous conditions, which would not have occurred if the Decree had not been issued.

527. In all long-term hydrocarbon agreements, it is usually set forth that price indicators may vary or disappear over time. As explained by Guichón, in those cases "mechanisms for reopening negotiations in case such source ceases to exist in the future or needs to be replaced with another one are provided."[177]

528. Indeed, the Claimants provided in their export agreements with Metrogas and AES Gener for the possibility of adjusting natural gas prices. In this regard, Guichón pointed out

> "As shown by the authorization file entitled Sierra Chata, EXPMEYOSP No. 750-003106/94, renamed as CUPAD S01:0331204/2004, price renegotiation mechanisms were established on page 108 (including the involvement of an expert), in the letter of 15 June 1994 (pages 182 to 194 —in particular, Section 3 of page 183 and page 184) and also in the letter from Petrolera Santa Fe which includes

[176] Presidential Decree No. 689/02 (Exhibit AR-142).
[177] Guichón Second Witness Statement, *supra* (n 149) ¶ 47.

> the letter of intent for the sale of Chilgener S.A., Metrogas S.A. and the Sierra Chata producers (Section 4 "price" on page 204). In fact, the renegotiations of prices deriving from these records do nothing but demonstrate the flexibility offered by the agreement."[178]

529. Further, there were no "specific guarantees" with the Claimants that basin prices would be used as price indicators in their export agreements.

530. Quite on the contrary, it was MEDA and MASA who voluntarily decided to assume the risk of a drop in domestic prices by structuring their export agreements with prices tied to domestic basin prices. That is, it was a risk that they could well not have assumed

531. Although the Claimants recognise that they "took on the business risk" of fluctuations in natural gas prices in the domestic market, they assert that they did not take on the "regulatory and sovereign risk".

532. However, as explained by Guichón, "the Argentine Government was under no obligation to create a long-term basin price indicator. In addition, an export agreement which would remain in force for about 15 years could not be exclusively based on an indicator which was incidentally implemented in late 1995, to be updated for 15 years…."[179]

533. Finally, and concerning the preceding paragraph, the Claimant's claim again presents a serious problem of admissibility and legal standing. The Claimants complain that the measures adopted by the State affected the evolution of a price that they had decided to use as a benchmark in their agreements entered into with other private parties. It is as if someone included in an agreement an adjustment mechanism that follows the evolution of prices of certain real property and then sued the State because

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[178] *Ibid*, ¶ 54.
[179] Guichón Second Witness Statement, *supra* (n 149) ¶ 51.

it establishes certain zoning restrictions preventing those prices from evolving in the manner expected by the parties under such private agreement. The owners of the real property would have standing to sue on the basis of the effects of such zoning restrictions, but someone who decides under an agreement to take such prices as a benchmark clearly does not have such standing to sue, regardless of whether using such benchmark constitutes usual "practice" or not in the market. Like in other claims raised by the Claimants, the admission of this claim would lead to absurd results, enabling the multiplication of claims by parties that would be indirectly affected by governmental measures as a result of provisions that they freely decided to include in their agreements with other private parties.

534. In conclusion, it is inadmissible to render Argentina liable for the business decision made by MEDA and MASA.

3. The Tribunal's Analysis

535. Argentina does not deny the Claimants' contention that Argentina's price interference measures caused damage to the Claimants' export business, since the Claimants' export contracts with Metrogas and Gener were based on Argentine basin prices. The price-adjustment formulas in the Claimants' export contracts with Metrogas and Gener link the determination of the minimum and maximum prices to the basin prices in the Neuquén Basin published periodically by ENARGAS. It is obvious that the Claimants when they linked their prices to the basin price in the Neuquén Basin did so in reliance on the stability of the Legal Framework and the Sierra Chata Concession.

536. When the GOA measures substantially altered the Legal Framework and the market pricing system that formed the basis of both basin prices and the specific guarantees granted to the Claimants, it undermined the price foundation of the Claimants' export contracts with Metrogas and Gener.

537. In setting Argentine basin prices as the reference price for their contracts, the Claimants of course took on the business risk of natural fluctuations in those prices, but they were not supposed to take on the risk that the Argentine Government – which had made specific guarantees to the Claimants to allow freely agreed prices to prevail – would unilaterally abrogate those commitments and then force the Claimants to submit their export permits to government review simply to have a price equilibrium in their private contracts. As the Claimants contend, this risk was a regulatory risk, and it was accounted for in the Argentine Government's commitments under the Sierra Chata Concession, the Legal Framework and the BIT.

538. On the grounds mentioned above, Argentina has violated Claimants rights also to the extent its price interference measures caused damage to Claimants' export business.

C. Export Restrictions

1. The Claimants' position

539. The volumes authorized by the Sierra Chata Gas Export Permit are firm, and not subject to interruption. The guarantees of the Legal Framework and the Chile-Argentina Energy Treaty in particular — along with the reliance on those guarantees by all energy market participants — substantiate this fact.

540. Relying on these firm export rights, investors including the Claimants made significant investments to develop and produce hydrocarbon reserves in Argentina over long time horizons to meet firm contractual commitments. In particular, investors dedicated significant capital to construct, expand, and maintain an adequate transportation infrastructure for gas. Exporting gas to Chile, which entailed crossing the Andes Mountains or the Magellan Strait, required complex and costly engineering projects. Investors would not have made these significant long-term investments if the export permits that the GOA granted were not firm.

541. Like private investors, the Chilean Government also considered that the Sierra Chata Gas Export Permit was firm. Chile would not have relied on gas exports from Argentina if it believed that Argentina had the right to interrupt the export permits without compensation. By 2004, Chile was absolutely dependent on gas from Argentina. It was buying 90% of Argentina's gas exports, and in turn, Chile generated 25% of its electricity from the imported gas As Mr. Juan A. Pardo, former General Counsel of MEDA and MASA explains:

> "Throughout more than ten years, all players in the hydrocarbon sector, including the Government itself, construed the nature and the scope of the commitments assumed in the applicable framework in the manner described in the preceding paragraphs. In sum, all relevant actors considered that the Government had guaranteed foreign investors clear rules under a legal framework that ensured long-term stability to hydrocarbon investments."[180]

542. The GOA also construed the rights it granted under export permits as firm. For this reason, it analyzed the impact that the export permits would have on the long-term domestic supply prior to authorizing gas exports. Moreover, the GOA differentiated the firm export volumes established in each export permit from Excess Gas exports which were subject to interruption in the event of a domestic supply shortage. By allowing the Claimants to export volumes of gas in excess of the firm volumes granted under the Sierra Chata Gas Export Permit, the GOA highlighted the firm nature of the export volumes that the permit guaranteed. To take the contrary view would conflate the concept of firm export volumes with the concept of Excess Gas volumes.

543. Neither the Claimants, their customers, Chile, nor Argentina expected that the firm volumes in the gas export permits were conditioned on the demands of domestic supply throughout the life of the permit. This understanding was consistent with the

[180] Witness Statement of Juan A Pardo of 16 February 2009 ¶ 40 (Exhibit C-5).

Chile-Argentina Energy Treaty and with the enormous amounts of capital that were invested in the gas export regime and infrastructure.

544. In April 2004, through the issuance of Resolution SE 265/04[181], Argentina began to restrict the gas exports of Argentine producers and sellers, including the Claimants, as a means of addressing the self-induced shortages in the domestic market. By doing so, the GOA disregarded the Claimants' right to freely market the gas they produce, as well as the Claimants' firm export rights under the Sierra Chata Gas Export Permit.

545. In compliance with an instruction contained in Resolution SE 265/04, the Undersecretariat of Fuels "temporarily" approved a Curtailment Program for Gas Exports and Use of Transportation Capacity (the "**Curtailment Program**"). The Curtailment Program provided for restrictions on: (i) all gas exports to the extent necessary to meet the domestic demand; and (ii) all gas transportation services related to exports if required to meet domestic demand.

546. Through the Curtailment Program, the Secretary of Energy imposed restrictions on the Claimants' exports to Chile. In turn, these export restrictions prevented the Claimants from exporting gas volumes even though they were previously committed under deliver-or-pay gas export sales contracts.

547. These measures violated the Claimants' rights and resulted (and continue to result) in a taking of revenues because they force the Claimants to deliver these export volumes to domestic users at prices that are substantially lower than those agreed in their export contracts. Despite this taking of revenues, the GOA breached its commitment to compensate the Claimants for export restrictions at the rate of at least 35% of the

[181] Resolution 265/04 (Exhibit C-55).

international price of the Arabian Light crude oil of 34° API for 1,000m³ of 9,300 KCal.

548. According to Resolution SE 265/04, these purportedly "temporary" measures would remain in effect until the Secretary of Energy "decides that the available quantities of gas at the injection points of the Argentine transportation system are sufficient to meet domestic demand." Since the GOA's actions artificially depress gas prices and drive up domestic demand, the resolution has effectively ensured that the GOA will continue imposing export restrictions indefinitely.

549. In June 2004, the Secretary of Energy issued Resolution SE 659/04[182], which amended the Curtailment Program. Through this Resolution, the GOA instructed the Claimants to supply additional gas volumes to the local market, thus resulting in a significant curtailment of gas exports.

550. Resolution SE 659/04 entitled gas producers affected by the export curtailments to sales prices that were equivalent to the prices established for each basin in the First Gas Agreement. As a consequence, gas producers received a much lower price than the price to which they were entitled under their natural gas export agreements.

551. Through Resolutions SE 752/05[183], 925/05[184], 1886/06[185], and 599/07[186], the GOA enacted additional measures that reaffirmed the GOA's decision to continue abrogating legal and contractual rights established in the Legal Framework, the Hydrocarbon Concessions and Contracts, and the Chile-Argentina Energy Treaty. These resolutions set forth a new mandatory mechanism for the purchase and sale of

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[182] Resolution SE 659/04 (Exhibit C-61).
[183] Resolution SE 752/05 (Exhibit C-64).
[184] Resolution SE 925/05 (Exhibit C-65).
[185] Resolution SE 1806/06 (Exhibit C-73).
[186] Resolution SE 599/07 (Exhibit C-75).

gas in the domestic market: they allow certain large users of gas, power generators, and CNG stations to place "irrevocable offers" to purchase gas directly from gas producers at regulated prices. If the aggregate domestic demand of these users is not satisfied, the shortfall must be supplied through additional gas requests to the local market at below-market prices fixed by the Secretary of Energy.

552. These measures required the Claimants to ignore their existing contractual commitments, and instead, deliver their gas production to large domestic users, power plants and CNG stations. Hence, the GOA abrogated the Claimants' vested legal and contractual rights to freely sell its gas production, undermined the Claimants' export rights, and violated the international commitments that the GOA assumed.

553. In addition, Resolution SE 752/05,[187] which allowed certain domestic customers to make irrevocable offers, put the Claimants in a no-win situation. If the Claimants do not "agree" to an irrevocable offer, then the Secretary of Energy requires them to supply gas to the domestic market at a price that is significantly lower than the price they would have received had they agreed to the irrevocable offer. But if the Claimants yield to the GOA's pressure and "agree" to the irrevocable offer, they would be prevented from meeting their export commitments in their contracts with export customers.

554. Far from being a transitory measure, the GOA intends the "irrevocable offer" mechanism to become permanent.

555. The GOA continued to impose export restrictions and in August 2005, the Energy Secretariat enacted Resolution SE 939/05[188], which provided a priority list for injecting gas into transportation pipelines. Resolution SE 939/05 prevented exporting

[187] Resolution SE 752/05 (Exhibit C-64).
[188] Resolution 939/05 (Exhibit C-65).

producers such as the Claimants from exporting gas if they had not previously met all of their government mandated or contractual commitments with their domestic customers.

556. Since 2007, the Director of Hydrocarbons Economy at the Energy Secretariat and other high-ranking officers have been informally ordering the Claimants to suspend all exports to Chile and deliver their production exclusively to the domestic market in accordance with a government-mandated priority for injections. These orders were not grounded on any of the existing resolutions imposing export restrictions.

557. Since April 2007, a government-mandated and controlled Committee has been determining how to reallocate gas produced in Argentina to mitigate the energy shortages. The Committee consists of transportation and distribution companies and officers of the Secretary of Energy and ENARGAS, the Argentine regulatory agency for gas distribution and transmission systems. At the Committee meetings, distribution companies report the volumes of gas they require, and based on this information, the Secretary of Energy usually requires that distribution companies' demands be met at the expense of export volumes.

558. In addition to the injection orders that the Secretary of Energy issued under Resolutions SE 659/04 and SE 752/05, Decision SSC 27/04, and the "informal" orders issued following each of the Committee meetings since July 2007, other senior Argentine officials have begun issuing administrative orders and controlling deliveries by Argentine gas producers like MASA. Through these orders (which in many cases are just verbal), Argentine officials inform gas transportation companies of the volumes of gas (if any) they may export. Transportation companies may not transport volumes in excess of the amounts that the officials authorize.

559. As noted, the GOA began in December 2006, when the First Gas Agreement expired, pressing gas producers like the Claimants to enter into a more drastic version of the

agreement (the "**Second Gas Agreement**"). The declared aim of the new agreement was to guarantee full supply to the domestic market while maintaining regulated prices at different levels for different categories of consumers.

560. Resolution SE 599/07 approved the terms and conditions of the Second Gas Agreement.[189] The Secretary of Energy issued that Resolution as an instrument to "persuade" gas producers to sign the Second Gas Agreement since the treatment granted to signing producers (the "**Signing Producers**") was more favourable than that granted to non-signing producers (the "**Non-Signing Producers**"). As explained by Ms. Valle:

> "The Government forced producers to execute the Second Natural Gas Agreement under the threat of imposing sanctions and subjecting the producers that refused to sign the "agreement" to discriminatory treatment."[190]

561. In the case of gas supply shortages in the domestic market, Resolution SE 599/07 provides that the GOA will "re-route" and curtail the exports and domestic sales of Signing Producers only after curtailing and "re-routing" the exports and domestic sales of Non-Signing Producers.[191] Thus, the Second Gas Agreement was in no way a voluntary agreement; it was coerced and extortive.

562. The main beneficiaries of the re-routed gas are the consumers included in the so-called "Priority Demand" (residential and small commercial users supplied by gas distribution companies). Of all customers, these consumers pay the lowest prices. Argentina forces Non-Signing Producers such as the Claimants to "re-route" gas shipments from customers paying the highest prices to consumers paying the lowest ones. These restrictions not only preclude MASA from complying with its existing

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[189] Resolution 599/07 (Exhibit C-75).
[190] Valle Witness Statement, *supra* (n 34) ¶ 60 (Exhibit C-4).
[191] Resolution SE 599/07, Arts. 9 and 10 (Exhibit C-75).

export commitments, but also obligate it to supply gas to domestic consumers with which it has no contractual relationships at substantially lower prices than the ones agreed under its export agreements.

563. In addition, although domestic consumers pay Signing Producers in accordance with the price formulas established in the Second Gas Agreement (which are also capped prices), domestic consumers pay Non-Signing Producers much lower prices for the same volumes. Consequently, the prices that MASA receives for its re-routed gas are not only substantially lower than those agreed in the contracts with its export customers, but they are also lower than the prices that the Signing Producers receive for their "re-routed" volumes.

564. Even though MASA ultimately chose not to sign the Second Gas Agreement, Resolution SE 599/07 presented MASA with two choices, both of which entailed bad outcomes: (i) to sign the Second Gas Agreement and consequently assume domestic supply commitments that it could not possibly fulfil without interrupting supplies under existing export contracts, or (ii) to become a Non-Signing Producer, and therefore, be the first to suffer from export curtailments and re-routing to domestic consumers at depressed, regulated, and discriminatory prices.

565. MASA refused to sign the Second Gas Agreement because it would have forced the company to terminate deliveries under its pre-existing export contracts. In addition, any "voluntary" agreement to the Second Gas Agreement might have precluded MASA from invoking its *force majeure* rights in disputes with its export client arising out of Argentina's export curtailments. MASA paid a price for not relenting to the GOA's coercion, because the Second Gas Agreement contained an inherent retaliation mechanism that subjected MASA and other Non-Signing Producers to additional restrictions and discriminatory treatment.

566. Through, *inter alia*, Resolutions SE 265/04, 659/04, and 752/05, Argentina repudiated the Claimants:

- right to freely dispose of and market the production of gas at deregulated prices;
- vested rights under the Sierra Chata Gas Export Permit to export certain firm volumes of gas; and
- right to receive as compensation (in case export or domestic restrictions are established) a sum equivalent to 35% of the international price of Arabian Light crude oil for the relevant energy equivalent unit of gas.

567. The GOA's restrictions on gas exports also violate the Chile-Argentina Energy Treaty by: (i) not providing a legal regime permitting free exports of gas; (ii) restricting exports that were approved based on sufficient reserves measured at the time the export permits were granted; and (iii) curtailing gas exports on a discriminatory basis.

568. Argentina's measures also adversely affected the Claimants' business relations with Chilean gas purchasers because the GOA's export restrictions impaired the Claimants' ability to meet their contractual deliveries. In addition, the gas export contracts contain strict delivery ("deliver-or-pay") obligations that subject the Claimants to liquidated damages and other penalties for not delivering, remedies that would impact both the Claimants' revenues and long term business prospects.

569. The GOA disregarded and even aggravated the negative impact that these restrictions have on the Claimants' business. As explained by Ms. Valle:

> "The Government did not assist us politically at all in our efforts to maintain acceptable commercial relationships with our Chilean customers. On the contrary, the Government actively aggravated the commercial tension its measures caused. For example, the Energy Secretariat sent a letter to AES Gener S.A., one of Mobil's customers, which stated that the export restrictions and curtailments did not

> constitute a *force majeure* event but were the result of the producers' behavior. Despite our efforts to reach an amicable solution, AES Gener sued Mobil and its partners in the Sierra Chata area in an arbitration proceeding under the rules of the International Chamber of Commerce."[192]

570. Argentina does not contest, but rather acknowledges, that it took the export curtailment and re-routing at issue. Through those measures, the Argentine Government:

- suspended firm export volumes under the Sierra Chata Gas Export Permit through Decision SSC 27/04, which was ratified and supplemented by Resolution SE 503/04; and

- imposed, on the basis of, *inter alia*, Resolutions SE 659/04, 752/05, 925/05, 1886/06 and 599/07, curtailments of authorized firm gas export volumes through orders to re-route gas to the domestic market at the discretion of the Secretary of Energy even when those deliveries conflicted with producers' existing contractual obligations.

571. Those measures re-routed the Claimants' export volumes to the domestic market at regulated prices that were substantially lower than the prices they would have received under their export contracts. As a consequence, the Claimants suffered severe damage to their export business, and the Argentine Government violated the Claimants' firm export rights, as well as their right to market gas freely at freely-agreed prices, under the Sierra Chata Export Permit, the Sierra Chata Concession, and the Legal Framework (which includes the Chile-Argentina Energy Treaty).

572. Argentina focuses on attempting to defend its measures through various ways, such as by alleging that: (i) producers "agreed" to have their exports restricted and re-routed;

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[192] Valle Witness Statement, *supra* (n 34) ¶ 71, (Exhibit C-4).

(ii) producers had various mitigation mechanisms available; (iii) producers such as the Claimants are responsible for the gas shortages that led to the export restriction and re-routing measures; and (iv) the Government's compensation obligations are null due to rising crude oil prices.

573. As noted, in 2004, the GOA's began restricting export volumes in order to serve the domestic demand that the Government created by freezing gas prices at absurdly low levels. Those measures had the effect of subjecting exports to the prior satisfaction of the artificially-stimulated domestic demand that resulted from Argentina's price interference measures. From the outset, the Government was well-aware that the applicable Legal Framework did not impose a domestic supply requirement on producers or allow for the uncompensated curtailment and re-routing of export volumes. In order to reduce its exposure for the violation of the Legal Framework and gas export permits, the Government began to seek an agreement from gas producers that would permit it to continue restricting exports on the basis of forced consent.

574. The First Gas Agreement, which the Claimants refused to sign, was the Government's first attempt to create the appearance of consent. The Irrevocable Standardized Offers program, which the Government implemented shortly thereafter, and the Second Gas Agreement, which the Claimants also refused to sign, operated in a similar fashion and were part of the Government's strategy to create the appearance of consent. In implementing those measures, the Argentine Government "invited" gas producers to commit gas volumes to the domestic market, which in most cases could only be done at the expense of restricting deliveries to their export customers. If producers did not accept the "invitation," the Argentine Government imposed restrictions on their exports and re-routed their volumes to the domestic market under conditions that were more onerous than those applying to the producers who had accepted the Government's "invitation".

575. In other words, the Government impaled producers with a "Morton's Fork"; either (i) yield to the Government's pressure to supply the domestic market, and by doing so, voluntarily fail to meet their delivery obligations to export customers and potentially give the appearance of consent to Argentina's wrongful measures, or (ii) as the Claimants did, refuse to assume domestic supply obligations and suffer even more burdensome export restriction and rerouting measures. Resolution SE 599/07, which approved the terms of the Second Gas Agreement, is clear that, in any event, those producers that refused to sign the agreement would be subjected to domestic supply obligations, have their volumes restricted first (before other producers), and receive the lowest tier of regulated prices.

576. Argentina further distorts the facts by alleging that the Claimants acted as "free riders" by not signing the Second Gas Agreement, since they allegedly benefitted from the supposed price increases provided by that agreement while not assuming the same domestic supply requirements as signing producers. Far from benefitting from this agreement, the Claimants suffered severe damages by refusing to sign, as explained above. Through the application of Resolution SE 599/07, since August 2007 the Government has allocated as much as 60% of the Claimants' production to the distribution companies that pay the lowest price for gas. In addition, far from establishing actual price increases, the Second Gas Agreement merely provided that the Government would discuss the segmentation of priority demand (*i.e.* residential and small commercial users) and analyze if it might at some time in the future seek an adjustment of the prices paid by high-income consumers. This constitutes further recognition by the Government that the prices paid by those consumers were inadequate and did not reflect market levels.

577. In a farfetched attempt to justify the reasonableness of its export restrictions and re-routings, Argentina argues that it offered gas exporters the possibility to continue exporting if they substituted the curtailed export volumes with alternative (*i.e.* liquid) fuels. By using gas substitutes to satisfy the domestic supply requirement that the

Government imposed, the Claimants would allegedly be able to export the volumes that would otherwise be curtailed to their export customers. Argentina's actual motivation to authorize this "option" was not to provide gas producers with a mitigation mechanism. Rather, Argentina provided this option in an effort to avoid incurring liability for violating its treaty obligations to Chile under the Chile-Argentina Energy Treaty. Not surprisingly then, the viability of this "option" for producers was merely ostensible.

578. In an attempt to evade responsibility and redirect the Tribunal's attention from the relevant points at issue in this case, Argentina alleges that the conduct of certain gas producers, and not its own measures, caused the gas shortages that Argentina began experiencing in 2004. In doing so, Argentina denies that its price interference measures artificially stimulated demand and that those same measures deprived producers of the incentives needed for further exploration and production activities, when it is well known (and acknowledged by the Government itself) that those factors were the primary causes of its gas shortages.

579. The principle of supply and demand operates in natural gas markets. All other factors being equal, if prices are low in comparison with substitute fuels, certain segments of consumers will consume more gas. Conversely, if the price of gas rises, consumption may decrease. The pattern of rising demand and falling production resulted directly from Argentina's measures maintaining artificially low prices.

580. Argentina alleges that the level of demand and the maturity of basins were not unforeseeable events based on the projections existing before the outburst of the crisis. It also alleges that the first signs of difficulties in the supply of natural gas to the domestic market became apparent in the first half of 2002, even though an official report prepared by the Energy Secretariat in May 2003 projected an aggregate gas demand (*i.e.*, domestic plus export demand) for 2004 that was lower than the actual volumes produced in that year.

581. Even if Argentina's allegations concerning projected demand were true, they would raise the question of why, if the Government understood at such an early point in time that gas demand was set to rise dramatically, did it engage in pricing policies that could only contribute to that increase while simultaneously preventing the replacement of reserves and development of new ones. Moreover, if the Government was aware that drastic increases in domestic demand were imminent as early as 2002 (or even before the crisis), why did it continue granting export permits through 2004. Even by the Government's own analysis of demand projections, it is evident that it mismanaged the situation despite advance warning of potential gas shortages.

582. For the purpose of this arbitration, Argentina blames the country's gas shortages on a write-off of natural gas reserves by producers, including the Claimants. In doing so, Argentina generally accuses gas producers in the country of overestimating their reserves and blames those producers for the "disappearance" of reserves on a national level. In alleging that reserves throughout the country "disappeared," Argentina fails to consider some elementary concepts concerning the economics and science of estimating gas reserves.

583. The Claimants are, and always have been, marginal gas producers in Argentina. In fact, the Claimants' share of Sierra Chata's and Aguaragüe's reserves during this period represented on average less than 1% and 1.5%, respectively, of Argentina's natural reserves. The Claimants' share of the production during the same period in both fields represented, on average, less than 3% of the total domestic gas production. Thus, any decrease in the Claimants' reserves and production levels would have had no significant impact on the country's overall supply of natural gas. Argentina's own damage experts recognize this fact when they express that "MASA and MEDA are marginal players in the natural gas market." In any event, Greco indicates that during

the 2002- 2008 period Sierra Chata actually discovered new reserves of 1,828 MM m3.[193] It follows that there is no substance to Argentina's allegation that the Claimants contributed to the countries' gas shortages.

584. One of the *a posteriori* explanations that the Argentine Government provided for imposing export restrictions is that producers allegedly breached their domestic supply quotas, despite the fact that producers had never had any obligation to supply the domestic market. In an attempt to justify its export restrictions, however, the Government invented the concept of collective and individual domestic supply obligations for producers in 2004.[194] Through the invention of this requirement, the Government tried to make producers the scapegoat for its own negligence and mismanagement of the gas sector.

585. Aside from relying on Article 6 of the Hydrocarbons Law as the legal basis for its newly-invented domestic supply quotas on producers, the Argentine Government fails to identify a single law or regulation establishing a specific quota that producers must meet either individually or collectively. Of course, no such requirement existed under the Legal Framework. As Sandleris and Schargrodsky concede, under the Legal Framework the Government placed the duty to guarantee the supply of the domestic market on gas distribution companies, not producers.[195]

586. Notably, even when Argentina began to impose domestic supply quotas in 2004, it issued Decision SSC 27/04, which distinguished between producers that had met their alleged domestic supply quotas and those that had not.[196] The Government included the Claimants among the group of producers that were meeting their domestic supply

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[193] Greco Report, *supra* (n 125) ¶ 89.
[194] Decision SSC 27/04, Eight Recital (Exhibit C-56).
[195] UTDT Report, *supra* (n 156) ¶ 88.
[196] Decision SCC 27/04 (Exhibit C-56).

quotas. Thus, Argentina cannot now accuse the Claimants of failing to meet any domestic supply quotas, even if such an obligation had existed in the first place, which it did not.

587. With respect to the Sierra Chata Export Permit specifically, as Bastos notes, the Government did not condition the granting of that permit on the maintenance of a certain level of reserves.[197] That the Government did impose such a condition when granting other export permits shows that it knew how to do so if it had wanted, but it did not. Accordingly, even if the Government had wanted to invoke the reserve declines in Sierra Chata as a reason for imposing export restrictions, it could not have done so. To raise this argument now, in light of the lack of a reserve maintenance requirement in the Sierra Chata Export Permit, would constitute an act of bad faith.

588. In any event, Argentina is precluded from alleging that producers failed to make necessary investments in production. The expert reports and witness statements that it submitted in this arbitration have acknowledged that, following 2002, producers contributed to increasing total national gas production by 38%. That such an increase took place despite the abnormally low natural gas prices that the Government imposed raises serious doubts about Argentina's claim that producers like the Claimants had underinvested.

2. Argentina's position

589. First of all, gas shortage in Argentina was not the result of an increase in gas demand due to the (alleged) interference of the Argentine Government with energy prices.

[197] Bastos Supplemental Report, *supra* (n 133) ¶ 109 (Exhibit C-504).

590. As expert Greco points out, "the main problem of the supply crisis was the shortage of gas in the fields and not the restrictions on the transportation system"[198]. As an evidence of this, starting in 2004, shortage of gas in the domestic market began to take place but, at the same time, there was available transportation capacity at the gas pipelines.

591. Furthermore, in spite of the increase in the gas demand in the last years, volume of gas delivered by producers was lower than expected in some demand forecasts prepared before the outburst of the crisis. Thus, as explained by expert Greco "gas supply shortage may not be attributed to an unforeseeable level of demand."[199]

592. In fact, the Energy Secretary Cameron states that "on the contrary, the 2001/2002 crisis only delayed the manifestation of the problem as, due to the reduction in GDP since 1998 forward, the increase in the gas consumption in Argentina was far below average values."[200]

593. Additionally, over time, there was a recovery in the price of natural gas. Particularly, Guichón mentioned that "the prices of liquefiable components, such as condensate gas, natural petrol and liquefied petroleum gas, which derive from the production of natural gas, remained in dollars and followed the evolution of the international price of oil."[201]

594. Secondly, the main cause of the gas supply crisis was the behaviour of some natural gas producers (like the Claimants). Lack of exploration investments on the part of producers gave rise to the shortage of gas, which prevented export of hydrocarbons and, simultaneously, the appropriate supply within the domestic market. In that

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[198] Greco Report, *supra* (n 125) ¶ 55.
[199] *Ibid* ¶ 131.
[200] Cameron Witness Statement, *supra* (n 107) ¶ 67.
[201] Guichón First Witness Statement, *supra* (n 149) ¶ 162.

connection, expert Greco points out that "The reduction in the exploration activity since 1998 is noteworthy. The average of exploration wells after 1998 is lower than half (61% lower) the average of the previous 28 years."[202]

595. On the other hand, there has been a strong decline in proved natural gas reserves across all the country's basins for reasons other than production.

596. In particular, MEDA and MASA natural gas reserves decreased sharply during the last years and in a higher percentage than the average for the country. As stated by experts Sandleris and Schardrodsky "MASA and MEDA's reserves dropped, between 1994 and 2008, by 65% in Aguaragüe and 63% in Chihuidos, [but] the average decline for the country was 26%."[203]

597. The Claimants never explained the reason why their export permit was suspended from the Aguaragüe area. The explanation is very simple: through Resolution SE 810/07 the export permit was suspended from the Aguaragüe area due to an inaccurate reserves statement made by the Consortium in which MASA participates when requesting authorization to export natural gas to Chile.

598. In the recitals of Resolution SE 810/07 it is stated that:

> "[T]he reserves estimation made in 1997 by the operating company of the fields involved in the AGUARAGUE and SAN ANTONIO SUR Concessions, at that time TECPETROL SOCIEDAD ANONIMA, and certified by an external audit hired to that end, GAFFNEY, CLINE & ASSOCIATES, that said estimation would be incorrect, from a technical point of view, showing the use of reserve evaluation practices not recommended by the specialized literature and revealing a strong optimistic bias in the weighting of existing reserves, as well as in the probabilistic classification made."[204]

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[202] *Ibid* ¶ 71.
[203] UTDT Report, *supra* (n 156) ¶ 127.
[204] Resolution SE 810/0, Recital 30 (Exhibit AR-233)

599. The evolution of Aguaragüe and San Antonio Sur field reserves shows a strong descending tendency in the ratio of reserves to production. In fact, there was a significant reduction in reserves and in the ratio reserves/production of the abovementioned fields of the Claimants.

600. To analyze the performance of the Claimants and assess whether they contributed to the shortage of natural gas in the domestic market it is necessary to take into account all their concessions, i.e. Aguaragüe and Sierra Chata.

601. MASA itself acknowledged that to analyze the degree of impairment of the domestic market it is necessary to take all its reserves into consideration, i.e. all the reserves of the North western Basin and the Neuquén Basin. In a Note addressed to the Energy Secretary Cameron to request the lift of the suspension of the export permit of Aguaragüe, MASA stated that´

> "In this manner and as a result of the termination of MASA export agreements for the "Sierra Chata" gas field, the volume of natural gas net reserves incorporated by MASA amount to 5,512,00 MM m3,which must be added to the availability of MASA natural gas reserves.
>
> It is out of the question that such reserves, once discounted the export volumes under other agreements, are available reserves for the domestic market supply, which offset any decline in the North western Basin."[205]

602. To justify the over-estimation of reserves in Aguaragüe and their responsibility for the disappearance of the 40,455,300,000 m3 of natural gas from their "certified" reserves, the Claimants assert that "the concept of reserves is not only tied to physical considerations but also to economic and regulatory elements" and therefore "existing

[205] Note of Mariano C. Vivas de Lorenzi, MASA's attorney-in-fact, addressed to the Energy Secretary Daniel Cameron, dated 8 February 2008 (Exhibit AR-308).

gas volumes which may be reported as reserves at a certain level of prices or costs may no longer be considered reserves if the prices or costs substantially change."

603. However, a decline in reserves does not always arise from the uncertainty of "future level of prices or costs". For instance, if the companies do not use reserve estimation techniques properly, reserves that are not such may be declared. This is what happened in the Aguaragüe and San Antonio Sur Areas where the "decline in reserves would result from mining risks, such as the flooding with water of the hydrocarbon reservoirs."

604. In fact, the estimation of reserves made in 1997 by the Aguaragüe Joint Venture (composed by MASA) at the time of requesting a natural gas export permit to Chile was not correct from a technical viewpoint since "it did not follow recommended practices for the assessment of reservoirs."

605. Even worse, the members of the Aguaragüe Joint Venture (composed by MASA) were aware since 1993, as a result of a report filed by the technical operator of the Concession, of the possibility of floods at the hydrocarbon reservoir. In other words, they knew it was likely that such event occurred during the execution of the export permit, thus seriously affecting the production of natural gas.

606. The Argentine Republic did not begin retaliatory proceedings against MASA for not agreeing to the Second Gas Agreement. The Aguaragüe Export Permit was suspended for a significant loss in the computable volume of natural gas reserves due to causes different from the gas production between December 1997 and December 2004.

607. The Aguaragüe Joint Venture (composed by MASA) contributed to the natural gas shortage in the domestic market by submitting inaccurate reports on the gas reserves available at the Aguaragüe and San Antonio Sur fields and making insufficient investments in additional exploration.

608. The Energy Secretary Cameron stated that:

> "In our country, there were many cases of understatements of reserves, the most relevant being the reclassification of reserves made by Petrobrás in 2003 on assets recently purchased to Pérez Companc, the reclassification by YPF in 2005 and 2006 and the sharp decline of the most important gas production concessions in the Noroeste Basin: Aguaragüe and Ramos."[206]

609. MEDA and MASA assert that they have not breached any obligation related to the Sierra Chata Concession and, particularly, that "the investment obligations imposed by the Hydrocarbons Law contain an economic component and do not require the Claimants to invest in a manner that is not economically sustainable." LECG also states that natural gas producers "have the option to reduce the supply to the market (leaving natural gas in the ground for better times)".[207]

610. Both MEDA and MASA are hydrocarbon concessionaires and their activities must conform to the provisions of the Hydrocarbons Law. In this regard, experts Sandleris and Schargrodsky explain that "As concessionaires, they must respect the regulatory framework and exploit the field that the Government has entrusted them with regularly, continuously, rationally and efficiently.[208]

611. However, according to the Sproule report, "in 2002, gas production from the Sierra Chata Field was reduced by the operator due to lack of available markets with gas prices that would sustain a return on investment." [209]It is to be noted that in 2002 natural gas export contracts were not pesified, and export restrictions and duties were

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[206] Cameron Witness Statement, *supra* (n 107) ¶ 71.
[207] LECG Second Report, *supra* (n 132) ¶ 45.
[208] UTDT Second Report, *supra* (n 135) ¶ 49.
[209] Expert Report of Sproule International Limited of 26 April 2010 [hereinafter "*Sproule Report*"] ¶ 109.

not applied to natural gas exports. As Cameron said, "2002 was an excellent year for natural gas exporters."[210]

612. Pursuant to Section 31 of the Hydrocarbons Law, concessionaires must exploit their fields "in pursuance of the most reasonable and efficient techniques… ensuring the maximum hydrocarbon production compatible with the proper and profitable exploitation of the field, as well as compliance with the criteria guaranteeing convenient preservation of the reserves."

613. Then, both the reduction in production in 2002 and the well opening-and-closing behaviour, performed by the Sierra Chata Consortium (composed by MEDA) are not in line with the Hydrocarbons Law and contributed to the natural gas shortage in the domestic market.

614. Whether MEDA and MASA have a small or large share in the total production of Argentina is irrelevant. What is relevant is to actually determine if they affected the domestic market supply. In that regard, Greco points out that "the fall in their production helped prevent supply from increasing to the extent required to satisfy demand."[211]

615. To summarize, the under-estimation of reserves, the lack of additional exploration by the Aguaragüe Joint Venture (composed by MASA), the decline in production in 2002 and the well opening-and-closing behaviour of the Sierra Chata Consortium (composed by MEDA) contributed to the gas shortage in Argentina. Ironically, the Claimants contributed to the situation that forced the Argentine Government to take the measures they now complain about.

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[210] Cameron Witness Statement, *supra* (n 107) ¶ 53.
[211] Greco, Second Report, *supra* (n 139) ¶ 88.

616. Moreover, the Claimants assure they do not claim for the natural gas volumes they export from the Aguaragüe area. However, it arises from LECG Report submitted by the Claimants that they claim for the restrictions placed on the MASA agreement with the power generator Termoandes.

617. In fact, MEDA and MASA try to deceive the Tribunal by hiding a claim for restrictions in the Aguaragüe area under another accusation: "price interference", which is also inappropriate since the MASA agreement with Termoandes is not subject to pesification.

618. As explained by experts Sandleris and Schargrodsky:

> "MASA and MEDA disguise this situation by calculating the damages under the line item "price interference in wholesale market". This is inaccurate, because the pesification of contracts did not reach the prices of Termoandes, and therefore, there was no intervention of the Argentine Government in prices. Contractual prices were agreed upon in US Dollars, and bore no relation to domestic prices. This is accepted by LECG, because in their valuation model real and counterfactual prices of Termoandes are identical. i.e., Claimants acknowledged there was no price interference in the case of Termoandes, but they quantify damages under the item price interference." [212]

619. Therefore, the Claimants' claim for their agreement with Termoandes must be dismissed by the Tribunal.

620. In short, reduction and overstatement of reserves on the part of some natural gas producers and, specifically, of MEDA and MASA were crucial to understand the causes of gas shortage in Argentina.

621. Natural gas export restrictions and re-routings were not unrelated to the behaviour of some hydrocarbon producers (such as the Claimants). In fact, in face of the domestic

[212] UTDT Report, *supra* (n 156) ¶ 243.

market shortage of gas supply caused by the behaviour of some hydrocarbon producers and pursuant to the Hydrocarbons Law as regards giving priority to domestic supply, the Secretary of Energy instructed producers to re-route a percentage of their natural gas exports to satisfy domestic market needs. Apart from the abovementioned measures which aimed at solving the serious gas shortage problems, other longer term measures were implemented with a twofold purpose: to achieve consensus among gas producers and to boost gas production increasing gas prices at the wellhead.

622. The Claimants argue that the Secretary of Energy had no legal grounds for imposing the re-routing on natural gas exports. This assertion is false.

623. In fact, paragraph 4, article 6 of the Hydrocarbons Law sets forth:

> "The Executive Branch shall allow exports of hydrocarbons or by-products not required for appropriate satisfaction of domestic demand, provided said exports are made at reasonable commercial prices and *shall, in that situation, set the criteria. that will govern the domestic market transactions, so as to enable a rational and fair market share for all the country producers."* [Emphasis added]

624. In this context, the provisions and resolutions issued by the Secretary of Energy have set forth throughout several periods, on the basis of rationality and fairness criteria, participation of all the country producers in the fulfilment of the domestic market needs. Besides, gas exports were restricted only to the extent producers could not comply with their domestic market share.

625. The export permit of Sierra Chata is not firm. On the contrary, when authorizing gas exports, the Secretary of Energy had to assess their impact on the domestic market and, in particular, whether they would affect the gas supply needs within the country. In other words, the entire country existing reserves were taken into account.

626. Subsequently, it could be proved that, in many cases, the information about reserves furnished by hydrocarbons producers was false or inaccurate. This false information

affected one of the prerequisites at the time of granting export permits. As was the case with the Consortium in which MASA participates, whose export permit for the Aguaragüe area was suspended.

627. In short, if at the time exports were requested the actual situation of proved reserves at the country level could have been verified, some requests may have been denied. Therefore, and contrary to the Claimants' assertion, there is no absolute right to export natural gas.

628. The Second Gas Agreement was once again willingly subscribed by most of hydrocarbons producers in Argentina (including, Repsol YPF, Total Austral, Pluspetrol, Wintershall, Pan American Energy and Petrobras Energía) and it is intended to remain effective until December 2011. It is simply absurd to believe that Argentina has the capacity to coerce several multinational oil companies (including one controlled by the Brazilian Government), which are among the leading companies in the world.

629. It is an open, voluntary agreement, i.e., any signatory producer to the agreement may terminate its participation, and any non-signatory producer may adhere during the entire term of the agreement. In other words, the Claimants may adhere to the agreement at any time during its term, if they consider it appropriate.

630. Moreover, in the Second Gas Agreement, producers undertook to supply the domestic market in a merely jointly manner, i.e. limiting each gas producer to supply a certain volume.

631. On the other hand, in case of a gas shortage of supply for the domestic market due to the behaviour of some producers, the Second Gas Agreement stipulates that the producers who would first supply their export gas volumes are the signatory ones and subsequently, if said volumes are not enough, non-signatory producers should satisfy

the domestic market, pursuant to the Hydrocarbons Law. Thus, there is no discrimination against non-signatory producers as the Claimants.

632. By means of the agreements entered into between the Argentine Republic and natural gas producers, it was possible to boost production for the domestic market of most producers and, based on a cost analysis, natural gas price increases at the wellhead were set for all producers.

633. Finally, it is worth mentioning that the Claimants state they did not sign the Second Gas Agreement because it meant "assuming domestic supply commitments that it could not possibly fulfil without interrupting supplies under existing export contracts." This is clearly shown by the fact that:

> "The production in the areas where MASA and MEDA operate dropped from 8.5 million m3/day (in average) before the crisis to around 5.2 million m3/day after the crisis. At the same time, national production rose from approximately 100 million m3/day before the crisis to 138.4 million m3/day after the crisis." [213]

634. To sum up, it can be concluded that the Claimants (as well as other hydrocarbon producers) are responsible for the energy shortage and in view of this situation the measures taken by the Secretary of Energy are reasonable and legitimate.

635. The measures adopted by the Argentine Republic during the crisis in order to ensure hydrocarbon domestic market satisfaction did not violate the applicable regulatory framework, the Treaty with Chile, and did not affect the right to the free disposition of hydrocarbons.

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[213] UTDT Report, supra (n 156) ¶ 139.

636. First, according to the Hydrocarbons Law (the most important rule governing the industry) only the export of hydrocarbons or by-products *not required for appropriate satisfaction of domestic demand* can be authorized.

637. In all the rules, either in the Gas Law, the LPG Law, or the Deregulation Decrees, article 6 of the Hydrocarbons Law and the need to ensure domestic market hydrocarbons supply were also expressly taken into account, and consequently, it was possible to establish restrictions on exports

638. Second, all the rules mentioned by the Claimants are below the Hydrocarbons Law and the other specified laws. Therefore, they can never modify or abrogate them. In the same vein, Dr. Mata states that "Decrees No. 1055/89, 1212/89, 2178/91, and 2411/91 are executive regulations of the Hydrocarbons Laws, HL, and the State Reform Law, SRL, contemplated in Article 99,2, AC.[214]

639. Even though the quoted rules do not have the scope the Claimants intend to assign them, should it be so, it should be taken into consideration that the rules whereby restrictions on exports were imposed are of the same or of a higher level than the ones quoted by the Claimants, thus as they are subsequent rules, the first ones would prevail.

640. Third, the Claimants are mistaken when they state that the Treaty with Chile was violated. On the contrary, the Treaty with Chile included the provision that natural gas export permits would be considered "to the extent domestic supply would not be jeopardized." Contrary to the arguments held by MEDA and MASA, the Treaty with Chile expressly takes into consideration the main objective of domestic market supply. The provisions of the treaty establish that export of gas will be allowed "based

[214] Mata Report, *supra* (n 129) ¶ 180.

on the reserves of the respective exploitation areas and their availability" and that "the legal framework applicable to the sale, export, import and transport of gas *is provided by the legislation of each State*…"[215]

641. In other words, far from rendering domestic legislation ineffective, the Treaty with Chile expressly ratifies its effectiveness. In addition, it also lays down the same principles as Argentine legislation does, such as the subordination of gas exports to the domestic market supply.

642. Fourth, the right to free disposition of hydrocarbons pursuant to the deregulation decrees is subject to domestic supply.

643. Finally, given the Argentine Government levies a tax on exports, tax collection increases as exports are made. Thus there is no incentive to establish unnecessary restrictions on exports. MEDA and MASA hold that they have the right to receive a compensation "for export restrictions at the rate of at least 35% of the international price of the Arabian Light crude oil of 34° API for 1,000m^3 of 9,300 KCal."

644. According to the Claimants, article 5 of Decree 1969/93[216] empowers the Holder of Permit to receive, for the time the [restriction] lasts, a value not below the one established in article 6 of Decree 1589 of December 27, 1989.[217]

645. However, article 6 of Decree 1589/89 sets forth that "in case the National Executive Branch should establish restrictions on crude oil and/or by-product exports, the provisions of article 6 of the Hydrocarbons Law shall apply."

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[215] Protocol Substituting Protocol No. 2 to the Agreement on Economic Complementary No. 16 between the Republic of Chile and the Argentine Republic, 27 November 1995, Art. 2 and 6, (Exhibit AR-79).
[216] Decree 1969/93 (Exhibit C-94).
[217] Decree 1589/89 (Exhibit C-15).

646. Article 6 of the Hydrocarbons Law establishes:

> "When crude oil international prices significantly increase due to *exceptional circumstances*, they shall not be considered for domestic market commercialization price fixing. In that case, domestic prices shall be fixed based on the actual exploitation costs, amortizations that technically correspond, and at a reasonable interest on the updated and depreciated investments." [Emphasis added]

647. Due to the significant increase in the international crude oil prices as a consequence of the exceptional circumstances, the international crude oil price cannot be used to fix domestic market prices. Therefore, the compensation amount of article 6 of Decree 1589/89 is not applicable.

648. Consequently, if the international crude oil price shall not be used to fix domestic market prices, then it cannot be used as reference to fix gas sales prices for the domestic market either.

649. In such context, and pursuant to current rules, the Secretary of Energy made a cost analysis for natural gas exploration and production in order to determine actual exploitation costs. Based on this cost analysis carried out by the Secretary of Energy, the First Gas Agreement was signed by most gas producers with purpose of restructuring the natural gas price.

650. As Dr. Mata explains:

> "After the 2001/2002 crisis, an agreement was entered into between the Secretary of Energy and most of the gas producers entitled "Agreement for the Implementation of the Normalization Model of Natural Gas Prices at the Entry Point to the Transport System," which was approved by the Ministry governing the sector by means of Resolution No. 208/04 of the Ministry of Federal Planning. Said Agreement was based on a cost study which had the purpose, in accordance with the recitals of the Resolution mentioned above, of "ensuring reasonable supply conditions and a resolution of the crisis by contemplating the situation of residential consumers and the sector of industrial consumers with less power to directly negotiate with producers." As may be observed, the Agreement with producers was the first step towards gradually solving the force majeure situation created by the crisis based on the

> principle of shared sacrifice and in accordance with the guidelines established by Articles 6, HL, and 6 of Decree No. 1589/89."[218]

651. All measures taken by the Argentine Republic to fight the shortage of hydrocarbons in the domestic market were aimed at ensuring self-supply, were legitimate and in line with the applicable legal framework.

652. Section 3 of Presidential Decree 1969/93[219] whereby the Exploration Permit on the Chihuidos Area was awarded and that led to the Exploitation Concession of Sierra Chata granted by Presidential Decree 824/95[220] establishes that

> "[…] shall own and freely dispose of hydrocarbons… in accordance with the provisions of Section 6 of Law No. 17,319, Section 15 of Presidential Decree No. 1055/89 dated 10 October 1989, Section 4 of Presidential Decree No. 1212/89 dated 8 November 1989, Sections 5 and 6 of Presidential Decree No. 1589/89 dated 27 December 1989 and Section 5 of Presidential Decree No. 2411 dated 12 November 1991."[221]

653. Even if it was true (which is not) that the Gas Law only governs natural gas exports Section 3 establishes that natural gas exports shall be authorized "to the extent domestic supply is not adversely affected."

654. Additionally, the rules that set the procedure to obtain natural gas export permits also give priority to the domestic market supply. Resolution SE 299/98 establishes that "export permits… shall be awarded provided that domestic supply is not adversely affected. Additionally, according to Resolution SE 131/01 "Section 3 of Law 24,076 establishes that natural gas export permits are subject to the domestic market supply."

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[218] Mata Report, *supra* (n 129) ¶ 299.
[219] Presidential Decree 1969/93 (Exhibit AR-75).
[220] Presidential Decree 824/95 (Exhibit C-95).
[221] Presidential Decree 2411/91 (Exhibit AR-75).

655. The principle of free availability of hydrocarbons established by the Deregulation Decrees and the Conversion Decree is a relative principle which is contingent upon the self-sufficiency of the domestic market.

656. The Claimants' argument that pursuant to Section 6 of Presidential Decree 1589/89, the Argentine Republic must pay compensation for imposing restrictions on natural gas exports can be rejected *in limine*, since the Claimants expressly hold that they do not base their damage calculation on that piece of legislation. In any case, the interpretation of MEDA and MASA of the rules on which they base their claim is wrong and aims at confusing the Tribunal.

657. Presidential Decree 1589/89 cannot grant rights broader than those granted by the Hydrocarbons Law as it implements such law. Section 6 of Presidential Decree 1589/89 expressly refers to the Hydrocarbons Law.

658. The importance of hydrocarbons to public interest is such that the Argentine Constitution itself prescribes that productive activities shall meet present needs without endangering those of future generations and the Argentine authorities shall provide for the rational use of natural resources and the preservation of the natural heritage.

659. In conclusion, the measures adopted by the Argentine Republic to defend the natural gas domestic supply are within the legal framework applicable to the MEDA and MASA concessions and were reasonably established in line with the principles set in that legal framework.

660. Resolution 140/96[222] whereby the natural gas export permit was awarded to the Sierra Chata Consortium is contingent upon and subject to the domestic market supply in

[222] Resolution 140/96, (Exhibit AR-81).

conformity with the applicable legal framework.

661. In fact, Section 1 of Resolution 140/96 awarded a natural gas export permit "for up to a firm volume of two million and five hundred thousand cubic meters per day (2,500,000m3/day) for a term no longer than fifteen (15) years *or until the volume of the remaining certified reserves was reached, calculated in accordance with Section 2 of this Resolution.*"

662. Additionally, Section 2 of Resolution 140/96 sets forth that "to calculate the remaining certified reserves… *the total volume of natural gas certified reserves* dated December 27, 1995 filed by the exporting consortium, i.e. seventeen thousand and thirty millions of cubic meters (17.030.000.000 m3) *should be subtracted from the natural gas volume actually delivered to the Distributor MetroGas S.A. in the domestic market at the beginning of the exports, as well as the volume to be delivered in the future* as per the local undertakings."

663. Moreover, Section 4 of Resolution 140/96 establishes that the total volume of gas authorized to be exported "will be annually adjusted in line with the volume actually exported and the volume actually delivered to the domestic market."

664. Experts Sandleris and Schargrodsky when explaining the characteristics of the Sierra Chata Permit state that:

> "This calculation method used to establish the amount authorised for export includes three key elements that define the permit:
>
> a) the basis on which the scope of the permit is established; that is, the authorised stock, is defined by the statement of reserves made by the company itself;
>
> b) the gas to be supplied to the domestic market (distribution company Metrogas) must be deducted from such amount, taking the volume of gas that had already been delivered at the commencement of exports as well as the gas to be sold in the future;

> c) the total gas volume that the consortium may export is not fixed and established by the Resolution; it is adjusted every year and depends on the reserves and on the gas sold in the domestic market."[223]

665. That is to say, the methodology used to calculate the total volume of natural gas authorized to be exported under the Sierra Chata Permit shows that it is not fixed and is subject to the domestic market.

666. To be awarded a natural gas export permit, one of the requirements that companies shall fulfil is the filing of a certificate of the reserves and the contracts with those requesting the exports

667. In that context, the Argentine Secretariat of Energy requested to the members of the Sierra Chata Consortium, among other information, "b) *the certified volumes of gas reserves, proved, developed and to be developed in the future on the Sierra Chata field…*; c) local undertakings in force to deliver gas for the next twenty years."

668. When hydrocarbon concessionaires obtain an export permit, they also agree to perform investments pursuant to Section 31 of the Hydrocarbons Law. Therefore, failure to make such investments could cause all or part of the reserves authorized to be exported to be inexistent.

669. When in the process of obtaining the export permit, the Sierra Chata Consortium filed an audit report of the reserves conducted by Gaffney, Cline & Associates Inc. According to that report, at the time of requesting the export permit, the consortium reserves included "3.3 billion m3 of undeveloped proved reserves and 3.03 billion m3 of probable reserves."

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[223] UTDT Second Report, *supra* (n 135) ¶ 131.

670. MEDA and MASA, as any other hydrocarbon producer in Argentina, knew that in the event of shortage of hydrocarbons to satisfy the needs of both the domestic market and exports, the legal framework applicable to the production of natural gas set forth that the Sierra Chata Export Permit was contingent upon the domestic market supply. This arises from Sections 3 and 6 of the Hydrocarbons Law and Section 3 of the Gas Law.

671. The Sierra Chata Export Permit is not an absolute right that cannot be limited or regulated. The opposite, which is the position of the Claimants, would mean that the Argentine Secretariat of Energy (as enforcement authority of the Hydrocarbons Law) would be limited even when the key requirement that led to the permit was no longer fulfilled, i.e. non-impairment of the domestic market.

672. The "firm and non-interruptible service" concept comes out of the Rules of Transportation and Distribution of Natural Gas, which states that as a matter of fact, the firm service may be interrupted in case of "emergency or *Force Majeure* events." This also proves that restrictions on natural gas exports – including "firm" export volumes – were and are legitimate in the event of lack of gas in the domestic market.

673. Additionally, the preference for the domestic supply cannot be limited only to the "time of the award" since permanent controls must be made to check that the domestic market is not being affected and that investments by producers- exporters of hydrocarbons (like MEDA and MASA) are being made.

674. The report of Sproule International Limited (hereinafter, the "**Sproule Report**") filed by the Claimants shows that the impairment analysis of supply must be made while the Sierra Chata Export Permit is effective and not just at the time the permit is awarded.

675. In fact, the Sproule Report when trying to justify the decline in reserves and production of the Claimants states that "reserves can be adjusted up or down" and that

they "change from one period to another not only due to production but also to technical and economic factors, such as technical revisions, acquisitions and dispositions, drilling, and economic factors."[224]

676. Then, if hydrocarbon reserves may vary from one year to the following due to different circumstances (involving producers or otherwise) as mentioned in the Sproule Report, it is logical and reasonable that the Argentine Secretariat of Energy (as enforcement authority of the Hydrocarbons Law) performs permanent and on going controls so that exports from the Sierra Chata concession do not affect self-sufficiency. Therefore, the argument of the Claimants that the Argentine Government must assess the domestic market supply at the time of awarding export permits is false and contradicts their own experts' reports.

677. In conclusion, the Sierra Chata Permit is contingent upon and subject to the non-impairment of domestic supply and compliance with certain investments.

678. On the basis of a cost study performed by the Argentine Secretariat of Energy that no hydrocarbon producer objected to, the First Gas Agreement was executed on 2 April 2004 by means of which a certain volume of gas was guaranteed for the domestic market. In other words, through the First Agreement, hydrocarbon producers voluntarily agreed to deliver certain volume of natural gas in exchange for the adjustment of the natural gas price.

679. In relation to the Second Gas Agreement, Energy Secretary Cameron explains that:

> The Agreement for the 2007-2011 period was entered into by most producers, who represent 90% of the natural gas production in Argentina. Among the signing producers are Petrobras and Total

[224] Sproule Report, *supra* (n 209) ¶¶ 98-99.

Austral, Claimant's partners in Sierra Chata. YPF, Tecpetrol and CGC, MASA's partners in Aguaragüe also signed the agreement.[225]

680. Any non-signatory producer (like the Claimants) may adhere to the agreement at any time and any signatory producer to the agreement may terminate its participation during the term of the Second Gas Agreement.

681. As expert Greco states, "even though Distribution Companies, as regulated utilities, are under a duty to supply users within the Licence area, this is not inconsistent with the priority given to domestic market supply over exports, by which producers must abide."[226]

682. Lastly, the Claimants state that "the authorization to supply the domestic market with gas, substitutes was illusory for at least three reasons: (i) the cost of gas substitutes was higher than the export price of gas; (ii) logistical constraints; and (iii) it was impracticable for carrying out significant long-term export contracts." The argument of the Claimants is wrong for several reasons.

683. First, pursuant to Resolution SE 659/04,[227] Disposition SSC 27/04[228] and Resolution SE752/05[229] upon requests for additional injection of gas made by the Argentine Secretariat of Energy originated by the shortage of such fuel in the domestic market, all hydrocarbon producers can choose to substitute the amount of natural gas requested with some equivalent energy source (mechanism called energy swap).

684. Second, the assertion of the Claimants and witness Valle that "to exercise the option of sending gas substitutes to the domestic market instead of their export volumes"

[225] Cameron Witness Statement, *supra* (n 107) ¶ 60.
[226] Greco Second Report, *supra* (n 139) ¶ 62.
[227] Resolution 659/03, Annex I, Section 15 (Exhibit AR-196).
[228] Decision SCC 27/04 (Exhibit AR-189).
[229] Resolution SE 725/05 (Exhibit AR-205).

would have led to "greater" loss or would have broken even only "if the customers agreed to share the incremental costs" is false (Rejoinder of the Argentine Republic ¶ 323).

685. According to the contract addenda, Chilean purchasers bore "all costs that Sellers [Sierra Chata producers Consortium] may incur in as a result of a proposal by Purchaser to Substitute natural gas or other equivalent sources of energy…" In other words, at doing a swap, its cost did not lead to economic restraints (Rejoinder of the Argentine Republic ¶ 324).

686. Third, there were no logistic constraints. Apart from being able to import alternative fuels, the Claimants produce and market hydrocarbons that are natural gas substitutes. In fact, a company of the same economic group as MEDA and MASA, ESSO Petrolera Argentina, has an oil refinery in the city of Campana, province of Buenos Aires, which produces fuel-oil and diesel

687. Lastly, the Claimants have many times requested to the Argentine Secretariat of Energy the swap, with equivalent sources of energy, the requests for additional injection of natural gas for the domestic market. This was acknowledged by witness Valle in her supplementary statement who asserted the Claimants "performed several energy substitutions with one of [our] Chilean costumers.[230]

688. The Energy Secretary explains that

> "These mechanisms have been widely used. As a matter of fact, MASA has used them more than once in relation to its contract for the provision of gas from Sierra Chata to its Chilean customers. The swaps requested and implemented by MASA were related to two thermal power plants: the San Nicolás Power Plant, where electric power can be

[230] Valle Supplementary Statement, *supra* (n 175) ¶ 29 (Exhibit C-512)

> generated through coal, fuel oil or natural gas, and the Puerto Power Plant, where swaps were linked to fuel oil equipment."[231].

689. To summarize, considering the problem of domestic market supply, the Argentine Secretariat of Energy summoned a meeting of hydrocarbon producers and voluntary agreements were executed that guaranteed sufficient volumes of natural gas supply. It is worth mentioning that the practice of executing agreements with private companies was followed by the United States government so that the different economic sectors could be in line with the circumstances resulting from the current international financial crisis.

3. The Tribunal' Analysis

690. The Tribunal has above under the heading "Applicable Regulatory Framework" (VI.B) held that the Deregulation Decrees enjoy legislative status and prevail over the Hydrocarbons Law passed in 1967 on the specific issues of gas prices and gas marketing. Moreover, the Tribunal has under the heading "Applicable Regulatory Framework" (VII) held that the Gas Law and not the Hydrocarbons Law regulates the marketing and the export of natural gas. Article 3 of the Gas Law, which is under the heading "Export and Import of Natural Gas", provides *inter alia*:

> "Natural gas exports must be approved in each case by the National Executive Power within a period of 90 days following the receipt of a request, provided that the domestic supply is not affected."

691. Thus, Article 3 of the Gas Law requires that export authorizations do not affect domestic supply. Dr. Martelli said at the oral hearing: "Once this Permit was granted, it was firm in the sense that it was an export commitment that was irrevocable and continuous under the volumes that were contracted and not the other volumes that

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[231] Cameron Witness Statement, *supra* (n 107) ¶ 90.

were subject of the possibility of being interrupted."[232] The Gas Law does not subject the continuity of a firm export permit to later events.[233] Dr. Bianchi said on cross examination that the analysis whether the requested export affects domestic supply is made "upon granting the authorization."[234] Also Article 12 of Resolution SE 299/98 (Natural Gas) provides after having referred to the 5-year policy review to be carried out by the SE: "In any case, the legal continuity of the export permits granted as of that date will not be affected."[235] The same principle is also adopted in Article 2 of the Chile-Argentina Energy Treaty, which confirms that any analysis on impact on domestic supply is performed at the time the export authorization is granted.[236] This also supports the view that any analysis of impact on domestic supply is performed at the time export authorisation is issued.

692. The fact that volumes of natural gas exported as excess amounts, i.e. exceeding the daily amount pursuant to Section 6 of the Sierra Chata Permit (Resolution 140/96), shall be counted as part of the total volume authorised to be exported hereby does not allow any other conclusion as to the meaning of the notion "firm".

693. From the Decree 1738/92 Annex I, Article 3(5), as amended by Decree 951/95, it can be seen that "firm volumes" are those that cannot be interrupted once their export has been approved by the export authorization and that "excess volumes" are those that may be interrupted if there are domestic supply difficulties.[237] Article 3(5) of the Article provides:

> "The authorization issued by the Executive power may provide for the export of excess Gas to the extent established therein, provided that

[232] Transcript in English, Day 5, p. 936.
[233] See Bianchi, Transcript in English Day 6, p. 1304-1305.
[234] Transcript in English, Day 6, p. 1299.
[235] Art. 12 (Exhibit C-36).
[236] Art. 2 (Exhibit C-89).
[237] Decree 951/95 (Exhibit C-31).

> said exports are subject to interruption if there are domestic supply difficulties. In this case, it is not required to obtain an approval for each excess gas export in the authorization; exporters will only be required to file with the Gas Regulator, for information purposes, the corresponding contracts, the corresponding contract including the interruptibility condition and the lack of compensation if such interruption occurs."

694. Also the Sierra Chata export authorization confirms the difference between "firm volumes" and "excess volumes". It authorizes in Article 1 the export of up to a specific quantity of firm volume of natural gas for a maximum of 15 years and of natural gas in excess of the quantity mentioned in the same Article, subject to the latter volume being interruptible for the needs of domestic supply.[238]

695. Argentina asserts that the term "firm" refers to a type of transportation service that may be interrupted whenever required for emergency or *force majeur* reasons and refers to the Gas Regulatory Decree, Annex I, Section 1 and Presidential Decree No. 2255/92, Annex A, Sub-Annex II, Section 2(p). It is, however established that "firm transportation" and "firm volumes" are different concepts.[239] Also Argentina's expert Mr. Nobilia said that an export permit which was granted when he acted as Chief Legal Counsel of YPF specifically distinguishes firm export volumes from firm transportation service as two distinct concepts.[240]

696. Moreover, Article 3 of the Chile-Argentina Energy Treaty provides in Article 3:

> "The parties guarantee the elimination of all legal, regulatory, and administrative restrictions on the export and transportation of any such natural gas that Argentine sellers agree to supply to Chile."

697. The Claimants' witness Mrs. Valle said at the hearing that the Claimants received up to three re-routing orders during the same day that included different volumes, often

[238] Resolution 140/96 (Exhibit C-628).
[239] See Bianchi, Transcript in English, Day 6 p. 1304-1305.
[240] Transcript in English, Day 7 p.1568.

notified informally (for instance by telephone) and without disclosing the recipient of the re-routed volumes. The Claimants were forced to breach their existing export contracts to deliver gas volumes to “anonymous” users with whom they had no contractual relationship. When the re-routing orders came, the Claimants were not told where the gas was going and was therefore for a long period of time, sometimes five or six months, unable to invoice the purchaser. The identified user said that the Claimants had not been the ones who had delivered gas to the user. The user failed to recognise the price or the user was waiting for a Government agency to confirm the price and the volume and the financial impact was substantial. Moreover, Mrs Valle said that as a result of the export curtailment and the Export Withholdings Mobil's export business in Argentina disappeared actually.[241] This testimony of Mrs. Valle has not been disputed by Argentina.

698. Mrs. Valles's witness statement also confirms that the Claimants did not sign the First Gas Agreement (2004) because this would have put them into breach of their existing export contracts, and because, in any event, the Claimants' supplies to the domestic market at the time covered the volumes under the “agreement.”[242] Moreover, Mrs. Valles's witness statement confirms that the Claimants refused to enter into the Second Gas Agreement for the same reason and also because doing so would be deemed a waiver of its vested rights to freely market its natural gas. Moreover, Mrs Valle said at the oral hearing that the Claimants were more impacted by the Second Gas Agreement than many other producers because the requested unreal volumes and since the volume of the non-signers were rerouted first and to the lower price users. [243] It is undisputed that the GOA applied both Gas Agreements to the Claimants. Pursuant to Resolution SE 599/07 signing producers are only required to

[241] Transcript in English, Day 4 p.730-736.
[242] Transcript in English, Day 4 p. 787-788.
[243] Transcript in English, Day 4 p. 736.

supply additional volumes once all the export volumes of the non-signing producers have been rerouted. [244] The Tribunal finds it established that the Claimants' rights to export authorized volumes of natural gas under the Sierra Chata concession have been severely impaired since a considerable part of firm export volumes from MASA's Sierra Chata Gas Production were re-routed to the domestic market.

699. The Tribunal finds it established that the Claimants' firm rights to export the volumes authorized under the Sierra Chata Gas Permit were severely impaired by numerous measures adopted since 2004. These measures prevented the Claimants from exporting gas from the Sierra Chata block and imposed re-routing obligations to the domestic market. The GOA did not condition the Sierra Chata Export Permit on the maintenance of a certain level of reserves.

D. Export Withholdings

1. The Claimants' position

700. Decree 1589/89, one of the Deregulation Decrees, provided in Article 3 that the export and import of hydrocarbons and their byproducts would be exempt from any present or *future* tariffs, duties, or withholdings.[245] In addition, the GOA granted safeguards against discriminatory or specific taxes.[246] Through Decree 1969/93, the GOA included both of these protections in the Sierra Chata Concession.[247] These were fundamental rules of the program to deregulate the oil and gas industry and were a major reason why the Claimants and other foreign investors had an overwhelmingly positive response to privatization. As explained by Professor Bianchi, the protections

[244] Art. 9 and 10 of Resolution 599/07 (Exhibit C-75).
[245] Art. 3 (Exhibit C-15).
[246] Plan Argentina, Art. 8, C-27. See also Conversion Decree, Art. 9 (Exhibit C-28).
[247] Decree 1969/69, Arts. 1, 6 (Exhibit C-94).

against the imposition of Export Withholdings under the Sierra Chata Concession qualify as tax stability provisions.[248]

701. Dr. Teijeiro, an expert in Argentine tax law, confirms that the mere imposition of Export Withholdings violates the tax stability guarantees that the Government gave through the Legal Framework and the Sierra Chata Concession.[249] Thus, when the Argentine Government began imposing Export Withholdings on gas in 2004, it did so in violation of its legal and contractual commitments to the Claimants. Other than a minor discrepancy over the effective rates resulting from the Government's calculation of Export Withholdings, there appears to be no dispute between the parties concerning whether, and at what rate, the Government imposed those measures.

702. By imposing Export Withholdings, the Argentine Government also violated its commitment to exempt the Claimants from specific and discriminatory taxes. Export Withholdings on natural gas were discriminatory because they vastly exceed the effective rate of export withholdings on crude oil by-products that compete with natural gas and the 5% export withholding rate for petrochemicals and fertilizers that use gas as a raw material. Dr. Teijeiro identifies three additional reasons why Export Withholdings constitute "specific" taxes and violate the prohibition on specific and discriminatory taxes.[250]

703. Thus, even leaving aside Argentina's specific commitment to exempt the Claimants from present and future Export Withholdings, the specific and discriminatory manner in which Argentina imposed those measures violated the Claimants' rights.

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[248] Third Legal Opinion by Alberto B. Bianchi, dated 22 April 2010 *[hereinafter "Bianchi Second Supplemental Opinion"*] ¶ 114 (Exhibit C-505).
[249] Legal Opinion of Guillermo O. Teijeiro Legal Opinion dated 23 April 2010 [hereinafter "*Teijeiro Legal Opinion"*] ¶ 6 (Exhibit C-509).
[250] Teijeiro Legal Opinion, *supra* (n 249) ¶ 23 (Exhibit C-609).

704. In 2002, the GOA completely disregarded these guarantees by enacting Law 25,561, which authorized the Executive Branch to impose export withholdings on hydrocarbons for a five-year period and authorized the Executive Branch to establish the respective applicable rates.[251] By virtue of Law 26,217, the GOA extended Export Withholdings through 2012.[252]

705. In May 2004, through Decree 645/04, Argentina imposed a 20% Export Withholding on the Claimants' gas exports, among other gaseous hydrocarbons.[253] In addition, it authorized the Ministry of Economy to modify the Export Withholding rate. At that time, the alleged purpose of Export Withholdings on gas was to align the tax treatment of gas with crude oil and byproducts.

706. In June 2006, Argentina and Bolivia entered into the Framework Agreement for the Sale of Gas and the Execution of Projects Concerning Energy Integration (the "**Framework Agreement**"). Under that Agreement, Argentina agreed to buy gas from Bolivia at US$ 5/MMBTU. This entailed a significant increase over the price Argentina had paid under a previous agreement with Bolivia (*i.e.*, US$ 3.18/MMBTU) and it was much higher than US$ 1.20/MMBTU, the average regulated price then paid to MASA and other Argentine producers.

707. The GOA decided to finance the import of the higher-priced Bolivian gas by further increasing the Export Withholding rate on domestic gas. Hence, in July 2006, the GOA (i) increased the Export Withholding rate for gas from 20% to 45%,[254] and (ii) arbitrarily modified the basis for calculating Export Withholdings; instead of calculating Export Withholdings based on the price that Argentine producers actually

[251] Art. 6, Law 25,561 (Exhibit C-41).
[252] Exhibit C-69.
[253] Art. 2 (Exhibit C-60).
[254] Decree 645/04 (Exhibit C-60).

received (*i.e.*, approximately US$ 1.65/MMBTU), Argentina began calculating the withholdings on the price at which it agreed to import gas from Bolivia (initially, US$ 5/MMBTU).[255]

708. These measures effectively increased Export Withholdings on gas to a flat rate of US$ 2.25/MMBTU (45% of US$ 5/MMBTU) and raised the effective Export Withholding rate more than 675%, which exceeded the average export price that Argentine gas exporters received from foreign customers by approximately 40%.[256] This amounts to 113% of the export price that the Claimants received and renders exporting gas unprofitable since all of the profit (and more) is taken by the GOA.[257]

709. Most recently, through Resolution MEP 127/08, the GOA once again (i) increased the applicable Export Withholding rate on gas (from 45% to 100%), and (ii) altered the basis on which it calculates Export Withholdings, disregarding the much lower export prices actually received by exporters such as MASA.[258] Instead of calculating Export Withholdings on the basis of the price at which MASA exports gas, the GOA uses artificial prices. Under Resolution MEP 534/06, the GOA calculated Export Withholdings based on the price at which it imports gas from Bolivia (currently US$ 10.30/MMBTU). Since early 2008, the GOA has calculated Export Withholdings on the highest prevailing rate for gas imports (during the winter of 2008, between US$ 14.5-17/MMBTU due to the import of LNG).[259]

710. Thus, Resolution MEP 127/08 entails a further increase of approximately 650% in the applicable Export Withholding rate. As a result, during the winter of 2008, export withholdings on gas exports in Argentina were approximately between US$ 14.5 and

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[255] Resolution MEP 534/06, Art. 1 (Exhibit C-71).
[256] Bastos Report, *supra* (n 57) ¶ 144 (Exhibit C-1).
[257] LECG Report, *supra* (n 22) ¶ 62 (Exhibit C-2).
[258] Resolution MEP 127/08 (Exhibit C-77). See also LECG Report ¶ 63 (Exhibit C-2).
[259] Resolution MEP 127/08, Art. 1 (Exhibit C-77).

17/MMBTU, that is between seven and eight times higher than the actual average export price they received by Argentine producers (around US$ 1.90/MMBTU). This equates to nearly 800% of the Claimants' export price.

711. This measure further aggravates the uncertainty and unpredictability of the Claimants' investment environment since the basis for calculating Export Withholdings has become dependent on future and uncertain events that have nothing to do with the Claimants' exports (such as changes in the purchase price of LNG).

712. In attempting to explain why it was imposing Export Withholdings, the GOA never settled on one rationale. The different reasons the GOA gave for Export Withholdings over time include the following:

- the alignment of the tax treatment of crude oil and its byproducts with gas;
- the need to consolidate the sustainability of the economic and fiscal plan; and
- the goal of capturing the allegedly extraordinary gains of the hydrocarbons business.

713. But as former Secretary Bastos notes, the motivation for these withholdings is political.[260]

714. The Claimants were not able to pass through Export Withholdings to their Chilean customers in the Sierra Chata field from June 2004 to July 2005, and although they are currently able to pass through Export Withholdings, there is no certainty that they

[260] Bastos Report, *supra* (n 57) ¶¶ 144-145.

will be able to do so in the future.[261] These measures also caused damage to the Claimants' investments by increasing royalty rates. In addition, as Ms. Valle notes, these developments had a negative impact on the Claimants' relationships with their Chilean customers.[262]

715. The Export Withholdings on gas violate the Chile-Argentina Energy Treaty, which prohibits discriminatory treatment of gas exports by Argentina.

716. Under Article 9 of the Chile-Argentina Energy Treaty, the tax treatment for gas exports may not exceed either the tax treatment for exports of petroleum products or the tax treatment for products that use gas as a raw material.[263] Even without taking into account their calculation based on a grossly exaggerated reference price, the Export Withholdings imposed on gas grossly exceed the 5% export withholding rate for petrochemicals and fertilizers that use gas as a raw material. They also significantly exceed the current 31.03% effective rate of Export Withholdings on crude oil.

717. This discriminatory treatment violates the plain requirement of the Chile- Argentina Energy Treaty and is contrary to the GOA's own statements in the decree that imposed the 20% Export Withholdings.

718. Despite the straightforward nature of the Claimants' Export Withholdings claim, Argentina seeks to justify those measures by arguing that Article 6 of the Sierra Chata Concession specifically subjected the Claimants to the general tax regime. In doing so, Argentina conveniently fails to include the full text of this provision, which expressly excludes "provisions that levy specifically or discriminatorily the person,

[261] LECG Report, *supra* (n 22) ¶ 64 (Exhibit C-2).
[262] Valle Witness Statement, *supra* (n 34) ¶¶ 81-82 and 84 (Exhibit C-4).
[263] Art. 9 (Exhibit C-89).

legal status, or activity of the permit or concession holder or the assets assigned to the respective works." When read in context, it becomes clear that Article 6 of the Sierra Chata Concession limits the application of general taxation legislation with respect to specific or discriminatory taxes.

719. In addition, reference to the general tax legislation does not bar the exemption from Export Withholdings established by Article 3 of Decree 1589/89, because the Sierra Chata Concession incorporates both types of protection. As explained by Professor Bianchi, Argentina's denial of limitations to the applicability of the general tax legislation entails the unacceptable proposition that there is a flagrant contradiction between Articles 2 and 6 of Decree 1969/93, which set forth the terms of the Sierra Chata Concession.

720. If taken to its logical conclusion, Argentina's proposition that the Claimants are subject to the general tax legislation despite receiving specific tax stability commitments would lead to the unacceptable conclusion that the Sierra Chata Concession included a protection that was ineffective *ab initio*. If the Argentine Government had the ability, as it now contends, to disregard or revoke these guarantees—which were granted throughout the full term of the concession—when problems arose, that would entail the unacceptable conclusion that the guarantees and promises made by the Argentine Government were devoid of any legal significance and were merely illusory

721. The Sierra Chata Concession created vested legal and contractual rights, as well as legitimate expectations for investments made in reliance on them. It follows that, even under Argentine law, the Argentine Government cannot unilaterally amend those rights, which were designed to induce investment, without paying compensation.

722. Argentina wrongly portrays the Claimants' claim regarding Export Withholdings as a challenge to its sovereign authority to amend its regulations. In support of this

contention, Argentina relies on the Argentine Supreme Court for the proposition that no one has a vested right to the maintenance of a certain regime. But none of the cases that Argentina cites involved tax exemptions that the Government granted through contracts or concessions. Rather, the claims in those cases were based on unilateral tax or other incentive measures. In making this argument, Argentina ignores that the Argentine Supreme Court has consistently held that, when an individual has fulfilled all substantial acts, conditions, and formal requirements under the provisions of a specific regulation, that individual has a vested right that the Government cannot abrogate through new legislation without violating the protection of property recognized by Article 17 of the National Constitution.[264]

723. Argentina also tries to justify its imposition of Export Withholdings by arguing that the exemption from those measures contained in Article 3 of Decree 1589/89 is a "privilege and therefore, is only temporary." The Argentine Government argues that it is unreasonable that such a provision could grant rights *ad infinitum*. Contrary to Argentina's position, through the exemption from Export Withholdings contained in the Sierra Chata Concession the Government created a vested right.[265] As explained by Professor Bianchi, even if *ad arguendo* the exemption established in Article 3 of Decree 1589/89 could be categorized as a privilege granted in accordance with Article 75(18) of the Argentine Constitution, it does not follow that the Government could simply remove that exemption without consequence. The Argentine Supreme Court has confirmed that tax exemptions constitute vested rights.[266] Thus, the Claimants are not claiming that Argentina cannot change its laws on Export Withholdings, but rather

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[264] Bianchi Legal Opinion, *supra* (n 100)¶¶ 156.170 (Exhibit C-3).

[265] Bianchi Legal Opinion ¶¶ 156-170 (Exhibit C-3), Teijeiro Legal Opinion, *supra* (n 249) ¶ 146 (Exhibit C-605).

[266] Bianchi Second Supplemental Opinion, *supra* (n 248) ¶ 146 (Exhibit C-505).

that it must respect the Claimants' vested legal and contractual right to be exempted from Export Withholdings or else pay compensation for failing to do so.

724. Argentina further argues that the Claimants could not expect to be exempt from Export Withholdings since the Government imposed withholdings on all exports as a general measure. Even if Argentina had treated all other exports the same as it treated gas, which it did not, that fact would not justify its repudiation of the Claimants' rights. First, unlike hydrocarbons, most goods had no protection against export withholdings. Second, the Government must respect the export withholding exemptions that it granted to specific goods even after the "general" imposition of export withholdings.[267] It follows that Argentina's attempt to justify export withholdings as a general measure fails as a matter of fact, as well as law.

725. Argentina argues that, under the Hydrocarbons Law, the Argentine Government is entitled to fix prices and quotas for hydrocarbon exports; thus, it concludes that the Argentine Government can also use export withholdings to reduce local prices. This argument fails to recognise that the Hydrocarbons Law only empowers the Government to fix crude oil prices, not those of natural gas; the Gas Law governs natural gas marketing and pricing. [268] Argentina also argues that the Hydrocarbons Law authorizes the Executive to establish subsidies or withholdings on exports if international prices increase or decrease substantially.

726. In addition, Argentina's logic that the power to impose export quotas entails the power to impose export withholdings is flawed from an economic standpoint. Export quotas and export withholdings are not interchangeable. Export quotas, which allow

[267] This is the case with forestry products, Law 25,080 (Exhibit C-524). See also Martelli Legal Opinion, *supra* (n 141) ¶¶ 209, 211-212 (Exhibit C-5080).
[268] Gas Law, Art. 83 (Exhibit C-31), Decree 2731/3 (Exhibit C-34). See also Martelli Legal Opinion, *supra* (n 141) ¶ 43 (Exhibit C-508).

producers to continue to collect the international prices for the gas that they do export, do not have the same effect on a gas producer as export withholdings, which effectively allow producers to collect only a reduced price, since they are supposed to be taxed on the prices producers actually receive. Thus Argentina is wrong to assert that its power under the Hydrocarbons Law to impose export quotas includes the power to impose export withholdings.

727. In any event, Decree 1589/89 (given its legislative status) supplemented and superseded Article 6 of the Hydrocarbons Law and effectively limited the scope of the Argentine Government's regulatory authority. That decree distinguishes between export quotas and export duties by providing specific guarantees with respect to each: Article 3 of Decree 1589/89 prohibits the imposition of Export Withholdings, while Article 6 of Decree 1589/89 protects (via compensation for price differentials) against the imposition of export restrictions and quotas.[269]

728. By providing that it could not impose export restrictions without paying compensation, the Argentine Government effectively restricted the scope of its regulatory authority and created legitimate expectations for investors.[270] Article 3 of Decree 1589/89 expressly prohibits "present" and "future" export withholdings in furtherance of both that law's objectives to promote production and the policies set forth by the Law of State Reform to deregulate the sector. Thus, neither the Executive nor the Energy Secretariat can, through implementing regulations (which do not enjoy legislative status) contravene the provisions of the Deregulation Decrees.

729. Argentina argues that the Claimants "erroneously claim that discriminatory treatment took place because the exports of crude oil and petrochemical products and fertilizers

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[269] Arts. 3, 6 (Exhibit C-15).
[270] Arts. 3, 6 (Exhibit C-15); Decree 1212/89, Art. 6 (Exhibit C-14).

using gas as raw material are subject to a lower rate than that imposed on natural gas exports." By pointing out that Argentina violated the provisions of the Chile-Argentina Energy Treaty through its discriminatory taxation measures, the Claimants are not "trying to harmonize the tax regime of Argentine exports". Rather, the Claimants are simply observing that, by imposing Export Withholdings, Argentina violated a treaty obligation that coincides with Argentina's domestic legal and contractual commitment to exempt the Claimants from discriminatory taxes.

730. Article 9 of the Chile-Argentina Energy Treaty provides that the Government cannot levy taxes on natural gas exports at a rate that is higher than the tax rate applying to the exports of crude oil byproducts or products that use gas as a raw material. Even without taking into account that the Argentine Government calculates Export Withholdings on a grossly exaggerated reference price, the Export Withholdings imposed on gas grossly exceed the 5% export withholding rate for petrochemicals and fertilizers that use gas as a raw material. They also significantly exceed the current 52% effective rate of Export Withholdings on crude oil byproducts. This is exactly the kind of distortion that the Chile-Argentina Energy Treaty and the Claimants' legal and contractual rights were aimed at preventing.

2. Argentina's position

731. The Claimants have not suffered the damages they allege in their Claim Memorial due to the hydrocarbon export withholding established by the Argentine Republic. They have passed through their value to the Chilean buyers. Consequently, the claim associated with damages as a result of export withholding must be dismissed.

732. In the amendments to the gas export contracts between the Producer Consortium of Sierra Chata and their Chilean customers (Metrogas and AES Gener) it is expressly

established that "the prices mentioned in items 1 and 2 include the export duties for the period from January 1, 2005 to December 31, 2006."[271]

733. As explained by experts Sandleris and Schargrodsky:

> "Claimants passed through the export tax to their Chilean customers as from January 2005, and not as from May 2005 as they claim. This is evidenced by point 3.1 of the addenda: "Point 3.1. The prices mentioned in points 1 and 2 include the export duties for the period between 1/1/2005 and 12/31/2006 […]." Points 1 and 2 referred to prices of around USD 1.90 MMBTU for the period between 1/1/05 and 4/30/05, USD 1.95 MMBTU between 5/1/05 and 9/30/05, USD 1.975 between 10/1/05 and 4/30/06 and USD 2 MMBTU between 5/1/06 and 12/31/06. MASA and MEDA, instead, argue that "From June 2004 through April 2005, Claimants were unable to pass through export taxes to their Sierra Chata Chilean customers[…]."The claim for export taxes between January and April 2005 is inadmissible."[272]

734. This means that since January 2005 up to the present moment, the Claimants have passed through the export duties to their Chilean customers and have therefore suffered no damages.

735. To make it very clear: from the foregoing it arises that the only (alleged) damage suffered by the Claimants is the application of an export duty of 20% during the six-month period (between July and December 2004) which, besides, only implies an actual value of 16%.

736. In fact, the Claimants acknowledge that during the period they could not pass through the export duties to their Chilean customers, the export duty "meant an effective rate of 16.67% since the amount of the Export Withholdings was deducted from the sales price."

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[271] *Addendum to the Sale and Purchase of Natural Gas Agreement between AES Gener S.A., Metrogas S.A. and the Consortium of Sierra Chata producers*, 26 April 2005, item 3.1 (Exhibit RA- 204); *see also* Greco Report, *supra* (n 125) ¶ 106.
[272] UTDT Report, *supra* (n 156) ¶ 151.

737. Therefore, the description above could never be construed as an expropriation on the part of the Argentine Republic in violation of its obligations pursuant to the BIT.

738. Furthermore, new contract addenda show that Chilean purchasers have reimbursed 100% of the export duties to the present.[273]

739. In addition, the reimbursement of export duties was not at all a new fact; actually the Claimants had, from the beginning of the business relationship[274]with the Chilean companies, contractual rights for these to bear any possible future taxes. This was recognized by Chilean counterparties in all the contract addenda.[275]

740. Moreover, Chilean purchasers reimbursed export duties even for the second half of 2004 (a period regarding which, in the Counter-Memorial, it was assumed that the Claimants had been unable to transfer the export duties). Hence, it would seem that the Claimants were reimbursed by absolutely all amounts paid as export duties. In fact, only this arises from the evidence submitted in the arbitration, which means that these claims raised by the Claimants constitute an abuse.

741. Finally, export duties were not applied on a differentiated or specific basis to the Claimants, on the contrary, apart from hydrocarbons, they were applied to a large

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[273] Contract addendum of 26 September 2006, Sections 2, 3, 4, 5, 6; Contract addendum of 31 January 2007, Section 2.1; Contract addendum of 1 July 2008, Section 1. *In*: File 750-003106/94 of the Natural Gas Export Authorization concerning the Sierra Chata field (Exhibit AR-306).

[274] *Natural Gas Export Agreement with Metrogas SA and Chilgener SA*, 23 October 1996, Section A.15: Taxes: the Purchasers shall be responsible for all taxes, levies, royalties and other charges applicable downstream from such interconnection point at Tratayen in the Neuquina Basin and all import duties applicable to the Natural Gas." The interconnection point at Tratayen is located within the Argentine Republic, in the province of Neuquén, a few miles away from the Sierra Chata field (Exhibit C-100).

[275] Contract addendum of 26 September 2006, recital 3; Contract addendum of 31 January 2007, Section 2.1. *In*: File 750-003106/94 of the Natural Gas Export Authorization concerning the Sierra Chata field (Exhibit AR-306).

number of commodities and manufactured products from the industrial and farming sectors. In this sense, Ratti indicates that:

> "[T]he Argentine Ministry of Economy fixed export duties for several products, including foodstuffs, such as fish, dairy products, eggs, honey, vegetables, edible fruits, coffee, tea, yerba mate, spices, etc.; industrial or medicinal plants, tobacco, salt, sulphur, plants and flowers, roots, soil and rocks, plaster, lime and cement, metalliferous minerals, slag and ashes, fertilizers, rubber and its by-products, wool, cotton, etc". [276]

742. Furthermore, Dr. Mata states that export duties applied to the Claimants "were the result of the ordinary exercise of powers by the State, were general, were not addressed to a specific operator of the activity, and there was no discrimination among the actors of the sector that were in the same situation.[277]

743. The Argentine Republic did not execute any tax stabilization agreement for the Claimants and the Chihuidos Concession was not included in an export withholding tax exemption, but on the contrary, it was expressly stated that "[t]he holders of Export Permits shall be subject to the general tax legislation that may apply."[278]

744. Furthermore, the rule specific to the business of export of natural gas produced in the Sierra Chata lot (Export Resolution 140/96) does not provide for personal exemptions. [279]As set forth in the tax legislation, exemptions are not presumed and a positive act granting them must exist.[280]

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[276] Witness Statement by Eduardo A. Ratti dated 19 November 2009 [hereinafter *"Ratti Witness Statement"*] ¶ 23.
[277] Mata Report, *supra* (n 129) ¶ 139.
[278] Decree 1969/93, Art. 6 (Exhibit RA-75).
[279] Resolution SO y SP 140/96 (Exhibit AR-81).
[280] Law No. 23,771, Section 4 (Exhibit AR-272); Resolutions DGI 4206/96 and 4191/96 (Exhibit AR-284).

745. In this respect, Dr. Mata explains that concessions to the Claimants are subject to the general tax legislation "and considering that the export withholdings are clearly taxes, it may be concluded that the "withholdings" are also included in the "general legislation" and, therefore, may be subject to such modifications as may be determined by the lawmaker…"[281]

746. The Argentine Government never waived the possibility of modifying rules or its tariff policy. Exemptions granted, on which the Claimants base their (alleged) right did not imply any waiver on the part of the Argentine Republic to exercise its tax authority (a feature of Nation Sovereignty) and to modify such rules.

747. There is no impediment for a subsequent rule of the same or higher level to modify the regulation of this issue in a reasonable manner. It is not a right vested *ad infinitum* but an applicable legal regime that can (obviously) be modified, like in any other legal system in the world.

748. The Claimants arguments related to exemptions show a clear oversight of the basic principles of general law, and of the rules that govern exemptions, in particular. Their stance implies maintaining inflexible tax clauses that would ban the legislator from levying certain taxable situations, creating a (groundless) privilege for certain companies, *ad infinitum.* The legislator is entitled to establish taxes and to modify them, both to obtain funds for the treasury and to comply, by means of said tool, with other purposes pursued by the Government. In this context, they are also entitled to establish exemptions or tax reliefs.

749. The exemptions, in particular, are exceptions –or situations of *privilege* or *preference*– established by the legislators for economic or social reasons *that address*

[281] Mata Report, *supra* (n 129) ¶ 135.

the situation that a country is going through at a certain time. On the basis of the same reasons as those for which they are used as a temporary instrument that can be resorted to by the legislator in a given situation, they may be modified at any time. They are exceptions from the obligation to pay and divert from the principles of generality and equality.

750. Although the Argentine Constitution empowers the legislator to grant privileges or exemptions in view of the country's prosperity, it expressly provides that they must be temporary. Furthermore, it is unreasonable to consider that a rule without a specific term should remain in force forever in the legal system.

751. It is a principle of Argentine law and of the law in general that *nobody is entitled to the maintenance of a particular legal regime.* The Claimants are not entitled to a crystallization of their right and they could not have any legitimate expectation that the regulation would never be modified.[282] In this regard, the Argentine Supreme Court has held that:

> "[N]obody has a vested right to the maintenance of the laws or the maintenance of the taxes created or exempted by them (Fallos: 288:279; 291:359; 299:93; 303:1835); and that the repeal of a tax exemption reaffirms the equality principle, which is the basis of tax and public burdens (Article 16 of the Argentine Constitution, final part) and obviously entails the legislator's intention that the tax be borne by the person benefitting from the exemption."[283]

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[282] *Parkerings-Companiet AS v Lithuania*, ICSID Case No ARB/05/08, Award (11 September 2007) [hereinafter "*Parkerings Award*"] ¶ 332 (LA AR-201); *see also EDF (Services) Limited v Romania* ICSID Case No ARB/05/13, Award (8 October 2009) [hereinafter "*EDF (Services) Award*"] ¶ 218 (Exhibit LA AR-190).

[283] Argentine Supreme Court of Justice, *Unola de Argentina Ltda v YPF y Banade s/ contrato de obra pública*, Fallos: 321:2683 (1998) (Exhibit LA AR-113).

752. The most important of the rules of the Regulatory Framework for the hydrocarbon sector, the Hydrocarbons Law, was not repealed. This law provides for the possibility of fixing prices and establishing hydrocarbon export quotas.[284]

753. Therefore, it is reasonable to conclude that export duties can be used to adjust domestic prices, which at the same time gives more freedom to companies. What is more, the Hydrocarbons Law provides that the Executive will allow exports to be made at "reasonable prices." If international prices happen to go up or down substantially, the Executive could very well provide for subsidies or export withholdings, respectively.

754. Lastly, neither Decree 824/95[285] granting a hydrocarbon exploitation concession on the Sierra Chata lot, nor SE Resolution 140/96[286] granting an authorization for export of gas volumes produced at that lot, provide for the alleged right to stability and to the exemption from the imposition of export duties relied upon by the Claimants.

755. In sum, the Argentine Republic never guaranteed tax stability to the Claimants and the Claimants do know that.

756. The Claimants maintain that "the Export Withholdings on gas violate the Chile-Argentina Energy Treaty, which prohibits discriminatory treatment of gas exports by Argentina."

757. Indeed, as acknowledged by the Claimants, the Economic Complementation Agreement between the Argentine Republic and the Republic of Chile acknowledges the power of the Argentine State to establish export withholdings on natural gas exports.

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284 Art. 6, ¶ 3 (Exhibit AR-1).
285 Decree 824/95 (Exhibit AR-78)
286 SE Resolution 140/96 (Exhibit AR-81).

758. Hence, it cannot be maintained that the Argentine Republic supposedly waived the right to establish hydrocarbon export duties, as the Claimants seem to allege in contradiction.

759. Even though the Claimants recognise that the Argentine Republic is authorized to establish withholdings on natural gas exports, they erroneously claim that a discriminatory treatment took place because the exports of crude oil and petrochemical products and fertilizers using gas as raw material are subject to a lower rate than that imposed on natural gas exports.

760. It is clear that this arbitration is not the appropriate venue for questioning the export duties imposed on crude oil exports or on the exports of petrochemical products and fertilizers. Furthermore, it is not the appropriate venue for trying to harmonize the tax regime of Argentine exports, especially when no losses have been sustained, insofar as, during the period in which they alleged to have been subject to "discriminatory treatment", the Claimants clearly carried over the export duties to their Chilean clients.

761. Nevertheless, Guichón points out that it "it should be underlined that the dispute settlement mechanisms provided for in the 2nd Additional Protocol were never used in connection with controversies relating to natural gas. Therefore, at no time were the parties declared to have committed a breach."[287]

762. Finally, it should be noted that the parties to Additional Protocol No. 2 are Argentina and Chile, and not the Claimants.

763. As a result of Argentina's worst ever social, economic and institutional crisis and the repeal of the convertibility regime, a massive devaluation of the local currency took

[287] Guichón Witness Statement, *supra* (n 149) ¶ 122.

place. In mid-2002, the Argentine peso plummeted by more than 200% as against the US Dollar and the fiscal deficit resulting from the recession and subsequent economic depression for more than 4 years was very serious. In that context, the Argentine Congress enacted the Emergency Law, which, among other things, establishes a series of export duties on broad sectors of the Argentine economy.

764. In addition to export duties on hydrocarbons (as set forth in Article 6 of the Emergency Law), other export duties on a large number of primary products and agricultural and industrial manufactures were established, with a view to generating tax revenues and reducing the impact of the currency devaluation on domestic prices.

765. Export duties on hydrocarbons were fixed at that time at values between 4% and 17%.[288] Two years later in 2004, with a view to according equal tax treatment to all hydrocarbons (because at the time the Claimants and the other gas exporters enjoyed a privileged situation), duties on the export of natural gas were imposed.[289]

766. As in the case of other sectors, the withholdings affected only a portion of the extraordinary windfall profits made by exporters as a result of the massive devaluation of the local currency. In addition, in the context in which they were adopted, the export withholdings made it possible to alleviate the inflation impact that the devaluation had on the prices of tradable goods. Along the same lines, Sandleris and Shargrodsky point out that:

> "The imposition of export taxes contributed to the two main objectives of economic policy in the post-crisis period: (i) to collect revenues directly from the sectors benefited by the devaluation, balancing fiscal accounts without repeating the contractionary tax policies that had led to the implosion of the economy in 2001; and (ii) to contain inflation reducing the impact of the devaluation on domestic prices, and

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[288] Decrees 310/02 (Exhibit AR-128) and 809/02 (Exhibit AR-145); *see also* Guichón Witness Statement, *supra* (n 149) ¶ 72.
[289] Decree 645/04, whereas clause 3 (Exhibit AR-139)

> preserving the benefits in terms of competitiveness of a high real exchange rate that encouraged import substitution and export growth."[290]

767. In the face of the considerable increase in the price of oil worldwide, hydrocarbon export duties were increased in what amounted to a proportional and appropriate economic policy. In May-September 2008, the crude oil price per barrel was USD 175. In that context, which was favourable to hydrocarbon production companies, the rate of the export duties applicable to prices above USD 45 was not increased.[291]

768. The increase of withholdings on natural gas exports as from 2006 was based on two reasons: on the one hand, the attempt to bring its tax treatment into line with the new value of withholdings on the rest of hydrocarbon products (around 45%), and, on the other, the dramatic increase in the price of gas that Argentina imports from Bolivia.[292]

769. Argentina is facing serious shortage issues due to the behaviour of many gas producers. In this context, there are basically two options: to find financing means in order to import Bolivian gas that satisfies a portion of the domestic demand, and to restrict exports. Certainly, it is unreasonable for the Claimants to expect that Argentina will not do anything about this, that it will not import gas and that it will allow all of the country's reserves to be exhausted at the same time.

3. The Tribunal's analysis

770. Article 3 (1) of Decree 1589/89 provides:

> "Concerning the export and import of hydrocarbons: The export and import of hydrocarbons and their byproducts is authorized and will be

[290] UTDT Report, *supra* (n 156) ¶ 187.
[291] MEP Resolution 394/07 (Exhibit AR-235).
[292] *See* MEP Resolution 534/06 (Exhibit AR-223); *see also El aumento sería de 62% para la Argentina*, CLARÍN, 7 January 2006 (Exhibit AR-219).

> exempt from any present or future tariffs, duties, or withholdings. It is also established that the export and import of hydrocarbons will not benefit from any present or future repayments or reimbursements and those existing will lapse as from the date the present Decree takes effect."

771. Moreover, Article 9 of Decree 2411/91 (the "**Conversion Decree**") provides:

> "The holders of the exploration permits or exploitation concessions shall be subject to applicable general tax legislation, but any provisions that may discriminatorily or specifically tax the person, legal status, or business of the permit or concession holder or the assets assigned to the respective tasks shall not be applicable."

772. Moreover Article 8 of Decree 2178/91 ("**Plan Argentina**") provides:

> "Since article 56, subsections c), and d) of Law 17319 is not applicable to hydrocarbon exploration permit holders and/or exploitation concessionaries, the shall be subject to the general laws on profit tax and shall be exempted from any provisions that may tax separately or specifically the person, their legal status, or activities, or the assets applied to the exploration or concession, or the tasks arising there from, including the disposal of the hydrocarbons produced."

773. Article 1 (1-2) and 6 (1) of Decree 1969/93 provide:

> "Article 1 -That the Memorandum of Understanding signed on March 18, 1993 between YPF SOCIEDAD ANÓNIMA, PETROLERA SANTA FE SOCIEDAD ANÓNIMA, SANTA FE ENERGY COMPANY OF ARGENTINA, INTERNATIONAL FINANCE CORPORATION, SOCIEDAD INTERNACIONAL PETROLERA SOCIEDAD ANÓNIMA, COMPAÑIA GENERAL DE COMBUSTIBLES SOCIEDAD ANÓNIMA, and B.H.P. PETROLEUM (ARGENTINA) INC., is hereby approved, a certified copy of which is made an integral part hereof as Annex I.
>
> As a result of the agreement reached and the provisions of Law No. 23,696, be Agreement No. 25,174 for the exploration and later exploitation of hydrocarbons in the CNQ-10 "CHIHUIDOS" Area, Province of Neuquén, which was approved by means of Decree No. 1573 dated November 3, 1988, converted into a hydrocarbon Exploration Permit, with the effect provided for in Law No. 17,319 and the modalities arising from Decrees No. 1055, dated October 10, 1989, No. 1212, dated November 8, 1989, No. 1589, dated December 27, 1989, and No. 2411, dated November 12, 1991 over the surface area covered by Agreement No. 25,174, identified ------

> Article 6 Permit holders shall be subject to the applicable general tax law. The provisions specifically levying taxes on the person, legal condition or activity of the Permit holder or the assets used to perform relevant activities shall not be applied."

774. Thus the exemption from any present or future tariffs, duties or withholdings provided for in Decree 1589/89 and the exemption from specific and discriminatory taxes provided for in Plan Argentina and the Conversion Decree were through Decree 1969/93 included in the Sierra Chata Concession. Therefore the Tribunal finds that the Claimants were protected from any present or future such measures, including *inter alia* export withholdings, for the full term of that concession. Thus the Sierra Chata concession created vested contractual tights which the GOA cannot unilaterally amend.

775. The question whether Argentina also violated the Chile-Argentina Energy Treaty through discriminatory taxation measures is not relevant in this case.

776. The question which amount of Export Withholdings was borne by MASA's Chilean customers will be evaluated in the context of compensation for BIT violations.

E. Royalties

1. The Claimants' position

777. These withholding measures also impacted on the royalties paid by the Claimants to their customers. The Legal Framework provides that the highest royalty rate that could be imposed on gas producers is 12%.[293] The Hydrocarbon Concessions and Contracts provide further guarantees to the Claimants in this respect. The Sierra Chata

[293] Hydrocarbons Law, Arts. 59, 62 (Exhibit C-8). See also Conversion Decree, Art. 10 (Exhibit C-28). This protection was also incorporated into the Hydrocarbon Concessions and Contracts. See Decree 305/92, Art. 8 (Exhibit C-96); Decree 1969/93, Art. 7 (Exhibit C-94); Chihuidos Memorandum of Understanding, Art. 13 (Exhibit C-93); and Decree 824/95, Art. 10 A (Exhibit C-95).

Concession provides that the highest royalty rate that could be imposed on the Claimants is 12%, and that it can only be calculated on the prices effectively collected.[294]

778. Under Law 25,561, however, the GOA prohibited the Claimants from deducting Export Withholdings payments when calculating royalties. This prohibition forced the Claimants to pay royalties on their gas export sales based on prices higher than they received (*i.e.*, without deducting Export Withholdings). Thus, in case the buyer assumes the obligation to cover the Export Withholdings, the GOA calculates the 12% royalty rate on the contract sales price (*e.g.*, US$ 1.65/MMBTU) plus the Export Withholding amount (US$ 17/MMBTU during the winter of 2008). This calculation yields a total sum of US$ 18.65/MMBTU. The 12% royalty in these cases is equivalent to US$ 2.238/MMBTU, which is higher than the sales price and effectively imposes a negative price.[295]

779. Argentina does not contest the existence or scope of the Claimants' right to a 12% maximum royalty rate calculated on the price they actually receive for their gas sales. Yet Argentina denies that the Province of Neuquén required the Claimants to pay royalties on a price higher than the one actually collected from the Claimants' foreign customers. Argentina further argues that "it was the Claimants, with the aim of transferring export duties to their Chilean clients, who negotiated and incorporated into the calculation basis for the payment of royalties the export duties." Both of those arguments distort the facts of this case.

[294] Decree 169/93 (Exhibit C-94).
[295] If, conversely, the buyer did not refund the Export Withholding amounts to the Argentine producer, the 12% royalty would be calculated on the basis of a notional price of approximately US$ 1.65/MMBTU, in spite of the fact that Export Withholdings turn it into a negative price. See Valle, Witness Statement, *supra* (n 34) ¶ 79 (Exhibit C-4).

780. First, by attempting to blame excess royalty payments on the Claimants, Argentina fails to mention that under Law 25,561 the Argentine Government expressly prohibited hydrocarbon producers, including the Claimants, from deducting Export Withholding payments when calculating royalties. This prohibition effectively violated the provisions of the Legal Framework and the Sierra Chata Concession that state that royalties may not exceed 12% of the price actually received by the producer.

781. Second, although as a mitigation measure the Claimants have been able to pass through the cost of Export Withholdings to their Chilean clients since April 2005, Argentina is wrong to deny that the Province of Neuquén has been collecting excess royalties from the Claimants. By adding the cost of Export Withholdings (*e.g.*, US$ 17/MMBTU during the winter of 2008) to the calculation, the Province of Neuquén claimed royalties on the basis of a price that exceeds the contractual export price that the Claimants receive (*e.g.*, US$ 1.65/MMBTU). The calculation that the Province applies results in a royalty calculation on the basis of an export price of US$ 18.65/MMBTU (US$ 1.65/MMBTU (export price) plus US$ 17/MMBTU (Export Withholdings)). The 12% royalty in these cases is equivalent to US$ 2.238/MMBTU, which is higher than the Claimants' export price and effectively imposes a negative price.[296]

782. This practice violates Argentina's commitment under the Legal Framework and the Sierra Chata Concession to refrain from charging a royalty rate that exceeds 12% calculated on the basis of the price that producers actually receive.[297] The Claimants were only able to partially pass-through to their export clients the incremental costs of

[296] Valle Witness Statement, *supra* (n 34) ¶ 79 (Exhibit C-4).
[297] Decree 1969/93, Art. 7 (Exhibit C-94). See also Hydrocarbons Law, Arts. 59, 62 (Exhibit C-8); Conversion Decree, Art. 10 (Exhibit C-28). This protection was also incorporated into the Hydrocarbon Concessions and Contracts; Decree 305/92, Art. 8 (Exhibit C-96); Decree 1969/93, Art. 7 (Exhibit C-94); Memorandum of Understanding for Conversion of Contract No. 25,174, Art. 13 (Exhibit C-93); Decree 824/95, Art. 10 (Exhibit C-95).

royalties as from February 2008. By alleging that the Claimants are responsible for their excess royalty payments because they did not fully succeed in modifying their gas export contracts to off-set the impact of Argentina's measures, Argentina improperly attempts to shift the consequences of the Government's wrongful conduct to the Claimants.

2. The Respondent's position

783. It is not correct, as the Claimants maintain that the province of Neuquén requires them to pay royalties on a price higher than that actually charged for gas exports to foreign clients.

784. To begin with, as reported by the province of Neuquén, "the amounts paid by Mobil Exploration and Development Argentina Inc. Sucursal Argentina and Mobil Argentina Sociedad Anónima on account of royalties were equivalent to 12%, as provided for by the legislation in force – Law No. 17319."

785. Indeed, the Hydrocarbons Law provides that "natural gas production shall be subject to the payment of monthly royalties equivalent to twelve per cent (12%) of the value of the volumes extracted and actually used …" and that "[i]n the case of hydrocarbon exports, the market value … shall be fixed on every occasion on the basis of the actual price charged by the concessionaire in the export …"

786. In turn, the modifications to the gas export agreements between the Consortium of Sierra Chata producers and their Chilean clients (Metrogas and AES Gener) expressly provide that "the prices [of natural gas] referred to in paragraphs 1 and 2 *include*

export duties for the 1/1/2005 - 31/12/2006 period."[298]

787. That is, it was the Claimants, with the aim of transferring export duties to their Chilean clients, who negotiated and incorporated into the calculation basis for the payment of royalties the export duties.

788. As explained by experts Sandleris and Schargrodsky

> "In our opinion, the alleged damages for excess royalties are originated in the same contractual deficiencies. In the addenda subsequent to 2002, Claimants could have foreseen the impact of export duties on royalties, thus establishing such a contractual price that the net price received is the price desired, but they failed to do so."[299]

789. The Argentine Republic has nothing to do with the private negotiation between the Claimants and their customers. It is a claim based on facts in which Argentina is not involved. Therefore, Argentina requests that the claim be dismissed by the Tribunal.

790. The royalties and any other items that may be deducted from their payment have been regulated since the passage of the Hydrocarbons Law. Since 1969, regulation has been uniform on that matter, as well as on the fact that export duties are excluded from deductible amounts.[300]

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[298] Decree No. 1671/69 (Exhibit AR-55), Decree No. 1055/89 (Exhibit AR-61), Decree No. 1757/90 (Exhibit AR-64), Decree No. 2178/91 (Exhibit AR-67), Decree No. 2411/91 (Exhibit AR-66), SC Resolution No. 5/91 (repealed; for exemplification purposes only) (Exhibit AR-65), SE Resolution No. 155/92 (Exhibit AR-73), Law No. 24145 (Exhibit AR-71), SE Resolution No. 188/93 (Exhibit AR-64), SE Resolution No. 232/02 (Exhibit AR-164), SE Resolution No. 435/04 (Exhibit AR-191).

[299] UTDT Report, *supra* (n 156) ¶ 248.

[300] Decree No. 1671/69 (Exhibit AR-55), Decree No. 1055/89 (Exhibit AR-61), Decree No. 1757/90 (Exhibit AR-64), Decree No. 2178/91 (Exhibit AR-67), Decree No. 2411/91 (Exhibit AR-66), SC Resolution No. 5/91 (repealed; for exemplification purposes only) (Exhibit AR-65), SE Resolution No. 155/92 (Exhibit AR-73), Law No. 24145 (Exhibit AR-71), SE Resolution No. 188/93 (Exhibit AR-64), SE Resolution No. 232/02 (Exhibit AR-164), SE Resolution No. 435/04 (Exhibit AR-191).

791. Consequently, the regulations that govern the Claimants' concession in Sierra Chata make no provision for further deductions from the payment of royalties other than the usual ones.[301]

792. Secondly, the difference between the versions of the facts provided by the witnesses and the experts for the Claimants is apparent. While LECG states that the period during which the Claimants had to bear the payment of the purportedly "excess royalties" runs from September 2006 to September 2008, [302]Mrs. Valle asserts that such period does not go beyond December 2007.[303]Making a submission in that fashion proves unserious, as it fails to contain reliable facts and which involves significant amounts claimed from the Argentine Republic, without a severe control of the allegations. The Argentine Republic requests that the Tribunal dismiss this claim submitted by the Claimants.

793. Last, neither do the several hydrocarbons agreements including provisions on royalties executed so far between the Argentine Executive and the companies in the sector establish any hypothetical deduction other than the usual ones.

794. In summary, the Claimants' claim for royalties is groundless.

795. The Argentine Republic does not attempt to "improperly shift" the consequences of its wrongful conduct, but rather the opposite: The Claimants insist on the Argentine Republic's becoming the insurer of their business activity.

796. There are contract documents, from the beginning in 1996 of the commercial relation between Sierra Chata and the Chilean purchasers, which defeat the claim from MEDA

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[301] Decree No. 1969/93, Art. 7 (Exhibit AR-75); Decree No. 824/95, Art. 10 (Exhibit AR-78); Resolution No.140/96 (Exhibit AR 81).
[302] LECG Report, *supra* (n 22) 103.
[303] Valle Witness Statement, *supra* (n 34) ¶ 84.

and MASA. These documents, together with the recent addenda, expressly state that excess royalties and "any impact on such royalties resulting from *their billing*"[304] shall be borne by the purchasers.

797. As can be seen, the dispute does not involve the percentage of royalties actually collected; according to the information provided by the Province of Neuquén, MEDA and MASA always paid 12%. The Claimants acknowledge that the claim involves the alleged "impact" that export duties may have on the final sale price, which will increase the amount subject to royalties. However, the contract provisions agreed with purchasers show that it is not unusual and unforeseeable that taxes indirectly increase royalties. The Claimants' claim involves matters that are inherent to the business itself.

798. The Claimants have been reimbursed by their Chilean counterparties for the "excess" royalty amounts. However, if there still were amounts pending reimbursement (which to date cannot be known for sure due to the lack of documentary evidence and contradictions between witnesses' testimonies), it would be the consequence of acts attributable to the management of MEDA and MASA.[305] Insisting on deceitful claims intended to confuse the issues under the analysis of the Tribunal and to remedy their own business contingencies is inacceptable. Finally, it is to be noted the most recent evidence disorder by the Claimants, who allege that they could only pass the royalty

[304] Contract addendum dated 26 September 2006, Sections. 2, 3, 4, 5, 6; Contract addendum dated 31 January 2007, Section 2.2; Contract addendum dated 1 July 2008, Section 1.3 (Exhibit AR-306). Contract for the export of natural gas with Metrogas SA and Chilgener SA, 23 October 1996, Section A.15: "Taxes: the Purchasers shall be responsible for all taxes, levies, royalties and other charges applicable downstream from such interconnection point at Tratayen in the Neuquina Basin and all import duties applicable to the Natural Gas."(Exhibit C-100) The interconnection point at Tratayen is located within the Argentine Republic, in the province of Neuquén, a few miles away from the Sierra Chata field.
[305] UTDT Report, *supra* (n 156) ¶ 248.

costs through "since February 2008" and, on the contrary, the addenda signed with their export customers establish the reimbursement of royalties since 2004.[306]

799. Since the matter submitted to the analysis of this Tribunal is not within the scope of the Tribunal's jurisdiction as a result of the application of Article XII of the BIT and, alternatively, considering the additional arguments already explained and presented in the Counter-Memorial, the Argentine Republic respectfully requests the Tribunal to reject this claim together with the relief sought regarding export duties

3. The Tribunal's Analysis

800. Articles 59 and 62 (1) of the Hydrocarbons law provide:

> "Article 59
>
> The exploitation concessionaire shall pay to the Federal State a monthly royalty of twelve percent (12%) of the production of liquid hydrocarbons at wellhead, which percentage may be reduced by the Federal Executive Power up to five percent (5%), taking into account the productivity, the conditions and location of the wells."
>
> "Article 62
>
> Natural Gas production shall pay a monthly royalty, calculated as a percentage of the volumes produced and effectively employed, accounting to twelve percent (12%), which the Executive Power may reduce to five percent, taking into consideration the factors indicated in article 59."

801. Article 7 (1) of the Sierra Chata Concession provides

> "ARTICLE 7.- In the event provided for in Article 2 of this Decree, the exploitation Concessionaire shall pay directly to the Province of

[306] Contract addendum dated 26 September 2006, Section 3. Also, Sections 2, 3, 4, 5, 6. In: File 750-003106/94 for the Authorization of Natural Gas Export concerning the Sierra Chata field (Exhibit AR-306).

> Neuquén, in the name of the FEDERAL GOVERNMENT, the royalties resulting from the application of Articles 59 and 62 of Law No. 17,319, paying up to TWELVE PER CENT (12%) of the production valued on the basis of the prices actually obtained in the trading operations of hydrocarbons produced in the Concession Area, with the deductions set forth in Articles 61, 62, and 63 of that law."

802. The fact that the Claimants were able to pass through the cost of Export Withholdings to their customers for some periods does not entitle the GOA or the Province of Neuquén to include Export Withholdings in its royalty calculation, because the Government, not the Claimants, actually collects the cost of the Export Withholdings. Therefore, the Tribunal finds that Export Withholdings are not part of the "price actually obtained" by the producer, which in accordance with the Hydrocarbons Law and the Sierra Chata Concession is the only price that may serve as the basis for the calculation of royalties.

803. The Tribunal finds that by adding the costs of Export Withholdings to the calculation, the Province of Neuquén has claimed on the basis of a price that exceeds the contractual export price that the Claimants receive.

804. The Tribunal finds that this practice violates Argentina's commitment under the Legal Framework, which is incorporated in the Sierra Chata Concession.

805. The question whether the Claimants have been reimbursed by their Chilean customers for any "excess royalty amount" will be evaluated in the context of compensation for BIT violations.

X. THE ALLEGED VIOLATIONS OF THE BIT

806. Before the Tribunal begins to evaluate the facts and contentions of the Parties in this case, in order to ascertain whether or not they show violations of the international standards of protection of foreign investments, the Tribunal considers it appropriate to identify the legal framework within which the factual aspects can and must be

examined. Once ascertained, the facts, as they result from the record, have to be analysed taking due account of the applicable rules. It is therefore important to identify the content and scope of the different standards benefitting foreign investors under the BIT.

A. GENERAL OBSERVATIONS ON THE DIFFERENT STANDARDS OF PROTECTION

807. The standards of protection applicable to foreign investors are stated in Article IV (1) and Article II (a) and (b) of the BIT.

808. Article IV (1) of the BIT provides:

> "Investments shall not be expropriated or nationalized either directly or indirectly through measures tantamount to expropriation or nationalization ("expropriation") except for a public purpose; in a non-discriminatory manner; upon payment of prompt, adequate and effective compensation; and in accordance with due process of law and the general principles of treatment provided for in Article II(2)."

809. Article II(2)(a) and (b) provide:

> "(a) Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law.
>
> (b) Neither Party shall in any way impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, or disposal of investments. For the purposes of dispute resolution under Articles VII and VIII, a measure may be arbitrary or discriminatory, notwithstanding the opportunity to review such measure in the courts or administrative tribunals of a Party."

810. The Tribunal finds that that ICSID case-law generates some confusion and overlap between these different standards of protection found in most BITs. The Tribunal will therefore try to clarify as much as possible the scope of the different standards of protection, because in our view they should not be used indifferently one for the other.

811. There is not always a clear distinction between indirect expropriation and violation of legitimate expectations, between the fair and equitable treatment (**"FET"**) and the full protection and security (**"FPS"**) standards, and sometimes between several standards of treatment, which are all amalgamated, and the distinction seems also difficult between arbitrary or discriminatory treatment and violation of the FET.

812. The Tribunal holds that FET is designed to guarantee that, in situations where the other more precise standards are not violated, but where there is an unreasonable interference bringing about an unjust result regarding an investor's expectations, that investor can claim a violation of the FET and obtain reparation therefore.

813. The Tribunal will below analyse interferences with the Claimants' investments successively with reference to the different standards of protection in a sequential order, proceeding from expropriation to FPS. The Tribunal will thus examine first whether there is an indirect expropriation, second whether there is arbitrary and discriminatory treatment, third whether there is a violation of the FET, and fourth whether there is a breach of FPS.

B. ARTICLE IV: INDIRECT EXPROPRIATION

814. The Tribunal will first address the complaints concerning acts of the GOA, other than tax measures complained of, which enter into the Tribunal's jurisdiction if they amount to an expropriation or relate to the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VII(1)(a) or (b) of the BIT.

1. Indirect Expropriation in General

815. Expropriation is not defined in Article IV of the BIT, which however mentions expropriation at the same level as nationalization and measures tantamount to expropriation or nationalization and sets out the conditions to be fulfilled if such acts

are to be consistent with the BIT. These conditions are that the measures (a) are taken for a public purpose; (b) in a non-discriminatory manner, upon payment of prompt, adequate and effective compensation; and (c) in accordance with due process of law and the general principles of treatment provided for in Article II (2).

816. As in most other BITs, expropriation under the terms of this BIT may be considered to be an act taken by a State in the exercise of its sovereignty by which an investor is involuntarily deprived of property. Property should in this context be given a broad meaning and cover any material and immaterial assets having an economic value, including concessions and contractual rights belonging to the investor. Expropriation is to be distinguished from less far-reaching measures which regulate or restrict the right to use property.

817. As held by the Tribunal in *El Paso*, "a general regulation is a lawful act rather than an expropriation if it is non-discriminatory, made for a public purpose and taken in conformity with due process. In other words, *in principle, general non-discriminatory regulatory measures, adopted in accordance with the rules of good faith and due process, do not entail a duty of compensation*".[307]

818. However, general regulations that are arbitrary, discriminatory, disproportionate or otherwise unfair can be considered amounting to indirect expropriation if they result in a neutralization of the foreign investor's property rights. The proportionality when making use of this right was recognised in *Tecmed*, which observed that "whether such actions or measures are proportional to the public interest presumably protected thereby and the protection legally granted to investments, taking into account that the significance of such impact, has a key role upon deciding the proportionality."[308]The

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[307] *El Paso Energy International v Argentine Republic*, ICSID Case No ARB/03/15, Award (31 October 2011) [hereinafter "*El Paso Award*"], ¶ 240 [Emphasis in the original].
[308] *Tecmed Award, supra* (n 95) ¶ 122.

need for proportionality of State measures interfering with private property has been stressed by the Tribunal in *LG&E*:

> "With respect to the power of the State to adopt its policies, it can generally be said that the State has the right to adopt measures having a social or general welfare purpose. In such a case, the measure must be accepted without any imposition of liability, except in cases where the State's action is obviously disproportionate to the need being addressed."[309]

819. As examples of possible exceptions from the principle that general regulations do not amount to indirect expropriation, it may be mentioned, first, that of an intentionally discriminatory regulation or an objectively discriminatory regulation. The Tribunal in the *Methanex* case clearly distinguished discriminatory regulations from non-discriminatory ones:

> "In the Tribunal's view, Methanex is correct that an intentionally discriminatory regulation against a foreign investor fulfills a key requirement for establishing expropriation. But as a matter of general international law, a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, inter alia, a foreign investor or investment is not deemed expropriatory and compensable unless specific commitments had been given by the regulating government to the then putative foreign investor contemplating investment that the government would refrain from such regulation."[310]

820. As another example can be mentioned a *disproportionate regulation*, meaning a regulation in which the interference with the private rights of the investors is disproportionate to the public interest. In other words, proportionality has to exist

[309] *LG&E Energy Corp, LG&E Capital Corp and LG&E International Inc v Argentine Republic,* Decision on Liability (3 October, 2006) [hereinafter "*LG&E Decision on Liability*"] ¶ 98.
[310] *Methanex v United States,*UNCITRAL (NAFTA), Final Award (7 August, 2005) [hereinafter "*Methanex Award*"] ¶ 7 of Part IV –Chapter D.

between the public purpose fostered by the regulation and the interference with the investors' property rights, as recognised in *Tecmed*.[311]

821. Thus, discriminatory or disproportionate general regulations may be considered expropriatory if there is a sufficient interference with the investor's right.

822. The Tribunal considers that at least one of the essential components of the property rights must have disappeared for an expropriation to have occurred. It is generally accepted that the decisive element in an indirect expropriation is the *loss of control* of a foreign investment, in the absence of any physical taking. In this regard, the *Pope & Talbot* tribunal concluded that "[w]hile it may sometimes be uncertain whether a particular interference with business activities amounts to an expropriation, the test is whether the interference is sufficiently restrictive to support a conclusion that the property has been taken from the owner."[312]

823. This approach has also been adopted in several of the Argentinian cases, resulting from the crisis, which brought about this arbitration. In *CMS*, the tribunal stated:

> "The essential question is therefore to establish whether the enjoyment of the property has been effectively neutralized. The standard that a number of tribunals have applied in recent cases where indirect expropriation has been contended is that of substantial deprivation."[313]

824. Then, applying this test to the case at hand, the tribunal considered that the measures adopted by the State did not deprive the investor of control over its investment and therefore concluded that there was no expropriation.

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[311] *Tecmed*, *supra* (n 95) ¶ 121.
[312] *Pope & Talbot Inc v Government of Canada,* UNCITRAL (NAFTA), Interim Award (29 May, 2003) [hereinafter "*Pope & Talbot Interim Award"*] ¶ 99.
[313] *CMS Award*, *supra* (n 97) ¶ 262.

825. In *Enron*[314] as well as in *Sempra*[315] the tribunals held that for expropriation to exist there must be a substantial deprivation and that such a deprivation occurs when the investor is forced to lose control over the investment. If the measures do not interfere with the control of the property, there can be no expropriation. This has been confirmed by the award in another Argentinian case, *Continental*, where an indirect expropriation was defined as amounting to

> " … limitations and hampering with property, short of outright suppression or deprivation, interfering with one or more key features, such as management, enjoyment, transferability, which are considered as tantamount to expropriation, because of their substantial impact on the effective right of property." [316]

2. A mere frustration of a foreign investor's legitimate expectations, is not an Indirect Expropriation

826. In the Tribunal's view, a mere frustrating of a foreign investor's legitimate expectations with respect to sovereign assurances is not an indirect expropriation. This was also stated, for example, by the *Waste Management* tribunal. The tribunal explicitly pointed out that "the loss of benefits or expectations is not a sufficient criterion for an expropriation, even if it is a necessary one."[317]

827. As Argentina argues, the *Tecmed* award, cited by the Claimants in support of their allegation that interference with the investor's expectations may amount to indirect expropriation, was in this regard criticized by the *MTD* annulment committee because

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[314] Enron Corporation and Ponderosa Assets LP v Argentine Republic, ICSID case No ARB/01/3, Award (22 May 2007) [hereinafter *"Enron Award"*] ¶ 245.

[315] *Sempra Energy International v Argentine Republic*, ICSID Case No. ARB/02/16, Award (28 September 2007) [hereinafter "*Sempra Award"*] ¶ 285.

[316] *Continental Casualty Company v Argentine Republic*, ICSID Case No. ARB/03/9, Award (5 September 2008) [hereinafter "*Continental Award"*] ¶ 276.

[317] *Waste Management, Inc v The United Mexican States* ICSID Case No ARB(AF)/00/3), Award (30 April 2004) [hereinafter "*Waste Management Award"*] ¶ 159.

the *Tecmed* tribunal had relied on the investor's expectations to determine that an expropriation had taken place:

> The *TECMED* Tribunal's apparent reliance on the foreign investor's expectations as the source of the host State's obligations (*such as the obligation to compensate for expropriation*) is questionable. The obligations of the host State towards foreign investors derive from the terms of the applicable investment treaty and not from any set of expectations, investors may have or claim to have. A tribunal which sought to generate from such expectations a set of rights different from those contained in or enforceable under the BIT might well exceed its powers, and if the difference were material might do so manifestly.[318]

828. In conclusion, consistently with mainstream case law, the Tribunal finds that for an expropriation to exist, the investor should be substantially deprived not only of the benefits, but also of the use of the investment. A mere frustration of investor's expectations, even when legitimate, which is not a result of an interference with the control or use or the investment, is not an indirect expropriation.

3. The Parties Positions on the Existence of an Expropriation

829. According to the Claimants, "Argentina has expropriated key legal and contractual rights and specific associated revenues of the Claimants." The Claimants do not complain about direct expropriation but argue that the question whether expropriation is direct or indirect has no bearing on the legal consequences of the act. The list of the expropriatory acts presented by the Claimant include the following: (i) abrogation and repudiation of key legal and contractual rights such as the Claimants' rights to freely dispose of and market hydrocarbon production and to freely agree on prices and currency payment; (ii) unilaterally changing the terms of the Claimants' private gas supply contracts; (iii) introducing Export Withholdings on hydrocarbon exports

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[318] *MTD Equity Sdn Bhd & MTD Chile SA v Republic of Chile*,] ICSID Case No ARB/01/7, Decision on Annulment (21 March 2007) [hereinafter *"MTD Decision on Annulment"*] ¶ 67 (emphasis added).

contrary to prior express undertakings; (iv) taking the right to export hydrocarbons; and (v) taking the Claimants' right to royalty rate stability.

830. The Claimants contend that the GOA "through a series of increasingly onerous measures" abrogated the Claimants' rights under the Legal Framework, the Hydrocarbon Concessions and Contracts and the Sierra Chata Gas Export Permit. Through their abrogation, Argentina, according to the Claimants, "expropriated the Claimants' legal and contractual rights and specific revenues directly, indirectly, and by measures tantamount to expropriation."

831. According to Argentina, first, none of the measures interfered with the Claimants' property rights, since the Claimants did not have a right to be excluded from pesification, a right to the non-application of export restrictions and re-routing or a right to be exempt from export withholdings: second, the measures challenged by the Claimants did not deprive them of control over their alleged investments. As regards export withholdings, Argentina argues that they did not cause a substantial interference.

832. First, it is Argentina's position that the measures challenged by the Claimants did not interfere with their property rights. The Claimants did not have a right to be excluded from pesification, or a right to the non-application of export restrictions and re-routing or a right to be exempt from export withholdings.

833. Second, Argentina contends that the measures challenged by the Claimants did not deprive them of control over their alleged investments. In this regard, the Claimants argue that they were deprived of effective control over their natural gas export business. Demanding compliance with the legal duty to supply the domestic market does amount to controlling the natural gas export business. The possibility of exporting natural gas subsists provided the duty to supply the domestic market is complied with (a limitation that has existed all along). Moreover, it has been held in

other cases that the establishment of restrictions, quotas or prohibitions on exports does not amount to expropriation.

834. Third, Resolution SE No. 659/04 affords the possibility of replacing volumes of natural gas by alternative fuel to comply with the duty to supply the domestic market. the Claimants could have opted for such possibility and exported natural gas to their Chilean customers, since the latter offered to pay for the alternative fuel.

835. Finally, Argentina argues, all the measures challenged by the Claimants were *bona fide* non-discriminatory regulatory measures within the police power of the State.´

4. The Tribunal's Analysis of the Alleged Expropriation of the Claimants' Legal and Contractual Rights

836. The Claimants contend that Argentina eviscerated the Claimants' export right through a series of export restrictions that resulted not only in a reduction of the Claimants' export capacity but also in the Claimants' inability to perform the very export contracts which the GOA had taken into consideration when granting the Sierra Chata Gas Export Permit. The GOA's export restrictions began by forcing the Claimants to supply additional gas to the local market, but soon escalated by coercing the Claimants to accept irrevocable offers from certain domestic consumers to purchase gas at regulated, below-market prices. The GOA also sought to coerce the Claimants to agree to further restrain their export rights through the Second Gas Agreement, which would have subjected the Claimants to additional domestic supply obligations and regulated prices. The Claimants refused, and as a consequence, effective control over their export business was taken by Argentina

837. According to the Claimants:

> "This drastic evisceration of rights subjected Claimants to forcible re-routing of their gas exports at below-market prices to sometimes unknown customers with whom they had no contractual relationship.

> Under this new paradigm, Claimants lost their firm export rights and effective control of their investments."[319]

838. Thus, the GOA expropriated the Claimants' right to export firm volumes of natural gas.

839. Moreover, the Claimants contend that through the interference in the Claimants' Dollar-denominated contracts by converting them into Pesos at an artificially-low and confiscatory exchange rate and by impeding the renegotiation of those prices between the Claimants and their main customers, the GOA took away the Claimants' legal and contractual rights to freely market their gas production and agree on prices and currency, as well as the specific revenues associated within those rights.

840. According to the Claimants, in addition, the GOA imposed export restrictions that further eroded the Claimants' right to dispose of gas production at freely-agreed prices. These measures restricted the Claimants' exports and forcefully re-routed gas export volumes to third-party domestic customers at regulated, below-market prices.

841. The Claimants contend that in particular, these measures have taken the Claimants' rights to freely dispose of and market gas and to enter into hydrocarbon sale contracts freely with customers on freely agreed terms, including price and currency. The GOA's measures created an environment that is inconsistent with the regime under which MEDA and MASA invested—a regime in which "the sale of gas between producers, distributors, and large users will be freely agreed between them."

842. The Claimants had a legitimate expectation that the GOA would not unilaterally interfere with the terms of their contracts with their customers, and that they could sell hydrocarbon production freely and at prices determined by negotiation and market

[319] Claimant's Memorial on the Merits ¶ 333.

forces, not ¨government mandate”. Because of the GOA’s repudiation of these basic legal rights, which formed part of the legal and business environment in which the Claimants invested, the Claimant contend that the GOA has indirectly expropriated the Claimants’ legal and contractual rights and specific revenues.

843. Taking into account what is said above under the heading “Indirect Expropriation in General” (IX.B.1) about indirect expropriation, the Tribunal concludes that there was no expropriation of the Claimants’ rights. First, a mere frustration of legitimate expectations is not an indirect expropriation. Second the measures questioned by the Claimants did not have the consequence that the Claimants were deprived of control of their investments.

C. INDIRECT EXPROPRIATION RELATING TO TAX MATTERS

1. The Parties’ Positions

844. The Claimants contend that the Export Withholdings imposed by the GOA resulted in the expropriation of the Claimants’ legal and contract rights.

845. According to the Claimants, Export Withholdings conflict with undertakings and assurances given by Argentina in good faith and are thus expropriatory. Under the Legal Framework and the Sierra Chata Concession, the GOA guaranteed the Claimants a stable tax regime and expressly exempted the Claimants from Export Withholdings and any other specific or discriminatory taxes. Export Withholdings violate express provisions of the Legal Framework, which apply to, and have been expressly incorporated into, the Claimants’ Hydrocarbon Concessions and Contracts. Furthermore, because they are asymmetric to the tax treatment of other petroleum products and “products which use gas as a raw material”, Export Withholdings on gas also violate the tax-treatment provision of the Chile-Argentina Energy Treaty.

846. Second, the Claimants contend, the manner in which Argentina took these rights and associated revenues is confiscatory. In 2004, when Argentina first took the Claimants right to be e exempt from export withholdings, it did so through an export-withholding rate of 20%, which was calculated based on the prices the Claimants actually received for their exports. In 2006, when the GOA raised the withholding rate to 45%, it arbitrarily changed the basis for calculating Export Withholdings disregarding the actual export prices received by the Claimants. Instead, the Government calculates the Export Withholdings on a deemed price; the price of expensive Bolivian gas that was imported by the GOA, yielding an effective withholding rate exceeding 100%. Since March 2008, the Argentine Government has imposed a 100% withholding rate calculated on an even higher deemed import price; the price for importing LNG, which yields an effective rate of up to 800%, a rate that is confiscatory by any notion of ‘the term.

847. According to the Claimants, each instance of Export Withholdings constitutes a taking of legal and contractual rights and specific revenues. The cumulative effect of the Export Withholdings has been to deprive the Claimants of the protections against such measures, which the GOA guaranteed the Claimants through contracts and legislation. The GOA’s Export Withholding rates constitute an expropriation of the Claimants’ vested legal and contractual rights to be exempt from Export Withholdings and to enjoy tax stability.

848. Moreover, the Claimants contend that the Export Withholding measures also violated the GOA’s legal and contractual commitment to refrain from imposing royalties on gas producers higher than 12%. The GOA made this guarantee under the Legal Framework and incorporated it into the Claimants’ Hydrocarbon Concessions and Contracts. Along with Law 25,561 – which prevents the Claimants from deducting their Export Withholding payments when calculating royalties –, the computation of Export Withholdings for gas exports results in an effective royalty rate that exceeds the contract price and is far above the statutory ceiling for royalty rates. Not only do

these measures expropriate the Claimants' legal and contractual rights, but they also interfere with the Claimants' activities and result in a substantial loss of revenues

849. The Claimants admit that taxation *per se* is of course a lawful sovereign activity, but asserts that Article XII expressly subjects Argentina's taxation measures to the scrutiny of the BIT's expropriation provision. The question is thus under what circumstances taxation measures may result in unlawful expropriation.

850. As regards export withholdings, Argentina contends that they did not cause a substantial interference, given that the Claimants passed their duties through to their Chilean customers, except for a six-month period during which they were subject to an effective rate of 16.67% Furthermore no royalties in excess of the 12% rate established in the Hydrocarbons Law have been demanded. The Claimants themselves included the export withholdings in the basis for calculating royalties. Argentina contends that these and all other measures were *bona fide* non-discriminatory regulatory measures within the police powers of the State.

2. The Tribunal's Analysis

851. Article XII of the BIT provides as follows:

> "1. With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party.
>
> 2. Nevertheless, the provisions of this Treaty, and in particular Articles VII and VIII, shall apply to matters of taxation only with respect to the following:
>
> (a) expropriation, pursuant to Article IV;
>
> (b) transfers, pursuant to Article V; or
>
> (c) the observance and enforcement of terms of an investment agreement or authorization as referred to in Article VII (1) (a) or (b), to the extent they are not subject to the dispute settlement provisions of a

> Convention for the avoidance of double taxation between the two Parties, or have been raised under such settlement provisions and are not resolved within a reasonable period of time."

852. It is common ground that the tax policy of a country is a matter relating to the sovereign power of the State and its power to impose taxes on its territory. Thus the State has a sovereign right to enact the tax measures it deems appropriate at any particular time. There is a presumption of validity in favour of legislative measures adopted by the State, and it is up to those who challenge such measures to demonstrate their invalidity. This idea has also been embodied in Article XII of the BIT, the effect of which is only to limit slightly the State's power to levy taxes.

853. Having regard to both the language used in Article XII (1) – "each party should strive" – and the fact that Article XII (2) excludes in matters of taxation, except in specific and limited cases, any review of a possible violation of the BIT standards, the Tribunal concludes that Article XII (1) creates only a best-effort obligation.

854. In as much as the Claimants' claim relates to tax matters, i.e. export withholdings and their impact on royalties, the issue is whether such taxes could qualify as an expropriation (point a).

855. The Tribunal will first look into the Export Withholdings in order to consider whether they can be considered an expropriation. The Emergency Law adopted on 6 January 2002 decided on the principle of such a tax, known as withholding on oil and gas and authorized the Executive Branch to impose export withholdings on hydrocarbons for a five-year period and to establish the respective rates:

> "The Executive Branch of Government shall be entitled to establish compensatory measures to avoid the unbalancing of financial institutions resulting from the provisions set forth in the preceding paragraph. These measures may include the issue of guaranteed

> national public bonds in foreign currency. For purpose of funding such guarantee, an export tax on hydrocarbons is hereby created for the term of FIVE (5) years, and the Executive Branch of Government shall be entitled to determine the corresponding tax rate."[320]

856. By virtue of Law 26,217,[321] the GOA extended the Export Withholdings through 2012.

857. In May 2004, through Decree 645/04, Argentina imposed a 20% Export Withholding on Claimant's gas exports, among other gaseous hydrocarbons[322]: this amounts to a 16,67% export duty on crude oil exports, as in Argentina the withholding is included in the amount used to calculate export duties and therefore a 20% export duty implies an actual 16.67% withholding. In addition, it authorized the Ministry of Economy to modify the Export Withholding rate.[323] At that time, the alleged purpose of Export Withholdings on gas was to align the tax treatment of gas with crude oil and by-products.[324]

858. Argentina and Bolivia had entered into the Framework Agreement for the Sale of Gas and the Execution Projects Concerning Energy Integration (the **"Framework Agreement"**) in June 2006. In July 2006, the GOA (i) increased the Export Withholding rate for gas from 20% to 45%.[325]

859. These measures raised the effective Export Withholding rate on gas more than 675% which according to the Bastos report exceeded the average export price that Argentine gas exporters received from foreign customers by approximately 40%.[326]This amounts according to the LECG Report to 113 % of the export price that the

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[320] Law No. 25,561 (Emergency Law), Title IV, Chapter I, Art. 6 § 2.
[321] Exhibit C-69.
[322] Decree 645/04, Art. 1.
[323] Decree 645/04, Art. 2.
[324] See Preamble of Decree 645/04.
[325] See Decree 645/04 and Resolution MEP 534/06, Art. 1.
[326] Bastos Report, *supra* (n 57) ¶ 144 (Exhibit C-1).

Claimants received and renders exporting gas unprofitable since all of the profit (and more) is taken by the GOA.[327]

860. Through Resolution MEP 127/08,[328] the GOA once again (i) increased the applicable Export Withholding rate on gas (from 45% to 100%), and (ii) alters the basis on which it calculates Export Withholdings, disregarding the much lower export prices received by exporters such as MASA. Instead of calculating Export Withholdings on the basis of the price at which MASA exports gas, the GOA uses artificial prices

861. Under Resolution MEP 534/06, the GOA calculated Export Withholdings based on the price at which it imports gas from Bolivia (currently US$ 10.30/MMBTU). Since early 2008, the GOA has calculated Export Withholdings on the highest prevailing rate for gas imports (during the winter of 2008, between US$ 14.5-17/MMBTU due to the import of LNG). Thus, Resolution MEP 127/08 entails a further increase of approximately 650%n in the applicable Export Withholding rate. As a result, during the winter of 2008, export withholdings on gas exports in Argentina were approximately between US$ 14.5 and 17/MMBTU, that is between seven and eight times higher than the actual average export price they received by Argentine producers (around US$ 1.90/MMBTU). This equates to nearly 800% of the Claimants' export price.

862. Turning now to the analysis of these matters, the Tribunal considers, first, that the creation of export duties on gas is a reasonable governmental regulation within the context of the crisis.

863. Under no circumstances may a tax less than 20% on exports be characterised as expropriation of an investment. The impact of the imposition of export withholdings

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[327] LECG Report, *supra* (n 22) ¶ 62 (Exhibit C-2).
[328] Resolution MEP 127/08 (Exhibit C-77), See also LECG Report, *supra* (n 22) ¶ 63 (Exhibit C-2).

at a rate of 16,67% and the consequence of the Export Withholdings that that royalty rate is higher than 12% and is above the statutory ceiling for the royalty rate cannot be deemed expropriatory. The same is true of the highest rates required subsequently taking into account that for the most part the amount was transferred to the clients of MASA.

864. In conclusion, the Tribunal, having analysed the Export Withholdings and their impact on the royalty rate does not consider that they amount to an indirect expropriation. Therefore, the Tribunal has no jurisdiction pursuant to Article XII (2)(a) of the BIT as far as the Export Withholdings and their impact on royalties are concerned.

D. ARTICLE II (2)(b) ARBITRARY AND DISCRIMINATORY TREATMENT

865. Article II (2) (b) of the BIT states:

> "Neither Party shall in any way impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments. For the purposes of dispute resolution under Articles VII and VIII, a measure may be arbitrary or discriminatory notwithstanding the opportunity to review such measure in the courts or administrative tribunals of a Party."

1. Arbitrary Treatment: Have The Claimants Been Treated Arbitrarily?

a. The Parties' Positions

866. According to the Claimants, the GOA's actions were arbitrary for three primary reasons: (1) they bear no rational relation to their stated purpose; (2) they were coercive and retaliatory; and (3) they were taken in a wilful disregard of due process and proper procedure. The Claimants argue that the Export Withholdings bear no rational relation to their stated purpose, the Second Gas Agreement punished producers who did not sign the agreement by: (i) imposing domestic supply

requirements on non-signing producers; (ii) rerouting the export gas of non-signing producers before that of signers; and (iii) re-routing it to the lowest paying domestic users. Resolution SE 599/07[329] contains a retaliatory mechanism that punishes Non-Signing producers by subjecting them to far worse treatment than that granted to Signing Producers.

867. Moreover, the Claimants contend that the GOA enacted certain measures without due regard to proper legal process and procedure. The method by which the GOA dismantled the Legal Framework and unwound its legal and contractual commitments under the Hydrocarbon Concessions and Contracts and the Sierra Chata Gas Export Permit was itself arbitrary. Furthermore, since 2007, the GOA has even subjected the Claimants to informal (often verbal) orders demanding that the Claimants supply gas to certain local companies or that the Claimants refrain from exporting gas volumes. According to the Claimants those orders do not even attempt to comply with proper procedures or the rule of law.

868. Argentina argues that the Claimants may not make a claim on tax matters alleging arbitrariness, since Article XII of the Treaty expressly excludes such types of claims and the distinction between the signatory and non-signatory producers did not amount to retaliation, but consisted merely of reasonable distinctions based on the fact that their situation was different. The purpose of the Second Gas Agreement is to guarantee the provision of a certain volume of natural gas to the domestic market. The orders given to the Claimants to provide gas to the domestic market were reasonable measures and they were founded on the priority goal of supplying the domestic market under the Hydrocarbon law.

[329] Resolution SE 599/07 (Exhibit C-75).

869. Moreover, Argentina denies that it disregarded "proper procedure and due process" in violating the Claimant's rights and dismantling the Legal Framework, since restrictions on export and demands for additional injections were legitimate measures pursuant to the applicable legal framework which were adopted in view of the gas shortage.

870. Finally, Argentina contends that the Argentine Secretary of Energy had broad powers to introduce modifications to dispatch rules and there have always been regulatory mechanism in place for natural gas prices in normal situations.

871. Argentina concludes that the measures adopted by ENARGAS (the Gas Regulator) and the Secretary of Energy after the 2002 crisis were far from being arbitrary and were adopted in accordance with the legal framework of natural gas and electricity.

b. The Tribunal's analysis

872. *Black's Law Dictionary* defines the word "arbitrary" as "[d]epending on individual discretion; specif. determined by a judge rather than by fixed rules, procedures, or law. In addition "arbitrary" (of a judicial decision) is defined as "founded on prejudice or preference rather than on reason or fact." [330]

873. According to international law, "[ar]bitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law. It is a wilful disregard of due process of law, an act which shocks, or at least surprises, a sense of juridical propriety."[331]

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[330] *Black's Law Dictionary*, 9th ed. (2009) p. 119.
[331] *Elettronica Sicula SpA* (*United States of America v Italy*) [hereinafter "*ELSI*"], Judgment (20 July, 1989) ICJ Rep 1989, p. 15 ¶ 128.

874. The Tribunal agrees with Argentina that the presence of arbitrariness must be determined in light of the circumstances of the case and that insofar as all the disputed measures were adopted within a context of social and economic crisis – and subsequent energy crisis – the existence of which is not a fact in issue, the governmental measures cannot be regarded arbitrary, notwithstanding any other disagreement between the parties as to the validity of such measures. Thus, for example, in the *Noble Ventures* case, the Tribunal considered that the measure challenged was not arbitrary as it was aimed at overcoming a social crisis.[332]

875. As the *El Paso* tribunal stated:

> "...if one is faced with a difficult economic situation, there are always several methods for dealing with it, depending on the circumstances, the political constraints incumbent on governments and their economic analyses, It is clear that neither the causes of, nor the answers to, Argentina's economic crisis at the end of 2001 have been the object of unanimous appraisal."[333]

876. There is no common analysis of the origin of the crisis. This was pointed out by the tribunal in the *CMS* case:

> "This crisis … stemmed basically from economic conditions that made it impossible to maintain the fixed exchange rate and which gradually led to the greatest default on foreign debt in history and the collapse of the Argentine financial markets. Some tend to fault foreign investors and put the blame on excessive privatization and globalization, while others see in it the result of not having carried out the liberalization program in its entirety and having allowed major governmental interferences in the functioning of the economy."[334]

877. As stated by the Tribunal in *LG&E*, the reactions to the crisis could of course have been different:

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[332] *Noble Ventures Inc v Romania*, ICSID Case No ARB 01/11, Award (12 October 2005) [hereinafter "*Noble Ventures Award"*] ¶ 177.
[333] *El Paso Award, supra* (n 307) ¶ 320,
[334] *CMS Award*, *supra* (n 97) ¶ 153.

> "... Argentina faced severe economic and social hardship from 2001 onwards and had to react to the circumstances prevailing at the time. Even though the measures adopted by Argentina may not have been the best, they were not taken lightly, without due consideration."

878. In the Tribunal's view it is likely that the GOA tried to take the best measures to cope with the situation. As shown by the diverging views expressed on the subject by commentators of the Argentinian crisis of 2001, it is very difficult to assess whether those measures were the best. The only issue to be verified by the Tribunal in this context is whether these measures were taken arbitrarily. In the Tribunal's view, based on the documents and the oral hearing, it seems that the measures adopted were the result of reasoned judgment rather than simple disregard of the rule of law, which means that they cannot be considered arbitrary. However, the Tribunal's analysis, characterising the measures as not arbitrary does not mean that such measures are characterised as fair and equitable or regarded as not having affected the stability of the legal framework under which gas producing companies in Argentina operated.

2. Discriminatory Treatment: Have the Claimants been discriminated against?

a. <u>The Parties' Positions</u>

879. According to the Claimants' memorial, Argentina's measures specifically targeted foreign owners of the privatised public industries and energy companies to bear the brunt of Argentina's measures and the country's economic downturn. The Claimants further contend:

> "In particular GOA's restrictions on exports are a classic case of discriminatory treatment. Under Resolution SE 599/07, the GOA heavily discriminated against GAS producers, like MASA who refused to sign the Second Gas Agreement. Resolution SE 599/07 set a new priority order for export curtailments and "re-routing" of gas volumes to the domestic market. In case of any shortfall in the gas supply to the domestic market, Resolution SE 599/07 requires that the export curtailments and re-routing measures first apply to Non-Signing Producers. Only after curtailing and re-routing the exports and

> domestic sales of Non-Signing Producers, do the restrictions apply, if required, to the exports and domestic sales of Signing Producers.
>
> Resolution SE 599/07 also establishes that Non-Signing Producers will be remunerated for their re-routed volumes at prices substantially lower than those paid to Signing Producers will. As a result, the prices Claimants receive for their re-routed gas volumes are not only substantially lower than those agreed in contracts with their export customers, but they are also lower than the prices the Signing Producers receive for their re-routed volumes. The GOA's regime of curtailing and re-routing is therefore discriminatory because it provides "differential treatment applied to people who are in similar situations." Moreover, these measures are not simply discriminatory in effect; they also explicitly intend to discriminate against producers who do not sign the Second Gas Agreement.
>
> In addition, the GOA's decision to alter the terms of private contracts constituted discriminatory treatment. By locking MEDA and MASA into frozen energy prices in Pesos at pre-devaluation levels while other sectors of the economy were not subject to price controls or similar restrictions, the GOA shifted the cost of the Peso's devaluation and Argentina's economic difficulties to energy companies. Essentially, Argentina forced the gas producers to bear a disproportionate portion of Argentina's financial difficulties in order to cross-subsidize the rest of its economy by approximately US$ 4.7 billion.[335]
>
> Further, the GOA's Export Withholdings are discriminatory. They tax gas exports at a rate that exceeds the tax treatment for exports of petroleum products and the tax treatment for products that use gas as a raw material in express contradiction of the protection against this type of discrimination established by the Chile-Argentina Energy Treaty. Through Export Withholdings, the GOA targeted gas producers with higher taxes to pay for expensive gas imports"

880. The Claimants conclude:

> "The above elements show that Argentina's conduct toward Claimants was discriminatory: (i) the GOA's hostility toward foreign investors; (ii) specific statements of high level Argentine officials targeting foreign investors (particularly in the energy sector); (iii) measures that had a disproportionate effect on the energy sector, and particularly, the hydrocarbon producers; and (iv) the GOA's overt discrimination

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[335] Claimants' Memorial on the Merits ¶¶ 360-363.

> between gas producers that acquiesced to its unlawful measures and those that did not."[336]

881. According to Argentina, the existence of discrimination in accordance with Article II.2 (b) of the BIT entails: (a) different treatment to the foreign investor on the basis of nationality; (b) less favourable treatment than that accorded to others in like circumstances; (c) intention to harm the foreign investor; (d) actual damage to the foreign investor; and (e) lack of reasonable grounds to provide differential treatment. Argentina asserts that these elements are cumulative.

882. Therefore Argentina concludes that for discrimination to exist

> "... the investor must be provided with differential treatment on the basis of nationality, which treatment must be less favorable than that accorded to other investors in a similar situation, must be provided with the intention to harm such investor, must cause actual damage to the investor and must not be justified by reasonable motives."

b. The Tribunal's Analysis

883. The Tribunal does not agree with Argentina's contention that the existence of discrimination in accordance with Article II (2) of the BIT entails different treatment to the foreign investor on the basis of nationality. As the Claimants submit Article II (2) expressly prohibits the impairment of investment through discrimination as an independent standard that does not require national treatment violation. The Tribunal finds that neither the ordinary meaning of "discrimination" in Article II (2), the context of the BIT, which includes a separate national treatment provision, nor the cases relied on by Argentina absent a distinctive treaty language, support requiring a national treatment violation in order to find a State measure discriminatory. As Professor Schreuer has observed, although most of the practice dealing with

[336] *Ibid*, para 364.

discrimination focuses on nationality, this does not mean that the issue of discrimination is necessarily restricted to nationality.[337]

884. There is common ground between the parties that unequal treatment is only discriminatory among subjects that are in like circumstances. However, the Respondent disagrees with the Claimants' contention that investors in different economic sectors may be in "like circumstances" for certain measures. In the Tribunal's view, the standard of the BIT, according to which *foreign investors* are protected against discrimination, does not entail the far-reaching consequence that a State cannot treat differently the economic actors in different sectors of the economy, as long as this differential treatment applies equally to national and foreign investors. However, the Tribunal agrees with the Claimants that depending on the nature of the measure at issue, the relevant circumstances for determining "likeness" between two economic actors and/or their respective sectors may differ. For example in *Occidental*, the Tribunal interpreted a BIT that provided for national treatment and held:

> "… "in like situations" cannot be interpreted in the narrow sense as advanced …as the purpose of national treatment is to protect investors as compared to local producers, and this cannot be done by addressing exclusively the sector in which that particular activity is undertaken."[338]

885. Also the tribunals in *Enron* and *Sempra* held that discrimination between sectors that was "capricious, irrational or absurd" would violate the BIT. [339]

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[337] C. Schreuer, *Protection against Arbitrary or Discriminatory Measures* at 12 and Rudolf Dolzer-Christoph.Schreuer, Principles of International Investment Law (2008) p.176.
[338] *Occidental Exploration and Production Company v Repuiblic of*, UNCITRAL, Award (1 July 2004) *Ecuador* [hereinafter *"Occidental Award"*] ¶ 173.
[339] *Enron Award*, *supra* (n 314) ¶ 282 and *Sempra*, *supra* (n 315) ¶ 319.

886. Moreover, the Tribunal does not agree that discriminatory measures require an intent to harm the investor in question. Such a requirement appears nowhere in the text of the BIT, and the case law interpreting the BIT does not support such a requirements. For instance, the Tribunal in Siemens held that "intent is not decisive or essential for a finding of discrimination, and that the impact of the measure on the investment would be the determining factor to ascertain whether it had resulted in non-discriminatory treatment."[340] The *LG&E* Tribunal held that "[i]n the context of investment treaties, and the obligation there under not to discriminate against foreign investors, a measure is considered discriminatory if the intent of the measure is to discriminate **or** if the measure has discriminatory effect" [emphasis added].[341] It is thus, as found by the Tribunal in *El Paso,* sufficient that, objectively, two similar situations are not treated similarly. [342]

887. As mentioned above, the standard of the BIT according to which *foreign investors* are protected against discrimination does not, in the Tribunal's view entail the far-reaching consequence that a State cannot treat differently the economic actors in different sectors of the economy, as long as this differential treatment applies equally to national and foreign investors. None of the impugned measures, adopted to face the economic crisis differentiated in legal terms between Argentinian nationals and companies or foreign or foreign-owned companies, on the other. There is no evidence that any foreign investor has received treatment different from that granted to its Argentinian counterparts, and the Claimants have received the same treatment as other investors in the same sector.

[340] *Siemens Award, supra* (n 96) ¶ 321.
[341] *LG&E Energy Corp, LG&E Capital Corp* and *LG&E International, Inc v Argentine Republic*, ICSID Case No ARB/02/1, Award (25 July 2007) [hereinafter "*LG&E Award"*] ¶ 146.
[342] *El Paso Award, supra* (n 307) ¶ 305.

888. The question that remains is whether the Claimants can be held to be in "like circumstances" as some other economic sector and the impugned measures therefore are discriminatory.

889. The Claimants' contend that the GOA's decision to lock gas producers into frozen energy prices in Pesos at pre-devaluation levels while other sectors of the economy were not subject to price controls was discriminatory. According to the Claimants the GOA thereby shifted the cost of the Peso's devaluation and Argentina's economic difficulties to energy companies and forced the gas producers to bear a disproportionate portion of Argentina's financial difficulties in order to cross-subsidize the rest of its economy by approximately US$4.7 billion.

890. The Tribunal finds that the Claimants have not established that this measure was specifically aimed at foreign companies and not of a general nature. It is not denied that other sectors of the economy were not subject to price control and similar restrictions as gas producers, but in the Tribunal's view, this does mean that the gas sector was discriminated. On the contrary, as stated by the tribunal in *El Paso,* the overall scheme adopted by the GOA had the objective of balancing for each sector the advantages or disadvantages of the general economic situation.[343] Moreover, the Presidential Decree No, 689/02 excluded natural gas purchase and sale export contracts from pesification. As far as the Gas Sector was concerned, the exports continued to be denominate in US dollars, whereas the gas producers' costs were still expressed in Argentine pesos, the gas producers seemed to be in a more favourable position than those which did not export.

891. The Claimants contend that the most direct act of discrimination of GOA against the Claimants was through the Second Gas Agreement and Resolution SE 599/07.

[343] *El Paso Award, supra* (n 307) ¶ 310.

Through those instruments, the GOA imposed an obligation on non-signing producers to supply the domestic market, which it did not impose on producers that acquiesced to the Government's pressure to sign the agreement. The reality was that the Government re-routed the gas of non-signing producers first to cover insufficiency in the supply quotas agreed by the signing producers, and sent those volumes to the customers that paid the lowest price for their gas.

892. The Tribunal is of the view that non-signatory producers are not in the same circumstances as signatory producers, since the latter have made commitments to supply the domestic market, while the former have not. The Second Gas Agreement was an open agreement, which means that anyone could enter into or terminate it at any time. As Argentina argues, producers who did not sign the agreement are required to comply with their legal duty to supply the domestic market because, unlike the signatory producers, they have not committed to contributing any exportable natural gas to the domestic market.

893. To conclude, it is the Tribunal's view that a differential treatment based on the existence of a different factual and legal situation does not breach the BIT standard. Here the Tribunal is in line with other Tribunals cited and finds itself in agreement with the Tribunals in *El Pas*o and *Enron*, which found no discrimination between the different sectors of economy, although they were treated differently, as there was no "capricious, irrational or absurd differentiation in the treatment accorded to the Claimants as compared to other entities or sectors." Thus, the Tribunal concludes that the Claimants have not proven any improper differentiation with could be held as discriminatory treatment.

E. FAIR AND EQUITABLE TREATMENT

894. Article II(2)(a) of the BIT provides;

> "Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law."

895. The BIT emphasises this treatment by including in its preamble: "agreeing that fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment and maximum effective use of economic resources."

896. As can be seen below, two main issues are raised by the application of the fair and equitable treatment (FET) standard in an arbitration case: the first concerns the relation of FET with general international law, whereas the second is the determination of its content and scope.

1. The Parties' positions

897. The Claimants aver that neither a proper interpretation of Article II(2)(a) of the BIT nor the case law and commentary support the view that the fair and equitable treatment standard in the BIT is equivalent to the minimum standard under customary international law. The Claimants refer to the wording "and shall in no case be accorded treatment less than that required by international law" and assert that the BITs use of the connector "and" indicates that the fair and equitable treatment standard is in addition to the treatment required by customary international law. Thus fair and equitable treatment requires something above and beyond customary international law. Moreover, the Claimants contend that numerous tribunals have confirmed that the distinction between the *lex specialis* fair and equitable treatment provisions found in many BITs and the minimum standard may be illusory in any event, because the minimum standard has evolved to provide a broad scope of investment protection.

898. According to the Claimants the protection of an investor's legitimate expectations constitutes an integral aspect of fair and equitable treatment. The Claimants acknowledge that legal stability is not the only goal outlined in the BIT's Preamble,

but maintain that providing a stable framework is certainly one of the BIT's most central goals.

899. The Claimants aver that they are not arguing that BITs are a form of risk insurance, are designed to guarantee the profitability of investments, or are a mechanism to avoid risks stemming from general conditions in the economy. Rather, in congruence with principles of good faith and the decisions of numerous investment treaty tribunals, the Claimants maintain that the BIT's fair and equitable treatment standard requires Argentina to honour the Claimants' legitimate expectations and provide a stable legal and business framework as Argentina undertook to do in the BIT's Preamble, the Argentine President's submittal letter to the Argentine Congress, the public proclamations of Argentine officials, the Legal Framework, and in the Claimants' investment instruments

900. Argentina begins its discussion of FET by stating that "the fair and equitable standard under the …BIT corresponds to the minimum standard under customary international law." According to Argentina this is how the parties to the Treaty have understood it and Article II (2) (a) of the BIT does not require treatment in addition to or beyond that which is required by the minimum standard under customary international law. As far as the content of the notion is concerned, Argentina refers to the award in *Waste Management*[344] and concludes that there is a violation of the international minimum standard "when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective."

901. Even if the Tribunal did not accept that the fair and equitable standard of treatment set out in Article II (2) (a) of the BIT as equivalent to the international law minimum

[344] *Waste Management Award, supra* (n 317) ¶ 98.

standard, Argentina contends that the fair and equitable standard of treatment is not a guarantee against changes in the regulatory framework on the basis of its legitimate interests.

902. Argentina concludes that that the fair and equitable standard of treatment interpreted in accordance with the general rule of interpretation requires the host state to act in good faith and accord transparent and reasonable treatment free from arbitrariness and discrimination, and it does not protect the alleged legitimate expectations of a stable legal and business framework.

903. In addition, Argentina asserts that a violation of the fair and equitable treatment standard cannot be determined in the abstract and that accordingly, the vicissitudes of the economy of the host State are relevant to determine the investor's legitimate expectations. Moreover, in assessing a possible breach of the fair and equitable standard of treatment, the host State is to be afforded a margin of appreciation in the exercise of its regulatory powers in the public interest and for public purpose reasons. Argentina concludes that in sum, to evaluate whether the fair and equitable treatment has been breached, the circumstances of the case must be taken into account and the host State must be given a margin of appreciation to take measures in the public interest.

904. In its Rejoinder Argentina contends that the statement that the fair and equitable treatment includes an obligation to satisfy or not to frustrate the legitimate expectations that the investor had when making the investment does not coincide, in any language, which may be attributed to the terms "fair and equitable treatment." In conclusion, Argentina contends that the fair and equitable treatment standard, interpreted in accordance with the general rule of interpretation, requires good-faith, transparent and reasonable treatment, free from arbitrariness and discrimination, and does not protect legitimate expectations to the extent of an absolute stability of the commercial and legal framework, divorced from real circumstances.

2. The Tribunal's Analysis of the Legal Standard

905. The arguments exchanged by the parties raise the following two main issues:

(a) Whether the standard of fair and equitable treatment (FET) is a standard which merely reflects the international minimum standard, as contained in customary international law, or offers an autonomous standard that is additional to general international law; and

(b) What is the substantive content and scope of the FET standard? In other words what conduct attributable to the State can be characterized as unfair and inequitable?

906. We shall address in turn the two issued raised by the FET.

a. <u>The Relation of Fair and Equitable Treatment with the International Minimum Standard</u>

907. As far as the relation between FET and the minimum standard of international law is concerned we note that several ICSID tribunals have dealt with this question. Two main approaches have been adopted by those Tribunals.

908. Under the first approach, FET merely reflects the international minimum standard of treatment, as contained in customary international law, inasmuch the respective case before the Tribunal is concerned. This position can be found in *CMS v. Argentina*:

> "282. There is one additional aspect the Tribunal must examine having heard the arguments of the parties. That is whether the standard of fair and equitable treatment is separate and more expansive than that of customary international law, as held by the tribunal in *Pope and Talbot*, or whether it is identical with the customary international law minimum standard as argued by Argentina.
>
> 283. The Tribunal is mindful of the discussion prompted by these arguments, particularly with reference to the NAFTA Free Trade

> Commission's Note of Interpretation identifying the fair and equitable treatment standard with that of customary international law (footnote omitted). This development has led to further treaty clarifications as in the Chile-United State Free Trade Agreement (footnote omitted).
>
> 284. While the choice between requiring a higher treaty standard and that of equating it with the international minimum standard might have relevance in the context of some disputes, the Tribunal is not persuaded that it is relevant in this case. In fact, the Treaty standard of fair and equitable treatment and its connection with the required stability and predictability of the business environment, founded on solemn legal and contractual commitments, is not different from the international law minimum standard and its evolution under customary law." [345]

909. The second approach is to interpret the relevant provisions in BITs autonomously on the basis of their respective wording. In other words FET is regarded as an autonomous concept. This approach can be found in *Azurix v. Argentina*. The Tribunal said:

> "The clause, as drafted, permits to interpret fair and equitable treatment and full protection and security as higher standards than required by international law. The purpose of the third sentence is to set a floor, not a ceiling, in order to avoid a possible interpretation of these standards below what is required by international law. While this conclusion results from the textual analysis of this provision, the Tribunal does not consider that it is of material significance for its application of the standard of fair and equitable treatment to the facts of the case. As it will be explained below, the minimum requirement to satisfy this standard has evolved and the Tribunal considers that its content is substantially similar whether the terms are interpreted in their ordinary meaning, as required by the Vienna Convention, or in accordance with customary international law." [346]

910. While one may, as the *Azurix* tribunal, from the textual analysis of Article II(2)(a) of the BIT conclude that the purpose of the third sentence is to set a floor, not a ceiling, in order to avoid a possible interpretation of these standards below what is required by international law, this Tribunal does not consider that this sentence is of material

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[345] *CMS Award, supra* (n 97) ¶ 282-284.
[346] *Azurix Award, supra* (n 97) ¶ 361.

significance for its application of the standard of fair and equitable treatment to the facts of the case. The scope and content of the minimum standard of international law is, as the FET standard, undefined or weakly defined. It is common ground that the minimum standard of international law has evolved over time. As can be seen from the quotations above from *Azurix*, it is difficult to make a distinction between the FET and the international minimum standard, as contained in customary international law. Although the *Azurix* tribunal found that the FET clause in the BIT permits to interpret FET as a higher standard than required by international law, it stated after this declaration that the minimum requirement to satisfy this standard has evolved and the Tribunal considers that its content is substantially similar whether the terms are interpreted in their ordinary meaning, as required by the Vienna Convention on the Law of Treaties (hereinafter the **"Vienna Convention")** or in accordance with customary international law. This Tribunal therefore does not find it necessary to further discuss whether FET is a standard which merely reflects the international minimum standard, as contained in customary international law, or offers an autonomous standard that is additional to general international law.

911. This Tribunal finds that the position according to which FET is equivalent to the international minimum standard is more in line with the evolution of investment law and international law and with the identical role assigned to FET and to the international minimum standard. In this Tribunal's view, the specific role played by both the general international minimum standard and the FET standard as found in BITs is to ensure that the treatment of foreign investments, which are protected by the national treatment and the most-favoured investors' clauses, do not fall below a certain minimum, in case the two mentioned standards do not live up to that minimum.

912. Thus, in the Tribunal's view the FET is not to be viewed with reference to national law – in which case it could be lower than required by international law – but has to be interpreted with reference to international law, the result being that it cannot go

below what is required by international law, which is the standard to be applied. But if national law or the treatment accorded to some foreigners exceeds this minimum international standard, it is one of the former that has to be applied. This Tribunal thus considers, like the *El Paso* Tribunal,[347] that the FET of the BIT is the international minimum standard required by international law, regardless of the protection afforded by the national legal orders.

b. The Content and Scope of Fair and Equitable Treatment

913. The term "fair and equitable treatment" is not defined. Pursuant to Article 31 (1) of 1969 Vienna Convention, a treaty is to be interpreted "in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose." As the Annulment Committee in the *CMS* case has noted ... the fair and equitable standard has been invoked in a great number of cases brought to ICSID arbitration and ...there is some variation in the practice of arbitral tribunals in this respect."[348]

914. The Tribunal agrees with the general description given by Claimant in its Memorial in the following citation:

> "It has become clear that the basic touchstone of fair and equitable is to be found in the legitimate expectations of the parties. In addition to protecting an investor's legitimate expectations, the fair and equitable treatment includes: the requirement of a stable, consistent, and predictable legal framework; transparency; procedural propriety and

[347] *El Paso Award, supra* (n 307) ¶ 337.
[348] *CMS Gas Transmission Company v The Argentine Republic*, ICSID Case No ARB/01/8, Decision of *ad hoc* Committee on the Application for Annulment (25 September 2007) [hereinafter "*CMS Decision on Annulment"*] note 86.

> due process; good faith; and freedom from harassment and coercion."[349]

915. However, within this general acceptable definition, some tribunals have extended the scope of the FET to a point where, in the view of this Tribunal the sovereign power of the state to regulate its economy is negated, as will be developed below.

3. The Different Conceptions used by Arbitral Tribunals

916. Some Tribunals have used a very broad conception of FET. The exigencies of FET have been described in *Tecmed* as follows:

> "To provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any pre-existing decisions or permits issued by the state that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the state to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation."[350]

917. However, the *ad hoc* Annulment Committee in the *MTD* case did not adopt the very broad definition in *Tecmed* on which the *MTD* tribunal had relied. It said:

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[349] Claimants' Memorial on the Merits ¶ 229 with reference to R.Dolzer and C. Schreuer, Principles of International Investment Law (Oxford 2008) p. 133.
[350] *Tecmed Award, supra* (n 95) ¶ 154.

> "According to the Respondent, "the *TecMed* programme for good governance" is extreme and does not reflect international law. The *TECMED* dictum is also subject to strenuous criticism from the Respondent's experts, Mr. Jan Paulsson and Sir Arthur Watts. They note, *inter alia*, the difference between the *TECMED* standard and that adopted in other cases, including one the Tribunal also cited in a footnote but without comment.
>
> The Committee can appreciate some aspects of these criticisms. For example the *TECMED* Tribunal's apparent reliance on the foreign investor's expectations as the source of the host State's obligations (such as the obligation to compensate for expropriation) is questionable. The obligations of the host State towards foreign investors derive from the terms of the applicable investment treaty and not from any set of expectations investors may have or claim to have. A tribunal which sought to generate from such expectations a set of rights different from those contained in or enforceable under the BIT might well exceed its powers, and if the difference were material might do so manifestly."[351]
>
> Secondly, in the Committee's view the formulation of the fair and equitable treatment standard adopted by the Tribunal was that contained in paragraph 113 of the Award, where it said:
>
> "in terms of the BIT, fair and equitable treatment should be understood to be treatment in an even-handed and just manner, conducive to fostering the promotion of foreign investment. Its terms are framed as a pro-active statement – 'to promote,' 'to create,' 'to stimulate' – rather than prescriptions for a passive behavior of the State or avoidance of prejudicial conduct to the investors."
>
> The *TECMED* dictum was cited in support of this standard, not in substitution for it."[352]

Moreover, the *ad hoc* Committee addresses the definition of FET given by the *MTD* tribunal and states as follows:

> "…a standard formulated in the terms of paragraph 113 is defensible. No doubt the extent to which a State is obliged under the fair and equitable treatment standard to be pro-active is open to debate, but that

[351] *MTD Decision on Annulment, supra* (n 318) ¶¶ 66-67.
[352] *Ibid* ¶ 70.

> is more a question of application of the standard than it is of formulation. In any event the emphasis in the Tribunal's formulation is on "treatment in an even-handed and just manner."[353]

918. As pointed out by the Claimants, the Committee also made the following remarks recognising the significance of an investor's legitimate expectations under investment treaties:

> "…legitimate expectations generated as a result of the investor's dealings with the competent authorities of the host State may be relevant to the application of the guarantees contained in an investment treaty. This is expressly accepted by the Respondent and in the case-law."[354]

919. Another slightly far-reaching conception which implies that the State is under an obligation to stabilise the legal and business framework in which the foreign investment was made, was adopted by the Tribunal in *Occidental*:

> "Although fair and equitable treatment is not defined in the Treaty, the Preamble clearly records the agreement of the parties that such treatment 'is desirable in order to maintain a stable framework for investment and maximum effective utilization of economic resources.' The stability of the legal and business framework is thus an essential element of fair and equitable treatment."[355]

920. The Tribunal further noted:

> "The relevant question for international law in this discussion is...whether the legal and business framework meets the requirement of stability and predictability under international law....there is certainly an obligation not to alter the legal and business environment in which the investment has been made. In this case it is the latter question that triggers a treatment that is not fair and equitable."[356]

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[353] *Ibid* ¶ 71.
[354] *MTD Decision on Annulment, supra* (n 318) ¶ 69.
[355] *Occidental Award, supra (*n 338) ¶ 183.
[356] *Ibid*, ¶191.

921. This conception was also adopted by ICSID tribunals in some of the already decided Argentinian cases. In those cases the Preamble of the Treaty was relied upon in order to identify the object and purpose of the BIT. The *CMS* tribunal referred to the Preamble of the Argentina-US BIT to construe the FET standard:

> "The Treaty Preamble makes it clear, however, that one principal objective of the protection envisaged is that fair and equitable treatment is desirable 'to maintain a stable framework for investments and maximum use of economic resources.' There can be no doubt, therefore, that a stable legal and business environment is an essential element of fair and equitable treatment."[357]

922. The tribunal in *LG&E* expressly approved the standard set by those Tribunals when analysing the BIT, and concluded:

> "In considering the context within which Argentina and the United States included the fair and equitable treatment standard, and its object and purpose the Tribunal observes in the Preamble of the Treaty that the two countries agreed that "fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment and maximum effective use of economic resources." In entering the Bilateral Treaty as a whole, the parties desired to "promote greater economic cooperation" and "stimulate the flow of private capital and the economic development of the parties". In light of these stated objectives, this Tribunal must conclude that stability of the legal and business framework is an essential element of fair and equitable treatment in this case, provided that they do not pose any danger for the existence of the host State itself."[358]

923. Moreover, the Tribunal referred, *inter alia*, to the *CMS* and *Occidental* cases and concluded:

> "These Tribunals have repeatedly concluded based on the specific language concerning fair and equitable treatment, and in the context of the stated objectives of the various treaties, that the stability of the legal and business framework in the State party is an essential element in the standard of what is fair and equitable treatment. As such, the Tribunal

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[357] *CMS Award*, *supra* (n 97) ¶ 274.
[358] *LG&E Decision on Liability, supra* (n 309) ¶ 124.

> considers this interpretation to be an emerging standard of fair and equitable treatment in international law." [359]
>
> * * * *
>
> "Thus, this Tribunal, having considered, as previously stated, the sources of international law, understands that the fair and equitable standard consists of the host State's consistent and transparent behavior, free of ambiguity that involves the obligation to grant and maintain a stable and predictable legal framework necessary to fulfil the justified expectations of the foreign investor."[360]

924. There are, however, ICSID tribunals that have adopted much narrower conceptions of FET. Such an approach, which considers that FET is only violated by wilful bad faith behaviour of the State, has been adopted by the Tribunal in *Genin*:

> "While the exact content of this standard is not clear, the Tribunal understands it to require an "international minimum standard" that is separate from domestic law, but that is, indeed, a *minimum* standard. Acts that would violate this minimum standard would include acts showing a wilful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith."[361]

925. The tribunal in the *EDF* case stated that:

> "The Tribunal shares the view expressed by other tribunals that one of the major components of the FET standard is the parties' legitimate and reasonable expectations with respect to the investment they have made. Claimant has specifically referred to this component. It comes into consideration whenever the treatment attributable to the State is in breach of representations made by it which were said to be reasonably relied upon by the Claimant…
>
> The idea that legitimate expectations, and therefore FET, imply the stability of the legal and business framework, may not be correct if stated in an overly-broad and unqualified formulation. The FET might then mean the virtual freezing of the legal regulation of economic

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[359] *Ibid*, ¶ 125.
[360] *Ibid*, ¶ 131.
[361] *Alex Genin and others v Republic of Estonia,* ICSID Case No. ARB/99/2, Award (25 June, 2001) ¶ 367.

> activities, in contrast with the State's normal regulatory power and the evolutionary character of economic life. Except where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework. Such expectation would be neither legitimate nor reasonable."[362]

926. The Tribunal in the *Parkerings* case held that:

> "It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilisation clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment. As a matter of fact, any businessman or investor knows that laws will evolve over time. What is prohibited however is for a State to act unfairly, unreasonably or inequitably in the exercise of its legislative power."[363]

927. Although there are different conceptions of FET emerging from ICSID case-law, the legitimate expectations of the investors have generally been considered central in the definition of FET, whatever its scope. As the Tribunal in the *El Paso* case stated, "[t]here is an overwhelming trend to consider the touchstone of fair and equitable treatment to be found in legitimate and reasonable expectations of the Parties, which derive from the obligation of good faith." [364] Thus the Tribunal in *Waste Management II* stated: "In applying this standard it is relevant that the treatment is in breach of representations made by the host state which were reasonably relied on by the claimant".[365] The tribunal in *Saluka* expressed the same idea, when stating: "The

[362] *EDF (Services) Award* (n 282) ¶ 216-217.
[363] *Parkerings Award, supra* (n 282) ¶ 332.
[364] *El Paso Award, supra* (n 307) ¶ 348.
[365] *Waste Management Award, supra* (n 317) ¶ 98.

standard of "fair and equitable treatment" is therefore closely tied to the notion of legitimate expectations which is the dominant element of that standard." [366]

4. The Tribunal's understanding of fair and equitable treatment

928. In the Tribunal's view, meeting the investor's legitimate concern of legal consistency, stability and predictability is a major but not the only ingredient of an investment-friendly climate in which the host state in turn can reasonably expect to attract foreign investment. However, the FET standard shall nevertheless not be understood to amount to a stabilisation clause, but will leave a measure of governmental space for regulation. As stated by the tribunal in *El Paso* the often repeated formula to the effect that "the stability of the legal and business framework is an essential element of fair and equitable treatment", if strictly applied is not realistic and "the BIT's purpose is not that the States guarantee that the economic and legal conditions in which investments take place will remain unchanged for ever."[367]

929. Even the Claimants accept the view that legal stability is not the only goal outlined in the BIT's Preamble, but maintain that providing a stable investment framework is certainly one of the BIT's most explicit goals. Moreover, in their Reply the Claimants stated that:

> "To summarize, Argentina rebuts a strawman by arguing that it was not required to freeze its legal system in place upon issuing guarantees in the Legal Framework and Claimants' investment instruments. Claimants are not arguing the BITs are a form of risk insurance, are designed to guarantee the profitability of investments, or are a mechanism to avoid risks stemming from general conditions in the economy." Rather, in congruence with principles of good faith and the decisions of numerous investment treaty tribunals, Claimants maintains that the BIT's fair and equitable treatment standard requires Argentina

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[366] *Saluka Investment BV v The Check Republic*, UNCITRAL, Partial Award (17 March 2006) [hereinafter "*Saluka Partial Award"*] ¶ 302.
[367] *El Paso Award, supra* (n 307) ¶ 350.

> to honor Claimants' legitimate expectations and provide a stable legal and business framework as Argentine undertook to do in the BIT's Preamble, the Argentine President's submittal letter to the Argentine Congress, the public proclamations of Argentine officials, the Legal Framework, and in Claimants´ investment instruments.[368]

930. This Tribunal cannot follow the line of cases in which fair and equitable treatment was seen as implying the stability of the legal and business framework.[369]

931. The Tribunal follows the overwhelming practice by ICSID tribunals mentioned above, which considers that the concept of fair and equitable treatment must be analysed with due consideration of the legitimate expectations of the Parties, but it will discuss the interpretation to be given to such a statement. At the outset the Tribunal notes that of course all expectations that an investor would like to rely on in order to maximise their benefits cannot be considered legitimate and reasonable. The Tribunal will below specify what in its opinion can be viewed as legitimate and reasonable expectations.

a. The Linkage of Fair and Equitable Treatment with Objective Legitimate and Reasonable Expectations of Foreign Investors

932. In the Tribunal's view foreign investors' legitimate and reasonable expectations, as well as their violation, have to be examined objectively. The Tribunal agrees with the following statement by the *CMS* Annulment Committee:

> "Although legitimate expectations might arise by reason of a course of dealing between the investor and the host state, these are not, as such legal obligations, though they may be relevant to the application of the fair and equitable treatment clause contained in the BIT."[370]

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[368] Claimants' Reply on the Merits, ¶ 208.
[369] See also *El Paso Award, supra* (n 307) ¶ 352.
[370] *CMS Decision on Annulment, supra* (n 348) ¶ 89.

933. This Tribunal considers that the notion of "legitimate expectations" is an objective concept, that is the result of balancing interests and rights, and it varies according to the context. Thus these expectations, as well as, their violation, have to be examined objectively.

b. <u>Legitimate Expectations can be breached even in the absence of bad faith of the State</u>

934. Although action in bad faith is a violation of fair and equitable treatment, a violation of the standard can be found even if there is a mere objective disregard of the rights enjoyed by the investor under the FET standard. Thus such a violation does not require bad faith on the part of the State. This has been stated in several ICSID awards.

935. In *CMS* the Tribunal said:

> "The Tribunal believes this is an objective requirement unrelated to whether the Respondent has had any deliberate intention or bad faith in adopting the measures." in question. Of course, such intention and bad faith can aggravate the situation but are not an essential element of the standard."[371]

936. Likewise in *Azurix*, the Tribunal explained:

> "To encourage and protect investment is the purpose of the BIT. It would be incoherent with such purpose and the expectations created by such a document to consider that a party to the BIT has breached the obligation of fair and equitable treatment only when it has acted in bad faith or its conduct can be qualified as outrageous or egregious."[372]

[371] *CMS Award, supra* (n 97) ¶ 280.
[372] *Azurix Award, supra* (n 97) ¶ 372.

937. This analysis was also followed in *LG&E*, where the Tribunal said that it "was not convinced that bad faith or something comparable would ever be necessary to find a violation of fair and equitable treatment"[373] and more recently in *El Paso.*[374]

c. Fair and Equitable Treatment May Protect Investors from Harassment and Coercion

938. There is some authority that the FET standard may also apply in situations of harassment and coercion directed at the investor. In *Pope & Talbot* SLD, a government regulatory authority, had launched a "verification review" against the investor that was confrontational and aggressive. The tribunal held that this investigation amounted to a violation of the fair and equitable treatment standard contained in Article 1105 of the NAFTA:

> "The relations between the SLD and the Investment during 1999 were more like combat than cooperative regulation, and the Tribunal finds that the SLD bears the overwhelming responsibility for this state of affairs… In its totality, the SLD's treatment of the Investment during 1999 in relation to the verification review process is nothing less than a denial of the fair treatment required by NAFTA Article 1105, and the Tribunal finds Canada liable to the Investor for the resultant damages."[375]

939. In its subsequent award, the *Pope & Talbot* tribunal described these actions by the regulatory authority as "threats and misrepresentations" and as "burdensome and confrontational" and confirmed its finding of a violation of the FET standard.[376]

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[373] *LG&E Decision on Liability. Supra* (n 309) ¶ 129.
[374] *El Paso Award*, *supra*(n 307) ¶ 357.
[375] *Pope & Talbot Inc v Government of Canada*, UNCITRAL (NAFTA), Award on the Merits of Face 2(10 April, 2001) ¶ 81.
[376] *Pope & Talbot Inc v Government of Canada*, UNCITRAL (NAFTA), Award in Respect of Damages (31 May, 2002) ¶¶ 67-69.

940. In *Tecmed*, an unlimited license for the operation of a landfill had been replaced by a license of limited duration. The tribunal applied a provision in the BIT between Mexico and Spain guaranteeing fair and equitable treatment according to international law. The tribunal found that the denial of the permit's renewal was designed to force the investor to relocate to another site, bearing the costs and the risks of a new business. The tribunal said:

> "Under such circumstances, such pressure involves forms of coercion that may be considered inconsistent with the fair and equitable treatment to be given to international investments under Article 4(1) of the Agreement and objectionable from the perspective of international law."[377]

941. Also the *LG&E* provides some authority for the proposition that an imposed alteration of a contract under the label of renegotiations and enforced waiver of a right to seek remedies amounts to a violation of the fair and equitable treatment standard. With respect to gas distribution licences, the Tribunal held:

> "Argentina also has acted unfairly and inequitably in forcing the licensees to renegotiate public service contracts, and waive the right to pursue claims against the Government, or risk rescission of the contracts. Even though the Gas Law provided for the renegotiation of public service contracts, in practice there was no real renegotiation, but rather the imposition of a process."[378]

d. Legitimate Expectations Result from a Confrontation of the Objective Expectations of Investors and the Right of the State to Regulate.

942. A balance should be established between the legitimate expectations of the foreign investor to make a fair return on its investment and the right of the host state to regulate its economy in the public interest. The *Saluka* tribunal stated:

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[377] *Tecmed Award, supra* (n 95)¶163.
[378] *LG&E Decision on Liability, supra* (n 309) ¶ 137.

> "No investor may reasonably expect that the circumstances prevailing at the time the investment is made remain totally unchanged. In order to determine whether frustration of the foreign investor's expectations was justified and reasonable, the host State's legitimate right subsequently to regulate domestic matters in the public interest must be taken into consideration as well."[379]

> "A foreign investor protected by the Treaty may in any case properly expect that the Czech Republic implements its policies *bona fide* by conduct that is, as far as it affects the investors' investment, reasonably justifiable by public policies and that such conduct does not manifestly violate the requirements of consistency, transparency, even-handedness and non-discrimination. In particular, any differential treatment of a foreign investor must not be based on unreasonable distinctions and demands, and must be justified by showing that it bears a reasonable relationship to rational policies not motivated by a preference for other investments over the foreign-owned investment."[380]

943. Thus an interpretation of the fair and equitable treatment standard in the light of the object and purpose of the BIT should strike a balance between the interests of foreign investors and States pursuance of the public interests.

e. Legitimate Expectations Necessarily Vary with the Circumstances

944. A violation of FET standard cannot be determined in the abstract. What is fair and reasonable in the light of a given circumstance may well not be so in the light of a different one. Thus_legitimate expectations necessarily vary with the surrounding circumstances. In *Noble Ventures* the tribunal explained that:

> "Although in this respect Art. II(2)(a) mirrors standard clauses in BITs and other international instruments and courts and tribunals have been concerned with violations of fair and equitable treatment standards, the

[379] *Saluka Partial Award, supra* (n 366) ¶ 305.
[380] *Ibid*, ¶ 307.

> question whether those standards have been violated has to be considered in the light of the circumstances of each case."[381]

945. Accordingly, the vicissitudes of the economy of the host State are relevant to determine the investor's legitimate expectations. If a State faces a serious economic crisis, this fact must be taken into consideration in assessing the scope of protection due to a foreign investor. Thus, for instance, in finding that the fair and equitable standard of treatment had not been breached, the *Noble Ventures* tribunal took into account "the indisputably dramatic economic situation" in Romania.[382]

946. Also the *Saluka* tribunal did not consider investors' expectations in absolute terms, existing in a vacuum and unchangeable in the light of the circumstances of the case and the environment. The Tribunal stated:

> "Moreover, the scope of the Treaty's protection of foreign investment against unfair and inequitable treatment cannot exclusively be determined by foreign investors' subjective motivations and considerations. Their expectations, in order for them to be protected, must rise to the level of legitimacy and reasonableness *in light of the circumstances.* "[383]

947. Also the tribunal in *Continental* stressed the importance of the circumstances, when evaluating a violation of FET:

> "Moreover, the content of the obligation incumbent upon the host state to treat a foreign investor in a fair and equitable manner, even when applicable "at all times" as specified in Art. II(2)(a) of the BIT, varies in part depending on the circumstances in which the standard is invoked: the concept of fairness being inherently related to keeping justice in variable factual contexts."[384]

948. More recently the tribunal in *El Paso* concluded:

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[381] *Noble Ventures Award, supra* (n 332) ¶ 181.
[382] *Noble Ventures Award, supra* (n 332) ¶ 182.
[383] *Saluka Partial Award, supra* (n 366) ¶ 304.
[384] *Continental Award, supra* (n 316) ¶ 255.

> "In sum, the Tribunal considers that FET is linked to the objective reasonable legitimate expectations of the investors and that these have to be evaluated considering all circumstances. As a consequence, *the legitimate expectations of a foreign investor can only be examined by having due regard to the general proposition that the State should not unreasonably modify the legal framework or modify it in contradiction with a specific commitment not to do so*, as will be shown below." [385]

949. This Tribunal agrees with that statement of the tribunal in *El Paso*.

5. How to define the standard of Fair and Equitable Treatment

a. Fair and Equitable Treatment Implies that there Is No Unreasonable or Unjustified Modification of the Legal Framework

950. Despite the standard reference to "the stability of the legal and business framework", this cannot, as stated by the Tribunal in El *Paso*, "mean that when concluding a BIT a state gives any guaranty to foreigners concerning its economic health and the maintenance of the economic conditions for business prevailing at the time of the investment."[386] This Tribunal agrees with the Tribunal in *Saluka*, which stated that:

> "This Tribunal would observe, however, that while it subscribes to the general thrust of these and similar statements [referring to the stability of the business and legal framework], it may be that, if their terms were to be taken too literally, they would impose upon host States' obligations which would be inappropriate and unrealistic."[387]

951. This Tribunal further shares the views of the tribunal in *Parkerings*, which stated:

> "It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a stabilisation clause or otherwise, there is

[385] *El Paso Award, supra* (n 307) ¶ 364.
[386] *El Paso Award, supra* (n 307) ¶ 365.
[387] *Saluka Partial Award, supra* (n 366) ¶ 304.

> nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment."[388]

952. As the tribunal in *El Paso* stated:

> "Under a FET clause, a foreign investor can expect that the rules will not be changed without justification of an economic, social or other nature. Conversely, it is unthinkable that a State could make a general commitment to all foreign investors never to change its legislation whatever the circumstances, and it would be unreasonable for an investor to rely on such a freeze."[389]

953. The same point was also made by the tribunal in Continental:

> "On the other hand, it would be unconscionable for a country to promise not to change its legislation as time and needs change, or even more to tie its hands by such a kind of stipulation in case a crisis of any type or origin arose. Such an implication as to stability in the BIT's Preamble would be contrary to an effective interpretation of the Treaty; reliance on such an implication by a foreign investor would be misplaced and, indeed, unreasonable."[390]

954. This Tribunal shares the views of the Tribunal in *El Paso*, which stated that

> "...fair and equitable treatment is a standard entailing reasonableness and proportionality. It ensures basically that the foreign investor is not unjustly treated, with due regard to all surrounding circumstances. FET is a means to guarantee justice to foreign investors.
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> There can be no legitimate expectations for anyone that the legal framework will remain unchanged in the face of an extremely severer economic crisis. No reasonable investor can have such an expectation unless very specific commitments have been made towards it or unless the alteration of the legal framework is total."[391]

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[388] *Parkerings Award, supra* (n 282) ¶ 332.
[389] *El Paso Award, supra* (n 307) ¶ 372.
[390] *Continental Award, supra* (n 316) ¶ 258.
[391] *El Paso Award, supra* (n 307) ¶¶ 373-374.

b. Fair and Equitable Treatment Implies that there is No Modification of the Legal Framework when Contrary Specific Commitments Have Been Made towards the Investor

955. The Tribunal holds that even a reasonable general regulation can be considered a violation of the FET standard, in case it violates a specific commitment towards the investor.

956. The tribunal in *Continental* addressed the question of what can be considered a specific commitment giving rise to "reasonable legitimate expectations" to the foreign investor. It insisted on the "specificity of the undertaking" that can give rise to reasonable legal expectations and for that purpose distinguished:[392]

- Political statements, which have the least legal value, "regrettably but notoriously" so;

- general legislative statements engender reduced expectations, especially with competent major international investors in a context where the political risk is high. Their enactment is by nature subject to subsequent modification, and possibly to withdrawal and cancellation, within the limits of respect of fundamental human rights and *ius cogens*;

- unilateral modification of contractual undertakings by governments, notably when issued in conformity with a legislative framework and aimed at obtaining financial resources from investors deserve clearly more scrutiny, in the light of the context, reasons, effects, since they generate as a rule legal rights and therefore expectations of compliance;

[392] *Continental Award, supra* (n 316) ¶ 261.

- centrality to the protected investment and impact of the changes on the operation of the foreign owned business in general including its profitability is also relevant; - good faith, absence of discrimination (generality of the measures challenged under the standard), relevance of the public interest pursued by the State, accompanying measures aimed at reducing the negative impact are also to be considered in order to ascertain fairness.

957. More recently, the Tribunal in *El Paso* stated that no general definition what constitutes a specific commitment can be given, but that two types of commitments might be considered "specific"; those specific as to their addressee and those specific regarding their object and purpose.[393] Further, the Tribunal in *El Paso* explained

> "First, in order to prevent a change in regulations being applied to an investor or certain behaviour of the State, there can indeed exist *specific commitments directly made to the investor* – for example in a contract or in a letter of intent, or even through a specific promise in a person-to-person business meeting – and not simply general statements in treaties or legislation which, because of their nature of general regulations, can evolve. The important aspect of the commitment is not so much that it is legally binding – which usually gives rise to some sort of responsibility if it is violated without a need to refer to FET – but that it contains a specific commitment directly made to the investor, on which the latter has relied.
>
> Second, a commitment can be considered specific if its *precise object was to give a real guarantee of stability to the investor*. Usually general texts cannot contain such commitments, as there is no guarantee that they will not be modified in due course. However, a reiteration of the same type of commitment in different types of general statements could, considering the circumstances, amount to a specific behaviour of the State, the object and purpose of which is to give the investor a guarantee on which it can justifiably rely."[394]

958. The Tribunal will follow the same logic as the tribunals in *Continental* and *El Paso* for deciding whether the Claimants can be considered to have had legitimate

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[393] El Paso Award, supra (n 307) ¶ 375.
[394] *Ibid*, ¶¶ 376-377.

expectations that the Regulatory Frameworks for gas would not be modified during the full course of its investment.

F. THE TRIBUNAL'S APPLICATION OF THE FAIR AND EQUITABLE STANDARD TO THE FACTS OF THE CASE

959. In the 1980s, government ownership of the most essential economic activities characterised Argentina's economic model. By 1980s, the GOA almost completely owned, and to a substantial extent operated the entire energy sector. In the case of the Argentine oil and gas industry, the public sector dominated the exploration, production, development, transportation, refining, and distribution of hydrocarbons. The private sector played only a secondary role, restricted to activities under service contracts with YPF, the former state-owned oil company, and with Gas del Estado, which owned and operated the gas transportation and distribution system. In the early 1990s the GOA privatised the utilities sector and deregulated the oil and gas industries. The new Legal Framework was designed to provide the stability and predictability needed to attract long-term foreign investments to the hydrocarbon sector. This new legal framework was modified during the Argentine economic crisis. It is the measures adopted then and thereafter by Argentina that are impugned by Claimants as a breach of its right to fair and equitable treatment under the BIT

1. The Parties' Positions

960. The Claimants contend that Argentina's price interference measures were unfair and inequitable. In particular Articles 14 and 15 of Decree 1055/89, the Gas Law and Decree 27131/93 grant natural gas producers the right to freely dispose of and market their natural gas production at deregulated prices. The Argentine Government incorporated this right in the Sierra Chata Concession and the Aguaragüe Contract. In this case, Argentina reinforced its specific guarantees of free marketing of natural gas at freely agreed prices through its reform of the entire natural gas regulatory system.

The Government expressly committed to refrain from imposing price controls or price freezes on natural gas distributors' tariffs and provided that tariffs would be adjusted to accurately reflect the cost of purchased gas. Similarly, the legal framework for power generation included the guarantee that, when reporting their cost for purposes of fixing the energy spot price, power generators would calculate and report their variable costs of production in US Dollars, including the cost of gas.

961. Moreover, the Claimants contend that the GOA interfered with the price of natural gas through numerous different measures taken *after* the pesification of the economy and that in fact, Argentina implemented most of the price interference measures at issue after 2003, the latest point in time that most observers, including Argentina's own witnesses and experts, agree marks the end of the Argentine financial crisis. According to the Claimants, another notable fact is that Argentina continues to unlawfully interfere in natural gas prices over eight years after pesification.

962. The Claimants argue that also Argentina's export curtailments and re-routings were unfair and inequitable. As to Argentina's assertion that the Claimants had no direct rights under the Chile-Argentina Energy Treaty because they are not a party to that treaty is in the Claimants' view misguided. The Claimants argue:

> "First, the Chile-Argentina Energy Treaty forms part of Argentine domestic law and prevails over domestic laws in case of inconsistency. As a result, it forms part of the Argentine Legal Framework governing natural gas exports, including Claimants' gas exports. Second, and just as importantly, Claimants invoke the Chile-Argentina Energy Treaty not merely as a part of Argentine law, but as collaborative evidence to support the reasonableness of Claimants' expectation that their export rights were firm. "[395]

963. Finally, the Claimants contend that Argentina's imposition of export withholdings violated the FET standard by creating a 20% Export Withholding on all gas exports.

[395] Claimants'Reply on the Merits ¶ 240.

964. Regarding the adaptation of domestic agreements (pesification) Argentina argues that it was considered legitimate both by Argentine courts and several ICSID tribunals. Moreover, Argentina points out that the Claimants were "part of the exclusive group of privileged parties which were expressly exempted from pesification in part of their business" (i.e. natural gas purchase and sale agreements for export purposes which were originally denominated in US dollars were excluded from the pesification).

965. According to Argentina, the need to adapt the licences of public utilities' companies, including gas transporting and distributing companies, cannot be considered a breach of the FET standard either, as such licences belong to the companies that act on their behalf, and the Claimants do not have the right to tell them how to operate.

966. Moreover, Argentina asserts that "in view of the circumstances experienced in Argentina due to the 2002 crisis, the measures adopted by Argentina aimed at restoring the natural gas price in a gradual and progressive manner are lawful and reasonable."

967. Argentina also contends that the Claimants' expectation that natural gas restrictions or re-routings would be imposed cannot be considered legitimate, since one of the basic tenets of the legal framework governing hydrocarbons is conditional upon the priority of domestic supply.

968. Finally Argentina contends that the Claimants may not make a claim on tax matters – such as export withholdings and royalties – alleging a violation of the FET standard, since Article XII of the BIT expressly exclude such types of claims. In any, case, if such type of claims were not excluded, Argentina contends that the imposition of export withholdings would not violate the FET standard. Argentina argues that there is no legitimate expectation that the host State's legislation would not be modified.

2. The Tribunal's Analysis

a. General Approach

969. The Tribunal does not doubt that the legal rights that Argentina granted through the BIT, the legal framework, the Hydrocarbon Concessions and Contracts, and the Sierra Chata Export Permit, as well as the GOA's public assurances, were fundamental to the Claimants' decisions to invest in Argentina. However, in the Tribunal's view no rule or even clear commitment embodied in a general piece of legislation can in itself be held a special commitment towards foreign investors, as such a conclusion would immobilise the legal order and prevent any adaptation to changed circumstances.

970. Further, a declaration made by a Head of State, e.g. the president of the Republic, is clearly a political statement to which only a limited confidence can be given. Such "representations" can of course contribute to inducing potential investors to invest in the sectors concerned. But, as the tribunal in *El Paso* stated . "it is one thing to be induced by political proposals to make an economic decision, and another thing to be able to rely on these proposals to claim legal guarantees."[396]

971. Not even the fact that the Preamble of the BIT states *inter alia:* "Agreeing that fair and equitable treatment of investment is desirable in order to maintain a stable framework for investment and maximum effective use of economic resources" can be held as a special commitment towards foreign investors, although the preamble pursuant to article 31(2) of the Vienna Convention is a means of interpretation of the treaty.

972. Therefore the Tribunal considers that the legitimate expectations of any investor entering in the gas market had to include the real possibility of reasonable changes

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[396] *El Paso Award, supra* (n 307) ¶ 395.

and amendments in the legal framework, made by the competent authorities within the limits of the powers conferred on them by the law, unless the GOA makes a specific commitment not to modify the existing framework.

b. Argentina's Price Interference Measures and Domestic Marketing Restrictions

973. Articles 14 and 15 of Decree 1055/89, the Gas Law and Decree 2731/93 grant natural gas producers the right to freely dispose of and market their gas at deregulated prices.[397] The GOA incorporated this right into the Sierra Chata Concession and the Aguaragüe Contract.[398] Thus the right to free marketing of natural gas at freely-agreed prices is not only provided for in the Legal Framework but also enshrined in both the Claimants' investments instruments. Therefore, the Tribunal considers that the GOA has made a commitment that gives rise to legitimate expectations for future state conduct concerning the right to free marketing of natural gas at freely agreed prices.

974. A *de facto* price freeze of natural gas resulted, *inter alia*, from the mandatory currency conversion of the prices the Claimants local customers paid to the Claimants.

975. The Tribunal has above found that ENARGAS is only authorised to intervene when prices passed through to tariffs exceed certain market levels. Since the Tribunal has also found that ENARGAS authority to regulate gas distribution prices is limited to

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[397] See Gas Law, Arts. 13 and 83 as well as Decree 2731/93, Annex I, Art. 1: "As from January 1, 1994, the price of natural gas is deregulated and, as from that date, gas supply and demand operations shall be freely agreed upon, pursuant to the provisions in this Decree and the supplementary rules issued by the Energy Secretariat." Moreover, Art. 13 of the Gas Law states: "Without prejudice of the rights granted to distributors under their licenses, any user may contract the purchase of natural gas directly with producers or marketers, freely agreeing the transactions' terms." *See also* Decree 1212/89, Art. 10.

[398] Decree 2446/92, Art. 9, Decree 1969/93, Art. 3.

protecting consumers from market collusion and price-fixing, ENARGAS exceeded the scope of its authority when it prohibited the pass-through of any increases of gas wellhead prices. Moreover, this Tribunal has found that the Secretary of Energy exceeded the scope its authority by preventing power generators from factoring gas price increases into their calculation of electricity spot prices.

976. As far as the GOA prevented gas distributors and power generators to pass through any increase in the well-head prices of gas demanded by the producers to tariffs, the renegotiation of prices could not prosper and, as a result, there was a *de facto* price freeze on natural gas in the domestic market, where the parity of the peso to the dollar no longer existed, the value of the peso having fallen to around 0.28 US dollars in May 2002.

977. Pursuant to Article 8 of Decree 214/02[399] the GOA instructed courts with jurisdiction over these matters to maintain and preserve existing contracts in Peso terms. In practice this measure precluded parties from terminating contracts prior to their expiration due to the GOA's alteration of the contract price or contract fixing mechanism.

978. Also the prices received by the Claimants following the First and Second Gas Agreements, which the Claimants did not sign, were regulated, a process to which the Claimants had not agreed. As mentioned above the re-routing measures issued by the Secretary of Energy (SE 503/04) of 21 May 2004 resulted in a loss of revenue for the Claimants equal to the difference of the price they would have received under the gas sale agreements and the much lower prices received for volumes routed to third parties.

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[399] Exhibit C-42.

979. Also through the Resolution SE 503/04 of 26 May 2004, issued by the Secretary of Energy, which authorised the Undersecretariat of Fuel to re-route the Claimants' gas production was in contradiction to GOA's above mentioned specific commitment.

980. The GOA has, as mentioned above, incorporated the right to freely dispose of and market their gas at deregulated prices into the Sierra Chata Concession and the Aguaragüe Contract. Therefore, the Tribunal concludes that also pesification, as far as it interfered with the Claimants' freely negotiated contracts, and the other above mentioned measures amount to an objective breach of the FET standard due under the Treaty. The Tribunal thus holds that the standard established in Article II(2)(a) of the Treaty has been reached and that to the extent that it results in a detriment to the Claimants' rights it will as such give rise to compensation.

c. <u>The Export Restrictions</u>

981. The Tribunal has above found that it established that the Claimants' rights to export authorised volumes of natural gas under the Sierra Chata concession have been severely impaired since firm export volumes were re-routed to the domestic market for over 70% of MASDA's Sierra Chata gas production.

982. By restricting the gas export of the Claimants', GOA disregarded Claimants' right to freely market the gas they produce, as well as the Claimants' firm export rights under the Sierra Chata Gas Export Permit.

983. The Tribunal finds that the shortage of gas in Argentina in 2004 has been established. The parties have made contradictory assessments concerning the causes of this shortage. However, in any case, this shortage is independent of the systematic crisis in 2001-2002 and, therefore, has to be considered on its own and not as a corollary of the aforementioned crisis. Export permits were given after an evaluation of the needs of the domestic supply. Leaving aside the provisions concerning the exports of excess gas, export authorisations were set as firm and definitive permits. Suspension or

removal of these permits was only possible under the circumstances provided for in the law. Argentina has not proven that the producers who were authorised to export firm volumes of natural gas had violated their legal obligations.

984. Therefore, the Tribunal concludes that also GOA's export restrictions amount to an objective breach of the fair and equitable treatment standard due under the Treaty. The Tribunal thus holds that the standard established in Article II(2)(a) of the Treaty has not been observed and that to the extent that its results in a detriment to the Claimants' rights it will as such give rise to compensation

d. Export Withholdings

985. Although the Export Withholdings are a matter of taxation they are a violation of an "investment agreement" or "investment authorization" as referred to in Article VII (1)(a) or (b) of the BIT. These are Hydrocarbons Concessions and Contracts as well as the Sierra Chata Permit, all of them being in the name of the Claimants (or one of them). These instruments contain in fact commitments of the State. Thus this Tribunal has under Article XII(2)(c) of the BIT jurisdiction also as far as the Export Withholdings are concerned.

986. The Tribunal has above found that the exemption from any present or future tariffs, duties or withholdings provided for in Decree 1589/89 and the exemption from specific discriminatory taxes provided for in Plan Argentina and the Conversion Decree were through Decree 1969/93 incorporated in the Sierra Chata Concession. This specific commitment constitutes the type of commitment that gives rise to legitimate expectations.

987. By imposing Export Withholdings, the GOA abrogated the Claimants' rights, which frustrated the Claimant's legitimate expectations. Therefore, the Tribunal concludes that this measure amounts to an objective breach of the fair and equitable treatment standard due under the Treaty. The Tribunal thus holds that the standard established

in Article II(2)(a) of the Treaty has not been observed and that to the extent that its results in a detriment to the Claimants' rights it will as such give rise to compensation.

G. FULL PROTECTION AND SECURITY

1. The Parties' Positions

988. According to the Claimants, the full protection and security (FPS) provision of the BIT provides protection beyond the customary international law standard. The Claimants consider that FPS imposes an obligation of vigilance and due diligence upon the GOA. To comply with FPS, a government's conduct must conform to its own national laws and be no less than "the minimum standard of vigilance and of care required by international law." The Claimants consider that it is not limited to physical security or the performance of the basic functions of the state. Moreover, the Claimants contend that the view has developed that measures which violate the fair and equitable treatment standard also violate the state's obligation to provide investors with full protection and security as well.

989. The Claimants contend that in this case, the GOA has failed to provide the Claimants with full protection and security in at least three ways: (1) by undermining the legal stability governing the Claimants' investment; (2) by seeking to coerce the Claimants to renegotiate their vested legal and contractual rights; (3) by harassing Claimants through both official and unofficial means, and (4) by creating a hostile environment against foreign investors.

990. Further, the Claimants argue that the GOA used its sovereign power to enact numerous measures that have: (i) dismantled the Legal Framework designed to protect the Claimants' investment; (ii) deprived the Claimants of their legal and contractual rights to deregulated prices and free marketing of production; (iii) imposed Export Withholdings; and (iv) imposed gas export restrictions and quotas, all

with full knowledge that these measures abrogate the essential rights it granted to the Claimants through the Legal Framework, the Hydrocarbon Concessions and Contracts, and the Sierra Chata Gas Export Permit. The Claimants assert that Argentina had a duty to protect the Claimants from the effects of these measures.

991. Moreover, the Claimants assert that Argentina's coercive negotiation tactics violate the FPS standard. Argentina first unilaterally reset the applicable legal framework and then repeatedly used producers' severely weakened bargaining position to elicit commitments to depressed prices and additional injections to the domestic market. Argentina also constructed the "agreements" to punish producers like the Claimants that chose to retain their right and upheld their commercial commitments instead of relenting to Argentina's demands. According to the Claimants, "instead of upholding the Claimants' rights, Argentina designed so-called "agreements" to undermine those rights, and then when its coercive measures did not comply with such "agreement", it punished producers who chose to keep their rights.

992. Further, the Claimants contend that Argentine officials have also resorted to harassing the Claimants. The Government sent letters to Claimants' customers that undermined the Claimants' legal position in pending litigation. The Energy Secretariat sent a letter to AES Gener S.A., one of Mobil's customers, which stated that the export restrictions and curtailments did not constitute a *force majeure* event but were the result of the producers' behaviour. Argentina had no legitimate interest in taking this action.

993. Finally, the Claimants argue that it is undisputed that Argentina further undermined the legal security of the Claimants' investment with its non-transparent practice of issuing *ad hoc* re-routing orders that sent the Claimants' gas production to anonymous customers at arbitrarily stipulated prices.

994. According to Argentina, "like the fair and equitable treatment standard, the protection and security standard relates to the international law minimum standard. Thus interpreted, the protection and security standard requires to provide the police protection required under customary international law."

995. Alternatively, if the Tribunal did not accept the interpretation of the protection and security standard set out in Article II.2(a) of the BIT as equivalent to the international law minimum standard, such provision would only impose on Argentina a due diligence obligation to provide investors with physical protection.

996. Further, Argentina argues that even if the protection and security standard were hypothetically considered to include the obligation to provide legal protection, the State would fulfil such obligation by keeping its judicial system fully available to the investor.

997. Finally Argentina argues that the Claimants' tax related claim regarding the alleged violation of the protection and security standard is excluded by virtue of Article XII of the BIT.

998. Argentina concludes that the measures challenged in this case do not violate the protection and security standard. In fact Argentina has complied with its due diligence obligation of providing physical protection to the Claimants. Furthermore, the Argentine judicial system was at all-time fully available for the Claimants.

2. The Tribunal's analysis

999. Article II.(2)(a) of the BIT requires that Argentina provides "full protection and security" to the Claimants' investment. The Tribunal considers, as the tribunal in *El Paso*, that the full protection and security standard is no more than the traditional obligation to protect aliens under customary international law and that it is a residual obligation provided for those cases in which the acts challenged may not in

themselves be attributed to the Government, but to a third party.[400] The commentators and case-law generally agrees that this standard imposes an obligation of vigilance and due diligence upon the government. The AAPL case approvingly quotes Professor Freeman's definition of due diligence:

> "The "due diligence" is nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances."[401]

1000. The *AMT* Tribunal explained:

> "The obligation incumbent on Zaire is an obligation of vigilance, in the sense that Zaire as the receiving state of investments made by AMT, an American company, shall take all measures necessary to ensure the full enjoyment of protection and security of its investment and should not be permitted to invoke its own legislation to detract from any such obligation. Zaire must show that it has taken all measure of precaution to protect the investments of AMT on its territory.
>
> These treatments of protection and security of investment required by the provisions of the BIT of which AMT is beneficiary must be in conformity with its applicable national laws and must not be any less than those recognized by international law. For the Tribunal, this last requirement is fundamental of the determination of the responsibility of Zaire. It is thus an objective obligation, which must not be inferior to the minimum standard of vigilance and of care required by international law."[402]

1001. This Tribunal agrees with the following statement by the Tribunal in *El Paso*:

> "The minimum standard of vigilance and care set by international law comprises a duty of prevention and a duty of repression. A well-established aspect of the international standard of treatment is that States must use "due diligence" to prevent wrongful injuries to the person or property of aliens caused by third parties within their

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[400] *El Paso Award*, *supra* (n 307) ¶ 522.
[401] *Asian Agricultural Producers Ltdv Sri Lanka*, ICSID Case No ARB/87/3), Award (27 June, 1990) ¶ 77.
[402] *American Facturing & Trading, Inc (AMT) v Republic of Zaire*, ICSID Case No ARB/93/1, Award (27 February, 1997) ¶ 6.05-6.06

> territory, and, if they did not succeed, exercise at least "due diligence" to punish such injuries. If a State fails to exercise due diligence to prevent or punish such injuries, it is responsible for this omission and is liable for the ensuing damage. It should be emphasised that the obligation to show "due diligence" does not mean that the State has to prevent each and every injury. Rather, the obligation is generally understood as requiring that the State take reasonable actions within its power to avoid injury when it is, or should be, aware that there is a risk of injury. The precise degree of care, of what is "reasonable" or "due," depends in part on the circumstances."[403]

1002. Consequently, the Tribunal finds that for the FPS standard to keep its own identity, it must be understood as the obligation of the host State to act with due diligence providing investors' physical protection to their investments and, if it comes to it, facilitate investors' access to justice. Going beyond this would lead to the confusion of this standard with other standards, particularly with the FET standard.

1003. However, the Claimants do not complain about a violation by Argentina of an obligation of prevention of repression. The same interpretation was made not only by the tribunal in El Paso, but also by the tribunal in *Tecmed*:

> "The Arbitral Tribunal considers that the Claimant has not furnished evidence to prove that the Mexican authorities, regardless of their level, have encouraged, fostered, or contributed their support to the people or groups that conducted the community and political movements against the Landfill, or that such authorities have participated in such movement."[404]

1004. The Claimants did not specify or determine the duty to act against a third party that would have been breached by Argentina under the BIT: all the impugned acts that allegedly violate the FPS standard are allegedly attributable to the GOA and not to any third party. In the present case none of the measures challenged by the Claimants were taken by a third party; they all emanated from the State itself. Consequently, the

[403] *El Paso Award, supra* (n 307) ¶ 523.
[404] *Tecmed Award, supra* (n 95) ¶ 176.

measures should only be assessed in the light of other BIT standards and cannot be examined from the angle of full protection and security.

1005. On these grounds the Tribunal concludes that no violation of the full protection and security clause has been established.

H. ARTICLE II(2)(c): THE UMBRELLA CLAUSE

1006. The so-called umbrella clause contained in Article II(2)(c) provides as follows:

> "Each party shall observe any obligation it may have entered into with regard to investments."

1. The Parties' Positions

1007. According to the Claimants, Argentina violated the BIT by failing to observe its obligations under Article II(2)(c). The Claimants contend that Argentina has since January 2002 repeatedly violated the Legal Framework, the Claimants' Hydrocarbon Concessions and Contracts, the Sierra Chata Gas Export Permit, and other specific commitments it had undertaken with regard to the Claimants' investments:

- "By a series of measures taken since January 2002, which (i) interfered with Claimants' contracts by forcefully converting Dollar-denominated receivables into Peso receivables at an artificially low exchange rate while simultaneously preventing Claimants' main customers from agreeing to price readjustments, and (ii) forced gas sales to third parties at well below-market regulated prices. Through these measures, Argentina breached its obligation to allow Claimants to market their production freely at deregulated prices. These measures specifically violated the GOA's obligations under Articles 14 and 15 of Decree 1055/89, Article 9 of Decree 1212/89, Articles 13 and 83 of the Gas Law, Article 1 of Annex I of Decree 2731/93, Article 3 of Decree 1969/93, and Article 4 of Decree 2446/92.

- By imposing increasingly onerous Export Withholdings, the GOA repeatedly violated its obligation to refrain from imposing future Export Withholdings on Claimants. These measures violated the GOA's obligations under Article 3 of Decree 1589/89, Articles 4 and 13 of the Chihuidos Memorandum of Understanding, and Articles 2 and 6 of Decree 1969/93.

- Export Withholdings also violate Argentina's guarantee of tax stability and its commitment not to impose discriminatory taxes on Claimants, or taxes that levy specifically their business or their assets, thus violating Article 13 of the Chihuidos Memorandum of Understanding and Article 6 of Decree 1969/93.

- Argentina's measures imposing Export Withholdings also violated the GOA's obligation to provide Claimants with royalty rate stability under Articles 59 and 62 of Law 17,319, Article 10 of Decree 2411/91, and Article15 of the Chihuidos Memorandum of Understanding, Article 10 of Decree 824/95, and Article 7 of Decree 1969/93.

- By placing a series of increasingly burdensome restrictions on Claimants' exports, the GOA repeatedly violated its obligation to guarantee Claimants' firm export rights to export their hydrocarbon production. Through its measures restricting hydrocarbon exports, the GOA violated its obligations to Claimants under Articles 1 and 2 of the Sierra Chata Gas Export Permit and Articles 1 through 3 of the Chile-Argentina Energy Treaty.

- Argentina has also violated its obligations to compensate Claimants for violating the rights granted under the Legal Framework (specifically Article 6 of Decree 1589/89), the Hydrocarbon Concessions and Contracts, and the Sierra Chata Gas Export Permit. Although the GOA expressly undertook several compensation obligations towards Claimants—including the obligations under Article 5 of the Chihuidos Memorandum of Understanding, and Article 5 of Decree 1969/93—Argentina never compensated Claimants for their losses."

1008. According to Argentina it follows from the interpretation of Article II(2)(c) of the BIT that:

(a) "for the umbrella clause to be applicable the host State must have assumed a legal obligation;

(b) the umbrella clause refers to specific obligations assumed vis-à-vis a specific investment, and the foreign investor cannot invoke provisions arising from the general laws of the host state;

(c) the umbrella clause only entitles the foreign investor to invoke obligations owed directly to it by the host state;

(d) the umbrella clause does not transform any contractual claim into a Treaty claim; and

(e) there can be no breach of the umbrella clause in the absence in the breach of the obligation which is relied on under the law applicable to such obligation."

1009. Argentina contends that none of the obligations invoked by the Claimants constitutes a specific commitment assumed by Argentina directly to MEDA and MASA. Therefore, there is no single obligation that may be invoked by the Claimants in this case under the umbrella clause. Further, Argentina argues that in any case, even if the provisions of the general legislation of the host state could give rise to obligations covered by the umbrella clause, the obligations alleged by the Claimants in this case are non-existent.

2. The Tribunal's Analysis

1010. The Tribunal will not discuss the jurisdictional aspects involved in the Respondent's argument, as these were dealt with above in the part of the award concerning jurisdiction. Regarding the merits of the argument, however, the Tribunal agrees with Argentina that for the umbrella clause to apply, the host state must have assumed a legal obligation. Moreover, the Tribunal agrees with Argentina that Article II (2) (c) is concerned with consensual obligations arising independently of the BIT itself (*i.e.* under the law of the host state or possibly under international law), which are not entered into *erga omnes* but with regard to particular persons and that they must be specific obligations concerning the investment. This position finds support in the Annulment Decision in the *CMS* case. The Committee stated:

> "In speaking of "any obligation it may have *entered into with regard to investments"*, it seems clear that Article II(2)(c) is concerned with consensual obligations arising independently of the BIT itself (*i.e.* under the law of the host state or possibly under international law): Further they must be specific obligations concerning the investment. They do not cover general requirements imposed by the law of the host state."
>
> Consensual obligations are not entered into *erga omnes* but with regard to particular persons. Similarly the performance of such obligations or

> requirements occurs with regard to, and as between, obligor and oblige.[405]

1011. The standard of protection of the treaty will be engaged only when there is a specific breach of the treaty rights and obligations or contract rights protected under the treaty. Purely commercial aspects of a contract might not be protected by the treaty, at least unless there is significant interference by governments or public agencies with the rights of the investor.

1012. None of the measures complied in this case can be described as a commercial question as they are all related to decisions by the government or public authorities that have resulted in the interferences and breaches noted.

1013. The Tribunal must therefore conclude that the obligation under the umbrella clause of Article II(2)(c) of the BIT has not been observed by Argentina, to the extent the obligations pertinent to the investment to which Argentina has specifically entered into with the Claimants have been breached and have resulted in the violation of the standards of protection under the BIT.

XI. ARE THE MEASURES CHALLENGED BY THE CLAIMANTS AUTHORISED BY ARTICLE IV(3) OR ARTICLED XI OF THE BIT OR CAN THEY BE EXCUSED ON ACCOUNT OF THE STATE OF NECESSITY?

1014. While Argentina denies having committed any breach of the BIT through its various measures challenged by the Claimants, Argentina also relies on three defences of a general character that would in its view render in any event its action entirely lawful. The first and second defences are based on the BIT, the first one on Article IV (3) and the second one on Article XI. The third defence is based on the doctrine of "state of

[405] *CMS Decision on Annulment, supra* (n 348) ¶ 95.

necessity" in customary international law, as codified by the International Law Commission ("**ILC**") in the ILC Articles on Responsibility of States for Internationally Wrongful Acts.

1015. The Tribunal will first examine the defence based on Article IV (3) of the BIT. Thereafter, the Tribunal will address Article XI of the BIT and Article 25 of the ILC Articles on Responsibility of States for Internationally Wrongful Acts. Also those two Articles are invoked by Argentina to avoid any responsibility for the alleged violations of the BIT. The Tribunal will concentrate on the arguments based on Article XI before dealing with the defence based on the "state of necessity" in customary international law. As it was also stated first by the Tribunal in *Continental* and thereafter by the Tribunal in *El Paso*, "the application of Article XI in the present case (if warranted) may be such as to render superfluous a detailed examination of the defence of necessity under general international law applied to the particular facts of the present dispute".[406] However, general principles of international law, including those embodied in Article 25, must be taken into account in the interpretation of Article XI. Article XI is the *lex specialis* and Article 25 is the *lex generalis*. As stated in the Decision on Annulment in *CMS:*

> "Article XI is a threshold requirement: if it applies, the substantive obligations under the Treaty do not apply. By contrast, Article 25 is an excuse which is only relevant once it has been decided that there has otherwise been a breach of those substantive obligations."[407]

A. Can the Violations Committed by Argentina Be Excused on the Basis of Article IV (3)

1016. Article IV (3) of the BIT provides:

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[406] *Continental Award*, supra (n 316) ¶162 and *El Paso Award*, supra (n 307) ¶ 552.
[407] *CMS Decision on Annulment, supra* (n 348) ¶ 129.

> "Nationals or companies of either Party whose investments suffer losses in the territory of the other Party owing to war or other armed conflict, revolution, state of national emergency, insurrection, civil disturbance or other similar events shall be accorded treatment by such other party no less favourable than accorded to its own nationals or companies of any third country, whichever is the more favorable treatment, as regards any measures it adopts in relation to such losses."

1. The Parties' Positions

1017. Argentina contends that Article IV. 3. is a special provision as compared to the other provisions of the BIT. Thus, under normal circumstances States are bound by Article II. 1 of the BIT, whereas if any of the events under Article IV. 3. arises, States are only under the obligation to accord treatment no less favourable than that accorded to its own nationals or to nationals of a third State.

1018. Thus, Argentina argues that if foreign investors suffer losses in cases of "state of national emergency" or "other similar events", the only obligation of the State under the Treaty, pursuant to Article IV.3, is not to discriminate if it decides to take measures in relation to such losses. Therefore, Argentina concludes that it fully complied with the special regime under the BIT for emergency situations and therefore, it did not violate any of the Treaty provisions.

1019. The Claimants contend that Article IV. 3 of the BIT is irrelevant in this case and refer to Professor Dolzer's statement. "[w]hile Art. XI addresses the legal status of host states in periods affecting public order, international peace and security, Art. IV sec. 3 pertains to the investor's right of compensation for losses owing to war and similar situations." Therefore, the Claimants argue that "[b]y its plain meaning, this provision entitles an investor to non-discriminatory treatment in the payment it receives for losses sustained during wartime when such treatment might not otherwise be available under customary international law."

1020. Moreover, the Claimants argue that "nothing about Article IV 3. suggests that it may be used by a party to avoid the responsibility to pay compensation for acts that violate

BIT's other provisions" and that "[e]ven less so can it be read as a general escape clause from treaty obligations and thus, does not result in excluding wrongfulness, liability and eventual compensation."

2. The Tribunals Analysis

1021. The Tribunal finds that Argentina's interpretation is not supported by the wording of Article IV.3 of the BIT and can therefore not agree with this interpretation. On the contrary, the Tribunal agrees with the Claimants that Article IV.3 of the BIT applies to measures a State adopts in relation to the losses referred to in that article, e.g. the investor's right to compensation owing to war and similar situations, but not to measures that cause such a loss. In the Tribunal's view, the plain meaning of the provision is, as stated by the Tribunal in *El Paso* "that the standard of treatment of the BIT – national treatment and most favoured nation treatment – have to be applied when a State tries to mitigate the consequences of war or other emergency."[408] Moreover, the analysis of the same provision made by the Tribunal in *CMS* is in line with this. That Tribunal stated:

> "The plain meaning of the Article is to provide a floor treatment for the investor in the context of the measures adopted in respect of the losses suffered in the emergency, not different from that applied to nationals or other foreigners. The Article does not derogate from the Treaty rights but rather ensures that any measures directed at offsetting or minimizing losses will be applied in a non-discriminatory manner."[409]

1022. The Tribunal therefore concludes that Article IV (3) does not deal with the matter at hand and consequently the violations by Argentina cannot be excused pursuant to that provision.

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[408] *El Paso Award, supra* (n 307) ¶ 559.
[409] *CMS Award, supra* (n 97) ¶ 375.

XII. ARE THE VIOLATIONS COMMITTED BY ARGENTINA EXCLUDED FROM THE SCOPE OF THE BIT UNDER ARTICLE XI?

1023. Argentina has in order to justify its conduct invoked Article XI of the BIT. The provision reads:

> "This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests."

1024. Before dealing with this defence it is, however, appropriate to emphasise the difference between the two defences based on Article XI of the BIT and on Article 25 of the ILC Articles on Responsibility of States for Internationally Wrongful Acts, which reflects general international law. Under Article XI of the BIT, measures necessary for the purposes mentioned in the Article are not in breach of the BIT. On the contrary, if the rules of general international law regarding necessity apply, this is, as stated by the Tribunal in *El Paso*, "a ground for precluding the wrongfulness of an act not in conformity with an international obligation."[410]

1025. Thus, in order to analyse the consequences of Article XI, the first question to answer is whether there was a situation of emergency as defined by that Article when the measures complained by the Claimants were taken. If the answer is in the affirmative, all the acts considered necessary by the Tribunal to cope with this situation are excluded from the scope of the BIT, the contrary being true of the acts not considered necessary by the Tribunal when the measures complained by the Claimant were taken. If the answer is in the negative, the Tribunal has to examine the different measures taken in order to determine whether they are or not in violation of one of the BIT standards of treatment of foreign investments. To analyse the consequences of Article

[410] *El Paso Award*, *supra* (n 307) ¶ 553.

25, the reverse approach is required. The Tribunal should first analyse whether or not the measures constitute a violation of the standards of treatment of the BIT. If the answer is no, this marks the end of the inquiry. If the answer is in the affirmative, the Tribunal has to consider whether the illegality can be set aside on account of a state of necessity.

1026. This Tribunal has, however, in order to analyse the consequences of Article XI decided to first answer the question whether by its behaviour Argentina has contributed to endangering its public order or essential security interests. If the answer is in the affirmative, the defence under Article XI shall not apply since the challenged measures would fail to qualify as "necessary" under that Article. If the answer is in the negative, the Tribunal has to examine whether there was a situation of emergency as defined by Article XI, in which case, in the affirmative, all acts considered necessary by the Tribunal to cope with that situation are excluded from the scope of the BIT.

1027. Taking into account the differences between the situation regulated under Article 25 of the ILC Articles and that addressed by Article XI of the BIT, the conditions of application are not the same. As stated by the tribunal in *Continental*

> "The strict condition to which the ILC text subjects the invocation of the defence of necessity by a State is explained by the fact that it can be invoked in any context against any international obligation. Therefore "it can only be accepted on an exceptional basis." This leads the Tribunal to the conclusion that invocation of Art. XI under this BIT, as a specific provision limiting the general investment protection obligations (of a "primary" nature) bilaterally agreed by the Contracting Parties, is not subject to the same conditions of application as the plea of necessity under general international law."[411]

[411] *Continental* Award, *supra* (n 316) ¶ 167.

1028. Nevertheless, there is a link between the two types of regulation. First of all, they both intend to provide flexibility in the application of international obligations, recognising that the necessity to protect national interest of a paramount importance may justify setting aside or suspending an obligation, or preventing liability from its breach. Further, the practical result of applying the carve-out of Article XI, rather than the defence of necessity, may be the same: condoning conduct that would otherwise be unlawful and thus removing the responsibility of the State. These connections may be relevant as to the interpretation of the bilateral provision in Article XI of the BIT, in that the customary concept of necessity may be relevant in this respect. The Tribunal will therefore focus on the analysis of Article XI and the conditions of its application, referring to the customary rule on State of Necessity (as enshrined in Art 25 of the ILC) only insofar as the concept there used assist in the interpretation of Article XI.

1029. Article XI of the BIT raises the following questions. Who is entitled to interpret Article XI authoritatively? Do the provisions of that Article apply to the present dispute? If so, does its applicability exonerate Argentina from any responsibility for BIT violations?

1. Who is entitled to Interpret Article XI? Is Article XI self-judging?

a. <u>Argentina's Position</u>

1030. Argentina contends that the Contracting Parties to the BIT, i.e. Argentina and the United States of America understood that each Contracting Party had the exclusive right to judge whether the measures taken under Article XI were necessary to maintain public order or to protect their essential security interests, subject only to the principle of good faith. Therefore, the Tribunal should upon evaluating whether Article XI is applicable in the instant case take into account the intention of the Contracting Parties to determine by themselves, whether the circumstances allow them to take measures under XI and upon such analysis assess whether said article has been invoked in good faith.

b. The Claimants' position

1031. The Claimants contend that Article XI of the BIT is not self-judging. In the Claimants view, the BIT is unambiguous that all of its provisions, including Article XI, are subject to investor-State Arbitration. Without qualification, through Article VII of the BIT, Argentina has consented to the jurisdiction of ICSID arbitration tribunal to adjudicate disputes under the BIT, and thus, the BIT's provisions fall under exclusive purview of the Tribunal's jurisdiction. Article XXI of the General Agreement on Tariffs and Trade ("**GATT**") carves like Article XI of the BIT out an exception for a country's "essential security interests", but unlike Article XI of the BIT, the GATT Article explicitly indicates that it is self-judging. The difference in language in that instrument is obvious: "action which it considers necessary" in Article XXI of the GATT as compared to "measures necessary" in Article XI of the BIT.

1032. According to the Claimants, a similar situation arose in the *Nicaragua* case,[412], where the ICJ had to decide whether the "essential security interests" provision of the 1956 Treaty of Friendship, Commerce and Navigation ("**FCN**") between Nicaragua and the US was self-judging. Article XXI of the FCN: "provided: "the present Treaty shall not preclude the application of measures . . . necessary to protect its essential security interests." The Court concluded that the reference to "essential security interests in Article XXI(1) of the FCN fell within the Court's jurisdiction as defined in the disputed settlement provision of Article XXIV of the same Treaty. The ICJ then

[412] International Court of Justice, *Case Concerning Military and Paramilitary Activities in and against Nicaragua* (*Nicaragua v United States of America*) ("*Nicaragua*").

compared Articled XXI of the FCN with Article XXI of the GATT and then noted the obvious distinction between "necessary" and "which it considers necessary.

1033. Moreover, the Claimants argue that the US certainly knows how to draft a self-judging exception when it wants to do so. The Protocol appended to the BIT with Russia,[413] which was negotiated in the same period as the US-Argentina BIT, states that "the Parties confirm their mutual understanding that whether a measure is undertaken by a Party to protect its essential security interests is self-judging." There is no similar statement in the Protocol to the US-Argentina BIT, even though paragraph six of the Protocol makes specific reference to Article XI of the Treaty and explains what another of its provisions means.

1034. Further, the Claimants contend that, even, if *quod non*, it could be inferred that the US intended that Article XI be self-judging, that intention alone would not suffice to make it so. According to Article 31(2) of the Vienna Convention, reference to extraneous agreements for guidance in interpreting treaty language refers to agreements "in connection with the conclusion of the treaty" and either entered into or accepted by all treaty parties. Likewise, Article 31(3) of the Vienna Convention refers to subsequent agreements and subsequent practice with regard to the treaty in question (not other treaties) that establishes an agreement regarding its interpretation. In addition, Article 31(4) of the Vienna Convention requires the establishment of both parties' intentions to give any term of the treaty a special meaning; as noted, it is accepted that, under customary international law, conclusive evidence is necessary to establish such a mutual intention at the time of concluding a treaty. No evidence has been produced by Argentina or its legal expert to show the required mutual intent between the US and Argentina on this issue.

[413] Treaty Concerning the Encouragement and Reciprocal Protection of Investment signed on 17 June 1992.

1035. The question of the self-judging nature of Article XI of the BIT came up, and was answered in the negative by the tribunal in *CMS*.[414] That tribunal determined that Article XI of the BIT is not "self-judging" and is subject to substantive review, rather than merely a "good faith" analysis. All subsequent tribunals examining this same evidence – including *LG&E*, *Enron*, *Sempra* and, *Continental Casualty* – have agreed that Article XI is not self-judging.[415]

1036. Finally, according to the Claimants even if one would conclude that, Article XI is self-judging and subject to a mere good faith standard, Article XI would be of no benefit to Argentina. The permanent repudiation of the Claimants' rights in response to a temporary "emergency" that has long since ended is simply not a good-faith invocation of Article XI.

c. The Tribunal's Analysis

1037. Pursuant to Article 31(1) of the Vienna Convention a treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty and in the light of its object and purpose. Thus any interpretation has to begin with an examination of the terms of the treaty in their ordinary meaning. The wording of the treaty is deemed to express the intention common to the Parties, and what the Parties effectively agreed to, even though a Party may have wished something else on one or another point. Consequently, in principle treaty rules must be regarded as being objective in nature. This means that, unless the contrary is specified, they are not self-judging.

[414] *CMS Award, supra* (n 97) ¶¶ 370,373.
[415] *LG&E Decision on Liability*, *supra* (n 309) ¶ 212, *Enron Award, supra* (n 314) ¶ 339, *Sempra Award, supra* (n 315) ¶ 338, *Continental Award, supra* (n 316) ¶¶ 187-188.

1038. The Tribunal considers that in principle, the ordinary meaning of a treaty is that given to its terms at the time of its conclusion. As stated by the tribunal in *El Paso*, changes occurring elsewhere, at a later stage, for instance when other, similar treaties are being negotiated or when a model treaty is being submitted to a national authority for approval, even if they happened before the treaty to be interpreted is ratified or comes into force, are irrelevant for establishing the meaning given to it.[416] Consequently, Argentina cannot rely on BITs negotiated after 1991 or on the 1992 Model Treaty.

1039. A treaty provision like Article XI of the BIT allowing for exceptions to the rights guaranteed in the same treaty must be attributed the ordinary meaning resulting from their text. A self-judging clause cannot be read into them, in particular when the treaty contains compromissory clauses, as in the instant case. This clearly results from the case-law.

1040. In *Nicaragua*, which apparently in this context, is the leading case, where the ICJ was confronted with an "essential security interest" clause in Article XXI of the Nicaragua-US Treaty of FCN. The same Treaty also contained a compromissory clause placing disputes pertaining to the interpretation and application of its provisions under the ICJ's jurisdiction. The ICJ held that the clause was not self-judging and found that it had jurisdiction to determine whether the essential security interests' clause was applicable. In this judgment, the ICJ rules that, in the absence of qualifying language, the text of the relevant provision must be interpreted as it is, according to its ordinary meaning, and cites *e contrario* Article XXI of the GATT, which, as Claimants submit, contains qualifying language.

1041. The Tribunal is of the view that the Nicaragua judgment is of particular importance in the instant case because it relates to a treaty which though not a BIT, also defines

[416] *El Paso Award, supra* (n 307) ¶ 591

and protects rights of individuals of one Party on the territory of the other and because the 1991 Argentina-US BIT, like the Nicaragua-US Treaty of FCN, contains a compromissory clause. The *Nicaragua* judgment was rendered in 1986 and the BIT was concluded in 1991. It is most unlikely that within this five year time-span the United States could have forgotten the judgment in *Nicaragua* which amounted to saying that if one wants a treaty clause to be self-judging, one has to use appropriate language and to obtain the other Party's consent. For these reasons, the Tribunal concludes that at the relevant time, the US did not seek to attribute self-judging character of Article XI of the BIT.

1042. This conclusion gets also support in decisions of ICSID tribunals concerning Article XI of the BIT. The tribunal in *CMS* determined that Article XI of the BIT is not self-judging and is subject to substantive review, rather than a merely a ”good faith” analysis:

> “The Tribunal is convinced that when States intend to create for themselves a right to determine unilaterally the legitimacy of extraordinary measures importing non-compliance with obligations assumed in a treaty, they do so expressly.”

The Tribunal continued:

> “[T]he Tribunal concludes first that the clause of Article XI is not a self-judging clause... [I]f the legitimacy of such measures is challenged before an international tribunal; it is not for the State in question but for the international jurisdiction to determine whether the plea of necessity may exclude wrongfulness...
>
> The Tribunal must conclude next that this judicial review is not limited to an examination of whether the plea has been invoked or the measures have been taken in good faith. It is a substantive review that must examine whether the state of necessity or emergency meets the requirements laid down by customary international law and the treaty

provisions and whether it thus is or is not able to preclude wrongfulness."[417]

1043. The above positions were also taken by the arbitral tribunal in *LG&E*. In its decision on liability the Tribunal held:

> "Certainly, the language of the BIT does not specify who should decide what constitutes essential security measures – either Argentina itself, subject to a review under good faith standard, or the Tribunal: Based on the evidence before the Tribunal regarding the understanding of the Parties in 1991 at the time the Treaty was signed, the Tribunal decides and concludes that the provision [Article XI] is not self-judging."[418]

1044. This passage is of particular interest because it emphasises that what matters is the Parties common intention *at the signature* in 1991, when negotiations had been concluded rather than subsequent events.

1045. Also the Tribunals in *Enron* and *Sempra* concluded "that Article XI [of the BIT] is not self-judging and that judicial review in its respect is not limited to an examination of whether its invocation or the measures adopted were taken in good faith."[419] Moreover, the Tribunal in *Continental* reached the same conclusion as to the non-self-judging nature of the recourse to Article XI of the BIT.[420]

1046. More recently, the Tribunal in *El Paso* shared the same view. In its award the tribunal said:

> "[T]he Tribunal considers that Article XI of the 1991 Argentina-US BIT is not self-judging. In other words, it is the duty of the Tribunal first to interpret Article XI and then to decide whether or not the situation that prevailed in Argentina at that time of the impugned

[417] *CMS Award, supra* (n 97) ¶¶ 370, 373-374.
[418] *LG&E Decision on Liability, supra* (n 309) ¶ 212.
[419] *Enron Award, supra* (n 314) ¶ 339, *Sempra Award, supra* (n 315) ¶ 388.
[420] *Continental Award, supra* (n 316) ¶¶ 187-188.

> measures can be subsumed under the exceptions listed in that Article."[421]

1047. The Tribunal finds the case-law reported above persuasive.

1048. According to Article 31(1) of the Vienna Convention, the terms of a treaty must be interpreted "in their context". That notion is defined by Article 31(2) of the Convention as including in addition to the text, including its preamble and annexes, (a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty and (b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

1049. The Tribunal considers that the BIT's preamble and the body of the text show that this Treaty aims at creating a stable investment climate in both countries. If the exceptions allowed by Article XI were considered self-judging, that purpose could not be achieved. There are no "agreements relating to the treaty made between all the parties in connection with the conclusion" of the BIT (Article 31(2) (a) of the Vienna Convention), nor is there any "instrument, which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty." Other BITs and the Model Treaty, invoked by Argentina are certainly not connected with the conclusion of the BIT.

1050. However, pursuant to Article 31(3) of the Vienna Convention there shall be taken into account together with the context: (a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions; (b) any subsequent practice in the application of the treaty which establishes the agreement of

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[421] *El Paso Award, supra* (n 307) ¶ 610.

the parties regarding its interpretation; and (c) any relevant rules of international laws applicable in the relation between the parties.

1051. The above-mentioned sub-paragraphs (a) and (c) of Article 31(3) of the Vienna Convention do not seem relevant in this context. However, sub-paragraph (b) – any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation – may have been relevant here, if Argentina had contended that the view on self-judging provisions of BITs or other agreements had changed after the signature of the BIT. However, Argentina has not done so in this case.

1052. Further, the *object* and *purpose* of the BIT (Article 31(1) of the Vienna Convention) has to be examined. The purpose of BITs such as the present one is to establish a climate inducing investors of one State to invest on the territory of the other by creating, for both sides, reasonable conditions for the making of investments. As stated by the Tribunal in *El Paso* "self-judging exceptions such as that allegedly introduced into Article XI of the Argentina-US BIT by tacit consent would give extremely large powers to the State on whose territory the investment was made – the reference to good faith is of little help – expose the investors to large risks."[422]

1053. Although the Vienna Convention places priority of textual interpretation in paragraphs 1 to 3 of Article 31, it however, makes space for the intentions of the parties in a somewhat subsidiary manner. In its paragraph 4, which provides that "[a] special meaning shall be given to a term if it is established that the parties so intended." Article 31 (4) must be read in conjunction with Article 32 of the Convention. Article 32 provides that recourse may be had to "supplementary means of interpretation, including the preparatory work of the treaty and the circumstances

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[422] *El Paso Award, supra* (n 307) ¶ 604.

of its conclusion, in order to confirm the meaning resulting from the application of Article 31, or to determine the meaning, when the interpretation according to Article 31: (a) leaves the meaning ambiguous or obscure; or (b) leads to a result which is manifestly absurd or unreasonable."

1054. The next question to consider is this whether the results of the interpretation of Article XI based on Article 31 of the Vienna Convention are confirmed if one turns to the supplementary means of interpretation mentioned in Article 32 of that Convention.

1055. The Tribunal has not found anything that would suggest that the interpretation of Article XI based on Article 31(1) to (3) of the Vienna Convention is wrong, ambiguous or obscure or would lead to a result which is manifestly absurd or unreasonable. On the contrary, insofar as any of the elements mentioned in Article 32 can be identified their use would confirm or at least not contradict the conclusion that Article XI does not have self-judging character. No preparatory work to the contrary has been identified. Declarations made in connection with other BITs or the 1992 Model Treaty do not qualify as preparatory work related to the present BIT. Neither have any circumstances surrounding the present BITs conclusion been shown that would contradict the same conclusion. In the light of the ICJ's judgment in the *Nicaragua* case it is clear that, to render a treaty provision self-judging, the intention to do so must be explicitly stated – which it was not – in particular where the treaty contains a compromissory clause, as is the case in the BIT.

1056. On the grounds set out above, the Tribunal considers that Article XI of BIT is not self-judging. Consequently, it is the Tribunal's task to interpret Article XI and to decide whether the situation that prevailed in Argentina at the time of the impugned measures can be subsumed under the exceptions mentioned in that Article.

2. The Interpretation of Article XI: a General Approach and Admissibility of the State's Defence under Article XI

1057. The Tribunal considers that the state of emergency referred to in Article XI can be of an economic nature, as stated by several other ICSID tribunals.[423] No responsibility should be found for damage suffered during the period of emergency, as the BIT does not apply in such a period, except if the State has substantially contributed to create it as it will be examined below.

1058. However, damages might be awarded for measures taken during the state of emergency and not cancelled when the state of emergency has ceased to exist or taken when such state had ceased to exist.

1059. This Tribunal finds it plain that Argentina's crisis faced in late 2001 and which continued into 2002 may fall within the scope of Article XI. As the tribunal in *Continental* stated:

> "It is impossible to deny, in the Tribunal's view, that a crisis that brought about the sudden and chaotic abandonment of the cardinal tenet of the country's economic life, such as the fixed convertibility rate which had been steadfastly recommended and supported for more than a decade by the IMF and the international community; the near collapse of the domestic economy; the soaring inflation; the leap in unemployment; the social hardships bringing down more than half of the population below the poverty line; the immediate threats to the health of young children, the sick and the most vulnerable members of the population, the widespread unrest and disorders; the real risk of insurrection and extreme political disturbances, the abrupt resignations of successive Presidents and the collapse of the Government, together with a partial breakdown of the political institutions and an extended vacuum of power; the resort to emergency legislation granting extraordinary legislative powers to the executive branch, that all of this, taken together, does not qualify as a situation where the maintenance of public order and the protection of essential security interest of Argentina as a state and as a country was vitally at stake. The fact that

[423] *CMS Award, supra* (n 97) ¶ 359, *LG&E Decision on Liability, supra* (n 309) ¶238, *Enron Award, supra* (n 314) ¶374, *Continental Award, supra* (n 316) ¶179 and *El Paso Award, supra* (n 307) ¶ 611.

> Argentina's Congress declared a "public emergency" in economic, financial, exchange, social and administrative matters in conformity with Art. 76 of its Constitution, and enacted a specific "Public Emergency Law" to cope with the crisis, is powerful evidence of its gravity such as that could not be addressed by ordinary measures. The protection of essential security interests recognized by Art. XI does not require that "total collapse" of the country or that a "catastrophic situation" has already occurred before responsible national authorities may have recourse to its protection. The invocation of the clause does not require that the situation has already degenerated into one that calls for the suspension of constitutional guarantees and fundamental liberties. There is no point in having such protection if there is nothing left to protect."[424]

1060. It is plain that Article XI shall be interpreted on the basis of the Vienna Convention on the Law of Treaties. Further, as stated above, the conditions of application of Article 25 of the ILC Articles on the Responsibility for Internationally Wrongful Acts and Article XI of the BIT are not the same. Thus, Article XI of the BIT, as a specific provision limiting the general investment protection obligations bilaterally agreed by the Contracting Parties, is not necessarily subject to the same conditions of application as the plea of necessity under general international law. However, as also recognised in *Continental*[425] and *El Paso*[426], concepts used in Article 25 of the ILC Articles on the Responsibility for Internationally Wrongful Acts "assist in the interpretation of Article XI itself." When interpreted in the light of these principles, the requirement under Article XI that the measures must be "necessary" presupposes that the State has at least not significantly contributed to creating the situation which it relies upon when claiming the lawfulness of its measures.

1061. Pursuant to Article 31(1) of the Vienna Convention, a treaty shall be interpreted in good faith and in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose. As can be seen

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[424] *Continental Award*, *supra* (n 316) ¶ 180.
[425] *Ibid* ¶ 168.
[426] *El Paso Award*, *supra* (n 307) ¶ 613.

from its preamble, the object and purpose of the BIT is *inter alia* to “maintain a stable framework for investment and maximum effective use of economic resources.”

1062. However, such economic stability can of course not be total. Also the environment for foreign investment changes, especially when extraordinary circumstances appear. The host State is usually not responsible for the consequences of a state of emergency. However, if the host state has significantly contributed to the situation, it will be responsible. A contrary opinion would, as stated by the Tribunal in *El Paso*, mean that Article XI of the BIT is not being interpreted in the light of its object and purpose, for that Treaty cannot possibly allow for the possibility that if the host State itself has caused or significantly helped to cause, intentionally or by omission, the situation and the consequences complained of, that State may shirk its obligation under the BIT by invoking Article XI.”[427]

1063. The ordinary meaning of “necessity” under Article XI of the BIT implies that the State invoking necessity did not create the situation of necessity. This based on the legal principle that “no one should reap advantages from its own wrong.[428]

1064. Article 31(3)(c) of the Vienna Convention provides that in the interpretation of a treaty, there shall be taken into account together with the context ”any relevant rules of international law applicable in the relations between the parties.” Although the BIT takes precedence over customary international law in the relation between the US and Argentina, this does not mean that customary international law is irrelevant in the case at hand. As stated by the Iran-US Claims Tribunal in the Amoco case:

> “...the rules of customary international law may be useful in order to fill in possible lacunae of the Treaty to ascertain the meaning of

[427] *El Paso Award*, *supr*a (n 307) ¶ 615.
[428] Bing Cheng, *General Principles of law as applied by international courts and tribunals*, 1953, para 150 (Exhibit C-457).

> undefined terms in its text or, more generally to aid interpretation and implementation of its provisions"[429]

1065. Article 31(3)(c) of the Vienna Convention provides that customary international law shall be taken into account in interpreting a treaty This was confirmed by the ICJ in the *Oil Platform* case:

> "The Court cannot accept that [the essential security interest provision] was intended to operate wholly independently of the relevant rules of international law… The application of the relevant rules of international law relating to this question thus forms an integral part of the task of interpretation …"[430]

1066. There can be no doubt that one of those general rules of international law is the one codified in Article 25(2) of the ILC's Articles on the Responsibility of States for Internationally Wrongful Acts which provides in part, that: "In any case, necessity may not be invoked by a State as ground for precluding wrongfulness if... (b) The State has contributed to the situation of necessity."

1067. Both parties note that the ILC Commentary on Article 25 explains that in order for a claim of necessity to be precluded under Article 25(2) (b), the State's contribution to the situation of necessity must be "sufficiently substantial and not merely incidental or peripheral."[431] It is common ground between the parties that this rule, as framed by the Commission, forms part of general international law.

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[429] *Amoco International Finance Corporation, Claimant v. Islamic Republic of Iran, National Iranian Oil Company, National Petrochemical Company and Kharg Chemical Company Limited,* ("*Amoco v Iran"),* Case No 56, Chamber 3, Award No 310-65-3 (14 July, 1987) ¶ 112.

[430] *Iran v United States, Case Concerning Oil Platforms,* ICJ Judgment on the Merits (6 November, 2003) para 41 (Exhibit AL RA-7).

[431] *Report of the International Law Commission on the work of the 33rd Sessio*n, UN. GAOR 56th Sess. Supp. No 10 Ch IV: Commentaries to the Articles on Responsibility of States for Internationally Wrongful Acts, commentary to Art. 25 ¶ 20.

1068. The rule has also been applied by ICSID tribunals in interpreting Article XI of the BIT. The tribunal in *LG&E* stated as follows:

> "The State must not have contributed to the production of the state of necessity. It seems logical that if the State has contributed to cause the emergency, it should be prevented from invoking the state of necessity. If there is fault by the State, the exception disappears, since in such case the causal relationship between the State's act and the damage caused is produced."[432]

1069. In *Continental* the tribunal stated, in connection with "essential security interests" referred to in Article XI of the BIT as follows:

> "...if a Contracting Party to the BIT has contributed to endangering its essential security interest, for the protection of which it has then adopted the challenged measures, those measures may fail to qualify as necessary" under Art. XI, since that Party could have pursued some other policy that would have rendered them unnecessary."[433]

1070. The Tribunal concludes that there is a rule of general international law, according to which Article XI is not applicable if the State concerned has significantly contributed to creating the necessity. This means that the rule in question may be used under Article 31 (3) of the Vienna Convention to ascertain the meaning of Article XI of the BIT. Thus, the Article cannot be invoked by a State having itself created such necessity or having substantially contributed to it.

1071. Before examining whether Argentina has contributed to creating the situation on which it relies under Article XI, it is appropriate to determine which Party bears the burden of proof in that regard. This Tribunal considers that the existence of the conditions for the application of Article XI, *i.e.* whether: (a) public order or essential security interests are at stake, and (b) whether the measures are necessary to maintain the former or protect the latter, is to be proven by the Respondent, since it relies on

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[432] *LG&E Decision on Liability, supra* (n 309) ¶ 256.
[433] *Continental Award, supra* (n 316) ¶ 234.

such facts to preclude a finding that the measures breached the BIT. Conversely, it is incumbent upon the Claimants to prove Argentina's contribution to bringing about the necessity of the measures since it relies on such a contribution as a defence against the application of Article XI.

3. The Application of Article XI: Has Argentina Contributed to the Economic Crisis of 2001

a. <u>The Claimants' Position</u>

1072. The Claimants contend that "Argentina's economic "emergency" of 2001 was almost entirely a result of its own economic policy failures".[434] In order to substantiate their position the Claimants have produced a report by a macroeconomic expert, Professor Sebastian Edwards, dated 26 April 2010 and accompanied by many exhibits ("**Edwards Report**"). The Tribunal will examine the Edwards Report as detailing the Claimants' position.

1073. According to the Edwards' Report, "the Argentine economic crisis of 2001-2002 was primarily self-induced."[435] The Report explains that "by failing to implement the package of policies required to support the currency board, Argentina created a weak economic system that was susceptible to crises and highly likely to amplify external shocks" and that during 1999-2000, and in spite of repeated warnings by the international financial community, a number of misguided policies were implemented." Further, the Report asserts that "throughout 2001 a series of serious policy blunders were made by the Government of Argentina, which transformed a recession into an economic crisis that resulted in the abandonment of the currency

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[434] *Claimants' Reply on the Merits,* ¶ 420.
[435] *Expert Report of Professor Sebastian Edwards* dated 26 April, 2010 [hereinafter "*Edwards Report"*] ¶ 6 and ¶ 87.

board. " In order for a pegged exchange rate regime – and in particular, for a currency board regime such as the one implemented in Argentina through the "Convertibility Law" in 1991 – to work properly, a number of supporting policies have to be implemented. These supportive policies include: (a) Fiscal balance; (b) labour markets flexibility; (c) a trade policy that truly opens the economy; and (d) a consistent and credible overall policy stance. Argentina was fully aware of this, but failed to implement many of these required supporting policies:

- **Fiscal balance:** Pegged exchange rate countries – and in particular currency board countries – need fiscal discipline. In the absence of balanced fiscal accounts, the currency board would not be credible, and the public would end up withdrawing deposits from the banking sector. This would restrict liquidity and will result in higher interest rates. The increase in interest rates would, in turn, provoke a decline in investment and a reduction in the rate of economic growth. Furthermore, during economic expansion, the public sector should run surpluses and build up fiscal reserves. These reserves should then be used during periods of economic downturn.[436]

- **Labour market flexibility:** In the absence of exchange rate flexibility**,** the economy needs labour market flexibility in order to accommodate external shocks. If the country has a pegged exchange rate, depreciation is ruled out by definition. Competitiveness must therefore be achieved through a reduction in labour costs. However, if the labour market is heavily regulated and inflexible, labour costs

[436] *Ibid*, ¶ 82.

will not decline, and competitiveness will not improve. In this case the outcome will be a higher rate of unemployment.[437]

- **An open trade sector:** Under fixed exchange rates the degree of openness of the economy is very important. If the economy has a low degree of openness and fixed exchange rates, a modest external shock will result in a large decline in growth, since in a relatively closed economy, GDP will have to contract significantly in order to bring about a modest reduction in imports. If, on the other hand, the economy is very open to trade, even a large external shock will have only a minor impact on economic activity.[438]

- **A strong credible policy stance:** For a currency board to be successful it is essential that the Government's resolve to maintain the peg remains credible. If the Government's credibility wanes, the public will reduce its holdings of the domestic currency: When this happens, bank deposits and bank liquidity will decline. An erosion of credibility will, in turn, translate into higher domestic interest rates, a slowdown in economic growth, new round of deposit withdrawals and further losses in credibility.[439]

1074. Recommendations to that effect were made repeatedly by the World Bank, IMF and independent analysts. It follows that the GOA knew precisely what it needed to do to make the currency board work. It also fully understood that if it did not implement the

[437] *Ibid.*
[438] *Ibid.*
[439] *Ibid.*

required reforms. Argentina's economy would remain highly vulnerable to external factors, and a future currency crisis would be inevitable.[440]

1075. Despite this knowledge, Argentina did not implement the measures required to ensure a proper and credible functioning of the currency board. The only exception was the strengthening of the banking system, where progress was made. First, in the fiscal arena, Argentina ran large and increasing deficits throughout the entire 1992-2000 period. During many of the "good years", when GDP growth was strong, and Argentina could have run surpluses to build up a fiscal reserve fund which can then be used during lean years characterized by slow growth: Argentina did not follow this simple countercyclical rule for fiscal policy. Instead it ran a pro-cyclical fiscal policy. During the "good years" when GDP growth was strong, the country still made very large deficits. Argentina real GDP growth exceeded 5% in 1991, 1992, 1993, 1994, 1996, and 1997.[441]

1076. Moreover, Argentina's fiscal problems were compounded by the GOA's efforts to conceal the true magnitude of the problem. Once discovered these manipulations damage the credibility of the currency board system. Although, the GOA could have implemented a variety of measures to strengthen fiscal discipline, one of the most obvious and significant steps that it could have taken – but did not – was to control provincial spending. Doing so would have required the Government to fundamentally reform Argentina's "Co-Participation Law" of 1988, which created very strong incentives for fiscal indiscipline on the part of the country's provincial governments. The Argentine federal government administered most of the country's main taxes, including income taxes; value added taxes and wealth taxes. The Co-Participation

[440] *Ibid*, ¶¶ 84-85.
[441] *Ibid*. ¶¶ 86 and 96-97.

Law provided for large transfers of those revenues from the federal government to the provincial governments.

1077. In addition, in the decade leading up to 2001 "emergency", the GOA also failed to significantly open its economy by reducing barriers to foreign trade. Between 1991 and 2001, Argentina had the lowest degree of openness of a group of 31 Latin American and Caribbean countries.[442]

1078. Finally, Argentina failed to liberalize its rigid labour market. When Argentine economy eventually experienced "negative demand shocks" in the late 1990s, labour market rigidities rendered Argentine business largely impotent to respond.[443]

1079. Taken together the above analysis shows that, during the 1990s, Argentina's leaders failed to implement fundamental reforms that they knew were necessary for the Argentine economy generally and the currency board, in particular, for domestic political reasons, the economy and the currency board were left highly vulnerable. The result was that when external shocks occurred starting in 1998, they had a far more serious impact on Argentina (and its currency board) than they should have had.

1080. During most of 2001, Argentina still had a chance of solving its problems without abandoning convertibility and devaluing the peso. Achieving this, however, required convincing market participants – both domestic and foreign – that the country could finally put in place deep and durable policy measures that would address the country's long time economic problems and weakness. This meant dealing with labour market regulations and inflexibilities, eliminating protectionist practices that kept the economy relatively closed to the rest of the world, and reforming the onerous and highly inefficient system of union-run social services ("*obras sociales*"). In addition,

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[442] Edwards Report, *supra* (n 435) ¶ 115.
[443] Edwards Report, *supra* (n 435) ¶ 109-114.

it was fundamentally important to address the highly destabilizing and perverse Co-Participation Law, and to avoid further increases in public debt that were not reflected in the official deficit numbers. However, instead of addressing the country's long-term problems, the government embarked on a series of short term manoeuvres many of which further eroded confidence, reduced credibility, and signalled a lack of commitment to the Convertibility Law.[444]

1081. According to the Claimants, one of the most important policy mistakes of 2001 was postponing fiscal and provincial adjustments until after the October 2001 elections. The Minister of Economy, Domingo Cavallo announced a "Zero Deficit" policy based on short term policies such as the reduction in government employees' salaries and pensions. Those measures, which were announced in July 2001, did not address the long-term factors behind the crisis such as the Co-Participation Law, and thus, lacked credibility. Political dynamics during the first three quarters of 2001 were dominated by the government coalition's concern about the congressional elections in October of that year. Campaigning required funding, and thus before October of 2001, provincial governors were unwilling to agree on a reduction of transfers to the provinces. On 15 October 2001, immediately after the congressional elections, the government sought to reach an agreement with the governors, in order to reform the Co-Participation Law, reducing the size of the public sector and restructuring provincial debts. Partisan politics, however, prevailed, and the governors refused to consider reforming the Co-participation Law or enacting other long term reforms. As the negotiations dragged on, depositors withdrew their funds from the banking sector, and Argentina continued losing credibility. In November 2001 Standard&Poor lowered Argentina's long-term sovereign rating to "selective default". At his point

[444] *Ibid*, ¶¶ 117 and 119.

both the Argentine public and international actors lost nearly all confidence in the GOA's willingness to support the currency board.[445]

1082. Contrary to what is contended by Argentina and its experts, external shocks did not play a decisive role in unleashing the crisis. Those shocks were not unique to Argentina. They also affected other Latin American countries. Indeed some other nations in the region were affected more significantly then Argentina. These external shocks were neither unexpected nor were they unusual. They were part of the normal behaviour of the international business cycle. These shocks were not permanent; they were temporary and after some time they reversed themselves.[446]

1083. The Claimants contend that temporal limitations are inherent in Article XI and points out that the *LG&E* Tribunal found that the situation that allegedly justified the application of Article XI ended in April 2003 and that the *Continental* Tribunal found that Argentina could not invoke Article XI for measures it took starting in 2003. These dates roughly accord with the opinion of most experts, including Argentina's, concerning the end point for Argentina's financial crisis. That Argentina has offered no evidence that its so-called situation of necessity persisted past the end-points determined by other tribunals and experts, renders its invocation of Article XI temporally irrelevant to the vast majority of issues in this case, including its interference with natural gas prices and all of its export restriction and withholding measures.

b. Argentina's position

1084. In its Counter-Memorial, Argentina, referring to Article 25 of the ILC Articles, denies having contributed to the state of necessity. According to Argentina such

[445] *Ibid*, ¶¶ 121-123.
[446] *Ibid*, ¶ 135.

contribution must be sufficiently substantial, and not merely incidental or peripheral, to disregard the existence of the state of necessity. Thus not just any state contribution to a situation of collapse is enough to rule out the possibility of asserting the state of necessity defence. Arguing otherwise would, according to Argentina, entail distorting the concept of necessity.

1085. Argentina did not contribute to the occurrence of the state of necessity to an extent such that the possibility of raising such defence is precluded, as it is evident that it never in the least sought to give rise to a situation in which it would stand as the main victim.[447]

1086. On the contrary, the instant case involved countless external factors that critically contributed to the emergency situation building up: 1. Sudden reversion of the flow of capitals; 2. Weakening in Argentina's trading partners' demand; 3. Marked decline in the prices of goods exported by Argentina; 4. Strong depreciation of the Brazilian currency – Brazil being Argentina's main trading partner and competitor; 5. Appreciation of the U.S. dollar and resulting over-appreciation of the Argentine peso; 6. Hike in the Federal Reserve's interest rates, bringing about a policy of economic contraction during a recession stage of the Argentine economy. In these external factors the Argentine Republic had little, if any, involvement, and which accumulated to concoct an *explosive cocktail* that largely exceeded the causation threshold required under the ILC Articles. Taking no action at all would have been detrimental to the society as a whole.[448]

1087. Regarding the defence of necessity, in its Rejoinder, Argentina deals separately with Article XI and Article 25 of the ILC Articles. However, Argentina refers essentially to

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[447] *Ibid*, ¶ 661.
[448] *Ibid*, ¶¶ 656-657.

Article 25 when dealing with the issue of "non-contribution."[449] Argentina addresses issues raised by the Edwards Report by relying on a Report by Professor Nouriel Roubini dated 8 August 2010 presented with the Rejoinder (the "**Roubini Report**"), the Report by Professors Mario Damill and Robert Frenkel dated 30 August 2010 also presented with the Rejoinder (the "S**econd Damill-Frenkel Report**") and a Report by Professor Barry Eichengreen (the "**Eichengreen Report**") dated 13 August 2010 presented with the Rejoinder as well. Further Argentina invokes another Report by Professors Mario Damill and Robert Frenkel and dated 26 November 2009 (the"**First Damill- Frenkel Report**") presented with Argentina's Counter-Memorial on the Merits. The main purpose of the Second Frankel-Damill Report is to respond to the observations about and objections to their earlier report contained in the report by Professor Sebastian Edwards dated 26 April 2010.[450] These Reports will be analysed hereafter to the extent that they deal with Argentina's contribution to the crisis.

1088. Argentina argues that the GOA attempted to run fiscal surpluses at the time of the currency board system and caused primary expenditure (i.e. excluding debt interest payments) to fall below the revenues raised while such system was in force.

1089. According to the Roubini Report, Argentina's fixed exchange rate regime was not viable or sustainable, since it was not consistent with economic or macroeconomic fundamentals that have worsened because of domestic and external shocks. Thus, when such regime becomes unsustainable, there will be a run on the reserves of the central bank (when capital controls are not imposed). After this occurred in Argentina, the only feasible and economically sensible option – after the currency

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[449] Rejoinder of the Argentine Republic ¶¶ 748-782.

[450] *Second Report for the Arbitration Procceeding Entitled "Mobil Exploration and Development Argentina Inc. Suc. Argentina and Mobil Argentina Sociedad Anónima v. the Argentine Republic* of 30 August 2010, prepared by *Professors Mario Damill and Roberto Frenkel* [hereinafter "*Second Damill-Frenkel Report"*] ¶ 3.

crisis forced the abandonment of the currency board – was a move to a float. The experience of Argentina with a currency crisis and a move to a float was not an exception but rather a rule among economies with fixed rates in the last decade.[451]

1090. In the case of Argentina, while for the first few years the currency board was viable based on economic fundamentals, starting in 1998 it became increasingly vulnerable and eventually not viable because of: i) a series of shocks of the economy; ii) large and eventually unsustainable external imbalances and loss of competitiveness; iii) large fiscal imbalances and debt accumulation; iv) structural vulnerabilities.[452]

1091. The external shocks identified by Roubini and starting in 1998 made the pegged parity increasingly unsustainable. Those shocks included a) a "sudden stop" of capital inflows in 1998 and 1999, making the cost of borrowing in international capital markets higher and its quantity much more limited; b) weakening of demand in major trading partners of Argentina, notably in Brazil during 1998; c) the strong fall in oil and other commodity prices that sharply worsened Argentina's terms of trade; d) the sharp devaluation of the Brazilian currency against the U.S: dollar in early 1999; e) the general strengthening of the U.S. dollar against the euro and other major currencies between 1998 and 2001, causing Argentina to lose competitiveness in European and other markets, because the nominal value of the Argentinean peso was tied to U.S. dollar; f) the tightening of monetary policy by the U.S. Fed between mid-1999 and mid-2000, driven by concerns in the U.S. about macroeconomic heating. The combination of these shocks led starting the second half of 1998, to

[451] Expert Report of Nouriel Roubini *dated 8 August, 2010*[hereinafter *"Roubini Report"*] ¶¶ 12-13 and 15.
[452] *Ibid*, ¶ 17.

slowdown of GDP growth and then an outright recession that continued and worsened until 2001.[453]

1092. In Argentina, persistent fiscal deficits led to an accumulation of growing stock of public debt, particularly as the economy began to shrink and interest rates rose after 1998. The fiscal deficits worsened after 1998 because of two factors; the worsening recession that led to a fall in revenues and a cyclical increase in spending, and the sharp increase in interest payments resulting from the sharp increase in the foreign debt sovereign spread and domestic interest rates following the collapse of capital flow to emerging markets in 1998. After 1998, fiscal deficit and debt accumulation was exacerbated by the increase in nominal and real interest rate for Argentina. That increase was driven by a combination of external and domestic factors: the sudden stop of capital flows to emerging markets in 1998; the worsening domestic fiscal position and the inability of successive governments to achieve primary surpluses large enough to stop an unsustainable debt dynamic.[454]

1093. In addition to the external shocks, lack of competitiveness, external imbalances and fiscal vulnerabilities, Argentina had a number of structural vulnerabilities that made its economy a poor candidate for a permanent fixed exchange rate or a currency board. Those structural vulnerabilities included: small degree of openness of the economy caused by an older history of inward-oriented trade policies; labour market rigidities; downward rigidity of nominal prices that required a long period of deflation to undo the real appreciation of the currency caused by domestic and external shocks; a very large debt to exports ratio and an enormous currency mismatch due to the fact

[453] *Ibid*, ¶¶ 18-19.
[454] *Ibid*, ¶¶ 21-22.

that almost all of Argentina's domestic and external government debt was denominated in dollars.[455]

1094. According to the Roubini Report these factors made the fixed exchange rate inconsistent with economic fundamentals and lead to a currency crisis. Argentina's macroeconomic hands were tied since it could not adjust its currency peg without bankrupting many firms and the government, it lacked an independent monetary policy, and its high existing debts left it unable to run a countercyclical fiscal policy[456]

1095. Roubini concludes:

> "In summary, the Argentine currency board regime was not sustainable and had to be abandoned given the external and other shocks that hit the economy. Given the macroeconomic conditions of Argentina, including a most severe economic depression, the currency board had to be abandoned. Also, the only really feasible and desirable exchange rate regime after the collapse of the peg was a floating exchange rate regime such as the one adopted by the local economic authorities in Argentina; alternatives such as dollarization were undesirable and/or unfeasible. The ensuing pesification of foreign currency liabilities was also the unavoidable consequence of the abandonment of the currency board and necessary to dampen the massive and severe real and financial distress of the economy following the currency board collapse."[457]

1096. According to the Second Damill-Frenkel Report since, economic science in general – and Edwards Report macroeconomics in particular – is not an experimental discipline, Edwards arguments must be understood as opinions of the author, rather than as scientific arguments subject to tests. Such opinions are grounded on Edwards' own knowledge as an economist and on references to other opinions and studies which are

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[455] *Ibid*, ¶ 24.
[456] *Ibid*, ¶¶ 30-31.
[457] *Ibid*, ¶ 113.

cited to reinforce the persuasiveness of his arguments.[458] Damill and Frenkel are of the view that external factors were the "proximate cause or trigger of the crisis. Such factors were the fall in the price of exports, the revaluation of the U.S. dollar, the generalised fall in the emerging markets' bond prices and the ensuing increase in country risk premiums and interest rates following the crisis in Southeast Asia, and the devaluation of the Brazilian currency.[459]

1097. As to individual issues raised by the Edwards Report, *inter alia* the following is noted by Damill and Frenkel:

> "Edwards' statement that labour market flexibility is one of the reforms which the GOA failed to implement is cantered upon the salary-exchange ratio. A larger drop in nominal salaries than that experienced would have probably led to more recession, bankruptcies, more or less widespread financial problems and a higher decoration in fiscal accounts as a result of the fall in the revenue from taxes and contributions to retirement plans. A sharp fall in salaries would probably tend to worsen the problems faced by the economy. "[460]

> "as to the measures which, according to Edwards should have been adopted in 2001 to avoid the devaluation, the default on public debt and the pesification, the main measure consisted in "a comprehensive voluntary debt exchange, with the assistance of the international community, by exchanging existing bonds for bonds with longer maturities and lower interest rates." Such extraordinary financial operation could only have taken place in the event that IMF or another financial institution or government had granted a subsidy or a certain type of guarantee for the new bonds issued by the GOA. A voluntary debt exchange was conducted in June 2001 (the so-called megaswap). However, the IMF did not take part therein and interest rates for the new bonds were considerably higher than those of the original bonds swapped. The megaswap had no respite to the escalation of the crisis."[461]

[458] Second Damill-Frenkel Report, *supra* (n 450) ¶ 26.
[459] *Ibid*, ¶ 28.
[460] *Ibid*, ¶¶ 34-47.
[461] Second Damill-Frenkel Report, *supra* (n 450) ¶¶ 44-45.

1098. With regard to the fiscal evolution, Edwards expresses opinions which are based upon citations or figures from secondary sources, selected as he deems fit. According to Edwards there was a noticeable improvement in the Argentine tax performance during the early years of the currency board: the consolidated adjusted deficit improved during 1992-1996, declined in 1997, climbed to 3.7% of GDP in 1998, to 6.6% in 1999 and it was 5.4% of GDP in 2000. According to Damill's and Frenkel's estimate, based on more reliable sources, the consolidated public sector average deficit for the 1991-1994 period was of only 0.56% of GDP. During such period Argentina's Public sector had a positive primary result of 1.3 of GDP *vis-à-vis* an average deficit of 4.4% of GDP between 1981 and 1991. The difference between the deficit figures derives mainly from the fact that the normalization of debts incurred by the public sector, particularly to pensioners and State providers before the implementation of the currency board system was in Edwards' secondary source recorded as an expense. Between 1995-1997, there was a slight deterioration in the Argentine fiscal situation. The average deficit for such three-year period was about 2.56% of GDP per year, i.e. two points of GDP higher than the average percentage for the 1991-1994 period. Such increase was mostly the result of the imbalance in public accounts which derived from the reform of the pension system which was both approved and implemented in 1994. Fiscal surplus cannot be assumed to be synonymous with immunity against crises. Neither does tax result showing a modest deficit lead to a critical outcome.[462]

1099. The reform in the distribution of taxes between the Federal State and the provinces, which is described by Edwards as a necessary reform, entails a major institutional-political problem, Argentina being a federal State. Mainly for that reason the implementation of such change constitutes a complex institutional-political task, as

[462] *Ibid*, ¶¶ 60-67.

well as a considerable source of conflict. Such reform poses a problem which not only takes time to solve, but requires negotiations and agreements as well, since the potential conflicts involved may produce short-term negative effects.[463]

1100. As to Edwards' argument that the negative external shocks were only temporary, it should be observed that that the temporary nature of an external shock does not preclude its ability to cause harm. Temporary shocks may have long-lasting effects.[464]

1101. Edwards' argument that the Argentine economy is "closed" and that such fact would have made things more difficult during the last phase of the currency board is misleading. At the beginning of the 1990's there was a shift to a new trade regime, where the economy was much more exposed to competition from imported goods. Even though trade policies may be modified through policies the modification of "openness measures", such as the ratio between international trade flows (export plus import) and product, does not exclusively depend on such policies. Any change in these relationships takes time and depends on people's behaviour and, what is very important, is affected by the devaluation of the real exchange rate as the value in local currency of exports and imports is a function of the exchange rate. The degree of openness increased until 1997, decreased in 1998-2001, to increase again thereafter. Thus it may hardly be argued that trade protectionism hindered the design of Argentina's economic policy under the currency board system.[465]

1102. The Eichengreen Report's conclusions also confirm the explanations provided by Damill-Frenkel and by Roubini, as well as the impact of external shocks on the development of the crisis. The existence of external shocks was a key element in the

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[463] *Ibid*, ¶ 71.
[464] Ibid, ¶ 74.
[465] Ibid, ¶¶ 115-116.

emergence of the crisis and this is the conclusion at which well-known international macroeconomic experts have arrived.

1103. In the opinion of Professor Eichengreen:

> "Argentina in fact made considerable progress in reforming its economic system in the early and mid-1990s. Commercial banks were privatized. Banks were relatively well capitalized. The authorities avoided incurring short-term debt that posed rollover risk. The capital account of the balance of payments was liberalized. Nonbank public enterprises were privatized. Tariffs and quotas were reduced. Initiatives were taken to reform labour as well as product markets. One reflection of these facts is that Argentine bond spreads were running below the Emerging Markets Index Plus average for emerging-market economies in 1997. Another reflection is the praise that Argentina received for its policies at the IMF-World Bank meetings in 1998"[466]

1104. Argentina concludes that it has been sufficiently demonstrated in this arbitration proceeding that the Argentine Republic did not contribute to create any of the crises which led to the adoption of the measures contested by the Claimants (unlike the Claimants, which did contribute to the energy shortage problems).

c. The Tribunal's Analysis

1105. At the outset, the Tribunal emphasises that States are basically free to adopt economic and monetary policies of their choice. This Tribunal is not subjecting past economic policies to any judicial, administrative or political review.

1106. In addressing the question whether Argentina contributed to the situation of emergency on which it relies, the Tribunal will be guided essentially by two considerations. It acknowledges on one hand Argentina's right as a sovereign state to choose the economic policy best suited to the needs of the population and on the other hand it will take due account of the fact that the protection offered by the BIT to the

[466] Expert Report of Barry Eichengreen dated13 August, 2010 ¶10.

Claimants' investment is suspended to the extent that Article XI is applicable. The Tribunal will also take into account the fact that the Claimants bear the burden of proof of the facts regarding Argentina's contribution to the economic crisis of 2001.

1107. Although the experts diverge in their analysis of Argentina's responsibility for causing the economic and currency crisis, there are a few aspects on which there is some convergence of opinions.

1108. Roubini, who is Argentina's expert, acknowledges the significant role that Argentina's fiscal deficits and debt accumulation played in provoking the currency crisis of 2001. Although maintaining that Argentina's fiscal problems were partly aggravated by recession and external interest rates after 1998, his report suggests that the GOA's lack of fiscal control was already a problem at that time, as is shown by the following quotations:

> "Argentina's fiscal deficits and debt accumulation worsened after 1998,"
>
> " In the case of Argentina, while for the first two years the currency board was viable based on economic fundamentals, starting in 1998 it became increasingly vulnerable and eventually not viable because of : ...iii) large fiscal imbalances and debt accumulation...,"
>
> "In Argentina, persistent fiscal deficits (and a partially botched social security privatisation in the 1990s) led to an accumulation of a growing stock of public debt, particularly as the economy began to shrink and interest rates rose after 1998."[467]

1109. Also the Claimants' expert, Edwards, considers the absence of fiscal discipline as one of the causes of the economic and currency crisis of 2001.[468]

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[467] Roubini Report, *supra* (n 451) ¶¶ 16-17 and 21.
[468] Edwards Report, *supra* (n 435) ¶ 95.

1110. Roubini also concurs with Edwards' view that Argentina's failure to liberalise labour markets and trade policies played a significant role in bringing about the 2001 currency crises. He concedes that also the "small degree of openness of the economy caused by an older history of inward-oriented trade policies and trade market rigidities" "made the fixed rate regime fragile and vulnerable to shocks."[469]

1111. As mentioned above, the experts diverge in their analysis of responsibility for causing the Argentina economic and currency crisis. The Edwards Report considers such crisis to have been primarily self-induced by Argentina. The Roubini Report holds that the essential factors of the crisis were external shocks and attributes the currency collapse to macroeconomic factors, although he concedes that "fiscal slippages did occur in Argentina in the 1990's"[470]

1112. The Second Damill-Frenkel Reports does not provide much evidence in support of its various contentions. This is conspicuous since that Report was meant to rebut the Edwards Report, a comprehensive detailed and well-documented work[471]Thus the remark that Edwards' arguments "must be understood as opinions of the author"[472] is misguided.

1113. The evidence filed in these proceedings shows clearly that both internal and external factors caused the crisis that occurred in Argentina at the end of 2001. Having fully considered the parties' arguments and the evidence before it, a majority of the Tribunal concludes that Argentina's failure to control several internal factors, in particular the fiscal deficit and debt accumulation and labour market rigidity,

[469] Roubini Report, *supra* (n 451) ¶ 24 title of Section V.
[470] Roubini Report, *supra* (n 451) ¶ 42.
[471] Edwards Report, *supra* (n 435) is accompanied by 142 exhibits.
[472] Second Darmill-Frenkel Report, *supra* (n 450) ¶26.

substantially contributed to the crisis. The progressive worsening of internal factors diminished Argentina's ability to respond adequately to external shocks.

1114. The Tribunal's conclusions find support in IMF Independent Evaluation Offices (IEO) Evaluation Report of 2004: "The IMF and Argentina 1991-2001."[473] The Report was examined [and presumably approved] by the Argentinean authorities and benefited from substantial contributions by Roubini.[474]

1115. The majority of this Tribunal finds the following passages of the IEO Executive Summary significant:

> "The crisis resulted from the failure of Argentine policymakers to take necessary corrective measures sufficiently early, particularly in the consistency of fiscal policy with their choice of exchange rate regime. The IMF on its part erred in the pre-crisis period by supporting the country's weak policies too long, even after it had become evident in the late 1990s that the political ability to deliver the necessary fiscal discipline and structural reforms was lacking."
>
> "While fiscal policy improved substantially from previous decades, the initial gains were not sustained, and the election-driven increase in public spending led to a sharp deterioration in fiscal discipline in 1999. As a result, the stock of public debt steadily increased, diminishing the ability of the authorities to use countercyclical fiscal policy when the recession deepened."
>
> "Insufficient attention was paid to the provincial finances, the sustainable level of public debt for a country with Argentina's economic characteristics was overestimated, and debt sustainability issues received limited attention."
>
> "The IMF correctly identified structural fiscal reforms, social security reform, labor market reform, and financial sector reform as essential to enhancing the medium-term viability of the convertibility regime, by promoting fiscal discipline, flexibility, and investment."

[473] Annex 51 to the Edwards Report, *supra* (n 435) Independent Evaluation Office, *The IMF and Argentina 1991-2001*, [*2004*] [hereinafter "*IMF, Evaluation Report*"] and (Exhibit C-662).
[474] IMF Evaluation Report p. vii.

> "Some gains were made in the early years, but the long-standing political obstacles to deeper reforms proved formidable. Little progress was made in later years, and the earlier reforms were even reversed in some cases."[475]

1116. Moreover, the majority of the Tribunal notes the following passages of the same report:

> "In the early 1990's, the IMF, the Argentine authorities, and most outside observers were in broad agreement that for convertibility to remain viable, the restrictive labor market practices that have evolved over the previous half century would have to be revised."
>
> "However progress in this critical area was negligible." [476]
>
> "Fiscal policy was the single most prominent topic of discussion between the IMF and the Argentine Authorities for virtually the entire period of convertibility. While fiscal policy often dominates the interactions with member countries, it assumed a particular importance in the case of Argentina. For one thing, there was a history of fiscal irresponsibility that had in the past contributed to repeated cycles of defaults and hyperinflation. Moreover, the choice of convertibility regime made fiscal policy especially important."[477]
>
> It is clear that Argentina's vulnerability arose from the inconsistency between the weakness of fiscal policy and its choice of the convertibility regime...If Argentina's public sector had generated surpluses in its fiscal account during the pre-crisis years, it could have avoided the tightening liquidity constrains in 2000 and the all funding crisis in the public sector in 2001. Argentina also would have enjoyed greater flexibility in using fiscal possibility to cope with the impact of adverse shocks and would have been spared from the need to contract policy when output was already declining.[478]

1117. A number of statements made by qualified international experts and by Argentina's former leaders confirm the substance of the Edwards Report as well as the analysis of the IEO Report.

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[475] IMF Evaluation Report p. 3-4
[476] IMF Evaluation Report p. 31.
[477] IMF Evaluation Report p. 23.
[478] IMF Evalutaion Report p. 14.

1118. The 1996 World Bank Report emphasized the need for “fiscal adjustment” at both the provincial and central governments levels that “must come” from expenditure reduction since the potential for revenue increases is limited.[479]

1119. The former Argentine Minister of the Economy and Finance Domingo Cavallo stated:

> “The most important lesson to be learned from the Argentine experience relates to the importance of fiscal policy and, particularly, of fiscal discipline during good times. In my 1994 interview, I emphasized the role of fiscal balance as a precondition for stability. However, stability requires more than just that. During periods of rapid growth and favorable external conditions, it is necessary to generate a fiscal surplus as a cushion for the negative external shocks that may show up unexpectedly at any moment. Argentina should have done this between 1991 and 1994, and again between 1996 and 1998, but it did not. Therefore, at the time of external shocks, it depended on foreign financing precisely at a time when foreign expectations turned sour.”[480]

1120. Eduardo Duhalde, President of Argentina, at the time of the crisis, observed in an Article published in the Financial Times on 12 July 2004.

> “In the case of Argentina, no one bears more of the blame for the crisis than Argentina itself. We spent more than we earned; we failed to complete the full cycle of economic reforms; and we tied ourselves to the most productive economy in the world without building our own productivity. Of course, this was compounded by the global decline in commodity price, by protectionism in key markets and by shifts in global capital flows. Yet Argentina’s crisis is largely home grown.”[481]

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[479] World Bank, *Argentina Provincial Finances Study: Selected Issues in Fiscal federalism*, July 1966, pp. iv-v (Exhibit C-630).

[480] Domingo Cavallo, *Eleven Years Later: What Went Wrong in Argentina 2003-2006*, HARV.INT’L. REV 42. 45 (2005) (Exhibit C-559).

[481] Eduardo Duhalde, *Argentina Regrets*, Financial Times (USA Edition), 12 July 2004 (Exhibit C-629).

1121. The Nobel Economist Gary Becker has concluded that: "The Argentine problem arose because spending by the Government, including the provinces, was very excessive and not controlled."[482]

1122. In an article published on 25 March 2002, Michael Mussa, Senior Fellow, Institute for International Economics in Washington D.C., wrote:

> "Enumerating the many things that contributed to Argentina's tragedy, however, should not obscure the critical failure of Argentina's economic policy that was a fundamental cause of the disaster – namely the chronic inability of the Argentinean authorities to run a responsible fiscal policy. This is an old and a sad story for Argentina."[483]

1123. The Tribunal finds, like the Tribunal in *Continental*, that "[e]ven *ex post facto*...qualified economic observers remain in disagreement as to the exact causes of the crisis and the mix of measures that might have avoided it.[484] However, since Article XI is not "self-judging", the Tribunal has, as said by the Tribunal in *El Paso*, "the power and the duty to make sure that all conditions for its application are satisfied, including the absence of a substantial contribution by Argentina to the crisis of 2001."[485]

1124. The Tribunal agrees that economic science in general – and macroeconomics in particular – is not an experimental discipline and that "in economic matters, the analysis of causation, that is the determination of which facts caused a certain other fact, or whether a certain fact was among the contributory causes of that certain other fact and whether its impact was material, does not lend itself to the same scientific

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[482] "El problema argentino surgió porqueel gasto deol gobierno, incluyendo a las provincias,fue muy exceesivo y no fue controlado." *Falta mucho para la recuperación Argentina, dice Gary s. Becker: reflexiones del Nobel de Economía 1992*, LA NACION, 17 August 2005 (Exhibit C-561).
[483] Michael Mussa, *Argentina and The Fund From TriumphcTo Tragedy*; Institute for International Economics, Washington D.C., 25 March 2002 p. 6 Annex 49 the Edwards Report.
[484] *Continental Award, supra* (n 316) ¶ 224.
[485] *El Paso Award, supra* (n 307) ¶ 665.

analysis as in the domain of the so-called exact sciences and of natural phenomena."[486] However, the evidence presented by the Claimants, including statements by Messrs. Cavallo and Duhalde, regarding the actions and omissions by Argentina until the end of 2001, support the conclusion of a majority of the Tribunal that Argentina contributed to the crisis to a substantial extent, so that Article XI cannot come to its rescue.

1125. Arbitrator Remiro Brotóns in disagreement states his reasons in a separate opinion.

4. Article XI of the BIT is subject to temporal limitations.

1126. Having regard to the fact that that the majority of the Tribunal has found that Argentina has substantially contributed to the situation on which Argentina relies under Article XI, there is no need to evaluate whether the impugned measures were "necessary" for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the protection of Argentina's own essential security interests within the meaning of the BIT. However for completeness of the analysis, the Tribunal unanimously emphasises that temporal limitations are inherent in Article XI of the BIT. The Tribunal considers that *all* the measures adopted or kept in force by the GOA after the date on which the 2001- 2002 crisis in Argentina was over were in no event necessary because of that crisis. The defence under Article XI of the BIT would therefore not be available regarding measures taken after the end of the crisis.

1127. The *LG&E* Tribunal found that crisis ended on 26 April 2003.[487] The tribunal in *Continental* found that Argentina could not invoke Article XI for measures it took

[486] *Continental Award, supra* (n 316), footnote 356.
[487] *LG&E Decision on Liability*, *supra* (n 309) ¶ 226.

starting 2003 [488] and according to Argentina's expert Eduardo Ratti the crisis ended even earlier.[489]

1128. The Tribunal considers that the crisis which would have justified application of Article XI absent Argentina's substantial contribution to its occurrence ended at the latest in April 2003.

1129. However, the shortage of natural gas in Argentina is an undisputed fact. The parties disagree concerning the reasons of this shortage. The Tribunal considers that this shortage is not a part of the crisis that broke out in late 2001 and ended at the latest in April 2003, and therefore has to be considered on its own and not as a corollary of that crisis. This view is also supported by the fact that in January 2002 gas export contracts were not included in the pesification. In fact, the export of natural gas provided a great amount of foreign currencies. The Tribunal recognises that the domestic supply of natural gas is a primary and fundamental objective in Argentina, as in any country. The same applies to taxes as a means to fulfil the needs of public services, including supply of energy. However, these are foreseeable circumstances that must be taken into account in a precautionary and prudent legislation.

1130. As regards export permits, the legislation in force before the adoption of the challenged measures warned repeatedly that the needs of the domestic market had to be guaranteed. Export permits were given after an evaluation of the domestic supply. Leaving aside the provisions concerning the exports of *excess gas*, export authorisations were set as firm and definitive permits. Argentina has not shown that the producers who were authorised to export firm volumes of natural gas had violated

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[488] *Continental Award*, *supra* (n 316) ¶¶ 221, 266 and 320.
[489] Ratti Witness Statement, *supra* (n 276) ¶¶ 15-16.

their legal obligations. Therefore, the Tribunal considers that Argentina's measures adopted to cope with the gas shortage do not fall within Article XI of the BIT.

1131. As to the export withholdings and the basis of calculation of the royalties, the challenged measures, although they were provided for by virtue of the Emergency Law, were only applied once the GOA took measures that restrict exports forcing the rerouting of volumes of gas to the domestic market. Therefore, the Tribunal considers that the relevance of Article XI of the BIT must be considered only from the perspective of the 2004 energy shortage. This leads to the same conclusion that has been reached as to the measures that restrict exports of natural gas forcing the rerouting of volumes of gas to the domestic market.

XIII. DECISION OF THE TRIBUNAL ON LIABILITY

1132. Based on the above reasoning and findings, the Tribunal DECIDES as follows:

a) The Tribunal has jurisdiction over this dispute as presented by the Claimants taking into account the conclusions under paragraph 284, 285 and 864;

b) Argentina breached its obligations under Article II(2)(a) of the BIT by failing to accord fair and equitable treatment to MEDA's and MASA's investment. as well as its obligations under Article II(2)(c) of the BIT to the extent the obligations pertinent to the investment to which Argentina has specifically entered into with the Claimants have been breached and have resulted in the violation of the standards of protection under the BIT;

c) All other Claims by MEDA and MASA are rejected;

d) The Argentine Republic is liable to MEDA and MASA for the aforementioned violations of the BIT and the damages thereby suffered by MEDA and MASA must be compensated by Argentina, as will be determined in a separate quantum phase of these arbitration proceedings, and in respect of which this Tribunal retains jurisdiction. The Tribunal will issue a separate order concerning the further proceedings for the quantum phase;

e) Any decision on costs of the arbitration is reserved.

Done in English and Spanish, both versions being equally authentic.

Professor Piero Bernardini
Arbitrator
Date: March 29, 2013

Professor Antonio Remiro Brotóns
Arbitrator
Date: March, 27, 2013
Subject to the attached individual opinion

Justice Gustaf Möller
President of the Tribunal
Date: 2 April 2013

SEPARATE OPINION OF PROFESSOR ANTONIO REMIRO BROTONS, ARBITRATOR

In order to proceed in logical order, I will explain my opinion in accordance with the following structure:

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A. Overview

1. I agree with the Tribunal's decision that it has jurisdiction over the dispute "taking into account the conclusions under paragraphs 284, 285 and 864" (para. 1132(*a*)), as well as its determination that the Argentine Republic is liable for breaching its obligations under Article II.2(a) of the Treaty between the Argentine Republic and the United States of America Concerning the Reciprocal Encouragement and Protection of Investment, by failing to provide fair and equitable treatment to the Claimants' investment, and Article II.2(c), "to the extent the obligations pertinent to the investment to which Argentina has specifically entered into with the Claimants have been breached and have resulted in the violation of the standards of protection under the BIT" (paras. 1132(b) and (c)).

2. I disagree, however, with respect to the reasoning of certain parts of the Decision. Therefore, despite my respect for the majority's view, I feel obliged to express my opinion.

3. My disagreement with the Tribunal's line of reasoning concerns, most of all, the interpretation of Article XI of the Treaty, under which the obligations undertaken by one Party shall not impede the application of measures necessary for the maintenance of public order or the protection of its own essential security interests, and its relation with the "state of necessity" under rules of general or customary international law, as put forward especially in paragraphs 1015, 1024-1029, 1057-1071, 1105-1124, 1126, and 1128.

4. The Tribunal (paras. 1024, 1060) claims to acknowledge and deems appropriate to emphasize the differences between, on the one hand, the provisions of Article XI of the Treaty and, on the other, the "state of necessity" as a circumstance that excludes the wrongfulness of

an act attributable to the State, as set out in Article 25 of the International Law Commission's (ILC) Draft Articles on Responsibility of States for Internationally Wrongful Acts (2001). The Tribunal, however, holds (para. 1015) that Article XI of the Treaty is *lex specialis* and Article 25 of the ILC Draft Articles is *lex generalis* and, less acceptable to me, uses the conditions for the application of "necessity" under Article 25 of the ILC Draft Articles (par. 1028, 1060) as the interpretative canon for Article XI of the Treaty.

5. Not only that. For the Tribunal, which largely follows the *El Paso* award (paras. 1024, 1060, 1062, 1123, 1124), the question of whether Argentina substantially contributed to the situation it attempted to mitigate with its measures (a requirement it takes from the "state of necessity") comes before the consideration of whether such measures are "necessary" to address threats to the "public order" or "essential security interests;" thus, if the answer to the first question is affirmative, it is no longer necessary to answer the second one as Article XI would not apply, given that no one can benefit from their own mistakes (paras. 1026, 1060, 1063, 1070, 1126). In the Tribunal's view, again following *El Paso*, the object and purpose of the Treaty requires the State be held liable if it has contributed, intentionally or by omission, to the state of emergency (para. 1062).

6. The Tribunal comes to the conclusion that Argentina's failure to control several internal factors, in particular the fiscal deficit, debt accumulation and labor market rigidity, substantially contributed to the crisis, while their progressive worsening, diminished the government's ability to face concurring external factors; consequently, the Tribunal rules out the application of Article XI of the Treaty (paras. 1113, 1124).

7. In my opinion, the Tribunal does not take into account the theoretical and operational differences between Article XI of the Treaty, the safeguard clause, and the "state of necessity", a circumstance that excludes the wrongfulness of an act pursuant to general rules of international law. The interpretation of Article XI cannot be supplemented by more rigorous requirements than those for the "state of necessity". That cannot be the reason to rule out the application of Article XI of the Treaty.

8. The reason why, in my opinion, Article XI of the Treaty fails to cover Argentina's measures concerning pesification and its consequences in the natural gas market, which are at issue in this case, is that Article XI was not designed to support a change of paradigm but only to suspend a paradigm in a state of emergency. Not only does Article XI have temporal limitations, but also structural ones. It cannot uphold measures that are not temporary but virtually permanent, although they may be formally disguised as temporary. Under a *bona fide* interpretation of Article XI, it is just not possible to use a state of emergency as an excuse to substantially alter the foundations of the neoliberal model underlying the obligations assumed under the Treaty. In order to achieve that goal, it is necessary to renegotiate or terminate the treaty.

9. Moreover, leaving Article XI aside, I do not believe that in a situation of crisis like the one experienced by Argentina the "fair and equitable treatment" standard provides for absolute protection of the legal stability commitments assumed by the host State towards the investor. It is fair and equitable for the foreign investor to share the burden placed on the shoulders of society as a whole, provided there is no arbitrariness or discrimination, and provided further

that the situation is not used to pave the way for a permanent change in the economic model underlying the protection system agreed on. In the case at hand, the latter requirement is not met. That is where the breach of the standard lies.

10. Finally, considering that the Tribunal determined in the Decision that Argentina has breached the "fair and equitable treatment" standard *vis-à-vis* the Claimants, the Decision was supposed to devote some paragraphs to rebutting the appropriateness of the "state of necessity," which was relied on by the Respondent to exclude the wrongfulness of its acts.

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B. The *Emergency Law* and its Consequences Concerning the Natural Gas Free Market

I. Article XI of the Bilateral Investment Treaty

11. Article XI of the Treaty between the Argentine Republic and the United States of America Concerning the Reciprocal Encouragement and Protection of Investment provides that the obligations undertaken by one of the Parties in relation to the treatment of the other Party's investments and investors "shall not preclude the application…of measures necessary for the maintenance of public order…or the protection of its own essential security interests."

12. Since the Treaty *shall not preclude the application* of these measures (those necessary for the maintenance of public order or the protection of the State's essential security interests), Article XI becomes a safeguard clause that excludes the application of the Treaty's substantive provisions when such measures are taken. Thus, Article XI defines the operational scope of the Treaty's material obligations.

13. In view of its own terms, this provision's analysis should come before any other on Argentina's violation – or not – of the rules on the treatment afforded to U.S. investments and investors. If the provision is applicable, any violation of the treatment standards under the Treaty would be irrelevant for the Tribunal to decide. If one concludes that the measures adopted, in this case the Emergency Law and the acts performed under such law, were necessary for the purposes mentioned above, it is unnecessary to further develop any arguments as to whether there was a violation of the treaty, or alternatively, no violation due to the exercise of the regulatory power.[1]

14. Moreover, the role played by Article XI, in the context of the Treaty and its logical order in Tribunal's reasoning, reveals its absolute theoretical independence from the "state of necessity" as a circumstance that excludes the *prima facie* wrongfulness of an act, something that can only be analyzed once the wrongful act – in this case, the violation of one or more treatment standards under the Treaty – has been verified.[2]

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[1] *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, § 187.

[2] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 162; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, § 204; *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 552.

15. The conceptual – and operational – independence of Article XI of the Treaty from the "state of necessity" has not always been duly noted in the past, even Argentina itself as Respondent was not a stranger to the confusion in some of its less recent arguments, amidst the high number of lawsuits filed in connection with foreign investments in its territory arising from the government measures taken in the first decade of this century.[3] Article XI is not the tabernacle of the customary "state of necessity".

16. Therefore, it is useful to insist that Article XI, on the one hand, and the "state of necessity" as a general rule of customary international law, on the other, are inherently different and operate in different and separate stages of the process of application of the law to the facts.

17. This conclusion has been increasingly supported by case law, as evidenced by the reasoning of the tribunal in *Continental,*[4] as well as that of the Annulment Committees in *CMS,*[5] *Sempra*[6] and *Enron,*[7] and the tribunal in *El Paso.*[8]

18. However, the proper conclusions of this line of reasoning are not always drawn, not only with regard to the logical order of the reasoning underlying the decision (as can be noted in our Decision, para. 1025), but also in connection with the interpretation of the provisions at stake where – as in our case, following *El Paso* – the tribunal resorts to the elements that characterize the "state of necessity" – required under Article 25 of the ILC Draft Articles – to sustain the explanation of Article XI of the Treaty.

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19. In *El Paso,* the tribunal states that "[o]f course, Article XI has to be interpreted taking into account general principles of international law, some of those being embodied in Article 25."[9] Article XI, the tribunal adds, "is the *lex specialis*, Article 25, the *lex generalis*."

20. This last remark could be accurate if it were simply construed to mean that Article XI, incorporated in a treaty, is a particular rule while Article 25 of the ILC Draft Articles aims at codifying a general rule. It would not be accurate, however, if it were meant to suggest that

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[3] *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, § 176.

[4] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 163-167

[5] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Argentine Republic's Application for Annulment, 8 September 2005, § 129-135.

[6] *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, § 159, 165, 185-189 195-209, 218, 219.

[7] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* 12 ICSID Case No. ARB/01/3 (United States/Argentina BIT) Decision on the Application for Annulment of the Argentine Republic, 30 July 2010, § 405.

[8] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 553 and 554.

[9] See § 552.

Article XI of the Treaty embodies, for the bilateral relations between Argentina and the United States, the general rule of Article 25 of the ILC Draft Articles.

21. In *El Paso*, the tribunal still finds that "the requirement under Article XI that the measures must be 'necessary' presupposes that the State has not contributed, by acts or omissions, to creating the situation which it relies on when claiming the lawfulness of its measures."[10]

22. The tribunal justifies this first by referring to the object and purpose of the Treaty ("to promote and improve the investment climate between the Contracting Parties, notably by establishing some stability regarding the status of investments") which, as inferred from the Treaty's Preamble, would call for liability of the host State for the consequences resulting from a state of emergency if such State has substantially contributed to it because, if this were so, the Treaty cannot allow the host State to avoid its obligations by resorting to Article XI.[11]

23. Second, the Tribunal adds, if Article 31.3(c) of the Vienna Convention on the Law of Treaties, dated May 23, 1969, provides that the interpretation of treaty rules should take into account, *inter alia*, "any relevant rules of international law applicable in the relations between the Parties,"[12] one of such rules would be that embodied in Article 25.2(b) of the ILC Draft Articles, pursuant to which "necessity may not be invoked by a State as a ground for precluding wrongfulness if...[t]he State has contributed (in a sufficiently substantial fashion and not merely incidental or peripheral, as noted in the commentary) to the situation of necessity."[13]

24. As already noted, the Decision in this case assumes almost literally the same rationale and its consequences.

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25. From my point of view, there is no objective ground that justifies this inference. When Article 31 of the Vienna Convention sets out what has been considered a "golden rule" or general rule of interpretation, it simply provides, in subsection 1, that "[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their *context* and in the light of its *object and purpose*" (emphasis added).

26. Relying on Article 31.3(c) of the Vienna Convention to justify the incorporation into Article XI of the rigorous rule of "state of necessity" is ignoring the *raison d'être* of a legal provision that, when requiring that interpretation takes into account, together with the context, "any relevant rules of international law applicable in the relations between the parties," attempts to save the unity of international law, ensure the observance of its imperative rules and consistency amongst different international obligations, without interfering with the interpretation of particular rules in accordance with the interpretative canon already established. The "state of necessity" rule is certainly not *pertinent* to the interpretation of a rule such as Article XI of the Treaty, which is very different conceptually. By way of example, the benefit intended to be achieved from the "state of necessity" rule could

[10] See § 613.
[11] See § 614 and 615.
[12] See § 616.
[13] See § 617 and 618.

also be achieved in opposite direction through reliance on the fundamental principle of a State's permanent sovereignty over its natural resources.

27. . The award rendered in *Continental* was also relied on, arguing that such award expressly verifies the link between Article XI of the Treaty and Article 25 of the ILC Draft Articles, because both attempt to render the application of international obligations more flexible and end up forgiving conducts that would otherwise be illegal; there lies the importance that the customary concept of "necessity" might have when it comes to interpreting Article XI.[14]

28. The tribunal in *Continental*, however, did not follow this path. Quite the opposite. Faced with the task of defining the content of the "necessity" concept in Article XI to determine whether the measures challenged by the claimant were necessary, the tribunal rejects the idea – given the different roles played by Article XI and "state of necessity" – that the interpretation of Article XI goes hand in hand with the requirements set by customary international law on the application of necessity. Considering that the wording of Article XI is rooted in the model clause included in U.S. friendship, commerce and navigations treaties – which, in turn, reflect the wording of Article XX of the 1947 GATT, – the tribunal deemed more appropriate to refer to GATT and WTO case law, which has largely addressed this concept within the context of economic measures that abrogate GATT obligations.[15] And faced with the argument that Argentina could not benefit from a "necessity" to which it had contributed, the tribunal concluded that Article 25 of the ILC Draft Articles could not be the yardstick as to the application of Article XI of the Treaty.[16]

29. As correctly pointed out in our case by the Respondent, it is one thing to interpret a phrase ("measures necessary") taking into account " any relevant rules of international law applicable in the relations between the parties" and a very different one to add requirements or demands to that expression that are not included in it.

30. On the other hand, Article 31.4 of the Vienna Convention provides that a "special" meaning will be given to a term if it is established that the parties so intended but, in the case at hand, there is no evidence that the parties intended to have Article XI interpreted on the basis of the requirements of "state of necessity" imposed by Article 25 of the ILC Draft Articles.

31. The Committee that annulled the award rendered in *Sempra* found that the tribunal exercised a manifest excess of powers by failing to correctly apply Article XI of the Treaty and concluded that Article 25 of the ILC Draft Articles was not an interpretative guide of the terms used in Article XI, but rather "[t]he most that can be said is that certain words or expressions are the same or similar."[17] The application of Article XI only requires that the measures be "necessary" to protect the objectives mentioned in the Article, not that they be necessary in accordance with the requirements of the "state of necessity".

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[14] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 168.

[15] § 192 *et seq*.

[16] § 234. Therefore, I believe the quote of this subsection included in the decision is out of place in the case at hand (par. 1069).

[17] *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Decision on the Argentine Republic's Application for Annulment of the Award, 29 June 2010, § 199.

32. Certainly, Article XI of the Treaty is not meant to *replace* as *lex specialis* or *incorporate* the "state of necessity" as an interpretative rule. By introducing the "state of necessity" conditions into Article XI of the Treaty by way of "interpretation", any operational exegesis of such provision based on its language and the intention of the parties therein reflected is neutralized; that is, any useful effect of Article XI of the Treaty is destroyed, which goes against the most basic rules of text interpretation.

33. Another thing is for the members of a tribunal to apply a more severe and restrictive interpretation of the terms of Article XI in view of its *object and purpose* if they consider such Article is restricted to protecting investments and investors.[18] This, however, would be a mistake because the object and purpose of these treaties also include the development of host countries ("greater economic cooperation," "the economic development of the Parties…,") they may not disregard the public interest to be safeguarded by the host State and, thus, they are to balance the interests of the State and those of investors.[19]

34. In the *El Paso* award, the tribunal recalls that "an interpretation of the fair and equitable treatment standard in the light of the object and purpose of the BIT may not exclusively rely on the interests of foreign investors," referring to and expressly citing the "father of the ICSID Convention" (Aron Broches), who in a lectures held at the Hague Academy of International Law in 1972 stated as follows: "The purpose of the Convention is to promote private foreign investment by improving the investment climate for investors and States alike. The drafters have taken great care to make it a balanced instrument *serving the interests of the host States as well as investors."*[20]

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35. Once the true nature of the rule embodied in Article XI of the Treaty is established and the initiatives to disguise it as the "state of necessity" are ruled out, Article XI should be interpreted within its own context in accordance with the general rule of Article 31.1 of the Vienna Convention.

36. Article XI should not be interpreted restrictively or broadly, but according to its own terms, in accordance with its ordinary meaning within the context in which it was drafted and considering its object and purpose.

37. As correctly noted by the tribunal in *El Paso*, pursuant to this rule "any interpretation has to begin with an examination of the *terms* of the treaty taken in the ordinary meaning. The wording of the treaty is deemed to express the intention common to the Parties, and what the Parties effectively agreed to, even though a Party might have wished otherwise on one or

[18] *Enron Corporation and Ponderosa Assets, L.P v. Argentine Republic*, ICSID Case No. ARB/01/3 (US/Argentina BIT) Award, 22 May 2007, § 331; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Award, 28 September 2007, § 373.

[19] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 359-360.

[20] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, [Aron Broches, "The Convention on the Settlement of Investment Disputes between States and Nationals of Other States", 136 Collected Courses, Hague Academy of International Law, (1972-II) p. 335 and p. 348. Emphasis added.]

another point. As long as such wishes are not expressed, the content of the treaty's provisions is paramount, and what is not there cannot be read into them...." [21]

38. Therefore, the application of Article XI of the Treaty depends on the measures adopted and implemented by Argentina being measures "necessary" for the maintenance of "public order" or for the protection of its "essential security interests". No more, no less. In this regard, let us recall that the parties' intention to provide an evolving meaning to terms of general nature, whose ability to evolve could not have been ignored by them and which are used in treaties executed for an indefinite or long period of time, should be presumed.[22]

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39. This is the sense in which the terms "public order" and "security" ought to be understood in a treaty – like the one at hand – executed for ten years and automatically renewable for an indefinite term unless one of the parties terminates it (Article XIV).

40. I believe we may share the criterion expressed in *Continental*, under which "public order" is a synonym for "public peace" which can be threatened by actual or potential insurrections, riots and violent disturbances; thus, the acts required to preserve or restore civil peace and ordinary social life, or to prevent and suppress events which might affect it – even if they are caused by serious economic and social difficulties – fall within the scope of application of Article XI of the Treaty.[23]

41. As to the concept of "essential security interests," it is undeniable that, particularly since the end of the *Cold War*, the concept has featured additional aspects other than the traditional military and defense against external threats dimension. Nowadays, we come across terms such as *economic* security, *energy* security, *ecological* security, *human* security...In *Continental*, the tribunal believes that the core of security interests includes not only political and military interests but also the economic security of States and of their population, concluding that a severe economic crisis may qualify under Article XI as affecting an "essential security interest."[24]

42. *CMS* and *LG&E* had already reached similar conclusions. In *CMS*, the tribunal noted that nothing in the object and purpose of the treaty could itself exclude economic crises from the scope of Article XI; what needed to be determined was how serious a crisis was supposed to be to qualify as an essential security interest.[25]

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[21] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 590

[22] *ICJ, Costa Rica v. Nicaragua*, *Dispute regarding navigational and related rights*, Judgment of 13 July 2009.§ 66: "... where the parties have used generic terms in a treaty, the parties necessarily having been aware that the meaning of the terms was likely to evolve over time, and where the treaty has been entered into for a very long period or is "of continuing duration," the parties must be presumed, as a general rule, to have intended those terms to have an evolving meaning."

[23] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 174.

[24] § 175, 178

[25] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 359-361.

43. In *LG&E*, the tribunal rejected the interpretation under which Article XI is only applicable to circumstances related to military action or war; concluding that a severe economic crisis does not threaten a State's essential security interest would minimize the chaos economy can create in the lives of the population and a government's capacity: "When a State's economic foundation is under siege, the severity of the problem can equal that of any military invasion."[26]

44. Likewise, in *Sempra*, the tribunal finds that nothing prevents it from interpreting that an economic emergency is included within the context of Article XI. Essential security interests may ultimately include events other than traditional military threats, which are the root of that legal concept in customary law.[27]

45. In *El Paso*, the tribunal "wishes to emphasize that a state of emergency can be of an economic nature, as stated by other ICSID tribunals in the Argentinian cases."[28]

46. Thus, there is no basis to hold that Article XI is not applicable to economic states of emergency. The threat to public order and the State's security posed by its failure to meet the basic services and needs of the population is not less serious than the threat of armed conflict or a chain of terrorist attacks.

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47. Based on the above premises, it can be easily deduced that the measures taken by Argentine authorities during the greatest economic and social crisis in its history were related, at their inception, to the maintenance of public order and the protection of essential security interests.

48. As summarized in *LG&E*, Argentina's essential security interests were threatened in December 2001. The State was faced with an extremely serious threat to its existence, its political and economic survival, the possibility to keep its basic public services running and the preservation of internal peace.[29]

49. In *Continental*, the tribunal provided a very accurate description of the crisis to conclude that it was covered by Article XI of the Treaty. The tribunal, after listing the series of political, economic and social calamities, noted that the fact that the Argentine Congress had declared a "public emergency" and enacted a specific law to face the crisis was powerful evidence of its seriousness – impossible to address through ordinary measures. The protection of essential security interests recognized by Article XI, the tribunal adds, does not require that "total collapse" of the country or that a "catastrophic situation" has already occurred or that the

[26] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, § 238, 251-253.

[27] *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Award, 28 September 2007, § 374.

[28] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 611.

[29] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, § 231-238, 257;

situation has already degenerated into one that calls for the suspension of constitutional guarantees. There is no point in having such protection if there is nothing left to protect.[30]

50. If what happened in Argentina was not a national emergency, it is hard to think of another situation that would be. It was precisely to address a situation like the one experienced by Argentina at the end of 2001 that a provision such as Article XI was stipulated.

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51. Were these measures "necessary"? As already stated – but it bears repeating – the standard to assess whether a measure is "necessary" under Article XI of the Treaty, which is a safeguard clause for such measures against the application of the other rules of the Treaty, does not have to match the standard of "state of necessity" as a state that excludes the wrongfulness of an act, pursuant to rules of general or customary international law, irrespective of the relation between such rules and Article 25 of the ILC Draft Articles.

52. Thus, by relying on the application of Article XI of the Treaty, Argentina is not supposed to prove that the measures taken were the "only way" to address a situation to which it had not substantially contributed with its own acts, as it would otherwise have to do if it relied on "state of necessity". Article XI does not contain these requirements.

53. For the *Continental* tribunal, the measures under Article XI are "necessary" when the State has no other reasonable, less restrictive and equally effective alternative to pursue the permitted regulatory objective. The tribunal is of the view that not every sacrifice can properly be imposed on a country's people in order to safeguard a policy that would ensure full respect towards the State's international financial obligations before a breach of those obligations can be considered justified as being "necessary" under Article XI of the Treaty. The standard of "reasonableness and proportionality" does not require as much.[31]

54. Moreover, while in view of the language used in Article XI it is inadmissible – as held unanimously by ICSID tribunals[32] and endorsed by the Decision (paras. 1030-1056) – to state that the Parties to the Treaty may unilaterally judge for themselves whether a measure is necessary or not to safeguard their public order or protect their essential security interests, it is only logical to expect that arbitrators, as an expression of self-control, behave prudently so as to recognize a certain margin of appreciation to States to take the measures they deem reasonable in good faith within the context in which they were adopted.

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[30] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 179-180

[31] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 227.

[32] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 359, 370, 373; *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, § 212-214; *Enron Corporation and Ponderosa Assets, L.P v. Argentine Republic*, ICSID Case No. ARB/01/3 (US/Argentina BIT) Award, 22 May 2007, § 332,337, 339; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16 (US/Argentina BIT) Award, 28 September 2007, § 374, 388; *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, §187; *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 588-610.

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55. Argentina was faced with an acute systemic crisis, "tragic and unprecedented" in the world, as described by Kenneth Rogoff, IMF Chief Economist. The recession, of an economic nature at the outset, led to a critical state of national emergency when it resulted in an institutional and social collapse without precedent in Argentine history, fueled by the absolute absence of external support, high foreign debt, depression, deflation, high unemployment rates, outrageous indigence levels and extreme poverty, social disintegration, lootings and urban violence, power vacuum, and a perspective of chaos in late 2001. The prospects were of the worst kind in 2002, with the media publishing catastrophic headlines every day.

56. Based on these premises, it is my understanding that the measures taken by Argentine authorities to address the crisis were reasonable and proportional to the crisis. They were the measures that a good family father would have taken, pursuant to the traditional standard set out in the Civil Code to assess due diligence. They were measures even more reasonable than those proposed in the alternative, despite not being the “only” measures available – a matter I believe to be insoluble considering that renowned economists have conflicting opinions about the issue which, while not substitutes for arbitrators’ legal analysis, are part of the background information of such analysis.

57. Undoubtedly, those measures were taken essentially for the sake of maintaining public order, conceived as social order, and defending Argentina’s institutional, economic and human security. Those measures required significant sacrifices from the population in general and from investors as well, both local and foreign, who could not expect to be protected in an ivory tower while the State was burning in flames. Ultimately, they were effective, because they eliminated the threats.

58. Indeed, the measures proved to be adequate means, a reasonable and effective response, to preserve the financial and economic system, escape from the chaos, pave the way for rapid economic growth and avoid hyperinflation. The measures were advantageous, not only for the people but also for local and foreign investors. The State’s authority needed to be rebuilt, the social weave, severely injured, needed to be restored, and greater damage to the business activity had to be prevented. The measures allowed for the maintenance of public order, seriously threatened, without resorting to solutions outside the scope of the Constitution; the protection of essential security interests, amidst popular discontent, without resorting to repression; and the preservation of the financial and economic system, which was heading for collapse.

59. Even in the *El Paso* award, the tribunal notes that “the measures adopted in the context of the crisis were not arbitrary but reasonable and consistent with the aim pursued. They were intended to face the extremely serious crisis that Argentina was going through and emanated from the police power regularly exercised by governments”[33] and acknowledges that “the subsequent evolution of the Argentinian economy might give some confirmation of the adequacy of the policy followed,”[34] although eventually, by majority vote, the tribunal decided

[33] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 Award, 31 October 2011, § 322.
[34] § 324.

not to grant the benefit under Article XI of the Treaty because "Argentina's failure to control several internal factors, in particular the fiscal deficit, debt accumulation and labor market rigidity, substantially contributed to the crisis," while their progressive worsening affected Argentina's ability to "respond adequately to external shocks."[35]

60. In line with this, in the case at hand, somewhere in the Decision (e.g., para. 878) the Tribunal notes that the Argentine Government tried to take the best measures to address the crisis and pointed out that whether such measures were indeed the best was difficult to assess, given the different opinions put forward by those who have analyzed the situation. The Tribunal acknowledges, based on the documents presented and the oral hearings, that the measures taken were seemingly the result of reasoned judgment, which did not prevent the Tribunal from depriving them of the benefit under Article XI of the Treaty because the majority considered that Argentina's failure to control several internal factors, in particular the fiscal deficit and debt accumulation and labor market rigidity, substantially contributed to the crisis. The progressive worsening of internal factors diminished Argentina's ability to respond adequately to external shocks (paras. 1113, 1124).

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61. The Claimants presented their case as though it were an ordinary dispute in an ordinary scenario, alien to the circumstances surrounding the situation described above and, therefore, taking the measures adopted out of context. As noted by the Respondent, which accused the Claimants of placing their claims in an inert space, the Claimants seek to present each measure separately, as if we were dealing with an abstract academic exercise instead of public policies aimed at addressing the country's problems in the face of the most dramatic situation in its history. Rebuilding the system after the convertibility regime, whose abrogation was an inevitable result of economic reality, called for the adjustment of a high number of rules and agreements that were linked to a fixed currency exchange system strongly supported by the international financial community. Thus, the measures are to be construed as a set of measures where the rearrangement of the natural gas prices needed to be understood in the context of the adjustment of all contracts in the domestic sphere.

62. If no measure had been taken after pesification, with thousands of contracts affected by it, serious damage would have been caused to both citizens and companies. In particular, it is untenable to argue that by isolating the core energy sector things might have worked out fine on their own. There lies the appropriateness of bringing Article XI of the Treaty into play to justify the authoritative intervention of public power and exclude the application of the substantive provisions of the Treaty whose operational scope is limited by the safeguard clause.

63. In *LG&E*, the tribunal noted that "[a] State may have several responses at its disposal to maintain public order or protect its essential security interests. In this sense,...Argentina's enactment of the Emergency Law was a necessary and legitimate measure on the part of the Argentine Government. Under the conditions the Government faced in December 2001, time was of the essence in crafting a response. Drafted in just six days, the Emergency Law took the swift, unilateral action against the economic crisis that was necessary at the time...; the

[35] § 656, 665.

provisions of the Emergency Law that abrogated calculation of the tariffs in U.S. dollars and PPI adjustments, as well as freezing tariffs, were necessary measures to deal with the extremely serious economic crisis."[36]

64. Likewise, in *Continental,* after analyzing the alternative measures available when the challenged measures were taken, the tribunal concludes that devaluating the peso and pesifying contracts was "inevitable" in the situation Argentina was facing in view of the unsustainability of the parity with the U.S. Dollar and in order to achieve a balanced distribution of the costs deriving from devaluation and the abandonment of convertibility once the fiction of the peso-dollar peg had been proved wrong by markets. The measures were sufficient to face the crisis and were reasonably and proportionally applied.[37]

65. In sum, based on the evidence available, Argentina's conduct generally met the requirements under Article XI to safeguard its hypothetical inconsistency with Argentina's substantial obligations.

66. The Tribunal, however, considers that the application of Article XI depends on verifying first that the State has not substantially contributed to the state of emergency that required the adoption of measures under Article XI. The Tribunal reaches this decision following *El Paso,* by way of interpretation, on the basis of Article 25.2(b) of the ILC Draft Articles which governs the "state of necessity", a concept that, as I have tried to prove, is quite different. Based on that interpretation, the Tribunal concluded that Article XI is not applicable because, in its opinion, Argentina substantially contributed to the crisis that it later attempted to mitigate with the challenged measures.

67. This requirement is not expressly nor impliedly set out in Article XI, nor can it be inferred from the general rule of interpretation embodied in Article 31 of the Vienna Convention, which has already been discussed. I must add that, even if I agreed with the Tribunal's premise – which I do not, – I would still be in disagreement with the Tribunal's conclusion. As will be noted further below, I believe Argentina's behavior was not a substantial cause for the systemic crisis that broke out in early 2001.

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68. Now, *temporary* restrictions are inherent in Article XI of the Treaty. The tribunals that have upheld the application of Article XI to Argentina's situation addressed by the Emergency Law share this view: "This exception is appropriate only in emergency situations; and once the situation has been overcome, i.e. certain degree of stability has been recovered, the State is no longer exempted from responsibility for any violation of its obligations under the international law and shall reassume them immediately."[38]

69. *LG&E*'s tribunal was more analytical when considering these restrictions. In the judgment of the tribunal, "from 1 December 2011 until 26 April 2003, Argentina was in a period of crisis during which it was necessary to enact measures to maintain public order and

[36] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 Decision on Liability, 3 October 2006, § 239-242.
[37] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 200, 206-214, 223-233.
[38] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 Decision on Liability, 3 October 2006, § 261.

protect its essential security interests."[39] These dates coincide, "on the one hand, with the… measure freezing funds, which prohibited bank account owners from withdrawing more than one thousand pesos monthly and, on the other hand, with the election of President Kirchner," and were chosen in view of the "notorious events that occurred."[40]

70. According to the *LG&E* tribunal, the outbreak of the crisis is to be set on December 1, 2001, a month before the enactment of the Emergency Law, because the state of emergency had already begun when the Law was approved (January 6, 2002), as successively extended.[41] The tribunal draws a distinction between "factual emergency," which would allow for Article XI of the Treaty to cover the measures taken until April 26, 2003, and "legislative emergency," which it attempts to discard in order to avoid the logical consequence that might imply the coverage of the measures taken during the Law operation, which is still in place.[42] The tribunal rightly notes that emergency periods should be "strictly exceptional and should be applied exclusively when faced with extraordinary circumstances."[43]

71. A rationale like the one in *LG&E* could be and is indeed shared by the Tribunal in the case at hand (para. 1128), although certain flexibility should be applied when defining the end of the state of emergency because it is too simple to set a fixed date to put an end to a period of *factual* emergency. Thus, in *Continental*, the tribunal denied Argentina the benefit of Article XI with respect to the measures taken in early 2003; conversely, the tribunal in *CMS* held that the crisis period ended somewhere between late 2004 and early 2005, arguing that while the crisis had not been completely overcome, particularly in the social sector, its repercussions were not as intense and widespread, and the Argentine economy had substantially improved.[44]

72. If this flexibility were applied, it would be correct to suggest that the state of emergency ended *throughout 2004*.

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73. However, Argentina urges the Tribunal to analyze whether the emergency measures were necessary to prevent a return to the crisis. Argentina argues that the duty to fulfill treaty obligations does not imply restoring the system in force before the crisis but to comply with treatment standards in the new context, which requires analyzing the new factual circumstances. The consequences of worsening living conditions, in particular for low-income citizens – cast into poverty and indigence – is a feature of the new social reality, claims the Respondent. Argentina is today the "country of the new poor" and poverty and indigence levels determine public policy. The country, Respondent adds, is faced with the challenge of social reconstruction in a polarized society, with significant sectors off the market both in terms of asset acquisition and education. Suggesting that the crisis ended somewhere between late 2002 and mid 2003 on the basis of references to economic recovery is wrong from a conceptual viewpoint. When a country hits the bottom, the crisis is not over. Argentina

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[39] See § 226.
[40] See § 230.
[41] In 2009, Law 26,563 extended the state of emergency for two additional years, until the end of 2011.
[42] See § 227-228.
[43] See § 228.
[44] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 249-250.

has still to recover the lost growth, it has not left the state of emergency behind. Reversing the measures taken, Respondent concludes, would bring back the threats of a crisis.

74. This argument, however, goes beyond the boundaries of Article XI, which was conceived to address specific situations within the framework of an agreed model of investment and investor treatment intended to be restored in all its terms and consequences once the circumstances that threatened the maintenance of public order or essential security interests are overcome.

75. In reality, taking into account the years that have gone by, what Argentina is saying is that the application of the treaty's neoliberal model is a permanent threat to Argentina's public order and security, which makes permanent the measures taken on the basis of emergency.[45] This, however, is alien to Article XI and part of another analysis, namely, the scope of the State's regulatory power to satisfy public interest and meet the commitments assumed towards the investments and investors protected under the Treaty. It is one thing to *suspend* the model for a while and a very different one to *abandon* it altogether when public interest is not deemed served by such model. If that were the case, what would be pertinent is the renegotiation of the treaty or its termination.

II. Fair and Equitable Treatment

76. Undoubtedly, there is tension between the State's regulatory power and the stability of the regulatory framework promised to the investor, which is considered an essential element of legitimate expectations. Fair and equitable treatment of the investor and investments requires that these expectations be respected. This tension significantly increases when the State has to face serious economic and social crises, systemic crises.

77. In *El Paso* award, the tribunal rightly noted that while "FET is linked to the objective reasonable legitimate expectations of the investors," these expectations "have to be evaluated considering all circumstances."[46] The standard entails "reasonableness and proportionality."[47] Following this criterion, "[t]here can be no legitimate expectation for anyone that the legal framework will remain unchanged in the face of an extremely severe economic crisis."[48] The *El Paso* tribunal notes that "... the measures adopted in the context of the crisis were not arbitrary but reasonable and consistent with the aim pursued. They were intended to face the extremely serious crisis that Argentina was going through and emanated from the police power regularly exercised by governments."[49]

[45] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 107.
[46] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 (US/Argentina BIT), Award, 31 October 2011, § 364.
[47] § 373.
[48] § 374.
[49] § 322.

78. Even tribunals mostly inclined to set limits to the State's regulatory power and expand investor's expectations recognize that upon a crisis, it is unthinkable for such crisis not to have consequences or for businesses to carry on as if nothing happened.[50]

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79. Tension increases even more when the investor, as in the case at hand, relies on the fact that the State assumed a particular and specific commitment of regulatory stability under the *umbrella clause* embodied in Article II.2(c) of the Treaty, pursuant to which: "Each Party shall observe any obligation it may have entered into with regard to investments."

80. First, it is necessary to fully understand what *umbrella clause* means.[51] While this general provision could be perfectly interpreted as a redundancy of *pacta sunt servanda*, it has generally been construed as transforming certain contract obligations assumed by the host State *vis-à-vis* the investor into *treaty* obligations and, therefore, such clause submits their enforceability to the dispute resolution mechanisms provided for in the treaty, avoiding the jurisdiction of the State's courts and/or other mechanisms agreed under contract.

81. In any case, applying the *umbrella clause* gives rise to two problems. The first problem lies in defining the boundaries between the contract obligations covered by the clause and those that are left out. In my opinion, there must be express stability commitments directly assumed by the host State *vis-à-vis* the investor in order for a contract obligation to be protected under the *umbrella clause*.

82. The second problem relates to the treatment that should be accorded to a contract obligation that is to be handled as a *treaty* obligation. It has been argued that one of the purposes of the *umbrella clause* was to prevent the State from depriving investors from their contract rights – considered by them as acquired rights – through a legislative or regulatory change of the applicable legal framework. If this were so, simply verifying the breach of contract obligations would be enough to hold that the treaty has been violated.

83. In my opinion, this point of view is inadmissible because it fully ignores the State's regulatory power, which is an attribute inherent in sovereignty whose exercise should be rooted in public interest and be judged under the circumstances. Therefore, if treaty coverage is extended to certain contract obligations, what follows is examining such obligations in light of the treatment standards agreed upon. No more, no less.[52]

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[50] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005, § 356; *Sempra Energy International v. The Argentine Republic*, ICSID Case No. ARB/02/16(US/Argentina BIT) Award, 28 September 2007, § 269, 346-347.

[51] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Argentine Republic's Application for Annulment, 8 September 2005, § 89-100; *Pan American Energy LLC and BP Argentina Exploration Company v. Argentina,* ICSID Case No. ARB/03/13 (US/Argentina BIT) *BP America Production Company, Pan American Sur S.R.L., Pan American Fueguina, S.R.L. and Pan American Continental, S.R.L. v. Argentina*, ICSID Case No. ARB/04/8, Decision on Preliminary Objections, 27 July 2006, § 96-116; *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 296-301.

[52] *Pan American Energy LLC and BP Argentina Exploration Company v. Argentina,* ICSID Case No. ARB/03/13 (US/Argentina BIT) *BP America Production Company, Pan American Sur S.R.L., Pan American*

84. This is the position the Tribunal in this case seems to uphold when it concludes (paras. 1013, 1132(b)) that Argentina has violated the *umbrella clause* embodied in Article II.2(c) of the Treaty "to the extent the obligations pertinent to the investment to which Argentina has specifically entered into with the Claimants have been breached and *have resulted in the violation of the standards of protection under the BIT*" (emphasis added). Of course, this is also my view.

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85. Now, under the circumstances, have investors been treated unfairly, inequitably, discriminatorily or arbitrarily? Or have they been deprived of their assets or defenses? The Tribunal understands and concludes that Argentina has breached the fair and equitable treatment standard (paras. 969-987 and 1132(b), in particular). I reach the same conclusion but following a different path.

86. Analyzing the impact of the *Emergency Law* (No. 25,561) and Decree No. 214/02 on pesification of the economy and the abrogation of the Convertibility Law, as well as the subsequent provisions on foreign investment treatment as of that date, implies considering from the outset whether, under the circumstances, the legislative change – *i.e.*, the loss of the legal stability Claimants claim to be an acquired right – breached the "fair and equitable treatment" standard under the Treaty.

87. In the *El Paso* award, the tribunal found the State may not unreasonably change the legal framework in violation of a very specific commitment not to do so, even if faced with an extremely serious economic crisis.[53] If it did, it could be said that the exercise of the State's regulatory power in disregard of a particular and specific obligation to keep the investment's legal framework in force is not consistent with the treatment standards under the Treaty, which are applicable when the tribunal concludes there is no state of emergency. The State has to be liable for its mistakes, notwithstanding the fact that all circumstances must be taken into account when assessing the standards agreed on and the consequences of their breach.

88. The way I see it, even if Article XI of the Treaty were set aside, the loss of legal stability Claimants consider to be an acquired right would not breach the "fair and equitable treatment" standard under Article II.2(a) of the Treaty if the significance of public interest in a state of emergency like the one experienced by Argentina and the role that State institutions are to play faced with such contingency are weighted, which would be required to exercise its undeniable regulatory power to its fullest.

89. It would have been irresponsible in that case not to take the measures challenged by the Claimants. They resemble travelers who are victims of a sunken ship and, when offered a seat in a lifeboat, waive their tickets claiming to be brought to shore in first class. It was fair and equitable for investors to share the burden imposed to others, whose dreams, expectations, hopes and also savings were vanished. There was no discrimination against them or

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Fueguina, S.R.L. and Pan American Continental, S.R.L. v. Argentina, ICSID Case No. ARB/04/8, Decision on Preliminary Objections, 27 July 2006, § 112; *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, § 124.

[53] *El Paso Energy International Company v. The Argentine Republic*, ICSID Case No. ARB/03/15 (US/Argentina BIT), Award, 31 October 2011, § 364, 374.

arbitrariness; simply, the same yardstick was used, the general rule. The Claimants, as the rest of the investors, were treated as mere mortals, not better or worse, under the circumstances – bad for all, disastrous for some (not the Claimants).

90. In response to those who take the requirements for the application of Article XI to their fullest, turning such provision into an *avant la lettre* clone of “state of necessity”, it could be suggested that, conversely, Article XI was conceived to eliminate any doubt regarding the consistency between the “fair and equitable treatment” standard and the measures adopted in a state of emergency and applied in violation of specific legal stability commitments. It could be argued that one of the reasons why host States have accepted standards as flexible as these concerning the treatment received by investors has been the incorporation of safeguard clauses like the one embodied in Article XI of the Treaty.

91. The pesification of the economy and the repeal of the Convertibility Law had a strong impact on the dollarized economy. Contract obligations agreed in USD were converted into pesos at par and adjustment clauses as well as clauses that provided for dollar or other foreign currency indexation, or which were based on price indexes of foreign countries, were abandoned. The Argentine peso soon reached an exchange rate of 4 - 1 as against the dollar when the Government allowed it to float freely (Decree No. 260/02). Contracts had to be adjusted to the new circumstances through renegotiation by the parties, which were invited to equally share the effects of the change, following the principle of shared sacrifice, or through court order when agreement was impossible (Decree No. 214/02, Article 8). Insofar as the Administration prevented gas distributors and energy generators from passing the increases in prices requested by producers through to tariffs, the renegotiation was unsuccessful and, therefore, a *de facto* freeze of natural gas prices followed in the domestic market, where the value of the peso had dropped to 0.28 USD in May 2002 and producers were not allowed to cancel their contracts.

92. There is no doubt this is not what the Claimants had expected when they invested in natural gas production. They claim the State interfered with price setting after pesifying the contracts and forbidding natural gas distributors and energy generators to pass through to consumers the cost overruns represented by the prices agreed with gas producers upon renegotiating the contracts with no strings attached. According to the Claimants – which hold themselves out as beneficiaries of specific commitments and guarantees made by the Argentine Government, – their situation was substantially different from that of the rest of the Argentine economy.

93. In my view, such a statement is unacceptable in the context of a crisis like the one Argentina went through. Even if we were to admit that the Argentine Government allegedly committed to providing a stable legal framework to investors as of the date of the investment, the dramatic change in circumstances from the last decade of the 20th century to the early 21st century gave rise to a situation from which such commitment could not escape and corrected the assessment of the “fair and equitable treatment” standard that would have otherwise covered the Claimant’s requests.

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94. Should we conclude, then, that the measures taken by Argentina stood up to and were consistent with the standards under the Treaty and, in particular, with the “fair and equitable treatment” standard embodied in Article II.2(a)?

95. Once again, the problem lies in setting the time periods within which to frame this interpretation of the standard. The criterion needs to be the one applied to the measures taken in a state of emergency invoking Article XI of the Treaty. If we understand that the "factual emergency," in the terms of the *LG&E* award, ended in late April 2003 or later, after the one-hundred-day grace period that is usually given to the administration (in this case, President Kirchner) after inauguration, the measures taken or extended afterwards could not benefit from the interpretation explained above. Any breach of a legal stability clause set out in contracts or licenses executed with the Claimants could not hide behind the State’s exercise of its regulatory power.

96. I have already stated, applying a flexible criterion, that the state of emergency ended “throughout 2004,” which would make me lean towards rescuing the First Gas Agreement signed on April 2, 2004 by the Argentine Government with the largest natural gas producers to ensure market supply, thus setting a price schedule that was supposed to provide a reasonable return on their investment and promising convergence to complete market deregulation when the Agreement came to an end (December 2006).

97. It is, however, an established fact that the promises contained in the First Gas Agreement were not met, which leads me to the conclusion that the adjustment and renegotiation process concerning natural gas production and supply contracts carried out from 2004 – upon violating the commitments undertaken by Argentina *vis-à-vis* the Claimants to ensure them a free market, free disposition of production, price deregulation, royalties and fiscal stability – breached the standard of “fair and equitable treatment” to which the Claimants were entitled under the Treaty.

98. Notwithstanding the above, other gas producers entered into agreements with the Government to ensure supply in exchange of guarantees of reasonable returns to producers through prices. This issue will need to be considered, of course, when determining the quantum of damages. Argentina has argued that, as a result of the agreements and programs sponsored by the Argentine Government, the wellhead price of natural gas recorded increases higher than transportation and distribution tariffs and, for most of demand, above the level prior to 2002 – exceeding, in some cases, the long-term contract projections signed in the 1990s. Thus, Argentina argues, the prices collected by the Claimants do not significantly differ from their projections, aside from the fact that the peso devaluation reduced their production costs in dollar terms.

99. That being said, there is no doubt there was a change from free prices to regulated prices and that the latter would remain in force irrespective of the exceptional circumstances that had justified such change, thus completely destroying the previous regulatory framework and breaching the specific obligations undertaken *vis-à-vis* the Claimants.[54] Even in times of

[54] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, § 139: "The Tribunal […] recognizes the economic hardships that occurred during this period, and certain political and social realities that at the time may have influenced the Government’s

"economic emergency," the Argentine Supreme Court does not validate legislation that overrides legally acquired rights on a permanent basis.

III. The State of Necessity

100. I have serious doubts about the appropriateness of giving a role to the "state of necessity" in an investment dispute between a host State and an investor, especially when it is framed within a treaty that includes a safeguard clause such as that embodied in Article XI of the U.S.-Argentina Treaty.

101. Is the "state of necessity" a defense that can operate in investor-State arbitration? This is no longer – or not only – about the practical consequence that, since the requirements of the safeguard clause (Article XI) are less stringent than those of the "state of necessity" under customary international law, an arbitrator who is not willing to apply the safeguard clause would be even less willing to ground a decision on the "state of necessity".

102. This is about being very clear –something which is often confusing (as it is in the Decision, paras. 1028, 1062, 1063, 1066) – that the ultimate non-enforcement of the Treaty's substantive provisions in view that the safeguard clause (Article XI) is applicable in a particular case, does not eliminate the host State's hypothetical international responsibility for acts that can be challenged by the investor's State, either because such State believes its rights have been overridden or when it exercises diplomatic protection of its nationals, provided the requirements for such mechanism are met.

103. It is in this context that the host State could invoke the "state of necessity" to exclude the wrongfulness of its behavior, leaving the door open – in any case – for the reparation of any damage or injury caused. The operation of Article XI of the Treaty does nothing but safeguard the application of the measures necessary to maintain public order and the State's essential security interests *vis-à-vis* treaty obligations while the state of emergency is in force, but does not affect – in any case – the assessment of its lawfulness under rules of customary international law or other obligations undertaken in other treaties or any other source of obligations recognized by international law.

104. Be that as it may, analyzing the "state of necessity" defense at least briefly is – as already stated – mandatory because it was relied on by the Respondent and extensively discussed during the proceedings, where markedly different viewpoints were put forward and the Tribunal – after ruling out the application of Article XI – reached the conclusion that the measures taken by Argentina breached the "fair and equitable treatment" standard of investments and investors under Article II.2(a) of the Treaty.

105. It has to be presumed that if the factual situation does not meet the requirements for the application of Article XI of the Treaty, it will be harder for it to do so for the "state of necessity", which is a more stringent standard. The Parties agree on the exceptional nature of this defense, subject to strict and rigorous requirements. International case law, such as that

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response...But…Argentina went too far by completely dismantling the very legal framework constructed to attract investors."

of the International Court of Justice[55] or ICSID tribunals,[56] confirms this view. Conversely, it could be argued that if these requirements were met in the case at hand, they would meet the requirements under Article XI more easily,[57] a conclusion that would also please those who claim that this safeguard clause is to be construed on the basis of the "state of necessity" as an interpretative rule.

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106. The first condition is that the party relying on the "state of necessity" has not contributed to the state of emergency. This contribution, as specified by the ILC in its commentary to Article 25 of its Draft Articles, must be *substantial.* However, as noted by the Annulment Committee in the *Enron* decision*,* it is worth wondering if the *substantial* nature of that contribution calls for evidence that the State has deliberately attempted to create the situation to escape a claim for wrongful behavior or if a lower or higher degree of recklessness or negligence when making its decisions would be enough.[58]

107. In the case at hand, as already stated, the Tribunal incorporated this condition to Article XI of the Treaty by way of interpretation. My disagreement with this decision, which destroys the very own significance of such provision as a safeguard clause, has already been noted. However, even if – hypothetically – I had accepted the premise set by the Tribunal, my conclusion would still have been the opposite because, in my view, the measures taken by the Respondent were not the substantial cause of the systemic crisis the Respondent attempted to address.

108. According to the Claimants, who follow to the letter the opinions put forward by Professor Edwards in his written reports and oral deposition before the Tribunal, it was Argentina's wrong policies, and not external shocks, the cause for the crisis that broke out in late 2001. The Claimants argue that Argentine authorities never had the will to implement the reforms they knew were indispensable to avoid that situation.

109. Irrespective of the reply by the Respondent to the opinions of Professor Edwards, and the value they might have to ground a legal decision,[59] our case involves a number of factors, both internal and external (reversal of capital flows, decrease in exports, lower prices for exports, the strong depreciation of the Brazilian currency – Argentina's largest trading partner and competitor, – appreciation of the USD, increase in interest rates of the Federal Reserve, implementation of an economic contraction policy in a recessive phase of the Argentine

[55] CIJ, *Gabcikovo-Nagymaros,*

[56] *CMS Gas Transmission Company v. The Argentine Republic*, ICSID Case No. ARB/01/8 (US/Argentina BIT) Award, 12 May 2005*,* § 317; *Enron Corporation and Ponderosa Assets, L.P v. Argentine Republic*, ICSID Case No. ARB/01/3 (US/Argentina BIT) Award, 22 May 2007, § 304.

[57] *LG&E v. Argentina,* ICSID Case No. ARB/02/1, Decision on Liability, 3 October 2006, § 245, 258.

[58] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* 12 ICSID Case No. ARB/01/3 (United States/Argentina BIT) Decision on the Application for Annulment of the Argentine Republic, 30 July 2010, § 387-389.

[59] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* 12 ICSID Case No. ARB/01/3 (United States/Argentina BIT) Decision on the Application for Annulment of the Argentine Republic, 30 July 2010, § 392-393.

economy, with which Argentina itself had little or nothing to do,...) which, together, led to the outbreak of the crisis.

110. Professor Roubini, at odds with Edwards, noted that “minimizing the importance of such external shocks and their association with collapses of many currency pegs, including Argentina, is inconsistent with the facts." According to Roubini, these “large, severe and persistent" factors were an essential element of the outbreak of the crisis; no other emerging country in similar circumstances has been faced with them in equal magnitude, succession, and pace. In my opinion, it cannot be argued that Argentina’s contribution to the crisis was *substantial* so as to prevail over external shocks.

111. Moreover, Argentina did try to implement the recommendations of international organizations; in fact, Argentine governments implemented major changes in economic policy following such recommendations, such as relaxing the labor market and opening to foreign trade so much so, as stated by Roubini, that Argentina became the “poster country” of the Washington Consensus. The IMF Managing Director presented Argentina as an example to follow: “Argentina has a story to tell the world….” The increase in disbursements to repay the debt was the main cause for fiscal deficit; the long-term cost of capital refinancing has more to do with the capital market than elements under the Argentine Government’s control. Fiscal deficit is not a synonym with economic collapse and *default* on debt: developed countries have fiscal deficits much higher than Argentina’s deficit during the entire crisis. With or without fiscal problems, there would have been a crisis.

112. As concluded by the tribunal in *LG&E*: “There is no serious evidence in the record that Argentina contributed to the crisis resulting in the state of necessity. In these circumstances, an economic recovery package was the only means to respond to the crisis. Although there may have been a number of ways to draft the economic recovery plan, the evidence before the Tribunal demonstrates that an across-the-board response was necessary, and the tariffs on public utilities had to be addressed.”[60]

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113. The second condition that, under Article 25 of the ILC Draft Articles, must be fulfilled for the “state of necessity” to operate is that the measures adopted be the “only way” to safeguard the State’s essential interests from the grave danger of social dissolution and political anarchy. If we were to follow the criterion adopted by the Annulment Committee in *Enron*, this defense will be excluded only if there is a feasible and effective alternative that does not entail a violation of international law or a less serious breach of such law.

114. However, who gets to decide if there is any such alternative? The tribunal when it renders the award, having the benefit of knowledge and experience that were not available to the Government when it had to take the measures? The tribunal, applying the reasonableness standard of a “good family father” adequately qualified, on the basis of the information available as of the date on which the decision was made? Or else – as equally reasonable people may argue – should the State have a *margin of appreciation*? The Annulment

[60] *LG&E v. Argentina,* ICSID Case No. ARB/02/1 (United States/Argentina BIT) Decision on Liability, 3 October 2006, par. 257.

Committee in *Enron* was faced with these same questions, considering that the tribunal that had rendered the award had failed to consider a number of essential matters to assess whether the "only-way" requirement had been met and, if it had considered them, had been unable to explain the reasons that led the tribunal to its decision.[61]

115. Arbitration case law supports recognizing that a host State has a margin of appreciation. In *Continental*, the tribunal held that "a time of grave crisis is not the time for nice judgments, particularly when examined by others with the disadvantage of hindsight."[62]

116. The Respondent noted that before taking the challenged measures it tried to overcome the situation with other measures that proved to be insufficient. De la Rúa's Administration did everything in an attempt to maintain the effectiveness of the Convertibility Law (Law No. 23,928), including public expenditure reduction programs (a 13-% reduction in state worker's salaries and pensions) and tax increases, with the support of the IMF (rescue plan in 2000 of forty billion USD from international Organizations and foreign States.) In March 2001, the Argentine Government implemented new measures: 1) a debt swap (*megaswap*) for approximately 30 billion USD to improve maturities; 2) the modification of the exchange rate parity by adding the Euro to the USD as the basis for conversion; 3) a program to adjust public expenditure to real earnings (zero deficit).

117. However, these measures fueled mistrust rather than trust by markets and citizens and massive bank deposit withdrawals followed (25% in 2001) as well as capital flight, a dramatic reduction in reserves (40% in 2001), the IMF suspension of disbursements of agreed loans (1.6 billion USD for the last quarter of 2001,) and fear of default on Argentina's sovereign debt. Therefore, on December 3, 2001 (Decree No. 1570), the Government was forced to freeze bank deposits – which, in practice, translated into the abandonment of the convertibility system – until the restructuring of the foreign debt was completed. On January 6, 2002, Emergency Law No. 25,561 was enacted as the only possible and effective response to the crisis.

118. Even before the state of emergency was declared, renowned economists (Krugman, Musso, Frenkel & Danill) had warned that pesification was the "only way" to overcome the crisis. The Central Bank reserves would have been insufficient to meet demand. Dollarization would have not avoided the collapse of the banking system. If contracts had not been adjusted, social tensions impossible to handle would have unleashed. The *LG&E* tribunal, after specifically describing the state of emergency in Argentina, concluded that the Emergency Law was the kind of swift unilateral action against the crisis necessary at the time. This view was shared by the *Continental* tribunal.

119. It is always possible to resort to a "*but-for*" line of reasoning to argue that other measures could have been taken. It is not possible, however, to prove that alternative

[61] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* 12 ICSID Case No. ARB/01/3 (United States/Argentina BIT) *D*ecision on the Application for Annulment of the Argentine Republic, 30 July 2010, § 367-378.

[62] *Continental Casualty Company v. Argentina*, ICSID Case No. ARB/03/9 (US/Argentina BIT) Award, 5 September 2008, § 181

measures would have proven more effective. Conversely, it can be argued that the measures actually implemented substantially contributed to avoiding that the worst catastrophic outcome of the crisis became true.

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120. With regard to the other requirements listed in Article 25 of the ILC Draft Articles, the third requirement – *i.e.*, that an essential interest of another State or of the international community as a whole be not impaired – is completely alien to the case submitted to this Tribunal.

121. The fourth requirement, equal treatment, is fully met. I hereby incorporate by way of reference the considerations on discrimination and arbitrariness included in the Decision (paras. 865-893).

122. The fifth and last requirement is that the treaty does not prohibit reliance on the "state of necessity". According to the Claimants, both the object and purpose of the U.S. - Argentina Treaty, as well as its specific provisions, would imply such prohibition. In their opinion, such Treaty was mainly executed to protect investors during harsh times, so interpreting that the Treaty would allow Argentina to rely on the "state of necessity" defense would be totally inconsistent with the primary object and purpose of its execution, even more so in light of the background of Argentine history. However, the consequences the Claimants intend to draw from the object and purpose of the Treaty are exaggerated. The Treaty's object and purpose are, as already noted, something more than simply protecting investments.

C. Measures Concerning Export Restrictions, Export Withholdings and Royalties

123. As far as the measures on export restrictions and the re-routing of a specified amount of gas to the domestic market are concerned – as well as those on export withholdings and royalties, – it is worth noting first that the Respondent itself seems to hesitate when referring to the appropriateness of relying on Article XI of the Treaty to justify such measures. On the first pages of its Rejoinder, the Respondent focuses the application of Article XI on the measures concerning contract pesification, while relying on the tribunal's lack of jurisdiction for the remainder measures, on the *fork-in-the-road* provision for export restrictions and gas re-routing to the domestic market, and the tax-matter exception provided for in Article XII.2 of the Treaty for export withholdings. It is only later that the Respondent goes back to Article XI looking for shelter with respect to all these measures and argues that the 2004 energy crisis created a situation that could have affected "public order".

124. The natural gas shortage in Argentina in 2004 is a proven fact. The Parties have submitted conflicting opinions on its cause. In any case, I believe this "crisis" is independent from the systemic crisis that broke out in the austral summer of 2001-2002 and, therefore, it should be assessed by its own merits and not as a corollary of the latter. In January 2002, export contracts were not affected by pesification. In fact, the export of natural gas made available a large amount of foreign currency to producers. Article XI of the Treaty or the interpretation we have proposed on the fair and equitable standard in the above paragraphs

may not cover for the measures taken to ensure domestic supply to the detriment of producers' export and fiscal stability rights previously recognized by the State. Undoubtedly, natural gas domestic supply is a primary and fundamental objective in any country, as well as collecting taxes, rates and duties to meet public service needs, including energy supply. However, these circumstances are completely foreseeable and need to be considered in any cautious and prudent law.

125. In fact, with regard to export permits, the legislation in force before the challenged measures were implemented provided over and over again that domestic market needs had to be met. These legal guarantees go against Argentina's argument, not for it. Export permits were granted after assessing domestic supply needs. Setting the provisions concerning excess gas exports aside, export authorizations were given as firm and final permits whose suspension or cancellation was only possible under the circumstances provided by law. Thus, Argentina should have demonstrated that producers holding export rights over certain natural gas volumes had breached their legal obligations. From this perspective, I understand that the measures taken were not – are not – *necessary* pursuant to a reasonable interpretation of Articles XI and II.2 (a) of the Treaty.

126. As far as the export withholdings and the calculation basis for the payment or royalties are concerned, the challenged measures were protected by the Emergency Law, but they were applied only after the Government decided to restrict exports and force the re-routing of certain natural gas volumes to the domestic market. Therefore, the appropriateness of Article XI of the Treaty needs to be considered only from the 2004 energy crisis viewpoint, which leads to the same conclusion reached on these measures. Argentina has breached the fiscal stability commitment assumed *vis-à-vis* the Claimants, covered by the *umbrella clause*, which is inconsistent with the fair and equitable treatment standard. A different issue is establishing the consequences with respect to damage and injury caused, which will be considered when determining the amount of reparation.

Professor Antonio Remiro Brotóns
Arbitrator
Date: March, 27, 2013