RESPONDENT'S COMMENTS ON THE ISSUE OF "INVESTMENT" WITHIN THE MEANING OF ARTICLE 25(1) OF THE ICSID CONVENTION

A. INTRODUCTION

1. The Secretary of the Tribunal, *vide* letter dated 14 March 2007 and on behalf of the Sole Arbitrator, had invited both the Claimant and the Respondent to provide any further written comments on the issue of "investment" within the meaning of Article 25(1) of the ICSID Convention as addressed by the Tribunal in **PSEG Global Inc. and Konya Ilgin Elektrik Uretim ve Ticaret Limited Sirketi v. Republic of Turkey** ("*Turkey case*").

B. COMMENTS

2. At the outset, it is noted that the Tribunal in the *Turkey case* decided that the dispute submitted by PSEG and Konya Ilgin Ltd. was within the jurisdiction of the Centre and competence of the Tribunal.

3. The Respondent's comments on the *Turkey case* will be directed to the issue of "investment" within the meaning of Article 25(1) of the ICSID Convention, namely:

(a) The existence of an "investment"; and

(b) Legal dispute arising directly out of an investment.

I. THE EXISTENCE OF AN "INVESTMENT"

(i) Definition of "investment"

4. As has been argued by the Respondent before[1], the ICSID Convention has deliberately omitted the definition of investment and left this definition for the interpretation of the parties[2]. In the *Turkey case*, the definition of "investment" is provided in **Article I(1)(c)** of the *Treaty between the United States of America and the Government of the Republic of Turkey Concerning the Reciprocal Encouragement and Protection of Investments* ("Treaty"). In our case, the definition of "investment" is provided in **Article 1(1)(a) and (b)** of the *Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Malaysia for the Promotion and Protection of Investments*[3] ("IGA"). Article 1(1)(b)(ii) of the IGA expressly provides that "investment" shall refer, "**in respect of investments in the territory of Malaysia, to all investments made in projects classified by the appropriate Ministry of Malaysia in accordance with its legislation and administrative practice as an "approved project"**".

5. It is submitted that these two definitions differ in respect of two important elements, namely, -

(a) In the Treaty, the definition includes service contracts, which is absent in the IGA; and

(b) The classification of an "approved project" for an investment as provided in the IGA is not present in the Treaty.

[1] See **paragraphs 3 and 4** of the Respondent's Comments dated 13 December 2006
[2] See **paragraph 74** of the Award
[3] See **Annex No. 38, Volume I** of the Respondent's Bundle of Documents filed in support of the Memorial on Objections to Jurisdiction (**RBD**)

6. In respect of paragraph 5(a) above, the inclusion of "service contract" in the definition of "investment" under Article I(1)(c) of the Treaty shows that the United States of America and the Government of the Republic of Turkey clearly intended that service contracts shall be regarded as investments eligible for protection under the Treaty. In contrast, the absence of any reference to "service contracts" in the IGA is a clear indication that the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Malaysia did not intend to include such contracts within the purview of the IGA. Therefore, it is submitted that on this point alone, the findings made in *the Turkey case* that the Tribunal has jurisdiction and competence to hear the dispute is distinguishable from the present case.

(ii) <u>Intention of the parties reflected in the contracts</u>

7. In the *Turkey case*, one of the Respondent's terms of the objection on the ground that there was no investment was that the project was still being negotiated and no consensus had ever been reached on those terms. The Tribunal ruled otherwise as the Turkish Council of State ("Danistay") had approved the Concession Contract. The language of the Contract and the circumstances demonstrated an intent by the parties to be bound although certain terms need to be agreed upon by the parties at a later stage. The Tribunal found that the Concession Contract was in existence, valid and binding in nature. As a result, the contract between the Claimants and the Respondent satisfied the requirement of "investment" as provided under Article I(1)(c) of the Treaty, thus prompting the Tribunal to hold that its jurisdiction is affirmed on this issue[4].

8. However, in our case, the Respondent has never disputed the existence of the Salvage Contract. What is being contended by the Respondent instead is

[4] See **paragraph 90** of the Award

that the Salvage Contract is a mere service contract which does not fall within the meaning of "investment" in Article 1(1) of the IGA.

9. A clear distinction can also be drawn from the facts of the *Turkey case* in light of the peculiarity of the facts, particularly in relation to the intention of the parties whilst negotiating and signing the Concession Contract. In paragraph 96 of the Award, the Tribunal stated, "*[t]here are, however, other documents which the Tribunal believes are particularly important in establishing the intent of the parties to conclude and be bound by the Contract. The most fundamental of these is evidently the Contract itself. There are many provisions in the Contract which evidence the intent of the parties to be bound.*"[5] Thus, in reaching its decision, the Tribunal in the *Turkey case* placed much emphasis on the intention of the parties in the conclusion of the contract (which in turn satisfied the requirements in Article I(1)(c) of the Treaty). In our case however, the Respondent submits that in the course of negotiations of the Salvage Contract, it was never contemplated nor intended by the parties that the Salvage Contract was to be treated as an investment within the meaning of the IGA. In other words, as has been submitted before[6], the negotiations of the Salvage Contract have shown that, from the very beginning, the parties intended to conclude merely a contract for service.

10. Furthermore, there is nothing in the Salvage Contract which expressly requires the Claimant to specifically invest in Malaysia, provide financing and/or undertake any other connected investments, unlike in the *Turkey case*. The Claimant in the present case might have expended its resources in terms of financial, personnel and equipment but that exercise does not necessarily convert it into an investment. In the *Turkey case*, the Claimants would have to make an investment as the very nature of the agreement is for the investor to undertake power generation activities specified therein. The Concession Contract

[5] See also **paragraph 103** of the Award
[6] See **paragraphs 22 to 28** of the Respondent's Comments dated 13 December 2006

refers specifically to investments, its amount, financing, period of implementation and a host of other investment-connected questions[7].

11. Hence, the Claimant in our case has to show that its project in the Salvage Contract is an "investment" within the meaning of Article 1(1)(a) of the IGA. Even if the Claimant is able to satisfy the Tribunal that service contracts are a form of "investment" within the meaning of Article 1(1)(a) of the IGA, the Claimant still has to fulfill the requirement of the classification of an "approved project" in sub-paragraph (b)(ii). Failure to do so would mean that the project is not accorded the protection under the terms of the IGA.

(iii) <u>Nature of the projects</u>

12. The Respondent submits that another factor that distinguishes our case and the *Turkey case* is the nature of the projects concerned. The *Turkey case* relates to the building and operating of generation facilities relating to the sale of generated electricity to TEAS, the Turkish state-owned electricity entity using a Build Operate Transfer model. In 1996, the parties initialed an Implementation Contract based on the factors as set out in an earlier Feasibility Study conducted in November 1995. This contract was then submitted to the Danistay for review and approved in the form of a Concession Contract. It should also be noted that the Implementation Contract allowed for a Long Term Energy Sales Agreement and Fund Agreement to be executed. This is in contrast to the facts of our case where the parties are dealing with a simple service contract for the salvage of artifacts and nothing akin to the construction of a power facility and direct investment as expressly required under the terms and conditions of the Concession Contract.

13. In addition, the Respondent submits that the Concession Contract in the *Turkey case* has fulfilled the Salini test as expounded in **<u>Salini Construttori</u>**

[7] See **paragraph 114** of the Award

S.P.A. and Italstrade S.PA. v. Kingdom of Morroco (*Salini case)*[8]. The electrical power plant project in the *Turkey case* was of "*such magnitude and complexity*" and involved a risk to the extent that the operation of the project constitutes a paramount significance in the economy and development of the country. In comparison to our case, the Respondent submits that the salvage operation did not involve any or a significant contribution to the economic development of the Respondent. The Salvage Contract is merely concerned with the recovery of the Diana wreck and its contents with **the sole purpose of archeological interest and the study of historical heritage of the Respondent**, as expressed in the Preamble to the Salvage Contract.[9] Comparing the *Turkey case* with our case, the financial spending and outlays of resources that were supposed to be made by the Claimants in the former were in response to the need for development of the infrastructure in the host state whereas in the present case, the Salvage Contract envisages a recovery of artifacts from the sea and such a venture is merely a contract for services and does not contribute significantly to the economic development of the Respondent.

II. LEGAL DISPUTE ARISING DIRECTLY OUT OF AN INVESTMENT

(iv) Definition of "investment dispute" in the *Turkey case*

14. In the *Turkey case*, unlike in the IGA, a definition of an "investment dispute" is provided for in Article VI (1) of the Treaty. From the said definition, there are three circumstances in which a dispute shall be regarded as an investment dispute, *viz* a dispute involving -

(a) the interpretation or application of an investment agreement between a Party and a national or company of the other Party;

[8] The elements in the *Salini case* are as discussed in **paragraphs 34 to 45** of the Respondent's Comments dated 13 December 2006
[9] See **Annex No. 6** of the RBD Vol. I.

(b) the interpretation or application of any investment authorization granted by a Party's foreign investment authority to such national or company; or

(c) an alleged breach of any right conferred or created by this Treaty with respect to an investment.

15. The Tribunal, after appraising itself of the details of the dispute, held that the dispute involved questions of interpretation or application of both the investment agreement and the investment authorization. It was also held that this finding is also applicable in respect of the Respondent's argument that there is no investment, agreement or authorization, as these very claims involve the interpretation of the Concession Contract and the authorization. The dispute therefore arose unequivocally directly out of the investment, subject to the proviso that the issue of what constitutes precisely an investment as opposed to mere preparatory activities pertains to the merits[10]. In other words, the Tribunal found that the dispute in the *Turkey case* fell perfectly within the definition of an "investment dispute" as provided in paragraphs (a) and (b) of Article VI (1) of the Treaty.

16. In relation to paragraph (c) of Article VI (1) of the Treaty, the Tribunal stated in paragraph 123 of the Award that *"[a]lthough it is not possible at this jurisdictional stage to decide whether breaches have been committed, the history and terms of the dispute described are indicative that the investment is in principle subject to protection under the Treaty and that the Claimants are entitled to have their complaint examined*." Accordingly, the Tribunal held in paragraph 124 of the Award that it has jurisdiction on this issue as the dispute concerned arises directly out of an investment in terms of the interpretation and application of the Concession Contract and the investment authorization, as well

[10] See **paragraphs 121** of the Award

as in terms of Treaty rights connected to the investment that could have been compromised. In sum, the Tribunal held that on the basis of the definition of "investment dispute" in the Treaty, and nothing else, the dispute in the *Turkey case* arose directly out of an investment, thus the jurisdictional requirements under Article 25(1) of the ICSID Convention are fulfilled.

17. Apart from the absence of a definition of "investment dispute" in the IGA, the difference between the *Turkey case* and our case is further exacerbated by the presence of Article 1(1)(b)(ii) which provides that the term "investment" defined in the IGA is restricted to all investments made in projects classified by the appropriate Ministry of Malaysia in accordance with its legislation and administrative practice as an "approved project".

18. Article 7 of the IGA provides as follows:

> "*(1) Each Contracting Party hereby consents to submit to the International Centre for the Settlement of Investment Disputes (hereinafter referred to as "the Centre") for settlement by conciliation or arbitration under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States opened for signature at Washington at 18 March 1965 any legal dispute arising between that Contracting Party and a national or company of the other Contracting Party concerning an* ***investment*** *of the latter in the territory of the former.*"[11]

The term "investment" in Article 7(1) is qualified by Article 1(1)(b)(ii) of the IGA in that the project in the "investment" must be classified as an "approved project" for it to be afforded protection under the IGA.

[11] Supra no. 3

19. This classification of "approved project" is expressly provided in the IGA as a culmination of the deliberations and negotiations between the Respondent and the U.K. Government[12]. As such, each party to the IGA is duty-bound to honour this sacrosanct mutual agreement, and each party must also be held accountable for its intention that has been reflected in the IGA.

20. In this respect, the Respondent submits that the mechanism adopted in opting for a narrower definition of investment in the IGA is nothing new or peculiar in as far as investment treaty is concerned. Under this mechanism, the host country reserves the right to screen on the establishment of individual investments. In this way, the host country does not exclude any category of investment a priori, but can exclude any specific investment. It ensures that only those investments that have been approved by the host country are entitled to protection under the investment treaty. Consequently, approval of the investment signifies, in principle, conformity to the host country's development goals[13].

21. In the case of investments made in Malaysia, the condition is that they will be protected only if they are classified as an "approved project". In other words, the approval granted is selective where the Respondent's obligation to protect investments is limited only to an "investment" in an "approved project". Professor Schreuer commented[14] that where the parties' consents are defined in an investment treaty, "*… sometimes the investment must be specifically approved by the host State.*" In must also be recalled that the IGA was concluded in 1981. At that point of time the Respondent was in need of foreign direct investment and long term capital investments in fixed assets in labour intensive manufacturing and other manufacturing industries-related infrastructure. The Respondent

[12] See **paragraphs 56 - 63** of the Respondent's Memorial on Objections to Jurisdiction dated 11 March 2006 (**Respondent's Memorial**)
[13] See *Scope and Definition*, UNCTAD/ITE/IIT/11 (Vol. II), pages 61 to 65
[14] See *The ICSID Convention: A Commentary*, Christoph H. Schreuer, page 130

wanted to create favourable conditions for greater investments in these sectors[15].

22. Therefore, a distinction must be drawn between the satisfaction of the requirements of an "investment" in the Treaty *viz-a-viz* the IGA. Under the Treaty, once the project or contract satisfies the requirements of the definition of an "investment", it then qualifies for protection under the Treaty. As far as other permits or authorizations as required under the law applicable to a foreign investment are concerned, they are required only for purposes of carrying out the activities pursuant to the investment. Whereas under the IGA, a project or contract will not automatically qualify for the protection afforded under the IGA unless and until that project or contract obtains the status as an "approved project" from the Ministry of International Trade and Industry ("MITI"). Hence, the authorizations required in the *Turkey case* and the classification of "approved project" in our case must not be taken in similar vein because the mechanism in which they operate differs. Furthermore, the authorizations and certificates highlighted by the Respondents in the *Turkey case* were not provided for in the definition of "investment" under Article I(1)(c) of the Treaty. On the other hand, the "approved project" classification is expressly provided in the definition of "investment" in Article 1(1)(b)(ii) of the IGA.

(v) <u>Consent</u>

23. As the issue of "investment" within the meaning of Article 25(1) of the ICSID Convention is being considered here, the Respondent submits that the element of consent of the parties must be re-emphasized. As has been consistently submitted, once the issue of the meaning of "investment" is raised, it is an inescapable fact that the consent of the parties, or rather the elements that constitute the consent must be given the utmost consideration. In other words, for an investment to be considered as "*the investment*" under Article 25(1) of the ICSID Convention, it must fulfill the requirements of consent that has been

[15] See **paragraphs 64 - 90** of the Respondent's Memorial

agreed to by the parties. In our case, the term "investment" as defined in Article 1(1) of the IGA is qualified by the requirement of it being classified as an "approved project".[16]

24. The Tribunal in the *Turkey case* clearly illustrates this principle by stating in paragraph 139 as follows:

> "*Yet it remains that the "subject matter" jurisdiction is determined by the consent of the Contracting State expressed in a separate instrument and by the definition of investment included in that expression of consent. True, it is governed by the Convention but it is not defined by it.*"

In our case, the consent of the Parties is expressed in the IGA and the definition of investment included in that expression of consent is Article 1(1)(b)(ii) that provides the requirement of the classification of an "approved project".

C. CONCLUSION

25. Based on the above discussion, the Respondent's comments on the *Turkey case vis-à-vis* our case can be summarized as follows:

(i) The definition of "investment" in the Treaty includes service contracts but this is not the case in the IGA;

(ii) There is no parallel to the notion of an "approved project" in the Treaty, whereas such a requirement exists under the IGA;

(iii) Intention of the parties in the *Turkey case* that the project is an investment is clearly reflected in the Treaty while the parties in our case had never intended the Salvage Contract to be an investment governed by the IGA;

[16] See **paragraph 102 to 109** of the Respondent's Memorial

(iv) The nature, magnitude and complexity of the project undertaken in the *Turkey case* were such that they fulfilled the test in the *Salini case* as to an "investment", whereas in our case, the test has not been met;

(v) The Tribunal's decision that it has jurisdiction over the dispute in the *Turkey case* was based entirely on the definition of "investment dispute" in the Treaty, whereby no similar definition is provided for in the IGA; and

(vi) The authorizations granted in the *Turkey case* are not to be treated in the same vein as the requirement for the classification of "approved project" in the IGA because they operate differently.

26. In conclusion, the Respondent reiterates that in order for this Tribunal to determine whether it has the jurisdiction and competence to hear the dispute referred to it by the Claimant in our case, the Tribunal must satisfy itself that there is "an investment" as envisaged by Article 25(1) of the ICSID Convention. Based on the facts of our case, the Respondent submits that the Claimant has failed to prove to the Tribunal that the Salvage Contract is "an investment" for purposes of Article 25(1) of the ICSID Convention and as intended by the parties in the IGA, due to the fact that it was never classified as an "approved project" as required by Article 1(1)(b)(ii), an essential requirement that has been expressly agreed to by the Respondent and the U.K. Government in the IGA.

Dated the 22nd day of March 2007.

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The **Respondent's Comments On The Issue Of "Investment" Within The Meaning Of Article 25(1) Of The ICSID Convention** is filed by the Attorney General's Chambers of Malaysia, Solicitors for the Respondent, whose address for service is at the International Affairs Division, Level 6, Block C3, Federal Government Administrative Centre, 62512, Putrajaya, Malaysia.

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