ALSA INTERNATIONAL MOOT COURT COMPETITION

KUALA LUMPUR REGIONAL CENTRE FOR ARBITRATION

2017

BETWEEN

EZKAR

(CLAIMANT)

AND

GOVERNMENT OF VERTLAND

(RESPONDENT)

MEMORIAL FOR THE RESPONDENT

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STATEMENT OF JURISDICTION

Pursuant to the Treaty between the Government of the Republic of Sanphancisco and the Government of the Federation of Vertland concerning the Encouragement and Reciprocal Protection of Investment ("**BIT**"), the parties, EZKar and the Government of Vertland (the "**Vertese Government**") (each a "**Party**", and collectively, the "**Parties**"), have agreed to submit the present dispute to ad-hoc arbitration in accordance with the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration (as adopted in 2013) (the "**UNCITRAL Rules**").

STATEMENT OF FACTS

1. The Claimant, EZKar, is a "ride-hailing" company incorporated in Sanphancisco which provides unlicensed transportation services. With the aim to revolutionise transport networks worldwide, EZKar set its sights on establishing operations in Vertland which then had a poor public transport system which was struggling to accommodate its population.

2. The Respondent, the Vertese Government, is known for their pro-foreign investment stance and policies which has since propelled Vertland, a developing country located in South East Asiana, to become one of the top markets of choice for foreign investors today. Through the enactment of a wide spectrum of investor-friendly policies, the Vertese Government has enabled Vertland to open up and diversify its economy and establish strong international trade relations. With the recent rise of technology companies, there has been a substantial increase in the number of technology companies venturing into Vertland. EZKar is one such company.

3. On 6 March 2007, the Claimant incorporated a wholly-owned subsidiary called EZKar-Vert in Vertland. To facilitate EZKar-Vert's entry into the transportation industry of Vertland, EZKar-Vert and Vertland-Move ("**V-M**"), Vertland's state-owned entity entrusted with the trgulation of public transportation in Vertland, entered into an agreement (the "**V-M Agreement**") which allowed EZKar-Vert to conduct its operations in Vertland with ease and exempted EZKar-Vert from the relevant licensing and safety laws otherwise application to transport services within the country for a period of ten (10) years, subject to renewal.

4. EZKar-Vert quickly established operations in Vertland and became hugely successful at its inception due to the widespread acceptance and adoption of EZKar-Vert's services by the Vertese population. Unsurprisingly, EZKar-Vert had a severe damaging impact on the taxi industry and was increasingly perceived by local taxi conglomerates as unfair competition due to the exemption it enjoyed despite being a private hire vehicle operator.

5. Later, the Claimant sold 49% stake in EZKar-Vert to a businessman called Nick Traviska who operate a garment manufacturing business in his home country, Azuria. Despite being a citizen of Azuria, Traviska is also entitled under Vertese laws to Vertese citizenship since his mother is a Vertese citizen.

6. After the 2014 election of a new hyper-nationalist leader, President Donald Trunk ("**President Trunk**"), there was increasing resentment against foreigners who were viewed as "job thieves" and frustration among the Vertese population with the government's failure to consider locals' needs. Consequently, in September 2015, a violent protest (the "**Protest**") led by hundreds of taxi drivers against EZKar-Vert's operations at EZKar-Vert's office ensued. Despite multiple calls to the Vertese police for help made by EZKar-Vert's employees, help did not arrive until late in the evening. By then, EZKar-Vert's office premises had been significantly damaged and the first few floors even looted by the protestors.

7. Upon taking office in 2015, President Trunk also enacted the following policies which effectively reversed prior policies, denied EZKar-Vert various rights and benefits which

it had previously enjoyed, and/or introduced onerous restrictions on EZKar-Vert's operations in Vertland:

(a) A retrospective reversal of an existing 50% tax rebate policy for foreign-owned enterprises which required such enterprises to pay back all tax exemptions enjoyed for up to ten (10) years since 2005 as back taxes (the "**tax regulations**");

(b) Imposition of a special fee on all new private cars purchased, including private-hire vehicles used for EZKar-Vert but excluding cars purchased for use as taxis, in the amount of an additional 50% of the car's open market value (the "**environmental regulations**");

(c) Enactment of the Trunk PH Law which:

(i) required private-hire vehicle operators to apply and obtain the necessary licences for the provision of private-hire vehicle services;

(ii) prohibited private-hire vehicles other than taxis from charging customers on the basis of distance travelled; and

(iii) prohibited the use of geolocation software by private-hire vehicles.

8. Concerned by President Trunk's new regulations and their impact on its rights and operations in Vertland, EZKar-Vert wrote to V-M on numerous occasions to seek

discussions and negotiations on the V-M Agreement. However, these were ignored by V-M.

9. Around the same period, the purchase of 500 new public buses aimed at alleviating the public transport shortage in Vertland was also carried out. The introduction of the cheaper and more convenient public-bus service unsurprisingly turned out to be a success. Consequently, the use of taxis or private car services (including EZKar-Vert's services) decreased by 7% in 2015.

10. Separately, in 2011, the Claimant sourced for and found office premises at a state-owned commercial development for which a lease agreement was entered into directly with the Respondent. Later, the Respondent, terminated the lease agreement without returning the deposit which EZKar-Vert had placed with it. This refusal to refund the said deposit which was in the sum of $75,000, was in breach of the lease agreement.

11. Also separately in early 2013, EZKar-Vert was sued by a victim of a car accident involving a car driven by a driver using the EZKar service. This driver was an underage driver who was driving without a valid driving license at the time of the accident. Subsequently, the Vertese trial court found EZKar-Vert liable for ensuring that its drivers held valid licenses and awarded $500,000 in damages to the victim and further imposed $100 million in punitive damages on EZKar-Vert. EZKar-Vert has since appealed the judgment and the appeal is currently pending before the Vertese Court of Appeal.

12. Finding it no longer viable to continue with EZKar-Vert's operations in Vertland, EZKar now submits the dispute to arbitration pursuant to the BIT. This arbitration is to be conducted in accordance with the UNCITRAL Rules.

PLEADINGS

I. THE TRIBUNAL LACKS JURISDICTION OVER THE PRESENT DISPUTE

A. The present dispute falls outside the scope of the BIT

1. The present dispute falls outside the scope of the BIT as the rights conferred upon EZKar-Vert to operate a transportation system in Vertland do not constitute "investment" under Article 1 of the BIT.

2. Investments held by a subsidiary are not considered as investments of an investor (i.e. the Claimant). In *Standard Chartered Bank v The United Republic of Tanzania*, the tribunal denied standing to Standard Chartered HK, a subsidiary of Standard Chartered Bank, to claim entitlement to the UK-Tanzania BIT protection.

3. Similarly, the investment legally held by EZKar-Vert should not be the subject of a claim brought by the Claimant. Moreover, EZKar-Vert does not come within the meaning of "investor of a Party" under Article 2 of the BIT since it is not an enterprise incorporated in Sanphancisco, but in Vertland itself.

4. Therefore, the Claimant is not entitled to bring a claim in respect of an investment held by EZKar-Vert, its subsidiary, under the BIT.

B. Article 17 applies to deny the Claimant and EZKar-Vert of the benefits under the BIT

5. Article 17 of the BIT applies to enable the Respondent (i.e. a "Party") to deny EZKar-Vert (i.e. an "investor of the other Party") of the benefits under the BIT. For denial of benefits to be invoked, either Article 17(1) or 17(2) must be satisfied. Under Article 17(1), two requirements must be met – namely:

(a) Persons of a non-Party must own or control the enterprise; *and*

(b) The denying Party does not:

(i) maintain diplomatic relations with the non-Party; or

(j) adopts or maintains measures with respect to the non-Party or a person of the non-Party that prohibits transactions with the enterprise or that would be violated or circumvented if the benefits of the BIT were accorded to the enterprise or to its investments.

6. Requirement (a) is met as EZKar-Vert (i.e. the "enterprise") is owned or controlled by Nick Traviska ("**Nick**"), who falls within the definition of a "person of a non-Party". Under the definition of an "investor of a Party" under Article 2, it was provided that a natural person who is a dual national is deemed to be exclusively a national of the state of his/her "*dominant and effective nationality*". The test of "dominant and effective nationality" was formulated in the *Nottebohm* case as follows:

"[International arbitrators] have given their preference to the real and effective nationality, that which accorded with the facts, that based on stronger factual ties between the person concerned and one of the States whose nationality is involved. Different factors are taken into consideration, and their importance will vary from one case to the next: the *habitual residence* of the individual concerned is an important factor, but there are other factors such as the *centre of his interests*, his *family ties*, his *participation in public life*, *attachment* shown by him for a given country and inculcated in his children, etc."

7. While Nick holds dual nationality of both Azuria and Vertland, Azuria remains to be the state of his dominant and effective nationality since Azuria is Nick's home country and thus, place of habitual residence, in which he established his main garment manufacturing business. Moreover, Nick's mother similarly resided in Azuria despite holding Vertese citizenship. Thus, Nick is regarded to be exclusively a national of Azuria under the BIT.

8. Accordingly, requirement (a) of Article 17(1) is met on the basis that Nick holds a substantial 49% controlling interest in EZKar-Vert.

9. Assuming that Vertland does not maintain diplomatic relations with Azuria, requirement (b) of Article 17(1) is also met. Alternatively, Article 17(2) will be satisfied in any case.

10. For Article 17(2), the two requirements to be met are:

(a) The enterprise has no substantial business activities in the territory of the other Party (i.e. Sanphancisco); and

(b) Persons of a non-Party or of the denying Party, own or control the enterprise.

11. Here, requirement (a) is met as EZKar-Vert (i.e. the enterprise) has no substantial business activities in Sanphancisco, being a subsidiary set up precisely for the purposes of facilitating the Claimant's entry into the Vertese transportation industry. Requirement (b) is also satisfied since Nick, a person of a non-Party (i.e. Azuria), owns/controls EZKar-Vert, as established above.

12. Thus, Article 17 is invoked to preclude this tribunal from exercising jurisdiction over the substantive claims in the present dispute.

II. SOME ACTS COMPLAINED OF CANNOT BE ATTRIBUTED TO THE RESPONDENT

13. The Respondent submits that not all the acts complained of by the Claimant is attributable to the Respondent. Amongst the acts complained of in this dispute – namely of the Vertese police, judiciary and V-M, only those of the police and the judiciary are attributable to the Respondent.

14. The general rule of attribution is that a state is responsible for all its organs under customary international law. The International Law Commission's Articles on State Responsibility ("**ARSIWA**") lays down the principle of attribution as follows:

"**Article 4 Conduct of organs of a State**

1. 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 organisation of the State*, and *whatever its character as an organ of the central government or of a territorial unit of the State*.

2. An organ includes any person or entity which has that status in accordance with the internal law of the State."

(emphasis added)

15. Accordingly, it is conceded that the Vertese police and judiciary, which exercise administrative and judicial functions respectively, are state organs. Thus, their acts can be attributed to the Respondent.

16. However, V-M's purported breaches of the V-M agreement cannot be attributed to the Respondent. V-M is neither a state organ, nor were the purported breaches in exercise of such governmental authority empowered by the laws of Vertland.

17. Generally, state entities are separate and their acts will not be attributed to the state. Since V-M is an entity with its separate legal personality, it is not a state organ, even if it has been empowered by the state to regulate public transportation.[1] It is further argued that

[1] Facts, at [4].

despite being empowered with governmental authority, purported breaches of V-M would not amount to exercising such governmental authority.

18. The purported breaches of V-M are not within the scope of its exercise of governmental authority. These breaches are merely breaches between contractual parties and cannot be associated with the exercise of the sovereign power given by the Federation of Vertland. These arguments will be further canvassed below.

III. BREACHES UNDER THE V-M AGREEMENT ARE NOT ACTIONABLE AS TREATY BREACHES UNDER THE BIT

19. For a breach under an agreement between two contracting parties not involving the State to be non-actionable as treaty breaches under the BIT, two arguments have to be canvassed:

(a) The BIT does not cover the obligations entered into by V-M; and

(b) V-M was not in exercise of sovereign power when it allegedly breached the V-M Agreement.

20. The Respondent submits that this has not been the case, that the BIT does not allow for such claims, and that V-M has not exercised any sovereign power. Indeed, V-M would not have had such power to conduct itself in breach of the V-M Agreement as alleged by the Claimant.

A. The BIT does not cover the obligations under the V-M Agreement

21. For the BIT to cover such obligations under the V-M Agreement, it has to be proven that there is an "umbrella clause" within the BIT which elevates contractual obligations entered into by State Entities to treaty obligations. Despite having denied that V-M's breaches are attributable to the Respondent, for sake of completeness, the Respondent will address the issue of whether the purported "umbrella clause" (i.e. Article 25) in the BIT may elevate contractual breaches under the V-M Agreement to treaty breaches actionable under the BIT.

22. Article 25(1) of the BIT states that:

> "A Party shall fulfil any other obligations it may have entered into with regard to investments in its territory by investors of the other Party."

23. The Respondent submits that on the correct interpretation of the Article, in the absence of clear intent of the signatories to the BIT, this Article should not elevate any breaches of obligations undertaken with respect to any particular investment to become a treaty breach.

24. Instead, the correct interpretation is that only contractual obligations have been violated to "such a magnitude as to trigger the Treaty protection".[2] This is in line with the case of *Joy Mining v Egypt*, where the tribunal took the view that the dispute regarding bank

[2] *Joy Mining v Egypt*.

guarantees, were commercial and contractual in nature, which was to be settled through the mechanism set forth by contract in question.

25. The Respondent submits that the correct interpretation would have to take into consideration that the V-M Agreement itself had a dispute resolution mechanism, which was to submit such disputes arising from the V-M Agreement for arbitration in accordance to the rules of the International Chamber of Commerce.[3] Since the V-M Agreement has no connection to the BIT, it is submitted that a broad interpretation should not be read into Article 25(1) of the BIT.

26. Consequently, Article 25(1) does not cover the alleged breaches which the Claimant purport, and thus the alleged breaches under the V-M Agreement should not be elevated to the level of treaty breaches under the BIT.

B. V-M has was not to in exercise of sovereign power when it allegedly breached the V-M Agreement

27. Taking the Claimant's case at its highest, even if V-M were proven to be an entity whose actions were attributable to the Respondent, and further, that Article 25(1) were to cover such contractual breaches, the alleged breaches are insufficient to amount to a treaty breach.

[3] Facts, at [6].

28. It was submitted that the tribunal in the case of *Duke Energy v Ecuador* was correct in recognising the difference between contractual breaches and treaty breaches. In that case, the tribunal stated that:

> "[i]n and of itself the violation of a contract does not amount to the violation of a treaty. This is only natural since treaty and contract breaches are different things, responding to different tests, subject to different rules." [4]

29. Accordingly, the correct test to determine whether a contractual breach can be elevated to a treaty breach is when "the behaviour of the party goes beyond that which an ordinary contracting party could adopt."[5] Consequently, the question to answer is whether V-M, in purportedly breaching the V-M Agreement, had indeed committed such actions which an ordinary party could adopt.

30. On the facts, what V-M has done was to ignore EZKar-Vert when EZKar-Vert was seeking discussions and negotiations. While the V-M Agreement did allow EZKar-Vert exemption from relevant licensing and safety laws, V-M has in no way acted in a manner in which a sovereign power can act in.

31. Consequently, even if the Claimant successfully proves that V-M's actions were attributable to the Respondent, and that Article 25(1) can be invoked, the Respondent submits that in the instant case, the Claimant will not be able to satisfy the test to elevate contractual breaches in the V-M Agreement to the level of treaty breaches under the BIT.

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[4] At [342].
[5] *Impregilo SpA v Pakistan, Decision on Jurisdiction,* ICSID Case No ARB/03/3, IIC 133 (2005), 22nd April 2005, at [260].

IV. THE RESPONDENT HAS NOT EXPROPRIATED THE CLAIMANT'S INVESTMENT

A. The enactment of the Trunk PH Law does not amount to indirect expropriation of benefits under the V-M Agreement

32. It is a well-accepted principle of international law that expropriation may occur *indirectly* to result in the "substantial deprivation of the use and value of the investment".[6] Generally, tribunals determine expropriation on a case-by-case basis by conducting a balancing test in light of all the circumstances. In doing so, the tribunal considers the following criteria:

(a) Degree of interference;

(b) Intention of the State;

(c) Impact of interference;

(d) Degree of the investor's expectation.[7]

33. In *Chemtura Corporation v Canada*, the tribunal observed that where qualifies as a substantial deprivation is a "fact sensitive exercise that must be conducted in the light of the circumstances. In *Metalclad Corporation v The United Mexican States*,[8] indirect expropriation was defined as "covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property".

[6] *Redfern* at [8.82]. See also *Arbitration in Singapore* at [20.081].
[7] *International Investment Arbitration* at 298, 299.
[8] At [103].

34. To begin with, the intention of the Trunk Administration was never to expropriate the Claimant's investment, but to restrict and regulate private-hire vehicle operators including EZKar-Vert and taxi companies. The degree of interference brought about by the Trunk PH Law was also not as significant as the Claimant made it out to be.

35. First, the imposition of the licensing requirement did not result in any interference since the licensing exemption which the Claimant was entitled to under the V-M Agreement was due to expire in 2005 in any case. Second, the prohibition of a distance-based charging system could not have "crippled" the operations of EZKar-Vert given the availability of other alternative ways in which EZKar-Vert can adopt to charge their customers. The same argument applies for the prohibition of geolocation software. Removing this feature does not in any way hinder EZKar-Vert's drivers from picking up prospective customers and performing their due services. It only made it less convenient for customers who are now prevented from knowing the availability of EZKar-Vert cars in the vicinity.

36. Accordingly, the impact of the alleged interference was grossly overstated by the Claimant. It could not reasonably be said that the Claimant was substantially deprived of the use and value of its investment, i.e. EZKar-Vert. At the most, the Trunk PH Law merely inconvenienced, rather than hindered the operations of EZKar-Vert.

37. Lastly, there could not have been any expectation on the part of the Claimant which would be frustrated by the enactment of the Trunk PH Law. The Respondent made no commitment or assurances that the Claimant will be immune from regulatory changes which may have an impact on their operations. The Respondent especially made no such

assurances that the Claimant is entitled to enjoy the licensing exemptions under the V-M Agreement for an indefinite period of time.

38. In any case, the enactment of the Trunk PH Law would have fell within the ambit of the exception under Article 6 as an expropriation made for a public purpose of regulating private-hire vehicle operators. Furthermore, it was enacted in a non-discriminatory manner and in accordance with the minimum standards of fair and equitable treatment and due process of law. Ultimately, it is submitted that the Claimant bore the risk of regulatory change.

B. The imposition of the restrictive tax regulations does not amount to indirect expropriation

(i) The Claimant has not satisfied the preconditions under Article 21 of the BIT to submit the claim to arbitration

39. Article 6 of the BIT does not apply to the enactment of the restrictive tax regulations as the Claimant has not satisfied the jurisdictional requirements under Article 21 of the BIT to submit the claim to arbitration. Article 21 provides that:

"…the claimant [to have] first referred to the competent tax authorities of both Parties in writing the issue of whether that taxation measure involves an expropriation…"

40. On the facts, this was not done. The Claimant merely wrote to V-M, who is not a competent tax authority, to seek discussions and negotiations on the V-M Agreement. In any case, even if Article 6 applies, the tax regulations do not amount to an expropriation.

(ii) The enactment of the restrictive tax regulations does not amount to expropriation

41. In *Burlington Resources v Ecuador*, the tribunal considered a tax measure to be tantamount to expropriation if it (i) "produces the effects required for any indirect expropriation"; and (ii) is "discriminatory, arbitrary and involves a denial of due process or an abuse of rights".

42. First, the imposition of the tax regulations does not substantially wipe out the profitability of the Claimant's investment. The prior tax rebates were independent and separate from the profits of EZKar-Vert. Moreover, the quantum of the tax now payable is unlikely to be a significant proportion of EZKar-Vert's total revenue such as to result in a substantial cut in EZKar-Vert's profits. Thus, the reversal of the prior tax rebates would not have substantially affected the profitability of EZKar-Vert.

43. Second, the operation of the tax regulations is not in any way discriminatory to the Claimant since it affects all foreign companies. As such, it cannot be established that the restrictive tax regulations constitute indirect expropriation of the Claimant's investment.

(iii) The enactment of the restrictive tax regulations falls within the exception under Article 6 of the BIT

44. Even if the enactment of the restrictive tax regulations constitutes expropriation, it nevertheless falls within the exception under Article 6 of the BIT. First, the reversal of the tax rebates was evidently for a public purpose. In *ADC v Hungary*,[9] the tribunal stated that the treaty requirement for "public purpose" requires some genuine interest of the public, and that there must be some public interest being served. The reversal of the tax rebates is of significant importance and impact to Vertland's economy, especially as it seeks to revitalise its local companies. Further, in light of the nationalistic movement, there is much public interest to be served in the enactment of the tax regulations.

45. Second, the reversal of the tax rebates are not discriminatory as they apply to all foreign companies in Vertland, and not just EZKar-Vert alone. In *ADC v Hungary*, the tribunal pointed out that for discrimination to exist, there must be different treatments to different parties.[10] Further, in *LIAMCO v Libya*, the tribunal also stated that discrimination would not be made out if the policies did not target companies of an exclusive nationality.[11]

46. Three conditions have to be fulfilled to establish discrimination:[12]

(a) there must be an appropriate comparator;

(b) there must have been a difference in treatment;

(c) the distinction within the basis of comparison must have been unreasonable.

47. The argument that the tax regulations discriminate against foreign companies is unsustainable. While there was an appropriate comparator against foreign companies, i.e.

[9] ICSID Case No. ARB/03/16, Award, 2 October 2006, at paras 429, 432.
[10] Paras 441 to 443.
[11] 12 April 1977, (1981) 20 ILM 1.
[12] *International Investment Law*, Chap VIII: Expropriation, at para 523.

local companies, and the tax regulations produce a difference in tax treatment between the two, this distinction made between the two was not in any way unreasonable. In fact, the Respondent had legitimate reasons for this legislative change. The reversal of the tax rebates is of paramount importance to Vertland's economic development, especially as Vertland seeks to revitalise its local companies and in light of the nationalistic movement.

C. The introduction of the competing public-bus service does not amount to indirect expropriation

48. The launch of a new public-bus service in Vertland does not constitute indirect expropriation of the Claimant's investment. It merely represented the exercise of the Respondent's power to adopt policies with a public purpose for the welfare of the society and in the wider public interest of the Vertland populace.

49. In the cases of *Azurix v Argentina* and *LG&E v Argentina*, the tribunals adopted a balancing test to determine whether a particular state measure amounted to expropriation. The need to balance between the host state's right to act in the public interest and the protection of the investor's rights was emphasised. Notably, the tribunals pointed to the need for there to be a "reasonable relationship of *proportionality* between the means employed and the aim sought to be realised". This means that the measures undertaken by the state must be proportionate to the public interest to be protected.

50. Here, the decision to introduce a public-bus service was made in furtherance of the legitimate aim of addressing the shortage of public transport in Vertland. Given the absence of any form of public transportation, the introduction of public buses was the

first ever mode of public transport in Vertland implemented by the Respondent in a bid to alleviate the shortage problem. This can hardly be regarded to be disproportionate to the Respondent's aim which was ultimately undertaken in the public interest.

51. Accordingly, the injection of new competition by the Respondent in the form of new public buses cannot amount to expropriation of the Claimant's investment. Even if it legally amounts to expropriation, it falls within the exception under Article 6 of the BIT as an expropriatory measure made for a public purpose of alleviating the public transport shortage in Vertland.

D. The wrongful termination of the lease agreement does not amount to direct expropriation

52. Direct expropriation is defined as the outright physical seizure of an investor's property, or the title to such property, by the host state.[13] The Respondent's termination of the lease agreement does not constitute such direct expropriation since it was of an ordinary contractual nature.[14]

53. In *Biwater Gauff v Tanzania*, the tribunal held that the termination of the lease by the Tanzanian government was an "ordinary behaviour of a contractual counterparty"[15] and could not therefore amount to expropriation as it cannot be said to be "procured" by the Tanzanian government as alleged. Moreover, the tribunal considered the question as to

[13] *Redfern* at [8.81].
[14] *Principles of International Investment Law*, at p. 109-110.
[15] At [492].

whether or not the termination was justified as a matter of contract to be immaterial and something which the tribunal need not resolve.

54. Similarly, the termination of the lease agreement cannot by itself amount to an expropriatory act, regardless of whether the said termination was wrongful or otherwise.

V. THE RESPONDENT HAS NOT BREACHED THE STANDARD OF FAIR AND EQUITABLE TREATMENT UNDER ARTICLE 5

55. The standard of fair and equitable treatment generally refers to treatment conducive to promoting or stimulating investment. In practice, it is often equated to the minimum international standard traditionally understood to be based on a standard of review set out in the 1928 Neer decision of the United States-Mexico General Claims Commission as follows:

> "[T]he treatment of an alien, in order to constitute an international delinquency, should amount to an *outrage*, to *bad faith*, to *wilful neglect of duty*, or to an *insufficiency of governmental action so far short of international standards that every reasonable and impartial man would readily recognise its insufficiency*."
>
> (emphasis added)

56. This was affirmed in *Genin v Estonia*, where the tribunal viewed the fair and equitable treatment standard as incorporating the minimum standard under international law. The same conclusion was also reached in *Occidental v Ecuador*.

57. More significantly, the adoption of the minimum international standard was explicitly endorsed in Article 1105 of the North American Free Trade Agreement ("**NAFTA**") in its heading titled "Minimum Standard of Treatment" and the inclusion of the fair and equitable treatment standard as referring to international law.[16] NAFTA Free Trade Commission's Notes of Interpretation issued on 31 July 2001 confirms this interpretation. Furthermore, certain other treaties also appear to support this interpretation of the fair and equitable treatment standard.[17]

58. The case of *Waste Management v Mexico* expounded on the content of the minimum standard of fair and equitable treatment. In the case, the tribunal stated that this minimum standard would be infringed by conduct which is "arbitrary, grossly unfair, unjust, idiosyncratic, is discriminatory and exposes the claimant to section or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety".[18]

A. The enactment of the Trunk PH Law did not breach minimum standards of fair and equitable treatment

59. The enactment of the Trunk PH Law did not breach the standard of fair and equitable treatment under Article 5 of the BIT, whether based on the minimum standards under international law or otherwise. There is no evidence that the enactment of the Trunk PH Law was in any way induced by bad faith or in manifest breach of due process.

[16] *The Law of Investment Treaties*, at p. 247. See also *Investor-State Arbitration*, at p. 491, 500.
[17] E.g. 2012 US Model BIT, Canada Model Foreign Investment Protection and Promotion Agreement etc. See *The Law of Investment Treaties*, at p. 246.
[18] *Principles of International Investment Law*, at p. 144.

60. In *CME v Czech Republic*, the tribunal found that Czech Republic's legislative and regulatory changes had unlawfully harmed CME's investment by altering the country's investment framework and held that the government had "breached its obligation of fair and equitable treatment by evisceration of the arrangements in reliance upon [which] the foreign investor was induced to invest".

61. The enactment of the Trunk PH Law could not be said to have breached any legitimate expectations of the Claimant may have had with regards to Vertland's legislative and regulatory framework when making the investment.

62. The Trunk PH Law was enacted 10 years after the V-M Agreement was entered into. The V-M Agreement, which exempted EZKar-Vert from the relevant licensing and safety laws otherwise applicable to transport services, was only for a term of 10 years (subject to renewal). It cannot be said to have breached the Claimant's legitimate expectations as to further enjoyment of rights under the V-M Agreement since the tax exemption would in any case have expired by the time Trunk PH Law was enacted.

63. Even if the investment was made on the grounds that private-hire vehicles can be used as an effective substitute for Vertland's lacking public transport system, the Respondent cannot be said to have represented to the Claimant that such grounds would extend beyond the 10-year period.

64. Furthermore, the Trunk PH Law had not been discriminatory against EZKar-Vert. The licensing requirements and the prohibition of geolocation software applied to all private-hire vehicles including taxis. As for the prohibition on the distance-based charging

system, there were reasonable grounds why such a prohibition was imposed only on EZKar-Vert's cars. It was to alleviate competitive pressures faced by the local taxi companies through differentiating the mode of operation of EZKar-Vert from that of the taxi companies. In any case, there are many other ways in which EZKar-Vert can choose to charge their customers, such as length of trip, real-time demand etc.

65. Thus, the conduct of the Respondent did not fall short of the minimum standards of fair and equitable treatment in respect of the Trunk PH Law.

B. The enactment of the restrictive tax regulations did not breach minimum standards of fair and equitable treatment

66. Similarly, the enactment of the restrictive tax regulations did not breach minimum standards of fair and equitable treatment under Article 5 of the BIT, whether based on the minimum standards under international law or otherwise.

67. In the case of *Toto Costruzioni v Lebanon* which concerned a claim based on changes to the tax regime, the tribunal considered that changes in the regulatory framework would be considered as breaches of the fair and equitable treatment standard only in the case of a "*drastic or discriminatory change* in the essential features of the transaction".[19] Such drastic or discriminatory consequence was not established as the additional cost of the increased taxes and custom duties was said to be small compared to the value of the project. Also, the changes to the tax regime was not discriminatory as it was applicable to all foreign investors and Lebanon nationals.

[19] At [244].

68. The same could be said for the present case. First, it could not be established that the reversal of the prior tax rebate policy was a drastic change given the inconsequential increase in EZKar-Vert's tax burden relative to the value of EZKar-Vert's investment in Vertland. Second, the tax regulations was not discriminatory since it applied to all foreign companies, and not just EZKar-Vert alone.

69. Thus, the conduct of the Respondent did not fall short of the minimum standards of fair and equitable treatment in respect of the tax regulations. Ultimately, it is submitted that the Claimant bore the risk of regulatory change.

C. The punitive judgment against EZKar-Vert did not breach minimum standards of fair and equitable treatment

70. The judgment which imposed $100 million in punitive damages against EZKar-Vert was not made in breach of the standards of fair and equitable treatment mandated under Article 5 of the BIT, whether based on the minimum standards under international law or otherwise. There is no evidence that the punitive judgment was in any way induced by bad faith or in manifest breach of due process.

71. It is well-settled that customary international law is concerned with denials of justice between private parties. In *Loewen v USA* ("*Loewen*"), the authorities on impugning court judgments against minimum international law standards were extensively discussed. It was identified that "*manifest injustice*", in the sense of a "lack of due process leading to an outcome which offends a sense of judicial propriety" must be established.

72. *Mondev International Ltd v USA* was cited for formulating the main question as:

> "… whether, at an international level and having regard to generally accepted standards of the administration of justice, a tribunal can conclude in the light of all the available facts that the impugned decision was clearly *improper* and *discreditable*, *with the result that the investment has been subjected to unfair and inequitable treatment*."

73. On the facts, there is no indication that the judgment was in any way improper and discreditable as a result of any manifest injustice in the decision-making process. First, unlike the facts in *Loewen*, there was no indication of any procedural defects and questionable methods employed by the counsels in the case.

74. Second, EZKar-Vert's exemption from licensing laws did not extend to basic driving licenses, but was instead referring specifically to licenses for operating a private vehicle hire service. It would be absurd that a service provider like EZKar-Vert would not be subject to the fundamental road traffic rules governing all vehicles on the roads of Vertland. Third, the quantum of the punitive damages, while high, was wholly justified given the severity of EZKar-Vert's oversight and the influence and impact of EZKar-Vert on the safety levels of Vertland's roads.

75. Accordingly, it cannot be established that the judgment involved a denial of justice to the Claimant. Thus, the conduct of the Respondent did not fall short of the minimum standards of fair and equitable treatment in respect of the Trunk PH Law.

D. The enactment of the environmental regulations did not breach minimum standards of fair and equitable treatment

76. The enactment of the environmental regulations by the Respondent has not breached the standard of fair and equitable treatment under Article 5 of the BIT, whether based on the minimum standards under international law or otherwise. There is no evidence that the enactment of the environmental regulations was in any way induced by bad faith or in manifest breach of due process.

77. Given that this issue implicates the environmental laws of Vertland, Article 5 must be read in conjunction with Article 12 of the BIT to identify the Respondent's commitments in respect of environmental laws. Particularly, Article 12(3) provides that "the Parties recognise that each Party retain the right to exercise discretion with respect to regulatory matters…where the course of action reflects a *reasonable* exercise of such discretion…".

78. Accordingly, the special fee imposed on private cars is a reasonable exercise of such discretion because there is a difference between taxis used for *public* transport (which is for a public purpose), and private cars, which is used for private purposes and, in the case of the Claimant, for business purposes.

79. Referring to the requirements for discrimination to be established,[20] this also means that the environmental regulations had not been discriminatory against EZKar-Vert since there was a reasonable basis for the differential treatment between cars used as taxis and EZKar-Vert's cars.

[20] See [25] above.

80. In any case, the Respondent had not, through the enactment of the environmental regulations, frustrated any legitimate expectations held by the Claimant. In fact, there were no such expectations given that the Respondent had not given any commitment or assurance that the Claimant would not be subject to any unfavourable environmental laws.

81. In *Methanex v USA*, it was held that "a non-discriminatory regulation for a public purpose, which is enacted in accordance with due process and, which affects, *inter alios*, a foreign investor or investment is not deemed… 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." Here, the environmental regulations were enacted in accordance with due process and for the public purposes of controlling carbon-emissions and reducing private car ownership.

82. Therefore, the environmental regulations did not fall short of the minimum standards of fair and equitable treatment. Ultimately, it is submitted that the Claimant bore the risk of regulatory change.

VI. THE RESPONDENT DID NOT FAIL TO PROVIDE FULL PROTECTION AND SECURITY UNDER ARTICLE 5 IN RESPECT OF THE PROTEST

A. The acts leading to the Protest cannot be attributed to the Respondent

83. In *Lauder v Czech Republic*, the tribunal opined that the obligation to provide full protection and security does not oblige parties to protect foreign investment against any possible loss of value caused by persons whose acts cannot be attributed to the State.[21]

84. Also, in *Tecmed v Mexiso*, the tribunal dismissed the claim based on a purported breach of the state's obligation to provide full protection and security since the claimant had not sufficiently proved that the Mexican authorities have "encouraged, fostered, or contributed their support to people or groups that conducted the community and political movements" or participated in such movements, and there was no evidence that the authorities had not reacted reasonably.

85. Similarly, the Respondent cannot be held liable for the damage to EZKar-Vert's investments as a result of the Protest which was carried out by the taxi drivers. Thus, the acts of the taxi drivers cannot be attributed to the Respondent, and the Respondent is not obliged to protect EZKar-Vert's office building against the Protest.

B. The Respondent has discharged its duty of due diligence to provide for the protection and security of EZKar-Vert

86. Applying where a foreign investment has been affected by civil strife and physical violence,[22] the standard of full protection and security obliges the host state to provide a certain level of protection to foreign investment from physical damage.[23] The core element under this standard is the "obligation to exercise due diligence in providing

[21] At [308].
[22] *Saluka v Czech Republic* at [483].
[23] *Rumeli v Kazakhstan*.

physical protection and security from injurious acts by government agents or third parties to the investor and its investment". This obligation must not fall short of the minimum standard of vigilance and care required by customary international law.[24]

87. In turn, the due diligence obligation requires a host state to undertake "reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances". [25] Accordingly, a failure to meet these expectations would constitute a breach of the protection and security standard. This was also endorsed in *Saluka v Czech Republic*.[26] Further, in *AAPL v Sri Lanka*, it was held that the pivotal thrust of protection and security imposes on the host State an obligation to take active measures for the protection of the foreign investment, namely, to prevent private actors from harming it.[27]

88. Even if the acts leading to the Protest are attributable to the Respondent, it is submitted that the Respondent is not liable since there was no evidence that the Vertese police took an unreasonably long time to arrive at the scene of the Protest.

[24] *The Law of Investment Treaties*, at p. 240.
[25] *The Law of Investment Treaties*, at p. 240.
[26] At [484].
[27] *International Investment Law*, at p. 778.

PRAYER OF RELIEF

For the foregoing reasons, the Respondent respectfully requests the Tribunal to declare that:

(a) The Respondent has not breached its obligations under the BIT;

(b) The Tribunal does not have jurisdiction over the present dispute;

(c) The acts of V-M cannot be attributed to the Respondent;

(d) The Respondent has not expropriated the Claimant's Investment;

(e) The Respondent has not breached the standard of fair and equitable treatment;

(f) The Respondent has not failed to provide full protection and security to the Claimant.

(Word Count: 7960)