PERMANENT COURT OF ARBITRATION

PCA Case No. 2016-74

BETWEEN:

ATTON BORO LIMITED	REPUBLIC OF MERCURIA
CLAIMANT	**RESPONDENT**

MEMORIAL FOR THE RESPONDENT

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INDEX OF ABBREVIATIONS

Basheera	The Kingdom of Basheera
BIT	Agreement between the Republic of Mercuria and the Kingdom of Basheera for the Promotion and Reciprocal Protection of Investments
Exh. 1	Notice of Arbitration Exhibit 1
Facts	Uncontested Facts
Germany-Ukraine BIT	Germany - Ukraine BIT (1993)
ICESCR Convention	International Covenant on Economic, Social and Cultural Rights
ICJ Statute	Statute of the International Court of Justice
LTA	The Long-Term Agreement concluded in 2004
Mercuria	Republic of Mercuria
NHA	National Health Authority of Mercuria
p./pp.	page/pages
Para./Paras.	Paragraph/Paragraphs
PO 1/2/3	Procedural Order No. 1/2/3
Reef	The People's Republic of Reef
The Award	The arbitral award passed by the Tribunal in Reef
UNCTAD	United Nations Conference on Trade and Development
US-Ecuador BIT	Ecuador - United States of America BIT (1993)
WTO	World Trade Organization

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STATEMENT OF FACTS

1. Claimant, Atton Boro Limited (**Atton Boro**), is a wholly-owned subsidiary of Atton Boro Group, whose primary holding company is a pharmaceutical corporation organized in Reef, Atton Boro and Company. Atton Boro Group obtained Mercurian patent for Valtervite and reassigned it to Atton Boro.

2. Respondent is the Republic of Mercuria (**Mercuria**), a developing country with 67 million people.

3. In 2003, reports revealed the imminent situation of greyscale (a critical epidemic disease). The Ministry of Health thus invited offers from pharmaceutical companies for supply of FDC greyscale medicines to ease this public health concern.

4. On 25 November 2004, Atton Boro and National Health Authority (NHA) entered into a Long-Term Agreement (LTA) where NHA would purchase Sanior whose main compound is Valtervite at a fixed 25% discount by periodically placing purchase orders. The LTA is valid for 10 years subject to Atton Boro's satisfactory performance. Even at 25% discount, the annual cost per patient would amount to USD 10,000.

5. In early 2008, due to fast prevalence of greyscale and unexpected growth of patients, NHA required renegotiation of the Sanior price and acquired an additional discount of 40%. In 10 June 2008, the NHA terminated the LTA for unsatisfactory performance of Atton Borro who later invoked arbitration against the NHA under the LTA. In January 2009, a Tribunal seated in Reef passed an award in favor of Atton Boro concerning the LTA.

6. On 3 March 2009, Atto Boro filed enforcement proceedings before the High Court of Mercuria and NHA made a public policy objection. On 10 January 2012, the Mercurian Parliament passed the Commercial Courts Act directing the High Court to constitute Commercial Benches which the Mercurian Supreme Court clarified as not having jurisdiction over enforcement proceedings in September 2013.

7. On 10 October 2009, Mercurian President promulgated National Legislation for

its Intellectual Property Law (Law No. 8458/09) which introduced compulsory authorization of patents.

8. On 17 April 2010, Mercurian High Court granted HG-Pharma, a Mercurian generic drug manufacturer's application for Atton Boro's patent, Valtervite until greyscale no longer threats public health and fixed 1% royalty rate. The generic drug reduced costs of medicines by 80% and saved 1.2 billion USD annually.

9. On 16 November 2016, Claimant filed Notice of Arbitration before Permanent Court of Arbitration against Mercuria invoking the dispute resolution clause contained in the Treaty between Mercuria and Basheera for the Promotion and Reciprocal Protection of Investment.

ARGUMENTS

A. THIS TRIBUNAL LACKS JURISDICTION OVER CLAIMS IN RELATIONS TO THE AWARD

1. According to Article 8 and Article 13 of the BIT, this Tribunal only has jurisdiction over "investment" under Article 1(1) of the BIT. Respondent submits that this Tribunal lacks jurisdiction over claims relating to the Award because the Award (1) is inconsistent with the definition of investment; and (2) has no territorial link with Mercuria. Finally, (3) the LTA, where the Award arose from, is not an investment.

(1) THE AWARD IS INCONSISTENT WITH THE DEFINITION OF INVESTMENT UNDER ARTICLE 1(1) OF THE BIT

2. Article 1.1 of the BIT provides a fairly broad definition of "investment". Pursuant to applicable rules on treaty interpretation, the term "investment" shall contain an inherent meaning, under which the Award does not fall.

(a) The term "*investment*" should contain an inherent economic meaning

3. Respondent contends that although Mercuria did not ratify the Vienna Convention on the Law of Treaties (*VCLT*), it is still bound by Article 31 and 32 of VCLT because they reflect customary international law,[1] affirmed by tribunals who almost invariably start by invoking Article 31 of the *VCLT* by interpreting treaties.[2] Therefore, Article 31 of the *VCLT* shall be used for interpretation.

4. Under Clause 1 of this Article 31, which provides 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."

[1] *Shaw*, p. 933; *Bosnia v. Serbia*, Pars. 160
[2] *AAPL v Sri Lanka (Award)*, Paras. 38-42; *Enron v Argentina (Jurisdiction)*, Para.32 ; *Plama v Bulgaria* (*Jurisdiction)*, Paras. 147-165; *Salini v Jordan (Jurisdiction)*, Para.75

5. This methodology supports that the term "investment" should be construed as to contain an inherent economic meaning.

6. Starting with the 'ordinary meaning' of "investment", academic commentary and arbitral jurisprudence have focused on the initial phase on economic terminology.[3] According to Professor *Douglas*,

> "[A]n investment, in order to qualify for investment treaty protection, must incorporate certain legal and economic characteristics. The economic characteristics derive from the common economic conception of foreign direct investment. "[4]

7. Douglas also stated that there should be an appropriate general test of what constitutes an "*investment*", to be applied in all investment treaty claims in spite of whether they are brought under the ICSID Convention or any other rules of arbitration.[5]

8. Respondent further contends that such interpretation is in line with the object and purpose of the BIT. The purpose of the BIT is to "*promote greater economic cooperation"* and *"stimulate the flow of private capital and the economic development*".[6] All these purposes concern the economic feature of investment. Thus, any putative investments must be in accord with economic characteristics. Specifically, according to the purpose of the BIT, there are three characteristics[7] that the investment shall entail: contribution to the host state, over a certain period of time, which involves some risk.[8]

9. This rationale has also been confirmed by non-ICSID tribunals. For example, in the case of *Romak v Uzbekistan*, the tribunal held that:

> "[A]sset types enumerated in the BIT's non-exhaustive list may exhibit these hallmarks. But if an asset does not correspond to the inherent definition of

[3] *Methanex v United States (Award)*, Part II, Chapter B, Paras. 15-23, Part IV, Chapter B, Para. 29 ; *Siemens v Argentina (Jurisdiction)*, Para.80
[4] *Douglas*, p. 342
[5] *Ibid.*, pp. 161 and 189
[6] Annex No. 1, p. 32, Preamble of the BIT
[7] *Salini v Morocco (Jurisdiciton)*, Para. 52
[8] *Fedax v Venezuela (Jurisdiction)*, Para. 43

> 'investment', the fact that it falls within one of the categories listed in Article 1 does not transform into an 'investment'."[9]

10. Hence, it is indisputable that the term "investment" must be construed as containing an inherent economic meaning.

(b) The Award cannot be considered as an investment because it lacks the economic characteristics of the "*investment*"

11. The Award directed NHA to pay 40 million US dollars for damages to Claimant under a commercial arbitration award. Respondent submits that it is a one-time payment requirement, which lacks any of those economic characteristics of investment.

12. First, Claimant is the ultimate recipient of this sum of money, which means the money will be flowing outside, making no contribution to Mercuria. Second, it entails no risk in investment context. The tribunal of *Romak v Uzbekistan* held that:

> "[A]ll contracts – including contracts that do not constitute an investment – carry the risk of non-performance. However, this kind of risk is pure commercial…An 'investment risk' entails a different kind of alea, a situation in which the investor cannot be sure of a return on his investment, and may not know the amount he will end up spending, even if all relevant counterparties discharge their contractual obligations."[10]

13. It is clear that the risk held in the Award was merely a possibility that the counterpart may not perform its legal duty. Such risk is purely a commercial risk, because by the time the Award was decided, Claimant did not spend more, or did not need to spend more in their alleged investment. Therefore, it cannot be deemed as the risk in investment context.

(c) The Award shall not fall within the scope of investment under either Article 1(1)(c) nor Article 1(1)(e) of the BIT

[9] *Romak v Uzbekistan (Award)*, Para. 207
[10] *Ibid.*, Paras. 229-230

14. Claimant may argue that the Award falls within Article 1(1)(c) or Article 1(1)(e) of the BIT. However, in *GEA v Ukraine*, the tribunal, held that an arbitral award did not fall within such investment category by giving the following reason:

> "*the Award rules upon rights and obligations arising out of an investment does not equate the Award with the investment itself"*[11]

15. Furthermore, as a medicine supply contract, the Award involves no natural resource exploration or cultivation described in Article 1(1)(e) which expressly refers to "rights to search for, cultivate, extract or exploit natural resources". Therefore, arguments based on either Article 1(1)(c) or Article 1(1)(e) must fail.

16. In conclusion, because the Award lacks the required economic characteristics of the investment, it cannot be considered as an investment. Therefore, this tribunal lacks jurisdiction over any claims in relation to it.

(2) THE AWARD LACKS ANY TERRITORIAL LINK TO MERCURIA

17. Alternatively, assuming but not conceding that the Award contains those economic characteristics of investment, the Award still cannot be deemed as investment because it lacks the territorial link to its host state, Mercuria which is a prerequisite under Article 1(1) of the BIT.

18. Article 1(1) of the BIT provides that

> "[T]he term 'investment' means any kind of asset held or invested either directly, or indirectly through an investor of a third state, by an investor of one Contracting Party in the territory of the other Contracting Party in accordance with the latter's laws…"

19. Therefore, any alleged investment that may fall within the definition under Article 1(1) of the BIT shall be in conformity with two requirements, namely the "territorial link", includes that: it shall be made in the territory of the Contracting Party and in accordance with the laws of that Contracting Party. However, in the

[11] *GEA v Ukraine (Award)*, Para.162

current dispute, the Award lacks both of these two requirements.

20. According to the facts, the commercial arbitral award in the current dispute was rendered by a tribunal seated in Reef. Thus, the Award was in accordance with Reef's procedural law in the whole process of arbitration. By no means can the Award itself can be deemed as an investment under the BIT because it was made neither in the territory of Mercuria, nor entirely under the Mercuria's law.

21. Such rationale has been confirmed in the dissenting opinion of Jurisdiction and admissibility in the case of *Abaclat v Argentine Republic*, where Professor Georges Abi-Saab held that:

> "A territorial link is inherent in the concept of "investment" under the BIT, in which the whole idea was to encourage the flow of private foreign investment to developing countries by offering an international guarantee in the form of an alternative neutral adjudication of disputes arising out of such investment in the territory of the host States."[12]

22. He argued that because the alleged investment, the financial securities and their underlying debt, had their *situs* outside Argentina, lacks the territorial link with its host state, the alleged investment falls outside the ambit of jurisdiction of the Tribunal *ratione materiae.*

23. Accordingly, on the condition that the Award was not made in the territory of Mercuria, or in accordance with Mercuria's law, it cannot be deemed as an investment under Article 1(1) of the BIT.

(3) THE LTA CANNOT BE CONSIDERED AS AN INVESTMENT UNDER THE BIT

24. Claimant may further argue that the Award shall be deemed as a continuation or transformation of the original investment, the LTA. Accordingly, Respondent submits that the LTA in the current dispute cannot be deemed as an investment, as well and this argument must fail.

[12] *Abaclat v Argentine Republic (Dissenting Opinion on Jurisdiction)*, Paras. 73-74

25. In the current dispute, the LTA is virtually a sale-purchase contract. The rights and obligations under this contract are simply related to commercial transactions, directing the NHA to pay for the medicine supplied by Claimant. As Respondent submitted before, the investment shall entail three economic characteristics, all of which the LTA did not contain.

26. First, the LTA makes no contribution of asset to Mercuria. As a sales contract, it directed Claimant to supply medicine to NHA. At the very moment when Claimant sold those medicines, it immediately lost all legal ties of this subject matter, leaving no contribution to Mercuria. This notion is affirmed by the tribunal in *Italy v Cuba*. When looking at a long-term medicine supply contract, that tribunal stated:

> "Whatever the duration of the commercial relations of the parties, the sale of goods is incompatible with the notion of contribution, since the execution of the contract causes the seller to lose all legal ties with the thing sold, which is replaced in his patrimony by amount of money generally coming out of the country of the claimed investment."[13]

27. Second, the LTA lacks risk in investment context. The tribunals in *Romak v Uzbekistan* and *Italy v Cuba* both found that investment risk refers to the situation in which the investor cannot be sure of a return on his investment, and may not know the amount he will end up spending.[14] The mere risk of non-payment which is not "*attached to the success or failure of the operation of the legal framework"* under the LTA is thus precluded.[15]

28. Therefore, the LTA cannot be deemed as an investment. Thus, the Award will not be viewed as a continuation of investment accordingly.

(4) CONCLUSION

29. In conclusion, because neither the Award itself, nor the LTA can be deemed as an investment, this Tribunal lacks jurisdiction over claims in relation to the Award.

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[13] *Italy v Cuba (Interim Award)*, Paras. 197-219
[14] *Ibid.*, Paras. 198-219
[15] *Ibid.*

B. CLAIMANT CANNOT AVAIL ITSELF OF THE BENEFITS OF THE BIT BY VIRTUE OF APPLICATION OF ARTICLE 2 OF THE BIT

30. Article 2 of the BIT, serving as a denial of benefits clause, is designed to exclude from treaty protections nationals of third States which claim rights through so-called "mailbox" companies that have no economic connection to the state whose nationality is invoked.[16] In the case at hand, Claimant, as a mailbox company, is such a disqualified investor.

31. Given that (1) Respondent invoked Article 2 to deny Claimant benefits in a timely manner after the initiation of arbitration, and that since (2) Article 2 can be applied retrospectively thus to affect the current claims and that (3) the substantive conditions set in Article 2(1) are met, Respondent accordingly submits that Claimant cannot avail itself of the benefits of the BIT by virtue of application of Article 2 of the BIT.

(1) RESPONDENT INVOKED ARTICLE 2 TO DENY CLAIMANT BENEFITS IN A TIMELY MANNER AFTER THE INITIATION OF ARBITRATION

32. Respondent invoked Article 2 in its Response[17] to deny Claimant the BIT benefits. This invocation of Article 2 is in a timely manner because first, there is no express or implied time limits can be found in the BIT to bar the exercise of denial after the commencement of arbitration; second, the invocation time corresponds to *PCA Arbitration Rules.*

33. At first, according to Article 31 of *VCLT*, the current BIT should be read primarily based on its text. While looking through the specific language of Article 2 of the BIT, no specific language therein imposes any restriction on the time of denial which can be construed to demonstrate the intention of the parties at the time of conclusion of the BIT.[18] This reasoning was affirmed in *EMELEC v Ecuador*[19] *and*

[16] *Ampal-American and others v Egyp*t (Jurisdiction), Para. 125
[17] Response to the Notice of Arbitration, Para. 5
[18] Annex No. 1; BIT, Article 2

in Ulysseas v Ecuador[20], where the tribunals recognized that the respondent's denial of benefits upon raising the objections on jurisdiction was timely because Article 1(2) of the US-Ecuador BIT did not contain express language which required prior consultation or temporal restrictions. As the current BIT resembles the US-Ecuador BIT in the textual sense, the Respondent's prompt invocation of Article 2 in its first response to the notice after the initiation of arbitration is valid in time as well.

34. Furthermore, according to *PCA Arbitration Rules,* a jurisdictional objection must be raised not later than in the statement of defense.[21] By exercising the right to deny Claimant the BIT's advantages in the Response[22], Respondent has complied with the time limit prescribed by the *PCA Arbitration Rules*. In conclusion, Respondent invoked Article 2 to deny Claimant benefits in a timely fashion.

(2) ARTICLE 2 CAN BE APPLIED RETROSPECTIVELY THUS TO AFFECT THE CURRENT CLAIMS

35. Respondent contends that because (a) retrospective application of Article 2 will not frustrate the legitimate expectations of investors, and (b) retrospective application of Article 2 is in line with the purpose of the denial of benefits clause, it can be applied retrospectively.

(a) Retrospective application of Article 2 will not frustrate the legitimate expectations of investors

36. Respondent asserts that sufficient information has already been provided to the investors when the BIT was made available to the public within which a clearly-drafted denial of benefits clause was present, and therefore retrospective application of denial of benefits clause will not frustrate the legitimate expectations Claimant relied on.

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19 *EMELEC v. Ecuador (Award),* Para. 71; US-Ecuador BIT, Article 1(2)
20 *Ulysseas v Ecuador (Interim Award),* Para. 172
21 *PCA Arbitration Rules,* Article 23.2
22 Response to the Notice of Arbitration, Para. 5

37. In *Ulysseas v Ecuador*[23], the tribunal held *"the protection afforded by the BIT is subject during the life of the investment to the possibility of a denial of the BIT's advantages by the host State"* and therefore there was no valid reasons to exclude retrospective effects. In addition, many scholars criticized the reasoning that the denial of benefits clause should not have retrospectivity. They find since having retrospective effect of denial of benefits clause would *"benefit the long-term cooperation between contracting parties by encouraging investors to be upfront about ownership, nationality and citizenship"* [24], it is unconvincing to argue that retrospective application will sabotage investors' legitimate expectations and hinder the certainty of legal framework.

38. It is Claimant itself, while knowing the specific conditions contained in the treaty, that has "opted to use an investment vehicle"[25] controlled by a company of a third country, which has no substantial business activities in the territory of the Contracting Party.[26] In conclusion, as *"the possibility for the host State to exercise the right in question is known to the investor from the time when it made its the investment"*[27], to render Article 2 applicable retrospectively is no frustration of legal certainty or legitimate expectations on part of the investors.

(b) Retrospective application of Article 2 is in line with the purpose of the denial of benefits clause

39. Furthermore, retrospective application of Article 2 is in line with the purpose of the denial of benefits clause in general. The tribunal in *Guaracachi v Bolivia* stated that:

> "the very purpose of the denial of benefits is to give the host states the possibility of withdrawing the benefits granted under the BIT to investors who invoke those benefits".[28]

40. In reality, the time of withdrawing is most likely the moment when the host state

[23] *Ulysseas v Ecuador (Interim Award)*, Para. 173
[24] *Chalker*, p. 17; *Mistelis/Baltag*, p. 1321
[25] *Guaracachi v Bolivia (Award)*, Para. 383
[26] *Ampal-American and others v Egypt (Jurisdiction)*, Para. 97
[27] *Ulysseas v Ecuador (Interim Award)*, Para. 173
[28] *Guaracachi v Bolivia (Award)*, Para. 376

discerns that these investors are only free riders attempting to get treatment provided by the BIT when it is sued against by those investors in a potential investment arbitration.[29]

41. Thus, if Article 2 cannot be applied retrospectively, states are left with no choice but to investigate all investors entering into its territory,[30] which is contrary to the promotion of foreign investments, but are also impossible to carry out.[31] In addition, the fulfilment of the aforementioned requirements is not static, which means it is only when a dispute arises that Respondent will be able to assess whether such requirements are met and decide whether it will deny the benefits of the treaty in respect of that particular dispute.[32]

42. As such, for the efficacy of the denial of benefits clause, it is proper that the application of Article 2 can be retrospective thus the denial is allowed to be "*activated*" when the benefits are being claimed.[33]

(3) THE SUBSTANTIVE CONDITIONS OF ARTICLE 2 ARE MET

43. Article 2 of the BIT provides in relevant part that an investor may be denied the BIT benefits if it is:

> "a legal entity, *if* citizens or nationals of a third state own or control such entity *and if* that entity has no substantial business activities in the territory of the Contracting Party in which it is organized…"

44. Respondent contends that the burden of proof of establishing the two cumulative substantive conditions contained in Article 2 is primarily on Claimant since it is in exclusive possession of necessary documents concerning its corporate structure.[34] In light of this, Respondent argues that the substantive conditions in Article 2 are met for (a) Claimant is owned and controlled by citizens or nationals of a third state; and (b) Claimant has no substantial business activities in Basheera.

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[29] *Essig*, p. 13
[30] *Kinner/Fischer/Almeida/Torres/Bidegain*, p. 472
[31] *Mistelis/Baltag*, pp. 78-82
[32] *Guaracachi v Bolivia (Award)*, Paras. 378-379
[33] *Ibid.*, Para. 376
[34] *Plama v Bulgaria (Jurisdiction)*, Para. 82

(a) Claimant is owned and controlled by citizens or nationals of a third state

45. Affirmed by the numerous tribunals when interpreting denial of benefits clauses which are almost identical to Article 2 of the current BIT, *"ownership"* should be deemed to include both *"indirect and beneficial ownership"* and *"control"* can mean *"control in fact"*.[35] In addition, in *Mobil v Venezuela*[36], the tribunal held on condition that 100 % of the share capital is owned by a non-party's company, the "control test" would be satisfied and it was not necessary to consider whether such control was exercised in fact.

46. In the current case, Claimant is a wholly-owned subsidiary of its parent company, AB and Group whose primary holding company is of Reef nationality.[37] Claimant's business strategy is under significant influence of AB and Company that it serves as the vehicle for carrying on business for it in South America and Africa.[38] Further, the shares of Claimant are currently held by AB Group affiliates, which are all ultimately controlled by AB and Company.[39]

47. Analogous to numerous similar findings in *Pac Rim*[40] and *Guaracachi*[41] where the tribunals held that the first condition of the denial of benefits clause is met since those investors were owned and ultimately controlled by companies of non-party nationality. In addition, in it is evident that Claimant is owned and controlled by Reef nationals, namely AB and Company, to render the first substantive condition satisfied.

(b) Claimant has no substantial business activities in Basheera

48. Respondent further submits that Claimant has no substantial business activities in the territory of Basheera. There is no unified standard for "substantial business

[35] *Plama v Bulgaria (Jurisdiction)*, Para. 170; *Aguas del Tunari v Bolivia (Jurisdiction)*, Paras. 233-234
[36] *Mobil v Venezuela (Jurisdiction)*, Para. 160
[37] Facts, p. 28, Para. 4
[38] *Ibid.*
[39] PO2, Para. 3
[40] *Pac Rim v El Salvador (Jurisdiction)*, Para. 4.82
[41] *Guaracachi v Bolivia (Award)*, Para. 370

activities" since it is a fact-specific issue. However, *Jagusch* and *Sinclair* find "substantial business activities" exist when the company is: engaged in buying, selling, and contracting in that territory beyond the normal activities or functions required merely by the fact of its corporate existence.[42] Besides, in *Guaracachi v Bolivia*, the tribunal held that the activities of denied investors must be examined along with looking to the purpose for its incorporation and its function in the structure its business group.[43]

49. First, in the current case, it is evident that Claimant incorporated in Basheera merely for taking treaty benefits of nationality, which reflected in the fact that Claimant was incorporated only 3 months after the BIT was assigned and its principal dealing was doing business surrounding LTA with NHA directed by Mercuria's government. Since "denial of benefits" clause can be viewed as a way of States tackling the abusive treaty shopping trend,[44] Claimant merely maintained the disguise of Basheera nationality to gain undeserved benefits for its foreign business which is in nature abusive.[45]

50. Second, the function of Claimant in the entire structure of AB Group is to serve as a "special purpose vehicle" (SPV) to manage patents in foreign jurisdictions and to provide support for its parent company—AB Group. [46] The fact that the Claimant had office, bank account and employees can only prove Claimant has a minimal presence in Basheera. Besides, the activities as a "patent holder" did not originate as part of the Claimant's own activities in Basheera and did not contribute to Basheera's economy, and therefore these limited activities fall short of the threshold of having its own substantial business activities in Basheera.[47]

51. Thus, given that the denial of benefits clause corresponds closely to the principle of reciprocity in public international law to guarantee that free riders without genuine

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[42] *Sinclair/Jagusch*, p. 20
[43] *Guaracachi v Bolivia (Award)*, Para. 368
[44] *Nikièma*, p.12; *Gastrell/Le Cannu*, p.81
[45] *Kirtley*, p. 438
[46] Facts, p. 28, Para. 4
[47] *Guaracachi v Bolivia (Award)*, Para. 369; *Pac Rim v El Salvador (Jurisdiction)*, Para. 4.72; *Sinclair/Jagusch*, p. 20

economic link to the BIT parties are excluded.[48]

(4) CONCLUSION

52. In conclusion, Respondent submits that (1) it invoked Article 2 to deny Claimant benefits in a timely fashion after the initiation of arbitration, and (2) Article 2 should be considered to have retrospective effect and eventually that (3) the substantive conditions set in Article 2(1) are met. Given the above, Respondent asserts that Claimant cannot avail itself of the benefits of the BIT by virtue of application of Article 2 of the BIT and all of its claims should be rendered inadmissible.

C. THE ENACTMENT OF LAW NO. 8458/09 AND THE GRANT OF A LICENSE FOR THE CLAIMANT'S INVENTION DO NOT AMOUNT TO A BREACH OF THE BIT

53. Respondent argues that Claimant's claims under this issue shall fail because (1) Claimant did not exhaust local remedies. Further, Respondent did not violate substantive provisions of the BIT. Notably, (2) Respondent did not expropriate Claimant's investments; and Respondent did not breach (3) the fair and equitable treatment or (4) other requirements of the BIT.

(1) CLAIMANT DID NOT EXHAUST LOCAL REMEDIES

54. Respondent contends that investment tribunals shall not serve as "*an appellate tier…of the national judiciary*" and shall only review the decision made by domestic courts with "*clear evidence of egregious and shocking conduct*".[49] Mercurian Court granted the license in conformity with the domestic law and "*residual discretionary powers*",[50] and "*Mercuria's law provides the patent holder the possibility to question the validity of the non-voluntary license and the royalty*".[51] Given the lack of egregious and shocking conduct, after **7** years, Claimant cannot raise claims under this issue when it chose not to seek local remedies.

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[48] *Gastrell/Le Cannu*, p. 81; *Sornarajah*, p. 218. *Shaw*, p. 7
[49] *Eli Lilly v Canada (Final Award)*, Paras. 224-225
[50] PO2, Para. 5
[51] PO3, lines 1578-1580

(2) RESPONDENT DID NOT EXPROPRIATE CLAIMANT'S INVESTMENT

55. By the enactment of Law No. 8458/09 and the grant of a license to HG-Pharma for Claimant's Mercurian Patent No. 0187204, Respondent did not commit expropriation, either (a) directly or (b) indirectly. Alternatively, (c) by virtue of Article 6(4) of the BIT, the challenged measures did not constitute indirect expropriation. Therefore, Respondent did not breach Article 6.

(a) Respondent did not directly expropriate Claimant's investment

56. Claimant's relevant investment under Article 1(1) of the BIT is its patents. The establishment of direct expropriation requires the "*formal transfer of the title of ownership*"[52]. After the involuntary licensing, Claimant still had the rights over its patent. Respondent did not take any title of Claimant and thus did not directly expropriate Claimant's investment.

(b) Respondent did not indirectly expropriate Claimant's investment

57. An indirect expropriation will "*be assumed in the event of a 'substantial deprivation' of an investment*"[53], which requires the inability of use and the loss of control of an investment.[54] A loss of benefit or "*reasonably-to-be-expected economic benefit*" could be one result of substantial deprivation of use or control, but not the indirect expropriation *per se*.[55]

58. The fact that Claimant withdrew from the Sanior market did not establish deprivation of use, because Claimant's activities were not blocked as a whole.[56] After the grant of the license, because Claimant "*was able to service its customers*", it still "*had the control and use of its property*".[57]

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[52] *El Paso v Argentina (Award)*, Para. 265
[53] *Dolzer/Schreuer*, p. 153
[54] *El Paso v Argentina (Award)*, Para. 245; *Fireman's Fund v Mexico (Award)*, Para. 176(c)
[55] *Waste Management v Mexico II (Award)*, Para. 159; *El Paso v Argentina (Award)*, Paras. 249-250.
[56] *Waste Management v Mexico II (Award)*, Para. 157
[57] *Ibid.*, Para. 159

59. In any event, the economic value of Claimant's investment was not substantially deprived. In *Philip Morris v Uruguay*, the tribunal found since the intellectual property legislation affected all trademarks of the claimant, the trademarks should be examined as a whole investment.[58] Similarly, since the new legal framework affected Claimant's various patents and Claimant with various patent products was still profitable, its investment was not substantially deprived.

60. As such, Claimant was not substantially deprived of the use and value of its investment and Respondent did not indirectly expropriate Claimant's investment.

(c) Respondent did not conduct expropriation under Article 6(4) of the BIT

61. Alternatively, Respondent contends that its acts did not constitute indirect expropriation under Article 6(4), which reads:

> "Non-discriminatory measures… applied to protect legitimate public welfare objectives, such as public health… do not constitute an indirect expropriation".

62. Under Article 6(4), there was no indirect expropriation because Respondent conducted (i) in pursuit of the welfare of public health and (ii) on a non-discriminatory basis.

(i) Respondent's conduct was in pursuit of the welfare of public health

63. Respondent "except in situations of blatant misuse of the power",[59] can determine whether a measure serves a public purpose,[60] which only requires a measure to have "*a reasonable nexus with the declared public purpose*".[61]

64. *ICESCR Convention*, to which Mercuria and Basheera are members,[62] recognizes "the right of everyone to the enjoyment of the highest attainable standard of physical and mental health." Respondent adopted the two challenged measures to fulfill its

[58] *Philip Morris v Uruguay (Award)*, Paras. 283-286
[59] *Vestey v Venezuela (Award)*, Para. 294
[60] *Crystallex v Venezuela (Award)*, Para. 712
[61] *Ibid.*, Para. 296
[62] PO3, lines 1565-1566

obligation to provide Mercurian citizens with universal access to affordable drugs. The challenged measures made a great success to safeguard public health and shall be deemed as applied for public welfare.

(ii) Respondent conducted on a non-discriminatory basis

65. Respondent contends that it adopted the two measures on a non-discriminatory basis. To claim otherwise, the burden is on Claimant to prove "*different treatment in similar circumstances without reasonable justification, typically on the basis of its nationality*."[63] However, Claimant cannot establish the cumulative conditions.

66. First, there were no eligible comparators. Discrimination can arise only if the circumstances allow the comparison of two similar situations.[64] Claimant fails to prove that there was any third party whose patent was applied for an involuntary license with more favorable treatment.

67. Claimant was not in similar situations with HG-Pharma and its shareholders. Being in the same sector is not sufficient to prove similar situations when financial terms and other conditions were different.[65] Claimant is a private entity seeking profits while 50% of HG-Pharma's shares are owned by the State and HG-Pharma supplies affordable drugs to fulfill its non-commercial public function.[66] Thus, there were no eligible comparators.

68. Second, there was no discriminatory effect against Claimant's nationality, without which discrimination cannot be established.[67] In *Eli Lilly v Canada*, the tribunal found that the claimant's patent being invalidated by the new patent act was rational because the Canadian legal system historically and necessarily evolves. Although since 2005, only foreigners' pharmaceutical patents had been invalidated, this was not sufficient to conclude discrimination.[68]

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[63] *Crystallex v Venezuela (Award)*, Para. 715; *Kinner/Fischer/Almeida/Torres/Bidegain*, p. 391
[64] *Kinner/Fischer/Almeida/Torres/Bidegain*, pp. 391-392; *Lemire v Ukraine (2010 Decision on Jurisdiction and Liability)*, Para. 392
[65] *Bayindir v Pakistan (Award)*, Para. 402; *Parkerings v Lithuania (Award)*, Paras. 88-91
[66] PO3, p. 50, lines 1591-1597
[67] *Siag v Egypy (Award)*, Para. 439
[68] *Eli Lilly v Canada (Final award)*, Paras. 418, 441

69. Similarly, the Mercurian legal system evolved to safeguard the public interest. The fact that Claimant was a foreign investor did not make the involuntary licensing of its patent discriminatory. Even if Claimant was the only one whose patent was licensed, it could not predict that there would not be other patents being licensed.[69] Therefore, Respondent did not discriminate against Claimant.

70. In conclusion, Respondent did not expropriate Claimant's investments in breach of Article 6.

(3) RESPONDENT DID NOT VIOLATED OBLIGATIONS OF FAIR AND EQUITABLE TREATMENT WITH REGARD TO CLAIMANT'S INVESTMENT

71. Respondent contends that it did not violate fair and equitable treatment ("**FET**") in breach of Article 3(2) of the BIT. Respondent submits that (a) Claims under FET shall be examined with the international minimum standard of protection. Furthermore, (b) Respondent did not frustrate Claimant's legitimate expectation, and (c) Claimant cannot establish violations of FET by its claims under *TRIPS Agreement*.

(a) Claims under FET shall be examined with the international minimum standard of protection

72. Respondent contends that the standard of FET refers to the international minimum standard, which is recognized by customary international law,[70] and also by tribunals that adopted an autonomous standard.[71] Under the international minimum standard of protection, a violation of FET requires a measure to be:

[69] *Glamis Gold v USA (Award)*, Para. 796
[70] *Rumeli Telekom v Kazakhstan (Award)*, Para. 611; *Duke Energy v Ecuador (Award)*, Para. 337; *Saluka v Czech Republic (Partial Award)*, Para. 291
[71] *Jan de Nul v. Egypt (Award)*, Paras. 187 and 192-194; *EDF v. Romania (Award)*, Para. 216; *Azurix v Argentina (Award)*, Paras. 368-370

> "sufficiently egregious and shocking… a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due process, evident discrimination…"[72]

73. In non-NAFTA cases such as *Genin v Estonia*, tribunals found that FET standard is "*indeed, an international minimum standard*" although the relevant FET clause did not directly refer to customary international law.[73] Similarly, without an express provision otherwise, Claimant's claims shall be examined under the minimum standard.

74. To contend a different standard, the burden is on Claimant to show that state practice and *opinio juris* have shown been established.[74] In any event, all of its claims shall fail.

(b) Respondent did not frustrate Claimant's legitimate expectation

75. The establishment of legitimate expectations has three requirements: specific assurance, reasonable expectation, and inducement of investment by the assurance.[75] Respondent contends that none of these requirements has been satisfied, and that without a stabilization clause, the expectation that the Mercurian legal framework would not change is not protected by the BIT.

(i) The BIT does not provide stabilization clause

76. As affirmed by the tribunals in *Total v Argentina*[76] and *Parkerings v Lithuania*[77], without a specific stabilization clause in the BIT or a specific promise, states' power to change legislation is not prevented by FET standard. The BIT does not contain a stabilization clause and Respondent never gave a specific promise of that kind.

77. Further, the general rules in domestic legislation *per se* do not imply the

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[72] *Ibid*., p. 273
[73] *Genin v Estonia (Award)*, Para. 9, 367
[74] *Glamis Gold v USA (Award)*, Para. 601
[75] *Micula v Romania (Final Award)*, Paras. 668-669; *Saluka v Czech Republic (Partial Award)*, Para. 304; *Glamis Gold v USA (Award)*, Para. 766
[76] *Total v Argentina (Liability)*, Para. 164
[77] *Parkerings v Lithuania (Award)*, Para. 332

immobilization of legal system.[78] Although Respondent did not adopt legislation of involuntary licenses before 2009, Claimant cannot rely on this to expect that Respondent would not change its legal framework or not grant an involuntary license.

78. Similarly, international treaties such as *TRIPS Agreement* cannot be the ground of Claimant's legitimate expectation. Even WTO members cannot rely on the alleged legitimate expectations resulting from *TRIPS Agreement*,[79] let alone Claimant, to whom Respondent has no obligation under *TRIPS Agreement*.[80]

(ii) Respondent did not induce Claimant's investment by a specific assurance

79. Respondent contends that legitimate expectations can only arise at the time the investment is made and the Claimant cannot rely on events afterwards.[81] Claimant's affected investment in this dispute is its patent. However, the patent was assigned to Claimant early in **1998**, years before the statement of Mercurian Minister of Health and the tweet of Mercurian President in **2004**. Apparently, Claimant could not be induced to invest by events that took place after its investment had already been made. Therefore, the said statement and the tweet cannot be deemed as assurance in the first place.

80. Further, the statement of Minister of Health and the tweet of Mercurian President were not specific to Claimant. First, the statement of Minister of Health did not give any specific promise to Claimant at all. The Minister only emphasized that Mercuria would "empower and engage right holders", rather than merely Claimant, to "pave the way forward and secure access to healthcare for all."[82] In addition, the President's tweet was posted towards "over 40 million" followers,[83] which could by no means give an assurance to Claimant. Moreover, the President's tweet only alleged to "do away with red tape"[84], which meant to simplify the paperwork, rather than to give

[78] *El Paso v Argentina (Award)*, Para. 394
[79] *India – Patents Appellate Body Report*, Paras. 33-42
[80] *Ruse-Khan*, p. 254
[81] *LG&E v Argentina (Award)*, Para. 130; *Tecmed v Mexico (Award)*, Para. 154; *BG v Argentina (Award)*, Paras. 297-298
[82] Annex No. 2, lines 1270-1271
[83] PO3, line 1568
[84] Facts, p. 29, Para. 8

priorities to Claimant.

(iii) Claimant's expectation was not reasonable

81. Respondent contends that Claimant's expectation that its patent would not be granted was unreasonable in the situation of severe prevalence of greyscale. The reasonableness should be examined in the social contexts,[85] such as the increasing awareness of environmental protection.[86]

82. When Claimant made its investment in 2004, after the 2003 annual report on health had already predicted a national greyscale crisis and the lack of mass production of medicines.[87] It is reasonable that Claimant should have anticipated that Respondent might take necessary measures such as the grant of a compulsory license. To have an expectation that Respondent would not take any measure when there was no effective treatment for greyscale,[88] could by no means be reasonable.

(iv) Respondent acted within its legitimate power

83. In any event, Respondent contends that it acted within its regulatory powers. The test for the frustration of investor's expectation is "whether government measures [have] exceed[ed] normal regulatory powers…beyond an acceptable margin of change".[89]

84. Greyscale is incurable and causes "*progressively stiffening muscles, swollen limbs, and severe joint pain*" to working age individuals.[90] In 2006, confirmed patients increased to **13** times as in 2003.[91] Unfortunately, the greyscale drugs would cost annually USD 10,000.[92] According to World Development Indicator 2011 published by the World Bank, the treatment of greyscale would cost around 80% of the total

[85] *Duke Energy v Ecuador (Award)*, Para. 340; *Micula v Romania (Final Award)*, Para. 669
[86] *Glamis v USA (Award)*, Para. 767
[87] Facts, p. 28, Para. 6
[88] PO3, lines 1583-1584
[89] *El Paso v Argentina (Award)*, Para. 402
[90] Annex No. 3, lines 1330-1332
[91] *Ibid*.
[92] *Ibid*., line 1354

annual income ($12,196) of a citizen from high income countries, which is absolutely unaffordable to people in Mercuria, a developing countries.

85. Before the compulsory license, as affirmed by the medical consensus, there was no available treatment for greyscale for at least **2** years.[93] In such a severe emergency, no investor could enjoy such a privilege to be excluded from the exercise of legitimate regulatory power.[94]

86. As such, Respondent did not frustrate any legitimate expectation protected by the BIT.

(c) Claimant cannot establish violations of FET by its claims under *TRIPS Agreement*

87. Respondent contends that (a) Claimant cannot raise violations of *TRIPS Agreement* before investment tribunals. Even taking *TRIPS Agreement* as reference, Respondent contends that it has not violated the BIT by violating any (b) procedural or (c) substantial provisions of *TRIPS Agreement*, notably Article 31.

(i) Claimant cannot raise violations of *TRIPS Agreement* before investment tribunals

88. First, Respondent argues that, *TRIPS Agreement* is not the applicable law in this dispute. According to Procedural Order No. 1, the only governing law herein is the BIT.[95]

89. Second, Claimant cannot incorporate provisions of *TRIPS Agreement* into the BIT by Article 3(2), Article 3(3), or Article 4. Given that *TRIPS Agreement* only provides obligations among the member states, the FET clause, umbrella clause, most favorable treatment clause cannot serve as a vehicle for any general claims based on

[93] PO3, lines 1583-1584; Facts, p. 30, Paras. 17 and 21
[94] *El Paso v Argentina (Award)*, Para. 401
[95] PO1, Para. 11

domestic or international law.[96] Neither does the *pacta sunt servanda* rationale apply.[97]

90. In addition, according to *Doha Declaration*, to which Respondent and Claimant's home state are members[98], Respondent enjoys significant flexibilities to interpret and implement *TRIPS Agreement* "*in a manner supportive of WTO Members' right to protect public health and, in particular, to promote access to medicines for all*".[99] This position was restated by WTO General Council in 2003.[100]

(ii) Respondent has not violated procedural provisions of *TRIPS Agreement*

91. Respondent has the autonomy to decide the grounds for granting involuntary licenses as affirmed by *Doha Declaration*.[101] Respondent contends that it granted the involuntary license in conformity with domestic laws and *TRIPS Agreement*, as shown in the Procedural Order No. 2:

> "The Court determined the non-voluntary license terms by interpreting the provisions of Section 23 C and exercising its residual discretionary powers."[102]

92. The relevant provisions are set forth in Article 31 of *TRIPS Agreement*, none of which have been violated. On the ground of non-commercial public use, the prior negotiations could be exempted.[103] In proceedings, "Atton Boro was impleaded as a party"[104] before Mercurian court. Thus the requirement of notification under Article 31(b) was satisfied.

93. In terms of the involuntary license, it was granted with the examination of "its individual merits"[105], and would expire when "greyscale was no longer a threat to

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[96] *Grand River v USA (Award)*, Para. 219*; Ruse-Khan*, pp. 258-263;
[97] *Ruse-Khan*, pp. 260-263
[98] PO2, Para. 2
[99] *Doha Declaration*, Para. 4
[100] *WTO's 2003 Decision*, Para. 9
[101] *Doha Declaration*, Para. 5
[102] PO2, Para. 5
[103] *TRIPS Agreement*, Article 31(b)
[104] PO3, line 1576
[105] *TRIPS Agreement*, Article 31 (a)

public health in Mercuria"[106], with the requirements of scope and duration in Article 31(c) satisfied. Also, the license is "non-exclusive"[107] and "non-assignable"[108]. Mercurian legislation further provides the possibility to "question the validity of the non-voluntary license and the royalty"[109] and therefore requirements of judicial review are satisfied.[110]

(iii) Respondent has not violated substantial provisions of *TRIPS Agreement*

94. First, Respondent has granted an adequate royalty in conformity with Article 31(h) of *TRIPS Agreement*. However, Claimant did not receive the royalty because it failed to provide the bank details.[111] The royalty of 1% of HG-Pharma's revenues is adequate under the reasonable standard adopted in Mercuria. In 2009-2010, to tackle other "*incurable, non-fatal diseases*" similar to greyscale, the royalty rates "*ranged from 0.5% to 3%*" and there was no dispute resulting from these decisions.[112]

95. Moreover, the royalty rate was also supported by the international practice. Lower royalties have been adopted by many developing countries such as Thailand and Indonesia to tackle diseases and be recognized as adequate remunerations.[113] In 2011, the year after the involuntary license was granted to HG-Pharma[114], UNCTAD pointed out: that "*[r]oyalty rates have differed widely in relation to non-voluntary licenses*"; that it could be "*as low as 0.01% (in the United States)*"; and that "*a 0.5% royalty rate may actually be an adequate rate of remuneration*."[115] For a developing country, the royalty rate is absolutely reasonable.

96. Second, the requirement of Article 31(f) that the use of the generic drugs was predominantly for domestic market was not violated. "*HG-Pharma did not export*

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[106] Facts, p. 30, Para. 21
[107] *TRIPS Agreement*, Article 31(d)
[108] *Ibid*, Article 31(e)
[109] PO3, lines 1578-1579
[110] *TRIPS Agreement*, Article 31(g), (i) and (j)
[111] PO3, lines 1598-1599
[112] *Ibid.*, lines 1588-1590
[113] *Indonesia Report*, p. 21
[114] Facts, p. 30, Para. 21
[115] *Indonesia Report*, p. 21

Valtervite".[116] After the first sale from HG-Pharma, the patent rights on the exported drugs have already been exhausted. The fact that the drugs were produced under an involuntary license could not change the question of exhaustion because Claimant has already been granted compensation in the form of a royalty.[117]

97. In addition, according to the wording of "predominantly", Article 31(f) only prohibits "recurrent and regular exports" rather than "one or two isolated cases of parallel exports".[118] Whether or not the patent is protected in the three neighbor countries, the export in a small quantity is allowed under Article 31.[119]

(4) ESPONDENT DID NOT BREACH OTHER PROVISIONS OF THE BIT

98. As stated above in the arguments of expropriation, Respondent did not violate the requirements of non-discrimination. Also, Respondent did not violate the requirements of due process and of transparency because Mercurian legal system provides accessible remedies to Claimant without any ambiguity,[120] and Respondent observe all domestic and international requirements.[121]

99. In addition, the two measures adopted by Respondent were reasonable, as supported in the arguments of expropriation. After 2 years of no access to medicines, there is a linkage between the measures and the purpose to safeguard public health, thus the measures were reasonable.[122]

(5) CONCLUSION

100. In conclusion, by the challenged measures, Respondent did not expropriate Claimant's investment, and did not violate FET and other obligations. Respondent did not breach the BIT, notably Articles 3 and 6.

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[116] PO2. Para. 5
[117] *Correa*, p. 85
[118] *De Carvalho*, pp. 416-417
[119] *Correa*, p. 85.
[120] PO3, lines 1578-1580; *Metalclad v Mexico (Award)*, Para. 76
[121] PO2, Para. 5
[122] *AES v Hungary (Award)*, Para. 10.3.7

D. MERCURIA IS NOT LIABLE UNDER THE BIT FOR THE CONDUCT OF ITS JUDICIARY IN RELATION TO THE ENFORCEMENT PROCEEDINGS.

101. Respondent submits that (1) Claimant failed to abide by the prerequisite element of exhaustion of local remedies, (2) Mercuria's judicial conduct does not constitute denial of justice; (3) Claimant cannot raise claims under effective means; and, (4) Respondent did not violate requirements of full protection and security.

(1) CLAIMANT FAILED TO ABIDE BY THE PREREQUISITE ELEMENT WHICH IS EXHAUSTION OF LOCAL REMEDIES

102. Respondent submits that exhaustion of local remedies is the prerequisite element to "*claim a judicial act is in violation of international law*".[123] As stated in *Loewen v USA*, the availability of the whole judicial system should be examined before establishing a violation of FET.[124] Respondent submits that Claimant's proceedings only covered part of Mercurian whole trial system, and Respondent should be given opportunity to remedy the default, if there's any, in the lower court before being accused of violation of international obligation.

(2) MERCURIAN SUPREME COURT'S CONDUCT IS NOT ARBITRARY AND IS NOT IN VIOLATION OF FET

103. Alternatively, Respondent submits that (a) the test to establish violation of national courts is a high threshold, (b) Mercurian courts conduct was reasonable and justifiable, and (c) the delay is reasonable and justifiable.

(a) The test to establish violation of national courts is a high threshold

104. As stressed by the tribunal in *Eli Lily v Canada*, the international tribunal "*is not the appellate tier in respect of the decision of the national judiciary*".[125] Rather, the *Eli Lily* tribunal contended that "only be in very exceptional occasions, in which

[123] *Loewen v USA (Award)*, Para. 167
[124] *Ibid.*, Para. 137
[125] *Eli Lily v Canada (Final Award)*, Para. 224

there's clear evidence of egregious and shocking conduct, that it will be appropriate for a [international] tribunal to assess such conduct against the obligations of the respondent State" under obligations of FET, such as denial of justice.[126]

105. This position is endorsed by various tribunals.[127] Therefore the standard to find the violation of obligation by a state's national courts is stringent and high.

(b) The Mercurian High Court's conduct is reasonable and justifiable

106. Respondent submits that the Mercurian Supreme Court's deviation from its previous decision is understandable under the context of national judicial reform.

107. Mercuria is a developing country with an overburdened judicial system and limited judicial resources.[128] To accelerate the efficiency of commercial affairs and promote investment, Respondent passed the 2012 Commercial Courts Act, as many countries did to reform its judiciary.[129] As stated in *Eli Lily v Canada*, "i*nternational tribunal is not the appellate tier of national court*", and "*considerable deference*" should be given to the decisions and conducts of domestic courts.[130] In this reformation context, the deviation of national courts is a just exercise of national judicial power.

108. India, for instance, also went through similar periods to clarify the jurisdiction of its newly set up commercial benches during 2009 to 2015, where cases were being constantly transferred back and forth.[131] Notably, over an identical issue of jurisdiction concerning foreign affairs, the same Indian court once made two completely contradictory decisions within just 10 days in 2015.[132] After that, international society, however, regarded this chaotic period reasonable and understandable, and the World Bank's report *Doing Business 2017* even applauded that India "*have embarked a fast-paced reform path*" and "*established effective*

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126 *Ibid.*
127 *Mondev v USA*(Award), Para. 127
128 Response to Notice of Arbitration, Para. 9
129 *Doing Business Report 2009*, pp. 51-52
130 *Eli Lily v Canada (Final Award)*, Para. 224
131 *Sulabh/Poorv*, Para. 78
132 *Roger v Mukesh*; *Ascot v Bon Vivant Life Style*

mechanisms for addressing commercial cases."[133] Similarly in this case, Mercurian court system cannot be perfected overnight. The process of refinement needs time just as every mature system once did. This was far from an egregious and shocking failure of judicial propriety, but exactly what it takes to make a better system. Therefore, Mercurian Supreme Court's conduct is justifiable.

(c) The delay of the enforcement proceedings is reasonable and justifiable

109. Respondent contends that delay of court proceedings *per se* does not constitute violations of the BIT. In *Toto v Lebanon*, the tribunal stated that "*it has to be conceded that international law has no strict standards to assess whether court delays are a denial of justice*."[134] As ruled in *White v India*, the assessment of whether a judicial delay amounts to a denial of justice is highly fact-sensitive and five factors need to be taken into consideration: the complexity of the proceedings, the need for swiftness, the behavior of the litigants involved, the significance of the interest at stake and the behavior of the courts themselves.[135]

(i) The enforcement proceedings are complex and involved significant interest

110. Respondent submits that the enforcement proceedings are complex due to its public policy concern. As Article V(2)(b) of *New York Convention* states, enforcement of arbitral award could be refused if it was contrary to the public policy.[136] As a party to the *New York Convention*, Mercuria was allowed to consider the merits of the award based on the defense of public policy by NHA, which made the enforcement proceedings more complex than normal procedure mechanism.[137]

111. Further, as ruled in *Frontier v Czech Republic*, public policy in Article 5(2)(b) of *New York Convention* referred to "*national conception of international public policy*", and that "*States enjoy a certain margin of appreciation in determining what*

[133] *Doing Business Report 2017*, p. 26, Para. 2
[134] *Toto v Lebanon (Jurisdiction)*, at Para. 155
[135] *White v India (Final Award)*, Para. 10.4.10
[136] *New York Convention*, Art. 5 (2)(b)
[137] *UNCITRAL Guidelines for New York Convention*, p. 248

their own conception of international public policy is".[138] Public health is obviously included in the normal conception of public policy.

(ii) The enforcement proceedings were not urgent

112. In *White v India*, in considering White Industry's enforcement award concerning 4 million USD, the tribunal ruled that the need for swiftness is less urgent for such kind of purely commercial matters because it is not a criminal or human right award.[139] In this case, the award ruled in Reef is also a purely commercial matter and is nothing more than pecuniary benefits for a commercial business company. Besides the Mercuria patent for Valtervite, Claimant still possesses a number of other patents.[140] Therefore, as a large international company, Claimant could still survive and maintain business in the market without the swift and alleged damages of enforcement. In conclusion, the enforcement proceedings lack the need for swiftness.

(iii) The behavior of the litigants involved

113. Respondent submits first that according to the rule of attribution under international law, NHA's behavior is not attributable to Respondent, as will be discussed in more detail in issue E.[141] Further, Respondent argues that the extension of the proceeding does not solely result from NHA. Atton Boro also asked for extension and it was Atton Boto which sough amicable settlement which further delayed the proceedings.[142] Moreover, Respondent submits that NHA's conduct did not seriously procrastinate the proceeding or violated procedural requirements. NHA tendered formal apologies to the court for its absence.[143] NHA had also submitted the joinder and rejoinder as required, give response on time during the hearing.[144] Therefore, the delay of the enforcement proceeding is the result of both sides of litigants.

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[138] *Frontier v Czech Republic (Final Award)*, Para. 527
[139] *White v India (Final Award)*, Para. 3.2.33, 10.4.14
[140] Facts, p. 31, Para. 25
[141] Issue E, Para. 125
[142] Exh. 1, Paras. 10, 43
[143] *Ibid*., Para. 22
[144] *Ibid.*, Paras. 10, 22, 23, 32

(iv) The behavior of the courts themselves

114. As the tribunal in *White v India* provided, "*international law does not provide fixed time limits within which certain classes of cases must be resolved*."[145] In *White v India* , even 10 years of delay was not considered a violation of FET.[146] In this case, 8 years for a developing nation and an overburdened judiciary, shall also fall short of the high threshold.[147]

115. Respondent further submits that the Mercurian judiciary afforded due process toward Claimant's case. The Mercurian High Court and Commercial Bench had warned NHA to hear the matter *ex-parte* or take adverse measures and successfully forced NHA to appear before the court and make apologies.[148] Moreover, the judge's comment in 8 November 2011 might be improper, but as confirmed by *Electrabel v Hungary* tribunal, a single comment showing different attitude could not establish unlawful bias.[149]

116. Even if the tribunal considers there were some inappropriate conducts during the enforcement proceedings, Respondent submits that such slight defects fall far from the high standard for denial of justice. In *White v India*, during enforcement proceedings at New Delhi High Court, Coal India missed deadlines to file rejoinder or objections 3 times without any reason while the Indian court remained silent and showed more tolerance to Coal India.[150] The tribunal in *White v India*, however, only considered such behavior to be "*less than ideal*", but never a breach of even "*effective means*", let alone denial of justice.[151] Therefore, Respondent's judiciary might be less ideal or far from perfect, but in no means should these imperfection be considered violation of BIT obligation.

(3) CLAIMANT CANNOT CLAIM PROTECTION UNDER EFFECTIVE MEANS

[145] *White v India (Final Award)*, Para. 10.4.9
[146] *Ibid.*, Para. 10.4.24
[147] Annex No.3, line. 1350
[148] Exh. 1, Paras. 4, 21, 22
[149] *Electrobel v Hungary (Award)*, Para. 175
[150] *White v Indi*a (*Final Award)*, Para. 11.4.4.
[151] *Ibid.*

117. In response to Claimant's statement in its Notice of Arbitration, "*the conduct of judiciary has failed to provide any effective means of asserting rights*", Respondent submits that Claimant cannot claim protection under effective means as the Basheera-Mercuria BIT does not stipulate such obligation and "*effective means*" only appeared in the preamble. In *Continental Casualty v Argentina*, the tribunal specifically noted that "*the obligation mentioned in the preamble of the BIT (stability of legal framework) was not a legal obligation for the Contracting Parties*."[152] The cases Claimant might rely on, such as *Chevron v Ecuador* and *Duke Energy v Ecuador*, all have a separate and specific article or provision in binding BITs specifying the "*effective means*" obligation, which is notably absent in the present case.[153] Therefore, Claimant cannot claim protection under the alleged "*effective means*" obligation.

(4) RESPONDENT IS NOT IN VIOLATION OF FULL PROTECTION AND SECURITY

118. As stated by *Saluka v Czech Republic* tribunal and confirmed by *Toto v Lebanon*, the full protection and security obligation ("FPS") "*does not address all kinds of impairment, but only those which affect the physical integrity of the investment against the use of force*."[154] No element of violence or force was included in the process of the enforcement proceeding and the award itself was intangible.[155] Therefore, Respondent did not violate its obligation of FPS.

119. Even if the Tribunal considers that FPS covers more than just physical protection, Respondent submits that first the standard for FPS is not strict liability but due diligence[156]; second, as ruled by *Ronald S. Lauder v Czech Republic*, "*Respondent's only duty under FPS was to keep its judicial system available for the Claimant*".[157] Respondent had ensured Claimant's access to Mercuria's judiciary, as

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[152] *Continental Casualty v Argentina (Award)*, Para. 258
[153] *USA-Ecuador BIT*, Art. Ⅱ (7)
[154] *Toto v Lebanon (Award)*, Para. 229
[155] *Saluka v Czech Republic (Partial Award)*, Para. 483
[156] *Frontier v Czech Republic (Final Award)*, Para. 436
[157] *Ronald S. Lauder v Czech Republic (Final Award*), Para. 314

illustrated by Claimant's appearance in the high court.[158] Therefore, there was no legal restriction blocking Claimant's judicial access and therefore no violation of FPS.

(5) CONCLUSION

120. In conclusion, Respondent submits that (1) Mercuria's judicial conduct does not constitute denial of justice; (2) Claimant cannot raise claims under effective means; and, (3) Respondent did not violate requirements of full protection and security.

E. TERMINATION OF THE LONG-TERM AGREEMENT BY NHA DOES NOT AMOUNT TO A VIOLATION OF ARTICLE 3(3) OF THE BIT

121. Respondent contends (1) NHA's conclusion and termination of LTA are not attributable to Respondent; (2) even if attribution is established, the termination of the LTA cannot amount to a violation of Article 3(3).

(1) NHA'S CONCLUSION AND BREACH OF THE LTA ARE NOT ATTRIBUTABLE TO RESPONDENT

122. NHA's conclusion and termination of LTA are not attributable to Respondent because (a) NHA is not a state organ; (b) NHA was acting in its commercial capacity in concluding and terminating the LTA. (c) No evidence shows Respondent has directed or controlled NHA's conducts concerning the LTA. (d) The mere existence of Article 3(3) does not change the party to the LTA, and in any event, attribution must first be established.

(a) NHA is not a state organ, *de jure* or *de facto*

123. Article 4 of ILC Articles provides that:

> "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 organization of the State,

[158] Exh. 1, Para. 1

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."[159]

124. Since NHA is not within the structure of the governmental organization of Mercuria and no internal law of Mercuria classifies NHA legally as an organ, it cannot be regarded as a state organ *de jure*.

125. Respondent acknowledges that State cannot evade responsibility for the conduct of a *de facto* state organ (a body which as a matter of practice is considered to be or acts as an organ, even if the domestic law does not classify the entity as an organ in a sense relevant to Article 4).[160] However, such equation may only take place in exceptional circumstances where the persons, groups or entities act in "complete dependence" on the State, of which they are ultimately merely the instrument.[161] To examine whether such complete dependence exists, reference shall be made to: (i) whether the non-state entity was created by the state; (ii) whether state involvement exceeded the provision of training and financial assistance; (iii) whether complete (as opposed to a degree of or potential for) control was exercised in fact; and (iv) whether the state selected, installed or paid the political leaders of the group.[162] Further provided in *Almas v. Poland*, Claimant must show NHA's "performance of core governmental function[s]" and "directly day-to-day subordination to central government" or "lack of all operational autonomy" to qualify under the above definition.[163]

126. In this case, although the NHA was set up by the Central Government of Mercuria in 1998, it has autonomy in relation to Respondent. The NHA can negotiate with legal persons to conclude a contract, conduct research on its own, perform the contract it has entered into with others and deal with lawsuits on its own behalf. This level of autonomy means that it cannot be considered as acting in complete dependence on Respondent. Further, NHA is a separate legal entity that operates

[159] *Comment on ILC Articles,* Article 4
[160] *Crawford, State Responsibility*, pp. 124-125.
[161] *Ibid.*, p. 125
[162] *Ibid.*; *Nicaragua*, Paras. 109, 115
[163] *Almas v. Poland*, Para. 207

independently.[164] As stated by the tribunal in *Bayinder v. Pakistan* which "discards the possibility of treating NHA as a State organ under Article 4 because of its separate legal status,"[165] this tribunal should accordingly find the same.

127. Consequently, the acts which the NHA has committed are not be imputable to Respondent.

(b) NHA is acting in its commercial capacity in concluding and terminating the LTA

128. Under Article 5 of the ILC Articles, attribution is established if an entity is "empowered with governmental authority and acting in that capacity in a particular instance".[166]

129. In order to apply Article 5, 2 limbs of conditions must be satisfied, first, NHA must be empowered by Mercuria's law to exercise governmental authority, and second the NHA must have acted in that sovereign capacity in conducting the action at stake. Claimant contends that NHA was merely acting in its commercial capacity when concluding and terminating the LTA, leaving the second limb of Article 5 unsatisfied.

130. In *Bosh v. Ukraine*, the tribunal found the university's conducts concerning the contract was not attributable to the state because "the University's decision to enter into and subsequently terminate the 2003 Contract with B&P did not relate to the exercise of the University's governmental authority".[167] The tribunal looked at the nature and purpose of the contract and found that the contract was "a private or commercial activity which was aimed to secure commercial benefits for both parties."[168] Based on this and the fact that the university always has the ability to engage in contractual activities as an independent entity, the tribunal held there was no attribution under Article 5.[169]

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[164] PO3, lines 1591-1592
[165] *Bayindir v. Pakistan (Award)*, Para. 119
[166] *Comment on ILC Articles*, p. 100
[167] *Bosh v Ukraine (Award)*, Para. 177
[168] *Ibid.*
[169] *Bosh v Ukraine (Award)*, Para. 178

131. Similarly, in the current dispute, NHA operates independently and has the ability to enter into contracts like any other commercial party.[170] It concluded the LTA within its commercial capacity that any other private party could have done the same without involvement of governmental authority.[171] Further, its termination of the LTA was subject to Claimant's unsatisfactory performance and unwillingness to negotiate on the price for Sanior, which is a reasonable commercial decision that can be made by any private entity. Hence, no attribution can be found under Article 5 since NHA is acting in its commercial capacity in concluding and terminating the LTA.

(c) No evidence shows Respondent has directed or controlled NHA's conducts concerning the LTA

132. Under Article 8 of the ILC Articles,

> "the conduct of...a group of persons shall be considered an act of a State under international law if the...group of persons is in fact acting on the instructions of, or under the direction and control of, that State in carrying out the conduct."

133. The fact that the State initially establishes a corporate entity, whether by a special law or otherwise, is not a sufficient basis for the attribution to the State of the subsequent conduct of that entity under Article 8.[172] In *Nicaragua*, the ICJ had adopted the "effective control" test to determine whether there is direction[173], which was later confirmed and applied by the tribunals in *Hamester v Ghana*[174], *Jan de Nul v Egypt*[175] and *White v India*[176].

134. Clearly, international jurisprudence is demanding in order to attribute the act of a person or entity to a State, as it requires both a general control of the State over the person or entity and a specific control of the State over the act at stake under Article

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[170] PO3, lines 1591-1592
[171] *Jan de Nul v. Egypt (Award),* Para. 170
[172] *Comment on ILC Articles*, p. 112
[173] *Nicaragua*, Para. 115
[174] *Hamester v Ghana (Award),* Para. 179
[175] *Jan de Nul v Egypt (Award),* Para. 173
[176] *White v India (Final Award),* Paras. 8.1.10-8.1.21

8.[177] Respondent contends that Claimant failed to show that Mercuria had both general control over the NHA as well as specific control over the particular acts in question. Respondent was not involved, either directly or indirectly, in the protracted negotiation of the detailed contractual terms of the LTA with Claimant.[178] Furthermore, Respondent did not carry out any monitoring of the NHA's contractual performance on a daily basis, which is required to find attribution under Article 8 as affirmed by the tribunal in *White Industries v India*.[179]

135. The only fact that shows some sort of control was the private meeting between the Minister for Health and the Director of the NHA, which was alleged to resolve budgetary problems. Respondent argues that a mere rumor is far from enough to prove Respondent's general control and specific control over the NHA.[180] In *Hamester v Ghana,* where a similar meeting occurred, the tribunal found there was no direction or control because the State merely informed and discussed the case with the entity, lacking the evidence showing the direct demand imposed on COCOBOD, the entity at stake.[181] Thus, all conduct concerning the LTA are not attributable to Respondent under Article 8, it is NHA, not Respondent, which was the counter-party to the LTA and was in charge of implementing it.

(d) The mere existence of Article 3(3) does not change the party to the LTA, in any event, attribution must be established

136. In *Impregilo v Pakistan*, the Tribunal considered that a guarantee in umbrella clause would not cover the contracts of relevance since those are agreements into which the host state has not entered.[182] Similarly, as held by the ad hoc Committee in *CMS v. Argentina,* the effect of the umbrella clause is not to transform the obligation which is relied on into something else; the content of the obligation is unaffected, as is its proper law. If this is so, it would appear that the parties to the obligation (i.e., the person bound by it and entitled to rely on it) are likewise not changed by reason of the

[177] *Jan de Nul v Egypt (Award)*, Para. 173
[178] PO3, lines 1594-1595
[179] *White v India (Final Award)*, Para. 8.1.8
[180] Facts, p. 30, Para. 16
[181] *Hamester v Ghana,* Para. 199
[182] *Impregilo v Pakistan (Jurisdiction)*, Para. 223.

umbrella clause.[183] The same position was also taken by the Tribunal in *EDF v Romania.*[184]

137. In this case, the Claimant concluded the LTA with the NHA, which had a legal personality distinct from the Respondent, regarding the purchase and supply of Sanior.[185] Respondent was not a party to the LTA and was not bound by the LTA. Neither could Article 3(3) make Respondent a counter party to the LTA. Claimant cannot rely merely on Article 3(3) to prove Respondent is a party to the LTA.

138. Under any of the tests that possibly apply, NHA's conducts at stake cannot be attributed to Respondent. Obligations under the LTA are solely assumed by NHA, a separate entity. Respondent can neither be regarded as a party to this contract, nor be held internationally liable for any of NHA's conducts.

(2) EVEN ASSUMING THAT ATTRIBUTION IS ESTABLISHED, OBLIGATIONS UNDER THE LTA ARE NOT COVERED BY ARTICLE 3(3) SUBJECT TO RESTRICTIVE INTERPRETATION

139. Even assuming that attribution is established, Respondent contends that termination of the LTA does not amount to a violation of Article 3(3) of the BIT because obligations under the LTA are not covered by Article 3(3) because (a) Article 3(3) only restrictively covers investment agreements in which the state is involved as a sovereign; (b) LTA is merely a commercial contract and the alleged breach is not a sovereign act.

(a) Article 3(3) only covers investment contracts in which the state is involved as a sovereign

140. Article 3(3) reads,

"Each Contracting Party shall observe any obligation it may have entered into

[183] *CMS v Argentina (Annulment)*, Para. 95 (c)
[184] *EDF v Romania (Award)*, Paras. 317-320
[185] Facts, p. 29, Paras. 8-9

with regard to investments of investors of the other Contracting Party."[186]

141. Respondent contends that this Article is subject to restrictive interpretation, covering only investment contracts, in which host states act as sovereign. Claimant may rely on the tribunals' analysis in *SGS v Philippines* and *Eureko v Poland* to advance a broad interpretation of Article 3(3) in terms of scope of protection. However, this would be against the object and purpose of the Treaty, which is a required element of treaty interpretation in customary international law provided by Article 31 of *VCLT*.[187]

142. The object and purpose shown in the preamble of the BIT concerned in this case does not show that the Contracting Parties intended to create more favorable conditions for investments by investors in the aforementioned cases. Instead, the preamble provides that both parties were "desiring to achieve the objectives in a manner consistent with the protection of health, safety, and the environment, and the promotion of internationally recognized labor rights". Therefore, the mutual intent of both parties was actually to strike a balance between the protection of investments and the State's right to regulate, which supports the balanced and restrictive approach of interpretation of Article 3(3), as affirmed by *El Paso v. Argentina.*[188]

143. Further, broad interpretation of Article 3(3) will render the rest of the treaty useless by converting every minor obligation into a BIT claim. In *SGS v Pakistan*, the tribunal considered that the notion that umbrella clause could transform any contractual claims into treaty claims is "so far-reaching in scope, so automatic and unqualified and sweeping in operation, so burdensome in its potential impact on the Contracting Party."[189] It further held that such overly broad interpretation is unreasonable as to "render the rest of the treaty superfluous" and resulted in "floodgate effect in international tribunals",[190] which was affirmed by Professor Christoph Schreuer.[191] Furthermore in *El Paso v Argentina*[192], *Pan America v*

[186] Annex. No. 1, the BIT
[187] *VCLT*, Article 31
[188] *El Paso v. Argentina (Jurisdiction)*, Para. 70; *SGS v. Pakistan (*Jurisdiction*)*, Para. 167
[189] *SGS v Pakistan (Jurisdiction)*, Paras. 166, 168
[190] *Ibid.*, Para. 167
[191] *Schreuer*, p. 255
[192] *El Paso v Argentina (Jurisdiction)*, Para 77

Argentina[193], tribunals agreed with the *SGS v Pakistan* tribunal and concluded that investment arbitration will cover only disputes concerning investment agreements or state contracts in which the state is involved as a sovereign but not mere commercial contracts.[194]

144. Lastly, not limiting the application of Article 3(3) may result in the destruction of distinction between national and international legal orders. As Thomas W. Wälde pointed out, international law only protects breaches and interference with contracts made with government, or subject to governmental powers, if the government exercised its particular sovereign prerogatives to escape from its contractual commitment or to interfere in a substantial way with such commitments.[195] Umbrella clauses should therefore only serve as a restrictive rule of exception to the general separation of States obligations under municipal and under international law.[196]

(b) LTA is merely a commercial contract and the alleged breach is not a sovereign act

145. Article 3(3) makes reference to obligations "with respect to investment". Provided by Stephan W. Schill, such umbrella clause only extends protection to contracts that constitutes investment themselves.[197]

146. As established in the first issue, the LTA concerns the purchase and supply of Sanior, which is a purely commercial contract.[198] It does not qualify as an investment protected under the BIT. Thus, it cannot be covered by Article 3(3).

147. In *Sempra v Argentina*, the Tribunal held that ordinary commercial breaches of a contract would not violate the umbrella clause in the Argentina-US BIT. Only a breach in the exercise of a sovereign state function or power but not the conduct of an ordinary contract party could effectuate a breach. Only when by sweeping changes, "the ordinary contractual breaches had been brought about in exercise of the state's

193 *Pan America v Argentina (Preliminary Objections)*, Para. 108
194 *Eureko v. Poland (Dissenting Opinion)*, Para. 11
195 *Wälde*, p. 225
196 *Noble Ventures v. Romania (Jurisdiction)*, Para. 55; *Schwebel*, p. 111
197 *Schill*, p. 86
198 Facts, p. 29, Paras. 9-10

public function" [199] or "reached severe magnitude"[200], can this Tribunal find a breach of the umbrella clause.

148. In the current dispute, Respondent never exercised sovereign power when it negotiated with Claimant and performed the LTA. Further, the termination of the LTA happened after NHA's renegotiation of the price for Sanior failed. [201] Such termination was purely a commercial contractual party's conduct and was provided as an express commercial right under the LTA agreed by Claimant.[202] Respondent never enacted laws or exercise administrative or judicial power to bring an end to the LTA. Consequently, such conduct does not constitute a sovereign act and therefore does not violate Article 3(3) of the BIT.

149. Even assuming attribution is established, Claimant's argument still fails because (a) Respondent's termination is not a breach of the LTA; and (b) obligations under the LTA, a pure commercial contract, nevertheless cannot be covered by Article 3(3) subject to proper restrictive interpretation of this clause.

(3) CONCLUSION

150. To conclude, (1) neither of NHA's conclusion nor termination of LTA is not attributable to Respondent; (2) the termination of the LTA amounts to no violation of Article 3(3). Hence, Claimant's requests must not be allowed.

[199] *Sempra v Argentina (Award)*, Paras. 305-14
[200] *Joy Mining v. Egypt (Jurisdiction)*, Para. 79
[201] Facts, p. 30, Para. 15
[202] *Ibid*., Para. 10

PRAYER FOR RELIEF

In light of the foregoing, Respondent respectfully requests this Tribunal to find that:

(A) This Tribunal lacks jurisdiction over claims in relation to the Award;

(B) Claimant has been effectively denied benefits of the BIT by virtue of Article 2;

(C) The enactment of Law No. 8458/09 and the grant of the license for the claimant's invention do not amount to a breach of the BIT;

(D) Respondent is not liable under the BIT for the conduct of its judiciary in relation to the enforcement proceedings;

(E) The termination of the LTA by NHA does not amount to a breach of the BIT.

RESPECTFULLY SUBMITTED ON 25 SEPTEMBER 2017 BY

TEAM GAJA

On behalf of Respondent,

Republic of Mercuria