ARBITRATION INSTITUTE OF THE

STOCKHOLM CHAMBER OF COMMERCE

ANATOLIE STATI, GABRIEL STATI, ASCOM GROUP S.A.,

AND TERRA RAF TRANS TRAIDING LTD.

Claimants

v.

REPUBLIC OF KAZAKHSTAN,

Respondent

STATEMENT OF CLAIM

May 18, 2011

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1. Anatolie Stati, Gabriel Stati, Ascom Group S.A. ("Ascom"), and Terra Raf Trans Traiding ("Terra Raf") (collectively, "Claimants") respectfully submit their Statement of Claim in this arbitration proceeding against the Republic of Kazakhstan ("Kazakhstan," "Government," or "State") under The Energy Charter Treaty ("ECT" or "Treaty").[1] This Statement of Claim is filed pursuant to Article 26 of the ECT and Article 24 of the Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce.

I. PRELIMINARY STATEMENT

A. Claimants' Kazakh Investments

2. This dispute arises out of Kazakhstan's illegal treatment and expropriation of Claimants' Kazakh oil and gas investments. Anatolie Stati and Gabriel Stati own 100% of Moldova-based Ascom and Gibraltar-based Terra Raf.[2] Ascom and Terra Raf were in turn 100% owners of the two illegally expropriated Kazakh energy companies at issue in this case: Kazpolmunay LLP ("KPM") and Tolkynneftegaz LLP ("TNG").[3]

3. KPM and TNG had contracts with Kazakhstan for the exploration and/or extraction of hydrocarbons (the "Subsoil Use Contracts"). The KPM and TNG Subsoil Use Contracts covered the Borankol field (Contract No. 305), the Tolkyn field (Contract No. 210), and the Contract 302 Properties (sometimes referred to as the "Tabyl block")[4] in the Pre-Caspian basin of western Kazakhstan, located in the Beyneu district of Kazakhstan's Mangystau region. KPM operated the Borankol field, and TNG operated the Tolkyn field and the Contract 302 Properties.

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1 The Energy Charter Treaty is attached as Claimants' Exhibit (hereinafter "C-") 1.

2 Ascom was founded by Claimant Anatolie Stati in 1994. It specializes in oil and gas exploration, development, production, trading, and oil field services. In addition to its Kazakh operations at issue in this case, Ascom has been the operator of the Gotur Depe and Barsa Gelmez oil fields in Turkmenistan; has provided extensive industry field services including construction of production facilities, pipelines, tanks, terminals, and compressor stations; holds an exploration and extraction contract for block 5B in Southern Sudan; and has concluded an exploration and production sharing contract for the Bardarash block with the Government of the Kurdistan Region of Iraq. *See* Witness Statement of Anatolie Stati dated May 17, 2011 ¶¶ 3, 6-12 (hereinafter "Stati Statement"). *See also*, Ascom website at http://www.ascom-sa.com/?p=278.

3 For a detailed description of Claimants' acquisition of its interests in KPM and TNG, *see infra*, Section III.A.

4 In its entirety, the "Contract 302 Properties" consists of the Tabyl area, the Munaibay area, the Tabyl West prospect, the Munaibay North prospect, the Bahyt prospect, and the Interoil Carboniferous Reef prospect. In shorthand, this group of Contract 302 Properties is often referred to collectively as the "Tabyl block."

4. Claimants' exploration in the Borankol and Tolkyn fields began in 2000. By 2008, Claimants had approximately 100 operational wells in the two fields, with approximately 80 of those producing at any given time in the range of 62 thousand barrels oil equivalent per day. Borankol field production was principally oil, with the oil sold to the export market. Tolkyn field production was a combination of gas and condensate, with the gas principally dedicated to local Kazakh municipal and utility consumption at fixed prices, and the condensate sold on export markets. In addition to rail transport of condensate, production from the Tolkyn and Borankol fields was delivered into two, proximately located trans-national main oil and gas transportation pipelines – the Uzen-Atyrau-Samara main oil pipeline owned and operated in Kazakhstan by KazTransOil, a subsidiary of Kazakhstan's State-owned oil and gas company, KazMunaiGas,[5] and the Central Asia-Center main gas pipeline, owned and operated in Kazakhstan by Intergas Central Asia JSC, also a subsidiary of KazMunaiGas.[6]

5. To support the wells and production, Claimants constructed an extensive infrastructure of field gathering pipelines, metering stations, processing and treatment facilities, and storage tanks. In 2006, Claimants commenced the development of a Liquefied Petroleum Gas ("LPG") processing facility, investing more than USD 245 million in its development and construction.[7] In addition to the Borankol and Tolkyn field production, Claimants conducted exploratory work and well testing in the Contract 302 Properties, making significant oil and gas finds in 2008-2009, and spending more than USD 43 million conducting the exploration work and drilling test wells.[8]

6. Since 2000, Claimants have invested more than USD 1 billion in exploration and development of the Borankol field, the Tolkyn field, and the

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[5] *See* "Uzen-Atyrau-Samara Oil Pipeline (Kazakhstan, Russian Federation)", at: http://www.iot.kiev.ua/index.php?option=com_content&view=article&id=79&Itemid=82&lang=en; KazMunaiGas website, at: http://www.kmg.kz/en/group_companies/subsidiary/kaztransoil/. This main oil pipeline is sometimes referred to as the "KazTransOil pipeline."

[6] *See* ICA Intergas Central Asia website, at: http://www.intergas.kz/eng/about/history/; KazMunaiGas website, at: http://www.kmg.kz/en/group_companies/subsidiary/kaztransgaz/.

[7] *See* Expert Report of FTI Consulting dated May 17, 2011 (hereinafter "FTI Report") ¶ 6.23.

[8] *See* FTI Report ¶ 6.21.

Contract 302 Properties,[9] and in the process have paid to the government of Kazakhstan more than USD 500 million in requisite fees and taxes.[10]

7. On July 21-22, 2010, Kazakhstan directly and unlawfully expropriated all of Claimants' Kazakh investments by unilaterally cancelling KPM's and TNG's Subsoil Use Contracts,[11] transferring KPM's and TNG's assets and operations to KazMunaiGas, and physically commandeering KPM's and TNG's offices using personnel from KazMunaiGas and the Kazakh Ministry of Oil and Gas.[12] The expropriation was purportedly based on a written list of eighteen alleged Subsoil Use Contract violations that KPM and TNG received from the State on July 16, 2010, less than a week before the expropriation occurred.[13]

8. The State's direct expropriation of the entirety of Claimants' investments in Kazakhstan was the culmination of an illegal campaign of indirect expropriation and unfair treatment that commenced on October 14, 2008. Between October 2008 and July 2010, the State lodged numerous false accusations of wrongful conduct against KPM and TNG and conducted a concerted harassment campaign that included farcical criminal charges, the jailing of KPM's general manager, the imposition of an arbitrary and debilitating criminal fine, the seizure of KPM's and TNG's assets and bank accounts, the freezing of the companies' equity interests, intrusive and unwarranted tax and State-agency audits, the wrongful imposition of exorbitant taxes and fees, and capricious reversals of pre-existing agreements between TNG and the State. Curiously, of the eighteen alleged violations of the Subsoil Use Contracts that the State relied upon for its direct expropriation of Claimants' investments in July 2010, fifteen bore no relation

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9 *See* Tristan Consolidated Financial Statement for 2009, at pp. 3 and 14, included in the data accompanying the FTI Report.

10 Witness Statement of Artur Lungu dated May 17, 2011 ¶ 15 (hereinafter "Lungu Statement").

11 *See* Notification No. 20-05-5150 from the Kazakh Ministry of Oil and Gas ("MOG") to KPM terminating the Borankol Subsoil Use Contract dated July 21, 2010, C-3; Notification No. 20-05-5151 from MOG to TNG terminating the Tolkyn Subsoil Use Contract dated July 21, 2010, C-4; Notification No. 14-05-5182 from MOG to TNG terminating the Subsoil Use Contract No. 302 dated July 22, 2010, C-5.

12 *See* Witness Statement of Alexandru Condorachi dated May 12, 2011 ¶ 50 (hereinafter "Condorachi Statement").

13 *See* Notice of infringement of obligations under the Borankol Subsoil Use Contract No. 305, from MOG to KPM, dated July 14, 2010, C-2; Notice of infringement of obligations under the Tolkyn Subsoil Use Contract No. 210, from MOG to TNG, dated July 14, 2010, C-6; Notice of infringement of obligations under the Subsoil Use Contract No. 302, from MOG to TNG, dated July 14, 2010, C-7.

whatsoever to the plethora of previous accusations and allegations that the State had levied against TNG and KPM during the harassment campaign spanning the October 2008 – July 2010 period. The remaining allegations were similarly unfounded.

B. The State's Indirect Expropriation of Claimants' Investments and Campaign of Unfair and Inequitable Treatment

9. This case is somewhat unusual because it involves not only the State's direct and unlawful expropriation of all of Claimants' investments without lawful justification or compensation, but also an indirect expropriation of those investments through a lengthy course of wrongful State conduct that saddled KPM and TNG with unfounded criminal, monetary, operational, and title-clouding liabilities. Kazakhstan's illegal seizure of the entirety of Claimants' investments in July 2010 was preceded by a campaign of illegal harassment and coercion that was quasi-medieval in nature.

10. In hindsight, from the beginning of its harassment campaign in October 2008, a complete expropriation of Claimants' investments was quite clearly the State's goal. The State, however, evidently felt the need to concoct some kind of colorable – or at least sufficiently confusing and impenetrable – bases for its eventual takeover. What Kazakhstan succeeded in concocting was a mish-mash of patently ridiculous and often self-contradictory accusations. But those accusations had a desirable, and quite clearly designed, side-effect for the State. They promptly interfered with Claimants efforts to sell their properties, and progressively devalued Claimants' investments. By preventing Claimants from selling their investments to any other foreign investor, the State cleared the path for its final step of complete expropriation.

11. This case is also somewhat unusual because the commencement of the State's campaign of indirect expropriation and illegal harassment can be traced to a date certain – October 14, 2008. It was on that date that the President of Kazakhstan, Nursultan Nazarbayev, issued instructions to the Kazakh Deputy Prime Minister and the head of the Kazakh Financial Police to "thoroughly investigate" all of Claimants' business activities in Kazakhstan.[14] Immediately thereafter, the Kazakh Financial Police ordered the commencement of an unprecedented array of global, harassing

[14] *See* President Nazarbayev's investigation instructions dated October 14, 2008, C-8.

audits and investigations of KPM and TNG by the State's Ministry of Energy and Mineral Resources ("MEMR"),[15] Tax Committee,[16] Customs Committee,[17] Geology Committee,[18] Ecology Committee,[19] Ministry of Emergency Situations,[20] and the National Bank of Kazakhstan.[21] Two significant events preceded this October 14, 2008, kick-off of the State's harassment campaign against Claimants.

12. First, in the summer of 2008, Claimants made a decision to sell their Borankol and Tolkyn producing properties, together with the LPG plant. Claimants directed their investment banker, Renaissance Capital, to organize a sale process, which was nick-named "Project Zenith." On July 18, 2008, Renaissance Capital circulated a "teaser," offering the properties to 129 prospective buyers, including Kazakhstan's State-owned KazMunaiGas.[22] In mid-August, Renaissance Capital distributed a detailed Information Memorandum regarding the properties to 41 parties, including KazMunaiGas, which had expressed an interest and signed a confidentiality agreement.[23] By October 1, 2008, Claimants had received eight, non-binding indicative offers for the properties, with the highest, USD 1.55 billion, offered by the Korea National Oil Corporation.[24] KazMunaiGas tendered an indicative offer of USD 754 million on September 25, 2008, the third lowest of the bids received.[25]

13. Second, in July of 2008, TNG discovered substantial oil and gas deposits in the East Munaibay structure of the Contract 302 Properties. TNG first

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15 *See* Order from the Financial Police to the MEMR dated October 20, 2008, C-9.

16 *See* Order from the Financial Police to the Tax Committee dated October 24, 2008, C-10.

17 *See* Order from the Financial Police to the Customs Committee dated October 18, 2008, C-11.

18 *See* Order from the Financial Police to the Geology Committee dated October 28, 2008, C-12.

19 *See* Order from the Financial Police to the Ecology Committee dated October 28, 2008, C-13.

20 *See* Letter from the Ministry of Emergency Situation to the Financial Police dated October 31, 2008, C-14.

21 *See* Order from the National Bank of Kazakhstan dated November 2008, C-15.

22 *See* Project Zenith - Opportunity to acquire attractive upstream oil & gas assets in Kazakhstan, dated July 18, 2008, C-16; Project Zenith – Overview of Non-Binding Offers, dated September 27, 2008, C-17.

23 *See* Project Zenith – Overview of Non-Binding Offers, dated September 27, 2008, C-17.

24 *See* Indicative Proposal for Project Zenith from Korea National Oil Corporation, dated September 26, 2008, C-18.

25 *See* Indicative Proposal for Project Zenith from KazMunaiGas dated September 25, 2008, C-19.

reported the East Munaibay find to the MEMR on July 24, 2008,[26] and filed with the MEMR a statement of its intention to begin the evaluation stage of the structure on August 13, 2008.[27] On October 7, 2008, the MEMR acknowledged TNG's application for evaluation of the discovery.[28] With the full extent and value of the Contract No. 302 resources still in the assessment stage, Claimants excluded a specific offer of the Contract 302 Properties from the Project Zenith sale process.[29]

14. Thus, by the fall of 2008, Kazakhstan knew that Claimants intended to sell the producing properties and the LPG plant; knew the probable market value of those properties; knew that the likely buyer would be another foreign investor; knew that potentially significant oil and gas deposits had been found in the Contract 302 Properties; and knew that Claimants would likely remain the foreign investor in control of the Contract No. 302 resources. With this information, and with a direct self-interest in gaining complete control over the existing Tolkyn and Borankol production, the LPG plant, and the potentially significant new deposits in the Contract 302 Properties, Kazakhstan evidently orchestrated a process that would prevent a sale to a foreign buyer and culminate in the expropriation of the entirety of Claimants' investments.

15. Indeed, a letter from the president of the public fund Blagovest to the Kazakh MEMR dated February 7, 2010 (the "Blagovest Letter"), confirms that nationalization of Claimants' investments became the State's goal in 2008.[30] The Blagovest Letter contains a series of suggestions clearly geared toward final expropriation of Claimants' Kazakh investments. Among other extraordinary comments, it states:

> **The suggestion offered for discussion may resolve the question of nationalization of the assets posed in 2008.**
>
> **The following are the tasks that may be resolved:**
>
> **- Establishing control over TNG and KPM ...**

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[26] *See* Letters from TNG to the Geology and Subsoil Use Committee of the MEMR and to the MEMR, dated July 24, 2008, C-20.

[27] *See* Application filed by TNG with the MEMR, with an evaluation program and explanatory note, dated August 11, 2008, C-21.

[28] *See* Letter from the MEMR to TNG, dated October 7, 2008, C-22.

[29] Lungu Statement ¶ 29; Stati Statement ¶ 17.

[30] *See* Letter from Blagovest President to MEMR, dated February 7, 2010, C-23.

> **- Petition to the international arbitration is excluded; ...**
>
> **The main idea – to separate interests of the companies (contract execution, jobs, salaries, interests of Kazakhstan) and interests of their owner (political ambition, indebtedness before investors).**[31]

16. After setting this goal of "nationalization" in 2008, and giving the Kazakh Financial Police the principal role in accomplishing it, the State set about concocting allegations and accusations against KPM and TNG. As mentioned above, fifteen of the eighteen alleged Subsoil Use Contract violations that the State compiled at the last minute to facilitate its ultimate, direct expropriation bore no relation at all to the allegations and accusations that the State made during the harassment campaign it commenced in October of 2008. Of the three that overlap, one happens to be both the most absurd and inhumane of the State's accusations – a trumped up criminal charge that led to the arrest and conviction of KPM's general manager and a four-year jail sentence.

17. The criminal charge was based on an accusation that KPM and TNG were operating "main" oil and gas transportation pipelines without a license. To support this ridiculous accusation, the State simply "reclassified" four isolated segments of the Borankol and Tolkyn field gathering systems as "main" pipelines. The pipelines comprising the field gathering systems of KPM and TNG, however, had been permissibly constructed under State guidelines, and licensed by the State, for the purpose of delivering oil and gas from the fields ***to*** the 1,380 kilometer long Uzen-Atyrau-Samara main oil pipeline, and the 4,892 kilometer long Central Asia-Center main pipeline – both of which are owned and operated in Kazakhstan by subsidiaries of State-owned KazMunaiGas.[32] Despite numerous examples of virtually identical field gathering systems throughout Kazakhstan, only segments of the KPM and TNG gathering systems were singled out by the State as purportedly constituting "main" pipelines. On the basis of that ridiculous allegation, KPM's

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[31] *Id*. (emphasis added). For a more complete discussion of the Blagovest Letter, *see infra*, Section IV.H.

[32] *See infra*, Section IV.B.1, and accompanying footnotes. *See also*, www.intergas.kz and www.kaztransoil.kz.

general manager was convicted and imprisoned, and a USD 145 million fine was levied against KPM, in criminal proceedings replete with due process violations.[33]

18. The State's trumped-up criminal charges against KPM and TNG, and the USD 145 million fine levied against KPM, were then used by the State as an excuse to:

- freeze Claimants' equity interests in KPM and TNG to prevent their alienation during the course of the criminal proceedings, a freeze that remains in place to this day despite the presumed non-existence of any remaining criminal proceedings against KPM and TNG;
- render collection orders against all of KPM's Kazakh bank accounts and seize the accounts and the cash within them;
- seize KPM's vehicles and place them in an impound yard;
- seize land administered by KPM in Beyneu district;
- seize KPM's oil pipeline from its processing and pumping unit to its Opornaya raw material resources base;
- seize KPM's accumulator oil tanks;
- prohibit KPM's transfer of oil from the oil accumulator tanks to the Uzen-Atyrau-Samara main oil pipeline operated by KazMunaiGas' subsidiary KazTransOil;
- prohibit contracting for the import and export of goods and property;[34]
- allege that "[u]nlicensed operation of trunk oil and gas pipelines [have] been admitted" by KPM and TNG, and that these "admissions" constituted violation of the KPM and TNG Subsoil Use Contracts;[35] and

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[33] For a detailed explanation of the sheer absurdity of the criminal charges, and the due process violations that accompanied the prosecution of KPM's general manager and KPM, *see infra*, Section IV.B.

[34] For a detailed explanation of the asset seizure actions taken by the State prior to its direct expropriation of Claimants' investments in July of 2010, *see infra*, Section IV.B.5.

[35] *See* Notice of infringement of obligations under the Borankol Subsoil Use Contract, from MOG to KPM, dated July 14, 2010, C-2; Notice of infringement of obligations under the Tolkyn Subsoil Use Contract, from MOG to TNG, dated July 14, 2010, C-6; Notice of infringement of obligations under Subsoil Use Contract No. 302, from MOG to TNG, dated July 14, 2010, C-7.

- use the alleged "admissions" of unlicensed main pipeline operations as an excuse to ultimately and directly expropriate Claimants' Kazakh investments.

19. While Kazakhstan's trumped-up criminal charges against KPM and its in-country manager were perhaps the most egregious acts of the Government's campaign of indirect expropriation and harassment during the October 2008 – July 2010 period, the campaign was hardly limited to those criminal charges. The campaign also included a variety of other acts and accusations that the State ultimately abandoned in July 2010 when it specified its eighteen "grounds" for its direct expropriation:

> a) A December 18, 2008 allegation that the State retained an active, exercisable pre-emptive right to purchase TNG arising out of the May 12, 2003 transfer of 100% of TNG's shares from Gheso, S.A., a subsidiary of Ascom, to Claimant Terra Raf, a pre-emptive right that had been previously and explicitly waived by the State. This alleged pre-emptive purchase right was undoubtedly abandoned by the State by July 2010 because its exercise would have involved an actual purchase of TNG from either Gheso or Terra Raf, something the State obviously had no intention of pursuing. Its assertion had the self-evident effect, however, of casting a cloud on Claimants' title to TNG, sending a discouraging message to any other prospective foreign investor wishing to purchase the company.[36]
>
> b) A February 10, 2009 assessment of USD 62 million in back corporate taxes and penalties based on a frivolous allegation that KPM and TNG had applied the wrong amortization rate to their drilling activities. This claim was necessarily abandoned by the State by July 2010 because, after a long and arduous fight by KPM and TNG through a court system being manipulated by the Financial Police, even the State's appellate courts ultimately did not endorse it, finally reversing the assessment in March 2010.[37]

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[36] For a more complete discussion of the pre-emptive rights issue, *see infra*, Section IV.C.

[37] For a more complete discussion of this corporate tax assessment, *see infra*, Section IV.D.

c) A preposterous July 3, 2008 allegation that the Borankol Subsoil Use Contract did not contain a Crude Oil Export Tax exemption that it most explicitly did, and an extortionate action to force payment of the contractually exempted Export duties by prohibiting oil exports. The State likely chose to abandon this claim by July 2010 not only because the Subsoil Use Contract provision is ironclad, but also because, while pursuing challenges to the export duty assessments in the Kazakh courts, KPM conditionally paid more than USD 10 million in unjustified export duties to avoid disruption to oil exports, which the State retained.[38]

d) A December 2009 assessment of USD 6 million for allegedly unpaid transfer pricing taxes. This assessment followed an exhaustive, thirteen-month financial audit ordered by the Financial Police that commenced in November 2008, an audit that conveniently gave the State access to all of the companies' financial records. The State most likely chose to abandon this allegedly unpaid tax assessment by July 2010 because the legal appeals of TNG and KPM challenging the assessment were still pending when the State directly expropriated Claimants' investments.[39]

C. The State's Direct Expropriation of Claimants' Investments

20. By notices dated July 14, 2010, but actually received by KPM and TNG on July 16, 2010, the Kazakh Ministry of Oil and Gas notified Claimants of eighteen alleged violations of the Subsoil Use Contract No. 305 (Borankol), Subsoil Use Contract No. 210 (Tolkyn), and the Subsoil Use Contract No. 302 (Tabyl Block)[40] and affiliated properties. The notices contained little explanation of the bases for the alleged violations – they simply listed the violations in conclusory fashion and instructed Claimants to respond to all of them in three days, by July 19,

[38] For a more complete discussion of this export duty assessment, *see infra*, Section IV.E.

[39] For a more complete discussion of this transfer pricing assessment, *see infra*, Section IV.F.

[40] *See* Notice of infringement of obligations under the Borankol Subsoil Use Contract No. 305, from MOG to KPM, dated July 14, 2010, C-2; Notice of infringement of obligations under the Tolkyn Subsoil Use Contract No. 210, from MOG to TNG, dated July 14, 2010, C-6; Notice of infringement of obligations under the Subsoil Use Contract No. 302, from MOG to TNG, dated July 14, 2010, C-7.

2010. The notices also contained the threat that failure to respond would result in termination of the Subsoil Use Contracts.

21. Despite the exceedingly short notice given by the State, both KPM and TNG submitted detailed responses to the alleged violations – describing how they were inaccurate and did not constitute violations at all – on July 19, 2010, as demanded by the Government.[41] The responses were completely ignored by the Kazakh authorities. On July 21, 2010, the State unilaterally terminated KPM's Subsoil Use Contract No. 305 covering the Borankol field and TNG's Subsoil Use Contract No. 210 covering the Tolkyn field. On July 22, 2010, it unilaterally terminated the Subsoil Use Contract No. 302 covering the Tabyl Block and other properties.

22. In a final twist of absurdity, the State did not terminate the Subsoil Use Contract No. 302 for the alleged contract violations listed in its July 14, 2010 notice, but allegedly because Contract No. 302 had expired on March 30, 2009. The State, however, had already agreed in writing to extend the Subsoil Use Contract No. 302 on April 9, 2009,[42] and had received from TNG the extension addendum for execution on May 4, 2009. The State simply never signed the extension addendum, despite its explicit agreement to do so. Thus, the State used its own bad faith failure for over a year to execute an already agreed-upon extension as an excuse to terminate Contract No. 302 in July of 2010.[43]

23. On July 22, 2010, Kazakhstan commandeered KPM's and TNG's offices, evicted KPM's and TNG's senior management, and proceeded to "re-hire" most of KPM's and TNG's personnel to maintain production operations.[44] The Government opened new accounts in the name of its 100% subsidiary,

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41 *See* Answer to the notification on infringement of obligations under Contract No. 305 to MOG from KPM, dated July 19, 2010, C-24; Answer to the notification on infringement of obligations under Contract No. 302 to MOG from TNG, dated July 19, 2010, C-25; Answer to the notification on infringement of obligations under Contract No. 210 to MOG from KPM, dated July 19, 2010, C-26.

42 *See* Letter from the MEMR to TNG, dated April 9, 2009, C-27.

43 For a more complete discussion of the approved extension for the Contract 302 Properties, *see infra*, Section IV.G.

44 Condorachi Statement ¶ 50.

KazMunaiGas, for the deposit of all revenues generated by KPM and TNG from their oil and gas production.[45] Kazakhstan's takeover was complete.

24. Kazakhstan's campaign of indirect expropriation and illegal harassment commencing in October 2008, as well as its ultimate direct expropriation of Claimants' investments in July 2010, violated a number of the standards of protection contained in the ECT. Kazakhstan's violations of the ECT and international law caused substantial damages to Claimants, which Claimants seek to recover in this proceeding.

II. JURISDICTION

25. Article 26 of the ECT grants Claimants the right to submit this dispute to international arbitration. Article 26 provides:

> SETTLEMENT OF DISPUTES BETWEEN AN INVESTOR AND A CONTRACTING PARTY
>
> (1) Disputes between a Contracting Party and an Investor of another Contracting Party relating to an Investment of the latter in the Area of the former, which concern an alleged breach of an obligation of the former under Part III shall, if possible, be settled amicably.
>
> (2) If such disputes can not be settled according to the provisions of paragraph (1) within a period of three months from the date on which either party to the dispute requested amicable settlement, the Investor party to the dispute may choose to submit it for resolution:
>
> (a) to the courts or administrative tribunals of the Contracting Party to the dispute;
>
> (b) in accordance with any applicable, previously agreed dispute settlement procedure; or
>
> (c) in accordance with the following paragraphs of this Article.
>
> (3) (a) Subject only to subparagraphs (b) and (c), each Contracting Party hereby gives its unconditional consent to the submission of a dispute to international arbitration or conciliation in accordance with the provisions of this Article.
>
> (b) (i) The Contracting Parties listed in Annex ID do not give such unconditional consent where the Investor has

[45] *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

> previously submitted the dispute under subparagraph (2) (a) or (b)…[46]
>
> (c) A Contracting Party listed in Annex IA does not give such unconditional consent with respect to a dispute arising under the last sentence of Article 10(1).[47]
>
> (4) In the event that an Investor chooses to submit the dispute for resolution under subparagraph (2) (c), the Investor shall further provide its consent in writing for the dispute to be submitted to: …
>
> (c) an arbitral proceeding under the Arbitration Institute of the Stockholm Chamber of Commerce. …
>
> (5) A tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law.

26. All of the requirements of Article 26 have been met in this case.

A. The Parties' Consent to Arbitration

27. In their Request for Arbitration dated July 26, 2010, Claimants consented to arbitration under the ECT and elected to submit this dispute to the Arbitration Institute of the Stockholm Chamber of Commerce in accordance with Article 26(4) of the ECT.

28. Kazakhstan consented to arbitration under the ECT by signing and ratifying the Treaty. The ECT entered into force for Kazakhstan on April 16, 1998.[48]

B. Claimants' Nationalities

29. Claimants Anatolie Stati and Gabriel Stati are dual citizens of Moldova and Romania. Both countries are contracting parties to the ECT.[49]

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[46] Kazakhstan has submitted a statement under Annex ID of the ECT. However, as discussed below, Claimants have not previously submitted this dispute to the courts or administrative tribunals of Kazakhstan or in accordance with any previously agreed dispute settlement procedure. While this case partially relates to litigation in Kazakhstan, that litigation does not involve the same parties or claims at issue in this treaty dispute, which is based on Kazakhstan's violations of the Treaty. Consequently, Kazakhstan's statement under Annex ID is irrelevant.

Furthermore, and in any event, Kazakhstan's statement under Annex ID is restricted to situations where domestic court litigation involves "the same dispute between the same parties and the same subject," which is not the case here. *See* Statement of Kazakhstan under Annex ID, C-1. Therefore, even if Kazakhstan's statement under Annex ID were relevant – which it is not – it would not prevent Claimants from bringing the current case based on violations of the ECT.

[47] Kazakhstan is not listed under Annex IA. Consequently, Claimants are entitled to assert a claim based on the last sentence of Article 10(1), the ECT's "umbrella clause," which they do.

[48] Date of the ECT's entry into force for Kazakhstan, C-28.

30. Claimant Ascom is incorporated under the laws of Moldova, a contracting party to the ECT.[50]

31. Claimant Terra Raf is incorporated under the laws of Gibraltar, an overseas territory of the United Kingdom.[51] In accordance with the United Kingdom's declaration under Article 45(1) of the ECT regarding provisional application of the Treaty, the ECT applies provisionally to Gibraltar.[52] The issue of the ECT's provisional application to Gibraltar was litigated in the case of *Petrobart (Gibraltar) v. The Kyrgyz Republic*. The *Petrobart* Tribunal concluded that the ECT applied provisionally to Gibraltar.[53]

32. Anatolie Stati owns 100% of Ascom,[54] and Ascom in turn owned 100% of KPM.[55] Anatolie Stati and Gabriel Stati each own 50% of Terra Raf,[56] and Terra Raf in turn owned 100% of TNG.[57] Anatolie Stati and Gabriel Stati therefore own and control all of the Kazakh investments at issue in this case through their ownership interests in Ascom and Terra Raf.

C. Dispute Concerning an "Investment"

33. Claimants' investments fall squarely within the broad definition of "Investment" contained in Article 1(6) of the ECT, which provides:

> "Investment" means every kind of asset, owned or controlled directly or indirectly by an Investor and includes:

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49 Copies of Anatolie Stati's Moldovan and Romanian passports and Gabriel Stati's Moldovan and Romanian passports, C-29 and C-30.

50 *See* Ascom's Certificate of Incorporation, C-31.

51 *See* Terra Raf Trans Traiding Ltd.'s Certificate of Incorporation, C-32. A further certificate and Terra Raf's Memorandum of Association, C-33.

52 *See* United Kingdom's declaration under Article 45(1) of the ECT regarding provisional application of the Treaty, C-34.

53 *Petrobart Limited v. Kyrgyz Republic*, SCC Arb. No. 126/2003, Award, March 29, 2005 (hereinafter "*Petrobart* Award"), C-204.

54 *See* List of Ascom shareholders, C-35.

55 *See* Articles of Association of Limited Liability Partnership "Kazpolmunay," C-36; KPM's Certificate of Incorporation, C-37.

56 *See* Terra Raf Trans Traiding Ltd.'s Certificate of Incorporation, C-32.

57 *See* Articles of Association of Limited Liability Partnership "Tolkynneftegaz," listing Terra Raf as the sole participant of the TNG partnership, C-39; TNG's Certificate of Incorporation, C-40.

> (a) tangible and intangible, and movable and immovable, property, and any property rights such as leases, mortgages, liens, and pledges;
>
> (b) a company or business enterprise, or shares, stock, or other forms of equity participation in a company or business enterprise, and bonds and other debt of a company or business enterprise;
>
> (c) claims to money and claims to performance pursuant to contract having an economic value and associated with an Investment;
>
> (d) Intellectual Property;
>
> (e) Returns;
>
> (f) any right conferred by law or contract or by virtue of any licences and permits granted pursuant to law to undertake any Economic Activity in the Energy Sector.
>
> A change in the form in which assets are invested does not affect their character as investments and the term "Investment" includes all investments, whether existing at or made after the later of the date of entry into force of this Treaty for the Contracting Party of the Investor making the investment and that for the Contracting Party in the Area of which the investment is made (hereinafter referred to as the "Effective Date") provided that the Treaty shall only apply to matters affecting such investments after the Effective Date.
>
> "Investment" refers to any investment associated with an Economic Activity in the Energy Sector.

34. Claimants' investments are indisputably "associated with an Economic Activity in the Energy Sector." KPM and TNG are energy companies that held contracts and licenses from Kazakhstan for the exploration and production of hydrocarbons. Claimants' tangible and intangible holdings in Kazakhstan included ownership of oil and gas wells, drilling equipment, gathering pipelines, treatment and storage facilities, vehicles, offices, a LPG facility, equity interests in KPM and TNG, and contractual rights conferred by Kazakhstan to KPM and TNG under the contracts and licenses for the Borankol field, the Tolkyn field, and the Contract 302 Properties.

35. All of the complained-of acts and omissions by Kazakhstan at issue in this case occurred well after the ECT entered into force for Moldova, Romania, and Kazakhstan on April 16, 1998.[58]

D. Dispute Relating to Part III of the ECT

36. The acts and omissions of Kazakhstan described in the present Statement of Claim violate a number of protections accorded to Claimants under Part III of the ECT, namely the protections found in Articles 10, 11, 13 and 14 of the Treaty. Kazakhstan's violations of those protections are addressed in detail in Section VII below.

E. Notice of Dispute

37. Article 26(2) of the ECT provides for a three-month notice period before the commencement of arbitration. That requirement is satisfied.

38. Claimants repeatedly notified Kazakh officials of the present dispute and, in the absence of an amicable settlement, of their intention to submit the present dispute to international arbitration. On March 18, 2009, Claimants wrote to Kazakhstan's MEMR offering to have the dispute arbitrated pursuant to the SCC Arbitration Rules.[59] The following day, Claimants attended a meeting with Kazakh authorities in order to pursue amicable settlement of the present dispute, but the meeting was fruitless.[60]

39. On May 7, 2009, Claimants wrote to the President of Kazakhstan, once again seeking an amicable settlement of the dispute and indicating their intention to submit the present dispute to international arbitration.[61]

40. After the Tribunal in this case had been constituted and a schedule for the proceeding established, Kazakhstan demanded a suspension of the proceeding to permit further settlement negotiations, contending that the preceding notifications and settlement efforts by Claimants had been inadequate and did not satisfy the Article 26(2) notice period. By agreement of the parties, and with the acquiescence of the Tribunal, the original schedule was modified to permit time for additional

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[58] Date of the ECT's entry into force for Moldova, Romania, and Kazakhstan, C-28.

[59] *See* Letter from Claimants to the MEMR dated March 18, 2009, C-41.

[60] *See* Draft Minutes of the meeting dated March 19, 2009, C-42.

[61] *See* Letter from Claimants to the President of Kazakhstan dated May 7, 2009, C-43.

settlement negotiations. Meetings between the parties were held on March 10, 2011, and were followed by subsequent exchanges of correspondence. Those discussions have not led to resolution of this dispute.

41. In view of the above, Claimants have indisputably complied with the requirements set forth under Article 26 of the ECT. This Tribunal therefore has jurisdiction over the present dispute.

III. CLAIMANTS' INVESTMENTS IN KAZAKHSTAN

A. Claimants' Acquisition of KPM and TNG

42. Claimants began investigating investment opportunities in Kazakhstan in 1999.[62] They identified KPM as an attractive opportunity because it held the exploration and production rights to the Borankol field, which covers approximately 37.41 square kilometers.[63] The Borankol structure was discovered in 1959, with test drilling finalized in 1973. It was viewed by many as having only marginal development potential, but Claimants saw significant potential reserves obscured by previously poor operation and management.[64]

43. KPM owned the Borankol rights pursuant to Contract No. 305 on Exploration and Extraction at the "Borankol" deposit (Mangystau Oblast), executed between the Agency of the Republic of Kazakhstan on Investments and KPM, and dated March 30, 1999 (the "KPM Subsoil Use Contract" or "Contract No. 305").[65]

44. Importantly, under the KPM Subsoil Use Contract, the Government guaranteed that the provisions of the Contract would remain in force for the duration

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62 Stati Statement ¶¶ 9, 13.

63 *See* License for the right to use subsoil issued to KPM, series MG No. 309-D (oil) dated May 23, 1997, Appendix 3, C-45.

64 Stati Statement ¶ 13.

65 Contract No. 305, C-45, Contract No. 305 was issued pursuant to the License for the right to use subsoil, series MG No. 309-D (oil) dated May 23, 1997, issued by the Government. *See* KPM License, C-45. The license was valid until May 23, 2022, with the possibility to extend. *See* Contract No. 305, Article 3.3, C-45. The duration of Contract No. 305 is 25 years, including a 4-year exploration period and a 21-year production period. Contract No. 305, Articles 9.1 and 11.1, C-45, Article 9.1 of Contract No. 305 specifically provides that: "The Exploration Period consists of 4 (four) consecutive years according to the License and may be extended twice with duration of each period up to two years by the mutual consent of the Parties and the Licensing authority in accordance with the Legislation on subsoil use." C-45. The 4-year exploration period was extended twice for two years and officially ended on March 29, 2007. Contract No. 305, Supplement dated May 19, 2003, and Addendum No. 4 dated February 1, 2005, C-45.

of the Contract,[66] and also guaranteed to stabilize the law applicable to the Contract by explicitly agreeing that "Changes and additions to the legislation made after the signature of the Contract that deteriorate the position of the Contractor shall not be applicable to this Contract."[67] The Government's undertaking also applied to the tax regime, which was stabilized to incorporate the tax legislation in effect on April 1, 1999.[68]

45. In December 1999, Ascom acquired a 62% interest in KPM and the KPM Subsoil Use Contract.[69] Ascom acquired the remaining 38% interest in 2004.[70] In May 2005, KPM was reorganized from a Joint Stock Company ("JSC") into a Limited Liability Partnership ("LLP").[71]

46. Through the acquisition of their interest in KPM, Claimants learned that the owners of TNG were also looking for operators and investors.[72] TNG owned the rights for exploration and extraction of hydrocarbons in the nearby Tolkyn field, which covers approximately 36.1 square kilometers.[73] The structure in the Tolkyn field had been discovered in 1992. As with Borankol, Tolkyn was viewed by many as a marginal prospect, but Claimants saw significant potential.[74] TNG owned the Tolkyn Field rights pursuant to Contract No. 210 on Exploration and Extraction at the "Tolkyn" deposit (Mangystau Oblast), executed between the Agency of the Republic of Kazakhstan on Investments and TNG, and dated August 12, 1998 (the "TNG Tolkyn Subsoil Use Contract" or "Contract No. 210").[75]

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66 Contract No. 305, Article 29.1, C-45.

67 Contract No. 305, Article 29.2, C-45.

68 Contract No. 305, Articles 17.11 and 29.2, C-45.

69 *See* Letter from the Agency of the Republic of Kazakhstan on Investments No. 3-3016 dated November 19, 1999, C-47; Letter from KPM to the Agency of the Republic of Kazakhstan on Investments dated December 23, 1999, C-49; Letter from Agency of the Republic of Kazakhstan on Investments to KPM dated December 30, 1999, C-48.

70 *See* Register of KPM's Shareholders No. 1395, dated 15 December 2004, C-50.

71 *See* Articles of Association of Limited Liability Partnership "Kazpolmunay" dated April 20, 2005, C-36.

72 Stati Statement ¶ 14.

73 *See* License for the right to use subsoil issued to TNG, series MG No. 242-D (oil) dated December 4, 1997, Appendix 3, C-52.

74 Stati Statement ¶ 14.

75 Contract No. 210, C-52. Contract No. 210 was issued pursuant to the License for the right to use subsoil, series MG No. 242-D (oil) dated December 4, 1997 issued by the Government. *See* TNG Tolkyn License, C-52. According to Contract No. 210, its duration is 21 years, including a 9-year

47. TNG also owned the hydrocarbon exploration rights in the Contract 302 Properties. TNG owned those rights pursuant to Contract No. 302, executed between the Agency of the Republic of Kazakhstan on Investments and TNG, and dated July 31, 1998 (the "302 Properties Subsoil Use Contract" or "Contract No. 302").[76] Contract No. provided for a six year exploration period with two permissible contractual extensions of two years each.[77] The exploration period was first extended until July 31, 2006.[78] Flooding from the Caspian Sea basin, however, suspended exploration work for two years and eight months. The MEMR therefore extended the exploration period until March 30, 2009, without counting this *force majeure* extension against the two permissible contractual extensions.[79] The second contractual extension of the exploration period was therefore scheduled to begin on March 30, 2009.[80]

48. As with KPM's Contract No. 305, the Government guaranteed to stabilize the law applicable to the TNG Contracts by explicitly agreeing that "Changes and additions to the legislation made after the signature of the Contract that deteriorate the position of the Contractor shall not be applicable to this Contract."[81] The Government's undertaking also applied to the tax regime, which was stabilized to incorporate the tax legislation in effect on April 1, 1999.[82]

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exploration period and a 12-year production period. *See* Contract No. 210, Article 3.4, C-52. Article 3 of Contract No. 210 was amended on May 28, 2002 to change the exploration period from three to five years due to changes in the applicable legislation. The exploration period was extended twice for two-years and officially ended on December 4, 2006. *See* Supplements to Contract No. 210 dated May 28, 2002, December 19, 2003, and February 1, 2005, C-52. Contract No. 210 was valid until December 4, 2018, with the possibility to extend. Contract No. 210, Article 3.4, C-52.

76 Contract No. 302, C-53. Contract No. 302 was issued pursuant to the License for the right to use subsoil, series NG No. 243-D (oil) dated December 4, 1997, issued by the Government. *See* License for the right to use subsoil issued to TNG, series MG No. 243-D (oil) dated December 4, 1997, C-53.

77 Contract No. 302, Article 3, C-53.

78 *See* Supplement to Contract No. 302 dated December 19, 2003, C-53.

79 *See* Supplement No. 5 to Contract No. 302 dated February 7, 2007, C-53.

80 *See* Contract No. 302, Article 3, as amended by Supplement No. 5 dated February 7, 2007, C-53.

81 Contract Nos. 210 and 302, Articles 24.1, C-52 and C-53.

82 Contract No. 210, Article 12.11, C-52; Contract No. 302, Article 24.1, C-53.

49. On May 17, 2000, Ascom acquired 75% of TNG and the TNG Subsoil Use Contracts.[83] As of July 2000, Claimants were the operators for both the Borankol and Tolkyn fields, as well as for the Contract 302 Properties.[84]

50. In March 2002, Ascom transferred its 75% interest in TNG to its subsidiary, Gheso S.A. ("Gheso").[85] Gheso also acquired the remaining 25% interest in TNG in April and May 2002, bringing Gheso's ownership interest in TNG to 100%.[86] In May 2003, Gheso transferred its 100% interest in TNG to its affiliate Terra Raf.[87] In May 2005, TNG was reorganized and transformed from a JSC to a LLP.[88]

51. Claimants notified Kazakhstan's MEMR of the KPM and TNG reorganizations from JSCs to LLPs in May 2005, and the Kazakh Ministry of Justice officially approved the transformations.[89] The changes from JSC to LLP were further memorialized in State-executed Supplements to the KPM and TNG Subsoil Use Contracts.[90]

B. Claimants' Development of Their Investments in Kazakhstan

1. The Borankol and Tolkyn Fields

52. The Tolkyn and Borankol fields are approximately 50 kilometers apart. Aktau, the capital of the Mangystau region where the fields are located, is approximately 400 and 500 kilometers, respectively, from the Borankol and the Tolkyn fields. The closest town from the Borankol field is Opornaya, which is

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83 *See* Sale and Purchase Agreements dated May 17, 2000, between Ascom, Kainar-Ltd. LLP, Dobro PKF LLP, and Anavi LLP, C-54.

84 Stati Statement ¶ 15.

85 *See* Sale and Purchase Agreement between Ascom and Gheso JSC, registered by the TNG's registrar on 13 March 2002, C-55.

86 *See* Sale and Purchase Agreements between Gheso JSC and Kainar-Ltd. LLP (dated April 30, 2002), C-56; Dobro PKF LLP (dated May 3, 2002), C-57; and Anavi LLP (dated May 3, 2002), C-58; Register of TNG's Shareholders dated 7 May 2002, C-59.

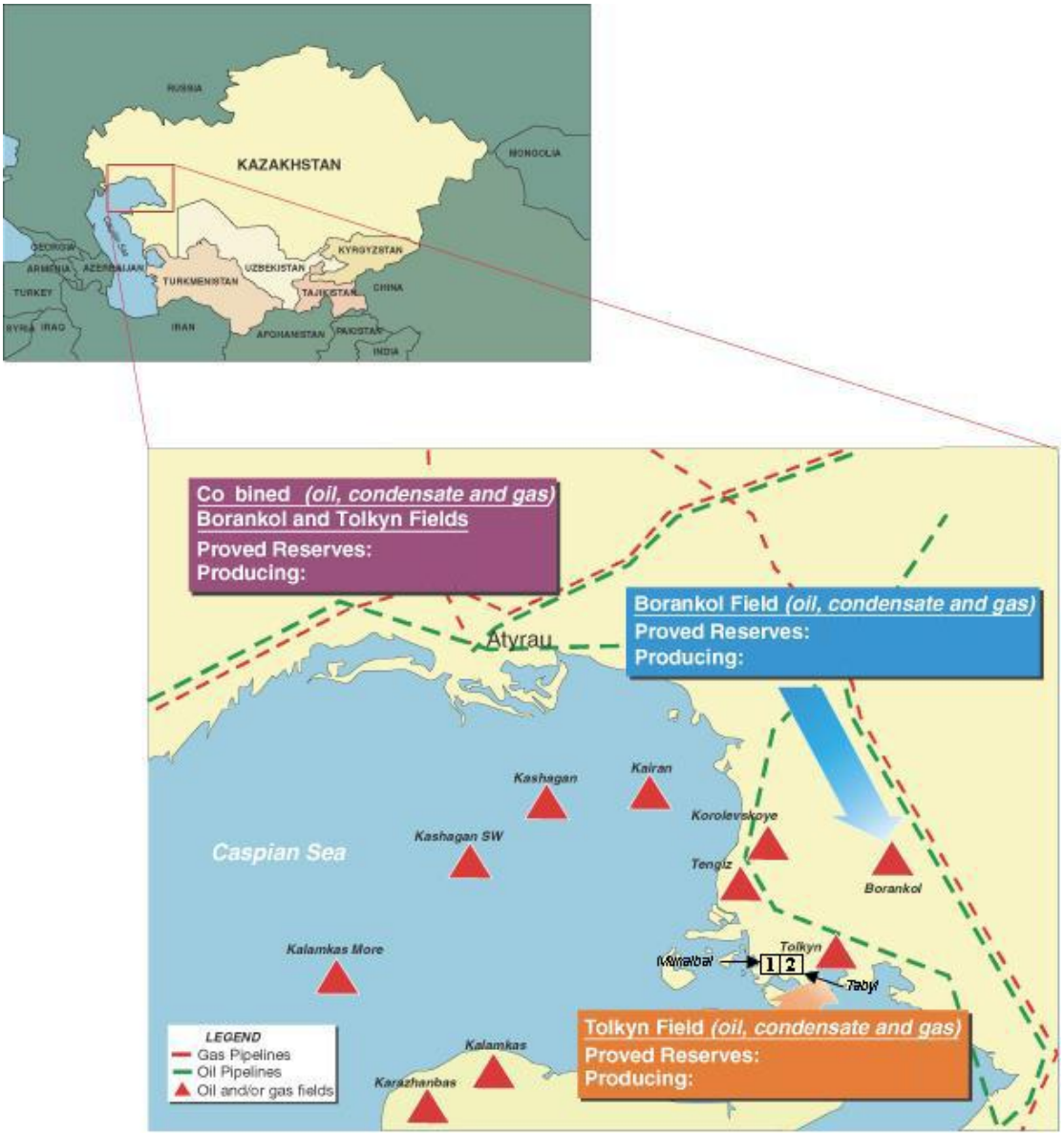
87 *See* Sale and Purchase Agreement between Gheso and Terra Raf dated May 12, 2003, C-60.

88 Articles of Association of Limited Liability Partnership "Tolkynneftegaz" dated April 12, 2005, C-39.

89 TNG's and KPM's Certificates of Registration respectively dated May 16 and 13, 2005, C-61 and C-62.

90 Supplement No. 5 to the KPM Subsoil Use Contract dated March 30, 2006; Supplement No. 7 to the TNG Tolkyn Subsoil Use Contract dated July 28, 2006; and Supplement No. 4 to the TNG Subsoil Use Contract No. 302 dated December 1, 2006, C-45, C-52, and C-53.

approximately 15 kilometers away. The map below shows the location of the fields and block within Kazakhstan:



53. Although located in a relatively remote region of Kazakhstan, the Borankol and Tolkyn fields were attractive investments for Claimants because of their untapped reserves potential, and because the fields are serviced by a railroad with a station in Opornaya and two main oil and gas transportation pipelines for long-distance delivery of the production to purchasers, end users, and product brokers.[91] In addition to rail transport of condensate, production from the Tolkyn and Borankol fields is delivered into the two, proximate main oil and gas

[91] *See* FTI Report, Figure 12.

transportation pipelines: (1) the Uzen-Atyrau-Samara main oil transportation pipeline, which is 1,380 kilometers in length and is owned and operated in Kazakhstan by KazTransOil JSC, a subsidiary of KazMunaiGas;[92] and (2) the Central Asia-Center main gas transportation pipeline, which is 4,892 kilometers in length and is operated in Kazakhstan by InterGas Central Asia JSC, also a subsidiary of KazMunaiGas.[93]

54. Claimants' substantial investment and rapid implementation of their exploration, drilling, and development programs yielded significant crude oil, condensate, and gas production from the Borankol and Tolkyn fields.[94] To handle this production, Claimants constructed an extensive infrastructure of gas processing and oil treatment facilities, storage tanks, and in-field gathering and delivery lines for transporting product from the well-head to processing, treatment, and storage facilities, as well as the Government-owned and operated main oil and gas pipelines. Because the Borankol field is closer to the Opornaya train station and the main oil and gas pipelines, both the oil treatment and gas processing facilities were located in the Borankol field.

55. The KPM and TNG gathering systems were designed to (i) deliver gas, oil and condensate from the Borankol and Tolkyn field wells to the Borankol field processing facilities, which separate oil from water (KPM) and gas from condensate (TNG) as necessary prerequisites for acceptance by the main pipelines; (ii) deliver gas directly from TNG's processing facility to the Central Asia-Center main gas pipeline; (iii) deliver oil and condensate from the processing facilities to KPM's and TNG's storage tanks; and (iv) deliver oil from KPM's storage tanks to the KazTransOil main oil pipeline. The diagram below shows the key facilities and infrastructure:

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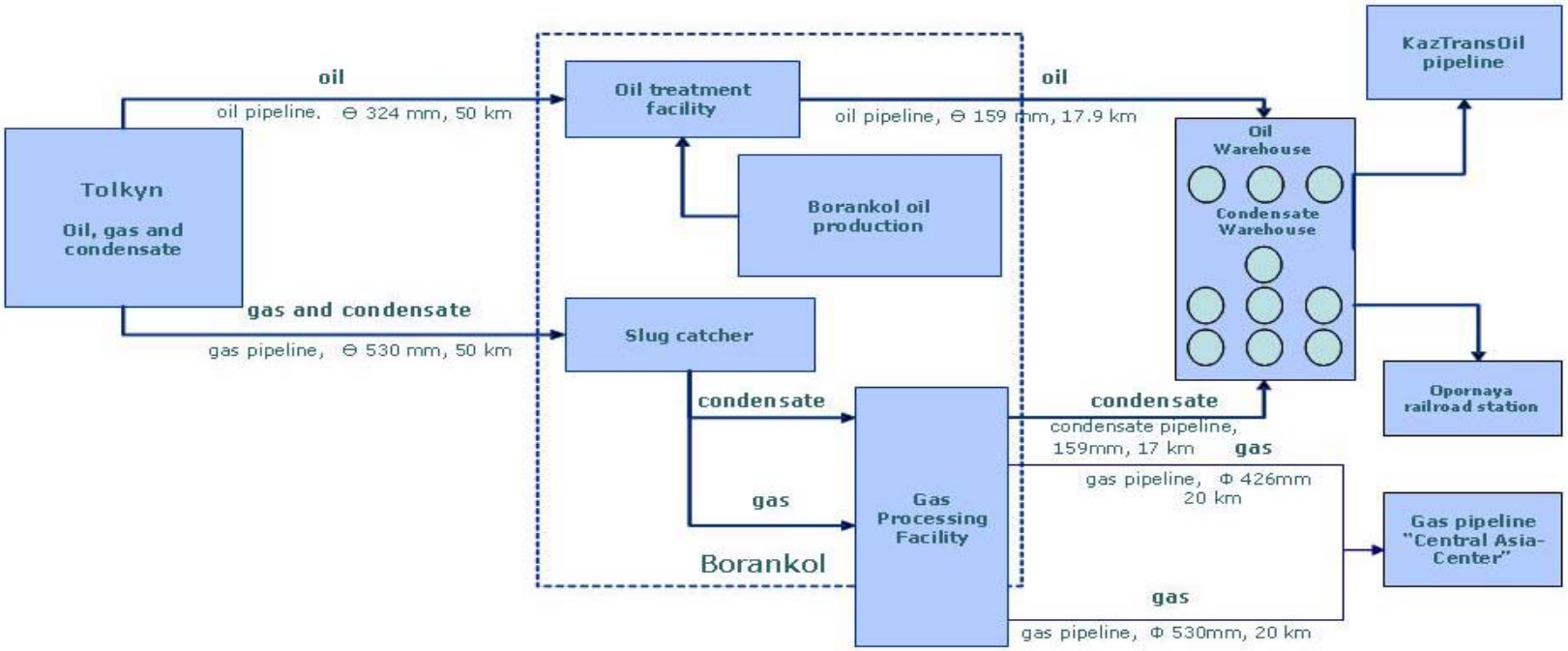
92 *See* "Uzen-Atyrau-Samara Oil Pipeline (Kazakhstan, Russian Federation)", at: http://www.iot.kiev.ua/index.php?option=com_content&view=article&id=79&Itemid=82&lang=en; KazMunaiGas website, at: http://www.kmg.kz/en/group_companies/subsidiary/kaztransoil/.

93 *See* ICA Intergas Central Asia website, at: http://www.intergas.kz/eng/about/history/; KazMunaiGas website, at: http://www.kmg.kz/en/group_companies/subsidiary/kaztransgaz/.

94 *See* FTI Report, Section 6.


oil
oil pipeline. Θ 324 mm, 50 km
Tolkyn
Oil, gas and condensate
gas and condensate
gas pipeline, Θ 530 mm, 50 km
Oil treatment facility
Borankol oil production
Slug catcher
condensate
gas
Gas Processing Facility
Borankol
oil
oil pipeline, Θ 159 mm, 17.9 km
condensate
condensate pipeline, 159mm, 17 km
gas
gas pipeline, Φ 426mm 20 km
gas
gas pipeline, Φ 530mm, 20 km
Oil Warehouse
Condensate Warehouse
KazTransOil pipeline
Opornaya railroad station
Gas pipeline "Central Asia-Center"

56. Oil and condensate production from the Borankol and Tolkyn fields was sold into the export market through sale arrangements with Vitol, one of the world's largest oil traders.[95] The price of oil under the contracts with Vitol was benchmarked against the international market price for Urals, while the condensate price was benchmarked against the international market price for Brent. Claimants delivered oil FOB Odessa through the KazTransOil main oil pipeline, and delivered condensate FCA Opornaya, where condensate was further routed by Vitol via railway to Caspian Sea ports, Finland, and Port Kavkaz in Russia.

57. TNG's gas production was historically sold through agreements with AktauGazServis, KazRosGaz, MAEK, and Kemikal, or to local Kazakhstan end users.[96] In early 2006, Claimants reduced their sale of gas outside the Mangystau region to accommodate a planned undertaking with the Moldovan Ministry of Industry and Infrastructure to deliver gas to Moldova at a substantial discount off the Gazprom price.[97] With its concentration of gas sales in the Mangystau region, the Kazakh Competition Authority concluded in 2006 that Claimants' market share had increased above 50% and included TNG on a register of market participants holding a dominant position in the Mangystau region gas market.[98] Once on the register, producers are prohibited from raising their gas prices without prior approval of the competition authority. Therefore, TNG sold its gas at prices well below those available on the international markets. Claimants sold at four different discounted prices: USD 10 per thousand cubic meter (mcm) for Beyneu buyers (the local population); USD 30 per mcm for buyers from the town of Aktau; USD 45 per mcm for MAEK, the operator of the local power plant; and USD 55 per mcm for other local companies.

58. In early 2007, Kazakhstan approached Claimants with a proposal for the provision of gas to KazAzot, a local chemical company, as part of a project of national priority.[99] Various Kazakh Ministries, the Governor of the Mangystau Region, KazAzot, and Mitsubishi, as general contractor, were projecting the

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95 *See* FTI Report ¶¶ 5.16-5.18.

96 *See* FTI Report ¶¶ 5.19.

97 Stati Statement ¶ 22; FTI Report ¶ 5.22.

98 Notification of the Competition Protection Committee of the Kazakh Ministry of Industry and Trade to TNG dated June 20, 2006, C-64.

99 Lungu Statement ¶ 19.

development of an ammonia-carbamide complex to produce fertilizers for national use in agriculture.[100] However, KazAzot needed to secure a gas supply.[101] TNG, the fourth largest gas producer in Kazakhstan, was the obvious contender, since TNG could reliably provide the requisite volumes of gas and was located near the planned chemical plant.[102] Therefore, the Kazakh MEMR drafted and sent to Claimants a Memorandum of Understanding for their approval.[103] Claimants agreed to provide certain volumes of gas to KazAzot provided that Claimants be allowed to export certain volumes of gas at international market prices.[104]

59. On May 7, 2007, Claimants, the MEMR, the Governor of the Mangystau Region, the operator of the main gas pipeline KazTransGas (a subsidiary of the national oil company KazMunaiGas), and the owner of a local chemical company KazAzot agreed to enter into gas supply and transport arrangements.[105] Pursuant to these arrangements, Claimants would sell certain volumes of gas at a price substantially above the discounted prices to KazAzot (first at near market prices, followed by at the international market price after two years), and TNG, through KazTransGas, will be allowed to export certain volumes of gas at international market prices.[106] Over the following year, Claimants conducted extensive negotiations to conclude the prices, volumes, and conditions of the agreement.[107]

60. On April 28, 2008, the MEMR, TNG, KazAzot, and KazTransGas entered into a first agreement setting out the parties' understanding.[108] On May 16, 2008, the Prime Minister of Kazakhstan, the MEMR, KazMunaiGas, KazTransGas, KazAzot, and TNG agreed that the parties should enter into tri-partite agreements to

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100 *Id*.

101 *Id*.

102 *Id*.

103 *Id*.

104 *Id*.

105 Memorandum of Understanding between the MEMR, the Governor of the Mangystau Region, KazMunaiGas, KasTransGas, KazAzot, Ascom, KPM, and TNG, dated May 7, 2007, C-300.

106 *Id.* For a complete description of TNG's agreements with the State for sale of gas at market prices, *see* FTI Report ¶¶ 5.21-5.34.

107 Lungu Statement ¶ 20.

108 Agreement for the Implementation of the Memorandum of Understanding of May 7, 2007 dated April 28, 2008, C-301.

resolve the issues.[109] Later in the summer of 2008, a tri-partite agreement followed between TNG, KazAzot, and KazTransGas setting out the formula for the price calculation, the volumes of gas concerned, and the conditions of supply and export.[110] Subsequently, Kazakhstan decided to replace KazTransGas with its parent company KazMunaiGas. A November 17, 2008 agreement memorialized the parties' agreement on price, volumes, and conditions.[111] TNG and KazMunaiGas signed the agreement and it was hand-delivered to KazAzot for signature, but KazAzot never signed the agreement.[112]

61. In late November 2008, KazAzot requested that KazMunaiGas perform another audit of the ammonia-carbamide complex project, especially regarding the delivery prices of gas, which KazAzot allegedly wanted reconsidered.[113] KazAzot indicated that it would sign the November 17, 2008 agreement within six months subject to the audit being performed.[114] In August 2009, Kazakhstan, the Governor of the Mangystau Region, KazAzot, and Mitsubishi confirmed their intention to go forward with the ammonia-carbamide complex. However, on August 26, 2009, the Governor of the Mangystau Region asked Prime Minister Massimov to accelerate the State's cancellation of TNG's and KPM's Subsoil Use Contracts and, implicitly, to transfer TNG's assets to KazAzot.[115] The Governor referred to instructions dated June 5, 2009 given by the Kazakh Prime Minister to the MEMR, the Minister of Finance, the Ministry of Justice, and the multi-billion sovereign wealth fund of Kazakhstan, Samruk-Kazyna.[116] The Prime Minister apparently instructed these Kazakh authorities to orchestrate the termination of Claimants' Subsoil Use Contracts.[117]

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109 Minutes of meeting between the MEMR, KazMunaiGas, KazTransGas, KazAzot, and TNG, dated May 16, 2008, C-63.

110 2008 tri-partite Agreement between TNG, KazTransGas, and KazAzot, C-302.

111 Tri-Partite Agreement between TNG, KazMunaiGas, and KazAzot, dated November 17, 2008, C-97.

112 Lungu Statement ¶ 21.

113 Lungu Statement ¶ 22.

114 Lungu Statement ¶ 22.

115 Letter from the Governor of the Mangystau Region to the Prime Minister of the Republic of Kazkahstan, dated August 26, 2008, C-293.

116 *Id.*

117 *Id.*

2. The LPG Plant

62. In 2006, TNG entered into an agreement with Vitol to construct and operate a liquefied petroleum gas processing facility ("LPG") plant.[118] At that time, TNG's direct gas production was sold locally at a heavily discounted price, and among the options for acquiring a higher and more attractive price for the gas was the sale of liquefied petroleum gas products. The LPG plant would have produced propane, butane, and pentane plus.[119] Unlike natural gas, LPG products can be delivered by means of rail and truck avoiding the Kazakhstan regulatory affects on pricing of products transmitted through the pipeline system.[120] The LPG plant was located on the Borankol field, within the gas and condensate processing facilities, and upon its completion, the plant would have been one of the largest in Kazakhstan. Claimants intended to sell the LPG products mainly in Poland, a steadily growing market, as well as other Eastern European countries, Turkey, and Morocco.[121]

63. Apart from gas produced at the Tolkyn and Borankol fields, the LPG plant would have had the capacity to process gas produced from the Contract 302 Properties, or alternatively from neighboring fields in the event that gas production from Claimants' fields declined below the LPG plant's capacity.[122]

64. Claimants invested more than USD 245 million in development and construction of the LPG plant.[123] Claimants were forced to halt construction of the LPG plant in May 2009 due to cash constraints and operational difficulties caused by the State's increasing harassment measures. When the State directly expropriated Claimants' investments in July 2010, the LPG plant was over 90% complete, with the requisite materials to finish construction already on site, and Claimants had also completed the associated power and water supply systems, sewage system, reservoirs, pumping units, and intermediate and final storage facilities.[124]

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[118] *See* FTI Report ¶¶ 6.22 - 6.24.

[119] *Id.* ¶ 6.22.

[120] *Id.* ¶ 6.24.

[121] *Id.*

[122] *See* Lungu Statement ¶ 26.

[123] *See* FTI Report ¶ 6.23.

[124] *See* Lungu Statement ¶ 27.

65. From the totality of events that subsequently unfolded, it is apparent that Claimants' LPG plant was itself one of the motivations for Kazakhstan's expropriation of Claimants' investments.[125] Kazakhstan acquired a nearly complete, state-of-the-art LPG plant at no cost – an asset Kazakhstan had listed on the Mangystau Region Development Plan as essential – along with substantial accompanying gas reserves and complex infrastructure.

3. Discoveries in the Contract 302 Properties

66. Through October of 2008, Claimants had invested approximately USD 43 million conducting exploration work in the Contract 302 Properties.[126] They conducted initial seismic work in the Contract 302 Properties starting in 2004. In late 2007, Claimants commenced a test well in the block's East Munaibay structure, and on July 20, 2008, discovered substantial oil and gas deposits.

67. TNG first reported the East Munaibay discovery to the MEMR on July 24, 2008,[127] and filed a statement of its intention to start the evaluation stage of the structure on August 11, 2008.[128] On October 7, 2008, the MEMR acknowledged TNG's application for evaluation of the discovery.[129] However, Claimants withdrew their statement of intention to begin evaluation on October 10, 2008, because they felt that it was still too early in the exploration stage to commence evaluation.[130] To continue the exploration stage in the Contract 302 Properties, Claimants notified the MEMR on October 14, 2008, of their intention to exercise their contractual right to extend the exploration period by two years, pursuant to Article 3 of Contract No. 302.[131]

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125 *See* Lungu Statement ¶ 28.

126 *See* FTI Report ¶ 6.21.

127 *See* Letters from TNG to the Geology and Subsoil Use Committee of the MEMR and to the MEMR, dated July 24, 2008, C-20.

128 *See* Application filed by TNG with the MEMR, with an evaluation program and explanatory note, dated August 11, 2008, C-21.

129 *See* Letter from the MEMR to TNG dated October 7, 2008, C-22.

130 *See* Letter from TNG to the MEMR dated October 10, 2008, C-66.

131 Application from TNG to the MEMR, with explanatory note and draft work program, dated October 14, 2008, C-67.

68. In October 2008, Claimants also commenced drilling an exploratory well in the Bahyt structure of the Contract 302 Properties, which had shown evidence of gas in the lower Triassic stratus.[132]

C. Claimants' Initial Efforts to Sell KPM and TNG and The First Round of Indicative Offers

69. In the summer of 2008, Claimants made an independent business decision to explore a sale of KPM, TNG, and the LPG plant.[133] The full extent and value of the deposits in the Contract 302 Properties were still in the assessment stage at that point, so Claimants did not offer the Contract 302 Properties in the sale process.[134] Claimants retained Renaissance Capital, a leading investment bank focused on the emerging markets of Russia, Ukraine, and Kazakhstan, to put together a sale process and procedure they referred to as "Project Zenith."[135] On July 18, 2008, Renaissance Capital sent out a "teaser" offer to 129 potential purchasers of the properties.[136] The potential purchasers that were targeted included KazMunaiGas.[137] In late July 2008, Claimants also retained the services of KPMG to perform vendor financial and tax due diligence.[138] On August 29, 2008, KPMG issued a complete Vendor Due Diligence presentation for "Project Zenith."[139]

70. Claimants and Renaissance Capital also prepared an Information Memorandum containing details about the properties, including their infrastructure, production, reserves and capacities.[140] In mid-August 2008, Renaissance Capital distributed the Information Memorandum to 41 parties that had expressed an interest in the properties and signed a confidentiality agreement,[141] including KazMunaiGas.

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132 *See* Application from TNG to the MEMR, with explanatory note and draft work program, dated October 14, 2008, C-67.

133 Stati Statement ¶ 17.

134 Lungu Statement ¶ 29; Stati Statement ¶ 17.

135 Stati Statement ¶ 18; Lungu Statement ¶ 29.

136 *See* Project Zenith - Opportunity to acquire attractive upstream oil & gas assets in Kazakhstan dated July 18, 2008, C-16. Project Zenith – Overview of Non-Binding Offers dated September 27, 2008, C-17.

137 *See* Project Zenith – Overview of Non-Binding Offers dated September 27, 2008, C-17.

138 *See* Engagement letter of KPMG dated July 29, 2008, C-68.

139 *See* Project Zenith – Vendor Due Diligence by KPMG dated August 29, 2008, C-69.

140 *See* Project Zenith – Information Memorandum, C-70.

141 *See* Project Zenith – Overview of Non-Binding Offers dated September 27, 2008, C-17.

71. By October 1, 2008, Claimants had received eight indicative offers for the properties. The top four bids were: USD 1.55 billion from Korea National Oil Company ("KNOC"); USD 1.3 billion from OMV E&P; USD 1 billion from Total; and USD 916 million from Turkish Petroleum Corporation. The lowest bid was USD 550 million from Meridian Oil. KazMunaiGas tendered the third lowest bid at 754 million.[142] The valuations for the individual property components by the bidders ranged between USD 90 and 248 million for the Borankol field;[143] USD 367 to 1,067 million for the Tolkyn field;[144] and USD 70 to 280 million for the LPG plant.[145]

72. In the second phase of Project Zenith, Claimants planned to provide the bidders access to an electronic data room containing significantly greater detail about the properties than the Information Memorandum.[146] The purpose of the data room was to permit the bidders to more fully assess the properties in anticipation of making binding offers, which the sale process contemplated being made by November 14, 2008.[147] However, Claimants were somewhat disappointed with the bid ranges being indicated and, although they conducted management presentations for some of the bidders and answered questions from the bidders, they decided not to open the data room or proceed to the binding bid phase in November 2008.[148]

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[142] *See* Indicative Offer for Project Zenith from Meridian Petroleum dated October 1, 2008 (for USD 550 million), C-71; Indicative Offer for Project Zenith from China National Petroleum Corporation dated September 2008 (for USD 621 million), C-72; Indicative Offer for Project Zenith from KazMunaiGas dated September 25, 2008 (for USD 754 million); Indicative Offer for Project Zenith from Safmar dated September 26, 2008 (for USD 820 million), C-73; Indicative Offer for Project Zenith from Turkish Petroleum Corporation (for USD 916 million), C-74; Indicative Offer for Project Zenith from Total dated September 26, 2008 (for USD 1 billion), C-75; Indicative Offer for Project Zenith from OMV dated September 26, 2008 (for USD 1.3 billion), C-76; Indicative Offer for Project Zenith from Korea National Oil Corporation dated September 26, 2008, C-18 (for USD 1.55 billion).

[143] *See* Indicative Offer for Project Zenith from Meridian Petroleum dated October 1, 2008, C-71; Indicative Offer for Project Zenith from China National Petroleum Corporation dated September 2008, C-72.

[144] *See* Indicative Offer for Project Zenith from China National Petroleum Corporation dated September 2008, C-72; Indicative Offer for Project Zenith from Korea National Oil Corporation dated September 26, 2008, C-18.

[145] *See* Indicative Offer for Project Zenith from Meridian Petroleum dated October 1, 2008, C-71; Indicative Offer for Project Zenith from Korea National Oil Corporation dated September 26, 2008, C-18.

[146] *See* Project Zenith – Overview of Non-Binding Offers dated September 27, 2008, C-17.

[147] *See id.*

[148] Lungu Statement ¶ 34.

KazMunaiGas was undoubtedly disappointed at being excluded from the second phase, which would have given it an opportunity to scour the data room.

73. The non-binding indicative offers that were received prior to commencement of the State's campaign of harassment and indirect expropriation nevertheless provide a record of the actual reaction of willing and able buyers to an offer of the properties by a willing and able seller, with each acting at arms' length in an open and unrestricted market, without compulsion to buy or sell, and each having knowledge of the relevant facts.

IV. KAZAKHSTAN'S CAMPAIGN OF HARASSMENT AND INTERFERENCE WITH CLAIMANTS' INVESTMENTS

A. President Nazarbayev's Order

74. On October 6, 2008, the former President of Moldova, Vladimir Voronin, wrote a letter to President Nursultan Nazarbayev of Kazakhstan making numerous false and defamatory personal accusations against Anatolie Stati.[149] Claimants learned of the letter, but at the time viewed it as merely political in nature, rather than potentially disastrous to any of their investments.[150] Mr. Stati has been a supporter of greater democracy in Moldova, and he frequently sparred with President Voronin, who was far less committed to Moldova's democratic transformation.[151]

75. At the time, Mr. Stati considered President Voronin's letter to President Nazarbayev to be little more than vicious political gamesmanship, the consequences of which, if any, would be confined to Moldovan domestic politics.[152] President Nazarbayev, on the other hand, clearly seized upon the letter as a pretext to launch a wide-ranging investigation of Claimants' investments in Kazakhstan.[153] On October 14, 2008, President Nazarbayev issued instructions to Kazakh Deputy Prime

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149 *See* Former President Voronin's October 6, 2008 letter to President Nazarbayev, C-77.

150 Stati Statement ¶ 21; Witness Statement of Grigore Pisica dated May 17, 2011 ¶ 9 (hereinafter "Pisica Statement").

151 Stati Statement ¶¶ 21-22.

152 Stati Statement ¶ 23.

153 Claimants have recently learned that former President Voronin may have composed his letter at the request of President Nazarbayev himself. In an interview in 2010, former President Voronin explained, "... Mr. Nazarbaev addressed me this question: (in Russian) 'Listen, you have there a businessman working and etc. Write me a letter: who may he be, etc.'" Mr. Voronin clearly complied. *See* Interview of former President Voronin during the television program "In Depth" on PROTV Chisinau, dated January 24, 2011, C-78.

Minister, Umirzak Shukeyev, and the head of the Financial Police, Sarybai Kalmurzayev to "thoroughly investigate" all of Claimants' business activities in Kazakhstan.[154]

76. On the heels of President Nazarbayev's order, and under the supervision of the Deputy Prime Minister, the Kazakh Financial Police ordered the commencement of numerous audits and investigations of KPM and TNG by:

- the MEMR;[155]
- the Tax Committee;[156]
- the Customs Committee;[157]
- the National Bank of Kazakhstan;[158]
- the Geology Committee;[159]
- the Ecology Committee;[160] and
- the Ministry of Emergency Situations.[161]

77. The concerted and comprehensive audits of KPM and TNG conducted by those State agencies were unprecedented in scope. KPM and TNG were faced with banking, regulatory, technical, legal, and tax investigations at the same time, all initiated by the Financial Police. Neither KPM nor TNG had ever been subjected to such an assault. Claimants' in-country management spent most of its time answering requests for documents and visits made by the agencies. As former General Manager of TNG and Deputy General Manager of KPM, Mr. Alexandru Cojin explains:

> Generally speaking . . . I have witnessed KPM and TNG transformed from working, fully operative and functional

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154 *See* Letter from former President Voronin to President Nazarbayev with President Nazarbayev's investigation instructions, dated October 14, 2008, C-8.

155 Order from the Financial Police to the MEMR, dated October 20, 2008, C-9.

156 Order from the Financial Police to the Tax Committee, dated October 24, 2008, C-10.

157 Order from the Financial Police to the Customs Committee, dated October 18, 2008, C-11.

158 Order from the National Bank of Kazakhstan, dated November 2008, C-15.

159 Order from the Financial Police to the Geology Committee, dated October 28, 2008, C-12.

160 Order from the Financial Police to the Ecology Committee, dated October 28, 2008, C-13.

161 *See* Letter from the Ministry of Emergency Situation to the Financial Police, dated October 31, 2008, C-14.

> oil and gas production companies to two bodies that exist to answer requests from various Government officials and write reports. This process began around November 2008 and continued for nearly two years.
>
> The requests that came were voluminous and clearly intended to harass us . . . . In November and December 2008, the Financial Police attended numerous inspections of KPM and TNG and repeatedly called and questioned company employees . . . .[162]

78. Similarly, KPM's and TNG's Technical Director explains the harassment campaign as follows:

> When the monitoring bodies came to the field, I typically met with them to guide them and cooperate with their inspections, so I have knowledge of how the number and complexity of inspections increased from late 2008 onward. As an example, under the previous normal business circumstances, we had [inspections] once a year. Starting around this time, however, these inspections increased to around once per quarter. . . . Just about every government agency that had anything at all to do with our business increased the number and the complexity of their inspections of our facilities. As a result, I met with representatives from nearly a dozen agencies for weeks at a time every three months. Obviously, these meetings involved a great deal of my and others' time and greatly interfered with our abilities to carry out necessary and day-to-day business operations.[163]

B. Kazakhstan's Fabricated Criminal Charges Against KPM and TNG

1. Kazakhstan "Reclassified" KPM's and TNG's Field Pipelines as "Main" Oil and Gas Transportation Pipelines

79. The State's fabricated criminal charges against KPM and TNG were among the most damaging and pernicious components of the State's harassment campaign. The charges were based on the State's arbitrary reclassification of isolated segments of the in-field pipelines in the KPM and TNG gathering systems as "main" or "trunk" pipelines (referred to hereafter as "main" pipelines), and on the

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[162] Witness Statement of Mr. Alexandru Cojin (hereinafter "Cojin Statement") ¶¶ 6-8.

[163] Witness Statement of Victor Romanosov, dated May 12, 2010 (hereinafter "Romanosov Statement") ¶ 26.

allegation that KPM and TNG operated their (newly reclassified) gathering lines as "main" pipelines without a proper license.[164]

80. Neither KPM nor TNG has ever owned or operated a "main" pipeline.[165] Hence, neither KPM nor TNG ever needed a license to own or operate a "main" pipeline.[166] Main oil and gas transportation pipelines for the transport of blended product from multiple producers are defined by specific construction, safety, and operational standards under Kazakh law.[167] There are only a few companies in Kazakhstan that actually ***do*** hold such licenses, including Intergas Central Asia JSC, the subsidiary of KazMunaiGas that operates the 4,892 kilometer long Central Asia-Center main gas transportation pipeline, and KazTransOil, the subsidiary of KazMunaiGas that operates the 1,380 kilometer long Uzen-Atyrau-Samara main oil transportation pipeline.

81. Main pipelines are defined pursuant to Article 1(14) of the Law on Oil of the Republic of Kazakhstan as follows:

> A main pipeline means an engineering facility, consisting of a linear pipeline part related above ground facilities, service lines, remote control and communication facilities designated for transportion of oil ***from the Contractor's pipeline to points of transshipment to another mode of transport or points of processing or consumption.*** Pipelines operating in the gathering main mode shall not be referred to as main pipelines.[168]

82. In-field oil and gas gathering systems like the ones constructed by TNG and KPM are designed to deliver oil and gas from the field ***to*** main oil and gas transportation pipelines. They consist of a network of internal-use field pipes that deliver product from the well heads to on-site field processing facilities; from the processing facilities either directly to a main transportation pipeline or to on-site field storage facilities; and from the storage facilities to a main transportation pipeline.

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164 *See* Pisica Statement ¶ 12; *see also* Cojin Statement ¶¶ 3-5.

165 Cojin Statement ¶¶ 3-5.

166 *Id*.

167 Condorachi Statement ¶ 8.

168 *See* Article 1(14) of the Kazakh Law on Oil dated June 28, 1995 No. 2350, C-80. *See also* Condorachi Statement ¶ 8.

Under Kazakh law, such field gathering systems fall under different construction, safety, and operational standards than those that apply to main pipelines.[169]

83. At each step of the design, construction, and implementation of its in-field pipelines, KPM and TNG obtained approvals and permits from the relevant supervisory State agencies.[170] Indeed, KPM and TNG integrated the State's recommendations and comments in the design and construction of their in-field pipelines.[171] For example, in 2002, KPM and TNG applied to the MEMR for the appropriate licenses covering its new gathering system, and the MEMR issued the licenses.[172] And in 2005, when the companies were transformed into limited liability companies, KPM and TNG applied to the MEMR for re-licensing of their field pipelines. The MEMR re-issued new licenses.[173]

84. For the KPM gathering system, the segment of field pipeline that the State arbitrarily chose to reclassify as "main" extends from the field oil processing facility to the field storage tanks.[174] For the TNG gathering system, the segments that the State arbitrarily chose to reclassify are two parallel segments of gas field pipelines that run from the gas processing facility to the delivery point into the Central Asia-Center main pipeline and a segment of condensate field pipeline that runs from the gas processing facility to the storage tanks for condensate.[175] The diagram below shows in red the segments that the State reclassified:[176]

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169 Answers to Notice of Termination of Subsoil Use Contracts dated July 19, 2010, C-24-25, and C-26.

170 Romanosov Statement ¶ 28.

171 *Id*.

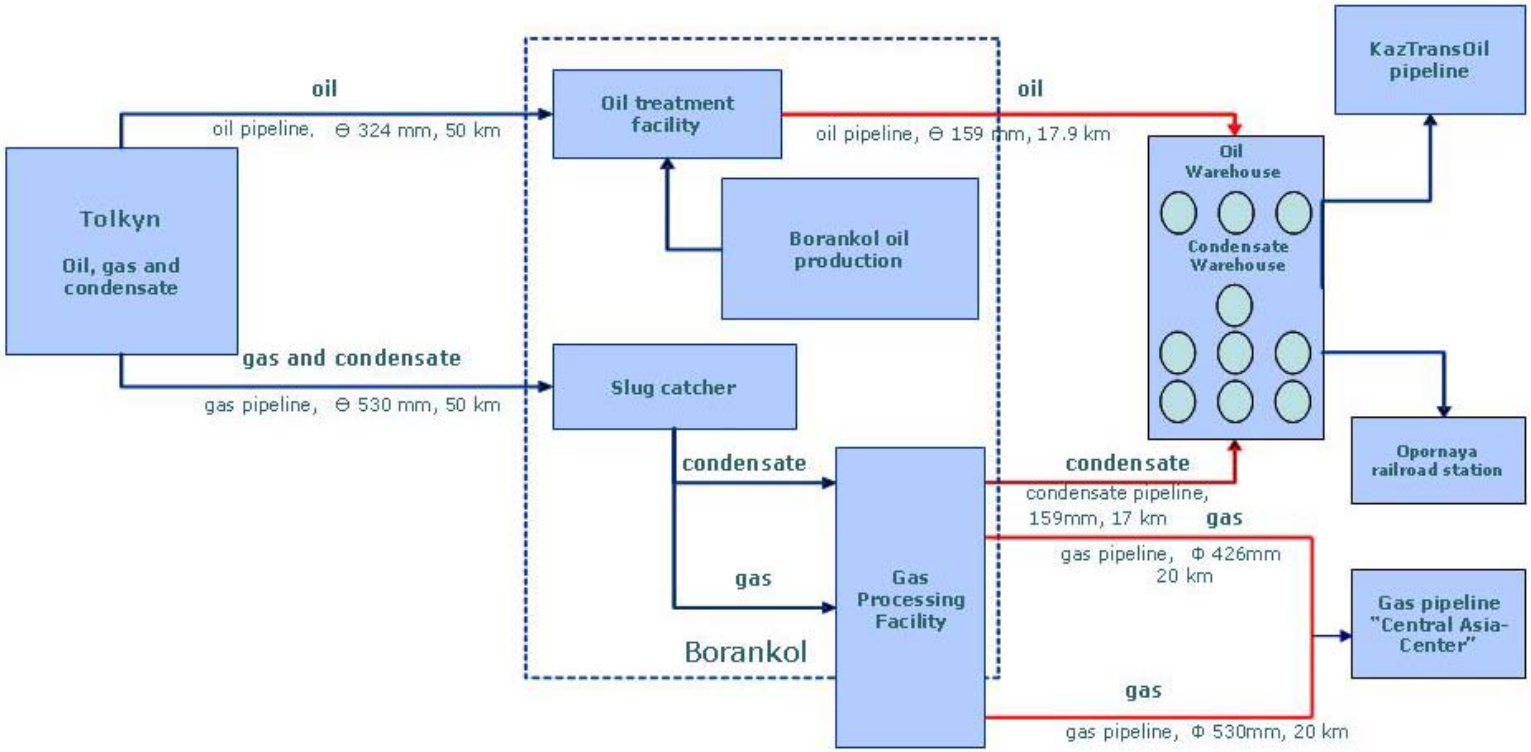
172 *See* Licenses issued to KPM and TNG dated September 26, 2002, C-81 and C-82; *see also,* Condorachi Statement ¶ 9.

173 *See* Licenses issued to KPM and TNG dated August 5, 2005, C-83 and C-84; *see also,* Condorachi Statement ¶ 9.

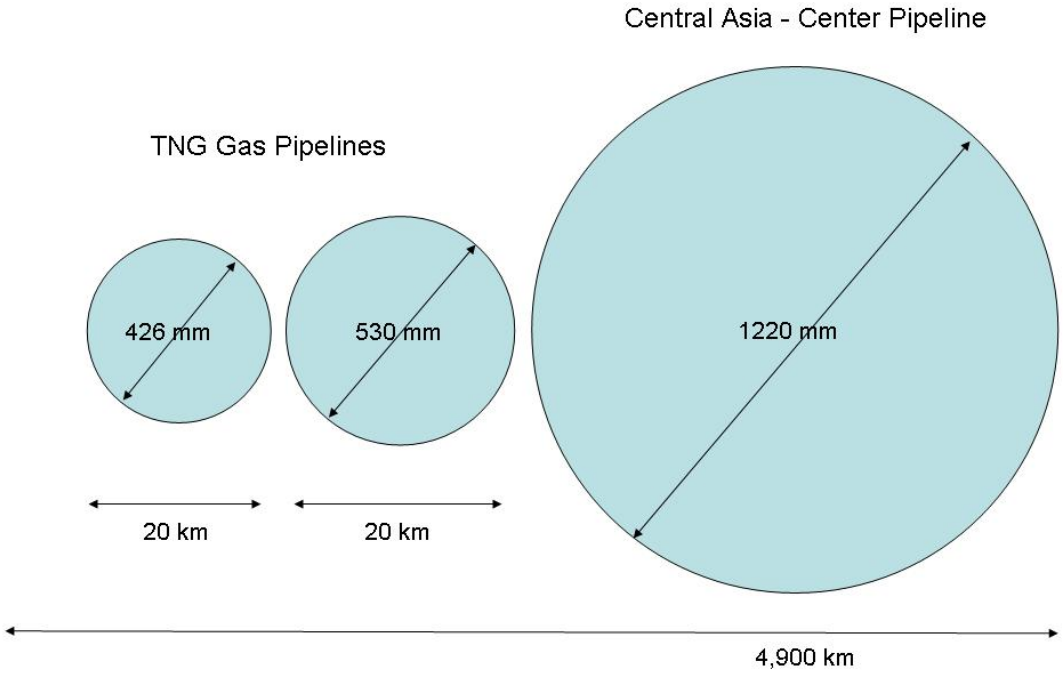
174 Report from the Tax Committee to the Financial Police dated December 2, 2008, C-85; *see also* Romanosov Statement ¶¶ 11-13.

175 Romanosov Statement ¶¶ 16-18.

176 Romanosov Statement ¶ 23.

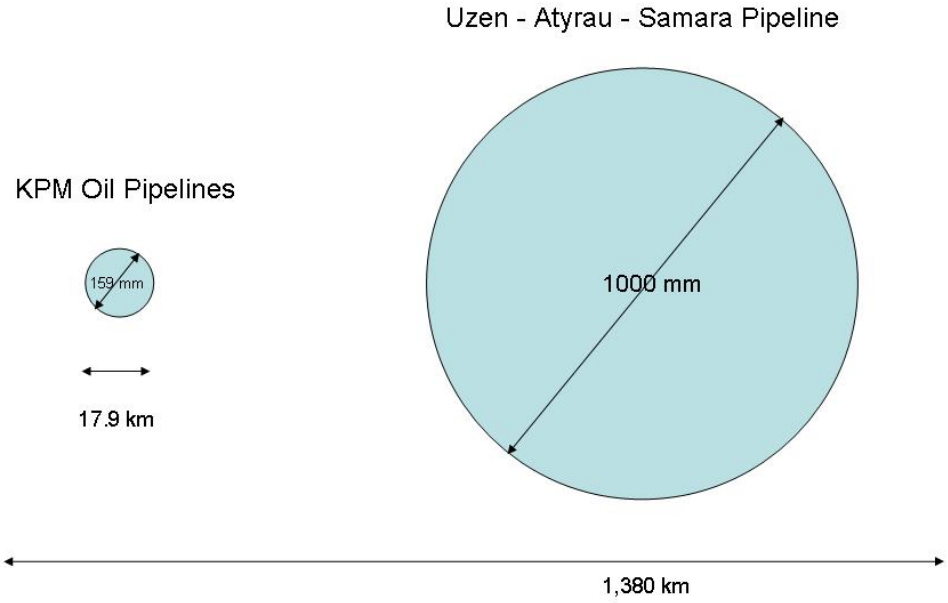

Tolkyn
Oil, gas and condensate
oil
oil pipeline, Θ 324 mm, 50 km
gas and condensate
gas pipeline, Θ 530 mm, 50 km
Oil treatment facility
Borankol oil production
Slug catcher
condensate
gas
Gas Processing Facility
Borankol
oil
oil pipeline, Θ 159 mm, 17.9 km
Oil Warehouse
Condensate Warehouse
KazTransOil pipeline
Opornaya railroad station
condensate
condensate pipeline, 159mm, 17 km
gas
gas pipeline, Φ 426mm 20 km
Gas pipeline "Central Asia-Center"
gas
gas pipeline, Φ 530mm, 20 km

85. To anyone familiar with the industry (and even some unfamiliar with the industry), the State's arbitrary reclassification of KPM's and TNG's in-field pipelines as "main" pipelines is absurd.[177] The drawing below shows the respective size and lengths of TNG's in-field gas pipelines compared to the actual main Central Asia-Center gas pipeline:



[177] *See* Condorachi Statement ¶ 8; Pisica Statement ¶ 15 ("This reclassification was astonishing and entirely baseless."); Romanosov Statement ¶ 22.

86. The absurdity is even more flagrant for KPM's in-field oil pipeline (which is the same diameter as TNG's condensate pipeline), as the comparison between KPM's gathering line and the KazTransOil main oil transportation pipeline illustrated below demonstrates:



87. The absurdity of the State's allegations was further underscored by the fact that the KPM and TNG gathering systems alone were subjected to "reclassification," despite virtually identical, even parallel, gathering systems being owned and operated by other oil and gas companies in the immediate vicinity – and indeed throughout Kazakhstan – none of which were subjected to reclassifications as "main" pipelines requiring licensure.[178] As Mr. Romanosov explains:

> [T]he Government clearly singled out our companies with these charges. Another company – a joint Kazakh / Turkish company called KazakhTurkMunai LLP – worked in the field adjacent to us. This company's pipelines ran parallel to our internal-use pipelines that the Government classified as "main" pipelines. The Government did not, however, bring any claim that KazakhTurkMunai was operating "main" pipelines, even though its pipelines were twice the size of ours. I personally questioned some of the

[178] Romanosov Statement ¶ 32.

> government inspectors about the difference in treatment, and they had no explanation for me. Another company, a state enterprise called Kulsarynefty, also operated a pipeline in a field adjacent to ours, and again, no claims of illegally operating a "main" pipeline were lodged against it. There is no justification for that difference in treatment.[179]

2. The Dogged Pursuit of the Criminal Charge by the Kazakh Financial Police

88. The facially absurd notion that KPM and TNG operated "main" pipelines apparently had its genesis with the Kazakh Financial Police. The effort to create a credible case from this claim, however, got off to a poor start, and the credibility of the case only went downhill from there.

89. The Geology Committee within the MEMR was among the agencies enlisted by the Financial Police in its October 2008 audit blitz, and on November 4, 2008, the Geology Committee commenced its unscheduled audit of KPM and TNG.[180] The Geology Committee concluded, on November 11, 2008, that both KPM and TNG were in compliance with their legal, regulatory, and contractual obligations.[181]

90. Despite this conclusion by the Geology Committee, the Financial Police asked the Agency for Regulation of Natural Monopolies whether licenses are required for operation of a main pipeline, and whether KPM and TNG hold such licenses.[182] In response to this curious inquiry, the Agency confirmed to the Financial Police on November 14, 2008 that KPM and TNG do not hold licenses to operate main pipelines, and that operation of a main pipeline requires such a license.[183] Based on this "finding" that Claimants lacked a license to operate a main pipeline, the Kazakh Financial Police promptly reclassified certain pipeline segments

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179 Romanosov Statement ¶ 32.

180 *See* Reports on the results of the unscheduled audit of off-schedule check of performance of the legislation of the Republic of Kazakhstan about oil, subsoil and subsoil use, and contract obligations of KPM and TNG dated November 11, 2008, C-86 and C-87.

181 *See* Reports on the results of the unscheduled audit of off-schedule check of performance of the legislation of the Republic of Kazakhstan about oil, subsoil and subsoil use, and contract obligations of KPM and TNG dated November 11, 2008, C-86 and C-87; *see also* Cojin Statement ¶¶ 4-5.

182 *See* Pisica Statement ¶¶ 13-14.

183 *See* Letter from the Agency for Regulation of Natural Monopolies to the Financial Police dated November 18, 2008, C-88.

within the KPM and TNG gathering system as "main" pipelines on November 17, 2008.[184]

91. KPM and TNG sought a second opinion from the Ministry of Emergency Situations, and, on November 19, 2008, the Ministry confirmed to KPM and TNG that "all pipelines operated by your enterprise, from the place of extraction to the point of transferring the hydrocarbons to the oil and gas main pipelines are ***not*** main pipelines."[185] Two days later, however, the Financial Police requested that the Ministry of Emergency Situations withdraw its conclusion, claiming that the Ministry was not authorized to interpret legislative provisions.[186] The Ministry of Emergency Situations eventually relented, and six months later, on May 13, 2009, it revoked its conclusion that the KPM and TNG gathering systems did not constitute main pipelines, apparently under continuing pressure from the Financial Police.[187]

92. Based on its spurious "finding" that Claimants lacked a main pipeline license to operate newly-relabeled segments of their gathering systems, the Kazakh Financial Police ordered a new audit of KPM and TNG on November 17, 2008, to determine the purported income from its main pipeline operations.[188] On December 2, 2008, the Tax Committee, at the request of the Financial Police, determined that the amount of KPM's and TNG's "illegal profit" from operation of their "main" pipelines was approximately 41.8 billion Tenge (approximately 348 million USD as of November 2008) for KPM, and 37.7 billion Tenge (approximately 314 million USD as of November 2008) for TNG.[189] Those were exceedingly crude calculations that simply amounted to ***all*** of KPM's oil and TNG's gas and condensate production revenues from the Borankol and Tolkyn fields for the audited period of 2005-

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184 *See* Order from the Financial Police to the Tax Committee regarding KPM dated November 17, 2008, C-89; Report from the Tax Committee to the Financial Police regarding TNG dated November 19, 2008, C-91; *see also* Cojin Statement ¶ 5.

185 *See* Letters from the Ministry of Emergency Situations to KPM and TNG dated November 19, 2009 (emphasis added), C-90 and C-91. *See* Pisica Statement ¶ 16 ("The Ministry of Emergency Situations was and is the state authority responsible for the supervision and control of industrial safety of main pipelines. Therefore, we considered that it knew or ought to know what a *bona fide* main pipeline was.").

186 *See* Letter from the Financial Police to the Ministry of Emergency Situations dated November 21, 2008, C-92.

187 *See* Letter from the Ministry of Emergency Situations dated May 13, 2009, C-93.

188 *See* Order from the Financial Police to the Tax Committee regarding KPM and TNG dated November 17, 2008, C-89.

189 *See* Reports from the Tax Committee to the Financial Police dated November 19, 2008, C-202.

2007.[190] By contrast, on May 18, 2009, the College of Experts of the Ministry of Justice calculated KPM's purported "illegal profits" from oil and gas transportation services at 5.9 million Tenge (approximately USD 48,300) for the period from 2002 through 2008.[191]

93. The ridiculous calculation of KPM's and TNG's allegedly enormous "profits" from operation of the reclassified field pipelines was needed by the State to pursue the criminal charges it planned. Under Article 190(2) of the Kazakh Criminal Code, the provision that the State employed to bring the charges, large amounts of illegal profits are required to transform what would otherwise be an administrative complaint into a full-fledged criminal prosecution. By using all of KPM's and TNG's oil and gas revenues from the Borankol and Tolkyn fields, without even deducting taxes paid or operating expenses, the Kazakh Financial Police ensured that KPM and TNG would be criminally prosecuted on false pretenses.

94. On December 24, 2008, the Financial Police notified KPM that it was the subject of a criminal investigation for operating a main pipeline without a license, which the Financial Police classified as "illegal entrepreneurial activity" under Article 190(2)(b) of the Kazakh Criminal Code.[192]

95. Immediately after the notification of the criminal investigation, on December 25, 2008, Mr. Rahimov of the Financial Police summoned and interrogated KPM's General Manager, Mr. Cornegruta. Mr. Cornegruta was, at that time, considered a witness by the Financial Police, meaning that he was not allowed to be accompanied by counsel. On December 26, 2008, Mr. Rahimov summoned and interrogated the then Deputy Manager General for Finance of KPM and TNG, Mr. Veaceslav Stejar.[193] And on December 30, 2008, the Financial Police conducted

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[190] Even if the criminal charge had been legitimate, the so-called "profits" from the operation of the reclassified pipelines should have been calculated as the revenues earned for the provision of oil and gas transportation services, which is the manner in which actual main pipelines make money. For the period from 2002 to 2008, these revenues would have amounted to approximately USD 60,000. *See* Pisica Statement ¶ 20 ("It is beyond belief that Kazakhstan could estimate our alleged 'illegal profits' as about 11,000 times the profits we would have made had KPM and TNG really operated a 'main' pipeline.").

[191] Expert Report No. 1537 of the Ministry of Justice dated May 18, 2009, C-184.

[192] *See* Letter from the Financial Police to KPM dated December 24, 2008, C-94. This means the financial police had conducted searches and interrogated personnel before notifying KPM that they had launched a criminal investigation. *See* Cojin Statement ¶¶ 4-8.

[193] Stejar Statement ¶¶ 5-9.

an on-site "investigation" at the Borankol and Tolkyn fields "although it clearly could not see the difference between a small, in-field pipeline and a giant, buried main pipeline."[194]

96. On January 19, 2009, KPM and TNG filed complaints against the illegal actions being taken by the Financial Police with the General Prosecutor's Office of Kazakhstan, the Ministry of Justice of the Republic of Kazakhstan, the Financial Police itself, the MEMR, and the Western Regional Transport Prosecutor.[195] On February 2, 2009, the Financial Police notified Claimants that their complaints were rejected and that TNG, too, was now the subject of a criminal investigation on the same basis.[196] On March 18, 2009, KPM and TNG filed a new complaint against the illegal actions being taken by the Financial Police with the General Prosecutor's Office of Kazakhstan.[197] KPM and TNG never received an answer.[198]

97. At the same time, Mr. Anatolie Stati was attempting to obtain high-level meetings in order to solve the problems faced by KPM and TNG. As he explains:

> Starting in November 2008, I attempted to obtain meetings with and have letters delivered to President Nazarbayev through well-known and respected politicians and businessmen: I wanted to be certain that President Nazarabyev would take our pleas into consideration and not simply dismiss our letters. For instance, Petru Lucinschi, a former President of Moldova, attempted to obtain a meeting on our behalf with the President. Similarly, the late Victor Chernomyrdin, a former Prime Minister of Russia and then Russia's Ambassador to Ukraine, tried to intervene in our favor. I also contacted Alexander Mashkevich, a Kazakh billionaire and the President of the Euro-Asian Jewish Congress, who promised to try

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194 *See* Minutes of the on-site investigation dated December 30, 2008, C-95; Pisica Statement ¶ 22.

195 *See* Complaints from KPM and TNG against the Financial Police to the General Prosecutor's Office of Kazakhstan, the Ministry of Justice of the Republic of Kazakhstan, the Financial Police itself, the MEMR, and the Western Regional Transport Prosecutor, dated January 19, 2009, C-46 and C-96.

196 *See* Letter from the Financial Police to TNG dated February 2, 2009, C-98. *See* Condorachi Statement ¶ 11.

197 Condorachi Statement ¶ 13.

198 *See* Condorachi Statement ¶ 13. In late March 2009, Claimants only received a letter implying that the criminal case against KPM might have been suspended.

> obtaining an audience with the President. However, President Nazarbayev refused to receive our messengers or messages.[199]

3. Numerous Expert Opinions Concluded that KPM's and TNG's Field Pipelines Were Not Main Pipelines

98. KPM and TNG promptly sought expert opinions to contest the charge that their reclassified field gathering lines were "main" pipelines. The Kazakh Scientific, Research, and Design Institute of Oil and Gas, a division of the Kazakh Institute of Oil and Gas of the National Oil Company, KazMunaiGas, concluded on January 5, 2009 that the reclassified pipelines owned by KPM and TNG "do ***not*** belong to the category of ***main*** pipelines and are designated to ensure the process of hydrocarbons production."[200]

99. Likewise, the Scientific, Research, and Design Institute of Oil and Gas Industry of NIPI Neftegaz concluded on January 9, 2009 that the reclassified pipelines owned by KPM and TNG were correctly "classified as ***in-field*** pipelines."[201]

100. Further, the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations of Kazakhstan concluded on January 8, 2009, as follows:

> [T]he LLP Kazpolmunay COTS-CRMB pipeline, 17 km long, with the diameter of 159 mm is a ***field pipeline***.
>
> The operation of the mentioned pipeline relates to the single technological process of oil production.
>
> *****
>
> [T]he LLP Tolkynneftegas pipelines:
>
> 1) Gas condensate pipeline OGEF-GaGCTP with the diameter of 530 mm and length of 50 km;
>
> 2) Gas pipeline GaGCTP-Final separator with the diameter of 530 mm and length of 20 km;

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199 Stati Statement ¶ 25.

200 *See* Letters from the Kazakh Scientific, Research, and Design Institute of Oil and Gas of the Kazakh Institute of Oil and Gas of the National Oil Company KazMunaiGas to KPM and TNG dated January 5, 2009, C-99 and C-100. (emphasis added)

201 *See* Letters from the Kazakh Scientific, Research, and Design Institute of Oil and Gas of NIPI Neftegaz to KPM and TNG dated January 9, 2009, C-101 and C-102. (emphasis added)

> 3) Gas pipeline GaGCTP-Final separator with the diameter of 426 mm and length of 20 km;
>
> 4) Gas condensate pipeline GaGCTP-CRMB with the diameter of 159 mm and length of 20 km are ***field pipelines***.
>
> The operation of the mentioned pipelines relates to the single technological process of gas and gas condensate production.[202]

101. Additionally, on April 13, 2009, five experts from the largest energy institute in Moscow, the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities, issued expert opinions affirming that the pipelines in question were not "main" pipelines. One of these experts, Mr. Rozhdestvenski, had actually drafted the construction regulations for oil pipelines for the Soviet Union, which are applied in Kazakhstan.[203] The Russian Institute concluded that the "considered pipelines:"

> - are not main pipelines;
>
> - are used in carrying out oil operations, and particularly the work on the oil extraction.[204]

102. The same institute and experts from the Moscow institute issued a supplementary expert opinion on August 25, 2009 confirming that KPM's reclassified pipeline was a "***field pipeline***" and that the unfounded report of the Kazakh Ministry of Justice "cannot serve as a ground to consider [KPM's reclassified pipeline] as a main pipeline."[205]

103. Finally, Mr. Suleymenov, the Director of the Institute of Private Law of the Kazakh Law University of the National Academy of Science, concluded on July 2, 2009, that KPM's reclassified pipeline,

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[202] *See* Reports from the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations of Kazakhstan for KPM and TNG dated January 8, 2009, C-103 and C-104. (emphasis in original)

[203] *See* Letter of the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities dated August 25, 2009, C-107.

[204] *See* Reports from the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities for KPM and TNG dated April 13 and April 15, 2009, C-105 and C-106. (emphasis added)

[205] *See* Report from the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations of Kazakhstan for KPM dated August 25, 2009, C-107. (emphasis added)

> designated to pump the oil from the Oil processing and pumping shop on the Borankol field to the cargo and raw materials base at Opornaya station[,] ***is included in the single technological process of oil extraction and it is not an oil main pipeline.***[206]

104. To combat this array of opinions from industry experts, on February 9, 2009, the Kazakh Financial Police ordered the College of Experts of the Ministry of Justice to produce an expert report concluding that the reclassified KPM gathering line was a "main" pipeline.[207] The Ministry of Justice appointed an individual who had no industry expertise in the classification of pipelines.[208] The State's "expert" quickly generated an entirely conclusory opinion dated February 13, 2009 supporting the reclassification.[209]

105. Armed with this one "expert" opinion from the Ministry of Justice, the Financial Police elected to disregard the numerous expert opinions obtained by TNG and KPM that clearly stated that their gathering systems were in-field pipelines and not main pipelines.

106. On March 19, 2009, nine of Claimants' representatives attended a meeting chaired by Mr. A. B. Batalov, the Executive Secretary of the MEMR, to discuss the various difficulties they faced in Kazakhstan, including the criminal charges.[210] At this meeting, Executive Secretary Batalov and his deputy indicated that the reclassification of sections of TNG's and KPM's in-field pipelines as "main" pipelines was, in the MEMR's view, due to a defect in the applicable legislation.[211] The MEMR also indicated that the Financial Police ought to rely on opinions of experts.[212] Mr. Batalov was subsequently fired as Executive Secretary of the MEMR on April 27, 2009.[213]

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206 *See* Legal Opinion of Mr. Suleymenov dated July 2, 2009, C-108. (emphasis added)

207 *See* Order from the Financial Police to the Ministry of Justice dated February 9, 2009, C-109.

208 *See* Pisica Statement ¶ 18.

209 *See* Expert Opinion of the Ministry of Justice dated February 13, 2009, C-110.

210 Draft Minutes of the meeting dated March 19, 2009, C-111. *See* Pisica Statement ¶ 32.

211 *See* Pisica Statement ¶ 35.

212 *See* Pisica Statement ¶ 35.

213 *See* Pisica Statement ¶ 43.

4. The Arrest and Sham Trial of KPM's General Manager

107. Mr. Serghey Cornegruta, KPM's General Manager, was arrested by the Financial Police on April 25, 2009, as he was leaving a meeting of the managers of the key regional companies organized by the Governor of the Mangystau region.[214] Mr. Cornegruta was taken in for interrogation at the regional offices of the Financial Police.[215]

108. Mr. Cornegruta was personally charged with having committed a crime of illegal entrepreneurial activity under Article 190(2)(b) of the Kazakh Criminal Code for owning and operating a main pipeline without a license. The charge was a travesty in its entirety. Neither KPM nor TNG operated "main" pipelines; Mr. Cornegruta did not own KPM; and Mr. Cornegruta was not an entrepreneur, but rather an employee of KPM. Under Kazakh law, an "entrepreneur" must register as such with the authorities and receive a certificate to engage in entrepreneurial activities, and entrepreneurs are subject to a discrete taxation regime. Mr. Cornegruta was clearly an employee of KPM. He had an employment contract with KPM, received a salary from KPM, had never been registered with the State as an entrepreneur, and had never been subject to or paid entrepreneur taxes.[216] He did not even own shares of KPM, but only worked as its General Manager.

109. Claimants, their employees, and the local community were shocked and dismayed by Mr. Cornegruta's arrest and hoped that the matter was a misunderstanding that would be resolved promptly.[217] Around April 26, 2009, Claimants filed complaints against the Financial Police, including its head investigator, Mr. Rahimov.[218] The same day, 900 employees of KPM, TNG, and CASCo that were on shift addressed and signed a letter to the Governor of the Mangystau Region expressing their concerns.[219]

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214 *See* Condorachi Statement ¶ 15. The Financial Police had first tried to serve Mr. Cornegruta with a summon shortly before midnight on April 24, 2009. *Id.* ¶ 14.

215 *See* Condorachi Statement ¶ 15.

216 *See* Certificate from the Tax Department of the Mangystau region dated July 29, 2009, C-112.

217 Stati Statement ¶ 26; Condorachi Statement ¶ 16; Pisica Statement ¶ 41.

218 *See* Complaints from Counsel for Mr. Cornegruta to the Mangystau Province Prosecutor's Office and the Western Regional Transport Prosecutor dated April 26, 2009, C-113; Condorachi Statement ¶ 19.

219 Romanosov Statement ¶ 31.

110. Claimants attempted to obtain Mr. Cornegruta's release on bail, and a number of well-respected figures in the Mangystau region offered guarantees. CASCo, a successful oil and gas servicing company in Kazakhstan, offered its offices as collateral.[220] However, in May 2009, the Aktau City Court and the Financial Police refused bail for Mr. Cornegruta, and he remained in jail pending his trial.

111. On May 6, 2009, the Financial Police raided KPM's and TNG's offices searching for the other General Managers of KPM, Messrs. Salagor and Spasov, and the General Manager of TNG, Mr. Cojin, as well as information on their whereabouts.[221] The three in-country managers had been charged with the same offense as Mr. Cornegruta. The initial phase of the search started at 4:20 p.m. on May 6 and ended at 4:15 a.m. on May 7, 2007.[222] During the entire time, the employees of KPM and TNG had to stand in the corridor in front of their closed offices waiting for the Financial Police to search the premises.[223] As Mr. Stejar explains:

> All employees were instructed to stand in the hallways near their offices so that the police could question them as they searched each office. One member of our staff began to film the search in order to document what was going on, but the policemen ordered him to stop. The policeman said that if the filming did not stop then all employees would have to stand facing the wall with their arms and legs spread. The policeman also stated that he had called for back-up forces and that they were waiting outside for anyone who did not cooperate.[224]

112. The Financial Police seized a number of personnel files from human resources, as well as other documents unrelated to their warrant. The Financial Police also searched through Mr. Cornegruta's flat and seized additional documents.[225]

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220 Condorachi Statement ¶ 20.

221 *See* Minutes of the search, dated May 6 and 7, 2009, C-114. Witness Statement of Veaceslav Stejar (hereinafter "Stejar Statement") ¶ 15.

222 *See* Minutes of the search, dated May 6 and 7, 2009, C-114.

223 Stejar Statement ¶¶ 16-17

224 Stejar Statement ¶ 17.

225 *See* Minutes of the search, dated May 6 and 7, 2009, C-114; Stejar Statement ¶ 18.

113. On May 7, 2009, Mr. Anatolie Stati, on behalf of Claimants, wrote to President Nazarbayev to obtain the release of Mr. Cornegruta, to protect the former and current management of KPM and TNG, and to end the dispute.[226] Mr. Stati, "deeply concerned about the fate of [his] in-country managers, especially Mr. Cornegruta … appealed to President Nazarbayev's common sense and humanity,"[227] and renewed his previous appeals. He wrote:

> [The issues faced by KPM and TNG], which are mostly invented and aimed at sabotaging and even putting an end to our activity in Kazakhstan, have been previously presented in detail to you and to the representatives of the competent ministries and institutions. …
>
> However, the controlling bodies of [the Republic of Kazakhstan], especially the Financial Police, have brought false accusations against the oil companies, based on the misinterpretation and tendentious application of the laws of the Republic of Kazakhstan, thereby seriously violating the rights of these companies. They went so far as to fabricate criminal lawsuits against the managers of the oil companies [TNG and KPM]. We are deeply concerned and indignant at the fact that these honest managers, who, for many years, have put a lot of hard work into the development of their enterprises are being arrested, imprisoned, humiliated, and treated no better than ordinary criminals, instead of being appreciated and respected for their activity.
>
> In consideration of the above stated facts, we once again appeal to the common sense of the officers and legislative bodies who allowed such situations to occur. We also require that you objectively evaluate our activity in [Kazakhstan] and personally intervene to put an end to this defiant attitude towards our companies and managers.[228]

President Nazarbayev ignored his appeal.[229]

114. Under Kazakh law, business entities cannot be prosecuted for crimes, although civil actions ancillary to a criminal proceeding can be pursued against a business. The State therefore brought its criminal action against Mr. Cornegruta personally, but surprisingly, it did not file an ancillary civil action against KPM. Thus, KPM was never named or made a party to the criminal action for allegedly

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[226] *See* Letter from Claimants to President Nazarbayev, dated May 7, 2009, C-43.

[227] Stati Statement ¶ 28.

[228] *See* Letter from Claimants to President Nazarbayev, dated May 7, 2009, C-43.

[229] *See* Pisica Statement ¶ 45.

operating a "main" pipeline without a license, and KPM was consequently not represented by counsel during the criminal trial of Mr. Cornegruta.

115. Mr. Cornegruta's trial lasted from July 30 until September 18, 2009. During the trial, the State introduced as its principal evidence a so-called "confession" that consisted of a letter Mr. Cornegruta had written on June 13, 2008 to the State's Agency for Regulation of Natural Monopolies.[230] Under the new 2008 Law on Licensing, KPM and TNG were required to renew their licenses.[231] KPM and TNG applied to the MEMR, which renewed the licenses for the activities for which it was still the competent licensing authority.[232] The MEMR informed KPM and TNG that the Agency for Regulation of Natural Monopolies had become the licensing authority for certain activities.[233] Therefore, following the recommendation from the MEMR, KPM wrote to the Agency for Regulation of Natural Monopolies to renew its licenses in case certain of its activities fell within the purview of that agency under the new Article 12(2) of the 2008 Law on Licensing.[234] In his letter, Mr. Cornegruta quoted verbatim a laundry list of licensing areas covered by Article 12(2) which included, among other activities, those involving "main gas and oil products pipelines."[235] The letter continued with the following specific request:

> We hereby send you the documentation for re-registration of the licenses ***for the right to perform activities in the production sector***:
>
> 1. Exploitation of mining, petrochemical, chemical, oil and gas refining productions, exploitation of gas, oil and oil products storage facilities;
>
> For the following subtypes of activities:

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230 *See* Letter from KPM to the Agency for Regulation of Natural Monopolies, dated June 13, 2008, C-115.

231 *See* Condorachi Statement ¶ 26.

232 *See id*.

233 *Id.*

234 *See* Article 12 of the Law on Licensing, dated January 11, 2007 No. 214, C-116. *See* Condorachi Statement ¶ 26 ("The letter in no way 'admitted' that KPM operated a 'main' pipeline for which it required a license (because it clearly did not), and it was complete nonsense for the Financial Police to characterize the letter in this way.")

235 *See* Article 12 of the Law on Licensing, dated January 11, 2007 No. 214, C-116.

> Exploitation of oil and oil products storage facilities (oil and gas storages, oil depots, tanks);
>
> Exploitation of equipments, units of the pumping compression station, tank batteries, and linear portions of the main gas and oil products pipeline, as well as of technological process equipment.[236]

116. Despite the fact that Mr. Cornegruta specifically referenced the "re-registration of licenses for the right to perform activities in the ***production*** sector," which was the only sector that KPM was involved in, and therefore the only pertinent area of licensure that KPM was interested in, the State seized on Mr. Cornegruta's quotation of the entire statutory list of activities covered by the statute. Since the quoted list included the words "main gas and oil products pipeline" from the new licensing law, the prosecutor argued that the letter constituted a "confession" by Mr. Cornegruta that KPM operated a "main" pipeline.

117. In his defense at trial, Mr. Cornegruta's counsel argued the obvious — that Mr. Cornegruta was not an entrepreneur, that he was an employee of KPM, that he did not own KPM, that his June 13, 2008 letter was not even remotely a "confession," and that the KPM gathering system did not include "main" pipelines.[237] Defense counsel introduced seven expert opinions explaining that the KPM gathering system pipelines were not "main" pipelines.[238] The Financial Police threatened two of the experts, who were Government employees, and those two experts withdrew their opinions.[239] The State introduced the single, February 13, 2009 opinion from the Ministry of Justice containing its conclusory statement that the KPM gathering system pipelines were "main" pipelines.[240]

118. On September 18, 2009, the Aktau City Court rendered a guilty verdict against Mr. Cornegruta for illegally engaging in entrepreneurial activities by operating the relabeled KPM "main" pipelines without a license. He was sentenced

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[236] Letter from KPM to the Agency for Regulation of Natural Monopolies dated June 13, 2008, C-115.

[237] *See* Section IV.B.3 above.

[238] *Id.*

[239] *See* Letter from the Ministry of Emergency Situations dated May 13, 2009, C-93.

[240] *See* Expert Opinion of the Ministry of Justice dated February 13, 2009, C-110.

to four years in prison.[241] Claimants and their employees were "stunned" by the decision and considered the trial to be a parody of justice.[242]

119. Additionally, despite the fact that KPM was not criminally indicted, named, made a party, present in court, or represented at the trial of Mr. Cornegruta, and despite the fact that the State had not brought a civil action against KPM, the Aktau City Court also rendered a verdict against KPM, ordering KPM to pay the Government a fine of approximately USD 145 million (21,675,854,578 Tenge).[243] This sum constituted all of KPM's oil and gas production revenues from March 2007 to May 2008, revenues on which KPM had already paid taxes to the State, and revenues that bore no relationship whatsoever to the transportation fees that are the sole income source for "main" pipeline operators.[244] Ironically, on May 18, 2009, the College of Experts of the Ministry of Justice had performed the same calculation of the alleged "illegal profits" and arrived at the sum of 1,935,547 Tenge (approximately USD 15,000) for the period from March 2007 through May 2008.[245]

120. Mr. Corngruta filed an appeal of his verdict with the Mangystau Regional Court. Because KPM was not a party to the initial trial, KPM was also not a party to, or represented in, the appeal proceedings. On November 12, 2009, the Mangystau Regional Court affirmed the verdicts of the Aktau City Court both against Mr. Cornegruta and the non-party KPM.[246] On November 23, 2009, Mr. Cornegruta was transferred from a temporary detention facility in Aktau to the prison in Atyrau.[247] Claimants and their employees were "disheartened" and Mr. Stati has seen "the devastating impact of [Mr. Cornegruta's] jail term on his wife and family."[248]

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241 Decision of the Aktau City Court dated September 18, 2009, C-117.

242 Stati Statement ¶ 29. Pisica Statement ¶ 48. Condorachi Statement ¶ 28 ("The court's decision defied any logic. … The four-year jail term for Mr. Cornegruta was illegal, inhumane, and illogical.").

243 Decision of the Aktau City Court dated September 18, 2009, C-117.

244 *See* Decision of the Aktau City Court dated September 18, 2009, C-117. *See* Condorachi Statement ¶ 28 ("The amount of the fine was astronomical…").

245 Expert Report No. 1537 of the Ministry of Justice dated May 18, 2009, C-184.

246 *See* Condorachi Statement ¶ 31.

247 *See id*.

248 Condorachi Statement ¶ 31; Stati Statement ¶ 29. *See also* Pisica Statement ¶ 50 ("Kazakh jails do not have a good reputation and we feared for his health, his sanity, and even his life. His wife

5. The Direct Interference with Claimants' Operations That Resulted From the Criminal Prosecution

121. The State commenced enforcement actions against KPM and TNG immediately after the arrest of Mr. Cornegruta. On April 30, 2009, the Financial Police issued resolutions for the arrest of KPM's and TNG's Subsoil Use Contracts, the KPM and TNG in-field pipelines that had been reclassified as main pipelines, the companies' equity interests, and the companies' vehicles.[249] On May 15, 2009, the Financial Police notified KPM and TNG that it had seized Claimants' equity interests in KPM and TNG two days before, on May 13, 2009. The asset and equity seizures were designed to prevent KPM and TNG from selling or transferring their interests during the course of the criminal proceeding against Mr. Cornegruta, although the assets could otherwise be used in normal business operations.

122. On June 12, 2009, Terra Raf and Ascom filed petitions to lift the seizure orders. Their petitions were denied on June 27, 2009.[250] On June 17, 2009, the Financial Police issued a press release announcing that the investigative phase of the criminal action had ended and that the four former and current in-country managers of KPM and TNG would be prosecuted for having realized an "illegal profit" of 147 billion Tenge (approximately USD 980 million as of June 2009).[251]

123. On December 29, 2009, after the verdict against Mr. Cornegruta was affirmed on appeal, the Aktau City Court issued a writ of execution against KPM for payment of USD 145 million, a figure that allegedly represented the portion of the total amount of so-called "illegal profit" that KPM realized during Mr. Cornegruta's tenure as General Manager of KPM.[252] The court determined that the total amount

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and family obviously also suffered from the separation and the stress associated with his detention.").

249 *See* Condorachi Statement ¶ 38.

250 Letter No. 15-1-569-09 from the Western Regional Transport Prosecutor to Ascom and Terra Raf, dated June 27, 2009, C-183.

251 *See* Press release of the Financial Police dated June 17, 2009 entitled "Case investigation regarding the leadership of 'Kazpolmunay' and 'Tolkynneftegaz' accused of illegal conduct of business activities has been finalized in the Mangystau Region," C-118.

252 *See* Writ of Execution Issued by the Aktau City Court of December 29, 2009, C-119; *see also* Decision of Aktau City Court, dated September 18, 2009, C-117; *see also* Cojin Statement ¶¶ 18,21.

of KPM's allegedly "illegal profit" amounted to over 65 billion Tenge (approximately USD 435 million as of June 2009).[253]

124. Following that writ of execution, the Judicial Executors began enforcement procedures in earnest against KPM by seizing its assets. Because KPM and TNG operated cooperative gathering systems and processing facilities, the seizures affected both businesses.

125. On January 10, 2010, the Chief of the Aktau Territorial Department of Judicial Executors issued a court order attaching several of what it referred to as KPM's "second-tier" bank accounts.[254] The seized accounts included two settlement accounts with Kazkommertsbank in Bostandykskyi District; forty-one settlement accounts with Kazkommertsbank in Aktau City; and nine settlement accounts with Halyk Bank of Kazakhstan in Aktau City.[255] The order included instructions to those banks to inform the judicial executor whenever it received any funds from KPM. The order also included a warning to KPM's General Manager and Chief Accountant that criminal responsibility could result from failing to comply.[256] At the time, KPM's General Manager was Veaceslav Stejar. KPM received this notice on January 21, 2010.

126. On January 22, 2010, the Chief of the Aktau Territorial Department issued another order finding that KPM had "not paid the debt to the state and [had] not fulfilled the requirements of the judicial executor in due time."[257] As a result, the Order attached eighteen different motor vehicles belonging to KPM. It also instructed the Road Police Department to take notice of the vehicles' registrations, and to seize and impound them in order to make a formal inventory of their value. KPM received a copy of this order on February 1, 2010.

127. On January 25, 2010, the Committee on Judicial Administration, a division of the Supreme Court of Kazakhstan, wrote to Mr. Stejar at KPM to inform him that the judicial acts pertaining to the Writ of Execution for 21.6 billion Tenge

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253 Decision of Aktau City Court, dated September 18, 2009, C-117.

254 *See* Order from Chief of Aktau Territorial Department, dated January 10, 2010, C-121.

255 *Id*.

256 *Id*.

257 *See* Order from Chief of Aktau Territorial Department, dated January 22, 2010, C-122.

remained unexecuted.[258] Further, the Deputy Administrator of Mangystau Oblast courts, Mr. Tursynbayev, instructed the Chief of Aktau Territorial Department to execute enforcement procedures by January 30, 2010.[259] The instructions included: (i) to visit the Borankol Village to confirm whether KPM was operating, and if so, to make an inventory of and attach its property; (ii) to demand all documentation from KPM; and (iii) to make note of and inventory any motor vehicles discovered that were previously attached.[260]

128. The Judicial Administration Committee informed Mr. Stejar that the judicial executors would execute enforcement procedures regarding the property and requested that Mr. Stejar meet with the executors regarding the property.[261] Mr. Stejar never attended this meeting, as he had left Kazakhstan soon after receiving this letter. However, on January 26, 2010, a property inventory was conducted listing 2,186 different assets, including 63 oil drilling wells, and 10 gas drilling wells.[262]

129. On February 19, 2010, the Chief of the Aktau Territorial Department issued yet another writ of execution, noting that prior collection orders had gone unfulfilled.[263] This Order formally attached the 2,186 assets listed in the January 26, 2010 inventory – a list that included everything from the companies' oil and gas wells to their tea, coffee, and sugar – and it specifically warned KPM's General Manager, Mr. Stejar, that he could face criminal responsibility for embezzlement or alienation of that property.[264] KPM received this Order on March 1, 2010.

130. On February 23, 2010, the Chief of Aktau Territorial Department issued a fourth order. That order prohibited KPM from executing necessary import and export formalities regarding the transportation of oil. It meant that KPM could

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258 *See* Letter from Judicial Administration Committee regarding failure to execute the order, dated January 25, 2010, C-123.

259 *See* Instruction from Deputy Administrator of Mangystau Oblast Courts to Chief of Aktau Territorial Department, dated January 25, 2010, C-124.

260 *Id*.

261 *See id*.

262 *See* Order from Chief of Aktau Territorial Department, dated February 19, 2010, C-125.

263 *Id*.

264 *Id.*

not deliver oil from its gathering system to the main pipeline operated by KazTransOil.[265]

131. On February 26, 2010, the Chief of Aktau Territorial Department issued yet another order. That Order stated:

> Within enforcement procedures it was established that the debtor "Kazpolmunai" LLP carries out exploration and extraction of raw hydrocarbon on Borankol field in Mangystau Oblast of the Republic of Kazakhstan according to subsoil use licenses and contracts and had oil pipeline, ***projected and constructed as field oil pipeline***, ***and designed for transportation of oil from the Oil treatment plant*** located on the territory of Borankol field to Commodities and raw material base on Opornaya station and metering station with further transfer of products ***to the system of main pipelines of "KazTransOil"*** JSC.[266]

The Order continued that, to ensure execution of the writ of enforcement, it is necessary to "attach the oil pipeline from OTP [oil treatment plant] to Opornaya CRMB of 18 kilometers long" as well as the accumulator oil tanks also belonging to KPM. That Order also prohibited KPM from transferring oil to the main pipeline operated by KazTransOil once its accumulator tanks reached capacity. As a result, with that Order, Kazakhstan further interfered with KPM's use of its gathering system.

132. Additionally, the February 26, 2010, Order betrayed the Government's understanding that it had prosecuted and convicted Mr. Cornegruta, and rendered a judgment against KPM, on false pretenses. KPM's "18 kilometer" pipeline attached by this Order was the same pipeline that the Kazakh authorities had falsely reclassified as a "main" pipeline in late 2008, which, as explained above, led to the verdict and writ of execution for 21.6 billion Tenge that the Aktau Territorial Department was attempting to enforce. In his Order, however, the Chief did not refer to the 18 kilometer pipeline as a main pipeline; rather, he explicitly stated that the 18 kilometer pipeline is a "field oil pipeline" and distinguished that pipeline from the "system of main pipelines" belonging to KazTransOil. The Order was the product of multiple visits to the site. It was apparently clear to whomever conducted

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[265] See Order from Chief of Aktau Territorial Department, dated February 23, 2010, C-298.

[266] *See* Order from Chief of Aktau Territorial Department, dated February 26, 2010, C-79.

those inspections that the 18 kilometer pipeline was in no way a "main" pipeline. A copy of this Order was sent to KPM on March 3, 2010.

133. On March 4, 2010, the Chief of the Aktau Territorial Department appealed to the President of the Second Aktau City Court for a change in the method and order of execution. He noted that, despite attaching fifty-two settlement accounts and numerous assets, "monetary resources by collection orders do not arrive to the deposit account."[267] As a result, he requested that the enforcement procedure be changed to an in-kind transfer of land lots, including the three previously-attached plots of real property, the 18 kilometer pipeline, KPM's Contract No. 305 over the Borankol field, and KPM's subsoil use license No. 309.

134. On March 15, 2010, the Chief of the Aktau Territorial Department issued another order for the valuation of KPM's assets.[268] This order included KPM's rights to three lots of property, one of which was located in Borankol Village (where KPM's offices and employee apartments are located) and two of which were located in the Borankol field. The order concluded by demanding appraisal of the three lots of property, as well as the eighteen motor vehicles, the 18 kilometer pipeline, the field camp, and the Borankol field that were attached in previous orders.

135. By this point, the court administrator had seized nearly every asset KPM held, including key oil production equipment and its oil reserves, and the administrator was on the verge of seeking formal transfer of title or sale of KPM's assets. KPM had already been struggling to remain in operation – with its bank accounts seized it had no formal way to pay employees, and with the property seizures it could not transport produced oil through its gathering system. KPM objected strenuously to the seizures and, on March 16, 2010, filed a motion to alter execution procedures so that production on the Borankol field could continue.[269]

136. KPM explained that the measures already taken risked the suspension of production, because, among other things, KPM had been prohibited from transferring oil to the KazTransOil main pipeline and from executing imports and

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[267] *See* Presentation on Change in Method and Order of Execution from Chief of Aktau Territorial Department to the President of Court No. 2 of Aktau City, dated March 4, 2010, C-127.

[268] *See* Order from Chief of Aktau Territorial Department, dated March 15, 2010, C-126.

[269] *See* Notices from Chief of Aktau Territorial Department of Judicial Executors, dated March 17, 2010, C-128 and C-295.

exports of goods and property. Even the seizure of motor vehicles, KPM explained, paralyzes its activity, as employees need to travel daily between various agencies and the field. KPM explained that in the oil production industry, it is nearly impossible to re-gain the level of production a contractor had after suspension of field operation, not to mention the costs and losses that are involved. In addition to the business consequences, KPM also listed the social consequences of halting production, namely, the delays in payment of salaries to employees, layoffs of employees, and a decrease in production that would adversely affect the regional population. KPM requested that execution measures be suspended in order to avoid complete suspension of production.

137. On March 17, 2010, the Acting Head of Aktau Territorial Department of Judicial Executors complied with KPM's request and issued two orders that suspended execution of the February 23, 2010, Order and the February 26, 2010, Order, respectively. Both confirmed that suspension was ordered "to avoid the suspension of production activity of 'Kazpolmunai' LLP."[270] Mr. Stejar explains that had those orders not been suspended, KPM and the region would have suffered an "ecological and social disaster of oil overflow" from the accumulator tanks.[271]

138. Nevertheless, on March 20, 2010, the Acting Chief of Aktau Territorial Department of Judicial Executors proposed that the Prosecutor initiate a criminal case against Mr. Stejar, then-General Manager of KPM, for failing to enforce the December 29, 2009, writ of execution against KPM.[272] KPM continued to receive notices to Mr. Stejar that he was failing to enforce the writ of execution and could be held criminally liable for his lack of action. KPM was never informed of the formal status of this criminal investigation, although a summons for Mr. Stejar to appear at the transport prosecutor's office was issued in or around September 2010.[273]

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[270] *See* Notices from Acting Head of Aktau Territorial Department of Judicial Executors, dated March 17, 2010, C-128 and C-295.

[271] Stejar Statement ¶ 25.

[272] *See* Proposal by the Judicial Administration Committee to the Prosecutor's Office, dated March 20, 2010, C-129.

[273] Stejar Statement ¶ 28.

139. On June 9, 2010, the Acting Chief of Aktau Territorial Department of Judicial Executors ordered the sale of KPM's assets.[274] That order explained that a sale must be of "the whole property as a single lot" to avoid suspension of oil and gas activities, which would affect oil and gas supply in the region as well as the activity of other oil and gas consumers, and disruption of employee salaries, which would result in lawsuits for the recovery of wages.[275] On June 15, 2010, the Acting Chief of Aktau Territorial Department again issued a "repeated warning" to Mr. Stejar of KPM, claiming that KPM operated and carried out oil and gas extraction, sold the products, and gained income, but did not voluntarily make any payments to the state budget as ordered by court decision.[276] The notice instructed KPM to execute the court order by paying 21.6 billion Tenge in full, or transferring assets corresponding to the amount owed, within two weeks time.

C. The State's Retroactive Reversal of its Pre-Emptive Rights Waiver

140. The State's fabricated criminal charges, subsequent jailing of KPM's General Manager, and imposition of a USD 145 million fine against KPM were among the most damaging and pernicious components of the State's harassment campaign. However, the State's harassment campaign contained numerous other components.

141. As described above, Gheso S.A., a subsidiary of Ascom, had acquired 100% of the shares in TNG by 2002.[277] In May of 2003, Gheso transferred its 100% interest in TNG to its affiliate Terra Raf.[278]

142. By provision in the TNG Subsoil Use Contract, transfer or sale of the Subsoil Use Contract's rights and obligations to new parties required the consent of the State, except for transfer to a subsidiary or affiliate.[279] Where a transfer to a new party was proposed, the State retained the right to disallow the transfer and to exercise a statutory pre-emptive right to purchase 100% of TNG.

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274 Order dated June 9, 2010, C-199.

275 *Id*.

276 Repeated Warning to KPM, dated June 15, 2010, C-201.

277 *See supra*, Section III.A.

278 *See* Sale and Purchase Agreement between Gheso and Terra Raf dated May 12, 2003, C-60.

279 Article 21.1 of the TNG Subsoil Use Contracts, C-52 and C-53.

143. On October 19, 2006, the State asked TNG whether any transfer of Ascom's interest had been made during the period from December 1, 2004 to October 19, 2006.[280] On October 30, 2006, TNG replied that Terra Raf was the sole interest holder in TNG and had been since the time of the 100% transfer from Gheso to Terra Raf in May of 2003.[281] Upon receiving this information, on February 13, 2007, the State requested that TNG retroactively apply for permission for the 2003 ownership transfer to Terra Raf.[282] TNG complied, and the State granted its permission for the transfer, accompanied by an explicit ruling that the May 12, 2003 transfer of TNG ownership from Gheso to Terra Raf was proper and the State's pre-emptive rights were not applicable to that transfer.[283]

144. Thereafter, on December 6, 2007, KPM and TNG applied to the MEMR for permits to allow them the potential transfer of their ownership interests to an affiliated entity for the purpose of conducting an IPO on the London Stock Exchange (a public offering that did not take place).[284] On December 26, 2007, the Kazakh Inter-institutional Committee recommended that the MEMR grant permission for these transfers and, at the same time, waive the State's pre-emptive rights to purchase 100% of KPM and TNG.[285] By letters dated December 29, 2007, the MEMR informed TNG and KPM that it permitted the transfers and that the State specifically waived its pre-emptive rights to purchase KPM and TNG.[286]

145. On December 18, 2008, after the Nazerbayev order to various Kazakh agencies to investigate and pursue KPM and TNG, the MEMR informed TNG that it was cancelling the State's unequivocal February 2007 approval of the 2003 transfer of 100% of the TNG shares from Gheso to Terra Raf,[287] and demanded that TNG submit a new application for permission allowing the transfer. The notice required

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280 *See* Letter from TNG to the MEMR dated October 30, 2006, C-131.

281 *Id*.

282 Letter from the MEMR to TNG dated February 13, 2007, C-132.

283 Letter from the General Prosecutor's Office to the MEMR dated February 21, 2007, C-133. *See also*, Excerpt from the Minutes of Meeting of the Appraisal Commission dated February 20, 2007 (deciding to allow the transfer of the shares of TNG from Gheso to Terra Raf), C-134.

284 *See*, for instance, Letter from KPM to the MEMR dated December 6, 2007, C-135.

285 *See* Letters from the MEMR to TNG and KPM dated December 29, 2007, C-139.

286 *Id*.

287 *See* Notice from the MEMR to TNG dated December 18, 2008, C-140.

TNG to submit all documentation regarding Terra Raf's ownership within 10 days, under threat that failure to do so would result in the MEMR unilaterally terminating TNG's Tolkyn and 302 Properties Subsoil Use Contracts. At the same time it sent its letter to TNG, the State issued a press release accusing Claimants of having "forged" documents to defraud the State of its rights.[288]

146. On December 22, 2008, TNG refused to submit the required documentation to the MEMR, and objected to the State's nonsensical reversal of its prior, explicit consent.[289] Mr. Grigore Pisica, the General Counsel of Ascom, considered the December 18, 2008 notice "insulting" and recalls that he "felt as if we had just been qualified as 'illegal shareholders' of TNG."[290]

147. On December 29, 2008, the MEMR required that TNG provide notarized documents evidencing the change in ownership of TNG.[291] TNG submitted the requested documents on January 20, 2009.[292]

148. On February 27, 2009, the State issued a new notice to TNG, stating that the transfer of TNG to Terra Raf had allegedly breached the State's statutory pre-emptive right to acquire TNG.[293] The State demanded that TNG submit a new application for the transfer to allow the State to "re-evaluate" its February 2007

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288 *See* Press release circulated on Interfax from the MEMR dated December 18, 2008, C-141.

289 *See* Letter from TNG to the MEMR dated December 22, 2008, C-142. There were several legal and factual problems with the State's new position. First, the December 18, 2008 notice failed to mention the December 29, 2007 State waiver of its pre-emptive rights to purchase 100% of KPM and TNG. *See* Letters from the MEMR to TNG and KPM dated December 29, 2007, C-139. Second, the transformation of TNG from an OJSC to an LLP in 2005, when Terra Raf was already the sole owner of TNG, had been repeatedly notified to and approved by the State at the time. *See*, for instance, TNG's Certificate of Incorporation dated May 16, 2005 stating: "This certificate grants the right to conduct business in accordance with constitutive documents within current legislation of the Republic of Kazakhstan", C-61. TNG's constitutive documents include its Articles of Association dated April 12, 2005, that provide in Article 1.3: "The Sole Participant of the Partnership is TERRA RAF TRANS TRAIDING LIMITED…," C-39. Letter from TNG to the MEMR dated May 25, 2005, C-143. Third, under the TNG Subsoil Use Contracts, the transfer of shares between affiliates did not require the written consent of Kazakhstan. *See* Articles 21.1 of the TNG Subsoil Use Contracts, C-52 and C-53. Fourth, Article 71 of the Law on Subsoil and Subsoil Use only introduced the State's pre-emptive right in Kazakh legislation as of December 8, 2004, more than a year and a half after the share transfer from Gheso to Terra. *See* Article 71 of the Law on Subsoil and Subsoil Use dated December 1, 2004. *See* Pisica Statement ¶ 27.

290 Pisica Statement ¶ 28.

291 *See* Letter from the MEMR to TNG dated December 29, 2008, C-144.

292 Letter from TNG to the MEMR, dated January 19, 2009, C-145. *See* Pisica Statement ¶ 28.

293 *See* Notice from the MEMR to TNG, dated February 27, 2009, C-146.

consent and waiver of its pre-emptive purchase right. Once again, the State threatened that failure to re-submit the application would result in the revocation of TNG's Subsoil Use Contracts.

149. By letter dated March 18, 2009, TNG responded to the State's February 27, 2009 notice of breach and offered the State three alternatives: (1) revocation of the purported "reversal" of the State's decision of February 27, 2009 regarding the violation by TNG of its Subsoil Use Contract and of the obligation to re-apply for a transfer permit; (2) TNG would re-apply for a transfer permit, if the State would agree to pay USD 1.347 billion in compensation if the permit was denied; or (3) referral of the dispute to the Arbitration Institute of the Stockholm Chamber of Commerce, and maintenance of TNG's *status quo* rights under the TNG Subsoil Use Contracts, pending a final, arbitral decision.[294]

150. The day after TNG filed its March 18, 2009 letter, Claimants attended a meeting at the MEMR offices.[295] The meeting was chaired by the MEMR Executive Secretary, Mr. A. B. Batalov, and attended by two other representatives of the MEMR and nine representatives of Terra Raf, TNG, Ascom, and KPM. All of the State's abusive actions against Claimants since the time of Nazarbayev's October 14, 2008 investigative directive were discussed at the meeting, including the State's purported "reversal" of its transfer consent and pre-emptive rights waiver. Claimants reiterated their objections to the MEMR's December 18, 2008 notice and their proposal that, should the State deny the permit, then it should agree to pay USD 1.347 billion in compensation for Terra Raf's interests in TNG.

151. MEMR Executive Secretary Batalov assured Claimants that all of the outstanding issues would be disposed of in favor of TNG and KPM, and that TNG's Subsoil Use Contracts would not be cancelled, if TNG simply submitted a new application for its transfer to Terra Raf and permitted the State to re-evaluate its prior consent.[296] Mr. Batalov also stated that, because the size and value of TNG had changed since the 2003 transfer to Terra Raf, the State would require a new and comprehensive evaluation of TNG's books and assets in order to properly re-

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294 *See* Letter from TNG to the MEMR, dated March 18, 2009, C-41; Pisica Statement ¶ 31; Lungu Statement ¶ 42.

295 *See* Pisica Statement ¶ 32; Lungu Statement ¶ 43.

296 Pisica Statement ¶ 33; Lungu Statement ¶ 44.

evaluate the transfer.[297] State-owned KazMunaiGas would conduct this new, comprehensive evaluation.[298]

152. Mr. Grigore Pisica prepared minutes of the meeting based on the notes taken by Claimants' representatives in attendance.[299] The minutes were offered to Mr. Batalov for his signature, but he refused to sign.[300] At the same time, Claimants requested another meeting with Executive Secretary Batalov, but he claimed to be too busy to participate.[301] However, Claimants obtained a meeting in the afternoon of March 19, 2009 with Mr. Batalov's deputy.[302] Claimants had a lengthy meeting with the Deputy Executive Secretary during which they confirmed the details of the filing of a new application.[303]

153. On March 24, 2009, based on Mr. Batalov's assurances and the verbal agreement reached at the March 19 meetings, TNG sent the State a request for a formal, written decision regarding the legitimacy of the State's prior waiver of it pre-emptive rights, and the legitimacy of the State's prior grant of the permit for transfer of TNG's ownership to Terra Raf.[304] On March 25, 2009, TNG sent the State a separate request for another formal, written decision regarding the right of TNG to transfer Terra Raf's ownership interests to a prospective third party buyer, including KazMunaiGas, based upon a competitive bidding process and direct negotiations.[305]

154. TNG never received a response to its March 24 and 25, 2009 requests for formal decisions, and the permit confirming – for a second time – the proper transfer of TNG ownership to Terra Raf was never granted.

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297 Pisica Statement ¶ 33; Lungu Statement ¶ 44.

298 Pisica Statement ¶ 33; Lungu Statement ¶ 44.

299 Pisica Statement ¶ 37; Lungu Statement ¶ 45.

300 *See* Draft Minutes of the meeting dated March 19, 2009, C-42. Pisica Statement ¶ 37; Lungu Statement ¶ 45.

301 Pisica Statement ¶ 37.

302 *Id*.

303 *Id*.

304 *See* Letter from TNG to the MEMR dated March 24, 2009, C-147. *See* Pisica Statement ¶ 38; Lungu Statement ¶ 46.

305 *See* Letter from TNG to the MEMR dated March 25, 2009, C-148. *See* Pisica Statement ¶ 38; Lungu Statement ¶ 46.

155. The title-clouding purpose of this illegitimate assertion of preemptive purchase rights served its purpose: potential buyers of TNG were concerned and Terra Raf was unable to sell its interest in TNG. And the State, not wishing to place itself in the position of having to actually purchase TNG from either Gheso or Terra Raf, simply dropped the issue when, in July 2010, it compiled the list of alleged Subsoil Use Contract violations that it used to directly expropriate Claimants' Kazakh investments

D. The State Improperly Assessed Alleged Corporate Back Taxes

156. Another element of the Government's harassment campaign involved assessment of allegedly unpaid corporate taxes. On November 10, 2008, the Tax Committee initiated a global audit of TNG and KPM at the request of the Financial Police.[306] The audits covered the period from January 1, 2005 through December 31, 2007 for KPM, and January 1, 2003 through December 31, 2007 for TNG.[307] The global audits pertained to corporate income tax, royalties, individual income tax, social tax, property tax, land tax, tax on vehicles, excise taxes, corporate income tax on non-resident legal entities, and income and payment for use of natural and other resources.[308]

157. At the end of its three-month audit, the Tax Committee had not found anything legitimately wrong, so it simply invented a violation based on an allegation that KPM and TNG had improperly amortized drilling expenses for the years 2005 to 2007. Based on this allegation, the Tax Committee assessed approximately 3.2 billion Tenge and 5.9 billion Tenge (approximately USD 22 and 40 million) in back corporate taxes and penalties against KPM and TNG, respectively.[309] This finding by the Tax Committee was, however, directly contrary to a previous assessment and to the contractually agreed upon amortization rates.

158. The Subsoil Use Contracts specifically provided for the stabilization of the tax regime to incorporate the tax legislation in force on April 1, 1999 for their

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306 *See* Instructions No. 28 and 29 of the Tax Committee dated November 10, 2008, C-149 and C-150.

307 *Id*.

308 *Id*.

309 *See* Notices No. 28 and No. 29 to KPM and TNG from the Tax Committee dated February 10, 2009, C-155.

duration.[310] Nevertheless, following yet another amendment to the Kazakh fiscal legislation, KPM and TNG agreed to negotiate with the State for addenda to the Subsoil Use Contracts in order to set out a procedure for application of a balanced, complete tax regime to their Contracts.[311]

159. When the Tax Committee concluded its audit on February 10, 2009, it notified KPM and TNG that the amortization rate stated in Article 23 of the tax law, and not the contractually agreed upon Article 20 rate, was retroactively applicable to the companies' well drilling costs for the years 2005 to 2007. It assessed against the companies approximately USD 62 million in back taxes and penalties, in clear violation of the contract terms.[312] On March 2, 2009, KPM and TNG filed separate complaints before the Tax Committee requesting cancellation of the February 10, 2009 notices.[313] The Tax Committee refused to consider the companies' complaints, and Claimants spent the next year and a half litigating the matter before the Kazakh courts.[314]

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[310] *See* Articles 17.11 and 29.2 of the KPM Subsoil Use Contract, Articles 12.11 and 24.1 of the TNG Tolkyn and 302 Properties Subsoil Use Contracts, C-45, C-52, and C-53.

[311] Under the Subsoil Use Contracts, amendments to the legislation made after the signature of the Contracts that deteriorate the position of the Contractor shall not be applicable to the Contracts. *See* Article 29.2 of the KPM Subsoil Use Contract, Articles 24.1 of the TNG Tolkyn and 302 Properties Subsoil Use Contracts, C-45, C-52, and C-53. The tax law in force on April 1, 1999 provided two different methods for amortization of the construction costs under articles 20 and 23. Article 20 allowed amortization of construction costs for tangibles such as wells, storage, and pipelines at up to 100% within the year that construction costs were incurred, and Article 23 allowed amortization of the same costs at up to 25% upon commencement of production. In early 2004, Claimants entered into Supplements to the Subsoil Use Contracts with the State that explicitly designated the Article 20 amortization rate of 100% as applicable to oilfield construction costs, including drilling activities. Claimants thereafter calculated their corporate income tax by using the amortization rate set out in Article 20 of the tax law and the supplement to their Subsoil Use Contracts, with the blessing of the State. *See* Articles 4.4.7.1 of Annex 2 of Supplement No. 3 to the KPM Subsoil Use Contract dated February 9, 2004, of Supplement No. 4 for the TNG Tolkyn Subsoil Use Contract dated January 28, 2004, and of Supplement No. 3 to the TNG 302 Properties Subsoil Use Contract dated January 28, 2004, C-45, C-52, and C-53.

[312] *See* Notices No. 28 and No. 29 to KPM and TNG from the Tax Committee dated February 10, 2009, C-155.

[313] *See* Complaints from KPM and TNG to the Tax Committee dated February 27, 2009, C-156.

[314] On July 1, 2009, KPM and TNG separately filed cases against the Tax Committee in the Astana Economic Court seeking cancellation of the February 10, 2009 notices. On September 8 and 9, 2009, the Court ruled against KPM and TNG, and found that the tax assessments were proper. KPM and TNG appealed the ruling, and the Civil Collegium of Astana Court reversed the Astana Economic Court's ruling on October 28, 2009, remanding it for a new hearing. The Astana Economic Court issued a new decision against KPM and TNG on December 25, 2009, and KPM and TNG appealed this decision on January 6, 2010.

160. While the matter was pending appeal, on February 3, 2010, the Ministry of Finance notified KPM that it was monitored for bankruptcy on January 26, 2010 for 3.8 billion Tenge, including interest.[315] The back taxes and penalties regarding the corporate income tax represented 85% of the amount notified by the Ministry of Finance, or 3.2 billion Tenge (approximately USD 40 million). In connection with what Claimants perceived as a bankruptcy notice,[316] the State filed a request with the Specialized Interdistrict Economic Court of Mangystau Region for external management of KPM (appointment of a bankruptcy administrator) on April 26, 2010.

E. The State Imposed Illegal Export Duties

161. In another egregious example of the exercise of State muscle to harass TNG and KPM, the Financial Police intervened in a pre-existing export duty dispute involving KPM. On October 18, 2008, the Financial Police instructed the Customs Committee to conduct an audit of KPM's and TNG's compliance with the export tax laws.[317] Through this audit, the Financial Police became aware of the pre-existing dispute, which involved a tax action brought by KPM for the illegal imposition of Crude Oil Export Taxes.

162. This pre-existing tax action arose as a consequence of the State's April 8, 2008, amendments to its 2005 Government Decree regarding the payment of export taxes. Pursuant to the 2008 amendments, a 109.91 USD/ton duty was imposed on exported crude oil. However, the amendment explicitly exempted application of the new tax to exported crude oil that had been extracted under Contracts on Extraction of Hydrocarbons (Subsoil Use Contracts), which like KPM's Subsoil Use Contract, contained specific exemptions from the Crude Oil Export Tax.[318]

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315 Bankruptcy Notice dated January 26, 2010, C-157. *See* Condorachi Statement ¶ 40.

316 Pisica Statement ¶ 54.

317 *See* Letter from the Financial Police to the Customs Committee dated October 18, 2008, C-11.

318 *See* Letter from the Financial Police to the Executive Secretary of the Ministry of Finance dated November 25, 2008, C-162. The KPM Subsoil Use Contract contained precisely such a contractual exemption, providing that "The Contractor shall not pay any export taxes for the export of any goods and products, including those previously imported." See Article 7.6.1.2 of the KPM subsoil Use Contract, as introduced by Supplement No. 3 dated February 9, 2004, C-45.

163. To avoid improper imposition of export taxes, KPM duly notified the Customs Committee of its contractual exemption. Despite the explicit exemption, however, the Customs Committee notified KPM on July 3 and 30, 2008, that Contract No. 305 contained no regulations as to the exemption from export tax and, thus, export tax shall be applicable to the crude oil exported under the foregoing contract.[319] Pursuant to this notice from the Customs Committee, KPM would have been prohibited from exporting 22,000 tones of crude oil for August 2008 absent payment of the Crude Oil Export Tax. To avoid imperiling this and subsequent exports, KPM conditionally paid the wrongfully imposed export taxes, and concurrently commenced a legal action challenging imposition of the tax.[320]

164. On November 19, 2008, KPM won in the court of first instance, which ruled that the imposition on KPM of the Crude Oil Export Tax was illegal.[321] By the date of that court decision, KPM had already paid approximately USD 10 million in Crude Oil Export Taxes. The court decision should have put the matter to rest. However, the following day, the Financial Police intervened, commenced an "investigation" concerning KPM's contractual export tax exemption, and ordered the Ministry of Finance to produce all the relevant documents regarding KPM's exemption from the payment of the export tax.[322]

165. On December 23, 2008, the Board of Appeal of the Mangystau Regional Court accepted an appeal of the November 19, 2008, court ruling in favor of KPM by the Aktau territorial customs body.[323] The Mangystau Regional Court

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[319] *See* Letter from the Financial Police to the Executive Secretary of the Ministry of Finance dated November 25, 2008, C-162.

[320] If exports are prohibited or curtailed, KPM must reduce field production because of storage capacity constraints. KPM's action on the illegal imposition of the crude Oil Export Tax was heard in the court of first instance on November 19, 2008. During the course of KPM's tax action, the State revised its position taken in its July 3, 2008 notice, revoking it and stating in a letter to KPM and the Aktau territorial customs body dated October 2, 2008, that a government committee set up on July 29, 2008, had "decided to exempt KPM from payment of Crude Oil Export Tax for the quantities exported under Contract no. 305 as of March 30, 1999." Letter from the Financial Police to the Executive Secretary of the Ministry of Finance dated November 25, 2008, C-162.

[321] *See* Decision of the Board of Appeal of the Mangystau Regional Court dated December 23, 2008, C-161.

[322] Letter from the Financial Police to the Executive Secretary of the Ministry of Finance dated November 25, 2008, C-162.

[323] Decision of the Board of Appeal of the Mangystau Regional Court dated December 23, 2008, C-161.

completely cancelled in cassation proceedings the November 19 ruling in favor of KPM, and KPM's subsequent appeals of this decision to the Mangystau Regional Court were dismissed.[324] The State therefore retained more than USD 10 million of patently improper export taxes that KPM had conditionally paid.

166. Subsequent to this Orwellian ruling by the courts, the State introduced a new tax provision effective January 1, 2009, which replaced crude oil export taxes with a Rent Tax for Export.[325] To prevent (at least theoretically) imposition of a double tax on the same quantities of exported crude oil beginning in January 2009, the State also issued a December 24, 2008 decision stating that the Crude Oil Export Tax would not be applicable to crude oil exports subject to the Rent Tax starting on January 1, 2009.

167. On December 30, 2008, KPM submitted to the Aktau territorial customs body a declaration for the quantities of crude oil to be exported by it in January 2009 (in the amount of about 21,000 tons). Pursuant to the December 24, 2008 decision, KPM did not pay the Crude Oil Export Tax for these January 2009 exports, and instead, paid the newly applicable Rent Tax for Export.

168. Once again, on September 30, 2009, the Financial Police intervened, ordering the Aktau territorial customs body to conduct a new audit of KPM based on its alleged failure to pay the explicitly inapplicable Crude Oil Export Tax for KPM's January 2009 exports.[326] On November 3, 2009, to put pressure on KPM to pay this inapplicable Crude Oil Export Tax, the Financial Police interrogated and intimidated Mr. Cornegruta, who was then in jail, and other employees of KPM.[327] Not coincidentally, the regional territorial customs body also informed KPM that it was required to pay the inapplicable Crude Oil Export Tax for its January 2009 exports, amounting to USD 4 million. At the time, Mr. Condorachi, the General Counsel of

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[324] Decision of the Board of Appeal of the Mangystau Regional Court dated December 23, 2008, C-161. The implausible ruling by the appellate courts was that oil did not constitute "goods" under the KPM contractual export exemption, or, as stated by the courts, "the term of hydrocarbons is embedded in the term crude oil, but they still can not agree with the conclusion that crude oil constitutes goods."

[325] *See* Condorachi Statement ¶ 34.

[326] *See* Condorachi Statement ¶ 34.

[327] Condorachi Statement ¶¶ 36-37.

KPM and Deputy General Counsel of TNG, was also interviewed by the Financial Police on October 22, 2009. He recalls:

> The interview lasted for about an hour. It appeared to be the view of the Financial Police that as an in-house lawyer, I was the person responsible for preventing the payment of the export tax. At that time, we could not pay the export tax even if it was owed (it was not, in our view); we simply did not have the money. The Financial Police seemed disappointed to learn that I only started working at KPM on January 20, 2009, and, therefore, I was not with the company at the time the customs declarations were drawn up for the Crude Oil Export Tax allegedly due. As they indicated, it meant they could not bring a criminal case against me. When I informed the Financial Police that we were acting in good faith and we were following the procedures laid down, the police officer stated that it did not matter since the courts would decide quickly.[328]

169. In January 2010, KPM commenced a legal action concerning the illegal imposition of the Crude Oil Export Tax on its January 2009 exports.[329] On March 3, 2010, the Interdistrict Economic Court of Mangystau Region dismissed KPM's action, and subsequent appeals of this decision against KPM were also dismissed.[330]

170. On February 24, 2010, the Regional Customs Committee notified KPM *and TNG* that the companies were liable for Crude Oil Export Tax on their January 2009 exports.[331] Ironically, on March 31, 2010, the Central Customs Committee cancelled the notifications to KPM and TNG and stated that, pursuant to their Subsoil Use Contracts, KPM and TNG were not liable for export taxes.[332]

171. Having served the purpose of both harassing KPM and extorting from it more than USD 10 million, the State chose not to raise the issue when, in July 2010, it compiled the list of alleged Subsoil Use Contract violations that it used to directly expropriate Claimants' Kazakh investments. Furthermore, it would have been an impossible task for the State to prove that its explicit violation of the KPM's Subsoil Use Contract constituted a Subsoil Use Contract violation by KPM.

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328 Condorachi Statement ¶ 35.

329 *See* Condorachi Statement ¶ 36.

330 *See* Condorachi Statement ¶ 37.

331 Notices from the Regional Customs Committee to KPM and TNG dated February 24, 2010, C-44.

332 Notices from the Central Customs Committee to KPM and TNG dated March 31, 2010, C-130.

F. The Transfer Price Audit and Dispute

172. On November 7, 2008, the Tax Committee initiated another, targeted audit of KPM and TNG at the request of the Financial Police regarding transfer pricing by the companies.[333] Under Kazakh law, the profits on oil and gas sales are not based on the contract price for which product is sold, but on a State-designated "market price" for the region in which the sale takes place. The State establishes this market price by consulting published average prices for a given region. If there is no average price for the delivery point, then the State artificially constructs one by taking an average price in an alternative region, and then deducting fictional expenses that would be incurred to transport the product from the actual delivery point to the selected, alternative region. By this rather convoluted process, contract sales that are below the State-designated "market price" are adjusted up for purposes of determining the taxable profit on a sale. Contract sales that are above the State designated market price, however, are taxed at the actual contract price and not adjusted down to the State-designated "market price."[334]

173. The Tax Committee transfer price audit lasted 13 months, ending in December of 2009.[335] Through this exhaustive audit, the State enabled itself to prowl through KPM's and TNG's financial records and examine all of the sales invoices of KPM and TNG from January 1, 2004, to December 31, 2007.[336]

174. At the end of this intrusive and lengthy audit, the State assessed approximately 700 million Tenge (USD 5 million) in back transfer price taxes and penalties.[337] Although KPM and TNG filed legal actions contesting the State's assessment, those legal actions remained pending as of the date of the State's abrogation of the KPM and TNG Subsoil Use Contracts and illegal expropriation of Claimants' investments. Undoubtedly because the legal actions were still pending, and because the audit procedure itself had evidently served its purpose, the State abandoned this issue when it compiled the July 2010 list of alleged Subsoil Use

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333 Letter from the Tax Committee to the Financial Police dated November 11, 2008, C-38.

334 *See* Condorachi Statement ¶ 32.

335 Notifications by the Tax Committee to KPM and TNG dated December 29, 2009, C-137 and C-138. *See* Condorachi Statement ¶ 33.

336 *See* Condorachi Statement ¶ 33.

337 Notifications by the Tax Committee to KPM and TNG dated December 29, 2009, C-137 and C-138.

Contract violations that it used to directly expropriate Claimants' Kazakh investments.

G. Kazakhstan's Bad Faith Refusal to Execute the Agreed-Upon Extension of the Contract 302 Properties Exploration Period

175. A critical element of the State's harassment campaign involved the Contract 302 Properties. On October 14, 2008, TNG notified the MEMR of its intention to exercise its contractual right to extend the exploration period in the Contract 302 Properties by two years, pursuant to Article 3 Contract No. 302.[338] In the following months, TNG repeatedly asked the MEMR to approve the extension of the exploration period prior to its expiration on March 30, 2009.[339] The MEMR simply ignored those requests.[340]

176. On March 9, 2009, TNG re-filed with the MEMR its notice of discovery in the East Munaibay structure, and concurrently filed a notice of discovery in the Bahyt structure.[341] TNG also notified the MEMR again of its intention to exercise its contractual right to extend the exploration period in the Contract 302 Properties by two years.

177. The State's refusal to execute the contractual extension of TNG's right to continue exploration in the Contract 302 Properties was also discussed with the MEMR Executive Secretary at the March 19, 2009 meeting.[342] The MEMR Executive Secretary endeavored to resolve this issue in favor of TNG by March 20, 2009, ten days prior to the expiration date of the exploration period. Despite this clear undertaking by the MEMR, TNG had to send reminder letters.[343]

178. Finally, after the expiration date, on April 9, 2009, the MEMR sent a letter expressly stating that "**[t]he extension of the exploration period is granted for a period of 2 years, until 03/30/2011**."[344] Accordingly, on May 4, 2009, TNG

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338 Application from TNG to the MEMR, with explanatory note and draft work program, dated October 14, 2008, C-67.

339 Letters from TNG to the MEMR dated February 16, 2009, C-166.

340 Pisica Statement ¶¶ 24-25.

341 Letters from TNG to the MEMR dated March 9, 2009, C-167.

342 Draft Minutes of the meeting dated March 19, 2009, C-42. *See* Pisica Statement ¶ 34.

343 Letter from TNG to the MEMR dated March 24, 2009, C-147.

344 Letter from the MEMR to TNG dated April 9, 2009, C-27

submitted Addendum No. 9 of Contract No. 302 to the MEMR for execution.[345] Despite repeated requests, TNG never received the MEMR's signature to the addendum extending TNG's exploration rights.[346] Consequently, TNG was contractually prohibited from further exploration of the Contract 302 Properties.

179. This bad faith refusal by the State to execute the addendum extending TNG's exploration rights prevented Claimants from continuing with their test wells and proving the full scope of the potentially substantial reserves in the Contract No. 302 prospect areas, areas in which Claimants had already conducted 3D and 2D seismic testing. Claimants' were therefore unable to establish the full monetary value of the reserves in the Contract 302 Properties, and their ability to market the properties in the Area, and to acquire full market value for their Kazakh investments, was severely undermined.

H. The Government's Harassment Campaign Served to Undermine the Market Value and Alienability of Claimants' Investments

180. The protracted State pre-emptive rights dispute, the intrusive tax and customs audits, the refusal to execute the expressly agreed-upon extension of the Contract No. 302 exploration period, the criminal actions and fines against TNG and KPM and their personnel, and the extraordinary enforcement measures taken in connection with the criminal action all had a self-evident effect: they saddled KPM and TNG with ownership and title concerns, hampered the companies' operations, created enormous monetary liabilities, monopolized precious management time and resources in protracted legal disputes, deprived Claimants of the opportunity to fully prove the reserves and market value of the Contract 302 Properties, and sent a deeply threatening message to any prospective foreign investor that was interested in purchasing the properties. It is evident that this protracted campaign of indirect expropriation by the State was designed to accomplish precisely the diminution in marketability and value and restraints on alienability that it did, and that the State had eventual direct expropriation as its ultimate goal when it commenced its campaign of harassment in late 2008.[347]

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345 Draft Addendum No. 9 to the TNG Subsoil Use Contract No. 302 dated April 30, 2009, C-168.

346 *See*, for instance, Letters from TNG to the MEMR dated September 17 and December 28, 2009, C-169 and C-170.

347 *See* Letter from Blagovest President to MEMR, dated February 7, 2010, C-23.

181. The State's ultimate goal of nationalization is confirmed by the Blagovest Letter, which was from the president of the public fund, Blagovest, to the Kazakh MEMR, sent on February 7, 2010.[348] In the letter, Blagovest's president proposes "discussion of the possible solution of the crisis surrounding TNG and KPM companies, owned by a Moldovan businessman named A. Stati," noting that to date, the "situation" has caused social tension due to possible suspension of oil and gas production, layoffs, and nonpayment of salaries.[349] The president also mentions a concern of "political profiteering" from this situation, both in Moldova, which was entering an election period, and internationally with respect to Kazakhstan, which was at the time chairing the Organization for Security and Cooperation in Europe.[350]

182. Importantly, the Blagovest's president stated:

> ***The suggestion offered for discussion may resolve the question of nationalization of the assets posed in 2008.***
>
> The following are the tasks that may be resolved:
>
> • ***Establishing control over TNG and KPM;***
>
> • Making sure that the companies are functioning as usual during the winter period, i.e., preservation of production cycle, jobs, payments of salaries, with the appointment of national experts to the key positions;
>
> • Initiation of admission by the owner of the companies that his actions related to type of control that he established over the companies were illegal;
>
> • Companies' acknowledgment of their breach of contract addressed to the authorized responsible governmental;
>
> • Joint development by the companies and the responsible government entity, with the initiative of the companies, a solution of the current situation;
>
> • Determination of debt's structure owed to the investors;
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> • Determination of flows of financing;

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348 *Id.*

349 *Id.*

350 *Id.*

> • ***Petition to the international arbitration is excluded;***
>
> • Excluding possible political speculation in the Republic of Moldova during the time when the Republic of Kazakhstan chairs OBSE;
>
> • Excluding potential problems with ROMPETROL;
>
> • Additional important questions are being resolved, including the rights of the companies for the ownership projects in Iraq and Sudan, because such projects are being conducted with Kazakhstan's funds.
>
> ***The main idea – to separate interests of the companies (contract execution, jobs, salaries, interests of Kazakhstan) and interests of their owner (political ambition, indebtedness before investors).***
>
> ***Fond "Blagovest" will act as the guarantor of execution of this offer. I hope that the resolution of the current problem will allow You to more effectively lead the Ministry for the benefit of all our people.***[351]

With this letter, which expressly states the Government's goal of "nationalization of the assets posed in 2008, the president of Blagovest was responding to a direct instruction from the President of Kazakhstan. Attached to the Blagovest letter was a personal instruction from President Nazarbayev, dated November 19, 2009. President Nazarbayev clearly wanted to strip the companies of their assets, while maintaining the assets operational. President Nazarbayev's personal instruction reads as follows:

> I request that you promptly review and make suggestions about the prospects of Open Company "Tolkynneftegas", "Borankol Gas Refining Factory", Open Company "Kazpolmunai",Open Company "KASCO" and the company "Caspian Gas Corporation" working on the fields of Beykeuskiy district of Mangistau region. The governor of the region K. Kusherbayev reported that as a result of inspections by law enforcement body it took place a full stop of trades (oil and gas extraction) and the construction of the Gas Refining Factory, compressor stations and gas gathering units. Nearly 3 thousand people are fired, that leads to the conditions for social tension. Why it is necessary to stop the production?

[351] *Id*. (emphasis added).

> I ask once again to revisit these issues in view of anti-crisis measures of the Government. Checks should not lead to problems with people who are working.[352]

183. Thus, it is clear that the Government's plan - devised as early as 2008 - was to gain control of KPM and TNG through nationalization, and in the process, to appear benevolent to the local population by avoiding disruption to oil and gas production, and escaping international liability by attempting to avoid international arbitration.[353]

184. The effect of Kazakhstan's planned actions on the marketability of Claimants investments was already evident when, in January 2009, Claimants made a business decision to proceed to the second phase of the Project Zenith sale process.[354] At that time, Claimants decided to include the Contract 302 Properties in the process, provided the buyer would agree to defer compensation for the block until its reserves had been established, a task that Claimants did not know at the time the State would render impossible.[355]

185. In re-opening the second phase of Project Zenith, Claimants instructed Renaissance Capital to contact seven of the eight interested bidders who had made indicative offers in the first round, specifically instructing Renaissance Capital not to re-contact KazMunaiGas at that time.[356] Two of the companies contacted expressed a renewed interest in the properties: Total and Turkish Petroleum Corporation.[357] In addition, a new interested party, PSA Energy Holding SPC, was also identified and signed a non-disclosure agreement so that it could proceed with due diligence.[358]

186. In mid-February 2009, these three companies were granted access to the electronic data room containing over 2,000 reports, agreements, surveys, maps, and other documents relating to KPM's and TNG's geological data, operations, and

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352 *Id*. (emphasis added).

353 *See* Stati Statement ¶ 30; *see also* Order from Chief of Aktau Territorial Department and KPM, dated June 9, 2010, C-199.

354 Stati Statement ¶ 31.

355 *Id*.

356 Lungu Statement ¶ 54; Stati Statement ¶ 33.

357 Lungu Statement ¶ 54; Stati Statement ¶ 33.

358 Lungu Statement ¶ 54; Stati Statement ¶ 33.

financial, tax, and legal matters.[359] The geological data contained in the data room included 3D seismic data, interpreted seismic horizons, faults (cuts and boundaries), and well tops and coordinates.[360] Turkish Petroleum Corporation and PSA Energy Holding SPC examined the data room, and subsequently withdrew from the bid process.[361]

187. Total examined the data room, and Claimants did a management presentation for Total in February 2009. After its examination of the data room and the management presentation, Total stated that they were going to talk with the Kazakh authorities about the properties before they would be willing to move ahead with a binding proposal.[362] Total talked to the Kazakh authorities in late February or early March 2009, and later sent a letter withdrawing from the bid process, allegedly for technical reasons relating to the properties.[363] As made clear by Mr. Lungu in his witness statement, however, Claimants believe that the Kazakh authorities discouraged Total from continuing the negotiation process, and believe that Total's real reason for withdrawing from the process was the ongoing State harassment campaign against KPM and TNG and its effect on operations, cash flow and clear title to the properties.[364]

188. In July 2009, KNOC expressed a renewed interest in the properties and re-entered the bid process.[365] KNOC examined the Project Zenith data room; Claimants conducted a management presentation for them in July; and representatives of KNOC also went for a site visit of the properties in August of 2009. However, as with Total, KNOC was only willing to proceed with a binding bid after it had spoken with the Kazakh authorities about the properties.[366] Claimants later learned that KNOC had spoken with the Kazakh authorities in late August or

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359 Lungu Statement ¶ 55.

360 *Id.*

361 *Id.* ¶ 56.

362 *Id.* ¶ 57.

363 Lungu Statement ¶ 57; *see also*, Letter from Total E&P to Renaissance Capital, dated July 24, 2009, C-296.

364 Lungu Statement ¶ 57; *see also*, Stati Statement ¶ 35.

365 Lungu Statement ¶ 60.

366 *Id.*

early September 2009.[367] After that conversation, Claimants never heard from KNOC again. Claimants believe that, as with Total, the Kazakh authorities discouraged KNOC from proceeding with negotiations, and that KNOC withdrew from the bid process because of the ongoing State harassment campaign against KPM and TNG and its effect on operations, cash flow and clear title to the properties.[368]

189. In August 2009, Claimants were also contacted by a company called Starleigh, a Kazakh-owned company that Claimants later learned was owned and controlled by Mr. Timur Kulibayev, President Nazarbayev's son-in-law and the head of KazMunaiGas.[369] Starleigh was represented by a middle man, Mr. Arvind Tiku, whom Claimants understand to be one of Mr. Kulibayev's business partners.[370]

190. Starleigh examined the Project Zenith data room, and after Claimants did a management presentation for them, they presented an initial bid of USD 450 million in October 2009.[371] Subsequently, in November 2009, Starleigh dropped its offer to USD 350 million, stating that they had concerns about the USD 145 million fine that had been imposed on KPM in connection with criminal action brought by the State, and that they believed it would cost them between USD 50 and 100 million to resolve the fine.[372] Later, in late 2009 or early 2010, Claimants met with Mr. Tiku of Starleigh in London. He informed them at that meeting that Starleigh was unwilling to proceed with an enterprise value bid for the companies, and instead would only be willing to make a bid consisting of a buy-out of the companies' Note-holders, and a payment of USD 50 million for our equity interests.[373]

191. The "re-evaluation" of the companies that had been ordered by Mr. Batalov in connection with the State's re-assertion of a pre-emptive right to purchase TNG consisted of an examination of the companies' books and records by KazMunaiGas, and an examination of the Project Zenith data room by KazMunaiGas

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367 *Id.; see also*, Stati Statement ¶ 35.

368 *Id.*

369 Lungu Statement ¶ 58; Stati Statement ¶ 39.

370 Lungu Statement ¶ 58; Stati Statement ¶ 39.

371 Lungu Statement ¶ 59.

372 *Id.*

373 Lungu Statement ¶ 59; Stati Statement ¶ 39.

in April 2009.[374] After this examination, Claimants met with KazMunaiGas in June 2009, and KazMunaiGas claimed at that time that the market value of TNG and KPM was equal to zero.[375] KazMunaiGas stated that they would only offer to pay the face value of Claimants debts and USD 50 million for Claimants equity interests, precisely the same terms that were later offered by Starleigh. Clearly KazMunaiGas was aware of Kazakhstan's evident goal of nationalizing the companies, and it was not inclined to offer to pay for what it would eventually get for free.[376]

192. In November 2009, Claimants were invited to attend a meeting with KazMunaiGas in Amsterdam.[377] When Mr. Stati and Mr. Lungu arrived, they saw principals of Claimants main Note-holders leaving the meeting room.[378] The Note-holders told them that KazMunaiGas had just offered 25 cents on the dollar to purchase their interests.[379] The Note-holders had refused the offer, and were clearly agitated and insulted by the encounter.[380] Mr. Stati and Mr. Lungu then met with representatives of KazMunaiGas, and KazMunaiGas presented them with an equally *de minimis* USD 20 million offer for their equity interests.[381] They refused the offer.[382]

193. Subsequently, on February 13, 2010, Claimants were able to negotiate an agreement for the sale of 100% of the shares and participatory interests in KPM and TNG to Cliffson Company S.A.[383] The total value of the agreement, including the buy-out of the companies' Note-holders and payment for Claimants equity interests, exceeded USD 930 million.[384]

194. One of the conditions in the purchase agreement was that the Kazakh Ministry of Oil and Gas (the "MOG", the successor to the MEMR) grant permission

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374 Lungu Statement ¶ 44, 61; *see also*, Pisica Statement ¶ 33.

375 Lungu Statement ¶ 61; Stati Statement ¶ 37.

376 Lungu Statement ¶ 61; Stati Statement ¶ 37.

377 Lungu Statement ¶ 62; Stati Statement ¶ 38.

378 Lungu Statement ¶ 62; Stati Statement ¶ 38.

379 Lungu Statement ¶ 62; Stati Statement ¶ 38.

380 Lungu Statement ¶ 62; Stati Statement ¶ 38.

381 Lungu Statement ¶ 62; Stati Statement ¶ 38.

382 Lungu Statement ¶ 62; Stati Statement ¶ 38.

383 Lungu Statement ¶ 63; Stati Statement ¶ 40.

384 Stati Statement ¶ 40.

for the sale, including waiver of the State's alleged pre-emptive right to purchase KPM and TNG.[385] KPM and TNG presented the appropriate applications for permission to the MOG, along with a request that the State waive its preemptive right to acquire KPM and TNG.[386] In response, the MOG stated that permission for the sale necessitated removal of the attachment orders by which the State had seized KPM and TNG assets, adding that, pursuant to the "seizure of assets of [KPM and TNG], including the subsoil use right and 100% participatory interest in the equity capital of the company, deals regarding the alienation of the subsoil use right are prohibited."[387] The MOG also claimed that it was in need of information about the financial solvency of Cliffson Company, as well as its technical and managerial capabilities.[388] The Ministry subsequently presented a list of additional materials to be submitted by KPM and TNG in order to determine the economic feasibility of the State's acquisition of KPM's and TNG's seized assets.[389]

195. KPM and TNG presented the materials requested by the MOG, but there was no reply from the Ministry.[390] Claimants subsequently received confirmation that Cliffson Company had submitted a letter to the MOG stating its refusal to purchase the interests in TNG and KPM under the February 13, 2010, agreement.[391]

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385 Lungu Statement ¶ 64.

386 *Id.*

387 *Id.*

388 *Id.*

389 *Id.*

390 *Id.* ¶ 65.

391 *Id.*

V. KAZAKHSTAN'S OUTRIGHT SEIZURE OF CLAIMANTS' INVESTMENTS

A. Direct Expropriation of Claimants' Investments

1. The State's Final Inspection Blitz

196. On January 25, 2010, the MEMR notified KPM and TNG that it would perform a week-long unscheduled inspection, allegedly to ensure compliance with Subsoil Use Contract obligations.[392]

197. On May 7, 2010, TNG received a notice from the MEMR Geological Committee that it had failed to comply with the annual working program for exploration required in Contract No. 302.[393] It requested that TNG respond with an explanation by May 20, 2010. Separately, on May 7, 2010, the Ministry of Oil and Gas wrote to TNG to notify it of inadequate fulfillment of license and contract provisions for 2009.[394] This notice requested that TNG "remove delays" in its 2009 Contract No. 302 work program and present to the Ministry a draft appendix for the 2010 work program within one month.

198. On May 27, 2010, TNG wrote to the Ministry of Oil and Gas, explaining that TNG had submitted in October 2008 an application for a two-year extension of the exploration period in its Contract 302 Properties, as well as the corresponding work program. TNG also explained that the MOG, in its letter of April 9, 2009, had expressly agreed to the extension; that in response to the MOG's April 9 letter, TNG had submitted the appropriate extension addendum for execution dated April 30, 2009; and that TNG had never received the executed extension from the MOG. Consequently, TNG suspended its exploration operations in the Contract 302 Properties so as not to be in breach of its obligations by conducting exploration activities without Ministry approval. As this issue was not the result of any failure to act on the part of TNG, TNG concluded its letter by affirming that in all other respects, its contractual obligations have been fulfilled - and "in some cases over-fulfilled" - for the Contract 302 Properties.

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[392] *See* MEMR Letter to KPM and TNG dated January 25, 2010, C-171; *see also* Order of January 22, 2010 regarding TNG, C-122 and Order of January 25, 2010 regarding KPM, C-124.

[393] *See* Notice from MEMR Committee for Geology and Subsoil Use to TNG, dated May 6, 2010, C-172.

[394] *See* Letter from MOG to TNG dated May 7, 2010, C-173.

199. On June 29, 2010, the General Prosecutor's office issued two orders for yet more unscheduled inspections of TNG and KPM, the purpose of which was, very broadly, to assess applicable legislation from the date each of the companies was established in 1997 to the present day.[395] The inspections would be conducted by multiple state agencies, including internal affairs, emergencies, oil and gas, labor, environmental protection, industry and new technologies, and territorial bodies.[396]

200. Thus, during June and July, 2010, a dozen Government agencies sent notices that unscheduled inspections of KPM and TNG would commence. The inspections were conducted by the Ministry of Oil and Gas; the Ministry of Emergency Situations; the Fire Inspectorate; the Ministry of Environment and Ecology;[397] the Sanitation Inspectorate; the State Standards Authority; the Ministry of Labor and Social Protection;[398] the Financial Police; the Architectural and Engineering Inspectorate; the Office of the Public Prosecutor;[399] the Immigration Police;[400] and the Office of Natural Resources.

201. On June 29, 2010, the Ministry of Industry and New Technologies' Geology and Subsoil Use Committee ordered a two-week inspection of KPM and TNG to determine whether the companies were in compliance with subsoil and subsoil use legislation.[401] On the same date, the Chief State Ecological Inspector of Mangystau Oblast notified KPM and TNG that an unscheduled inspection would take place beginning June 30, 2010, to inspect for compliance with environmental protection legislation.[402] Also on that date, the State Labor Inspector sent notices to

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395 *See* Decision No. 37 from the Public Prosecutor's Office to KPM, dated June 29, 2010, C-174; Decision No. 38 from Public Prosecutor's Office to TNG, dated June 29, 2010, C-175.

396 Condorachi Statement ¶¶ 42-43.

397 *See* Notification No. 48 of June 29, 2010, from Chief State Ecological Inspector to TNG and KPM, C-182.

398 *See* June 28, 2010 notice of inspection from Labor Department, C-177.

399 *See* June 29, 2010 notice of inspection from the Public Prosecutor's Office, C-178.

400 *See* July 1, 2010 notice of inspection from Immigration Police, C-179.

401 *See* Order No. 65 from MINT, Geology and Subsoil Use Committee, dated June 29, 2010, C-180; *see also* Notification No. 18-05-2076 from MEMR, Geology and Subsoil Use Committee to KPM and TNG, C-181.

402 *See* Notification No. 48 of June 29, 2010, from Chief State Ecological Inspector to TNG and KPM, C-182.

KPM and TNG that unscheduled inspections would take place.[403] Likewise, the Immigration Police sent notifications of inspections that were to take place from July 1, 2010, to July 29, 2010, in order to ensure that neither KPM nor TNG was in violation of Kazakhstan's "immigration" legislation.[404]

202. The Ministry of Oil and Gas also conducted inspections, claiming that it wanted to inspect for compliance with Subsoil Use Contract provisions and compliance with the Subsoil and Subsoil Use Law.[405] That was the very same purpose that the MOG had given for its prior inspections just six months before, during which it had found no major infringements.

203. On July 4, 2010, members of the same team from the Financial Police responsible for the arrest of Mr. Cornegruta and the threats against numerous employees of KPM and TNG arrived on the premises to conduct their investigation.[406] July 4, 2010, was the Sunday of a long holiday week-end, and the Financial Police requested access to the Human Resources Department.[407] Claimants feared that a search through personnel files would lead to another arrest and ordered the middle-management of KPM and TNG to evacuate Kazakhstan.[408]

204. In addition to these inspections, on July 9, 2010, a representative from Mangystau Oblast's Entrepreneurship and Industry Department, a division of the Regional Authority of Mangystau, called TNG to inform it that Kazakh Prime Minister K.K. Massimov planned to visit the LPG plant during a working trip to the region.[409] In advance of this trip, the Governor of the Mangystau region planned to visit the facilities to inspect the LPG plant, as well as to ensure certain preparations had been completed. He instructed TNG to prepare and/or construct: (i) landing pads in the vicinity of the LPG plant in order to support the arrival of three

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403 *See* Letter No. 06-02/2383 from State Labor Inspector to TNG, dated June 28, 2010, C-177; Letter No. 06-02/2384 from State Labor Inspector to KPM, dated June 28, 2010, C-177.

404 *See* July 1, 2010, notice of inspection from migration police to KPM, C-179; *see also* July 1, 2010, notice of inspection from migration police to TNG, C-179.

405 *See* Notice No. 14-05-4539 from MOG to TNG dated June 29, 2010, C-185.

406 Condorachi Statement ¶¶ 44-45.

407 Condorachi Statement ¶ 44.

408 Stati Statement ¶ 41 ("I wanted to avoid having more personnel thrown in jail."); Condorachi Statement ¶ 45; Pisica Statement ¶ 56.

409 *See* Telephone Message No. 05 of July 9, 2010, signed by L. Ulzhabayeva, C-186; *see also* Telephone Message No. 319 of July 12, 2010, signed by S. Bermuhamedov., C-299.

helicopters; (ii) a presentation of the LPG Plant project, including photographs, technological specifications, and remaining financing required; and (iii) a platform on which discussion of the project could take place.[410]

205. In further preparation for the visit, the Governor's office again contacted TNG on July 12, 2010, to request that it make its Land Cruiser and other automobiles available for the entire delegation, as well as drivers.[411] The Land Cruiser was one of the vehicles that had been arrested in prior seizure orders that year. The members of the Government delegation would include the Prime Minister, the Minister of Oil and Gas, the regional Governor, and several other high-level officials.

2. The Government's Eleventh-Hour Attempt to Find Violations of KPM's and TNG's Subsoil Use Contracts

206. By notices dated July 14, 2010, but actually received by KPM and TNG on July 16, 2010, the Ministry of Oil and Gas informed KPM and TNG of alleged Subsoil Use Contract violations, which it claimed to have discovered during its inspections. With respect to KPM's Borankol Contract No. 305, the Ministry of Oil and Gas alleged:

- that KPM had provided no information regarding its Work Program;
- that KPM had not fulfilled obligations relating to instruction and training of a Kazakh specialist;
- that KPM had failed to pay 114,809 USD in costs;
- that KPM had failed to pay contributions to the liquidation fund, as required;
- that KPM had failed to timely and completely pay taxes;
- the KPM had admitted that it operated main oil and gas pipelines without a license; and
- that KPM had violated its obligations regarding acquisition of goods, works, and services.[412]

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410 *See* Telephone Message No. 05 of July 9, 2010, signed by L. Ulzhabayeva, C-186; *see also* Romanosov Statement ¶ 37.

411 Telephone Message No. 319 of July 12, 2010, signed by S. Bermuhamedov, C-299.

412 *See* Notice of infringement of obligations under Contract No. 305, from MOG to KPM, dated July 14, 2010, C-2.

The Ministry of Oil and Gas gave little explanation of the reasoning behind the alleged violations and did not provide support for the allegations; rather, it merely provided a list of conclusory statements. The notice instructed KPM to respond within five days, *i.e.*, by July 19, 2010, with explanations regarding the allegations. The MOG also stated that failure to respond could result in termination of the Borankol Contract. Other than the obvious reference to the State's criminal action against KPM, itself falsely couched as an "admission" that KPM had operated a "main" oil and gas pipeline without a license, KPM had never before been accused of any of the listed violations.

207. With respect to TNG's Tolkyn Contract No. 210, the MOG alleged:

- that TNG had provided no information regarding execution of its Work Program;
- that TNG had not provided annexes regarding the training of employees;
- that TNG had failed to instruct and train a Kazakh specialist as required in the contract;
- that TNG had failed to pay costs amounting to over 84,000 USD; and
- that TNG had admitted operation of trunk oil and gas pipelines without a license; and
- that TNG had violated its obligations regarding acquisition of goods, works, and services.[413]

Again, no adequate reasoning or evidence accompanied the list; it was merely a series of conclusory statements. The notice instructed TNG to respond within five days, *i.e.*, by July 19, 2010, with an explanation regarding the allegations. The MOG also stated that failure to respond could result in termination of Contract No. 210. And again, other than the obvious reference to the State's criminal action against TNG, itself falsely couched as an "admission" that TNG had operated a "main" oil and gas pipeline without a license, TNG had never before been accused of any of the listed violations.

[413] *See* Notice of infringement of obligations under Contract No. 210, from MOG to TNG, dated July 14, 2010, C-4.

208. Regarding TNG's Contract No. 302, the Ministry of Oil and Gas alleged the following:

- that TNG had provided no information regarding its Work Program;
- that TNG had not provided annexes regarding employee training;
- that TNG had not fulfilled its obligation to instruct and train a Kazakh specialist;
- that TNG had admitted to the unlicensed operation of main oil and gas pipelines; and
- that TNG had violated its obligations regarding acquisition of goods, works, and services.[414]

Again, no adequate reasoning behind the allegations was given. The notice instructed TNG to respond within five days, *i.e.*, by July 19, 2010, with an explanation regarding the allegations. The MOG also stated that failure to respond could result in termination of Contract No. 302. Other than the references to 1) TNG's work program for the Contract 302 Properties, which had been the subject of the May 2010 inquiry by the MEMR's Geological Committee, and to which TNG had already provided an explanation, and 2) the bizarre reference to the criminal action, which was not relevant to TNG's Contract No. 302 operations and which was falsely couched as an "admission" that TNG had operated a "main" pipeline without a license, TNG had never before been accused of the alleged violations.

209. Despite the exceedingly short notice given by the MOG for a response, both KPM and TNG submitted detailed responses to each of the alleged violations on July 19, 2010, as demanded.[415] KPM explained that it submitted quarterly reports on the execution of the annual work program, as required by Kazakh law.[416] It stated that these reports were discussed in Technical Committee meeting minutes, which it attached, and it explained that copies of the reports were

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414 *See* Notice of infringement of obligations under Contract No. 302, from MOG to TNG, dated July 14, 2010, C-5.

415 *See* Answer to the notification on infringement of obligations under Contract No. 305 to MOG from KPM, dated July 19, 2010, C-24; *See* Answer to the notification on infringement of obligations under Contract No. 210 to MOG from TNG, dated July 19, 2010, C-26; *See* Answer to the notification on infringement of obligations under Contract No. 302 to MOG from TNG, dated July 19, 2010, C-25.

416 *See* Answer to the notification on infringement of obligations under Contract No. 305 to MOG from KPM, dated July 19, 2010, C-24.

given to government agencies each time an inspection occurred.[417] KPM had, in fact, given these documents to the MEMR during the prior inspections that year, on January 22, 2010, and on June 28, 2010.[418] Consequently, there was no reason for the Ministry to claim that KPM had not complied with its work program requirements.

210. Further, KPM explained that the amount of funds allocated for employee training was approximately USD 461,200, an amount that exceeded the actual amount needed for training all of KPM's employees.[419] KPM also explained that it had twice written to the Ministry of Oil and Gas, asking where the superfluous funds should be transferred, but never received a response.[420] Copies of the letters were attached. Thus, the Ministry's allegation that KPM failed to train its employees, seemingly stemming solely from a notation of unused training funds from KPM's books, was completely without merit.

211. Regarding the claim that KPM failed to pay costs amounting to US 114,809, KPM explained that this figure was a direct result of the Financial Police seizing KPM's assets in May 2009 and the judicial executor seizing bank accounts in January 2010.[421] These seizures were a result of the criminal investigation the State initiated, which KPM explained, amounted to *force majeure* under the contract.[422] KPM also explained that it was similarly unable to pay the USD 10,000 owed to the liquidation fund, and various taxes, as a result of financial constraints the criminal investigations caused.[423] Because the State's actions amounted to *force majeure* under the contract, KPM was not contractually liable for these costs.[424]

212. KPM then addressed the claim that it had admitted operation of main oil and gas pipelines without a license. It explained that no so-called "trunk"

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417 *Id.*

418 *Id.*

419 *Id.*

420 *Id.*

421 *Id.*

422 *Id.*

423 *Id.*

424 *Id.*

pipelines were listed in its balance sheet, and that KPM had never exploited a trunk or main pipeline. KPM attached numerous letters that had been previously sent to government agencies in this regard, including the conclusion from the MEMR in February 2010 that the 18 kilometer pipeline in question was part of a single technological process of the oil production system, and as such, could not be classified as a "main" pipeline. Thus, by the Government's own conclusion, KPM could not be said to have illegally operated a main pipeline.

213. Finally, KPM responded to the allegation regarding its obligation to purchase goods, works, and services, by simply referring the Ministry to its previously submitted "notes and objections" explaining how this issue too, like all of the other claims, was groundless.

214. Similar to KPM, TNG responded to the substantive complaints from the Ministry regarding its Contract Nos. 210 and 302. Many of the explanations had the same basis as those KPM presented, including, especially, TNG's correspondence regarding the incorrect claim that it illegally operated main oil and gas pipelines and the supporting conclusion from the MEMR in this respect. Specifically regarding the Tolkyn Subsoil Use Contract (Contract No. 210), TNG attached all of the necessary supporting documentation to show that none of the Ministry's claims were proper, including documentation regarding its work programs, employee training, payment in fact of the costs the Ministry claimed it had not paid, and the purchase of goods, works, and services.[425]

215. With respect to Contract No. 302, TNG provided similar documentation of execution of its work program as required, its training programs, and the purchase of goods, works, and services.[426] In response to the Ministry's claim that TNG illegally operated main oil and gas pipelines, which the Ministry alleged was also a violation of Contract No. 302, TNG referred the Ministry to previously submitted documentation. TNG explained that the reclassified "main" pipelines were in-field pipelines, constructed on the basis of Contract No. 210 – and not Contract No. 303 – and in accordance with procedures agreed upon with the

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[425] Answer to the notification on infringement of obligations under Contract No. 210 to MOG from TNG, dated July 19, 2010, C-26.

[426] *See* Answer to the notification on infringement of obligations under Contract No. 302 to MOG from TNG, dated July 19, 2010, C-25

competent Kazakh authorities.[427] In fact, Contract No. 302, which gave TNG exploration rights in the areas surrounding the Tabyl Block, had nothing at all to do with the classification of pipelines in TNG's gathering system.

216. Thus, it was clear that the Ministry of Oil and Gas had no real understanding of the very contract provisions it was claiming TNG had violated. It was also clear that the Government would use the fabricated "main" pipeline issue wherever and however it saw fit, in an attempt to harm – and ultimately control – Claimants' investments, contrary to the decisions and findings of other Governmental agencies.

B. The State's Abrogation of the KPM and TNG Contracts

217. By notices dated July 21, 2010, just two days after the July 19 deadline that the State had given to KPM and TNG for their responses to the State's listed Subsoil Use Contract violations, the State repudiated the Borankol and Tolkyn Contracts (Contract Nos. 305 and 210).[428] By notice dated July 22, 2010, just three days after the July 19 deadline that the State had given TNG to respond to the State's alleged violations, the State terminated the Contract No. 302.[429] That Contract, however, was not terminated for the reasons contained in the State's list of alleged contract violations. The State claimed instead that Contract No. 302 had expired on March 30, 2009. In short, the State used as an excuse to terminate Contract No. 302 its own bad faith refusal for over a year to execute an extension to which it had already agreed.

218. On July 21, 2010, the Kazakh Prime Minister, along with his entourage that included the Minister of Oil and Gas and the Aktau Regional Governor, visited Claimants' LPG plant to personally carry out the expropriation of all of Claimants' Kazakh investments. By this time, all of KPM's and TNG's General Managers had left Kazakhstan, because they feared they would be arrested in connection with the companies' criminal investigations and enforcement procedures as Mr. Cornegruta had been. Thus, when the delegation arrived, the

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427 *See id.*

428 *See* Notification No. 20-05-5150 from the Kazakh Ministry of Oil and Gas ("MOG") to KPM terminating the Borankol Subsoil Use Contract, dated July 21, 2010, C-3; Notification No. 20-05-5151 from MOG to TNG terminating the Tolkyn Subsoil Use Contract, dated July 21, 2010, C-4.

429 *See* Notification No. 14-05-5182 from MOG to TNG terminating Contract No. 302, dated July 22, 2010, C-5.

highest-level employee left in the country to meet with them was KPM's and TNG's Technical Director, Mr. Romanosov. He describes the meeting with the delegation as follows:

> At the meeting, the Minister of Oil and Gas announced that our companies had "numerous" violations registered against us. He said that on the basis of these violations, he had been instructed to inform us that our contracts were terminated. Then, the Prime Minister asked the Minister of Oil and Gas whether the decision was in accordance with legislative norms. The Minister responded that it was. Then the Prime Minister turned to the Governor of the Mangystau region and asked for his opinion. The Governor replied that he believed the decision was correct. At that time, the Prime Minister stated that he supported the decision. He then made a few general statements regarding social tensions in the area and the need to find proper solutions.
>
> When the Prime Minister was finished speaking, the Governor announced that TNG's LPG plant was included in the list of objects of strategic importance to Kazakhstan, and as a result it was necessary for the Government to ensure its completion. He explained that the Government taking over construction on the LPG plant, which KPM and TNG had halted following the Government's earlier seizure, which had previously been seized, would enable the creation of new jobs.[430]

219. The Kazakh press also reported on the Prime Minster's visit and the abrogation of KPM's and TNG's contracts. As the website Zakon reported,

> The Government of Kazakhstan canceled the contract for construction of Borankol Gas Processing Plant in Mangystau Oblast, concluded with the oil company "Tolkynneftegaz" …
>
> Statements to this end were made by the Minister of Oil and Gas Sauat Mynbayev during the working visit of the Prime-minister Karim Massimov to Mangistau region. The minister said that as of tomorrow the temporary administration of the GPP is to be carried out by the National Company KazMunayGaz.[431]

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[430] Romanosov Statement ¶¶ 38-39.

[431] *See* Media article, "'Tolkynneftegaz' was denied the right to build Borankol Gas Processing Plant," www.zakon.kz dated July 21, 2010, C-187.

220. As a result of the expropriation, and to protect their jobs, nearly 900 employees of KPM and TNG resigned effective July 21, 2010.[432] Most of these employees were then re-hired by KazMunaiGas in the same positions they held while employed by TNG and KPM.

221. The July 21, 2010, expropriation was based on Acting Prime Minister A. Magauov's order for the Minister of Oil and Gas, "to terminate unilaterally" TNG's Contract No. 210 (covering the Tolkyn field) and KPM's Contract No. 305 (covering the Borankol field) "in order not to allow prejudicing economic and ecological security of the state, as well as social and political situation according to [the Law on Subsoil and Subsoil Use]."[433] That order directed the Department of Subsoil Use Contracts and Production Sharing Agreements to (i) ensure the legislative transfer of contractual territory in those contracts in trust of the national oil company, KazMunaiGas; and (ii) notify TNG, KPM, and KazMunaiGas of the need to take measures regarding transfer of the infrastructure and equipment into temporary possession and use.[434]

222. In the termination notices faxed to KPM and TNG on July 22, 2010, the Ministry of Oil and Gas similarly informed the companies that their respective contractual territories in Contract Nos. 210 and 305 were:

> to be transferred by the former subsoil user to temporary possession and use by national company [KazMunaiGas] for the period until the transfer of property to new subsoil user. In case of absence of the former subsoil user or his evasion of transferring the property to national company, the competent body acts as his agent as regards this property.[435]

223. Kazakhstan's unilateral repudiation of the contracts came as a shock to Claimants. The full effects of the Government's actions, and what practical steps Claimants were to take next were unclear. The General Manager of TNG, Mr.

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[432] *See, e.g.*, Order No. 588 regarding Staff, from TNG, dated July 21, 2010, C-188 (with employee resignation letters attached).

[433] *See* Order No. 255 of the Ministry of Oil and Gas, dated July 21, 2010, C-189.

[434] *See* Order No. 255 of the Ministry of Oil and Gas, dated July 21, 2010, C-189.

[435] *See* Letter No. 20-05-5150 from MOG to KPM, dated July 21, 2010, C-3; Letter No. 20-05-5151 from MOG to TNG, dated July 21, 2010, C-4.

Eduard Calancea, attended a telephone call with representatives from the Ministry of Oil and Gas and KazMunaiGas on July 22, 2010 to discuss those issues.

224. During the call, Mr. Calancea inquired about the Contract 302 Properties, which were not mentioned in the notices from the Ministry. Mr. Ongarbaev, on behalf of the Ministry of Oil and Gas, responded, "We shall not refer to it right now, because the situation differs a little bit in its case, but generally speaking I can tell you that there is an order on contract cancellation due to its expiration."[436] After the call, as Mr. Ongarbaev had mentioned, TNG received a notification from the Ministry of Oil and Gas that its Contract No. 302 was terminated due to expiration of the contract.[437] The notice stated that it was issued "according to … the order of the Ministry of Oil and Gas of the Republic of Kazakhstan No. 254 of July 21, 2010." As explained above, the Government used its own failure to execute the extension it approved to "justify" the improper termination of Contract No. 302.

225. After clarifying on the call that he wanted only to discuss the contracts relating to the Tolkyn and Borankol fields (Contract Nos. 210 and 305), Mr. Ongarbaev then explained that a primary concern of the cancellation process was to ensure continuity of oil and gas production because, as he said, "we are aware of objections that might occur following such order, *probably even arbitration proceedings*."[438]

226. Mr. Calancea then asked whether the Ministry intended to comply with the contract terms, which required a 90-day notice period in the event of the State's unilateral termination in order for the termination to be effective. In response, Mr. Ongarbaev responded, "Well, generally speaking, the procedure that is being launched right now is aimed to ensure all such conditions. The fact is that production continues, and ***practically from the moment of termination the company has no longer rights over such products***, which are being extracted, over the

[436] *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

[437] *See* Notification No. 14-05-5182 from MOG to TNG, dated July 22, 2010, C-5.

[438] *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

hydrocarbons."[439] When Mr. Calancea asked on what date the Ministry considered the contracts terminated, Mr. Ongarbaev responded that it was July 21, 2010.

227. Later in the conversation, Mr. Calancea learned that KazMunaiGas and the Ministry of Oil and Gas had, on July 21, 2010, signed "an agreement of beneficial ownership over the subsoil area." Thereafter, the representative of KazMunaiGas, Mr. Utigaliev Esengali Kajugalyevich, explained that it would act as a "trust company" to ensure that continuous production occurred, that social ambiance of the region was maintained, and that no workers were terminated. He then explained that there were several variants of acquiescence to this agreement from which the companies could choose.

228. Mr. Utigaliev explained that the preferred solution would be for KPM and TNG to sign an agreement with KazMunaiGas for property trust, which would basically substitute KazMunaiGas for KPM and TNG in all of their operations. Mr. Utigaliev then explained that "a new account is being opened today, an escrow account, and everything that has been extracted since [July] 22nd, extracted oil and payment for oil, gas and condensate - such income shall arrive in the special account."[440] He explained that it was urgent that they reach an agreement that day, since that day's production by KPM and TNG would, according to the State's account of events, be illegal.

229. The call ended after Mr. Calancea confirmed that the grounds for unilateral termination of the contracts were the Ministry's notifications of non-execution of various contract provisions of July 14, 2010. KPM and TNG had thoroughly responded to those allegations on July 19, 2010, but their responses had been ignored by the Government.

230. Mr. Calancea requested that a draft substitution agreement be sent to the companies for consideration. A draft was ultimately sent, but its terms were unacceptable to Claimants. Thus, KPM and TNG never signed any type of transfer agreement with KazMunaiGas.

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439 *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

440 *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

C. The Direct Expropriation of Claimants' Property and Equipment

231. On July 22, 2010, as explained on the phone call, all revenues generated from oil and gas production went to a separate escrow account held by KazMunaiGas. The day after the announcement of unilateral contract repudiation, KazMunaiGas personnel arrived at KPM's and TNG's office to begin working at what they then considered their oil and gas production business.[441] KazMunaiGas rehired employees of KPM and TNG that had resigned.[442] Employees that wanted to continue working for the shareholders of KPM and TNG felt it necessary to leave Kazakhstan. As Mr. Romanosov explains:

> I left Kazakhstan soon after this announcement, and resigned as an employee of KPM and TNG. Since I had significant experience in operating Tolkyn and Borankol fields, I could have applied tow ork in my previous capacity for the company that took over our operations, KazMunaiTeniz. However, I did not want to continue working under the stressful conditions the Kazakh Government was capable of creating. Consequently, I transferred to Chisinau where I now work in a similar capacity for Ascom Group.[443]

232. Consistent with KazMunaiGas's representations from the July 22, 2010, conference call, KPM and TNG received letters from the Ministry of Oil and Gas on July 23, 2010, stating as follows:

> [W]e inform you that due to the unilateral termination of the contract from 00 hrs. 00 min. of July 22, 2010 all products produced on the enterprise are transferred to the ownership of the Republic of Kazakhstan.[444]

233. Kazakhstan knowingly engaged in its illegal scheme to effect the final takeover of Claimants' investments. In September of 2009, the MEMR had written to the Ministry of Industry and Trade seeking proposals on ways to acquire the assets of KPM and TNG. The Ministry responded that transfer of their property and subsoil use rights without agreement of KPM's and TNG's owners would be

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441 Condorachi Statement ¶ 50.

442 *Id*.

443 Romanosov Statement ¶ 40.

444 Letter No. 14-05-5199, from MOG to KPM, dated July 22, 2010, C-191; Letter No. 14-05-5200, from MOG to TNG, dated July 14, 2010, C-192. The letter sent to TNG was dated July 14, 2010, which suggests that the Ministry planned to terminate KPM's and TNG's contracts all along, and regardless of KPM's and TNG's responses to the Ministry's allegations of contract "violations."

unconstitutional. The Ministry further stated that, despite the criminal cases against KPM and TNG, the Government could not lawfully unilaterally terminate the subsoil use contracts and transfer their assets to the State. Kazakhstan not only knew that its plan would violate its domestic law and the contracts' terms, but it also knew that its illegal plan would subject it to international responsibility in arbitration proceedings. The Ministry of Industry and Trade warned the MEMR that its plan "may lead to continuous international court proceedings" and "have a negative impact on the image and investment attractiveness of the Republic of Kazakhstan." Nevertheless, the State carried out its illegal scheme without regard for its legal obligations to Claimants and despite those clear warnings.[445]

234. After KPM and TNG personnel were effectively ousted from their positions and Claimants' investments were seized, Mr. Anatolie Stati and the General Managers of KPM and TNG wrote letters to the Ministry of Oil and Gas, expressing their objections to its actions and to the "unprincipled seizure of [their] investments in Kazakhstan."[446] The letters stated:

> We are genuinely surprised and disappointed in [the decision to unilaterally terminate the contracts], but it is your choice. ***From our point of view, it represents total lawlessness which marked the completion of the process of expropriation not only of legal, contractual rights, but also owned assets of the enterprise***.
>
> ***At the same time, we inform you that [KPM/TNG] did not and is not going to transfer anything, including facilities and equipment requested by you, to "OC "KazMunaiGas"*** JSC. According to [the terms of Contract Nos. 302 and 210] "*All tangible and intangible assets acquired by the Contractor with a view to exploring and extracting hydrocarbons are the property of the Contractor*." [And:] "*In case of termination of the Contract, the Contractor is entitled to independently dispose of the property which is in his ownership.*"
>
> Accordingly, from 00 hrs. 00 min. of July 22, 2010 the State has been operating [Borankol and Tolkyn] field subsoil, using and operating other people's property without and against consent of the owner . . .

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445 Letter from MEMR to the Ministry of Industry and Trade, dated September 28, 2009, C-294.

446 *See* Letter Ref. No. 854 from KPM to MOG, dated July 24, 2010, C-193; Letter Ref. No. 1378 from TNG to MOG, dated July 24, 2010, C-194.

> ***[W]e ask to order immediate removal of MOG and KMG staff from [KPM and TNG offices] located in Aktau City…***[447]

235. On the same day, Mr. Anatolie Stati and the General Managers of KPM and TNG formally informed all of their personnel of the Government's actions and that ownership of the production in Tolkyn and Borankol fields had been transferred to the Government of Kazakhstan.[448] Since both KPM and TNG had been prohibited from transferring any assets, including finances, they would be unable to pay any further salaries to employees. Thus, the managers apologized to the employees and informed them that the responsibility for ensuring payment of their wages had passed to the State along with the transfer of the companies' other assets.

236. The Ministry of Oil and Gas had made clear that ownership of KPM's and TNG's property with respect to the complete technological process for oil and gas production had passed to the Republic of Kazakhstan. Yet neither KPM nor TNG had agreed to the transfer of any property, and they had not been given any formal documentation of transfer of title, if any existed. As a result, on August 26, 2010, KPM and TNG wrote to the Ministry to inquire about the status of their assets after the cancellation of the three contracts.[449] As property owners, KPM and TNG should have at least been notified of the transmission of its property to another entity in order to monitor what they own. Yet the State refused to provide even this courtesy. KPM and TNG received no response to their requests.

237. Claimants later learned that KazMunaiGas's subsidiary, KazMunaiTeniz, created a branch in Aktau and transferred administration of KPM's and TNG's operations to that branch to carry out the hydrocarbons production.[450] Despite the Ministry's assessment of its takeover of Claimants investment as a "temporary administration" of the business, KazMunaiGas's transfer to its subsidiary

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447 *See* Letter Ref. No. 854 from KPM to MOG, dated July 24, 2010, C-193; Letter Ref. No. 1378 from TNG to MOG, dated July 24, 2010, C-194.

448 *See* Letter No. 853 from KPM to Personnel of KPM, dated July 24, 2010, C-195; Letter No. 1371 from TNG to TNG Personnel, dated July 24, 2010, C-196.

449 *See* Letter No. 891 from KPM to MOG, dated August 26, 2010, C-197; Letter No. 1420 from TNG to MOG, dated August 26, 2010, C-198.

450 Condorachi Statement ¶ 49.

KazMunaiTeniz is clear evidence that the State is enjoying full ownership, maintenance, use, and disposal of Claimants' investments in Claimants' place.[451]

238. Thus, in less than two short years, the Government became aware of successful and valuable assets belonging to Claimants, decided it wanted to own the assets instead, launched an unfair, egregious, and ultimately successful campaign to expropriate those assets, and now intends to profit from their sale.[452] Those actions constitute serious violations of the Energy Charter Treaty and international law, for which Kazakhstan is responsible.

VI. GOVERNING LAW

239. In consenting to resolve this dispute under the ECT, the parties have designated the ECT as the agreed choice of "law or rules of law" between the parties for purposes of the first paragraph of Article 22 of the SCC Rules. Article 22(1) of the SCC Arbitration Rules provides:

> The Arbitral Tribunal shall decide the merits of the dispute on the basis of the law(s) or rules of law agreed upon by the parties. In the absence of such agreement, the Arbitral Tribunal shall apply the law or rules of law which it considers to be most appropriate.

240. In the present case, the ECT is the *lex specialis* agreed by the parties. Article 26(6) of the ECT contains an express choice of law provision:

> A Tribunal established under paragraph (4) shall decide the issues in dispute in accordance with this Treaty and applicable rules and principles of international law.

241. Consequently, the ECT, as supplemented and interpreted by applicable rules and principles of international law, is the governing law to be applied by the Tribunal in this proceeding. Such an approach is also required by fundamental rules of international law, such as those contained in the Vienna Convention on the Law of Treaties (the "Vienna Convention"), which provides that

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451 Condorachi Statement ¶¶ 50-52.

452 Stati Statement ¶ 44 ("For ten years, I heavily invested in Kazakhstan and successfully developed TNG and KPM. In eighteen months, and despite best efforts of me and my team, Kazakhstan devalued and ultimately destroyed my investments in the country.").

treaties are "governed by international law" and must be interpreted in light of "any relevant rules of international law applicable."[453]

242. In sum, the ECT is the parties' agreed choice of law under Article 22(1) of the SCC Rules, and it is to be supplemented, interpreted, and applied in accordance with applicable rules and principles of international law.[454] Kazakh law is irrelevant to this dispute as a matter of law and may not influence the Tribunal's determination of whether Kazakhstan violated the ECT and international law. At most, Kazakh law may be relevant as a matter of fact, to be considered by the Tribunal along with other facts of this case.[455]

VII. KAZAKHSTAN VIOLATED ITS OBLIGATIONS UNDER THE ECT AND INTERNATIONAL LAW

A. Kazakhstan Unlawfully Expropriated Claimants' Investments

243. The expropriation provision of the ECT is Article 13, which provides:

> (1) Investments of Investors of a Contracting Party in the Area of any other Contracting Party shall not be nationalized, expropriated or subjected to a measure or measures having effect equivalent to nationalization of expropriation (hereinafter referred to as "Expropriation") except where such Expropriation is:
>
> a) for a purpose which is in the public interest;
>
> (b) not discriminatory;
>
> (c) carried out under due process of law; and
>
> (d) accompanied by the payment of prompt, adequate and effective compensation. . . .

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[453] The Vienna Convention on the Law of Treaties provides that treaties are "governed by international law" and must be interpreted in the light of "any relevant rules of international law applicable." Vienna Convention, Arts. 2(1)(a), 31(3)(c), C-203. Kazakhstan and Moldova are party to the Vienna Convention, which is also assumed to apply to Gibraltar. *See* http://untreaty.un.org/ilc/texts/1_1.htm and http://www.fco.gov.uk/en/publications-and-documents/treaties/uk-overseas-territories/browse-by-overseas-territory/gibraltar.

[454] *See*, for cases under the ECT, *Petrobart* Award, at 23, C-204; *Ioannis Kardassopoulos and Ron Fuchs v. The Republic of Georgia*, ICSID Case No. ARB/05/18, Award, March 3, 2010 ("*Kardassopoulos* Award"), ¶ 216, C-205. *See also*, for non-ECT investment treaty cases, *ADC Affiliate Limited and ADC & ADMC Management Limited v. Republic of Hungary,* ICSID Case No. ARB/03/16, Award, October 2, 2006 ("*ADC* Award"), ¶¶ 290, 292, C-206; *Alpha Projektholding GmbH v. Ukraine*, ICSID Case No. ARB/07/16, Award, November 8, 2010 ("*Alpha* Award"), ¶¶ 233, C-207.

[455] *Petrobart* Award, at 23, C-204. *See also Kardassopoulos* Award, ¶ 216, C-205.

> (3) For the avoidance of doubt, Expropriation shall include situations where a Contracting Party expropriates the assets of a company or enterprise in its Area in which an Investor of any other Contracting Party has an Investment including through the ownership of shares.[456]

244. Article 13 thus prohibits two types of expropriatory measures to the extent such measures are not carried out in accordance with its requirements: (1) "direct" expropriation of an investment of an investor of another Contracting Party; and (2) "indirect" expropriation or a "measure or measures having effect equivalent to nationalization or expropriation."[457]

245. The ICSID Tribunal in *Compañía del Desarrollo de Santa Elena, S.A. v. Costa Rica* summarized the state of international expropriation law in this way:

> There is ample authority for the proposition that a property has been expropriated when the effect of the measures taken by the state has been to deprive the owner of title, possession or access to the benefit and economic use of his property. 'A deprivation or taking of property may occur under international law through interference by a state in the use of that property or with the enjoyment of its benefits, even where legal title to the property is not affected.'[458]

246. Further, as expressly stated in Article 13(3) of the ECT, expropriation includes the expropriation by the host state of the assets of a company or enterprise in which an investor has an investment, including through the ownership of shares. That is precisely the situation in the present case: Claimants held investments and assets in Kazakhstan through KPM and TNG. Their investments likewise included their direct and indirect shareholding in those two companies.

247. Kazakhstan directly expropriated Claimants' investments in July 2010. That direct expropriation was the culmination of a process of indirect expropriation which started in the fall of 2008. Those two distinct breaches of Article 13 of the ECT are discussed in the following sections.

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[456] Article 13(3) of the ECT, C-1.

[457] C. Schreuer, *The Concept of Expropriation under the ECT and Other Investment Protection Treaties*, *in* INVESTMENT ARBITRATION AND THE ENERGY CHARTER TREATY (2006), C-212.

[458] *Compañía del Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica*, ICSID Case No. ARB/96/1, Final Award, February 17, 2000 ("*Santa Elena* Award"), ¶ 77, C-213.

1. Kazakhstan Directly Expropriated Claimants' Investments in July 2010

248. On July 21, 2010, Kazakhstan abrogated KPM's and TNG's Subsoil Use Contracts. On July 22, 2010, Kazakhstan physically seized Claimants' offices, equipment, hydrocarbon production, revenues, and remaining assets and investments. Through those two series of acts, Claimants definitively and permanently lost all rights to and economic benefit from their investments, and Kazakhstan gained full legal control, physical possession, and use of Claimants' investments.

a. The Legal Standard of Direct Expropriation

249. The July 2010 seizures by Kazakhstan are classic examples of "direct" expropriation. "Direct" expropriation refers to an overt seizure of a foreign investor's property, or the title to such property, by the host state.

250. The definition of "direct" expropriation dates back to the early 1960s, when a number of international law scholars began to draw a conceptual distinction between "direct" and "indirect" expropriation. The 1961 Harvard Draft Convention on the International Responsibility of States for Injuries to Aliens described direct expropriation as "an outright taking of property."[459] In the Twelfth Annual Goff Lecture delivered in December 2004, Yves Fortier likewise defined direct expropriation as "the compulsory transfer of title to property to the State or a third party, or the outright seizure of property by the State."[460]

251. The ICSID case of *Santa Elena* concerned a direct expropriation by Costa Rica.[461] The claimant had purchased a large-scale property known as "Santa Elena" in Costa Rica for purposes of developing large portions of the property as a tourist resort and residential community. Eight years later, the Costa Rican Government expropriated the property for the ecological purpose of expanding an adjacent national park. The expropriation was accomplished by a formal decree that seized the property and transferred it to the National Parks Service of the Costa Rican Ministry of Agriculture. Those events were so clearly an instance of direct

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459 *See* Article 10(3)(a) of the Draft Convention on the International Responsibility of States for Injuries to Aliens, *in* Louis B. Sohn & Richard R. Baxter, RESPONSIBILITY OF STATES FOR INJURIES TO THE ECONOMIC INTERESTS OF ALIENS, 55 AJIL 545, 553 (1961), C-214.

460 L.Y. Fortier, *Indirect Expropriation in the Law of International Investment: I Know It When I See It, or Caveat Investor*, ICSID REV. – F.I.L.J. 293, 297 (Fall 2004), C-215.

461 *Santa Elena* Award, C-213.

expropriation that, in the subsequent ICSID arbitration, Costa Rica did not contest that it had expropriated the Santa Elena property or that it owed compensation to the claimant. Instead, the issue in dispute was the amount of compensation that was due.[462] Confirming that formal transfer of title is not a prerequisite for a formal or direct expropriation, the Tribunal in *Santa Elena v. Costa Rica* found that the "expropriation" occurred on the date of the expropriation decree of May 5, 1978, even though this decree still had to be implemented and did not, in itself, formally transfer title.[463]

252. Tribunals in a number of recent cases have held that the host state directly expropriated an investment, including investments that consisted of intangible property. In the case of *Kardassopoulos and Fuchs v. Georgia*, brought under a BIT and the ECT, the claimant, Ioannis Kardassopoulos, successfully argued that Georgia had unlawfully expropriated his investment. Georgia had issued a decree that extinguished the rights of a local company, GTI, in a pipeline and had issued an order extinguishing GTI's rights over future pipelines.[464] Mr. Kardassopoulos held an interest in GTI. The Tribunal found that "the circumstances of Mr. Kardassopoulos' claim present a classic case of direct expropriation, Decree No. 178 having deprived GTI of its rights in the early oil pipeline and Mr. Kardassopoulos' interest therein."[465]

b. Kazakhstan Directly Expropriated Claimants' Investments in July 2010

253. Applying these legal rules, it is beyond dispute that Kazakhstan directly expropriated Claimants' investments on July 21-22, 2010, by seizing Claimants' rights under the KPM and TNG Subsoil Use Contracts and by seizing legal and physical control of the assets held by Claimants through KPM and TNG.

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462 *Id*. ¶ 34.

463 *Santa Elena* Award, ¶¶ 76-81, C-213. *See also*, Wena *Hotels, Ltd. v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4, Award, December 8, 2000 ¶ 99 ("*Wena* Award"), C-216.

464 *Kardassopoulos* Award ¶ 351, C-205.

465 *Kardassopoulos* Award ¶ 387, C-205. *See also*, Waguih Siag and Clorinda Vecchi v. Arab Republic of Egypt, ICSID No. ARB/05/15, Award, June 1, 2009 ("*Siag* Award"), C-217; *See also*, *Bernardus Henricus Funnekotter and others v. Republic of Zimbabwe*, ICSID Case No. ARB/05/6, Award, April 22, 2009 ("*Bernardus et al.* Award"), C-218.

254. On July 21, 2010, Kazakhstan directly expropriated Claimants' KPM and TNG Subsoil Use Contracts by unilaterally abrogating the contracts and transferring the rights under the contracts to State-owned KazMunaiGas. In the words of Yves Fortier, that act was a "compulsory transfer of title to property to the State."[466] The Government explicitly stated that the subsoil area subject to the Subsoil Use Contracts "was transferred in trust of [the National Company] OC 'KazMunaiGas' JSC."[467] The Government likewise explicitly stated that "facilities and equipment that ensure the continuity of technological process and industrial safety are to be transferred by the former subsoil user to the national company [KazMunaiGas] for temporary use and possession until the transfer of the property to a new subsoil user … [and until then] the competent Body shall acts as his agent of such property."[468]

255. Further, the Ministry confirmed that its unilateral contract repudiation resulted in the immediate expropriation of Claimants' contractual rights to ownership over produced oil, gas, and condensate. It stated that "from the moment of termination the company has no longer rights over the products, that are being extracted, over the hydrocarbons."[469]

256. Those seizures of legal title were personally instructed and overseen by the Kazakh Prime Minister, along with the Minister of Oil and Gas and the regional Governor, during their visit to Claimants' LPG plant to announce the seizures. The following day, Kazakhstan seized physical control of Claimants' investments. On July 22, 2010, Kazakhstan seized Claimants' offices, equipment, production, revenue, and other investments and operations, when a group of thirteen high-ranking officials from the MOG and KazMunaiGas arrived at Claimants' offices in Aktau, Kazakhstan. KazMunaiGas explained that government escrow accounts were being opened the same day, and "everything that has been extracted since [July] 22nd, extracted oil and payment for oil, gas and condensate - such income

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466 L.Y. Fortier, *Indirect Expropriation in the Law of International Investment: I Know It When I See It, or Caveat Investor*, ICSID REV. – F.I.L.J. 293, 297 (Fall 2004), C-215.

467 *See* Notification No. 20-05-5150 from the Kazakh Ministry of Oil and Gas to KPM terminating the Borankol Subsoil Use Contract dated July 21, 2010, C-3; Notification No. 20-05-5151 from MOG to TNG terminating the Tolkyn Subsoil Use Contract dated July 21, 2010, C-4.

468 *Id.*

469 *See* Stenograph of the telephone conversation of July 22, 2010, C-190.

shall be deposited in the special account."[470] The MOG's and KazMunaiGas' occupation of Claimants' offices and transfer of personnel and assets totally deprived Claimants of physical possession and control of their revenues, assets, and means of production.

257. Such outright seizure of physical assets, contractual rights and legal title are textbook examples of "direct" expropriation. It is indisputable that Kazakhstan directly expropriated Claimants' investments under Article 13 of the ECT and international law in July 2010.

2. Kazakhstan Indirectly Expropriated Claimants' Investments Starting in October 2008

a. The Legal Standard of Indirect Expropriation

258. While Kazakhstan's expropriation of Claimants' investments in July 2010 was overt and indisputable, that act of "direct" expropriation was, in reality, merely the culmination of a campaign of "indirect" expropriation that commenced in October 2008. Between October 2008 and July 2010, Kazakhstan subjected Claimants and their investments to a variety of egregious forms of harassment that clearly amount to "indirect" expropriation under the ECT and international law. If Kazakhstan's seizures of July 2010 were textbook examples of "direct" expropriation, its severe acts of interference with Claimants' investments over the October 2008-July 2010 period were equally classic examples of "indirect" expropriation. The Tribunal should have no difficulty concluding that Kazakhstan's violation of Article 13 of the ECT and international law commenced in October 2008.

259. "Indirect expropriation" is widely understood as interference with an investment that "leaves the investor's title untouched but deprives him of the possibility to utilize the investment in a meaningful way."[471] It has long been accepted in international law that an expropriation may occur in the absence of a formal decree or the outright seizure of property. One of the earliest scholars to articulate the concept of indirect expropriation was Professor G. C. Christie, who in

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[470] *Id.*

[471] R. Dolzer & C. Schreuer, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW (Oxford 2008), at 92 ("Dolzer & Schreuer"), C-219. *See also*, UNCTAD, *Taking Property* (2000), C-231

analyzing the decisions in the *German Interest in* Polish *Upper Silesia*[472] and *Norwegian Shipowners*' cases,[473] concluded that those decisions:

> show that a State may expropriate property, where it interferes with it, even though the State expressly disclaims any such intention. More important, … even though a State may not purport to interfere with rights to property, it may, by its actions, render those rights so useless that it will be deemed to have expropriated them.[474]

260. The Iran-US Claims Tribunal has consistently recognized the concept of indirect expropriation:

> [T]he Tribunal has consistently ruled that interference by the Government with the alien's enjoyment of the incidents of ownership – such as the use or control of the property, or the income and economic benefits derived therefrom – constitutes a compensable taking.[475]

261. Investment treaty tribunals have repeatedly recognized the concept of indirect expropriation. In *Metalclad Corp. v. The United Mexican States*, which involved the denial of a construction permit and the classification of land as a national area for the protection of rare cactus, a NAFTA Tribunal ruled that "expropriation under NAFTA includes … covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in

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[472] *Case Concerning Certain German Interests in Polish Upper Silesia*, Judgment, August 25, 1925, 1926 P.C.I.J. (ser. A) No. 7, C-220.

[473] *Norwegian Shipowners' Claims (Norway v. USA)*, Award of October 13, 1922, Int'l. Arb. Awards 309 (1922), C-221

[474] G.C. Christie, *What Constitutes a Taking of Property under International Law?*, 38 BRIT. Y.B. INT'L L. 305, 311 (1962), C-222.

[475] Charles N. Brower, *Current Developments in the Law of Expropriation and Compensation: A Preliminary Survey of Awards of the Iran-United States Claims Tribunal*, 21 INT'L L. 639, 643 (1987), C-223. *Starrett Housing Corp. v. Iran*, Final Award, 16 Iran-US CTR 112, C-224 (appointment of a "temporary" manager by Iran) ("… it is recognized in international law that measures taken by a State can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the State does not purport to have expropriated them and the legal title to the property formally remains with the original owner"); *Tippetts, Abbett, Mc Stratton v. TAMS-AFFA*, Award No. 141-7-2 (June 22, 1984), C-225 ("A deprivation or taking of property may occur under international law through interference by a state in the use of that property or with the enjoyment of its benefits, even where legal title to the property is not affected. While assumption of control over property by a government does not automatically and immediately justify a conclusion that the property has been taken by the government, thus requiring compensation under international law, such a conclusion is warranted whenever events demonstrate that the owner was deprived of fundamental rights of ownership and it appears that this deprivation is not merely ephemeral.")

significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State."[476]

262. In the case of *CME v. The Czech Republic*, which involved interference with an investor's contractual rights by a regulatory authority, the tribunal held:

> The Respondent's view that the Media Council's actions did not deprive the Claimants of its worth, as there has been no physical taking of the property by the State or because the original License … always has been held by the original Licensee and kept untouched, is irrelevant. What was touched and indeed destroyed was the Claimant's and its predecessor's investment as protected by the Treaty. What was destroyed was the commercial value of the investment … by reason of coercion exerted by the Media Council.[477] …
>
> The expropriation claim is sustained despite the fact that the Media Council did not expropriate CME by express measures of expropriation. *De facto* expropriations or indirect expropriations, *i.e.* measures that do not involve an overt taking but that effectively neutralized the benefit of the property of the foreign owner, are subject to expropriation claims. This is undisputed under international law.
>
> Furthermore, it makes no difference whether the deprivation was caused by actions or inactions.[478]

263. More recently, in *Alpha v. Ukraine*, the tribunal found that Ukraine had indirectly expropriated the claimant's investment, which consisted of contractual rights. The case involved a series of agreements entered into for the reconstruction,

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[476] *Metalclad Corp. v. The United Mexican States* (ICSID Case No. ARB(AF)/97/1), Award, August 30, 2000, ¶ 103 ("*Metalclad* Award"), C-226. The *Metalclad* Award was partially set aside by the British Columbia Supreme Court on unrelated grounds. *See also*, *Goetz and Others v. Republic of Burundi*, Award, February 10, 1999 ("*Goetz* Award"), ¶ 124, C-227 ("Since… the revocation of the free zone certificate forced them to stop all activity …, which deprived their investments of all utility and deprived the claimant investors of the benefit which they could have expected from their investments, the contentious measure could be regarded as a 'measure having a similar effect' to a measure depriving of or restricting ownership in the sense of Article 4 of the Investment Treaty."); *Middle East Cement Shipping and Handling Co. S. A. v. Arab Republic of Egypt*, Award, April 12, 2002 ("*Middle East Cement* Award"), ¶ 107, C-228. *See also*, *Técnicas Medioambientales Tecmed S.A. v. The United Mexican States*, ICSID Case No. ARB AF/00/2, Award, May 29, 2003 ¶ 149, C-209.

[477] *CME Czech Rep. B.V. (Netherlands) v. The Czech Republic*, UNCITRAL, Partial Award, September 13, 2001 ("*CME* Partial Award") ¶ 591, C-229.

[478] *CME* Partial Award ¶¶ 604-605, C-229.

renovation and operation of a state-owned hotel in Kiev, Ukraine. Alpha did not receive the payments to which it was entitled under joint activity agreements ("JAAs") entered into with the hotel. The tribunal found that Ukrainian authorities instructed the hotel to discontinue payments to Alpha and were responsible for the failure of the hotel to meet its contractual obligations under the JAAs.[479] The tribunal explained:

> It is well-established that a government action need not amount to an outright seizure or transfer of title in order to amount to an expropriation under international law. … Thus, even if the 1998 and 1999 JAA remain nominally in force, Claimant's investment may still have been expropriated if the contracts have been "rendered useless" by the actions of the Ukraine government. However, in order to establish an indirect expropriation of this sort, it is necessary to demonstrate that the investment has been deprived of a significant part of its value. …
>
> Given that Claimant's investment has been substantially deprived of value, that such deprivation is effectively permanent, and that the deprivation was the result of government action, the Tribunal finds that Claimant's rights under the JAAs have been expropriated in violation of Article 4(1) of the UABIT.[480]

264. An oft-cited example of indirect expropriation under international law is the case of *Biloune v. Ghana*.[481] In that UNCITRAL arbitration, a Syrian investor had invested in the development of a resort complex in Ghana through a local subsidiary (MDCL). After remodeling and construction work had been substantially completed, the Ghanaian authorities issued a stop work order based on the lack of a building permit, and demolished a portion of the project. Mr. Biloune was subjected to financial scrutiny and required to submit an assets declaration form. He was eventually arrested, detained for 13 days without charge, and then deported from Ghana without possibility of re-entry.

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479 *Alpha* Award ¶ 397, C-207.

480 *Alpha* Award, ¶¶ 408, 410, C-207.

481 *Biloune and Marine Drive Complex Ltd v. Ghana Investments Centre and the Government of Ghana*, Award on Jurisdiction and Liability, October 27, 1989, 95 I.L.R. 183 (June 30, 1990) ("*Biloune* Award"), C-235.

265. In the arbitration, Mr. Biloune argued that these events, including his arrest and deportation, constituted an indirect expropriation of his investments. The Tribunal, applying customary international law, agreed:

> [T]he conjunction of the stop work order, the demolition, the summons, the arrest, the detention, the requirement of filing assets declaration forms, and the deportation of Mr. Biloune without possibility of re-entry had the effect of causing the irreparable cessation of work on the project. Given the central role of Mr. Biloune in promoting, financing and managing MDCL, his expulsion from the country effectively prevented MDCL from further pursuing the project. In the view of the Tribunal, such prevention of MDCL from pursuing its approved project would constitute constructive expropriation of MDCL's contractual rights in the project and, accordingly, the expropriation of the value of Mr. Biloune's interest in MDCL.[482]

266. The recent award in *RosInvest v. Russia* related to the expropriation by the Russian Federation of the assets of Yukos, in which the claimant had a shareholding. The Russian Tax Ministry undertook tax audits of Yukos, which resulted in tax assessments on Yukos and the auction of Yukos' assets. The Tribunal concluded that Russia's application of its tax law, the tax assessments of Yukos and the auction of Yukos' assets were not *bona fide* and resulted in an unlawful expropriation of RosInvest's investment. The Tribunal first set out its approach in the following terms: "an assessment of whether Respondent breached the IPPA can only be effectively made if and after the conduct as a whole is reviewed, rather than isolated aspects ... the Tribunal will … turn to its own considerations as to whether Respondent's measures, seen together and in their cumulative effect, can be considered as a breach of the IPPA."[483]

267. The *RosInvest* Tribunal went on to find that:

> It is undisputed that Respondent's measures resulted in the deprivation of Yukos' assets. It is also undisputed, as Respondent correctly argues, that States have a wide latitude in imposing and enforcing taxation laws even if resulting in substantial deprivation. The only question is

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[482] *Id.* ¶ 209. Another case of indirect expropriation is that of *Rumeli Telekom A.S. and Telsim Mobil Telekomikasyon Hizmetleri A.S. v. Kazakhstan*, ICSID Case No. ARB/05/16, Award, July 29, 2008 ("*Rumeli* Award") ¶ 708, C-236.

[483] *RosInvestCo UK Ltd. v. The Russian Federation*, SCC Case No. Arb. V079/2005, Final Award, September 12, 2010 ("*RosInvest* Award") ¶ 410, C-151.

> whether Respondent's measures can be justified as falling within this latitude of discretion. In this regard, the Tribunal refers to its considerations above with respect to the application of Russian tax law, the tax assessment, and the auctions which resulted in the conclusion that Respondent's actions towards Yukos cannot be justified by its authority to apply and enforce its tax laws.[484] …
>
> These facts suggest that measures taken [by Russia] were linked to the strategic objective of returning petroleum assets to the control of the Russian State and to an effort to suppress a political opponent. …
>
> In conclusion, therefore, the Tribunal considers that the totality of Respondents' measures were structured in such a way to remove Yukos' assets from the control of the company and the individuals associated with Yukos. They must be seen as elements in the cumulative treatment of Yukos for what seems to have been the intended purpose.

268. With respect to tax measures in particular the *Yukos* Tribunal further explained:

> [I]t is generally accepted that the mere fact that measures by a host state are taken in the form of application and enforcement of its tax law, does not prevent a tribunal from examining whether this conduct of the host state must be considered, under the applicable BIT or other international treaties on investment protection, as an abuse of tax law to in fact enact an expropriation. …
>
> [T]hese measures in their totality, including but going beyond the application of tax law, can only be understood to have had the aim to deprive Yukos from its assets. Such a taking would only be admissible under Article 5 if the conditions of that provisions are fulfilled [which the Tribunal found they were not]. …
>
> Therefore, the Tribunal concludes that Respondents' measures seen in their cumulative effect towards Yukos, were an unlawful expropriation under Article 5 IPPA.[485]

269. In sum, international tribunals have found that a variety of measures, including measures purportedly related to enforcement of tax obligations, may constitute an indirect expropriation. Such measures may include interference with

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[484] *Id.* ¶ 574.

[485] *Id.* ¶¶ 625, 627-8, 630, and 633.

contractual rights, wrongful exercises of judicial or administrative authority, enforcement of tax laws in a manner that is not *bona fide*, harassment of key personnel and other interference with the management or operations of a company, and the revocation or denial of a license or a permit. In each case the inquiry is whether the measure(s) in question, standing alone or taken as a whole, have the effect of depriving the owner, in whole or in significant part, of the use or control of his investment or the income and economic benefits associated with the investment.

b. Kazakhstan Indirectly Expropriated Claimants' Investments

270. In the present case, Kazakhstan's measures from October 2008 to July 2010 thoroughly interfered with Claimants' use and control of their investments and caused significant damage to the alienability and economic potential of those investments. From October 2008 onward, Kazakhstan deliberately interfered with, harassed, and damaged Claimants' investments through a variety of measures that impeded Claimants' ability to use, control, enjoy, or dispose of their investments.

271. Kazakhstan's campaign of indirect expropriation commenced on October 14, 2008, when President Nazarbayev personally ordered the Kazakh Financial Police and a variety of other Governmental agencies to "fully investigate" Claimants' business activities in Kazakhstan. The Financial Police and seven other ministries and agencies started their harassment campaign in earnest on the heels of President Nazarbayev's directive. Kazakhstan's harassment campaign – which included a groundless criminal prosecution and conviction of KPM's in-country manager (and a similarly groundless criminal verdict against KPM), freezing KPM's assets, multiple assessments of improper taxes, reversal of prior State approvals and waiver of the State's pre-emptive rights, and refusal to execute the agreed exploration period extension – entail "indirect" expropriation under Article 13 of the ECT and international law.

272. Kazakhstan's campaign of interference began with measures to frustrate any possibility of Claimants being able to fully operate, control, enjoy, or sell KPM and TNG. This was accomplished by raising contract and other legal disputes that clouded the title of the businesses, questioned their legality, and significantly diminished their value. Those measures were followed by a trumped-up

criminal prosecution of KPM's in-country manager and threats to other managers of KPM and TNG.

273. In September 2008, Claimants had begun to accept bids for the sale of KPM and TNG. However, the initial bid process did not include the Contract 302 Properties, which Claimants had good reason to believe contained significant reserves. Claimants attempted to continue exploration in the Contract 302 Properties to determine its proper value for sale, but the Government took steps to ensure they would be unable to do so. As one of many measures taken against Claimants' investments, the State refused to extend TNG's exploration period in the Contract 302 Properties, despite prior Governmental approval and TNG's clear intentions to exercise its rights to conduct exploration. The MEMR refused to send TNG a signed addendum extending TNG's exploration rights, which denied TNG's contractual right to continue exploration. The wrongful refusal to execute the addendum prevented Claimants from proving the Contract 302 Properties' reserves and thereby affected the market value of that asset. Further, the State subsequently claimed Contract No. 302 terminated on its own accord upon the State's refusal to execute the required extension of TNG's exploration rights, which was not in accordance with contractual termination provisions.

274. Another early measure of interference began in November 2008, when the Tax Committee initiated an audit of KPM and TNG and assessed approximately USD 6 million in back "transfer" price taxes and penalties. KPM and TNG spent the following months contesting this assessment in Kazakhstan's courts, legal actions that remained pending at the time Kazakhstan abrogated KPM's and TNG's Subsoil Use Contracts and directly expropriated Claimants' investments in July 2010.

275. Even more harmful, the February 10, 2009, refusal by Kazakhstan to apply amortization rates as contractually agreed in the KPM and TNG Subsoil Use Contracts raised additional concerns about the companies' financial health. The State wrongfully assessed against the companies approximately USD 69 million in back taxes on corporate income and associated penalties. In early 2010, the State pursued bankruptcy proceedings against KPM, further disrupting KPM's ability to operate and driving down the value of Claimants' investments.

276. On December 18, 2008, the State reversed its earlier position and cancelled its prior approval of the 2003 transfer of TNG to Terra Raf, as well as its prior waiver of pre-emptive rights to purchase 100% of KPM and TNG, all amidst threats of termination of the Subsoil Use Contracts. Despite the Government's verbal assurances, it never granted the permit to "re-allow" the transfer of TNG's ownership to Terra Raf. From December 2008 onward, the lingering transfer and pre-emptive rights issues consumed an extraordinary amount of time, attention, and resources, and severely affected the marketability of TNG and KPM.

277. Furthermore, on September 30, 2009, the State revived a dispute with KPM regarding payment of the explicitly inapplicable Crude Oil Export Tax for KPM's January 2009 exports, resulting in a purported financial penalty of over USD 10 million.

278. The above measures, which resulted from the personal instruction of Kazakhstan's President, involved a variety of trumped-up contract, tax, and legal violations resulting from the never-ending series of "audits" and "inspections." They not only discouraged any potential third-party buyer from paying a fair market value for KPM, TNG, or the companies' discrete assets; they also required an inordinate amount of time and expense to challenge before Kazakhstan's various administrative and judicial bodies. In effect, from October 2008 onward, KPM and TNG only existed to respond to and attempt to challenge the extraordinary measures of harassment inflicted on the companies by Kazakhstan. Those challenges were ultimately futile.

279. However, as egregious and unlawful as those measures were, they paled in comparison to the criminal campaign Kazakhstan waged against KPM, TNG, and their personnel based on Kazakhstan's arbitrary reclassification of in-field pipelines of KPM and TNG gathering systems as "main" (or "trunk" pipelines), and on the alleged failure of KPM and TNG to hold "main" pipeline licenses to operate the arbitrarily reclassified gathering lines. As evidenced by numerous expert reports and confirmed by common sense, neither KPM nor TNG ever operated "main" pipelines. The Government's reclassification of the companies' in-field lines as "main" pipelines was a crude fabrication designed to justify a baseless criminal campaign of harassment and interference.

280. Kazakhstan's groundless reclassification formed the basis for its criminal prosecution of KPM's in-country manager, Mr. Cornegruta, and his arrest, sham trial, and incarceration. It was likewise the basis for Kazakhstan's "conviction" of KPM – in the context of Mr. Cornegruta's criminal trial, to which KPM was not a party – as well as similar threats of criminal prosecution levied against TNG and other in-country executives of KPM and TNG.

281. In conjunction with the criminal case, on April 30 and May 15, 2009, the Financial Police issued seizure orders against (i) KPM's Subsoil Use Contract, oilfield pipelines, and vehicles; (ii) TNG's Subsoil Use Contracts, and oilfield gas and condensate pipelines; and (iii) Claimants' participatory interests in KPM and TNG. Those preliminary seizures were designed to prevent KPM and TNG from selling or transferring their assets during the course of the criminal proceedings, thereby preventing Claimants from disposing of their investments in Kazakhstan. Needless to say, those seizures and the criminal case massively interfered with Claimants' ability to enjoy or dispose of their investments, and they further diminished their market value.

282. On September 18, 2009, the Aktau City Court sentenced Mr. Cornegruta to four years in prison on the pretense that he illegally engaged in entrepreneurial activities by operating the alleged KPM "main" pipelines without a license. The Aktau Court also rendered a verdict against KPM, which was not a party to the criminal proceeding, ordering KPM to pay the Government a fine of approximately USD 145 million, a clearly unreasonable sum. As described above, the prosecution and conviction of Mr. Cornegruta and KPM, the enforcement measures against KPM, and the subsequent jailing of Mr. Cornegruta were flawed both substantively and procedurally and amounted to egregious violations of due process.

283. In a manner similar to the acts of Ghana in *Biloune*, but considerably more severe, Kazakhstan's criminal prosecution and prolonged detention of Mr. Cornegruta seriously impaired the value of Claimants' investments. The financial scrutiny, multiple criminal investigations, and ultimate jailing of Mr. Cornegruta, a key member of Claimants' management team, caused irreparable harm to KPM and TNG. That severe interference with Claimants' right to manage their investments also resulted in untold hours and resources spent preparing Mr. Cornegruta's

defense, as well as his and KPM's appeals. Mr. Cornegruta's wrongful arrest, conviction, and incarceration, combined with identical threats made by the State against TNG and both companies' other managers, meant that no key manager of KPM and TNG could safely remain in Kazakhstan to oversee and direct the companies' operations. They were forced to flee. Claimants were thus forced to manage KPM and TNG remotely, even as the State's other measures of harassment required continual responses and attention. The situation was precarious at best.

284. Kazakhstan went on to engage in concerted and continuing efforts to enforce its fabricated USD 145 million fine against KPM, resulting in the inalienability of Claimants' assets and bringing to bear myriad execution measures (as described above). The seizure of Claimants' operations interfered with rights under the Subsoil Use Contracts, measures that the *CME* and *Alpha* Tribunals deemed to be expropriatory. Those execution measures also led to the flight of more key personnel and further paralyzed Claimants' operations in Kazakhstan.

285. Kazakhstan's measures of indirect expropriation were extraordinary in severity, number, and variety. This is not a case of "creeping" expropriation, in which a series of fairly minor regulatory acts cumulatively amount to an "indirect" expropriation. Kazakhstan's measures were extreme, and any number of them individually constitute an act of "indirect" expropriation under international law. Considered cumulatively, the conclusion that Kazakhstan indirectly expropriated Claimants' investments commencing in October 2008 should be inescapable.

3. Kazakhstan's Expropriation of Claimants' Investments Was Unlawful

286. Article 13 of the ECT expressly prohibits any measure of expropriation (direct or indirect) by Kazakhstan that does not cumulatively satisfy four distinct requirements: the expropriation must be "(a) for a purpose which is in the public interest; (b) not discriminatory; (c) carried out under due process of law; and (d) accompanied by the payment of prompt, adequate and effective compensation."[486]

287. The terms of Article 13(1), in which the conjunctive "and" is used, require compliance with each of the four listed requirements in order for an

[486] Article 13(1) of the ECT, C-1.

expropriation to be deemed lawful and not entail a breach of the ECT.[487] In the ECT case of *Kardassopoulos and Fuchs v. Georgia*, the Tribunal concluded that Georgia's expropriation of Mr. Kardassopoulos' investment was unlawful "as it violated at least one of the prescribed conditions for lawful expropriation."[488]

288. Kazakhstan met none of the four requirements for a lawful expropriation in this case. Its acts of direct and indirect expropriation therefore violated Article 13 of the ECT and international law.

a. The Expropriation Was Not "For a Purpose Which Is In The Public Interest"

289. The requirement that an expropriation be in the "public interest" in order to be deemed lawful is fundamental. Without it, no investor would ever be secure, as governments could expropriate private investments at will. Governments do have a right to expropriate lawfully. But as *quid pro quo* for this right they are bound to limit expropriations to those of a genuine "public interest." The Tribunal in *LETCO v. Liberia* referred to the requirement as "a *bona fide* public purpose."[489]

290. As the renowned scholar Garcia Amador has explained, this requirement is "the least" that can be expected of an expropriating state, because a taking for the public good is the very *raison d'être* of expropriation:

> [T]he least that can be required of the State is that it should exercise [the] power [to expropriate] only when the measure is clearly justified by the public interest. Any other view would condone and even facilitate the abusive exercise of the power to expropriate and give legal sanction to manifestly arbitrary acts of expropriation [. . .] [A]ll states should comply with the condition or requirement which is common to all; namely, that the power to expropriate should be exercised only when expropriation is necessary and is justified by a genuinely public purpose or reason. If this *raison d'être* is plainly absent, the measure

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487 *See* UNCTAD, *Bilateral Investment Treaties in the Mid-1990s* (United Nations 1998) at 66, C-237; Dolzer & Schreuer at 89-91, C-219.

488 *Kardassopoulos* Award, ¶¶ 407-408, C-205. See also, *Bernardus et al.* Award ¶ 98 ("The Tribunal observes that the conditions enumerated in Article 6 are cumulative. In other terms, if any of those conditions is violated, there is a breach of Article 6."), C-218; *Siag* Award ¶ 428, C-217. *See also*, Dolzer & Schreuer at 91, C-219.

489 *LETCO v. Liberia*, ICSID Case No. ARB/83/2, Award, March 31, 1986, at 665, Section IV, C-239. *See also*, UNGA Resolution 1803 (XVII), UN GAOR, 17th Session, Agenda Item 39 ¶ 4, UN Doc. A/RES/1803(XVII) (1962), C-238.

> of expropriation is "arbitrary" and therefore involves the international responsibility of the State.[490]

291. In *ADC v. Hungary*, pursuant to legislative changes, the claimants' rights relating to the operation, use and exploitation of airport terminals in Hungary had ceased to exist. As the *ADC* Tribunal noted, it is not sufficient for a state to merely assert that a "public interest" was served by its conduct:

> . . . a treaty requirement for '*public interest*' requires some genuine interest of the public. If a mere reference to '*public interest*' can magically put such interest into existence and therefore satisfy this requirement, then this requirement would be rendered meaningless.[491]

292. In *ADC*, Hungary had vaguely referred to "activities of strategic importance" and "contractual non-performance."[492] Upon examination, however, the Tribunal concluded that "no satisfactory explanation has ever been given for the takeover and none of the reasons now sought to be relied upon are tenable."[493] The Tribunal found that the expropriation was not proven to be in the public interest, and therefore, was unlawful.[494]

293. Kazakhstan never seriously alleged that its expropriatory measures in this case were taken in the public interest, and in any event, that requirement was certainly not satisfied.[495] To begin with, the public interest was not served by

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[490] F.V. García Amador, Special Rapporteur's Report, Int'l Law Commission, *State Responsibility*, Y.B. INT'L L. COM. ¶ 59 (1959), C-240.

[491] *ADC* Award ¶ 432, C-206.

[492] *Id*. ¶¶ 273-81.

[493] *Id*. ¶ 285.

[494] *Id*. ¶¶ 429, 433, 445, 476. *See also*, *Siemens A.G. v. Argentina*, ICSID Case No. ARB/02/08, Award, February 6, 2007 ("*Siemens* Award"), ¶ 273, C-232 (" . . . there is no evidence of a public purpose in the measures prior to the issuance of Decree 669/01. It was an exercise of public authority to reduce the costs to Argentina of the Contract recently awarded through public competitive bidding, and as part of a change of policy by a new Administration eager to distance itself from its predecessor.").

[495] Various Kazakh officials at times made vague references to the need to ease social tensions. However, that cannot amount to justification for the expropriation on the basis of public interest, as the Government's measures of expropriation caused the tensions in question. The population of Aktau was directly affected by the threats to KPM's and TNG's operations and production, because many of them depended upon the companies for work, and nearly all of them depended upon a steady production of natural gas. That was a key reason why the Government expropriated Claimants' investments in a way that would not disturb production. It is not the case, however, that the expropriation needed to occur to avoid those social tensions. The Government's mistreatment of Claimants' investments led to whatever social tensions existed.

unjustified prosecutions and convictions that violated Kazakhstan's own laws and amounted to egregious violations of substantive and procedural due process. The criminal charge against Mr. Cornegruta, which led to his conviction as well as that of the non-party KPM, was based on the frivolous accusation that KPM's in-field gathering lines amounted to "main" pipelines. That accusation was groundless – indeed, comical to anyone involved in the industry – and defied common sense. It was contrary to Kazakhstan's legal and regulatory provisions governing what constituted "main pipelines," contrary to Kazakhstan's own approvals of KPM's in-field systems, and belied by the admissions of numerous Kazakh officials as well as the findings of multiple independent experts. It was also contrary to Kazakhstan's classification and treatment of every other oil and gas producer in the country, all of whom operate in-field gathering systems, and none of whom have ever been accused of operating "main" pipelines. Based as they were on a groundless, frivolous accusation, Kazakhstan's criminal prosecution of Mr. Cornegruta and criminal conviction of Mr. Cornegruta and KPM were not in the public interest.

294. Kazakhstan's other measures of harassment and interference likewise did not serve public interest. Rather, they were designed to diminish the marketability and restrict the alienability of Claimants' investments, until the State seized them outright. Kazakhstan refused to execute the agreed-upon extension of Contract No. 302 in order to prevent Claimants from further ascertaining the value of their investments. That was clearly not in the public interest. Similarly, the pre-emptive right dispute was fabricated by the Government in order to cloud Claimants' title to their property, thus preventing a sale of Claimants' investments. That also served no public interest. Kazakhstan's intrusive tax and customs audits and ensuing wrongful assessment of back corporate and transfer price taxes, as well as its imposition of illegal export duties, served no other purpose than to send a threatening message to prospective investors.

295. Kazakhstan's direct expropriation of Claimants' investments in July 2010, through its abrogation of the Subsoil Use Contracts and physical seizure of Claimants' assets also did not serve any public purpose. No such purpose was stated or provided. The State simply seized KPM and TNG and their rights, assets, and

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No public interest is served by a Government alleviating problems that the Government caused and that should not have existed in the first place.

revenues, and gifted the companies to KazMunaiGas. KazMunaiGas took over their operations, equipment, and personnel, and continued to operate them for the State's benefit.

296. Because Kazakhstan's measures of expropriation – both indirect and direct - were not for a purpose that was in the public interest, the Tribunal should conclude that Kazakhstan's expropriation of Claimants' investments was unlawful under Article 13 of the ECT and international law.

b. Kazakhstan's Measures Were Not "Carried Out Under Due Process of Law"

297. Kazakhstan's indirect and direct measures of expropriation also violated the most elementary notions of due process. In particular, Kazakhstan's malicious criminal prosecution of Mr. Cornegruta, which led to his conviction as well as that of the non-party KPM, involved egregious violations of due process. Kazakhstan's other unjustified acts of harassment and interference with the operations of KPM and TNG during the October 2008 through July 2010 period, as well as its direct expropriation of July 2010, also violated basic notions of due process and fair play.

298. "Due process" encompasses both procedural and substantive fairness. In *ADC v. Hungary*, the Tribunal described the "due process of law" requirement as follows:

> The Tribunal agrees with the Claimants that "*due process of law*," in the expropriation context, demands an actual and substantive legal procedure for a foreign investor to raise its claims against the depriving actions already undertaken or about to be taken against it. Some basic legal mechanisms, such as reasonable advance notice, a fair hearing and an unbiased and impartial adjudicator to assess the actions in dispute, are expected to be readily available and accessible to the investor to make such legal procedure meaningful. In general, the legal procedure must be of a nature to grant an affected investor a reasonable chance within a reasonable time to claim its legitimate rights and have its claims heard. If no legal procedure of such nature exists at all, the argument that "*the actions are taken under*

> *due process of law*" rings hollow. And that is exactly what the Tribunal finds in the present case.[496]

299. In *Kardassopoulos*, the Tribunal found that the expropriation at issue was not in accordance with due process of law, thereby violating Article 13(1) of the ECT. Agreeing with the above-reproduced paragraph of the *ADC v. Hungary* award, it held:

> As in *ADC*, the Respondent in the present case failed to ensure that there was a procedure or mechanism in place, either before the taking or thereafter, which allowed Mr. Kardassopoulos, within a reasonable period of time, to have his claims heard.
>
> Rather, contrary to several elements which may be considered to form part of the due process obligation, such as reasonable advance notice and a fair hearing, the expropriation of Mr. Kardassopoulos' rights was carried out in a manner that can be best described as opaque.[497]

300. The failures of due process at issue in this case are markedly more numerous and severe than those at issue in *ADC* and *Kardassopoulos*. The Tribunal in both of those cases found that the host States had not given the investors a reasonable opportunity to be heard following an expropriation. In the present case, Claimants were given no chance at all to be heard or to object to the direct expropriation that occurred in July 2010. Furthermore, despite their many efforts to contest Kazakhstan's various measures of indirect expropriation during the October 2008 – July 2010 period, all of Claimants' objections, explanations, and appeals for assistance fell on deaf ears. Claimants vigorously contested the various audits, inspections, findings, criminal charges, fines and seizures levied during that period, but all of their complaints fell upon deaf ears.

301. Kazakhstan's most blatant "due process" violations during the period were the arrest, criminal prosecution, trial, and conviction of Mr. Cornegruta, as well as the conviction of KPM, which was not a party to the Cornegruta proceeding. The Cornegruta trial was littered with due process violations. The criminal charge of engaging in illegal entrepreneurial activities by operating KPM's alleged "main"

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[496] *ADC* Award, ¶ 395, C-206. *See* also, *Compañiá de Aguas del Aconquija S.A. and Universal v. Argentine Republic*, ICSID Case No. ARB/97/3, Award, November 21, 2000 ("*Vivendi* Award"), C-241; *Goetz* Award, C-227.

[497] *Kardassopoulos* Award ¶¶ 396-7, C-205.

pipelines without a license was entirely fabricated, and factually incorrect in two major respects. First, Mr. Cornegruta was not and never had been an entrepreneur under Kazakh law. He did not own any stake in KPM; rather, he was merely a salaried manager. Claimants wrote to the Kazakh prosecutors in charge to complain that the arrest of Mr. Cornegruta was unlawful, but those pleas were ignored.

302. Second, none of the pipelines KPM (or, for that matter, TNG) operated were "main" pipelines. The "main pipeline" accusation was entirely fabricated by Kazakhstan's authorities. It was contrary to Kazakhstan's own approvals of KPM's in-field gathering systems, contradicted by multiple admissions of Kazakh officials, demonstrated to be frivolous by the reports of numerous independent experts, and belied by Kazakhstan's classification and treatment of in-field gathering systems operated by every other oil and gas producer in the country. The only "expert" who supported the State's accusation was an employee of the Ministry of Justice, and his opinion was contradicted by every industry expert that also investigated the issue.

303. During Mr. Cornegruta's trial, an obviously partial court rendered the verdict demanded by the State. The prosecutor and judge relied upon an "admission" by Mr. Cornegruta that consisted of him reciting a statutory list of activities that included the phrase "main gas and oil products pipeline." The court ignored seven expert opinions introduced by defense counsel explaining that the KPM gathering system pipelines were not "main" pipelines (two of which were withdrawn due to threats by the Financial Police). The court relied upon the lone "expert" report submitted by the Ministry of Justice at the behest of the Financial Police. The court convicted Mr. Cornegruta of the crime of "engaging in illegal entrepreneurial activity" on the basis that he operated "main" pipelines without a license and sentenced him to four years in prison.

304. Compounding the travesty of justice and violations of due process, the court also rendered a verdict against KPM, which was not a party to the criminal proceeding. Under Kazakh law, business entities cannot be prosecuted for crimes. KPM was never named or made a party to the criminal proceeding. Consequently, KPM was not represented by counsel during the criminal trial against Mr. Cornegruta. Additionally, the court ordered KPM to pay the Government a fine of approximately USD 145 million. That sum bore no relation to the charge; rather, it

simply constituted all of KPM's oil and gas production revenues from March 2007 to May 2008, on which KPM had already paid taxes to the State. Those revenues (for which no attendant costs were deducted) bore no relationship whatsoever to the transportation fees that are the sole income for "main" pipeline operations. Finally, the court made no effort to formally serve the verdict on KPM, to simply deliver it to KPM, or to provide notice of its content. It was only after the enforcement bailiff had commenced enforcement of the verdict against KPM's assets that KPM finally received an official copy of the verdict.

305. The injustices continued even after the trial. Mr. Cornegruta filed an appeal with the Mangystau Regional Court. Because KPM was not a party to the trial proceedings, KPM was not a party to, or represented in, the appellate proceeding. Nevertheless, on November 12, 2009, the Regional Court affirmed the verdicts of the Aktau Court against both Mr. Cornegruta and the non-party KPM.

306. On January 25, 2010, once it had finally received official notice of the lower court verdict, KPM filed an independent appeal of the Aktau Court verdict with the Board of Appeals of the Mangystau Regional Court. On January 29, 2010, the Court denied KPM's right to appeal the verdict, holding that the appeal was made too late. The Regional Court held that the appeal was too late despite the fact that the lower court's failure to timely apprise KPM of its verdict had caused the delay. The lower court's September 18, 2009 verdict against KPM was not delivered to the company until January 14, 2010, and the court itself never officially notified KPM of the verdict.

307. While egregious, Kazakhstan's due process violations did not begin or end with Kazakhstan's malicious prosecution of Mr. Cornegruta and outrageous convictions of Mr. Cornegruta and KPM. A variety of severe measures of harassment, seizures, and executions plagued KPM and TNG (another non-party to the criminal case) between late 2008 and mid-2010. As described above, criminal investigations against both KPM and TNG were the purported bases for multiple investigations of KPM and TNG, interrogations of their personnel, raids on their offices, and threats against other key in-country managers that caused them to flee the country.

308. The various investigations were baseless, unfair, politically-motivated, and pursued without regard to due process or any heed paid to KPM's and TNG's complaints or its explanations of the various issues. In hindsight, it is clear that in late 2008, the Government devised a plan to interfere with Claimants' investments in Kazakhstan, diminish their value to Claimants, and ultimately nationalize them.[498] Kazakhstan did not explain to KPM and TNG the legal grounds for its various audits and investigations, and they were none. In fact, in some cases, the companies' complaints simply prompted further investigations and harassment. TNG's general director, Alexandru Cojin, explains that Kazakhstan decided to investigate TNG for alleged illegal entrepreneurial activity only *after* TNG wrote to complain of the illegal acts the financial police committed by seizing documents and interrogating employees.[499]

309. Upon learning of the criminal investigation against KPM, Claimants filed complaints with four different government agencies[500] against the Financial Police due to its illegal actions and to obtain the dismissal of the criminal case against KPM. Those officials did not address Claimants' complaints, but summarily dismissed them. Claimants wrote again to the Prosecutor's office in March 2009 to complain that the criminal investigations were illegal. Again, Kazakhstan ignored that plea.[501]

310. In addition to the unfair and illegal criminal investigations, Kazakhstan committed due process violations with regard to Claimants' rights to extend the exploration period for the Contract 302 Properties and to confirm ownership of TNG to Terra Raf. Again, Kazakhstan completely ignored Claimants' requests for action and assistance. Kazakh authorities ignored Claimants repeated letters regarding the extension of Contract No. 302for nearly six months, starting in October 2008; then assured Claimants it would approve the extension; and then altogether failed to issue the approval. Similarly, Government officials never

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498 *See* Letter from Blagovest President to MEMR, dated February 7, 2010, C-23.

499 Cojin Statement ¶¶ 4-12.

500 Complaints from KPM against the Financial Police to the with the General Prosecutor's Office of Kazakhstan, the Ministry of Justice of the Republic of Kazakhstan, the Financial Police itself, the MEMR, and the Western Regional Transport Prosecutor, dated January 19, 2009, C-96.

501 Letter to the General Prosecutor's Office dated March 18, 2009, C-154.

answered Claimants' March 2009 request that it confirm Terra Raf as the legitimate owner of TNG. Those failures prevented Claimants from selling KPM and TNG.

311. As if the above-mentioned conduct were not enough, Kazakhstan followed it in mid-2010 with new allegations of unfounded contract violations; unilateral, illegal cancellation of KPM's and TNG's contracts; and the complete takeover of KPM and TNG, which forced the Claimants' remaining personnel to resign and/or flee the country.

312. KPM and TNG were given only three days to respond to and explain the multiple allegations of violation of their Subsoil Use Contracts before the contracts were repudiated. The lack of a reasonable amount of time to respond alone constitutes a violation of due process. However, Kazakhstan's conduct went further, because KPM and TNG did respond with thorough explanations addressing the unfounded allegations. Kazakhstan wholly ignored the responses timely provided by KPM and TNG.[502] Instead, Kazakhstan unilaterally repudiated the Subsoil Use Contracts and physically took over KPM and TNG.

313. The violations of due process committed by Kazakhstan in this case are extraordinary in number, variety, scale, and severity. They render Kazakhstan's (indirect and direct) expropriations of Claimants' investments illegal under Article 13 of the ECT and international law. As discussed further below, Kazakhstan's egregious violations of due process also violate the ECT's "most constant protection and security," fair and equitable treatment, and impairment clauses.

c. Kazakhstan Did Not Pay "Prompt, Adequate and Effective Compensation"

314. Kazakhstan's expropriation of Claimants' investments was also unlawful because the State failed to pay Claimants "prompt, adequate and effective compensation," as required by Article 13 of the ECT and international law. Kazakhstan has never paid any compensation to Claimants for the expropriation of their investments.

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[502] *See* Notice of infringement of obligations under the Borankol Subsoil Use Contract, from MOG to KPM dated July 14, 2010, C-2; Notice of infringement of obligations under the Tolkyn Subsoil Use Contract, from MOG to TNG dated July 14, 2010, C-6; Notice of infringement of obligations under the Subsoil Use Contract No. 302, from MOG to TNG dated July 14, 2010, C-7.

315. Article 13's requirement that any expropriation be accompanied by "prompt, adequate, and effective compensation" is solidly grounded in international law. The rule has been confirmed by numerous tribunals and recognized by a wide array of international scholars.[503]

316. In the present case, Kazakhstan has never paid any compensation to Claimants for its expropriation of their investments. It is therefore indisputable that Kazakhstan's (indirect and direct) expropriations of Claimants' investments were unlawful under Article 13 of the ECT and international law.

d. Kazakhstan's Expropriations Were Discriminatory

317. Kazakhstan's expropriatory measures were also illegal under Article 13 of the ECT and international law because they were discriminatory. Kazakhstan's

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[503] *See e.g.*, Dolzer & Schreuer, at 110, C-219; *Pope & Talbot Inc. v. The Government of Canada,* Interim Award, June 26, 2000 *("Pope & Talbot* Interim Award") ¶ 99, C-244; *Santa Elena* Award ¶ 72, C-213; *Azurix Corp. v. The Argentine Republic,* ICSID Case No. ARB/01/12, Award, July 14, 2006 ("*Azurix* Award") ¶ 309, C-245; *Tecmed* Award ¶ 121, C-209; *Phelps Dodge Corp. v. Iran*, Case No. 99, Award No. 217-99-2, March 19, 1986, 10 IRAN-US CL. TRIB. REP. 121, 130, C-246; *Amoco Int'l Fin. Corp. v. Iran*, Case No. 56, Partial Award No. 310-56-3, 15 Iran-U.S. CL. TRIB. REP. 288 ¶¶ 112, 189, 199-193 (July 14, 1987) ("[A] lawful expropriation must give rise to 'the payment of fair compensation, or of the just price of what was expropriated.' Such an obligation is imposed by a specific rule of the international law of expropriation."), C-247; *Biloune Award*, C-235. *See also* E. Lauterpacht, *Issues of Compensation and Nationality in the Taking of Energy Investments*, 8 J. ENERGY & NAT. RES. L. 241, 243 (1990), C-248 ("Whatever the form of the taking by the State of a foreign investment, it is not usually in itself internationally unlawful if it satisfies certain conditions. One is that the taking should be for a public purpose. A second is that it should not be discriminatory. A third is that the taking should be accompanied by compensation."); P. Muchlinski, *Multinational Enterprises and the Law* 504 (Wiley-Blackwell 1999), C-249, setting out the elements of lawful expropriation; M.N. Shaw, INTERNATIONAL LAW 739 (Cambridge Univ. Press, 5th ed. 2004), C-211 ("International law will clearly be engaged where the expropriation is unlawful, either because of, for example, the discriminatory manner in which it is carried out or the offering of inadequate or no compensation."); I. Brownlie, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 519 (Oxford Univ. Press, 6th ed. 2003), C-210 ("The majority of states accept the principle of compensation."); C.F. Amerasinghe, STATE RESPONSIBILITY FOR INJURIES TO ALIENS 147 (Clarendon Press 1967), C-250 ("[T]he practice of the majority of States in paying compensation, whether by treaty or by legislation, lends itself to the conclusion that the rule that that compensation is payable which was applicable to expropriation has not been changed. . . . It is submitted that the rule that there must be compensation permits of no exceptions, and that it applies to all forms of expropriation, including nationalization."); G. Georgiev, *The Award in Saluka Investments v. Czech Republic*, THE REASONS REQUIREMENT IN INTERNATIONAL INVESTMENT ARBITRATION at 175 *et seq*. (G. Aguilar-Alvarez and M. Reisman, eds. 2008), C-251. *See Trustees of the Late Duke of Westminster's Estate v. United Kingdom*, 5 E.H.R.R. 440, 448 (1983), C-252. *Compañía de Aguas del Aconquija and Vivendi Universal v. Argentine Republic*, ICSID Case No. ARB/97/3, Award, August 20, 2007, ("*Vivendi II* Award") ¶ 7.5.21, C-253. See also, *Siemens* Award, ¶ 273, C-232; *Azurix Corp. v. The Argentine Republic,* ICSID Case No. ARB/01/12, Decision on Annulment, September 1, 2009 ¶ 324, C-254; *Bernardus et al.* Award ¶¶ 98, 107, C-218. *Kardassopoulos* Award ¶¶ 389-90, 405, C-205. *See also*, *Rumeli* Award ¶ 706 (finding that the expropriation was unlawful because "the valuation placed on Claimants' shares was manifestly and grossly inadequate compared to the compensation which the Tribunal there holds to be necessary in order to afford adequate compensation under the BIT and the FIL."), C-236.

discrimination also violates the ECT's fair and equitable treatment standard and the ECT's impairment clause. For reasons of brevity, Claimants respectfully refers the Tribunal to the discussions of discrimination in the sections below as an additional basis for concluding that Kazakhstan's expropriations were illegal.

B. Kazakhstan Failed to Provide the Most Constant Protection and Security to Claimants' Investments

1. The Standard of Protection Required by the Treaty and International Law

318. Article 10(1) of the ECT provides that investments "shall enjoy the most constant protection and security." This provision is similar to – but notably stronger than - the more commonly-used language in investment treaties that obligates host States to provide "full protection and security" to investments. Claimants in this case are entitled to the more robust protection accorded by the ECT.[504]

319. The requirement of protection and security contained in Article 10(1) of the ECT, as well as that existing under international law, imposes an obligation of vigilance and due diligence upon Kazakhstan with respect to the protection of investments. That obligation has been acknowledged and explained by a number of international tribunals faced with similar – albeit less robust – provisions in other investment treaties. The standard's origins referred to "physical" protection and security, such as the protection to be afforded by a police or security force. Today, however, the standard indisputably extends to "legal" protection and security, such as that provided by a state's judicial or regulatory organs.

320. In an early case, *AAPL v. Sri Lanka*, the Tribunal described the "duty to protect" as an obligation to provide "due diligence." It approvingly quoted Professor Freeman's definition of that term: "The 'due diligence' [required] is nothing more nor less than the reasonable measures of prevention which a well-administered government could be expected to exercise under similar circumstances."[505] The *AAPL* Tribunal concluded that "adequate protection afforded

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[504] *See* Article 10(7) of the ECT, C-1.

[505] *AAPL* Award ¶ 77, C-255.

by the host State authorities constitutes a primary obligation" under international law.[506]

321. In a similar vein, the *American Manufacturing & Trading, Inc. v. Zaire* tribunal described the standard of full protection and security as follows:

> The obligation incumbent upon Zaire is an obligation of vigilance, in the sense that Zaire as the receiving State of investments made by AMT, an American company, shall take all measures necessary to ensure the full enjoyment of protection and security of its investment and should not be permitted to invoke its own legislation to detract from any such obligation. Zaire must show that it has taken all measures of precaution to protect the investments of AMT on its territory. It has not done so.[507]

322. The *AMT* tribunal further held that in order to satisfy the protection and security standard contained in the BIT, Zaire had to comply with its own national laws:

> These treatments of protection and security of investment required by the provisions of the BIT of which AMT is beneficiary must be in conformity with its applicable national laws and must not be any less than those recognized by international law. For the Tribunal, this last requirement is fundamental for the determination of the responsibility of Zaire. It is thus an objective obligation which must not be inferior to the minimum standard of vigilance and of care required by international law.[508]

323. The Tribunal readily concluded that Zaire had violated its obligation of protection and security, because it had taken "no measure whatever that would serve to ensure the protection and security of the investment in question."[509] This finding illustrates that the duty to protect is an affirmative obligation, and omissions by a host state will result in violation of that duty.

324. Although the older *AAPL* and *AMT* cases involved issues of physical protection and security, the full protection and security standard is not limited to

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506 *Id.* ¶ 76.

507 *American Manufacturing & Trading, Inc. v. Zaire,* ICSID Case No. ARB/93/1, Award, February 21, 1997, ¶ 6.05, C-256.

508 *Id.* ¶ 6.06.

509 *Id.* ¶¶ 6.08, 6.11.

issues of physical protection.[510] In the words of Dolzer & Schreuer: "the contemporary understanding extends beyond physical protection to guarantees against infringements of the investor's rights by operation of laws and regulations of the host state."[511]

325. A number of investment treaty tribunals have recently applied the standard to the "legal" protection and security of an investment. In *CME v. Czech Republic*, the Czech Media Council approved the right of an investor to use a particular television license, but then later actions effectively revoked the prior approval of the arrangement.[512] The Tribunal found that the Czech Republic, via the Media Council, breached its obligation to provide the investor with full protection and security by revoking the licensing right.[513] Specifically, the Tribunal determined that the Czech Republic's obligation extended to the provision of not just physical, but also legal security to the investment: "The host State is obligated to ensure that neither by amendment of its laws nor by actions of its administrative bodies is the agreed and approved security and protection of the foreign investor's investment withdrawn or devalued."[514]

326. Likewise, in *Siemens v. Argentina*, Argentina had suspended services under a contract concluded with the Claimant and then sought to renegotiate the contract "for the sole purpose of reducing its costs, unsupported by any declaration of public interest."[515] Based on these grounds and others, the Tribunal concluded that Argentina had violated the full protection and security clause (and the fair and equitable treatment clause) contained in the BIT. The Tribunal found that, because the relevant BIT protected tangible and intangible investments, the obligation to provide full protection and security extended beyond physical protection.[516]

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[510] *See also*, *Wena* Award ¶¶ 85, 88-91, 131, C-216.

[511] Dolzer & Schreuer, at 149, C-219.

[512] *CME* Partial Award ¶¶ 427, 520, 539, 559-560 (*see* generally ¶¶ 460-574), C-229.

[513] *Id.* ¶ 613.

[514] *Id*.

[515] *Siemens* Award ¶ 308, C-232.

[516] *Id.*,¶ 303. *See also*, *Azurix* Award ¶ 408, C-245 (" . . . full protection and security was understood to go beyond protection and security ensured by the police. It is not only a matter of physical security; the stability afforded by a secure investment environment is as important from an investor's point of view.").

327. *Vivendi II* involved a concession agreement for water services and the provincial authorities' unilateral modification of tariffs and the forced renegotiation of a contract.[517] The Tribunal held:

> [T]he Tribunal notes that the text of Article 5(1) does not limit the obligation to providing reasonable protection and security from "physical interferences," as Respondent argues. If the parties to the BIT had intended to limit the obligation to "physical interferences", they could have done so by including words to that effect in the section. In the absence of such words of limitation, the scope of the Article 5(1) protection should be interpreted to apply to reach any act or measure which deprives an investor's investment of protection and full security, providing, in accordance with the Treaty's specific wording, the act or measure also constitutes unfair and inequitable treatment. Such actions or measures need not threaten physical possession or the legally protected terms of operation of the investment.[518]

328. The Tribunal stated, "[t]hus protection and full security (*sometimes full protection and security*) can apply to more than physical security of an investor or its property, because either could be subject to harassment without being physically harmed or seized."[519] Of course, that conclusion is all the more resonant under the ECT, which does not merely provide for "full protection and security," but, rather, requires that the "most constant protection and security" be afforded to investments.

2. Kazakhstan Failed to Provide the "Most Constant Protection and Security" to Claimants' Investments

329. Kazakhstan's violations of the "most constant protection and security" provision of the ECT and the standard of protection required by international law are blatant and cannot be seriously disputed.

330. In terms of physical security, Kazakhstan arrested and jailed the general manager of KPM, Mr. Cornegruta, on fabricated charges. Kazakhstan initiated criminal investigations against no fewer than four other of Claimants' general managers and threatened their arrest, such that they found it necessary to flee

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517 *See Azurix* Award ¶ 408.

518 *Vivendi II* Award ¶ 7.4.15, C-253.

519 *Id.* ¶ 7.4.17 (emphasis added).

the country. Kazakhstan also summoned, interrogated, and threatened a number of Claimants' employees, including Messrs. Condorachi, Cornegruta, Stejar and Cojin. Such acts against Claimants' key in-country personnel, which were based on the Government's trumped-up criminal allegations, violated Kazakhstan's affirmative obligation to provide the most constant protection and security to Claimants' investments.[520]

331. Kazakhstan also violated the "most constant protection and security" standard with regard to Claimants' physical assets and contractual rights by commandeering KPM's and TNG's offices and transferring operations, revenues, and hydrocarbons productions to KazMunaiGas.[521]

332. Kazakhstan did not merely fail to physically protect Claimants' investments. Rather, the Government itself was the perpetrator of the lack of protection and insecurity. In addition to the various deliberate acts it took to undermine the security of Claimants' investments, Government officials altogether failed to acknowledge or meaningfully respond to Claimants' repeated protests and requests for assistance. Throughout this Statement of Claim, Claimants have listed a number of instances in which Kazakhstan failed to protect Claimants and their investments or meaningfully respond to their requests for assistance. The most egregious examples are summarized below:

- On January 19, 2009, Claimants filed complaints with the Western Regional Transport Prosecutor, the General Prosecutor's Office, the Ministry of Justice, and the MEMR against the Financial Police in respect to its illegal actions and to obtain the dismissal of the criminal case against KPM. The only answer Claimants received was a notice from the Financial Police that their complaints were dismissed and that a criminal case also being initiated against TNG.
- On March 18, 2009, Claimants submitted a new complaint with the General Prosecutor's Office regarding the illegal

[520] Kazakhstan's acts also violated its obligation to permit Claimants to employ key personnel under Article 11(2) of the ECT, C-1. Article 11(2) provides: "A Contracting Party shall permit Investors of another Contracting Party which have Investments in its Area, and Investments of such Investors, to employ any key person of the Investor's or the Investment's choice regardless of nationality and citizenship provided that such key person has been permitted to enter, stay and work in the Area of the former Contracting Party and that the employment concerned conformed with the terms, conditions and time limits of the permission granted to such key person."

[521] *See* Section V.C.

initiation of criminal cases against KPM and TNG. Claimants never received an answer to this complaint.

- In the period from October 2008-March 2009, Claimants wrote to the MEMR to obtain the extension of the exploration period for Contract No. 302 prior to its expiration on March 30, 2009. The extension was never granted, in violation of the Government's commitments.
- As per the request of the MEMR, on April 30, 2009, Claimants submitted addendum No. 9 to Contract No. 302 for the extension of the exploration period for execution by the MEMR. Claimants never received an answer to this request for an extension.
- On March 24 and 25, 2009, Claimants requested that Kazakhstan confirm that Terra Raf was the legitimate owner of TNG and confirm its prior waiver of its pre-emptive rights. Claimants never received an answer to this request.
- On April 26-27, 2009, Claimants filed complaints with the Regional Prosecutor's Office and the Western Regional Transport Prosecutor regarding the arrest of Mr. Cornegruta. Claimants never received an answer to their complaints.
- On May 7, 2009, Claimants appealed directly to President Nazarbayev to obtain the release of Mr. Cornegruta, protect the former and current management of KPM and TNG, and end the dispute. President Nazarbayev ignored the request and never responded.
- After Mr. Cornegruta was sentenced to four years in prison, his wife and Claimants obtained an undertaking from Moldova to request the transfer of Mr. Cornegruta to serve his sentence in his home country, closer to his family. However, the Kazakh Prosecutor General, at the request of the Financial Police, always requested further assurances from Moldova that he would indeed serve his sentence. In the end, Kazakhstan refused to extradite him.[522]
- Kazakhstan improperly assessed alleged corporate back taxes and penalties against KPM and TNG in the amount of approximately USD 62 million. While KPM's and TNG's court challenges to those assessments were pending, Kazakhstan issued a bankruptcy notice on February 3, 2010.
- On July 16, 2010, despite being only given three days to respond to the accusations of alleged violations of the Subsoil Use Contracts, KPM and TNG provided detailed explanations refuting the State's accusations. Claimants' timely responses

[522] Pisica Statement ¶ 51. *See also* Letter from the General Prosecutor's Office of Kazakhstan to the Ministry of Justice of Moldova, dated June 10, 2010, C-200.

were ignored, and Kazakhstan unilaterally repudiated the Subsoil Use Contracts.

333. Kazakhstan's failure to respond to Claimants' numerous requests for assistance – not to mention its egregious failures to provide protection and security to Claimants' investments in the first place – make its breaches of Article 10(1) of the ECT and international law all the more severe.

334. In addition to the failures to provide physical and legal protection and security and the repeated failures to respond to Claimants' requests for assistance cited above, Kazakhstan violated the ECT's "most constant protection and security" standard in a number of other ways. Kazakhstan harassed Claimants by unduly requesting the payment of taxes and customs duties that were not due and that had no basis in Kazakh law, and it launched a variety of illegal investigations and interrogations of KPM, TNG, and their employees. Moreover, Kazakhstan arbitrarily and retroactively reversed its consent to Terra Raf's 2003 acquisition of TNG, as well as its prior pre-emptive right waiver. That materially impacted the legal security and situation of TNG.

335. Kazakhstan also failed to provide legal security by ignoring contractual provisions as agreed by the parties. That failure occurred when Kazakhstan refused to execute the previously-approved extension of TNG's exploratory rights in the Contract 302 Properties, and again when Kazakhstan unlawfully (and unilaterally) terminated KPM's and TNG's Subsoil Use Contracts after lodging baseless allegations of contract violations. Each of those measures is a far cry from providing the "most constant legal protection and security" required by the ECT.

336. In sum, Kazakhstan repeatedly violated the "most constant protection and security" standard contained in Article 10(1) of the ECT, as well as the standard of protection and security required by international law. It failed to provide physical security by arresting one in-country manager, forcing others to flee, and physically seizing Claimants' property; and it failed to provide legal security by disregarding contractual agreements and its own laws, by failing to provide Claimants with any meaningful opportunity to challenge its actions, and by repeatedly ignoring Claimants' multiple requests for assistance. The Tribunal should not hesitate to

conclude that Kazakhstan failed to provide the "most constant protection and security" to Claimants' investments.

C. Kazakhstan Violated the ECT's Fair and Equitable Treatment Provision

1. The Fair and Equitable Treatment Standard

337. Under Article 10(1) of the ECT, Kazakhstan was obligated to treat Claimants' investments fairly and equitably. That provision states:

> Each Contracting Party shall, in accordance with the provisions of this Treaty, encourage and create stable, equitable, favourable and transparent conditions for Investors of other Contracting Parties to make Investments in its Area. Such conditions shall include a commitment to accord at all times to Investments of other Contracting Parties fair and equitable treatment.

338. Other than what is suggested by the first sentence of Article 10(1) in terms of Kazakhstan's obligations to "encourage and create stable, equitable, favourable, and transparent conditions for Investors," the ECT does not precisely define what constitutes "fair and equitable treatment." Therefore, the Tribunal "will have to decide whether in all the circumstances the conduct in issue is fair and equitable or unfair and inequitable."[523]

339. The fair and equitable treatment standard in Article 10(1) of the ECT must be interpreted in good faith in accordance with the ordinary meaning to be given to its terms in their context and in light of the object and purpose of the treaty.[524] Given the breadth of the terms "fair" and "equitable," as well as their context in the ECT and the object and purpose of the Treaty, the fair and equitable

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[523] F.A. Mann, *British Treaties for the Promotion and Protection of Investments*, 52 BRIT. Y.B. INT'L L. 241, 244 (1982), at 241-244, C-257. *See also Rumeli* Award ¶ 610, C-236.

[524] *See, e.g.*, Vienna Convention, Art. 31, C-203; *Asian Agricultural Products Ltd. v. Sri Lanka*, ICSID Case No. ARB/87/3 , Final Award of June 27, 1990 ¶¶ 38-42 ("*AAPL* Award), C-255; *MTD v. Chile*, ICSID Case No. ARB/01/7, Award, May 25, 2004 ¶ 112, ("*MTD* Award"), C-258; *Tecmed* Award ¶ 155, C-209; *Saluka v. Czech Republic*, UNCITRAL, Partial Award, March 17, 2006 ¶¶ 296 *et seq.* ("*Saluka* Partial Award"), C-259; *Azurix* Award ¶ 361, C-245; *Eureko B. V. v. Poland* (Ad Hoc), Partial Award, August 19, 2005 ¶ 247, ("*Eureko* Partial Award"), C-260; *PSEG Global et al. v. Republic of Turkey*, ICSID Case No. ARB/02/5, Award, January 19, 2007 ¶ 239, C-261; *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Argentine Republic*, ICSID Case No. ARB/02/1, Decision on Liability, October 3, 2006 ¶ 122 ("*LG&E* Decision on Liability"), C-262; *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, May 22, 2007 ¶ 259 ("*Enron* Award"), C-263; *Kardassopoulos and Fuchs* Award ¶ 429, C-205.

treatment standard in the ECT prohibits a wide array of governmental misconduct, including the various acts of misconduct and wrongful omissions at issue in this case.

340. Investment treaty tribunals have routinely applied an "ordinary meaning" approach to the terms "fair" and "equitable." For instance, the ICSID Tribunal in *MTD v. Chile* concluded that the "ordinary meaning" of "fair and equitable" is "just, even-handed, unbiased, legitimate."[525]

341. With respect to context, the Tribunal in *Saluka* explained that context included the treaty article in which the fair and equitable treatment standard is found, as well as the other provisions in the relevant treaty, including the Preamble.[526] Thus, as noted above, the relevant context of the fair and equitable treatment provision in the ECT includes the first sentence of Article 10(1), which requires Kazakhstan to "encourage and create stable, equitable, favourable and transparent conditions for Investors." Also relevant is the ECT's Preamble, which includes as a goal "to catalyze economic growth by means of measures to liberalize investment and trade in energy."[527]

342. Article 2 of the ECT (Purpose of the Treaty) states that the purpose of the Treaty is as follows:

> This Treaty establishes a legal framework in order to promote long-term cooperation in the energy field, based on complementarities and mutual benefits, in accordance with the objectives and principles of the [European Energy] Charter.

343. The ECT Readers' Guide sheds further light on the ECT's object and purpose, which include in particular "boost[ing] investor confidence and to contribute to an increase in international investment flows."[528]

344. In interpreting the ECT's fair and equitable treatment standard, the Tribunal should also consider the manner in which the standard has been interpreted

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[525] *See MTD* Award ¶ 113, C-258; *See also Azurix* Award ¶ 360, C-245; and *Siemens* Award ¶ 290, C-232: "In their ordinary meaning, the terms 'fair,' and 'equitable' mean 'just,' 'even-handed,' 'unbiased,' 'legitimate.'"

[526] *Saluka* Partial Award ¶¶ 298-99, C-259. This approach is consistent with Article 31(2)(a) of the Vienna Convention, which explicitly mentions a treaty's preamble among the appropriate sources of meaning for interpreting individual treaty provisions. Vienna Convention, Art. 31(2)(a), C-203

[527] ECT Preamble and Article 10(1), C-1.

[528] Readers' Guide, at 9, 19, C-264.

and applied under international law, particularly by the many investment treaty tribunals that have considered the standard in recent years. Over the past five to ten years, the fair and equitable treatment standard has become one of the most prominent standards in investment treaty jurisprudence. A considerable body of case law has imparted specific meaning and content to the standard. Although the standard is inherently flexible and potentially applicable to any type of host state misconduct (including both acts and omissions), recurring fact patterns and similarities between cases have enabled international tribunals and scholars to articulate categories of behavior that clearly violate the standard.

345. Today, it is clear that the fair and equitable treatment standard prohibits at least the following types of state misconduct:

- Actions that violate an investor's legitimate expectations in relation to the investment;[529]
- Conduct that creates an unstable or unpredictable legal framework or business environment for the investment;[530]
- Conduct that violates due process[531] or results in a "denial of justice,"[532] including (but not limited to) improper judicial or

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[529] *See, e.g.*, Dolzer & Schreuer, at 146 (2008), C-219; *Rumeli* Award ¶ 609, C-236; *Occidental Exploration and Production Company v. The Republic of Ecuador*, LCIA Case No. UN3467, Final Award of July 1, 2004 ¶¶ 183-185 ("*Occidental* Award"), C-233; *CME* Partial Award ¶ 611, C-229; *CMS Gas Transmission Co. v. The Argentine Republic*, ICSID Case No. ARB/01/8, Award, May 22, 2005 ¶¶ 274-76 ("*CMS* Award"), C-65; *Azurix* Award, ¶ 372, C-245; *PSEG* Award ¶ 240, C-261; *Saluka* Partial Award ¶ 301-03, C-259; *MTD* Award ¶¶ 113-15, C-258; *Eureko* Partial Award ¶ 235 C-260; *Metalclad* Award ¶ 85, C-226; *Waste Management, Inc. v. Mexico*, ICSID Case No. ARB(AF)/00/3 (NAFTA), Award, April 30, 2004 ("*Waste Management* Award"), C-234; *LG&E* Decision on Liability ¶¶ 124-25 C-262; *Enron* Award ¶¶ 259-60, 262, C-263; *Sempra v. Argentina*, ICSID Case No. ARB/02/16, Award, September 28, 2007, ("*Sempra* Award") ¶¶ 298-300, C-265; *Thunderbird v. Mexico* (UNCITRAL-NAFTA), Final Award, January 26, 2006 ¶ 147, C-266 ("*Thunderbid* Award"); *Siemens* Award ¶¶ 297-99, C-232; *ADC* Award ¶¶ 423-25, 445 C-206; *Bogdanov et al. v. Moldova*, SCC Case Award, September 22, 2005 ¶ 72 C-267; *BG Group Plc v. Argentina*, UNCITRAL, Award, December 24, 2007 ¶¶ 294-300 ("*BG* Award"), C-268; *National Grid v. Argentine Republic*, UNCITRAL, Nov. 3, 2008 ¶ 179, Award, C-269; *Siag v. Egypt*, ICSID Case No. ARB/05/15, Award, June 1, 2009 ¶ 450, C-217; *Biwater Gauff v. Tanzania*, ICSID Case No. ARB/05/22, Award, July 24, 2008 ¶ 602 (internal citations omitted) ¶ 615 ("*Biwater* Award"), C-270; *Suez and others v. Argentina*, Decision on Liability, ICSID Case No ARB/03/17, July 30, 2010 ¶ 203 ("*Suez* Decision on Liability"), C-271. *Tecmed* Award ¶ 154, C-209.

[530] *See LG&E* Decision on Liability ¶¶ 127-131 ("the fair and equitable treatment standard consists of the host state's consistent and transparent behaviour, free of ambiguity that involves the obligation to grant and maintain a stable and predictable legal framework necessary to fulfill the justified expectations of the foreign investor."), C-262. Notably, the *Occidental v. Ecuador* tribunal, in finding a breach of the FET standard, emphasized that "stability of the legal and business framework is . . . an essential element of fair and equitable treatment." *Occidental* Award, ¶ 190-1, C-233; *see also Saluka* Award, ¶¶ 301-303, C-259.

administrative proceedings as well as governmental interference in such proceedings;[533]

- Interference with a contractual relationship;[534]
- Actions that treat an investor or an investment inconsistently,[535] ambiguously, or with a lack of transparency;[536]
- Failure to sufficiently notify an investor in advance of impending acts that will impact the investment;[537]
- Actions that are discriminatory;[538]
- Harassment or coercive conduct;[539] and

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[531] Dolzer & Schreuer, C-219; *see also*, *Tecmed* Award, ¶¶ 153, 174, C-209 (stating that "It is understood that the fair and equitable treatment principle included in international agreements for the protection of foreign investments expresses '. . . the international law requirements of due process, economic rights, obligations of good faith and natural justice.'").

[532] Harvard Research, Art. 9 (1929), reported in American Journal of International Law, April 1929, C-272. *See also*, Alvyn Freeman, "The International Responsibility of States for Denial of Justice", (Kraus Reprint Co. 1970), at 252, C-273; *Vivendi II* Award, ¶7.4.11, C-253; *Vivendi* Award, ¶ 80, C-241 (finding that the standard would be violated if Claimants were denied access to pursue remedies in court, were treated unfairly in court, or if the judgments were substantively unfair); *Waste Management* Award, ¶ 98, C-234; *Mondev International Ltd. v USA*, ICSID Case No. ARB(AF)/99/2, Award of October 11, 2002, ¶ 127 C-274; *Loewen Group, Inc., and Raymond L. Loewen v. US*, ICSID Case No. ARB(AF)/98/3, Award of June 26, 2003, ¶ 132, C-275.

[533] *Petrobart* Award, C-204 (stating that "Government intervention in judicial proceedings is not in conformity with the rule of law in a democratic society").

[534] *Alpha* Award, ¶¶ 420 and 422, C-207; *see also*, *Eureko* Partial Award ¶ 132, C-260; *Suez* Decision on Liability, ¶¶ 203, 231 C-271; *Rumeli* Award, ¶ 615, C-236.

[535] *MTD Equity Sdn Bhd. v. Chile* Award ¶¶ 53-57, 80, 165, C-258 (concluding that the FET standard was breached because "two arms of the same Government" had acted inconsistently toward the same investor, and noting that the host state "has an obligation to act coherently and apply its policies consistently, independently of how diligent an investor is.").

[536] *See, e.g.*, *Tecmed* Award, ¶¶ 172-174, C-209; *Saluka* Partial Award, ¶¶ 420-423, C-259 ("The Czech Government's exchange of views with Saluka/Nomura and IPB on possible solutions for IPB also lacked sufficient transparency to allow Saluka/Nomura and IPB to understand exactly what the Government's preconditions for an acceptable solution were… . The Government failed to respond in any constructive way."); *see also* UNCTAD, *Fair and Equitable Treatment*, UNCTAD Series on Issues in International Investment Agreements at 51 (United Nations 1999) (references omitted), C-276.

[537] *Metalclad* Award, ¶ 91, C-226; *see also Middle East Cement* Award, ¶143, C-228 (the case involved Egypt's failure to notify the claimant of the auction of a ship it owned. The Tribunal held that although Egypt had satisfied the notice had satisfied the notice provisions under domestic law, Egypt violated the fair and equitable treatment requirement because "a matter as important as the seizure and auctioning of a ship of the Claimant should have been notified by a direct communication"); *Tecmed* Award, ¶ 162, C-209.

[538] *Waste Management* Award, ¶ 98, C-234; *MTD* Award, ¶ 109, C-258; *see also Eureko* Partial Award, ¶¶ 36-41, C-260.

- Conduct that is in bad faith.[540]

346. The Tribunal in *Waste Management v. Mexico* captured a number of those types of state misconduct that violate the fair and equitable treatment standard when it stated:

> [F]air and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candor in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.[541]

347. Similarly, in perhaps the most frequently quoted articulation of the fair and equitable treatment standard, the Tribunal in *Tecmed v. Mexico* stated that it:

> requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and to comply with such regulations... The foreign investor also expects the host State to act consistently, *i.e.* without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its

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539 *Vivendi II* Award, ¶¶ 7.4.37 and 7.4.39, C-253; *LG&E* Decision on Liability, ¶¶ 39 and 68, C-262; *Enron* Award, ¶ 266, C-263; *Suez* Decision on Liability, C-271; *Pope & Talbot* Interim Award ¶ 181, C-244.

540 *See*, *e.g.*, *Waste Management* Award ¶ 138, C-234; *Saluka* Partial Award ¶ 407, C-259; *Tecmed* Award, ¶ 124, C-209; Dolzer & Schreuer, at 146, C-219; *Siag* Award ¶ 450, C-217 ("The general, if not cardinal, principle of customary international law that States must act in good faith is thus a useful yardstick by which to measure the Fair and Equitable standard."); *CMS* Award ¶ 280, C-65; *Vivendi II* Award ¶ 7.4.12, C-253; *LG&E* Decision on Liability ¶ 129, C-262; *Azurix* Award ¶ 372, C-245; *Enron* Award ¶ 263, C-263; *BG* Award ¶ 301, C-268; *Siemens* Award ¶¶ 293-300, C-232; and *Occidental* Award ¶ 186, C-233.

541 *Waste Management, Inc. v. United Mexican States* (Number 2), ICSID Case No. ARB(AF)/00/3 Award ¶ 98, April 30, 2004, C-234.

> commercial and business activities. The foreign investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation.[542]

348. The *Tecmed* Tribunal's description of the fair and equitable treatment standard has been widely quoted, approved, and applied by investment treaty tribunals, including *CMS*, *Azurix*, *MTD*, *Occidental*, *LG&E*, *BG*, and *Suez*, among others.

349. A remarkable feature of the present case is that Kazakhstan has violated nearly every single aspect of the fair and equitable treatment standard that has been articulated to date. In previous cases in which a violation of the standard has occurred, tribunals have typically focused on one or two particular types of state misconduct that violates the standard. Kazakhstan's conduct in this case is so outrageous and severe in so many different respects that the present Tribunal will suffer no such limitation. As with expropriation and the ECT's most constant protection and security provision, the conclusion that Kazakhstan violated the fair and equitable treatment provision of the ECT should be indisputable.

2. Kazakhstan Failed to Treat the Claimants' Investments Fairly and Equitably

350. In the interests of efficiency and brevity, Claimants will not describe again at length every act or omission by Kazakhstan that violated its duty to treat Claimants' investments fairly and equitably. Rather, Claimants respectfully refer the Tribunal to Sections IV and V above, which contain Claimants' detailed discussions of Kazakhstan's campaign of harassment and interference toward Claimants and their investments during the October 2008 - July 2010 period as well as Kazakhstan's outright seizure of Claimants' investments in July 2010. Nearly every single act or omission by Kazakhstan during its campaign of harassment and interference, as well as its outright seizure of Claimants' investment in 2010, was markedly unfair and inequitable and is exactly the type of state misconduct that investment treaty tribunals have found to violate the standard.

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[542] *Tecmed* Award ¶ 154, C-209.

351. Nevertheless, at the risk of not doing justice to the number and severity of Kazakhstan's breaches of the fair and equitable standard, Claimants will combine some of Kazakhstan's most egregious acts and omissions and summarize the principle ways in which Kazakhstan violated the fair and equitable treatment standard in this case. They include: 1) fabricating the grounds for criminal actions against Mr. Cornegruta, KPM, and TNG; 2) trying and convicting Mr. Cornegruta in a sham trial that also delivered a verdict against the non-party KPM; 3) preventing Claimants from proving the reserves and potential of the Contract 302 Properties; 4) saddling KPM and TNG with ownership and title concerns that destroyed Claimants' ability to dispose of their investments at market value; 5) destroying the ability of KPM and TNG to operate normally; and 6) fabricating the grounds for the direct seizures of Claimants' investments in July 2010.

a. Kazakhstan Fabricated the Grounds for Criminal Actions Against KPM, TNG, and Key Personnel

- The State's criminal campaign against KPM and TNG was based on its arbitrary, unfair, and false "reclassification" of certain in-field pipelines as "main" pipelines. Even industry experts from the MEMR acknowledged that neither KPM nor TNG operated "main" pipelines,[543] yet the State persisted in harassing KPM and TNG and subjecting their personnel to criminal investigations.
- Moreover, Kazakhstan applied its unfair "reclassification" in an inconsistent manner. The financial police, the prosecution, and the judge presiding at Mr. Cornegruta's trial all concluded that KPM's oil pipeline segment was a "main" pipeline, but the Judicial Executor tasked with enforcing the court's order against KPM admitted that the segment was merely a "field" pipeline.[544]
- Key to its fabricated charge was Kazakhstan's claim that KPM and TNG generated "illegal profits" from operating a main pipeline without a license. But the so-called "illegal profits" the State calculated – amounting to over 65 billion Tenge for KPM and over 82 billion Tenge for TNG – simply reflected the total amount of revenue KPM and TNG generated for oil, gas, and condensate production from 2002 through 2008.[545] The State's calculations were unfair because they did not consider KPM's and TNG's costs or expenses, and they did not correspond to the transportation fees that would have applied if the pipeline segments at issue were truly "main" pipelines.

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[543] *See* section IV.B.3, *supra*.

[544] *See* ¶ IV.B.3, *supra*. According to the *MTD* tribunal, inconsistent conduct from multiple organs of government amounts to unfair and inequitable treatment.

[545] *See*, *e.g.*, Cojin Statement ¶ 7.

Furthermore, key personnel were targeted as criminally responsible for the funds that corresponded to the dates of their respective tenures as General Directors.

- Kazakhstan's "reclassification" was also discriminatory. KPM and TNG gathering systems alone were subjected to "reclassifications," despite similar gathering systems being owned and operated by other oil and gas companies in the immediate vicinity and throughout Kazakhstan.[546]

- The criminal actions frustrated Claimants' legitimate expectations that their investments held valid licenses to operate, and that the State would "use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments."[547] The actions also violated Claimants' legitimate expectations concerning proper, fair Governmental conduct.

b. Kazakhstan Tried and Convicted Mr. Cornegruta (and Non-Party KPM) in a Sham Trial

- Kazakhstan's guilty verdicts against Mr. Cornegruta and KPM were factually incorrect, politically motivated, and riddled with due process violations. KPM was convicted in that proceeding, when it was not even named as a party and could not be named a party under Kazakh law. KPM was not officially notified of the proceeding, nor was it represented by counsel or allowed to appeal.[548] The entire process was an improper judicial proceeding, which the *Petrobart* tribunal found to breach the fair and equitable treatment provision.[549]

- In addition, Kazakhstan directly interfered in the judicial proceeding. Mr. Cornegruta's witnesses were threatened by the Financial Police and forced to withdraw their expert opinions.[550] Kazakhstan's interference in the criminal proceeding and the conviction of non-party KPM ensured that Claimants would not have "a real possibility to present [their] position" on Mr. Cornegruta's and KPM's behalf, which the *Rumeli* and *Tecmed* tribunals deemed contrary to due process and a breach of the fair and equitable treatment standard.[551]

- The criminal proceeding also amounted to a denial of justice under international law. Denial of justice has been defined as a "gross

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[546] Romanosov Statement ¶ 32.

[547] *Tecmed* Award ¶ 154, C-209.

[548] *See* Section IV.B.4, *supra*.

[549] *See*, *generally*, *Petrobart* Award, at 18, C-204.

[550] *See Pisica* Statement ¶ 16. *See also* Letter from the Financial Police to the Ministry of Emergency Situations, dated November 21, 2008, C-92; Letter from the Ministry of Emergency Situations, dated May 13, 2005, C-93.

[551] *See Rumeli* Award, C-236, and *Tecmed* Award, C-209.

deficiency in the administration of judicial… process, failure to provide those guarantees which are generally considered indispensable to the proper administration of justice, [and] a manifestly unjust judgment." Tribunals have also identified both "denials of review" and "judgments in violation of national and international laws" as an instances of denial of justice.[552] Kazakhstan's failure to guarantee even the most elementary notions of due process and a fair trial amount to "gross deficiencies" in the judicial process and can in no way be considered just.

c. Kazakhstan Prevented Claimants from Proving Reserves and the Potential of the 302 Contract Properties

- Kazakhstan's refusal to approve TNG's contractual rights to continue exploration in the 302 Contract Properties comprises two distinct breaches of the fair and equitable treatment provision. First, Kazakhstan simply ignored TNG's requests for an extension for nearly six months. Failing to respond to TNG's repeated requests destabilized Claimants' business environment, created a lack of transparency, and violated Claimants' right to be notified of acts or omissions that would impact its investment.

- Second, Kazakhstan frustrated Claimants' legitimate expectations that the exploration period would be extended. At the latest, Kazakhstan created that expectation in the spring of 2009, when it specifically assured TNG that it approved TNG's extension request and that it would timely execute the necessary addendum.[553] Despite multiple subsequent requests from TNG that Kazakhstan merely formalize what it had already approved, Kazakhstan failed to do so.

- The State's wrongful refusal to execute the addendum extending TNG's exploration rights in the Contract 302 Properties prevented Claimants from proving the Contract 302 Properties' reserves, which in turn prevented them from establishing the market value of their Kazakh investments. At best, Kazakhstan's failure to execute its previously-approved addendum was a failure to treat Claimants' investments consistently and amounted to gross negligence.

- More likely, however, that conduct represents deliberate interference with Claimants' rights over their investments, including KPM's and TNG's contract rights, because Kazakhstan never communicated any change in its position to them and gave them no justification for its refusal. Furthermore, Kazakhstan's conduct was in bad faith, since the refusal was later revealed to have been fuel for the Government's

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[552] Harvard Research, Art. 9 (1929), reported in American Journal of International Law, April 1929, C-272.

[553] Draft Minutes of the meeting dated March 19, 2009, C-42; Letter from the MEMR to TNG dated April 9, 2009, C-27.

ulterior motive of taking over TNG's operations in the Contract 302 Properties, an area in which TNG had already discovered substantial resources.

d. Kazakhstan Destroyed Claimants' Ability to Dispose of Their Investments at Market Value

- Each of Kazakhstan's measures aimed at preventing Claimants from disposing of their investments violates the fair and equitable treatment provision.

- Kazakhstan assessed approximately USD 6 million in back transfer price taxes and penalties against the companies. Those taxes and penalties were incorrect and led to months of litigation that was still pending at the time of the State's outright expropriation in July 2010. Any potential buyer would have been put off, at best, by on-going questions and disputes regarding this tax delinquency.

- Additionally, Kazakhstan raised questions as to the true ownership of TNG and clouded Terra Raf's title when, on December 18, 2008, it retroactively revoked its prior, express consent for the transfer of TNG's ownership from Gheso to Terra Raf and its prior waiver of pre-emptive rights. That conduct was inconsistent and not transparent.

- Kazakhstan's reversal of its prior approval of the transfer of TNG to Terra Raf and of its pre-emptive right waiver is analogous to the facts of *CME v. Czech Republic*, where the tribunal found that the host state's reversal of a prior approval leading to the "evisceration of the arrangements in reliance upon with the foreign investor was induced to invest"[554] breached the fair and equitable treatment provision.

- Moreover, in direct violation of specific contractual and legal provisions that exempted KPM from paying export taxes, the Customs Committee wrongly prohibited KPM from exporting 22,000 tones of crude oil without paying the Crude Oil Export Tax. KPM conditionally paid the wrongfully imposed export taxes, and commenced legal actions challenging the imposition of the tax.

- The State then introduced a new tax provision that replaced crude oil export taxes with a Rent Tax for Export. When a court decision exempted KPM from paying the Crude Oil Export Tax for its January 2009 exports, but instead obliged KPM to pay the newly applicable Rent Tax for Export, the Financial Police intervened. The Aktau territorial customs body subsequently informed KPM that it was required to pay the Crude Oil Export Tax, amounting to USD 4 million, which led to KPM filing additional legal challenges. The Financial Police's interference in KPM's and TNG's contractual

[554] *CME* Partial Award ¶ 611, C-229.

relationship with the Ministry amounts to a violation of Kazakhstan's duty to treat Claimants' investments fairly and equitably. The changes of opinion with respect to export taxes also frustrated Claimants' legitimate expectations that that they would benefit from a contractually agreed tax exemption.[555]

- Kazakhstan acted inconsistently and without transparency by continually changing its position on KPM's and TNG's transfer prices, corporate taxes, export tax exemptions, amortization rates, the extension of TNG's exploration period, and the State's pre-emptive rights. The imposition of clearly improper tax rates is tantamount to extortion.

- Kazakhstan conducted all of the above-mentioned acts in bad faith, because, as of late 2008, Kazakhstan's goal was to take over Claimants' investments. The measures that prevented Claimants from selling their investments furthered that goal.

e. Kazakhstan Destroyed KPM's and TNG's Ability to Operate Normally

- In addition to preventing Claimants from selling their investments, the burdensome taxes that Kazakhstan tried to impose on KPM and TNG, as discussed above, significantly impaired Claimants' ability to operate their investments normally. The months of litigation and negotiation over what should have been uncontroversial contractual and legal provisions created an unstable and unpredictable business environment for Claimants.

- In addition, Kazakhstan launched multiple surprise inspections, raids, and interrogations of Claimants' personnel, which severely hampered Claimants' ability to carry out daily operations as they had in the preceding years. Kazakhstan effectively converted KPM and TNG into companies that existed merely to write reports and answer duplicative and unnecessary questions.

- Kazakhstan also subjected Claimants' personnel to harassing and coercive conduct during its raids and interrogations. It arrested KPM's General Director, Mr. Cornegruta, and waged criminal investigations against other general directors, causing them to flee Kazakhstan. Claimants were unable to keep key personnel in Kazakhstan due to their fear of arrest and prosecution as a result of Kazakhstan's actions.

- Following the conviction of Mr. Cornegruta, Kazakhstan interfered with Claimants' ability to operate KPM and TNG normally by seizing all of their assets and ordering the forced sale of the company. In addition to the burdensome disruptions to normal business operations

[555] *See*, *generally*, *Occidental* Award, C-233.

that the seizure orders caused, KPM and TNG were forced to spend valuable time and resources challenging the orders and protecting their businesses.

f. Kazakhstan Fabricated "Grounds" for the Direct Seizures of Claimants' Investments in June 2010

- Kazakhstan's fabrication of more than a dozen alleged violations of KPM's and TNG's Subsoil Use Contracts violated Claimants' right to fair and equitable treatment in multiple ways. The eleventh-hour allegations of breach were utterly without merit. For example, the Ministry of Oil and Gas raised its tired claim that TNG operated a main pipeline without a license as a ground for claiming breach of TNG's Contract No. 302, even though that contract for exploration in the area surrounding the Tabyl Block had nothing at all to do with KPM's or TNG's gathering systems. The Ministry later admitted that the violations it had alleged only days before were not the reasons for terminating Contract No. 302.

- Even if the allegations had merit, which they did not, Kazakhstan's conduct violated the fair and equitable treatment provision because Claimants were not given the opportunity to meaningfully dispute or to correct the alleged contractual violations.[556] As they only had three days to respond to the State's claims, they "did not have a real possibility to present their position,"[557] or to reach an agreement with Kazakhstan upon steps to be taken to address the alleged problems.[558] Kazakhstan's unilateral contract terminations were also not transparent, because Kazakhstan terminated the contracts as a result of new claims, and despite the Claimants sending the very explanations Kazakhstan demanded on threat of termination.

- Kazakhstan frustrated Claimants' legitimate expectations by wrongfully terminating the contracts before their expiry and in breach of their provisions. For example, the Ministry admitted that it considered the termination of Claimants' contracts effective immediately, and as a result, it transferred ownership of all of KPM's and TNG's property to the State at the 00:00 hour on July 22, 2010. That was a breach of a contractually-mandated 90 day notice period before termination of a contract would be effective.

- Kazakhstan's unilateral abrogation of Claimants' contract rights formed the basis of its outright expropriation of KPM and TNG on July 22, 2010, an act that included the takeover of all of Claimants' investments in Kazakhstan. In no way can the seizure of Claimants' investments be in accord with Kazakhstan's duty to treat Claimants' investments fairly and equitably.

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556 *See Tecmed* Award, C-209.

557 *See Rumeli* Award, C-236.

558 *See Metalclad* Award, C-226.

- Finally, the State acted in bad faith by unilaterally repudiating KPM's and TNG's contracts and unlawfully seizing Claimants' Kazakh investments. Those measures were the final step in what was shown to be the State's months-long, self-serving scheme to gain control and nationalize those investments.

D. Kazakhstan Impaired Claimants' Investments Through Unreasonable and Discriminatory Measures

352. Article 10(1) of the ECT provides that "no Contracting Party shall in any way impair by unreasonable or discriminatory measures" the "management, maintenance, use, enjoyment or disposal" of an investment.

353. From the commencement of its extraordinary campaign of harassment and coercion in October 2008, Kazakhstan severely impaired Claimants' ability to manage, maintain, use, enjoy, and dispose of their investments. Claimants will not repeat again in detail each of the many acts and omissions by Kazakhstan during the October 2008 – July 2010 period that impaired their ability to manage, enjoy, or dispose of their investments at market prices. The "impairment" of Claimants' investments during that period is indisputable. Of course, Kazakhstan's outright seizures of Claimants' investments in July 2010 also constituted "impairment." But by that point in time, Claimants' investments in KPM and TNG had already been impaired for the previous twenty months.

354. The only question is therefore whether Kazakhstan's acts and omissions were "unreasonable" **or** "discriminatory," either one of which is sufficient for the Tribunal to conclude that Kazakhstan violated the ECT's impairment clause.[559] In reality, Kazakhstan's acts and omissions were both. They were "unreasonable" for the same reasons that they were unfair and inequitable and violated the ECT's requirements for a lawful expropriation. They were discriminatory because they singled out Claimants for differential treatment from other investors in Kazakhstan's oil and gas industry.[560] In particular, no other

[559] *See Azurix* Award, ¶ 391 ("The Tribunal agrees with the interpretation of the Claimant that a measure needs only to be arbitrary to constitute a breach of the BIT. This interpretation has not been contested by the Respondent and it follows from the alternative way in which the term "measures" is qualified by the adjectives "arbitrary or discriminatory."), C-245.

[560] Kazakhstan's conduct as described in Section VII.D also violated the national treatment and most-favored-nation provision of the ECT. Article 10(7) of the ECT provides: "Each Contracting Party shall accord to Investments in its Area of Investors of other Contracting Parties, and their related activities including management, maintenance, use, enjoyment or disposal, treatment no

investors' in-field gathering systems were reclassified as "main" pipelines, and no other investors were subjected to criminal prosecution based on that trumped-up charge.

355. The Vienna Convention mandates that a treaty is to be interpreted according to the ordinary meaning of its terms.[561] The definition of "unreasonable" is "not fair or acceptable." "Reasonable" is defined as "based on or using good judgment and therefore fair and practical."[562]

356. In *Saluka v. Czech Republic*, the tribunal stated that reasonableness requires a state's conduct to bear "a reasonable relationship to some rational policy."[563]

357. In *CME*, the tribunal found the Czech Republic's actions to be "unreasonable" because its acts were unjustified and improper. It stated that

> the determination of reasonableness is in its essence a matter for the arbitrator's judgment. That judgment must be exercised within the context of asking what the parties to bilateral investment treaties should jointly anticipate, in advance of a challenged action, to be appropriate behaviour in light of the goals of the Treaty.[564]
>
> Finding a breach of the impairment clause, the tribunal explained:
>
> On the face of it, the Media Council's actions and inactions in 1996 and 1999 were unreasonable as the clear intention of the 1996 actions was to deprive the foreign investor of the exclusive use of the License under the MOA and the clear intention of the 1999 actions and inactions was to

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less favourable than that which it accords to Investments of its own Investors or of the Investors of any other Contracting Party or any third state and their related activities including management, maintenance, use, enjoyment or disposal, whichever is the most favourable," C-1. Claimants reserve their rights to develop this claim further. *See*, *Pope & Talbot, Inc. v. Canada*, UNCITRAL (NAFTA) Award of 10 April 2001 ("*Pope & Talbot* Award"), ¶¶ 30, 43, 56, 70, 78, C-312; *Marvin Feldman v. Mexico*, ICSID Case No. ARB (AF)/99/1, NAFTA Award of 16 December 2002, ¶¶ 165-166, C-283. *See also*, *Most-favoured nation treatment*, UNCTAD Series on Issues in International Investment Agreements II (United Nations 2010), Executive Summary and at 26, C-284.

561 Vienna Convention, Art. 31(1), C-203; *see BG v. Argentina* Award ¶¶ 340-343, C-268.

562 Definition for "unreasonable," Cambridge Dictionary of American English, C-277.

563 *Saluka* Partial Award ¶ 460, C-259.

564 *CME* Partial Award ¶ 158, C-229.

> collude with the foreign investor's Czech business partner to deprive the foreign investor of its investment.[565]

"Depriving the foreign investor of its investment" was clearly the intention of Kazakhstan's conduct in this case as well.

358. "Discrimination," on the other hand, means "differential treatment; especially, a failure to treat all persons equally when no reasonable distinction can be found between those favored and those not favored."[566] According to Professor A. F. M. Maniruzzaman: "The concept of discrimination entails two elements: first, the measures directed against a particular party must be for reasons unrelated to the substance of the matter .... Second, discrimination entails like persons being treated in an inequivalent manner."[567]

359. As stated by the ICSID Tribunal in *Goetz v. Burundi*: "discrimination supposes a differential treatment applied to people who are in similar situations."[568] Professor Kenneth Vandevelde has further explained that anti-discrimination provisions in BITs prohibit measures that are both "discriminatory in effect as well as those which are intentionally discriminatory."[569] In *Saluka*, the Tribunal held that "the standard of 'non-discrimination' requires a rational justification of any differential treatment of a foreign investor."[570]

360. Kazakhstan's singling out of KPM and TNG for its extraordinary campaign of harassment and coercion between October 2008 and July 2010 was

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[565] *CME* Partial Award ¶ 612, C-229. *See also*, *Saluka* Partial Award ¶ 466 (finding that the Czech Republic impaired the "enjoyment" of Saluka's investment through unreasonable and discriminatory measures), C-259.

[566] Black's Law Dictionary, 7th ed., C-278.

[567] A. F. M. Maniruzzaman, *Expropriation of Alien Property and the Principle of Non-Discrimination in International Law of Foreign Investment: An Overview*, 8 J. TRANSNAT'L L. & POL'Y 57, 59 (Fall 1998) (footnote omitted), C-279.

[568] *Goetz* Award ¶ 121 ("Une discrimination suppose un traitement différencié appliqué à des personnes se trouvant dans des situations semblables ..."), C-227. *See also*, *Nykombs v. Latvia*, at 34 (concluding that Latvia had subjected the Claimant's investment to discriminatory measures consisting of the failure by Nykombs' state-owned local partner to pay it a double tariff, while paying it to two other local companies. The tribunal found that the "three companies are comparable, and subject to the same laws and regulations", that "the burden of proof lies with the Respondent to prove that no discrimination has taken place" and that "such burden of proof has not been satisfied." The Tribunal therefore concluded that Latvia had violated Article 10(1) of the ECT.), C-281. *See also*, *BG* Award, ¶ 356, C-268.

[569] K.J. Vandevelde, UNITED STATES INVESTMENT TREATIES: POLICY AND PRACTICE at 77, C-280.

[570] *Saluka* Partial Award ¶ 460, C-259.

discriminatory, as was its singling out of KPM and TNG for its direct seizures of July 2010. Kazakhstan did not subject other similarly situated investors in its oil and gas sector to such mistreatment, and it did not provide any rational, sensible justification for its conduct.

361. During the harassment and coercion campaign of October 2008 - July 2010, a number of its individual acts were also discriminatory. Most notable was its reclassification of KPM's and TNG's in-field systems as "main" pipelines and criminal prosecutions, fines, and seizures based on that spurious reclassification.

362. In summary fashion, Claimants list below a number of Kazakhstan's acts and omissions that were indisputably "unreasonable" or "discriminatory," and that indisputably impaired Claimants' "management, maintenance, use, enjoyment or disposal" of their investments, in violation of the ECT's impairment clause:

- Kazakhstan's "reclassification" of some of KPM's and TNG's pipelines as "main" pipelines, and the resulting criminal proceedings against, conviction, and incarceration of Mr. Cornegruta, as well as its criminal verdict against the non-party KPM, were clearly unreasonable. There was no "main" pipeline, as later acknowledged by the MEMR itself, and Mr. Cornegruta was not an "entrepreneur" under Kazakh law. Further, KPM was not named as a party to the criminal proceedings in which it was found guilty and sentenced to pay an unreasonable fine that bore no relation to the "main" pipeline transportation fees. KPM's assets were frozen, and it was effectively barred from lodging an appeal against its conviction.
- The reclassification and the resulting criminal proceedings were also discriminatory: KPM and TNG gathering systems alone were subjected to such "reclassifications" and prosecutions, despite the fact that neighboring companies (and operators throughout the country) owned and operated similar (and often larger) pipelines in their in-field gathering systems.
- Kazakhstan's reversal of its prior approval of the transfer of KPM to Terra Raf and of its pre-emptive rights waiver, and its failure to respond to Terra Raf's requests for decisions on those two matters, were plainly unreasonable. They contradicted Kazakhstan's prior approval and assurances and were not based on a rational justification. The uncertainty thereby created impaired Claimants' investments, particularly Claimants' ability to market KPM and TNG and their assets to prospective buyers.

- Kazakhstan's refusal to extend TNG's exploration period in the Contract 302 Properties was unreasonable, because the State expressly agreed to the extension and provided no justification for its refusal to execute the extension. The failure to extend the exploration period prevented Claimants from pursuing exploration and establishing the reserves of the Contract 302 Properties.
- Kazakhstan's treatment of amortization rates was also unreasonable, because it violated express contract terms. This measure resulted in Kazakhstan demanding the payment by KPM and TNG of USD 69 million in back taxes and penalties that were not in fact owed.
- Likewise, the imposition of an export tax was also unreasonable, because KPM's Subsoil Use Contract contained an export tax exemption, and because Kazakhstan's decision of December 24, 2008, stated that the export tax would not be applicable.
- Kazakhstan's unilateral repudiation of KPM and TNG's Subsoil Oil Contracts in July 2010, was exceedingly unreasonable. It was based on spurious alleged violations of the contracts, which KPM and TNG timely explained, responses that Kazakhstan ignored. While Claimants' investments had already been impaired for twenty months by July 2010, the repudiations obviously resulted in the total impairment of Claimants' investments, which were illegally seized.

E. Kazakhstan Failed to Observe Obligations It Entered Into With Respect to Claimants' Investments

363. Article 10(1) of the ECT contains what is known as an "umbrella clause." It provides:

> Each Contracting Party shall observe any obligations it has entered into with an investor or an Investment of an Investor of any other Contracting Party.[571]

364. The ECT's broadly-worded umbrella clause is noteworthy in that it covers undertakings entered into by Kazakhstan with an investor **or** with an investment. That clearly encompasses the obligations Kazakhstan entered into with respect to KPM and TNG, which are two of Claimants' "investments" in this case.

[571] Article 26(3)(c) of the ECT allows the possibility of a contracting state to opt-out of dispute resolution with respect to the umbrella clause, C-1. However, Kazakhstan has not disclaimed its consent as required to opt-out of that part of the Treaty. Consequently, Claimants are entitled to assert this claim.

365. A broadly-worded umbrella clause such as Article 10(1) of the ECT brings *any* obligation of a host state regarding an investment under the protective "umbrella" of the Treaty. It is specifically intended to expand the reach of the Treaty's protections to obligations that are not covered by the Treaty's other substantive provisions. The Readers' Guide to the ECT explains:

> This provision covers any contract that a host country has concluded with a subsidiary of the foreign investor in the host country, or a contract between the host country and the parent company of the subsidiary.
>
> Respect of the international principle of "pacta sunt servanda" is of particular relevance in the energy sector where most major investments are made on the basis of an individual contract between the investor and the state.
>
> Article 10 (1) has the important effect that a breach of an individual investment contract by the host country becomes a violation of the ECT. As a result, the foreign investor and its home country may invoke the dispute settlement mechanism of the Treaty.[572]

366. Additionally, a number of investment treaty tribunals have held that not only contractual obligations, but also obligations undertaken through law or regulation, fall within the scope of an umbrella clause.[573]

367. As the *Eureko v. Poland* Tribunal explained:

> [The Treaty's "umbrella clause"] provides that each Contracting Party "shall observe any obligations it may have entered into with regard to investments of investors of the other Contracting Party." . . . Thus, insofar as the Government of Poland has entered into obligations vis-à-vis Eureko with regard to the latter's investments, and insofar as the Tribunal has found that the Respondent has acted in breach of those obligations, it stands, *prima facie*, in violation of Article 3.5 of the Treaty. . . .
>
> The plain meaning – the "ordinary meaning" – of a provision prescribing that a State "shall observe any obligations it may have entered into" with regard to certain foreign investments is not obscure. The phrase, "shall observe" is imperative and categorical. "Any" obligations is capacious; it means not only obligations of a certain type,

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572 Readers' Guide, page 26, C-264.

573 *See*, *e.g.*, *SGS v. Philippines*, ¶¶ 127-128, C-282; *LG&E* Decision on Liability, ¶175, C-262.

> but "any" – that is to say, all – obligations entered into with regard to investments of investors of the other Contracting Party.[574]

368. The *Eureko* Tribunal stressed that it was obliged to interpret the umbrella clause in a manner that gave it substantive meaning. Relying on the "cardinal rule of the interpretation of treaties that each and every operative clause of a treaty is to be interpreted as meaningful rather than meaningless," the Tribunal stated:

> It follows that the effect of Article 3.5 [the umbrella clause] in this proceeding cannot be overlooked, or equated with the Treaty's provisions for fair and equitable treatment, national treatment, most-favored-nation treatment, deprivation of investments, and full protection and security. On the contrary, Article 3.5 must be interpreted to mean something in itself.[575]

369. Applying this interpretation, the *Eureko* tribunal held that breaches by Poland of its obligations that were not covered by the treaty's other provisions would nevertheless "transgress Poland's Treaty commitment to 'observe any obligations it may have entered into' with regard to Eureko's investments."[576]

370. Similarly, in *Enron v. Argentina*, the tribunal examined the umbrella clause and found that "[u]nder its ordinary meaning the phrase 'any obligation' refers to obligations regardless of their nature. Tribunals interpreting this expression have found it to cover both contractual obligations such as payment as well as obligations assumed through law or regulation."[577]

371. In the present case, Kazakhstan undertook a series of contractual and legal obligations with regard to Claimants' investments, each of which it breached. Kazakhstan's breaches of its contractual and legal obligations have been explained at

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[574] *Eureko* Partial Award, ¶¶ 244, 246, C-260.

[575] *Id*. ¶¶ 248-249.

[576] *Id.* ¶ 250.

[577] *Enron* Award, ¶ 274 (inner quotations omitted) (award partially annulled on separate grounds) (finding a breach of the umbrella clause as a result of breaches of obligations undertaken under both contract and law and regulation in respect of the investment), C-263. *See also*, *LG&E* Decision on Liability ¶ 170 (finding a breach of the umbrella clause and implying that a State may breach the umbrella clause by breaching obligations undertaken under both contract or law), C-262.

length in preceding sections. Consequently, a summary of those breaches suffices her:

- Kazakhstan "reclassified" KPM's and TNG's pipelines as "main" pipelines, in violation of its Law on Oil and its regulations applicable to the construction, safety and operation of in-field and main pipelines.[578]
- Kazakhstan arrested, convicted, and incarcerated Mr. Cornegruta, in violation of general principles of due process and Articles 12, 16 of the Kazakh Constitution recognizing each person's human rights and freedom.[579]
- Kazakhstan issued a criminal verdict against the non-party KPM, froze KPM's assets, and barred KPM from lodging an appeal against its conviction, in violation of general principles of due process and of Article 77(3) of the Kazakh Constitution.[580]
- Kazakhstan approved the transfer of TNG to Terra Raf and waived its pre-emptive rights, and then later rescinded its express approval and waiver;
- Kazakhstan refused to extend TNG's exploration period in the Contract 302 Properties although it had expressly approved that extension, which prevented Claimants from establishing the reserves and potential of that area;

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[578] *See* Section IV.B.3 above.

[579] Article 12 of the Kazakh Constitution provides in relevant part:

1. Human rights and freedoms in the Republic of Kazakhstan shall be recognized and guaranteed in accordance with this Constitution.

2. Human rights and freedoms shall belong to everyone by virtue of birth, be recognized as absolute and inalienable, and define the contents and implementation of laws and other regulatory legal acts.

Article 16 of the Kazakh Constitution provides in relevant part:

1. Everyone shall have the right to personal freedom.

2. Arrest and detention shall be allowed only in cases stipulated by law and only with the sanction of a court or prosecutor of law. The detained person shall be provided with the right to appeal. Without the sanction of a procurator, a person may be detained for a period no more than seventy-two hours.

Article 77(3)(9) of the Kazakh Constitution provides: "No person may be sentenced on the basis of his own admission of guilt." During Mr. Cornegruta's trial, the Prosecutor used as its principal evidence a so-called "confession" that consisted of a June 13, 2008 letter from KPM to the State's Agency for Regulation of Natural Monopolies. Even if one was to consider that this letter constituted a "confession" (which it is not even remotely), the Prosecutor should not have been allowed to rely on the June 13, 2008 letter.

The Kazakh Constitution is available at:

http://www.kazakhstan.orexca.com/kazakhstan_constitution.shtml.

[580] Article 77(3)(4) of the Constitution of Kazakhstan provides that "everyone shall have the right to be heard in court."

- Kazakhstan imposed amortization rates at higher than contractually-agreed rates, despite the fact that the Subsoil Use Contracts contained legal and tax stabilization clauses;
- Kazakhstan failed to abide by an exemption of the Crude Oil Export Tax in KPM's Subsoil Use Contract, despite the fact that the Subsoil Use Contracts contained legal and tax stabilization clauses; and
- Kazakhstan wrongfully and unilaterally repudiated KPM's and TNG's Subsoil Use Contracts, in violation of contract terms.
- Kazakhstan illegally seized Claimants' investments, in violation of Articles 6 and 26 of its Constitution protecting private property.[581]

372. Each of those measures was a distinct violation of the ECT's umbrella clause.

F. Kazakhstan's Failed to Provide Effective Means for the Assertion of Claims and the Enforcement of Rights

373. Article 10(12) of the ECT provides:

> Each Contracting Party shall ensure that its domestic law provides effective means for the assertion of claims and the enforcement of rights with respect to Investments, investment agreements, and investment authorizations.

374. As with other provisions of the ECT on the treatment of the investments, the obligation under Article 10(12) is distinct from customary international law. It is also distinct from (albeit similar to) the concept of denial of justice. As stated by the Tribunal in a Partial Award recently rendered in *Chevron v. Ecuador*, which involved a similarly worded provision:

> The obligations created under [the similarly-worded] Article II(7) overlap significantly with the prohibition of denial of justice under customary international law… Article II(7), however, appears in the BIT as an independent, specific treaty obligation and does not make any explicit reference to denial of justice or customary international law. The Tribunal thus finds that Article II(7), setting out an "effective means" standard, constitutes a lex specialis and not a mere restatement of the law on denial of justice. Indeed, the latter intent could have been easily expressed through the inclusion of explicit language

[581] Articles 6 and 26(3) of the Constitution of Kazakhstan provide: "The Republic of Kazakhstan shall recognize and by the same token protect state and private property." and "No one may be deprived of his property unless otherwise stipulated by a court decision."

> to that effect or by using language corresponding to the prevailing standard for denial of justice at the time of drafting. The Tribunal notes that this interpretation accords with the approach taken in Amto v. Ukraine . . . , which considered the identically worded provision found at Article 10(2) of the Energy Charter Treaty.[582] . . .
>
> [T]he Tribunal agrees with the Claimants that a distinct and potentially less-demanding test is applicable under this provision as compared to denial of justice under customary international law. . . . [A] failure of domestic courts to enforce rights "effectively" will constitute a violation of Article II(7), which may not always be sufficient to find a denial of justice under customary international law.[583]

375. The *Chevron v. Ecuador* tribunal went on to interpret the "effective means" obligation as allowing the Tribunal to examine the state's conduct in individual cases, and not merely the system of laws and institutions in place.[584]

376. The *Chevron* tribunal considered the lack of justice experienced by claimants in Ecuador so grave that it concluded, "It thus falls to the Tribunal to step into the shoes of the Ecuadorian courts and decide the merits of the cases as it determines a fair and impartial judge in Ecuador would have decided the matter."[585]

377. In the present case, the Tribunal need not assess the criminal case against Mr. Cornegruta and KPM *de novo* to determine that the Kazakh court issued decisions against Claimants that a "fair and impartial" Kazakh judge would never have reached. A fair and impartial judge would not have convicted KPM, which was not even named as a party in the criminal proceeding and could not have been, since criminal charges may not be brought against a company under Kazakh law. It would not have convicted KPM and Mr. Cornegruta when KPM had never operated a "main" pipeline, as acknowledged by the State itself in MEMR reports, and when Mr. Cornegruta was not an "entrepreneur" under Kazakh law but merely an employee of KPM. Additionally, a fair and impartial judge would have considered all the evidence before it. The Kazakh judge disregarded multiple expert reports

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582 *Chevron Corporation (USA) and Texaco Petroleum Company (USA) v. The Republic of Ecuador*, UNCITRAL, PCA Case No. 34877, Partial Award of March 30, 2010 ("*Chevron* Partial Award") ¶ 242, C-285.

583 *Chevron* Partial Award ¶ 244, C-285.

584 *Id*. ¶ 247.

585 *Id*. ¶ 379.

from Claimants and based his decision solely on an unfounded and conclusory opinion from a Ministry of Justice employee.

378. Further, a fair and impartial judge would have given KPM the opportunity to defend itself. It would not have confirmed the convictions on appeal and effectively prevented KPM from exercising its right to appeal.

379. The acts of Kazakhstan's courts at issue in this case were deplorable. They clearly violate the Treaty's most constant protection and security clause, its fair and equitable treatment clause, and its impairment clause. They just as clearly violate Article 10(12) of the ECT, which is specifically designed to prevent the travesties of justice that occurred in this case, by ensuring that an investor has an effective means to enforce its legal rights. Claimants had no ability to enforce their legal rights, and Kazakhstan is indisputably liable under the ECT for denying them the ability to do so.

380. The misconduct of Kazakhstan at issue in this case was brazen and deplorable and leaves no doubt that Kazakhstan is liable to Claimants under the ECT and international law. Kazakhstan violated nearly every single one of the principal protections afforded foreign investors under the ECT and international law. To the extent several of those protections are broad and composed of multiple components or have been articulated by tribunals in various ways (most notably the "fair and equitable treatment" and "protection and security" standards), Kazakhstan violated those standards in nearly every way they have been articulated.

381. Kazakhstan's liability to Claimants on so many counts is a direct result of the outrageous nature of its conduct and the variety of ways in which it mistreated Claimants and their investments. As the distinguished members of this Tribunal will appreciate, there are not many investment treaty cases that involve so many discrete, severe acts of coercion, harassment, and indirect expropriation, including a malicious criminal prosecution that involved multiple denials of justice, followed by a categorical outright expropriation of the entirety of a claimant's investments.

382. This case also demonstrates the continuing relevance of several standards of protection for foreign investors that have been somewhat overshadowed in recent years. As many governments have become more sophisticated or subtle in

the manner in which they mistreat foreign investors, international tribunals and scholars have sought to define the outer limits of concepts such as "creeping expropriation" and "fair and equitable treatment." Kazakhstan's conduct in this case was brazen and unsophisticated and poignantly illustrates that international law standards such as "full" or "most constant" "protection and security" remain relevant today.

383. Ultimately, of course, any one of Kazakhstan's violations of the ECT or international law is sufficient to render Kazakhstan liable to Claimants in this case. Nevertheless, it bears noting that Claimants and their investments were mistreated by Kazakhstan in almost every way imaginable.

VIII. COMPENSATION

A. Considerations that Bear on the Determination of the Appropriate Standard of Compensation, the Valuation Date, and the Amount of Compensation

384. Claimants have established several key facts that the Tribunal must consider in determining the proper standard for compensation, the date upon which to value the loss of Claimants' investments, and the amount of compensation owed.

385. First, and most obviously, there is the fact of Kazakhstan's direct expropriation of Claimants' investments. The State's notices dated July 21, 2010 abrogating the Subsoil Use Contracts of KPM and TNG, and the State's subsequent July 22, 2010 physical seizure of Claimants' properties and facilities, constitute a direct expropriation for which compensation is indisputably required, and for which the State has provided no compensation.

386. Second, this direct expropriation was just the State's final act of malfeasance. A lengthy series of unlawful State acts preceded this expropriation, acts that constituted acts of indirect expropriation, and acts that discretely constituted breaches of the ECT's other substantive protections (*e.g*, the ECT's "most constant protection and security" fair and equitable treatment, and impairment provisions). Those acts commenced in earnest on the heels of President Nazarbayev's Ocotber 14, 2008 directive and lasted until the direct expropriation of July 21-22, 2010.

387. Third, Kazakhstan's expropriation of Claimants' investments was unlawful. Kazakhstan's indirect expropriation and ultimate direct expropriation were

in violation of Article 13 of the ECT because they (i) were not "for a purpose which is in the public interest," (ii) were "discriminatory," (iii) were not "carried out under due process of law," and (iv) involved the payment of no "compensation" whatsoever. Kazakhstan's breaches of the ECT's other substantive provisions were also unlawful.

388. Fourth, Claimants have demonstrated that, shortly before the October 14, 2008 commencement of the State's harassment campaign, Claimants received eight indicative offers for the Tolkyn and Borankol fields and related assets, including the LPG Plant, ranging from a high of USD 1.55 billion to a low of USD 621 million. Thus, immediately prior to commencement of the State's concerted campaign of malfeasance, there is a factual record of the actual reaction of willing and able buyers to an offer of a portion of Claimants' investments by a willing and able seller, with each acting at arms length in an open and unrestricted market, without compulsion to buy or sell, and each having reasonable knowledge of the relevant facts.

B. The Tribunal Should Compensate Claimants for All Damages Sustained As a Consequence of Kazakhstan's Breaches of the ECT

389. The Tribunal should determine the compensation that Kazakhstan owes to Claimants for its breaches of the ECT in the first instance by reference to any *lex specialis* in the ECT. The only *lex specialis* standard of compensation found in the ECT is in Article 13, which sets out the conditions with which Kazakhstan must comply in order to lawfully expropriate or nationalize investments (or take measures with similar effect). It provides that any expropriation that complies with Article 13(1)'s other requirements (*i.e.*, the taking is for a public purpose, in accordance with due process of law, and is non-discriminatory), shall be "accompanied by the payment of prompt, adequate and effective compensation," which compensation shall further consist of the following:

> Such compensation shall amount to the fair market value of the Investment expropriated at the time immediately before the Expropriation or impending Expropriation became known in such a way as to affect the value of the

> Investment (hereinafter referred to as the "Valuation Date").[586]

390. While the ECT does not define "fair market value," it is universally defined to mean:

> The price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arms length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts.[587]

391. Accordingly, in the highly unlikely event the Tribunal determines that Kazakhstan's expropriation of Claimants' investments was lawful, Claimants should receive compensation equivalent to the fair market value of their investments.

392. It is Claimants' contention, however, that they have established beyond cavil the unlawful nature of Kazakhstan's conduct. The ECT is silent as to the standard of compensation for unlawful expropriation, just as it is silent as to the standard of compensation for breaches of the ECT's other substantive protections (*e.g*, the ECT's "most constant protection and security," fair and equitable treatment, and impairment provisions). In these circumstances, customary international law fills the *lacuna* and provides the governing rules of compensation.[588]

393. For example, as with the ECT, the BIT at issue in *ADC v. Hungary* was silent regarding the standard of compensation for an unlawful expropriation. The Tribunal held as a consequence that customary international law fills the gap and provides the governing compensation principles:

> Since the BIT does not contain any *lex specialis* rules that govern the issue of the standard for assessing damages in the case of an unlawful expropriation, the Tribunal is

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586 ECT Art. 13 (1), C-1.

587 American Society of Appraisers, *ASA Business Valuation Standards* at 27 (2008) ("ASA Standards"), C-286.

588 *See Kardassopoulos and Fuchs* Award, at ¶¶ 503-505 (applying as "the appropriate standard of compensation" the international law principals set out in *Factory at Chorzów (Germany v. Poland)*, 1928 PCIJ Rep. Series A No. 13 (Sept. 13) ("*Chorzów Factory*", C-165), C-205, and the International Law Commission's ("ILC") draft Articles on Responsibility of States for Internationally Wrongful Acts, Article 36), C-160. *Cf. Petrobart* Award, at 77-78, C-204.

> required to apply the default standard contained in customary international law in the present case.[589]

394. Similarly, with respect to the ECT, the Tribunal in *Kardassopoulos* held that the State's expropriation of equity rights in an oil pipeline facility in Georgia constituted a "classic case of direct expropriation," and that the expropriation was unlawful because it was carried out in violation of the ECT's due process requirement.[590] In its discussion of the appropriate standard of compensation for this unlawful expropriation, the Tribunal applied customary principles of international law, noting that, while both parties agreed that the ECT provided the appropriate standard of compensation in the event of a lawful expropriation, both parties also started their analysis of the appropriate standard of compensation in the event of an unlawful expropriation with the principles set out in *Chorzów Factory*.[591]

395. *Chorzów Factory* set out the now well-established international law principle that a claimant whose investment has been subject to unlawful State action is entitled to compensation by means of, first, restitution in kind or its monetary equivalent, and second, compensation for any additional loss not covered by restitution in kind or its monetary equivalent. The case arose from Poland's unlawful seizure of a factory owned by a German national. According to the Permanent Court of International Justice:

> It follows that the compensation due to the German Government is not necessarily limited to the value of the undertaking at the moment of dispossession, plus interest to the day of payment. This limitation would only be admissible if the Polish Government had had the right to expropriate. . . . [S]uch a limitation might result in placing Germany and the interests protected by the Geneva Convention, on behalf of which interests the German Government is acting, in a situation more unfavourable than that in which Germany and these interests would have been if Poland had respected the said Convention. Such a consequence would not only be unjust, but also and above all incompatible with the aim of [the Convention].

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589 *ADC Affiliate Ltd. v. Hungary* (ICSID Case No. ARB/03/16), Award, Oct. 2, 2006, ¶¶ 481, 483, C-206.

590 *Kardassopoulos* Award ¶¶ 386-390, C-205.

591 *Id.* ¶¶ 502-503.

> The essential principle contained in the actual notion of an illegal act – a principle which seems to be established by international practice and in particular by the decisions of arbitral tribunals – is that reparation must, as far as possible, wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed. Restitution in kind, or, if this is not possible, payment of a sum corresponding to the value which a restitution in kind would bear; the award, if need be, of damages for loss sustained which would not be covered by restitution in kind or payment in place of it – such are the principles which should serve to determine the amount of compensation due for an act contrary to international law.[592]

396. The *Chorzów Factory* standard continues to be cited and followed in contemporary cases.[593] According to the Tribunal in *ADC*, "there can be no doubt about the present vitality of the *Chorzów Factory* principle, its full current vigor having been repeatedly attested to by the International Court of Justice."[594]

397. Articles 31 to 36 of the 2001 Articles on State Responsibility of the International Law Commission (ILC Articles) confirm this standard. Article 31 of the ILC Articles ("Reparation") provides:

> 1. The responsible State is under an obligation to make full reparation for the injury caused by the internationally wrongful act.
>
> 2. Injury includes any damage, whether material or moral, caused by the internationally wrongful act of a State.

398. Article 35 of the ILC Articles ("Restitution") adds:

> A State responsible for an internationally wrongful act is under an obligation to make restitution, that is, to re-establish the situation which existed before the wrongful act was committed . . .

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[592] *Chorzów Factory*, at 47, C-165.

[593] *ADC* Award ¶ 493 ("there can be no doubt about the present vitality of the *Chorzów Factory* principle, its full current vigor having been repeatedly attested to by the International Court of Justice."), C-206. The Tribunal in the recent *Vivendi* Award issued a similar statement: "There can be no doubt about the vitality of [the *Chorzów Factory*] statement of the damages standard under customary international law, which has been affirmed and applied by numerous international tribunals as well as the PCIJ's successor, the International Court of Justice." *Vivendi II* Award ¶ 8.2.5, C-253.

[594] *ADC v. Hungary* ¶ 493, C-206.

399. Articles 36 of the ILC Articles ("Compensation") states:

> 1. The State responsible for an internationally wrongful act is under an obligation to compensate for the damage caused thereby, insofar as such damage is not made good by restitution.
>
> 2. The compensation shall cover any financially assessable damage including loss of profits insofar as it is established.

400. The term "any financially assessable" damage is consistent with the principle of "full" compensation, which is widely accepted in both expropriation and non-expropriation cases. Thus, in a recent non-expropriation case, the Tribunal *LG&E v. Argentina* stated that it "agrees with the Claimants that the appropriate standard for reparation under international law is 'full' reparation as set out by the Permanent Court of International Justice in the *Factory at Chorzów* case and codified in Article 31 of the International Law Commission Draft Articles on Responsibility of States for Internationally Wrongful Acts."[595]

401. These authorities make clear that, under international law, Claimants are entitled to be fully compensated irrespective of whichever ECT breach or breaches the Tribunal may find: "International law requires that damages be sufficient to fully compensate a foreign investor for the harms caused by a host government, regardless of whether they are the result of expropriation or some other breach of law."[596] Thus, in *MTD v. Chile* the Tribunal observed:

> [T]he BIT provides for the standard of compensation applicable to expropriation, "prompt, adequate and effective" (Article 4(c)). It does not provide what this standard should be in the cases of compensation for breaches of the BIT on other grounds. The Claimants have proposed the classic standard enounced by the Permanent Court of Justice in the *Factory at Chorzów*: compensation should "wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that had not been committed." The

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[595] *LG&E Energy Corp. v. Argentina* (ICSID Case No. ARB/02/1), Award, July 25, 2007 ¶ 31, C-314.

[596] Henry Weisburg & Christopher Ryan, *Means to be made whole: Damages in the context of international investment arbitration*, at 172, found in EVALUATION OF DAMAGES IN INTERNATIONAL ARBITRATION, Dossiers ICC Institute of World Business Law (Yves Derains and Richard H. Kreindler eds.) (2006), C-305.

> Respondent has not objected to the application of this standard and no differentiation has been made about the standard of compensation in relation to the grounds on which it is justified. Therefore, the Tribunal will apply the standard of compensation proposed by the Claimants to the extent of the damages awarded.[597]

402. A number of other cases have confirmed Claimants' entitlement to full compensation for Treaty violations other than expropriation.[598] For example, the *Vivendi* Tribunal observed: "Based on these principles, and absent limiting terms in the relevant treaty, it is generally accepted today that, regardless of the type of investment, and regardless of the nature of the illegitimate measure, the level of damages awarded in international investment arbitration is supposed to be sufficient to compensate the affected party fully and to eliminate the consequences of the state's action."[599]

403. Kazakhstan must, therefore, "re-establish the situation which existed" before the wrongful acts, that is, before the commencement of the State's unlawful conduct. Since Claimants are not requesting restitution in kind of their investment, Kazakhstan must pay the monetary equivalent, that is, in the words of *Chorzów Factory*, a sum which would "wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not

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[597] *MTD Equity Sdn. Bhd. v. Chile* (ICSID Case No. ARB/01/7), Award of May 25, 2004, ¶ 238 (footnote omitted), C-258. *See also Duke Energy Electroquil Partners v. Ecuador* (ICSID Case No. ARB/04/19), Award of Aug. 18, 2008, ¶¶ 467-468, C-306 ("The Claimants are correct in stating that the consequences of the breach of an international obligation should be determined by recourse to international law. Under international law, it is well established that the principal consequence of committing a wrongful act is the obligation for the party to repair the injury caused by that act … In the circumstances, the Tribunal considers that the principle of the *Factory at Chorzów* according to which any award should '*as far as possible wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed*' constitutes good guidance. The Tribunal notes that the principle of 'full' compensation has been further codified in Article 31 of the International Law Commission Articles on Responsibility of States for Internationally Wrongful Acts and sees no reason not to apply this provision by analogy to investor-state arbitration.") (footnotes omitted).

[598] *AAPL v. Sri Lanka* (ICSID Case No. ARB/87/3), Award of June 27, 1990, 30 ILM 580 (1991), ¶¶ 87-88, C-255.

[599] *Vivendi v. Argentina* ¶ 8.2.7, C-253. *See also,* C.F. Amerasinghe, *Issues of Compensation for the Taking of Alien Property in the Light of Recent Cases and Practice*, 41 ICLQ (1992) 22, 37-38, ("It is important in all cases to distinguish between unlawful takings of property and lawful takings. In the former what is due is damages. In the latter the alien must be compensated. There is clearly a distinction between the two cases, damages being naturally usually heavier than compensation"), C-163. *See also* D. Bowett, *Claims between States and Private Entities*: *The Twilight Zone of International Law* (1986) 35 CATHOLIC UNIVERSITY LAW REVIEW 929, 938, ("it may be best to refer to compensation as the remedy for a lawful taking or termination of contract and damages as the remedy for an unlawful taking or termination"), C-164.

been committed." In addition, Kazakhstan must pay "damages for loss sustained which would not be covered by restitution in kind or payment in place of it." As quoted above, Article 31 of the ILC Articles explains that this covers "any damage, whether material or moral" caused by the unlawful expropriation. Article 36 of the ILC Articles, in turn, provides that these damages must "cover any financially assessable damage including loss of profits insofar as it is established."

C. The Appropriate Valuation Date Is October 14, 2008

404. It is generally accepted that a damage valuation for treaty-breaching conduct must exclude "any diminution in value attributable to wrongful acts" of the government.[600] This approach accords with the universal principle of law that a wrongdoer should not benefit from his wrong — *commodum ex inuria sua nemu habere debet.* As stated by Judge Brower in *Amoco*: "[N]o system of law sensibly can be understood as intended to reward unlawful conduct."[601] Consequently, as Professors Reisman and Sloane explain:

> The depressing effect on values of threats or acts of nationalization must be ignored in ascertaining the market value of subsequently nationalized enterprises. Valuation in such cases is 'calculated as if the expropriation or other governmental act had not occurred and was not threatened.'[602]

405. Moreover, when faced with an indirect expropriation, in the words of Professors Reisman and Sloane, "the 'moment of expropriation' should be distinguished from the 'moment of valuation.'"[603] Consequently, in the present case, the date when the indirect expropriation identifiably started, after which the market value of Claimants investments inexorably deteriorated as a consequence of the State's harassment campaign, is the proper valuation date. As Reisman and Sloane put it,

> to calculate fair market value on the date of the *last* 'measure tantamount to expropriation' that 'ripened' into a manifest expropriation would be . . . to assess an

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600 *Starrett Housing Corp.* (1984) 4 Iran-US CTR 122, 23 ILM 1090, 1133 and 1137, C-224.

601 *Amoco* Award (Concurring Opinion of J. Brower) ¶ 17 n.22, C-247.

602 W. Michael Reisman & Robert D. Sloane, *Indirect Expropriation and Its Valuation in the BIT Generation*, 74 BRIT. Y.B. INT'L L. 115, 149 (2004), C-230.

603 *Id.*

> investment's value at the very 'moment' when the accretion of unlawful acts of the host state has *so dramatically devalued* the investment as to render it *de facto* expropriated — its 'practical and economic use' having been, by that time, 'irretrievably lost.'[604]

The persuasive reasoning in support of this conclusion deserves full quotation:

> Were the critical moment of expropriation for purposes of valuation set at the date of the *last* of the series of deleterious governmental acts of malfeasance or nonfeasance that 'ripened into a more or less irreversible deprivation of the [investment]', then the fair market value of that investment may well be determined to be substantially less than were the critical moment set at the date of one of the earlier acts. The ironic, indeed perverse, result of that theory would be to reward states for accomplishing expropriation *tranche par tranche* rather than *d'un coup* and to encourage states to accomplish expropriation furtively, either by a creeping or disguised series of regulatory acts and omissions of nebulous legality (creeping expropriation) or by evasion or abdication of the often politically difficult task of establishing an appropriate normative environment for investment (consequential expropriation). Conversely, it would penalize foreign investors for attempting to avoid expropriation and sustain their investments by, *inter alia*, fortifying them with additional capital in the face of measures of nebulous legality. These results would be calamitous . . . contrary to the objectives of BITs, they would encourage foreign investors promptly to resort to compulsory dispute-resolution at an early stage rather than seek to resolve matters amicably through negotiation with the host state — lest the investor risk losing potential compensation as the fair market value of its investment progressively depreciates with each subsequent measure 'tantamount to expropriation.'[605]

406. Under the above-noted principles, Kazakhstan should not be allowed to benefit from its own wrongful conduct between 2008 and 2010 that had the intended effect of degrading the financial condition and market value of Claimants' investments. The 2009 Tristan Oil Ltd. ("Tristan")[606] consolidated financial

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[604] *Id*. at 147.

[605] *Id.* at 146.

[606] Tristan Oil Ltd. was incorporated in 2006 as a special purpose vehicle solely for the purpose of issuing Notes jointly and severally guaranteed on a senior secured basis by KPM and TNG.

statements offer a telling picture of the debilitating effects of the State's harassment campaign on the financial condition of KPM and TNG throughout 2009, as well as the progressively deteriorating market value of the companies.[607]

407. Given the impact of the State's concerted harassment campaign, which constituted a breach not only of the ECT's expropriation proscription but also of the various other treaty protections provided to investors, the proper date for assessing the fair market value of Claimants' investments is October 14, 2008, when the State's misconduct began. Furthermore, October 14, 2008 was the date that the State itself chose to deliberately launch a campaign that had the very intent to devalue Claimants' investments and ultimately nationalize them. Respondent should consequently get no benefit of the doubt regarding the precise date when the State's harassment campaign took the first dollar off of the value of Claimants' investments, and the Tribunal should reject out of hand any such exercise in the parsing of dates.

D. Components of Claimants' Damages Claim

408. In order to analyze and value the damage caused to Claimants by the State's treaty-breaching conduct, Claimants have retained Howard Rosen and Laura Hardin with FTI Consulting as economic experts,[608] and James Latham and Michael Nowicki of Ryder Scott Company L.P. as reserves and geology experts.[609]

409. Using the reserves and geological analysis provided by Ryder Scott, FTI has analyzed Claimants' economic damages in two component pieces The first component, for which a fair market value has been assessed as of October 14, 2008, consists of the properties that were offered in the initial phase of the Project Zenith sale process — the Tolkyn and Borankol fields and their related assets, including the LPG Plant. The second component, for which a prospective valuation has been provided, consists of the Contract 302 Properties together with an enhanced market

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Proceeds from the Notes were used to repay KPM and TNG existing debt, and for KPM and TNG working capital, general corporate purposes, and capital expenditures. *See* Lungu Statement, ¶ 6.

607 *See* discussion *supra* at Section IV.H.

608 The professional qualifications of Mr. Rosen and Ms. Hardin are attached as Appendix B and C respectively to the FTI Report.

609 The professional qualifications of Mr. Latham as primary petroleum engineer, and of Mr. Nowicki as primary geoscientist, are attached as Exhibits 2 and 3 respectively to Expert Report of Ryder Scott Company, L.P. (the "Ryder Scott Report").

value of the LPG plant based on profits that could have been earned if the potential gas volumes from the Contract 302 Properties were available to feed the plant.

1. Claimants' Damages Relating to the Tolkyn Field, Borankol Field, and the LPG Plant

410. The calculation performed by FTI for the Tolkyn field, Borankol field, and LPG plant is a straightforward exercise in determining the fair market value, or "enterprise value," of these investments. The producing oil and gas properties in the Borankol and Tolkyn fields are susceptible to standard income and market valuation approaches because both fields are mature and have extensive production histories. FTI calculated the Borankol and Tolkyn field fair market value using a discounted cash flow ("DCF") approach,[610] a calculation that employs well-recognized valuation tools that are no doubt familiar to this Tribunal. For the LPG plant, which was in the final stages of construction when it was expropriated, FTI calculated the fair market value on a cost basis.[611] The cost basis approach is inherently very conservative because it provides only a statement of Claimants' actual lost investment in the design and construction of the facility, and does not reflect any value attributable to Claimants' loss of the opportunity to earn profits from the operation of the facility.

a. FTI's Valuation of the Borankol and Tolkyn Fields

411. In performing its primary market valuation of the Borankol and Tolkyn fields using an income, or DCF, approach,[612] FTI relied on Ryder Scott's

- projected 2P reserves estimates for the fields;[613]
- projected annual production for the Borankol field from 2008 to 2022 based on the duration of Contract No. 305 and information that was available as at October 14, 2008;[614]

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610 *See* FTI Report, at ¶¶ 2.1, 9.9-9.94.

611 *See* FTI Report, at ¶¶ 2.1, 13.1-13.4.

612 FTI's DCF analyses of the fair market value of the Borankol and Tolkyn fields are contained in sections of 11 and 12 respectively of FTI's Report.

613 FTI Report ¶¶ 11.1 (Borankol), 12.1 (Tolkyn). 2P Reserves are defined by the Society of Petroleum Engineers as hydrocarbon accumulations that are both "Proved and Probable." FTI Report fn. 48.

614 FTI Report ¶ 11.2.

- projected annual production for the Tolkyn field from 2008 to 2018 based on the duration of Contract No. 210 and information that was available as at October 14, 2008;[615] and
- drilling, completion, and recompletion schedules for the fields for the purposes of projecting future capital expenditures.[616]

412. For its revenue calculations, FTI established certain future prices for the Borankol field crude oil and natural gas, and the Tolkyn field gas condensate and natural gas.[617] For the Borankol crude oil, FTI calculated future prices by comparing the historical correlation of Urals crude (the price applicable to Borankol's crude) to Brent crude between 1997 and 2008, and then applied that historical correlation to the available Brent Futures Curve to derive a Urals futures curve (which is not publically available).[618]

413. For future prices of gas condensate, which Claimants sold at Brent crude oil prices, FTI used the Brent Crude Oil Futures Curve as of October 2008 and applied the average annual USD prices per barrel to Tolkyn production.[619]

414. For future prices of natural gas, FTI based its calculation on the evidentiary record that indicated that but for the State's interference, Claimants would have been able to sell their gas under the terms of a negotiated 2008 agreement that provided for (1) the sale of certain volumes of gas to KazAzot first at near market prices followed by the international market price after two years; and 2) the export of certain volumes of gas at international market prices through KazTransGas.[620]

415. For its calculation of future capital expenditures over the relevant time periods, FTI calculated the average cost of new wells by reviewing historical capital

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615 FTI Report ¶ 12.2.

616 FTI Report ¶¶ 11.3 (Borankol), 12.3 (Tolkyn).

617 Borankol field principally produces oil, but also produces certain quantities of natural gas, and Tolkyn is a large natural gas field that also produces a significant amount of gas condensate. *See* FTI Report ¶ 6.2.

618 FTI Report ¶¶ 11.12-11.13.

619 FTI Report ¶ 12.9.

620 *See* Lungu Statement, ¶¶ 19-22; discussion *supra* at ¶¶ 57-61; FTI Report ¶¶ 5.21-5.34.

expenditures by Claimants in the two fields.[621] For recompletion costs, FTI relied on Ryder Scott input regarding historical recompletions to calculate an average cost to recomplete the existing wells.[622]

416. FTI modeled operating expenditures for the relevant time periods as two components, fixed costs and variable costs. FTI reviewed total variable costs to total barrels of liquid and gas produced to calculate a per barrel variable operating cost, and assumed the individual average of KPM's and TNG's 2007 and 2008 reported operating expenses as a reasonable basis for future fixed and variable operating costs for the Borankol field and Tolkyn fields respectively.[623]

417. With respect to depreciation for tax purposes, which varies by type of fixed asset, FTI applied the various depreciation rates to the beginning-of-period's remaining balance of the categorized fixed asset investments for Borankol and Tolkyn.[624] For its calculation of future tax liabilities, FTI took into consideration the tax stability clauses in Contracts Nos. 305 and 210, and applied the contractually proper provisions of the 1995 Kazakh tax code pertaining to applicable taxes.[625]

418. Using these assumptions, and applying a discount rate adjusted for inflation of 13%,[626] FTI calculated the following enterprise values for the Borankol and Tolkyn fields before the application of pre-award interest: (1) Borankol field -- USD 193 million,[627] and (2) Tolkyn field -- USD 561 million.[628]

b. FTI's Valuation of the LPG Plant

419. FTI has applied the book value of the LPG plant as a proxy for fair market value.[629] FTI viewed this as the most appropriate valuation methodology under the circumstances because "the value of the LPG Plant, assuming the use of

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621 FTI Report ¶¶ 11. 5-11.11 (Borankol), 12.4-12.6 (Tolkyn).

622 FTI Report ¶¶ 11.10 (Borankol), 12.6 (Tolkyn).

623 FTI Report ¶ 11.27.

624 FTI Report ¶¶ 11.28-11.29 (Borankol), 12.12 (Tolkyn).

625 FTI Report ¶¶ 11.30-11.41 (Borankol), 12.13 (Tolkyn).

626 FTI's analysis of the basis for its discount rate is discussed in detail in paragraphs 11.43-11.67 of the FTI Report.

627 FTI Report ¶ 11.68.

628 FTI Report ¶ 12.16.

629 FTI Report ¶¶ 13.1-13.4.

Borankol and Tolkyn field volumes only, is less than the book value of assets which is the total incurred capital expenditures of the LPG as at the Valuation Date."[630] This approach is inherently very conservative because it does not provide a value for Claimants' lost opportunity to earn profits from the use of the LPG Plant upon its completion.[631]

420. FTI used the net book value of the LPG plant as reflected in the Tristan Consolidated Financial Statements as at September 30, 2008, which was USD 208.5 million.[632]

2. Claimants' Damages to the Contract 302 Properties and the Consequent Additional Lost Value From the LPG Plant

421. The damages calculation for the Contract 302 Properties, and the enhanced market value of the LPG plant based on profits that Claimants could have earned if allowed to process the potential gas volumes from the Contract 302 Properties, presents a greater valuation challenge. The Contract 302 Properties consist of six resource areas. Two of the areas, the Tabyl and the Munaibay, had successful test wells drilled in them by Claimants and are classified by Claimants' reserves expert, Ryder Scott, as contingent resources.[633] The remaining four areas, the Tabyl West, Munaibay North, Bahyt, and Interoil Carboniferous Reef, had seismic work done in them and a test well drilled in the Bahyt area, although the test

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630 *Id.*

631 As explained by FTI, "[i]t is our understanding from discussions with the Claimants that their original intention was to run the LPG Plant at full capacity based on additional volumes that they would obtain from the Contract 302 Properties and from other local producers of gas. It is our further understanding that the Former General Director of TNG held preliminary discussions with gas producers in nearby gas fields at Kazahturkmunay and Prorva, although a final agreement was not signed." While evidence is unavailable as to what the cost per 1,000 cubic meters would have been for these additional volumes of gas, FTI nevertheless points out that third party gas volumes were being produced in close proximity to the LPG plant, and that this third party gas would have contributed to the value of the plant if a reliable estimate of future pricing arrangements for receipt of this additional gas could be derived. However, in the absence of this evidence, FTI did not assume a "full capacity" scenario.

632 FTI Report ¶ 13.4.

633 *See* Ryder Scott Report, at p. 5 *and* Exhibit No. 4, p. 7. Contingent resources "are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from ***known accumulations***, but the applied project(s) are not yet considered mature enough for commercial development due to one or more contingencies. . . . Contingent resources are further categorized in accordance with level of certainty associated with the estimates and may be sub-classified based on project maturity and/or characterized by their economic status." *See* Ryder Scott Report, at p. 5.

well had not yet been drilled deep enough to test the potential Artinskian Dolomite reservoir.[634] These latter four areas are classified by Ryder Scott as prospective resources.[635]

422. Claimants spent approximately USD 43 million conducting exploratory work on the Contract 302 Properties,[636] including the drilling of the test wells and the acquisition of seismic data. With their exploration program still in progress, Claimants did not offer the Contract 302 Properties in the initial phase of the Project Zenith sale process in 2008, and offered the properties in the second phase of the Project Zenith sale process in 2009 only on the condition that the price for the properties be set following completion of Claimants' exploratory work and proof of reserves. In short, Claimants had no interest in selling the Contract 302 Properties until they could prove the reserves and realize the full value for their investments. The State's actions here deprived Claimants of both the opportunity to fully prove the Contract 302 Properties' reserves, and, by ultimate expropriation, to realize any value for the properties at all.

423. In Dr. Ripinsky and Mr. Williams' treatise on *Damages in International Investment Law*, they summarized general principles of loss of opportunity as follows:

> Where a tribunal cannot accept a claim for lost profits as not sufficiently certain, it may choose to award, instead, a compensation for the loss of business (commercial) opportunity, or for the loss of a chance. This head of damage appears to be a sub-species of lost profits, which is resorted to when the available data does not allow making a more precise calculation of lost profits. The concept of the loss of opportunity, or the loss of a chance, is recognised in a number of national legal systems, as well as in the

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634 *See* Ryder Scott Report, Exhibit No. 4, pp. 8-9.

635 *See* Ryder Scott Report, at pp. 5-6. Prospective resources "are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from ***undiscovered accumulations*** by application of future development projects. Prospective Resources have both an associated chance of discovery and a chance of development. Prospective Resources are further subdivided in accordance with the level of certainty associated with recoverable estimates assuming their discovery and development and may be sub-classified based on project maturity." *See* Ryder Scott Report, at pp. 5-6.

636 *See* FTI Report, at ¶ 6.21.

> UNIDROIT Principles of International Commercial Contracts.[637]

424. In a similar case involving the expropriation of an opportunity to earn future profits for an unproved oil and gas concession, the tribunal in *Sapphire International Petroleum, Ltd. v. National Iranian Oil Company* awarded compensation after making the following observation:

> Since the question concerns the concession of an area which has not yet been prospected and where therefore the presence of oil-bearing beds in commercially workable quantities was and still is today uncertain, the existence of damage is not without doubt. No one today can affirm that the operation would have been profitable, and no one can deny it. But if the existence of damage is uncertain, it is nevertheless clear that the plaintiff had an opportunity to discover oil, an opportunity which both parties regarded as very favourable. Does the loss of this opportunity give the right to compensation? It is not necessary to prove the exact damage suffered in order to award damages. On the contrary, when such proof is impossible, particularly as a result of the behaviour of the author of the damage, it is enough for the judge to be able to admit with sufficient probability the existence and extent of the damage.[638]

425. The *Sapphire International* tribunal noted that the claimant had submitted expert geological analysis of the oil and gas prospect that made "it possible to affirm that there is a very strong chance, but not a certainty, that deposits of commercially workable oil exist in the concession area."[639] The tribunal further posited:

> Another factor to be considered is that NIOC, who certainly have an extensive documentation available and possess great experience, would not have made a concession of an area where they did not think that there was a serious chance of discovering oil. It is reasonable to suppose that they would not have required a minimum investment of $U.S. 8,000,000 from a company if they did not think that these investments had a serious possibility of being turned

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[637] Ripinsky and K. Williams, *Damages in International Investment Law* (BIICL, 2008) at p. 291, C-307; UNIDROIT Principles of International Commercial Contracts Art. 7.4.3(3) (2004), *available at* http://www.unidroit.org/english/principles/contracts/main.htm, C-120.

[638] *Sapphire Int'l Petrol. Ltd. v. Nat'l Iranian Oil Co.*, Arbitral Award (Mar. 15, 1963), at 187-88, C-308.

[639] *Id.* at 188.

> to a profit, of which they and the Iranian Government would take the largest share.[640]

426. As in *Sapphire International*, where a minimum exploration investment of USD 8 million was contractually required by the Iran, a minimum work program for exploration and production testing operations was required of Claimants by Kazakhstan under the terms of Contract No. 302.[641] The Contract No. 302 minimum work program investment was USD 27,300,000.[642] And as in *Sapphire International*, Kazakhstan would clearly not have granted Contract No. 302, with its sizable minimum work program budget, if it did not know the seriousness of the prospect.

427. However, unlike *Sapphire International*, where the claimant had spent USD 1,018,932 on actual prospecting work,[643] only a fraction of the contractual minimum exploration budget under the concession, Claimants here spent approximately USD 43 million in their exploration work, significantly more than the minimum exploration budget in Contract No. 302. Furthermore, in *Sapphire* the claimant had performed no drilling, no seismic work, and the only bases for assessing the prospect was summarized by the claimants' expert as follows: "[T]he geology of the undersoil should be deduced from the geology of the surface of the concession, from a geophysical survey of the terrain and from the generally known structure of the Middle East." Here, Claimants have already successfully test drilled the Tabyl and Munabai areas, conducted seismic work in the Tabyl West, Munaibay North, Bahyt, and Interoil Carboniferous Reef areas, and commenced a test well in the Bahyt area, that has log data to approximately 3950 meters.[644] The totality of the data available for estimating quantities of hydrocarbons in the Contract 302 Properties is therefore significant.

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640 *Id.* at 189.

641 Contract No. 302, "Section 7. Work Program", C-53

642 *Id.*

643 *Sapphire Int'l*, at 187, C-308.

644 See File: 2.2.3.12.2.1 Well 1 Bahyt dates.las, Ryder Scott accompanying data.

428. The recent case of *Gemplus and Talsud v Mexico* is also instructive regarding the concept of "certainty," which is properly both "*relative and reasonable in its application*".[645] As the tribunal in *Talsud* stated:

> Applying international law to the present case, the Tribunal is influenced by two related factors. First, the Tribunal rejects any argument that because the quantification of loss or damage in the form of lost future profits is uncertain or difficult, that the Claimants should be treated in this case as having failed to prove an essential element of their claims in respect of lost future profits, with the result that their claims for compensation should be dismissed. The Tribunal considers that this approach is not required by the terms of either BIT or international law; and that it would also produce a harsh and unfair result in this case. The Tribunal emphasises that it is here addressing contingent future events and not actual past events; it is seeking to determine not what did or did not happen as past facts but what could have happened in the future. This exercise necessarily involves the Tribunal in assessing whether such future events would have occurred and in quantifying that assessment in money terms, as compensation. It is not always possible for a claimant to prove that a future event could or could not happen with certainty; and a tribunal can only evaluate the chances of such a future event happening. That is not therefore an exercise in certainty, as such; but it is, in the circumstances, an exercise in "sufficient certainty", as indicated by the ILC's Commentary cited above.
>
> Second, the Tribunal is mindful of the fact that the Claimant's evidential difficulties in proving their claim for loss of future profits are directly caused by the breaches of the BITs by the Respondent responsible for such loss. If there had been no such breaches, the Concessionaire would have had an opportunity to restore the project, as originally envisaged; and it could then have been seen, as actual facts, whether and, if so, to what extent the restored project would have been profitable for the Concessionaire and, indirectly, the Claimants. **The Tribunal considers that, as a general legal principle, when a respondent has committed a legal wrong causing loss to a claimant (as found by a tribunal), the respondent is not entitled to invoke the burden of proof as to the amount of compensation for such loss to the extent that it would compound the respondent's wrongs and unfairly defeat**

[645] *Talsud SA v United Mexican States*, ICSID Case No. ARB(AF)/04/4, Award dated 16 June 2010, C-309.

> **the claimant's claim for compensation** - as was indicated in the *Sapphire* award regarding the "behaviour of the author of the damage"…. At this point, confronted by evidential difficulties created by the respondent's own wrongs, the tribunal considers that the claimant's burden of proof may be satisfied to the tribunal's satisfaction, subject to the respondent itself proving otherwise.[646]

429. In the same manner, the Tribunal in *Lemire v Ukraine* stated:

> The Tribunal agrees that it is a commonly accepted standard for awarding forward looking compensation that damages must not be speculative or uncertain, but proved with reasonable certainty; the level of certainty is unlikely, however, to be the same with respect to the conclusion that damages have been caused, and the precise quantification of such damages. Once causation has been established, and it has been proven that the *in bonis* party has indeed suffered a loss, less certainty is required in proof of the actual amount of damages; for this latter determination Claimant only needs to provide a basis upon which the Tribunal can, with reasonable confidence, estimate the extent of the loss.[647]

430. In discussing the requisite certainty required of lost profits calculations in connection with the analogous "new business" doctrine, Professor John Y. Gotanda, a leading scholar on damages in international law, pointed out that the doctrine "should [not] limit a legitimate claim for lost profits. To do so would leave the injured party less than whole, fail to achieve the goal of full compensation, and provide a windfall to the wrongdoer."[648] Professor Gotanda surveys recent case law and arbitral awards and observes that many jurisdictions no longer require that the amount of lost profits be proven with complete certainty; rather, uncertainty alone does not (and should not) bar recovery.

431. These cases and commentators recognize the broad discretion that arbitrators have in awarding damages for serious breaches of international law. This

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646 *Talsud SA v United Mexican States*, ICSID Case No. ARB(AF)/04/4, Award dated 16 June 2010, paras. 13-91 – 13-92, C-309.

647 *Lemire v Ukraine*, ICSID Case No. ARB/06/18, Award dated 28 March 2011, para. 246, C-61.

648 John Y. Gotanda, *Recovering Lost Profits in International Disputes*, 36 G'TOWN J. INT'L LAW 61, 111 (2004), C-62.

is consistent with how compensation issues are addressed in legal systems worldwide.[649]

432. International treaties also provide tribunals with discretion in calculating damages. The UN Convention on Contracts for the International Sale of Goods (CISG) does not provide specific guidelines for the calculation of damages, but instead suggests discretion by mandating that the court or arbitral tribunal "calculate loss in the manner which is best suited to the circumstances."[650] Additionally, the UNIDROIT Principles of International Commercial Contracts explicitly give a tribunal the discretion to set the amount of damages if the claimant cannot establish the amount with sufficient certainty.[651]

433. The Tribunal should account for the following considerations in assessing the full and appropriate amount of damages to be attributed to Claimants' loss of their investment in the Contract 302 Properties as a result of the treaty-breaching conduct of Respondent.

434. The first is the egregiousness of the State's overall conduct in this case. The Tribunal should take note of the State's criminal prosecution, four year prison sentence, and jailing of Mr. Cornegruta on what were transparently ridiculous charges when it determines the totality of the damages to be awarded. The Tribunal should also weigh the State's intimidation of KPM and TNG employees, as well as the climate of fear for personal safety and freedom that the State created with its arbitrary fabrication of jailable offenses and its incessant rounds of global audits and investigations by every agency the State could muster. The State in this case pursued a deliberately cruel campaign of harassment and intimidation, using its governmental powers to fearful effect, all in an effort to devalue Claimants' investments and ultimately nationalize them.

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649 *See generally* Gotanda, *supra* (noting that because the laws of most countries provide little or no guidance, most countries simply give the judge or jury broad discretion to fix damages).

650 Secretariat Commentary ¶ 4, in guide to CISG art. 74, *available at* http://www.cisg.law.pace.edu/cisg/text/secomm/secomm-74.html (last visited Dec. 22, 2009), C-152.

651 *See* UNIDROIT Principles of International Commercial Contracts Art. 7.4.3(3) (2004), *available at* http://www.unidroit.org/english/principles/contracts/main.htm (last visited Dec. 22, 2009), C-120.

435. Second, the Tribunal should consider the potential for spectacularly unjust enrichment of the State. The State now holds both the contingent resources in the Tabyl and Munaibay areas that Claimants' expended the effort and money to establish, and the prospective resources for which Claimants had already conducted seismic work and geological evaluation, including the costly process of commencing a test well in the Bahyt area. These resources combined hold the potential for enormous value. The State should not be permitted to sit on the Contract 302 Properties without appropriate payment until after rendition of an award, and only then to prove the bargain that it illegally acquired.

436. Third, the lack of any intention on the part of Claimants to sell the Contract 302 Properties without fully proving their potential reserves should be considered, as well as the manifest intention of Claimants to prove those reserves. The Claimants' firm belief in the potential for the Contract 302 Properties was reflected not only in their over USD 40 million investment in exploration activities, but also in their over USD 200 million investment in the LPG Plant, which had a design capacity that contemplated significant gas production from the Contract 302 Properties. The State is well aware of the full potential of these Properties, and it is quite evident that the State deliberately delayed the exploration extension to which it had already agreed to prevent Claimants from proving that value.

437. And fourth, while the existing data regarding the Contract 302 Properties is not complete due to the State's misconduct, the relatively significant quantity of data that does exist needs to be put into its proper context. As FTI points out:

> In evaluating properties with contingent and prospective resources, investors often make adjustments to the potential value of a project based on their assessment of various categories of risk related to these properties. The categories of risk include geological and geophysical risks, engineering risks, and commercial risks. The assessment of these factors, particularly relating to engineering and commercial risks, can vary widely depending on the investor, with the assessment of the engineering and commercial risk factors being dependent on the engineering and fiscal wherewithal of a prospective investor. The categories of potential risk factors, however, are not identical for contingent and prospective resources, both of which exist in the Contract 302 Properties. If these risk

> factors were to be applied here, they would therefore need to be properly divided between the contingent and prospective resources. For example, for the contingent resources in the Tabyl and Munaibai areas, there is a discovered and tested hydrocarbon accumulation, and the geological and geophysical risk factors that may be applicable to those contingent resources differ substantially from those that may be applicable to the prospective resources.[652]

438. Given the totality of the circumstances surrounding the State's expropriation and severe mistreatment of Claimants' investments, and the considerations enumerated above, Claimants believe that these various risk factors should not be applied at all in assessing the appropriate damages to be awarded for the 302 Properties. In other words, it is the State, and not the Claimants, who should bear those risks as a consequence of the State's deplorable conduct in this case. However, to the extent the Tribunal disagrees, Claimants believe that very careful and cautious consideration should be given to any application of these factors.

a. FTI's Prospective Valuation of the Contract 302 Properties

439. Ryder Scott provided FTI with three estimations of production for each of the geographical areas covered by Contract No. 302 ranging from low to high. For contingent resources in the Tabyl and Munaibay areas, Ryder Scott labelled its low estimate 1C, its middle estimate 2C, and its high estimate 3C. For the prospective resources in the Tabyl West, Munaibay North, Bahyt, and Interoil Carboniferous Reef, Ryder Scott labelled the three estimates progressively Low Estimate, Best Estimate, and High Estimate. For purposes of its Prospective Valuation, FTI used Ryder Scott's "2C" estimate for the contingent resources, and "Best Estimate" for the prospective resources.[653]

440. Because Claimants believe that application of the various risk factors discussed in paragraph 437 above would be inappropriate in light of the considerations enumerated above, including the States' illegal conduct, on the request of Claimants FTI did not apply any risk factors to the "2C" and "Best

[652] FTI Report, n.242.

[653] FTI Report ¶ 15.6.

Estimate" resource estimations provided by Ryder Scott, and treated these estimates instead as proven reserves.[654]

441. Ryder Scott provided FTI with a development plan for the "2C" and "Best Estimate" resource estimations that included exploratory wells, new production wells, and recompletions for the contingent resources, and new production wells for the prospective resources.[655]

442. FTI estimated the capital costs for the Contract 302 Properties using the Ryder Scott development plant, Claimants' historical drilling costs, and information acquired in discussions with Ryder Scott relating to the costs of exploratory wells and wells drilled deeper than Claimants historical drilling depths.[656]

443. FTI used the same information for prices of crude oil, natural gas, and gas condensate that it had used in connection with their DCF analysis of the Borankol and Tolkyn fields to determine potential revenues from the Contract 302 Properties.[657]

444. Because the Contract 302 Properties have not yet produced and therefore have no operating cost history, FTI used the same estimates for operating costs that it had applied to the Tolkyn field. However, fixed administrative expenditures were reduced by 50% on the assumption that TNG would only incur incremental administrative expenses above the historical TNG fixed administrative expenses.[658]

445. FTI applied the same depreciation methodology that they had applied to the Borankol and Tolkyn fields, and, because the specific tax rates for the Contract 302 Properties will only be known once the Properties are declared commercial, FTI applied the same tax estimation methodology that they had applied to the Borankol and Tolkyn fields.

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654 *Id.*

655 FTI Report ¶¶ 15.8-15.10.

656 FTI Report ¶¶ 15.8-15.13.

657 FTI Report ¶ 15.14.

658 FTI Report ¶ 15.19.

446. Using these assumptions, and applying a discount rate adjusted for inflation of 13%,[659] FTI calculated a prospective value of the Contract 302 Properties before the application of pre-award interest of USD 1,766 million.[660]

b. FTI's Calculation of Additional Lost Value From the LPG Plant

447. FTI conducted a valuation of the LPG plant under the assumption that the plant would process gas not only from the Borankol and Tolkyn field, but also from the Contract 302 Properties. Under this assumption, FTI forecasted cash flows for the plant from a start date of October 1, 2009 (the projected completion date for the plant as of the October 14, 2008 valuation date) to 2022.[661]

448. Ryder Scott provided a forecast of plant utilization, and FTI extrapolated the LPG products for the Contract 302 Properties based on the same factors and assumptions used in connection with the Tolkyn field.[662]

449. The LPG plant was almost complete as of the October 14, 2008 valuation date, with USD 208.5 million in capital expenditures having already been made. TNG's contemporaneous forecast of additional capital expenditure on the plant was USD 24.1 million, which FTI applied over the period October 14, 2008 to September 30, 2009.[663]

450. Because there is no futures market for LPG products, FTI established a futures curve for LPG by correlating the historical spot prices of Propane and Butane with the European Brent crude oil spot prices over the period of January 1997 to September 2008, and then applying this correlation to the Brent crude oil futures pricing curve as of the Valuation Date. By this methodology, FTI calculated a future price for products from the LPG plant.[664]

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659 FTI's analysis of the basis for its discount rate is at paragraphs 11.43-11.67 of the FTI Report.

660 FTI Report ¶ 15.19. The value of the individual properties comprising this total sum is: For the Contingent Properties: Tabyl, $44.384 million (3%); Munaibay, $388.130 (22%). For the Prospective Properties: Tabyl West, $24.587 million (1%); Munaibay North, $41.958 million (2%); Carboniferous Reef, $1,202.974 million (68%); Bahyt, $57.689 million (3%). This same analysis using the un-risked Ryder Scott "3C" and "High Estimate" resource estimations yields a total value of $6.291 billion. *See* FTI Report, fn. 236.

661 FTI Report ¶¶ 16.1-16.3; 16.6.

662 FTI Report ¶ 16.4.

663 FTI Report ¶ 16.6.

664 FTI Report ¶¶ 16.7-16.10.

451. FTI calculated operating expenses and LPG product transportation costs from internal forecasts created by Claimants, used the Kazakh tax code provisions for depreciation of LPG plants to calculate the depreciation rate, and assumed that the plant would be taxed as a legal entity which is not subject to the specific oil and gas tax regime of Kazakhstan in calculating tax liabilities.[665]

452. Using these assumptions, and applying a discount rate adjusted for inflation of 13%,[666] FTI calculated a prospective value of the LPG plant before the application of pre-award interest of USD 334 million.[667]

E. Moral Damages

453. Claimants well recognize the principle that the Tribunal is only to award moral damages under exceptional circumstances,[668] and they do not request such relief lightly here. The malevolent nature of the State's conduct in this case, however, fairly mandates the request. The circumstances surrounding the criminal prosecution and jailing of KPM's general manager have been described in detail above, and the Tribunal should not overlook the State's inhumanity in its treatment of Mr. Cornegruta. Neither should the Tribunal overlook the State's deliberate use of Mr. Cornegruta as an example to intimidate Claimants' personnel, to sew deep concern for his -- and their own -- safety, and to demonstrate the State's unchecked power to imprison at will and without cause. As Mr. Pisica describes the prevailing thoughts upon the swift denial of Mr. Cornegruta's appeal:

> Mr. Cornegruta quickly appealed his sentence and the Mangystau Regional Court swiftly rejected his appeal on November 12, 2009. He was transferred from the temporary detention facility in Aktau to jail in Atyrau to serve his sentence. Kazakh jails do not have a good reputation and we feared for his health, his sanity, and even

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665 FTI Report ¶¶ 16.16-16.17.

666 FTI's analysis of the basis for its discount rate is at paragraphs 11.43-11.67 of the FTI Report.

667 FTI Report ¶ 15.19. The value of the individual properties comprising this total sum is: For the Contingent Properties: Tabyl, $44.384 million (3%); Munaibay, $388.130 (22%). For the Prospective Properties: Tabyl West, $24.587 million (1%); Munaibay North, $41.958 million (2%); Carboniferous Reef, $1,202.974 million (68%); Bahyt, $57.689 million (3%). This same analysis using the un-risked Ryder Scott "3C" and "High Estimate" resource estimations yields a total value of $6.291 billion. *See* FTI Report, fn. 236.

668 *See Desert Line Projects LLC v. Republic of Yemen,* ICSID (W. Bank) Case No. ARB/05/17, Award, ¶ 289 (Feb. 6, 2008) ("Even if investment treaties primarily aim at protecting property and economic values, they do not exclude, as such, that a party may, in exceptional circumstances, ask for compensation for moral damages."), C-136.

> his life. His wife and family obviously also suffered from the separation and the stress associated with his detention.[669]

454. And as Mr. Condorachi describes the reaction to the pointless May 6 raid of Claimants' offices shortly after Mr. Cornegruta's detention:

> On April 27, 2009, the Aktau City Court decided to remand Mr. Cornegruta into custody until May 20, 2009. We tried to obtain his release and offered to substitute jailing with a milder form of control and we offered to post bail. CASCo offered its offices as collateral for Mr. Cornegruta's release on bail. Other local individuals also made bail proposals. Our offers were left unanswered and the requests for release before the courts were denied.
>
> On May 6, 2009, the Financial Police searched the offices of KPM, TNG, and CASCo on the pretense of finding Messrs. Salagor and Spasov, the former General Directors of KPM, and Mr. Cojin, the Director of TNG, as well as information regarding them and Mr. Cornegruta. The General Directors had left Kazakhstan. At the time, I was on holiday in Moldova, but I quickly learned about the over-night search.
>
> By that date, the Financial Police had gathered all the available information regarding the accounting, costs, volumes, and technical aspects for the pipelines, the appointment documents for the directors, the human resources documents, etc. Since the Financial Police had removed most, if not all, of the files it needed through the audits or during that last raid, the on-site visits from the Financial Police decreased substantially. Nonetheless, this raid left the employees all even more scared than before, but we continued to perform our duties as well as possible under incredibly hostile circumstances.[670]

455. The State here used its police powers not only to fabricate criminal offenses from whole cloth, but also to charge and to physically hunt Claimants' personnel, distorting justice to impose a perdurable sense of impending danger. As Mr. Pisica tellingly describes the May 6 raid:

> In another twist, on May 6, 2009, the Financial Police raided KPM's and TNG's offices searching for other General Directors of KPM, Messrs. Salagor and Spasov,

669 Pisica Statement, ¶ 50.

670 Condorachi Statement, ¶¶ 20-22.

> and the General Director of TNG, Mr. Cojin, as well as for information on their whereabouts. The three in-country managers had been charged of the same offense as Mr. Cornegruta. The twelve-hour search started at 4:20 p.m. on May 6 and ended at 4:15 a.m. on May 7. During the entire time, the employees of KPM and TNG had to stand in the corridor in front of their closed offices waiting for the Financial Police to search the premises.[671]

456. And as Mr. Romanosov makes clear, by July 2010, the State had largely succeeded at its task, driving Claimants' key personnel from Kazakhstan out of fear of imprisonment:

> On July 21, 2010, the Prime Minister and his delegation arrived by helicopter. I personally met with the delegation, as I was the only high-level manager remaining in Aktau at the time. The others had left the country in the previous months because they feared they would be arrested as Mr. Cornegruta had been.[672]

457. These are precisely the exceptional circumstances that justify an award of moral damages.

458. It is well accepted that tribunals have the authority to grant an award for moral damages. As stated by Ripinsky and Williams, "[t]here is no doubt that international law also allows compensation for moral damage."[673] The ILC's Special Rapportuer Arangio-Ruiz stated in his 1989 report that "the practice and literature of international law show that moral (or nonpatrimonial) losses caused to private parties by an internationally wrongful act are to be compensated as an integral part of the principal damage suffered . . ."[674]

459. Article 31 of the ILC's Articles on State Responsibility also confirms that injury for internationally wrongful conduct includes moral damages. "2. Injury includes any damage, whether material or moral, caused by the internationally wrongful act of State." The ILC's commentary also makes this point. "International

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671 Pisica Statement, ¶ 44.

672 Romanosov Statement, ¶ 37.

673 Ripinsky and Williams, at 307, C-307.

674 G Arangio-Ruiz, Special Rapportuer, *Second Report on State Responsibility*, A/CN.4/425 & Corr 1 and 1 & Corr 1, II Y.B. Int'l. L. Comm'n. ¶ 9 (1989), C-310.

tribunals have frequently granted pecuniary compensation for moral injury to private parties."[675]

460. While moral damage awards are most often associated with human rights violations, awarded to redress injuries to an individual, they are not unprecedented in international arbitrations.[676] The recent case of *Desert Line v. Yemen* is instructive. *Desert Line* arose out of a dispute over payments for road work conducted for the government of Yemen. Desert Line alleged that its personnel had been imprisoned for four days, harassed by the Yemini military, and threatened and assaulted with artillery by tribal militants.[677] Desert Line claimed that it was entitled to moral damages because: (i) Desert Line's executives suffered stress and anxiety from being intimidated, harassed, threatened, and detained; and (ii) Desert Line's business credit, reputation, and prestige had been tarnished.[678]

461. In analyzing Desert Line's claim, the tribunal noted that investment treaties "do not exclude, as such, that a party may, in exceptional circumstances, ask for compensation for moral damages," and that "[i]t is also generally recognized that a legal person (as opposed to a natural one) may be awarded moral damages, including loss of reputation."[679] With respect to the inherent difficulty in quantifying moral damages, the tribunal stated:

> The Arbitral Tribunal knows that it is difficult, if not impossible, to substantiate a prejudice of the kind ascertained in the present award. Still, as it was held in the Lusitania cases, non-material damages may be "very real, and the mere fact that they are difficult to measure or estimate by monetary standards makes them none the less real and affords no reason why the injured person should not be compensated."[680]

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675 ILC Articles on State Responsibility, Art. 31, cm.16 n.573 (citing *Chevreau* (*Fr. v. U.K.*), Award, Mar. 4, 1930 ("*Chevreau* Award"), 2 R.I.A.A. 1113 (1923); 27(1) Am. J. Int'l. L. 153 (1933); *Gage Case*, Award, ("*Gage* Award"), 9 R.I.A.A. 225 (1903); *Di Caro Case* (*It. v. Venez.*), Award, ("*Di Caro* Case"), 10 R.I.A.A. 597 (1903); *Heirs of Jean Maninat* (*Fr. v. Venez.*), Award, July 31, 1905 ("*Maninat* Case"), 10 R.I.A.A. 55 (1903)).

676 *See* Parish, Nelson, Rosenberg, *Awarding Moral Damages to Respondent States in Investment Arbitration*, Berkeley Journal of International Law, Vol. 29:1, pp. 103-04, 106, C-311.

677 *Desert Line v. Yemen*, ¶¶ 33-34, 166, C-136.

678 *Id.* ¶ 286.

679 *Id.* ¶ 289.

680 *Id.* ¶ 289 (quoting U.S. V. Germany, November 1923, VII RIAA 32, at p. 42, quoted with approval in James Crawford, ILC Articles on State Responsibility, at p. 223 et seq.).

462. Finding that the physical duress exerted on Desert Line's executives was malicious, the tribunal held the government of Yemen was liable "for the injury suffered by the Claimant, whether it be bodily, moral or material in nature."[681] The tribunal awarded USD 15.5 million in compensatory damages, and USD 1 million for moral damages.[682]

463. In the present case, by contrast to *Desert Line* where the period and scope of Yemeni intimidation was limited, Claimants' General Manager was wrongfully imprisoned with a four year sentence, and Claimants' personnel were driven from the Kazakhstan by governmental intimidation and threats of additional imprisonments of key personnel. A substantial award of moral damages is certainly warranted here.

464. Claimants' therefore seek, in addition to their compensatory damages, an award of moral damages in a sum that the Tribunal deems just and proper.

F. Summary of Damages

465. Claimants' compensation claim for damages to their investments in Kazakhstan consists of the following elements:

Fair Market Value of Borankol Field	**USD 193 Million**
Fair Market Value of Tolkyn Field	**USD 561 Million**
Prospective Value of the Contract 302 Properties	**USD 1,766 Million**
Prospective Value of LPG Plant With 302 Property Gas	**USD 344 Million**[683]

466. In addition to the foregoing, Claimants seek the recovery of moral damages in a sum to be determined by the Tribunal.

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681 *Desert Line v. Yemen*, 290.

682 *See* Parish, Nelson, Rosenberg, *Awarding Moral Damages to Respondent States in Investment Arbitration*, p. 109 (converting the award into US dollars), C-311.

683 In the event the Tribunal chooses not to award the prospective value of the LPG Plant with 302 Property Gas, Claimants request an award of the net book value of the LPG Plant, which FTI calculates to be USD 209 Million.

467. Claimants further seek the recovery of the additional interest and penalties on delinquent payments on the Notes issued by Tristan Oil Ltd. that were jointly and severally guaranteed on a senior secured basis by KPM and TNG. The additional interest and penalties on the Notes would not otherwise have been incurred had Tristan been able to make timely payments, payments that now cannot be made as direct consequence of Kazakhstan's expropriation of KPM and TNG.

468. Claimants further request that pre-award interest be applied to the value of each of the separate elements of Claimants' damages claim from October 14, 2008 to the date of the Award at a rate that is appropriate to compensate Claimants for the period of time that they have been deprived of the full value of their investments. Claimants believe that an appropriate pre-award interest rate would be either the Kazakhstan sovereign debt rate or the cost of debt for the Notes guaranteed by KPM and TNG. Claimants will provide a calculation of pre-award interest closer to the date of the merits hearing.

469. Claimants further seek post-award interest (until the date Kazakhstan pays the award in full) at the highest possible lawful rate. As noted by the Tribunal in *Asian Agriculture Products v. Sri Lanka*, "interest becomes an integral part of the compensation itself, and should run consequently from the date when the State's international responsibility became engaged."[684] Because international law recognizes that compound interest is the generally-accepted standard in international investment arbitrations, Claimants further request that any awards of interest granted by this Tribunal be compounded.[685]

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[684] *Asian Agricultural Prods. Ltd. v. Sri Lanka* (ICSID Case No. ARB/87/3), Award, June 27, 1990, ¶ 114, C-255.

[685] *See, e.g., Wena Hotels Ltd. v. Egypt* (ICSID Case No. ARB/98/4), Award of Dec. 8, 2000, 41 ILM 896, 919 ("This Tribunal also has determined that compound interest will best 'restore the claimant to a reasonable approximation of the position in which it would have been if the wrongful act had not taken place.' . . . This Tribunal believes that an award of compound (as opposed to simple) interest is generally appropriate in most modern, commercial arbitrations."), C-216; *Azurix Corp. v. Argentina* (ICSID Case No. ARB/01/12), Award of July 14, 2006, ¶ 440 ("The Tribunal considers that compound interest reflects the reality of financial transactions, and best approximates the value lost by an investor."), C-245; *Vivendi v. Argentina* (ICSID Case No. ARB/97/3), Award of Aug. 20, 2007, ¶ 9.2.6 ("[A] number of international tribunals have recently expressed the view that compound interest should be available as a matter of course if economic reality requires such an award to place the claimant in the position it would have been in had it never been injured."), C-253.

IX. REQUEST FOR RELIEF

470. For the reasons set forth herein, Claimants request an award granting them the following relief:

- a declaration that Kazakhstan has violated the ECT and international law with respect to Claimants' investments;
- compensation to Claimants for all damages they have suffered, as set forth herein and as may be further developed and quantified in the course of this proceeding;
- all costs of this proceeding, including Claimants' attorneys' fees and expenses;
- pre-award interest from October 14, 2008 to the date of the Award;
- an award of interest until the date of Kazakhstan's final satisfaction of the Award; and
- any other relief the Tribunal may deem just and proper.

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