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

CLAIMANTS' FIRST POST HEARING BRIEF

April 8, 2013

KING & SPALDING
Counsel for Claimants

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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 First Post Hearing Brief in this arbitration proceeding against the Republic of Kazakhstan ("Kazakhstan" or "Respondent") under the Energy Charter Treaty ("ECT" or "Treaty") pursuant to Procedural Order No. 10.[1]

I. SUMMARY OF KEY POINTS

2. This First Post Hearing Brief addresses the most salient points from the hearings held in October 2012 and January 2013 and summarizes Claimants' positions on the key factual and legal issues in this case, including the proper quantum of damages to be awarded.[2] Claimants continue to rely upon their previous pleadings and on the witness statements, expert reports, exhibits, legal authorities, and oral argument and testimony previously presented to the Tribunal.

3. This case involves a number of disparate issues, and the record is voluminous and complex. At the same time, Kazakhstan has significantly exacerbated the volume and complexity of the case through repeated instances of procedural misconduct, the most egregious of which occurred in the latter stages. Most notably, Kazakhstan submitted an entirely new case on quantum shortly before the January 2013 Hearing, and it cavalierly attempted to jettison its first quantum report filed with its Statement of Defense. Claimants are therefore in the unprecedented situation of being required to address a new case on quantum in this Post Hearing Brief.

4. Just as remarkably, three weeks ago — well after the January 2013 Hearing — Kazakhstan finally disclosed the four critical valuation and diligence documents that it had deliberately withheld from Claimants and the Tribunal since Procedural Order No. 2 of February 3, 2012. Kazakhstan sheepishly forwarded those documents to Claimants and the Tribunal without so much as an explanation for their delinquent production, and it is now apparent why Kazakhstan violated the Tribunal's production order for so long. As Claimants had surmised, the

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[1] All defined terms in this Post Hearing Brief shall be understood to have the same meaning as in Statement of Claim, Reply on Jurisdiction and Liability, and Reply on Quantum, unless otherwise specified.

[2] The Hearing on Jurisdiction and Liability that took place from October 1-8, 2012, is referred to herein as the "October 2012 Hearing" and the Hearing on Quantum that took place from January 28-31, 2013, is referred to herein as the "January 2013 Hearing."

documents are fatal to significant portions of Kazakhstan's case. Claimants must also summarize their contents, which are voluminous, for the first time in this brief.

5. Due to the volume and breadth of issues to be covered, Claimants begin by summarizing the key points of this dispute. Each of the following points is discussed more fully in the sections that follow.

A. Kazakhstan Has No Case on Jurisdiction

6. Kazakhstan does not have — and never did have — any credible jurisdictional objections. Claimants are indisputably "Investors" who made qualifying "Investments" protected by the ECT.

7. Claimants invested in Kazakhstan through KPM and TNG. According to Kazakhstan's own figures, between 2000 and 2009, Claimants invested US $473 million in KPM and US $693 million in TNG, a total in excess of US $1.1 billion. KPM and TNG also paid over US $350 million in tax revenues to the Kazakh State. KPM and TNG permanently employed nearly 1,000 Kazakh workers, and TNG employed some 3,000 additional contract workers to construct the LPG Plant.

8. Claimants' substantial investments transformed the previously fallow Borankol and Tolkyn fields into significant producers of oil, gas, and condensate. By 2010, Claimants had over 70 operational wells in the Borankol field and a total of 40 wells in the Tolkyn field and Contract 302 area. As of 2008, Claimants had produced 12 million barrels of oil and condensate ("MBbls") and 22 billion cubic feet ("bcf") of gas from the Borankol field, and 11 MBbls oil and condensate and 246 bcf of gas from the Tolkyn field. As a result of Claimants' investments, TNG became the fourth largest gas producer in Kazakhstan.

9. Claimants also invested more than US $240 million in construction of an LPG Plant, which was substantially complete before construction was halted as a result of the State's misconduct. Kazakhstan viewed the LPG Plant as a "strategic asset" for the Mangystau region. Claimants also conducted extensive exploration and production work on TNG's Contract 302 Properties, including drilling the "Munaibay 1" well, shooting 3D seismic, and acquiring a deep drilling rig to explore the considerable "Interoil Reef" prospect.

B. Prior to Nazarbayev's Directive of October 14, 2008, Claimants Experienced No Trouble With the Kazakh State

10. Kazakhstan's case on liability has always suffered from an "elephant in the room" — namely, the simple but telling fact that prior to President Nazarbayev's directive of October 14, 2008, Claimants and their companies had enjoyed eight years of positive, productive relations with the Kazakh Government. That changed abruptly in the weeks following President Nazarbayev's personal instruction to "thoroughly check" KPM and TNG. During the previous eight years, however, Kazakh agencies had routinely inspected and audited the companies' operations and accounts and had consistently given them "clean bills of health."

11. Notably, there had never been any allegation that KPM's or TNG's field pipelines were "main" pipelines, because they obviously were not. And Kazakhstan had taken express positions on other issues that it would directly contradict after October 2008 (and in this case). A simple review of Kazakhstan's change of position before and after October 14, 2008, demonstrates that President Nazarbayev's order caused the harm Claimants suffered in this case.

C. Kazakhstan's Case on Liability Fell Apart at the October 2012 Hearing

12. Prior to the October 2012 Hearing, Kazakhstan's case on liability already faced an uphill struggle. A veritable mountain of documentary evidence, supported by credible statements from Claimants' witnesses, indicated that Kazakhstan had deliberately targeted KPM and TNG with an extraordinary campaign of harassment and coercion. The documentary record clearly indicated that State agencies, led by the executive's Financial Police, had pursued KPM and TNG (and their personnel) on multiple fronts, including trumped-up charges of criminal wrongdoing, which caused immediate harm to Claimants' investments.

13. What remained of Kazakhstan's case on liability imploded at the October 2012 Hearing. Most notably, the Tribunal was left with no doubt that Kazakhstan's "main" pipeline allegation against KPM and TNG — the "hook" upon which Kazakhstan hung its criminal case against KPM's General Director, Mr. Cornegruta and the fine imposed against KPM — was entirely contrived. The testimony of Kazakhstan's witnesses Turganbayev, Kravchenko, A. Rakhimov, and Baymaganbetov, confirmed without a doubt that the criminal process was a sham from beginning to end.

14. The Tribunal learned how the Financial Police settled upon the "main" pipeline allegation, doctored inspection reports to state that KPM and TNG did not have the requisite licenses, and calculated the devastating penalty that would be imposed from illegal operation of a "main" pipeline — all before any Kazakh authority had concluded that KPM or TNG in fact operated a "main" pipeline. In fact, no competent Kazakh regulatory authority ever reached such a conclusion, and Kazakhstan now takes the remarkable position that no regulatory agency is even competent to determine whether a pipeline is main or not.

15. The testimony of Kazakhstan's Minister of Oil and Gas, Mr. Mynbaev, was equally devastating in relation to Kazakhstan's treatment of TNG's Contract No. 302. Minister Mynbaev testified that Claimants were entitled to "count on" the extension of Contract No. 302 that his ministry had granted. He also poignantly failed to explain how Kazakhstan could have terminated Contract No. 302 in July 2010 (as it did) if the contract had, in fact, expired in March 2009.

16. Minister Mynbaev also conceded that KPM and TNG had been in full compliance with their contractual obligations in early 2010, casting serious doubt on Kazakhstan's purported rationale for the direct seizures of July 2010. Mr. Kravchenko put the nails in the lid of that coffin, conceding that the Financial Police had played a direct role in the termination of the companies' Subsoil Use Contracts.

D. Kazakhstan Breached the ECT in Multiple Respects

17. The campaign against Claimants' investments in KPM and TNG that Kazakhstan commenced in the final quarter of 2008 breached the ECT and international law in multiple respects. It clearly entailed indirect expropriation, because it materially interfered with Claimants' ability to manage, use, and dispose of their investments. The measures Kazakhstan adopted — interference with contractual rights, wrongful exercises of administrative and judicial authority, sequestration of the companies' assets and Claimants' shares, assessment of spurious tax penalties, and harassment and persecution of key personnel — all fall squarely within the bounds of indirect expropriation as understood in international law and treaty practice.

18. Kazakhstan's campaign was equally a violation of the ECT's fair and equitable treatment and impairment provisions, as well as its "most constant protection and security" clause. Kazakhstan subjected Claimants' investments in KPM and TNG to severe harassment

and coercion as well as inconsistent and contradictory conduct, and it created an environment that was thoroughly unstable and unpredictable (if not treacherous). Kazakhstan also flagrantly violated due process and committed "denial of justice" in relation to KPM and its general director. At the same time, Kazakhstan's state apparatus, led by the Financial Police, utterly failed to provide legal (and in some cases physical) protection and security to Claimants' investments and personnel, much less the "most constant protection and security" required by the ECT.

19. Kazakhstan also breached key provisions of Claimants' Subsoil Use Contracts. For example, Kazakhstan imposed groundless and extra-contractual tax assessments on KPM and TNG, and perhaps most notably, it terminated those contracts in violation of their termination provisions. Those acts were breaches of the ECT's "umbrella clause."

20. In July 2010, Kazakhstan directly expropriated Claimants' investments by terminating KPM's and TNG's Subsoil Use Contracts and seizing their assets outright. Like the campaign that preceded it, Kazakhstan's ultimate expropriation was thoroughly groundless and illegal. By that point, however, Claimants' investments had already suffered 20 months of indirect expropriation and other mistreatment that clearly violated the standards of protection afforded by the ECT and international law.

E. October 14, 2008 is the Correct Valuation Date, Because Nazarbayev's Directive Resulted in Almost Immediate Harm to Claimants' Investments

21. President Nazarbayev unleashed the forces of the Kazakh State with his directive of October 14, 2008. That is the correct valuation date in this case for at least three reasons.

22. First, Kazakhstan's campaign against Claimants' investments in KPM and TNG, which commenced immediately after the directive, breached the ECT and international law in multiple respects. Kazakhstan is liable for the harms caused by those breaches.

23. Second, Kazakhstan's 2008 campaign materially harmed Claimants' investments almost immediately, and the injuries continued throughout the period. Within days of Nazarbayev's order, the investigations of KPM and TNG, led by the Financial Police, were well underway. On December 15, 2008, the Financial Police had initiated a formal criminal investigation against KPM. Furthermore, on December 18, 2008, the MEMR deliberately leaked false and malicious accusations to the INTERFAX news agency, accusing Claimants of fraud

and forgery, and clouding title to TNG. On the very same day, Credit Suisse contacted Claimants about the story, and it shortly thereafter chose not to proceed with a US $150-175 loan facility as a direct consequence of Kazakhstan's allegations. In early January 2009, the Fitch and Moodys ratings agencies placed Tristan's long-term debt rating on negative watch as a result of the INTERFAX release and the State's criminal investigation of the companies, and a series of downgrades followed in 2009 and 2010 as a direct result of Kazakhstan's illegal actions.

24. Claimants could not operate or manage their companies normally in that devastating environment, yet Kazakhstan's campaign continued and the consequences mounted. Claimants struggled to restart the Project Zenith sales process. Mr. Stati was forced to halt construction of the LPG Plant, as the State's campaign made it too risky to invest additional capital. Vitol opportunistically withdrew from the venture in 2009 and increased Claimants' financial exposure to the subsequent seizure. Claimants had to turn to the Laren loan sharks for emergency financing on disastrous terms. Claimants were unable and unwilling to take the risk of investing increasingly scarce capital to progress drilling and development at Borankol and Tolkyn. Gas-purchasing "middlemen" controlled by the State or its ruling clan either disappeared or refused to post credit, causing Claimants to reasonably conclude that they were too risky to deal with on export contracts.

25. Third, in light of the vicious downward spiral caused and fueled by the State's campaign, October 14, 2008, is the last date on which the Tribunal can assign a value to Claimants' investments that is not diminished by the consequences of Kazakhstan's illegal conduct.

F. The Four Valuation and Diligence Documents that Kazakhstan Withheld from the Tribunal Are Fatal to Kazakhstan's Position on Key Issues

26. Amongst its other procedural misconduct in this arbitration, Kazakhstan deliberately withheld from Claimants and the Tribunal four critical, contemporaneous valuation and diligence documents prepared for and by its state-owned gas company, KazMunaiGas Exploration & Production ("KMG E&P"), after KMG E&P and its advisors had full access to Claimants' data room in the spring of 2009. The four documents are an 89-page valuation of KPM's and TNG's assets performed by the Royal Bank of Scotland ("RBS") in mid-2009; a 182-page financial and tax due diligence report prepared by PricewaterhouseCoopers ("PwC") in

mid-2009; a 384-page legal due diligence report prepared by Squire Sanders with the assistance of Kazakh counsel, in mid-2009; and a 17-page asset valuation prepared internally by KMG E&P in September 2008. Kazakhstan and its counsel withheld the documents from Claimants and the Tribunal throughout the briefing phases and the hearing phase of this case, only disclosing them by email on March 14, 2013 (leaving Claimants and their experts less than one month to review them).

27. It is now clear why Kazakhstan withheld the documents for so long. The documents are fatal to Kazakhstan's position on a number of key issues and demonstrate that Kazakhstan made a number of arguments in this case that it knew were inaccurate. For instance, the RBS, PwC, and Squire Sanders reports each conclude that Contract No. 302 had been extended until March 30, 2011. Additionally, the RBS report, as Claimants correctly presumed, bases its gas pricing assumptions on a scenario in which 80% of all of TNG's gas would be sold on the export market. The RBS report also expressly assumes that Claimants' LPG plant would source gas not only from its Borankol and Tolkyn fields, but also from third parties. Even more fundamentally, the RBS report generally corroborates the valuation work performed by Claimants' experts at FTI, and demonstrates that the valuations of Deloitte GmbH are ridiculously low.

28. For its part, the PwC report establishes that Kazakhstan's US $62 million back tax claim is a red herring. The Squire Sanders report concludes that there was no material issue regarding KPM's share issuance or consent for various share transfers, contradicting several of Kazakhstan's frivolous jurisdictional contentions. It also analyzed the State's baseless pre-emptive rights claim over the Gheso-to-Terra Raf transfer of TNG shares and determined it was "unlikely" the claim had merit.

G. Kazakhstan's Damages Experts Have No Credibility

29. This may be the first treaty arbitration in which a respondent state has attempted to completely abandon its first quantum report filed with its Statement of Defense. Kazakhstan did not merely seek to distance itself from a portion of its first quantum submission; rather, it purported to abandon the entire report of Deloitte TCF. Several weeks before the January 2013 Hearing, Kazakhstan informed the Tribunal that its new experts at Deloitte GmbH did not rely

upon the Deloitte TCF report in any way, that there was no interdependency between the two reports, and that it refused to bring any of the authors of the Deloitte TCF report to the hearing.

30. At the January 2013 Hearing, the mystery surrounding the Deloitte TCF report deepened. Mr. Gruhn of Deloitte GmbH testified that he had not had any contact with Deloitte TCF, did not know who the author of the Deloitte TCF report was, and could not even confirm whether anyone at Deloitte TCF authored the report.

31. For its part, Deloitte GmbH submitted a report that is thoroughly undermined by the contemporaneous RBS Asset Valuation, which Mr. Gruhn and his team had in their possession and clearly reviewed in the process of compiling their report.

32. Those episodes speak volumes about the general credibility of the reports submitted by Kazakhstan's damages experts. But at the level of detail — facts, figures, and evidence — their lack of credibility is even worse. The main "takeaways" from the January 2013 Hearing were that Deloitte GmbH had relied wholesale on the work of Gaffney, Cline, and Associates ("GCA"), and that GCA's work was little more than guesswork. As a consequence, the reports of both sets of experts are inherently unreliable.

33. GCA's conclusions, which serve as the backbone for Deloitte GmbH's production and cost calculations, are barely more than unsupported assumptions. Notably, in violation of accepted treaty practice and Article 5(2)(e) of the IBA Rules on the Taking of Evidence in International Arbitration, GCA failed to provide any back-up data, modeling, or materials to support most of the conclusions in its two reports. Without such information, it is impossible to test GCA's conclusions or undertake any meaningful assessment of their reasonableness or accuracy. The Tribunal has no choice but to conclude that the vast majority of GCA's work is unsupportable. Insofar as Deloitte GmbH relies on GCA — which, again, it does heavily — Deloitte GmbH's conclusions are unsupportable as well.

34. GCA's assumptions are even more suspect because it is obvious that they were chosen to intentionally drive down Deloitte GmbH's valuation of Claimants' investments. The January 2013 Hearing exposed the results-driven nature of GCA's assumptions. GCA front-loaded capital costs, inflated development costs, assumed protracted exploration phases, ignored behind-pipe reserves, and so on in an apparent effort to produce the results its client demanded. To the extent it did not rely upon GCA — which is limited — Deloitte GmbH employed the

same trick, ignoring the RBS Asset Assessment at its fingertips and making outcome-driven assumptions about matters such as the availability of gas export markets and third-party gas to feed the LPG Plant.

H. Claimants' Valuations Are Supported by Contemporaneous, Independent Indicators of Value

35. Claimants' valuations of their investments are fundamentally sound and credible, as demonstrated by the fact that they are supported by multiple contemporaneous valuations performed by sophisticated third parties. Furthermore, they have been "reality-checked" by Claimants' experts — all of whose work is backed up with underlying data and modeling — against other independent indicators of value. The 89-page RBS Asset Valuation of mid-2009, performed with full access to Claimants' data room, clearly supports the main planks of Claimants' valuation. So too do the numerous indicative offers received from sophisticated energy companies during Project Zenith, as well as the arms-length Cliffson transaction of early 2010. FTI has also analyzed the trading prices of comparable companies, the terms of comparable transactions, and the trading value of the Tristan debt — all of which likewise support Claimants' valuation.

36. Indeed, the valuation of Respondent's experts is the lone "outlier" in a sea of evidence indicating that the fair market value of Claimants' investments was within the range calculated by FTI. This is the "elephant in the room" for Kazakhstan's case on quantum. "Everyone else" did not get it wrong, and the Tribunal should disregard the obvious outlier.

I. Enterprise Value is the Appropriate Measure of Damages

37. The "enterprise value" of Claimants' "Investments," KPM and TNG, is the appropriate measure of damages in this case, as it is in most treaty arbitrations involving "investments" in wholly–owned companies established in the host state. "Enterprise value" means the value of the companies' assets without deducting the companies' debts.

38. Kazakhstan's argument that the Tribunal should award "equity value" — *i.e.*, that it should deduct the debts of KPM and TNG — is wrong as a matter of fact and of law. Fundamentally, Kazakhstan's "equity value" argument is wrong because Kazakhstan seized all the assets of KPM and TNG, without assuming or extinguishing their debts. By seizing their

assets, Kazakhstan left KPM and TNG unable to satisfy their debts, and Claimants remain responsible for doing so from the proceeds of any award in this case.

39. The clear terms of the ECT as well as established treaty practice indicate that compensation should include the debts of KPM and TNG, especially in cases such as the present in which Claimants remain responsible for the debts. Indeed, Kazakhstan has conceded that if Claimants remain responsible for the debts of KPM and TNG — which they clearly do — an award of "enterprise value" would be appropriate. An award of "enterprise value" is also necessary to prevent the unjust enrichment of Kazakhstan.

J. The Tribunal Should Award a Significant Sum for Claimants' Lost Opportunity to Drill the Contract 302 Areas, Because That Opportunity Was Lost as a Result of Kazakhstan's Misconduct

40. Claimants have firmly established that Kazakhstan agreed to extend Contract 302 until March 30, 2011, but wrongfully failed to execute the required addendum to the exploration contract. Claimants have also conclusively demonstrated that they were actively in the process of exploring and drilling in the Contract 302 areas in late 2008 and early 2009 — until the State's refusal to execute the addendum and other misconduct stymied their exploration activities — and that they had the intent and the means to continue exploration through March 2011. Claimants were particularly active in relation to the substantial Interoil Reef prospect, in respect of which they had shot and interpreted 3D seismic and acquired a specialized deep drilling rig that was being prepared for transport to Kazakhstan.

41. As a direct result of Kazakhstan's refusal to execute the addendum and its campaign against KPM and TNG, Claimants were prevented from advancing their exploration activities and drilling the wells necessary to determine if hydrocarbons were present in the Contract 302 areas, at what depths, and in what quantities and qualities. The only exception was Munaibay Oil, where sufficient drilling had been completed to confirm a significant discovery. For the other Contract 302 properties, however — including the Interoil Reef — the State's illegal conduct halted exploration prior to the point at which Claimants had obtained all the data necessary for their experts in this case to establish a fair market value. Claimants therefore had no choice but to submit a prospective valuation for the Contract 302 properties (except for Munaibay Oil).

42. The Tribunal should nevertheless exercise its discretion to award a significant portion of the Contract 302 prospective valuation to Claimants under the "loss of opportunity" doctrine. That doctrine exists precisely for situations such as this in which claimants have been unable to demonstrate their losses with greater certainty as a direct result of the host state's illegal conduct. A number of treaty tribunals have relied on the doctrine in circumstances such as the present, and this Tribunal should do the same. Indeed, a failure to do so would reward Kazakhstan for its misconduct.

II. THE TRIBUNAL MUST REJECT KAZAKHSTAN'S JURISDICTIONAL OBJECTIONS

43. No doubt exists that the Tribunal has jurisdiction to decide this dispute pursuant to Article 26 of the ECT. After making a number of jurisdictional arguments in its Statement of Defense, Kazakhstan has abandoned some of its more outlandish objections in its Rejoinder on Jurisdiction and Liability and at the October 2012 Hearing. Nevertheless, its case on jurisdiction remains a shambles.

44. Kazakhstan has now abandoned its argument that jurisdiction was somehow lacking as a result of its retained sovereignty over natural resources under Article 18 of the ECT.[3] Additionally, at the October 2012 Hearing, Kazakhstan failed to maintain its earlier contention that Claimants had not satisfied the three-month "cooling off" period. Claimants will therefore not repeat their demonstration that the parties complied with that requirement, particularly since this proceeding was stayed for three months precisely to avoid any disagreement on that issue.[4]

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[3] *See* Statement of Defense Section 11; *cf.* Rejoinder on Jurisdiction and Liability.

[4] Reply on Jurisdiction and Liability ¶¶ 53-75. It suffices to note that Kazakhstan's only "support" for its claim in its Rejoinder on Jurisdiction that a stay cannot be conflated with a "cooling off" period is a sentence from Kazakhstan's own letter pre-dating the stay of the proceedings and quoted entirely out of context. Kazakhstan deliberately obscured the facts by failing to refer to its own curing proposal, set forth immediately preceding the sentence that Kazakhstan quoted in support of its argument, that "the proceedings be suspended during the three-month period in satisfaction of that jurisdictional requirement." *See* Rejoinder on Jurisdiction and Liability ¶¶ 237-39 and fn 222 (quoting a letter from counsel for Kazakhstan to the President of this Tribunal, January 18, 2011, at 3: "Respondent is prepared to fully brief this issue on Submissions, at the appropriate time directed by the Tribunal. However, taking note of the Tribunal's preference against bifurcation, and to avoid compounding the prejudice that has occurred as a result of Claimants' non-compliance with the treaty, we propose that the Tribunal order Claimants to engage in amicable settlement discussions as required by Article 26 of the ECT, and that the proceedings be suspended during the three-month period in satisfaction of that jurisdictional requirement. We offer this as a practical solution that best serves the interests of the parties notwithstanding the fact that this jurisdictional defect could result in dismissal after full briefing and hearing on

45. Kazakhstan also has abandoned its novel contention that the Russian version of the ECT contains an "ambiguous and thus pathological reference" to the Stockholm Chamber of Commerce.[5] As explained by Claimants in their Reply on Jurisdiction and Liability and the accompanying expert report of Professor Amkhan, Kazakhstan clearly consented to the submission of disputes under the ECT to the Arbitration Institute of the Stockholm Chamber of Commerce.[6]

46. Claimants address the remainder of Kazakhstan's flawed jurisdictional objections in turn.

A. Claimants Are "Investors" under the ECT

1. Kazakhstan's Personal Attacks Against Messrs. Stati Are Unsupported and Irrelevant

47. In its Rejoinder on Jurisdiction and Liability,[7] the accompanying "expert" report of Martha Brill Olcott,[8] and its Opening Presentation at the October 2012 Hearing,[9] Kazakhstan contended that this Tribunal should inquire into the "nature of the claimants seeking protection" and "their general conduct" regarding their foreign investments to determine whether Messrs. Stati qualify as "investors" under the ECT for purposes of this dispute.[10] No legal authority exists reading such additional requirements into Article 1(7) of the ECT. Furthermore, Kazakhstan's expert on international law and the ECT, Dr. Tietje, does not address Professor

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the merits. *See Western NIS Enterprise Fund v. Ukraine,* ICSID Case No. ARB/04/2, Order of March 16, 2006 (finding that the notice period was 'an important element of the State's consent to arbitration' and ordering a suspension of the proceedings to satisfy the six-month waiting period of the applicable treaty).").

5 *See* Statement of Defense, Section 6; Rejoinder on Jurisdiction and Liability, ¶¶ 241-243.

6 *See* Reply on Jurisdiction and Liability, Section II.A; Expert Opinion by Professor Adnan Amkhan Bayno dated May 6, 2012 (hereinafter "Amkhan Opinion") Section 5.3. In response, Kazakhstan only offered unsupported and conclusory remarks that an "irremovable discrepancy" among the various official versions of the ECT rendered the arbitration clause in the ECT non-existent. Rejoinder on Jurisdiction and Liability, ¶¶ 241-43. Kazakhstan's international law and ECT expert, Dr. Tietje, would not even address (much less agree with) Kazakhstan's position in his legal opinion. *See* Legal Opinion of Dr. Chistian Tietje dated August 8, 2012 (hereinafter "Tietje Opinion"). Therefore, Professor Amkhan's expert opinion remains uncontested, and common sense demands that this objection be rejected.

7 Rejoinder on Jurisdiction and Liability ¶¶ 24-46.

8 Expert Report of Martha Brill Olcott dated August 8, 2012 (hereinafter "First Olcott Report") ¶¶ 93-161.

9 Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slides 4-7.

10 Rejoinder on Jurisdiction and Liability ¶ 22.

Amkhan's detailed analysis of the definition of "investor" under the ECT, which stands uncontested.[11]

48. The Tribunal should give no weight to Kazakhstan's tabloid descriptions of Mr. Anatolie Stati as a "puppet" for "political interests" and of Mr. Gabriel Stati as a "playboy" and "hard partier."[12] Those allegations stem from a collection of internet gossip compiled by Kazakhstan's "expert on everything," Martha Brill Olcott.[13] Kazakhstan's personal attacks on Messrs. Stati's reputation and business experience smack of desperation by a party with a losing case.

49. Pursuant to Article 1(7) of the ECT, "Investor … means a natural person having the citizenship or nationality of or who is permanently residing in that Contracting Party in accordance with its applicable law."[14] Claimants Gabriel and Anatolie Stati have demonstrated that they each hold "the citizenship or nationality" of both Moldova and Romania[15] and that Moldova and Romania are Contracting Parties to the ECT.[16] That evidence, which Kazakhstan no longer contests, is the end of the analysis.[17] Therefore, Claimants Gabriel and Anatolie Stati qualify as "investors" under Article 1(7) of the ECT.

2. Kazakhstan's Reliance on Article 17 of the ECT Is Misplaced

50. Kazakhstan improperly seeks retroactively to deny the benefits of the ECT to Ascom under Article 17(1) of the ECT. Article 17(1) provides that a legal entity controlled by nationals of a third, non-Contracting Party and which has no connection to a Contracting Party

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11 Amkhan Opinion ¶¶ 70-86.

12 Rejoinder on Jurisdiction and Liability ¶¶ 31 and 34; Respondent's Opening Presentation on Jurisdiction, slides 4-7; Respondent's Opening Presentation, Tr. October 2012 Hearing, Day 1, 18:12-18; 21:20-24.

13 First Olcott Report ¶¶ 93-161. For instance, Mrs. Olcott accuses Mr. Stati of having stolen information from Upetrom thanks to an engineer who allegedly smuggled out confidential documents to Ascom. *See* First Olcott Report ¶ 129. However, as explained by Mr. Stati during the hearing, had Ms. Olcott followed up the story until it unfolded she would have discovered that "Mr. Tomescu [Socolescu] received apologies and he was proved innocent." Stati Testimony, Tr. October 2012 Hearing, Day 2, 26:19-20. For another instance of unprofessional reliance on internet research, *see* Stati Testimony, Tr. October 2012 Hearing, Day 2, 27:1-4 (where Mr. Stati explains that one source relied upon by Professor Olcott threatened Mr. Stati with extortion before he published false claims of impropriety).

14 ECT art. 1(7), C-1.

15 Anatolie Stati's Moldovan and Romanian identification cards and passports, C-29; Gabriel Stati's Moldovan and Romanian identification cards, C-30; Gabriel Stati's Moldovan and Romanian passports, C-365.

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

17 *Comp.* Statement of Defense Section 8 with Rejoinder on Jurisdiction and Liability ¶¶ 19-23.

may be denied the benefits of ECT protection.[18] Kazakhstan contends that Ascom, a Moldovan company, is controlled by citizens of a "third state," Romania, and that Ascom has no substantial business activity in Moldova.[19]

51. Claimants will not repeat at length all the reasons why Kazakhstan's argument is legally and factually wrong.[20] In summary, Article 17 pertains to the merits of the dispute, not jurisdiction,[21] and can only be exercised prospectively – not retroactively.[22] Kazakhstan failed to invoke Article 17 before it breached the ECT and the present dispute arose.

52. But even if Article 17 were applicable, Ascom is a company incorporated in Moldova,[23] with substantial business activity in that country.[24] Mr. Anatolie Stati, the sole shareholder of Ascom,[25] is a dual Romanian and Moldovan citizen.[26] Both Moldova and Romania are Contracting Parties to the ECT.[27] Therefore, Romania is not a "third state" for the purposes of Article 17 of the ECT.[28] Thus, neither of the cumulative requirements of Article 17 is satisfied.[29]

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[18] Statement of Defense Section 8; Rejoinder on Jurisdiction and Liability ¶¶ 47-61; Respondent's Opening Presentation on Jurisdiction, slide 8. ECT art. 17(1), C-1.

[19] Claimants note that Kazakhstan erroneously asserts that Ascom is controlled by Gabriel and Anatolie Stati. Anatolie Stati is the sole shareholder of Ascom. *See* Rejoinder on Jurisdiction and Liability ¶ 51. Lists of Ascom's Shareholders as at September 2, 2002, October 15, 2008, and February 15, 2010, C-391, C-35, and C-392.

[20] Reply on Jurisdiction and Liability ¶¶ 85-95. Amkhan Opinion ¶¶ 160-85.

[21] Reply on Jurisdiction and Liability ¶ 89; Amkhan Opinion ¶ 183. *See Plama Consortium Limited v Republic of Bulgaria,* ICSID Case No. ARB/03/24, Decision on Jurisdiction, February 8, 2005 (hereinafter "*Plama* Decision on Jurisdiction") ¶¶ 146-51, R-32; *Yukos Universal Ltd. (Isle of Man) v. Russian Federation*, PCA Case No. AA 227, Interim Award on Jurisdiction and Admissibility, November 30, 2009 (hereinafter "*Yukos* Interim Award") ¶ 441, C-360.

[22] Reply on Jurisdiction and Liability ¶¶ 90-2; Amkhan Opinion ¶¶ 162-65. *See Plama* Decision on Jurisdiction ¶¶ 155, 158, 162, 164, R-32; *Yukos* Interim Award, ¶ 456, 458-9, C-360.

[23] Ascom's Certificate of Incorporation, Exhibit C-31; *See also*, Lists of Ascom's Shareholders as at September 2, 2002, October 15, 2008, and February 15, 2010, C-391, C-35, and C-392. *See also*, Letter from B. Paritov, Financial Police, to R. Ibraimov, Financial Police, C-366.

[24] During the October 2012 Hearing, Mr. Anatolie Stati testified that Ascom employed 380 persons in Chisinau before Kazakhstan's misconduct forced him to reduce the number of employees to 111. Stati Testimony, Tr. October 2012 Hearing, Day 2, 3:25-4:8.

[25] Lists of Ascom's Shareholders as at September 2, 2002, October 15, 2008, and February 15, 2010, C-391, C-35, and C-392. *See also* Letter from B. Paritov, Financial Police, to R. Ibraimov, Financial Police, C-366.

[26] Anatolie Stati's Moldovan and Romanian identification cards and passports, C-29.

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

[28] Reply on Jurisdiction and Liability ¶ 94; Amkhan Opinion ¶¶ 172-76. *Plama* Decision on Jurisdiction ¶ 170, R-32; *Yukos* Interim Award ¶¶ 538, 542, 546, C-360. In this respect, Kazakhstan's reliance on the use of "third state" in the definition of "Transit" in Article 7(10)(a)(i) of the ECT to refer to a Contracting Party is also

3. Jurisdiction Over Terra Raf Is Proper

53. In its Rejoinder on Jurisdiction and Liability and the accompanying expert report of Dr. Tietje, Kazakhstan incorrectly argued that this Tribunal does not have jurisdiction over Claimant Terra Raf because the ECT does not apply provisionally to Gibraltar (where Terra Raf is incorporated)[30] and, alternatively, because Gibraltar is not bound by the ECT as part of the European Union, a Contracting Party to the ECT.[31] Both arguments are wrong.

54. Claimants maintain the position expressed in their Reply on Jurisdiction and Liability and in the Expert Opinion of Professor Amkhan:[32] the ECT applies provisionally to Gibraltar pursuant to Article 45(1) of the Treaty.[33] The United Kingdom's ratification of the ECT does not constitute a *de facto* termination of the ECT's provisional application to Gibraltar,[34] because termination of provisional application of the ECT cannot be implied, but instead requires a specific written notification to the Depository. The United Kingdom made no such notification with respect to Gibraltar. The *Petrobart v. Kyrgyzstan* tribunal correctly endorsed this interpretation of the ECT.[35]

55. In his opinion, Dr. Tietje simply criticizes the *Petrobart* tribunal's conclusion, alleging that it "disregards the importance of protecting the sovereignty and interests of states."[36] He provides no support for this perfunctory conclusion aside from a limited reference to the United Kingdom's treaty practice. Dr. Tietje alleges that the United Kingdom's treaty practice since 1967 is not to make a declaration regarding inclusion of an overseas territory at the time of

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misplaced. This Article refers to three states: the originating state, the destination state, and the state through which the Energy Materials and Products are transported. Therefore, the ECT refers to the destination state as a "third state" simply because it is the third of three states mentioned in that Article.

29 Ultimately, the issue is also irrelevant because Ascom is owned and controlled by Mr. Anatolie Stati, whose indirect investments in Kazakhstan are protected under the ECT, regardless of Ascom's "status."

30 Terra Raf's Certificates of Incorporation, March 1, 1999, November 22, 2007, and July 5, 2011, C-32, C-396, C-367.

31 Statement of Defense Section 8; Rejoinder on Jurisdiction and Liability ¶¶ 62-72; Tietje Opinion Section II; Respondent's Opening Presentation on Jurisdiction, slide 8.

32 Reply on Jurisdiction and Liability ¶¶ 96-112; Amkhan Opinion ¶¶ 235-260.

33 ECT art. 45(1), C-1. United Kingdom's declaration under Article 45(1) of the ECT, December 17, 1994, C-34.

34 United Kingdom's instrument of ratification, December 13, 1996, C-370; United Kingdom's Note Verbale No. 2004/184 addressed to the Depository of the ECT, July 27, 2004, R-51.

35 *See Petrobart Limited v. Kyrgyz Republic,* SCC Arb. No. 126/2003, Award, March 29, 2005 (hereinafter "*Petrobart* Award") at 62-3, C-204; *Petrobart Limited v. Kyrgyz Republic,* Case No. T 3739-03, Svea Court of Appeal, April 13, 2006, 13 ICSID REP. 369 (2008) at 376, C-369.

36 Tietje Opinion ¶ 41.

signature of a treaty since such a declaration "would anyway usually have to be reconfirmed at the time of ratification."[37] For whatever reason, the United Kingdom obviously decided to break from that alleged practice at the time it signed the ECT, because the United Kingdom did confirm that the ECT provisionally applied to Gibraltar. The ECT continues to apply to Gibraltar since the United Kingdom did not notify the Depository in writing of termination of provisional application.

56. The ECT also applies to Gibraltar because Gibraltar is part of the European Union, which is a separate party to the ECT.[38] Contrary to Kazakhstan's assertion,[39] the alleged nature of the ECT as a "mixed agreement" is of no import. The relevant factor is that Gibraltar is a European territory, which falls within the Area of the European Union for purposes of the ECT.[40] Gibraltar itself considers that the ECT applies to it on that basis.[41]

57. For the foregoing reasons, Terra Raf is a qualified "investor" under the ECT.[42]

B. Claimants Made Protected "Investments" under the ECT

58. Kazakhstan curiously contends that Claimants have not made investments protected by the ECT because Claimants' investments allegedly do not satisfy an "inherent meaning" of the term "investment" that Kazakhstan purports to find in customary international law.[43] Kazakhstan contends that: (1) Claimants did not make substantial contributions that entailed risk to Claimants themselves; (2) Claimants' investments did not further Kazakhstan's development; and (3) Claimants' investments were not legal or made in good faith. Kazakhstan's allegations are erroneous because they: (1) seek to alter the definition of

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37 Tietje Opinion ¶ 36 (quoting I. Hendry & S. Dickson, BRITISH OVERSEAS TERRITORIES LAW (Hart 2011) at 254) (emphasis added).

38 Energy Charter, Charter Members and Observers, European Community (now part of the EU) and Euratom, C-373.

39 Statement of Defense Section 8; Rejoinder on Jurisdiction and Liability ¶¶ 62-72; Tietje Opinion Section II; Respondent's Opening Presentation on Jurisdiction, slide 8.

40 Reply on Jurisdiction and Liability ¶¶ 108-12; Amkhan Opinion ¶¶ 250-9.

41 Question and Answer No. 1094 of 2008, Gibraltar Hansards of Questions, at 562, C-374.

42 Ultimately, this issue is of little practical consequence. Messrs. Anatolie and Gabriel Stati, Terra Raf's shareholders, are qualified "investors" under the ECT, and their indirect investments in Kazakhstan, through Terra Raf, are clearly protected by the ECT. Thus, while Kazakhstan has failed to demonstrate that Terra Raf is not a protected "investor" and its arguments to that effect should be rejected, the investments of Messrs. Stati made through Terra Raf are protected regardless.

43 Statement of Defense Section 9; Rejoinder on Jurisdiction and Liability ¶¶ 73-108; Tietje Opinion Section I; Respondent's Opening Presentation on Jurisdiction, slides 10-13.

"investment" under the ECT; and (2) are factually wrong, *i.e.*, Claimants' substantial investments clearly satisfy the inapplicable standard that Kazakhstan advocates.

1. The Definition of "Investment" in Article 1(6) of the ECT Applies, Rather Than the Narrower Definition Proffered by Kazakhstan

59. Kazakhstan's argument that Claimants have not made "investments" that are protected by the ECT relies on a purported definition of that term that Kazakhstan draws from the term's "inherent meaning" and customary international law.[44] Kazakhstan again attempts to add requirements to the ECT that are not present in the Treaty. Article 1(6) of the ECT defines the term "investment" broadly as "every kind of asset, owned or controlled directly or indirectly by an Investor," including tangible and intangible assets, a company or business enterprise, shares, equity participation, debt, claims to money or to performance, returns, and any rights conferred by law or contract.[45] Nothing in the ECT or case law involving the Treaty indicates that the ECT's carefully crafted definition of "investment" may be supplanted with a narrower definition allegedly drawn from customary international law. Allegations of vague (and unproven) legal principles cannot override the specific terms of a treaty.

60. The so-called "*Salini* test," a controversial "test" sometimes applied in ICSID jurisprudence (because the ICSID Convention does not define "investment"), does not apply to disputes under the ECT, because the Treaty specifically defines qualifying "investments."[46] Kazakhstan purports to rely upon four cases – two of which are unpublished – for its argument. Yet even in those cases, the tribunals did not strictly apply the "*Salini* test."[47]

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44 Statement of Defense Section 9; Rejoinder on Jurisdiction and Liability ¶¶ 73-108; Tietje Opinion Section I; Respondent's Opening Presentation on Jurisdiction, slides 10-13.

45 ECT art. 1(6), C-1.

46 Reply on Jurisdiction and Liability ¶¶ 114-129. Kazakhstan's reliance on the decisions in *Salini v. Morocco*, *Phoenix v. Czech Republic*, and *Bayindir v. Pakistan* is ironic considering Respondent argues elsewhere in its Rejoinder on Jurisdiction and Liability that "there is no doctrine of precedent in international investment treaty arbitration, each case must be dealt separately in accordance with the particular treaty and particular facts in question." *See* Rejoinder on Jurisdiction and Liability ¶¶ 229, 236.

47 Statement of Defense Section 9; Rejoinder on Jurisdiction and Liability ¶¶ 73-108; Tietje Opinion Section I; Respondent's Opening Presentation on Jurisdiction, slides 10-13. *See Alps Finance and Trade AG. V. Slovak Republic*, UNCITRAL, Award, March 5, 2011, ¶ 241, R-220; Hepburn/Peterson, "Ethiopia prevailed in face of foreign investor's attempt to use investment treaty to sue over ICC arbitral award," in *Investment Arbitration Reporter*, March 4, 2012, R-221; *Pren Nreka v Czech Republic*, commented in *Investment Arbitration Reporter*, vol. 11, 2008, R-222; *Romak S.A. v. Uzbekistan*, PCA Case No. AA280, Award, November 26, 2009, ¶ 207, R-224. The tribunals in these cases merely found that an investment required a certain level of contribution, risk, and duration; the tribunals did not require satisfaction of the other elements of the *Salini* test.

61. The "*Salini* test" is not an international legal standard, even in ICSID jurisprudence. For instance, in its recent decision on jurisdiction and liability, the *Ambiente Ufficio v. Argentina* tribunal held that "the *Salini* criteria, if useful at all, must not be conceived of as expressing jurisdictional requirements *stricto sensu*."[48] At most, the criteria are "guidelines" that may be applied "in a flexible manner" to consider whether an "investment" has been made for purposes of Article 25 of the ICSID Convention.[49]

62. Regardless, the "*Salini* test" debate is irrelevant. Claimants' massive, long-term investments in Kazakhstan satisfy any conceivable definition of "investment" in customary international law.

2. Claimants Made Substantial Investments in Kazakhstan

63. Claimants made substantial, long-term investments in Kazakhstan that significantly benefited the Kazakh economy. Like most major oil and gas exploration projects, Claimants' investments entailed substantial risk.

64. Claimants initially "invested" in Kazakhstan by paying over US $12 million to acquire 100 percent of the shares of KPM and TNG.[50] This is undisputed.

65. Claimants also made substantial post-acquisition "investments." As the MEMR recognized in February 2010, Claimants invested US $473 million in KPM and US $693 million in TNG, a total in excess of US $1.1 billion, between 2000 and the end of 2009.[51] Those amounts exceeded the companies' working program obligations by US $400 million (or 650%) for KPM and US $475 million (or 320%) for TNG.[52] Those funds were spent developing KPM and TNG and their oil and gas fields into successful, productive operations, including shooting

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48 *Ambiente Ufficio S.P.A. and others v. Argentine Republic*, ICSID Case No.ARB/08/9, Decision on Jurisdiction and Admissibility, February 8, 2013 (hereinafter "*Ambiente* Decision on Jurisdiction") ¶ 479, C-726.

49 *Ambiente* Decision on Jurisdiction ¶ 481, C-726.

50 Sale and Purchase Agreements between Gheso and Kainar, Dobro, and Anavi, April 30 and May 3, 2002, C-56 to C-58; Wire transfers from Ascom to Telwin Limited, Testep Enterprises, and Maraday Business, October 28, 1999 to July 18, 2000, C-379; Wire transfers from Ascom to Camestix, November 26 and December 14, 2004, C-382; and Wire transfers from Ascom to TNG and Kaihar, May 31, 2000, C-383. In its Rejoinder on Jurisdiction and Liability, Kazakhstan admitted that Claimants paid US$10.5 million in respect of the shares in KPM and US$1.56 million in respect of the shares of TNG. Rejoinder on Jurisdiction and Liability ¶¶ 117-118; *see also* Squire Sanders Legal Due Diligence Report, July 30, 2009, at 65 and 119-20, C-725.

51 Report of the MEMR on Unscheduled Inspection for KPM, February 6, 2010, Section VII, C-385 and Report of the MEMR on Unscheduled Inspection for TNG, February 5, 2010, Section 9, C-386.

52 Report of the MEMR on Unscheduled Inspection for KPM, February 6, 2010, Section VII, C-385 and Report of the MEMR on Unscheduled Inspection for TNG, February 5, 2010, Section 9, C-386.

and processing 2D and 3D seismic data, completing substantial drilling programs, and constructing modern integrated production and processing facilities from the well-heads to delivery of oil and gas into Kazakhstan's state-owned main pipelines.

66. Claimants' massive investments transformed KPM and TNG's largely fallow fields at the time of Claimants' acquisition into thriving producing properties by the time of Nazarbayev's October 2008 order. As Mr. Stati summarized at the October 2012 Hearing:

> These fields … by definition of the Ministry of Geology of the USSR, held no prospects. The Kazakhstan partners in three years had done almost nothing, and we had very little time left to complete the minimal programme, and we were told by the akim, Mr Kiyinov, that if we failed to complete the minimal programme, the licence may be revoked, so we should be very cautious. … And we were able to actually outperform the programme by some 20% both physically and financially. … We drilled a large number of wells, and we were also referred to as an exemplary operation.[53]

67. Kazakhstan presents no evidence to contradict those plain facts. Instead, Kazakhstan argues that Claimants should not be credited for their post-acquisition investments in KPM and TNG because "[p]ost-acquisition contributions came from Tristan bondholders."[54] That argument is wrong for two reasons. First, Claimants did not conduct the Tristan bond offering until December 2006.[55] By that point, Claimants had already directly invested hundreds of millions of dollars in KPM and TNG through shareholder loans and reinvested earnings, which Claimants chose to reinvest in Kazakhstan rather than distribute as dividends. Second, Claimants likewise "invested" the funds received from the Tristan note offering. Tristan was nothing more than an SPV created to raise funds for Claimants to invest in Kazakhstan, which they did by pledging their entire equity interest in KPM and TNG as security for the notes.

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[53] A. Stati Testimony, Tr. October 2012 Hearing, Day 2, 7:3-8:1. Claimants note that the parties have not yet agreed on corrections to the transcript of the October 2012 and January 2013 Hearings. Therefore, Claimants rely on the currently unedited transcripts but have made some corrections where necessary. Claimants anticipate that the parties may submit agreed, corrected transcripts after the date of this submission; therefore, Claimants reserve their right to fully correct the transcripts from both Hearings.

[54] Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slide 16.

[55] Tristan Indenture, December 20, 2006, C-584.

a. Claimants' Direct Investments in KPM and TNG

68. Claimants initially funded the operations of KPM and TNG through shareholder loans. Article 1(6) of the ECT specifically includes "bonds and other debt of a company or business enterprise" in the definition of "Investment."[56] Additionally, numerous tribunals, such as the tribunals in *Nykomb v. Latvia*, *Link-Trading v. Moldova*, and *Sempra v. Argentina*, have concluded that loans are protected investments under an investment treaty.[57]

69. Claimants also made substantial contributions to KPM and TNG through the reinvestment of earnings. From 2003 to 2008, KPM and TNG earned more than US $465 million in net profits, almost all of which was reinvested in the companies to further develop their productive capacity and infrastructure.[58] Consequently, by the end of 2008, KPM and TNG had nearly US $400 million in retained earnings on their balance sheets.[59]

70. Kazakhstan attempts to disregard Claimants' substantial reinvestment of profits on the spurious ground that "there was little financial contribution which actually came from Claimants themselves."[60] That argument misapprehends basic business principles as well as the protection afforded by the ECT to an Investor's freedom of control over its profits.

71. Article 14(1) of the ECT expressly guaranteed Claimants the right take the profits of KPM and TNG in the form of dividends and spend or invest them as they saw fit.[61] Consequently, when Claimants chose to reinvest those profits back into the companies in hopes of earning even greater profits later — hopes that were dashed when Kazakhstan illegally seized

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56 ECT art. 1(6), C-1.

57 *Nykomb Synergetics Technology Holding AB v. Latvia*, SCC (ECT), Award, December 16, 2003 ¶ 2.1, C-281; *Link-Trading Joint Stock Co. v. Moldova*, UNCITRAL, Award on Jurisdiction, February 16, 2001, at 8, C-339; *Sempra v. Argentina*, ICSID Case No. ARB/02/16, Award, September 28, 2007 ¶¶ 214-15, C-265.

58 Financial Statements of KPM and TNG, at F-44 and F-78 (2003-2005), C-707; Financial Statements of KPM and TNG, at F-77 and F-100 (2006), C-706; Financial and Operating Data attached to 2007 Tristan Annual Report, at F-73, F-109 (2007), R-37.4; Financial and Operating Data attached to 2008 Tristan Annual Report, at F-69, F-105 (2008), R-37.5.

59 Financial and Operating Data attached to 2008 Tristan Annual Report, at F-70 and F-106, R-37.5.

60 Rejoinder on Jurisdiction and Liability ¶ 124.

61 Article 14(1) of the ECT expressly guarantees the freedom of Investors to transfer "Returns" out of Kazakhstan. Article 1(9) defines "Returns" to mean: "the amounts derived from or associated with an Investment, irrespective of the form in which they are paid, including profits, dividends, interest, capital gains, royalty payments, management, technical assistance or other fees and payments in kind." ECT arts 14(1) and 1(9), C-1.

the companies' assets — Claimants invested those monies in KPM and TNG. It is precisely for situations like this case that the ECT's definition of "Investment" expressly includes "Returns."[62]

b. Claimants' Investments of the Tristan Loan Proceeds

72. Claimants also financed KPM and TNG in part through third-party loans. Kazakhstan argues that this financial structure deprives the Tribunal of jurisdiction because it shielded Claimants from risk in relation to their investments in KPM and TNG. Kazakhstan's arguments are factually and legally meritless. The Tristan loan structure did not insulate Claimants from the risks of investing the loan proceeds.

73. KPM and TNG initially obtained third-party debt financing from a Kazakh bank, Kazcommerzbank. The balance on those loans varied over time and was approximately US $145 million at the end of 2006.[63] Thus, at the time of the initial Tristan note offering, KPM and TNG were financed with a mix of equity contributed by Claimants (including reinvested earnings and shareholder loans, which are economically similar to equity) and third-party bank debt.

74. In 2006, Claimants refinanced the debt portion of KPM and TNG's capital structure through the Tristan note offering. As Ascom's Chief Financial Officer, Artur Lungu, testified, Claimants pursued that transaction in order to increase the available credit line and to obtain better credit terms.[64] Claimants structured that note issuance through a single note offering by Tristan, rather than having KPM and TNG issue the notes directly, because that reduced transaction costs and allowed Claimants to present the assets of both companies as a single "package of guarantees" in order to make the notes more attractive to investors.[65]

75. Although issued by Tristan, the notes were secured entirely by the assets of KPM and TNG and pledges of Claimants' equity interests in KPM and TNG. The respected investment bank Jeffries underwrote the note offering, which, along with its legal advisors from White & Case, conducted significant due diligence on the companies.[66] The initial purchasers of the notes, which totaled US $300 million in December 2006 plus an additional offering of

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62 ECT art. 1(6), C-1.

63 Audited Financial Statements of KPM and TNG, at F-124, C-706.

64 Lungu Testimony, Tr. October 2012 Hearing, Day 1, 195:9-17.

65 Lungu Testimony, Tr. October 2012 Hearing, Day 1, 195:18-196:17.

66 Lungu Testimony, Tr. October 2012 Hearing, Day 1, 196:18-197:11.

US $120 million in June 2007, included many large institutional investors such as UBS and Goldman Sachs.[67] In short, the Tristan note offering was a normal public debt offering in which sophisticated investors examined the business and financial status of KPM and TNG and found them worthy of a substantial extension of credit.

76. That fact belies Kazakhstan's argument that Claimants themselves had no valuable "investments" in KPM and TNG. Large institutional investors of course would not loan US $420 million to finance KPM and TNG if that were the total value of the businesses. Rather, such investors would (and did) ensure that the businesses had a significant "equity cushion" to support that amount of debt. The fact that large institutional investors purchased the notes indicates that the market believed Claimants held very substantial and valuable investments in KPM and TNG.

77. Moreover, at all times Claimants' investments in KPM and TNG remained at risk. Claimants Terra Raf and Ascom pledged their entire equity interests in KPM and TNG to the Tristan noteholders as security for the notes. Furthermore, the pledge agreements expressly provided that if Tristan defaulted, the noteholders were:

> entitled to receive and apply any and all dividend and other payment or distribution of any kind relating to the Participatory Interest as if the Pledgeholder were the holder of the Participatory Interest in and towards discharge of the Secured Obligations until such time as the Secured Obligations are fully discharged...[68]

Thus, the pledge agreements obligated Ascom and Terra Raf to provide <u>any payments of any kind</u> that they received as a result of their investments in KPM and TNG to the Tristan noteholders in the event of default, which would include any payments that Ascom and Terra Raf receive through this arbitration.

78. Claimants' pledge of their entire equity interests in KPM and TNG, and of any monies that Ascom and Terra Raf received in relation to those investments, are themselves "investments" under the ECT. Under Article 1(6) of the ECT, "investment" is defined in a broad

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[67] Expert report of Klepikova regarding the bonds, November 18, 2011, R-37.2. Tristan Oil also issued an additional US $111.1 million in notes in June 2009 in order to secure emergency bridge financing (*i.e.*, the "Laren transaction"), as a direct result of Kazakhstan's illegal actions. Second Witness Statement of Artur Lungu ¶ 10.

[68] *See* Ascom and Terra Raf Pledge Agreements § 6, C-585.

way, and expressly includes "pledges."[69] Even if one engrafts onto the definition of "investment" the additional "*Salini* test" requirements that Kazakhstan proffers — namely, substantial contribution, risk, duration, and benefit to the host State — the pledges easily qualify. They are substantial contributions to KPM and TNG in the form of legal obligations that enabled KPM and TNG to raise hundreds of millions of dollars from the Tristan noteholders. Those contributions entailed substantial risk, namely, Claimants' risk of losing their entire equity stakes in KPM and TNG and any payment received through arbitration. Those contributions had a lengthy duration; Claimants entered into the Pledge Agreements in 2006, and they remain in force today. And the contribution benefited Kazakhstan, because it enabled KPM and TNG to raise hundreds of millions of dollars to finance operations that provided jobs to hundreds of Kazakh citizens and significant tax revenues to the Kazakh treasury.

79. An analogous situation was presented in *Enron v. Argentina*. In that case, Enron financed its capital contribution to its Argentine operating company, TGS, through a combination of its own capital injection and a loan by Chase to an Enron-controlled holding company, CIESA, which used the loan proceeds to meet TGS's capital funding requirements. Enron guaranteed CIESA's repayment of the Chase loan, similar to the pledges that Claimants executed in favor of the Tristan noteholders. The *Enron* tribunal correctly observed that such a guaranty should effectively be treated as part of the investment, noting that "[s]uch practice will as a rule not affect the determination of the value of the shareholding for compensation purposes. In fact, because the parent company shall normally be liable for such debt, it would be entitled to recover the entire equity interest" (*i.e.*, without deducting the debt in valuing the equity stake).[70] The *Enron* tribunal in no way suggested that the existence of such a debt structure raised any issues regarding its jurisdiction over Enron's claims — which, of course, it did not.[71]

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[69] ECT art. 1(6), C-1.

[70] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, May 22, 2007 ¶ 392 (emphasis added), C-263.

[71] Additionally, Mr. Stati is the sole shareholder of Tristan, and thus is an indirect investor with respect to Tristan's loans to KPM and TNG. Under the ECT, an "Investment" includes debt investments that are owned or controlled "directly or indirectly" by an Investor. *See* ECT art. 1(6)(a), C-1. Thus, Mr. Stati has standing and the Tribunal has jurisdiction with respect to Mr. Stati's indirect investment of the Tristan note proceeds in KPM and TNG. Furthermore, Mr. Stati did face some personal risk for the entire Tristan debt. Although he did not personally guarantee the Tristan notes, he faced potential personal exposure on the Tristan debt as Tristan Oil's sole shareholder and director. The validity of the corporate shield between Mr. Stati and Tristan Oil has not been determined by any court or tribunal, and will not be litigated because Mr. Stati was able to resolve all questions of personal liability with the Tristan noteholders amicably in the Sharing Agreement (discussed

80. In short, the fact that KPM and TNG were financed partly with the Tristan debt in no way deprives this Tribunal of jurisdiction. Claimants plainly are "Investors" who made "Investments" as defined in the ECT. Those investments included not only Claimants' debt and equity contributions to those companies, but also the pledges of their entire equity interests and any proceeds received through arbitration as security for the Tristan debt. As discussed further in Section V.E below, for that fundamental reason (among others), in calculating the quantum of the award it is not appropriate to deduct the amount of that debt from the value of the enterprises that Kazakhstan seized. Just as clearly, the existence of that debt in no way deprives this Tribunal of jurisdiction.

3. Claimants' Investments Benefited Kazakhstan

81. Kazakhstan's assertion that Claimants' investments have not contributed to Kazakhstan's economy is both irrelevant for purposes of jurisdiction and wrong.[72] Kazakhstan contradicts its own argument by highlighting the "strategic role" of Claimants' investments in Kazakhstan.[73] Kazakhstan recognizes in its pleadings that "the oil and gas fields had regional strategic importance and … the stop in production could have led to serious social unrest within the Mangystau region."[74] In short, Claimants' investments were not only beneficial to Kazakhstan, but also have been repeatedly described by Kazakhstan as essential to the well-being of the region.

82. Claimants' investments also contributed substantially to the Kazakh treasury. For the period from 2000 until the end of 2009, KPM and TNG paid US $163 and US $187 million in taxes and administrative expenses, including legitimate corporate and transfer pricing taxes and royalties.[75]

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further below). Thus, the degree of Mr. Stati's personal exposure for the Tristan debt is unquantifiable. That risk, however, certainly was not zero, as Kazakhstan asserts. Rejoinder on Quantum ¶¶ 381-383 ("It must therefore be assumed that Claimants are functionally no longer liable to the noteholders in any way.").

72 Rejoinder on Jurisdiction and Liability ¶¶ 133-145; First Olcott Report ¶¶ 162-74; Respondent's Opening Presentation on Jurisdiction, slide 20.

73 Statement of Defense ¶¶ 31.52, 31.59(c), and 31.129; Rejoinder on Jurisdiction and Liability ¶¶ 328, 360, and 694.

74 Rejoinder on Jurisdiction and Liability ¶ 694. *See also*, Statement of Defense ¶¶ 31.52, 31.59(c), 31.129.

75 Report of the MEMR on Unscheduled Inspection for KPM, February 6, 2010, Table 2, C-385 and Report of the MEMR on Unscheduled Inspection for TNG, February 5, 2010, Annex 1, C-386.

83. TNG also held a strategic position in Kazakhstan as the fourth largest producer of gas in the country.[76] As acknowledged by Kazakhstan in its pleadings, the gas supplied by KPM and TNG to the local power plant covered 80% of its demand.[77] In addition, KPM and TNG supplied gas to local Kazakh end users, especially for heating during the winter months, at severely discounted prices.[78]

84. Claimants' investments also benefited Kazakhstan by ensuring stable work for nearly 1,000 Kazakh citizens. Kazakhstan's claim of an alleged risk of "serious social unrest"[79] in the event KPM and TNG ceased operations contradicts its argument that Claimants' investments did not benefit Kazakhstan. Kazakhstan was apparently concerned that the 921 employees of KPM and TNG (94% of whom were local Kazakh citizens) would be out of work if KPM and TNG stopped operating.[80]

85. In summary, Claimants' investments were essential to the Mangystau region and of strategic importance for Kazakhstan. Claimants positively and substantially contributed to the economy of Kazakhstan, and those contributions cannot be seriously contested.

4. Claimants' Investments Were Legal

86. Kazakhstan has claimed that Claimants made several minor clerical errors when acquiring and registering KPM and TNG, ostensibly rendering their investments "illegal."[81] Claimants have conclusively demonstrated that such errors either did not occur or did not result

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[76] Bloomberg, "Kazakhstan Gas Production to Increase 12 Percent This Year," March 15, 2011, C-712 and "Kazakhstan Plans to Increase Gas Production", March 15, 2011, C-713.

[77] Statement of Defense ¶¶ 31.52, 31.59(c), and 31.129.

[78] *See* First FTI Report ¶ 5.19.

[79] Statement of Defense ¶¶ 31.52, 31.59(c), and 31.129; Rejoinder on Jurisdiction and Liability ¶¶ 328, 360, and 694.

[80] Report of the MEMR on Unscheduled Inspection for KPM, February 6, 2010, Section XII, C-385 and Report of the MEMR on Unscheduled Inspection for TNG, February 5, 2010, Conclusion, Point 3.5, C-386. But even after Kazakhstan's unilateral repudiation of KPM's and TNG's Subsoil Use Contract in July 2010, Claimants encouraged those employees to sign on to work for the new operator, KazMunaiGaz. *See* First Witness Statement of Alexandru Condorachi dated May 12, 2011 (hereinafter "First Condorachi Statement") ¶ 50. Thus, Claimants' found, hired, and trained KazMunaiGaz's current workforce on the Tolkyn and Borankol fields.

[81] Statement of Defense Section 9; Rejoinder on Jurisdiction and Liability ¶¶ 146-204; Respondent's Opening Presentation on Jurisdiction, slides 21-23.

in any "illegality" as a matter of Kazakh law, and that, in any event, minute administrative requirements of domestic law have no impact upon the Tribunal's jurisdiction.[82]

87. The ECT does not require exacting servitude to the minutiae of domestic legal or administrative requirements in order for an "investment" to qualify for protection.[83] No such requirement exists in customary international law either. Even in cases brought under an investment treaty that expressly requires an investment be made in accordance with domestic law — which the ECT does not — tribunals have excluded an investment from protection only in instances of calculated misconduct "amounting to fraud."[84] Kazakhstan has neither alleged nor proven that Claimants committed any act of fraud in acquiring or registering their Kazakh operating companies. Rather, Kazakhstan relies on minor clerical errors that are irrelevant to jurisdiction under the ECT and, for the most part, never even occurred.

a. KPM's Share Registration Is Valid

88. Contrary to Kazakhstan's assertion, Claimants do not admit that they breached Kazakh law regarding the registration of KPM's share issuance.[85] Rather, Claimants acknowledge that the previous shareholders of KPM failed to register KPM's initial share issuance as required by the articles of the Law on Securities Market applicable at the time.[86] Kazakhstan itself recognizes that a distinction must be made between failings by the former shareholders of a local investment vehicle and failings by claimants in an arbitration.[87] Investment treaty tribunals make the same distinction. For example, the *Saluka* tribunal accepted jurisdiction over claims by Saluka despite the Czech Republic's objection to jurisdiction based on alleged illegalities by Nomura, the former shareholder of IPB (the Czech investment vehicle)

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82 Reply on Jurisdiction and Liability ¶¶ 130-38. *See Tokios Tokeles v. Ukraine*, ICSID Case No. ARB/02/18, Decision on Jurisdiction, April 29, 2004, ¶¶ 85-86, C-401.

83 Reply on Jurisdiction and Liability ¶¶ 130-38.

84 *Plama Consortium Ltd. v. Bulgaria*, ICSID Case No. ARB/03/24, Award, August 27, 2008 ¶ 135, C-400; *see also*, *Phoenix Action Ltd v Czech Republic*, ICSID Case No ARB/06/5, Award, April 15, 2009 ¶ 144, R-31.

85 Rejoinder on Jurisdiction and Liability ¶ 147.

86 Reply on Jurisdiction and Liability ¶¶ 142-5.

87 Rejoinder on Jurisdiction and Liability, fn 126.

from which Saluka acquired its shares.[88] As in the *Saluka* case, alleged technical illegalities by the former shareholders of KPM cannot taint Claimants' title to the shares in this arbitration.

89. The argument Kazakhstan has raised is plainly a *post hoc* attempt to create an issue where none existed before this arbitration. Kazakhstan claims that under Article 16(1) of the Law on Securities Market, a newly established joint-stock company must register its initial share issuance within three months of its registration as a legal entity.[89] KPM was registered as a closed joint-stock company on March 24, 1997,[90] and Kazakhstan claims that the then-shareholders never registered the shares. To Claimants' knowledge (and Kazakhstan has not suggested otherwise), Kazakhstan took no action against the then-shareholders as a result of that omission.

90. Article 16 of the Law on Securities Market provided that, in the event of a violation of the registration requirement, the "competent authority has a right to file a lawsuit in court to claim such company's reorganization or liquidation."[91] Kazakhstan never sought KPM's reorganization or liquidation[92] or took any other action indicating that the registration requirement was of any import. Kazakhstan has never alleged that it suffered any injury from the supposed breach or explained what effect, if any, the breach should have had on Claimants' rights, ownership, and control over KPM. Rather, Kazakhstan signed the Subsoil Use Contract with KPM on March 30, 1999; it monitored, audited, and approved KPM's operations for a decade as Claimants explored the Borankol fields and produced hydrocarbons; and it reaped the benefits of those operations by accepting millions of dollars in taxes and royalties and the long-term employment of its citizens. Kazakhstan is clearly estopped from raising this minor clerical issue as a jurisdictional objection in this proceeding.

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88 *Saluka Investments B.V. (The Netherlands) v. The Czech Republic*, UNCITRAL, Partial Award, March 17, 2006 ¶¶ 217-8, C-259.

89 Articles 16 and 17 of the Law on Securities Market dated March 5, 1997, R-7.

90 Charter and Foundation Agreement of KPM dated March 24, 1997, C-407 and C-408.

91 Article 16 of the Law on Securities Market dated March 5, 1997, R-7.

92 Kazakhstan relies on Article 17(2) to claim that KPM's share issuance is invalid and any subsequent attempt to cure this invalidity is ineffective, but it cannot deny that the invalidation of shares requires the intervention of a court, which Kazakhstan also never sought. *See* Rejoinder on Jurisdiction and Liability ¶¶ 183-188; *see also* Article 17 of the Law on Securities Market dated March 5, 1997, R-7; *cf.* Article 157(1) of the Kazakh Civil Code, C-403.

91. Moreover, regardless of whether any technical violation occurred when KPM was formed, Claimants promptly cured the alleged registration defect upon their acquisition of 62% of KPM's shares in 1999. By that time, Kazakhstan had substantially amended Article 16 of the Law on Securities Market, releasing closed joint-stock companies from the obligation to register their initial and subsequent share issues.[93] The new law only required KPM to obtain a national identification number (issued by the Kazakh National Securities Commission after review of the necessary documents), and it did not impose a time limit on obtaining the number. [94]

92. On December 13, 1999, the Ministry of Justice re-registered KPM following its change of shareholders.[95] On January 24, 2000, the Kazakh National Securities Commission issued a national identification number with respect to KPM's initial issuance of shares.[96] The next day, KPM placed its shares amongst it shareholders and recorded the placement in its share register.[97] On April 9, 2003, the National Bank of Kazakhstan issued a report on the approval of the issuance of shares.[98] On May 13, 2005, the Kazakh Ministry of Justice approved and registered KPM's transformation from a closed joint-stock company into a limited liability partnership.[99] Thus, any "irregularities" with the registration of KPM's shares no longer existed, at the latest, as of the transformation in May 2005, after which Claimant Ascom unquestionably owned and controlled its investment KPM.

93. Notably, it is now apparent that international legal counsel to KMG E&P, Squire Sanders, shared the opinion that there was no material issue regarding KPM's share issuance. In one of the diligence reports that Kazakhstan withheld from Claimants and the Tribunal, Squire Sanders (assisted by the Kazakh law firm Olympex) concluded that

> KPM's registration documents meet the requirements of the laws of Kazakhstan and bear the stamps of the competent governmental

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93 Law of the Republic of Kazakhstan No. 282-1 "On Amendments to Certain Legislative Acts of the Republic of Kazakhstan on Questions Related to Joint-Stock Companies" dated July 10, 1998, C-404.

94 Order of the Kazakhstan National Securities Commission No. 144 "On Interim Procedure for Assignment of Identification Numbers to Certain Types of Shares Emissions" dated August 14, 1998, C-405.

95 Certificate of State Registration of KPM dated December 13, 1999, R-12; Letter from KPM to the Agency on Investments dated December 23, 1999, C-49.

96 Letter from the Kazakh National Securities Commission to KPM dated January 24, 2000, C-406.

97 Excerpt from the Register of KPM's shareholders, January 25, 2000, C-378.

98 Notification of approval of report on the results of KPM's shares issue and placement dated April 9, 2003, Exhibit 7 to First Maggs Report.

99 KPM's Certificate of Registration as a Limited Liability Partnership dated May 13, 2005, C-37.

> authorities of Kazakhstan. Considering that the re-registration of a legal entity in Kazakhstan must be effected by virtue of a resolution of the subject company's shareholders and information on the preceding registration of KPM, we believe that risks inherent in the legality of the procedure for KPM's original establishment and subsequent registration are minimal.[100]

Kazakhstan had access to that information, withheld it in violation of the Tribunal's orders, and nevertheless pursued its baseless claim of illegality regarding KPM's registration.

94. In short, this jurisdictional "objection" is a contrivance. Kazakhstan never claimed any irregularity regarding KPM's registration before its Statement of Defense in November 2011, some fourteen years after the fact, eleven years after the statute of limitations expired, and two years after KMG's legal counsel confirmed it was not problematic.[101] The Tribunal should reject the "objection."

b. KPM and TNG Did Not Lack Any Required Consent for the Transfer of Shares to Ascom and Terra Raf

95. Kazakhstan also argues that when Claimants acquired their shares in KPM and TNG, they should have complied with the requirement in Article 53(1) of the 1995 Law on Oil to obtain consent to the share transfers from the Licensing and Competent Authorities.[102] However, at the date of Claimants' acquisition of the KPM and TNG shares, Article 53(1) no longer applied, and its successor provision only required consent for transfer of a subsoil use contract, not for transfer of shares in a subsoil user. Moreover, in light of the confusion surrounding the changing provisions at the time, Claimants sought consent for their initial acquisition of shares in KPM (which preceded the acquisition of the shares in TNG), and Kazakhstan's "Competent

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[100] Squire Sanders Legal Due Diligence Report, July 30, 2009, at 64, C-725. Squire Sanders also noted that "[a]s at the date of this Report [July 30, 2009], KPM's foundation agreement is no longer relevant owing to the absence of a participant in KPM other than Ascom." *Id*. at 63, C-725.

[101] *See* Articles 178(1), 179(3), and 180(2) of the Civil Code of Kazakhstan, C-403; Squire Sanders Legal Due Diligence Report, July 30, 2009, at 64, C-725.

[102] Respondent claims for the first time in its Rejoinder on Jurisdiction and Liability that the transfer of shares would have been invalid pursuant to Article 14 of the 1996 Law on Subsoil Use. (Rejoinder on Jurisdiction and Liability ¶ 160.) Although this argument is irrelevant (as Article 14 of the 1996 Law on Subsoil Use required a consent for a transfer of subsoil use rights from one subsoil user to another as opposed to a transfer of shares in a subsoil user), Claimants note that (i) Article 53 of the Law on Oil provides no consequences for its violation and (ii) no principle of legal interpretation allows for the application of a sanction contained in one law (Article 14 of the Law on Subsoil Use) for the violation of a different obligation to the violation of an obligation in another law (Article 53 of the Law on Oil).

Authority" informed Claimants that no such consent was required. Kazakhstan is estopped to claim otherwise for purposes of this proceeding.

96. As with its claim about KPM's share registration, Kazakhstan never once raised any concerns about the alleged absence of consent during the many years prior to this proceeding. Furthermore, in its lengthy Legal Due Diligence Report prepared for KMG E&P, Squire Sanders extensively examined the validity of Claimants' ownership of KPM and TNG and did not raise any concerns regarding the alleged lack of consent that Kazakhstan has raised as a jurisdictional objection in this case.[103]

97. Article 53(1) of the 1995 Law on Oil on transfer of rights and obligations provided:

> Contractor can transfer to a physical person or legal entity or international organization all or part of its rights and obligations under the [subsoil use] agreement, including by means of alienation of a majority stake of shares, only upon written consent of a Licensing and Competent Authority. The conditions for the transfer of rights and obligations to a subsidiary are stipulated in the Contract.[104]

Thus, Article 53 of the 1995 Law on Oil required consent from the competent and licensing authorities for transfer of subsoil use rights from one user to another and for transfer of a majority shareholding in a subsoil user. By contrast, on transfer of the right of subsoil use, Article 14(1) of the 1996 Law on Subsoil Use only required consent for the transfer of subsoil use right from one user to another:

> Transfer of the Right of Subsoil Use by the Subsoil User to another person made on a paid or unpaid bases, including transfer as a contribution to the charter capital of a legal person being created, with the exception of the transfer of the Right of Subsoil Use in pledge, shall be made only with the permission of the Competent Body (or the authorized State body).[105]

98. As explained by Claimants in their Reply on Jurisdiction and Liability, in August 1999, Kazakhstan abolished its dual licensing and contracting system with respect to subsoil use

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[103] Squire Sanders Legal Due Diligence Report, July 30, 2009, C-725; *see* M. Suleimenov Testimony, Tr. October 2012 Hearing, Day 4, 162:7-163:4.

[104] 1995 Law on Oil, art. 53(1), C-411.

[105] *See* First Maggs Report ¶ 51.

and moved to a contract-only system (the "1999 Amendments").[106] All of Claimants' acquisitions of shares in KPM and TNG occurred after the elimination of the licensing regime. The 1999 Amendments amended the 1996 Law on Subsoil Use, but failed to directly amend the Law on Oil. Nonetheless, the 1999 Amendments contained a savings clause in Article 2(3) that effectively "froze" the pre-existing licenses, which could only be suspended or withdrawn — but not amended — by the State authorities.[107]

99. Kazakhstan argues that the earlier 1995 Law on Oil should prevail over the later 1996 Law on Subsoil Use or that both should apply cumulatively.[108] That position, however, contradicts Kazakh laws governing the hierarchy of statutory acts according to which provisions of a later act shall prevail.[109]

100. Moreover, because the interpretation of the laws after the 1999 Amendments was at best unclear, KPM submitted a request to the Competent Authority, the Agency on Investment, for consent with respect to Claimants' first acquisition of shares in Kazakhstan (Ascom's acquisition of 62% of KPM) on November 18, 1999. The Agency on Investment answered:

> In response to your request to provide a consent for inclusion of IFG "ASCOM" S.A. into the shareholding structure of CJSC JV "Kazpolmunay with a 62% share in the charter capital including the rights provided under the contract, we inform:
>
> A decision on change in shareholding structure is within the powers of the general shareholders' meeting.[110]

101. The Agency on Investment further instructed KPM that, "upon the change in the shareholding structure, you should apply to the Competent Authority in order to implement

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[106] Reply on Jurisdiction and Liability ¶ 157; Law on Amendments and Additions to certain legislative acts of the Republic of Kazakhstan relating to subsurface use and the conduct of petroleum operations in the Republic of Kazakhstan dated August 11, 1999, and effective from September 1, 1999, C-410.

[107] Law on Amendments and Additions to certain legislative acts of the Republic of Kazakhstan relating to subsurface use and the conduct of petroleum operations in the Republic of Kazakhstan dated August 11, 1999 and effective from September 1, 1999, C-410.

[108] Rejoinder on Jurisdiction and Liability ¶¶ 154-156. Clearly, if both articles apply cumulatively, then Kazakhstan would have been in the paradoxical situation of requiring Subsoil Users to apply for permission from the Licensing Authority even if their Subsoil Use Contract had been issued without a corresponding License under the new regime.

[109] Law of the Republic of Kazakhstan on Normative Legal Acts dated March 24, 1998, Article 6(2), C-412.

[110] Letter No. 01-37 from the Agency on Investment to KPM, November 19, 1999 (emphasis added), C-47.

respective changes in the license."[111] Indeed, the Competent Authority was the liaison between the Contractor or subsoil user and the Licensing Authority pursuant to the Subsoil Use Contracts and the Subsoil Use Law.[112] Upon acquisition of the shareholding, in December 1999, KPM applied to the Competent Authority, the Agency on Investment, for an explanation of these issues. The Agency on Investment informed KPM that:

> In line with the amendments and supplements to the Republic of Kazakhstan Law "On Subsoil and Subsoil Use" adopted on 11.08.1999, Licenses for Subsoil Use are no longer issued, and amendments or supplements to previously granted licenses are no longer performed.[113]

102. By this letter the Competent Authority indicated that it would not apply to the Licensing Authority to amend the Subsoil Use License. The Government of Kazakhstan subsequently endorsed this interpretation in minutes of a meeting dated May 14, 2002:

> [I]n line with the annulment of the licensing procedure regarding the granting of subsoil use rights as set forth in the Republic of Kazakhstan Law of 11th August 1999 … [a]mendment of subsoil use conditions shall be performed through amendment of the respective subsoil use contractual provisions, agreed between the Subsoil User and the Competent Authority, acting within the framework of its competency; without performing any modifications to licenses granted earlier. A Government's decision in this case is not needed.[114]

103. The MEMR also confirmed this position in a letter to the Financial Police dated December 4, 2008:

> Law of the Republic of Kazakhstan No. 467 of August 11, 1999 abolished the licensing system for granting subsoil use rights.

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111 Letter No. 01-37 from the Agency on Investment to KPM, November 19, 1999, C-47.

112 Contract No. 305, Articles 7.3.2 and 7.4.2, C-45; Contract No. 210, Articles 6.3.2 and 6.4.2, C-52; Contract No. 302, Articles 6.3.3 and 6.4.2, C-53; and 1996 Subsoil Use Law, Article 8(1)(6), C-413.

113 Letter No. 3-199 from the Agency on Investment to KPM dated January 18, 2000, C-420.

114 Minutes of Governmental Meeting No. 17-23/1-404 dated May 14, 2002, C-421. In this respect, Claimants note that Professor Ilyasova points to the fact that a number of licenses were amended in 2001. *See* Expert Report from Professor Ilyasova, Answer to question 5) and Appendices 1 and 2. However, Professor Ilyasova does not list license changes after July 2001 and all amendments to the licenses concerned the duration of the license, the mining allotment (Appendix 1) or a change in the subsoil user rather than in the shareholders of the subsoil user (Appendix 2).

> Therefore, the Ministry of Energy and Mineral Resources of the Republic of Kazakhstan did not amend the subsoil use licenses of TOO SP Kazpolmunay and TOO Tolkynneftegaz.[115]

104. Even if Kazakhstan could somehow establish that those representations to Claimants were wrong — which it has not done — Claimants relied on those interpretations of Kazakh law by the relevant State authorities. Kazakhstan cannot now contradict its previous interpretations in order to suit its purpose in the present arbitration.

c. Kazakhstan Had No Pre-Emptive Right Over TNG

105. On December 18, 2008, as part of its expropriatory campaign, Kazakhstan publicly accused Claimants of defrauding the State of its pre-emptive right to purchase TNG by forging certain documents pertaining to the date of transfer of TNG's shares from Gheso to Terra Raf.[116] Kazakhstan has raised the same unfounded allegations as an objection to the Tribunal's jurisdiction.[117] Its argument is factually and legally wrong.

106. The State's pre-emptive right to acquire shares in subsoil users arose on December 8, 2004 pursuant to the enactment of Law No. 2-III, which amended Article 71 of the 1996 Law on Subsoil Use.[118] The law applied only prospectively, *i.e.*, it did not give Kazakhstan preemptive rights for share transfers that occurred prior to December 2004. Kazakhstan does not contest that fact. The last transfer of shares in TNG occurred when Claimant Terra Raf acquired 100% of TNG from Gheso pursuant to a May 12, 2003 share purchase agreement.[119] Therefore, Kazakhstan had no pre-emptive right with respect to any acquisition or share transfer in TNG. That is — or should have been — the end of the matter.

107. Nonetheless, to Claimants' surprise, in February 2007 Kazakhstan requested that TNG apply for a retroactive consent for the 2003 transfer of TNG shares from Gheso to Terra

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115 Letter from the MEMR to the Financial Police, December 4, 2008, C-422.

116 INTERFAX article attached to email from Crédit Suisse to A. Lungu, December 18, 2008, C-625; Notice letter from the MEMR to TNG, December 18, 2008, C-140.

117 Statement of Defense § 13; Rejoinder on Jurisdiction and Liability ¶¶ 158-180.

118 Law No. 2-III of the Republic of Kazakhstan "On introduction of amendments and additions to some legislative acts of the Republic of Kazakhstan concerning subsoil use and performance of oil operations in the Republic of Kazakhstan," December 1, 2004, R-19.

119 Sale and Purchase Agreement between Gheso and Terra Raf, May 12, 2003, C-60.

Raf.[120] Although TNG disagreed that such consent was required, TNG complied because there was no reason to think that Kazakhstan would decline consent. In its consent application, TNG also emphasized that the State's preemptive right did not apply because the last transfer of shares in TNG occurred on May 12, 2003, before the creation of the State's pre-emptive right in December 2004. On February 21, 2007, the MEMR informed TNG that the Appraisal Commission, which had responsibility for deciding requests for alienations of subsoil use agreements, issued a ruling expressly approving the 2003 transfer from Gheso to Terra Raf.[121] Moreover, that ruling also expressly confirmed that the State's pre-emptive right did not apply because it "does not have retroactive value and does not apply to the relationships appeared as a result of the concluded contract prior to its coming into force."[122] Once again, that was — or should have been — the end of the matter.

108. Kazakhstan has argued in this proceeding — with no legal or factual basis whatsoever — that the pre-emptive rights law applied to the transfer of shares in TNG from Gheso to Terra Raf because that transfer was not "completed" until May 16, 2005. That contention is "based" on Kazakhstan's malicious "leak" to the financial press of December 18, 2008, in which the MEMR went so far as to accuse Claimants of failing to disclose that the transfer from Gheso to Terra Raf had not occurred until May 16, 2005.[123] Kazakhstan has never substantiated that allegation, because it cannot. As conceded by Kazakhstan's expert, Professor Ilyasova,[124] a change of shareholders in an open joint-stock company (such as TNG at the time) required registration of the change with the companies' registrar, but not re-registration with the State authorities. As evidenced by Exhibits R-18,[125] R-39,[126] and C-418,[127] TNG's registrar —

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

121 Letter from the MEMR to TNG attaching the Minutes of Meeting of the Appraisal Commission dated February 21, 2007 and Minutes of the Appraisal Commission dated February 20, 2007, C-415 and C-134.

122 Minutes of the Appraisal Commission, February 20, 2007, C-134. The MEMR confirmed that position in December 2007 when it waived the State's pre-emptive right in connection with Claimants' planned IPO on the London Stock Exchange, without raising any objection as to any consent or pre-emptive right defects concerning Terra Raf's ownership of TNG. *See* Letters from KPM and TNG to the MEMR dated December 6, 2007 and Letters from the MEMR to KPM and TNG dated December 29, 2007, C-135, C-423, and C-139.

123 INTERFAX article attached to email from Crédit Suisse to A. Lungu, December 18, 2008, C-625.

124 Expert Report from Professor Ilyasova, Answer to question 8(b) at 46-48.

125 Register of Operations for TNG by its Registrar at various point in time attached to letter from Registrar Zerde to TNG dated January 16, 2009, R-18.

126 Data on the value of shares of TNG from the register of transfers, Zerde, dated January 16, 2009, R-39.

127 Extract from the register of shareholders of TNG dated May 28, 2003, C-418.

Invest Service — registered the share transfer from Gheso to Terra Raf on May 28, 2003.[128] Kazakhstan's witness, Mr. Ongarbaev, also confirmed at the October 2012 Hearing that the Gheso-Terra Raf transfer was registered on May 28, 2003.[129] Therefore, Claimants "completed" the process of transfer at the latest on May 28, 2003, prior to the State acquiring a pre-emptive right.

109. Kazakhstan's reference to May 16, 2005, as the alleged operative date is a deliberate "misunderstanding." That date is unrelated to any change of shareholding in TNG. Rather, on that date, TNG was reorganized from an open joint-stock company into a limited liability partnership, and the reorganization was re-registered with the State authorities.[130] Those events had nothing to do with the transfer of the shareholding of TNG from Gheso to Terra Raf and are completely irrelevant to the pre-emptive right issue.

110. Kazakhstan's jurisdictional objection on this point is a red herring. Other than using its baseless allegation to defame Claimants in December 2008, Kazakhstan never raised the issue prior to this proceeding, except to unnecessarily confirm to Claimants in 2007 that there was no issue. As with the previous two objections, KMG's international counsel, Squire Sanders, did not raise any concerns. Indeed, Squire Sanders analyzed the pre-emptive rights topic and found that it was "unlikely" that this issue could lead to termination of TNG's subsoil use contracts.[131] As with Kazakhstan's other jurisdictional objections, this issue is nothing more than a contrivance that the Tribunal should reject.

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[128] *See* stamp from TNG's registrar Invest-Service with handwritten note "28.05.03" on the Russian original of the Sale and Purchase Agreement between Gheso and Terra Raf dated May 12, 2003, C-60. Kazakhstan now alleges that "Claimants have produced a document dated 15 September 2004, which expressly refers to Ascom being the owner of TNG as at that date." Rejoinder on Jurisdiction and Liability ¶ 173. That contention is highly misleading. Claimants produced Exhibit C-514 in order to demonstrate the interest of Mr. Kulibayev in KPM and TNG. Exhibit C-514 is a memorandum prepared by GazImpex project manager to Mr. Kulibayev. Claimants did not prepare this document and cannot be held to its inaccuracies.

[129] Ongarbaev Testimony, Tr. October 2012 Hearing, Day 6, 62:19-24; *see also* Pisica Testimony, Tr. October 2012 Hearing, Day 2, 60:25-61:21; Squire Sanders Legal Due Diligence Report, July 30, 2009, at 119, C-725.

[130] Notarized copy of TNG's Certificate of Registration as a Limited Liability Partnership issued by the Ministry of Justice on May 16, 2005, C-40.

[131] Squire Sanders Legal Due Diligence Report, July 30, 2009, at 166, C-725.

C. Kazakhstan's Allegations Regarding Evidentiary Misconduct on the Part of Claimants Are Ludicrous

111. During its opening presentation at the October 2012 Hearing, Kazakhstan accused Claimants of intentionally submitting misleading translations, illegally-obtained documents, and "documents that are not genuine as proof."[132] Although Kazakhstan tried to frame its allegations as objections to jurisdiction, the accusations are clearly irrelevant to the Tribunal's jurisdiction and are at most a procedural issue. Moreover, the accusations are baseless, but Claimants will nevertheless briefly respond to them for the sake of completeness.

112. Kazakhstan's argument that Claimants knowingly submitted mistranslated documents in order to "commit an attempted procedural fraud"[133] would be laughable if it were not offensive. Claimants submitted over 500 exhibits and supporting documents to their various expert reports requiring translation in this arbitration. Given the volume and difficulty of the translations, one could reasonably expect minor errors.[134] Kazakhstan has failed to refer the Tribunal to any alleged translation errors by Claimants that were material, much less intentional. For instance, Kazakhstan takes exception to Claimants' translation of the Russian words "тщательно проверить" as "investigate" and insists that they mean "thoroughly check."[135] This is a distinction without a difference: the two expressions have the same meaning, and Kazakhstan has not explained what impact the difference in those words could possibly have on the case.

113. Kazakhstan also contests Claimants' translation of the MEMR's letter to TNG of April 9, 2009, granting the extension of Contract No. 302.[136] Again, the difference between

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132 Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slides 25-46.

133 Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slide 45.

134 In typical international arbitration practice, parties normally solve inaccuracies in translation simply by submitting an amended translation. If a substantial disagreement as to the meaning or substance arises, the Tribunal will have two versions of a translation to form a conclusion about the evidence. Claimants have always been cognizant of the fact that the Tribunal is comprised of one native-Russian speaker, and that Kazakhstan's legal team includes several native-Russian speakers. Therefore, any discrepancies in translation should be immediately apparent and easily remedied. Instead of raising a procedural dispute as to specific translations, however, Kazakhstan attempts to make a mountain out of a molehill and accuses Claimants of fraud.

135 Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slide 28.

136 Rejoinder on Jurisdiction and Liability ¶¶ 419-24. Claimants' version of that letter states "the Minister of energy and mineral resources of the Republic of Kazakhstan, decided the following: The extension of the exploration period is granted for a period of 2 years, until 03/30/2011. The appropriate modifications will be introduced in the Contract no. 302 of 07/31/ 2008 by July 2, 2009." In contrast, Kazakhstan's version states:

those translations is lost on Claimants, and even Kazakhstan "admit[s] that the Russian wording generally allows for both translations."[137]

114. In marked contrast to Kazakhstan's emphasis on "distinctions without a difference," Claimants have demonstrated that Kazakhstan has made numerous — and quite material — translation errors and omissions. The witness statement of Mr. Ongarbaev is a prime example of a translation Kazakhstan submitted that is riddled with serious mistakes and gross omissions.[138] Kazakhstan deleted entire paragraphs and added sentences in its "translation" of that statement from Russian into English.[139] For instance, Kazakhstan failed to translate an entire paragraph of the Russian original statement concerning KPM's and TNG's alleged violations of their obligations in July 2010.[140] Kazakhstan also erased Mr. Ongarbaev's reference to the role of the Financial Police in the July 2010 audits, which is particularly egregious given counsel's comments in the opening statement at the October 2012 Hearing that the Financial Police were not involved in those inspections.[141]

115. Similarly, Kazakhstan provides no support — because none exists — for its baseless allegation that Claimants altered documents. For instance, Kazakhstan contends that Claimants doctored Exhibit C-520, a letter from Terra Raf to KazRosGas, because Terra Raf's incorporation number on that document is not accurate.[142] A more realistic explanation is that

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"The Ministry of Energy and Mineral Resources of the Republic of Kazakhstan … has resolved to: Permit extension of the exploration period by 2 years until 30.03.2011. Contract No. 302 dated 31.07.1998 to be amended accordingly by 02 July 2009." *See* Letter from the MEMR to TNG, April 9, 2009, C-27 and R-163.1.

137 Rejoinder on Jurisdiction and Liability ¶ 421.

138 Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, C-720. *See also*, Updated Translation of Witness Statement of Mirbulat Zarifovich Ongarbaev submitted by Kazakhstan on December 1, 2012.

139 Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, C-720.

140 Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, ¶ 2.11, C-720; *see also*, Kazakhstan's Updated Translation of Witness Statement of M. Ongarbaev ¶ 2.11 (second paragraph numbered 2.9).

141 Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, ¶ 2.5, C-720. Similarly, Kazakhstan simply deleted a sentence whereby Mr. Ongarbaev purported to attach to his statement requests for additional information to subsoil users seeking waiver of the State's preemptive rights and Kazakhstan never provided these requests. Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, ¶ 6.4, C-720. *See also*, Kazakhstan's Updated Translation of Witness Statement of M. Ongarbaev.

142 Respondent's Opening Presentation on Jurisdiction, slide 43.

the discrepancy is due to a clerical error that occurred when the document was created.[143] Kazakhstan bears the burden of proof to establish that this error was intentional, and how such an alleged misrepresentation affects this case. Kazakhstan cannot meet that burden, because Claimants plainly did not alter the document and the error in Terra Raf's incorporation number is of no import.

116. Lastly, Kazakhstan accuses Claimants of having "in fact corrupted Kazakh officials" in order to obtain internal government documents.[144] Kazakhstan's sole basis for this claim is the fact that "Claimants were able to present documents in this arbitration which should normally never have been in their possession."[145] Kazakhstan lists seven documents that it considers "confidential internal government documents."[146] Kazakhstan has not established that all of those documents were confidential — indeed, some of them certainly were not.[147] In any event, Claimants have explained that certain Kazakh officials were (unsurprisingly) sympathetic to their plight and provided them with a limited number of internal documents. However, none of the documents was obtained improperly, and Respondent has never questioned their authenticity.

117. Kazakhstan's claim that Claimants produced an "illegally obtained transcript with own amendments as evidence of their case" is another example of its baseless accusations.[148] As Mr. Condorachi explained during the October 2012 Hearing, the electronic, unsigned copy of the hearing minutes of Mr. Cornegruta's trial that Claimants submitted as Exhibit C-704 came from

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143 Similarly, Kazakhstan is blowing out of proportion the minor differences between two documents evidencing wire transfers at Exhibits C-459 and C-702, one unsigned and one signed. *See* Respondent's Opening Presentation on Jurisdiction, October 2012 Hearing, slides 37-9.

144 Rejoinder on Jurisdiction and Liability ¶ 213.

145 Rejoinder on Jurisdiction and Liability ¶ 213.

146 Rejoinder on Jurisdiction and Liability ¶ 214. Kazakhstan also claims that Exhibit C-134 was somehow improperly obtained by Claimants and vaguely disputes its authenticity (Rejoinder on Jurisdiction and Liability ¶ 166). As explained by Claimants, the excerpt from the Minutes of Meeting of the Appraisal Commission dated February 20, 2007 (Exhibit C-134) was transmitted by the MEMR to TNG as attachment to a letter dated February 21, 2007 (Exhibit C-415). *See* Reply on Jurisdiction and Liability ¶ 168.

147 For example, Kazakhstan claims that Claimants illegally obtained a copy of President Nazarbayev's October 2008 order (Exhibit C-8). Rejoinder on Jurisdiction and Liability ¶ 213. That order is the first piece of evidence listed in Mr. Cornegruta's criminal case file. Hearing Minutes from Mr. Cornegruta's Trial, July 30 to September 14, 2009, at 103, C-704. By including that document in Mr. Cornegruta's criminal case file, Kazakhstan can hardly claim that it was an internal government document that should not have come into Claimants' possession.

148 Respondent's Opening Presentation on Jurisdiction, slide 30.

the court.[149] Claimants produced that document in this arbitration exactly as they received it. Its own witness, Mr. Kravchenko, explained that it is routine for draft minutes of a trial to be prepared by a secretary to the court and then subsequently amended by the judge.[150] It is thus unsurprising that Claimants obtained and produced in this arbitration the draft transcript that was prepared prior to the judge's subsequent amendments.

118. Kazakhstan also contends that Claimants improperly obtained the Blagovest letter, produced as Exhibit C-23. Like its other allegations, Kazakhstan cannot prove that claim. Mr. Stati explained that the Blagovest letter was found at KPM's offices, on the desk of Mr. Andreyev, KPM's then-General Director, along with other documents.[151] Kazakhstan's witness, Mr. Zakharov, further explained why Andreyev had a copy of that letter.[152] It is therefore entirely unremarkable that Claimants obtained a copy.

119. Kazakhstan also wildly claims that Claimants forged Exhibit C-711, a report from Mr. S. Rakhimov to the Chief of the Financial Police.[153] Kazakhstan fails to provide any convincing explanation for why Claimants would waste any time or energy to create 11 "fake" reports outlining alleged violations of KPM and TNG in July 2010.[154] And it cannot deny, because Mr. S. Rakhimov himself confirmed, that various Kazakh ministries, led by the Financial Police, were in fact preparing inspection reports of KPM and TNG in July 2010.[155] Thus it is not surprising that interim reports were sent to the Financial Police, probably so that the Financial Police could approve and/or influence their results, as it did in November 2008.

120. Kazakhstan's baseless contentions regarding evidentiary misconduct on the part of Claimants have fallen flat on their face. At the October 2012 Hearing, Claimants categorically denied Kazakhstan's allegations and challenged Kazakhstan to prove them. It did not even attempt to do so at that hearing, and it cannot do so now.

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149 Condorachi Testimony, Tr. October 2012 Hearing, Day 2, 141:3-17.

150 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 47:12-49-13.

151 Stati Testimony, Tr. October 2012 Hearing, Day 2, 23:13-18. Mr. Kravchenko has indicated that he will initiate a criminal case to clarify how Claimants obtained the transcript. Tr. October 2012 Hearing, Day 4, 55:1-5.

152 Witness Statement of Yuri Zakharov dated October 28, 2011, R-178.

153 A. Kravchenko, Tr. October 2012 Hearing, Day 4, 117:7-120:3.

154 Reports from Mr. Rakhimov to the Chief of the Financial Police, July 9, 2010, C-711.

155 Tr. October 2012 Hearing, Day 6, 31:6-32:23; 33:6-10.

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121. In conclusion, this Tribunal has jurisdiction over this dispute. Kazakhstan has made a number of frivolous jurisdictional objections, none of which has sustained a review of the relevant facts or rules of international and domestic law. The Tribunal should not hesitate to conclude that it has jurisdiction to rule upon the merits of this dispute, and the evident lack of substance to Kazakhstan's case on jurisdiction should influence the Tribunal's award of costs in this proceeding.

III. KAZAKHSTAN VIOLATED THE ECT AND INTERNATIONAL LAW

A. The Key Facts Of This Case Are Beyond Dispute

122. Claimants have established the main factual elements of their case. Claimants have shown that they made major investments in Kazakhstan through KPM and TNG, and that they transformed idle, largely forgotten oil and gas fields into significant producing resources. With that transformation, Claimants earned significant profits, provided benefits to the Kazakh economy, and generated substantial revenues for the Kazakh state. It was only after Claimants developed KPM and TNG into "strategic assets" that Kazakhstan initiated its campaign against Claimants' investments. Claimants have presented substantial documentary evidence that is corroborated by witness testimony, and they reviewed the salient facts at the October 2012 Hearing. The following is a brief summary of the key facts that have been established.

123. The contributions Claimants made to Kazakhstan and its economy were substantial. Over 90% of KPM's and TNG's work force was comprised of local Kazakh citizens. Claimants employed nearly 1,000 local Kazakh workers on a permanent basis, and many more throughout the years on specific projects, including construction of the LPG plant. Additionally, Claimants invested over US $1.1 billion into KPM and TNG throughout the life of their investments in Kazakhstan. KPM and TNG paid Kazakhstan US $163 and $187 million, respectively, in taxes and administrative expenses, including legitimate corporate and transfer pricing taxes and royalties, between 2000 and 2009.[156]

[156] Report of the MEMR on Unscheduled Inspection for KPM, February 6, 2010, Table 2, C-385 and Report of the MEMR on Unscheduled Inspection for TNG, February 5, 2010, Annex 1, C-386.

124. Claimants' transformation of the Borankol and Tolkyn fields from fallow, abandoned fields into highly-successful production operations is beyond dispute.[157] The Borankol field had been explored for 36 years and had remained largely unproductive prior to Claimants' investments. Kazakhstan's own MEMR noted that Claimants more than doubled KPM's well count from 2001 to 2008,[158] and by the time Kazakhstan directly expropriated KPM's assets in 2010, Claimants were operating 73 active wells in the Borankol field.[159]

125. The Tolkyn field was similarly barren prior to Claimants' investment in TNG. Claimants re-worked the field, restored existing wells, carried out new seismic surveys, and drilled new wells in order to produce enough gas to exceed the demand of the local Kazakh communities. The MEMR noted that TNG's resource base (the Tolkyn field reserves) and its development system "insure reliable and stable operation of the entire system, as well as fulfill the needs for energy resources of population and enterprises in Mangistau region."[160] Claimants' transformation of the Tolkyn field was to such a degree that, in 2007, they were able to double the capacity of TNG's gas processing facilities and, as a result, significantly increase TNG's rate of production by September 2007.[161] Claimants' investments in TNG caused it to become Kazakhstan's fourth largest gas producer.[162]

126. Claimants built all the infrastructure required to exploit and sell oil and gas from the Borankol and Tolkyn fields. They completed a state-of-the-art processing facility, supported

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[157] For the Kazakh government's reports in this respect, *see* Report on the results of the unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use, and contract obligations of KPM, November 4-11, 2008, C-86; Report on the results of the unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use, and contract obligations of TNG, November 4-11, 2008, C-87; Reports of the MEMR for KPM, January 25 - February 6, 2010, C-385; Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386; Act on results of unscheduled inspection of performance of Kazakh legislation on subsoil and subsoil use of KPM, June 30 - July 7, 2010, C-689; Acts on the Unscheduled Inspection of TNG from the Geology Committee, July 16, 2010, C-315; Certificate on the results of planned check of performance of Kazakh legislation on subsoil use and contract obligations for TNG, July 1-12, 2008, C-683; Report by MEMR on the results of planned check of performance of Kazakh legislation on subsoil use and contract obligations for KPM, July 1-12, 2008, C-691; and Report on the Results of a Special-Purpose Inspection of KPM, May 22-25, 2007, C-690.

[158] Report on the results of the unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use, and contract obligations of KPM, November 4-11, 2008, C-86.

[159] Act on results of unscheduled inspection of performance of Kazakh legislation on subsoil and subsoil use of KPM, June 30 - July 7, 2010, C-689.

[160] Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

[161] *See* Broscaru Witness Statement ¶ 9.

[162] N. Gizitdinov, Bloomberg, "Kazakhstan Gas Production to Increase 12 Percent This Year," March 15, 2011, C-712.

by all the equipment necessary for gathering, treatment, de-watering, testing, measurement, pumping, pre-heating, pressurizing, and transport of oil and gas from the companies' production facilities to the Kazakh main oil and gas pipelines.[163] It is thus unsurprising that, under Claimants' management, KPM and TNG greatly exceeded their work program obligations. The MEMR noted that Claimants' investments in KPM exceeded KPM's work program and contractual obligations by 6.6 times (an excess of over US $400 million),[164] and their investments in TNG exceeded its obligations by a factor of 3.4 (an excess of over US $450 million).[165] Indeed, at the end of 2008, both KPM and TNG had generated and reinvested record-breaking profits, a feat they intended to become a trend in subsequent years with the completion of the LPG plant and their planned exploitation of the Contract 302 Properties.

127. In addition to their oil and gas production and processing facilities, Claimants were in the process of constructing an integrated LPG plant designed to produce propane, butane, and pentane-plus from TNG's gas production. Claimants invested more than US $240 million in construction of the LPG plant,[166] and they were near completion of the facility when they decided to halt further expenditures in May 2009 in the midst of the State's coercion campaign.[167] That investment was planned to reap even more benefits for the Kazakh economy, in no small measure because it was also designed to produce LPG products from the gas of neighboring producers. The MEMR's Geology Committee confirmed the plant's strategic importance in July 2010 when it stated that upon completion, the LPG plant "would be of great regional and industrial importance for development of the region."[168]

128. Claimants also made significant investments in TNG's Contract 302 Properties (also sometimes collectively referred to as the "Tabyl Block"). The Contract 302 Properties are comprised of six different areas referred to as Tabyl, Tabyl West, Bahyt, Munaibay North, Munaibay (or Munaibay Main), and the Interoil Reef, which is located below the Munaibay

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[163] Borankol Raw Materials Base Project prepared by NIPI Neftegaz, 2001, C-465; Certificate on the results of planned performance inspection of Kazakh legislation on subsoil and subsoil use and contract obligations of TNG, July 1-12, 2008, C-683; Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

[164] Reports of the MEMR for KPM, January 25 - February 6, 2010, C-385.

[165] Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

[166] Of that sum, US $66 million came from Vitol. As discussed in Section V.C.3.b, Vitol made an initial equity contribution of US $20 million and an additional US $46 million in debt financing.

[167] *See* Broscaru Testimony, Tr. January 2013 Hearing, Day 2, 31:14-23; *see also* First Lungu Statement ¶ 27.

[168] Act on the Unscheduled Inspection of TNG from the Geology Committee, July 16, 2010, C-315.

surface area. Because the Interoil Reef is located at some 6000 meters under Munaibay and is a carboniferous structure, it is also sometimes referred to as the Munaibay Reef or the Carboniferous Reef. Claimants' investments in the Contract 302 Properties included ordering and carrying out 2D and 3D seismic surveys and acquiring an ultra-deep drilling rig in order to exploit hydrocarbons from the Interoil Reef, and they led to significant discoveries of potential reserves in the Contract 302 Properties.[169]

129. In July 2008, Claimants informed the MEMR that TNG had discovered a significant oil and gas field by drilling the Munaibay No. 1 well in Contract No. 302, "which represented sufficient interest to carry out [an appraisal] of this field."[170] On October 10, 2008, TNG informed the MEMR that it planned to continue exploring the Contract 302 area because the Munaibay No. 1 well suggested "a high probability of additional discovery of more deep-lying raw hydrocarbon reservoirs on Munaibay area."[171] That was a direct reference to the Interoil Reef.[172] TNG also informed the MEMR that there were "raw hydrocarbon reservoirs in the exploration well No. 1 on the nearest Bahyt area."[173] TNG then applied to the MEMR to extend the exploration period of Contract 302.[174]

130. Also in the summer and early fall of 2008, Claimants were poised to complete a significant gas export deal. TNG had signed a contract with KazAzot to supply gas to its planned ammonia plant, and it was negotiating with KazTransGas to secure a gas export arrangement as part of that deal.[175] After Gasprom indicated to KazMunaiGas National Company ("KMG NC") that such an export deal should be arranged through their joint venture KazRosGas instead,[176] KMG NC replaced KazTransGas as the exporting partner in the contract with TNG. KMG NC and TNG signed the export deal in November 2008.[177]

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169 Stati Testimony, Tr. January 2013 Hearing, Day 2, 84:3-85:15.

170 Letter from TNG to the Geology and Subsoil Use Committee of the MEMR, July 24, 2008, C-20.

171 Letter from TNG to the MEMR, October 10, 2008, C-66.

172 *See* Tr. January 2013 Hearing, Day 1, 250:22-250:25.

173 Letter from TNG to the MEMR, October 10, 2008, C-66.

174 Application from TNG to the MEMR, October 14, 2008, C-67.

175 Agreement between KazAzot, TNG and KazTransGaz, 2008, C-302.

176 Letter from Gazprom to KazMunaiGas, October 27, 2008, R-343.

177 Tri-partite Agreement between TNG, KazMunaiGas, and KazAzot, November 17, 2008, C-97.

131. Having completed a transformation of the Borankol and Tolkyn fields and positioned KPM and TNG for success and increasing profits in subsequent years, Claimants decided to sell their producing investments in Kazakhstan. A successful first offer for the sale of KPM's and TNG's assets (without the Contract 302 Properties) in September 2008 drew the attention of the Kazakh state-owned oil and gas company, KMG E&P, as well as international oil and gas companies such as KNOC, OMV E&P, Total E&P, Turkish Petroleum Corp, and attracted indicative offers for the assets ranging from US $550 million to US $1.55 billion.[178]

132. Importantly, during the life of Claimants' investments, from 1999 until the fall of 2008, they encountered no serious problems with any governmental bodies. But the attractive transformation, which Claimants achieved in just under a decade, obviously grabbed the attention of Kazakhstan's leaders. President Nazarbayev colluded with the then-President of Moldova, Vladimir Voronin, to devise a pretext for inspecting, and ultimately seizing, Claimants' investments.[179] Kazakhstan has not denied that President Nazarbayev asked President Voronin to write a formal letter accusing Anatolie Stati of wrongdoing.[180] As the Tribunal is well aware, that letter and President Nazarbayev's October 14, 2008 order to his Financial Police to carry out a thorough investigation of Mr. Stati's companies marked the beginning of the end for KPM and TNG.

133. Kazakhstan originally attempted to justify President Nazarbayev's order as "routine." But that argument fell apart at the October 2012 Hearing, when the Minister of Oil and Gas, Mr. Mynbaev, testified that there was nothing at all routine about President Nazarbayev directing the Financial Police to inspect KPM and TNG. Minister Mynbaev testified as follows:

> Q: Is it unusual, Minister, for the President of Kazakhstan to direct the financial police to inspect energy companies?
>
> A: This happens not often, I would say.

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[178] Project Zenith - Overview of Non-Binding Offers, September 27, 2008, C-17; Indicative Proposal for Project Zenith from NKOC, September 26, 2008, C-18; Indicative Proposal for Project Zenith from KazMunaiGas, September 25, 2008, C-19; Indicative Offer for Project Zenith from Meridian Petroleum, October 1, 2008, C-71; Indicative Offer for Project Zenith from China National Petroleum Corporation, September 2008, C-72; Indicative Offer for Project Zenith from Safmar, September 26, 2008, C-73; Indicative Offer for Project Zenith from Turkish Petroleum Corp., C-74; Indicative Offer for Project Zenith from Total, September 26, 2008, C-75; and Indicative Offer for Project Zenith from OMV, September 26, 2008, C-76.

[179] Interview of former President Voronin during the television program "In Depth" on PROTV Chisinau, January 24, 2011, C-78.

[180] Second Expert Report of Martha Brill Olcott dated August 7, 2012 (hereinafter "Second Olcott Report"), ¶ 179.

Q: It was pretty extraordinary, wasn't it?

A: I think I would agree that this is quite a rare situation.[181]

134. Claimants' expert on Kazakhstan's political climate, Scott Horton, has explained the "rare situation" when the Kazakh Financial Police becomes involved and raises allegations of a foreign investor's misconduct: it is a tool Kazakhstan uses to attempt to shroud an illegal nationalization with an air of legitimacy.[182] Mr. Horton writes:

> [T]he Financial Police emerged as the preferred tool of natural resource nationalism — supporting efforts to repress, limit or eliminate entirely unwanted foreign investment in the natural resources sector. Political leaders recognized that outright expropriation could have unpleasant consequences in international commercial arbitrations. But, they reasoned, a taking that was cloaked in a series of tax assessments, fines, penalties and adjustments of licenses or permits might be more plausibly accepted as normal, if somewhat harsh, administrative process.[183]

135. That description is emblematic of what happened in the present case. Over a period of almost seven months, from mid-October 2008 to mid-May 2009, the Financial Police carried out numerous inspections and searches of KPM and TNG, each of which was highly disruptive and designed to find (or create) a hook on which to hang Claimants.[184] Claimants' legal counsel for KPM and TNG, Mr. Alexander Condorachi, testified that the inspections

> were seriously disruptive ... for the work of the company... [O]n top of distracting people from performing their daily duties, these inspections also carried with them emotional disruption, because it was quite unpleasant to be in this atmosphere and in the environment created around the company due to these multiple and massive inspections, very intensive ones. ... [The Financial Police]

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[181] Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 98:19-25.

[182] Kazakhstan disputes Claimants' assertion that the Financial Police are under the control of President Nazarbayev, and instead tries to argue that the Financial Police is an "independent" and "accountable agency." *See* Rejoinder on Liability ¶ 248. That is untrue. President Nazarbayev established the Financial Police by Presidential Decree No. 536 on January 22, 2001, and according to the regulations governing its work (also approved by Presidential Decree), the Financial Police is directly subordinated and accountable to the President.

[183] Horton Report ¶ 63.

[184] *See, e.g.*, Order from Financial Police to MEMR, October 20, 2008, C-9; Order from Financial Police to the Tax Committee, October 24, 2008, C-10; Order from the Financial Police to the Customs Committee, October 18, 2008, C-11; Order from the Financial Police to the Geology Committee, October, 28, 2008, C-12; Letter from the Financial Police to the Ecology Committee, October 28, 2008, C-13; Letter to the Ministry of Emergency Situations from its Mangystau Region Department, October 31, 2008, C-14; and Letter from the National Bank of Kazakhstan to the Financial Police, November 2008, C-15.

> extracted all the documents which have to do with our commercial activities, starting with the invoices, loading bills, bills of lading, shipping documents and so on, not to mention any drafts and design documentation; everything that has to do with those ... pipelines' construction, and not to mention any enquiries, answers to the enquiries, correspondence and so on.[185]

Mr. Condorachi further explained that the inspections continued without abatement for approximately seven months. He testified that

> if not on a daily basis, the financial inspection officials visited [KPM and TNG] at least every other day in the winter [of 2008] and early spring of 2009, and they were quite demanding, including the deadlines that they gave us to provide them with the information. They didn't care if the management was present or not, because officially the management must be in place when documents are extracted and acts — receipts of such documents were signed; they would basically just stay in the room until we delivered what they wanted us to deliver, and wouldn't leave...[186]

136. Before the inspection period ended and as described in detail in Section III.B.1, below, Kazakhstan's Financial Police had fabricated the basis for a crime.[187] Former General Director of TNG, Mr. Alexandru Cojin, explained at the October 2012 Hearing that the Financial Police forced the Geology Committee to include a statement in its November 2008 inspection reports that KPM and TNG did not have licenses to operate main pipelines.[188] The Financial Police also insisted that Mr. Cojin and Mr. Cornegruta sign off on those reports, which were later used to support Kazakhstan's criminal claims against Mr. Cornegruta and ultimate verdict against Mr. Cornegruta and KPM.[189] Kazakhstan opened a formal criminal case against KPM on December 15, 2008, and against TNG in the weeks following.[190] Kazakhstan also issued

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185 Tr. October 2012 Hearing, Day 2, 149:3-151:4.

186 Condorachi Testimony, Tr. October 2012 Hearing, Day 2, 151:5-152:2.

187 *See* Report on results of unscheduled inspection of Geology Committee, November 4-11, 2008, C-86; Letter from the Agency for Regulation of Natural Monopolies to the Financial Police, November 18, 2008, C-88; Order from the Financial Police to the Tax Committee regarding KPM, November 17, 2008, C-89; and Statement determining the income received as a result of transportation and further sale of oil for KPM and TNG, November 19, 2008, C-450.

188 Cojin Testimony, Tr. October 2012 Hearing, Day 3, 26:8-22; *see also* section III.B.1, *infra*.

189 *Id*.

190 *See* Order Initiating Criminal Proceedings, December 15, 2008, C-632.

warrants for the arrest of key managers and the Financial Police targeted, followed, and interrogated the companies' personnel.[191]

137. In addition to waging criminal investigations against the companies, Kazakhstan slandered them in the press. On December 18, 2008, the financial press reported spurious allegations by the MEMR that Claimants had forged their ownership documents of TNG, which allegedly defrauded Kazakhstan of its pre-emptive right to acquire TNG.[192] As Claimants have established, however, Kazakhstan did not even have a pre-emptive right during the time period when it claimed that ownership of TNG was illegally transferred, and Kazakhstan never substantiated its allegations of forgery and fraud.[193] Kazakhstan's malicious publication of false allegations caused Credit Suisse to back out of a beneficial financing arrangement that Claimants were on the cusp of securing, which subsequently became extremely significant as financial conditions worsened in 2009.[194]

138. Thus, before the end of 2008, Kazakhstan bombarded KPM and TNG with investigations, primed KPM for a preordained criminal conviction, and publicly clouded the title to TNG. Any potential buyer — of which there were several major international oil and gas companies at the time — would have backed away from companies with such charges hanging over them.

139. Kazakhstan's campaign continued throughout 2009. On February 10, 2009, the Kazakh tax authorities issued a baseless back tax assessment against KPM and TNG and claimed that the companies owed upward of US $62 million.[195] On April 25, 2009, Kazakhstan arrested KPM's General Manager, Mr. Cornegruta. That arrest caused other high-level managers of both KPM and TNG to flee Kazakhstan. After a trial that amounted to a denial of justice, Kazakhstan

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[191] Letter from the Financial Police to KPM and TNG, December 24, 2008, C-94; Summons to Witnesses from the Financial Police, December 24, 2008, C-654; First Cojin Statement ¶¶ 13-24; First Stejar Statement ¶¶ 15-29; *see also* Indictment of Mr. Cornegruta, June 27, 2009, at 17, 19 (noting the "international search" for Messrs. Spasov, Salagor, and Cojin), C-454.

[192] Notice from the MEMR to TNG, December 18, 2008, C-140; Press release circulated on INTERFAX from MEMR, December 18, 2008, C-141; Email from A. Petrosius to A. Lungu, December 18, 2008, C-625.

[193] *See* section II.B.4.c, *supra*.

[194] Email from A. Petrosius to A. Lungu, with attachment of Indicative Term Sheet from Credit Suisse, December 5, 2008, C-521; Letter from Merix International Ventures, Ltd. to Credit Suisse, October 23, 2008, C-523.

[195] Notice Nos. 28 and 29 to KPM and TNG from the Tax Committee, February 10, 2009, C-155; Complaint from TNG to the Tax Committee, February 27, 2009, C-156. That dispute was the largest of three baseless tax disputes Kazakhstan created in the wake of the 2008 investigation directive. *See* Statement of Claim ¶¶ 156-174; Reply on Jurisdiction and Liability ¶¶ 231-239.

sentenced Mr. Cornegruta to four years of hard labor in Kazakh prison, and it assessed a fine against KPM — which was not a party to the case — of US $145 million for Mr. Cornegruta's alleged crime.

140. Within days of Mr. Cornegruta's arrest, on April 30, 2009, the Financial Police ordered the sequestration of 100% of KPM's and TNG's shares,[196] as well as their Subsoil Use Contracts,[197] and key property (including their pipelines).[198] Those measures expressly prohibited Claimants from carrying out "any actions related to the alienation or transfer of the sequestered property...to third parties."[199] Those orders came into force before the end of May 2009, as a result of the fabricated criminal accusation that KPM's and TNG's pipelines were "main" pipelines, but well before the criminal court had issued any judgment against Mr. Cornegruta and KPM. They also ensured that Claimants would not be able to sell KPM, TNG, or their assets (in the unlikely case that Claimants could secure a buyer notwithstanding the cloud over their title to TNG, the public claims of fraud, and the other troubles Kazakhstan had caused them by this point in time).

141. After the judgment was issued, Kazakhstan continued its enforcement measures into 2010, while depriving KPM of any right to appeal the decision being enforced against it.[200] Those measures included freezing KPM's bank accounts, prohibiting KPM from import and export operations, and calling for the sale of KPM's property to satisfy the US $145 million penalty.

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196 *See* Orders to arrest all shares of KPM and TNG, April 30, 2009, C-486 and C-487; Minutes of the arrest of KPM's and TNG's shares, May 13, 2009, C-488 and C-489.

197 *See* Order to arrest KPM's Contract No. 305, April 30, 2009, C-490; Order to arrest TNG's Contracts No. 210 and No. 302, April 30, 2009, C-491.

198 *See* Order to arrest KPM's pipeline, April 30, 2009, C-492; Minutes of the arrest of KPM's pipeline, May 13, 2009, C-493; Order to arrest TNG's gas pipeline, April 30, 2009, C-494; Minutes of the arrest of TNG's pipeline, May 13, 2009, C-495; Order to arrest TNG's condensate pipeline, April 30, 2009, C-496; Order to arrest KPM's motor vehicles, April 30, 2009, C-497; Minutes of the arrest of KPM's motor vehicles, May 13, 2009, C-498; Order regarding arrest of KPM's property, May 13, 2009, C-499; Letter from Financial Police requesting value of arrested property, May 19, 2009, C-500.

199 *See, e.g.*, Minutes of the arrest of KPM's shares, May 13, 2009, C-488.

200 *See* Order on initiation of enforcement proceedings, January 5, 2010, C-501; Arrest of KPM's funds, February 26, 2010, C-502; Order for transfer of KPM's funds, March 15, 2010, C-504; Order for transfer of KPM's funds, March 18, 2010, C-505; Order for transfer of KPM's funds, April 28, 2010, C-506; Notice of arrest of KPM's extracted hydrocarbons, May 11, 2010, C-507; *see also* Section III.B.1.e, *infra*, regarding KPM's attempts to appeal and challenge the penalty and enforcement measures.

142. The MEMR conducted another full-scale inspection of KPM and TNG in January 2010.[201] That inspection resulted in no allegations that the companies had violated their subsoil use contracts and instead confirmed that KPM and TNG had each exceeded their work program requirements notwithstanding the onslaught of governmental harassment.[202] Kazakhstan thus needed another excuse to pursue Claimants. In June 2010, purportedly responding to a brief hand-written complaint of four local residents to the General Prosecutor's Office in Astana, the Financial Police spear-headed a final inspection barrage against KPM and TNG. At the October 2012 Hearing, the Tribunal learned that this final round of inspections was in fact ordered by the Kazakh Prime Minister.[203] Armed with a second executive mandate, Kazakhstan's various ministries concocted a handful of meritless allegations that the companies had committed breaches of their legal and contractual obligations. Within one week of notifying KPM and TNG of those allegations, the MEMR descended on the premises, cancelled the contracts, and seized the companies' assets. Kazakhstan's official takeover was complete.

143. The following timeline illustrates the progression of Claimants' companies from successful oil and gas production businesses up until late 2008, and the many ways in which Kazakhstan's executive-mandated coercion campaign harmed Claimants after October 14, 2008, culminating in the direct expropriation of July 2010.

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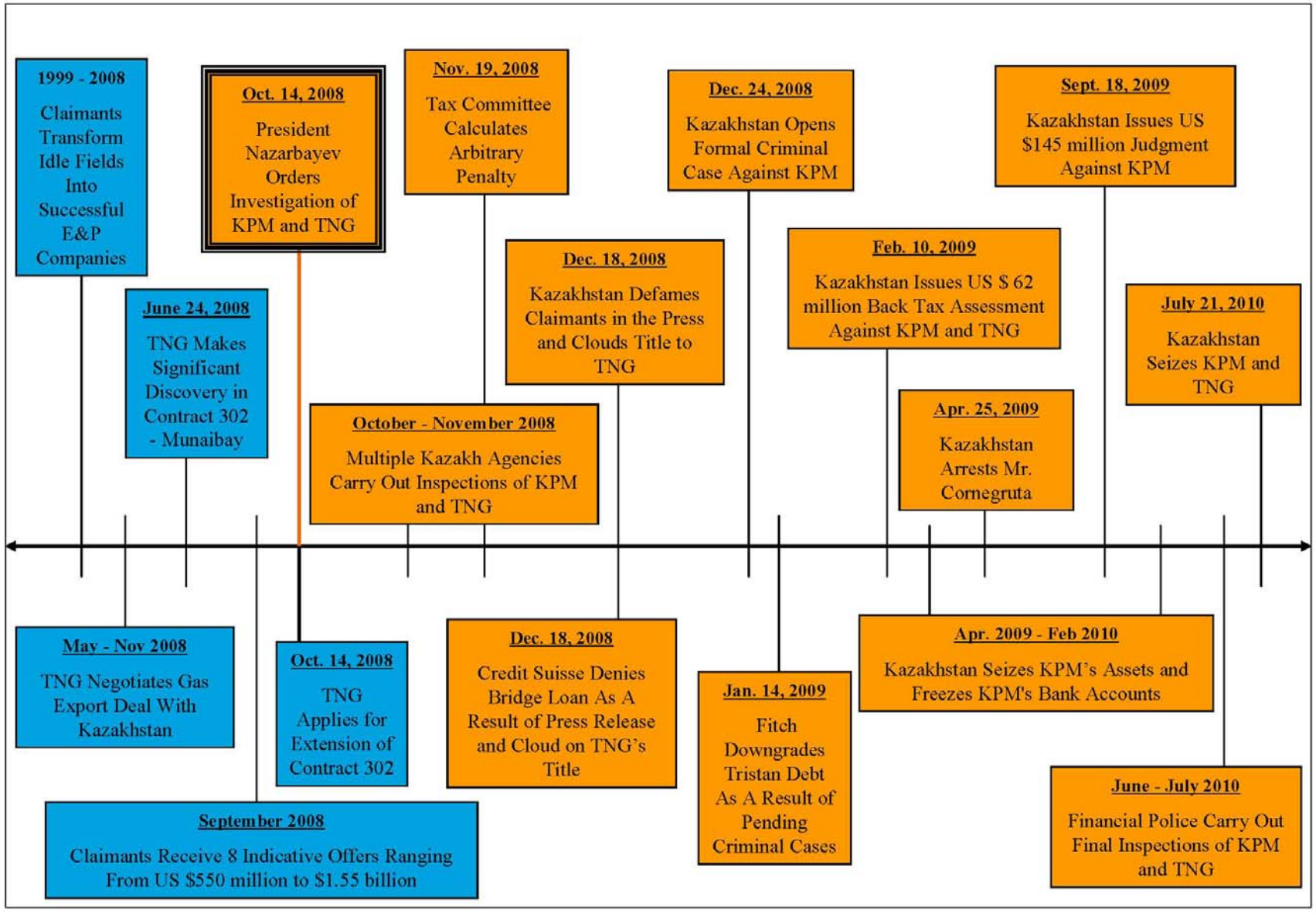
[201] Reports of the MEMR for KPM, January 25 - February 6, 2010, C-385; Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

[202] *Id*.

[203] Report from Rakhimov to Chief of Financial Police, July 9, 2010, C-711.


1999 - 2008
Claimants Transform Idle Fields Into Successful E&P Companies
June 24, 2008
TNG Makes Significant Discovery in Contract 302 - Munaibay
May - Nov 2008
TNG Negotiates Gas Export Deal With Kazakhstan
September 2008
Claimants Receive 8 Indicative Offers Ranging From US $550 million to $1.55 billion
Oct. 14, 2008
President Nazarbayev Orders Investigation of KPM and TNG
Oct. 14, 2008
TNG Applies for Extension of Contract 302
Nov. 19, 2008
Tax Committee Calculates Arbitrary Penalty
October - November 2008
Multiple Kazakh Agencies Carry Out Inspections of KPM and TNG
Dec. 18, 2008
Kazakhstan Defames Claimants in the Press and Clouds Title to TNG
Dec. 18, 2008
Credit Suisse Denies Bridge Loan As A Result of Press Release and Cloud on TNG's Title
Dec. 24, 2008
Kazakhstan Opens Formal Criminal Case Against KPM
Jan. 14, 2009
Fitch Downgrades Tristan Debt As A Result of Pending Criminal Cases
Feb. 10, 2009
Kazakhstan Issues US $ 62 million Back Tax Assessment Against KPM and TNG
Apr. 25, 2009
Kazakhstan Arrests Mr. Cornegruta
Apr. 2009 - Feb 2010
Kazakhstan Seizes KPM's Assets and Freezes KPM's Bank Accounts
Sept. 18, 2009
Kazakhstan Issues US $145 million Judgment Against KPM
July 21, 2010
Kazakhstan Seizes KPM and TNG
June - July 2010
Financial Police Carry Out Final Inspections of KPM and TNG

144. As can be seen, immediately following the October 14, 2008, order to thoroughly investigate Mr. Stati's companies, (i) Kazakhstan's Financial Police carried out disruptive and intimidating inspections and fabricated the basis for a groundless criminal conviction, which it then enforced against KPM by way of a US $145 million penalty, and (ii) Kazakhstan clouded the title to TNG with false claims of forgery and a pre-emptive right, which scared away potential buyers and much-needed financing. Those specific acts destroyed Claimants' ability to sell their investments in 2008 and grossly interfered with their ability to manage the companies. That damage done, Kazakhstan continued to harm Claimants in early 2009 by imposing a baseless US $62 million back tax assessment against the companies, which risked their bankruptcy; by failing to execute the extension of Claimants' Contract No. 302, which interfered with Claimants' attempts to prove the Contract No. 302 reserves; and by seizing KPM's bank accounts and attaching all of its assets, which directly harmed the business and hampered KPM's ability to operate. All of that Treaty-breaching mistreatment and resulting harm occurred long before Kazakhstan's Ministry of Oil and Gas finally seized KPM's and TNG's assets in July 2010.

145. The multitude of misconduct carried out in response to Nazarbayev's October 14, 2008, order substantially interfered with Claimants' ability to manage, control, and dispose of their investments. Claimants' personnel were diverted from their usual duties and forced to monitor, respond to, follow-up on, and challenge each of Kazakhstan's illegal actions. Claimants have produced evidence of no fewer than 14 acts that Kazakhstan waged against their investments, causing substantial interference with Claimants' normal business operations, prior to the July 2010 direct expropriation:

No.	Act / Issue	Duration
1	2008 Audits / Inspections Led by Financial Police[204]	October - December 2008
2	Financial Police Searches of KPM and TNG and Seizures of Corporate Documents[205]	December 2008 - May 2009

[204] *See*, *e.g.*, President Nazarbayev's Investigation Instructions, October 14, 2008, C-8; Order from the Financial Police to MEMR, October 20, 2009, C-9; Order from the Financial Police to the Tax Committee, October 24, 2008, C-10; Order from the Financial Police to the Geology Committee, October 28, 2008, C-12; Letter from the National Bank of Kazakhstan to Financial Police, November 2008, C-15; Inspection Results from Geology Committee, November 4-11, 2008, C-86 and C-87; Letter from the MEMR to the Financial Police, December 4, 2008, C-422; Letter from Financial Police to Deputy Prime Minister of Kazakhstan, December 10, 2008, C-448; Letter from the Financial Police to KPM and TNG, December 24, 2008, C-94.

3	False Preemptive Right Claim and Allegations of Fraud and Forgery[206]	December 2008, but never pursued
4	Contract 302 Extension Request and Agreed but Unexecuted Extension[207]	October 2008 - July 2010
5	Wrongful Corporate Back Tax Dispute[208]	November 2008 / February 2009 - June 2010; settled and then revived after July 2010 seizure
6	Baseless Export Tax Dispute[209]	November 2008 - March 2010
7	Groundless Transfer Price Dispute[210]	November 2008 - July 2010; litigation still pending as of seizure
8	Criminal Investigation of KPM and TNG[211] (including KPM's efforts to appeal judgment)	November/December 2008 - May/July 2010

[205] *See*, *e.g.*, Minutes of the On-Site Investigation, December 30, 2008, C-95; Order on Performance of Seizure of Documents from TNG, December 26, 2008, C-605 and C-606; Letter from Financial Police to KPM requesting documents, January 23, 2009, C-607; Reports and Protocols of seizure of KPM's and TNG's documents, February - April, 2009, C-608, C-609, C-610, C-611, C-612, C-613, C-614, C-615, C-616, C-617, and C-618; Minutes of the On Site Search, May 6-7, 2009, C-114; Document Request from Financial Police to KPM, May 15, 2009, C-668.

[206] *See*, *e.g.*, Notice from the MEMR to TNG, December 18, 2008, C-140; Press release circulated on INTERFAX from the MEMR, December 18, 2008, C-141 and C-625; Letter from TNG to MEMR, December 22, 2008, C-142; Letter from MEMR to TNG, December 29, 2008, C-144; Letter from TNG to MEMR, January 19, 2009, C-145; Notice from the MEMR to TNG, February 27, 2009, C-146; Letter from TNG and Terra Raf to MEMR, March 18, 2009, C-41; Letters from TNG to MEMR, March 2009, C-147 and C-148.

[207] *See*, *e.g.*, Application from TNG to MEMR, October 14, 2008, C-67; Letter from TNG to MEMR, February 16, 2009, C-166; Letters from TNG to MEMR, March 9, 2009, C-167; Draft Minutes of Meeting between MEMR and Claimants, March 19, 2009, C-42 and C-111; Letter from the MEMR to TNG, April 9, 2009, C-27; Draft Addendum to Contract 302, April 30, 2009, C-168; Letter from TNG to MEMR, September 17, 2009, C-169; Letter from TNG to MEMR, December 28, 2009, C-170; Notice from MEMR to TNG, May 6, 2010, C-172; Letter from MOG to TNG, May 7, 2010, C-173.

[208] *See*, *e.g.*, Instructions of the Tax Committee, November 10, 2008, C-149 and C-150; Notices to KPM and TNG from the Tax Committee, February 10, 2009, C-155; Complaint from TNG to the Tax Committee, February 27, 2009, C-156; *see also* the various court decisions on this issue, Exhibits 7 to 13 to Second Maggs Report.

[209] *See*, *e.g.*, Order from the Financial Police to the Customs Committee, October 18, 2008, C-11; Decision of the Board of Appeal of the Mangystau Regional Court, December 23, 2008, C-161; Letter from the Financial Police to the Executive Secretary of the Ministry of Finance, November 25, 2008, C-162; Notices from the Regional Customs Committee to KPM and TNG, February 24, 2010, C-44 and C-479; Notices from the Central Customs Committee to KPM, March 31, 2010, C-130; First Condorachi Statement at ¶¶ 34-37.

[210] *See*, *e.g.*, Letter from Tax Committee to Financial Police, November 13, 2008, C-38; Notifications of the Tax Committee to KPM and TNG, December 29, 2009, C-137 and C-138, *see also* First Condorachi Statement at ¶¶ 32-33.

[211] *See*, *e.g.*, Letter from Financial Police to Deputy Prime Minister of Kazakhstan, December 10, 2008, C-448; Order Initiating Criminal Proceedings, December 15, 2008, C-632; Letter from Financial Police to KPM and TNG, December 24, 2008, C-94; Resolution on the preliminary investigation, January 14, 2009, C-453; Letter from Financial Police to TNG, February 2, 2009, C-98; Press Release of Financial Police, June 17, 2009, C-118; Letter from KPM to Aktau City Court, September 22, 2009, C-705; KPM's Claim of Appeal, January 25, 2010, C-481; KPM's request for court decision, January 14, 2010, C-566; KPM's complaint

9	Mr. Cornegruta's Arrest, Prosecution, and Sentence[212]	April 2009 - June 2010 (and beyond)
10	Sequestration of KPM's and TNG's Assets and Shares, and Enforcement Actions Against KPM[213]	April 2009 - June 2010
11	Bankruptcy Charges[214]	January 2010 - April 2010
12	January / February 2010 MEMR Inspections[215]	January - February 2010
13	Interference with Cliffson Sale[216]	April - June 2010
14	June/July 2010 Inspections / Contract Termination / Assets Seizure[217]	June/July 2010

regarding challenge of court decision, January 21, 2010, C-567; KPM's Challenge, February 8, 2010, C-637; KPM's claim of appeal, February 25, 2010, C-640; KPM's Claims of Cassation, March 26, 2010, C-670 and May 11, 2010, C-642.

212 *See*, *e.g.*, Indictment of Mr. Cornegruta, June 27, 2009, C-454; Complaint on behalf of Mr. Cornegruta, C-113; Request from Mr. Cornegruta to Stop Criminal Proceeding, June 15, 2009, C-478; Order on Refusal, May 8, 2009, C-563; Motion to Stop Criminal Proceeding, July 30, 2009, C-601; Order declining petition, July 31, 2009, C-602; Request to not detain Mr. Cornegruta, April 27, 2009, C-633; Request to terminate proceeding, October 19, 2009, C-634 and September 19, 2009, C-656; Complaint to Regional Prosecutor regarding Illegal Arrest, May 20, 2009, C-658; Judgment of Aktau City Court, September 18, 2009, C-117; Appeal, October 1, 2009, C-659; Appeal, October 5, 2009, C-660; Decision on Appeal, November 12, 2009, C-565; Letter from the General Prosecutor's Office to the Ministry of Justice of Moldova, June 10, 2010, C-200.

213 *See*, *e.g.*, Orders to Arrest all Shares of KPM and TNG, April 30, 2009, C-486 and C-487; Order to Arrest Contract 305, April 30, 2009, C-490; Order to Arrest Contracts 210 and 302, April 30, 2009, C-491; Order to Arrest KPM's Pipeline, April 30, 2009, C-492; Orders to Arrest TNG's Pipelines, April 30, 2009, C-494 and C-496; Order regarding arrest of KPM's Property, May 13, 2009, C-499, Letter from Financial Police to KPM requesting value of arrested property, May 19, 2009, C-500; Writ of Execution, December 29, 2009, C-119; Orders from Enforcement Officers to KPM, January - March 2010, C-121, C-122, C-79, C-298 and C-126; Order on Enforcement Proceeding, January 5, 2010, C-501, Orders on Transfer of Funds, March 2010, C-503, C-504, C-505, and C-506; Order on arrest of KPM's extracted hydrocarbons, May 11, 2010, C-507; Order regarding selling the whole property of KPM, June 9, 2010, C-199; Repeated Warning to KPM, June 15, 2010, C-201.

214 *See*, *e.g.*, Bankruptcy Notice, January 26, 2010, C-157; *see also* First Pisica Statement ¶¶ 54-55; First Condorachi Statement ¶¶ 38-41.

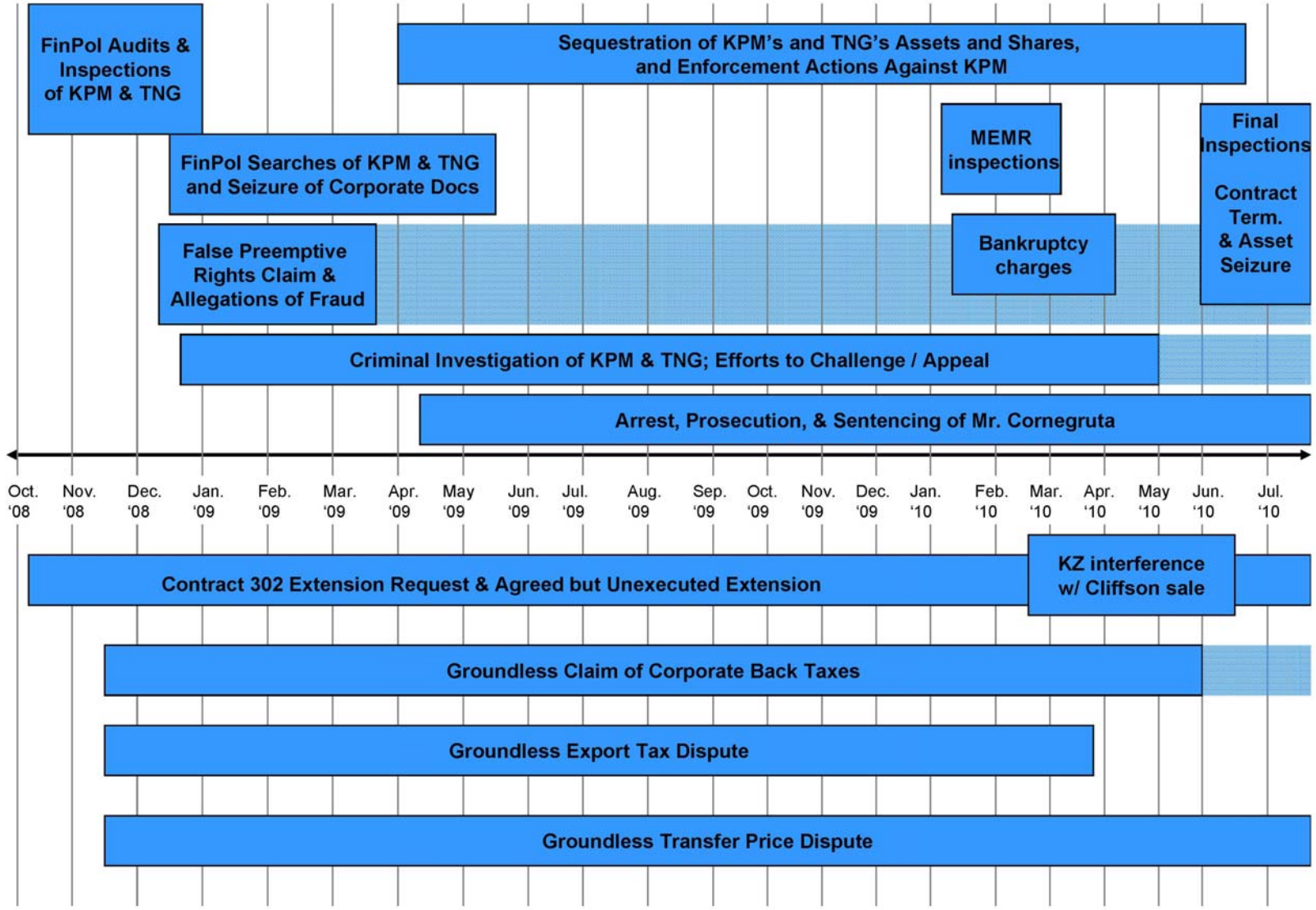
215 *See*, *e.g.*, MEMR Letter to KPM and TNG, January 25, 2010, C-171; Reports of the MEMR for KPM and TNG, January-February 2010, C-385 and C-386; Minutes on the Results of the Extraordinary Verification of the fulfillment of contractual and licensing obligations, January-February 2010, C-599.

216 *See*, *e.g.*, Letters from KPM and TNG to MOG and MIT, April 12, 2010, C-524, C-525, C-526, and C-527; Letters from MOG to KPM and TNG, April 30, 2010, C-528 and C-529; Letters from MOG to KPM and TNG, June 1, 2010, C-530 and C-531; Letters from KPM and TNG to MOG, June 12, 2010, C-532 and C-533; Cliffson Transaction Data sent to the State, June 2010, C-671; *see also* Calancea Testimony, Tr. October 2012 Hearing, Day 3, 59:18-67:17.

217 *See*, *e.g.*, Notices of Inspection of KPM and TNG, June-July 2010, C-174, C-175, C-177, C-178, C-179, C-180, C-181, C-182, and C-185; Notices to KPM and TNG of infringement of contractual obligations, July 14, 2010, C-2, C-6, and C-7; Answers from KPM and TNG to the notification of contract infringements, July 19, 2010, C-24, C-25, and C-26; Acts on the Unscheduled Inspections, June-July, 2010, C-315, C-647, C-648, C-649, C-650, C-651, C-652, C-653, C-687, C-688, and C-689; Notices terminating KPM's and TNG's Subsoil Use Contracts, July 21, 2010, C-3, C-4, and C-5.

The impact of those acts on KPM's and TNG's day-to-day operations is temporally depicted in the following graph.

KAZAKH INTERFERENCE WITH DAILY OPERATIONS OF KPM AND TNG



146. Kazakhstan cannot credibly deny any of the foregoing facts. Instead, its feeble defense is that (i) all of the actions just described were perfectly legal and (ii) the facts just described did not cause any damage to Claimants. Throughout this submission, Claimants detail the reasons why neither assertion has any merit. Put simply, Kazakhstan's unlawful acts and the substantial harms caused to Claimants' investments are indisputable.

B. President Nazarbayev's October 2008 Order Commenced An Illegal Campaign Against Claimants

147. Kazakhstan violated the ECT and international law by using President Nazarbayev's October 14, 2008, instruction to "thoroughly check" Claimants' companies as a pretext to fabricate a number of groundless allegations against Claimants, the most egregious of which are addressed in detail in the following sections. First, by mid-November 2008, less than one month from the date of Nazarbayev's order, Kazakhstan's Financial Police had manufactured the grounds for a baseless criminal accusation, which Kazakhstan ultimately used to secure a guilty verdict and a ruinous fine against KPM. As discussed below, everything about the criminal investigation, prosecution, penalty, and enforcement was preordained by the Financial Police.

148. In December 2008, Kazakhstan also publicly defamed Claimants and clouded their title to TNG, causing the immediate loss of an important financing deal and undermining Claimants' ability to dispose of the company. Additionally, for the better part of 2009 and into 2010, Kazakhstan strung along Claimants by undertaking to extend Contract No. 302 and then refusing to execute the extension. In February 2009, using the 2008 inspections as a pretext, Kazakhstan crippled Claimants with illegal and baseless tax assessments, ensuring that Claimants would spend months litigating Kazakhstan's spurious claims of millions of dollars in groundless assessments. Finally, because none of its previous acts, while each harmful and devastating to Claimants' plans and operations, succeeded in coercing Claimants into abandoning their investments, Kazakhstan initiated its final inspections in June and July 2010, through which Kazakhstan effected the direct expropriation of Claimants' investments by fabricating alleged contract violations.

149. Each of those acts of misconduct is clearly established by conclusive evidence in this case; indeed, much of that evidence is not disputed. Each of those acts also constitutes a separate, individual breach of the ECT and international law. Taken together, Kazakhstan's liability to Claimants is indisputable.

1. Kazakhstan Fabricated the "Main Pipeline" Issue to Bring About a Criminal Conviction and Devastating Fine

150. By November 2008, Kazakhstan had manufactured a false claim that KPM operated a "main" pipeline without a license, and it had determined the enormous penalty that it would enforce against KPM as a result. Immediately following President Nazarbayev's October 14, 2008, order to "thoroughly check" KPM and TNG, Kazakhstan's Financial Police initiated and orchestrated a multitude of inspections of the companies.

151. The Kazakh agencies that carried out those inspections at the behest of the Financial Police included the MEMR, the Tax Committee of the Ministry of Finance, the Customs Control Committee, the Geology and Subsoil Use Committee, the Ecology Committee, the Ministry of Emergency Situations, and the Kazakh National Bank.[218] Since KPM and TNG were both subject to regular monitoring and scheduled inspections by those same agencies, if any irregularity — much less any illegality — with respect to their operations existed, those agencies would have identified it long before. That is especially true for something as obvious and immovable as the operation of a "main" pipeline without a license.

152. In fact, none of the post-October 2008 inspections carried out under "cover" of Nazarbayev's directive indicated any violations of any laws, and none of the agencies that regularly inspected the companies raised any claims of illegality as a result of those inspections. Consequently, the Financial Police intervened and concocted an illegality.

153. It soon became obvious that the Financial Police were looking for a "hook" on which to base an allegation. As TNG's General Manager, Mr. Cojin, testified during the October 2012 Hearing:

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[218] Letter from MEMR to Financial Police, October 24, 2008, C-432; Letter from Financial Police to Geology and Subsoil Use Committee of MEMR, October 28, 2008, C-433; Resolution from Financial Police on inspection of KPM by National Bank of Kazakhstan, October 28, 2008, C-434; Resolution from Financial Police for inspection of TNG by Geology Committee, October 28, 2008, C-435; Resolution from Financial Police for a complete tax audit of KPM, October 28, 2008, C-436; Resolution from Financial Police for Inspection of KPM's Work Safety Conditions by the Ministry of Emergency Situations, October 28, 2008, C-437; Financial Police Report Regarding Compliance with Licensing and Contractual Conditions, October 30, 2008, C-438; Letter from the Ministry of Emergency Situations to the Financial Police, undated, C-439; Letter from Financial Police to Committee of Customs Control, November 7, 2008, C-440; Letter from Financial Police to Agency for Regulation of Natural Monopolies, November 12, 2008, C-441; Letter from Financial Police to Customs Control Committee, November 12, 2008, C-442; Letter from MEMR to Financial Police regarding exports of KPM and TNG, November 14, 2008, C-443; Letter from MEMR to Financial Police regarding Acts of Inspection of TNG, November 18, 2008, C-445; Resolution for examination of TNG by the Customs Control Department, November 18, 2008, C-446; Order from Financial Police for a Comprehensive Tax Inspection of KPM, November 28, 2008, C-447.

> I had never experienced and the company had never experienced criminal accusations, and it was unusual for us because the volumes of the information which were requested, and the directions of the investigation of the financial police, gave us reason to think that they came to the company in order to find something criminal. And that's what they've picked up on: that was the main pipelines allegations.[219]

154. It did not take the Financial Police long to identify which agency it could manipulate — the Geology Committee of the MEMR — and to manufacture grounds for the criminal allegation that KPM and TNG operated "main" pipelines without a license. Indeed, within one month of President Nazarbayev's October 14, 2008, order, Kazakhstan's Financial Police had created the basis for what would become an unlawful criminal conviction of KPM's General Manager and a devastating fine against KPM in the amount of US $145 million. The Financial Police accomplished that goal by interfering in the results of the inspection that the MEMR's Geology Committee carried out from November 4 through 11, 2008.[220]

155. After its inspection of KPM and TNG, the Geology Committee prepared conclusions dated November 11, 2008.[221] Following those conclusions, the Financial Police took over the process and, on November 12, 2008, wrote to the Agency for the Regulation of Natural Monopolies ("ARNM") to confirm whether KPM and TNG held licenses to operate main oil and gas pipelines.[222] There was no reason for the Financial Police to confirm that KPM and TNG did not have licenses to operate main pipelines, however, because KPM and TNG never contended that they held such licenses or operated main pipelines. Nevertheless, the Financial Police considered that information significant and insisted that it be included in the inspection reports as "additional information" to the Geology Committee's conclusions.

156. That "additional information" would serve as the basis for the criminal allegation that KPM and TNG operated main pipelines without the proper license. The "additional information" that the Financial Police insisted be included in the Geology Committee's report read as follows:

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219 Cojin Testimony, Tr. October 2012 Hearing, Day 3, 28:15-22.

220 Report on unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use and contractual obligations of KPM, November 4-11, 2008, C-86; Report on unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use and contractual obligations of TNG, November 4-11, 2008, C-87.

221 *Id*.

222 Second Turganbayev Statement ¶¶ 5.1-5.2; *see also* Letter from the Agency for Regulation of Natural Monopolies to the Financial Police, November 18, 2008, C-88.

> According to the reply of the Republic of Kazakhstan's Agency on Regulation of Natural Monopolies, [TNG] and [KPM] have licenses [for] the following form of activity "operation of industrial explosive and mining facilities, elevating constructions, and also coppers, vessels and the pipelines working under pressure, drillings for oil and gas" granted by the Department of Energy and Mineral Resources of the Republic of Kazakhstan.
>
> The above-stated licenses issued to these legal entities ... do not give them the right to use the main gas pipelines, oil pipelines and oil-products pipelines.[223]

157. At that October 2012 Hearing, Mr. Cojin, who was present during the meetings with the Financial Police and the finalization of the Geology Committee's Acts of Inspection, described how the Financial Police insisted upon the inclusion of that language:

> At the final stage of the inspection, one of the officers of the financial police was very active and insisted that we should include this second sentence which describes the situation that we don't have a license or licenses for operating main pipelines. Mr. Cornegruta at that time was there. We asked why this was needed and he said, "This is needed." We refused to sign this document, and then we were told that, "In this case your inspection protocol will not be confirmed, and this will create great problems for you with observance of the contract," because in this way the contract would be violated. So the representative of the ministry said … "Look, you don't have main pipelines, why don't you wish to sign this sentence?"[224]

Despite the managers' initial hesitation to sign the reports with the language added by the Financial Police, the MEMR's acknowledgement that the pipelines in question were not "main" and the Financial Police's threat that failure to complete the inspection process would result in "great problems" for the companies caused the general managers to sign the reports on November 14, 2008.

158. Armed with the facially innocuous and uncontested confirmation that KPM and TNG did not have main pipeline licenses, the Financial Police ordered the Tax Department of the Ministry of Finance to calculate "the amount of income gained as result of carrying out activity without a license."[225] The Financial Police instructed that the calculation include "the amount of profit gained by Kazpolmunay LLP as result of transportation and

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[223] Report on unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use and contractual obligations of KPM, November 4-11, 2008, C-86; Report on unscheduled audit of performance of Kazakh legislation on oil, subsoil and subsoil use and contractual obligations of TNG, November 4-11, 2008, C-87.

[224] Cojin Testimony, Tr. October 2012 Hearing, Day 3, 26:8-22.

[225] Order from the Financial Police to the Tax Committee, November 17, 2008, C-89.

subsequent sale of its crude oil through the oil products pipeline belonging to Kazpolmunay LLP."[226] Notably, the instruction asked for a calculation of KPM's profits for "the subsequent sale of its crude oil," rather than merely any profits resulting from the operation of the pipeline. The only reason for such an instruction was to ensure a calculation beyond the meager profits KPM earned from providing oil transport services to TNG (its only customer). The stage was set for the Tax Committee to calculate a very large sum, which would be used to calculate the criminal penalty and satisfy the requirements for a serious offense.

159. Mr. Turganbayev's testimony at the October 2012 Hearing underscored the contrived, pre-ordained nature of the entire exercise. Mr. Turganbayev, the Financial Police officer who was leading the investigation in November 2008, confirmed that he ordered a calculation of the penalty that should be imposed on KPM for operating a main pipeline without a license before any Kazakh authority had concluded that any of the pipelines KPM operated were "main" pipelines. He testified as follows:

> Q. …by November 14th 2008 this geology committee report is signed, and it contains this language in here regarding the fact that KPM and TNG do not have licenses to use main pipelines; is that accurate?
>
> A. … "Additional information"…
>
> Q. … And then three days later, on November 17th 2008, you instruct the tax committee to calculate the amount of income for transportation and sale of crude oil through the pipeline in question; correct? …
>
> A. Yes, that's correct. Yes. ...
>
> Q. Had any governmental agency in Kazakhstan determined that KPM operated a main pipeline before you instructed the tax committee to calculate the amount of income earned from operation of that pipeline; yes or no?
>
> A. If you look at the first part of my decision, it says: "Pursuant to reply of the Agency ... for Regulation of Natural Monopolies ... Kazpolmunay ... does not have a state license for operation of trunk gas ... pipelines." This was the sufficient grounds for me to start this investigation. ...
>
> Q. By the time you asked the tax committee to calculate the amount of income earned by KPM through operation of a main pipeline, had any governmental agency in Kazakhstan concluded that KPM in fact operated a main pipeline?

[226] Order from the Financial Police to the Tax Committee, November 17, 2008 (emphasis added), C-89.

A. No. No.[227]

160. For its part, the Tax Department was obviously unconcerned by the missing predicate for the Financial Police's request — namely, a finding that KPM operated a "main" pipeline. Within two days of the Financial Police's instruction, on November 19, 2008, the Tax Department responded to the Financial Police with a report determining the amount of alleged "illegal profits" KPM received as a result of operating their own field pipelines.[228] As specifically instructed by the Financial Police, that report calculated the total illegal profit that KPM allegedly earned in 2005, 2006, and 2007 for sales of its crude oil, an amount in excess of 41 billion Tenge (approximately US $272 million today).

161. Ultimately, Kazakhstan succeeded in assessing about half of that figure against KPM as the penalty for its "crime." The ultimate assessment — again, almost entirely comprised of revenues from sales of oil — corresponded to the years that Mr. Cornegruta served as General Director of KPM. As Claimants demonstrated during the October 2012 Hearing, that penalty — 21.7 billion Tenge (US $145 million) — was both enormous and devastating. It was more than double KPM's highest-ever annual profits (which it earned in 2008), and it also greatly exceeded KPM's profits for 2007 and 2008 combined.

162. Even more incredibly, that figure was more than the total profits of KazTransOil — the largest transporter of oil in the country and the actual operator of Kazakhstan's "main" oil pipeline — in 2008.[229] Putting the sum of the fine in perspective underscores the deliberately abusive nature of Kazakhstan's penalty.

	Kazakh Tenge	US Dollars
Penalty Imposed Against KPM	21.7 Billion	$145 Million
KPM's Total Profits		2007: $23.5 Million
		2008: $66 Million
KazTransOil's Total Profits	2007: 14 Billion	
	2008: 20 Billion	

[227] Turganbayev Testimony, Tr. October 2012 Hearing, Day 5, 93:7-96:4.

[228] Statement determining the income received as a result of transportation and further sale of oil for KPM and TNG, November 19, 2008, C-450.

[229] KazTransOil Annual Report, 2008, C-708.

163. Again, the outrageous size of the penalty was a direct result of the Financial Police deliberately magnifying the alleged "illegal profit" by adding KPM's entire revenue on sales of its oil to the nominal service fee it received from TNG for transport services. At the October 2012 Hearing, Kazakhstan's Deputy General Prosecutor, Mr. Kravchenko, confirmed that Kazakhstan needed such a large penalty in order to secure a guilty verdict, because one element of the criminal offense that the prosecution had to establish in court was that Mr. Cornegruta obtained "illegal" profits in "an especially large amount."[230] Mr. Kravchenko testified as follows:

> Q. … Could Mr. Cornegruta have possibly have been found guilty of the crime of illegal entrepreneurial activity in an especially large amount had the prosecution and the court only relied on the income generated through operation and providing services through this pipeline?
>
> A. Maybe not in an especially large amount. ...[231]

164. Mr. Kravchenko also confirmed that, if Kazakhstan had instead calculated as the illegal profits the money that KPM earned solely from "operating" the 17.9 kilometer pipeline — *i.e.*, the transport service fee it received from TNG — Mr. Cornegruta would not have been convicted and the monetary assessment against KPM (if there would have been one) would have been insignificant. He testified:

> Q. ... I calculate [the service fee KPM earned for operating the 17.9 kilometer pipeline] as about US$12,650. Does that sound about right?
>
> A. It must be correct, yes.
>
> Q. Would you agree with me that in addition to falling below the threshold necessary to find Mr. Cornegruta guilty of the crime charged, a fine of US$12,650 would not have had much impact on KPM?
>
> A. Well, apparently one has to accept that this amount would be less burdensome for KPM.
>
> Q. Dramatically less burdensome than the US$145 million fine, wouldn't you say?
>
> A. Yes.[232]

165. Again, it was the Financial Police's decision to use all of KPM's revenue from sales of oil in calculating the fine, rather than merely the few thousand dollars KPM earned

[230] Kazakh Criminal Code, art. 190(2)(b), C-508.

[231] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 101:13-19.

[232] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 102:1-12.

from "operating" the pipeline. While that was already apparent from the documentary evidence, Mr. Turganbayev of the Financial Police confirmed as much during the October 2012 Hearing. He testified:

> Q. So I take it then that it was your own personal determination that the profits from operation of a main pipeline would include subsequent marketing or sales of oil. Is that correct?
>
> A. That's correct.[233]

166. Furthermore, Mr. Turganbayev confirmed that the Tax Committee, when making its calculation, was not concerned whether the pipeline in question was "main" or not, or whether any Kazakh agency had yet concluded whether the pipeline was "main." The Tax Committee simply calculated all of KPM's revenue as is was instructed to do by the Financial Police:

> Q. The point is the tax committee is calculating profits on this alleged operation of a main pipeline, but nobody has yet concluded that there is in fact such a main pipeline in operation, right?
>
> A. I believe the tax committee does not necessarily have to separate between main pipelines or in-field pipelines; this is not the area of their field of competence. They just calculated the income which was obtained through KPM pipeline. ...[234]

167. With the calculation in hand as of November 19, 2008, the Financial Police knew that, if only it could establish that KPM's field pipeline was a main pipeline, it could devastate the company with a serious criminal conviction and multi-million dollar fine. It was time to take the next step.

a. The Financial Police Rejected Multiple Confirmations From Kazakh Agencies and Industry Specialists That KPM's and TNG's Pipelines Were Not Main Pipelines

168. In the weeks following the Tax Department's November 19, 2008, conclusion that KPM earned allegedly "illegal" profits in excess of 41 billion Tenge for "operating" a main pipeline without a license, the investigation was handed over to the Chief Investigator of the Financial Police, Mr. Arman Rakhimov. Mr. Rakhimov initiated the formal criminal case against KPM on December 15, 2008.[235] During the October 2012 Hearing, Mr. Rakhimov confirmed that his decision to bring a criminal case against KPM for operating a main

[233] Turganbayev Testimony, Tr. October 2012 Hearing, Day 5, 97:22-98-1.

[234] Turganbayev Testimony, Tr. October 2012 Hearing, Day 5, 101:14-22.

[235] Order Initiating Criminal Proceedings, December 15, 2008, C-632.

pipeline without a license was made without any evidence that KPM actually operated a main pipeline. He testified:

> Q. [Regarding] C-632 … nowhere in that resolution on your decision to initiate and accept a criminal case is there any suggestion or statement that KPM operates a main pipeline; correct? ...
>
> A. You are right.[236]

169. In this arbitration, Kazakhstan claims that KPM's 17.9 kilometer pipeline that formed the subject of the criminal case "was always a trunk pipeline."[237] But none of the frequent inspections carried out at KPM and TNG in the decade prior to October 2008 ever suggested that KPM or TNG operated main pipelines or that they lacked a requisite license, and multiple agencies approved the construction and operation of the pipelines in question.[238] Thus, Kazakhstan would have the Tribunal believe that, for over six years, numerous competent Kazakh authorities conducting regular inspections of KPM and TNG failed to notice Claimants' alleged operation of a "main" pipeline without a license, a fact that "just happened" to be discovered once the Financial Police became involved on the heels of Nazarbayev's directive. That is fanciful. Indeed, as explained below, no Kazakh authority with any knowledge of KPM's and TNG's operations, nor any industry specialist, ever accepted it.

170. In any event, with no Kazakh authority having ever suggested (much less concluded) that KPM or TNG operated a "main" pipeline, the Financial Police began looking for an authority to give them the answer they needed. And in doing so, they ran into trouble, because the ministries they approached did not give them the answer they wanted. Initially, the Financial Police approached the MEMR and the ARNM, one of which should have been a "competent" authority to determine the issue. In December 2008, Senior Inspector Turganbayev reported to the Deputy Prime Minister of Kazakhstan that

> in the absence of a conclusion by a competent authority, it is impossible to make a lawful procedural decision in respect of this case.

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236 *See* Rahkimov Testimony, Tr. October 2012 Hearing, Day 5, 20:11-21:1.

237 Rejoinder on Jurisdiction and Liability ¶ 451.

238 *See* Reply on Jurisdiction and Liability ¶¶ 270-5; Claimants' Opening Presentation on Liability, slide 33. *See*, for instance, KPM's Subsoil Use License, May 23, 1997, C-45; Decision of the Working Group (including the Ministry of Emergency Situations) on the commissioning of KPM's pipeline, March 4, 2002, C-469; License issued by the MEMR to KPM for hazardous activity, September 26, 2002, C-81; Renewal of License by MEMR to KPM for hazardous activity, August 5, 2005, C-83; and Renewal of License by MEMR to KPM, May 29, 2008, C-472.

> In this respect, the [Financial Police] sent requests to the current and former licensors – Agency of RK on Regulation of Natural Monopolies and the Ministry of Energy and Mineral Resources asking to provide a conclusion on determination of a type of the pipelines operated by "Kazpolmunay" LLP and "Tolkynneftegas" LLP, taking into account the functions actually performed by the above mentioned pipelines.[239]

171. But neither of the two ministries that the Financial Police initially approached — the MEMR or the ARNM — supported the Financial Police's conclusion that KPM's and TNG's pipelines were "main" pipelines.[240] On January 5, 2009, Chief Investigator Rakhimov of the Financial Police asked the MEMR to ascertain whether KPM's 17.9 kilometer pipeline was a main pipeline.[241] On February 4, 2009, the MEMR provided the Financial Police with an answer that it did not like: the MEMR concluded that the KPM pipeline that was the subject of the criminal investigation "belong(s) to pipelines working as a gathering manifold" and "is not a main pipeline."[242] After receiving that answer, the Financial Police reversed its position on whether the MEMR was a "competent" authority to render an opinion on the matter.[243] The ARNM, for its part, did not opine on the matter aside from confirming that KPM and TNG did not hold main pipeline licenses.

172. The Financial Police also received statements that the pipelines in question were field pipelines from multiple sources at the Ministry for Emergency Situations ("MES"). That agency is charged with monitoring the safety of all pipeline operations, and it is the

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239 Letter from the Financial Police to the Deputy Prime Minister of Kazakhstan, December 10, 2008 (emphasis added), C-448.

240 It is clear in this arbitration that neither ministry wants to be held responsible for contradicting the Financial Police, as both ministries have claimed that the other was the "competent" authority to state the classification of a pipeline. Minister Mynbaev of the MEMR stated that, as of June 2007, the ARNM was the competent authority to determine whether TNG and KPM operated main pipelines. Tr. October 2012 Hearing, Day 3, 95:11-16; 108:11-16. However, Mr. Akhmetov, the Executive Secretary of the ARNM, denied this. He said "pipeline classification and the monitoring of pipelines are not under the jurisdiction of the [ARNM]." Witness Statement of Rustam Nurlanovich Akhmetov dated August 10, 2012 (hereinafter "Akhmetov Statement") ¶ 3.1; *see also* Tr. October 2012 Hearing, Day 6, 39:2-16. Minister Mynbaev claimed that that was "surprising." Tr. October 2012 Hearing, Day 3, 95:17-22. As Mr. Turganbayev's December 10, 2008, letter shows, however, at the time the Financial Police obviously considered that both agencies were competent. Letter from the Financial Police to the Deputy Prime Minister of Kazakhstan, December 10, 2008, C-448.

241 Request from the Financial Police to the MEMR, January 5, 2009, C-718; Third Witness Statement of Arman Tastemirovich Rakhimov dated September 30, 2012 (hereinafter "Third Rakhimov Statement") ¶ 3.1-3.2; A. Rakhimov, Tr. October 2012 Hearing, Day 5, 46:6-47:4.

242 Answer from the MEMR to the Financial Police, February 4, 2009, C-719; Third Rakhimov Statement ¶ 3.3; A. Rakhimov, Tr. October 2012 Hearing, Day 5, 47:12-49:2.

243 Tr. October 2012 Hearing, Day 5, 49:25-51:2.

agency that KMG, at least, considered "competent" to classify pipelines at the time.[244] On November 19, 2008, the Department of the MES for the Mangystau Oblast stated its conclusion that the pipelines were "not main pipelines."[245] On January 8, 2009, the National Scientific and Research Centre on Industrial Safety of the MES again confirmed that the relevant KPM and TNG pipelines were "field pipelines."[246] An inspector for the MES also testified during Mr. Cornegruta's criminal trial that the reclassified KPM pipeline was not a main pipeline.[247] The MES was, therefore, consistently adamant that KPM's reclassified pipeline was not a main pipeline. As it did with the MEMR's opinion, however, the Financial Police rejected the conclusions of the MES.[248] Unsurprisingly, in this arbitration Kazakhstan dismisses the MES's conclusions by claiming that the MES was "not the competent authority" to opine on the matter.[249]

173. In addition to those Kazakh agencies, industry specialists at the time concurred that KPM's and TNG's pipelines were not main pipelines. The research and design institute of KMG NC concluded, on January 5, 2009, that the KPM and TNG reclassified pipelines "do not belong to the category of main pipelines and are designated to ensure the process of hydrocarbons production."[250] Similarly, NIPI Neftegaz, an expert in the design of oil and gas pipelines, concluded that the reclassified KPM and TNG pipelines were field pipelines, and not main pipelines.[251] Those conclusions were provided to the Financial Police.[252] Yet, as it

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244 Letter from KazMunaiGas to the Vice Minister of Energy and Mineral Resources, December 25, 2008, C-604.

245 Letter from the Ministry of Emergency Situations to KPM, November 19, 2008, C-90.

246 Reports from the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations for KPM and TNG, January 8, 2009, C-103 and C-104.

247 Hearing Minutes from Mr. Cornegruta's trial, August 13, 2009, at 51-3, C-704.

248 Tr. October 2012 Hearing, Day 5, 45:20-24.

249 Statement of Defense ¶ 26.4. M. Akhmetov of the ARNM also argued that "classifying pipelines is outside [the Ministry of Emergency Situations'] area of competence. Tr. October 2012 Hearing, Day 6, 42:12-20. Chief Investigator Rakhimov attempted to justify that conclusion by claiming (without support) that KazMunaiGas was referring to the Ministry of Emergency Situations itself, not its Department for the Mangystau Region. Tr. October 2012 Hearing, Day 5, 39:17-41:19. Kazakhstan's position as to whether, or why, those two departments would not share competence over this issue is altogether unclear.

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

251 Letters from the Kazakh Scientific, Research, and Design Institute of Oil and Gas of NIPI Neftegaz to KPM and TNG, January 9, 2009, C-101 and C-102; A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 36:3-13. *See also* Expert report from the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities for KPM and TNG, April 13, 2009 (concluding that the reclassified pipelines are field pipelines), C-105 and C-106. Letter and Advice Note from the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations of Kazakhstan for KPM, August 25, 2009, C-107.

252 *See* Decision of the Aktau City Court, September 18, 2009 at 9, C-117.

had done with the conclusions of the Kazakh agencies, the Financial Police disregarded them.[253]

b. Kazakhstan Invented a "Legal" Definition of Main Pipeline to Justify Its Contention That No Kazakh Industry Authority Is Competent

174. In fact, months would pass before the Financial Police found someone to sign on to its contrived allegation that KPM's pipeline was a "main" pipeline. And in this arbitration, Kazakhstan has been forced to make the unbelievable claim that no industry authority in Kazakhstan is competent to classify main pipelines, because the question is a matter of law.[254]

175. At the October 2012 Hearing, Mr. Akhmetov of the ARNM tried to reinforce Kazakhstan's incredible position that no relevant industry authority in Kazakhstan is competent to opine on the matter, because it is a legal question. He testified that if an oil and gas operator has a question regarding the classification of a pipeline or whether it requires a license, it should direct that question to the General Prosecutor's Office![255] Thus, Kazakhstan's surreal position is that Claimants should have asked the Kazakh authority that was criminally prosecuting their general director whether the grounds for that prosecution were accurate. In the same vein, Kazakhstan has argued that "[u]ltimately, the decision on classification of pipelines is one for the Judge to take in her discretion."[256] Kazakhstan's position is thus reduced to this: a foreign investor can only learn whether it operates a pipeline that requires a main pipeline license once its general director shows up shackled in court.

176. Kazakhstan's contention that whether a pipeline is "main" is "purely a legal question" is fundamentally wrong. Kazakhstan's own Minister of Oil and Gas, Minister Mynbaev, does not even support that argument, because he testified at the October 2012 Hearing that the determination of whether a pipeline is "main" or not is a "question of purely technical definition."[257] Moreover, the Law on Oil specifically excludes pipelines involved in the "single technological process" of oil and gas production from classification as "main"

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253 Tr. October 2012 Hearing, Day 5, 44:17-50:10; *see* Decision of the Aktau City Court, September 18, 2009 at 9, C-117.

254 Rejoinder on Jurisdiction and Liability ¶¶ 513-26.

255 Tr. October 2012 Hearing, Day 6, 44:4-8 and 44:12-16.

256 Rejoinder on Jurisdiction and Liability ¶ 581.

257 Tr. October 2012 Hearing, Day 3, 89:12-22 (emphasis added).

pipelines,[258] and the MEMR confirmed that the pipelines in question were part of KPM's and TNG's "single technological process" of oil and gas production.[259]

177. Chief Investigator Rakhimov admitted that, when he claimed that KPM's pipeline was a "main" pipeline for purposes of criminally prosecuting Mr. Cornegruta, he relied on "normative [legislative] acts" and not "technical specifications and the like."[260] If he had considered the technical characteristics of field and main pipelines, there is no way that he (or any rational observer) could have concluded that KPM's pipeline was a main pipeline.

178. Because the matter is a determination that anyone knowledgeable of production operations could make, it is not surprising that Kazakhstan's legal argument on this issue is full of holes. Kazakhstan's own legal expert, Professor Didenko, does not concur with Kazakhstan's position that the matter is "purely a legal question." In his opinion, Professor Didenko could not (and did not) limit his analysis to Kazakh legal provisions. Instead, he explained that the "definition of trunk pipelines can be found in various judicial acts and technical documents."[261] He claimed that those

> definitions differ from each other, and therefore it is necessary to establish a single understanding, using the interpretations of the appropriate norms and regulations.[262]

That self-serving contention enabled Professor Didenko to create his own personal definition of "main" pipeline that is completely unsupported by the law or industry standards. In his report, he claimed that main pipelines have the following four characteristics:

- they are located outside contract (industrial) territory;
- they transport self-produced oil and oil belonging to another entity;
- they transport marketable oil (prepared in accordance with the requirements of technical regulations); and

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258 *See* First Expert Report of Professor Suleymenov dated May 6, 2012 (hereinafter "First Suleymenov Report") ¶¶ 42-44. *See* Romanosov Testimony, Tr. October 2012 Hearing, Day 2, 95:11-14. Kazakh Law on Oil No. 2350, art. 1(14), June 28, 1995 (in force in 2008), C-80.

259 *See, e.g.*, Report of the MEMR for KPM, February 5, 2010, C-385.

260 Tr. October 2012 Hearing, Day 5, 31:21-24.

261 Expert Report of Professor Didenko dated August 9, 2012 (hereinafter "Didenko Expert Report") at 7 (emphasis added). *See also* Letter from the MEMR to A. Rakhimov of the Financial Police, February 13, 2009, Exhibit 4 to Third Rakhimov Statement; A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 52:22-53:4.

262 Didenko Expert Report at 7.

- they transport oil to places of reloading to another mode of transport, consumption, and storage.[263]

179. As Professor Suleymenov explains in detail in his second expert report,[264] Professor Didenko's criteria are plucked from thin air:

> In short, the applicable laws do not support Mr. Didenko's conclusions; Mr. Didenko's conclusions rest only on flawed interpretation of the laws. Neither a pipeline's extension beyond the contract territory,[265] nor the transport of refined oil, nor transshipment into a different means of transportation, nor the transport of oil for third parties are conclusive criteria for classifying a pipeline as a trunk pipeline and may be characteristic of any other pipeline, including industrial pipelines used at facilities ancillary to production (for instance, the KPM Pipeline Segment transporting oil to the OSF).[266]

180. The reality is that what constitutes a "main" pipeline is fully understood in the industry and in Kazakhstan, and Professor Didenko's "made for arbitration" definition is unsupportable in law, fact, or logic. While all oil and gas operations must be conducted within the broad confines of the law, the technical parameters are important, can be outcome-determinative, and cannot be dismissed. All of the Kazakh authorities familiar with the industry standards and the technical parameters who considered this matter agreed that KPM's and TNG's pipelines were field pipelines. Only one person concluded otherwise at the time, and he had no expertise in the matter: Mr. Baymaganbetov, the Financial Police's hand-picked "expert."

c. The Financial Police Hand-Picked an "Expert" To Support Its Desired Conclusion

181. After the Financial Police eliminated all competent authorities from its list of potential experts, because each one had separately concluded that KPM and TNG did not operate main pipelines, on February 9, 2009, Chief Investigator Rakhimov ordered a forensic construction and technical expert review from Mr. Baymaganbetov of the Ministry of

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263 Didenko Expert Report at 20.

264 Second Suleymenov Report ¶¶ 6-51.

265 At the October 2012 Hearing, Mr. Cojin testified that it would, in fact, be dangerous for an oil and gas company to construct its gathering system on the Contract Area, essentially on top of its drilling operations and that Kazakhstan approved KPM's and TNG's use of land outside their respective contractual territories for the construction of their field pipelines. Cojin Testimony, Tr. October 2012 Hearing, Day 3, 11:25-12:14; 14:1-3. *See also* First Suleymenov Report ¶ 49.

266 Second Suleymenov Report ¶ 42.

Justice.[267] The Financial Police carefully controlled Mr. Baymaganbetov's review and analysis of the pipeline issue to ensure that his conclusion would accord with the Financial Police's intended result.

182. Most tellingly, the Financial Police decided upon the materials that Mr. Baymaganbetov would use for his review. Early in this proceeding, Kazakhstan attempted to hide the fact that Senior Inspector Turganbayev provided all the materials for Mr. Baymaganbetov to use in preparing his report. Mr. Turganbayev initially claimed that he did not participate in the criminal investigation after December 2008 when he handed over the pre-investigation file to Chief Investigator Rakhimov.[268] Moreover, Kazakhstan was initially adamant that there was a clear distinction between the "inspection" phase and the "investigation" phase of the Financial Police's pursuit of KPM and TNG.[269] However, Mr. Turganbayev admitted during the October 2012 Hearing that, in fact, he met with Mr. Baymaganbetov in February 2009, after his role in the case had supposedly ended, in order to provide him with the only materials he would use to prepare his "expert" opinion.[270]

183. Moreover, during the October 2012 Hearing, Chief Investigator Rakhimov confirmed that, under Kazakh law, a forensic expert can only rely on the documents the Financial Police provide for his review (except if the expert requests additional materials, which Mr. Baymaganbetov did not do).[271] The Financial Police provided only a very limited number of documents to Mr. Baymaganbetov, restricting his review to documents that would support a finding that KPM operated a "main" pipeline and purposefully omitting the materials that would indicate the opposite conclusion. The documents on which Mr. Baymaganbetov's "expert" report was based were:

- the Financial Police's 2-page order for an expert evaluation;
- a working project for construction of the Borankol Raw Materials Base;

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267 Order from the Financial Police to the Ministry of Justice, February 9, 2009, C-109.

268 Second Witness Statement of Daniyar Mukhanovich Turganbayev dated August 12, 2012 (hereinafter "Second Turganbayev Statement") ¶ 6.3; Tr. October 2012 Hearing, Day 5, 104:25-105:19.

269 Opening Statement of Dr. Nacimiento, Tr. October 2012 Hearing, Day 1, 156:6-10.

270 Tr. October 2012 Hearing, Day 5, 106:17-23. *See also* Report on Inspection of the Material Evidence, February 10, 2009, R-246; Witness Statement of Salamat Sartevich Baymaganbetov dated August 10, 2012 (hereinafter "Baymaganbetov Statement") ¶¶ 3.3, 3.5.

271 A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 57:25-59:24.

- a copy of the 2002 commissioning Act on KPM's "Oil pipeline of Borankol Field to Commodities and Raw Material Base of Opornaya Station;" and

- two technical specifications: SNiP 2.05.06-85* and SNiP III-42-80*.[272]

184. The first document was in fact the Financial Police's order to perform the expert review. That document contained no information about what constitutes a main pipeline.[273] The second document was the Borankol Raw Materials Base Project prepared by NIPI Neftegaz, an industry expert that had concluded in a separate report that the KPM pipeline at issue was not a main pipeline.[274] Notably, the Financial Police did not disclose NIPI Neftegaz's separate report to Mr. Baymaganbetov. The third document was the Decision of the Working Group on the commissioning of KPM's pipeline, in which the MES participated.[275] As previously noted, the MES had repeatedly concluded that the reclassified KPM pipeline was a gathering pipeline, not a main pipeline.[276] The Financial Police also withheld that information from Mr. Baymaganbetov.[277]

185. Finally, the Financial Police only provided two SNiPs (technical specifications) to Mr. Baymaganbetov. Both SNiPs were the technical specifications for main pipelines, not field pipelines.[278] Neither the Borankol Raw Materials Base Project nor the Decision of the Working Group on the commissioning of KPM's pipeline refer to those SNiPs,[279] but they do refer to the technical specifications for field pipelines. The Financial Police did not provide those technical specifications governing field pipelines to Mr. Baymaganbetov either, and despite the fact that both the Base Project and the commissioning

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272 Expert Opinion of the Ministry of Justice, February 13, 2009, C-110; A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 60:10-64:2. *See also*, Report on Inspection of the Material Evidence, February 10, 2009, R-246.

273 A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 60:10-64:2.

274 Borankol Raw Materials Base Project prepared by NIPI Neftegaz, 2001, C-465. Letters from the Kazakh Scientific, Research, and Design Institute of Oil and Gas of NIPI Neftegaz to KPM and TNG, January 9, 2009, C-101 and C-102; A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 36:3-13 and 64:15-25.

275 Decision of the Working Group on the commissioning of KPM's pipeline, March 4, 2002, C-469. A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 64:15-25.

276 Letter from the Ministry of Emergency Situations to KPM, November 19, 2008, C-90; Reports from the National Scientific and Research Center on Industrial Safety Issues of the Ministry of Emergency Situations for KPM and TNG, January 8, 2009, C-103 and C-104. Testimony of an inspector for the Ministry of Emergency Situations, Hearing Minutes from Mr. Cornegruta's trial, August 13, 2009, at 50-3, C-704.

277 A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 71:4-71:18; S. Baymaganbetov Testimony, Tr. October 2012 Hearing, Day 6, 103:16-18.

278 A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 73:18-25.

279 S. Baymaganbetov Testimony, Tr. October 2012 Hearing, Day 6, 88:11-17, 89:8-11, and 14-17.

report mention them, Mr. Baymaganbetov did not consider it necessary or material to request them for consideration in preparing his "expert" report.

186. In addition to the confirmations from the MES and NIPI Neftegaz discussed earlier, two additional industry authorities issued reports confirming that KPM's pipeline was not a main pipeline in April 2009. They were the Russian Science & Research Institute for the Construction and Operation of Pipelines and Professor Suleymenov, who drafted Kazakhstan's Law on Oil and serves as Claimants' expert in this case.[280] At the October 2012 Hearing, Chief Investigator Rakhimov confirmed that the Financial Police did not give any of those four expert reports — all of which concluded that KPM's pipeline was a field pipeline — to Mr. Baymaganbetov. Rakhimov testified as follows:

> ... [A]ll the four letters, all the four opinions that were produced by Mr Cornegruta in the criminal case, or the opinions which stated [that] this pipeline was not trunk pipeline, were not given to the expert.[281]

187. In addition to limiting his review to the materials provided by the Financial Police, Mr. Baymaganbetov did not judge it necessary to visit KPM's facilities and inspect KPM's pipeline in order to determine whether it was a "main" pipeline.[282] Mr. Baymaganbetov claims that within two days, having reviewed only the documents described above and without the benefit of a site visit, he was in a position to conclude that KPM operated a main pipeline. The Financial Police and the judge at Mr. Cornegruta's trial relied solely on Mr. Baymaganbetov's "expert" opinion to find that Mr. Cornegruta had committed a crime by operating a "main" pipeline without a license, to sentence him to four years in Kazakh jail, and to assess a devastating US $145 million fine against non-party KPM.

d. The Prosecution and Trial of Mr. Cornegruta, Which Resulted In A Devastating Penalty Against KPM, Was an Egregious Denial of Justice

188. The Financial Police's concocted "main" pipeline allegation against Mr. Cornegruta and KPM amounted to a denial of justice and clearly violated the ECT's fair and

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[280] Expert Report from the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities for KPM, April 13, 2009, C-105; Expert report from the Russian Science and Research Institute for the Construction and Operation of Pipelines and Energy Facilities for TNG, April 13, 2009, C-106; Legal Opinion of Mr. Suleymenov, July 2, 2009, C-108.

[281] A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 71:4-71:18; S. Baymaganbetov Testimony, Tr. October 2012 Hearing, Day 6, 103:16-18.

[282] As explained by Mr. Romanosov, one can conclude that the pipeline is not a main pipeline after "only having looked at the facility itself." Tr. October 2012 Hearing, Day 2, 102:18-25.

equitable treatment and "most constant protection and security" standards. So, too, were the next steps in the process, namely, the criminal prosecution and trial of Mr. Cornegruta, which resulted in a US $145 million penalty against KPM. The prosecution, trial, and verdict were so riddled with due process violations that no independent or impartial tribunal could reasonably conclude that Kazakhstan afforded justice to Mr. Cornegruta or KPM.

189. Notably, Kazakhstan's breaches of Mr. Cornegruta's rights directly affected KPM, because Mr. Cornegruta's conviction served as the basis for the devastating penalty imposed on KPM. Kazakhstan also denied justice to KPM by bungling the process from the beginning in relation to KPM itself — in particular, by failing to include KPM in the proceeding or otherwise permitting KPM an opportunity to be heard and defend its position.

190. At the October 2012 Hearing, Kazakhstan's Deputy General Prosecutor, Mr. Kravchenko, admitted that, as a matter of Kazakh law, KPM could not be subject to criminal liability. He testified as follows:

> Q. Now, it's correct, is it not, that under Kazakhstan's criminal law, only a sane natural person who has reached the age of maturity is subject to criminal liability; correct?
>
> A. Yes, it is so. ...
>
> Q. So it was actually not possible for KPM to be charged with the crime that Mr. Cornegruta was charged with, right?
>
> A. Not in the criminal process; that's correct.[283]

191. That correct statement of the law is far removed from Kazakhstan's original claim in this proceeding regarding "quasi-criminal responsibility for corporate entities," which Kazakhstan has now (understandably) abandoned.[284] Mr. Kravchenko's concession is consistent with the 2004 Regulatory Resolution from the Supreme Court of Kazakhstan, which states that "profits from the commission of a crime in the sphere of economic activities ... are subject to recovery from the guilty person."[285] Thus, according to Kazakh law, Kazakhstan could not find KPM guilty of the crime of illegal entrepreneurial activity and it could not lawfully recover illegal profits from KPM.

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283 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 66:9-23.

284 Statement of Defense ¶¶ 27.11 *et seq.*; *see also* Maulenov opinion (R-140).

285 Regulatory Resolution of Supreme Court of Kazakhstan, June 18, 2004 ¶ 19 (emphasis added), Exhibit 2 to First Malinovsky Report; Normative Resolution of the Supreme Court of Kazakhstan, June 18, 2004, R-144. The Supreme Court's 2004 Regulatory Resolution is also instructive when assessing Kazakhstan's argument that any funds resulting in criminal unjust enrichment (regardless of how they were acquired or by whom) should be returned to the State. The nature of unjust enrichment requires that a party has benefited (*i.e.*, has been enriched). Thus, even if Kazakhstan could recover funds from KPM, it would be limited to only that which benefited KPM, which could only constitute KPM's profits, and not its revenues.

192. At the October 2012 Hearing, Mr. Kravchenko attempted to retroactively justify Kazakhstan's obvious violation of its own law by claiming that there were "other routes" to make KPM a party to a legal action and enforce a criminal conviction against it, such as "civil law responsibility," which he testified, "should be taken up and reviewed by a court."[286] Irrespective of whether Mr. Kravchenko is correct, there is no question that Kazakhstan did not take such a "route" with respect to KPM in the present case. KPM was not included in Mr. Cornegruta's criminal case in any capacity; it was not named as either a criminal or a civil party; it did not participate in the proceeding; and no civil claim was ever brought against KPM.

193. Furthermore, Kazakhstan has not demonstrated that some "other" lawful route for enforcing a criminal judgment against non-party KPM even exists under Kazakh law. When asked whether there was any provision of Kazakhstan's civil law, Criminal Code, or Code of Criminal Procedure that enabled a judgment stemming from the conviction of Mr. Cornegruta to be imposed and enforced against KPM, Mr. Kravchenko could only reference a vague recollection of "certain court rulings" that he claimed supported that practice.[287] He could not name those court rulings, he admitted that he could not "give an exact reference," and indeed, he did not mention any such decisions in his witness statement.[288]

194. Aside from Mr. Kravchenko's on-the-spot speculation, Kazakhstan relies solely on self-selected portions of four domestic cases for its supposition that a criminal judgment can be lawfully enforced against a non-party that admittedly was not (and could not be) responsible for the crime.[289] When read in their entirety, however, those cases do not support Kazakhstan's position. In brief, only one of the four cases Kazakhstan relies upon is relevant to the present dispute, because only one case, from the Taraza City Court, has anything at all to do with an allegation of "illegal entrepreneurial activity" under Article 190 of the Kazakh Criminal Code. That case actually contradicts Kazakhstan's position, because

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[286] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 69:25-70:4.

[287] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 69:16-72:15.

[288] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 69:16-72:15; *see also* Second Kravchenko Witness Statement.

[289] Incredibly, Kazakhstan only produced 1 page excerpts from each of the original, Russian versions of those cases, which collectively comprise hundreds of pages. *See* R-248; R-249; R-250; and R-251. Because that partial production greatly misconstrues the substance of those cases, Claimants submit them in full, with partial translations of the relevant portions, as Exhibits with this submission. *See* Judgment #1-122-2010 and Case Minutes of Taraza City Court #2, September 22, 2010 (full version of case submitted as R-248), C-727; Judgment # 1-829-2010 and Case Minutes of Aktobe City Court #2, June 25, 2010 (full version of case submitted as R-249), C-728; Judgment # 1-771-2010 and Case Minutes of Aktobe City Court #2, July 9, 2010 (full version of case submitted as R-250), C-729; Judgment # 1-947-2010 and Case Minutes of Aktobe City Court #2, August 25, 2010 (full version of case submitted as R-251), C-730.

the Taraza court expressly stated that it could not determine "the issue of collection of damages" "due to absence of a civil claim" before it.[290] Therefore, the only relevant court decision Kazakhstan can point to confirms that — contrary to Kazakhstan's position in this arbitration — a civil claim ancillary to a criminal proceeding is required in order to recover money from a corporate entity in relation to a crime. Again, no civil claim was brought against KPM.

195. The other three cases cited by Kazakhstan are irrelevant, because they concern only allegations of tax evasion under Article 222 of the Kazakh Criminal Code.[291] The funds ordered recovered from the respective corporate entities in those cases were the taxes lawfully owed by the companies themselves in any event.[292] No analogy can be drawn from that situation to the present one, where Kazakhstan ordered the recovery of funds from KPM that KPM did not otherwise lawfully owe. Additionally, and unlike the case of KPM, civil claims were brought in connection with at least two of those other criminal cases.[293]

196. In short, Kazakhstan violated KPM's rights when it attributed Mr. Cornegruta's alleged crime to KPM, because there was no legal basis to do so. Kazakhstan also violated KPM's due process rights by refusing to permit KPM an opportunity to participate in the trial process and be heard. As justification for that undisputed fact, Kazakhstan has tried to impute Mr. Cornegruta's involvement and representation in the trial

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[290] Incidentally, that damage was for crimes other than for illegal entrepreneurial activity that were also at issue in that case. Judgment #1-122-2010 and Case Minutes of Taraza City Court #2, September 22, 2010 (full version of case submitted as R-248) at 189, C-727. Moreover, the Taraza court expressly stated that the property and money that was ordered recovered from the corporate entities for the State budget comprised "the property used to carry out illegal entrepreneurial activity." *Id*. at 196, C-727. Under Kazakh law, the property used to carry out a crime may be confiscated, but importantly, in Mr. Cornegruta's case, the court found that the property used to carry out illegal entrepreneurial activity was KPM's pipeline (not any funds) and that it was not subject to collection. *See* Judgment of Aktau City Court, September 18, 2009, at 11-12, C-117. It is also worth noting that in the Taraza case, the court decided that other corporate property and funds were subject to collection after "hearing a case on economic dispute under the civil claim in the interdistrict economic court." Judgment #1-122-2010 and Case Minutes of Taraza City Court #2, September 22, 2010 (full version of case submitted as R-248) at 196, C-727.

[291] Judgment # 1-829-2010 and Case Minutes of Aktobe City Court #2, June 25, 2010 (full version of case submitted as R-249), C-728; Judgment # 1-771-2010 and Case Minutes of Aktobe City Court #2, July 9, 2010 (full version of case submitted as R-250), C-729; Judgment # 1-947-2010 and Case Minutes of Aktobe City Court #2, August 25, 2010 (full version of case submitted as R-251), C-730.

[292] *See, e.g.*, Judgment # 1-829-2010 and Case Minutes of Aktobe City Court #2, June 25, 2010 (full version of case submitted as R-249), C-728 (the amount of taxes found to be owed by the company was the same amount of funds ordered recovered from the company).

[293] Judgment # 1-829-2010 and Case Minutes of Aktobe City Court #2, June 25, 2010 (full version of case submitted as R-249) at PDF p. 2 of English version, C-728; Judgment # 1-771-2010 and Case Minutes of Aktobe City Court #2, July 9, 2010 (full version of case submitted as R-250) at PDF p. 3 of English version, C-729. It can be seen that a civil claim was brought in connection with those criminal cases because, in the respective hearing minutes, the chairman advises each civil defendant of his rights under Article 78 of the Criminal Procedure Code.

to KPM. Kazakhstan has claimed that since Mr. Cornegruta worked for KPM, KPM had full information about what transpired during the trial and could participate in the case through Mr. Cornegruta.

197. But that is no substitute for actual participation or legal representation. At the October 2012 Hearing, Mr. Condorachi explained why:

> The problem is that they [KPM's representatives] only had the opportunity to read the materials which were gathered, but they had no possibility to participate in the investigation or demand additional expertise.… Cornegruta's lawyers who participated in the process were his defense lawyers. They were not retained by the company, they were not the lawyers of the company, and they were not strictly speaking obliged to report to me.[294]

198. It should be elementary that KPM could not adequately defend itself at Mr. Cornegruta's trial. KPM had no reason to believe that any "defense" was necessary, because it could not have guessed that any judgment resulting from Mr. Cornegruta's conviction would be rendered and enforced against it. Due process requires a party to be made aware of the claims against it and provided an opportunity to defend itself. Kazakhstan afforded neither of those fundamental rights to KPM.

199. In addition to holding KPM responsible for a crime it did not commit without affording KPM any ability to challenge that process, Kazakhstan committed a number of other breaches of due process in its trial of Mr. Cornegruta. The judgment explicitly confirms that the judge excluded four expert reports submitted by Mr. Cornegruta's defense that established his innocence.[295] Those reports all confirm that the pipeline at issue was not a main pipeline. Those were the same expert reports that, as mentioned above, Mr. Rakhimov deliberately kept away from Kazakhstan's judicial "expert," Mr. Baymaganbetov.[296] The exclusion of those reports was not a matter of the judge considering the evidence and concluding that they were not compelling; rather, she simply excluded the reports from the case altogether. Her summary exclusion of exculpatory evidence underscores the biased nature of the trial.

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[294] Condorachi Testimony, Tr. October 2012 Hearing, Day 2, 137:7-11 and 138:5-11 (emphasis added).

[295] Decision of the Aktau City Court, September 18, 2009, at 9-10, C-117.

[296] A. Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 71:14-20 ("all the four opinions that were produced by Mr. Cornegruta in the criminal case, or the opinions which stated [that] this pipeline was not trunk pipeline, were not given to the expert").

200. The only explanation that the judge gave for excluding those reports was the fact that the authors of the reports did not appear in court to testify about them.[297] However, as Professor Malinovsky explained, there is no requirement under Kazakh law that the authors of those expert reports appear in order for the reports to be considered.[298] And even if there were, the judge rejected Mr. Cornegruta's specific request that the trial schedule be postponed to permit the authors of three of the reports the opportunity to appear.

201. On August 26, 2009, day seven of the trial, Mr. Cornegruta's defense counsel motioned for a postponement of less than one week so that the judge and counsel could question the authors of the expert reports that contradicted the conclusions of Mr. Baymaganbetov.[299] The defense team argued that the appearance of its experts was necessary because of "the dramatic difference between the conclusions" of its experts and Mr. Baymaganbetov.[300] The judge denied that motion "on the spot" and gave no explanation for her ruling.[301] Because the findings of Mr. Cornegruta's experts were significantly more considered and compelling that Mr. Baymaganbetov's cursory analysis, an impartial court could not have reasonably reached a guilty verdict if the reports had been admitted and considered or if their authors had been permitted to testify.

202. The fact that neither Mr. Cornegruta nor KPM could have expected fair treatment during the criminal investigation, prosecution, and conviction is confirmed by Kazakhstan's own expert, Martha Brill Olcott. She explains the rule of law in Kazakhstan as follows:

> Kazakhstan has many good laws, but no one in authority is particularly interested in enforcing them. It also lacks an independent parliament, an independent judiciary, and popularly accountable local governments.[302]

203. If any doubt remains as to the biased nature of the criminal case, the Hearing Minutes (trial transcripts) put those doubts to rest. The Minutes conclusively establish the Financial Police's involvement in the prosecution and influence over the trial process. On the second day of the trial, August 6, 2009, Mr. Cornegruta's defense counsel requested that the judge order Financial Police officer Zlupacarov, who was physically present, dismissed from

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297 Decision of the Aktau City Court, September 18, 2009, at 10, C-117.

298 First Malinovsky Opinion at 24-26.

299 Hearing Minutes at 65, C-704.

300 Hearing Minutes at 65, C-704.

301 Hearing Minutes at 66, C-704.

302 M. Olcott, *Kazakhstan: Unfulfilled Promise?* at 243, Exhibit 1 to First Olcott Report.

the courtroom and the proceeding.[303] Mr. Cornegruta's counsel explained that, from the beginning of the trial, a group from the Financial Police had remained gathered in the court hall and that the captain, Mr. Zlupacarov, had informed them that he was part of the "escort group for this lawsuit" and that the case was under "their control."[304] Counsel also complained that, on July 30 and 31, 2009, Mr. Zlupacarov had chased after Mr. Cornegruta's attorneys and his wife, while driving after and filming them from his car.[305]

204. There can be no serious argument as to whether Kazakhstan's "control" of the criminal case amounts to a denial of justice, because it constitutes State interference and influence over the outcome of the trial.[306] Kazakhstan's denial of justice against KPM and its general manager is a clear breach of its duty under the ECT to accord fair and equitable treatment to Claimants' investments.[307]

e. Kazakhstan Ignored Claimants' Complaints and Prevented KPM From Appealing the Judgment Against It

205. Claimants have submitted voluminous evidence demonstrating that they complained repeatedly to Kazakh officials about the handling of the investigation, prosecution, and conviction of Mr. Cornegruta and KPM.[308] However, those complaints fell

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303 Hearing Minutes at 24-27, C-704.

304 Hearing Minutes at 24, C-704.

305 Hearing Minutes at 24, C-704.

306 Even under Kazakh law, the act of state authorities like the Financial Police taking a case that is being considered by a court under their control is a violation of Kazakh law and "shall be regarded as interference into the judicial process with the aim to prevent justice." *See* Hearing Minutes at 26, C-704 (*citing* Resolution of the Plenum of the Supreme Court of Kazakhstan No. 1 of May 14, 1998, cl. 4). Further proof that the criminal case was under the "control" of President Nazarbayev is a telephone message from the Head of the Financial Police. Telephone Message from V.I. Andreev to B.Z. Paritov, C-731.

307 *See*, *e.g.*, Reply on Jurisdiction and Liability ¶¶ 501-515 (regarding the criminal investigations and trial as a breach of the fair and equitable treatment standard). Kazakhstan's misconduct regarding the criminal prosecution and trial also constitute breaches of other ECT standards. *See*, *e.g.*, *id*. ¶¶ 475-480 (regarding the criminal investigations and trial as an unlawful, indirect expropriation), ¶¶ 485-496 (regarding Kazakhstan' breach of the most constant protection and security standard), and ¶¶ 517, 524, 528, 530-535 (regarding Kazakhstan's breach of the impairment clause).

308 *See, e.g.*, Letter from Claimants to the President of Kazakhstan, May 7, 2009, C-43; Complaint from TNG to the MEMR, January 19, 2009, C-46; Complaints from KPM against the Financial Police to the Ministry of Justice, the Financial Police, the MEMR, the Regional Transport Prosecutor, January 19, 2009, and Complaint from KPM and TNG to the General Prosecutor's Office, March 18, 2009, C-96; Letter to the General Prosecutor's Office, March 18, 2009, C-154; Complaint from TNG to Ministry of Justice regarding acts of the Financial Police, January 19, 2009, C-620; Complaint from TNG to MEMR, January 19, 2009, C-621; Complaint from TNG to Financial Police, January 19, 2009, C-622; Complaint from TNG to General Prosecutor, January 19, 2009, C-623; Complaint of KPM to General Prosecutor, January 19, 2009, C-624; Complaint from KPM to General Prosecutor, January 20, 2009, C-626; Complaint from KPM to Regional Transport Prosecutor, January 20, 2009, C-627; Letter from Transport Prosecutor forwarding KPM's and TNG's Complaints, January 21, 2009, C-628; Correspondence between KPM and Kazakh authorities regarding illegality of inspections and seizures, January-February 2009, C-629; Correspondence between TNG and Kazakh authorities regarding illegality of inspections and seizures, January-February 2009, C-630;

upon deaf ears and did nothing to stop (or even slow) the process. As Mr. Condorachi cogently explained during the October 2012 Hearing:

> Every time we had an opportunity and every time we had a reason, we would send a complaint to the General Prosecutor's Office. ... Only at a later stage we learnt that the General Prosecutor and the transport prosecutor and even the regional prosecutor never saw these materials; they only made enquiries. But the financial police, using the excuse that this is a case under investigation or there is an expertise ongoing, would give them this excuse and not provide the materials...
>
> Although the ... financial police had a duty to provide the materials to either Mangystau local prosecutor's office, or transport prosecutor's office, or regional prosecutor's office, or General Prosecutor's Office, this [has] never been done. I don't think we can speak about protection or freedoms and rights which were duly protected through these authorities.[309]

206. Kazakhstan's own witnesses confirm that Claimants complained to multiple Kazakh officials. Mr. Kravchenko testified that the Prosecutor's Office received "eight such complaints" during the course of the criminal investigation from KPM and TNG and "one more complaint from Terra Raf and Ascom" directly.[310] Mr. Rakhimov similarly testified that "there were plenty of complaints regarding [the Financial Police's] investigative activities," so much so that he found it "strange" that there was no complaint regarding the May 2009 raid on KPM's and TNG's office.[311] Regarding the conduct of the criminal case, Mr. Rakhimov admitted:

> Q. ... [D]o you recall that a number of written complaints were filed on behalf of KPM and TNG with the Ministry of Justice regarding the conduct of the criminal case?
>
> A. Well, you know, my answer is that there were many complaints… There were complaints to the Prosecutor's Office. There were complaints possibly to the agency.[312]

207. Kazakhstan contends that KPM could have contested the judgment and the enforcement procedure against it by appealing the verdict within the time permitted under the

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Letter from KPM and TNG to President Nazarbayev, March 24, 2009, C-631; Letter from Terra Raf to the Akim of Mangystau Region, February 23, 2009, C-664; Letter from Ascom to the Akim of Mangystau Region, February 25, 2009, C-666; and Letter from A. Stati to President Nazarbayev, November 7, 2008, C-700. Kazakhstan's claim that Claimants failed to exhaust legal remedies is highly misleading because it ignores the multitude of complaints that KPM and TNG made throughout the entire process, as listed above.

309 Condorachi Testimony, Tr. October 2012 Hearing, Day 2, 132:1-133:4.

310 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 44:3-13.

311 Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 84:11-14.

312 Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 85:19-86:12.

law, but that KPM failed to do so. That argument is disingenuous for at least two reasons. First, since KPM was not a party to the criminal case, it was not permitted under Kazakh law to appeal the decision. Mr. Kravchenko confirmed that point at the October 2012 Hearing:

> Q. Kazakhstan law does not provide the ability for a non-party to a case to file an appeal, does it?
>
> A. That's right. That's exactly what it is.[313]

208. Second, KPM nevertheless requested a certified copy of the judgment precisely so that it could file an appeal in timely fashion. However, the Aktau City Court refused to provide KPM a certified copy of the judgment, presumably because KPM was not a party to the case.[314] Mr. Kravchenko testified:

> Q. Are you aware that on September 22nd 2009, four days into [the 15 day appeal] window, the non-party KPM requested a certified copy of the court judgment?
>
> A. I believe so, yes. I can agree, yes. ...
>
> Q. You are not aware of any evidence to suggest that the copy of the judgment was sent to KPM in either October or November 2009, are you?
>
> A. That's correct.[315]

209. Mr. Kravchenko later conceded that if "KPM requested a certified copy of the judgment within the appeal deadline and that request was refused, it was unfair for the appeal to later be rejected on the basis that it was not timely filed."[316] But Mr. Kravchenko added a caveat that that result would be unfair "only if the decision to refuse to provide the copy ... had been challenged or appealed."[317]

210. The evidence shows, however, that KPM did challenge the court's refusal to send KPM a copy of the court judgment. KPM sent a "separate complaint" to the Chamber of Appeal of the Mangystau Oblast Court, complaining that, among other defects, "[t]he court sentence was not sent to 'Kazpolmunay' LLP, the right of 'Kazpolmunay' LLP for the sentence contestation, [and] the order and period for the sentence contestation were not

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313 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 104:15-17.

314 *See* KPM's request for the court judgment, September 22, 2009, C-705.

315 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 105:2-21; KPM's request for the court judgment, September 22, 2009, C-705.

316 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 107:24-108:7.

317 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 107:24-108:7.

explained."[318] KPM further complained that "the court refused to provide 'Kazpolmunay' LLP with the copy of the contested sentence," and thus, "'Kazpolmunay' LLP had no opportunity to appeal against the sentence within the period established by the law."[319] As with KPM's (and TNG's) other complaints, however, that appeal to the Mangystau court was futile.

* * *

211. The evidence conclusively establishes that the entire criminal process resulting in the judgment against Mr. Cornegruta and KPM was a sham from beginning to end. The criminal allegation of operating a "main" pipeline without a license was contrived; the amount of "illegal" profit KPM allegedly made from "operating" a "main" pipeline was deliberately engineered to include onward sales of oil, which permitted a more serious criminal charge and a devastating penalty; the evidence that KPM in fact operated a "main" pipeline was manufactured by the state's hand-picked expert, and mountains of contrary evidence from competent authorities and experts was ignored; the most basic notions of due process were violated in the conduct of the trial and the appeal process; and throughout, Claimants' and KPM's complaints about the abusive process were ignored.

212. After the criminal judgment was issued in late 2009, Kazakhstan pursued damaging enforcement measures against KPM to recover the US $145 million in alleged "illegal" profits. Kazakhstan issued a writ of execution against KPM on December 29, 2009,[320] and it seized KPM's bank accounts on January 10, 2010.[321] Kazakhstan continued its enforcement measures over the next several months, attaching KPM's motor vehicles and ordering their impoundment, and attaching KPM's land, buildings, and other property.[322]

213. Kazakhstan directly interfered with KPM's ability to carry out the sale of hydrocarbons by prohibiting KPM from importing or exporting any goods;[323] it interfered with KPM's ability to operate normally by freezing its bank accounts and transferring KPM's funds to the State;[324] and, once it determined that selling KPM's entire property would not

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318 Challenge of court's refusal to reinstate term for a claim of appeal, February 8, 2010, at 2, C-637.

319 *Id*.

320 Writ of Execution, December 29, 2009, C-119.

321 Order from Aktau Enforcement Officers to KPM, January 10, 2010, C-121.

322 Order from Aktau Enforcement Officers to KPM, January 22, 2010, C-122; Order from Aktau Enforcement Officers to KPM, February 26, 2010, C-79; and Order from Aktau Enforcement Officers to KPM, March 15, 2010, C-126.

323 Order from Chief of Aktau Enforcement Department to KPM, February 23, 2010, C-298.

324 Orders on Transfer of Funds, March 2010, C-503, C-504, C-505, and C-506.

recover the full value of the US $145 million fine, Kazakhstan resolved to seize KPM's produced hydrocarbons directly.[325] Those direct interferences with KPM's ability to operate also impacted TNG. As Mr. Calancea testified:

> Kazakhstan's acts of enforcement against KPM, which commenced in January 2010, had a direct impact on TNG, because TNG and KPM used much of the same infrastructure to operate. TNG had also been struggling to operate normally since Kazakhstan began harassing the companies and interfering in their operations in October 2008. Thus, in order to avoid devastating social, economic, and environmental consequences to the region, and as TNG was a major producer of gas in the region, TNG used any funds that it could spare from its own operations to cover KPM's expenses. We provided funds to ensure the payment of salaries to KPM's employees and for operating expenses so that oil production could be performed in accordance with the approved development programs for the Borankol field.[326]

2. Kazakhstan Publicly Defamed Claimants And Manufactured a "Preemptive Right" Claim To Cloud Title To TNG

214. In late 2008, Kazakhstan fabricated grounds to cast doubt over Claimants' title to TNG. It did so by manufacturing a claim that Gheso had transferred its shares in TNG to Terra Raf on May 16, 2005, and not on May 12, 2003, the date the transaction was validly registered in accordance with Kazakh law.[327] On December 18, 2008, Kazakhstan revoked its February 20, 2007, *post hoc* consent to the transfer and spuriously asserted a "preemptive right" over TNG's shares.[328] Claimants have conclusively demonstrated in Section II.B.4.c that Kazakhstan's assertion of a preemptive right over TNG in December 2008 was unfounded in fact and in law.

215. On December 18, 2008, the very same day Kazakhstan notified Claimants of its alleged "preemptive right," Kazakhstan intentionally leaked its claim to the financial press.

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325 Order on arrest of KPM's extracted hydrocarbons, May 11, 2010, C-507; Repeated Warning to KPM, June 15, 2010, C-201.

326 Calancea Statement ¶ 2; *see also* Calancea Testimony, Tr. October 2012 Hearing, Day 3, 67:20-68:10.

327 Notice letter from the MEMR to TNG, December 18, 2008, C-140.

328 Notice letter from the MEMR to TNG, December 18, 2008, C-140. Kazakhstan also contends that Claimants have produced a document which expressly refers to Ascom as being the shareholder of TNG (Rejoinder on Jurisdiction and Liability ¶ 173). This allegation is entirely misleading since the document referred to is a letter from GazImpex to Mr. Kulibayev dated September 15, 2004 (Exhibit C-514). Claimants cannot be held responsible for the errors of third parties regarding the ownership of TNG.

Its leak also included scurrilous accusations of fraud and forgery that were totally unfounded and never pursued or mentioned again, much less proven.[329]

216. Far from denying that it maliciously defamed Claimants, in this arbitration Kazakhstan simply asserts that it does "not know whether anyone from the Ministry disclosed information to INTERFAX," but that such a leak would constitute a violation of the Code of Honor of Government Employees.[330] Thus, it is not apparent that Kazakhstan has concerned itself at all regarding the libel committed at the hands of its officials. Even if Kazakhstan could establish that it did not publish the false statements — which it has not done and cannot do, because the leak indisputably came from the MEMR — Kazakhstan never attempted to remedy the harm done by its libelous publication, which it concedes is a violation of Kazakh law. Kazakhstan's December 18, 2008, letter, its public defamation of Claimants, and its failure to set the public record straight are clear breaches of the ECT and international law,[331] and they resulted in significant, financial harm to Claimants.

217. As further explained in Section IV.A.1, one immediate effect of the defamatory leak was that Credit Suisse decided not to execute the term sheet for a US $150-175 million credit facility it was on the verge of concluding with Claimants.[332] The loss of the Credit Suisse facility ultimately forced Claimants, in June 2009, to resort to the Laren loan sharks for US $60 million in emergency bridge financing.[333] The "horrendous" conditions of the Laren loan (as Kazakhstan accurately puts it) caused further financial duress. As Mr. Lungu testified, Claimants would not have needed to enter into the Laren loan if they had

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329 Press release circulated on INTERFAX from the MEMR attached to email from Credit Suisse to A. Lungu, December 18, 2008, C-625; Notice letter from the MEMR to TNG, December 18, 2008, C-140.

330 *See* Rejoinder on Jurisdiction and Liability ¶¶ 171-2; *cf.* Witness Statement of Mirbulat Zarifovich Ongarbaev dated August 2, 2012, Amended translation, ¶ 5.10, C-720.

331 As Claimants already demonstrated, Kazakhstan's arbitrary claim of an alleged pre-emptive right over TNG and its false announcement of "irregularities" at TNG constitute indirect expropriation, failure to provide the most constant protection and security, unfair and inequitable treatment, unreasonable and discriminatory measures, and failure to observe the obligations Kazakhstan entered into with respect to Claimants' investment. *See*, *e.g.*, Statement of Claim ¶¶ 272, 276, 334, 351, 362, and 371-72; Reply on Jurisdiction and Liability ¶¶ 478-9, 501, 514, 531, and 546.

332 A. Lungu Testimony, Tr. January 2013 Hearing, Day 1, 179:23-180:5. *See also* Second Lungu Statement ¶ 7; A. Stati Testimony, Tr. January 2013 Hearing, Day 2, 83:1-11; Indicative Term Sheet from Credit Suisse, December 5, 2008, C-521; Email from Antanas Petrosius of Credit Suisse to Artur Lungu, December 18, 2008, C-625.

333 Respondent's Opening Presentation on Liability, October 2012 Hearing, slide 55. Tristan Oil Annual Report for the Year Ended December 31, 2009 at 18, FTI First Scope of Review No. 68.

obtained financing on commercial terms from Credit Suisse, as was on the verge of occurring in December 2008.[334]

218. Kazakhstan's public allegations of fraud and its alleged preemptive right also hindered Claimants' efforts to proceed with Project Zenith by casting serious doubts over Claimants' title to TNG, and they "very considerably affected [Claimants'] image in the international market."[335] KMG E&P, which remained interested in acquiring Claimants' assets, exploited Claimants' inability to sell to international companies by making progressively smaller offers throughout the course of 2009.[336] As Mr. Medet Suleimenov of KMG E&P testified, "any kind of information that became public — or not even public — any kind of information ... does affect the price" an interested buyer would be willing to pay for a company.[337]

219. The impact of Kazakhstan's spurious preemptive right claim and its defamatory leak is conclusively demonstrated. On January 14, 2009, the Fitch ratings agency issued a rating watch for Tristan's long term default rating and senior secured rating, citing both the cloud on TNG's title and the criminal investigation of KPM as the reason.[338] Dow Jones reported that "Fitch believes that a negative resolution of either of the authorities' actions will have a significant negative impact on Tristan's operational and financial profile."[339]

220. If there had been any merit to Kazakhstan's accusations of forgery or fraud, or if it actually had a valid claim to a pre-emptive right as it contended, Kazakhstan would have acted upon those claims.[340] Tellingly, it never did so. Indeed, Mr. Medet Suleimenov testified at the October 2012 Hearing that Kazakhstan's preemptive right could have been exercised in favor of state-owned KMG E&P.[341] Thus, if its claims to a preemptive right had any merit, Kazakhstan's own oil and gas company could have acquired TNG through the

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334 A. Lungu Testimony, Tr. January 2013 Hearing, Day 1, 179:23-180:5. *See also* Second Lungu Statement ¶ 7; A. Stati Testimony, Tr. January 2013 Hearing, Day 2, 83:1-11; Indicative Term Sheet from Credit Suisse, December 5, 2008, C-521; Email from Antanas Petrosius of Credit Suisse to Artur Lungu, December 18, 2008, C-625.

335 A. Lungu Testimony, Tr. January 2013 Hearing, Day 1, 179:23-180:7; A. Stati Testimony, Tr. January 2013 Hearing, Day 2, 83:1-14.

336 Medet Suleimenov Statement ¶¶ 2.12-2.25.

337 Tr. October 2012 Hearing, Day 4, 157:1-16.

338 DOW JONES NEWSWIRES, *Fitch Places Tristan Oil on Rating Watch Negative*, January 14, 2009, C-590.

339 *Id.*

340 *See* First Maggs Report ¶ 66.

341 Medet Suleimenov Testimony, Tr. October 2012 Hearing, Day 4, 137:23-140:3.

exercise of the State's preemptive right.[342] But because Kazakhstan's claim to a preemptive right was groundless, even KMG K&P did not attempt to acquire TNG that way. Instead, it sought access to Claimants' data room and pursued the extensive due diligence that resulted in the reports that Kazakhstan has only recently disclosed to Claimants and the Tribunal.

3. Kazakhstan Refused to Honor Its Commitment to Extend Contract No. 302

221. Kazakhstan also materially harmed Claimants' investments in TNG by agreeing to extend the exploration contract for the Contract 302 Properties, then reneging on that agreement. The evidence conclusively establishes that Kazakhstan committed to extend TNG's Contract No. 302 for a period of two years, but then breached that commitment by failing to sign the addendum to the contract formalizing the extension. Claimants have also shown that Kazakhstan's reversal of its position and deliberate, bad faith refusal to execute the extension violated Kazakh law, the ECT, and international law.[343]

222. Kazakhstan has attempted in vain to maintain its position that it never agreed to an extension of TNG's Contract No. 302 and that it had no obligation to extend the Contract.[344] In the alternative, Kazakhstan has argued that it could have extended the exploration period for only two of the Contract 302 Properties and that TNG would have been under the obligation to relinquish the rest of the Contract Area by the end of the extension, *i.e.*, March 30, 2011.[345] Kazakhstan's arguments are unpersuasive.

223. Kazakhstan's claim that it did not agree to extend Contract No. 302 is contrary to Kazakh law, the statements of its witnesses, Kazakhstan's own conduct at the time, and the contemporaneous documents. On April 2, 2009, the Expert Commission of the MEMR issued a "Resolution" "[t]o permit the extension of the exploration period for two years until 30

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342 Medet Suleimenov Testimony, Tr. October 2012 Hearing, Day 4, 137:23-140:3.

343 Kazakhstan directly and indirectly expropriated Claimants' investment in Contract No. 302, failed to provide the most constant protection and security to Claimants' investment and to treat Claimants' investment fairly and equitably, impaired Claimants' investment through unreasonable and discriminatory measures, and failed to observe the obligations it entered into with respect to Claimants' investment. *See*, for instance, Statement of Claim ¶¶ 273, 332, 351, 362, and 371; Reply on Jurisdiction and Liability ¶¶ 478-9, 495, 514, 524, 533, and 546.

344 Rejoinder on Jurisdiction and Liability ¶¶ 412-36; Respondent's Opening Presentation on Liability, slides 14-5. Kazakhstan also alleges that the contract extension was impossible without an extension of the underlying Subsoil Use License. Even if an amendment to the Subsoil Use License was still required after the 1999 Amendments – which was not the case, pursuant to the Subsoil Use Contracts and the Subsoil Use Law, the Competent Authority was responsible for applying to the Licensing Authority for any required amendments to the Subsoil Use License. The Subsoil User was neither obliged nor authorized to directly seek amendments to its Licenses from the Licensing Authority. *See* Contract No. 302, arts. 6.3.3 and 6.4.2, C-53; 1996 Subsoil Use Law, art. 8(1)(6), C-413; First Maggs Report ¶¶ 57-8.

345 Rejoinder on Quantum ¶¶ 54-68; Respondent's Opening Presentation on Quantum, slide 24.

March 2011 and amend Contract 302 dated 31 July 1998 accordingly before 2 July 2009."[346] The MEMR transmitted the recommendation to TNG a week later, clearly endorsing the Expert Commission's resolution. The MEMR's transmittal letter stated:

> [The MEMR] has resolved to: Permit extension of the exploration period by 2 years until 30.03.2011.
>
> Contract No. 302 dated 31.07.1998 to be amended accordingly by 02 July 2009.[347]

That document is one for which Kazakhstan has disputed Claimants' English translation. But even Kazakhstan's translation, which is quoted above, shows that the MEMR expressly agreed to extend Contract No. 302 and undertook to execute the extension.[348] Those commitments entailed legal obligations under Kazakh law and the ECT's umbrella clause, and gave rise to a legitimate expectation under the Treaty's fair and equitable treatment provision.

224. Kazakhstan's expert on Kazakh oil and gas laws, Professor Ilyasova, explains that according to Article 26(4) of the Law on Oil regarding the procedure for contract extension,[349] the MEMR is obliged to enter the relevant amendments into the contract once it has taken a "positive decision" to extend a Subsoil Use Contract.[350] In his second opinion, Professor Suleymenov concurs that after the MEMR affirmed, on April 9, 2009, its positive decision to "permit extension of the exploration period by 2 years," Kazakhstan was clearly under a legal obligation to execute a contract addendum to formalize its agreed extension.[351] As both parties' Kazakh oil and gas law experts agree, that is the end of the matter under domestic law.

225. Furthermore, the testimony of Kazakhstan's own witnesses supports Claimants' interpretation of the Expert Commission's recommendation and the transmittal letter from the MEMR. Minister Mynbaev confirmed that "the decision actually is made by the competent authority, but the commission gives recommendations. The commission gives

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346 Minutes No. 7 of the Meeting of the Expert Commission for Subsoil Users, April 2, 2009, R-163.2.

347 Letter from the MEMR to TNG, April 9, 2009, R-163.1.

348 Second Suleymenov Report ¶¶ 55-60.

349 Law on Oil, Art. 26(4), Exhibit 4f to Ilyasaova Report.

350 Ilyasova Report at 28.

351 Letter from the MEMR to TNG, April 9, 2009, R-163.1. Draft Addendum No. 9 to TNG Contract No. 302, April 30, 2009, C-168. *See also*, Second Suleymenov Report ¶ 63. In addition, as Professor Suleymenov explains, if the MEMR decided to rescind its positive decision, it would have had to issue a new decision to the subsoil user based on another recommendation from its Expert Commission. Second Suleymenov Report ¶ 58.

recommendation as to whether the subsoil user may count on extension or not."[352] Therefore, the recommendation of the commission is not a mere piece of paper, as Kazakhstan wishes the Tribunal to believe. Rather, the recommendation establishes an expectation that the subsoil user is entitled to rely upon.

226. Kazakhstan's witness Mr. Ongarbaev, formerly of the MEMR, was even more direct. He testified that "[i]n the spring of 2009 it was decided to allow the extension."[353]

227. The concessions by Kazakhstan's witnesses are underscored by Kazakhstan's own conduct at the time. KMG E&P, the state-owned oil company, was actively engaged in discussions and diligence to acquire TNG's rights under Contract No. 302. It is entirely implausible that KMG would have engaged in extensive diligence relating to Contract No. 302 throughout the spring and summer of 2009 if it had not been satisfied that the MEMR had agreed to extend TNG's exploration rights to the block, and that the extension addendum was a mere formality.

228. Indeed, the belatedly-produced asset valuations and due diligence reports prepared for KMG in the summer of 2009, when KMG E&P was still very much interested in acquiring KPM and TNG,[354] confirm that Contract No. 302 would be extended. Squire Sanders and the local Kazakh law firm Olympex, which conducted the legal due diligence for KMG, concluded as follows:

> We have been provided with a copy of MEMR Letter No. 14-05-3106 of 9 April 2009 which gives permission to extend the exploration period under Contract No. 302 for 2 years until 30 March 2011. According to the materials provided by TNG, the estimated expiry date of the Contract is 30 March 2011. ...
>
> In granting this permission MEMR also stated (Letter No. 14-05-3106 of 09 April 2009) that it was necessary "to incorporate changes into Contract No. 302 by 02 July 2009.[355]

229. Similarly, PwC stated in its due diligence report that "TNG has already received an approval from the MEMR to extend the exploration period until 30 March 2011," and RBS concurred in its asset valuation that Contract No. 302 "expires on 30 March

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352 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 113:19-23 (emphasis added).

353 Ongarbaev Testimony, Tr. October 2012 Hearing, Day 6, 68:11-69:2. *See also* Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 115:13-18.

354 *See* KMG 2008 Asset Valuation, September 2008, at 5, C-722 (stating that while Contract No. 302 was not officially part of the Project Zenith sale, "it seems expedient to evaluate this block").

355 Squire Sanders Legal Due Diligence Report, July 30, 2009, at 152, 161, C-725 (emphasis in original).

2011."[356] One of the primary reasons Kazakhstan withheld those documents from Claimants and the Tribunal for so long is that they directly contradict its position on the Contract No. 302 extension.

230. In short, the evidence overwhelmingly demonstrates that Kazakhstan agreed to extend Contract No. 302, then reneged on that commitment.[357] In turn, the manner in which Kazakhstan dragged Claimants along on this issue, then ultimately refused to execute the addendum, had obvious impacts upon TNG's ability to conduct further exploration work on the Contract No. 302 prospects in 2009, most notably the Interoil Reef. Having completed 3D seismic on the Interoil Reef and received positive results, and having acquired the deep drilling rig it needed, TNG was poised to commence that exploration at exactly the same time it was awaiting the MEMR's fulfillment of its commitment.

231. Indeed, had TNG known that Kazakhstan would ultimately refuse to execute the extension, TNG could have proceeded to the appraisal phase of the Munaibay Main area, based on its June 2008 discovery from the Munaibay No. 1 well, as it had intended to do.[358] Because Kazakhstan had not yet indicated that it would extend the exploration period, on March 9, 2009, TNG informed the MEMR of its intention to submit an application to enter the estimation and appraisal stage based on a deeper discovery it had made at the Munaibay No. 1 well and another discovery it had made in the Bahyt area.[359] But TNG did not pursue those applications once the MEMR granted its request to extend the exploration period of Contract No. 302 on April 9, 2009, because it quite reasonably believed there was no need to do so.

232. Kazakhstan has also contended that any exploration activities during an extended exploration period would have needed to be limited to the two areas of Contract No. 302 specifically mentioned in the work program attached to TNG's October 14, 2008,

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[356] PwC Due Diligence Report, June 30, 2009, at 31, C-724; RBS 2009 Asset Valuation, July 31, 2009, slide 8, C-723.

[357] As Professor Suleymenov explains, and contrary to Kazakhstan's allegations, TNG had no means to challenge the MEMR's lack of response before the Kazakh courts. Second Suleimenov Report ¶ 65.

[358] Letter from TNG to the Geology and Subsoil Use Committee of the MEMR, July 24, 2008, C-20 (informing the MEMR that "within 60 days we will prepare Application for introduction of the Estimation Stage and Appraisal program which will include anticipated schedule and volume of works in monetary and physical terms"); *see also* Law on Oil, art. 26(4), which states: "In case of discovering oil, the contractor has right to extend the duration of the contract for the period required for appraisal of the commercial discovery." Exhibit 4f to Ilyasaova Report. In addition, Article 3.4 of Contract No. 302 provides that "[n]ot later than 45 (forty-five) days after receipt by the Competent Body of the foregoing application for introduction of an Appraisal Stage and of the Appraisal Program, the Competent Body and the Contractor shall agree on the duration of the Appraisal Stage." Contract No. 302, July 31, 1998, C-53.

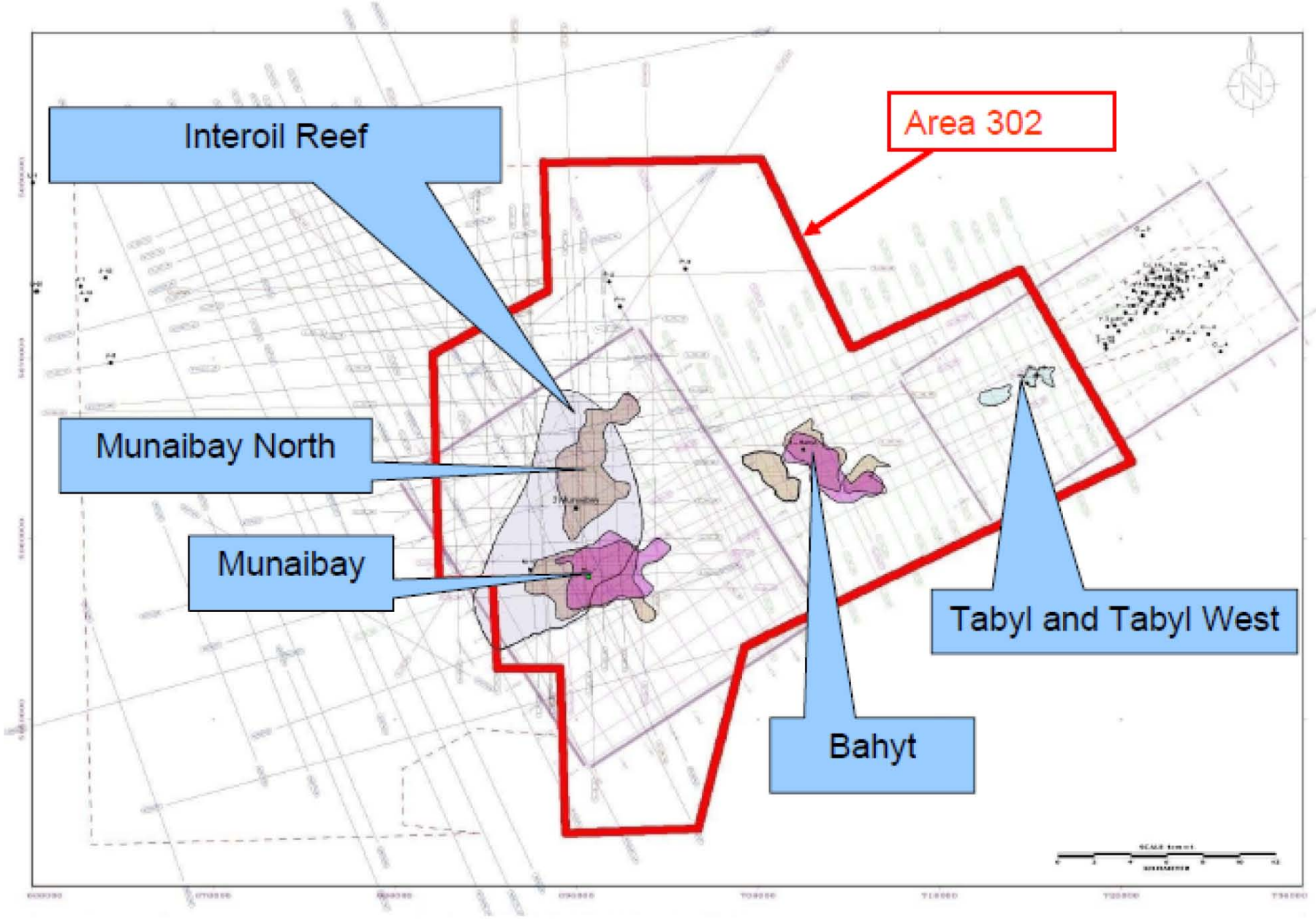
[359] Letter from TNG to the MEMR, March 9, 2009, C-167.

extension request.[360] However, Kazakhstan provides no support for that argument, because none exists.

233. As shown on the map below, the Contract 302 territory includes six contingent or prospective hydrocarbon deposits: Bahyt; Munaibay (also called Munaibay Main); the Interoil Reef (located below Munaibay); Munaibay North; Tabyl; and Tabyl West.[361]

[360] Respondents' Rejoinder on Quantum ¶¶ 56-59. Kazakhstan argues that the work program is both a commitment from TNG to work and a limit on the scope of possible exploration work. There is no support that a work program limits the scope of potential work that may be performed.

[361] *See* First Expert Report of Ryder Scott dated May 15, 2011 (hereinafter "First Ryder Scott Report") at 5 and at Exhibit 12; Tabyl Block (Contract 302 Area) – Deep Munaibay Reef Build-Up Prospect (attached to Claimants' email dated February 18, 2013), C-732; *see also* Respondent's Opening Presentation on Quantum, slide 23.


Interoil Reef
Area 302
Munaibay North
Munaibay
Tabyl and Tabyl West
Bahyt

234. Claimants were always clear regarding their intention and desire to explore the entire contractual area. For example, on October 10, 2008, TNG informed Kazakhstan that it was withdrawing its August 2008 application to move to the appraisal phase for Munaibay, precisely because it intended "to take this opportunity to fully and thoroughly explore the contractual territory."[362] TNG's reason for that decision was that the Munaibay No. 1 well suggested "a high probability of additional discovery of more deep-lying raw hydrocarbon reservoirs on Munaibay area."[363] As Mr. Lungu testified at the January 2013 Hearing, that is a "direct reference" to the Interoil Reef, which is located some 6,000 meters below the Munaibay surface area.[364]

235. Accordingly, on October 14, 2008, TNG submitted a request to extend the exploration period of Contract No. 302 for two years for the entire territory.[365] Kazakhstan's argument is derived solely from the minimum work program attached to TNG's extension request, which refers to Claimants' immediate budget outlays to drill in Munaibay and Bahyt.[366] There is nothing in either the express provisions of Contract No. 302 or in Kazakh law that limited TNG's exploration activities to the areas mentioned in a minimum work program. To the contrary, such work programs are routinely amended. As Mr. Cojin testified, there was nothing to prohibit KPM and TNG from amending their work program, or from conducting activities above and beyond their minimum commitments, which they had routinely done in the past.[367] Kazakhstan would have benefited from any additional exploration and hydrocarbon discoveries, so it would have had no reason to prevent that work.[368]

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362 Letter from TNG to the MEMR, October 10, 2008, C-66; *see also* Letters from TNG to the Geology and Subsoil Use Committee of the MEMR, to the MEMR and to Zapkaznedra, July 24, 2008, C-20; Application filed by TNG with the MEMR, August 11, 2008, C-21.

363 Letter from TNG to the MEMR, October 10, 2008, C-66.

364 *See* Lungu Testimony, Tr. January 2013 Hearing, Day 1, 250:22-250:25 (corrected transcription).

365 Application from TNG to the MEMR, October 14, 2008, C-67.

366 *See* Application from TNG to MEMR, October 14, 2008 (with attached work program), C-67; *see also* Draft Addendum No. 9 to Contract No. 302, April 30, 2009 (with attached, updated work program), C-168. The draft addendum confirms that the proposed work program is a Minimum Work Program because the program is included in a new Section 7.6.4, amending Section 7.6 of the contract. In Contract 302, C-53, Section 7.6 addresses "Minimum Work Program." Another section of the contract, Section 7.3, addresses the Annual Work Program and Budget. Annual Work Programs require MEMR approval to amend (§ 7.4), but MEMR approval is not required to exceed the work set out in a Minimum Work Program.

367 A. Cojin Testimony, Tr. January 2013 Hearing, Day 2, 64: 7-19; 65:1-11.

368 Kazakhstan's own experts at GCA confirm that changes to work programs are possible. *See, e.g.*, First GCA Report ¶ 106

236. The Kazakh authorities fully understood Claimants' intentions. In its April 2, 2009 Resolution, the Expert Commission concluded that the entire Contract 302 Area would be explored:

> Additional time is needed to complete the drilling of deep wells in the Munaibai East and Bahyt areas and to conduct a comprehensive and detailed survey of the contract area in order to obtain sufficient information for its assessment.[369]

237. Kazakhstan's unfair refusal to execute the agreed extension precluded Claimants from pursuing exploration activities, proving the full value of the Contract No. 302 Properties, and interfered with Claimants' ability to use and dispose of their investments in violation of the ECT and international law.

4. Kazakhstan Created an After-the-Fact Tax Dispute To Saddle KPM and TNG With A Groundless US $62 Million Assessment

238. Kazakhstan's claim that KPM and TNG owe US $62 million in corporate back taxes is simply another contrived allegation stemming from Nazarbayev's October 2008 directive and the outcome-driven investigative onslaught that followed. Scott Horton, Claimants' expert on Kazakhstan's political environment, explains that fabricating tax disputes is a well-recognized strategy Kazakhstan uses to pursue investors who have fallen out of favor with the President. He notes that

> a [U.S.] State Department investment climate statement on Kazakhstan reads, "In practice the application of tax laws has been uneven, and in some cases blatantly unfair. This has been particularly true in cases where a company is involved in another, unrelated dispute with authorities."[370]

239. PriceWaterhouseCoopers confirms that view. In its advice to KMG E&P during the Project Zenith due diligence, PwC noted that Kazakhstan's tax legislation is "often ambiguous and … subject to frequent, sometimes retroactive changes."[371] It further explained that "tax authorities often make arbitrary assessments" and that "insignificant details … can be the basis upon which the validity of a transaction is challenged."[372] PwC also warned that "Kazakhstan's tax authorities do and will seize every opportunity to challenge a particular

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369 Minutes No. 7 of the Meeting of the Expert Commission for Subsoil Users, April 2, 2009 (emphasis added), R-163.2.

370 Horton report ¶ 62.

371 PwC Due Diligence Report, June 30, 2009, at 161, C-724.

372 PwC Due Diligence Report, June 30, 2009, at 161, C-724.

transaction, especially those involving subsoil users and/or substantial amounts of money" and that "tax audits are often conducted by the tax authorities in an aggressive and disruptive manner, resulting in an unnecessary seizure of substantial volumes of documentation and becoming, in practice, a very time-consuming and costly process for taxpayers."[373]

240. It is thus common practice for Kazakhstan to apply its tax laws inconsistently and unfairly and to raise tax disputes on top of other allegations waged against a targeted foreign investor. That adequately describes the corporate tax dispute that Kazakhstan raised, for the first time, in February 2009, following a lengthy, disruptive audit.

241. As explained below, Kazakhstan is wrong on the substance of that dispute. The companies' historical approach toward their tax filings, which Kazakhstan approved prior to October 2008, belies Kazakhstan's *post hoc* legal position in the corporate tax "dispute." Both the Kazakh appellate court and Court of Cassation rejected Kazakhstan's position and endorsed Claimants' position on the matter, and the "dispute" was settled in Claimants' favor before Kazakhstan directly expropriated KPM and TNG in July 2010. Moreover, even if Kazakhstan were correct on the legal interpretation of its tax laws — which it is not — the back taxes that KPM and TNG allegedly owe would be nowhere near US $62 million.

a. Kazakhstan's Position On the Corporate Tax Dispute Is Wrong on Its Merits

242. As of 2004, all three of Claimants' subsoil use contracts contained the same tax provisions that governed how KPM and TNG could deduct various expenses in any given year. Under the contract provisions, KPM and TNG deducted "expenses for the acquisition of fixed assets and construction expenses" under Article 20 of the Tax Law, which permitted immediate, 100% depreciations of those expenses in the year they were incurred.[374] KPM and TNG included well-drilling expenses in that category because (i) a well is a fixed asset and (ii) new wells are constructed (and acquired) by drilling.[375] That was the companies' common and historical practice, and for years prior to October 14, 2008, the Kazakh tax authorities repeatedly approved the companies' method of depreciating drilling expenses.[376]

243. In a report from the Tax Committee dated February 10, 2009, however, Kazakhstan abruptly changed its position on the manner in which KPM and TNG depreciated

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373 PwC Due Diligence Report, June 30, 2009, at 161, C-724.

374 Contract No. 305, March 30, 1999, C-45; Contract No. 210, August 12, 1998, C-52; and Contract No. 302, July 31, 1998, at Sections 4.4.7.1, 4.4.7.4 (sub-point 8) and 4.4.7.11 of the 2004 Supplement, C-53.

375 *See generally* Second Maggs Report ¶¶ 6-33.

376 Second Maggs Report ¶¶ 12-16, 23-24, 33.

drilling expenses and demanded that such expenses be depreciated under Article 23 of the Tax Law, rather than Article 20. Expenses subject to Article 23, according to the law, were to be capitalized the year they were incurred and depreciated gradually at a rate of 25% per year. Kazakhstan's expert Professor Balco described Article 23 as a "specific article dealing with expenditures which may not even qualify as an asset, but they are subject to capitalization and subsequent depreciation."[377] Generally speaking, Article 23 of the Tax Law stipulates that certain expenses relating to "geological research and development" be depreciated in that way.

244. Claimants' Subsoil Use Contracts specified the expenses that were subject to Article 23. Article 4.4.7.12 stated that four types of expenses were to be depreciated under Article 23: (i) expenses for "intangible assets relative to the right for acquisition of geological survey, Exploration and Production;" (ii) expenses for a "subscription bonus;" (iii) expenses for a "bonus of commercial discovery;" and (iv) any expenditures covered under item 2.3.[378] Kazakhstan does not contend that any of the first three expenses are applicable here; rather, it claims that KPM's and TNG's well-drilling expenses are "covered under item 2.3" of those contracts.

245. As was explained during the Hearing on Quantum, Article 2.3 of the subsoil use contracts specifically excludes "expenses for acquisition of fixed assets and own-account construction expenses." It provides:

> **2.3 Principles of tax accounting of Contractor's expenses during different periods of Contractual activity**
>
> 2.3.1 Prior to Production, all expenses related to conduct of Contractual activity, except for the expenses for acquisition of fixed assets and own-account construction expenses, shall be subject to inclusion into expenses determined by the Contractor under Article 23 of the Tax Law and accounting on such a group shall be performed under item 4.4.7.12 of the Procedure.
>
> 2.3.2. Since commencement of Production, Contractor shall maintain tax accounting of expenses as follows:
>
> 1. expenses for geological prospecting and exploration operations listed in item 6.2.5 of the Procedure, except for expenses incurred for acquisition of fixed assets and own-account construction, capitalized before completion of Exploration operations.

[377] Balco Testimony, Tr. January 2013 Hearing, Day 3, 57:20-24.

[378] Contract No. 305, March 30, 1999, C-45; Contract No. 210, August 12, 1998, C-52; and Contract No. 302, July 31, 1998, at Sections 4.4.7.12 of the 2004 Supplement, C-53.

> 2. with respect to the sold production, expenses for the Reporting period shall be considered costs of production and expenses relative to its sale;
> 3. other expenses shall be considered in accordance with the norms of this Procedure.
>
> 2.3.3 Expenses for acquisition of fixed assets and own-account construction shall be entered in accordance with items 4.4.7.1 - 4.4.7.11 of this Procedure.[379]

246. Kazakhstan's Tax Committee specifically noted the special treatment provided to "expenses for acquisition of fixed assets and own-account construction" in Article 2.3 of the Subsoil Use Contracts when it issued its Act of Inspection of the companies on September 9, 2005, before the State's harassment campaign.[380] After the State's harassment campaign had commenced, however, the Tax Committee paraphrased, rather than quoted, Article 2.3 in its inspection report, deliberately omitting the reference to the exception for "expenses for acquisition of fixed assets and own-account construction."[381]

247. Notwithstanding Kazakhstan's about-face on its historical approval of the companies' tax depreciation rates, its post-2008 position that drilling expenses should be depreciated under Article 23 contradicts the clear wording of the Subsoil Use Contracts. As Professor Maggs explains, in considering a contract under Kazakh law, one must "take into account the literal meaning of words and expressions."[382] Article 4.4.7.4 of the Contracts allowed "expenditures for own-account construction" to be depreciated under Article 20 of the Tax Law. If there is any doubt as to the meaning of those terms, one need look no further than the MEMR. Professor Maggs notes that

> The Ministry of Energy and Mineral Resources of the Republic of Kazakhstan has taken the position that the drilling of wells is a construction expense. This is an authoritative statement of the literal meaning of the words [of the contracts].[383]

248. It follows from the MEMR's "authoritative statement" and the parties' historical practice that KPM's and TNG's drilling expenses were properly depreciated under Article 20 of the Tax Law. Even Kazakhstan's expert Deloitte agrees with Claimants'

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379 Contract No. 305, March 30, 1999, C-45; Contract No. 210, August 12, 1998, C-52; and Contract No. 302, July 31, 1998, C-53 at Section 2.3 of the 2004 Supplement (emphasis added).

380 Second Maggs Report ¶¶ 12-14 (*citing* Act of Inspection #32 of KPM for 2003-2004 activity, September 9, 2005, Exhibit 1).

381 Second Maggs Report ¶ 15.

382 Second Maggs Report ¶¶ 25-27 (*citing* Kazakh Civil Code art. 392).

383 Second Maggs Report ¶ 27.

interpretation of the tax provisions at issue, because in its model of Claimants' damages, it deducted all of KPM's and TNG's capital expenditures, including drilling expenses, in the year incurred. Deloitte explained, "Depreciation charges were planned by writing off the complete capital expenditure of the respective year in line with subsoil use contracts," citing Section 4.4.7.11 of the 2004 supplement to the Subsoil Use Contracts.[384] Section 4.4.7.11 is the provision allowing KPM and TNG to depreciate 100% of "expenditures for own-account construction" during the year incurred.[385]

249. Even assuming, however, that Kazakhstan's post-October 2008 interpretation of those amortization provisions were correct — which it is clearly not — the "back taxes" that KPM and TNG would owe would amount to a mere fraction of Kazakhstan's claim of US $62 million. That is because, as Professor Balco agreed, the issue is not whether the drilling expenses could be deducted at all, but when they would be deducted. Professor Balco testified as follows:

> Q. Isn't it the case then that the issue here is not whether these deductions could be taken, but when they could be taken?
>
> A. That's right.
>
> Q. So, in other words, claimants argue that these expenses could have been deducted 100% in the year that they were incurred, whereas the Republic claims that they could only be deducted 25% in that year and then capitalized and further gradually deducted over time?
>
> A. That's correct.[386]

250. The Tax Committee's assessment of US $62 million is not correct, because, as FTI explains, it only considered the tax savings that would have accrued during the three year period of the tax audit.[387] Thus, even if the Tax Committee's calculation of alleged back taxes was correct as of February 2009, when it made its assessment, that figure is no longer applicable, because it does not take into consideration the deductions the companies would have been able to make in subsequent years. As FTI explains:

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[384] *See* Deloitte Report ¶¶ 286, 309, 334, 355, 378, 402, 426, 452. Deloitte cited to "point 4.4.4.7.11" of the Subsoil Use Contracts, but this appears to be a typographical error (inclusion of an additional 4) because no such provision appears in the contracts.

[385] Contract No. 305, March 30, 1999, C-45; Contract No. 210, August 12, 1998, C-52; and Contract No. 302, July 31, 1998, C-53 at Section 4.4.7.11 of the 2004 Supplement. That provision also mirrors Article 20(10) of the Tax Code.

[386] Balco Testimony, Tr. January 2013 Hearing, Day 3, 63:3-12.

[387] Third FTI Report ¶ 6.112.

> [I]f the Tribunal finds that the assessment of additional taxes and penalties was lawful, both the valuation conclusions presented by FTI and Deloitte would have to be amended. This is because any additional taxes (excluding penalties) that would have been paid by KPM and TNG as a result of a misapplication of the tax code with respect to depreciation would be offset by future tax benefits accrued as a result of an increase, all things being held equal, in capital deductions over time. Therefore, the back-tax assessment calculated as of February 2009 cannot be applied against KPM and TNG today without amending the calculation to take into account subsequent available deductions. …
>
> FTI has prepared an example below comparing a 100.0% depreciation rate versus a 25.0% depreciation rate over 10 years for a notional $4,000 capital expenditure:

Figure 15 – Capital Expenditures Example

Description	1	2	3	4	5	6	7	8	9	10
Opening balance	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Expenditures	$ 1,000	$ 1,000	$ 1,000	$ 1,000	$ -	$ -	$ -	$ -	$ -	$ -
Depreciation Rate (100.0%)	$ (1,000)	$ (1,000)	$ (1,000)	$ (1,000)	$ -	$ -	$ -	$ -	$ -	$ -
Closing balance	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Total capital expenditures	**$ 4,000**									
Total depreciation	**$ (4,000)**									

Description	1	2	3	4	5	6	7	8	9	10
Opening balance	$ -	$ 750	$ 1,313	$ 1,734	$ 2,051	$ 1,538	$ 1,154	$ 865	$ 648	$ 487
Expenditures	$ 1,000	$ 1,000	$ 1,000	$ 1,000	$ -	$ -	$ -	$ -	$ -	$ -
Depreciation Rate (25.0%)	$ (250)	$ (438)	$ (578)	$ (684)	$ (513)	$ (385)	$ (288)	$ (216)	$ (162)	$ (487)
Closing balance	$ 750	$ 1,313	$ 1,734	$ 2,051	$ 1,538	$ 1,154	$ 865	$ 649	$ 487	$ -
Total capital expenditures	**$ 4,000**									
Total depreciation	**$ (4,000)**									

> As shown above, depreciation equalizes over time.[388]

251. Indeed, PriceWaterhouseCoopers confirmed that point in its due diligence report of KPM and TNG. It stated that, if the companies lost their (then-pending) legal challenge of the tax assessment, "the remaining portion ... of additional [corporate income tax] would be only a cash flow issue: [KPM and TNG] will be required to pay the tax now but would be able to take deductions of the challenged expenses in future (*i.e.*, the tax authorities are challenging the timing of deductions rather than the right to deduct the well construction expenses). Therefore, [KPM and TNG] should be able to deduct the same amount of well construction expenses but at lower depreciation rates through a longer period of time."[389]

252. Kazakhstan has introduced no evidence showing what sum KPM and TNG would owe today, assuming Kazakhstan's legal position were correct (which Claimants dispute). Nevertheless, it is clear that the back taxes Kazakhstan claims are owed are only a fraction of the US $62 million it asserts in this proceeding. The Tribunal does not need to

[388] Third FTI Report ¶¶ 6.109-6.111, Figure 15 (emphasis added).

[389] PwC Due Diligence Report, June 30, 2009, at 80 (emphasis added), C-724.

concern itself with the proper calculation, however, because as shown above and in the following section, Claimants' position on the applicable tax provisions is the correct view.

b. Kazakh Courts Vindicated Claimants' Position on the Tax Dispute

253. The foregoing discussion on the substance of the tax dispute is largely academic for the Tribunal's purposes. That is, the Tribunal need not undertake to perform its own analysis of the contractual language and the Kazakh tax laws, because, after an exhaustive judicial process, the Kazakh domestic courts resolved this matter in favor of Claimants.

254. Professor Maggs explains the procedural background of the domestic litigation on this issue:

> There were a number of court decisions involving the issue of depreciation of costs of well-drilling by KPM and TNG. While the Specialized Interdistrict Economic Court of Almaty (the court of first instance with jurisdiction over tax challenges), issued a decision on September 8, 2009, rejecting TNG's challenge to Kazakhstan's revised tax assessment for 2005-2007 and a decision on September 9, 2009, rejecting KPM's challenge to its revised tax assessment for 2005-2007, on appeal, the Division for Civil Cases of the City of Astana issued decisions on October 28, 2009, reversing and remanding the September 8 and September 9 decisions. The appeal court's reasoning was that the trial court had failed to consider the extensive evidence KPM and TNG had presented establishing that the drilling of wells constituted "own-account construction."
>
> On December 25, 2009, the Specialized Interdistrict Court of Almaty issued a decision on the remanded cases, which had been combined into a single case. The Specialized Interdistrict Court again rejected the challenges by TNG and KPM to the tax reassessment.
>
> TNG and KPM again appealed to the appellate instance, the Division for Civil Cases of the City of Astana, which issued a decision on April 23, 2010, again reversing the trial court decision.
>
> ...
>
> Kazakhstan appealed the April 23, 2010, decision of the appellate court to the [Court of Cassation], which heard the case on June 22, 2010, agreed with the reasoning of the appellate court, and affirmed the appellate court decision.[390]

[390] Second Maggs Report ¶¶ 17-20.

255. Kazakhstan is asking the Tribunal to disregard the sixteen months of litigation that Claimants pursued in order to be vindicated on this baseless tax dispute, because, it argues, the Kazakh Supreme Court overturned the decisions of the appellate court and the Court of Cassation on November 3, 2010, after the July 2010 direct expropriation. The Tribunal should disregard that decision of the Kazakh Supreme Court for two reasons.

256. First, as Professor Maggs explains, that decision is suspect at best, and marks a complete change of the Supreme Court's position on this issue.[391] Additionally, the Supreme Court decision contained no independent reasoning; it merely repeated the arguments of the tax authorities and reinstated the decision of the trial court, which had already been found by the appellate courts to have failed to consider the extensive evidence presented by KPM and TNG that the drilling of wells constituted "own-account construction." Upon comparing the extensive reasoning of the appellate court and the Court of Cassation with the total lack of reasoning from the Supreme Court, it is difficult for an independent expert to conclude that the Supreme Court was correct on the law. In that respect, it is notable that during cross-examination, Professor Balco admitted that he did not even consider the opinions of the Kazakh appellate court or the Court of Cassation. He testified:

> Q. Did you review all four Kazakh court decisions on this issue when you were preparing your report?
>
> A. I didn't have available the two decisions that were mentioned yesterday. I tried to access them and they are not available to me.
>
> Q. Did counsel for Kazakhstan provide you with all the materials you would need to prepare your report?
>
> A. They did provide me with the materials that I considered necessary. And I actually yesterday asked, after these two decisions were mentioned, I asked to have an access to those; unfortunately they were not able to locate it.[392]

257. Second, Professor Maggs notes that the timing of the Supreme Court decision, shortly after the State's expropriation of Claimants' investments in KPM and TNG, "raises serious questions" as to the cause of the change of judicial opinion on the matter.[393] As Professor Maggs explains, by July 2010, the decision of the Court of Cassation in Claimants' favor had entered into force and was considered final, although, for a period of one year it was subject to limited, discretionary review by the Supervisory Judicial Division for Civil and

[391] Second Maggs Report ¶¶ 21-23.

[392] Balco Testimony, Tr. January 2013 Hearing, Day 3, 84:7-17.

[393] Second Maggs Report ¶ 23.

Administrative Cases of the Supreme Court. Mr. Condorachi explained at the October 2012 Hearing that, before the seizure in July 2010, the matter had been finally resolved and neither KPM nor TNG owed any corporate back taxes. He stated:

> So the notices of the tax committee were found by Astana court as void, and the way that the taxes were calculated were considered invalid. The tax committee challenged this decision in cassation [court], and [as of] the moment of expropriation the decision entered [had] into force; and as you see, only after expropriation this decision was challenged again. So at the moment of expropriation there was no valid back-taxes, and all the instances, including cassation instances, supported the position of KPM.[394]

258. Indeed, Claimants were not even aware of the November 3, 2010, supervisory review decision of the Supreme Court until Kazakhstan mentioned it in its Statement of Defense in this arbitration. Claimants do not know whether the Kazakh authorities who managed KPM's and TNG's interests after the expropriation participated in the Supreme Court case or ensured that KPM and TNG were properly defended. Kazakhstan has presented no evidence in that regard.

259. The entire corporate back tax assessment was nothing more than a contrivance intended to harass Claimants and cause their companies severe financial duress. Kazakhstan has now, belatedly, focused on the tax claim in an attempt to lessen its liability to Claimants. Mr. Taras Khalelov, KPM's and TNG's trust manager, confirmed both points at the Hearing on Quantum when he was questioned on the matter. He testified as follows:

> Q. Was any of the money in the escrow account used to pay $62 million for corporate back-taxes that the government claims was owed?
>
> A. Are you speaking about penalties? Penalties or — if you are speaking about penalties, I don't know about any penalties being paid. Especially on behalf of Kazakhstan, I guess there are certain authorities dealing with these issues or some state bodies dealing with these issues.
>
> Q. So you have no personal knowledge as to whether any of the money in escrow has been paid in relation to any of the penalties that were imposed on KPM or TNG?
>
> A. I don't know about any penalties of KPM and TNG. The only thing I can say is that this escrow account, I can only say that

[394] Condorachi Testimony, Tr. October 2012 Hearing, Day 3, 5:25-6:25.

> current and regular taxes are being paid from this escrow account, but I know nothing about any penalties or not being paid from it.[395]

260. If the corporate back tax assessment were valid, Kazakhstan would be obliged, under Kazakh law, to recover those funds from KPM and TNG directly. Kazakhstan has not done so, either because the issue was a farce to begin with or because Kazakhstan seeks to keep the issue "alive" for a damages reduction in this case (or both).

261. The corporate back tax assessment is clearly a breach of the ECT. Kazakhstan applied its tax laws in an inconsistent and unfair manner, and as part of its overall campaign of harassment and indirect expropriation. Prior to October 2008, Kazakhstan endorsed Claimants' method of deducting expenses, and only after its harassment campaign commenced did it begin to allege that those deductions were improper. The assessment of US $62 million was in bad faith, and it does not even correspond to the taxes KPM and TNG would owe if Kazakhstan's position on this matter were correct. Furthermore, since the tax provisions were codified in Claimants' subsoil use contracts, Kazakhstan's baseless back tax assessment is a clear breach of the umbrella clause. The Tribunal should not hesitate to reject Kazakhstan's position on this matter.

5. Kazakhstan Devised A Final Scheme to Formally Seize KPM's and TNG's Assets

262. As of mid-2010, Kazakhstan had frozen KPM's assets, frozen KPM's bank accounts, and initiated (unsuccessful) bankruptcy proceedings against KPM. Further, Kazakhstan had effectively taken away TNG's Contract No. 302 by failing to execute the agreed extension. Kazakhstan had not cleared the spurious cloud it had created over TNG's title, and it had embroiled both KPM and TNG in unnecessary, protracted tax litigation. Kazakhstan's misconduct over the preceding twenty months had driven KPM's and TNG's upper-level management from the country and severely hampered the operations of the companies.

263. Despite that barrage of misconduct, and while Kazakhstan's efforts had seriously damaged the value of Claimants' investments and undermined Claimants' ability to manage or dispose of them, Kazakhstan had failed to force Claimants to voluntarily surrender them or sell them to KMG at a firesale price. Kazakhstan therefore decided to step in and seize Claimants' investments outright.

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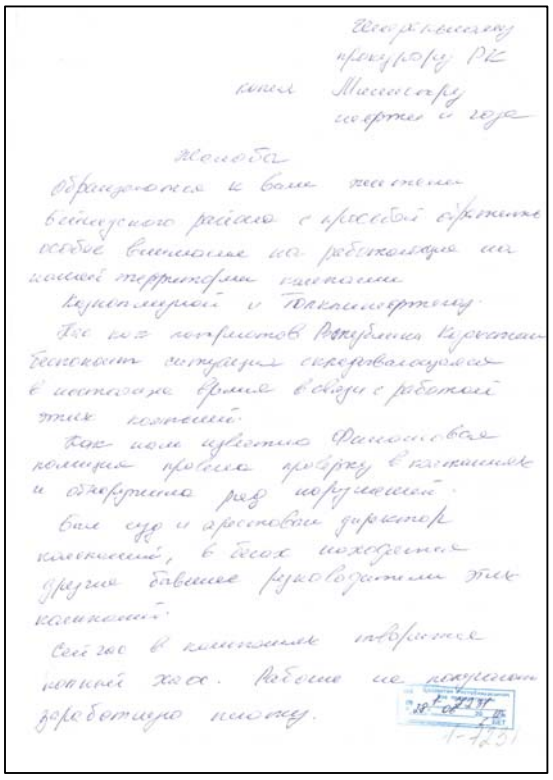
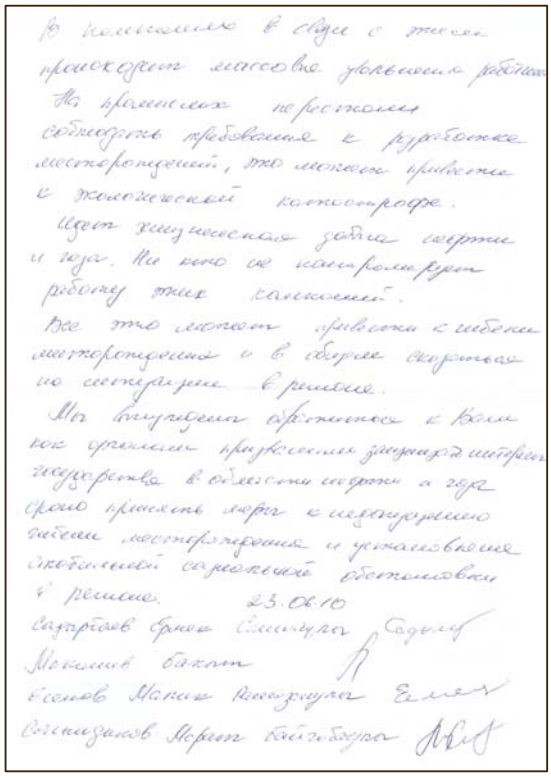
[395] Khalelov Testimony, Tr. January 2013 Hearing, Day 2, 151:3-19.

264. At the end of June 2010, the Prime Minister of Kazakhstan ordered a final round of inspections of the companies, once again led by the Financial Police. Since there was no credible ground on which to base such an inspection, Kazakhstan relied on vague and dubious "complaints" about the companies, allegedly raised by four unknown residents of the Mangystau region. It is Kazakhstan's case that the following two-page, handwritten letter served as the basis for its Prime Minister and Deputy General Prosecutor to order more than a half-dozen agencies, once again led by the Financial Police, to inspect KPM and TNG:[396]





265. In one of the more memorable moments of the October 2012 Hearing, Kazakhstan's Deputy General Prosecutor, Mr. Kravchenko, tried to sell this incredible story to the Tribunal. He testified as follows:

> Q. … this complaint from these four citizens was received on June 28th 2010; correct?
>
> A. Indeed. ...
>
> Q. So your testimony is that based on this two-page handwritten note from four citizens—as well as what you mention in paragraphs 7.6(a) and (b), of which there is no evidence in the record—based on that, you sent out instructions to a number of agencies to investigate this complaint, right?

[396] Exhibit 1 to Second Kravchenko Statement.

> A. That's correct. That was it. ...
>
> Q. … you received this two-page handwritten note from four unknown citizens, and on the very same day you order at least seven national agencies to inspect KPM and TNG. Is that your testimony?
>
> A. Absolutely right.
>
> Q. Is that the way things normally work with your office in Kazakhstan: you just get a complaint from some unknown citizens, and the very same day you send out half the government to check it out?
>
> A. No, that's not the regular practice as such.[397]

266. Indeed, it was not "regular practice as such." Putting aside the fact that Kazakhstan's senior leaders sent multiple agencies to inspect KPM and TNG anew, the personal involvement of the Prime Minister and the renewed involvement of the Financial Police demonstrate that Kazakhstan's actions in mid-2010 were the final act in Kazakhstan's scheme to wrest ownership and control of Claimants' investments.

267. At the October 2012 Hearing, counsel for Kazakhstan chastised Claimants for the suggestion that there was such a scheme or that it involved the Financial Police. Counsel asserted:

> The claimants present all inspections as part of one coordinated attack. They call the July 2010 inspections even the financial inspection blitz. These inspections originated with the General Prosecutor's Office, they have nothing to do with the financial police, and the financial police is who the claimants say are at the centre of the conspiracy. You will hear again Mr. Kravchenko, who can explain the structure.[398]

268. Mr. Kravchenko certainly did explain the "structure." When faced with evidence of the Financial Police's involvement in the final 2010 wave of inspections, he could not deny it:

> Q. ... the letter does in fact indicate the involvement of the financial police at this point in time with these inspections at the end of June/beginning of July 2010; is that correct?
>
> A. I do not deny that the financial police was involved.[399]

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[397] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 108:24-114:2.

[398] Opening Statement of Dr. Nacimiento, Tr. October 2012 Hearing, Day 1, 157:2-9.

[399] Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 120:17-21. Claimants' counsel for KPM and TNG, Mr. Condorachi, also testified that the Financial Police were present in KPM's and TNG's offices in July 2010. Tr. October 2012 Hearing, Day 2, 120:16-122:9.

269. Mr. Serik Rakhimov, one of the Financial Policemen who was actually present during the July 2010 inspections, also confirmed that he and Mr. Arman Rakhimov of the Financial Police headed the working group that was assembled specifically to deal with the "problem" of KPM and TNG. He testified as follows:

> Q. Were you present at KPM or TNG's offices in July 2010?
>
> A. The offices of KPM and TNG are situated in the same building and I did actually visit this building. ...
>
> Q. What were you doing there?
>
> A. My task was to supervise the observance of the proper procedures and legality in the seizure of documents, so that there will be, for example, no resistance to or refusals to provide the necessary documents to the working group, and to generally supervise the observance of order. ...
>
> Q. If you remember, approximately how many members from the financial police were involved in this working group in July 2010?
>
> A. We were only two. There were only two people from the financial police.
>
> Q. And that's yourself, and who was the other officer?
>
> A. Yes, and my namesake, Arman Rakhimov.[400]

270. The presence of the Financial Police at KPM's and TNG's offices in July 2010 to "supervise" the inspections caused Claimants' remaining foreign personnel to leave the country. Mr. Condorachi, who witnessed the Financial Police searching the companies' files on July 4, 2010, explained that, as a result, Claimants' management decided it would be best that he and several other middle managers leave Kazakhstan. Mr. Condorachi testified that the decision was made because "previous experience of our dealings with financial police... ended up jailing one of our employees."[401]

271. With no management left to challenge the Financial Police or the other seven ministries that ransacked KPM's and TNG's offices, Kazakh officials seized the companies' geological data and its remaining business documents, and carried out the final "inspections" that would quickly result in the final, direct expropriation of Claimants' investments in Kazakhstan.

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[400] S. Rakhimov Testimony, Tr. October 2012 Hearing, Day 6, 31:6-32:23.

[401] Condorachi Testimony, Tr. October 2012 Hearing, Day 2, 120:16-122:9.

6. Kazakhstan Terminated Claimants' Subsoil Use Contracts and Seized the Companies' Assets Without Due Process and On Contrived Grounds

272. In September 2009, the Ministry of Oil and Gas had analyzed KPM's and TNG's Subsoil Use Contracts and concluded that "there are no direct grounds for termination of contracts since there are no facts established by a court evidencing a failure to fulfill the contract and/or work program."[402] Additionally, a comprehensive inspection of the companies' operations in January 2010 revealed no grounds on which to terminate the contracts.[403] The results of that inspection show quite the opposite — that KPM and TNG had each vastly exceeded their contractual obligations.

273. Minister Mynbaev was forced to admit as much during the October 2012 Hearing. He testified as follows:

> Q. ... you order the unscheduled inspection, as of January 22nd 2010, of [TNG]; and there is also a similar order, bearing your signature, with respect to [KPM]. Correct?
>
> A. I recall signing these documents, I believe I did, in respect of both companies.
>
> Q. Then if we look back at the results of that inspection that you ordered, which is at [Exhibits C-385 and C-386] in your binder ... both of those inspections in fact concluded that my clients were in compliance with their subsoil use contract obligations; correct?
>
> A. Apparently so.[404]

274. Indeed, the inspection report concerning KPM's Borankol field stated: "The obligations regarding the minimum work program for the period 1999 — 2009 amounted to a total of [71.9 million] US dollars. *De facto* there were performed works amounting to [473 million] US dollars, which exceeds [the] amount of contractual obligations by 6.6 times."[405] The inspection of TNG concluded its actual expenditures were 3.4 times greater than its contractual obligations.[406]

275. Thus, there was no reason to re-inspect the companies in June 2010, less than six months after they were found to have substantially exceeded their obligations. The June-

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

403 Reports of the MEMR for KPM, January 25 - February 6, 2010, C-385; Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

404 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 131:3-15.

405 Reports of the MEMR for KPM, January 25 - February 6, 2010, at 5, C-385.

406 Reports of the MEMR for TNG, January 25 - February 5, 2010, C-386.

July 2010 inspections were simply a pretext for Kazakhstan to manufacture its planned expropriation. That is evidenced by the fact that the notices of alleged contract violations were sent to KPM and TNG before the Kazakh authorities concluded their inspections and reported the results and before they disclosed the results to KPM and TNG.[407] Indeed, Kazakhstan failed to give proper notice to KPM and TNG and it denied KPM and TNG a right to appeal the inspection reports, as required by Kazakhstan's Law on Private Business.[408]

276. Those breaches of procedure constitute clear violations of Claimants' due process rights, under any legal standard, and they are breaches of Article 72 of Kazakhstan's Subsoil Law of 2010 and Section 38 of Kazakhstan's Law on Private Business. As Mr. Eduard Calancea testified, those legal provisions state

> that unless there are objections [to the inspection results], [the acts of inspection] should be served within three days. And [KPM and TNG] had objections. So the timeline indicated [in the legal provisions] was in case there were no objections, but [KPM and TNG] had objections and you can see these objections in our letters.[409]

277. Kazakhstan tries to justify its clear breach of that process by claiming that, regardless of the legal formalities ensuring that an investor has advance notice of an alleged breach, Claimants should have been on notice of the alleged violations, because they arose during the course of inspections in which personnel from the companies participated.[410] Kazakhstan has provided no evidence to support that position — it is sheer conjecture from Mr. Ongarbaev. In any event, Mr. Calancea confirmed at the October 2012 Hearing that it is simply not accurate. He testified:

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[407] Kazakhstan sent its notices of alleged contract violations to KPM and TNG on July 14, 2010 (C-2, C-6, and C-7), but at that time, inspections by the Ministry of Oil and Gas, the Department for Emergency Situations, the Geology Committee, and Ministry of Industries and New Technologies were not yet completed. *See* Act on Results of Inspection of KPM from Department of Emergency Situations, July 15, 2010, C-647; Act on Results of Inspection of TNG from Department of Emergency Situations, July 15, 2010, C-648; Act on the Unscheduled Inspection Regarding the Fulfillment of Contractual Obligations of KPM from the Ministry of Oil and Gas, July 15, 2010, C-649; Act on the unscheduled Inspection Regarding the Fulfillment of Contractual Obligations of TNG from the Ministry of Oil and Gas, July 15, 2010, C-650; Act on Unscheduled Inspection of KPM by the Geology Committee, July 16, 2010, C-651; Act on Unscheduled Inspection of TNG by the Geology Committee, July 16, 2010, C-315; Act on Results of Inspection of KPM, June-July, 2010 from Ministry of Industries and New Technologies, July 20, 2010, C-652; Act of Results of Inspection of TNG, June-July, 2010 from the Ministry of Industries and New Technologies, July 20, 2010, C-653.

[408] Reply on Jurisdiction and Liability ¶ 344 (*citing* Law on Private Business, July 17, 2009, with amendments as of April 2, 2010, cl. 38, C-510).

[409] Calancea Testimony, Tr. October 2012 Hearing, Day 3, 49:9-13.

[410] *See* Ongarbaev Witness Statement ¶ 2.8.

> [KPM and TNG] could not know about the breaches in the course of these inspections. There were technical personnel involved in the inspections, but we were not given the acts so that we could get aware [of what was found]. Therefore we cannot say that we knew about the breaches. And in our opinion there were no breaches at all.[411]

278. Kazakhstan's final act was assisted by the change in its Subsoil Use Law that was approved on June 24, 2010, days before the inspections were carried out. The new law permitted Kazakhstan to terminate contracts when a contractor failed to cure "two or more" contract violations.[412] The amendment also deleted the previous requirement that breaches of contract needed to be "substantial" before Kazakhstan could lawfully terminate a subsoil use contract. Kazakhstan's own expert on contract law, Professor Illyasova, explains that, even under the new law, allegations of contract violations needed to be made in "good faith." As explained in the following section, the allegations Kazakhstan raised were neither "substantial" nor in "good faith."

279. Professor Suleymenov, who drafted the previous version of Kazakhstan's Subsoil Use Law, describes the new provision on contract termination as a "corruption" provision.[413] That is because it gave Kazakhstan wide-ranging, domestic legal cover to create allegations of contract violations according to its whims. That is precisely what occurred here.

a. The alleged "violations" did not merit termination of the contracts

280. The alleged "violations" that Kazakhstan cited in mid-July 2010 were not a serious or well-founded basis on which to terminate the subsoil use contracts. Instead, they either related to minor issues that the companies had previously tried to resolve with Kazakhstan or were utter fabrications.

281. With respect to KPM, three of the seven alleged contract violations were claims that KPM failed to satisfy minor financial obligations to Kazakhstan. The purported obligations involved (i) historic costs that KPM typically paid on a quarterly basis, (ii) contributions to the Kazakh liquidation fund, and (iii) some unidentified outstanding taxes.

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411 Calancea Testimony, October 2012 Hearing, Day 3, 50:5-10.

412 As explained in the Reply on Jurisdiction and Liability, the new law on Subsoil Use did not actually apply to Claimants' Subsoil Use Contracts, because the amended law itself preserved the terms of pre-existing licenses and contracts. *See* Reply on Jurisdiction and Liability ¶ 351 (*citing* article 129(4) of the amended Law on Subsoil Use, C-508).

413 *See* Second Suleymenov Report ¶ 68 (referring to his interview, Exhibit 23 to Suleymenov Reports).

282. At the October 2012 Hearing, Kazakhstan completely misrepresented the nature of the first allegation listed above, claiming that KPM owed US $114 million to Kazakhstan in historic costs as of July 2010 that it could not afford to pay.[414] After Claimants corrected Kazakhstan that the actual number in dispute was US $114 thousand,[415] Claimants' General Counsel Mr. Pisica explained that the failure to pay that sum was not due to any financial hardship of the company, but instead to the fact that Kazakhstan had frozen KPM's assets and bank accounts.[416] Mr. Pisica also confirmed that KPM would have been in a position to pay the US $114,000 in historic costs if its bank accounts had not been frozen.[417]

283. The same reasoning applied to the second alleged contract violation, which was that KPM's allegedly failed to pay US $10,000 into the liquidation fund. KPM could not make that minor payment because Kazakhstan had frozen its bank account — not because KPM could not otherwise afford to do so. When responding to those claims of contract "violations," KPM noted two previous letters it had sent to Kazakhstan, in June 2009 and November 2009, explaining its situation *vis-à-vis* the payments owed in historic costs and to the liquidation fund and asking for advice.[418] Kazakhstan ignored both of those letters.

284. Kazakhstan's third claim that KPM failed to pay certain "taxes and other obligatory payments to the budget" is completely unsupported.[419] Kazakhstan did not even notify KPM how much in taxes or other payments it owed.[420] To be clear, that allegation could not have been a reference to the alleged US $62 million corporate back tax assessment, because in the previous month the Kazakh Court of Cassation had ruled that neither KPM nor TNG owed those taxes.[421] In response to the vague and unsubstantiated allegation of tax arrears, KPM disputed that any outstanding tax amounts actually existed and explained that,

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414 Tr. October 2012 Hearing, Day 2, 79:18-81:3.

415 The due diligence that Kazakhstan belatedly produced also confirms that figure. *See*, *e.g.*, Squire Sanders Legal Due Diligence Report, July 30, 2009, at 27, point 32, C-725; *see also* PwC Due Diligence Report, June 30, 2009, at 60, C-724.

416 Pisica Testimony, Tr. October 2012 Hearing, Day 2, 81:7-83:7.

417 Pisica Testimony, Tr. October 2012 Hearing, Day 2, 81:7-83:7.

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

419 Notice of infringement of obligations under the Borankol Subsoil Use Contract No. 305 from MOG to KPM, July 14, 2010, C-2.

420 Notice of infringement of obligations under the Borankol Subsoil Use Contract No. 305 from MOG to KPM, July 14, 2010, C-2.

421 *See* Section III.B.4, *supra*.

even if they were proven, KPM would be prevented from paying them because its bank accounts were frozen.[422]

285. The remaining allegations against KPM were similarly groundless. Kazakhstan's fourth allegation was that KPM failed to fulfill its obligation to train Kazakh specialists. KPM explained that it had satisfied its training requirement using less than the full amount of funds allocated for training, and it had asked Kazakhstan where the remaining funds should be sent.[423] Kazakhstan ignored that letter. Minister Mynbaev tried to address that alleged violation at the October 2012 Hearing, but he could offer no explanation for why it was a valid ground for terminating KPM's contract.[424]

286. The fifth groundless allegation was that KPM did not provide information regarding its compliance with its contractual work programs. As Claimants have noted previously, the allegation was not that KPM failed to meet its work program obligations, but merely that it did not provide information regarding its fulfillment of those obligations. That claim was false, as KPM explained in response to the allegation: KPM historically filed quarterly and annual reports on its work program compliance, and the MEMR itself had inspected KPM in January 2010 and concluded that KPM had exceeded its obligations.[425] Similarly, KPM explained that the (sixth) allegation that it breached obligations regarding the acquisition of goods, works, and services was false, and it appended notes to the July 2010 inspection report explaining why it was false.[426]

287. The seventh and final violation that allegedly merited the termination of KPM's contract was Kazakhstan's tired claim that KPM operated a main pipeline without a license.[427] Claimants have explained repeatedly why that claim was false and how it was used as a pretext in multiple contexts, including the final seizure.[428] In short, there was no substance or significance to any of the seven "grounds" for terminating KPM's contracts.

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

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

424 Mynbaev Testimony, October 2012 Hearing, Day 3 at 140:19-141:11.

425 Answer to the notification on infringement of obligations under Contract No. 305 to MOG from KPM, July 19, 2010, C-24; *see also* Reports of the MEMR for KPM, January 25 - February 6, 2010, C-385.

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

427 Notice of infringement of obligations under the Borankol Subsoil Use Contract No. 305 from MOG to KPM, July 14, 2010, C-2.

428 *See* Section III.B.1, *supra*.

288. The six allegations that TNG violated Contract No. 210 were equally meritless. Like KPM, TNG explained that information regarding fulfillment of its work programs had been sent to Kazakhstan on multiple previous occasions.[429] Kazakhstan also accused TNG of failing to provide annexes regarding the training of employees. TNG explained that those had been provided, along with its annual reports, and TNG provided them again in its July 19, 2010 response.[430] TNG also explained that, like KPM, it had written to the Ministry of Oil and Gas to determine where to send its excess funds for training Kazakh specialists, which the Ministry ignored.[431] In response to the claim that TNG owed some US $84,000 in historic costs, TNG explained and demonstrated that it properly paid its historic costs on a quarterly basis and that it had no arrears.[432] TNG also explained, just as KPM had done, that it did not operate a main pipeline and that it had not breached any obligations for the acquisition of goods, works, or services.[433]

289. Amazingly, Kazakhstan also issued a notice of alleged violations with respect to TNG's Contract No. 302. Kazakhstan claimed that TNG had violated Contract No. 302 on five grounds: (i) the same alleged failure to provide information regarding its work program; (ii) the same supposed failure to provide annexes regarding employee training; (iii) the same contention that TNG had not trained Kazakh specialists; (iv) the false criminal allegation that TNG operated a main pipeline without a license; and (v) the same vague obligation that TNG had breached its obligations regarding the acquisition of goods, works, and services.[434]

290. Unfortunately for Kazakhstan, that is the same contract that, in this arbitration, Kazakhstan claims was not extended — and actually expired — in March 2009. Because TNG obviously would not have had these obligations if Contract No. 302 had expired, it is clear that Kazakhstan considered that Contract No. 302 had, in fact, been extended. Not even Minister Mynbaev could explain why Kazakhstan claimed TNG breached Contract No. 302 in

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

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

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

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

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

434 Notice of infringement of obligations under Subsoil Use Contract No. 302 from MOG to TNG, July 14, 2010, C-7.

July 2010 when it had allegedly expired in March 2009. At the October 2012 Hearing, Minister Mynbaev testified as follows:

> Q. You would agree that for such a significant decision being made by a letter of July 14th 2010, your ministry would not be giving a notice of infringement for a contract that had in fact expired over a year earlier?
>
> A. I think one would need to look into the formal legal aspects, and I can't comment on this.[435]

291. Moreover, Contract No. 302 was an exploration contract.[436] TNG did not own or operate any transport pipelines — field or main — with respect to its Contract No. 302 operations. Thus, the termination of Contract No. 302 on the basis that TNG operated a main pipeline without a license underscores that the entire process was a farce. Minister Mynbaev could not explain that anomaly either:

> Q. … Do you know why my client is being given a ground for potential termination of its contract no. 302 for operating a trunk pipeline with respect to that contract?
>
> A. I don't know. In this case I don't know this.[437]

292. Beyond the unsupported nature of its allegations, Kazakhstan failed to permit Claimants a reasonable opportunity to cure or even explain the alleged violations before it terminated the contracts on July 21, 2010. As Claimants have explained, and as their witnesses testified, KPM and TNG received the notices of alleged contract infringements on July 16, 2010, and those notices required KPM and TNG to respond and cure each violation by July 19, 2010. Even if the allegations were valid — which they were not — it would not have been possible for KPM and TNG to cure them all in three days' time. Such a short period for redress was unfair, in bad faith, and also highlights the contrived nature of the exercise.

293. At the October 2012 Hearing, counsel for Kazakhstan attempted in vain to establish that Kazakhstan did not, in fact, grant KPM and TNG only three days to cure the alleged violations before terminating the contracts. However, the testimony of Mr. Pisica, Claimants' General Counsel, put the matter beyond doubt. He explained that

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435 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 126:15-20.

436 Contract No. 302, July 31, 1998, C-53.

437 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 127:5-10.

> during [the three day] period you have to submit explanations on reasons for failure to observe the contractual provisions ... and documents witnessing the rectification of these breaches.
>
> So my reply to your question is to be found in the phrase [in the notifications] "to submit all the necessary documents confirming that these violations have been cured." So within these days we were supposed to submit all the documents corroborating the elimination of the violations. ... If documents confirming such eliminations are requested, it means actually that we were requested first to eliminate the violations and then submit documents confirming this.[438]

294. In sum, Kazakhstan created bogus allegations, established an impossible time period for redress, and even though KPM and TNG thoroughly explained of why the allegations were wrong, Kazakhstan ignored those explanations and terminated the contracts anyway. The spurious grounds for termination of the subsoil use contracts and the manner in which the terminations occurred clearly violate the ECT and international law, not to mention the termination provisions in the contracts themselves.

b. Kazakhstan's *Post Hoc* Justifications for Termination and Seizure Are Equally Baseless

295. Given the dubious grounds Kazakhstan raised to justify its unlawful termination of Claimants' subsoil use contracts in July 2010, it is perhaps unsurprising that Kazakhstan has, in this arbitration, made new claims purporting to justify its unlawful termination of those contracts and seizure of KPM's and TNG's assets. None of Kazakhstan's retroactive justifications for its conduct could possibly shield Kazakhstan from liability under the ECT or international law, as there is no convincing evidence that they motivated Kazakhstan's conduct at the time. Nevertheless, Claimants will briefly respond to Kazakhstan's *post-hoc* justifications, because they are inaccurate.

296. At the October 2012 Hearing, Minister Mynbaev claimed that the specific "violations" that Kazakhstan raised in its July 14, 2010, notices were not the "key" reasons for terminating the contracts. Minister Mynbaev testified:

> But the key reason, once again, was something else. The fact is that it was impossible not to terminate this contract in July because there were no managers present at this field. Essentially there was already a social conflict at this field: the workers were already

[438] Pisica Testimony, October 2012 Hearing, Day 2 at 77:13-79:4. The notifications that Kazakhstan sent to KPM and TNG are Exhibits C-2, C-6, and C-7.

> gathering there and demanding payment of their wages and work.[439]

297. Other witnesses for Respondent have alluded to this completely unproven claim that contract termination and transfer of subsoil use rights were necessary to avoid "social tension" in the region. For example, Deputy General Prosecutor Kravchenko testified that "the situation [at KPM and TNG] was not that good, to put it mildly, and this social tension was increasing among the employees ... and it could not be excluded that such a social explosion could affect the entire region."[440] A vague concern that something "could" happen is hardly proof of a situation so dire that it required Kazakhstan to commit the illegal acts of unilaterally terminating the contracts and seizing the companies' assets.

298. Kazakhstan's attempted portrayal of social tension is flatly contradicted by two witnesses with direct personal knowledge of the activities of KPM and TNG in July 2010: Mr. Calancea, then-general manager of TNG, and Mr. Ongarbaev, Kazakhstan's witness from the Ministry of Oil and Gas who ordered the July 2010 inspections.

299. Mr. Calancea confirmed that

> [regarding Kazakhstan's reference] to social duties, social commitments, I don't understand what he means, because we paid the salaries, wages, and we observed all our commitments in the social sphere. We maintained the production. None of the workers left the field. Everyone was operating as normally as one could under these complicated conditions. ...[441]

He also explained that, after Kazakhstan seized KPM's bank accounts, Claimants "used TNG's funds in order to cover the operational expenses of KPM, in particular paying salaries to the employees of KPM."[442]

300. Indeed, there is no evidence showing that KPM and TNG did not pay salaries or that there was any risk of social unrest. Mr. Ongarbaev confirmed that there was no risk of the hundreds of local Kazakh residents who worked for KPM and TNG leaving their jobs. They stayed on their jobs and simply began working for the companies' new Kazakh managers upon the takeover:

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439 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 141:12-18.

440 Kravchenko Testimony, Tr. October 2012 Hearing, Day 4, 114:14-20.

441 Calancea Testimony, Tr. October 2012 Hearing, Day 3, 55:17-23 (emphasis added).

442 Calancea Testimony, Tr. October 2012 Hearing, Day 3, 68:2-4.

> Q. Are you aware that about 99% of the personnel on the fields were Kazakh, who had no intention to and in fact did not leave their jobs?
>
> A. I know that the personnel of the company still is working there.
>
> Q. Right. They simply resigned their work contracts with KazMunaiGas's subsidiary TenizMunaiGas, right?
>
> A. Yes, they concluded contracts with the trust manager, the company which is carrying out trust management.[443]

301. Kazakhstan has also suggested that the conditions of KPM's and TNG's oil and gas fields required State intervention.[444] That claim is also false. As previously noted, the MEMR itself concluded, in January 2010, that KPM and TNG had greatly exceeded their financial obligations to invest in the fields, as required under the work programs. Furthermore, the July 2010, geology and subsoil use inspection of KPM concluded that as of 2009, KPM's "active stock of output wells reached 66, compared with 65 planned. The active stock of intake wells reached 4, [the] number equal to projected wells."[445]

302. Kazakhstan's own geological experts, GCA, who visited the fields, confirm that any suggestion that KPM's and TNG's fields were deteriorating in July 2010 is false. The experts from GCA testified that the fields were in fine condition when they conducted a site visit as part of their preparation for the arbitration. GCA testified as follows:

> Q. On the field site inspection — and I guess this would be for you, Mr Wood — should we take it that what you saw were wells and other work sites in an acceptable, good oilfield practice standard?
>
> A. I didn't personally make the visit; one of my engineers did, an engineer who is very familiar with development projects in Russia, Kazakhstan, Azerbaijan. And yes, he reported that in general terms the quality of the facilities, the general housekeeping — which to us is always a good indicator — was perfectly adequate for the region.[446]

303. There is no basis for the assertion that seizure was necessary to prevent impending damage to the fields. As Claimants have demonstrated and their witnesses have

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443 Ongarbaev Testimony, Tr. October 2012 Hearing, Day 6, 70:20-71:3.

444 *See* Tr. October 2012 Hearing, Day 3, 133:18-24.

445 Act on Results of Unscheduled Inspection of Compliance with Subsoil Use Legislation by KPM, June 30 - July 7, 2010, C-689. Indeed, with respect to Borankol field, Kazakhstan's own experts, GCA, confirm that by the end of 2009, "production targets were achieved without the need to implement the full [2007-2022] drilling plan." Second GCA Report ¶ 65.

446 Tr. January 2013 Hearing, Day 4, 33:19-34:4. The "perfectly adequate" condition of the fields was not due to any work carried out after July 2010, because neither KMG nor KazMunaiTeniz has performed any field development work since taking over. *Id.* 33:25-34:3.

testified, despite Kazakhstan forcing their upper-management from the country, they did have personnel on the ground in July 2010, production of oil and gas did not stop, and the companies maintained the employment of local, Kazakh employees and always paid their wages.[447]

304. Indeed, even while being formally divested of their companies, in the midst of Kazakhstan's seizures, Claimants ensured that KPM's and TNG's production operations would not stop, and that their employees would not lose their jobs, precisely because either result would have been irresponsible and potentially harmful to the region. Mr. Calancea testified:

> Since we are an oil company operating under international regulations and rules, we are fully aware what might be the outcome of closure of production. Therefore we always took measures in order to secure a gradual transfer, if one might say so, of the production cycle to avoid grave consequences, environmental, technological or social.[448]

He continued that, during the takeover, KPM and TNG

> gave special directives, which can be confirmed by our technical staff, that we demanded them to keep the existing production schedule. So I don't see any problems here. This is normal international practice. …
>
> A normal oil company working in international projects will never allow a situation to arise where our actions would cause damage or loss of an oilfield, therefore we gave instructions to our technical personnel to keep working. And moreover, we wrote letters from our company in which we asked the personnel under these conditions to enter — subsequently to enter employment with the company which took over our fields.[449]

305. Try as it may, Kazakhstan cannot even muster a credible *post-hoc* rationalization for its illegal conduct. Even if a retroactive justification were legally relevant — which it is not — there was no significant social tension, no existing nor impending damage to the fields or operations, nor anything else that justified Kazakhstan's illegal seizures.

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[447] *See* Calancea Statement ¶ 2.

[448] Calancea Testimony, Tr. October 2012 Hearing, Day 3, 55:10-16.

[449] Calancea Testimony, Tr. October 2012 Hearing, Day 3, 55:23-57:7.

C. Kazakhstan's Senior Leaders Directed the Campaign Against KPM and TNG

306. The primary acts for which Kazakhstan should be held liable in this case have been detailed above and in Claimants' previous pleadings. They constitute severe, incontrovertible violations of Claimants' rights as well as breaches of the ECT and international law — not only in the aggregate, but individually as well.

307. To be clear, the ECT, international law, or treaty practice do not require Claimants to demonstrate that the egregious acts of mistreatment suffered by their investments were part of a coordinated "scheme" or plan. Rather, Claimants must simply show that State conduct violative of the ECT and international law harmed their investments — and that they have done in spades.

308. At the same time, this case is exceptional in that Claimants have established that Kazakhstan's mistreatment of their investments was a coordinated scheme for Kazakhstan to gain control of KPM's and TNG's assets, either at a firesale price or (as ultimately occurred) for free. The evidence discussed in the previous sections conclusively demonstrates that the Financial Police deliberately engineered the spurious criminal charge that resulted in the devastating fine against KPM; that the Government intentionally and baselessly clouded Claimants' title to TNG and defamed Claimants; that the Government agreed to extend Contract No. 302 and then unjustifiably reneged on that commitment; and that the Prime Minister, Deputy General Prosecutor of Kazakhstan, and Financial Police engineered the final, outright seizure of Claimants' investments on spurious grounds in July 2010.

309. Sadly, there is also considerable evidence that the very highest levels of Kazakh government and political elite — including President Nazarbayev and his son-in-law, Timur Kulibayev, who runs (and owns much of) the country's energy sector — personally directed the events of this case, or at least were fully aware of them and did nothing to prevent their occurence. As Claimants cannot accurately tell the true story of this dispute by ignoring that evidence, it is summarized in the following sections.

1. Claimants Have Produced Direct Evidence Of An Executive-Mandated Taking

310. Claimants have produced a number of communications from senior Kazakh officials evidencing motive to divest Claimants of their investments. A review of no more than five key documents shows that the Nazarbayev Administration (specifically, the

President himself, his Head of Administration, the Prime Minister, and the Financial Police) cooperated with the heads of important government ministries (including the MEMR, the Ministry of Finance, and the Ministry of Justice) to interfere with Claimants' investments and transfer control of KPM's and TNG's assets to the State. Claimants describe those documents below.

a. President Nazarbayev Personally Ordered the Thorough Investigation of Claimants' Companies

311. Kazakhstan does not contest the fact that President Nazarbayev ordered his Deputy Prime Minister and his Head of Financial Police to "thoroughly check" the work of KPM and TNG and to make a decision on their future "in the best interests of the country" on October 14, 2008.[450] As Claimants' expert Scott Horton explains, the meaning of such an order from the President himself, especially in an autocratic state such as Kazakhstan, is obvious: unleash all the forces of government, directed by the Financial Police, to raise (or to create) any and all problems for the foreign investor-owners.[451] The Kazakh Prime Minister, the Financial Police, and over a half-dozen Ministries and departments immediately carried out those instructions with zest and zeal, which almost dutifully resulted in harm to Claimants' ability to manage, control, and dispose of their investments.

312. President Nazarbayev was not, as Kazakhstan has suggested, merely following up on criminal allegations made by another head of State.[452] Indeed, none of the criminal allegations against Mr. Anatolie Stati were even investigated, and the agencies involved soon confirmed that there were no grounds on which to personally prosecute Mr. Stati.[453] Instead, President Nazarbayev used Moldovan President Voronin's letter as a pretext to launch the campaign. Kazakhstan's attempts to distance Nazarbayev personally from the instruction and the ensuing investigations were belied by the testimony of Kazakhstan's Minister of Oil and Gas, Mr. Mynbaev, at the October 2012 Hearing. His testimony confirmed that the 2008 inspections and investigations were the result of President Nazarbayev's order.[454]

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[450] President Nazarbayev's Investigation Instructions, October 14, 2008, C-8. *See also* Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 87:3-9.

[451] Horton Report at ¶¶ 174-175.

[452] Counsel for Kazakhstan claimed that Nazarbayev's order was "really the minimum that was required from him from a foreign policy perspective" and was merely a matter of "etiquette." Tirado Opening Statement, Tr. October 2012 Hearing, Day 1 at 143:7-13.

[453] *See* Order on Refusal to Initiate a Criminal Case Against A. Stati, May 18, 2009, C-431.

[454] Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 87:14-24.

313. Minister Mynbaev also agreed that "President Nazarbayev is very hands-on when it comes to the operations of foreign investors in the oil and gas sector."[455] He also concluded that the President of Kazakhstan does "not often" "direct the financial police to inspect energy companies."[456]

314. Similarly, Mr. Arman Rakhimov of the Financial Police testified that he had never before October 2008 received a direct instruction from the President to look into a potential criminal matter.[457] It is worth noting, however, that Mr. Rakhimov had received at least one previous criminal allegation against KPM from other sources, and that allegation turned out to be false.[458] It is telling that an instruction from the President led to a different result entirely.

315. Kazakhstan's own expert, Martha Brill Olcott, explains that "Kazakh political life at its highest circles includes a culture of trying to please the president and of seeking to anticipate his whims."[459] As demonstrated below, members of the highest political circles were involved in carrying out President Nazarbayev's wishes in relation to Claimants' investments.

b. National Kazakh Authorities Wanted to Acquire KPM and TNG, and Local Kazakh Authorities Suggested Early Termination Of Their Subsoil Use Contracts

316. Further evidence of the high-level interest in taking over KPM and TNG is an August 26, 2009, letter from the Akim of Mangystau region to the Prime Minister of Kazakhstan. The Akim wrote the Prime Minister because, as Minister Mynbaev testified, "matters of [the] oil and gas sector belong directly to the Prime Minister's authority."[460] Additionally, the August 2009 letter references instructions that the Prime Minister issued in June 2009 with respect to KPM and TNG. Notably, Kazakhstan has not produced those instructions in this proceeding, although they are clearly highly relevant to the State's motives with respect to Claimants' investments.

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455 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 99:15-19.

456 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 98:19-25.

457 Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 82:15-24.

458 Rakhimov Testimony, Tr. October 2012 Hearing, Day 5, 81:24-82:6 ("…I recall that in September the department of financial police of Mangystau investigated the case of illegal return of VAT to Kazpolmunay, and it would be more logical in the framework of that case to carry out some investigative activities. And we did study that case and we understood that it had no potential, the case that was initiated by Mangystau department.")

459 M. Olcott, *Kazakhstan: Unfulfilled Promise?* at 248 (Ex. 1 to First Olcott Report).

460 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 87:10-13.

317. Nevertheless, the August 2009 letter explains that the Prime Minister instructed the MEMR, the Ministry of Justice, the Ministry of Finance, and the national welfare fund Samruk-Kazyna to make a decision regarding the "State's buyout" of KPM and TNG.[461] That letter further indicates that Samruk-Kazyna, headed by Timur Kulibayev at the time, had expressed interest in acquiring KPM and TNG.[462] It states that while Samruk-Kazyna had "provisional estimates of the assets of Ascom Group," it had not yet been able to make an offer, because the MEMR had failed to comply with the Prime Minister's instructions to conduct an "institutional analysis" of the companies.[463]

318. The August 2009 letter to the Prime Minister also indicates that the MEMR (later reorganized into the Ministry of Oil and Gas) was not cooperating with the Prime Minister, the Ministry of Finance, the Ministry of Justice, and the Akim in making a decision regarding the buyout. As a result of the MEMR's failure to cooperate, the Akim of the Mangystau region asked the Prime Minister of Kazakhstan to direct the MEMR "to give instructions about speeding up the commencement of proceedings on termination of the Contract of Subsoil Use."[464]

319. As Minister Mynbaev testified at the October Hearing, the MEMR was actually defending KPM and TNG at the time, against the other Kazakh authorities involved, in an effort to protect them from a unilateral takeover.[465] That admission of Minister Mynbaev is telling. Why would the MEMR need to "defend" KPM and TNG if they were not the target of an impending government takeover? And why would the MEMR have been willing to defend the companies if they were not innocent of the baseless charges Kazakhstan had brought against them?

320. The MEMR, headed by Minister Mynbaev, had direct authority over KPM's and TNG's operations.[466] Thus, he and his Ministry had direct and in-depth knowledge of KPM's and TNG's operations: the licenses they held, the classification of their pipelines, their production forecasts, and their revenues and profits. The MEMR knew that Claimants had operated KPM and TNG in a fully compliant manner from 1999 to 2008 and that there were

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461 Letter from the Akim of Mangystau Oblast to the Prime Minister, August 26, 2009, C-293.

462 Letter from the Akim of Mangystau Oblast to the Prime Minister, August 26, 2009, C-293.

463 Letter from the Akim of Mangystau Oblast to the Prime Minister, August 26, 2009, C-293.

464 Letter from the Akim of Mangystau Oblast to the Prime Minister, August 26, 2009, C-293.

465 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 161:12-18 and 132:1-4 ("I did not want to terminate these contracts. I did not want to. It seemed that the investor must find a way to resolve his issues.").

466 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 86:10-14.

no grounds on which to pursue Claimants or bring about the ruin of their companies. Ultimately, the MEMR's defense of KPM and TNG was powerless against the other authorities within the executive branch, but its initial refusal to "join the bandwagon" is telling.

c. The MEMR Confirmed That A "Free of Charge Transfer of Assets" Would be Illegal and That There Were No Grounds For Early Termination of the Subsoil Use Contracts

321. Further evidence of discussions among high-level Kazakh officials regarding the acquisition of KPM's and TNG's assets is a letter from the MEMR of September 28, 2009, responding to an "order" of President Nazarbayev's Head of Administration, A. Musin. As with the Prime Minister's June 2009 instructions regarding acquisition of KPM and TNG, Kazakhstan has not produced the September 21, 2009, order from the Nazarbayev administration. Nevertheless, the MEMR's response to that order shows that the subject of the order was "acquisition of assets of [TNG] by KaspyAzot LLP" and it (at a minimum) contemplated "making offers on a free of charge transfer of assets of TNG."[467]

322. The MEMR's attempts in mid-2009 to "defend" the companies is confirmed in that letter. When asked about this letter at the October 2012 Hearing, Minister Mynbaev stated:

> Actually we, the ministry, tried to defend these two companies as long as it could, and this lasted until July 2010. We were actively defending them, and there were no free of charge transfer of assets.[468]

323. In response to the planned "free of charge transfer of assets" mentioned in the letter, the MEMR wrote that the companies' owners did not agree to such a transfer, and that a transfer of those assets without the owners' agreement would be "impossible" and contrary to Kazakhstan's Constitution.[469] The MEMR stated explicitly that "neither a competent body nor other interested state bodies have the right to unilaterally take a decision on a free of charge transfer of assets" of the companies.[470] The MEMR also noted that KPM and TNG had initiated negotiations with KMG NC and KMG E&P for the sale of TNG, and as a result,

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

468 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 161:12-18.

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

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

"a complex assessment of [the] companies' assets was initiated with a view to determine their fair market value."[471]

324. Despite those ongoing negotiations, and in response to the Mangystau Akim's earlier letter asking the Prime Minister to direct the MEMR to "speed[] up the commencement of proceedings on termination of [KPM's and TNG's subsoil use contracts],"[472] the MEMR also noted that its "analysis of the contracts has shown that there are no direct grounds for termination of contracts since there are no facts established by a court evidencing a failure to fulfill the contract and/or work program."[473]

325. The MEMR further noted that it could not

> unilaterally terminate the contracts and take a corresponding decision on alienation of the companies' assets in favor of the state, since it may lead to longstanding international court proceedings, initiated by the holders of the above mentioned bonds and have a negative impact on the image and investment attractiveness of the Republic of Kazakhstan.[474]

Thus, the MEMR clearly understood that Kazakhstan would face international liability for unilaterally terminating KPM's and TNG's contracts and transferring the companies' assets to the State. The fact that the MEMR actually had to write to other Kazakh authorities to explain that a transfer of the companies' assets without compensation and a unilateral termination of their subsoil use contracts would be illegal speaks volumes about the rule of law in Kazakhstan.

326. The MEMR's letter also confirms that, while senior government officials were contemplating a "free of charge transfer" of Claimants' assets and the "unilateral termination" of their Subsoil Use Contracts, they had also set up a working group to discuss KPM's and TNG's operations, no doubt to find another way to finish off the planned taking. The working group was comprised of members of (i) President Nazarbayev's Administration; (ii) the Akim of Mangystau region; (iii) the Financial Police; (iv) the Tax Committee of the Ministry of Finance; (v) the MEMR's Geology and Subsoil Use Committee; (vi) Samruk-Kazyna (controlled by Timur Kulibayev); (vii) KMG NC; and (viii) KMG E&P.[475] More direct

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

472 Letter from the Akim of Mangystau Oblast to the Prime Minister, August 26, 2009, C-293.

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

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

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

evidence of a concerted effort among the highest levels of the Kazakh government is difficult to imagine.

327. The MEMR ended its letter by confirming that it was planning, along with KMG NC, to negotiate directly with the owners of KPM and TNG, that is, Claimants, on the sale of their assets, and it suggested that KMG, Samruk-Kazyna, and the Mangystau Akim consider buying TNG. Of course, no such sale was finalized because Kazakhstan did not want to pay Claimants any significant value for their investments. At that point in time — September 2009 — the State-owned oil and gas company had valued KPM's and TNG's assets at no less than US $612 million, but it had offered Claimants only US $50 million in June 2009 for those assets (and it would drop that offer to US $20 million by November 2009).[476]

d. President Nazarbayev Issued a Second Personal Instruction Regarding KPM and TNG in 2009

328. In November 2009, a little over one year after President Nazarbayev first instructed his officials to "thoroughly investigate" KPM and TNG, the Kazakh President issued another "personal instruction."[477] That instruction was directed to Prime Minister Masimov, Minister Mynbaev, and Timur Kulibayev, and it requested "suggestions about the prospects" of KPM and TNG.[478]

329. The President complained that "as a result of inspections by law enforcement … it took place a full stop of trades (oil and gas extraction) and the construction of the [LPG Plant], compressor stations and gas gathering units" and that "nearly 3 thousand people are fired."[479] That is direct evidence of the harm caused to KPM and TNG as a result of the October 14, 2008, order to "thoroughly check" the companies' activities.

330. The three thousand people who were "fired" were the contract workers who had been employed to construct TNG's LPG plant (not KPM's and TNG's nearly 1,000 other employees, who remained to the end and were re-hired by the State's managers).[480] As Mr. Stati testified, construction of the LPG Plant was stopped in the spring of 2009 because he did

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476 RBS 2009 Asset Valuation, July 31, 2009, slides 36-7, C-723. *See* First Stati Statement ¶¶ 37-38; First Lungu Statement ¶¶ 61-62.

477 Attachment to C-23 ("Personal Instruction" from President Nazarbayev of Nov. 23, 2009).

478 Attachment to C-23 ("Personal Instruction" from President Nazarbayev of Nov. 23, 2009).

479 Attachment to C-23 ("Personal Instruction" from President Nazarbayev of Nov. 23, 2009).

480 *See* Attachment to C-23 ("Personal Instruction" from President Nazarbayev of Nov. 23, 2009); Stati Testimony, Tr. October 2012 Hearing, Day 2, 43:23-24.

not want to complete a new lucrative investment in the country when Kazakhstan had already interfered with Mr. Stati's efforts to sell or manage his companies and it was clear that Kazakhstan was primed to take them over.[481]

331. Clearly aware that his previous instructions led to the disruption of KPM's and TNG's operations — and therefore were not "continued operations in the best interests of the country"[482] — the President asked his Head of Administration, A Musin, to "control" the situation.[483]

332. That instruction, issued in November 2009, is further evidence of the ongoing involvement of the highest levels of government in the demise of Claimants' investments in Kazakhstan. Minister Mynbaev confirmed that the inclusion of Mr. Timur Kulibayev on this instruction signifies that the State-owned national oil company was still looking into acquiring KPM and TNG one way or another.[484]

333. Minister Mynbaev also testified on cross-examination that

> the fact that the head of state gives an instruction here to look into these issues and resolve it, this was the starting point for our work. ... even after this instruction, the actual termination of the contract happened only eight months afterwards. So throughout this period attempts were being made to find a solution.[485]

334. Thus, whereas before this instruction, the MEMR tried to "defend" the companies from the executive's and other agencies' takeover campaign, the November 2009 instruction was the "starting point" for the MEMR's "work" to unilaterally terminate KPM's and TNG's contracts. From Minister Mynbaev's perspective, President Nazarbayev's November 2009 instruction clearly marked the turning point in the MEMR's position toward KPM and TNG.

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481 Second Stati Statement ¶ 40.

482 President Nazarbayev's investigation instructions, October 14, 2008, C-8.

483 Attachment to C-23 ("Personal Instruction" from President Nazarbayev of Nov. 23, 2009).

484 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 173:25-174:5 ("Q. ... as of the date of this instruction, the national oil company was looking into the potential for acquiring, one way or another, the assets of TNG and KPM; correct? A. If these issues were not resolved, then the national company, or any other potential investors, would be able to look into the possible acquisition.").

485 Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 173:8-14.

e. The Blagovest Letter Indicates That the Takeover Was Planned As Early As 2008

335. On February 7, 2010, the President of the Kazakh social fund "Blagovest" wrote to Minister Mynbaev to make a suggestion to "resolve the question of nationalization of the assets posed in 2008."[486] His proposal included "establishing control over TNG and KPM" while avoiding "petition to international arbitration."[487] The "main idea" behind the proposal was to "separate interests of the companies (contract execution, jobs, salaries, interests of Kazakhstan) and interests of their owner."[488]

336. Kazakhstan does not deny the substance of that letter, which was authored by President Nazarbayev's appointee to head Kazakhstan's Assembly of Tribal Nations, Mr. Yuri Zakharov. However, Kazakhstan has deliberately obscured a complete explanation of the letter. It first introduced a witness statement from Mr. Zakharov himself, who explained that both he and KPM's former general director, Mr. Andreyev, prepared and sent the letter. He said: "Andreyev proposed a prepared text of the letter addressed to the Ministry, which we sent. Andreyev also noted that in case of resolution of the issue, the trust may count on the financing of social projects."[489] Thus, Mr. Zakharov admitted that he aided Mr. Andreyev in communicating with the MEMR and proposing a method for nationalization of KPM and TNG.

337. Further, Mr. Zakharov admitted that both he and Mr. Andreyev met with the MEMR. He said in his witness statement that "[a]bout a month after sending the letter, ... by order of the Minister of Energy Mynbayev, I met with the Executive Secretary of the Ministry Safinov."[490] That statement is somewhat inconsistent with the testimony of Minister Mynbaev, who suggested that he "didn't have any particular desire to speak seriously to these people" and that he did not see the letter until Mr. Zakharov and Mr. Andreyev came to visit him of their own accord.[491]

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[486] Letter from Blagovest President to MEMR, February 17, 2010 (emphasis added), C-23.

[487] Letter from Blagovest President to MEMR, February 17, 2010, C-23.

[488] Letter from Blagovest President to MEMR, February 17, 2010, C-23.

[489] First Witness Statement of Yuri Zakharov at Question 7, R-178.

[490] First Witness Statement of Yuri Zakharov at Question 13, R-178 (emphasis added).

[491] Mynbaev Testimony, Tr. October 2012 Hearing, Day 3, 167:17-169:25 (Mynbaev further testified that after he "read the first page of this letter, [he] didn't even continue, … didn't finish its reading, [but] just bid them goodbye." That, too, is inconsistent with Mr. Zakharov's testimony that Mynbaev "ordered" him to attend a meeting regarding the letter.).

338. Claimants intended to ask Mr. Zakharov to explain to the Tribunal, under oath, the circumstances giving rise to his letter and the "question of nationalization" of KPM and TNG "posed in 2008."[492] Tellingly, Kazakhstan refused to present Mr. Zakharov for questioning at the October 2012 Hearing, despite his being expressly called by Claimants for cross-examination. Kazakhstan obviously did not want the Tribunal to learn the truth from Mr. Zakharov and did not want to risk potential inconsistencies between Mr. Zakharov's and Minister Mynbaev's testimonies.

* * *

339. In summary, the Tribunal has the following evidence of the direct involvement of Kazakhstan's political elite in the mistreatment and seizure of Claimants' investments, which strongly suggests a coordinated scheme emanating from the highest levels of Government:

- President Nazarbayev's October 14, 2008, order to thoroughly investigate KPM and TNG;
- Letter from the Akim of Mangystau to the Prime Minister, dated August 26, 2009, referencing the Prime Minister's June 2009 instructions to the MEMR, Ministry of Justice, Ministry of Finance, and Samruk-Kazyna to make a decision regarding the "State's buyout" of KPM and TNG;
- September 2009 Letter from MEMR referencing the proposed "free of charge transfer of assets" of KPM and TNG and the "unilateral termination" of their subsoil use contracts;
- President Nazarbayev's "personal instruction" of November 2009 to the Prime Minister, Minister Mynbaev, Timur Kulibayev, and others, to resolve the issues of KPM and TNG; and
- Finally, the letter from the President of Blagovest, referencing Kazakhstan's specific "plan of nationalization posed in 2008."

Again, while there is no requirement that Claimants demonstrate the existence of such a scheme, Claimants respectfully submit that the evidence speaks for itself.

340. Importantly, although Kazakhstan was surprised (and obviously dismayed) to learn that Claimants were aware of those documents, Kazakhstan does not contest their validity, nor does it dispute that the various letters and instructions were received and carried out. Instead, Kazakhstan attempts to dismiss the documentary evidence by suggesting (without proof) that Claimants either received the documents illegally or have misrepresented

[492] Letter from Blagovest President to MEMR, February 17, 2010, C-23.

them.[493] Kazakhstan has not presented a scintilla of evidence supporting its allegation that the documents were obtained illegally, which they were not. As to the accuracy of Claimants' descriptions of their contents, Claimants invite the Tribunal to review the documents on its own.

341. Furthermore, with the exception of Minister Mynbaev, whose testimony on certain aspects of this evidence is contradicted by a witness Kazakhstan refused to present, Kazakhstan chose not to present the authors or recipients of the communications to testify before the Tribunal. Consequently, the Tribunal can only conclude that the documents speak for themselves.

IV. KAZAKHSTAN CAUSED HARM TO CLAIMANTS' INVESTMENTS

342. Kazakhstan asserts that its actions, even if they violated international law, caused no injury to Claimants. Rather, according to Kazakhstan, all of Claimants' injuries — beginning with the 2008 campaign and including the final seizure of KPM's and TNG's assets in July 2010 — resulted from some combination of Claimants' mismanagement of the companies and geological and market factors that had nothing to do with Kazakhstan. Kazakhstan goes so far as to suggest that Claimants abandoned KPM and TNG when they saw that the companies were doomed to fail, and concocted the claims in this arbitration to salvage some value from the investments. Kazakhstan's contentions are simply false; they are belied by the evidence in the record (some of which Kazakhstan withheld from production notwithstanding this Tribunal's orders until the eleventh hour) and common sense.

343. The evidence demonstrates that KPM and TNG were well-financed, well-managed, and successful businesses from the time Claimants acquired them right up until the Kazakh government, at its highest levels, trained its sights on the companies in October 2008. The companies were extremely profitable through the third quarter of 2008. Claimants received numerous, substantial indicative offers to purchase them in September 2008. Then, beginning almost immediately after President Nazarbayev issued his instruction on October 14, 2008, the companies' fortunes changed drastically, in ways that are directly attributable to Kazakhstan.

344. Of course, the global financial crisis and decline in world oil prices that began in the summer of 2008 posed challenges for KPM and TNG, as they did for many oil and gas producers. Kazakhstan, however, distorts and exaggerates the difficulties posed by those

[493] *See* Section II.C, *supra*.

events in order to deflect its own responsibility for KPM's and TNG's problems. The fact is that KPM and TNG would have readily endured the temporary downtown in oil prices in 2008-2009 but for Kazakhstan's actions, and in fact did continue basic operations right up until Kazakhstan's final seizure of the companies' assets in July 2010.

345. The simple fact is that Kazakhstan's harassment campaign caused substantial injury to Claimants' investments almost immediately after President Nazarbayev issued his order. That injury included: (1) injury to Claimants' reputation and access to credit; (2) interference with TNG's completion of the LPG Plant; (3) interference with normal development in Borankol and Tolkyn; (4) interference with exploration of the Contract 302 area; (5) a substantial deleterious effect on the revenues of KPM and TNG; (6) interference with Claimants' ability to sell their investments; and (7) the commencement of a malicious criminal investigation that ultimately resulted in the total loss of all assets.

A. Kazakhstan's Actions Caused Substantial Injury Almost Immediately After President Nazarbayev's Order

1. Injury to Reputation and Credit

346. Very shortly after President Nazarbayev issued his order on October 14, 2008, Kazakhstan's actions began to injure Claimants' reputation and access to credit. Claimants believe that the Nazarbayev order (and subsequent criminal investigation, which officially commenced on December 15, 2008) was broadly known in the Kazakh oil and gas industry shortly after it was issued, but they obviously cannot say exactly how quickly and how broadly word of President Nazarbayev's order spread.

347. No later than December 18, 2008, however, Kazakhstan's actions had a direct and profound impact on Claimants' reputation. As has been well-documented, on that day, the INTERFAX news agency published an article that publicly announced the MEMR's decision to revoke its approval of Claimant Terra Raf's acquisition of TNG.[494] Moreover, the article extensively quoted the MEMR's accusations that Claimants had forged documents in order to defraud the State of its pre-emptive right to purchase TNG, that Claimants' ownership of TNG was illegal, and that "violations" regarding TNG's organization and registration "infringe upon the interests of the country."[495] Those allegations were patently false, and Kazakhstan has never offered a shred of proof to substantiate them.

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[494] INTERFAX News Article, December 18, 2008, C-625.

[495] INTERFAX News Article, December 18, 2008, C-625.

348. Amazingly, Kazakhstan's only response on this issue is that the news article was not an "official press release of the MEMR."[496] Kazakhstan would have the Tribunal check its common sense at the door. The article quotes extensively from a source within the MEMR, and Kazakhstan does not deny that. Moreover, Kazakhstan has presented no explanation of how or why that leak to the financial press could have occurred other than as part of a concerted effort to impugn Claimants' integrity and cloud their title to TNG. Regardless of what Kazakhstan considers "official," or why that is even relevant,[497] the Tribunal should see that article for what it is and the harmful impact it had.

349. That article, combined with Kazakhstan's other harassing behavior, indisputably had a serious negative impact on Claimants' credit and reputation. On January 14, 2009, the Fitch ratings agency placed Tristan's long term default rating and senior unsecured rating of 'B+' on Rating Watch Negative, citing the issues raised in the December 18, 2008, INTERFAX article and Kazakhstan's criminal investigation of KPM.[498] The language of the Fitch announcement is worth revisiting, because it establishes an indisputable link between the State's improper conduct and the injury to Claimants' reputation and access to credit:

> The RWN reflects Fitch's concern of a potential negative impact relating to the latest actions of the Kazakh authorities on Tristan's financial standing and business prospects. The Ministry of Energy and Mineral Resources of Kazakhstan (MEMR) cancelled a previously issued waiver of the state's pre-emptive rights in respect to one of the two operating companies of Tristan — Tolkynneftegaz LLP (TNG) (accounting for about 69% of the group's 9M08 revenue and 77% of operating profit) — which may result in a revocation of TNG's subsoil use contract. Furthermore, the other operating company of the group — Kazpolmunay LLP (KPM) — is subject to a criminal investigation.

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496 Rejoinder on Jurisdiction and Liability ¶ 171.

497 Bizarrely, Kazakhstan cites for its argument that the press release is not attributable to the State Article 7 ILC Draft Articles on State Responsibility, which reads: "The conduct of an organ of a State or of a person or entity empowered to exercise elements of the governmental authority shall be considered an act of the State under international law if the organ, person or entity acts in that capacity, even if its exceeds its authority or contravenes instructions." *See* Rejoinder on Jurisdiction and Liability ¶ 750. That provision supports the exact opposite of Kazakhstan's position. Given the level of detail in the information that the INTERFAX article sources to the MEMR, there can be no doubt that the source had some capacity with the MEMR, likely at a high level. Thus, even if that MEMR official exceeded his authority in leaking that information to the financial press, that leak nonetheless is attributable to Kazakhstan under the very authority that Kazakhstan cites.

498 *See Fitch Places Tristan Oil Ltd. on Rating Watch Negative*, DOW JONES INTERNATIONAL NEWS, January 14, 2009, C-590.

> Fitch believes that a negative resolution of either of the authorities' actions will have a significant negative impact on Tristan's operational and financial profile, and is thus likely to result in a multi-notch rating downgrade. Although TNG is the larger of the two operating companies, Fitch believes that the group does not have sufficient financial cushion to service its debt (two Eurobond issues totaling USD420m due in 2012) and cover capex needs in case of a detachment of either of the companies.[499]

350. Moreover, the INTERFAX article on December 18, 2009, directly interfered with a specific financing transaction that Claimants were negotiating at the time with Credit Suisse. On December 5, 2008, Credit Suisse sent Claimants a term sheet for a US $150-175 million bridge loan facility. Claimants and Credit Suisse already had negotiated terms for the loan, and by December 5, Credit Suisse indicated that it was nearly ready to execute the term sheet.[500] On December 18, 2008, however, Mr. Antanas Petrosius of Credit Suisse sent Mr. Lungu the INTERFAX article accusing Terra Raf of forgery and fraud, and stated that he "[w]ould appreciate some colour on the [State's accusations]."[501] In follow-up discussions, Credit Suisse said it would not provide the bridge loan until Claimants resolved their disputes with the Kazakhstan government.[502]

351. Kazakhstan's only response to that fact — apart from its incorrect arguments that the MEMR's position on the pre-emptive rights issue was legal and that the INTERFAX article is not attributable to the Republic — is a baseless challenge to Mr. Lungu's credibility.[503] Kazakhstan expresses incredulity that there is no document from Credit Suisse backing out of the loan because "negotiations were to a large extent held via email."[504] The email exchange between Messrs. Petrosius and Lungu, however, expressly indicated that they were attempting to reach each other by phone, with Mr. Petrosius writing at the end, "Tried returning your call. Please call me on +447786660459 when you free up."[505] It thus is hardly surprising that the subsequent conversation occurred by telephone rather than email.

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499 *See Fitch Places Tristan Oil Ltd. on Rating Watch Negative*, DOW JONES INTERNATIONAL NEWS, January 14, 2009, C-590.

500 Second Lungu Statement ¶ 7; Indicative Term Sheet from Credit Suisse, December 5, 2008, C-521.

501 Second Lungu Statement ¶ 7; Email from Antanas Petrosius to Artur Lungu, December 18, 2008, C-625.

502 Second Lungu Statement ¶ 7.

503 Kazakhstan also argues that "Claimants could have at least provided witness testimony from Credit Suisse." Rejoinder on Jurisdiction and Liability ¶ 749. Unfortunately, unlike for Kazakhstan, Claimants' ability to "encourage" third-party witnesses to travel long distances to give testimony in a dispute in which they have no stake is quite limited.

504 Rejoinder on Jurisdiction and Liability ¶ 749.

505 Email from Antanas Petrosius to Artur Lungu, December 18, 2008, C-625.

352. Moreover, Kazakhstan had every opportunity to cross-examine Mr. Lungu about this conversation, but did not ask him a single question about it. While it is certainly Kazakhstan's prerogative to hurl stones at a witness's credibility from a safe distance, the strength of its accusations should be judged accordingly. Given that Mr. Lungu's statement is corroborated by his email exchange with Mr. Petrosius, and that Fitch cited the INTERFAX article in its ratings watch notice, the Tribunal is well-justified in concluding that Credit Suisse backed out of the bridge financing because of the MEMR's accusations in the INTERFAX article.

353. Claimants' inability to obtain that financing had serious consequences. For example, as Mr. Lungu testified, Claimants would not have needed to enter into the Laren transaction in June 2009 if they had obtained the Credit Suisse financing. The Laren facility required Tristan to issue an additional US $111 million in notes, on top of a US $60 million promissory note, in order to raise US $60 million in financing needed to pay tax and interest obligations.[506] It was truly "desperation financing," intended to keep the companies afloat until they could be sold or the temporary liquidity crunch eased. That strategy worked, but at substantial cost — most importantly, the issuance of US $111 million in additional Tristan debt that would not exist today but for Kazakhstan's actions.

354. In the KMG valuation documents that Kazakhstan belatedly produced on March 14, 2013, RBS and PwC express some confusion regarding the terms of the Laren transaction, suggesting that Laren is an affiliate of Mr. Stati and still holds the US $111 million in notes issued in connection with that transaction.[507] Lest there be any confusion here, that is not correct. Laren was a special-purpose entity that was organized in the British Virgin Islands to facilitate the emergency financing transaction. Laren borrowed US $60 million from a group of third-party hedge funds (the "Laren Lenders").[508] Laren loaned US $25.5 million of those proceeds to Montvale, which Montvale in turn paid to KPM and TNG in satisfaction of outstanding trade payables. KPM and TNG used those funds to pay excess profit taxes.

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506 Second Lungu Statement ¶ 10.

507 *See* RBS 2009 Asset Valuation, July 31, 2009, slide 40, C-723 (assuming that Claimants would receive the value of any acquisition of the US $111 million in new notes because Laren is a related party); PwC Due Diligence Report, June 30, 2009, at 21, C-724.

508 Laren Facility Agreement, June 11, 2009, at 96, C-733. The Laren Lenders included Avelade Holdings Ltd., GLG Atlas Macro Fund, Renaissance Securities (Cyprus) Ltd., Sputnik Group Ltd., Vision Advisors III Ltd., and GLG Atlas Value & Recovery Fund.

355. Laren used the other US $30 million in proceeds to purchase US $111 million (face value) in new notes from Tristan, and Tristan in turn used those funds to make the June 2009 coupon payment on the Tristan notes. Under the Laren Facility Agreement and related Note Transfer Agreement, however, Laren transferred the new notes to the Laren Lenders for no additional consideration.[509] The deal was structured that way to give the Laren Lenders some security rights that were on an equal level with the Tristan noteholders, because the guarantees that KPM and TNG gave for the Laren debt were subordinate to the Tristan note guarantees. Under the agreement transferring the notes, Laren had the ability to reacquire a large portion of the notes from the Laren Lenders if it repaid the Loan Facility within a very short time (4-6 weeks).[510] When Claimants were unable to make that repayment, the Laren Lenders — who are not affiliated in any way with Mr. Stati — kept the new notes.

356. In short, the terms of the Laren transaction were extremely onerous, requiring a US $60 million promissory note (at 35% interest) plus US $111 million in new notes in exchange for US $60 million in emergency financing, and a personal guarantee from Mr. Stati. While Kazakhstan is not responsible for all of the market conditions that led Claimants to need additional financing in June 2009, it is directly responsible for Claimants needing to obtain that financing from the equivalent of loan sharks rather than on reasonable commercial terms from Credit Suisse.

357. The initial negative ratings watch notice from Fitch in January 2009 was followed by a series of negative notices and downgrades by Fitch and Moody's, the other ratings agency that followed Tristan Oil, in 2009 and 2010.[511] The MEMR's threat to cancel Claimants' ownership of TNG based on the bogus preemptive right argument and the government's criminal investigation of KPM and TNG featured prominently in all of those downgrades. Additionally, the ratings agencies issued downgrades based on the new debt associated with the Laren transaction that Claimants were forced to enter into as a result of Kazakhstan's actions, and of course on Kazakhstan's termination of the Subsoil Use Contracts in July 2010. Stronger evidence of the effect of Kazakhstan's illegal conduct on the market reputation of Claimants' businesses is difficult to imagine.

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[509] Laren Facility Agreement, June 11, 2009, at 21, C-733; Note Transfer Agreement, § 2, C-734.

[510] Note Transfer Agreement, § 6.2, C-734.

[511] *See* Fitch Ratings Actions, C-743; Moody's Ratings Actions, C-744.

2. Interference With Construction of the LPG Plant

358. In November-December 2008, shortly after President Nazarbayev issued his investigation order, construction on the LPG Plant slowed significantly because the non-Kazakh workers on the project were unable to renew their work permits. Mr. Broscaru explained:

> Construction proceeded smoothly until around November/ December of 2008. Many of the workers employed in the project were non-Kazakhs having the necessary work permits. Around that time, I began receiving reports from project managers that the non-Kazakh workers were refused to obtain renewals of their work permits by the Kazakhstan authorities. That had never been a problem in the past. When I asked why this was occurring, I was told about the letter from the Moldovan President Voronin and President Nazarbayev's subsequent order to start the investigations. According to the Kazakh engineers who were trying to work with government authorities to renew the non-Kazakhs' work permits, the government would not renew those permits until the investigation ordered by President Nazarbayev was completed.
>
> Consequently, the works on the LPG Plant slowed significantly in the winter of 2008-2009. Some work continued using Kazakh personnel, but most of the work halted due to the absence of the non-Kazakh workers.[512]

That testimony is unrebutted.

359. Moreover, in the spring of 2009, construction on the LPG Plant paused indefinitely. Although Mr. Stati made that decision, Kazakhstan's illegal actions forced him to do so, in two ways.

360. First, TNG's liquidity position was deteriorating. While Kazakhstan was not responsible for all of that, it was responsible for a significant part (as discussed further below). Moreover, regardless of the reasons for TNG's weak cash position in the early summer of 2009, Kazakhstan caused Claimants to lose the Credit Suisse facility that would have provided additional working capital at that critical time.

361. Second, as Mr. Stati has explained, Kazakhstan's actions had changed the investment environment to the point where it was simply too risky to invest additional (increasingly scarce) capital on construction of the LPG Plant:

> Kazakhstan's actions had created an extremely risky business environment. There was the persistent threat of additional arrests,

[512] Broscaru Statement ¶¶ 25-26.

> asset seizures, fines, audits, and investigations, and the potential for Kazakhstan's outright seizure of all of my assets was increasingly real. Faced with this climate of fear and uncertainty, I chose in May of 2009 to postpone the LPG Plant project, having already spent more than USD 245 million toward its construction. I knew that Kazakhstan viewed the LPG Plant as a strategic asset, and I knew that it was a highly likely target for sequestration or even seizure. I therefore saw little business reason to add the additional capital and (by then increasingly scarce) manpower necessary to complete the project if I was only going to see it or its liquids production simply taken by Kazakhstan.[513]

Mr. Stati's decision to pause construction of the LPG Plant until the situation with the government improved or the assets were sold to a new owner was a prudent response to Kazakhstan's actions, which by that time included the public disparagement of TNG as well the malicious criminal investigation of KPM and TNG and the spurious charge of operating a "main" pipeline without a license.

362. That decision, however, had significant negative consequences. TNG had invested a substantial amount of capital in the LPG Plant, which subsequently sat idle. But for Kazakhstan's actions, the LPG Plant would have gone online in June of 2009,[514] providing a valuable uplift on the revenue earned from the Tolkyn gas at a critical time.

363. Moreover, the delay in construction of the LPG Plant increased the ultimate cost of completing the plant. As GCA acknowledges, completing the plant after a substantial delay would entail "costs for surveys, re-engagement of the contractor and equipment refurbishment or replacement" that would not have been necessary absent the delay.[515] In fact, GCA quantified the cost attributable to the delay at US $50 million.[516] Kazakhstan's actions caused that delay, and as discussed further in Section V, this is one of the many reasons that Kazakhstan's valuation date is incorrect.

364. Additionally, the conditions that caused Mr. Stati to pause his investment in the LPG Plant also caused Vitol to retract a substantial part of its debt financing for the project. As Mr. Lungu explained, Vitol had agreed to pay half the construction cost through

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513 Second Stati Statement ¶ 40.

514 Broscaru Statement ¶ 28.

515 First GCA Report ¶ 63.

516 Tr. January 2013 Hearing, Day 4, 15:1-12.

prepayments for oil that worked like a revolving line of credit.[517] Beginning in June of 2009, however, Vitol began to draw down that line of credit:

> Q. So did Vitol begin to draw down its prepayments?
>
> A. Yes, basically the way it worked, we continued to produce, we continued to deliver, because Vitol had an exclusive right to all the so-called TNG and KPM export entitlements, so we had to go through Vitol to sell it, but we did not get money from Vitol.
>
> Q. Okay. What effect did that have on the company's working capital position?
>
> A. Direct negative effect, because you don't get money. [518]

As a result, Vitol — which was obligated to fund half the cost of constructing the LPG Plant — ultimately drew down the amount of its total financing for the project to US $66 million.[519] As Mr. Stati explained, Vitol justified its reduction in investment in the LPG Plant based on the risky environment created by Kazakhstan:

> The same thing with a firm called Vitol, who did not pay for the condensate and oil delivered to Vitol, although our contract forced us to only deliver to Vitol alone. And they justified nonpayment for the resources supplied by them returning the investment that they had made into LPG, because they considered that the risk was so high. So they found this way instead to return their investments.[520]

3. Interference With Development of Tolkyn and Borankol

365. As with the LPG Plant, the hostile investment environment created by Kazakhstan also forced Mr. Stati to reduce development efforts in the Tolkyn and Borankol fields. That included the decision not to drill (or recomplete) thirteen wells at Borankol and Tolkyn in 2009-2010.[521] As Mr. Stati explained his decision:

> Ascom's engineers told me that these wells would have provided substantially enhanced production, and I discussed at length with my engineers and finance staff the costs and benefits of drilling these wells. I decided that to proceed with them did not make business sense because they, or their enhanced production, were likely to become just additional assets for Kazakhstan to attach,

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[517] Tr. January 2013 Hearing, Day 1, 183:25-184:18.

[518] Tr. January 2013 Hearing, Day 1, 185:13-185:21.

[519] Tr. January 2013 Hearing, Day 1, 248:13-248:20.

[520] Tr. October 2012 Hearing, Day 2, 43:1-43:8.

[521] Second Stati Statement ¶ 44.

> levy against, or seize. In hindsight, my decision to forego the capital expenses for the LPG Plant and additional drilling turned out to be perfectly correct, since Kazakhstan ultimately seized all of my assets.[522]

366. The reduced development of Tolkyn and Borankol injured Claimants in at least three ways. First, KPM and TNG lost the revenue they would have earned from their planned production during 2009 and 2010. Kazakhstan and Deloitte have made much of the fact that Claimants' valuation date supposedly allowed Claimants to benefit from production in that period. In addition to the reasons why that view is wrong as a matter of standard valuation principles (discussed in Section V), it also is wrong as a matter of fact because Kazakhstan's illegal actions caused Claimants not to produce as much in that time period as they would have produced otherwise.

367. Second, that gap in development efforts artificially depressed the production "curve" at Tolkyn and Borankol. As discussed further below in Section V.B.2, that is another of the many reasons why Kazakhstan's valuation date and approach to valuation are wrong. The production at July 2010 that forms the basis for GCA's decline curve analysis is significantly lower than it would have been if Claimants had been able to develop the fields without interference by Kazakhstan. As Mr. Latham of Ryder Scott testified:

> I think I'd have to use Borankol field as a classic example of where the quandary is here. In the Borankol field, let's say, for example, if we elected to say: okay, take the reserves that were estimated as of 07/21/2010, just add back to that the production that occurred in the meantime to, you know, adjust it to an effective date of 10/14/2008 — or, by contrast, do it the other way around — frankly, it's not very effective because prior to the effective date of 10/14/2008, before the alleged interference of the respondent, it's fairly noticeable that a lot of things occurred in the fields that were not a continuation, a normal continuation of operations. For example, at Borankol the production rates dropped off just incredibly quickly.
>
> THE CHAIRMAN: You mean after October 14th?
>
> A. (By MR LATHAM) Yes. It's hard to quantify the amount, but it was readily apparent that wells are not being worked over.[523]

[522] Second Stati Statement ¶ 45.

[523] Tr. January 2013 Hearing, Day 4, 35:2-20.

368. Third, Claimants were unable to respond promptly to the watering issues at the Tolkyn field. As James Latham of Ryder Scott testified, one of the corrective actions to remedy excess water would have been to drill additional wells:

> [I]f there were going to be continuing water problems in the future, we would probably be well advised (a) to moderate the rates, which has already been done, and (b) to ensure that we have as many — I want to use the word straws in the ground, so that we can still manage to recover gas from the reservoir without creating tremendous localized drawdown. In other words, rather than try to produce a few wells at very high rates, try to produce as many as possible at more moderate rates, and I think with the implementation of the plan that we have suggested, I think it will help in the process of mitigating the effects of the water.[524]

To be clear, the production of water at Tolkyn was a natural phenomenon. It was not, as Kazakhstan contends, a result of any imprudent operations or mismanagement of the Tolkyn field. Far from blaming Claimants for that phenomenon, Kazakhstan bears responsibility for preventing Claimants from implementing normal field management practices to address it in 2009 and 2010.

4. Interference With Exploration of the Contract 302 Area

369. As discussed above, on October 10, 2008, TNG informed the MEMR that it no longer wished to enter the estimation phase in relation to Munaibay, and instead intended to exercise the clause enabling a two-year extension of the entire exploration Contract No. 302. The reason TNG gave for that decision was clear:

> The ground for taking decision regarding the recall of the Application for estimation stage introduction constituted in the following: drilling of the well No. 1 Munaibay (planned depth – 6000 meters) still continues and there is a high probability of additional discovery of more deep-lying raw hydrocarbon reservoirs on Munaibay area and raw hydrocarbon reservoirs in the exploration well No. 1 on the nearest Bahyt area which is under mounting.
>
> Besides, there is an opportunity to extend the exploration period by 2 (two) years more according to provisions of the item 3.3 of the chapter 3 of the Contract No. 302 of July 31, 1998 on exploration of raw hydrocarbon on the blocks XXX-14-F (partially), 15-A (partially), D (partially), E (partially), F (partially), XXXI-14-C (partially), 15-A (partially), B (partially), C (partially) on the territory of Mangystau Oblast (hereinafter – Contract) in the edition set in the Appendix No. 5 of February 07, 2007 to the

[524] Tr. January 2013 Hearing, Day 4, 24:11-22.

> Contract. Therefore, "Tolkynneftegas" LLP intends to take this opportunity to fully and thoroughly explore the contractual territory and obtain sufficient information to carry out operations on its estimation.[525]

As Mr. Lungu confirmed, the reference to the possibility of discovering "more deep-lying raw hydrocarbon reservoirs on Munaibay area" is a direct reference to the Interoil Reef structure.[526] Thus, TNG clearly signaled its intent as of October 10, 2008 — prior to the beginning of Kazakhstan's expropriation campaign — to "thoroughly explore" the entire 302 territory, including the Reef structure.

370. TNG reconfirmed its intent to explore the Interoil Reef structure in its request to extend Contract 302, submitted on October 14, 2008. That letter unmistakably stated TNG's intent to complete drilling the Munaibay 1 well to its planned depth of 6,000 meters, and potentially to drill a second ultradeep well, in order to explore the Reef structure:

> [I]it is necessary to continue geological exploration operations since by 30.03.2009, 2 deep exploration wells, one of which – well No. 1 Munaibay is ultradeep and also is the discoverer of HC reservoirs in oversaline Jurassic and Triassic deposits will be under construction. By the letter No.1645T of July 24, 2008, MEMR and Geological Committee were notified about discovery of HC deposits on Munaibay area. There is a high probability of discovering new deep subsalt horizons with oil-and-gas saturation. ...
>
> It should be mentioned that drilling of well No.1 Munaibay has a huge scientific purpose for the study of high-perspective deep horizons in Pre-Caspian area of Western Kazakhstan which was interrupted about 20 years ago and may be resumed only now. Discovery of new HC deposits on depths of over 5-6 km will give a huge impetus for exploration works by other subsoil users in this area, which will definitely result in great HC reserves additions for the Republic of Kazakhstan and discovery of large deeply submerged reef fields of the type Tengiz and Kashagan.
>
> The Minimum working program for the period of exploration extension from 31.03.2009 does not provide for drilling of the second ultradeep well, since the first one has not reached the planned depth and has not been tested yet. It is planned to finish these operations in 2009. In case of discovery of HC reservoirs in subsalt deposits the application for the stage of appraisal with

[525] TNG Letter to MEMR of October 10, 2008 (emphasis added), C-66.

[526] Tr. January 2013 Hearing, Day 1, 250:22-250:25. That testimony was incorrectly transcribed as "a direct reference to the restructuring." Mr. Lungu in fact testified that the reference in Exhibit C-66 to "more deep-lying raw hydrocarbons" was a "direct reference to the reef structure."

> the corresponding program of ultradeep drilling will be necessarily submitted.[527]

The underlined references to "deep subsalt horizons," "new HC deposits on depths of over 5-6 km," and "large deeply submerged reef fields" are unmistakable references to the Interoil Reef structure. That application also makes clear that TNG expected the completion of the Munaibay No. 1 well to its planned depth to potentially penetrate the Reef, or at the very least, to yield valuable information about the reef structure.

371. Kazakhstan is incorrect that TNG's failure to include the second ultradeep well — the Munaibay No. 3 — well in the work program that it submitted with its extension request means that it had no intent or ability to explore the Reef. As TNG made clear in its request, it did not include that well in the work program because it wanted to complete the Munaibay No. 1 well before committing itself to undertake additional exploration work.[528] As Kazakhstan's own experts at GCA have acknowledged, "[c]hanges to the work programme are possible if initial exploration work demonstrates changes in the prospectivity of the field."[529] Moreover, as Mr. Cojin testified, the MEMR had never precluded TNG from conducting additional exploration work not contained in a work program:

> We were never limited in the possibility to explore; namely the working plan is the minimum document, the minimum amount of investments that we had planned to carry out for the purpose of exploration of these areas, and the ministry was always happy and always had good intentions about an investor, or ourselves namely, who would increase the volumes under the working plan.[530]

It simply makes no sense that the MEMR would prevent TNG from amending the work program to drill an additional well to explore the reef structure — unless, of course, Kazakhstan were intentionally trying to prevent TNG from making a valuable discovery on the Reef.

372. Claimants also took concrete steps to enable TNG's exploration of the Interoil Reef. TNG had stopped drilling the Munaibay No. 1 well because it encountered pressures that exceeded the capacity of its existing drilling equipment. To address that problem, Claimants acquired a heavier drilling rig. As Mr. Romanosov explained:

> Q. So why was it necessary to buy a new rig, or another rig?

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527 TNG Application to Extend Contract 302, October 14, 2008 (emphasis added), C-67.

528 TNG Application to Extend Contract 302, October 14, 2008, C-67.

529 First GCA Report ¶ 106.

530 Tr. January 2013 Hearing, Day 2, 64:13-19.

> A. In order to drill this well and in order to explore this field — because we already believed we were dealing with a field — we needed more capacity of a rig, because in the first well we actually found ourselves in a situation where we've discovered new geologic environment and some complications, and in order to increase the safety of drilling, we needed a more capable rig. This is normal practice. ...
>
> Q. What kind of complications did you encounter?
>
> A. There were oil and gas abundances, and certain pressures, pressures of 1.48, if I remember correctly, and this is quite a significant problem which could have led to fountains. And this is just technological specifics; when you drill the wells, you had to change the construction of the well due to these circumstances. So when we drilled Munaibay 2, we already changed the technologies; and of course we took it into consideration for drilling Munaibay. So the new technology would allow us to isolate the horizons where we would deal with those extremely high pressure, and that would allow us to continue working in regular pressure regime.
>
> Q. So this was the reason why Munaibay 1 finished at 4,000 feet?
>
> A. 4,700 metres.[531]

373. As Mr. Stati explained, Claimants acquired the rig in the summer of 2008 from a company in Georgia, and made preparations to transport the rig to Kazakhstan:

> In the summer — if I remember correctly, it was in July — we purchased a heavy drilling rig in Georgia from a state company called InterCharbolServis(?). I trust it's a Georgian name; I might be mistaken in spelling it. And we prepared — we disassembled the rig and prepared it for transportation to Kazakhstan, and we had agreed the terms with the transport companies on which it would be transported. But of course at that time we started experiencing harassment.[532]

374. As a result of Kazakhstan's harassment campaign, Mr. Stati decided in 2009 not to move the new drilling rig to Kazakhstan:

> Q. Mr. Stati, we heard today that you decided to buy a rig in 2008. Do you know when, when in 2008?
>
> A. We did not decide; we actually did buy. I believe it was in late July.
>
> Q. Then you decided not to bring that rig to Kazakhstan; is that correct?

[531] Tr. January 2013 Hearing, Day 2, 67:1-68:17.

[532] Tr. January 2013 Hearing, Day 2, 84:11-19.

> A. That's correct. The situation was such that it was impossible.
>
> Q. When did you take that decision?
>
> A. In 2009.
>
> Q. Do you know when in 2009?
>
> A. Well, frankly, after 18th December, once the ministry gave its resolution on the breach of preemptive rights, we became very careful in relation to Kazakhstan because we understood the Kazakhstan Government's intentions and we became very careful.[533]

Thus, Kazakhstan's harassment campaign directly interfered with TNG's efforts to explore the Contract 302 area, and to prove the resource potential of the Interoil Reef prospect.

375. In fact, but for Kazakhstan's actions, it is possible that TNG would have penetrated the Reef with the Munaibay No. 1 well before Contract 302 was set to expire on March 30, 2009. Under Section 3.4 of Contract 302, if TNG had discovered hydrocarbons in the Interoil Reef (or for that matter, in any of the other areas within the Contract 302 territory), it would have been entitled to enter into the Appraisal Phase with respect to the Reef as a matter of right.[534] If TNG subsequently had determined during the Appraisal Stage that the Reef or other fields contained a Commercial Discovery, Section 8.5 of Contract 302 obligated the MEMR to "use its best efforts under the current Legislation to procure the granting of the Production License to the Contractor and hold in good faith negotiations with the latter on the terms and conditions of the Contract for Production."[535] Thus, Kazakhstan's actions prevented TNG from entering the Appraisal Stage and potentially making a Commercial Discovery on Contract 302, regardless of whether, as Claimants maintain, Kazakhstan was obligated to extend Contract 302.

376. Moreover, Kazakhstan's refusal to execute the formal extension of Contract 302 clearly prevented TNG from conducting further exploration work on the area. But for Kazakhstan's actions, Claimants readily could have completed exploration of the Reef structure long before Contract 302's new expiration date of March 30, 2011. As Mr. Romanosov testified, and as Ryder Scott confirmed, a reasonable estimate of the time it would take to drill one well to the Reef structure is six months.[536] Thus, if Claimants had

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[533] Tr. January 2013 Hearing, Day 2, 114:25-115:15.

[534] Contract No. 302 § 3.4, C-53. That section further provides that "the Competent Body and the Contractor shall agree on the duration of the Appraisal Stage."

[535] Contract No. 302 § 8.5, C-53.

[536] Tr. January 2013 Hearing, Day 2, 6:12-7:2; Tr. January 2013 Hearing, Day 3, 161:17-162:2. Kazakhstan's argument that Claimants would have needed one year to conduct seismic analysis of the reef before drilling

moved their new drilling rig into Kazakhstan in early 2009 as originally planned, they easily could have completed the Munaibay No. 1 well, drilled the Munaibay No. 3 well, and even drilled an additional appraisal well if appropriate before March 30, 2011.

377. Thus, without question, Kazakhstan's violations injured Claimants by preventing them from proving the full extent and recoverability of the resources in the Contract 302 Properties. As discussed further below, that harmed Claimants, among other ways, by stifling their ability to demonstrate recoverable resources in the Contract 302 Properties and interfering with their efforts to sell the investments.

5. Interference With Gas Sales

378. Claimants already have discussed several ways that Kazakhstan's conduct interfered with KPM's and TNG's revenues and cash flows, including: (1) precluding Claimants from obtaining bridge financing from Credit Suisse; (2) causing Vitol to draw down on its prepayment credit arrangements; (3) interfering with the companies' normal development activities, which would have resulted in increased production; and (4) preventing completion of the LPG Plant, which would have increased TNG's revenues from the gas it produced. On top of those injuries, Kazakhstan also interfered with TNG's sales of gas and condensate in 2009.[537]

379. As Claimants explained in their Reply Memorial on Jurisdiction and Liability, TNG's inability to find a buyer for gas in the summer months of 2009 can only be seen as part of Kazakhstan's campaign to put pressure on Claimants.[538] Although the drop in local consumer demand was a seasonal phenomenon, TNG previously had made up such shortfalls by selling gas to exporters like Kemikal.[539] In late 2008, however, Kemikal inexplicably refused to post bank guarantees that were part of its credit terms.[540] Because Kemikal was controlled by Timur Kulibayev, Claimants realized after learning of President Nazarbayev's

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an initial exploration well is wrong. Claimants already had 3D seismic on the reef structure in early 2009. Although a small part of the reef is not covered by that seismic because it is outside the contract area, an additional seismic on that small area is not necessary to drill an exploration well. As Ryder Scott explains, the primary geological risk with the reef structure lies in its reservoir characteristics, which can be proven only by drilling a well. Ryder Scott's Third Report ¶ 29. Thus, a prudent operator would be able to drill an exploration well based on the data available in early 2009.

537 Gas and condensate are produced together, so production of condensate necessarily decreased also when TNG shut in wells to reduce gas production due to lack of a buyer.

538 *See* Reply Memorial on Jurisdiction and Liability ¶ 382.

539 TNG also reduced production in the summer of 2007, but that was a voluntary step in order to negotiate a higher price with Kemikal. *See* Second Lungu Statement ¶¶ 3-5. TNG had never before encountered a situation in which no exporter would take its gas at any price.

540 Second Lungu Statement ¶ 6.

investigation order that continued sales to Kemikal would be extremely risky. Without the bank guarantees, TNG could not assure payment from Kemikal, and continued sales to that company would only provide another avenue for government harassment and theft.

380. Kazakhstan attempts to rebut Claimants' explanation of that situation by portraying Kemikal as an arms' length third party over whom the State had no control, and TNG's decision not to renew the Kemikal contract as a voluntary decision in the ordinary course of business. Those contentions are naïve and wrong.

381. Kazakhstan first argues that Claimants have not proven that Kulibayev owned or controlled Kemikal. Professor Olcott, however, testified that Kemikal was "managed by Samruk-Kazyna."[541] Samruk-Kazyna is the Kazakh state welfare fund, and is 100% owned and controlled by Kazakhstan.[542] Thus, Kazakhstan controlled Kemikal regardless of Kulibayev's involvement. Moreover, Kulibayev has always been extremely close to Samruk-Kazyna. As Olcott herself explained, "much of Samruk's history is interwoven with that of Timur Kulibayev, who began serving as deputy manager of the holding company shortly after the company's launch in 2006, left in 2007, and then returned as deputy CEO in 2008, when Samruk's responsibilities increased."[543]

382. Kazakhstan also argues that "even if Kulibayev controlled Kemikal, this would not trigger any responsibility of the Republic." Quoting Professor Olcott, Kazakhstan asserts that Claimants' argument

> confuses Kulibayev the manager and state servant with Kulibayev the business magnate; and the two roles are distinct. Any action Mr. Kulibayev may have taken as a manager of a private company would clearly not be influenced by his position as manager of state-owned companies.[544]

In addition to the fact that Kemikal was not a private company, that argument is either extremely naïve or asks the Tribunal to be so. Mr. Kulibayev is the son-in-law of President Nazarbayev, the top decision-maker in Kazakhstan's energy sector, and was personally involved in the harassment campaign directed at Claimants.[545] The suggestion that Kulibayev would refrain from using every option available to put pressure on Claimants based on some

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[541] Tr. January 2013 Hearing, Day 3, 49:14-19.

[542] Horton Report ¶ 33. Moreover, Minister Mynbaev testified that Timur Kulibayev was the head of Samruk-Kazyna. Tr. October 2012 Hearing, Day 3, 173:18-19.

[543] M. Olcott, *Kazakhstan: Unfulfilled Promise?* at 266, Exhibit 1 to First Olcott Report.

[544] Rejoinder on Jurisdiction and Liability ¶ 756.

[545] Personal Instruction of President Nazarbayev, November 23, 2009, attached to Blagovest Letter, C-23.

high-minded notion of separateness between state functions and private business functions is fanciful.[546]

383. Additionally, Kazakhstan's direct interference with the management of TNG also contributed to the gas sales problem. Following the arrest of Mr. Cornegruta on April 25, 2009, a majority of the senior management of KPM and TNG wisely decided to leave Kazakhstan, including TNG's general director, Mr. Cojin.[547] Moreover, both before and after Mr. Cornegruta's arrest, the management of TNG had to devote much of its time to responding to the State's various harassment actions, rather than the day-to-day management of the company. Thus, when TNG needed its senior management to devote its time and energies to locating additional gas buyers, its general director was not in the country, and its remaining management was occupied responding to Kazakhstan's harassment.

6. Interference With Ability to Sell the Investments

384. Kazakhstan's illegal conduct also significantly interfered with Claimants' ability to sell or dispose of their investments in KPM and TNG. On this issue, Kazakhstan contends that Claimants have presented no direct evidence proving that Kazakhstan's actions prohibited a sale or were the singular cause of any potential buyer's decision not to buy Claimants' Kazakhstan investments. Kazakhstan not only misstates the evidence, but also the burden of proof on Claimants.

385. To begin with, in addition to the cloud title that Kazakhstan created with its December 18, 2008, press release, Claimants have presented direct evidence of the State's interference with their ability to sell KPM and TNG as of April 30, 2009, when Kazakhstan froze their shares in the companies. The report on the sequestration of shares specifically

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[546] Kazakhstan's also is incorrect that such actions by Kemikal would be "*jure gestionis*" and thus not attributable to the State. Claimants' contention is that Kemikal's decision to stop dealing with TNG on normal commercial terms was not made in the course of normal commercial activity, but in fact was taken in furtherance of the State's campaign to harass Claimants. According to the very authorities that Kazakhstan relies on, the conduct of an entity that is not an organ of the State nonetheless will be attributable to the State of conduct shall be attributable to the State only if the State "directed or controlled the specific operation and the conduct complained of was an integral part of that operation." *See White Industries Australia Limited v. The Republic of India*, UNCITRAL, Final Award, November 30, 2011, ¶ 8.1.7, R-267, *citing* James Crawford, *The International Law Commission's Articles on State Responsibility* (2002), at ll0 ¶ 3.

[547] Second Stati Statement ¶ 28; First Cojin Statement ¶ 22.

notes that Claimants are "prohibited [from carrying] out any actions related to the alienation or transfer of [their] 100% share ownership in the statutory capital … to third parties."[548]

386. Moreover, the evidence shows that Kazakhstan's actions materially affected several potential buyers involved in the Project Zenith sale process. For instance, Medet Suleimenov testified unambiguously that KMG E&P's negative valuation of KPM and TNG in the summer of 2009 took into account numerous aspects of Kazakhstan's harassment of Claimants. After testifying that KMG E&P had concluded that KPM and TNG had an equity value of "minus 50 or minus 100 million," Mr. Suleimenov testified that the liability side of that valuation included debts and obligations stemming directly from Kazakhstan's mistreatment of the companies:

> A. In addition to the debt and cash there are also risks linked to the activities of the company, which are not entered into the balance sheet but were discovered in the due diligence process. They were identified and evaluated, with the assistance of our consultants, in monetary terms.
>
> Q. I see. Well, I want to make sure I understand what debts were included in the liability side of that valuation. Let's look at some of the different debts that you reference in your witness statement. In paragraph 2.17 you reference $531.1 million of total debt on Tristan Oil notes. Was that included in the liability side of the negative valuation?
>
> A. Yes, of course, and not only these figures.
>
> Q. So other debts that you discovered during the due diligence process were included in the liability side of that valuation; is that what you are testifying?
>
> A. Absolutely right.
>
> Q. Maybe we will see some of those in section 2.23 of your witness statement. You reference there, in 2.23(a): "A USD 1 billion claim by the Financial Police regarding the unlicensed operation of main oil and gas pipelines ..." Was that claim included in the liabilities side of that valuation?
>
> A. Absolutely.
>
> Q. What about the "USD 87 million claim for additional tax payments" in 2.23(b): was that included in the liabilities side of that negative valuation?
>
> A. Yes, it was.

[548] *See* Order to arrest all shares of KPM, April 30, 2009, C-486; Order to arrest all shares of TNG, April 30, 2009, C-487; Minutes of the arrest of KPM's shares, May 13, 2009, C-488; Minutes of the arrest of TNG's shares, May 13, 2009, C-489.

> Q. What about the "USD 29 million claim for payments of export duties" referenced in part (c): was that included on the liabilities side of the balance sheet valuation that turned out to be negative in the spring of 2009?
>
> A. Yes, of course.
>
> Q. Is the same also true for the items referenced in paragraph 2.23(d) and (e): the "USD 95 million loan obtained by an affiliate company Montvale" and the "USD 60 million loan obtained by the affiliated company Laren"?
>
> A. That's right, both.[549]

387. Thus, KMG E&P's valuation considered, at a minimum, US $1.287 billion in liabilities that are attributable to Kazakhstan's harassment campaign.[550]

388. The RBS Report confirms that RBS and KMG E&P deducted liabilities attributable to Kazakhstan from their valuation. That assessment concluded that KPM and TNG had an enterprise value of US $612 million in the base case. RBS, however, deducted the US $111 million in new Tristan notes issued to the Laren Lenders from the enterprise value to arrive at the equity value for KPM and TNG.[551] Moreover, the description of its valuation methodology states that "[c]ontingent liabilities were extracted from PwC report and incorporated into the model."[552] The slide in the RBS report on contingent liabilities identifies numerous alleged liabilities that are directly attributable to Kazakhstan's illegal conduct (*e.g.*, tax liabilities, criminal penalties, and the guarantee of the US $60 million Laren loan), and arrives at a risk-weighted total of US $243.5 million in contingent liabilities.[553] The RBS Report incorporated these liabilities as deductions from its enterprise valuation.[554]

389. Mr. Medet Suleimenov also testified that KMG E&P confirmed its valuation by examining the trading price of the Tristan debt.[555] The market price of that debt, however, was negatively affected by Kazakhstan's illegal actions. As Mr. Suleimenov acknowledged,

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549 Tr. October 2012 Hearing, Day 4, 152:5-153:20.

550 This figure includes: (a) US $111 million in Tristan notes issued in connection with the Laren transaction; (b) a US $1 billion claim by the Financial Police for unlicensed operation of a main pipeline; (c) US $87 million claim for back tax payments; (d) US $29 million claim for export duties; and (e) US $60 million owed under the Laren facility.

551 RBS 2009 Asset Valuation, July 31, 2009, slides 40-41, C-723.

552 RBS 2009 Asset Valuation, July 31, 2009, slide 29, C-723.

553 RBS 2009 Asset Valuation, July 31, 2009, slide 62, C-723.

554 RBS 2009 Asset Valuation, July 31, 2009, slide 40-41, C-723. As FTI explains, RBS only includes the Tristan notes, accrued interest, and cash in its calculation of net debt, which it deducts from the enterprise value to arrive at an equity value. Thus, the other contingent liabilities must be included in its model of enterprise value (as stated on page 29), which is not fully transparent in the report itself. *See* Third FTI Report ¶ 3.20.

555 Medet Suleimenov Statement ¶ 2.18.

"any kind of information that became public — or not even public — any kind of information may affect the price or does affect the price" of the debt.[556] In light of the Fitch press release putting the Tristan debt on ratings watch as a direct result of the MEMR's December 18, 2008, press release and the criminal investigation, there can be no doubt that the market "priced in" the risk associated with Kazakhstan's illegal actions into the trading price of the Tristan debt. Thus, Kazakhstan's actions affected KMG E&P's valuation of KPM and TNG in this way as well.

390. Kazakhstan also overstates the evidence regarding the reasons why Total did not consummate a purchase of Claimants' investments. To begin with, Mr. Chagnoux of Total was simply not a credible witness. His assertion that Renaissance Capital had pressured Total to increase its indicative offer to obtain access to the data room is belied by the cover email attaching the revised indicative offer, which states that Total was providing a value for the LPG Plant pursuant to the bidding instructions.[557] Chagnoux's explanation for that discrepancy was that he had been dishonest when he told Claimants that Total valued the LPG Plant at US $100 million:

> Q. Did you state earlier that you believed at the time that the LPG plant had a negative value?
>
> A. Yes.
>
> Q. So were you being dishonest by stating in your offer that you were offering $100 million for the LPG plant?
>
> A. To a certain extent, yes. [558]

Moreover, his entire attitude towards Claimants smacked of hurt feelings that Claimants initially did not consider Total's offer good enough to move on to Phase 2 of the sale process:

> Q. As a buyer, wouldn't it be in your interest to know if your valuation does not meet the seller's expectations so that you can either decide to increase your bid or move along to the next project and not waste your time and money on that one?
>
> A. No. We knew that we were a good buyer, we knew that we were to continue. It was a big opportunity for us, and we were a good buyer for the seller. So we were sure that we would go to the data room and that we were to continue the process. It was just irritating. ...

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[556] Tr. October 2012 Hearing, Day 4, 157:14-16.

[557] Chagnoux Statement ¶ 2.2; Chagnoux Annexes I and II with attached email from Louis Caillard to Renaissance Capital, October 6, 2008.

[558] Tr. October 2012 Hearing, Day 4, 21:13-18.

> It's the standard practice that all companies in that situation, we put a reasonable offer on the table, in the upper range of their evaluation. And this is what we had done with 900, and we were really surprised to see that 900 was not sufficient because it was really the upper range, and we really had a bad feeling with Mr. Rusinov saying this was not sufficient. We were telling him, "Look, we know what we are doing with the information you have provided us. 900 is already a good figure."[559]

Additionally, Mr. Chagnoux offered substantial testimony regarding what occurred at the meeting with Claimants' management in March 2009, but he admitted under cross-examination that he was not even present at the meeting.[560]

391. Furthermore, Mr. Chagnoux clearly has a very cozy relationship with Kazakhstan and its counsel. He was unable to provide any satisfactory explanation as to why Total voluntarily provided details of its admittedly confidential negotiations with Claimants to the Kazakh Minister of Oil and Gas when it was under no legal obligation to do so.[561] Also, Mr. Chagnoux met with counsel for Kazakhstan to prepare for his testimony, at which time counsel provided confidential information from this arbitration (in particular, indicative offers of other Project Zenith bidders) to Mr. Chagnoux.[562] It certainly seems that Mr. Chagnoux and Total have been motivated by a desire to curry favor with Kazakhstan.

392. Be that as it may, Mr. Chagnoux's testimony regarding why Total did not complete a purchase of Claimants' investments rang hollow. In his letter to the Ministry of Oil and Gas, Mr. Chagnoux stated that Total lost interest in the transaction after viewing more data because it was "disappointed both with the data regarding the existing field production (Barankol) and with the potential for additional reserves."[563] At the October 2012 Hearing, however, when asked to explain Total's disappointment with Borankol's existing production, he did not identify any problems with Borankol's existing production; rather, he testified that Total saw little room for increasing the reserves.[564] Moreover, Borankol accounted for less than 20% of Total's original US $900 million indicative offer.[565] Mr. Chagnoux admitted that Total had no disappointment with existing production at the Tolkyn field, which accounted

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559 Tr. October 2012 Hearing, Day 4, 15:13-16:16.

560 Tr. October 2012 Hearing, Day 4, 24:24-25:10.

561 Tr. October 2012 Hearing, Day 4, 36:13-37:15. Mr. Chagnoux's response explains only that Total felt it could provide information on its negotiations with Claimants to the MOG. He never explained why it did.

562 Tr. October 2012 Hearing, Day 4, 21:24-22:17.

563 Letter of *Total E&P Activites Petrolieres* regarding Project Zenith, August 23, 2011, R-41.4.

564 Tr. October 2012 Hearing, Day 4, 28:6-22.

565 Tr. October 2012 Hearing, Day 4, 27:21-28:2.

for more than 80% of Total's indicative offer.[566] Something does not add up from Mr. Chagnoux's vague "explanation" of why Total lost interest in the deal.

393. Furthermore, Mr. Chagnoux's testimony demonstrated that Kazakhstan in fact did interfere with Claimants' sale efforts by preventing them from proving the resources in the Interoil Reef structure. Mr. Chagnoux admitted that Total was interested in the "exploration target," by which he meant Contract 302, and in particular, the Interoil Reef.[567] Total had doubts about the closure on the reef structure, however, which prevented Total from moving forward with the deal unless it obtained more information reducing the risks:

> MR HAIGH: And what I'm curious about is that it seems to me that it's still keeping the door open, in the sense that it's asking for further information. Is that a —
>
> A. Yes, it was basically — that's exactly as you say, "If you could provide us with more information overcoming our doubt, we could continue assessing this exploration target." And we were never provided that information. And probably Mallard at that time already knew that it was impossible to get this kind — to reach this level of confidence.
>
> MR HAIGH: I don't know whether I can go along with your speculation as to what Mr Mallard was really thinking, but I see what he wrote in any event. He seemed to be keeping the door open.
>
> A. To receive more information that would reduce his doubts.[568]

394. Kazakhstan, however, prevented Claimants from providing additional information to Total about the Reef by failing to complete the extension of Contract 302, and by creating an investment environment that precluded Claimants from implementing and completing TNG's exploration plans.

395. Kazakhstan also mischaracterizes the significance of the testimony regarding the reasons KNOC did not complete a purchase. Mr. Kim of KNOC testified that TNG's inability to export gas was the principal reason that KNOC decided not to complete a purchase of KPM and TNG. As Claimants have shown in their Reply on Quantum and at the January 2013 Hearing, however, TNG's inability to export gas was directly attributable to Kazakhstan's illegal actions. Thus, like the testimony of Mr. Chagnoux, Mr. Kim's testimony

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[566] Tr. October 2012 Hearing, Day 4, 27:17-28:2.

[567] Tr. October 2012 Hearing, Day 4, 32:1-7.

[568] Tr. October 2012 Hearing, Day 4, 33:3-13, 39:8-23.

underscores the impact of Kazakhstan's misconduct on the sales process and Claimants' ability to dispose of their investments.

396. Finally, Kazakhstan seeks to hold Claimants to an impossibly high burden of proof in its pleadings on this topic. It is simply not possible for Claimants to show by direct evidence how Kazakhstan's actions affected the internal decision-making processes of various potential buyers in the marketplace. That is especially true of potential buyers such as Total and KNOC that have ongoing operations in Kazakhstan and, thus, every incentive to curry favor with — or refrain from alienating — the Kazakh government.

397. The Tribunal is not required to check its common sense at the door, and Claimants are not required to prove the impossible. As discussed above, a careful review of the testimony of Mr. Chagnoux and Mr. Kim indicates that Kazakhstan's illegal conduct had negative impacts on the sales process. When that testimony is combined with the evidence of the effect of the INTERFAX article on the Credit Suisse negotiations, the Fitch ratings watch notice, the trading price of the Tristan notes following that notice,[569] the share and asset freezes in the midst of the baseless criminal investigation, and the evidence that RBS and KMG E&P considered Claimants' troubles with the government in analyzing the potential purchase of KPM and TNG, the Tribunal should draw the reasonable conclusion that Kazakhstan's actions interfered with Claimants' ability to sell their investments.

7. Total Loss of the Assets

398. Obviously, Kazakhstan's termination of the Subsoil Use Contracts and seizure of all the assets of KPM and TNG in July 2010 caused enormous injury to Claimants, who thereby irrevocably lost the ability to sell the assets or use them productively to generate profits. As shown in the preceding sections, however, Claimants had lost meaningful control over their investments long before the final seizure. The seizure was merely the final move in a series of illegal acts from late 2008 onward, each of which seriously impacted Claimants' ability to profitably and successfully operate, manage, control, and dispose of their investments.

[569] The trading price of the Tristan notes dropped 20%, from US $37.50 to US $30, following publication of the Fitch ratings watch announcement. *See* Quoted Yield to Maturity of the Notes, at 20, Exhibit E to First FTI Report.

B. Kazakhstan's Alternative Causation Theories Are Belied by the Evidence and Common Sense

399. In its Rejoinder on Jurisdiction and Liability, Kazakhstan argues that "[e]xternal circumstances and Claimants' own actions led to a deterioration of value of KPM and TNG and their abandonment by the alleged investors."[570] In support of this argument, Kazakhstan alleges that a laundry list of factors — including the Tristan debt structure, the drop in oil prices in 2008-2009, and the "constant withdrawal of cash from the companies" — led to "a severe underfunding of KPM and TNG and subsequently, to the companies no longer complying with their obligations under the Subsoil Use Contracts and Kazakh law. The eventual termination of the contracts was a logical consequence."[571]

400. That argument is sheer fantasy. Kazakhstan either distorts or greatly exaggerates — sometimes both — every one of the factors that it claims caused KPM and TNG to be underfunded. Moreover, Kazakhstan's primary evidence for this argument is the "expert" report of Professor Olcott, who is a political scientist with no background in economics or finance, and who is simply not qualified to opine on the financial condition of KPM and TNG. The Tribunal should reject this theory outright.

1. KPM and TNG Were Never Overexposed to Debt

401. In Section X.2 of its Rejoinder on Jurisdiction and Liability, Kazakhstan argues that the Tristan debt structure overleveraged KPM and TNG, which made them extremely vulnerable to a drop in revenues. Kazakhstan also argues that "the Tristan structure was directed at maximizing the income of Tristan Oil and various other offshore Stati subsidiaries while minimizing the income of KPM and TNG." Those arguments are objectively and demonstrably wrong, and demonstrate the lack of rigor in Kazakhstan's (and Professor Olcott's) financial analyses.

402. To begin with, that argument is based on nothing but Kazakhstan's bald assertion. Kazakhstan calculates that the annual interest payment on the original US $420 million in Tristan notes was US $44.1 million, which "translated into yearly interest rates of 15-16% which KPM and TNG had to pay." It then asserts, citing no support whatsoever, that "[i]t stands to reason that such a continuous and heavy financial burden had a negative impact on KPM's and TNG's operations."[572] Kazakhstan's bare assertion of what "stands to reason,"

[570] Rejoinder on Jurisdiction and Liability § X.

[571] Rejoinder on Jurisdiction and Liability ¶¶ 724-25.

[572] Rejoinder on Jurisdiction and Liability ¶¶ 734-735.

however, is no substitute for evidence or sound analysis. Its supposed financial expert, Professor Olcott, performs no ratio tests or other standard financial analysis of the companies' ability to service the debt, or any comparison of that debt load to comparable companies, to support her opinion that the debt overburdened the companies.

403. FTI, on the other hand, has analyzed the finances of KPM and TNG, and concludes that they were in good financial condition prior to October 2008. On September 30, 2008, KPM and TNG had "current ratios" of 3.1 and 3.0, respectively.[573] Under this common liquidity-measuring financial ratio, which compares current assets to current liabilities, a company is generally deemed to be liquid when the ratio is above 1.[574] The companies also had combined retained earnings in excess of US $365 million on September 30, 2008.[575] Additionally, the fact that the companies were able to attract a US $150-175 million bridge loan from Credit Suisse in the midst of the financial crisis — that is, before the MEMR's defamation in the financial press scared Credit Suisse away — confirms that the companies were financially stable prior to the Government's harassment.[576]

404. There also is no evidence to support Kazakhstan's accusation that the Tristan structure was designed to maximize the income of Tristan Oil and other offshore subsidiaries while minimizing the income of KPM and TNG. Again, Kazakhstan's only support for this assertion is Professor Olcott, the political scientist.[577] Olcott, in turn, simply asserts that "the annual reports of Tristan Oil make [this] clear," without specifying what in those reports makes the allegations clear, or how.[578] Kazakhstan makes that unsubstantiated claim solely to assert that the financial structure "was presumably intended to minimize the amount of income taxable by the Kazakh authorities."[579] However, Kazakhstan does not even assert that the debt structure in fact reduced the taxes paid by KPM and TNG, or that such tax minimization, if it occurred, was improper.[580] The Tribunal should ignore these scurrilous and unsupported accusations of Kazakhstan and its "expert."

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573 Third FTI Report ¶ 11.10.

574 Third FTI Report ¶ 11.10.

575 Third FTI Report ¶ 11.11.

576 Third FTI Report ¶ 11.12.

577 Rejoinder on Jurisdiction and Liability, n. 767.

578 First Olcott Report ¶ 164.

579 Rejoinder on Jurisdiction and Liability ¶ 737.

580 As FTI observes, there is nothing inherently improper about executing a lawful tax planning strategy. Third FTI Report ¶ 11.15. Kazakhstan's tax authorities had full capability to audit KPM and TNG, and those authorities never asserted that KPM and TNG were "offshoring" funds to improperly reduce tax liability.

2. Claimants' Search for Bridge Financing Does Not Show That KPM and TNG Faced a "Serious Liquidity Shortage" Prior to November 2008

405. As further support for its argument that the finances of KPM and TNG were in "bad shape" prior to any impact from Kazakhstan's actions, Kazakhstan argues that Claimants' search for a bridge loan in November 2008 "is a clear sign that already in November 2008, the companies were facing serious liquidity shortages."[581] Kazakhstan misstates the facts regarding when and why Claimants began seeking a bridge loan, and how Kazakhstan's interference with that search injured KPM and TNG.

406. Claimants did not initially seek bridge financing because of a shortfall of working capital. As Mr. Lungu testified, Claimants originally conceived of the bridge financing in the early fall of 2008 on the recommendation of their investment bankers at Renaissance Capital who were handling the Project Zenith sale process. The goal was to obtain a partial advance on the proceeds of the sale in order to reinvest the proceeds in other projects as soon as possible:

> In the fall of 2008, at the beginning of the fall, we were at the end of the second stage for the sale of the assets, the Zenith Project. The money we got from that, we wanted to reinvest that money into other investment opportunities in the area of oil and gas in Iraq. Any opportunity should be used as soon as it comes up, and we needed a limited bridge loan that would be guaranteed by the future money we would get from the sale of the assets.[582]

Mr. Lungu then explained that later, in December 2008, the bridge loan also made sense to provide some reasonable protection against falling oil and gas prices:

> [T]here was a dual rationale here: on the one hand, we still had the opportunities [in Iraq] that justified the bridge loan, and we were not able to defer them fully; and on the other hand, we saw that prices were going down, and we thought it would be reasonable for us to make ourselves — to make our company guaranteed in case this downfall in prices should continue.[583]

The fact that Claimants viewed a bridge loan in December 2008 as reasonable insurance against the possible consequences of a declining price environment (in addition to the original

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[581] Rejoinder on Jurisdiction and Liability ¶ 742.

[582] Tr. October 2012 Hearing, Day 1, 199:7-199:18. Mr. Lungu misspoke in stating that the Claimants were at the end of the second stage of Project Zenith in the fall of 2008. It is undisputed that they were at the end of the first stage, contemplating the beginning of the second stage. *See* First Lungu Statement ¶ 34.

[583] Tr. October 2012 Hearing, Day 1, 200:2-200:9.

purpose of facilitating their investments in Iraq) hardly shows that KPM and TNG already faced "serious liquidity shortages" in November 2008.

407. Additionally, although Kazakhstan sabotaged the Credit Suisse financing in December 2008 with its defamatory press statements, the liquidity position at KPM and TNG did not become highly problematic until June 2009, when Claimants were forced to enter into the Laren transaction in order to make major tax and interest payments. Kazakhstan's argument that the going-concern qualification issued by the companies' auditors for the first quarter 2009 financials shows that the companies were in serious financial trouble much earlier is highly disingenuous.[584] To begin with, the auditors' report that Kazakhstan cites is dated June 10, 2009, and expressly states that the going concern qualification was based on events "subsequent to March 31, 2009."[585] More importantly, the major reasons that the auditors gave for the going concern qualification were Kazakhstan's freezing of KPM's and TNG's assets and Claimants' equity interests in KPM and TNG, the criminal investigation of KPM and TNG, and the US $62 million back tax assessment.[586] Liquidity trouble was the last (and shortest) of the reasons the auditors listed.[587] The fact that the auditors saw Kazakhstan's targeted harassment of KPM and TNG as a threat to those companies' ability to remain as going concerns proves how Kazakhstan did cause injury to Claimants, not the opposite.

408. Moreover, even if KPM and TNG were in a tight liquidity position by June 2009 — which Claimants acknowledge, although as discussed above, that was mainly due to Kazakhstan's conduct — that fact in no way reduces the injurious impact of Kazakhstan's interference with the Credit Suisse financing. In fact, it amplifies it because Kazakhstan prevented Claimants from obtaining additional working capital on reasonable terms at a critical time, forcing Claimants to turn to the Laren loan sharks instead.

3. Kazakhstan Overstates the Impact of Oil and Gas Price Declines in 2008-2009

409. Claimants have never denied that falling oil and gas prices in late 2008 and 2009 created challenging conditions in the oil and gas business. Kazakhstan, however, vastly

584 Rejoinder on Jurisdiction and Liability ¶ 745.

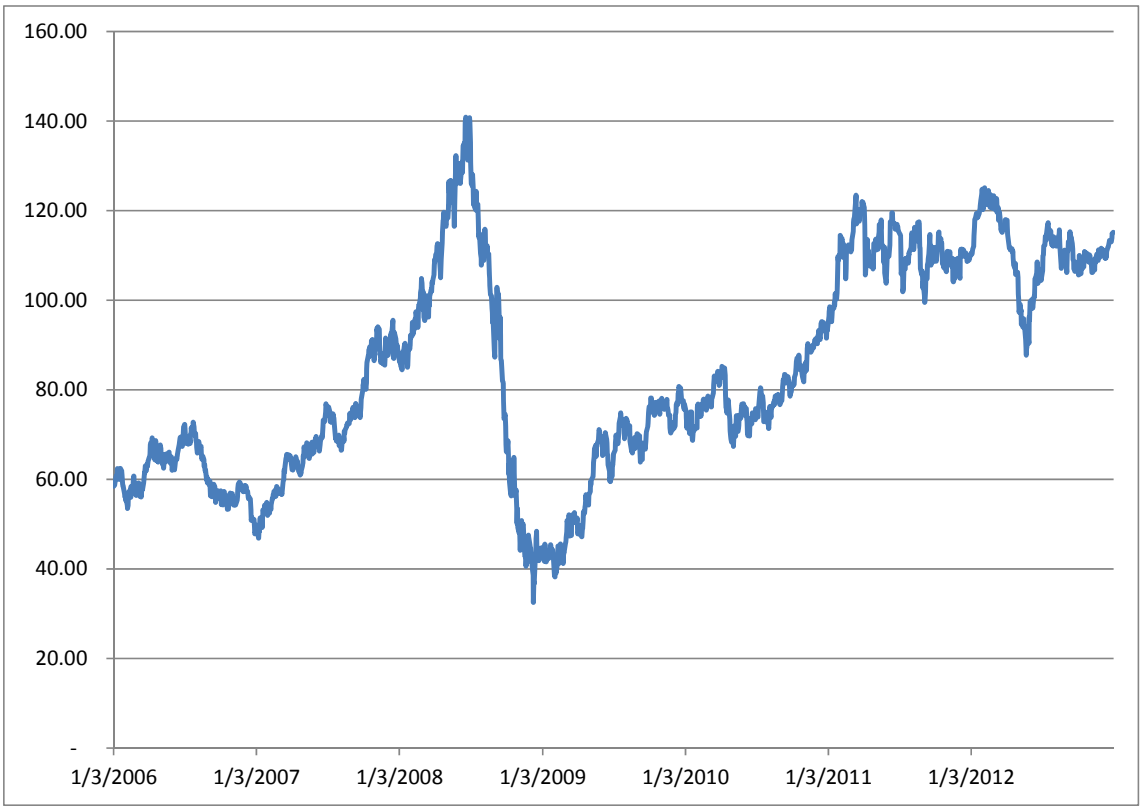
585 Tristan Oil Ltd. Interim Report for the Three Months Ended March 31, 2009, at F-2-F-3, R-262.

586 Tristan Oil Ltd. Interim Report for the Three Months Ended March 31, 2009, at F-2-F-3, R-262.

587 Tristan Oil Ltd. Interim Report for the Three Months Ended March 31, 2009, at F-3, R-262.

exaggerates the impact of those market conditions on Claimants' investments. The dip in prices was quite short, and the effect on the finances of KPM and TNG was similarly limited.

410. To create the illusion that the "decline was rather dramatic," Kazakhstan cites Tristan's Annual Report for 2009, which stated that "sales decreased to $174.8 million for the year ended December 31, 2009 from $504.6 million for the year ended December 31, 2008, a decrease of 65.4%."[588] The year 2008, however, was itself an anomaly because oil prices climbed to unprecedented highs. The following chart of Urals Mediterranean oil prices tells the full tale:[589]



411. As late as October 1, 2007, oil prices were below US $80 per barrel. Prices then climbed quickly and dramatically, to an all-time high of around US $140 per barrel in June 2008. As a result of the global financial crisis and recession, prices then plummeted just as quickly, bottoming out below US $32 per barrel in December 2008. The trough was short-lived, however, with prices returning to US $50 per barrel by March 2009, and US $70 per barrel by June 2009.

[588] Rejoinder on Jurisdiction and Liability ¶ 740.

[589] *See* Third FTI Report, Exhibit 1.

412. Moreover, gas prices did not decline significantly at all. The companies' average realized price for gas declined only 14.2% from 2008 to 2009 (from US $1.36/mcf to US $1.17/mcf).[590] The 52.1% decline in the companies' gas sales revenue from 2008 to 2009 thus was due primarily to reduced sales volumes, which as discussed above, are attributable to Kazakhstan's interference.

413. The salient point is that the truly difficult pricing environment was limited to oil and was temporary — it was over before the fourth quarter of 2009. While oil prices did not climb back close to 2008 levels for several years more (*e.g.*, US $123 per barrel on April 11, 2011), KPM and TNG did not need prices to remain at 2008 levels to be highly profitable. This is evidenced by the fact that KPM and TNG recorded a combined net profit in 2007 of US $81.5 million (notably, after paying interest on the Tristan debt), when prices averaged less than US $70.[591] It is also confirmed by the market for the Tristan notes, which were trading around 96% of face value in October 2007.[592]

414. Finally, even with the low oil prices in 2009 — and even with all of the extraordinary difficulties resulting from Kazakhstan's expropriation campaign — KPM and TNG did not record substantial losses. In fact, KPM recorded a net loss of only US $13 million and TNG recorded a net profit of US $9.4 million — again, after paying interest on the Tristan debt.[593]

415. In short, this is not the picture of two companies that were overleveraged and on the precipice of failure. As Mr. Lungu put it:

> [T]he financial situation that was generated at the end of 2008 and the beginning of 2009 was caused by objective factors, and we could have dealt with that quite easily; but we were affected, impacted, by the State of Kazakhstan, and I mentioned the actions against us. ...
>
> There was a certain cash deficit that was motivated by the factors, that is loss — drop of prices and a lack of contracts on the local market, a lack of demand. But there were also extraordinary factors that led to the complication of this situation because, in our opinion, if the environment had been normal, even if there are such

590 2009 Annual Report of Tristan Oil at 10, R-37.6.

591 2007 Annual Report of Tristan Oil and attached Audited Financial Statements at 6, F-73, and F-109, R-37.4.

592 First FTI Report, Exhibit E.

593 Audited Financial Statements Attached to 2009 Annual Report of Tristan Oil at F-69 and F-105, R-37.6.

> temporary financial constraints, they can be sorted out, they can be solved.[594]

In short, Kazakhstan's argument that the market situation confronting KPM and TNG was so severe that their failure was inevitable, and that Claimants instead abandoned the companies, is belied by the objective evidence.

4. Claimants Did Not Strip KPM and TNG of Cash in 2009 and 2010

416. The final piece of Kazakhstan's "alternative causation" theory is its allegation that Claimants aggressively and improperly extracted cash from KPM and TNG in preparation to abandon them. Kazakhstan points to the extension of payment terms for KPM and TNG's main liquids buyers (Stadoil and General Affinity) in 2009, KPM's declaration of a US $52.6 million dividend at the end of 2009,[595] and Tristan Oil's payment of a US $3.86 million bonus to Mr. Stati at the end of 2009. Kazakhstan's speculation that these events were part of a plan to strip KPM and TNG of cash before abandonment is baseless and wrong.

417. First, Kazakhstan's insinuation that the extension of credit terms for the liquids buyers was anything other than a reasonable decision in the ordinary course of business is unfounded. According to KPMG's Auditors' Report, "the management of Tolkynneftegaz LLP and Kazpolmunay LLP agreed to extend the payment terms for their largest customers, Stadoil Ltd. and General Affinity Ltd., which are related parties, after they were informed that these customers would not be able to comply with existing contractual payment terms."[596] It is hardly surprising that with the onset of the global financial crisis and the associated rapid price declines in 2009, slow payments and defaults cascaded through the industry. Claimants fully acknowledge that slow payment by buyers was one of the factors that contributed to the tight liquidity situation in the middle of 2009, but the suggestion that that situation was voluntary — which would mean that Claimants preferred the highly unattractive Laren transaction to simply collecting receivables from their customers — is absurd.

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[594] Tr. October 2012 Hearing, Day 1, 201:17-201:22, 213:12-213:19.

[595] Although Kazakhstan does not reference it, KPM also declared a non-cash dividend in the amount of US $19.4 million (including withholding tax at 15%) on March 31, 2010. There is a reference to this dividend in Tristan Oil's 2009 Annual Report as having occurred on March 31, 2009, but that reference is a typographical error as evidenced by the fact that it is discussed in the section addressing "Events Subsequent to December 31, 2009." 2009 Annual Report of Tristan Oil, at 18, R-37.6. KPMG's Auditors' report also confirms that the two dividends occurred "at 31 December 2009 and subsequent to this date." *Id*. at F-4 (PDF page 24).

[596] Audited Financial Statements attached to 2009 Annual Report of Tristan Oil, at F-3 (PDF page 23), R-37.6; *see also id*. at F-4 (PDF page 24), F-56 (PDF page 76), and F-74.

418. Second, KPM declared dividends in late 2009 and 2010 in order to mitigate the harm caused by Kazakhstan's illegal actions. Importantly, those dividends were in the form of an assignment of trade receivables, and "did not result in any cash being paid to the shareholder of KPM."[597] The reason for this should be obvious: by late 2009, any money that flowed into KPM's bank accounts was at risk of immediate seizure to satisfy the illegal US $145 million criminal penalty that Kazakhstan had imposed against KPM on September 18, 2009.[598] As Mr. Lungu testified, it was only prudent for Claimants to minimize the assets that Kazakhstan could illegally seize:

> Q. And why did KPM pay a dividend in 2009 if it was experiencing cashflow problems? Wouldn't that just make a bad situation worse?
>
> A. Well, this happened at the beginning of 2009, at the end of 2009 and the beginning of 2010, when we already knew that the State of Kazakhstan had decided to take over Kazpolmunay, when the legal order against Mr Cornegruta became effective and when they applied the penalty of $145 million, and the company could not pay such an amount. It was unreasonable, and we understood that they had made their decision and we tried to protect what we could still protect at that time.[599]

419. Additionally, Tristan Oil owed a substantial coupon payment (of around US $28 million) to the noteholders on December 31, 2009.[600] The assignment of receivables allowed Tristan to collect funds that otherwise may have been frozen in KPM's bank accounts, and Tristan made the coupon payment in full.[601] At the October 2012 Hearing, Kazakhstan made much of the fact that KPM's dividends allegedly violated the Tristan Indenture (although it has never been clear why any such breach is relevant to the claims here).[602] It is telling, however, that the Tristan noteholders did not place Tristan in default based on those dividend payments, which is a strong indicator that the noteholders were satisfied with the steps that Claimants took to enable that coupon payment.

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[597] 2009 Annual Report of Tristan Oil, R-37.6 at 4.

[598] The statement by Professor Olcott that the dividends and bonuses show that Claimants had decided to "liquidate their investments in Kazakhstan" before the US $145 million penalty was issued against KPM is laughable. The dividends and bonus payment she points to all occurred after that penalty was issued at the very end of 2009, and the only basis for her argument is that these dividends and bonuses were discussed in the audit that covered all of 2009. First Olcott Report ¶ 173. That aptly demonstrates the rigor of Professor Olcott's financial analysis.

[599] Tr. October 2012 Hearing, Day 1, 202-20-202:6.

[600] Audited Financial Statements Attached to 2009 Annual Report of Tristan Oil at F-73, R-37.6.

[601] Audited Financial Statements Attached to 2009 Annual Report of Tristan Oil at F-70, F-73, R-37.6.

[602] Tr. October 2012 Hearing, Day 1, 180:4-180:10 ("And KPM declared $52.6 million in dividends, which was prohibited by the bond regime.").

420. Finally, Tristan Oil's payment to Mr. Stati of a US $3.86 million bonus at the end of 2009 is a non-issue. Mr. Stati has financial obligations of his own, and as he testified, he has a legal right to receive the profits of his investments.[603] Moreover, as discussed above, the tight liquidity conditions that existed in the middle of 2009 were essentially over by the end of 2009. The payment of a US $3.86 million bonus to Mr. Stati did not exacerbate any liquidity problems of KPM and TNG at that time, because there were none.[604]

421. In short, Kazakhstan's argument that these transactions show that Claimants had abandoned their investments, and were removing as much cash as possible, is baseless. To the contrary, KPM's assignment of receivables was part of an effort to protect Claimants' investments by preventing a default on the Tristan notes. That is consistent with the uncontradicted evidence that Claimants went to great lengths to continue paying KPM's employees after its accounts were frozen in 2010, including having TNG pay those employees from its accounts. It also consistent with Claimants' entry into the highly unattractive Laren transaction, in which Mr. Stati gave a personal guarantee, in order to raise funds needed to keep the companies alive.[605] Far from abandoning their investments, Claimants made every effort to protect them, right up until Kazakhstan ultimately seized them in July 2010.

* * *

422. In summary, Claimants have amply demonstrated that Kazakhstan's actions caused myriad serious injuries to Claimants' investments beginning shortly after President Nazarbayev issued his investigation order on October 14, 2008, continuing over the next twenty months, and ending with the final seizure of the assets of KPM and TNG in July 2010. Kazakhstan's theory that the woes of KPM and TNG result solely from Claimants' management or market conditions outside the State's control is bogus, unsupported, and a clear attempt to distract attention from its own clear misconduct.

V. QUANTUM

423. As set out above, it is beyond dispute that Kazakhstan's violations of the ECT caused serious damage to Claimants' investments in Kazakhstan. It is a broadly-recognized

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603 Stati Testimony, Tr. October 2012 Hearing, Day 2, 46:2-46:4.

604 That is wholly consistent with Claimants' position that Kazakhstan itself is responsible for KPM's inability to make two small payments, totaling approximately US $124,000, that Kazakhstan asserts among the bases for terminating KPM's Subsoil Use Contract. As discussed in Section III.B.6 above, KPM could not make those payments because Kazakhstan had frozen its bank accounts, not because it lacked the funds.

605 *See* Laren Facility Agreement, at 12-13, C-733.

principle of international law that once the fact of damage is established, Tribunals have broad discretion to establish the appropriate quantum of compensation. As the annulment committee in *Rumeli v. Kazakhstan* put it in rejecting Kazakhstan's challenge to the quantum determination in that case:

> [T]ribunals are generally allowed a considerable measure of discretion in determining issues of quantum. ... This is not a matter to be resolved simply on the basis of the burden of proof. To be sure, the tribunal must be satisfied that the claimant has suffered some damage under the relevant head as a result of the respondent's breach. But once it is satisfied of this, the determination of the precise amount of this damage is a matter for the tribunal's informed estimation in light of all the evidence available to it.[606]

424. In a case of expropriation, compensation normally is determined by reference to the fair market value of the asset that was expropriated.[607] Moreover, the same standard of compensation applies to Kazakhstan's other violations of the ECT, including its breach of the FET obligation. Numerous tribunals have "borrowed" from the fair market value standard typically applied in expropriation cases to determine damages for other violations of investment treaties. For example, in *CMS v. Argentina*, the tribunal concluded that fair market value is the correct standard on a claim not involving expropriation when "the cumulative nature of the breaches … results in important long-term losses."[608] Likewise, in *GemPlus v. Mexico*, the tribunal considered the decision in *CMS*, as well as similar decisions in *Vivendi v. Argentina*, *Azurix v. Argentina*, and *M.T.D. v. Chile*, and concluded that it need not "distinguish between compensation for unlawful expropriation and compensation for breach of the FET standards."[609] Here, the cumulative effect of Kazakhstan's numerous breaches of its obligations under the ECT caused serious long-term losses, and thus fair market value of the assets of KPM and TNG is the appropriate measure of damages for all of Claimants' claims.

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606 *Kazakhstan v. Rumeli*, ICSID Case No ARB/05/16, Decision of Ad Hoc Committee on Annulment, March 25, 2010, ¶¶ 146-47, C-735.

607 *Kazakhstan v. Rumeli*, ICSID Case No ARB/05/16, Decision of Ad Hoc Committee on Annulment, March 25, 2010, ¶ 150, C-735.

608 *CMS v. Argentina*, ICSID Case No. ARB/01/8, Award, May 12, 2005, C-65.

609 *Gemplus S.A. and Talsud S.A. v. United Mexican States*, ICSID Case No. ARB(AF)/04/4, Award, June 16, 2010, ¶ 12-52, C-309.

A. October 14, 2008 Is the Correct Valuation Date

425. In their Reply Memorials on Jurisdiction and Liability and on Quantum, as well as at the January 2013 Hearing, Claimants demonstrated why the Tribunal should adopt the valuation date of October 14, 2008, under well-established principles of international law.[610] Claimants stand by those submissions, and will not repeat them here. Rather, Claimants will elaborate on some of the key factual and economic reasons why October 14, 2008, is the correct valuation date in this case, and why Kazakhstan's proposed valuation date of July 22, 2010, clearly is not.

1. Claimants' Valuation Date of October 14, 2008, Is Necessary to Make Claimants Whole

426. Under the facts of this case, a valuation date of October 14, 2008, is necessary to fully compensate Claimants for the injuries caused by Kazakhstan's violations of the ECT and international law. Abundant evidence makes clear that Kazakhstan decided in the fall of 2008 to expropriate Claimants' investments and initiated the campaign to do so on October 14, 2008. The campaign upon which Kazakhstan embarked on that date and in the weeks immediately following Nazarbayev's directive was not only a campaign of indirect expropriation; it was also markedly unfair and inequitable, a material impairment of Claimants investments by unreasonable measures, and an abject failure to provide Claimants' investments with "the most constant protection and security."[611]

427. Over the course of the next twenty months, Kazakhstan took a number of actions aimed at devaluing Claimants' investments to pressure Claimants to sell at a coerced price or to create a pretext for terminating the subsoil use contracts. As discussed at length in Section IV, above, those actions impaired the value of Claimants' investments in innumerable ways that are not susceptible to individuation and quantification. In order to fully eliminate the value-depressing effects of the State's actions in the quantification of damages, it is therefore necessary to value Claimants' investments before the State's illegal actions commenced. As Mr. Rosen of FTI explained:

> Q. What is your understanding of the factors that, in your view as a valuation expert, are relevant to the appropriateness of one valuation date or another?

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610 *See* Reply on Jurisdiction and Liability § VII.B; Reply on Quantum, *passim*.

611 *See* Statement of Claim ¶¶ 258-383; *see also* Reply on Jurisdiction and Liability ¶¶ 469-555.

> A. So in general, and in this particular case, there is an allegation of actions by the state that served to, at first instance, diminish the value of an asset, and then later take the asset. Therefore, in order to measure the economic impact to the claimant, it is necessary to look at the value of those assets before any of those actions that may have impacted the value, and then eventually result in the taking of the assets is considered.[612]

428. Kazakhstan's valuation date of July 22, 2010, does not take into account any of the value-depressing effects of the State's actions. By simply calculating the alleged value of KPM's and TNG's assets at that date, Kazakhstan would afford no compensation for:

- The diminution in value of KPM and TNG caused by the bogus allegation that they engaged in criminal misconduct that would result in "death penalty" fines by operating main pipelines without a license;
- Its complete interference with normal business operations and Claimants' attempts to sell KPM and TNG by freezing their shares, Subsoil Use Contracts, and property;
- The impairment of production by KPM and TNG resulting from the interference in normal field development efforts;
- The impairment of TNG's revenues, and the increase in completion cost, resulting from the non-completion of the LPG Plant;
- The impairment of TNG's revenues resulting from interference with TNG's normal gas sales efforts;
- The cost to Claimants of borrowing money from the loan shark Laren Lenders rather than Credit Suisse; and
- The lost opportunity to sell their investments free from the State's defamatory accusations and cloud on the title of TNG.

For this reason, Kazakhstan's valuation date is simply wrong as a matter of both fact and law. It fails to address major aspects of Claimants' case and would not compensate Claimants for multiple injuries caused by Kazakhstan's misconduct well before the final, outright seizure in July 2010. As Mr. Rosen of FTI explained it:

> Q. Why would a date in July 2010 be an inappropriate valuation date in a case like this, in your view?
>
> A. Again, it comes down to: the claimant is making their case that damages flow from a series of events, and the Tribunal will decide

[612] Tr. January 2013 Hearing, Day 4, 44:8-19.

> if that's right or not. But my job is not to decide that. My job is to provide the Tribunal with a number that: if they do decide that, what is the damage?
>
> So to choose a date that by definition includes all of the actions of the government prior to the taking by definition excludes all of those value-depressing events. So from my point of view I did not find it helpful to look at that valuation date.[613]

429. Additionally, Kazakhstan's valuation date of July 22, 2010, does not account at all for the effect of Kazakhstan's actions on Claimants' reputation and ability to sell the investments free from interference by the State. Such an ability is embodied in the definition of fair market value, which both sides agree is the basic standard of damages under international law. As explained by Mr. Rosen of FTI:

> Generally, compensation to a claimant is to be based on putting them back in a position they would have been but for the alleged actions, and for that the standard of fair value or fair market value is traditionally the measure we use.
>
> A definition that's commonly accepted on a global basis by valuation professionals is that fair market value should be expressed in terms of what transaction would occur between informed, prudent parties in an open and unrestricted market, under no compulsion to transact and at a specific point in time. All of those individual elements are important considerations for a valuation expert.[614]

430. The last day that Claimants had an opportunity to sell their investments in an open and unrestricted market, under no compulsion to transact, was October 14, 2008 (or very shortly thereafter). After learning of President Nazarbayev's order — and certainly no later than the contrived investigative findings against KPM and TNG of November 14, 2008, the launch of the formal criminal investigation of KPM on December 15, 2008, and the MEMR's planted article in the financial press on December 18, 2008 — Claimants faced enormous pressure to sell in order to mitigate the harm stemming from Kazakhstan's misconduct. Also, the MEMR's press release eliminated an open and unrestricted market for the investments because it clouded Claimants' title to TNG and defamed Claimants' reputation. The criminal investigations likewise defamed the companies' reputations and created obvious concerns for potential investors, as reflected in the Fitch ratings notice that followed within weeks.

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[613] Tr. January 2013 Hearing, Day 4, 45:11-23.

[614] Tr. January 2013 Hearing, Day 4, 43:1-13.

2. A Valuation Date of October 14, 2008, Does Not Give Claimants "Double Compensation"

431. In its Rejoinder on Quantum, Kazakhstan wrongly asserts that

> the inappropriately early valuation date also allows Claimants to disregard significant income that KPM and TNG created between 14 October 2008 and the termination of the contracts on 21 July 2010. In a blatant attempt to obtain double compensation, Claimants, through the setting of the valuation date, do not take account of the income during that period, even though this income runs into hundreds of millions of USD — which were transferred out of the Republic of Kazakhstan and not subjected to Kazakh taxation.[615]

That argument is both misleading and mistaken. KPM and TNG did not earn hundreds of millions of dollars between October 10, 2008, and July 22, 2010, and Kazakhstan's argument misrepresents the evidence from Deloitte that it relies upon. Moreover, an award of damages based on a valuation date of October 14, 2008, does not overcompensate Claimants because Claimants have not included any working capital in their enterprise valuation, and the distributions that Claimants made in 2009 and 2010 were of profits earned before Claimants' valuation date.

432. Kazakhstan repeatedly asserts that "Claimants disingenuously claim compensation for profit they already have pocketed."[616] Kazakhstan argues that the Tribunal "should deduce [sic] the income earned until 21 July, 2010," and citing Deloitte, asserts that the amount of such income is US $226.6 million (which Deloitte later increased in its amended report shortly before the Hearing on Quantum to US $302.3 million).[617] That assertion misrepresents what Deloitte said, and it is false.

433. Deloitte never stated that KPM and TNG earned US $226.6 million, US $302.3 million, or indeed anything at all, between October 14, 2008, and July 21, 2010. Rather, Deloitte said that "the production in this period [between the valuation dates] constitutes one of several causes for differences in value attributed to the Tolkyn and Borankol fields by FTI and Deloitte," and that "the production assumed by FTI" during that time period had a value of US $226.6 million (later, US $302.3 million) in FTI's model.[618] That is not remotely the same as a conclusion that KPM and TNG earned that money, much

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615 Rejoinder on Quantum ¶18(b); *see also id*. ¶¶ 442-446.

616 Rejoinder on Quantum, Section D.II.

617 Rejoinder on Quantum ¶¶ 445-446; Deloitte Amendment Report, January 22, 2013, ¶ 3.

618 Deloitte GmbH Report ¶¶ 193-195.

less that Claimants "pocketed" it. Instead, what Deloitte purports to calculate is the amount that FTI assumes that KPM and TNG would have earned in the time period between October 14, 2008, and July 21, 2010, but for interference by Kazakhstan.

434. It is not appropriate to deduct the amount that KPM and TNG could have earned in that time period but for interference from Kazakhstan from FTI's valuation because Claimants were not able to operate KPM and TNG without interference from Kazakhstan. KPM and TNG did not produce as much oil and gas as they could have absent State interference because Claimants wisely paused drilling and workover activities in the fields. KPM and TNG did not produce as much oil and gas as they could have absent State interference because Kazakhstan's actions required them to reduce production at Tolkyn in the spring and summer of 2009. TNG did not earn as much money as it could have absent State interference because Kazakhstan prevented it from bringing the LPG Plant online in June of 2009. Moreover, Kazakhstan impeded Claimants' efforts to sell the companies, and thus to reap the value in FTI's damages model attributable to the time period between the valuation dates through such a sale. Deducting the amount of value in FTI's damages model attributable to the time period between the parties' valuation dates would improperly deny Claimants any compensation for the injuries that Kazakhstan caused in that interval. That is precisely why Claimants' valuation date of October 14, 2008, is the correct one.

435. Additionally, Claimants did not "pocket" hundreds of millions of dollars attributable to the time period after the October 14, 2008, valuation date. Kazakhstan's only argument to support this brazen misrepresentation is that KPM assigned US $81.2 million in receivables to Tristan Oil and Ascom in the form of loan payments and dividends in 2009.[619] As discussed above in Section IV.B.4, however, Claimants reinvested much of those distributions in KPM and TNG by using the funds to pay the companies' obligations (*i.e.*, the Tristan coupon payment). More importantly, those funds represented profits that KPM and TNG had earned prior to the October 14, 2008 valuation date. At the end of September 2008, KPM and TNG combined had US $221.5 million in net working capital (cash, cash equivalents, and receivables less current liabilities), and more than US $367 million in retained earnings, on their balance sheets.[620] Those assets were the results of the successful operations of KPM and TNG prior to that time, and Claimants' subsequent distribution of

[619] Rejoinder on Quantum ¶ 443.

[620] Reviewed Financial Statements for Nine Months Ended September 30, 2008, attached to Tristan Oil Interim Report for the Nine Months Ended September 30, 2008, at F-69, F-105, Exhibit FTI-69 to First FTI Report.

those profits in no way affects how damages should be calculated because Claimants have not included working capital in their enterprise valuation.

436. Kazakhstan's argument demonstrates a fundamental misunderstanding of how an asset sale, which is the fundamental basis of Claimants' damages claim, actually works. As discussed more fully below in Section V.E, Claimants request damages in the amount of the value of the assets that Kazakhstan seized on the day it began its campaign to devalue and seize them. This is the equivalent of a hypothetical asset sale, *i.e.*, what Kazakhstan would have had to pay for the assets if it had bought them from Claimants in an asset sale on October 14, 2008, rather than launching a campaign to drive down their value and seize them under a pretext. In a typical asset sale, the seller either retains all of the existing working capital or the buyer pays the seller for the working capital (*e.g.*, buys the receivables).

437. Here, Claimants have not included any claim for the value of the working capital on the balance sheets of KPM and TNG on October 14, 2008. If they had, then it would be necessary to reduce Claimants' damages by the amount of the working capital that KPM and TNG subsequently distributed to Claimants to avoid double-counting. Because they have not, no reduction is necessary or appropriate.[621]

438. Finally, Claimants must respond briefly to Kazakhstan's unsupported accusation that Claimants caused hundreds of millions of dollars to be "transferred out of the Republic and not subjected to Kazakh taxation."[622] Kazakhstan lobs that accusation early in its Rejoinder on Quantum in order to paint Claimants as tax scofflaws, but it has provided no evidence (or indeed, even further argument) to support that accusation anywhere in its submissions or at the hearings. Nor is it evident how the assignment of receivables would even affect the amount of taxes that KPM and TNG owed to Kazakhstan. The assignment of receivables affects the companies' balance sheets and cash flow statements, but it has no effect whatsoever on the calculation of income on which corporate income taxes are levied. And while dividends are subject to a 15% withholding tax on nonresidents, KPM paid that tax on the dividends it declared in late 2009 and 2010.[623] The Tribunal should disregard that accusation for the unsupported, scurrilous attempt at character assassination that it is.

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621 Furthermore, as FTI observes, KPM's and TNG's operations generated negative cash flows through the end of 2009, around the time that they made the distributions that Kazakhstan complains about. Third FTI Report ¶¶ 7.33-7.36. There is no evidence that KPM and TNG generated any net cash flows that were earned after the October 14, 2008 valuation date that were distributed to Claimants. *Id.* ¶ 7.36.

622 Rejoinder on Quantum ¶ 18(b).

623 Audited Financial Statements attached to 2009 Annual Report of Tristan Oil, at F-37, R-37.6.

B. The Valuation Analyses of FTI and Ryder Scott Are Substantially More Accurate and Reliable Than the Corresponding Work by Deloitte GmbH and GCA

439. Respondent has introduced two markedly different geology and engineering reports by GCA, and two markedly different valuation reports, one allegedly by Deloitte TCF, and one by Deloitte GmbH. Respondent submitted the undated and unsigned Deloitte TCF report, and the first GCA report, with its Statement of Defense in November 2011. Following receipt of Claimants' Reply Memorial on Quantum and the rebuttal reports from FTI and Ryder Scott, Respondent evidently decided that the Deloitte TCF report was a tactical mistake, and that it needed an entirely new, and lower overall, valuation of Claimants' investments. Hence, 60 days before commencement of the Quantum Hearing, Respondent submitted with its Rejoinder on Quantum a valuation report by Deloitte GmbH that completely supplants the Deloitte TCF report, and an almost unrecognizably new and revised report by GCA.

440. A close examination of these reports, however, as well as testimony presented at the Quantum Hearing, make clear that the work of GCA and Deloitte GmbH is not sufficiently reliable or accurate to serve as the basis for a calculation of damages in this case. GCA's analysis, which forms the basis for all of Deloitte GmbH's production and cost assumptions, is totally unsupported and, frankly, shoddy. Deloitte GmbH adopts that analysis wholesale, and then compounds GCA's errors with faulty assumptions about gas prices and other serious defects in its valuation methodology — including its complete failure to check its DCF valuation against other indicators of value. The result is a valuation that is so far removed from reality that this Tribunal should disregard it entirely.

1. The Tribunal Should Disregard Kazakhstan's Entire Valuation Because It Is Based on Opaque and Unsupported Assertions

441. The Tribunal will search the record in vain for <u>any</u> back up materials supporting the summary tables and conclusions in GCA's reports. GCA's representatives at the Quantum Hearing confirmed that GCA's reports completely lack any such support. For example, Michael Wood, who provided the capex and opex estimates contained in the two GCA reports, testified variously:

> Q. ... Could you point the Tribunal to anywhere in the record any of the work that you say you have done is reflected? (Pause) ...

> A. ... In both reports we presented only summary-level cost estimates. ...[624]
>
> Q. My question for you is — it's very nice to have the summary data — can you point the Tribunal to where in this record in this proceeding there is any support for the numbers that you provided?
>
> A. I have the support; I haven't provided it. That's commercially confidential. ...[625]
>
> Q. You indicated that you had vendor data to support your compression cost estimate. There is no evidence in the record of that; correct?
>
> A. That's correct. Such data from vendors we get regularly; it's confidential, I couldn't give that to anybody....[626]

Similarly, Stephen Wright, who provided GCA's geological and reserves analysis, testified:

> Q. [W]here in the record can you point the Tribunal to any of the analysis that you performed? Have you produced any written analysis of this, or is this just an opinion that's expressed in one or two sentences?
>
> A. It is reported here in our report only.
>
> Q. You've produced no data, no written support, no modeling, no analyses whatsoever; is that correct?
>
> A. No.
>
> Q. That's true for all of your reserve estimates. You produced nothing to support the estimates contained in this report; is that correct?
>
> A. That's correct.[627]

442. With no analytical or documentary support, the Tribunal and Claimants simply cannot scrutinize or verify GCA's summary assertions and conclusions. This is all the more troubling because, as discussed further below, there are wild swings and contradictions between GCA's two reports, GCA consistently "cherry-picks" assumptions to drive costs up and revenues down, and GCA's entire method of analysis is alarmingly lax. Examples of this pattern include:

- In its first report, GCA assumes an unexplained, and frankly uncommercial, "limited work program" for Borankol with no major investment for enhancing recoveries from the behind-pipe reserves,

[624] Tr. January 2013 Hearing, Day 3, 205:24-206:9.

[625] Tr. January 2013 Hearing, Day 3, 206:17-22.

[626] Tr. January 2013 Hearing, Day 3, 207:15-20.

[627] Tr. January 2013 Hearing, Day 3, 214:9-21.

resulting in a gross understatement of the recoverable reserves for Borankol;

- In its second report, GCA simply asserts that it had considered the Borankol behind-pipe reserves in its first report, then summarily increases its estimates of recoverable reserves from existing wells, adding estimates for recoverable behind-pipe reserves, and adding estimated well recompletions;
- Despite increasing its Borankol behind-pipe reserves estimates in its second report, GCA still grossly understates those reserves;
- GCA invents a need for expensive compression on the Tolkyn field based on the fact that the 2007 Field Development Plan called for compression, while it simultaneously ignores that Plan's much higher projections of gas production which served as the predicate for the anticipated need for compression;
- GCA exaggerates the impact of water production in the Tolkyn field;
- GCA ignores the Artinskian Dolomite behind-pipe reserves in the Tolkyn field;
- In its second report, GCA summarily decreases its production estimates by 29% and increases its well count (and hence its capital costs) by 300% on Munaibay, thereby negating Deloitte TCF's previous US $68 million valuation of Munaibay Oil resources, and facilitating Deloitte GmbH's negative US $297.7 valuation of Munaibay Oil resources;
- In its second report, GCA skews the DCF calculation to drive down value by front-loading $220 million in capital costs for "pre-drilling" wells in Munaibay, and providing no contemporaneous production from those wells;
- GCA inflates development costs for the Interoil Reef prospect by assuming a 100% chance of H_2S in the gas production based on analogizing that prospect to the Tengiz field, but conveniently omits characteristics of those fields that reflect significantly higher condensate yields that would, were GCA to be consistent, increase revenue assumptions by billions of dollars;
- GCA assumes a protracted exploration phase for the Interoil Reef prospect, including the acquisition of additional and unnecessary 3D seismic, that could not be completed within the allotted exploration period;
- GCA assumes with no support whatsoever that gas from the Center-Asia-Center Pipeline would be compositionally unusable in the LPG Plant; and
- GCA arbitrarily assigns a $100 million completion cost to the LPG Plant.

In light of these serious questions surrounding the substance of GCA's conclusions, the lack of transparency in its analysis and failure to document its work strongly suggest that GCA was engaged in an effort to arbitrarily maximize cost estimates, minimize reserve and production estimates, and accelerate costs while delaying revenues wherever possible.

443. Regardless of GCA's motive, however, its failure to explain and document its analysis makes its conclusions wholly unreliable. Article 5(2)(e) of the IBA Rules on the Taking of Evidence in International Arbitration states very plainly that a party-appointed expert's report "shall contain … his or her expert opinions and conclusions, including a description of the methods, evidence and information used in arriving at the conclusions. Documents on which the Party-Appointed Expert relies that have not already been submitted shall be provided."[628] The commentary to that rule explains, logically enough, that "[t]his information is required in order to place the other party in a position meaningfully to evaluate the expert report."[629] Likewise, the Tribunal cannot meaningfully evaluate GCA's expert opinions without the explanation of its methods and the supporting documentation that the IBA Rules require. Rather, Kazakhstan asks the Tribunal to take GCA on faith. As explained in the sections that follow, the errors that are apparent in GCA's work make such faith completely inappropriate, and the Tribunal should disregard GCA's opinions entirely.

444. Moreover, Mr. Wood's reliance on alleged "commercial confidentiality" as an excuse for GCA's failure to provide the backup for its conclusions is no justification for GCA's (and Kazakhstan's) failure to follow the IBA Rules and standard expert practice in treaty arbitrations. As Mr. Latham from Ryder Scott testified, if the confidentiality of a document prohibits its disclosure to the Tribunal and parties in an arbitration, an expert should not rely on it, and should locate an alternative source of data.[630] Mr. Wood's excuse simply does not hold water and is difficult to take seriously.

445. Moreover, Deloitte GmbH relied entirely on GCA for all of the key development schedule, well count, capital expense (capex), operating expense (opex), and oil and gas reserve and production estimates that it employed in its valuation.[631] That is not surprising as to the geology and engineering issues (which would be outside of Deloitte's area of expertise), but it is unusual that Deloitte relied entirely on geologists and engineers for capex and opex estimates. At the Quantum Hearing, however, Mr. Gruhn made clear that Deloitte GmbH's reliance on GCA's unsourced cost estimates was absolute, without any

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628 *See* IBA Rules on Taking of Evidence in International Arbitration, art. 5(2)(e).

629 *See* Commentary on Revised Text of the 2010 IBA Rules on Taking of Evidence in International Arbitration at 19, Annex 16 to Claimants' Motion to Compel, January 2, 2013.

630 *See* Latham Testimony, Tr. January 2013 Hearing, Day 4, 26:12-27:12.

631 Deloitte GmbH report at 9-10 ¶ 1(2); Tr. January 2013 Hearing, Day 4, 137:5-8. Although Kazakhstan has withdrawn the Deloitte TCF report, it likewise is apparent from the Deloitte TCF report that it similarly made wholesale use of GCA's estimates without independent verification. Deloitte TCF Report ¶¶ 1.9, 3.1.

effort either to independently verify their reasonableness or accuracy, or to compare them against any of Claimants' historical costs:

> Q. Now, for your assumptions regarding capex and opex you relied entirely on Gaffney Cline & Associates; correct?
>
> A. That's correct. ... [632]
>
> Q. ... Do you agree that your report does not reflect any work to verify the reasonableness or the accuracy of the assumptions regarding capex and opex by GCA? In your report, sir.
>
> A. In my report it's only mentioned that we relied on analyses by Gaffney Cline. ...
>
> Q. So your report does not reflect any effort to compare the cost assumptions made by GCA against any historical data regarding KPM and TNG's actual historical capex or opex cost, does it?
>
> A. I had vast opportunity to discuss everything over the whole stretch of time, until 30th November, when this report was written, with GCA, and this has been done in face-to-face meetings in London, in Frankfurt, and various telephone conferences.
>
> Q. I'm asking you, sir, about what's reflected in your report. There is no discussion in your report about comparing GCA's cost assumptions —
>
> A. We don't —
>
> Q. — against any historical reality benchmarks, is there?
>
> A. Yes, that is true.[633]

446. Irrespective of how many meetings Mr. Gruhn claims to have had with GCA, what remains is the fact that all of the capex, opex, and production forecast inputs into Deloitte GmbH's DCF valuations are based entirely on GCA's opaque, unsupported, and (as discussed below) freely-fluctuating estimates without any verification by Deloitte GmbH. In short, GCA's estimates are the foundation of Respondent's entire DCF valuation, and the massive defects in GCA's analysis render Kazakhstan's entire valuation completely unreliable. Claimants urge the Tribunal to disregard the reports of GCA and Deloitte GmbH — as well as that of Deloitte TCF, which suffers from the same defects and also has been withdrawn — in their entirety when assessing the appropriate damages to award.

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[632] Tr. January 2013 Hearing, Day 4, 137:5-8.

[633] Tr. January 2013 Hearing, Day 4, 138:1-6, 11-25.

2. GCA's Reserve and Cost Estimates Are Based on Lax and Flawed Methodology

447. The defects in GCA's reports are not limited to its failure to "show its work." Rather, it is apparent from a close review of what is in those reports, as well as from testimony at the Quantum Hearing, that GCA's entire analysis is based on a shoddy "back of the envelope" approach that lacks rigor and reliability, and appears designed to increase cost and lower production estimates at every turn.

448. To understand the superficiality of the work performed by GCA, it is helpful first to review the fully documented, transparent, and independent analysis that Ryder Scott conducted. That work included:

- A quantitative petrophysical analysis, which included analysis of all penetrated reservoirs and all wells where log data was available, which yielded:
  - Top and base of reservoir picks;
  - Net pay calculations; and
  - Average porosity and water saturation in intervals that passed net pay cutoffs.
- A review of completion intervals, which together with the petrophysical analysis was used to determine hydrocarbon-water contacts.
- Interpretation of seismic data, which included:
  - Receipt of interpreted seismic horizons from Claimants for all top reservoir surfaces;
  - Review of velocity information to verify that the seismic horizons tied to the top of the reservoir picks from the petrophysical analysis;
  - Modification of the seismic horizons as appropriate; and
  - Generation of structure maps in time for all seismic horizons which tied to top reservoir picks.
- Structural and Net Pay Mapping, which included:
  - Loading surface location and datum elevation information for all wells, as well as deviation surveys for deviated wells, into Geographix, and generation of base maps to be used both in reservoir mapping and to correct reservoir picks to true vertical depth sub-sea;
  - Construction of top of reservoir structure maps in depth for all reservoirs using seismic interpretation time grids, seismic velocity information, and the top reservoir picks from the petrophysical analysis;

- Construction of net sand distribution maps (net sand isochore maps) for all reservoirs using the net sand counts (which are intervals with sufficient reservoir quality to contribute to production) for each well from the petrophysical analysis;
- Construction of net pay isochore maps (which reflect net sand above the hydrocarbon-water-contact) for all reservoirs using the top reservoir structure maps in depth and the net sand distribution maps; and
- Use of the net pay isochore maps to calculate estimated net reservoir volume for each reservoir, to identify recompletion candidates, and to assist in the reserve assignments for individually scheduled well recompletions.

- Calculation of volumetric estimates of original hydrocarbons in place for all reservoirs using:
  - The net reservoir volume calculated from the net pay isochore maps;
  - The average porosity and water saturation calculated from the petrophysical analysis for intervals passing net pay cutoffs; and
  - Reservoir pressure, temperature, and fluid properties.
- A gas material balance analysis, which is a graphical technique displaying the relationship between bottom hole pressure and fluid properties to cumulative gas production, and incorporates compensation for formation(rock), formation water, and aquifer expansion, providing a more rigorous overall reservoir analysis.
- Analysis of production performance for each well and reservoir, including
  - historical production (gas, oil, water);
  - cumulative production;
  - material balance (gas);
  - gas to oil ratios;
  - condensate yield;
  - flowing tube pressures; and
  - analysis of all available well test data.[634]

Ryder Scott's thorough analyses reflect the work that a prudent operator would perform or commission to properly assess reserves and resources, including the sorts of analyses routinely performed for valuation purposes in a significant commercial transaction.

449. By contrast, GCA did no independent petrophysical analysis,[635] seismic analysis,[636] well log analysis,[637] mapping,[638] or material balance analysis.[639] Furthermore, it

[634] Third Ryder Scott Report Exhibit 16.

[635] Tr. January 2013 Hearing, Day 3, 112:12-16.

did not perform any independent analytical work to assess behind-pipe reserves or specific, accompanying well recompletions.[640] As both Mr. Nowicki and Mr. Latham testified, in the absence of such work, there can be no reliable estimate of reserves and resources for a fair market valuation.[641]

450. What GCA claims that it did do was summarized by Mr. Goodearl:

> But as part of the overall process you also have to do what we call reality checks, and sometimes it is worth doing a back-of-the-envelope check. Fortunately, we haven't just done that; we have reviewed and we have audited the information that we have. Not just the Ryder Scott maps and data; we have also used also as a basis for our work the FDP or the field development plans provided by the reserve institutes in Kazakhstan and the monitoring reports associated with those.[642]

451. Being charitable to GCA, this is an admission that GCA simply reviewed the work performed by Ryder Scott, and development plans and monitoring reports prepared by several state institutes. Reviewing work performed by others, however, is no substitute for independent, thorough geological analysis like that performed by Ryder Scott. Moreover, the State "Monitoring Reports" that Mr. Goodearl refers to, which are identified in GCA's second report as the 2010 KazNIPIMunaiGas and NIPINeftegas reports,[643] are nowhere to be found in the record. And the State Field Development Plans that Mr. Goodearl refers to, which are presumably the 2007 KazNIPIMunaiGas and NIPINeftegas plans,[644] are not in the record, are merely conclusions that lack detailed underlying analysis, and are of exceedingly doubtful use in establishing reserves, future production, and operational estimates for a July 2010 valuation. Furthermore, as shown below, GCA's alleged "auditing" of the 2007 Field

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636 Tr. January 2013 Hearing, Day 3, 112:12-16.

637 Tr. January 2013 Hearing, Day 3, 107:3-5.

638 Tr. January 2013 Hearing, Day 3, 108:22-23.

639 Tr. January 2013 Hearing, Day 3, 115:7-11.

640 Tr. January 2013 Hearing, Day 3, 119:18-21.

641 Tr. January 2013 Hearing, Day 3, 112:17-23; 119:22-120:3.

642 Tr. January 2013 Hearing, Day 3, 187:10-18.

643 Second GCA Report ¶¶ 23, 65.

644 In its second report, GCA specifically identifies the 2007 KazNIPIMunaiGas Field Development Plan, which covered the Tolkyn field, in its second report. Second GCA Report ¶¶ 26, 34. However, GCA only generically refers to a "2007 FDP" in its discussion of the Borankol field. Second GCA Report ¶¶ 54, 56, 59, 65, 67-70. GCA is presumably referring to the 2007 NIPINeftegas Field Development Plan, which covered the Borankol field. Neither Kazakhstan nor GCA submitted this important document that forms the basis of so much of GCA's opinion into the record. Claimants submitted a translation of the cover page to identify the author of the plan, but otherwise, there is no English translation of this long and complex document in the record.

Development Plans in fact consists of disingenuous use of those Plans to drive up costs while ignoring them in its estimation of reserves and production.

452. The bottom line is that GCA's approach resulted in numerous, serious errors in its analysis that can be divined from its reports and the testimony at the Quantum Hearing.

a. Borankol Field

453. Deloitte TCF's US $16 million valuation of the Borankol field, and Deloitte GmbH's $62.8 million valuation, were both the direct products of the summary reserves estimates contained in GCA's two reports. In its first report, GCA forecast future, recoverable oil and condensate reserves from Borankol of only 5.45 million barrels (MBbls), and indeed inexplicably cut off its forecast prior to expiration of the contract.[645] In its second report, GCA increased its estimate of recoverable oil and condensate reserves to 8.65 MBbls based on no new data, and with no cogent explanation. Both of these estimates are baseless.

454. While it appears that GCA used some type of decline curve analysis to derive its first forecast, GCA provided no clue or any documentation in its first report about its specific methodology.[646] Nor did GCA provide any explanation at all as to why it chose to cut off the forecast prior to expiration of the contract. Indeed, the entirety of GCA's analysis regarding its Borankol forecast in its first report is contained in four narrative paragraphs and one summary table, which do not reference any behind-pipe reserves in the Borankol field or any well recompletions to recover those reserves.[647]

455. To put the absurdity of this initial forecast in perspective, Ryder Scott's estimate of 18.8 MBbls of remaining crude oil and condensate in the Borankol field as of October 14, 2008, is 344% of GCA's initial estimate of 5.45 MBbls as of July 21, 2010.[648] Cumulative production between October of 2008 and July of 2010 in the Borankol field was approximately 2.3 MBbls of oil and condensate, which means that GCA's forecasted future production ignored 11.05 MBbls of recoverable crude oil and condensate.[649] GCA did this by simply assuming a "limited work program" for the Borankol field.[650] It provided no explanation as to what that limited work program entailed, why such a limited work program

[645] First GCA Report, Appendix III, Table AII.2.

[646] Tr. January 2013 Hearing, Day 3, 120:21-121:5.

[647] First GCA Report ¶¶ 44-47, and Appendix III, Table AII.2.

[648] Second Ryder Scott Report at 8-9.

[649] Second Ryder Scott Report at 8-9.

[650] First GCA Report ¶ 47.

should be assumed, or why a prudent operator would leave otherwise recoverable reserves in the ground. Simply ignoring a vast quantity of recoverable crude oil and condensate without explanation is not, to say the least, a credible method of valuing an oil field.

456. In its second report, GCA states that its initial reserves estimate, and its assumed "limited work plan," were both the product of its review of "the FDP," presumably the 2007 NIPIneftegas Field Development Plan[651] (although GCA does not explicitly identify which Field Development Plan it refers to).[652] GCA then simply asserts that its cryptic initial reserves estimate had in fact considered behind-pipe reserves, stating summarily that its initial estimate of 5.45 MBbls in total future recovery had included (without disclosure) recovery of 2.35 MBbls in behind-pipe reserves from 34 well recompletions, and 3.16 MBbls in recovery from existing wells.[653] GCA then summarily increases (i) its behind-pipe reserves estimate to 3.95 MBbls, (ii) its well recompletions to 43, and (iii) its estimate of recovery from existing wells to 5.05 MBbls, an amount suspiciously close to its original 5.45 MBbls total recovery estimate.[654] From all appearances, GCA simply covered its tracks by tacking on some portion of the substantial behind-pipe reserves that it concedes should be considered in any reserves estimate, but failed to consider in its first report.

457. Despite its addition of behind-pipe recovery in its second report, however, GCA still grossly underestimates the total recoverable reserves in Borankol by 10.2 MBbls. The following table (slide 40 of Claimants' opening presentation at the Quantum hearing) shows a comparison of Ryder Scott's Borankol reserves estimate and GCA's two conflicting estimates from its first and second reports:

651 2007 NIPIneftegas Field Development Plan (in Russian), C-682.

652 Second GCA Report ¶¶ 54, 56.

653 Second GCA Report ¶ 57.

654 Second GCA Report ¶ 70.

Borankol - Comparison of RSC and GCA			
	RSC	**GCA Nov. 2011 Report**	**GCA Nov. 2012 Report**
Future oil production from existing wells[1]	6,688 MBbl	3,161 MBbl	5,059 MBbl
Future oil production from recompletions and completions[2]	12,092 MBbl (behind pipe & undeveloped)	2,351 MBbl (behind pipe)	3,592 MBbl (behind pipe)
Future gas production[3]	27.6 BCF	3.3 BCF	3.3 BCF
Number of recompletions[4]	58	34	43
Number of new wells[5]	4	0	0

1. RSC 5/11 Rpt., p. 1 & Disc 1, PHDWin file, Borankol Producing Summary; GCA 11/12 Rpt., ¶¶ 57, 70
2. RSC 5/11 Rpt., p. 1 & Disc 1, PHDWin file, Borankol Behind Pipe & Undeveloped; GCA 11/12 Rpt., ¶¶ 57, 70
3. RSC 5/11 Rpt., p. 1; GCA 11/11 Rpt., AII.2; GCA 11/12 Rpt., Table Aii.2
4. FTI 5/11 Rpt., p. 70, Table 11; GCA 11/12 Rpt., ¶¶ 57, 70
5. FTI 5/11 Rpt., p. 70, Table 11

458. The reason for GCA's continuing underestimation in its second report can be found in the new methodology it adopted.[655] As Ryder Scott explains in its Third Report, GCA's methodology for its revised reserves estimates consisted of two components: (1) projected total future production from existing wells based on an "oil cut vs. cumulative oil production" plot and (2) projected production of behind-pipe reserves from 43 unidentified well recompletions based on a "type well" analysis.[656]

459. The oil cut versus cumulative production methodology employed by GCA for its estimate of future production from existing wells is not a reliable approach. As Ryder Scott explains in greater detail, that is one variety of decline curve analysis that attempts to extrapolate future production from historical production.[657] Because it does not take into consideration individual well production characteristics, the geophysical characteristics of a reservoir, or volumetric analysis — all of which Ryder Scott employed in establishing its

655 GCA clearly abandoned whatever inexplicable estimation methodology it had used in its first report. *See* Latham Testimony, Tr. January 2013 Hearing, Day 3, 121:17-122:5 ("With respect to Borankol, they definitely made a change in methodology from the first report to the second report.")

656 Third Ryder Scott Report ¶ 46.

657 *See also* Latham Testimony, Tr. January 2013 Hearing, Day 3, at 120:7-11 ("Decline curve analysis is kind of a group term that refers to a whole variety of techniques, all of which have one thing in common, and that's historical performance data is used as the basis for determining the remaining reserves.").

estimate — GCA's method is very much influenced by the overall history of operations in a field, or the lack thereof, at any particular time.[658] Variables such as the number of wells that have been drilled or worked over recently, the amount of expenditures to maintain and/or enhance production during specific periods, the impact of external factors such as weather events, market events, or governmental interference, and numerous other day-to-day operational considerations that affect a field's production at any given time can make this methodology unreliable for projecting future production.[659]

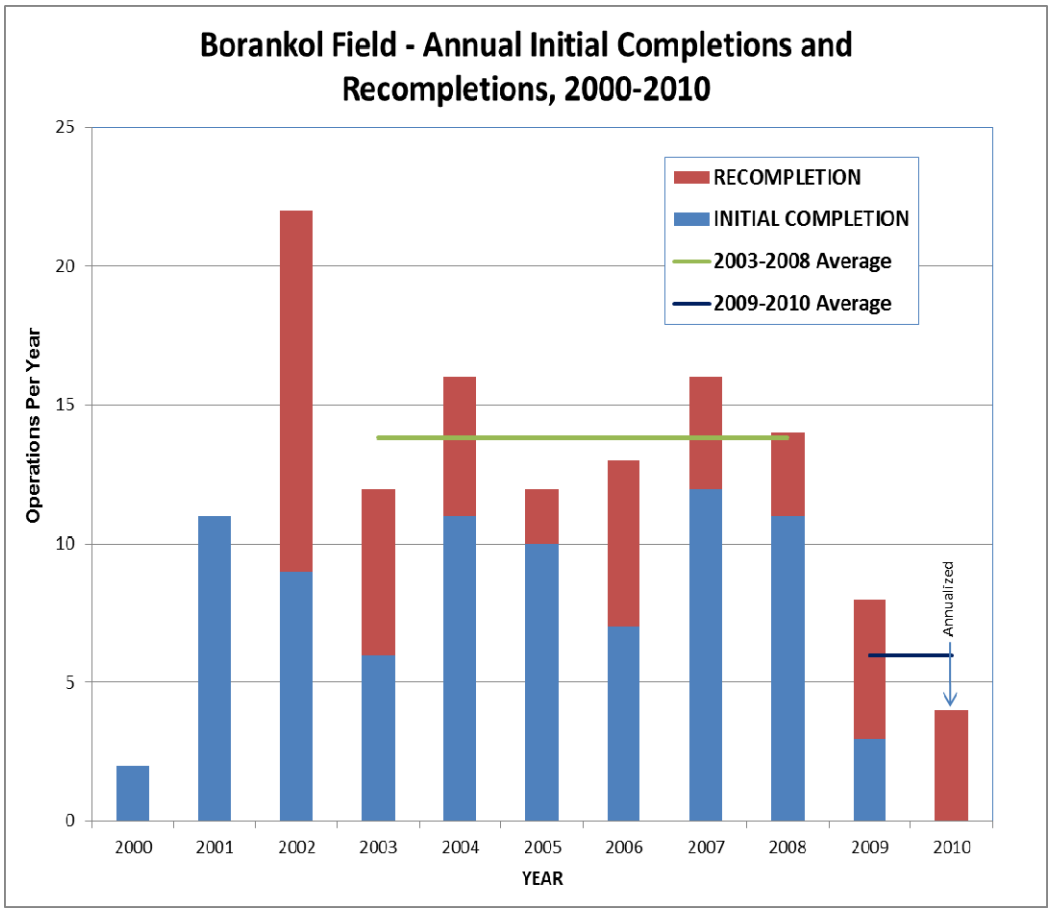
460. In the present case, there was a steep decline in Borankol production in the 2009 to 2010 time period. This production decline is not explained by depletion of the reservoirs.[660] Rather, this decline resulted from the pronounced reduction in field completion and workover operations in 2009 and 2010, which itself was a direct product of the State's campaign against KPM and TNG and Claimants' corresponding decision to minimize their exposure in the face of obvious risks.[661] This is demonstrated in the chart below:

[658] Third Ryder Scott Report ¶¶ 46-47.

[659] *Id.* at ¶¶ 50-51.

[660] *Id.* at ¶ 50.

[661] *See* First Post-Hearing Brief, *supra*, at III.B.



For the period 2003 to 2008, the annual number of operations in the field, initial completions plus recompletions, averaged 13.83.[662] For the period 2009 to 2010, they averaged only 6.[663]

461. As Ryder Scott points out, the resulting performance of the Borankol field was heavily influenced by those operational reductions — themselves a product of Kazakhstan's campaign — and they are a significant factor both in the observed Borankol production decline for the period 2009 to 2010, and in the declining oil cuts prior to Respondent's July 2010 valuation date.[664] Thus, GCA's estimates of future production through its chosen decline curve methodology do not take into account either the production aberrations in 2009 and 2010, or the enhanced production from a future re-commencement of completion operations. This renders GCA's decline curve prediction of total future production from operationally-hobbled 2009-2010 production inherently unreliable.

662 Third Ryder Scott Report ¶ 51.

663 *Id.*

664 *Id.*

462. GCA itself acknowledges that there was an operational curtailment in 2009 and 2010. However, it disingenuously attributes the curtailment to the 2007 Field Development Plan, while criticizing Ryder Scott for employing a rigorous volumetric analysis that eliminates the inherent flaws in GCA's own decline curve analysis:

> It is inappropriate to place such emphasis, as does RS, on the volumetric reserves estimates when historical performance tells a different story. RS's forecast is consistent with the base field decline rate up until October, 2008, which GCA believes is not representative, as this has been supported by a full development drilling programme. The actual decline rate since October, 2008 reflects a reduced drilling programme, as per the FDP and is, therefore, more representative.[665]

463. GCA's argument, however, flips causation on its head. GCA acknowledges that the 2007 Field Development Plan called for 45 new wells and 44 recompletions between 2007 and 2022, and that through the end of 2009, actual drilling and recompletion work was less than that called for in the Plan.[666] GCA then simply concludes, with no basis, that the reduction in operations beginning in 2009 was the result of a reduction in actual recoverable reserves rather than the cause of the decline in production over that period.[667] That conclusion, however, would require the kind of geophysical and volumetric analysis that GCA did not conduct. GCA identifies no geological reason why development work in the Borankol field slowed, and its reliance on reduced development efforts to minimize reserve estimates under a decline-curve analysis is exactly backwards.

464. Moreover, GCA compounded this error in its selection of methodology with errors in the actual calculation of its oil cuts.[668] An oil cut versus cumulative production methodology is based on the ratio of oil and water contained in historical production. As explained in depth in Ryder Scott's Third Report, GCA miscalculated that ratio because it used a conversion factor for the water component based on fresh water, when in fact the water in the Borankol field is salt water (which has a higher specific gravity than fresh water).[669]

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665 Second GCA Report ¶ 67.

666 Second GCA Report ¶ 65. GCA also recognizes that Field Development Plans are adjusted regularly to accommodate the inherent updates in knowledge concerning a field's recoverable reserves that accompany ongoing operations. Second GCA Report ¶ 8 ("Development plans must, therefore, have the flexibility to be revised and updated as new information becomes available.").

667 Second GCA Report ¶¶ 65-68.

668 Third Ryder Scott Report ¶ 48.

669 Third Ryder Scott Report ¶ 48.

The net effect of this error is that each of GCA's calculated oil cut values is too low, thereby understating the recoverable quantities of oil from existing wells by 15%.[670]

465. GCA's purported "type well" analysis of behind-pipe reserves fares no better. As best Claimants and Ryder Scott can tell, this alleged analysis consisted of GCA's imagining of a single hypothetical "type well" from undisclosed historical production data, and then extrapolating potentially recoverable behind-pipe reserves for all of the actual wells in the Borankol field from this one hypothetical well.[671] GCA did not disclose the assumed characteristics of this hypothetical well, or provide any of the data or computations by which it arrived at those characteristics.[672] Indeed, apart from GCA's bare assertion, the record contains no evidence that GCA actually conducted a type well analysis at all. This "take my word for it" methodology fails any credibility test.

466. Moreover, even assuming GCA actually did perform a type well analysis, that methodology is highly flawed because it wrongly assumes that all wells are created equal. This is a basic error in GCA's hyper-simplistic, field-wide methodology. In fact, different wells have vastly different potential for behind-pipe reserves due to variations in what reservoirs remain to be recompleted and when. As Ryder Scott explains, a prudent operator generally completes wells "up the hole," exhausting production in lower reservoirs before moving up to complete higher reservoirs.[673] In Borankol, a number of wells have substantial behind-pipe reserves in higher reservoirs that have not been touched at all because those wells are still quite productive in lower reservoirs.[674] On the other hand, other wells in shallower parts of the field (*i.e.*, on the edge of the reservoirs) have been recompleted already with relatively little productivity.[675] Imagining a hypothetical type well based on historical field-wide production — which includes production from marginal wells on the edge of the reservoir — says essentially nothing about the potential behind-pipe reserves for wells in more productive parts of the reservoir that have never been recompleted.[676] This is exactly why a well-by-well analysis is required, and a field-wide analysis is deficient.

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[670] Third Ryder Scott Report ¶ 48.
[671] Third Ryder Scott Report ¶ 48.
[672] Third Ryder Scott Report ¶ 52.
[673] Third Ryder Scott Report ¶¶ 57-58.
[674] Third Ryder Scott Report ¶ 58.
[675] Third Ryder Scott Report ¶ 57.
[676] Third Ryder Scott Report ¶ 58.

467. Unlike GCA, Ryder Scott performed a well-by-well analysis. In brief, as Mr. Latham explained, Ryder Scott used its net isochore maps for each reservoir zone to identify specific well candidates for recompletion.[677] Allocation of remaining reserves to those wells was based on identified reservoir thickness (or "net pay"), and the structural position of the candidate in the reservoir. Ryder Scott identified when specific well bores would become available for recompletion over the remaining life of the contract based on its projection of when the well would exhaust production from lower reservoirs. As explained by Mr. Latham, Ryder Scott then constructed a well-by-well grid summarizing the available and unavailable well bores.[678] This is exactly what a prudent operator would do to maximize recovery from the lower J-VII reservoir before recompleting geologically isolated upper zones.

468. Ironically, Kazakhstan criticized Ryder Scott's thorough behind-pipe analysis by displaying a graph of behind-pipe estimates,[679] and claiming that:

> Ryder Scott also overestimate the potential of the so-called behind-pipe reserves. These are reserves that can be reached by using an existing well, sealing off some of its deeper levels and using it to access shallower parts of a reservoir.[680]
>
> [T]his graph shows nicely the bump that Ryder Scott assume in the later years. This bump stems from the recompletions that Ryder Scott incorrectly assumes to perform strongly.[681]

469. That is exactly backward. Ryder Scott correctly assumed that those recompletions would perform strongly based on its thorough geological analysis of the reserves in the untapped higher-lying reservoirs. There is nothing unusual about the "bump" in Ryder Scott's production profile because a prudent operator would exhaust production from existing completions in declining zones before moving into those higher zones that have more remaining productivity.[682] As Mr. Latham explained (with respect to Kazakhstan's graph):

> The field decline, which in this case showing roughly around 2009, that you see between 2008 and 2013, is largely reflective of natural decline of the existing producing wells, augmented by a comparatively small number of recompletions during that

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677 Latham Testimony, Tr. January 2013 Hearing, Day 3, 116:11-118:14.

678 Latham Testimony, Tr. January 2013 Hearing, Day 3, 116:11-118:14.

679 Respondent's Opening Presentation on Quantum, January 2013 Hearing, Slide 53.

680 Respondent's Opening Statement, Tr. January 2013 Hearing, Day 1, 150:1-5.

681 Respondent's Opening Statement, Tr. January 2013 Hearing, Day 1, 160:7-11.

682 Third Ryder Scott Report ¶ 58.

> timeframe, averaging about three per year. However, in 2014, as the existing completions declined to marginal rates, there is an increase in the number of work-overs going over between the period 2014 and 2017, averaging seven and a half a year. The increase in production is just a natural extension of a prudent operator's plans to maximize recovery in the reservoirs.[683]

470. GCA incorrectly assumed that recompletions would not perform strongly because it based its type well on the historical performance of wells in less productive parts of the reservoir. Because GCA did not schedule any individual wells for recompletion, and did not identify by well, location, or targeted formation any of the summary 43 recompletions it assumed in its second report,[684] GCA's production profile reflects a fictional decline curve that no prudent operator would ever expect to see.

b. Tolkyn Field

471. GCA's inclusion of a front-loaded capital expenditure for unnecessary compression drives down Deloitte GmbH's DCF valuation of the Tolkyn field substantially. In its first report, GCA claimed that there would be a need for compression in the Tolkyn field beginning in 2012, providing scant justification,[685] resulting in a projected US $40 million capital expenditure in 2011.[686] As Mr. Wood made clear at the Quantum Hearing, GCA is perfectly aware of the value-suppressing effect front-loaded capex has on a DCF calculation:

> Q. Do you know the impact that the acceleration of capital cost has on a DCF model?
>
> A. I am very well aware of that, yes.[687]

472. GCA concedes in its second report and in testimony that no such compression was actually installed in 2011, and none has been installed to date.[688] Ryder Scott also has explained that no one would have expected such compression to be required in the Tolkyn field as of October 2008 or July 2010.[689] GCA persists in assuming that a requirement for such compression would have been expected at its July 2010 valuation date, based primarily

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683 Latham Testimony, Tr. January 2013 Hearing, Day 3, 118:24-119:11.

684 Latham Testimony, Tr. January 2013 Hearing, Day 3, 119:12-17.

685 First GCA Report ¶ 26. In its first report, GCA says only: "Due to declining reservoir pressure, compression will be needed in the field from 2012. This is required to boost the flowing wellhead pressure to a level adequate for processing and onward transport of the gas."

686 First GCA Report, Appendix III, Table AII.1 and note 1.

687 GCA Testimony, Tr. January 2013 Hearing, Day 3, 218:3-5.

688 Second GCA Report ¶ 41; GCA Testimony, Tr. January 2013 Hearing, Day 3, 253:16-254:5.

689 Second Ryder Scott Report at 4-5; Third Ryder Scott Report ¶ 45.c(i); Latham Testimony, Tr. January 2013 Hearing, Day 4, 5:7-6:17, 10:24-11:22.

on the fact that the 2007 KazNIPIMunaiGas Field Development Plan contemplated the installation of compression at Tolkyn in 2012. GCA attempts to leave the impression that a plan for installation of compression in a State Development Plan mandates its installation, but GCA has admitted that Field Development Plans are freely amended to accommodate changes in the requirements of a field.[690] No prudent operator or buyer of the Tolkyn assets would plan to spend millions on compression that it concluded was unnecessary simply because it was contemplated in a dated Field Development Plan.

473. Moreover, that argument plainly demonstrates GCA's penchant for cherry-picking assumptions to increase costs while decreasing production estimates. As GCA acknowledges, the rationale for the installation of compression in the 2007 Field Development Plan was an assumption about production rates that did not come to pass:

> The table on page 224 of the KazNIPIMunaiGas 2007 FDP demonstrates that at a plateau gas production rate of 2.5 BCM a year, by 2012 the pipeline inlet pressure at Tolkyn would be c 85 bar with an arrival pressure at Borankol of only c 19 bar. Compression would have been required at this point to maintain flow through both the pipeline and processing facilities, i.e. necessitating the installation of compression during 2011 in order to meet the shortfall in 2012. Actual operating conditions by mid 2010 were such that a gas production rate of 2.5 BCM a year was no longer practical. This might have deferred the need for the compression beyond 2011, but there would still be a requirement for it.[691]

Thus, GCA acknowledges that by its valuation date, the production assumptions on which the 2007 Field Development Plan based its expectation of a need for compression in 2012 were no longer valid. Moreover, as the following table illustrates, GCA's projections of future production are well below those in the Field Development Plan.[692]

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690 Second GCA Report ¶ 26 ("Compression is also part of the 2007 development plan ... which RS has failed to acknowledge.").

691 Second GCA Report ¶ 34 (emphasis added).

692 Second GCA Report, Table AII.1.

	GCA[693]		2007 Field Development Plan[694]	
	Gas (MMm^3)	**Condensate and Oil (Mtonnes)**	**Gas (MMm^3)**	**Condensate and Oil (Mtonnes)**
2011	1152	146.7	2500	153
2012	1088.7	123.3	2500	136
2013	851.6	88.3	2284	137
2014	668.8	60.9	1888	131
2015	533.4	44.4	1455	121
2016	430.2	33.9	985	91
2017	339.6	26.1	479	46
2018	268.7	20.2	226	22

Clearly, GCA only relies on the 2007 FDP when it is beneficial to increase cost assumptions, but ignores that plan's expected production profile.

474. Ryder Scott, on the other hand, correctly analyzes both the production profile and the need for compression at Tolkyn independently as of its October 14, 2008, valuation date. By that time, operating conditions at Tolkyn had changed, which resulted in an amendment to the Field Development Plan for 2009 shortly thereafter that reduced targeted annual production from 2.5 BCM to 1.8 BCM.[695] Ryder Scott's production projection is based on the data available in October 2008, and is significantly lower than the production projection in 2007 Field Development Plan. And consistently, Ryder Scott analyzes the need for compression (or lack thereof) based on the data available at that time, rather than data from the 2007 FDP that no longer was relevant. In short, the original 2007 Field Development Plan is simply irrelevant to any consideration of whether compression is a future requirement in the Tolkyn Field as of October 2008, much less July 2010.

693 Second GCA Report Table AII.1

694 2007 Tolkyn Field Development Plan, at 224, C-681

695 *See* 2010 State inspection minutes § 5, C-599. ("In 2009, within the ordinary report on the author inspection for the implementation of the exploitation project, amendments have been operated concerning the natural gas and condensate gas extraction volumes from the Artinskian condensate gas deposit of the Republic of Kazakhstan (Protocol of ṬKR No. 59/October 1st, 2009). The takeover rate was reduced from 2.5 billion m3/year to 1.8 billion m3/year. Cause: complications generated by the sustained rate of gas capture from the deposit (flooding and others). The named reduction of the extraction volumes applied for the period 2009 – 2010, until the elaboration of a new design document.")

475. GCA's fall-back position is that flowing tube pressures extant in July of 2010 indicate that some compression will be required at some point in time. That is, of course, no justification at all for its projection of US $40 million in compression capex in 2011. It is also factually wrong. As Ryder Scott points out in its Third Report:

> As of 14/10/2008, only three of the Artinskian producing wells exhibited any material water production. All of the remaining wells were producing with high flowing tubing pressures. As of 21/7/2010, several additional wells exhibited high water production, but the remaining nine wells were more than capable, flowing with pressures of 131-151 bar, far in excess of the minimum pipeline delivery requirements.[696]

A prudent operator would not install expensive compression to marginally assist wells that already were producing poorly while the most productive wells in the field did not need any pressure support at all.

476. GCA conceded this point at the Quantum Hearing, with Mr. Goodearl testifying that:

> If we look at the flowing wellhead pressures as at July 2010, of the wells that had pressures reported on them, Mr. Latham was correct in stating that there were relatively fewer of those wells which were approaching the wellhead pressure limits. The majority of the wells were still producing at a little over 100 bar.[697]

477. That concession effectively ends any debate concerning the need for compression in 2012, and certainly removes from any calculation of costs for the Tolkyn field a US $40 million capex expenditure for unnecessary compression in 2011.

c. Munaibay Oil

478. To assess the Munaibay Oil resources, Ryder Scott analyzed the available seismic data, conducted an independent petrophysical and geophysical analysis of the area, analyzed the well logs and the test well results from the Munaibay #1 test well, and separately analyzed two additional zones that had been identified but not tested by the Munaibay #1 test well.[698] From its thorough analysis, Ryder Scott projected a total recovery of 53.285 MBbls of oil, and a need for a total of 75 development wells and one exploration well.[699]

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696 Third Ryder Scott Report ¶ 42, and Table 3.

697 GCA Testimony, Tr. January 2013 Hearing, Day 4, 6:23-7:3.

698 Third Ryder Scott Report, Exhibit 16; Tr. January 2013 Hearing, Day 3, 105:23-106:21, 109:7-18.

699 First Ryder Scott Report, Exhibit 12; First FTI Report, Exhibit J.

479. By contrast, GCA's analysis of Munaibay Oil clearly demonstrates its careless, finger-in-the-wind methodology. In its first report, GCA projected total recovery of 41.6 MBbls of oil from the area requiring a total of 13 wells (one appraisal well and twelve development wells).[700] Based on that well count, GCA projected total capex of US $218 million, total opex of US $53 million, and exploration costs of US $21 million. In its second report, however, GCA more than quadrupled its projected well count to 53 wells (one appraisal well and 52 development wells), but reduced its projection of total recovery by 29% (to 29.8 MBbls of oil).[701] Its new development plan — more wells for less oil — increased its projected total capex to US $828 million and total opex of US $188.5 million (increases of 379% and 356% respectively).[702]

480. Not surprisingly, this massive increase in projected cost and sizeable decrease in projected production summarily wiped out the US $68 million in value that Deloitte TCF had originally attributed to Munaibay Oil based on GCA's first report. The only explanation that GCA gave for this monumental change was as follows:

> GCA has adjusted its assessment of the Munaibay Oil discovery based on further analysis of well performance. ... The Munaibay-1 well tested oil and gas over a number of intervals, but only one tested oil at commercial rates of about 60 m^3/day. This is considerably less than rates assumed in the GCA November, 2011 report, and this has been adjusted accordingly.[703]

481. GCA does not state specifically what it overlooked in its analysis of the well-test results in its first report. There is no indication that it reviewed or analyzed any of the well logs, did any seismic analysis, or performed any petrophysical or geological analysis. And consistent with its overall practice, GCA produced no documentation or data whatsoever to support either its first projections or its revisions to those projections.[704] At the Hearing on Quantum, GCA added to that scant record of analysis only that it had reviewed "some of the older Triassic reservoirs … in the Tolkyn field."[705] That is not an analysis designed to yield any kind of reliable projections.

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700 First GCA Report, Tables AIII.9 and AIII.4

701 Second GCA Report ¶ 124 and Table AIII.4.

702 Second GCA Report Table A.III.4.

703 Second GCA Report ¶ 123.

704 *See* Third Ryder Scott Report ¶ 64.

705 GCA Testimony, Tr. January 2013 Hearing, Day 3, 184:6-8.

482. Furthermore, GCA compounded that error by baselessly front-loading the development costs while delaying the assumed production and revenues. Comparing the capex schedule in Table AIII.4 with the drilling schedule in paragraph 124 of GCA's second report, it is apparent that GCA projects all capital cost to be spent by 2018, while wells continue to be drilled until 2022 and production does not peak until 2023.[706] Mr. Wood confirmed this at the Quantum Hearing:

> Q. And you look at the years 2019-2022 where you have 16 wells being drilled; do you see that?
>
> A. Yes.
>
> Q. You see no capital cost; correct?
>
> A. Not at that time, no.
>
> Q. So you've accelerated $220 million plus of capital costs into the earlier years; correct?
>
> A. It does look on inspection that that is the case.
>
> Q. Do you know the impact that the acceleration of capital cost has on a DCF model?
>
> A. I am very well aware of that, yes.
>
> Q. So the DCF model prepared by Deloitte, depending upon your appendix to your second report, obviously overstates capital cost in earlier years and therefore deflates the value of my client's business; correct?
>
> A. Yes, it does appear that I have continued the cost profile at six wells per year rather than dropping to four, and have chopped it off four years early.[707]

483. That front-loading of US $220 million in capital expenditures is further exacerbated by an inexplicable projection that no oil whatsoever, and hence no revenue, would be produced from Munaibay Oil until 2014, despite what GCA called the "pre-drilling" of 12 development wells in 2012 and 2013 at a cost of US $159.6 million.[708]

484. These wild swings in GCA's analysis without any satisfactory explanation strongly suggest that GCA simply manipulated its numbers to drive the value of Munaibay Oil below zero. Even if that is not the case, these unexplained swings demonstrate that GCA's analysis is too suspect to form the basis for a damages calculation in this case.

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[706] Second GCA Report ¶ 124 and Table A.III.4.

[707] GCA Testimony, Tr. January 2013 Hearing, Day 3, 217:19-218:13.

[708] GCA Testimony, Tr. January 2013 Hearing, Day 3, 220:3-12; Second GCA Report ¶ 124 and Table A.III.4.

d. Interoil Reef

485. With respect to the Interoil Reef, GCA assumes a protracted and unreasonable exploration schedule that, by design, could not be accomplished by the exploration deadline of March 2011. Most importantly, GCA assumes that additional 3D seismic was required to assess the prospect before drilling, despite the existence of ample 3D coverage on which to base an exploration drilling decision. At the Quantum Hearing, GCA attempted to justify that delay based on the possible presence of toxic gases in the reef structure, arguing that "a prudent operator would not drill such a feature, with potentially extreme pressures and toxic gases, without acquiring the best possible dataset on which to make its assessment."[709] That is a red herring. TNG already had a good 3D seismic survey over the location of the optimal site for the Munaibay-3 exploration well, and additional 3D over the small portion of the Reef structure that extended outside the Contract 302 territory would not have provided any additional information about the makeup of the gas in the Reef, or how to drill the Munaibay-3 well. As Ryder Scott concludes in its Third Report, assuming that TNG had been able to use the deep-drilling rig that Claimants acquired in 2008, there were no safety or engineering obstacles to drilling an exploratory well to the Interoil Reef structure immediately.

486. Conducting additional 3D seismic on the small portion of the reef structure outside the Contract 302 boundary might have provided additional information about the closure of the trap on that edge of the Reef. But as Ryder Scott explains, trap risk is not the main geological risk driving uncertainty regarding the prospectivity of the Reef. The main risk is reservoir risk (*e.g.*, porosity of the rock), and drilling a well is the only way to test that.[710] Thus, an operator faced with a deadline plainly would drill an exploration well rather than conduct additional seismic of limited utility that would risk blowing the deadline to make a commercial discovery.[711]

487. GCA, and hence Deloitte, also build into their respective evaluations of the Interoil Reef prospect a 100% chance that significant H_2S contamination is present in the reef gas.[712] GCA acknowledges that it does not know whether the reef gas contains H_2S (*i.e.*, the

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[709] GCA Testimony, Tr. January 2013 Hearing, Day 3, 228:13-20.

[710] Third Ryder Scott Report ¶ 29.

[711] Mr. Wright of GCA acknowledged at the Quantum Hearing that the decision of when to drill an exploration well lies in the discretion of the operator, and that an operator facing a deadline would have a strong incentive to drill the well as soon as possible. *See* GCA Testimony, Tr. January 2013 Hearing, Day 3, 228:13-20.

[712] GCA Testimony, Tr. January 2013 Hearing, Day 3, 183:4-7.

gas is "sour"), and only opines that it is "likely."[713] GCA and Deloitte GmbH, however, then model the cost assumptions for developing the Reef prospect based on a 100% certainty of H_2S contamination. Infrastructure cost attributable to H_2S contamination accounts for nearly half of the US $2 billion in expected capex in GCA's development model.[714] There are at least three fatal problems with this approach.

488. First, the geological basis for GCA's opinion that gas in the reef structure "likely" is sour is highly suspect. GCA supports this position by analogy to the Kashagan and Tengiz fields.[715] As Ryder Scott explains, however, those fields, located 140 and 45 kilometers from the Interoil Reef prospect (respectively), do not provide a reliable basis for GCA's assumptions.[716] The source rocks for H_2S generation form in very specific environments and are not typically widespread.[717] Although H_2S-generating source rocks appear to be prevalent in certain parts of the Pre-Caspian Basin, there is no reason to believe that they are equally prevalent in other parts of the basin, which are likely to have had significantly different environmental conditions at the time of deposit. Thus, it is more important to look at local data than data from more distant sources in trying to assess the likely composition of gas that may be trapped in the Interoil Reef structure.[718] The target for the Interoil Reef prospect is a pre-salt carbonate similar in geologic age and seismically analogous to the Artinskian Dolomite in the much closer Tolkyn field, which has an H_2S content on the order of 0.3%.[719] Although the Tolkyn Artinskian Dolomite is slightly younger in geologic age than the target for the Interoil Reef, it is difficult to understand how the gas from the Artinskian Dolomite at Tolkyn could have escaped H_2S contamination if a significant H_2S source was nearby.

489. Second, GCA again "cherry picks" assumptions in analogizing the Interoil Reef to the Tengiz and Kashagan fields. Those fields have markedly different fluid characteristics than the Tolkyn field, namely, a higher (and substantially more valuable) condensate yield.[720] In particular, GCA's primary analog, Tengiz, has a condensate yield in the range of 465 Bbl/MMcf of gas, while GCA projects only 60 Bbl/MMcf of gas for the

[713] Second GCA Report ¶ 111; GCA Testimony, Tr. January 2013 Hearing, Day 3, 182:24-183:5.
[714] Second GCA Report, Table A.III.1; Tr., January 2013 Hearing, Day 3, 202:1-14.
[715] Second GCA Report ¶¶ 103, 108.
[716] Third Ryder Scott Report ¶ 32.
[717] Third Ryder Scott Report ¶ 31.
[718] Third Ryder Scott Report ¶¶ 32-3.
[719] Third Ryder Scott Report ¶ 32.
[720] Third Ryder Scott Report ¶ 36.

Reef. GCA thus analogizes the Interoil Reef to Tengiz for purposes of projecting high concentrations of contaminants but completely ignores the revenue-enhancing aspects of the that field. There is no rational, geologic basis for drawing such a distinction. As Ryder Scott and FTI explain, that is a significant oversight that, if corrected, could add a billion dollars or more of present-value revenues to Deloitte GmbH's DCF model for the Reef.[721] Ryder Scott reasonably concluded that Tolkyn is the closest analog for estimating the composition of the Interoil Reef gas, and consistently modeled both the likelihood of contaminants and the condensate yield on Tolkyn gas.[722] If GCA thinks Kashagan and Tengiz are closer analogs, it must take the good with the bad.

490. Third, it is not reasonable to build a DCF model around a 100% certainty of H_2S contamination when GCA acknowledges that such contamination is not certain, and only opines that it is likely. In light of the suspect basis for GCA's opinion and the fact that Kazakhstan's illegal conduct is the reason why TNG could not drill the exploration well that would conclusively demonstrate the quality of the gas, it is far more reasonable to assume that the gas is not sour. But at a minimum, in light of the huge cost impact of this assumption, GCA and Deloitte GmbH should have developed alternative weighted scenarios that more accurately reflect this uncertainty. That is precisely what Deloitte GmbH did with gas export uncertainty (albeit incorrectly, as discussed below). The failure of GCA and Deloitte GmbH to do the same with respect to this major uncertainty is unjustifiable.

3. Deloitte GmbH Compounded GCA's Errors With Unsupportable Assumptions and Methodology Errors of Its Own

491. As described above, Deloitte GmbH's wholesale reliance on GCA for its production and cost assumptions means that the reliability problems plaguing GCA's work infect Deloitte GmbH's conclusions as well. Deloitte GmbH, however, compounds those problems with several serious errors of its own. Some of the errors in Deloitte GmbH's analysis are discussed in Section V.C below, in response to Kazakhstan's criticisms of FTI's valuations. Also, the Third Report of FTI — which was FTI's first opportunity to comment on Deloitte GmbH's work at all — discusses these various errors at length. This section will touch on only a few of the major flaws in Deloitte GmbH's work.

[721] Third Ryder Scott Report ¶ 36; Third FTI Report ¶¶ 8.10 - 8.18.

[722] Third Ryder Scott Report ¶ 36.

a. Deloitte GmbH's Unsupportable Gas Pricing Assumptions

492. FTI made the reasonable assumption that, as of October 14, 2008, a willing buyer of TNG would expect the company to be able to sell gas on the export market, and to acquire prevailing international export prices for those sales. TNG had the contractual right to export gas under the terms of its Subsoil Use Contract,[723] and there had been a lengthy negotiation beginning in May 2007 for a three-party contract between TNG, KMG, and KazAzot (the "Tripartite Agreement") that explicitly provided for both TNG gas exports and payment of prevailing export prices.[724] Pursuant to the terms of the Tripartite Agreement, TNG would have sold a portion of its gas to local industrial users, a portion to KazAzot at a premium to domestic prices, and a portion to KMG, to be exported via KazTransGas and paid for at prevailing export prices.[725] The history of the State's active pursuit of this Tripartite Agreement provided every indication that gas exports at international export prices were an imminent development in 2008.[726]

493. The assumption that TNG would receive international export prices is also directly reflected in the indicative offers that Claimants received for TNG's Tolkyn field in the initial round of Project Zenith.[727] Among the initial round of indicative offers received by Claimants, the Tolkyn field as a segregated component was valued by KNOC at US $1,067 million on an enterprise value basis, by OMV Exploration & Production GmbH at US $952 million on an enterprise value basis, and by Total at US $730 million on an equity basis using DCF methodology. The magnitude of these offers indicates that they certainly contemplated receipt of export prices for TNG's gas as a critical component.

494. Kazakhstan argues that FTI's approach is unreasonable because TNG had only sold gas to domestic purchasers in the past, the only pipeline for exporting Kazakh gas ran through Russia, and Russia constrained the price and volume of gas exported from Kazakhstan. It has failed to recognize, however, the rapidly changing gas market in Kazakhstan in 2008. At that time, the increasing demand for gas was breaking Russia's monopolistic stranglehold on the export of Kazakh gas. As noted by the Oxford Institute for Energy Studies published in November 2008:

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723 *See* Contract No. 210 § 6, ¶ 6.1.12, C-52.

724 *See* First FTI Report ¶¶ 5.21-5.34; Statement of Claim ¶¶ 57-61.

725 *See* First FTI Report ¶¶ 5.26, 5.30, 5.31.

726 *See* Statement of Claim ¶¶ 57-61.

727 *See* Second FTI Report ¶ 6.10.

> The ever-increasing interest of Beijing, Washington and Brussels in securing Central Asian energy supplies as an alternative (mainly to Russian and Middle Eastern/African sources) has prompted Moscow to offer greater incentives to Kazakhstan, and other Central Asian producers, to ship their oil and gas through Russian territory instead. It is thus unsurprising that Russia has already agreed to pay European prices (minus transport and other related costs) for Central Asian gas from 1 January 2009. Kazakhstan estimates that the result of these arrangements will be 60–70% gas price increases from the 2008 level of $180 per thousand cubic metres ($/mcm) to $306/mcm in January 2009. However, future export prices for Central Asian gas will depend on the volatility of oil markets. … Starting in January 2009, Central Asian gas will be sold to Russia at 'European prices.'[728]

495. Deloitte GmbH quotes that very passage in its report,[729] but nevertheless negates the proper conclusion to be drawn from it by creating a weighted average estimate of three scenarios premised on whether TNG would be able to export gas at all. Deloitte GmbH's scenarios are:

> 1) A "contract scenario," which assumes that TNG would continue selling all of its gas under the same commercial terms as its existing contracts, despite the dramatic changes opening up the market for the export of Kazakh gas. Deloitte purportedly estimated this scenario as 65% of its weighted average.[730]
>
> 2) A "transition scenario," which gradually increases prices to netback export prices over a 10-year period. Deloitte purportedly estimated this scenario at only 30% of its weighted average.[731]
>
> 3) An "export scenario," which assumes that TNG would sell 80% of its gas at export prices and 20% of its gas domestically at all times. Deloitte purportedly estimated this scenario as only 5% of its weighted average gas price.[732]

496. Deloitte GmbH had originally assigned entirely different weighted averages to those scenarios, but evidently at the instruction of Kazakhstan, re-weighted the averages to reduce the probability that TNG would be able to export any of its gas at all. The original tables by which Deloitte calculated those three scenarios (Exhibit 3 to Deloitte's report)

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728 *Shamil Midkhatovich Yenikeyeff*, Kazakhstan's Gas: Export Markets and Export Routes, Oxford Institute for Energy Studies, at 15, 38-9 (November 2008) (emphasis added), C-674. Indeed, Kazakhstan became a net exporter of gas in 2009, with exports exceeding imports by 134 Bcf. *See* EIA Country Report, Kazakhstan Energy Data, Statistics, and Analysis - Oil, Gas, Electricity, Coal (November 2010) at 6, FTI First Scope of Review No. 99.

729 Deloitte GmbH Report ¶ 80.

730 Deloitte GmbH Report ¶¶ 243-48.

731 *Id.*

732 *Id.*

contained weighted averages of 50% for the contract scenario, 25% for the transition scenario, and 25% for the export scenario.[733] When those three scenarios found their way into the body of the report, however, they had been altered to the 65%, 30%, and 5% averages to drive down the estimates of future gas sales revenue by TNG, and concomitantly the value of the Tolkyn field.[734] Mr. Gruhn matter-of-factly acknowledged those rather dramatic changes at the Hearing on Quantum, offering no explanation for them.[735]

497. Mr. Gruhn also acknowledged that Deloitte TCF had assumed a 100% chance of what Deloitte GmbH classified as the transition scenario based on Deloitte TCF's review of a Kazakh Ministry of Oil and Gas (MOG) plan. Consistent with Kazakhstan's practice in this case of secreting key information, Deloitte TCF never produced that MOG plan, and remarkably, Mr. Gruhn testified as follows about the Deloitte TCF gas pricing estimate and the mysterious MOG plan:

> Q. And Deloitte TCF assumed — that was their only scenario; they attributed 100% to that scenario?
>
> A. Yes. To my greatest surprise, actually, because I was not able to really find this MOG plan.
>
> Q. Did you ask?
>
> A. Oh, yes, I did.
>
> Q. You were unable to find out who authored that report, so I guess you were unable to find the explanation for why your colleagues in Kazakhstan assumed that that was the appropriate gas price forecast?
>
> A. At the time they felt this was a plausible — perhaps the most plausible — assumption.[736]

In short, Mr. Gruhn ignored the opinions of his Kazakh colleagues about the Kazakh gas market that were based on Kazakh government sources that he never saw, without even consulting his colleagues.

498. Even more remarkably, Deloitte GmbH completely ignored the gas pricing assumptions made in connection with the 2009 RBS Asset Assessment, despite, as noted above, having it in its possession and citing it in its report. The RBS Assessment, as Claimants correctly presumed, bases its gas pricing assumptions entirely on a scenario in

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733 *Id.* Exhibit 3.

734 *Id.* ¶ 248.

735 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 131:23-133:21.

736 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 130:9-20.

which 80% of all of TNG's gas would be sold on the export market, and 20% would be sold on the domestic market.[737] The different valuations of the Tolkyn field that the RBS Assessment reaches, ranging from US $527 million to US $765 million, are based on different export prices that the companies could be presumed to receive, not on whether TNG would be able to export gas.[738]

499. The RBS Asset Assessment is fatal to Deloitte GmbH's 5% weighting of its "expert scenario," which is undoubtedly one of the principal reasons Kazakhstan violated the Tribunal's orders and withheld the RBS Assessment for so long. That is also no doubt why Kazakhstan had to turn to its political scientist, Professor Olcott, to offer an "expert" opinion on Kazakh gas exports and pricing, and why Deloitte GmbH apparently was instructed to remove all references to the RBS Assessment from its report (which it goofed), despite clearly having relied on the RBS Assessment at one stage of drafting its report.

500. Kazakhstan and its experts have no credibility on this issue. The Tribunal should adopt FTI's reasonable assumption, based on the Tri-partite Agreement that was signed by KMG as well as other evidence in the record, that a buyer of TNG in 2008 would have expected the company to be able to sell gas on the export market and to obtain prevailing international export prices for those sales. The fact that RBS made the same assumption in 2009 strongly corroborates that conclusion.

b. Deloitte GmbH Fails to Consider Other Valuation Evidence and to Test Its Conclusions Using Other Valuation Methods

501. Perhaps most importantly, Deloitte GmbH wholly ignores substantial other evidence of the value of the very same assets, including two complete valuations performed by other valuation experts, Deloitte TCF and RBS. Likewise, Deloitte GmbH fails to test its conclusions based on DCF models using other valuation methods, such as a market method.

502. These failures are inconsistent with accepted industry practices for a valuation expert. As explained in FTI's third report, the valuation industry broadly recognizes standards that require valuation experts to consider other valuations of the same assets and explain any material differences. For example, the Canadian Institute of Mining, Metallurgy, and Petroleum has published standards regarding the valuation of mineral properties. Paragraph 8.5 of the CIMVAL standard reads:

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[737] RBS 2009 Asset Valuation, July 31, 2009, slides 36-37, C-723.

[738] RBS 2009 Asset Valuation, July 31, 2009, slides 36-37, C-723.

> The Valuation Report must specify the Valuation Date and refer to all previous Valuations of the subject Mineral Property within the last twenty four months and explain any Material differences between them and the present Valuation.[739]

Similar requirements are found under the South African Mineral Asset Valuation Code and the valuation code of the Australasian Institute of Mining and Metallurgy.[740] "While these valuation standards are not binding for the purposes of this arbitration, they are broadly observed in the mining and petroleum markets and have been adopted by both securities regulators and stock exchanges in their respective jurisdictions."[741]

503. Similarly, it is important to test the results of a DCF model against other indicators of value in the market. The quality of a DCF model and the conclusions that can be drawn from it are directly related to the quality of the inputs. Therefore, while a DCF valuation may be precise if the quality of the inputs is high, it is important to test the conclusions reached against other indicators of value in the market.

504. Unlike FTI, Deloitte GmbH in this case did not consider and explain other relevant valuations, or test its conclusions against other indicators of value in the market. Deloitte GmbH has not explained its failure to follow these broadly-recognized standards of valuation, and as shown below, the only reasonable conclusion is that other evidence of value confirms that its DCF valuation is an extraordinary outlier.

i. Deloitte TCF Valuation

505. As the Tribunal is well aware, Kazakhstan has made every effort to distance itself from the valuations contained in the Deloitte TCF report, which Kazakhstan submitted along with its Statement of Defense. Kazakhstan refused to present anyone at the Hearing on Quantum to be cross-examined about the contents of that report,[742] and in correspondence to the Tribunal, Kazakhstan represented that "[n]o findings of Deloitte TCF were relied upon by Deloitte GmbH," and that "[t]here is no interdependency between the Deloitte TCF and Deloitte GmbH report…."[743] The testimony of Thomas Gruhn of Deloitte GmbH at the Hearing on Quantum confirmed that Kazakhstan has abandoned the Deloitte TCF report. Mr.

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739 Third FTI Report ¶ 8.168.

740 Third FTI Report ¶ 8.169.

741 Third FTI Report ¶ 8.169.

742 *See* Respondent's letter to the Tribunal dated December 10, 2012, in which Respondent refused to present any representative of Deloitte TCF to testify at the Quantum Hearing, and stated in no uncertain terms that it would instead present only one of the authors of the Deloitte GmbH report.

743 *See* Respondent's letter to the Tribunal dated December 13, 2012.

Gruhn testified that the Deloitte GmbH report was "a completely independent valuation;"[744] that he had no contact with, nor received any work files from, Deloitte TCF;[745] that he did not know who the author of the Deloitte TCF report was;[746] and that he could not confirm whether anyone at Deloitte TCF even authored the report bearing its company logo.[747]

506. Setting aside the mystery surrounding the Deloitte TCF report — which calls into question whether Kazakhstan acted in good faith in submitting it in the first place — Deloitte GmbH is not free as an independent valuation expert simply to disregard that report. There are numerous differences between the Deloitte TCF and Deloitte GmbH valuations, and it was incumbent on Deloitte GmbH to explain the basis for those differences.

507. Deloitte GmbH does purport to comment on the differences between its report and that of Deloitte TCF in Appendix II to its report. That appendix, however, merely identifies the differences without explaining the rationale for the different assumptions. For example, on the issue of gas pricing, Deloitte GmbH merely states, "[w]e have applied three different gas price scenarios to our valuations ("Contracts" with a weighting of 65%, "Transition" with a weighting of 30% and "Exports" with a weighting of 5%) as discussed above."[748] That does not explain why Deloitte GmbH rejected the assumptions made in a prior valuation by its Kazakh colleagues.

508. Another stark difference between the Deloitte reports is Deloitte TCF's recognition that the LPG Plant has any value at all, attributing to it US $24 to $32 million in scrap value.[749] Deloitte GmbH asserts that it did not calculate a scrap value because "no sufficiently detailed information was available to us allowing a precise calculation of the salvage value," but it does not explain why Deloitte TCF was able to calculate such a value based on (presumably) the same information.[750]

509. Another major difference between the two Deloitte reports is Deloitte TCF's explicit recognition that the Contract 302 Properties have significant value — albeit still grossly understated by Deloitte TCF. The Deloitte TCF report ascribed US $68 million to the

744 *See* Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 126:7-16.
745 *Id.*
746 *See* Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 125:20-126:1.
747 *See* Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 126:17-25.
748 Deloitte GmbH Report ¶ 468.
749 Deloitte TCF Report ¶¶ 9.22, 11.1, and Table 11.3.
750 Deloitte GmbH Report ¶ 463.

Munaibay Oil resources in Block 302, which Deloitte GmbH values at less than zero.[751] Deloitte TCF's conclusion was directly contrary to Kazakhstan's repeated, unfounded assertion in its Rejoinder on Quantum that the vast potential resources in the Contract 302 Properties could not be exploited economically and were completely worthless.[752]

510. The combined result of these differences, along with all the other "tweaks" between the Deloitte TCF and Deloitte GmbH valuations, was a reduction in the total calculation from US $229-237 million to US $186 million — a decrease of US $43-51 million, or approximately 20 percent. But this net result masks the gigantic swings in the NPV calculations between the two valuations because Deloitte GmbH "zeroed out" the net present value for any asset that it concluded had a negative NPV. This chart more accurately captures the extent of the swings from Deloitte TCF to Deloitte GmbH on the four assets that Deloitte TCF gave a positive value:

Differences in NPV Between Deloitte DCF and Deloitte GmbH			
Property	**Deloitte TCF**[753]	**Deloitte GmbH**[754]	**Difference in Dollars**
Tolkyn	US $121 million	US $123.2 million	Increase US $2.2 million
Borankol	US $16 million	US $62.8 million	Increase US $46.8 million
LPG Plant	US $24 to $32 million	US $ (89.1 million)	Decrease US $113.1 to $121.1 million
Munaibay Oil	US $68 million	US $ (297.7 million)	Decrease US $365.7 million
Total NPV	**US $229 to $237 million**	**US $(200.8 million)**	**Decrease US $429.8 to $437.8 million**
Total Deviation in NPV			**US $527.8 to $535.8 million**

[751] Deloitte TCF Report ¶ 11.4.

[752] Rejoinder on Quantum at 25-29.

511. As can be seen, Deloitte GmbH's NPV calculations on these four assets differed from Deloitte TCF's calculations by a total of US $527.8 - 535.8 million (with increases and decreases partially offsetting to a total reduction of US $429.8 - 437.8 million). That is a massive unexplained "miss" by one or both of these experts, and it renders both of their reports completely unreliable.

512. Kazakhstan obviously wants the Tribunal to disregard only Deloitte TCF's opinion as if that report never existed. That is the wrong conclusion. Such massive unexplained discrepancies between the two reports, which are based so thoroughly on opaque assumptions by GCA, show that both reports lack the rigor and integrity necessary to form the basis for a damages calculation in this case.

ii. RBS Valuation

513. Deloitte GmbH also completely disregards the highly relevant, contemporaneous 2009 RBS Asset Assessment, which RBS prepared for state-owned KMG E&P. The RBS Assessment is dated July 31, 2009, and has an effective valuation date of October 1, 2009 — less than ten months prior to Deloitte GmbH's July 2010 valuation date.[755] That valuation also came after the brunt of the price collapse and other market events that Kazakhstan claims independently devalued KPM and TNG. Additionally, the 89-page RBS Assessment was accompanied by, and cross-referenced against, a 388-page Legal Due Diligence report by Squire Sanders,[756] and a 175-page Financial, Tax and Environmental Due Diligence report by PriceWaterhouseCoopers.[757] Those reports represent a comprehensive review of KPM and TNG for which there is no comparable counterpart in the scant Deloitte GmbH scope of review.[758] Any reasonably diligent valuator would consider it as a matter of course, and, in accordance with common valuation standards, "explain any material differences" between that valuation and its own.

514. The RBS Assessment largely corroborates FTI's valuation, and wholly undermines Deloitte GmbH's conclusions. Three things jump out in RBS's valuation that cannot be reconciled with Deloitte GmbH's value-depressing assumptions. First, RBS

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753 Deloitte TCF Report ¶¶ 11.1, 11.4.

754 Deloitte GmbH Report ¶ 465.

755 The RBS 2009 Asset Valuation is dated July 31, 2009, but states that its valuation date is October 1, 2009. *See* RBS 2009 Asset Valuation, July 31, 2009, slides 34-35, C-723.

756 Squire Sanders Legal Due Diligence Report, July 30, 2009, C-725.

757 PwC Due Diligence Report, June 30, 2009, C-725.

758 Deloitte GmbH Report ¶¶ 8-9.

concluded that "80% of gas is expected to be exported," and this is true in its base case as well as its "special case" (which also assumed 80% exports but at higher prices).[759] Second, RBS stated expressly that the "LPG Plant is assumed to source gas from both its fields, Borankol and Tolkyn, and also from third parties. Going forward share of gas acquired from third parties is increasing."[760] Third, RBS concluded that Contract 302 "expires on 30 March 2011," *i.e.*, that the two-year extension that the MEMR said had been granted on April 9, 2009, in fact had been granted.[761] That destroys three pillars of Kazakhstan's and Deloitte GmbH's valuation.

515. Furthermore, the values that RBS assigns to KPM and TNG (without considering Contract 302) are several multiples higher than Deloitte GmbH's conclusions. As FTI explains further, RBS examines a default case and a special case (which differ based on gas price assumptions), and a low, base, and high set in each case (which differ based on oil and condensate price assumptions), resulting in six total scenarios.[762] RBS provides a valuation range for each scenario. The median in the Default-Base scenario results in a value for KPM and TNG of US $612 million, which RBS uses as its baseline valuation of enterprise value. The median in the Special-Base scenario has a value of US $760 million, which RBS discusses as its alternative high valuation.[763] The total spread in all the different scenarios ranges from US $272 million to US $1,094 million. Several things stand out from these figures:

- First, the US $612 million valuation that RBS uses as its baseline valuation is US $426 million (329%) higher than Deloitte GmbH's valuation for the same assets;
- Second, the US $760 million valuation that RBS uses as its alternative high valuation is US $574 million (408%) higher than Deloitte GmbH's valuation for the same assets; and
- Third, the absolute lowest value contemplated by RBS — the worst of worst case scenarios — is US $86 million (46%) higher than Deloitte GmbH's valuation for the same assets.

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759 RBS 2009 Asset Valuation, July 31, 2009, slides 36-37, 47, C-723.

760 RBS 2009 Asset Valuation, July 31, 2009, slide 47, C-723.

761 RBS 2009 Asset Valuation, July 31, 2009, slide 8, C-723. RBS presumably based this conclusion on the Squire Sanders report, which likewise concluded that Contract 302 had been extended to March 30, 2011. *See* PwC Due Diligence Report, June 30, 2009, at 161, C-724.

762 *See* Third FTI Report ¶¶ 3.8-3.24, discussing RBS 2009 Asset Valuation, July 31, 2009, slides 34-37, C-723.

763 RBS 2009 Asset Valuation, July 31, 2009, slide 34, C-723.

516. Additionally, it is fairly evident that the RBS valuation erred on the low side. RBS valued the Borankol field at only US $19 million, while even Deloitte GmbH concludes that Borankol had a much higher value (US $62.8 million) in July 2010. Moreover, the RBS Report indicates that the enterprise value (of US $612 million in the Default-Base scenario to US $760 million in the Special-Base scenario) is artificially depressed by as much as US $243.5 million through the incorrect deduction of contingent liabilities, many of which were attributable to Kazakhstan's illegal actions. The RBS Report states that the contingent liabilities are "incorporated into the model" prior to application of the discounted cash flow analysis, *i.e.*, in the enterprise value.[764] Those contingent liabilities, however, include the Laren debt and tax liabilities that resulted from Kazakhstan's illegal actions, and also appear to double-count projected capital expenditures that likely were considered elsewhere in the DCF model of enterprise value.[765] Because Kazakhstan wrongfully withheld this valuation until March 14, 2013, Claimants lost the opportunity to question Medet Suleimenov (who supervised the valuation for KMG E&P)[766] to confirm that these contingent liabilities were incorrectly deducted from enterprise value. Accordingly, the Tribunal should draw the reasonable inference that they were incorrectly deducted, which increases the enterprise value conclusion in the RBS Assessment to US $855.5 million (in the Default-Base scenario) to US $1,003.5 million (in the Special Base scenario).

517. Deloitte GmbH does not say a word in its report to explain the massive divergence of its conclusions from this contemporaneous valuation of the very same assets prepared by a sophisticated, objective, fully-informed analyst in a report prepared for the state-controlled oil company. Deloitte GmbH had access to the RBS Assessment, cited to it in its report,[767] and Mr. Gruhn confirmed in his testimony that he had reviewed the Assessment:

> Q. ... If you go all the way over to the right, where you have the information source, you identify that as being sourced to the "RBS report scenario." Do you see that?
>
> A. Yes, I see that.

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764 RBS Asset Valuation, July 31, 2009, slide 29, C-723. The contingent liabilities clearly are not incorporated as long -term debt that are deducted from enterprise value to arrive at equity value (on page 40-41), because the Tristan notes are the only debts included in that calculation. As FTI explains, it is thus logical to infer that RBS incorporated the contingent liabilities as short-term liabilities that reduced working capital in the enterprise valuation. *See* Third FTI Report ¶ 3.20.

765 Third FTI Report ¶ 3.51.

766 *See* RBS Asset Valuation, July 31, 2009, slide 11, C-723.

767 Deloitte GmbH Report, at 146, Exhibit 3, "information source" column.

> Q. That is a report that RBS prepared for KazMunaiGas to value the assets of KPM and TNG; correct?
>
> A. Yes, correct.
>
> Q. And you have seen that?
>
> A. I have seen that report.
>
> Q. Have you reviewed the entire report?
>
> A. Not the entire report. I would say I got that report, I think, early October, and I looked at it, quite obviously, because it was about the same assets and you could, well, possibly get some information out of it, therefore I read it.[768]

Immediately after offering that testimony, however, Mr. Gruhn made an all-too-anxious effort to distance himself from the RBS Assessment, explaining that he had not "relied" upon it:

> Q. Were you provided with that report by counsel for the respondent?
>
> A. Yes.
>
> Q. Given that you reference that report in Exhibit 3, why is it not listed in your scope of work?
>
> A. Well, it is a reference which was never to be a reference or source. And if you look at the primary sources which are listed in the report, you won't find this, and you won't find in all of the 225 pages any place where it is either mentioned or from which you conclude that this is consistent with our report. So it's definitely not a source. I have definitely not relied on anything in that report. It is a plain fact that the companies operating in Kazakhstan have to service their region with gas.
>
> THE CHAIRMAN: Mr Gruhn, make an effort to just stick to the question. I am aware that there are many explanations that you can give, but in the interests of counsel, I think if you —
>
> A. I understood his question: did I rely on this, and did I —
>
> THE CHAIRMAN: And the answer is no?
>
> A. The answer is no.[769]

518. That testimony revealed more than he presumably intended. Two questions arising from Mr. Gruhn's testimony come to mind. First, why did Mr. Gruhn choose not to "rely on," or consider, the RBS Assessment? He had been hired by Kazakhstan to value Claimants' investments as of July 2010, and he had in his possession a closely-proximate State-sponsored valuation of the same investments. Second, who told Mr. Gruhn that the

[768] Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 134:3-17.

[769] Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 136:3-25 (emphasis added).

RBS Assessment was "a reference which was never to be a reference or source?" The answers seem obvious. Unless Deloitte GmbH chose of its own accord to ignore extremely relevant information in its possession (which is highly unlikely), it must have received instructions from Kazakhstan not to consider the RBS Assessment, not to include in its report any comparative analysis between Deloitte's valuation and the RBS valuation, and to exclude any reference to the RBS Assessment from its report. Unfortunately for Kazakhstan, Deloitte GmbH "goofed" on the final instruction and left a reference to the RBS Assessment in its report. It is therefore clear that Deloitte GmbH at one point considered the RBS Assessment to be the relevant document it actually is.

iii. Other Evidence of Value

519. Deloitte GmbH also did not test its DCF valuations against any other market indicators of value. In contrast, FTI looked at five other indicators of value — and now has considered six, after Kazakhstan finally produced the RBS report — all of which tend to corroborate its results. These "reality checks" on value included analysis of: (1) the Project Zenith indicative offers; (2) trading prices of comparable companies; (3) reported terms of comparable transaction; (4) trading value of the Tristan debt; and (5) the Cliffson transaction. Apart from two paragraphs commenting on the relevance of the Cliffson transaction, Deloitte GmbH did not even comment on any of these alternative indicators of value in its report. At the Quantum Hearing, Kazakhstan and Deloitte GmbH belatedly tried to downplay the relevance of these other indicators of value, but their criticisms all miss the mark.

520. First, Mr. Gruhn of Deloitte GmbH argued that the comparable companies and transactions that FTI analyzed are not all that comparable because the companies in question had primarily oil assets rather than a mix of oil and gas assets. While it is true that the companies involved in those two analyses were primarily oil-producers, that does not diminish the value of those analyses as corroboration of FTI's conclusions or excuse Deloitte's failure to conduct any reality-check of its work. There are few (if any) publicly-reported companies and transactions in Kazakhstan involving producers with primarily gas resources.[770] Consequently, a valuator must rely on the most similar comparables that it can find. Notably, in the 2008 KMG E&P Analysis (which Kazakhstan belatedly produced on March 14, 2013), KMG E&P performed a market comparables analysis that looked at many

[770] Third FTI Report ¶ 4.68.

of the same companies that FTI did.[771] Likewise, the 2009 RBS Assessment also "checked" its valuation against comparable companies and transactions involving many of the same comps that FTI examined.[772] While KMG E&P did note that the companies it examined were primarily oil producers rather than gas producers, neither KMG E&P nor RBS made any adjustments to their market assessments based on that fact or otherwise indicated that those assessments should be disregarded as corroboration of their own valuations.

521. At the Quantum Hearing, Mr. Gruhn also questioned FTI's analysis of the implied enterprise value based on the market value of the Tristan debt guaranteed by KPM and TNG.[773] More broadly, Mr. Gruhn argued that one cannot infer that a specific company has a capital structure that mirrors the industry average.[774] That ignores, however, that prudent lenders constrain the ability of a company to borrow beyond its capacity, and that sophisticated markets will "price-in" the risk of a company maintaining a capital structure that is materially out of line with the industry into the trading price of public debt.[775] Mr. Gruhn also argued that the Tristan notes were trading at around 65% of face value at the end of September 2008, suggesting that the markets had priced such risk into the Tristan notes.[776] As Mr. Rosen corrected, however, the Tristan notes were trading at very close to face value just a few weeks before, and the trading price only declined because of the market's general aversion to risk and lack of liquidity in the credit crisis following the Lehman bankruptcy, not because of any factors specific to KPM and TNG.[777] FTI confirms this in its Third Report by analyzing the trading pattern of other oil and gas companies at the time, which experienced similar declines.[778] Mr. Gruhn's criticisms do not diminish this analysis as a secondary

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771 KMG 2008 Asset Valuation, September 2008, slide 13, C-722.

772 RBS 2009 Asset Valuation, July 31, 2009, slides 81-84, C-723.

773 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 165:1-8. To refresh, on the valuation date of October 14, 2008, the market value of the publicly-traded Tristan notes was US $274 million, and they were trading at approximately 65% of their face value of US $420 million. The median Morningstar energy exploration company composite, 5-year average of debt to total capital as of the end of September 2008 was 19.5%. In other words, the average debt to total capital structure (sometimes called "gearing") for companies in the same industry sector as KPM and TNG was 19.5%. From this average industry gearing of 19.5% as of the end of September, FTI noted that one could imply a market value of KPM and TNG at October 14, 2008, of approximately US $1.4 billion (*i.e.*, US $274 million is 19.5% of US $1.4 billion). First FTI Report ¶¶ 14.19-14.24.

774 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 166:23-167:11.

775 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 164:5-20.

776 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 165:1-8 ("the equity must have diminished or even vanished or even be negative before the value of debt would reach that low levels").

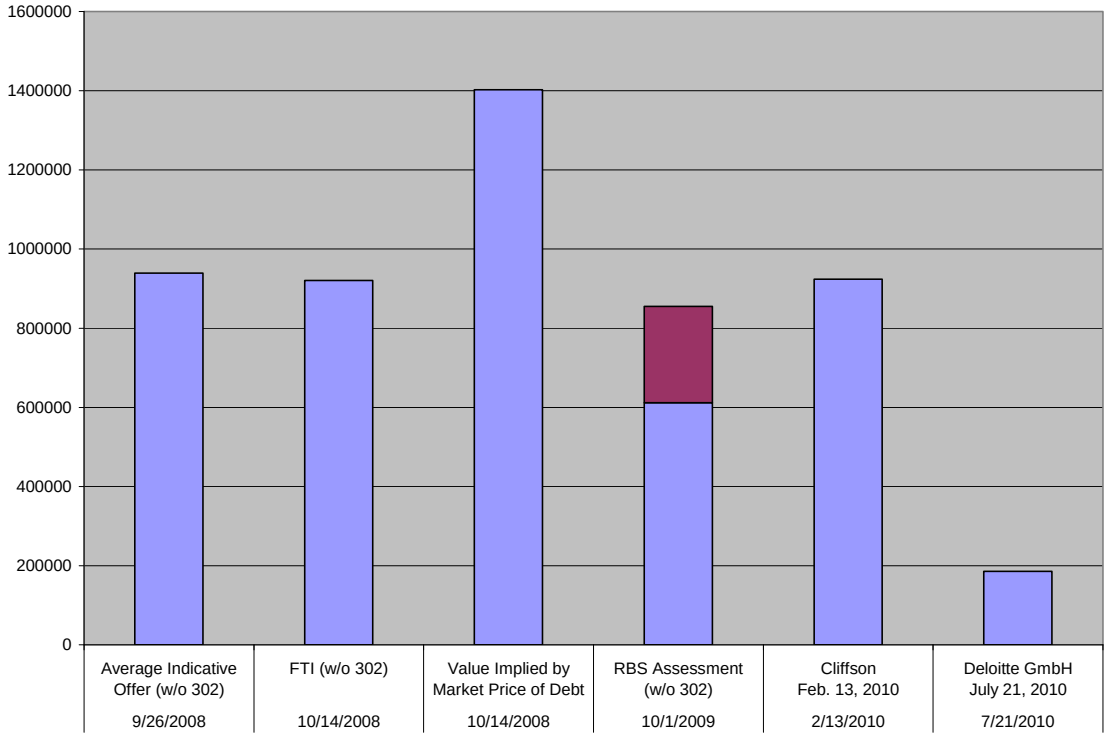
777 FTI Testimony, Tr. January 2013 Hearing, Day 4, 171:8-24.

778 Third FTI Report ¶¶ 10.219-10.224.

indicator of value, and do not excuse Deloitte GmbH's failure to consider any market-based "reality checks" on its valuation.

c. Deloitte GmbH's Valuation Is the Clear Outlier and Should Be Disregarded

522. The following chart compares Deloitte GmbH's valuation of the Tolkyn, Borankol, and LPG Plant assets with other relevant indicators of value (excluding 302 where appropriate):[779]



523. Deloitte GmbH is plainly the outlier, by a factor of three or more in every case. In light of the unsupported and baseless assumptions in GCA's work, the further unsupported assumptions in Deloitte GmbH's analysis, and the patent machinations to drive up costs and drive down revenues that are evident throughout both reports, the Tribunal should disregard Kazakhstan's valuation entirely.

[779] The purple portion of the bar for the RBS Assessment reflects the potential additional value attributable to the contingent liabilities that RBS apparently deducted from its enterprise value, as discussed below in Section V.D.1. Even disregarding that correction, the US $612 million base case valuation by RBS is more than three times Deloitte GmbH's valuation.

C. Kazakhstan's Criticisms of Claimants' Damages Claim Miss the Mark

1. Borankol, Tolkyn, and Munaibay Oil

524. Claimants and Kazakhstan have both valued the Tolkyn field, Borankol field, and Munaibay Oil discovery using the DCF method. There is no dispute that the DCF method is appropriate for the valuation of those assets. As discussed in the prior section, the DCF valuation performed by FTI relying on the geological analysis of Ryder Scott is far more robust, reliable, and accurate than the corresponding work performed by Deloitte GmbH and GCA. Moreover, Kazakhstan's primary criticisms of FTI's valuation — based on the valuation date, gas price assumptions, and use of enterprise rather than equity value — are incorrect for reasons discussed elsewhere in this submission.

525. Kazakhstan and Deloitte GmbH do not level any meaningful criticisms of the cost assumptions in FTI's DCF valuations of the Tolkyn, Borankol, and Munaibay assets. At the Quantum Hearing, Kazakhstan devoted substantial attention to pointing out what it contends are FTI's failure to include adequate costs for infrastructure (and time to build the infrastructure) to deal with potential H_2S contamination in gas from the Interoil Reef structure. As discussed in Section V.C.2.b, however, that was not an error by FTI. Rather, FTI expressly assumed that there would be no H_2S in the Interoil Reef structure on the instruction of counsel for Claimants, based on the legal argument that Kazakhstan should not benefit from speculative risk factors that it prevented Claimants from quantifying. Those criticisms thus do not call into question FTI's overall approach to cost assumptions. Moreover, Kazakhstan and Deloitte GmbH do not level any similar criticisms of FTI's cost assumptions for Borankol, Tolkyn, and Munaibay Oil.

526. Additionally, Kazakhstan and Deloitte GmbH have no significant criticisms of the various methodological judgments in FTI's DCF models (*e.g.*, FTI's approach to interest rates, currency, inflation issues, *etc*.). In its report submitted with Kazakhstan's Rejoinder on Quantum, Deloitte GmbH did point out two such errors in FTI's DCF models regarding a mismatch of real and nominal interest rate assumptions and a failure to annualize certain partial-year costs into full-year costs. FTI has acknowledged and corrected those errors even

though doing so reduced its valuation of the Tolkyn, Borankol, and Munaibay assets by approximately US $130 million.[780]

527. For all these reasons, as well as the points set out in Section V.B above, the Tribunal should award damages for the Tolkyn, Borankol, and Munaibay Oil assets based on the DCF calculations performed by FTI and relying on the geological analysis of Ryder Scott. Those amounts are:

Tolkyn	**US $478,927,000**
Borankol	**US $197,013,000**
Munaibay Oil	**US $96,808,000**

2. Contract 302 (Investment Cost and Lost Opportunity)

528. With respect to all of the Contract 302 areas except Munaibay Oil, the Tribunal is presented with a greater valuation quandary: the key data needed to determine the fair market value of those properties is missing because Kazakhstan wrongfully prevented Claimants from drilling the exploration wells necessary to determine whether hydrocarbons are present, in what quantities, at what depths, and the like. By wrongfully preventing Claimants from drilling, Kazakhstan also precluded a determination as to whether H_2S contamination would have been an issue.

529. Kazakhstan seeks to take advantage of the situation by holding Claimants to the standard of reasonable certainty that typically applies in lost profits cases, knowing full well that its own misconduct is the reason Claimants cannot meet that standard. Kazakhstan then compounds that offense by asserting that Claimants are being disingenuous in submitting a prospective valuation that fails to account for any risks. Kazakhstan's arguments are legally and factually wrong.

[780] These mistakes do not undermine the overall reliability of FTI's work, as do the numerous errors, unsupported assumptions, and wild swings in conclusions undermine the reliability of the work performed by GCA and Deloitte GmbH. FTI has explained the origin of those errors and corrected them. Moreover, Deloitte GmbH has had ample opportunity to scour FTI's work for any other mistakes, and has identified none. That highlights why it is important for an expert to explain its methodology and document its work. Unlike the case with FTI, which did thoroughly explain and document its work, it is very difficult for Claimants and the Tribunal to know what other errors and/or manipulations are embedded in GCA's opaque analysis that Deloitte GmbH adopts wholesale.

530. To begin with, Claimants and FTI have been up front with Kazakhstan and the Tribunal that the prospective value for the 302 properties is an unrisked valuation. In their Statement of Claim, Claimants explained very clearly that:

> 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 Estimate" resource estimations provided by Ryder Scott, treating these estimates instead as proven reserves.[781]

531. Likewise, FTI plainly stated that:

> For purposes of this Prospective Valuation, we have been asked to apply the un-risked '2C Estimate' and 'Best Estimate.' This calculation assumes that all the Contract 302 Properties resources are proven reserves, and that the '2C Estimate' and 'Best Estimate' production projections are fully achieved.[782]

532. Claimants then demonstrated that international law gives the Tribunal "discretion to set the amount of damages if the Claimant cannot establish the amount with sufficient certainty," and argued that the Tribunal should consider various factors, including the egregiousness of Kazakhstan's conduct and the fact that Kazakhstan is responsible for Claimants' evidentiary quandary, in exercising that discretion.[783]

533. Thus, all of Kazakhstan's bluster in its Rejoinder on Quantum and at the Quantum Hearing to the effect that Claimants are attempting to mislead the Tribunal about the level of certainty of the prospective valuation, and that this "speaks volumes about the credibility of Claimants' case on damages" and the "professional ethics" of FTI, is just that: bluster.[784] Moreover, it is bluster aimed at distracting the Tribunal from the substantial errors in Kazakhstan's legal arguments regarding the availability of damages for lost opportunities under international law. As discussed further below, Kazakhstan significantly misstates and understates the substantial legal authority supporting an award of damages for the loss of opportunity in an amount determined by the Tribunal in its discretion.

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781 Statement of Claim ¶ 440.

782 First FTI Report ¶ 15.6.

783 Statement of Claim ¶¶ 423-38.

784 Rejoinder on Quantum ¶ 7.

a. Substantial Legal Authority Supports an Award of Damages for Loss of Opportunity in an Amount Determined Within the Discretion of the Tribunal

534. Claimants have previously addressed the legal standards for the award of damages for a loss of opportunity, and will not repeat that entire discussion here.[785] Rather, Claimants will respond to Kazakhstan's argument in its Rejoinder on Quantum that there is "[n]o general acceptance of the concept of loss of opportunity."[786] Kazakhstan misstates the applicable law, and its conclusion is wrong.

535. Tribunals have awarded damages for loss of opportunity — even when the amount of damages cannot be proven with reasonable certainty — in many investment arbitrations. The leading case, which Claimants have discussed at length, is *Sapphire International v. NIOC*. Kazakhstan's attempt to distinguish the award in *Sapphire* from the present case confirms, rather than undermines, the usefulness of that decision in awarding damages for the 302 properties.

536. First, Kazakhstan argues that the US $2 million award for loss of opportunity in *Sapphire* "contrast[s] starkly with the exorbitant claim of US $1.58 billion at stake in the dispute at hand."[787] To begin with, the tribunal in *Sapphire* awarded US $2,650,874 for the loss of opportunity claim, comprised of US $650,874 for expenses incurred plus US $2 million for the investor's loss of potential profit.[788] Moreover, the absolute size of the award is meaningless; that case involved a much smaller prospect than the areas at issue here. What is relevant is that: (1) the tribunal awarded out-of-pocket expenses plus a portion of the amount of total profit that the investor could have earned; and (2) the tribunal arrived at the amount of the US $2 million for lost potential profit in its discretion, based solely on the investor's evidence of "a rough estimate, which shows the simple order of magnitude," of the net income that the investor would have earned "if everything goes as well as possible."[789]

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785 *See* Statement of Claim ¶¶ 422-432; Rejoinder on Quantum ¶¶ 58-60.

786 Rejoinder on Quantum ¶ 105.

787 Rejoinder on Quantum ¶ 109.

788 *Sapphire Int'l Petrol. Ltd. v. Nat'l Iranian Oil Co.*, Award, March 15, 1963, 35 I.L.R. 136, 190 (hereinafter "*Sapphire* Award"), C-308.

789 *Sapphire* Award at 189, C-308. The investor in *Sapphire* submitted evidence that it would have earned US $46 million in net profits from the investment if everything had gone as well as possible. The Tribunal's award of US $2 million for lost potential profits (in addition to expenses incurred) thus amounted to 4.35% of the investor's total potential profit. The investor's geological evidence, however, did not include seismic or any exploration wells, and consisted only of an expert's opinion that "the 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." Thus, the investor in *Sapphire* presented

That corresponds closely to Claimants' approach here of seeking damages for their out-of-pocket expenses plus a portion of the prospective value (*i.e.*, the net income they would have earned if they succeeded in developing Contract 302 at the mid-case of potential value).

537. Second, Kazakhstan's argument that the *Sapphire* decision should be discounted because the arbitrator "determined the amount of compensation by reference to his powers *ex aequo et bono*" is erroneous.[790] In context, the arbitrator's reference to powers "*ex aequo et bono*" simply meant judicial discretion. As explained by Ripinsky and Williams in their summary of the *Sapphire* case:

> In this case the arbitrator used the term 'ex aequo et bono' to refer to judicial discretion, rather than in the sense this term is used in Article 38(2) of the ICJ Statute (deciding a case on the principles of fairness, rather than under the rules of positive law). Here, the arbitrator did not depart from the rules of positive law but simply exercised its discretion within the boundaries afforded by those rules to fix the amount of lost profit.[791]

The tribunal in *Gemplus and Talsud v. Mexico*, discussed further below, also confirmed that an award of damages for loss of opportunity lies in the discretion of the arbitrators, without resort to powers *ex aequo et bono*.[792] There should be no dispute that this Tribunal has significant discretion to fix the amount of damages within the boundaries afforded by applicable law.

538. Kazakhstan also attempts to portray *Sapphire* as "the singular cases" [sic] in which tribunals have awarded damages for loss of opportunity. In fact, however, tribunals have awarded damages for loss of opportunity in a number of cases, relying on *Sapphire*, their own broad discretion, and general principles of compensation in international law.

539. One such case is *AIG Capital Partners, Inc. and CJSC Tema Real Estate Co. v. Kazakhstan*.[793] The tribunal in that case held that Kazakhstan had illegally expropriated claimants' investment in a residential real estate project in Almaty in violation of the United States-Kazakhstan BIT. The project had a total planned investment of US $16.3 million, but

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significantly less evidence than Claimants have here from which to draw an estimate of the likelihood of success.

790 Rejoinder on Quantum ¶ 111.

791 Ripinsky and Williams, Case Summary of *Sapphire International Petroleums Ltd. v. National Iranian Oil Company* (BIICL 2008), at 9, C-736.

792 *Gemplus S.A. and Talsud S.A. v. United Mexican States*, ICSID Case No. ARB(AF)/04/4, Award, June 16, 2010 (hereinafter "*Gemplus* Award") ¶¶ 12-57 and 13-85, C-309.

793 *AIG Capital Partners, Inc. and CJSC Tema Real Estate Co. v. Kazakhstan*, ICSID Case No. ARB/01/6, Award, October 7, 2003 (hereinafter "*AIG* Award"), C-737.

Kazakhstan cancelled the project and physically and forcibly dispossessed the claimants from the project site after the claimants had invested only US $3.5 million.[794] The *AIG* tribunal rejected the DCF method for estimating the value of the investment because "the enterprise did not exist as an income generating entity at all, and since it did not exist for a sufficient period of time, it could not generate business data necessary for proving its profitability with reasonable certainty."[795] Nonetheless, the *AIG* tribunal determined that its award needed to return the claimants to the position they would have occupied if the expropriation had not taken place, and set about to determine "in what manner claimants are to be compensated for the termination of the 'opportunity to make a commercial success of the project.'"[796] The tribunal awarded two components of damages: (1) US $3.56 million for out-of-pocket expenses; and (2) the 30% return that claimants expected to earn on the full US $16.3 million investment, less interest at a rate of 6% on the US $12.74 million that the claimants never actually invested.[797] The tribunal awarded this amount based solely on an Appraisal Report created by the claimants before commencing the project that projected a 30% return on investment.

540. Another illustrative case in *SPP v. Egypt*.[798] The tribunal in that case held that Egypt had lawfully expropriated the claimant's investment in a tourist complex. The tribunal declined to estimate the value of the investment on the basis of the DCF method because the project was "in its infancy" at the time of expropriation and thus had "very little history on which to base the projected revenues."[799] Nevertheless, the tribunal awarded damages consisting of the claimant's out-of-pocket expenses plus an additional amount to compensate for the loss of the "opportunity of making a commercial success of the project."[800] The tribunal based this decision on the fact that the expropriated company already had sold building sites worth more than twice the claimants' out-of-pocket expenses, and "construction involving roads, water and sewage systems, reservoirs, artificial lakes and a golf course had commenced and the design work for two hotels had been completed."[801] Considering that

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[794] *AIG* Award ¶¶ 3.2(B) and (F), C-737.

[795] *AIG* Award ¶ 12.1.10, C-737.

[796] *AIG* Award ¶ 12.3.1, C-737.

[797] *AIG* Award ¶ 12.3.2, C-737.

[798] *Southern Pacific Properties (Middle East) Ltd. v. Egypt*, ICSID Case No. ARB/84/3, Award, May 20, 1992 (hereinafter "*SPP* Award"), C-550.

[799] *SPP* Award ¶ 188, C-550.

[800] *SPP* Award ¶ 257, C-550.

[801] *SPP* Award ¶ 214, C-550.

evidence, the tribunal concluded that it "cannot accept that the project did not have a value in excess of the claimants' out-of-pocket expenses."[802]

541. The *SPP* tribunal then set about "to determine the amount by which the value of the claimants' investment in ETDC exceeded their out-of-pocket expenses," noting expressly that "[t]his determination necessarily involves an element of subjectivism and, consequently, some uncertainty."[803] The tribunal based its valuation of the loss of opportunity on the difference between the revenue from the completed site sales and the amount of expenses incurred (even though the existing sales represented only a small fraction of the total project), finding that this represented "the minimum measure of the value to be ascribed to the opportunity to make a commercial success of the project."[804] Thus, the tribunal used its discretion to award damages for the loss of opportunity based on the value of the revenues earned to date, even though there was a possibility that the project ultimately would not have been profitable if completed.

542. Drawing on both the *Sapphire* and *SPP* cases, the tribunal in *Gemplus* (mentioned above) also awarded damages for loss of opportunity, and discussed the applicable law at length. In *Gemplus*, the tribunal held that Mexico had breached the fair and equitable treatment and expropriation obligations under the France-Mexico and Argentina-Mexico BITs by revoking Claimants' concession to establish a national motor vehicle registry. The tribunal awarded Claimants almost US $11 million as damages for lost opportunity to make future profits, plus compound interest.[805] The tribunal rejected the DCF method of valuation because the status of the business during the short time period that it had operated (less than a year) "was far too uncertain and incomplete to provide any sufficient factual basis for the DCF method."[806] The tribunal, however, also rejected the respondent's proposed methods based on asset and tax value because they did not "take any account of the Concessionaire's most valuable intangible asset as at 24 June 2001, namely its future income stream reasonably anticipated from the Concession Agreement under its remaining ten-year term."[807]

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802 *SPP* Award ¶ 214, C-550.

803 *SPP* Award ¶ 215, C-550.

804 *SPP* Award ¶¶ 216-217, C-550.

805 *Gemplus* Award ¶¶ 18-5 and 18-6, C-309.

806 *Gemplus* Award ¶ 13-72, C-309.

807 *Gemplus* Award ¶ 13-73, C-309.

543. Instead, the tribunal awarded damages based on a "modified form of the income-based approach."[808] The tribunal first noted that factors unrelated to Mexico's treaty violations made it "significantly more than 50% probable that the Concessionaire would fail and significantly less than 50% possible that it would succeed."[809] It then set about awarding damages for claimants' loss of the opportunity to succeed. The tribunal identified two related principles that influenced its conclusion:

> 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 emphasizes 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.
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> 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 the claimant's claim for compensation - as was indicated in the Sapphire award regarding the "behavior of the author of the

[808] *Gemplus* Award ¶ 13-75, C-309.

[809] *Gemplus* Award ¶ 13-76, C-309.

> damage" (see above). 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.[810]

544. With these twin principles guiding it, the *Gemplus* tribunal returned to the main issue before it, namely, "how to assess, in money terms, the Concessionaire's lost opportunity (or chance) to make future profits for the remainder of the Concession Agreement's period." Noting again that the likelihood of success on the lost chance "was clearly not 100%; nor was it manifestly 0%," the tribunal concluded:

> In the Tribunal's view, there was therefore as of 24 June 2001 no certainty or realistic expectation of this project's profitability as originally envisaged, but there was nonetheless a reasonable opportunity. That opportunity, however small, has a monetary value for the purpose of Article 36 of the IL[C] Articles and the indemnities for compensation provided by the two BITs.
>
> It remains extremely difficult for the Tribunal to assess the value of this lost opportunity in money terms. First, the commercial, legal, political and other risks confronting the Concessionaire were considerable and are not susceptible to any useful analysis expressed in percentages. Moreover, the Claimants' claims for compensation are necessarily based only indirectly on the Concessionaire's future performance. Yet, the hypothetical willing seller of the Claimants' shares and their hypothetical willing buyer, as business people, would have been able to strike a price for such shares. It is a fact that business people can agree a price notwithstanding expert accountants respectively advising them that only a higher or lower price is appropriate. Second, the fact that this exercise is difficult is due directly to the Respondent's breaches of the two BITs which have made it almost impossible for the Claimants to show how the Concessionaire could or would have made use of that lost opportunity. As already decided by the Tribunal above, it would be wrong in principle to deprive or diminish the Claimants of the monetary value of that lost opportunity on lack of evidential grounds when that lack of evidence is directly attributable to the Respondent's own wrongs. This is not therefore a case where the burden of proof lay exclusively on the Claimants: and, in the Tribunal's view, it was also for the Respondent to prove the contrary. It did not do so.
>
> Having in mind all the legal principles and other factors above, taking the hypothetically willing buyer and willing seller materially informed as to their intended transaction on 24 June 2001, the Tribunal determines in the exercise of its arbitral discretion that the price agreed by these hypothetical parties for the

[810] *Gemplus* Award ¶¶ 13-91 and 13-92, C-309.

> Claimants' shares in the Concessionaire would have been (in total) the sum of MXN 130,000,000 or US $14,340,872 (at the then prevailing rate of exchange: MXN 9.065 = US$1)."[811]

Thus, the tribunal determined the amount of damages to award for the lost opportunity based solely on its own discretion.

545. The *Gemplus* tribunal also relied on several other authorities for its decision. For instance, that tribunal cited the following observation from Ripinsky & Williams in their treatise on *Damages in International Investment Law*:

> 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 UNIDROIT Principles of International Commercial Contracts. The latter provide in Article 7.4.3(2) that "[c]ompensation may be due for the loss of a chance in proportion to the probability of its occurrence". It is suggested that a chance of making a profit is an asset with a value of its own, and that compensation for the loss of a chance is an alternative to the award of lost profits proper in cases where the claimant has failed to prove the amount of the alleged loss of profit with the required degree of certainty, but where the tribunal was satisfied that the loss in fact occurred. Loss of a chance can thus be used as a tool allowing the injured party to receive some form of compensation for the loss of a chance to make a profit. In theory, the loss of a chance is assessed by reference to the degree of probability of the chance turning out in the plaintiff's favour, although in practice the amount awarded on this account is often discretionary.[812]

Kazakhstan cites this treatise, but only for the proposition that a claim for lost opportunity is a subspecies of a claim for lost profits, which Claimants do not dispute.[813] Kazakhstan wholly ignores the commentators' discussion of the various authorities supporting the award of such damages in the discretion of the Tribunal.

546. Additionally, the *Gemplus* tribunal also observed that the concept of damages for the loss of a chance (opportunity) is recognized in many national systems of law, and that

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[811] *Gemplus* Award ¶¶ 13-98 to 13-100, C-309.

[812] *Gemplus* Award ¶¶ 13-98 to 13-87, C-309.

[813] Rejoinder on Quantum ¶ 113.

"it is there also compatible with legal requirements to prove damages with a degree of certainty (including certainty on a balance of probabilities); and it does not depend upon the tribunal or court acting *ex aequo et bono*."[814] In particular, the tribunal noted that English law has long recognized the concept of lost opportunity damages in both tort and contract law, citing a case in which an English court awarded damages to a plaintiff who was wrongly deprived of the opportunity to appear in a pageant competition.[815] The court awarded "substantial damages" for the loss of the opportunity to compete (even though the plaintiff was only one of 50 competitors from which just 12 winners could be chosen) based on a balance of probabilities. While that court emphasized that the uncertainties made the valuation exercise "not only difficult but incapable of being carried out with certainty or precision," it "rejected the notion 'with emphasis' that, because such precision was not possible, then no damages could be ordered at all." The *Gemplus* tribunal also noted that other common law jurisdictions have adopted a broadly similar approach to English law.

547. At least two other investment arbitration decisions support the award of damages for lost opportunity. In *SOABI v. Senegal*, the tribunal awarded damages for loss of opportunity.[816] The tribunal held that Senegal breached its obligations to the claimant by terminating its contract to develop low-income housing and a factory for the prefabrication of concrete. The tribunal rejected the respondent's argument that "strict criteria of quantifiability and certainty must be applied" to the claim, noting that "only in rare cases will lost profits flowing from the breach of a long-term contract for the construction and sale of homes be precisely calculable."[817] The tribunal went on to note that while the claimant's project was subject to certain imponderable risks, this fact "does not affect the admissibility of SOABI's claim: 'In contrast with hypothetical damage, the occurrence of which is purely conjectural, damage may be assessed in terms of the probability of lost opportunity, and is thus compensable.'"[818] The tribunal observed that when it is not possible to calculate the profits that would have been made had the parties' relationship not been terminated, "[w]hat gives rise to the claim in damages is not the loss of profits itself, but rather the loss of opportunity, the value of which is set in the discretion of the judge or arbitrator, as the case

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[814] *Gemplus* Award ¶¶ 13-98 to 13-88, C-309.

[815] *Gemplus* Award ¶¶ 13-98 to 13-89, C-309, *citing Chaplin v Hicks* [1911] 2 KB 786.

[816] *Société Ouest Africaine des Bétons Industriels (SOABI) v Senegal*, ICSID Case No. ARB/82/1, Award, February 25, 1988 (hereinafter "*SOABI* Award"), C-738.

[817] *SOABI* Award ¶ 6.18, C-738.

[818] *SOABI* Award ¶ 6.18, C-738.

may be."[819] The *SOABI* tribunal awarded damages of 150 million francs in its own discretion.[820]

548. Additionally, in *Lemire v. Ukraine*, the tribunal found that Ukraine had breached its obligations of fair and equitable treatment in preventing the claimant from obtaining radio broadcasting licenses.[821] Because the licenses were awarded through a public tender process in which other applicants might have prevailed, the question arose whether the claimant's injury was the loss of a chance. The tribunal observed that "[c]ompensation for a lost chance is admissible, and is normally calculated as the hypothetical maximum loss, multiplied by the probability of the chance coming to fruition."[822] The tribunal, however, concluded that the injury was not the loss of a chance because the claimant likely would have obtained the licenses but for the state's conduct.[823]

549. Thus, Kazakhstan's argument that tribunals other than *Sapphire* have uniformly rejected the concept of damages for loss of opportunity is plainly wrong. Moreover, the only case that Kazakhstan cites as rejecting the concept, *Chevron v. Ecuador*, is utterly inapposite. The tribunal in that case found that Ecuador had violated its obligations under the United States-Ecuador BIT by delaying and otherwise impeding the claimant's breach-of-contract cases in Ecuador courts.[824] The respondent argued that the underlying court cases were in essence a chance, and thus that the claimant's damages had to be reduced by the likelihood of prevailing on those claims. The tribunal rejected that argument primarily because its obligation in that context was to "determine what TexPet should have received in judgments issued by the Ecuadorian courts. No matter what their estimation of the merits of the claims, it is clear that the Ecuadorian courts would not have applied a discount factor based on the doctrine of 'loss of chance' when issuing a judgment."[825]

550. While the *Chevron* tribunal did note that the loss of chance doctrine does not have wide acceptance across legal systems, it also observed that the principle is applied "in exceptional situations where there exists a 'harm whose existence cannot be disputed but

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819 *SOABI* Award ¶ 7.13, C-738.

820 *SOABI* Award ¶ 7.19, C-738.

821 *Joseph Charles Lemire v. Ukraine*, ICSID Case No. ARB/06/18, Award, March 28, 2011 (hereinafter "*Lemire* Award"), C-61.

822 *Lemire* Award ¶ 251, C-61.

823 *Lemire* Award ¶¶ 179, 251, C-61.

824 *Chevron Corp. (USA) and Texaco Petroleum Co. (USA) v. Republic of Ecuador*, UNCITRAL, Partial Award on the Merits, March 30, 2010 (hereinafter "*Chevron* Partial Award"), C-285.

825 *Chevron* Partial Award ¶ 378, C-285.

which … is difficult to quantify.'"[826] The tribunal, however, found no exceptional difficulty in determining what would have occurred but for Ecuador's breach because the essential uncertainty — how a fair and impartial Ecuador judge would have decided the underlying lawsuits — was within the core competence of the tribunal, and all the necessary evidence to decide those outcomes was available. That is markedly different from this case, where the essential uncertainties — the presence and quantities of hydrocarbons, the presence of contaminants, etc. — are unknowable because Kazakhstan's illegal actions prevented Claimants from fully exploring the Contract 302 Properties.[827]

551. The decisions in *Lemire v. Ukraine* and *Chevron v. Ecuador* also dispatch another of Kazakhstan's arguments, namely that Claimants must prove a very strong chance — "significantly more than 50%" — that the 302 opportunity would have been successful to recover damages for loss of the opportunity.[828] If Claimants' likelihood of success were greater than 50%, their claim would not be for loss of opportunity, and they would be able to recover the full amount of lost profits without any discounting for likelihood of success. That was the essential reason that the *Lemire* and *Chevron* tribunals did not apply the loss of opportunity doctrine. The loss of opportunity doctrine exists precisely for those situations when the Claimant cannot show that its likelihood of success is greater than 50% because its opportunity to do so was precluded by the State's own actions.

552. Finally, Kazakhstan's argument that scholars have shown a "lack of acceptance" to the concept of damages for loss of opportunity also misrepresents the body of scholarship on the subject. The only scholar that Kazakhstan cites is Professor Marboe, for the proposition that "[Awarding compensation for the loss of opportunity] is […] neither a widely accepted nor a very precise practice."[829] Professor Marboe, however, in fact notes earlier in her book that "[i]n view of the difficulty in determining long-term profits precisely, a number of arbitral tribunals awarded lump sums for the loss of profits or for the loss of 'opportunity' or loss of a 'chance,'" citing the *Sapphire* and *SOABI* cases.[830] Indeed, the entirety of the quotation that Kazakhstan recites out of context reads:

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[826] *Chevron* Partial Award ¶ 382, C-285, *citing* UNIDROIT Principles of International Commercial Contracts with Official Commentary, art. 7.4.3(2) (1994).

[827] *Chevron* Partial Award ¶¶ 379, 382, C-285.

[828] Rejoinder on Quantum ¶ 115.

[829] Rejoinder on Quantum ¶ 107.

[830] Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (Oxford 2009) § 3.219, C-739.

> It seems, therefore, that between the rejection of awarding 'speculative' profits and lost profits which can be proved with sufficient certainty, there is a 'grey zone' where the 'probability' of profits would be enough. In those cases, lump sums have been awarded to account for the loss of a 'chance' or 'opportunity' to generate profits. This is, however, neither a widely accepted nor a very precise practice.[831]

Thus, far from supporting Kazakhstan's point, Professor Marboe concludes that there are circumstances in which an award of damages for loss of opportunity is appropriate.

b. Application of the Law on Loss of Opportunity to the Contract 302 Prospects

553. The substantial authority laid out above clearly supports an award of damages in this case for the Claimants' loss of the opportunity to make a commercial success of Contract 302. As discussed at length in Claimants' prior submissions, there is ample evidence that the Contract 302 Properties held substantial opportunity for large fields of commercially exploitable oil and gas. The only reason that Claimants cannot show the Tribunal exactly which of the Contract 302 Properties were commercially exploitable, and to what degree, is because of Kazakhstan's illegal actions. Otherwise, Claimants were ready, willing, and able to explore and develop those areas and had every intention of doing so.

554. The challenge for this Tribunal is arriving at a fair value of the opportunity lost. As outlined above, numerous tribunals — including *Sapphire*, *AIG Capital*, and *SPP* — awarded claimants' out-of-pocket expenses plus an amount to compensate for the lost potential "upside" of the opportunity. Claimants invested US $31,330,000 in exploring Contract 302, including acquiring and analyzing seismic data, other geophysical work, and drilling the incomplete Bayht exploration well.[832] (That amount excludes what Claimants invested in the Munaibay 1 well, in order to avoid double-counting with Claimants' claim for market value damages for Munaibay Oil based on a DCF model set out in Section V.C.1 above.) Thus, that value represents the starting point of damages that the Tribunal should award for Contract 302.

555. Based on all the authorities set out above, the Tribunal also should render a substantial award for the Claimants' loss of the ability to make the Contract 302 Properties a commercial success. That amount ultimately must be determined in the Tribunal's discretion.

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[831] Irmgard Marboe, *Calculation of Compensation and Damages in International Investment Law* (Oxford 2009) § 3.225, R-324.

[832] FTI First Scope of Review No. 37.

The starting point for the analysis is the prospective value for the Contract 302 Properties (other than Munaibay Oil) of US $1,498,017,000 which represents the middle case of the potential net income that Claimants could have earned from those areas but for Kazakhstan's actions. The amount of that prospective value that the Tribunal awards to Claimants is within the Tribunal's discretion to decide, based on factors such as the likelihood of success, the potential for unjust enrichment of the State, and the fact that Kazakhstan is responsible for Claimants' inability to prove these losses with greater certainty.

556. In this case, this last factor is of critical importance, as illustrated by the issue of H_2S contamination. Kazakhstan's supposition that gas in the Reef structure contains high quantities of H_2S is the centerpiece of its argument that the prospect would be uneconomical to produce. Kazakhstan and Deloitte base that assertion solely on GCA, which asserts merely that it is "most-likely" that the gas is sour based on experience in other fields hundreds of kilometers away.[833] GCA, however, does not quantify whether this likelihood is 51%, 100%, or somewhere in between, and its entire hypothesis is entirely speculative. Yet Kazakhstan simply assumes the worst case scenario — a 100% likelihood that the Reef gas is sour. This is the exact opposite of the correct approach, because Kazakhstan's actions are the only reason that Claimants and the Tribunal do not know with certainty whether and to what extent the gas is sour. The Tribunal should reject that approach.

557. In light of the egregiousness of Kazakhstan's conduct, the potential for enormous unjust enrichment to the State, and the fact that the State is responsible for Claimants' inability to prove their damage with greater certainty, Claimants request that the Tribunal award a return of Claimants' out-of-pocket investment plus a substantial portion of the prospective value for the Contract 302 Properties (other than Munaibay Oil, addressed in Section V.C.1 above). Those amounts are:

Investment Cost (excluding Munaibay Oil)	**US $31,330,000**
Prospective Value	**US $1,636,900,000**
Munaibay Oil Prospective Value	**(US $138,883,000)**
Prospective Value (Other Than Munaibay Oil)	**US $1,498,017,000**

[833] Second GCA Report ¶ 107.

3. LPG Plant (Investment Cost and Lost Opportunity)

558. Claimants' damages claim for the LPG Plant is similar to their claim for the Contract 302 Properties. They invested a substantial amount of money in construction of the plant, but due to Kazakhstan's illegal actions, they were unable to complete it and make a commercial success of the venture. Moreover, Kazakhstan's actions prevented Claimants from developing the evidence needed to value the plant on a fair market value basis.

559. Kazakhstan argues that this means the plant is worthless, contending that Claimants cannot prove that they would have had adequate supplies of gas from Contract 302 or third-party sources to run the plant economically. As discussed in the prior section, however, the Tribunal should reject that argument — just as the tribunals in *Sapphire*, *Gemplus*, and other cases did — because Kazakhstan should not benefit from the evidentiary uncertainty resulting from its own misconduct. Rather, the Tribunal should award damages for the amount of the Claimants' investment in the LPG Plant, and some portion for the lost opportunity to make a commercial success of the project.

a. Investment Cost Basis Is an Appropriate Standard of Valuation for the LPG Plant

560. At the Quantum Hearing, Howard Rosen of FTI clearly articulated the rationale for valuing the LPG Plant on a cost basis:

> I then looked at the third asset that was owned by TNG, the LPG plant, and determined — because it did not have an operating history and there was some uncertainty surrounding the potential profitability and value of that asset, needed to make a determination whether or not it was a going concern or not.
>
> In valuation, when you do a fair market value, you come to a fork in the road: is a business a going concern or it is not? If it is a going concern, then there is another fork in the road, and the fork in the road is: how do I value this? Do I look at it on a cashflow basis or do I look at it on an asset basis?
>
> In this case, because I did not have sufficient information to look at it on a cashflow basis to determine value, I looked at it on a cost basis or an investment basis, and determined the value of the LPG plant on that basis.
>
> In arriving at my decision that it was a going concern, I needed to consider the availability of potential supply from primarily Tolkyn and Borankol; the possibility that there would have been supply from the 302 properties had they in fact been developed; the

> possibility that other gas producers in the region would have chosen, from an economic perspective, to put their gas through that plant in order to extract additional value; and then again, the possibility that gas would have been supplied from the central pipeline, the CAC, which ran in reasonable proximity to the plant. Again, from an economic perspective, did it make sense that people would put their gas through this plant to extract additional value?
>
> I satisfied myself that it was reasonable as a going concern, and therefore that's why I arrived at the cost basis for that.[834]

561. Kazakhstan and Deloitte take a wrong turn at the first fork in the road, concluding incorrectly that the LPG Plant would have been scrapped, rather than completed and operated as a going concern. Kazakhstan's position is based on the assumption that no one would have completed the LPG Plant and put it into operation because the plant had a NPV of US $-89.8 million as of Kazakhstan's July 22, 2010 valuation date. There are numerous flaws to that argument.

562. First, Kazakhstan's valuation assumes a completion cost of US $100 million, which massively overstates the capital cost required to complete the plant. At the Quantum Hearing, GCA admitted that wholly undocumented cost assumption, US $50 million, was attributable to the need to restart construction from a mothball condition. Mr. Wood testified, "On the basis that the work on the plant had never stopped, then I think a $50 million estimate would have been appropriate."[835] But for Kazakhstan's illegal actions, however, work on the plant never would have stopped, and thus it is inappropriate to include that cost in a calculation of the damages necessary to put Claimants in the position they would have occupied but for Kazakhstan's misconduct.[836] That error alone accounts for more than half of Kazakhstan's negative valuation for the LPG Plant.

563. Kazakhstan's incorrect valuation date also understates the amount of gas available from the Borankol and Tolkyn fields to load the LPG Plant. The main thrust of Kazakhstan's argument is that gas from Borankol and Tolkyn "would only suffice to operate the plant for four years before it would need to be shut in."[837] Deloitte reaches that

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834 FTI Testimony, Tr. January 2013 Hearing, Day 4, 46:8-47:16.

835 GCA Testimony, Tr. January 2013 Hearing, Day 4, 15:10-12.

836 *See* Section V.A.2, *supra*.

837 Rejoinder on Quantum ¶ 141.

conclusion, however, by incorrectly assuming that the LPG Plant would not start up until mid-2011.[838] It bases that assumption on GCA, which states:

> [I]f project sanction had occurred at the effective date (21st July 2010), provided there was adequate confidence in future gas production from the Fields, the Borankol LPG Plant start-up could have been achieved by mid-2011.[839]

564. That assumption is plainly wrong, and demonstrates the error in Kazakhstan's valuation date. The unrebutted evidence in the case is that Kazakhstan's illegal action began interfering with construction of the LPG Plant in November or December 2008, and that but for that interference, the LPG Plant would have gone online in June 2009.[840] By wrongfully assuming — contrary to all the evidence — that the LPG Plant would not go online until mid-2011, Kazakhstan's valuation date mistakenly fails to account for two full years in which the LPG Plant could have processed gas from Tolkyn and Borankol but for Kazakhstan's violations.

565. Additionally, Kazakhstan fails to account at all for the potential of loading the LPG Plant with gas from third-party sources. Citing Deloitte, Kazakhstan argues in its Rejoinder on Quantum that the "viability of the LPG plant stands or fails with the development of the Interoil Reef property."[841] Deloitte, however, simply disregarded any evidence regarding third-party gas. Deloitte states:

> According to FTI and the witness statement by Mr. Broscaru, the supply to the LPG Plant was depending on the gas production of the Tolkyn field and — given the declining production of the Tolkyn field — on the (potential) gas production of the Contract 302 Properties.
>
> As is evident from the declining estimated future production of the Tolkyn field and the contingent gas resources of the various Contract 302 Properties, the supply to the LPG plant would depend on the production of the Interoil Reef. The viability of the LPG plant stands or falls with the development of the Interoil Reef property.[842]

566. That misstates the evidence from FTI and Mr. Broscaru. First, Mr. Broscaru very clearly explained in his witness statement that third-party gas sources were available to

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838 Deloitte GmbH Report, Exhibit 9, at 154.

839 Second GCA Report ¶ 74.

840 *See* Section V.A.2, *supra*.

841 Rejoinder on Quantum ¶ 149.

842 Deloitte GmbH Report ¶¶ 182-183.

load the LPG Plant. After explaining that TNG expected to load the LPG Plant solely from its own gas, Mr. Broscaru then explained at length that TNG could also use the plant to process gas on behalf of other producers:

> Moreover, the LPG Plant had the capability to process gas supplied by third party sources. In fact, the Kazakhstan government pressured TNG to build the LPG Plant precisely because it offered the ability to process gas on behalf of other producers. There are numerous oil and gas fields in the vicinity of the LPG Plant that produce natural gas, including "associated gas" (i.e., gas produced by wells that primarily produce oil). Many of those producers did not have the facilities to process gas for delivery into a main pipeline, and so historically flared gas at the wellhead. In 2006, however, Kazakhstan enacted new laws to reduce gas flaring, which required producers either to build gas processing facilities of their own, process their gas at another producer's facilities (e.g., TNG's), or find some use for unprocessed gas. For many producers, however, it would not be economical to build processing facilities of their own. Thus, the Kazakhstan government encouraged TNG to expand its gas processing facilities and build the LPG Plant in order to provide these services to other neighboring producers. They permitted us to work. We were regularly sending our representatives, engineers to Atyrau to check and to approve the use of contracted materials and equipments at the LPG Plant.
>
> One concrete example of this is KazakhTurkMunai, a company that produces oil and gas from a field adjacent to Borankol. In 2007, KazakhTurkMunai and TNG entered into an agreement for TNG to process up to 200 mmcm of gas produced by KazakhTurkMunai annually for a processing fee. TNG constructed an inlet into its gathering system allowing KazakhTurkMunai to process its gas through TNG's facilities before delivering it to the CAC pipeline. Although that agreement did not provide for extraction of LPGs (because the LPG Plant did not yet exist), the ability to extract LPGs from other producers' gas would only enhance the economics of such arrangements for both TNG and the other suppliers. Thus, the design documents performed by Casco – Petrostar concerning the connection to KazTurkMunai operator were finalized and we applied them exactly.
>
> Furthermore, the CAC pipeline runs within 18 kilometers from the LPG Plant. As discussed above, the CAC pipeline transports gas containing LPG elements delivered by other producers which do not possess LPG Plants. Even if there had been no sources of local natural gas supply from TNG and other nearby producers, the LPG Plant still could have been used to extract valuable LPGs from the CAC pipeline.[843]

[843] Broscaru Statement ¶¶ 18-20.

That testimony is unrebutted, including the testimony that the Kazakh government pressured TNG to expand its processing capacity and build the LPG Plant in order to process gas from neighboring producers.

567. The Joint Operating Agreement for the operation of the LPG Plant (concluded among Ascom, Terra Raf, TNG, and Vitol) confirms that the parties anticipated supplying the plant with third-party gas. The contract defines the term "Gas Contract" to mean "the agreement(s) pursuant to which third party gas is supplied to the Plant."[844] The contract also addresses requirements for approval and pricing (*i.e.*, prevailing market rates) for any such Gas Contract to supply third-party gas to the LPG Plant.[845]

568. Additionally, FTI has never stated that the viability of the LPG Plant depends solely on gas from the Tolkyn field and Contract 302 properties. Rather, FTI based its cost value approach largely on the fact that the LPG Plant could service gas volumes from other producers.[846] In its Reply Report, FTI did remove third-party gas sources from its *prospective* valuation of the LPG Plant — *i.e.*, FTI's unrisked NPV valuation of the LPG Plant assuming full production from Contract 302 — because of uncertainty regarding terms of third-party gas sources.[847] FTI did not, however, change its reliance on the availability of third-party sources as a premise for its cost valuation of the LPG Plant.[848] This goes to the essence of why a cost valuation is a reasonable valuation approach here: there is sufficient evidence that the LPG Plant would have been operated as a going concern to value it as such, but there is not sufficient evidence of the terms on which it would have been operated to value it on a cash flow basis.

569. Deloitte, on the other hand, simply ignores all evidence regarding the potential to load the LPG Plant with gas from other producers. In addition to the evidence from Mr. Broscaru and FTI that TNG could obtain gas from third parties to process in the LPG Plant, Deloitte and Kazakhstan utterly disregard the possibility that TNG could have sold the plant to a third party that had its own gas to run through the plant. One such third party was KMG E&P, which made an indicative offer of US $199 million for the LPG Plant in September 2008. Importantly, KMG E&P arrived at that figure using a mixed comparative value and cost approach, not based on a discounted cash flow analysis:

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844 LPG Joint Operating Agreement § 1.1, First FTI Scope of Review No. 44.

845 LPG Joint Operating Agreement § 7.2, First FTI Scope of Review No. 44.

846 First FTI Report ¶¶ 13.2-13.4.

847 Second FTI Report ¶ 2.41.

848 Second FTI Report ¶¶ 2.39 -2.40; FTI Testimony, Tr. January 2013 Hearing, Day 4, 110:4-22.

> The value of the LPG plant was calculated as an arithmetical average between the matrix of comparative method value and cost method value. EV/EBITDA multiple of 5.5x was used as a base for comparative method valuation. Historical costs of US $193 million were used as a base for cost method valuation.[849]

The fact that the State-controlled E&P company used cost basis to value the LPG Plant contradicts Kazakhstan's argument that cost basis is an improper valuation method. It also strongly suggests that KMG E&P saw the value of the LPG Plant as independent from the potential profits to be earned from processing TNG's gas alone.

570. Moreover, the 2009 RBS Assessment also assumed that the LPG Plant would be loaded primarily with third-party gas, based on discussions with KMG E&P.[850] Thus there is a clear and uncontradicted factual basis to assume that the LPG Plant could have been operated economically using gas from sources other than the Tolkyn and Borankol fields. Moreover, RBS valued the LPG Plant at up to US $86 million in its base case and US $146 million in its high case. That valuation should set the absolute minimum amount that the Tribunal should award for the LPG Plant.

571. At the Quantum Hearing, when confronted with the issue of potential buyers that may have had their own gas to run through the plant, Mr. Gruhn of Deloitte gave a nonsensical answer:

> Q. If TNG was able to find potential buyers who had supplies of gas of their own to load into the plant, isn't it possible that those buyers would have a different valuation of what that plant is worth?
>
> A. Well, actually, if that LPG plant could be run over the life of 20 years at full capacity, the value would be totally different. But the question is: would anybody want to pay for that, bringing the gas himself, which is a synergy effect which is not allocated to the asset itself, and it's certainly not something that could be done on the basis of TNG and [KPM's] situation contracts. There is simply no basis to assume this.[851]

572. It is obvious that Kazakhstan and Deloitte simply never considered the possibility at all. Rather, they simplistically assumed that if TNG could not load the plant

[849] KazMunaiGas E&P Indicative Offer, September 25, 2008, C-19.

[850] RBS 2009 Asset Valuation, July 31, 2009, slide 47, C-723.

[851] Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 142:6-17.

with gas of its own, its only alternative would be to sell the LPG Plant for salvage value rather than as a going concern.[852] And there is simply no basis to assume that.

b. Kazakhstan's Other Criticisms of Claimants' LPG Plant Valuation Are Equally Meritless

573. Kazakhstan casts a variety of other aspersions on the LPG Plant project, and on Claimants' management of that project, in an effort to portray the project in a dismal light. Those arguments are largely irrelevant to the value of the LPG Plant, but Claimants will nevertheless address them in turn.

574. In its Rejoinder on Quantum, Kazakhstan argues that Claimants had only a US $20 million equity investment in the LPG Plant. In Kazakhstan's typical fashion, this argument plays fast and loose with the facts, failing to distinguish between early plans and what subsequently occurred. The document that Kazakhstan cites for this assertion is an undated, draft business plan for the LPG Plant that was prepared by Vitol.[853] It is true that Claimants and Vitol originally planned to finance the LPG Plant through a combination of: (1) a US $20 million "equity" contribution from Vitol;[854] (2) a US $20 million equity contribution from Ascom (or an affiliate); and (3) the remainder through debt financing, split between Vitol (through the prepayment mechanisms in the COMSAs) and project financing from KazCommerzBank.[855] That financing structure is irrelevant for purposes of quantum,

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[852] Rejoinder on Quantum ¶¶ 154-164 ("Claimants are at best entitled to Salvage Value.").

[853] *See* Rejoinder on Quantum ¶ 139, n. 117, *citing* Ascom LPG Plant – Business Plan, R-333. That exhibit is undated, but from context (*e.g.*, the reference in the second paragraph that "all agreements between Ascom and Vitol have been completed"), it appears that the draft was created shortly after the Joint Operating Agreement for the LPG Plant was executed on June 27, 2006. The document is plainly a draft, as evidenced by the numerous blanks in the last four pages of the document. The document also clearly was prepared by Vitol, as evidenced by the penultimate paragraph on the third page, which states that the COMSA agreements are "being used as a basis for introducing our debt financing into the structure. Ascom are financing their share through US$20M in equity and debt funding raised through KKB directly to TNG." Moreover, Mr. Lungu confirmed that Exhibit R-333 was created by Vitol, most likely in 2006. *See* Lungu Testimony, Tr. January 2013 Hearing, Day 1, 200:12-16.

[854] References to Vitol's "equity" contribution to the LPG Plant project should not be confused with an ownership interest in the LPG Plant itself. Vitol provided its "equity" contribution through a loan agreement with Claimants. *See* LPG Plant Joint Operating Agreement §§ 2.1-2.5, First FTI Scope of Review No. 44. That contribution constituted equity insofar as it gave Vitol a contractual right to share in the profits of the LPG Plant. It did not give Vitol any ownership interest in the LPG Plant itself. *See* Vitol's Draft LPG Plant Business Plan at 3, R-333 ("Vitol will not actually be able to buy share ownership in the plant but will gain the financial benefit. We will purchase a 50% share in the Joint Operating Agreement and the Trading Company.") As discussed further below, the fact that Vitol has certain contractual rights regarding the profits of the LPG Plant does not require any reduction of Claimants' damages attributable to Kazakhstan's seizure of that asset.

[855] LPG Plant Joint Operating Agreement §§ 2.1-2.5, First FTI Scope of Review No. 44; Vitol's Draft LPG Plant Business Plan, R-333.

because, at all times prior to the July 2010 seizure, TNG was the 100% legal owner of the plant.

575. The intended financing structure, however, never came to pass. Claimants retired all KazCommerzBank debt in 2007,[856] and as discussed above, Vitol drew down its debt financing for the LPG Plant to a total of US $46 million (in addition to its US $20 million "equity" contribution) as a result of the actions of Kazakhstan.[857] Thus, TNG financed all of the construction of the LPG Plant (apart from the US $66 million provided by Vitol) out of its general treasury.

576. In addition to incorrectly suggesting that TNG's investment in the LPG Plant was limited to its original equity contribution, Kazakhstan argues that the LPG Plant became a "black hole" because construction costs increased dramatically from its original plan to what it ultimately would cost to complete. While construction costs did increase, Kazakhstan greatly exaggerates the significance of this fact by failing to account for the substantial inflation and increase in LPG Prices over the same period. As FTI explains, there was significant inflation in Kazakhstan in 2007-2008 (nearly 30% in consumer prices and 68% in producer prices).[858] Likewise, average LPG prices increased more than 60% from 2006 to 2009.[859] Construction costs for a project like the LPG Plant tend to trend with the prices of their outputs because market demand for raw project materials (*i.e.* steel pipes) and construction capacity tends to increase as other market participants commence projects to take advantage of rising commodity output prices.[860] Thus, the increase in the cost of the LPG Plant correlates both with observed increases in inflation and LPG product prices, the latter of which also drove increasing economic expectations for the plant.[861]

577. Kazakhstan makes a similar mistake regarding the fact that construction of the LPG Plant experienced some delays. Kazakhstan asserts that TNG originally targeted start-up for October 2007, but its only support for that is the draft Vitol business plan that had that date in brackets. Moreover, even assuming that was the original plan, Kazakhstan has not shown how a 20-month delay in start-up would cause the LPG Plant to become a "black

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856 Audited Financial Statements attached to 2007 Annual Report of Tristan Oil at F-139, R-37.4.

857 *See* Section IV.A.2, *supra*.

858 Third FTI Report ¶¶ 5.23-5.24.

859 Third FTI Report ¶ 5.27.

860 Third FTI Report ¶ 5.20.

861 Third FTI Report ¶ 5.29.

hole." In light of the ability to load the LPG Plant with gas from Contract 302 and/or third-party suppliers, a delay in the start-up date does not shorten the usable life of the plant at all.

578. At the Hearing on Quantum, Kazakhstan also bizarrely focused on one line in the KPMG Vendor Due Diligence report in which KPMG stated that "there has been no delays and plant is expected to be completed on time and within the budget."[862] Kazakhstan's point presumably is that Claimants misled KPMG about the status of the project. That very same document, however, repeatedly states that the "[p]lanned launch date for the plant is Q2 2009," which was absolutely true.[863] Moreover, KPMG also clarified that "[a]s of 17 May 2008 total cost of the LPG plant construction was estimated to be approximately USD233 million."[864] At the time the KPMG Report was prepared, the project was expected to be completed on budget, and in fact would have been completed close to that amount but for Kazakhstan's interference.

579. Finally, Deloitte argues that the LPG Plant was "speculative from the start." Using the valuation metrics that Mr. Broscaru described in his witness statement, Deloitte attempts to create a cash flows and a valuation model that it concludes had a value of US $108.2 million. Deloitte, however, makes a fundamental error in its calculation. Mr. Broscaru stated that TNG expected the LPG Plant to generate US $1 billion in revenue and US $500 million in profit over 10 years.[865] Deloitte, however, spreads those cash flows over 20 years, effectively cutting them in half. FTI has corrected Deloitte's error, and concludes that an accurate "simplified model" results in a positive NPV of US $92 million.

c. LPG Plant Valuation

580. Based on the foregoing, the Tribunal should award damages for the LPG Plant equal to Claimants' investment in that facility, plus a substantial portion of the prospective value that Claimants could have realized from processing gas from the Contract 302 Properties in the LPG Plant. Those amounts are:

862 Project Zenith – Vendor Due Diligence by KPMG, August 29, 2008, at 89, C-69.
863 Project Zenith – Vendor Due Diligence by KPMG, August 29, 2008, at 89, C-69.
864 Project Zenith – Vendor Due Diligence by KPMG, August 29, 2008, at 89, C-69.
865 Broscaru Statement ¶ 14.

Investment Cost	**US $245,000,000**
Prospective Value	**US $329,077,000**
Prospective Value Above Cost	**US $84,077,000**

D. Valuations on Alternative Valuation Dates

581. As discussed in Section V.A above, the correct valuation date in this case is October 14, 2008, because that is the last date on which Claimants investments can be valued without incorporating impairment to value flowing from Kazakhstan's own misconduct. Kazakhstan's proposed valuation date of July 22, 2010, fails to respond to Claimants' claims because it does not even attempt to quantify the value by which Claimants' assets were impaired by Kazakhstan's illegal actions. Thus, presented with this binary choice, the Tribunal should adopt Claimants' valuation date of October 14, 2008. Claimants firmly maintain their request that the Tribunal do so.

582. However, in the unlikely event the Tribunal concludes that a valuation date after October 14, 2008, is appropriate, there is substantial evidence in the record supporting valuations at later dates that are significantly higher than Deloitte GmbH's contrived undervaluation as of July 22, 2010. Such evidence includes the RBS Assessment conducted for KMG E&P on July 31, 2009 (with a valuation as of October 2009), and the Cliffson transaction that Claimants executed on February 13, 2010 (and that remained pending until at least June 7, 2010).

1. The RBS Valuation

583. As discussed above in Section V.B.3.b.ii, RBS conducted a comprehensive valuation of the Tolkyn, Borankol, and LPG Plant assets for KMG E&P in the summer of 2009. RBS based its valuation on: (1) the 2009 reserve report prepared by Miller Lents; (2) detailed legal due diligence by Squire Sanders; (3) detailed financial, tax, and environmental due diligence by PWC; (4) discussions with management of KPM and TNG; and (5) "valuation discussions with KMG EP."[866] The valuation, dated July 31, 2009, with a valuation date of October 1, 2009, concluded that Tolkyn, Borankol, and the LPG Plant had a combined enterprise value ranging from US $612 million in the Default-Base scenario up to

[866] *See* RBS 2009 Asset Valuation, July 31, 2009, slides 11-12, 35, C-723.

US $760 million assuming higher gas pricing in the Special-Base scenario.[867] RBS did not value the Contract 302 Properties.[868]

584. In the unlikely event the Tribunal declines to adopt Claimants' October 14, 2008, valuation date and FTI's valuation, the RBS valuation represents an alternative that should establish the minimum value for the Borankol, Tolkyn, and LPG Plant assets. RBS conducted that valuation as of October 1, 2009, after the MEMR had declared that Claimants did not own TNG and after Kazakhstan had imprisoned KPM's general director and imposed a devastating US $145 million criminal penalty against KPM. That valuation also occurred after the worst of the global financial crisis and trough in oil prices had passed, and after the so-called "watering" problems at Tolkyn were known. Thus, the gist of Kazakhstan's criticisms of Claimants' valuation date, which are invalid to begin with, certainly do not apply to a valuation as of October 1, 2009.

585. Additionally, the Tribunal should not entertain any arguments Kazakhstan may raise that the RBS valuation somehow overstates the value of Borankol, Tolkyn, and LPG Plant. RBS was a sophisticated, independent valuation expert, and it prepared its valuation for the state-controlled oil company for purposes of a potential transaction, not litigation. Moreover, Kazakhstan's belated production of the valuation wrongly prevented Claimants from questioning any witnesses — including Medet Suleimenov, who supervised its preparation —about the assumptions and methodology used in the report. Thus, while the Tribunal should draw all reasonable inferences that RBS understated the value of those properties (as explained above, by undervaluing Borankol and incorrectly deducting contingent liabilities), any consideration of arguments by Kazakhstan to reduce the RBS valuation would be a gross violation of Claimants' procedural rights.

2. The Cliffson Transaction

586. As discussed in their previous submissions, Claimants concluded an arms' length contract to sell all of the assets at issue in this arbitration to a third party, Cliffson, on February 13, 2010.[869] The terms of the Cliffson agreement were US $267 million for 100% of the equity interests in TNG, KPM, and Tristan, with Cliffson assuming all of those

[867] *See* RBS 2009 Asset Valuation, July 31, 2009, slide 36-37, C-723.

[868] *See* RBS 2009 Asset Valuation, July 31, 2009, slide 29 (stating that RBS valued the Tolkyn and Borankol fields and LPG Plant), C-723.

[869] *See* Reply on Jurisdiction and Liability ¶¶ 418-422; Reply on Quantum ¶¶ 5-7.

companies' liabilities. This equates to an enterprise value for the assets of KPM and TNG of approximately US $924 million.[870]

587. Although the Cliffson transaction never closed, it remained pending until June 7, 2010, at the earliest. On that date, Cliffson apparently sent a letter to the Ministry of Oil & Gas stating that it no longer wished to pursue the transaction (although Cliffson never informed Claimants, and Claimants only saw this letter when it was produced in this arbitration). Thus, the Cliffson transaction is quite proximate to Kazakhstan's proposed valuation date. Moreover, because it was a real transaction for the assets in question with an arms' length purchaser, it is much more reliable evidence of value than Deloitte GmbH's unreliable DCF valuation.

588. Kazakhstan's various arguments to undermine the reliability of the Cliffson transaction as evidence of value all miss the mark. First, Kazakhstan's assertion that the Cliffson deal cannot be "described as an arm's length transaction" is baseless.[871] Claimants have identified the principals of Cliffson (the Aussabayev family), and have described the contentious negotiations that occurred leading up to the execution of the Cliffson SPA.[872] Kazakhstan presents no evidence whatsoever that the relationship between Claimants and the Aussabayevs was anything other than arm's length, because there is none.

589. Instead, Kazakhstan speculates that the relationship must have been something other than arm's length because of what it characterizes as unusual timing and terms of the transaction. Kazakhstan's argument mischaracterizes the facts, but it also draws the wrong conclusions regarding the way in which that deal was negotiated and consummated.

590. First, the discussions between Claimants and the principals of Cliffson began in November 2009, although the discussions at that time were with a different Aussabayev company called Grand Petroleum.[873] The Aussabayevs were represented by sophisticated advisors, including a family office in London and the law firm of Cleary Gottlieb.[874] Claimants provided the Aussabayevs's advisors with full access to the Project Zenith

[870] Reply on Jurisdiction and Liability ¶ 418; Second FTI Report ¶ 3.6.

[871] Rejoinder on Quantum ¶ 398.

[872] Reply on Quantum ¶¶ 5-6; Second Stati Statement ¶¶ 27-34.

[873] Lungu Testimony, Tr. January 2013 Hearing, Day 1, 191:22-192:24.

[874] Lungu Testimony, Tr. January 2013 Hearing, Day 1, 194:8-15.

information and data room.[875] Thus, the Aussabayevs had significant time to conduct due diligence on the companies.

591. Nonetheless, Claimants acknowledge that there was an unusual aspect to the negotiations with the Aussabayevs, because the preliminary MOU that the Aussabayevs executed in November 2009 provided that the purchase price would not change no matter what the results of their diligence might be.[876] It did change, because the Aussabayevs reneged on that commitment in the negotiations for the final SPA, reducing their offer on the purported basis that they would be required to pay the penalties that Kazakhstan had imposed in its harassment campaign.[877] But regardless, the fact that Claimants and the Aussabayevs agreed to a price before the Aussabayevs conducted substantial diligence is not evidence that the Aussabayevs were not serious buyers or were somehow closely related to the Claimants. Rather, it shows that the Aussabayevs were well-connected insiders who knew the value of the assets they were purchasing, and knew they were buying them at a bargain price due to the distress caused by Kazakhstan's actions. In fact, they presented themselves as insiders with close connections to the Ministry of Oil & Gas and full information about the companies when the negotiations began.[878]

592. Likewise, there is no merit to Kazakhstan's argument that the SPA was unusually short and vague regarding the obligations and liabilities of the companies that Cliffson was buying. That agreement did set out in detail the liabilities with third parties that Cliffson would be assuming.[879]

593. Additionally, the fact that the transaction did not close does not undermine its relevance as evidence of value of the companies. Kazakhstan asserts that Cliffson "tried to hinder the closing of the SPA," speculating that this is best explained by Cliffson realizing after it signed the SPA that it was paying more than fair market value. That speculation is totally unfounded.

594. First, Kazakhstan's argument that Cliffson failed to take steps to obtain government approval of the transaction mischaracterizes the evidence. The letter that Mr. Stati wrote to Cliffson on March 9, 2010, complained specifically that Cliffson had not

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875 Lungu Testimony, Tr. January 2013 Hearing, Day 1, 192:20-24.

876 Lungu Testimony, Tr. January 2013 Hearing, Day 1, 192:13-19.

877 Stati Testimony, Tr. January 2013 Hearing, Day 2, 91:23-92:16.

878 Lungu Testimony, Tr. January 2013 Hearing, Day 1, 191:25-192:6.

879 *See* Third FTI Report ¶ 7.12.

implemented its agreement in the Side Letter to the Cliffson SPA to cause the Kazakh government to back off from its harassment of KPM.[880] Claimants do not know if that was because Cliffson was unwilling or unable to obtain those results. In any event, that letter does not indicate that Cliffson had backed away from its obligation to work the back channels to obtain government approval of the sale transaction. To the contrary, Cliffson repeatedly told Claimants that they were working on obtaining government approval.[881]

595. Second, the fact that government approval of the transaction never came tells the Tribunal nothing about the reasons why it never came. In Claimants' view, it is because powerful interests in the Kazakhstan government who were planning to seize Claimants' investments persuaded the Aussabayevs not to proceed with the transaction, and Cliffson's June 7, 2010, letter backing out of the transaction was a pretext. It is also possible that the Aussabayevs realized they could not untangle the thicket of criminal investigations, convictions, penalties, tax assessments, and other results of Kazakhstan's harassment campaign as easily as they once believed. It is likewise possible that they had financial troubles of their own, and were unable to perform the transaction. In fact, any of those explanations is far more plausible than Kazakhstan's rank, illogical speculation that Cliffson belatedly realized that the fire-sale price it negotiated with a buyer under severe duress was more than fair market value for the assets untarnished by the government's actions. As FTI observes, absent a reason to believe that the buyer's re-evaluation of value was the reason that the transaction did not close, the agreed price remains a reliable indicator of value even though the transaction was not consummated.[882]

596. Accordingly, if the Tribunal elects to use a valuation date of July 22, 2010, it should award damages equal to no less than the US $924 million enterprise value of the Cliffson transaction. In fact, because Claimants accepted that transaction under substantial duress, the Tribunal should exercise its discretion to increase the amount of damages above the value of the transaction accordingly.

E. Enterprise Value Is the Correct Measure of Damages

597. Claimants seek an award of damages based on the enterprise value of their "Investments," KPM and TNG. "Enterprise value" means the value of the companies' assets without deducting the companies' debts. Enterprise value is the appropriate measure of

[880] Amendments to Cliffson Sale Agreement of February 13, 2010 and related documents, C-701.1.

[881] Lungu Testimony, Tr. January 2013 Hearing, Day 1, 196:18-22.

[882] Third FTI Report ¶ 7.9.

damages in investment treaty cases involving "investments" in wholly-owned companies established in the host State.

598. Kazakhstan argues that equity value — *i.e.*, assets minus debts — is the correct measure of damages. But Kazakhstan's position is wrong as a matter of treaty law, as well as illogical and unwarranted in light of the specific facts of this case.

599. The Tribunal's task is to value the harms caused by Kazakhstan to the "Investments" at issue in this case, namely, KPM and TNG. At its most basic level, Kazakhstan's "equity value" argument is wrong because it did not seize Claimants' equity in KPM and TNG. Rather, Kazakhstan seized all of the assets of KPM and TNG, without assuming or extinguishing their debts (including the main debt at issue, the Tristan notes). By seizing their assets, Kazakhstan left KPM and TNG unable to satisfy their debts. Accordingly, the injury suffered by Claimants' "Investments," KPM and TNG, includes not only the assets that were seized, but also the debts that the companies are unable to repay as a direct result of the asset seizures.

600. The ECT, scholarly commentary, and basic economic logic provides no support for Kazakhstan's invitation to the Tribunal to distinguish between the companies' assets and their debts and only award equity value. It would also clearly lead to the unjust enrichment of Kazakhstan, which has seized all the assets of KPM and TNG without assuming their liabilities.[883]

601. Kazakhstan is liable for the injuries suffered by Claimants' "Investments," KPM and TNG, irrespective of whether Claimants remain liable for the debts of the companies (but all the more so in light of the fact that Claimants do remain liable). The only relevant question regarding Kazakhstan's liability in relation to the companies' debts is whether its mistreatment of KPM and TNG — including its ultimate seizure of their assets — caused the companies to be unable to repay their debts (*i.e.*, whether there is a "causal link" between the State's illegal conduct and the companies' inability to satisfy their liabilities). That is clearly the case here.

602. There is no further requirement that Claimants demonstrate that they are directly responsible for KPM's and TNG's debts. Even if they were not directly responsible for those debts, Claimants would still own "Investments" (KPM and TNG) whose value has

[883] Conversely, no unjust enrichment would inure to Claimants, since damages in excess of the value of their equity stakes in KPM and TNG would and must be used to repay the companies' debts for which Claimants remain liable.

been decimated by being left with substantial liabilities that cannot be paid as a direct result of Kazakhstan's illegal conduct. Under the ECT and international law, Kazakhstan would remain liable to Claimants for decimating the value of their "Investments," and it would remain the Tribunal's task to quantify the loss in value suffered by those "Investments" as a result of Kazakhstan's treaty breaches. Whether or not Claimants are directly responsible for the companies' debts, the companies owned by Claimants — which are the protected "Investments" under the ECT — clearly suffered losses in value through 1) Kazakhstan's seizures of their assets, and 2) their consequent inability to pay their liabilities. Together, those two types of losses represent the "enterprise value" of KPM and TNG.

603. In this case, however, it is academic whether Kazakhstan is liable to pay "enterprise value" even if Claimants did not remain directly responsible for the debts of KPM and TNG. That is because 1) Claimants do, in fact, remain directly responsible for the debts of KPM and TNG; and 2) Kazakhstan agrees that insofar as Claimants remain responsible for those debts, "enterprise value" is the correct measure of damages.

604. In its Rejoinder on Quantum, Kazakhstan very plainly stated:

> By not deducting the debt under the Tristan notes from the asset values calculated by their expert, Claimants are essentially claiming damages that only the noteholders could allege to have suffered. Such approach would be correct if Claimants were themselves liable to the noteholders for such alleged damage. However, as set out above, due to the peculiarities of the securing mechanisms implemented, Claimants can practically no longer be liable.[884]

605. Thus, both sides fully agree that enterprise value is the correct measure of damages if Claimants remain responsible for the debts of KPM and TNG. While Kazakhstan is wrong that it would not be liable for enterprise value even if Claimants were not directly responsible for the debts of KPM and TNG (assuming its misconduct ruined KPM's and TNG's ability to pay those debts — which it did), there is no debate that Kazakhstan must pay enterprise value in the event Claimants are responsible for KPM's and TNG's debts.

[884] Rejoinder on Quantum ¶ 383 (emphasis added). Kazakhstan is not alone in this view. In the *Enron v. Argentina* case, the Tribunal stated: "The Respondent and its experts maintain that claiming compensation for 35.5% assumes that the Claimants are taking charge of CIESA's debt on their behalf, which is not the case, thus resulting in depleting CIESA and impeding that creditors collect their debt." *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3, Award, May 22, 2007 ¶ 194 (emphasis added), C-263. In other words, Argentina recognized that if the Claimants were in fact taking charge of such debt, it should not be deducted from the compensation due.

Claimants are, in fact, directly responsible for those debts, which puts the matter beyond doubt.

1. Enterprise Value Is the Correct Measure of Damage Under the ECT

606. Investment treaties are designed to protect covered "investments" in the host State, which more often than not are locally-incorporated companies or other business enterprises owned or controlled directly or indirectly by one or more foreign shareholders with the nationality of the other Contracting State to the treaty. The definition of "investment" under such treaties is invariably broad and usually expressly made without limitation. A locally-incorporated company or enterprise is almost always a covered "investment," because this is one of the most common forms of foreign direct investment.

607. The ECT is no different. It specifically defines as a covered "Investment" to mean "every kind of asset, owned or controlled directly or indirectly by an Investor," and specifically includes:

> 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…[885]

Here, the relevant "Investments" were KPM and TNG, each a "company or business enterprise" that was 100% "owned or controlled directly or indirectly" by Claimants. It follows from the ECT's plain language that Kazakhstan must compensate Claimants for the injury to KPM and TNG as a result of its mistreatment and seizure of all of their operating assets.

608. Nothing in the ECT supports Kazakhstan's argument that Claimants' damages are limited to the value of their shareholdings in KPM and TNG. The treaty broadly defines covered "Investment" to include "every kind of asset" that an Investor owns or controls *directly or indirectly*, specifically including a "company or business enterprise or shares, stock, or other forms of equity participation in a company or business enterprise…."[886] The use of the disjunctive "or" in this definition clearly provides that an "Investment" is not limited to an Investor's shareholding in a company or business enterprise, but in fact can include the company or business enterprise itself, and the assets of the company or business enterprise. There is no question that the assets of KPM and TNG are "Investments" protected

[885] ECT art. 1(6)(b), C-1.

[886] ECT art. 13(1), C-1.

by the treaty. Moreover, the expropriation section of the ECT clearly provides that the compensation due for a lawful expropriation "shall amount to the fair market value of the Investment expropriated."[887] Here, that was the assets of KPM and TNG, not their equity.

609. Scholarly commentary also supports this approach. For instance, in their well-known treatise *Damages in International Investment Law*, Ripinsky and Williams point specifically to the ECT as an example of a treaty whose definition of "investment" supports viewing damages from the perspective of the underlying business unit operating in the host State rather than the shareholding:

> For example, the Energy Charter Treaty defines investment as 'every kind of asset *owned or controlled directly or indirectly* by an Investor'. Under this kind of definition, appearing in many investment treaties, all assets which are owned or controlled directly or indirectly by an investor meet the treaty's definition of investment. Therefore, if a tribunal establishes that the claimant owns or controls the local subsidiary, there is room for finding that the underlying business unit (as opposed to the shareholding itself) is also indirectly owned by the claimant and, therefore, constitutes its protected investment.[888]

610. They also point out that "[t]he decision to treat the underlying business unit as the protected investment of a claimant-shareholder can be reached with greater comfort where the investment is entirely (albeit indirectly) owned and controlled by the claimant, particularly where the treaty specifically provides protections for investments indirectly owned and controlled."[889] That is precisely the case here because Claimants own 100% of the shares of KPM and TNG, and the ECT contains the requisite language regarding indirect ownership and control.

611. Kazakhstan's argument that damages under international law must be limited to equity value is wrong because, among other reasons, Kazakhstan falsely equates fair market value with equity value. In its opening at the Hearing on Quantum, Kazakhstan argued:

- Under international law, in principle, the fair market value at the valuation date has to be compensated
- Equity value — not enterprise value — reflects the fair market value

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887 ECT art. 1(6) (emphasis added), C-1.

888 Ripinsky & Williams, *Damages in International Investment Law* 2008, at 151 (footnote omitted) (emphasis in original), C-740.

889 Ripinsky & Williams, *Damages in International Investment Law* 2008, at 152, C-740.

- Any potential buyer of KPM and TNG would have deducted the companies' debt from KPM's and TNG's enterprise value
- Any fair market value claimed in these proceedings must hence fully reflect the companies' debt at the valuation date.[890]

That is a false syllogism and wrong as a matter of international practice. While fair market value is the typical measure for quantifying damages under international law, it does not follow that fair market value necessarily equates to equity value because assets also can be quantified according to their fair market value. As Mr. Rosen of FTI explained, enterprise value is "the value of the operating assets as determined appropriately, whether it's through an NPV or some other valuation mechanism to determine fair market value. That is the enterprise value."[891] Notably, Mr. Gruhn of Deloitte GmbH agreed with that characterization.[892]

612. Kazakhstan's supposition about what a potential buyer would have paid for KPM and TNG clearly illustrates this point, and the mistake in Kazakhstan's reasoning. It is only true that "[a]ny potential buyer of KPM and TNG would have deducted the companies' debt from KPM's and TNG's enterprise value" if the buyer were acquiring the equity, and thus assuming all the liabilities itself. Businesses are just as frequently sold in asset transactions, in which the buyer takes the assets and the seller retains the debts (or more commonly, pays off the debts from the proceeds of the sale). In an asset transaction, the purchase price is based on the fair market value of the assets being acquired (*i.e.*, the enterprise value), with no deduction for the amount of the debts that the seller retains. The situation here is equivalent to an asset transaction because Kazakhstan took the assets of KPM and TNG, but did not assume (or extinguish) those companies' liabilities.[893]

613. In short, the fact that fair market value is the typical measure of damages under international law says nothing about whether that measure should be applied to the underlying businesses or the claimants' equity stake. In this case, it is precisely because Kazakhstan seized the assets of KPM and TNG without assuming or extinguishing the debts that the fair

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890 Respondent's Opening Submission on Quantum, slide 58 (emphasis in original).

891 FTI Testimony, Tr. January 2013 Hearing, Day 4, 148:16-20.

892 Deloitte GmbH Testimony, Tr. January 2013 Hearing, Day 4, 149:2.

893 Similarly, Claimants are analogous to the seller in an asset transaction, who must use the proceeds of the "sale" (here, the award of damages) to pay off the debts for which they remain liable.

market value of the companies' assets (or "enterprises"), and not just the equity, is the appropriate measure of damages.

614. International practice likewise indicates that the Tribunal should adopt an enterprise valuation. As with many issues related to quantum, the starting point is the seminal decision in *Chorzów Factory*. In that case, the Permanent Court of International Justice followed this basic principle of compensation for violations of international law:

> 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.[894]

Here, the situation that would have existed but for Kazakhstan's illegal acts is that Claimants, as owners of KPM and TNG, were entitled to direct the cash flows of the enterprises as they deemed fit in the exercise of their management control. That situation naturally included the ability to use the cash flows of KPM and TNG to pay off the Tristan debt, and distribute the remaining cash flows to Claimants as dividends. To re-establish that situation, *i.e.*, to enable Claimants to pay off the Tristan debt out of the cash flows of KPM and TNG and receive the remaining cash flows free of all debt, compensation must be based on the discounted cash flows of the companies without first deducting the debt. Thus, under the basic principle of *Chorzów Factory*, compensation in this case must be based on the DCF value of the enterprises of KPM and TNG.

615. The case of *Enron v. Argentina* also addresses this issue, and further supports Claimants' position. In that case, Enron was a minority owner of the Argentine company TGS, owning some of TGS's equity directly and some through an Enron-controlled holding company, CIESA. Enron financed its capital contribution to TGS in part through a loan by Chase to CIESA, which Enron initially guaranteed. Addressing whether the value of Enron's stake in TGS should be reduced by the amount of the financing that Chase (a third party)

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[894] *Case Concerning the Factory at Chorzów (Ger. v. Pol.),* Judgment, Sept. 13, 1928,1928 P.C.I.J. (ser. A), No. 17, ¶ 125 (emphasis added), C-165.

provided to TGS through CIESA (a non-party affiliate of Enron), the Tribunal answered in the negative:

> The Tribunal notes that the financing of the parent company's (i.e., Enron) final investment (i.e., TGS) through the indebtedness of the holding company (i.e., CIESA) is a normal investment practice. Such practice will as a rule not affect the determination of the value of the shareholding for compensation purposes. In fact, because the parent company shall normally be liable for such debt, it would be entitled to recover the entire equity interest.[895]

616. The present case is very similar to *Enron*. The Tristan noteholders (*i.e.*, third parties equivalent to Chase) loaned money to KPM and TNG through Tristan Oil (*i.e.*, a non-party affiliate equivalent to CIESA), and Claimants (like Enron) guaranteed that debt through the Pledge Agreements. Thus, the normal rule stated by the *Enron* Tribunal that third-party financing "will as a rule not affect the determination of the value of the shareholding for compensation purposes" should apply in this case.

2. In Any Event, Enterprise Value Is the Correct Measure of Damage Because Claimants Remain Responsible for the Tristan Debt

617. In this case, however, it is academic whether Kazakhstan would be required to pay enterprise value for KPM and TNG even if Claimants were not responsible for the debts of KPM and TNG, because Claimants are responsible for the debts of KPM and TNG. Kazakhstan's arguments to the contrary are based on untenable interpretations of the security provisions for the Tristan debt that it manufactured belatedly at the Quantum Hearing after it originally misinterpreted those provisions in its prior submissions.

618. As noted above, Kazakhstan expressly admitted in its Rejoinder on Quantum that enterprise value "would be correct if Claimants were themselves liable to the noteholders."[896] Thus, both parties agree that enterprise value is the appropriate measure of damages — and equity value is not — insofar as Claimants remain directly responsible for KPM's and TNG's debts. Claimants do, in fact, remain directly responsible for those debts. As a consequence, there is no question that "enterprise value" is the appropriate measure of damages in this case.

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[895] *Enron Corporation and Ponderosa Assets, L.P. v. Argentine Republic,* ICSID Case No. ARB/01/3, Award, May 22, 2007, ¶ 392, C-263 (emphasis added). Enron subsequently ceased to guarantee the CIESA loan, and the Tribunal addressed this fact separately from the "normal rule" it just identified. Here, however, Claimants remain liable for the debt.

[896] Rejoinder on Quantum ¶ 383.

619. Kazakhstan's "equity value only" argument is based on the assumption that the Tristan debt is true third-party debt, *i.e.*, a loan from unrelated third parties directly into KPM and TNG for which Claimants have no liability. However, that assumption is wrong. The Tristan noteholders loaned money to KPM and TNG through Tristan Oil (which is wholly-owned by Mr. Stati), and Ascom and Terra Raf pledged their equity investments in KPM and TNG and any payments related thereto — including any proceeds of this arbitration — as security for the Tristan debt. Thus, the Claimants: (1) have always been obligated to repay the Tristan noteholders from the proceeds of any award; (2) further reinforced that obligation through the Sharing Agreement, and (3) have repeatedly, consistently, and unequivocally undertaken before this Tribunal (and for the avoidance of doubt, hereby commit and undertake yet again) to repay the Tristan noteholders from the proceeds of any award under the procedures set out in the Sharing Agreement.[897]

620. Accordingly, even if equity value were the standard measure of damages for the expropriation of an enterprise (which Claimants dispute for the reasons stated above), or even if it were relevant whether Claimants are directly responsible for the debts of KPM and TNG (which Claimants also dispute for the reasons stated above), enterprise value would still be the correct measure of damages here because Claimants retain their obligation to repay the Tristan debt out of their equity or any payments related thereto. By assuming that liability in the Pledge Agreements, Claimants effectively became lenders to KPM and TNG, and their continuing obligation to repay the Tristan noteholders out of the proceeds of any award is part of both Claimants' investment and the injury for which compensation is being awarded. Indeed, to award equity value rather than enterprise value would grossly undercompensate Claimants and unjustly enrich Kazakhstan.

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[897] In this respect, the situation here is rather analogous to the recent Award in *Occidental Petr. Corp. v. Ecuador*, ICSID Case No. ARB/06/11, Award, October 5, 2012, R-355. In that case, discussed in more detail below, the claimants, which were the US parent company Occidental Petroleum Corp. and its operating subsidiary, Occidental Exploration and Production Company ("OEPC"), sought damages for 100% of the losses they suffered when Ecuador expropriated OEPC's interest in an oil production-sharing agreement ("PSA"). Shortly before the expropriation, OEPC had attempted to farm out 40% of legal title to its interest in the PSA to Alberta Energy Corp. ("AEC"). Ecuador argued that the farmout was a breach of the PSA because it was unauthorized, and it cited that breach as the basis for its termination of the PSA. The Tribunal ultimately held that although the farmout was ineffective under New York and Ecuadorian law, Ecuador's act in terminating the PSA was tantamount to an expropriation. Turning to compensation, because the Tribunal had held that the farmout was ineffective, it held that OEPC remained owner of legal title to, and thus was entitled to claim for, 100% of the value of the terminated PSA, not just the post-farmout 60%. Importantly, however, it also relied on the fact that OEPC had entered into a separate post-termination agreement with AEC to deliver 40% of the proceeds of the Award, and that to award only 60% would unjustly enrich Ecuador. *Id.* ¶¶ 654-55. The same is true here, since Claimants are contractually obligated (through the pledges and/or Sharing Agreement, which is similar in effect to the OEPC-AEC agreement) to repay the Tristan noteholders from the proceeds of the award, and to award Claimants only equity value would cause a spectacular unjust enrichment to Kazakhstan.

a. Claimants Are Responsible for the Tristan Debt

621. As Claimants described more fully in Section VII.A of their Reply on Jurisdiction and Liability, and in Section I.B.2.b above, Tristan issued notes with a face value of US $531.1 million, which matured on January 1, 2012. Tristan, in turn, loaned most of the proceeds of those notes to KPM and TNG, which used the funds to retire other debt and to finance construction and operations.[898] Tristan was a special purpose entity that was formed to facilitate a single note offering secured by the combined assets of KPM and TNG. As such, Tristan had no assets to repay the notes, and the expectation of all parties was that the notes would be repaid from the profits of KPM and TNG. Consequently, KPM and TNG guaranteed repayment of all obligations under the Tristan notes.[899]

622. The KPM and TNG guarantees, however, were not the only security for the Tristan notes. Ascom and Terra Raf also pledged 100% of their Participation Interests in KPM and TNG — *i.e.*, all of their equity in the companies — as security for the Tristan notes.[900] Moreover, those Pledge Agreements not only pledged Ascom and Terra Raf's Participation Interests as security for the notes, but also any money that Ascom and Terra Raf receive in respect of those Participation Interests. It is worth revisiting that provision in full:

> On the occurrence of an Event of Default, (a) the Collateral may be realised in whole or in part by the Pledgeholder in a compulsory extra-judicial procedure in accordance with Kazakhstan Law or otherwise as may be permitted by Kazakhstan Law or any other applicable law, and (b) the Pledgeholder is entitled to receive and apply any and all dividend and other payment or distributions of any kind relating to the Participatory Interest as if the Pledgeholder were the holder of the Participatory Interest in and towards discharge of the Secured Obligations until such time as the Secured Obligations are fully discharged without prejudice to its rights under the Documents and without any obligation to exercise such rights prior to enforcement of or action under this Agreement, and (c) exercise the voting rights attached to the Participatory Interest.[901]

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[898] Of the US $420 million raised through the first two note offerings in 2006 and 2007, Tristan loaned US$325 million to KPM and TNG. *See* Audited Financial Statements attached to 2007 Annual Report of Tristan Oil at F-62, R-37.5. Tristan loaned approximately US $75 million of those proceeds to Terra Raf, and the remainder of the proceeds (approximately US $20 million) paid expenses of the note offerings. *Id*. The US $111.1 million of notes issued in June 2009 were issued as security for a US $60 million loan facility from Laren Holdings. *See* Second Lungu Statement ¶ 10.

[899] *See* Tristan Note Indenture ¶ 11.01, C-584.

[900] *See* Ascom and Terra Raf Pledge Agreements § 6, C-585.

[901] *See* Ascom and Terra Raf Pledge Agreements § 6 (emphasis added), C-585.

The underlined language plainly obligates Ascom and Terra Raf to satisfy the claims of the Tristan noteholders out of any payments they receive relating to their Participatory Interests in KPM and TNG, which would include any payments they receive through an award in this arbitration.

623. In its Rejoinder on Quantum, Kazakhstan simply misconstrued the Pledge Agreements. Kazakhstan argued that the pledges by Ascom and Terra Raf "were limited to their shares [in KPM and TNG]. For Ascom and Terra Raf, this follows from the fact that the collateral pledged in Section 2 of the respective pledge agreements is not the full capital of Ascom and Terra Raf but rather only the shares in KPM and TNG."[902] In support of this assertion, Kazakhstan cites Section 1 of the Pledge Agreements, which defines "Collateral" to mean "the Participatory Interest and all dividends and other distributions connected to the Participatory Interest."[903] Kazakhstan, however, completely ignores Section 6 of the Pledge Agreements (even though that is the provision cited by Claimants in paragraph 572 of their Reply on Jurisdiction and Liability). Section 6 plainly granted the Tristan noteholders security rights that were greater than the defined term "Collateral." Section 6(a) addresses the noteholders' rights to realize the "Collateral," but Section 6(b) gives the noteholders an additional right to "receive and apply any and all dividend and other payment or distributions of any kind relating to the Participatory Interest."[904] Whether deliberately or inadvertently, Kazakhstan simply ignored that provision in its Rejoinder on Quantum, and argued incorrectly that any claim by the noteholders against Ascom and Terra Raf "would be limited to the value of the shares pledged."[905]

624. After Claimants pointed out Kazakhstan's apparent mistake in its Opposition to Respondent's Application for Postponement of the Quantum Hearing,[906] Kazakhstan quickly changed its argument. At the Hearing on Quantum, Kazakhstan for the first time pressed the argument that "only payments by KPM and TNG are covered" by Section 6(b) of the Pledge Agreements, and "[t]he provision aims to ensure that Claimants cannot withdraw capital from the companies and thus devalue the pledges."[907] Nothing in Section 6(b) of the Pledge Agreements supports that argument. The provision broadly applies to "<u>any and all</u>

[902] Rejoinder on Quantum ¶ 376(f).

[903] Rejoinder on Quantum ¶ 376(f), n. 317.

[904] *See* Ascom and Terra Raf Pledge Agreements § 6, C-585.

[905] Rejoinder on Quantum ¶ 383, n. 328.

[906] *See* Claimants' Opposition to Respondent's Application for Postponement of the Hearing on Quantum, January 7, 2013 ¶¶ 20-21.

[907] Respondent's Opening Submission on Quantum, January 2013 Hearing, slide 62.

dividend and other payment or distributions of any kind relating to the Participatory Interest." The provision contains no hint of a restriction in its application to payments received from KPM and TNG, although it would have been quite easy to include such a restriction if one had been intended.

625. Moreover, while one aim of Section 6(b) no doubt was to ensure that the noteholders would receive the benefit of any capital distributions that might devalue the pledges, the language clearly is broad enough also to ensure that the noteholders receive the benefit of any payments Claimants receive as compensation for Kazakhstan's mistreatment or expropriation of the companies (which likewise devalued the pledges). Moreover, as Squire Sanders noted in its legal due diligence review for KMG E&P, transfer of the participation interests pursuant to the Pledge Agreements is subject to the State's preemptive right under Article 71 of the Subsoil Law.[908] That raises the prospect that Ascom and Terra Raf may be unable to deliver their Participation Interests in KPM and TNG to the noteholders, and instead would receive compensation from Kazakhstan for those shares upon the State's exercise of its preemptive right. It thus stands to reason that a key purpose of the provision in Section 6(b) was to ensure that the noteholders received the benefit of any payments from Kazakhstan in respect of Ascom and Terra Raf's Participation Interests in KPM and TNG. That is exactly what an award in this arbitration would represent, albeit as the result of violations of the ECT rather than through the legitimate exercise of Kazakhstan's preemptive right.

626. It is very nice for Kazakhstan to provide its opinion to the Tribunal regarding the meaning of contracts to which it is not a party, but Kazakhstan's self-serving interpretation of Section 6(b) is no guarantee that an ICC arbitration tribunal — which would decide any dispute between the noteholders and Ascom and Terra Raf under Section 12 of the Pledge Agreements — would agree with that position. In fact, not only do Claimants believe they likely would lose such an argument, but also they do not agree that Kazakhstan's interpretation was what the parties to the Pledge Agreements intended them to mean. Kazakhstan's position in essence would require Claimants to press unreasonable, aggressive, and arguably bad-faith arguments in an effort to stiff their creditors in order to mitigate their losses and reduce the damages that Kazakhstan must pay. Kazakhstan has cited no authority, however, and Claimants are aware of none, that requires Claimants to do anything of the sort.

[908] Squire Sanders Legal Due Diligence Report, July 30, 2009, at 66, C-725.

b. The Sharing Agreement Did Not Create or Materially Alter Claimants' Obligations Regarding the Tristan Debt

627. At the Hearing on Quantum, Kazakhstan compounded its misreading of the Pledge Agreements with the ridiculous argument that Claimants had voluntarily assumed liability to the Tristan Noteholders under the Sharing Agreement:

> - With the Sharing Agreement, Claimants may have agreed to partially pay the noteholders with the amounts due under a possible award in their favour.
> - However, the Claimants assumed such liability voluntarily and after the fact.
> - The Republic cannot be held liable for such unilateral action of Claimants.[909]

That argument fundamentally misconstrues the Sharing Agreement, which was a renegotiation of Claimants' existing obligations rather than a voluntary assumption of new liability. Moreover, Claimants do not seek to hold Kazakhstan liable under the Sharing Agreement. An award of enterprise value is proper independent of the Sharing Agreement, and the Sharing Agreement is only relevant to this arbitration insofar as it confirms Claimants' intent to perform their contractual obligations to the Tristan noteholders.[910]

628. Along with Tristan Oil, Claimants entered into the Sharing Agreement with a subgroup of the Tristan noteholders on December 17, 2012. The Sharing Agreement was subsequently presented to all of the Tristan noteholders through a consent solicitation that ended on February 14, 2013, with holders of 99.8% of the Tristan notes accepting the Sharing Agreement.[911] Thus, the Sharing Agreement effectively amended the Tristan notes and related security arrangements for essentially all of the Tristan noteholders.

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[909] Respondent's Opening Submission on Quantum, slide 63.

[910] As noted, the *Occidental* Tribunal relied on a similar *ex post* agreement in awarding OEPC 100% of the value of its expropriated PSA, the proceeds of which OEPC was obliged to deliver 40% to AEC, its farmout partner. The Tribunal quoted the agreement in pertinent part as follows: "If Occidental receives any monetary award from the Government of Ecuador as a result of the Government's actions to enforce caducity and terminate Occidental's contract with respect to Block 15, Occidental agrees that the Company [AEC] is entitled to a 40% share in the net amount received, after all costs and expenses of the Caducity Proceedings have been reimbursed or paid (in calculating such amount there shall be no double counting)." *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. Republic of Ecuador*, ICSID Case No. ARB/06/11, Award, October 5, 2012 ¶ 654, n.114, R-355. In the same way that the Sharing Agreement reinforced Claimants' existing obligations to the Tristan noteholders under the Pledge Agreements, the OEPC-AEC agreement reinforced OEPC's existing obligations to AEC under the farmout agreement. In no way did the Tribunal consider that the *ex post* nature of the agreement rendered it a "voluntary" one to be disregarded for compensation purposes. The same is true here.

[911] Tristan Oil Press Release, "Completion of Offer to Exchange and Consent Solicitation," February 19, 2013, C-741.

629. The Sharing Agreement and related implementing agreements have the length and complexity that one would expect of an agreement affecting publicly-traded debt, but the essential terms are fairly straightforward:

- Claimants agree to continue diligent pursuit of this arbitration and to use commercially reasonable efforts to collect any award in the arbitration;[912]
- Claimants agree not to settle their claims against Kazakhstan without the Participating Noteholders' consent (unless the settlement would result in full payment to the Participating Noteholders);[913]
- Claimants agree to deposit any proceeds received from the arbitration in a secure trust account in New York;
- The trustee of that account will distribute the proceeds according to an agreed distribution "waterfall," in which:
    - The first US $15 million will go to Claimants to cover legal fees associated with the arbitration and negotiation and implementation of the Sharing Agreement;[914]
    - The next US $3 million will go to the Noteholders who negotiated the Sharing Agreement and the Trustee to cover their legal fees;[915]
    - Sums received thereafter will be shared 70% to the Participating Noteholders and 30% to Claimants until the Participating Noteholders receive all of the principal and interest due under the Modified Notes;[916] and
    - Any additional amounts will go 100% to Claimants;[917]
- The Participating Noteholders agree to forebear from pursuing default-related remedies until January 1, 2016;[918]
- On January 1, 2016, Claimants and Tristan Oil will receive a release on the following terms:
    - If the Participating Noteholders have received a specified "Minimum Payment" (set at 70% of the

[912] Sharing Agreement ¶ 5(c), C-721.

[913] Sharing Agreement ¶ 5(b), C-721.

[914] Sharing Agreement § 4(b)(i), C-721.

[915] Sharing Agreement § 4(b)(ii), C-721.

[916] Sharing Agreement § 4(b)(iii), C-721. The Modified Notes did not alter the principal or interest accrued before January 1, 2012, but did alter the amount of interest due after January 1, 2012 by tying it to the rate of interest awarded in this arbitration. *Id*. § 1 (definition of Outstanding Amount and Special Interest).

[917] Sharing Agreement § 4(b)(iv), C-721.

[918] Sharing Agreement § 6(a), C-721.

principal and interest outstanding on January 1, 2012, plus interest thereon), Claimants will receive a total release and Tristan Oil can redeem the Modified Notes for US $1;[919] or

- If the Participating Noteholders have not received the Minimum Payment, the Modified Notes and existing security agreements remain in effect, but Claimants receive a release of any liability they may have outside of those security agreements and the Sharing Agreement.[920]

630. Thus, to be certain, Claimants did not assume any new monetary liability to the Tristan noteholders in the Sharing Agreement. As discussed in the preceding section, the Pledge Agreements always obligated Ascom and Terra Raf to turn over any proceeds of this arbitration to the Tristan noteholders from dollar one.[921] Far from assuming new liability, the Sharing Agreement simply reorders the respective priorities of the Claimants and Participating Noteholders so that Claimants will share in any proceeds of this arbitration from dollar one. Kazakhstan's suggestion that Claimants would voluntarily assume liability to share 70% of any award in this arbitration when they had no previous obligation to do so assumes that Claimants are patently naïve, and borders on the absurd.

631. Furthermore, the Sharing Agreement does not materially reduce Claimants' basic liability to the Tristan noteholders either, at least insofar as the award in this arbitration is in the range requested by Claimants. In that case, the payment priority "waterfall" will result in total payments to the Tristan noteholders and Claimants that are almost identical to the situation that would have resulted under the Pledge Agreements (*i.e.*, the noteholders are repaid in full, and Claimants receive 100% over that amount). The fundamental purpose and effect of the Sharing Agreement is to provide both sides with a clear set of agreed rights and obligations that are most relevant if the award in this arbitration is significantly less than the range requested by Claimants. In that case, Claimants will share in the award from dollar one and receive a total release in 2016 (if the noteholders have recovered at least 70% of the amount outstanding). In exchange, the noteholders ensure that Claimants are properly

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[919] Sharing Agreement § 7(a), C-721.

[920] Sharing Agreement § 7(c), C-721.

[921] The Sharing Agreement does apply personally to Anatoli and Gabrial Stati, who previously had not given any personal guarantees or pledges through which the Tristan noteholders could assert claims to the proceeds of this arbitration. This, however, was not a material expansion of Claimants' liability to the Tristan noteholders. Claimants have never requested, and would not expect the Tribunal to indulge any request, to structure an award in this case to "cut out" Ascom and Terra Raf so as to avoid their obligations under the Pledge Agreements.

incentivized to pursue collection of any award (which may not have been in Claimants' interests if all proceeds would go to the noteholders under the Pledge Agreements), and also receive a right to approve any settlement.

632. Claimants and Kazakhstan do agree on one thing — the Sharing Agreement arose long after the fact, and thus should not have any bearing on the calculation of the amount due to Claimants as of the Valuation Date. Claimants, however, do not base their claim for enterprise value on the Sharing Agreement in any way. Rather, to the extent Claimants' liability to the noteholders is relevant to that issue, that liability is found primarily in the Pledge Agreements, which were in effect on the Valuation Date. The Sharing Agreement is relevant only insofar as it reconfirms Claimants' intent to honor their obligations to the Tristan noteholders and underscores the inaccuracy of Kazakhstan's claim that Claimants do not remain responsible for those obligations.

c. Awarding Equity Value Would Undercompensate Claimants and Unjustly Enrich Kazakhstan

633. The fundamental aim of the principle of full compensation under international law is to ensure that an injured party is fully compensated by a State's unlawful acts, and to ensure that the State is not unjustly enriched by its unlawful acts. Here, an award of equity value would grossly undercompensate Claimants and unjustly enrich Kazakhstan.

634. First, an award of equity value would grossly undercompensate Claimants for the value of their equity. By way of example (using a hypothetical round numbers for simplicity of explanation), if the assets of KPM and TNG that Kazakhstan seized had a fair market value of US $1 billion and the outstanding Tristan debt were US $531 million, the value of Claimants' equity in KPM and TNG would be US $469 million. If the Tribunal awarded just the equity value (US $469 million in this example), that entire amount would go to satisfy Ascom and Terra Raf's liability to the Tristan noteholders under Section 6 of the Pledge Agreements (without considering the impact of the Sharing Agreement, which is discussed below). In other words, an award of equity value would in fact give Claimants less than the full value of their equity because some (and perhaps all) of the award would go to satisfy liabilities to third parties that, but for Kazakhstan's violations, would have been satisfied with the profits of KPM and TNG. In contrast, an award of the enterprise value (US $1 billion in this illustrative example) would satisfy Ascom and Terra Raf's liability to the Tristan noteholders, leaving Claimants with the value of their equity interest in KPM and TNG (US $469 million in the example), free and clear of all debts. Thus, an award of

enterprise value is the proper measure of compensation to put Claimants in the position they would have occupied but for Kazakhstan's violations.

635. Additionally, an award of equity value would unjustly enrich Kazakhstan by allowing it to obtain assets unencumbered by liabilities for a fraction of their value. In the same example, for instance, an award of equity value would allow Kazakhstan to obtain assets worth US $1 billion while paying only US $469 million to Claimants. Claimants' subsequent payment to the noteholders under the Pledge Agreements would effectively eliminate any claims that the noteholders may have against the assets of KPM and TNG, or against Kazakhstan itself (to the extent that the noteholders have any claims directly against Kazakhstan, which to date they have never asserted). Thus, an award of equity value in this illustrative example would allow Kazakhstan to keep assets worth US $1 billion while paying only US $469 million, and without facing any further liabilities. In contrast, an award of the enterprise value (US $1 billion in this example) would require Kazakhstan to pay the full value of the assets its expropriated, and would not subject Kazakhstan to any further liability (because any claims of the noteholders would be extinguished by Claimants' performance of their obligations under the Pledge Agreements).

636. The Sharing Agreement does change the order of allocation of any award proceeds between Claimants and the Noteholders, but only until the Noteholders are fully repaid. That fact does not (1) result in any unjust enrichment to Claimants from an award of enterprise value; or (2) fully ameliorate the gross undercompensation to Claimants and unjust enrichment of Kazakhstan that would result from an award of equity value. For instance, in the illustrative example above, an equity value award of US $469 million would be divided under the Sharing Agreement with US $318.7 million to the Noteholders and US $150.3 million to Claimants. Thus, Claimants would still receive far less than the actual value of their equity, and Kazakhstan would still receive assets worth US $1 billion while paying only US $500 million. In contrast, an enterprise value award of US $1 billion would still be divided under the Sharing Agreement with US $531 million to noteholders and US $469 million to Claimants.[922]

[922] This calculation ignores the effect of interest for purposes of clearly illustrating this point. In fact, the Sharing Agreement bases the cap on what the Participating Noteholders can receive not on the original US $531 million face value of the notes, but on the value including interest at the time of recovery. That amount was US $642,643,100 as of January 1, 2012, and will grow at the rate of interest that the Tribunal grants in its award. *See* Sharing Agreement § 1 (definitions of Original Amount, Outstanding Amount, and Special Interest), C-721. Because it is not known what that amount will be at the time of recovery, and

637. Kazakhstan's argument at the Hearing on Quantum that an enterprise value award would unjustly enrich Claimants is based entirely on the Sharing Agreement, and assumes that the enterprise value is less than or close to the value of the debt. Under Kazakhstan's view that the correct enterprise value is only US $186 million, Claimants' equity would be worth nothing, but Claimants would receive US $65.4 million of an enterprise value award under the Sharing Agreement.[923] Such an outcome, however, would not be in any way unjust because it results from a voluntary renegotiation of the priority of claims between Claimants and the noteholders that the noteholders voluntarily accepted. Kazakhstan would still pay only US $186 million for assets worth US $186 million in such a scenario, and thus any "enrichment" of Claimants would be at the (voluntary) expense of the noteholders, not Kazakhstan. In contrast, an award of equity value (US $0 in Kazakhstan's view) would still result in gross unjust enrichment to Kazakhstan by allowing it to obtain assets worth at least US $186 million for free.

638. In part because of this risk of undercompensation to Claimants and unjust enrichment to wrongdoing States, it has long been observed that damages should not be reduced by the amount of any obligations that Claimants owe to third parties. That is true even if that means that third parties ultimately may receive a portion of the proceeds of the arbitration by virtue of contractual or other enforceable undertakings by Claimants to those third parties. For example, in considering what scope of injuries are compensable under international law, the *Chorzów Factory* court explained:

> On approaching this question, it should first be observed that, in estimating the damage caused by an unlawful act, only the value of property, rights and interests which have been affected and the owner of which is the person on whose behalf compensation is claimed, or the damage done to whom is to serve as a means of gauging the reparation claimed, must be taken into account. This principle, which is accepted in the jurisprudence of arbitral tribunals, has the effect, on the one hand, of excluding from the damage to be estimated, injury resulting for third parties from the unlawful act and, on the other hand, of <u>not excluding from the damage the amount of debts and other obligations for which the injured party is responsible</u>. The damage suffered by the Oberschlesische in respect of the Chorzów undertaking is therefore equivalent to the total value — but to that total only — of the

because the amount of interest granted by the Tribunal should mirror the additional amounts due on the notes due to interest, the point above is more clearly understood without considering the effect of interest.

[923] Respondent's Opening Submission on Quantum, slides 67-68.

> property, rights and interests of this Company in that undertaking, without deducting liabilities.[924]

Thus, Claimants' damages should not be reduced by the amount of their obligations to the Tristan noteholders (or anyone else) because such a reduction would undercompensate Claimants and unjustly enrich Kazakhstan.

639. More recently, the tribunal in *Occidental v. Ecuador* applied that principle to reject Ecuador's efforts to reduce the award by deducting obligations that the claimant OEPC owed to third parties. In that case, OEPC had entered into a Farmout Agreement that purported to sell 40% of its stake in the local operating company to a third party, AEC. The Tribunal determined that the assignment in the Farmout Agreement was invalid, and thus that OEPC could recover 100% of the value of the investment. Ecuador, however, argued that the award nonetheless needed to be reduced by 40% to avoid overcompensating OEPC for an interest that it already had sold to AEC. Relying on the *Chorzów Factory* passage cited in the previous paragraph, the *Occidental* Tribunal flatly rejected that argument:

> In relation to unjust enrichment, there was produced to the Tribunal the letter agreement of February 22, 2006 between OEPC and Andes whereby OEPC is obliged to compensate Andes to the level of 40% of any compensation it receives from action taken against Ecuador regarding the termination of the Participation Contract. Even without this letter agreement, the Tribunal notes that the invalidity of the assignment under New York and Ecuadorian law does not mean that AEC (or Andes) may not have recourse against OEPC under the Farmout Agreement. As mentioned earlier, the unauthorized assignment does not invalidate the Farmout Agreement as between the assignor, OEPC and the assignee, AEC nor is the legal position affected by the fact that the assignor and the assignee actually implemented *inter se* parts of the legally invalid and unauthorized assignment. OEPC promised to deliver certain rights to AEC under the Farmout Agreement, but due to its failure to secure authorisation from the Ministry it was in breach of that promise. This breach of contract may form the basis of a claim by AEC (or Andes) against OEPC. These factors weigh heavily against any unjust enrichment arguments raised in respect to OEPC's entitlement to receive compensation for 100% of the interests in the Participation Contract.
>
> In this respect, by far the greater risk of unjust enrichment lies at the door of Ecuador. Ecuador would be unjustly enriched if only obliged to compensate for 60% of a 100% unlawful taking. …

[924] *Case Concerning the Factory at Chorzów (Ger. v. Pol.),* Judgment, Sept. 13, 1928, 1928 P.C.I.J. (ser. A), No. 17 ¶ 79 (emphasis added), C-165.

> As a matter of international law, any liability that OEPC might have to AEC or Andes under various other agreements (including the Farmout Agreement) does not affect the Claimants' right to receive compensation from Ecuador. Ecuador cannot discount OEPC's claim by reference to liabilities that may be owed to third parties such as AEC. This principle is clearly recognised in the *Chorzów Factory* dictum [quoting the passage discussed above].[925]

640. Similarly, Kazakhstan here cannot discount Claimants' claim by reference to liabilities that Claimants owe to third parties, such as the Tristan noteholders. To do so would result in undercompensation to Claimants and unjust enrichment to Kazakhstan, and runs afoul of longstanding principles of international law.

3. Enterprise Value Damages Likewise Should Not Be Reduced by the Vitol, Tax, and Other Alleged Debts

641. In addition to the primary Tristan debt, Kazakhstan also argues that a damages award to Claimants must be reduced by the amount of other debts allegedly owed by KPM and TNG, including: (1) amounts owed to Vitol under the COMSA prepayment terms and LPG financing arrangements; (2) outstanding debts under the Laren facility; and (3) the US $62 million corporate back tax assessment. Kazakhstan's argument is wrong. Those alleged debts should not be deducted from Claimants damages for all the reasons applicable to the Tristan debt, discussed above, as well as for some additional reasons particular to those alleged debts. Thus, Claimants will briefly address those alleged debts separately.

a. Obligations to Vitol

642. Kazakhstan asserts that Claimants' damages must be reduced by amounts owed to Vitol in two different, but related, ways. First, Kazakhstan argues that Claimants' damages for the LPG Plant must be reduced by some unspecified amount because Vitol was a fifty-fifty joint venture partner in the LPG Plant.[926] Second, Kazakhstan argues that Claimants' damages must be reduced by the amount of the debt allegedly owed by Montvale to Vitol under the COMSA prepayment arrangement, which KPM and TNG guaranteed.[927] Those arguments are legally and factually mistaken.

643. To begin with, Vitol never owned any equitable interest in the LPG Plant whatsoever. Rather, Vitol was party to a contractual arrangement in which it was supposed to

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[925] *Occidental Petroleum Corporation and Occidental Exploration and Production Company v. Republic of Ecuador*, ICSID Case No. ARB/06/11, Award, October 5, 2012 ¶¶ 654-56, R-355.

[926] Rejoinder on Quantum ¶¶ 208-211.

[927] Rejoinder on Quantum ¶ 386.

provide half of the financing for the construction of the LPG Plant (although it did not) in exchange for the right to market the offtake of the plant and receive a portion of the plant's profits.[928] As Mr. Lungu explained:

> Q. Did Vitol own part of the LPG plant?
>
> A. No, Vitol never had an ownership right in the LPG plant. Vitol had, under the joint operating agreement, had rights to profits, to future profits that would be generated from the operations of the LPG plant, but they never had a title.
>
> Q. Were those rights in the nature of an ownership interest in the plant or were they a contractual obligation?
>
> A. These were contractual obligations. So by contract, whenever the project, the LPG plant, would produce or generate certain profits, then those profits were supposed to be distributed in a way that both Vitol and us would decide.[929]

Additionally, the prepayment arrangement that KPM and TNG guaranteed was the mechanism through which Vitol was supposed to fund its portion of the debt financing for construction of the LPG Plant.[930]

644. Furthermore, both Ascom and Terra Raf are parties to the Joint Operating Agreement with Vitol for the LPG Plant project.[931] That agreement addressed the rights of the parties upon termination, including in the event that the Government of Kazakhstan asserted rights to the LPG Plant:

> Parties expressly agree that, in case of a termination of this Agreement, they shall cooperate and act in such a manner so that, at all times, with no exception (save as required by law, unless agreed differently in writing between the Parties), the VITOL Rights shall be transferred into the direct or indirect full ownership of ASCOM. In the event that the Government seeks to assert any rights of pre-emption, VITOL will still be entitled to payment from ASCOM of the Fair Value price at the time prescribed in Clause 8.3 and ASCOM shall seek to recover such amounts from the Government.[932]

Thus, under the very agreement that Kazakhstan contends required TNG to share its profits with Vitol, the parties contemplated that all of Vitol's rights would transfer to Ascom upon

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928 LPG Joint Operating Agreement, First FTI Scope of Review No. 44.

929 Lungu Testimony, Tr. January 2013 Hearing, Day 1, 185:22-186:9.

930 LPG Joint Operating Agreement § 2.3, First FTI Scope of Review No. 44; *see also* Lungu Testimony, Tr. January 2013 Hearing, Day 1, 185:4-6.

931 LPG Joint Operating Agreement, First FTI Scope of Review No. 44.

932 LPG Joint Operating Agreement § 11.4, First FTI Scope of Review No. 44.

termination, and that Ascom would seek compensation from the Government in the event the government asserted ownership rights over the LPG Plant.

645. Thus, this situation perfectly illustrates the soundness of the principle articulated by the court in *Chorzów Factory*, and applied recently by the tribunal in *Occidental v. Ecuador*, that a claimant's damages should not be reduced by the amount of its contractual obligations to third parties. The issue before this Tribunal is the value of Claimants' "Investments," including the LPG Plant, that Kazakhstan seized illegally. Vitol never had any ownership interest in that Plant and was never an "Investor" for purposes of the ECT. To the extent that Claimants owe contractual obligations to Vitol under the Joint Operating Agreement, that issue is not before this Tribunal.[933] Accordingly, the Tribunal should not consider any such obligations, which are disputed, in calculating the amount of compensation due to Claimants for the assets that Kazakhstan wrongfully seized.

b. Laren Debt

646. As discussed above, Claimants' entry into the Laren transaction is one of the injuries caused by Kazakhstan's illegal actions. Kazakhstan has not and cannot explain why it ever would be appropriate to reduce Claimants' damages by the amount of indebtedness that Kazakhstan itself caused Claimants to undertake.

647. In any event, the Laren loan facility has been repaid.[934] Thus, even under Kazakhstan's incorrect argument, it would be improper to deduct the amount of that debt from any damages awarded to Claimants.

c. Alleged Corporate Back Tax Obligations

648. As discussed above in Section III.B.4, Kazakhstan's position on the corporate back tax dispute is wrong on the merits. Kazakhstan engineered that tax claim as part of its campaign to harass Claimants. Moreover, KPM and TNG prevailed in their court challenges of the tax assessment, and the only appellate decision finding in favor of Kazakhstan came after Claimants' investments were seized, in a review process that Claimants did not participate in or even know about. The US $62 million tax debt is invalid and itself a

[933] To be clear, the exact extent of Claimants' obligations to Vitol, if any, under the Joint Operating Agreement currently are unsettled because Vitol breached its obligation to provide 50% of the financing for the LPG Plant. By the end of the relationship, Vitol had reduced the amount of its total financing for the LPG Plant to only US $66 million by drawing down on its prepayments under the TNG and KPM COMSAs. This Tribunal, however, need not decide that dispute.

[934] Lungu Testimony, Tr. January 2013 Hearing, Day 1, 191:2-21.

violation of Claimants' rights under international law, and thus it would be inappropriate to reduce the amount of the enterprise value of Claimants' investments by such an invalid debt.

649. Moreover, the US $62 million that Kazakhstan claims is not the actual amount that Claimants would owe even if Kazakhstan's legal argument were correct. That is because the disputed tax issue concerned the timing of deductions, not whether the deductions were proper at all. Thus, even if KPM and TNG improperly deducted some expenses in 2005-2007, they would have been entitled to claim higher deductions in later years that would have reduced their taxes in those years. The benefit of those deductions is not included in the US $62 million assessment, and Kazakhstan has presented no evidence of the actual amount of net tax debt, if any, that KPM and TNG owed even if its legal argument were correct.

F. Claimants Are Entitled to Recover Compound Interest

650. As discussed in Claimants' Statement of Claim and Reply on Quantum, it is well-settled under international law that an award of interest is appropriate to fully compensate Claimants for the injury caused by Kazakhstan.[935] Likewise, the overwhelming trend in recent years has been to award compound interest in investment treaty cases because compound interest is the norm in commercial financing transactions, and thus compound interest is necessary to fully compensate the Claimants for the loss of opportunity to invest the funds.[936] In its Rejoinder on Quantum, Kazakhstan does not dispute the appropriateness in general of awarding interest, and compounding that interest, in this case.[937]

651. Rather, Kazakhstan argues that the rate of interest should be set "based on what Claimants could have earned by investing the amounts due under the award," and proposes the extremely low benchmark rate applicable to 6-month U.S Treasury bills.[938] There are several fundamental problems with that argument.

652. First, the "investment approach" proffered by Kazakhstan — *i.e.*, that the rate should mirror what Claimants could have earned by investing the amount due under the award — is not well-suited to the facts of this case because Claimants have maintained debt that would have been paid off but for Kazakhstan's conduct. As Ripinsky and Williams note (citing Professor Marboe):

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935 Statement of Claim ¶¶ 468-49; Reply on Quantum § IV.

936 *See* Reply on Quantum ¶¶ 89-90.

937 Rejoinder on Quantum § E.I.

938 Rejoinder on Quantum ¶¶ 482 and 493.

> [I]f a loan was taken in order to bridge the period without the money, it is evident that the interest actually paid by the claimant becomes the measure of damages. In these circumstances, it would be appropriate to use the interest rate equal to the one charged to the claimant.[939]

653. Claimants plainly have incurred debt that they would not have incurred but for Kazakhstan's actions. Most importantly, if Kazakhstan had not commenced its illegal campaign in 2008, Claimants would not have incurred the Laren debt and would have paid off the Tristan notes. The interest rate on the Laren loan (not including the value attributable to the US $111 million in new notes issued in connection with that loan) was 35%, and that loan remained outstanding until late 2011.[940] The loan on the Tristan notes, which remain outstanding today, is 10.5%. Thus, an interest rate of 10.5% conservatively reflects Claimants' actual borrowing costs that are attributable to Kazakhstan's misconduct.

654. In fact, if the Tribunal does not award interest equivalent at least to the borrowing rate under the Tristan notes, then it should include as a component of its award the interest that has accrued on the Tristan notes since October 14, 2008. If Kazakhstan had not launched its campaign on that date, but instead had acquired Claimants' assets legally, Claimants would have paid off the notes and they would not have continued to accrue interest to this day. Thus, Claimants included a request for this component of damage in its Reply on Quantum.[941] The simplest way to compensate Claimants for this injury, however, is to award interest at the rate of 10.5%.

655. Alternatively, even if the Tribunal elects to follow the "investment approach," the rate of U.S. T-bills is not an appropriate rate. Claimants could have earned a much higher return on investing the amounts due under the award if they had been paid promptly when Kazakhstan began its campaign in 2008. Claimants are not in the business of investing in U.S. Treasury bills; they invest in oil and gas projects around the world, including in Iraq and Southern Sudan, that have the potential for enormous returns on investment. An award of interest based on U.S. T-bill rates would dramatically undercompensate Claimants for the lost ability to invest that capital in projects that fully utilize the Claimants' substantial technical and economic expertise.

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939 Ripinsky & Williams, DAMAGES IN INTERNATIONAL INVESTMENT LAW (BIICL 2008) at 370, C-740, *citing* I. Marboe, "Compensation and Damages in International Law: The Limits of Market Value," 7 *Journal of World Investment and Trade* 754 (2006).

940 *See* Laren Settlement Agreement, June 11, 2009, C-733.

941 Reply on Quantum § V.

656. While Claimants are not advocating an interest rate based on the internal rate of return on their other investments, this point does highlight that the rate of interest should be tailored to what an investor like the Claimants, rather than a hypothetical investor anywhere in the world, could have earned by investing the funds. The Tribunal in *Sylvania v. Iran* observed this concept when it held that, absent a contractual rate, it "will derive a rate of interest based approximately on the amount that the successful claimant would have been in a position to have earned if it had been paid in time and thus had the funds available to invest in a form of commercial investment in common use in its own country."[942] Thus, a rate of interest available from a commercial bank in Moldova is more appropriate than the rate on U.S. T-bills. FTI has provided the applicable interest rates in its Third Report at paragraph 13.2 and Figure 32.

657. Moreover, Kazakhstan's argument that the interest rate should be based on U.S. T-bill rates because the currency of the award will be in U.S. dollars misses the mark. Claimants agree that there is a currency component to commercial interest rates, and that an appropriate rate should be a commercial rate applicable to investments of U.S. dollars. That does not equate, however, to a rate available in the United States, much less a rate applicable to U.S. T-bills. Moldovan commercial banks accept deposits in U.S. dollars, and thus an interest rate on U.S. dollar deposits in a Moldovan bank is the most appropriate rate of interest if the Tribunal follows the "investment approach." FTI has provided rates on U.S. dollar deposits available from a leading commercial bank in Moldova.

G. Claimants Are Entitled to Recover Moral Damages

658. Kazakhstan argues that the Tribunal should not award moral damages to Claimants because (i) it claims that the amount requested is not in line with investment arbitration jurisprudence;[943] and (ii) it alleges that the claim is based only on the "unfounded imprisonment of Mr. Cornegruta" and the May 2009 raid of KPM and TNG, neither of which caused any real moral harm to Claimants.[944] Both arguments are insufficient to relieve Kazakhstan of the responsibility to compensate Claimants for the significant stress, anxiety, mental anguish, and reputational harm that it imposed on them with its intimidation tactics, false criminal accusations, defamation, and ultimate, outright seizure of their investments.

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942 *Sylvania Technical Systems, Inc. v. Iran*, Iran-U.S. Cl. Trib., Award No. 180-64-1, June 27, 1985, C-742.

943 Rejoinder on Quantum ¶ 12.

944 Rejoinder on Quantum ¶ 500.

659. First, the amount of compensation that Claimants are seeking is not unreasonable, particularly given that it is not possible to put a monetary value on the personal distress Claimants suffered. Claimants have asked for a sum equivalent to 10% of the compensatory damages awarded. Kazakhstan's sole response to the amount claimed is to complain that if the Tribunal awards all of the compensatory damages Claimants request, the award of moral damage would be over US $250 million, which is "extraordinary" when compared to the US $1 million awarded in the *Desert Line* case.[945] That is simply irrelevant. This Tribunal is not bound by previous investment arbitration decisions and is free to decide on its own how much Claimants should be compensated for the moral harm they endured. Claimants have never questioned the Tribunal's discretion in awarding a figure it finds most appropriate to compensate for that harm.

660. Kazakhstan also focuses on Chief Investigator Rakhimov's account of the two-day raid the Financial Police carried out at KPM and TNG to suggest that there was nothing about Kazakhstan's conduct that merits an award of moral damages.[946] Not only does that argument ignore the more than 22 months of mistreatment Kazakhstan inflicted on Claimants, but also Mr. Rakhimov's account of that raid is in dispute. The account of Claimants' witness, Mr. Stejar, completely contradicts Kazakhstan's assertion that the Financial Police carried out the May 2009 raid with "consideration and caution."[947] Rather, Mr. Stejar explains that the raid was aggressive and intimidating. He states:

> The policemen had an aggressive attitude, and [they] explained that they would call for additional forces if anyone failed to cooperate. They suggested that backup forces were near the building. Because of their aggressive manner, some of our female employees became scared and began to cry. Our employees were aware that Mr. Cornegruta had been arrested several days before, and all feared what the Government might do next.... One member of our staff began to film the search in order to document what was going on, but a policeman ordered him to stop.... The policeman also stated that he had called for backup forces and that they were waiting outside for anyone who did not cooperate.[948]

661. The Financial Police's conduct during that raid was not in accordance with the legal standard Kazakhstan claims must be met here, namely whether the acts complained of

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945 Rejoinder on Quantum ¶ 517.

946 Rejoinder on Quantum ¶¶ 504-507.

947 Rejoinder on Quantum ¶ 507.

948 First Stejar Statement ¶¶ 16-17.

were carried out in a manner in which agencies of "civilized nations are expected to act."[949] Nor can any of the other ill-treatment that occurred from October 2008 to July 2010 — including a sham criminal prosecution that amounted to a denial of justice — be said to fall within that standard. Kazakhstan cannot escape the implications of all of its acts by myopically singling out either the May 2009 raid or the arrest and imprisonment of Mr. Cornegruta.

662. The claim for moral damage is a claim for the moral suffering of Claimants. It is not, as Kazakhstan contends, a claim brought by or on behalf of Mr. Cornegruta.[950] While Mr. Cornegruta obviously suffered greatly at the hands of Kazakhstan, it does not follow from that fact that Claimants were left unaffected. To the contrary, Claimants suffered through years of Kazakhstan's misconduct as it carried out its pre-meditated plan. As Mr. Cojin explains, KPM's and TNG's managers worked in Kazakhstan under threats and harassment, while being targeted, monitored, and followed by the Financial Police, before they were finally forced to flee the country.[951] Kazakhstan has not disputed that testimony.

663. Nor can Kazakhstan deny that it had issued arrest warrants for three of Claimants' managers in addition to Mr. Cornegruta. All of those actions caused tremendous stress, anxiety, and other mental suffering for Mr. Stati and Claimants' other senior management. They had to endure the effects of Kazakhstan's mistreatment of their personnel and attacks on their own reputations, from afar, and with no recourse. They had to watch helplessly as the personnel they hired to work in Kazakhstan were relentlessly hunted by the Financial Police, while one was arrested on a false pretext and sentenced to four years in Kazakh jail. The idea that none of Kazakhstan's harmful actions caused Claimants any moral suffering could not be further from the truth. Therefore, Claimants firmly maintain their request for moral damages.

VI. REQUEST FOR RELIEF

664. For the reasons set forth herein, Claimants respectfully request an award granting them the following relief:

- A declaration that Kazakhstan has violated the ECT and international law with respect to Claimants' investments;

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[949] Rejoinder on Quantum ¶ 503; *See also*, Statement of Defense ¶ 55.2(b).

[950] Rejoinder on Quantum ¶ 513.

[951] *See, e.g.*, First Cojin Statement ¶¶ 15, 22.

- Compensation to Claimants for all damages they have suffered, as set forth in Claimants' Statement of Claim and Reply on Quantum and as further updated at the January 2013 Hearing and in this submission, currently corresponding to the following amounts:

Tolkyn	**US $478,927,000**
Borankol	**US $197,013,000**
Munaibay Oil	**US $96,808,000**
LPG Plant	**US $245,000,000 cost plus discretionary portion of US $84,077,000**
Contract 302 (other than Munaibay Oil)	**US $31,330,000 cost plus discretionary portion of US $1,498,017,000**

- All costs of this proceeding, including Claimants' attorneys' fees and expenses as well as fees and expenses of the Tribunal and the SCC;

- Pre-award compound interest at a rate of 10.5% from October 14, 2008 to the date of the Award;

- An award of compound interest at a rate of 10.5% until the date of Kazakhstan's final satisfaction of the Award; and

- Any other relief the Tribunal may deem just and proper.

Dated: April 8, 2013

Respectfully submitted,

KING & SPALDING

Reginald R. Smith
Kevin D. Mohr
James E. Toher
1100 Louisiana, Suite 4000
Houston, Texas 77002
U.S.A.

Kenneth R. Fleuriet
Héloïse Hervé
Amy Roebuck Frey
12, Cours Albert 1er
75008 Paris
France

Alexandra Kotlyachkova
Valeriya Subocheva
Tsvetnoy Bulvar, 2
127051 Moscow
Russian Federation