

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

WASHINGTON D.C.

IN THE PROCEEDING BETWEEN

SGS SOCIÉTÉ GÉNÉRALE DE SURVEILLANCE S.A.

(Claimant)

and

THE REPUBLIC OF PARAGUAY

(Respondent)

ICSID Case No. ARB/07/29

Award

Members of the Tribunal:

Dr. Stanimir A. Alexandrov, President

Mr. Donald Francis Donovan

Dr. Pablo García Mexía

Secretary of the Tribunal: Mrs. Mercedes Cordido-Freytes de Kurowski

Representing Claimant:

Mr. Olivier Merkt and Mr. Nicolas Grégoire
*Société Générale de Surveillance S.A., Geneva,
Switzerland*

and

Mr. Paul Friedland and Mr. Damien Nyer
White & Case LLP, New York

Representing Respondent:

Dr. José Enrique García Ávalos
*Procurador General de la República del Paraguay,
Asunción, Paraguay*

and

Mr. Brian C. Dunning, Ms. Irene Ribeiro Gee,
and Mr. David Cinotti
Venable LLP, New York

Date of Dispatch to the Parties: 10 February 2012

Table of Contents

I.	PROCEDURAL BACKGROUND.....	1
A.	Initiation of the Arbitration.....	1
B.	Objections of Respondent to Jurisdiction	2
C.	Decision on Jurisdiction.....	3
D.	Submissions on the Merits	4
E.	Hearing on the Merits	4
F.	Submissions on Costs and Fees and the Closure of the Proceedings	5
II.	FACTUAL BACKGROUND.....	5
A.	The Contract.....	5
B.	Unpaid Invoices	8
C.	Discussions Regarding Respondent’s Failure to Pay Invoices During the Term of the Contract.....	9
D.	Uncontested Nature of the Facts.....	18
III.	MERITS OF CLAIMS.....	18
A.	Assessment of Claims Under Article 11 of the BIT	19
1.	Tribunal’s Decision on Jurisdiction	20
2.	Whether Respondent Has Failed to Guarantee the Observance of Its Contractual Commitments	22
3.	Article 11 Claims Based on Alleged Extra-Contractual Commitments	46
IV.	CLAIMANT’S REMAINING CLAIMS	47
V.	RESPONDENT’S CLAIM OF PREJUDICE.....	48
VI.	DAMAGES.....	49
A.	Claimant’s Position.....	49
B.	Respondent’s Position.....	51
C.	Tribunal’s Analysis.....	52

VII.	COSTS	54
VIII.	AWARD	55

I. PROCEDURAL BACKGROUND

A. Initiation of the Arbitration

1. On 19 October 2007, the International Centre for Settlement of Investment Disputes (“ICSID” or the “Centre”) received a request for arbitration dated 16 October 2007 (the “Request”) from SGS Société Générale de Surveillance S.A. (“SGS” or “Claimant”) against the Republic of Paraguay (“Paraguay” or “Respondent”) (collectively, the “parties”). The Request was made under the Agreement on the Promotion and Reciprocal Protection of Investments between Switzerland and Paraguay signed 31 January 1992 and entered into force 28 September 1992 (the “BIT” or the “Treaty”), and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (“ICSID Convention” or “Convention”).
2. On 19 November 2007, the Deputy Secretary-General of ICSID sent Claimant and Respondent a Notice of Registration in accordance with Article 36(3) of the ICSID Convention.
3. On 30 January 2008, Claimant requested, in accordance with Rule 2(3) of the ICSID Rules of Procedure for Arbitration Proceedings (“Arbitration Rules”), that the Arbitral Tribunal be constituted in accordance with the provisions of Article 37(2)(b) of the Convention. This letter was acknowledged by a letter from ICSID to the parties of the same date. It was accordingly confirmed that: (1) the Tribunal would consist of three arbitrators; (2) one arbitrator would be appointed by each party and the third, the president of the Tribunal, would be appointed by agreement of the parties; and (3) the appointments would follow the procedures set out in Rule 3 of the Arbitration Rules.
4. By letter dated 31 January 2008, Claimant appointed Mr. Donald Francis Donovan, Esq., a national of the United States of America, as a member of the Tribunal. On 31 March 2008, Respondent appointed Dr. Pablo García Mexía, a national of Spain. No objections were raised to either appointment.
5. On 20 February 2008, the parties having failed to reach agreement on the appointment of the President of the Tribunal, Claimant requested the appointment of the presiding

arbitrator by the Chairman of the ICSID Administrative Council as provided for in Article 38 of the Convention and Rule 4(1) of the Arbitration Rules.

6. By letter of 20 May 2008, the Chairman of the ICSID Administrative Council appointed Dr. Stanimir A. Alexandrov, a national of Bulgaria, as the third arbitrator and president of the Tribunal. No objections were raised to this appointment.
7. The Tribunal was officially constituted on 27 May 2008, in accordance with the Convention and ICSID Arbitration Rules. Mr. Gonzalo Flores, Senior Counsel, ICSID, was initially designated to serve as the Secretary of the Tribunal. On 16 April 2009, the Acting Secretary-General informed the Tribunal that due to the redistribution of the Centre's workload, Dr. Sergio Puig de la Parra, ICSID, would serve as the new Secretary of the Tribunal. On November 5, 2010, the Secretary-General informed the Tribunal that Dr. Puig would be replaced by Mrs. Mercedes Cordido-Freytes de Kurowski.

B. Objections of Respondent to Jurisdiction

8. On 8 April 2008, Respondent submitted a Memorial with Objections to Jurisdiction to the Centre. At the first session of the Tribunal on 30 June 2008, Respondent provided a supplemental submission on its objections to jurisdiction. The supplemental submission was dated 26 June 2008. The two submissions together constituted Respondent's Memorial on Jurisdiction.
9. Claimant submitted its Counter-Memorial on Jurisdiction on 22 September 2008.
10. The first session of the Tribunal was held at the seat of the Centre in Washington, D.C. At the session, the Tribunal heard the parties' proposals for addressing the objections to jurisdiction raised in Respondent's Memorial with Objections to Jurisdiction. It was agreed that the proceedings on the merits would be suspended as envisaged in Article 41(2) of the ICSID Convention and Arbitration Rule 41(3) pending resolution of Respondent's jurisdictional objections.
11. The hearing on Respondent's objections to jurisdiction was held in Washington, D.C., on 6 April 2009.

12. The parties were represented as follows:

Claimant

Mr. Paul Friedland, Mr. Mark Luz, Mr. Rafael E. Llano Oddone and Mr. Damien Nyer, White & Case LLP

Mr. Nicolas Grégoire, SGS

Respondent

Dr. José Enrique García Ávalos, Attorney General of the Republic of Paraguay

Mr. Raúl Sapena, Counsel to the Treasury of the Republic of Paraguay

Mr. Jorge Brizuela, Embassy of the Republic of Paraguay in Washington, D.C.

Mr. Pedro Espínola Vargas Peña, Advisor to the Executive Director, the World Bank

Mr. Agustin Saguier Abente, Saguier Abente Law Firm

Mr. Brian C. Dunning and Ms. Irene R. Dubowy, Thompson & Knight LLP

13. Messrs. García and Dunning and Ms. Dubowy addressed the Tribunal on behalf of Respondent. Mr. Friedland addressed the Tribunal on behalf of Claimant.

14. On 9 June 2009, Respondent wrote to draw the Tribunal's attention to the decision on jurisdiction rendered on 29 May 2009 in the case of *BIVAC v. Paraguay*.¹ The Tribunal granted both parties leave to file brief post-hearing submissions limited to the relevance of the *BIVAC* decision to arguments already put forward by the parties in the present case. Respondent made its filing by letter dated 3 July 2009, with Claimant following suit by letter dated 23 July 2009.

C. Decision on Jurisdiction

15. On 12 February 2010, the Tribunal issued its Decision on Jurisdiction. The Tribunal dismissed Respondent's objections and concluded that it had jurisdiction to decide Claimant's claims under Articles 4(1), 4(2) and 11 of the Treaty. The Tribunal decided

¹ *Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC B.V. v. Republic of Paraguay*, ICSID Case No. ARB/07/9, Decision of the Tribunal on Objections to Jurisdiction, 29 May 2009.

to reserve any decision on the allocation of costs until the conclusion of the proceedings. A copy of the Decision on Jurisdiction is attached to this Award, and is part of it.

D. Submissions on the Merits

16. After consultation with the parties, the Tribunal issued a procedural order on 24 March 2010 setting the schedule for submissions on the merits.
17. On 31 May 2010, Claimant submitted its Memorial on the Merits. Claimant also submitted witness statements from Mr. Carlos Musalem, the SGS Country Manager in Paraguay during the events giving rise to this dispute, and Mr. Michael Lironi, Vice President, Finance and Administration, of the Governments and Institutions Services Division of SGS in Geneva.
18. By letter dated 10 September 2010, counsel for Respondent requested a modification of the submission schedule to allow Respondent an additional six weeks, until 1 November 2010, to submit its Counter-Memorial. By letter dated 15 September 2010, Claimant proposed an alternative deadline of 6 October 2010. On 16 September 2010, the Tribunal informed the parties that it decided to grant Respondent's request to move the due date of the Counter-Memorial to 1 November 2010. On that date, Respondent submitted its Counter-Memorial on the Merits.
19. On 28 February 2011, Claimant submitted its Reply on the Merits. Claimant also submitted a second witness statement from Mr. Musalem. On 1 April 2011, Respondent submitted its Rejoinder on the Merits.

E. Hearing on the Merits

20. The hearing on the merits was held in Washington, D.C. on 4 May 2011 and 5 May 2011.
21. The parties were represented as follows:

Claimant

Mr. Paul Friedland, Mr. Rafael E. Llano Oddone, Mr. Francisco Guzman and Mr. Damien Nyer, White & Case LLP

Mr. Nicolas Grégoire and Mr. Olivier Merkt, SGS

Respondent

Dr. José Enrique García Ávalos, Attorney General of the Republic of Paraguay

Mr. Raúl Sapena, Counsel to the Treasury of the Republic of Paraguay

Mr. Brian C. Dunning and Mr. David N. Cinotti, Venable LLP

22. Messrs. Friedland and Nyer addressed the Tribunal on behalf of Claimant. Messrs. García, Dunning and Cinotti addressed the Tribunal on behalf of Respondent.
23. Mr. Musalem testified in person, and Mr. Lironi testified by video conference. Both Mr. Musalem and Mr. Lironi were examined and cross-examined on the first day of the hearing.
24. At the end of the hearing, the President of the Tribunal requested that the parties prepare submissions on costs and fees, and that such submissions be presented to the Tribunal no later than the end of July 2011.

F. Submissions on Costs and Fees and the Closure of the Proceedings

25. On 1 July 2011, Respondent provided its Statement of Costs, in which it claimed US\$ 696,985.20 in fees and US\$ 31,222.03 in costs. On the same day, Claimant provided its Statement of Costs, in which it claimed US\$ 1,792,605.95 in legal fees and US\$ 1,121,180.55 in other costs and disbursements. On January 24, 2012, the Tribunal declared the proceedings closed, pursuant to Rule 38(1) of the Arbitration Rules.

II. FACTUAL BACKGROUND

A. The Contract

26. In 1995, the Ministry of Finance of Paraguay invited five companies – SGS; Bureau Veritas, Inspection, Valuation, Assessment and Control, BIVAC B.V. (“BIVAC”); Cotecna Inspection S.A.; Inchcape Testing Services Ltd.; and Inspectorate Worldwide Services – to submit their bids to provide “pre-shipment” inspection services, *i.e.*, services involving the inspection of imported goods prior to shipment to ensure the

accurate collection of import information and facilitate collection of customs duties. SGS and BIVAC were selected. On 6 May 1996, the Ministry of Finance and SGS signed an Agreement on the Rendering of Technical Services for Import Pre-shipment Inspection (the “Contract”).² The Contract was to remain in effect for three years, starting on 15 July 1996.

27. Under the heading “NATURE AND SUBJECT-MATTER OF THE AGREEMENT,” the Contract states that the pre-shipment inspection program was designed “with the purpose of optimizing the tax collection volume and to improve the mechanisms for controlling the compliance with the tax obligations referred to [*sic*] the import transactions”³
28. In broad terms, the Contract required SGS to provide three categories of “technical services”:
29. Under Articles 2.1 through 2.8 of the Contract, SGS was to provide pre-shipment inspection and related services, which would include the issuance of Inspection Certificates or Discrepancy Reports, as discussed below.
30. Under Article 2.9 of the Contract, SGS was to provide training to Paraguayan Customs officials that would “include . . . the techniques used by SGS personnel, the technical, administrative and organizational procedures, with the purpose of reaching an efficient and effective execution and protection of tax revenues and to make up a body of officials specialized in customs valuation.”
31. Under Article 2.10 of the Contract, SGS was to help create a Customs database for organizing the information in the Inspection Certificates and train Paraguayan officials to use the database.
32. The process for conducting pre-shipment inspections took place in several stages. Importers would submit requests to an SGS liaison office in Paraguay to inspect designated shipments. SGS established a liaison office in Asunción, as well as two smaller offices in Ciudad del Este and Encarnación, to assist in its performance under the

² Contract, Ex. C-4.

³ Contract, Ex. C-4.

Contract. If SGS determined that an inspection was necessary, it would, pursuant to Article 2.1 of the Contract, “carry out the physical inspection of goods prior to shipment, in the country of origin, in order to determine if the goods submitted to inspection correspond to what the importer has declared to SGS.” In certain instances, SGS informed an importer that an inspection was not necessary.⁴ Pursuant to Article 2.2 of the Contract, if SGS determined that an inspection was necessary, it would “verify the price invoiced by the seller and . . . establish whether this is within the reasonable limits, for the export price levels, prevailing in such market or in the international market.” In accordance with Articles 2.3 and 2.4 of the Contract, SGS would provide Customs with its opinion on the appropriate customs value and tariff classification of the shipment, and, under Article 2.6, verify the country of origin.

33. After the inspection, pursuant to Article 2.8 of the Contract, SGS would provide Customs with a copy of either an Inspection Certificate or, if SGS disagreed with the importer’s shipment documentation, a Discrepancy Report. Under Article 5.2 of the Contract, SGS would also provide Customs with a monthly report that would include, among other things, the details of the inspections conducted during the month.
34. Under Article 4 of the Contract, for each inspection, Paraguay agreed to pay SGS the larger of (a) a fee equal to 1.3% of the FOB value of the goods shown in the Inspection Certificate or the Discrepancy Report or (b) US\$ 280. SGS would send the Ministry a monthly invoice denominated in U.S. dollars, and the invoices were to be paid within 20 days after receipt. Under Article 4.5 of the Contract, if the Ministry of Finance disputed an invoice, the Ministry was required to pay any undisputed amounts. According to Article 5.6 of the Contract, SGS was not to be “liable for any claim not filed within twelve (12) months upon the issuance date of the Inspection Certificate.”
35. Pursuant to Article 5.4 of the Contract, SGS posted a US\$ 250,000 performance bond.
36. Article 9 of the Contract contained a forum selection clause that stated that “[a]ny conflict, controversy or claim deriving from or in connection with this Agreement,

⁴ Day 1 Tr. (Merits) at pp. 163-164.

breach, termination or invalidity, shall be submitted to the Courts of the City of Asunción under the Law of Paraguay.”

37. The Contract contained several mechanisms for termination. Under Article 7.1 of the Contract, either party could terminate the Contract for non-compliance by the other party. Under Article 7.2, the Ministry of Finance could, with 120 days’ notice, unilaterally terminate the Contract on grounds of “opportunity, merit or convenience.” Finally, under Article 8.2, the Contract would terminate if, at least four months before the Contract was to expire, either party notified the other party that it did not intend to renew the Contract.
38. In addition to the Contract, Paraguay issued several regulations governing the provision of services. These included Resolution 1171 of 3 July 1996 (“Resolution 1171”) that, among other things, required inspections for small shipments valued at less than US\$ 3,000 when such shipments were part of a larger order or a consolidated bill of lading that exceeded US\$ 3,000. In addition, Resolution 1579 of 10 September 1996 (“Resolution 1579”) exempted certain shipments from pre-shipment inspection, including “[a]quellas importaciones liberadas y las exoneradas de los tributos aduaneros e internos, contenidas en las disposiciones de caracter general o en Leyes Especiales.”⁵

B. Unpaid Invoices

39. The Contract commenced in July 1996. As discussed in detail below, the parties decided by mutual agreement not to renew the Contract at the end of its initial three-year term, and the Contract was terminated in June 1999. During the term of the Contract, SGS conducted approximately 100,000 inspections and issued 35 monthly invoices.⁶ The Ministry of Finance paid only 10 of those invoices.⁷ Twenty-five of SGS’s 35 invoices were not paid, totaling (in principal, not including interest) US\$ 39,025,950.86.⁸ These facts are not in dispute.

⁵ Respondent translates this provision as exempting from inspection “any and all tax free imports free and clear of those duties or internal taxes, as described in general or special laws.” Respondent’s Counter-Memorial at para. 24. The translation in Claimant’s Ex. C-76 is slightly different: “Those imports released and those exempted from customs duties and internal taxes contained in the general provisions or Special Laws.”

⁶ Lironi Statement at para. 17.

⁷ Lironi Statement at para. 17.

⁸ Lironi Statement at para. 18.

C. Discussions Regarding Respondent's Failure to Pay Invoices During the Term of the Contract

40. Between July 1996 and the time when the Contract was terminated in June 1999, officials from SGS and the Government of Paraguay engaged in an ongoing dialogue regarding the unpaid invoices and the terms of the Contract.
41. Paraguay paid the invoices covering the period July-November 1996. The December 1996 invoice was paid several months late⁹ and the Paraguayan Congress failed to allocate funds to pay Claimant's invoices for 1997.¹⁰ According to Mr. Musalem, the Minister of Finance told SGS in March 1997 that the failure to allocate funds for 1997 was an oversight and that "a provision would be made for the payment of the invoices in the budget of the following year."¹¹
42. In an exchange of letters with the Ministry of Finance in March and April 1997, SGS offered to modify the payment terms of the Contract, and the Ministry of Finance offered to pay SGS at least in part for services performed in 1997.¹² The Ministry of Finance also indicated in its letter that it "would propose a budget increase to the National Parliament" so that the payments might be increased later in 1997 and that, "starting in January 1998, the payments would be made normally and regularly since we would be including these expenses in the 1998 budget."¹³
43. SGS eventually accepted a repayment plan proposed by Paraguay. It also agreed to reduce the minimum fee to US\$ 200 per inspection and agreed to two changes with respect to inspections of oil products.¹⁴ First, SGS agreed to reduce retroactively the *ad valorem* fee on oil products from 1.3% to 0.8% of the FOB value for the period January-

⁹ Lironi Statement, Annex B.

¹⁰ First Musalem Statement at para. 35; Ex. C-84.

¹¹ First Musalem Statement at para. 35.

¹² Claimant's Memorial at 57-58, *citing* Exs. C-82 and C-83; First Musalem Statement at para. 37.

¹³ Letter from Ministry of Finance to SGS and BIVAC dated 7 April 1997, Ex. C-83.

¹⁴ Letter from SGS and BIVAC to Customs dated 7 October 1997, Ex. C-87.

August 1997. SGS credited the Ministry for the difference.¹⁵ Second, SGS agreed to stop inspections of oil products altogether as of 1 September 1997.¹⁶

44. In the meantime, SGS continued to conduct inspections and submit monthly invoices to the Ministry. In July 1998, the Ministry sent a letter to SGS in which it “acknowledge[d] receipt of [SGS’s invoices]” that “pertain[ed] to the preshipment inspection services rendered to the government of the Republic of Paraguay,” totaling, at that time, approximately US\$ 24 million, and stated that “[t]his sum represents the outstanding debt payable by the Paraguayan State in favor of SGS.”¹⁷ The letter also stated as follows:

This Ministry wishes to comply with the payment for the services rendered in 1998 pursuant to the contractual provisions and with respect to the debt accrued in 1997, we inform you that this Ministry is reviewing and analyzing the possibilities and legal mechanisms that would permit the regularization of this debt to our mutual satisfaction.¹⁸

45. In September 1998, the Ministry of Finance requested that the Office of the Comptroller General of Paraguay review the SGS and BIVAC contracts.¹⁹ SGS claims that it learned of this investigation through the newspapers.²⁰ SGS informed the Ministry of Finance that it was willing to work with the Comptroller to resolve any outstanding issues.²¹ At SGS’s request, SGS met with the Comptroller General on 11 November 1998,²² and, on 2 December 1998, wrote a letter to the Comptroller General explaining that it believed payment was being withheld due to the Comptroller General’s inquiry and offering its assistance to provide whatever information was needed.²³ In a letter to SGS dated 9 December 1998, the Comptroller General stated that “the work of the Office of the Comptroller General at the Ministry [of Finance] has nothing to do with the payment of

¹⁵ Letter from SGS to the Ministry of Finance dated 1 October 1997, Ex. C-86.

¹⁶ Letter from SGS to the Ministry of Finance dated 1 October 1997, Ex. C-86; Letter from SGS and BIVAC to Customs dated 7 October 1997, Ex. C-87; First Musalem Statement at para. 38; Lironi Statement at para. 16.

¹⁷ Letter No. 663 from Minister of Finance to SGS Liaison Office General Manager dated 28 July 1998, Ex. C-16.

¹⁸ Letter No. 663 from Minister of Finance to SGS Liaison Office General Manager dated 28 July 1998, Ex. C-16.

¹⁹ Comptroller General Resolution No. 853 dated 30 September 1998, Ex. C-19.

²⁰ Claimant’s Memorial at paras. 71-72, *citing* Letter from SGS to the Ministry of Finance dated 16 November 1998, Ex. C-97.

²¹ Letter from SGS to the Ministry of Finance dated 16 November 1998, Ex. C-97.

²² First Musalem Statement at para. 41; Letter from SGS to the Comptroller General dated 2 December 1998, Ex. C-98.

²³ Letter from SGS to the Comptroller General dated 2 December 1998, Ex. C-98.

fees for services rendered”²⁴ The Comptroller General issued its report on 22 February 1999, and recommended that the Ministry of Finance prepare technical studies to “determine whether the contracting of these inspection companies, really contribute [*sic*] to optimize the volume of the tax collections and to improve the mechanisms for controlling the compliance with the tax obligations, so as to be able to determine the economic convenience of this type of contracting”²⁵

46. By 1999, the parties began to speak openly of terminating the Contract. On 27 January 1999, SGS told the Ministry of Finance that it would be authorized to terminate the Contract within 15 business days if Paraguay did not make a good faith partial payment of US\$ 5,000,000.²⁶ The Ministry responded by a letter dated 29 January 1999, in which it stated that the delays in payment were due to “the mismanagement of the year 1998 Budget carried out by the previous Government, as it was publicly and timely denounced by this Administration and many of these commitments were not even accounted for, with the logical difficulty involved.” The letter went on to state that the “current Administration will soon start to make [dis]bursements in order to meet the obligations that have been assumed and fulfilled in accordance with the legal rules in force.”²⁷
47. On 19 February 1999, the President of Paraguay issued a decree authorizing the Ministry of Finance to terminate its contracts with SGS and BIVAC pursuant to Article 8.2 of the Contract, which, as noted, allows a party not to renew the Contract after expiration of the initial three-year term.²⁸ According to Mr. Musalem, the Minister of Finance told SGS a few days later that he would try to make a good faith payment on the outstanding debt, and, soon thereafter, the Ministry paid SGS’s August 1998 invoice.²⁹ SGS wrote to the

²⁴ Claimant’s Memorial at paras. 74-75; Letter from the Comptroller General to SGS dated 9 December 1998, Ex. C-99.

²⁵ Report by the Comptroller General of Paraguay entitled “Special Exam on the Contracting Process of the Companies B.I.V.A.C. International and S.G.S. de Surveillance” dated 22 February 1999, Ex. C-101.

²⁶ Claimant’s Memorial at para. 77; Letter from SGS Senior Executive Vice President to Minister of Finance dated 27 January 1999, Ex. C-26.

²⁷ Claimant’s Memorial at para. 78, Letter No. 111 from Minister of Finance to SGS (Geneva) dated 29 January 1999, Ex. C-27.

²⁸ Claimant’s Memorial at para. 80, *citing* Decree No. 2003 dated 19 February 1999, Ex. C-28.

²⁹ Claimant’s Memorial at paras. 85-86; First Musalem Statement at para. 44; Lironi Statement, Annex B; Letter from SGS to Ministry of Finance dated 23 February 1999, Ex. C-102.

Minister of Finance on 10 March 1999, stating that, in light of the payment, it would delay terminating the Contract.³⁰

48. The Government of Paraguay resigned in March 1999 following the assassination of the Vice-President. According to Claimant, the new President, Luis González Macchi, met with SGS and asked that it continue providing services. According to Mr. Musalem, “[d]uring this meeting, the President also called the newly appointed Minister of Finance and instructed him to grant [SGS] a meeting in order to reach an agreement to put an end to [SGS’s] claim.”³¹ According to Mr. Musalem, a few days later “the Minister [of Finance] reiterated the Government’s commitment to pay SGS”³² In April, SGS wrote a letter to the Minister of Finance explaining that it would postpone terminating the Contract and expressing the hope that it would be paid.³³ SGS also referred to the possibility of entering into a new agreement with the Ministry.
49. On 30 April 1999, the Ministry of Finance sent a letter to SGS indicating that the Ministry “has referred the case in question to various technical offices of the Institution for their information and consideration. Once these offices have made the relevant report, the Ministry of Finance will be ready to take a stance on the matter.”³⁴
50. According to Mr. Musalem, the Ministry of Finance and SGS mutually agreed in a meeting on 1 June 1999 to terminate the Contract.³⁵ The effective date for termination was fixed as 7 June 1999.³⁶ The Ministry wrote to SGS, stating the parties’ obligations under the Contract would be terminated “except for the rights and actions already acquired”³⁷ SGS agreed and referred to the outstanding amounts owed under the

³⁰ Claimant’s Memorial at para. 86; Letter from SGS to Ministry of Finance dated 10 March 1999, Ex. C-106.

³¹ First Musalem Statement at para. 46.

³² First Musalem Statement at para. 47.

³³ Claimant’s Memorial at para. 92; Letter from SGS to Ministry of Finance dated 6 April 1999, Ex. C-107.

³⁴ Letter from Ministry of Finance to SGS dated 30 April 1999, Ex. C-108; Claimant’s Memorial at para. 93.

³⁵ Claimant’s Memorial at para. 94; First Musalem Statement at para 50.

³⁶ Claimant’s Memorial at para. 96.

³⁷ Letter No. 1083 from Minister of Finance to SGS Senior Executive Vice President dated 4 June 1999, Ex. C-32.

Contract through May 1999.³⁸ The Ministry of Finance released the performance bond posted by SGS.³⁹

51. In July 1999, the Prosecutor General asked the Ministry of Finance to withhold payment from SGS and BIVAC “until such time as the [Comptroller General’s] Special Examination has concluded, unless these firms submit supporting documentation to sufficiently prove the outstanding debt.”⁴⁰
52. In a letter dated 22 July 1999 from SGS to the Minister of Finance, SGS stated that the parties “agreed [at an earlier meeting] on the settling of the outstanding debt.”⁴¹ However, on 27 August 1999, the Minister of Finance responded by stating that, “With respect to this, I am sorry to express that it is impossible to proceed as requested, due to the reasons personally described during [our] conversation”⁴² SGS expressed disappointment and offered new terms for resolving the matter.⁴³ On 20 October 1999, the Administrative Director of the Ministry of Finance provided a chart to SGS summarizing the outstanding invoices totaling US\$ 39,025,950.31.⁴⁴
53. Press reports from November 1999 indicated that the 2000 National Budget did not allocate funds to pay SGS.⁴⁵ According to Claimant, this fact was confirmed in a report by the Swiss Embassy of meetings in July 2000 between Swiss and Paraguayan officials.⁴⁶ According to the report, Mr. Rubén Darío Maciel, Director General for Budget, stated:

³⁸ Letter from SGS Vice President to Minister of Finance dated 4 June 1999, Ex. C-33.

³⁹ Claimant’s Memorial at para. 97, *citing* Lironi Statement at para. 22; UBS Letter to SGS dated 12 October 1999, Ex. C-115.

⁴⁰ Claimant’s Memorial at para. 99; Letter from Prosecutor General to Ministry of Finance dated 14 July 1999, Ex. C-110.

⁴¹ Claimant’s Memorial at para. 101; Letter from SGS Senior Executive Vice President to Minister of Finance dated 22 July 1999, Ex. C-34.

⁴² Claimant’s Memorial at para. 103; Letter from Ministry of Finance to SGS dated 27 August 1999, Ex. C-112.

⁴³ Claimant’s Memorial at para. 104; Letter from SGS Senior Executive Vice President to Minister of Finance dated 16 September 1999, Ex. C-35.

⁴⁴ Claimant’s Memorial at para. 106; Letter No. 351 from Administrative Director, Ministry of Finance to SGS (Geneva) dated 20 October 1999, Ex. C-37.

⁴⁵ Claimant’s Memorial at para. 107; Newspaper clipping titled “Switzerland Demands Paraguay Payment of US\$ 30 Million Debt” dated 26 November 1999, Ex. C-116

⁴⁶ Claimant’s Memorial at para. 108; Internal Letter from the Swiss Chargé d’affaires dated 17 July 2000 (emphasis in original), Ex. C-120.

In 1999, Paraguay disbursed an amount of 22,523,855,917 Guaranís . . . under the budgetary heading “Other Fees.” According to [Rubén Darío Maciel], this amount was supposedly paid to SGS’s competitor, Bureau Veritas/Bivac. The **2000 budget**, for which I was able to consult the entry “Other Fees,” does not provide for any payment to SGS or Bivac. Still according to [Rubén Darío Maciel], parliament supposedly prohibited other payments from being recorded in this category without its approval, hence the need for the treasury department to submit an ad hoc legislative bill to parliament, which has not been done.

54. A local newspaper story reported on 16 September 2000 that the Minister of Finance stated that the SGS and BIVAC contracts were “illegal.”⁴⁷ According to the report:

The head of the Treasury said that there was evidence that the accounts were unlawfully assumed during the Wasmosy administration. He recalled that on his first day in office, he was asked to sign an authorization for payment to the two companies for 28,000 million guaranis, which he refused to do. However, [the Minister] was not clear when asked whether the case would be taken to the Paraguayan courts.

55. In February 2001, the Ministry of Foreign Affairs wrote to the Ministry of Finance, asking that the Ministry “consider acknowledging the aforementioned debt obligations and also to analyze a payment plan that will allow us to negotiate with such firms.”⁴⁸ In response, the Counsel of the Treasury issued an opinion concluding that the contracts with SGS and BIVAC were valid. However, it also stated (in para. 5) that “the Comptroller General of Paraguay is verifying the services provided by the contracting companies in order to determine whether the works performed comply with the contract and the principles and rules governing this type of business transactions” and (in para. 7) that “the Paraguayan State cannot pay outstanding debts until the Comptroller General’s Special Examination is concluded.” The opinion recommended (in para. 10.2) that “[t]he Ministry of Finance shall take action to request the budget items for the payment of the debts owed to SGS and BIVAC INTERNACIONAL, in accordance with the final

⁴⁷ Claimant’s Memorial at paras. 111-112; Newspaper clipping titled “Debt Undertaken by [President] Wasmosy with SGS and BIVAC Is Illegal” dated 16 September 2000, Ex. C-121.

⁴⁸ Opinion No. 139 issued by Legal Counsel for the Counsel of the Treasury, Ministry of Finance dated 12 February 2001, Ex. C-42.

settlement to be made based on the special examination performed by the Comptroller General of Paraguay.”⁴⁹

56. On 31 July 2001, a Paraguayan newspaper reported an announcement by the Minister of Finance that “not a single guaraní [will be paid] without congressional authorization since the debts are not in the budget.”⁵⁰ According to the newspaper account, the Minister noted that the Comptroller General has raised questions “regarding the legality of the agreements signed with [SGS and BIVAC], which means that it is not appropriate to pay any debt” and that the Comptroller General’s report had been sent to Treasury’s legal office.
57. In late 2001, SGS sought confirmation from the Ministry of Finance that it should be clear of taxes, as provided in Article 4.6 of the Contract.⁵¹ On 4 January 2002, the Ministry of Finance sent SGS an opinion by an internal Ministry attorney confirming that SGS’s work was tax-free.⁵² Five days later, SGS forwarded the opinion to the Ministry’s Tax Collections Office.⁵³
58. On 18 January 2002, a criminal prosecutor requested that the Tax Collections Office confirm whether SGS was applying for a tax exemption.⁵⁴ The request was in connection with an investigation of an unnamed individual for “breach of trust.” The Ministry of Finance told the prosecutor that SGS had not submitted any tax returns.⁵⁵ In February 2002, the prosecutor determined that the tax issue did not relate to her investigation of the breach of trust case. However, she ordered that the information she had collected be sent

⁴⁹ Opinion No. 139 issued by Legal Counsel for the Counsel of the Treasury, Ministry of Finance dated 12 February 2001, Ex. C-42.

⁵⁰ Claimant’s Memorial at para. 121; Newspaper clipping titled “Debt to SGS and BIVAC Will Not Be Paid” dated 31 July 2001, Ex. C-122.

⁵¹ Article 4.6 of the Contract, entitled “Tax incidence,” states, “The fees and method of payment set forth herein have been agreed free of taxes. In the event of an amendment of the tax rules in force, the former shall be adjusted to the extent required in order to be kept at the level initially agreed upon.” Contract, Ex. C-4.

⁵² Letter from the Ministry of Finance to SGS dated 4 January 2002, Ex. C-124.

⁵³ Claimant’s Memorial at 125; Letter from SGS to the Tax Collections Office dated 9 January 2002, Ex. C-126.

⁵⁴ Claimant’s Memorial at para. 126; Letter from Prosecutor Delvalle to Under-Ministry of Taxation of the Ministry of Finance dated 18 January 2002, Ex. C-127.

⁵⁵ Letter from Ministry of Finance to Prosecutor Delvalle dated 25 January 2002, Ex. C-128.

to the Attorney General for “investigation into acts of tax evasion.”⁵⁶ According to Claimant, the inquiry was dismissed on 16 December 2002.⁵⁷

59. According to press reports, after a new government took office in 2003, the Minister of Finance stated, with reference to the debt to SGS and BIVAC, that Paraguay would “seek to honor all commitments that are proper and within the law.”⁵⁸ Nevertheless, in March 2004, the Vice-Minister of Finance issued Resolution 274, which suspended payments “until establishing whether it is true that there were possible irregularities on the part of the companies contracted in accordance with the contract”⁵⁹ Resolution 274 also established a Commission to negotiate any payment once it had “establish[ed] the final position of the Ministry of Finance concerning whether or not it is appropriate to pay the pending debt to the inspection companies.” The Commission was to report back to the Minister of Finance by 3 September 2004; however, its mandate was extended and the Commission was eventually disbanded in February 2005 without issuing a substantive report.⁶⁰ The Commission concluded that “the determination of the level of compliance with the contract by the companies BIVAC and SGS goes beyond the financial scope of this Commission and requires highly specific technical customs studies, as well as the examination of all the back-up documentation of the operations carried out.” It then recommended that Customs continue the examination.⁶¹
60. The Ministry of Finance thereafter ordered Customs to start a new inquiry. However, in May 2005, the press reported that National Director of Customs Margarita Díaz de Vivar admitted that “[p]revious customs administrations acknowledged the existence of debts to the inspection companies SGS and BIVAC . . . [but] Díaz de Vivar explained that

⁵⁶ Resolution No. 14 dated 11 February 2002, Ex. C-129.

⁵⁷ Claimant’s Memorial at paras. 127-128; Prosecution Request dated 19 November 2002, Ex. C-130; Judgment No. 1984 dated 16 December 2002, Ex. C-131.

⁵⁸ Claimant’s Memorial at para. 130; Newspaper clipping titled “Borda Believes that Certain Debts Are Litigious” dated 1 October 2003, Ex. C-132.

⁵⁹ Claimant’s Memorial at para. 133; Minister of Finance Resolution No. 274 dated 3 June 2004, Ex. C-47.

⁶⁰ Claimant’s Memorial at paras. 135-136; Minister of Finance Resolution No. 687 dated 4 November 2004, Ex. C-48; Ministry of Finance Resolution No. 43 dated 3 February 2005, Ex. C-50.

⁶¹ Ministry of Finance Resolution No. 43 dated 3 February 2005, Ex. C-50.

currently the case is no longer in the hands of Customs and that the matter must be decided by the Ministry of the Treasury.”⁶²

61. In May 2005, the Ministry of Finance launched an investigation of SGS’s and BIVAC’s performance, and, based on an exchange of letters between the parties, it appears that a special committee was continuing to investigate the matter as late as the second half of 2006.⁶³
62. In the meantime, SGS and the Ministry of Finance continued to discuss the matter, and the Paraguayan Government continued to struggle with how to proceed. In June 2005, SGS wrote to the Ministry of Finance requesting a proposed payment plan.⁶⁴ In August 2005, the Comptroller General issued a report noting that the Ministry of Finance did not include the debt to SGS in the Ministry’s balance sheet for the 2004 fiscal period.⁶⁵ In 2006-2007, SGS wrote a number of letters to the Ministry of Finance, proposing settlement terms and requesting new negotiations.⁶⁶ A letter from SGS from April 2007 recounts a meeting with the Minister of Finance on 18 December 2006 in which the Minister expressed an interest in SGS’s proposal to negotiate a monthly payment plan.⁶⁷ An SGS letter dated 24 May 2007 recounts a meeting with the Minister of Finance on 10 May 2007 in which the Minister offered to set up a meeting with the President to present the debt situation and make proposals to finalize an agreement.⁶⁸ In addition to

⁶² Newspaper clipping titled “Previous Customs Acknowledged Debts to SGS and BIVAC” dated 12 May 2005, Ex. C-136.

⁶³ Claimant’s Memorial at paras. 138, 143; Newspaper clipping titled “Ministry of Finance Announces Investigation of Debts to SGS and BIVAC” dated 7 May 2005, Ex. C-135; Letter from SGS to Ministry of Finance dated 8 November 2006, Ex. C-138.

⁶⁴ Letter from SGS Legal Counsel to Minister of Finance dated 8 June 2005, Ex. C-51.

⁶⁵ Comptroller General Internal Report dated 25 August 2005, Ex. C-54.

⁶⁶ Letter from SGS to Ministry of Finance dated 7 February 2006, Ex. C-137; Letter from SGS to Minister of Finance dated 3 April 2006, Ex. C-56; Letter from SGS to Minister of Finance dated 1 September 2006, Ex. C-57; Letter from SGS to Minister of Finance dated 8 November 2006, Ex. C-138; Letter from SGS to Minister of Finance dated 9 November 2006, Ex. C-139; Letter from SGS to Minister of Finance dated 5 December 2006, Ex. C-140; Letter from SGS to Minister of Finance dated 12 January 2007, Ex. C-60; Letter from SGS to Vice Minister of Finance dated 14 January 2007, Ex. C-61; Letter from SGS to Minister of Finance dated 17 April 2007, Ex. C-62; Letter from SGS to Minister of Finance dated 24 May 2007, Ex. C-63.

⁶⁷ Letter from SGS to Minister of Finance dated 17 April 2007, Ex. C-62.

⁶⁸ Letter from SGS to Minister of Finance dated 24 May 2007, Ex. C-63.

the referenced letters, and after the Contract's termination in June 1999, SGS sent interest invoices to the Ministry of Finance between April 2000 and March 2006.⁶⁹

63. After SGS continued to demand payment of the outstanding debt under the Contract, and after BIVAC initiated arbitration proceedings in February 2007 with respect to unpaid debts accrued under its own contract, the President of Paraguay issued Decree No. 10485 on June 22, 2007, directing the Attorney General to "determine the existence and legal enforceability of the claims" by BIVAC and SGS. Decree 10485 stated, "In order to safeguard the proprietary interests of the Government, it is first necessary to verify that the services were actually performed in order to determine the material and legal existence of the alleged credit claimed, with the pertinent clarification that the administrative measure does not signify recognition, confirmation or acceptance of the claims of the affected companies and/or cause disruptions or suspensions in statutory periods."⁷⁰
64. Claimant initiated this arbitration in October 2007.

D. Uncontested Nature of the Facts

65. The general sequence of events described above and contemporaneous written documentation are not in dispute. Respondent questions the recollection of Mr. Musalem, as his written and oral testimony was prepared several years after the events in question took place. Respondent also asserts that at no point did Paraguay make an unequivocal promise to pay and that much of the discussion between the parties is protected by settlement privilege. The Tribunal will address the relevance of these matters in due course. However, apart from these points, neither party contests the occurrence of the events as described.

III. MERITS OF CLAIMS

66. Claimant alleges that Respondent breached its obligations under Article 11 of the BIT to observe commitments it entered into with SGS. Claimant also alleges that Respondent impaired Claimant's investment by undue and discriminatory measures in violation of

⁶⁹ Lironi Statement at para. 19; Interest Invoices, Ex. C-144.

⁷⁰ Decree No. 10485 dated 22 June 2007, Ex. C-141.

Article 4(1) of the BIT and denied Claimant fair and equitable treatment in violation of Article 4(2) of the BIT.

67. For the reasons explained below, the Tribunal concludes that Respondent breached its obligations under Article 11 of the BIT. Therefore, it need not address Claimant’s claims under Article 4(1) and 4(2) of the BIT, as they arise out of identical facts and would not, even if the Tribunal were to find a violation, result in increasing the damages owed to Claimant. The Tribunal shall return to this matter after its discussion of the claims under Article 11.

A. Assessment of Claims Under Article 11 of the BIT

68. Article 11 of the BIT, the so-called “umbrella clause,” states that “[e]ither Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the other investors of the Contracting Party.”

69. Claimant makes two related but independent claims under Article 11. First, Claimant asserts that Respondent breached the Contract by failing to meet its payment obligations, and such breach in itself amounts to a breach of Article 11. Second, Claimant asserts that Respondent made – and broke – additional promises to pay SGS’s invoices through various oral and written representations during and after the term of the Contract. Claimant asserts that these additional representations are enforceable commitments under Article 11.

70. Respondent raises several objections to Claimant’s claims under Article 11, each of which will be addressed below. However, prior to doing so, and given the overlap between Respondent’s defenses on the merits and the arguments it raised during the jurisdictional stage of the proceedings, the Tribunal shall begin its examination of Claimant’s Article 11 claims with a summary of its relevant findings from the Decision on Jurisdiction. The Tribunal will then refer to these findings in its analysis of the specific arguments Claimant and Respondent presented during the merits phase.

1. Tribunal's Decision on Jurisdiction

71. In its Decision on Jurisdiction, the Tribunal made three findings with respect to Claimant's claims under Article 11: (a) the Tribunal had jurisdiction over the claims; (b) having taken jurisdiction over the claims, the Tribunal was required to decide them notwithstanding the existence of the forum selection clause in the Contract; and (c) the claims were admissible. We will not repeat the reasoning behind each of these findings, as the Decision on Jurisdiction is incorporated in full here. However, in the course of its analysis, the Tribunal reached several conclusions that are directly relevant to its assessment of the merits of the claims and that bear repeating.

72. First, the Tribunal rejected Respondent's argument that a mere breach of contract cannot rise to the level of a breach of Article 11 unless it is coupled with additional "sovereign" action. The Tribunal concluded (at para. 167) that, "even as to the Article 11 claims that are predicated directly on Paraguay's alleged breach of the Contract, we have no hesitation in treating the Contract's obligations as 'commitments' within the meaning of Article 11." The Tribunal explained as follows (at para. 168):

Given the unqualified text of Article 11 of the Treaty, and its ordinary meaning, we see no basis to import into Article 11 the non-textual limitations that Respondent proposed in its Reply. Article 11 does not exclude commercial contracts of the State from its scope. Likewise, Article 11 does not state that its constant guarantee of observance of such commitments may be breached only through actions that a commercial counterparty cannot take, through abuses of state power, or through exertions of undue government influence. . . . In effect, we see no basis on the face of the clause to believe that it should mean anything other than what it says—that the State is obliged to guarantee the observance of its commitments with respect to the investments of the other State party's investors. (Citations omitted).

73. The Tribunal also concluded that, even if it were necessary to show an abuse of sovereign authority in order to prove an Article 11 claim, a breach of contract by Paraguay could very well constitute a sovereign act. As stated in the Decision on Jurisdiction (at para. 135), "Logically, one can characterize every act by a sovereign State as a 'sovereign act'—including the State's acts to breach or terminate contracts to which the State is a party. It is thus difficult to articulate a basis on which the State's actions, solely because

they occur in the context of a contract or a commercial transaction, are somehow no longer acts of the State, for which the State may be held internationally responsible.”

74. The consequence of the Tribunal’s holding is that Claimant can prove an Article 11 claim if it can prove that Paraguay failed to observe its commitments under the Contract, regardless of whether Paraguayan officials subsequently acknowledged the debt to Claimant through additional written or verbal assurances of payment, or took some other form of “sovereign action” such as amending a law or regulation in a manner that prevented payment of SGS’s invoices.
75. Second, the Tribunal (at paras. 173-185) rejected Respondent’s argument that the forum selection clause in the Contract deprived the Tribunal of jurisdiction to hear Claimant’s Article 11 claims or rendered such claims inadmissible to the extent such claims were premised on a theory that Respondent breached the Contract. The Tribunal found that, having already decided that it had jurisdiction over the claims, it was compelled to decide them. The Tribunal concluded (at para. 172) that “a decision to decline to hear SGS’s claims under Article 11 on the grounds that they should instead be directed to the courts of Asunción would place the Tribunal at risk of failing to carry out its mandate under the Treaty and the ICSID Convention.”
76. Third, the Tribunal concluded that its finding that it had jurisdiction over claims for Paraguay’s alleged failure to observe its contractual commitments under Article 11 is consistent with the Parties’ intent when negotiating the BIT. The Tribunal stated (at para. 176), “[t]he State parties to the BIT intended, to provide this Treaty protection in addition to whatever rights the investor could negotiate for itself in a contract or could find under domestic law, and they gave the investor the option to enforce it, including through arbitrations such as this one” (citations omitted).
77. None of the above findings excluded the possibility that any additional statements or alleged promises to pay made by Paraguayan officials might in themselves constitute binding commitments under Article 11 of the BIT. Indeed, the Tribunal concluded (at para. 167) that Article 11 “creates an obligation for the State to constantly guarantee observance of its commitments entered into with respect to investments of investors of

the other Party. The obligation has no limitations on its face—it apparently applies to all such commitments, whether established by contract or by law, unilaterally or bilaterally, etc.” Oral and written representations outside the Contract could, therefore, be enforceable under Article 11 in certain circumstances. However, the Tribunal clearly found in its Decision on Jurisdiction that it was not necessary to prove the binding nature – or even the relevance – of such statements outside the Contract in order to prove a claim that a party’s failure to meet its contractual commitments itself violated Article 11.

78. With this background, the Tribunal will now turn to the parties’ arguments presented during the merits phase of the proceeding.

2. Whether Respondent Has Failed to Guarantee the Observance of Its Contractual Commitments

a. Claimant Has Met Its Initial Burden of Proof That Respondent Has Failed to Guarantee the Observance of Its Contractual Commitments

79. As stated in *Soufraki v. United Arab Emirates*, “In accordance with accepted international (and general national) practice, a party bears the burden of proof in establishing the facts that he asserts.”⁷¹ Consequently, Claimant bears the initial burden of proof in substantiating its claims, and Respondent bears the burden of proving its defenses. Claimant thus bears the burden of proving that Respondent’s failure to pay SGS’s invoices breached Respondent’s contractual commitments and, therefore, Article 11 of the BIT. Respondent bears the burden of proving its defenses by showing, for example, that Respondent’s failure to pay the invoices is justified by Claimant’s own breaches of its contractual obligations or is otherwise excused.

80. On the facts before us, it is clear that Claimant has met its initial burden of proof. It is not disputed that Paraguay has failed to pay 25 invoices to SGS, totaling in principal US\$ 39,025,950.86. It is also undisputed that such invoices were issued pursuant to the

⁷¹ *Hussein Nuaman Soufraki v. United Arab Emirates*, ICSID Case No. ARB/02/7, Award, 7 July 2004, para. 58. See also *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*, ICSID Case No. ARB/99/6, Award, 12 April 2002, para. 90; *Alpha Projektholding GMBH v. Ukraine*, ICSID Case No. ARB/07/16, Award, 8 November 2010, para. 236; *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka*, ICSID Case No. ARB/87/3, Final Award, 27 June 1990, para 56.

Contract, and failure to pay properly issued invoices constitutes a breach of Paraguay's contractual commitments. Furthermore, as the Tribunal has already found, a Party's failure to observe its contractual commitments may in itself constitute a breach of Article 11 of the BIT. Therefore, Claimant has met its initial burden of proof that Paraguay has failed to observe its contractual commitments and has shifted the burden onto Respondent to prove its defenses that the non-payment was justifiable.

b. Respondent's Defenses

81. Respondent makes three principal arguments in its defense: (i) the alleged breach of its contractual commitments was "committed by Paraguay (if at all) as a normal market player and did not involve abuse of its sovereign powers"; (ii) in any event, the forum selection clause in the Contract precludes a finding of liability; and (iii) Claimant itself breached the Contract, and such breach relieves Respondent of its contractual obligations. The Tribunal shall examine each of these defenses in turn.

(i) Respondent's Argument That Paraguay Did Not Abuse Its Sovereign Powers

(a) Respondent's Position

82. Respondent asserts that a breach of contract by a State may only violate an umbrella clause in a BIT if the government action in question constituted an abuse of sovereign authority. According to Respondent, "SGS must establish that Paraguay abused its government power," and mere non-payment of invoices is not sufficient to establish a breach of Article 11.⁷² Even assuming Respondent breached its contractual commitments, Respondent argues, Paraguay's actions "are of the kind that can and often do occur in private commercial transactions, and without more, they cannot be characterized as instances of 'abuse of government power.'" "After all," Respondent argues, "mere non-payment of sums allegedly due under a contract is an act that any private party could engage in."⁷³

⁷² Respondent's Counter-Memorial at para. 78.

⁷³ Respondent's Counter-Memorial at para. 87.

83. Respondent recognizes that the Tribunal has already concluded in its Decision on Jurisdiction that a mere breach of contract could in itself violate Article 11 without being coupled with an abuse of sovereign authority. However, Respondent argues that the Tribunal mischaracterized its argument in the Decision on Jurisdiction. To ensure that there is no confusion on the matter, the Tribunal shall quote Respondent's clarification of its position:⁷⁴

Paraguay does not sustain that every breach of contract by the State will automatically be insulated from international liability. Some contractual breaches may in certain circumstances not present here may [*sic*] derive from an abuse of government power, and as a result may be actionable under a fair and equitable treatment standard or even an umbrella clause. However, other contractual breaches, such as simple breaches of payment obligations do not entail abuse of government power, and as a result are not protected by the umbrella clause.

84. In support of its position, Respondent cites a string of cases including *Siemens v. Argentina*, *Bayindir v. Pakistan*, *RFCC v. Morocco*, *Waste Management v. Mexico*, *Impregilo v. Pakistan* and *Duke v. Ecuador*⁷⁵ for the proposition that a government's breach of contract can only rise to the level of a breach of the BIT if it involved an abuse of sovereign authority.

85. Respondent also urges the Tribunal not to construe Article 11 in broader terms than the Swiss Government has construed a similar provision in the Swiss-Pakistan BIT.⁷⁶ In addition, Respondent argues that the Tribunal should conclude, like the *SGS v. Pakistan* tribunal, that the umbrella clause does not extend to breach of contract claims.⁷⁷

86. Respondent argues that Claimant has not proven that Paraguay abused its sovereign authority, and, therefore, has not proven that Respondent breached Article 11 of the BIT.

⁷⁴ Respondent's Counter-Memorial at para. 79.

⁷⁵ *Siemens A.G. v. Argentine Republic*, ICSID Case No. ARB/02/8, Award, 6 February 2007, para. 253; *Bayindir Insaat Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Award, 27 August 2009, para. 179; *Consortium R.F.C.C. v. Kingdom of Morocco*, ICSID Case No. ARB/00/6, Award, 22 December 2003, paras. 51, 100; *Waste Management Inc. v. United Mexican States*, ICSID Case No. ARB(AF)/00/3, Award, 30 April 2004, para. 115; *Impregilo S.p.A. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/3, Decision on Jurisdiction, 22 April 2005, paras. 259-62; *Duke Energy Electroquil Partners v. Republic of Ecuador*, ICSID Case No. ARB/04/19, Award, 18 August 2008, para. 340.

⁷⁶ Respondent's Counter-Memorial at para. 92.

⁷⁷ Respondent's Counter-Memorial at para. 93 and n. 94.

While Claimant pointed to several acts and statements by Paraguayan government authorities as “sovereign” acts that blocked payment to SGS, Respondent argues that such acts were not sufficient to prove Claimant’s claim. According to Respondent:⁷⁸

Paraguay’s supposedly obstreperous post-breach conduct makes it no different Like Paraguay here, any commercial party could have multiple changes in leadership in a short period of time, conduct more than one internal inquiry into its rights and obligations under a contract and object at various times and in different ways to aspects of the counterparty’s performance. And, like a private commercial party would do, the government of Paraguay made itself subject to the jurisdiction of its judicial system for the resolution of disputes over its conduct.

(b) Claimant’s Position

87. Claimant notes that the Tribunal has already decided in the Decision on Jurisdiction that a breach of contract could violate Article 11 even if there was no abuse of sovereign authority. Claimant argues that the decisions that Respondent cites in favor of its position either did not require the exercise of sovereign power in order to establish a breach of an international obligation or, with respect to the sections of the awards upon which Respondent relies, did not deal with a claim under an umbrella clause. In fact, Claimant contends, the *Siemens* tribunal actually adopted an approach similar to that taken in the Decision on Jurisdiction.⁷⁹
88. Claimant furthermore argues that, even if it must prove an abuse of sovereign authority in order to prove an Article 11 claim, “in the years that followed the termination of the Contract, Paraguay commissioned investigations and inquiries into the Contract and the debt to SGS, with the effect of stalling payment.”⁸⁰ In Claimant’s view, these acts constitute the type of sovereign acts that Respondent claims are necessary prerequisites to an Article 11 claim. According to Claimant, these are not the acts of a private party. In Claimant’s view, “A private corporation cannot cloak its acts with the mantle of governmental authority. Nor can a private corporation invoke at will the machinery of the criminal justice system. Nor would SGS have seen parties distinct from its

⁷⁸ Respondent’s Counter-Memorial at para. 87.

⁷⁹ Claimant’s Reply at para. 80.

⁸⁰ Claimant’s Reply at para. 66.

contractual counter-party, such as the Prosecutor General and the Comptroller General, inject themselves into the performance of the Contract, had it been dealing with a private corporation.”⁸¹

(c) Tribunal’s Analysis

89. The Tribunal does not accept Respondent’s argument that an abuse of sovereign authority is necessary to prove a violation of Article 11. Indeed, despite Respondent’s protestations to the contrary, there is no meaningful distinction between the argument Respondent has raised in the merits phase and the argument that Respondent raised – and the Tribunal rejected – during the jurisdictional phase of the proceeding.
90. Article 11 of the BIT states, “Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the investors of the other Contracting Party.” As a matter of the ordinary meaning of the term, a contractual obligation is the prototypical legally binding “commitment.” Hence, applying standard principles of treaty interpretation,⁸² a contractual obligation is a “commitment” within the meaning of Article 11.
91. Article 11 requires the “observance” of commitments. Also as a matter of the ordinary meaning of the term, a failure to meet one’s obligations under a contract is clearly a failure to “observe” one’s commitments. There is nothing in Article 11 that states or implies that a government will only fail to observe its commitments if it abuses its sovereign authority. Hence, again applying standard principles of treaty interpretation, a breach of contract by Paraguay with respect to an investment of a Swiss investor is a breach of Article 11.
92. Most of the decisions that Respondent cites in support of its position are inapposite, in that they do not stand for the proposition that an abuse of sovereign authority is necessary in order to establish a breach of an umbrella clause. The section of *Bayindir* (at para. 180) upon which Respondent relies dealt with a fair and equitable treatment claim. The

⁸¹ Claimant’s Reply at para. 69.

⁸² Article 31(1) of the Vienna Convention on the Law of Treaties states that, “[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.”

same is true with respect to Respondent's citation to the *RFCC* (at paras. 51, 100), *Waste Management* (at para. 115), and *Duke* (at paras. 332-345) awards. *Impregilo* (at paras. 259-285) dealt with claims for breach of the fair and equitable treatment standard, imposition of unfair and discriminatory measures, and expropriation without compensation.

93. Respondent cites *SGS v. Pakistan* for the proposition that the “commitment” protected by an umbrella clause does not include mere contracts.⁸³ However, as the Tribunal already decided in the Decision on Jurisdiction, Article 11 of the BIT provides no basis for excluding contracts from the scope of “commitments” covered in the article. As stated in the Decision on Jurisdiction (at para. 169), on this point it is “parting ways with the decision in *SGS v. Pakistan*” Similarly, the Tribunal disagrees with the *Siemens* award to the extent that it concluded that an abuse of sovereign power was necessary to establish a breach of an umbrella clause. In so doing, the Tribunal follows the reasoning of other ICSID tribunals that have concluded that the umbrella clause may apply whether or not the exercise of sovereign power is involved.⁸⁴
94. With respect to Respondent's concern that the Tribunal is construing the umbrella clause more broadly than the Swiss Government,⁸⁵ the Tribunal need only note that both it and the Swiss Government are in accord that Article 11 extends to contractual commitments. Again, the Tribunal already addressed this matter in the Decision on Jurisdiction (at para. 169).
95. In light of these conclusions, the parties' discussion of whether Paraguay took actions of a sovereign nature, and, if so, whether such actions were an abuse of government authority, is irrelevant. In short, if Paraguay failed to observe its contractual commitments, then it breached Article 11. No further examination of whether Paraguay's actions are properly characterized as “sovereign” or “commercial” in nature is necessary.

⁸³ Respondent's Counter-Memorial at para. 93.

⁸⁴ See, e.g., *Burlington Resources Inc. and others v. Republic of Ecuador and Empresa Estatal Petróleos del Ecuador (PetroEcuador)*, ICSID Case No. ARB/08/5, Decision on Jurisdiction, 2 June 2010, para. 190; *Duke Energy Electroquil Partners & Electroquil S.A. v. Republic of Ecuador*, ICSID Case No. ARB/04/19, Award, 18 August 2008, para. 320 (recognizing that the majority of decisions that have addressed the issue have not found that “sovereign interference” is necessary to establish a breach of an umbrella clause).

⁸⁵ Respondent's Counter-Memorial at paras. 92-93.

(ii) Respondent’s Argument That the Forum Selection Clause Precludes a Finding of Liability

(a) Respondent’s Position

96. Respondent argues that, under Paraguayan law and the terms of the Contract, the forum selection clause in Article 9 of the Contract precludes a finding of liability by the Tribunal. As explained above, Article 9 of the Contract states that “[a]ny conflict, controversy or claim deriving from or arising in connection with this Agreement, breach, termination or invalidity, shall be submitted to the Courts of the City of Asunción under the Law of Paraguay.” Respondent argues that the forum selection clause precludes the Tribunal from finding Respondent liable for its failure to observe its contractual commitments because any determination of whether Respondent breached the Contract must be submitted to local courts.
97. Respondent asserts that this argument pertains to the merits of the dispute. According to Respondent, the forum selection clause in Article 9 of the Contract and the payment obligations set forth in Article 4 of the Contract comprise a single, unified obligation. According to Respondent, “the ‘commitment’ that Paraguay made was to pay SGS or to resolve disputes about payment in the local courts. It has not breached that commitment; the Paraguayan courts have been available throughout the parties’ dispute to resolve SGS’s claims to payment.”⁸⁶
98. Respondent recognizes that the Tribunal has already concluded in the Decision on Jurisdiction that the forum selection clause does not deprive the Tribunal of jurisdiction or render Claimant’s claims inadmissible. Respondent argues that the position it has articulated at the merits stage is not incompatible with the Tribunal’s previous decision. Respondent argues that “the issue for the merits is not whether the Tribunal should decline to hear the claim based on the forum-selection clause (*i.e.*, in favor of an alternative local forum), but whether SGS has failed to prove its claim because Paraguay

⁸⁶ Respondent’s Rejoinder at para. 45.

has never repudiated its commitment of a local forum to resolve disputes regarding payment. That merits issue has not been decided.”⁸⁷

99. Respondent further recognizes that the Swiss Government, one of the Parties to the BIT, has taken the position that an umbrella clause covers claims for mere breaches of contract but argues that “[t]he Swiss government did not address whether a contract as a whole makes up the relevant contractual commitment (as Paraguay maintains), or whether each contractual clause can be divided into a separate commitment (as SGS argues).”⁸⁸ In other words, Respondent argues that the Swiss Government’s position on the scope of an umbrella clause did not preclude the possibility that a forum selection clause in a contract could prevent a finding of liability under the BIT, at least as long as the Respondent remains willing to submit the contractual dispute for resolution in accordance with such clause.

(b) Claimant’s Position

100. Claimant argues that the Tribunal’s Decision on Jurisdiction already rejected Respondent’s argument that the forum selection clause in the Contract prevented the Tribunal from finding Respondent liable under Article 11.⁸⁹ According to Claimant, “What Paraguay seems to suggest is that this Tribunal is not the permissible forum to make such a finding of breach. This conclusion, of course, flies in the face of the Tribunal’s earlier findings in its Decision on Jurisdiction that the Tribunal has jurisdiction over SGS’s Article 11 claim and that such claim is immediately admissible despite the forum selection clause.”⁹⁰

(c) Tribunal’s Analysis

101. The Tribunal does not accept Respondent’s argument. The law applicable to Claimant’s claim is the BIT, including Article 11 of the BIT and the investor-state dispute settlement provisions in Article 9 of the BIT. Article 11 requires Respondent to observe its commitments with respect to Swiss investors. The “commitment” at issue in this dispute

⁸⁷ Respondent’s Rejoinder at para. 46.

⁸⁸ Respondent’s Rejoinder at para. 48.

⁸⁹ Claimant’s Reply at paras. 86-89.

⁹⁰ Claimant’s Reply at para. 88.

is the Contract. There is no dispute that the Contract requires payment in accordance with the invoicing procedures set forth therein and that Respondent has not paid the vast majority of the invoices SGS issued. In these circumstances, the Tribunal has no difficulty concluding that Respondent did not fulfill its contractual commitments.

102. Respondent goes to great pains to argue that it is not rearguing the Tribunal's jurisdictional finding but is making a defense on the merits. Respondent argues that it cannot be found to have failed to observe its contractual commitments unless Claimant proves that Respondent has failed to meet its payment obligations under the Contract *and* frustrated the operation of the forum selection clause. These two elements are, in Respondent's view, part and parcel of a single contractual commitment. Therefore, Respondent argues, a mere failure to meet its payment obligations does not in itself breach the Contract, much less the BIT.
103. Respondent's argument can be summarized as follows: (1) Article 11 of the BIT requires compliance with the Contract; (2) the Contract requires that Respondent pay SGS; (3) while Respondent has not paid most of SGS's invoices, the Contract states that any disputes regarding payment must be submitted to local courts; and (4) until the local courts resolve the dispute, Respondent is not in breach of its contractual obligations.
104. There are several problems with Respondent's defense. First, Respondent has not cited any legal authority, including under Paraguayan law, in support of its position. Certainly, there is nothing explicit in the Contract on that point. In fact, Article 7.1 of the Contract, which allows one party to terminate the Contract for the other party's breach of contract, implies the opposite, *i.e.*, that no court determination or frustration of the forum selection clause is necessary for a breach to have occurred.⁹¹

⁹¹ Article 7.1 of the Contract states as follows:

The parties may terminate this Agreement by reason of non-compliance with the provisions set forth herein and with the applicable legal provisions.

If non-compliance is attributable to THE MINISTRY, SGS shall notify the grounds invoked which, if not remedied in a reasonable period of time, shall authorize the termination of the agreement.

If the non-compliance is attributable to SGS, THE MINISTRY shall notify the grounds invoked, setting forth a term within which contractual and legal provisions shall be fulfilled, as required by the public interest, and which, if not met duly and timely, shall produce the agreement termination effect by law.

105. Second, in the absence of any legal authority to the contrary, in the Tribunal's view, it is clear that the payment and dispute resolution provisions in the Contract are not alternative options but two discrete obligations. If Respondent failed to comply with its payment obligations and if it frustrated Claimant's attempt to submit disputes to local courts in accordance with the forum selection clause, then, in the Tribunal's view, Respondent would have failed to comply with two commitments under the Contract, not one. The two obligations are discrete, separate commitments as between the parties. Assuming the contrary would, in effect, imply that one can only breach a contract when it breaches, not one, but more than one of its clauses.
106. Stated differently, Respondent's argument, taken on its face, lacks logical coherence. Paraguay argues that "the 'commitment' that Paraguay made was to pay SGS or to resolve disputes about payment in the local courts."⁹² This cannot be correct. It cannot be that Paraguay had the option of *either* paying its invoices *or* submitting the dispute to local courts.
107. Third, if Respondent negotiated the Contract in the expectation that the forum selection clause in the Contract would negate its responsibility under the BIT, then Respondent's assumptions were misplaced. Respondent argues that the forum selection clause was part of the bargain the parties struck when negotiating the Contract, and that a finding of liability by the Tribunal would undermine that bargain because all of the substantive requirements of the Contract were negotiated under the expectation that any disputes would be submitted to local courts. However, Respondent ignores the fact that, in addition to agreeing to the forum selection clause in the Contract, it separately agreed to arbitration in accordance with the BIT. By doing so, Respondent offered to Swiss investors an alternative forum for dispute settlement. The BIT arbitration mechanism formed part of the applicable legal framework and became, in effect, an irrevocable part of the bargain.
108. The flaw in Respondent's position is well illustrated by the position it has taken in this arbitration as to its own allegations of breach. As discussed in further detail below,

⁹² Respondent's Rejoinder at para. 45.

Respondent argues at length that it was justified in withholding payment because Claimant breached its obligations under the Contract. For example, in Respondent's Rejoinder (at para. 49), Respondent argues, "Because the Contract requires SGS to comply strictly with the terms of the Contract, any of these three grounds [related to SGS's alleged failure to meet its obligations] rendered SGS in breach of the Contract. Under Paraguayan law, therefore, Paraguay was entitled to withhold payments and did not breach its contractual 'commitments.'" Yet, if Respondent is correct that its payment obligations are part of a unified obligation with the forum selection clause, then so too are Claimant's performance commitments. There was certainly no disclaimer in Respondent's discussion of Claimant's alleged breaches – or in any contemporaneous documentation that Respondent has produced regarding Claimant's performance – that would indicate that Claimant cannot breach its contractual obligations until such time as it may refuse to submit disputes for resolution in local courts.

109. Respondent's argument is, in effect, simply an attempt to relitigate the arguments it raised in the jurisdictional stage, and which the Tribunal rejected. In the Decision on Jurisdiction, the Tribunal found that the forum selection clause did not deprive the Tribunal of jurisdiction over the dispute nor did it render Claimant's claims inadmissible. Furthermore, the Tribunal found that, once having taken jurisdiction over the claims, it was compelled to decide them. The Tribunal would not be deciding the claims if it now concludes that the claims must be resolved by local courts. Respondent's attempt now to repackage its argument as a defense on the merits does not change that conclusion.

(iii) Respondent's Argument That Claimant Breached the Contract

110. Respondent argues that its failure to pay SGS's invoices is excused by the fact that Claimant breached its own obligations under the Contract. According to Respondent, "Even a small deviation from the Programme's requirements—and SGS's deviation was anything but small—excused Paraguay's performance."⁹³ Respondent claims that,

⁹³ Respondent's Counter-Memorial at para. 114.

“[u]nder Paraguayan law, therefore, Paraguay was entitled to withhold payments and did not breach its contractual ‘commitments.’”⁹⁴

111. Respondent argues that Claimant breached its obligations by: (a) failing to train Customs officials and establish a usable database; (b) issuing multiple invoices for certain Certificates of Inspection; (c) improperly conducting inspections and issuing invoices for imports from the Mercosur region; and (d) improperly conducting inspections and issuing invoices for imports of petroleum products. The Tribunal shall examine each of these allegations below.

(a) Whether Claimant Breached Its Contractual Obligations with Respect to Training Customs Officials and the Establishment of a Database

(1) Respondent’s Position

112. Respondent alleges that Claimant breached its obligations under Articles 2.9 and 2.10 of the Contract. Under Article 2.9 of the Contract (“Technical Cooperation”), SGS was required to provide training twice a year for up to six Customs officials. The training program was to “include, but not [be] limited to, the techniques used by SGS personnel, the technical, administrative and organizational procedures, with the purpose of reaching an efficient and effective execution and protection of tax revenues and to make up a body of officials specialized in customs valuation.”

113. Under Article 2.10 of the Contract, SGS was to help create a database for Customs “based upon the information contained in the Inspection Certificates issued by it.” SGS was also to “provide Customs with technical assistance and advice for the creation of programs and procedures that may enable the monitoring of the database”

114. According to Respondent, the training and database were intended not simply to enhance revenue collection but to enable local customs authorities to operate a customs system independently, with the longer term objective of creating an efficient and modern customs system to strengthen the local economy. Respondent argues that SGS merely held a few small training sessions in Paraguay and simply turned over the raw data in the

⁹⁴ Respondent’s Rejoinder at para. 49.

Inspection Certificates in digital form. According to Respondent, “These actions, although important, are insufficient to demonstrate that SGS discharged its technical assistance obligations so as to permit Customs to perform price comparisons using a database developed by SGS and BIVAC. No database or usable data was ever given to Paraguay.”⁹⁵

115. In support of its position, Respondent refers to a 30 March 1999 report by the Comptroller General of Customs,⁹⁶ a 22 June 1999 report to the Minister of Finance,⁹⁷ and a 28 January 2003 report of the Ministry of Finance’s internal auditor,⁹⁸ which, Respondent claims, found that SGS had not met its obligations under the Contract.

(2) Claimant’s Position

116. Claimant argues that it met its obligation to provide training under Article 2.9 of the Contract by providing equipment to Customs and training officials on the methodologies and procedures of tariff classification and valuation.⁹⁹ SGS claims that it met its obligations under Article 2.10 of the Contract by providing Customs with software, computers, and modem connections, and providing Customs with data from the Inspection Certificates in electronic form. Furthermore, Mr. Musalem testified that SGS conducted several training seminars for Customs officials and trained Customs officials on the equipment and the database that SGS provided. According to Claimant, SGS employees traveled to Paraguay from Miami, Peru and Ecuador to provide training. SGS claims that it spent approximately US\$ 317,000 on these training programs, and Customs never complained directly to SGS about the training program.
117. Claimant questions the accuracy of the 30 March 1999 Customs report and the 28 January 2003 report of Ministry of Finance’s internal auditor. Claimant notes that neither report provided evidence for its conclusions. Claimant believes that Customs’ conclusions in the March 1999 report were due to a general lack of knowledge of the

⁹⁵ Respondent’s Counter-Memorial at para. 39.

⁹⁶ Report from Victor José Soler to Celso Guillermo Romero Rolón dated 30 March 1999, Ex. RE-2 (“Customs Report”).

⁹⁷ Report from Internal Auditors to Minister of Finance dated 22 June 1999, Ex. RE-17.

⁹⁸ Report from Internal Audit Coordinator to Minister of Finance dated 28 January 2003, Ex. RE-18.

⁹⁹ See First Musalem Statement at paras. 32-34.

services SGS was providing. For example, in response to a 30 July 1998 request by Customs, SGS provided a full report showing that “[t]he analysis, development, testing and approval of the databases for Customs have been performed and coordinated” and that the relevant customs information had been transferred and updated weekly.¹⁰⁰ According to Claimant, the fact that Customs did not already possess this information, and instead required a full reporting by SGS, indicates that Customs was not fully aware of the services that SGS had been providing. According to Claimant, “As with Customs’ unawareness in July 1998 of the technical services provided by SGS with respect to the database (clarified through SGS’s August 1998 letter), the Customs inspector’s unawareness in March 1999 of SGS’s training services can be explained only by a lack of internal coordination and thoroughness.”¹⁰¹

118. Claimant argues that both the 2003 report and the June 1999 report that Respondent cites merely refer back to the March 1999 report and, therefore, have the same deficiencies.¹⁰²

(3) Tribunal’s Analysis

119. In the Tribunal’s view, Respondent has not carried its burden of proving that Claimant failed to meet its contractual obligations under Articles 2.9 and 2.10 of the Contract. Claimant has provided contemporaneous documentation (in the form of its 1998 letter to Customs) as well as testimony from Mr. Musalem, a knowledgeable and credible witness, regarding the services that it provided.¹⁰³ Such services included training, the provision of hardware and software, and the provision of data for the database. No evidence has been provided that Respondent contested the information in SGS’s 1998 letter. The author of the first document invoked by Respondent, *i.e.*, the Customs Report dated 30 March 1999,¹⁰⁴ expressly admits that he is “totally ignorant” (“cabe manifestar el total desconocimiento”) of most of the issues referred to in the Report and in the Contract. The Report simply states that the training “has not been done” but does not provide any

¹⁰⁰ Letter from SGS to Customs dated 4 August 1998, Ex. C-90. SGS also provided an internal company e-mail dated 3 August 1998 that explains how SGS coordinated with a Customs representative to provide weekly file updates for the database. Internal e-mail dated 3 August 1998, Ex. C-89.

¹⁰¹ Claimant’s Memorial at para. 52.

¹⁰² Day 1 Tr. (Merits) at p. 44.

¹⁰³ See First Musalem Statement at paras. 32-34.

¹⁰⁴ Customs Report dated 30 March 1999, Ex. RE-2.

further justification. The other two documents that Respondent relies upon are conclusory and fail to identify deficiencies in the services SGS provided with any meaningful specificity.

120. Furthermore, as Claimant notes and Respondent does not dispute, the reports were never provided to Claimant and, therefore, any discrepancies were clearly not significant enough to be brought to Claimant's attention during the life of the Contract. In fact, there is no evidence that any problem with respect to SGS's training program was raised during any of the weekly (and sometimes more frequent) meetings between SGS and Customs.¹⁰⁵ The Tribunal finds it telling that, so far as the record reflects, Respondent made no contemporaneous complaints about SGS's compliance with its training obligations under the Contract.
121. In any case, even if SGS has breached its obligations, Respondent has provided no legal authority supporting its position that it would therefore be relieved of any obligation to make payments under the Contract even while continuing to accept SGS's inspection services. No provision in the Contract provides such authority. In fact, under Article 7.1 of the Contract, if one party believes that the other has breached its contractual obligations, the proper remedy for the aggrieved party is to terminate the Contract for non-performance and, subject to the limitation of liability in Article 5.3, seek damages for any harm suffered. But the Contract does not allow the allegedly aggrieved party to continue to demand performance while simply ceasing to meet its own contractual obligations.

¹⁰⁵ Day 1 Tr. (Merits) at pp. 166:14-22, 167:1-9. Mr. Musalem testified that "meetings were held on a weekly basis, or even twice weekly, with the government, with customs, with the director of customs, specifically who was the person who would receive our certificates and was going to use them for clearance of merchandise through customs We never, on the part of the government, nor the ministry or customs, did we hear any protests regarding any poor practice or poor implantation [*sic*] of the contract. Until the day I left Paraguay, I never received anything from the government, from any authority, from the three administrations during that period."

(b) Multiple Invoices for Certain Inspection Certificates

(1) Respondent's Position

122. According to Respondent, Articles 6 and 16 of Resolution 1171 required that SGS issue only a single Inspection Certificate for each commercial invoice associated with an imported shipment. Respondent translates Article 16 of Resolution 1171 to require the issuance of “one” Inspection Certificate.¹⁰⁶
123. Respondent argues that Claimant violated this requirement by “routinely” issuing multiple Inspection Certificates. In support of its position, Respondent points to a 22 June 1999 internal report to the Minister of Finance, which concluded as follows:¹⁰⁷

There is . . . evidence of bills of lading for amounts higher than \$21,800 that have two, three or more Certificates of Inspection, which, in many cases, do not reach individually the minimum amount. The inspection companies present their assessment as separate inspections, and in cases of convenience they charge the minimum fee, in open contradiction to what is established in Article No. 6, 4th paragraph, which requires in all cases that the inspection company treat these together, when they refer to a single operation.

(2) Claimant's Position

124. Claimant notes that SGS was never provided with the 1999 report of the Ministry of Finance to which Respondent refers, and was not otherwise put on notice of any problems with its invoicing practices during the weekly meetings with Customs. In any

¹⁰⁶ Respondent's Counter-Memorial at para. 44, n. 45. Article 16 of Resolution 1171 states, “[U]na vez recibida del exportador la factura comercial y/u otros documentos requeridos por las Empresas Verificadoras, y después de comprobar que la cantidad, precio y descripción de los bienes consignados en dicha factura correspondan a los resultados de la inspección física y comparación de precio, o cuando las anomalías observadas hayan sido corregidas, las Empresas Verificadoras emitirán un Certificado de Inspección.” Respondent translates Article 16 as follows: “[O]nce the commercial invoice or other documents requested by the Verifying Companies is received from the exporter, and after the verification that the quantity, price and description of goods consigned in said commercial invoice correspond to the results of the physical inspection and price comparison, or, in the event of any discrepancies, once these discrepancies have been resolved and corrected, the Verifying Companies shall issue one Inspection Certificate.”

¹⁰⁷ Respondent's Counter-Memorial at para. 46, n. 47.

case, according to Claimant, the report did not find that SGS engaged in wrongdoing but merely stated that it was:¹⁰⁸

necessary to improve the legal framework governing the work of the inspection companies, especially as concerns payments for services, as such framework does not today contemplate several situations that currently result in a significant loss for the State, contrary to what we consider to be the object of implementation of this program, *i.e.*, increase tax collection.

125. In other words, according to Claimant, the report was describing certain adjustments that needed to be made to the Contract but did not conclude that Claimant was breaching its existing contractual obligations.
126. Furthermore, Claimant argues, its conduct was appropriate and, in fact, necessary in order to meet its contractual commitments. Claimant describes two situations in which multiple Inspection Certificates would be necessary for a single invoice. First, large sales associated with a single invoice might be divided into a number of lower value shipments. In these situations, SGS would need to inspect each individual shipment and issue multiple Inspection Certificates, even though there would be only one commercial invoice. Claimant believes that this procedure fully conformed with Article 6, paragraph 2, of Resolution 1171, which states that “Partial shipments with values of less than THREE THOUSAND U.S. DOLLARS (US\$ 3000) FOB that are part of a request or purchase/sale order exceeding THREE THOUSAND U.S. DOLLARS (US\$ 3000) FOB shall be subject to Pre-shipment Inspection.”
127. Second, SGS would need to issue multiple Inspection Certificates when several exporters shipped goods that were combined into a single import shipment. In this situation, SGS would need to inspect the goods of each exporter separately. Claimant argues that this approach was mandated by Article 6, paragraph 4, of Resolution 1171, which states that “Merchandise shipped to the same importer or by a single shipper from several suppliers and consolidated in a single bill of lading shall be subject to the Pre-shipment Inspection

¹⁰⁸ Claimant’s Reply at para. 36, *citing* Report from Internal Auditors to Minister of Finance dated 22 June 1999, Ex. RE-17.

Program if the total amount thereof equals or exceeds THREE THOUSAND U.S. DOLLARS (US\$ 3000) FOB.”

128. Claimant argues that, properly translated, Article 6 of Resolution 1171 does not limit the number of Inspection Certificates to one per invoice.¹⁰⁹ It also argues that, pursuant to Article 4.1.1 of the Contract, it was entitled to submit an invoice for each inspection.¹¹⁰

(3) Tribunal’s Analysis

129. The Tribunal finds that Respondent has not carried its burden of proof that Claimant’s invoicing practices were impermissible.
130. Resolution 1171 states that, in the two circumstances described by Claimant, SGS was required to conduct a pre-shipment inspection. The only apparent way SGS could do so was for SGS to inspect the small shipments associated with the larger invoice.
131. Resolution 1171 is not clear how such inspections should be charged, and neither party has provided legal authority to assist the Tribunal in understanding how Resolution 1171 should be interpreted. In the Tribunal’s view, it would not be reasonable to conclude that the parties intended that SGS charge nothing for the inspections. We are left, then, with deciding whether SGS should have charged the minimum fee for each inspection, or whether it should have charged Respondent based on a percentage of the shipment as a whole.
132. SGS charged the minimum amount. In the Tribunal’s view, this was a reasonable approach, as there is no evidence to show that the cost of any individual inspection would be lower if the component shipments were of lower value. Furthermore, there is no dispute that SGS’s uniform practice throughout the performance of the Contract was to charge the minimum fee in these circumstances, yet Respondent has provided no evidence that it told SGS that it objected to this approach. As noted above, Claimant’s witness, Mr. Musalem, testified that SGS and Customs met on a weekly basis, and

¹⁰⁹ Claimant’s Reply at para 33, n. 35.

¹¹⁰ Day 1 Tr. (Merits) at p. 35. Article 4.1.1 of the Contract states, “The fees for the Technical Services shall be calculated upon 1.3 % (one point three percent) on the FOB value of the goods shown in the Inspection Certificate or in the Discrepancy Report and expressed in United States dollars.”

sometimes twice weekly, and Customs never raised concerns.¹¹¹ Even if the March 1999 report concluded that Claimant’s methodology was inappropriate, Claimant notes – and Respondent does not dispute – that the report was not communicated to Claimant at the time.¹¹² In the circumstances here, we find persuasive in interpreting the Contract the parties’ uncontentious conduct in performing it. The Tribunal therefore concludes that Claimant’s invoicing methodology did not violate its contractual obligations.

(c) Mercosur Program

(1) Respondent’s Position

133. Respondent argues that SGS improperly inspected goods originating from the Mercosur region. Resolution 1579 exempted from inspection “[a]quellas importaciones liberadas y las exoneradas de los tributos aduaneros e internos, contenidas en las disposiciones de caracter general o en Leyes Especiales,” which Respondent translates as “any and all tax free imports free and clear of those duties or internal taxes, as described in general or special laws.”¹¹³ Respondent argues that duty-free goods coming from free trade areas (such as Mercosur) were thereby exempt from pre-shipment inspection.
134. Respondent argues that inspections of imports from the Mercosur region likely accounted for a very significant portion of SGS’s total inspections. According to Respondent, imports from Mercosur countries represented over 50% of all imports into Paraguay during the life of the Contract.¹¹⁴ (Respondent later estimated that imports from the Mercosur region accounted for closer to 70% of the goods SGS inspected).¹¹⁵ Extrapolating from the import data, Respondent argues that at least 50% of all of SGS’s Inspection Certificates were associated with Mercosur imports and, therefore, improper. Citing a 28 January 2003 internal report of the Ministry of Finance, Respondent argues that “[t]he indiscriminate inspection of goods without regard to the Programme’s

¹¹¹ Day 1 Tr. (Merits) at p. 166:14-167:9.

¹¹² Claimant’s Reply at para. 32.

¹¹³ Respondent’s Counter-Memorial at para. 24.

¹¹⁴ Respondent’s Counter-Memorial at para. 25.

¹¹⁵ Day 1 Tr. (Merits) at p. 75:1-11.

regulations was duly noted by the Paraguayan authorities during SGS's performance and afterward."¹¹⁶

135. Respondent also argues that inspections were not necessary to confirm the origin of Mercosur goods as the Treaty of Asunción requires Paraguay to accept at face value the import declaration that goods originate in a Mercosur country. Respondent notes that Mercosur goods could only be imported with a declaration certifying that the goods came from a Mercosur country and that, under the terms of the Treaty of Asunción, "[i]n no case may the importing country hold up import procedures for products covered by the certificates [of origin]."¹¹⁷
136. Respondent argues that an internal report to the Minister of Finance, dated 22 June 1999, concluded that, for imports from Mercosur countries, Paraguay receives no customs duties and can receive as little as 1.5% in VAT. Therefore, Respondent argues, if Paraguay has to pay SGS fees of 1.3%, it only retains 0.2% in revenue. The report therefore concludes that the legal framework should be improved.¹¹⁸
137. Respondent notes Claimant's argument (discussed in further detail below) that the exemption in Resolution 1579 applied only to imports that were exempt from both duties *and* taxes. However, Respondent argues that the exemption should be interpreted to apply to goods that were exempt from *either* duties *or* taxes.¹¹⁹
138. Respondent also notes Claimant's argument that inspections were necessary because VAT and other taxes were assessed based on import value, and most Mercosur imports were subject to taxes. However, Respondent argues that even if goods imported from Mercosur countries were subject to VAT and other taxes assessed on the basis of import value, Paraguay was obligated to accept the importer declarations at face value, and so no inspection was needed.¹²⁰ Respondent also argues that Claimant admits that not all imports from the Mercosur region were subject to VAT or other taxes, Claimant has not

¹¹⁶ Respondent's Counter-Memorial at para. 51, *citing* Report from Internal Audit Coordinator to Minister of Finance dated 28 January 2003, Ex. RE-18.

¹¹⁷ *See* Annex II, Chapter II, Articles 11 and 16 of the Treaty of Asunción, Ex. RE-26.

¹¹⁸ *See* Report from Internal Auditors to Minister of Finance dated 22 June 1999, Ex. RE-17.

¹¹⁹ Respondent's Rejoinder at paras. 15-18.

¹²⁰ Respondent's Rejoinder at para. 19.

adequately proven the percentage of such imports that were subject to taxes, and Claimant has not shown that it did not inspect the portion of Mercosur imports that were exempt from taxes.¹²¹

(2) Claimant's Position

139. Claimant does not deny that it inspected imports from the Mercosur region but argues that it was required to do so. Claimant argues that it would be “inconceivable” that Customs and the Ministry of Finance had not caught the error if SGS was, in fact, improperly inspecting more than 50% of the imports into Paraguay or that Customs would not have brought it to Claimant’s attention.¹²²
140. Claimant raises several arguments in support of its position. First, according to Claimant, SGS was required to confirm that the origin of the goods was properly designated. Claimant refers specifically to Article 2(6) of the Contract, which stated that “SGS shall prove the country of origin of goods based upon the documents issued by official entities or authorized agencies, submitted by the supplier upon the importer’s request, for the consideration thereof in the cases of tariff treatments and special regimes.” In Claimant’s view, imports from the Mercosur region are subject to a “special regime.”¹²³
141. Second, according to Claimant, Resolution 1579 did not exempt imports from the Mercosur region from inspection. Claimant translates Resolution 1579 as exempting “[t]hose imports released and those exempted from customs duties and internal taxes contained in the general provisions or Special Laws.”¹²⁴ In Claimant’s view, Resolution 1579 exempted from inspection only those goods that were exempted from *both* customs duties *and* internal taxes, such as VAT and sales tax.¹²⁵ While goods originating from the Mercosur region were usually exempt from customs duties, they were not usually exempt from VAT. Claimant notes that more than 90% of goods from Mercosur were subject to VAT and taxed, and VAT and sales tax were paid based on the price referenced in the Inspection Certificate provided by the inspection company, either SGS or BIVAC.

¹²¹ Respondent’s Rejoinder at para. 20.

¹²² Claimant’s Reply at para. 43.

¹²³ Day 1 Tr. (Merits) at p. 29:1-5.

¹²⁴ Claimant’s Reply at para. 40.

¹²⁵ Claimant’s Reply at para. 41.

142. Third, with respect to the 2003 internal Ministry of Finance report to which Respondent refers, Claimant notes that the document was produced four years after the fact, and, therefore, questions its accuracy.¹²⁶
143. Fourth, with respect to the 1999 internal report of the Ministry of Finance, Claimant argues that this document did not, in fact, conclude that SGS was improperly inspecting Mercosur imports. Instead, in Claimant's view, it was arguing only for a change of the existing legal framework in light of the fact that Respondent retained very little revenue after SGS's fees were paid.
144. Fifth, Claimant emphasizes that SGS conducted inspections at the request of importers. Claimant argues that an importer would not request an inspection of a shipment from the Mercosur region if it did not need one.¹²⁷ Claimant also notes that, if an inspection were not necessary, then SGS would decline to carry it out. If the importer nevertheless wanted to have its shipment inspected, it would be charged directly for the service.¹²⁸
145. Finally, Claimant notes that Customs never raised concerns about its inspection and invoicing practices despite the fact that SGS and Customs met weekly (and sometimes twice weekly) to discuss SGS's invoices.¹²⁹

(3) Tribunal's Analysis

146. The Tribunal finds that Respondent has not carried its burden of proof in establishing that Claimant improperly inspected shipments from the Mercosur region. Respondent has provided no legal authority for its position apart from the language of Resolution 1579. In the Tribunal's view, however, the language of Resolution 1579 supports Claimant's position.
147. Resolution 1579 exempts from inspection those goods that are exempted from customs duties and internal taxes. The Tribunal interprets the relevant provision, as written and in

¹²⁶ Claimant's Reply at para. 45.

¹²⁷ Day 1 Tr. (Merits) at p. 142:5-15.

¹²⁸ Day 1 Tr. (Merits) at pp. 160, 163-164:2. Claimant also argues that SGS could not charge the importer for an inspection of a shipment from the Mercosur region because that would constitute an impermissible restraint on trade. Day 1 Tr. (Merits) at p. 199:8-14.

¹²⁹ Day 1 Tr. (Merits) at pp. 166-167.

context, as exempting a single class of goods, *i.e.*, those that are exempt from both customs duties and internal taxes. In fact, the preamble to Resolution 1579 states in its second paragraph that the purpose of the Resolution is to ensure that merchandise is not subject to pre-shipment inspection if the merchandise is exempt from “*all* customs duties and non-customs taxes” (“*todo* tributo, aduanero y no aduanero”) (emphasis added). Moreover, Respondent’s reading would lead to a perverse result. Respondent argues that the phrase should be interpreted to exempt goods from inspection if they were exempt from *either* customs duties *or* internal taxes. However, under this interpretation, goods that were exempt from internal taxes but *assessed customs duties* would also be exempt from inspection.¹³⁰ The Tribunal finds it difficult to believe that the parties intended such a result given that the primary purpose of the pre-shipment inspection process was to ensure the proper collection of customs duties.

148. Furthermore, as Claimant argues and Respondent does not dispute, imports from the Mercosur region were subject to VAT and sales tax, and such taxes were assessed based on the price referenced in the Inspection Certificate. While Respondent argues that the Treaty of Asunción requires Paraguay to accept, for duty assessment purposes, the declared customs value without the need for an inspection, the portions of the Treaty of Asunción on which Respondent relies do not require Paraguay to accept the declared value for purposes of assessing internal taxes. Therefore, it does, in fact, appear to the Tribunal that it was necessary for SGS to conduct the inspections for tax assessment purposes, and it would be remarkable if SGS were prohibited from invoicing for them, particularly if, as Respondent argues, such imports accounted for 50-70% of the total imports into Paraguay. The Tribunal is also persuaded that it would be unlikely for an importer to request an inspection for an import from the Mercosur region that was exempt from both customs duties and internal taxes. For these reasons, the Tribunal concludes that Respondent has not carried its burden in proving that Claimant breached its contractual commitments.

¹³⁰ It is not clear whether there is a class of goods that is subject to internal taxes but not tariffs. However, if there is no such class of goods, then it would make little sense to exempt that non-existent class from inspection.

149. The Tribunal again notes that Claimant's witness, Mr. Musalem, testified that SGS and Customs met weekly, and sometimes twice a week, to discuss the Inspection Certificates, and yet, according to Mr. Musalem, Customs never raised any objections to the invoices associated with Mercosur imports.¹³¹ Respondent has not presented evidence contradicting Mr. Musalem's testimony. Again, we find persuasive the common understanding of the Contract reflected in the parties' contemporaneous performance.

(d) Petroleum-Related Invoices

(1) Respondent's Position

150. Respondent argues that SGS improperly inspected imports of certain petroleum products even though SGS agreed to cease inspecting petroleum shipments as of 1 September 1997. According to Respondent, SGS charged Paraguay approximately US\$ 65,800.00 for inspections on and after that date for imports by Petropar, Paraguay's state oil company.¹³² According to Respondent, SGS is not entitled to damages for unpaid invoices associated with those inspections.

(2) Claimant's Position

151. Claimant notes that this issue was not raised until Respondent's Rejoinder. In any case, Claimant argues that such imports were not of petroleum products but of equipment. It further argues that, to the extent any invoices from September 1997 were associated with petroleum products, it retroactively credited Paraguay for these amounts.¹³³

(3) Tribunal's Analysis

152. The Tribunal concludes that Respondent has not carried its burden in proving that Claimant improperly invoiced Paraguay for the inspection of petroleum imports after 1 September 1997. Respondent has provided no evidence that the imports in question were for petroleum products rather than equipment and has not disputed Claimant's contention that it credited Paraguay for any invoices associated with petroleum product shipments in September 1997.

¹³¹ See, e.g., Day 1 Tr. (Merits) at pp. 166:14-167:9.

¹³² Respondent's Rejoinder at para. 29.

¹³³ Day 1 Tr. (Merits) at pp. 40:17-41:7; Day 1 Tr. (Merits) at p. 136.

c. Conclusion

153. On the basis of the foregoing, the Tribunal concludes that Respondent has failed to meet its contractual commitments and that such breach violates Respondent's obligation under Article 11 of the BIT to observe "the commitments it has entered into with respect to the investments of the other investors of the Contracting Party."
154. Claimant has demonstrated, and Respondent does not dispute, that Claimant's invoices were not paid. Furthermore, Respondent has failed to carry its burden of proof in showing that the non-payment was justified due to Claimant's failure to meet its contractual obligations. Indeed, it does not appear that Respondent raised any complaint with Claimant regarding its invoicing procedures during the life of the Contract. The failure of Respondent to raise any concerns during the life of the Contract is particularly telling given the ample opportunity it had to do so during Customs' weekly meetings with SGS.
155. The Tribunal also notes that, according to Article 4.5 of the Contract, "[s]hould any discrepancy event arise between the Ministry and SGS, in connection with the documentation attached to the invoice, payment of the non-objected amounts shall be made, the parties having to promptly settle such discrepancies." Therefore, if there were any disagreement between the parties regarding the invoices, Respondent could have paid the uncontested portions of the invoices and contested the remainder. Respondent did not, however, contest the invoices at the time. Eventually, Respondent simply ceased making payments, but it did not link the non-payment to Claimant's invoicing practices and did not pay even plainly uncontested amounts.
156. Accordingly, the Tribunal finds that Respondent has failed to observe its contractual commitments in breach of Article 11 of the BIT.

3. Article 11 Claims Based on Alleged Extra-Contractual Commitments

157. Claimant asserts that the "extra-contractual" statements made by Paraguayan officials promising to pay SGS's invoices created additional enforceable commitments under Article 11 of the BIT. Respondent has argued that any statements by Paraguayan

officials outside the Contract itself are not binding promises that are enforceable under Article 11. Respondent also argues that any such statements are inadmissible as they related to settlement discussions between the parties.

158. The Tribunal concludes that it need not resolve these matters. Even if the extra-contractual statements Claimant references constituted binding commitments, and even if Respondent broke such commitments, the breach would not result in any additional liability on behalf of Respondent. Even under Claimant's argument, the extra-contractual statements were merely promises to meet Respondent's underlying commitments under the Contract, and the Tribunal has already decided that Respondent has failed to observe those commitments. Having reached that conclusion, the Tribunal need not decide whether Respondent made additional promises that at best merely confirmed those commitments.
159. With respect to the admissibility of the extra-contractual statements, the Tribunal did not rely upon those statements in reaching its conclusion that Respondent failed to observe its commitments under the Contract. Therefore, the Tribunal need not resolve the issue of whether the statements are protected as settlement discussions or otherwise inadmissible.

IV. CLAIMANT'S REMAINING CLAIMS

160. In addition to its claims under Article 11 of the BIT, Claimant asserts that Respondent's actions impaired Claimant's investment by undue and discriminatory measures in violation of Article 4(1) of the BIT and amounted to a denial of fair and equitable treatment under Article 4(2) of the BIT.
161. In light of the Tribunal's conclusion that Respondent breached Article 11 of the BIT by failing to meet its payment obligations under the Contract, the Tribunal need not address Claimant's remaining claims. Each of those claims arises from the same facts, and reduces to a claim that Respondent failed to pay the invoices. Even if the Tribunal were

to find in favor of Claimant with respect to these claims, Claimant's damages would be unchanged. Therefore, any additional legal findings on these matters are unnecessary.¹³⁴

V. RESPONDENT'S CLAIM OF PREJUDICE

162. Respondent argues that its defense of this case was unduly prejudiced by the fact that Claimant waited several years after the termination of the Contract to initiate dispute settlement proceedings. During the intervening period, Respondent argues, records were lost and personnel changed.
163. In the Tribunal's view, Respondent was not prejudiced by the passage of time. Again, the basic facts are not in dispute. It is not disputed that Respondent was obligated to pay properly issued invoices. As discussed above, Respondent has failed to do so, and there is no evidence to the contrary.
164. Furthermore, Respondent has argued throughout the arbitration that it continued to review SGS's performance of the Contract long after the agreement had terminated, and at least until 2006. Respondent must have believed that its own internal records were sufficient at least for purposes of those reviews, as it was able at the time to reach certain internal conclusions on certain aspects of the Contract, as discussed above. At a minimum, as it was itself continuing to review the matter with the ultimate objective of deciding whether or not payment was appropriate, it was incumbent on Respondent to preserve its own records. If it failed to do so, Claimant cannot be required to bear the consequences.
165. Finally, Respondent was well aware that Claimant continued to seek payment of its invoices. As Claimant notes, the delay in initiating the arbitration is in part due to the

¹³⁴ While the Tribunal need not resolve Claimant's claims that Respondent has breached the fair and equitable treatment standard, the Tribunal notes that there is support for the proposition that a breach of contract may rise to the level of a breach of the fair and equitable treatment obligation. *See, e.g., News from ICSID*, Vol. 11, No. 1 (Winter 1994), at 5 (noting that the Investment Protection Principles adopted in 1992 by the Council of the European Communities to provide details for the application of the investment protection and promotion principles contained in the Fourth Lomé Convention on cooperation between the group of African, Caribbean, and Pacific countries and the EC and its Member States, define "fair and equitable" treatment to encompass observance of undertakings); UNCTAD, Fair and Equitable Treatment 35 (UNCTAD Series on Issues in International Investment Agreements, 1999) (concluding, with reference to the United Kingdom model BIT, that "the idea of *pacta sunt servanda* . . . may also be viewed as a part of the fair and equitable standard").

fact that the parties were continuing to discuss ways to resolve the dispute during the several years after the Contract terminated. Respondent certainly knew that the claims for payment had not been forgotten or withdrawn, even if it could not know with certainty that Claimant would initiate arbitration proceedings. The fact that it did not retain and protect its records is an unfortunate problem of its own making. In light of these considerations, the Tribunal does not believe that Respondent has been unfairly prejudiced.

166. The Tribunal also notes that, unlike certain other investment agreements, the BIT at issue in this dispute does not contain a limitation period that would prevent Claimant from bringing a claim several years after the events in question took place. Therefore, there is no basis in the text to punish Claimant for failing to exercise its rights sooner.

VI. DAMAGES

A. Claimant's Position

167. Claimant claims that it is entitled to damages equal to the sum of the unpaid invoices plus interest accruing from July 1999.
168. Over the course of the Contract, SGS issued 35 invoices to Respondent. Respondent paid 10 of those invoices, leaving 25 unpaid. The total of the unpaid invoices is US\$ 39,025,950.86.¹³⁵
169. Claimant calculated interest by applying, on a simple rather than compound basis, the U.S. dollar 30-day LIBOR rate average for each month plus two percentage points, starting in July 1999. Claimant does not claim interest for any period prior to July 1999.¹³⁶ Calculated in this manner, Claimant claims damages for interest in the amount of approximately US\$ 22.5 million through February 2011.¹³⁷
170. Claimant argues that LIBOR plus two percentage points is the appropriate interest rate “[b]ecause, for companies like SGS, commercial borrowing is usually more expensive

¹³⁵ See Lironi Statement, Annexes B and C.

¹³⁶ See, e.g., Day 2 Tr. (Merits) at pp. 287-292.

¹³⁷ Interest Calculations as of 28 February 2011 and projected to 30 September 2011, prepared by M. K. Lironi, Ex. C-158.

than the LIBOR rate, [and] it is SGS's practice in pre-shipment inspection contracts similar to the Contract to mark up the referenced LIBOR rate by 2 percentage points when calculating interest on overdue payments."¹³⁸ Claimant also refers to a letter SGS submitted to the Ministry of Finance dated 16 September 1999, in which it noted that it would be charging interest at the rate of LIBOR plus two percentage points starting on 1 July 1999.¹³⁹

171. Claimant asserts that its position that interest should accrue from July 1999, the first month after the Contract was terminated, is consistent with Article 38(2) of the International Law Commission's (ILC) Articles on State Responsibility and the UNIDROIT Principles of International Commercial Contracts. Claimant argues that both documents suggest that interest should begin to accrue from the time when payment is due. Claimant notes Respondent's argument (discussed below) that, under Paraguayan law, interest should only begin to accrue on the date Claimant initiated arbitration. However, Claimant argues that the cases Respondent cites are inapposite as they do not deal with unpaid contractual obligations.¹⁴⁰
172. Claimant also notes Respondent's argument that Claimant waited several years after termination of the Contract to initiate arbitration and should have mitigated its losses either by terminating the Contract once payments ceased or by initiating dispute settlement proceedings earlier. However, according to Claimant, "[a]n injured party does not fail to 'mitigate' its losses by not commencing legal action to prevent interest from accruing, especially where, as here, the contention is merely that legal action (resort to courts in Paraguay) should have been commenced sooner than it ultimately was (this arbitration). Interest is not an independent head of damage, but an aspect of the full reparation due for a loss."¹⁴¹ Furthermore, Claimant argues, Claimant did not terminate the Contract because Respondent continued to promise to make payments.¹⁴²

¹³⁸ Lironi Statement at para. 21.

¹³⁹ Claimant's Memorial at para. 214; Letter from SGS to Minister of Finance dated 16 September 1999, Ex. C-35.

¹⁴⁰ Claimant's Reply at para. 236, n. 361.

¹⁴¹ Claimant's Reply at para. 231.

¹⁴² Claimant's Reply at para. 232.

173. Finally, Claimant notes Respondent’s argument that Claimant is inappropriately availing itself of the arbitration process to insulate itself from the risks of investing in Paraguay. However, according to Claimant, “Paraguay does not allege any lack of diligence on the part of SGS when entering into the Contract, and it sits ill in Paraguay’s mouth to suggest that SGS should not have trusted its contractual counterparty, the Ministry of Finance, or relied on the representations of the President of Paraguay and the Minister of Justice.”¹⁴³

B. Respondent’s Position

174. Respondent does not dispute Claimant’s mathematical calculations,¹⁴⁴ but contests several of Claimant’s underlying assumptions.¹⁴⁵

175. First, Respondent argues that Claimant has not proven that any breach of Articles 4(1) and 4(2) of the BIT was the proximate cause of any damages Claimant may have suffered. Rather, Respondent argues, any damages were related solely to the alleged breach of the Contract.¹⁴⁶ Respondent argues that “if SGS was damaged in the amount of \$60 million—a claim Paraguay categorically rejects—those damages are the consequence of Paraguay’s supposed breach of the Contract, a dispute we argue can only be resolved in Paraguay’s courts.”¹⁴⁷ As a result, according to Respondent, “aside from the contractual losses, which SGS can recover only if it prevails on its Article 11 claim, SGS does not allege any losses arising from the violation of BIT provisions.”¹⁴⁸

176. Second, Respondent argues that Claimant is not entitled to damages for invoices associated with inspections on Mercosur imports and for damages associated with multiple invoices for single shipments.

177. Third, Respondent notes that it has been hindered in its defense against Claimant’s damages claims by the fact that it does not possess all of the Inspection Certificates.

¹⁴³ Claimant’s Reply at para. 233.

¹⁴⁴ See, Day 2 Tr. (Merits) at p. 298:2-14.

¹⁴⁵ See, Day 1 Tr. (Merits) at pp. 102:19-105.

¹⁴⁶ Respondent’s Counter-Memorial at paras. 223-226; Respondent’s Rejoinder at paras. 179-180.

¹⁴⁷ Respondent’s Counter-Memorial at para. 223.

¹⁴⁸ Respondent’s Counter-Memorial at para. 224.

178. Fourth, Respondent argues that Claimant is using the arbitration to insulate itself from the risks of investing in Paraguay, and that Claimant should have taken steps to mitigate any damages. Respondent argues that “SGS willfully, or at least negligently, let the interest on the purported debt mount by failing to exercise its contractual right to recover the debt in local courts.”¹⁴⁹ Respondent also notes that Claimant let the damages continue to mount rather than terminate the arrangement in accordance with the terms of the Contract.¹⁵⁰ At a minimum, Respondent asserts, Claimant should not be entitled to interest, particularly given the long delay in initiating dispute settlement proceedings. Respondent argues that its position is consistent with the ILC’s Commentary to the Articles on State Responsibility, which state that “failure to make a timely claim for payment is relevant in deciding whether to allow interest.”¹⁵¹
179. Alternatively, Respondent argues that Paraguayan law requires that interest accrue beginning only on the date Claimant initiated arbitration.¹⁵² Respondent furthermore asserts that Claimant’s suggested interest rate is too high but does not suggest an alternative rate.¹⁵³

C. Tribunal’s Analysis

180. The Tribunal concludes that Claimant is entitled to damages equal to the amount of the unpaid invoices plus interest accruing from July 1999. Respondent itself concedes that, if Claimant were to prevail on its Article 11 claim arising out of Respondent’s breach of contract, then Claimant would be entitled to damages. The Tribunal has upheld that claim and damages are, therefore, appropriate.
181. Different legal issues arise with respect to Claimant’s claims for principal and interest, and the Tribunal shall address each category separately.
182. With respect to principal, the Tribunal finds that Claimant is entitled to the entire amount of the unpaid invoices totaling US\$ 39,025,950.86. While Respondent argues that it has

¹⁴⁹ Respondent’s Counter-Memorial at para. 234.

¹⁵⁰ Respondent’s Counter-Memorial at para. 236.

¹⁵¹ Respondent’s Rejoinder at para. 181.

¹⁵² Respondent’s Counter-Memorial at para. 239.

¹⁵³ Day 1 Tr. (Merits) at p. 105.

been prejudiced by the fact that it does not have copies of all of the underlying Inspection Certificates, Claimant has provided copies of the invoices,¹⁵⁴ and Respondent has not provided evidence questioning their accuracy or authenticity. The Tribunal has also already rejected Respondent's argument that SGS improperly submitted invoices associated with inspections of Mercosur imports and issued multiple invoices for single shipments. As a result, no offset or deduction from the principal would be appropriate.

183. With respect to interest, whether or not interest awarded to compensate for the time value of money lost as a result of a wrongful failure to make a payment on the date due may be characterized as an independent head of damage, there can be no doubt that it is an essential component of full reparation. Nor can it be said that it would be in any way punitive or unfair to award interest given that Respondent has been in possession of the unpaid sums for several years and has presumably made use of those funds. If it had not been in possession of those funds, then it presumably would have had to borrow the money and been required to repay it with interest. It is fully appropriate, therefore, to apply interest to the principal awarded to Claimant.
184. The virtually universal principle of international law and international arbitration practice in the case of a delayed payment of monetary obligations due is to apply interest as of the date payment became due. This is clear, for example, from the ILC's Articles on State Responsibility.¹⁵⁵ The Tribunal notes that here Claimant has adopted the conservative approach of requesting interest only as from July 1999, the date of contract termination, rather than from the date when each invoice became due.
185. The Tribunal agrees with Claimant that the authorities Respondent cites for the proposition that Paraguayan law permits interest only from the date the claim is filed are inapposite in that they do not deal with contract claims. As noted, Respondent points to the statement in the Commentary to the Articles on State Responsibility that a "failure to make a timely claim for payment is relevant in deciding whether to allow interest." However, the "claim" to which the Commentary refers is not the initiation of the dispute

¹⁵⁴ SGS unpaid invoices with accompanying credit notes, Ex. C-143.

¹⁵⁵ According to Article 38(2) of the ILC's Article on State Responsibility, "Interest runs from the date when the principal sum should have been paid until the date the obligation to pay is fulfilled."

but the time when the injured party demanded payment.¹⁵⁶ In this case, Claimant first demanded payment of its invoices during the life of the contract, and indicated in July 1999 that it would assess interest in the amount of LIBOR plus two percentage points. Claimant's claim for payment was clearly timely, indeed it was contemporaneous with Respondent's non-payment. The Tribunal concludes, therefore, that even were interest to run only from the date of demand for payment, rather than the date of non-payment, interest should begin to accrue in July 1999.

186. Claimant has requested simple interest based on the U.S. dollar 30-day LIBOR rate average (the "LIBOR rate") plus two percentage points.¹⁵⁷ Claimant has explained this is the rate SGS typically charges on unpaid invoices.

187. The Tribunal notes that the Contract does not specify the amount of interest to be paid on unpaid amounts, and, in fact, does not refer to interest at all. Claimant's 16 September 1999 letter to the Ministry of Finance indicating that it would charge interest at the rate of LIBOR plus two percentage points was merely a unilateral statement of intent, which was neither accepted nor apparently even acknowledged by Respondent. Neither Respondent nor this Tribunal is bound by that rate.

188. In light of all the circumstances in this case, the Tribunal has concluded that it would be appropriate to apply the LIBOR rate plus one percentage point.

VII. COSTS

189. Claimant seeks an award for costs based on Respondent's continuing refusal to pay the invoices and Respondent's failure to pay its share of the costs associated with this

¹⁵⁶ The relevant paragraph appears on p. 109, n. 619 of the Commentary (Ex. RL-48) and states:

Using the date of the breach as the starting date for calculation of the interest term is problematic as there may be difficulties in determining that date, and many legal systems require a demand for payment by the claimant before interest will run. The date of formal demand was taken as the relevant date in the *Russian Indemnity* case . . . by analogy from the general position in European legal systems. In any event, failure to make a timely claim for payment is relevant in deciding whether to allow interest.

¹⁵⁷ The Tribunal notes that Claimant's spreadsheet showing its calculation of interest based on LIBOR plus two percentage points appears to contain an error for the applicable interest in June 2006. The spreadsheet shows an interest rate of 5.2455%, which appears to be the LIBOR rate rather than LIBOR plus two percentage points. Assuming that the applicable interest rate should have been LIBOR plus two percentage points, correcting the error would increase Claimant's claimed damages by approximately US\$ 100,000.

proceeding.¹⁵⁸ On July 1, 2011, Claimant provided its Statement of Costs, in which it claimed US\$ 1,792,605.95 in legal fees and US\$ 1,121,180.55 in other costs and disbursements.

190. Respondent also seeks an award of legal fees and related expenses, travel and lodging costs, and the costs of the arbitration. Respondent argues that an award of costs and fees would be appropriate given that Claimant alleges only a breach of contract, which in Respondent's view is not actionable under the BIT, and such contract contains a forum selection clause that precludes arbitration.¹⁵⁹ In its 1 July 2011 Statement of Costs, Respondent requested US\$ 696,985.20 in fees and US\$ 31,222.03 in costs.
191. In the absence of agreement of the parties with respect to the allocation of costs, Article 61(2) of the Convention authorizes the Tribunal to "assess the expenses incurred by the parties in connection with the proceedings, and [to] decide how and by whom those expenses, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre shall be paid."
192. The Tribunal believes that both sides have presented their positions ably and in good faith, and neither has caused undue delay or expense in the proceeding. However, Respondent has not paid its portion of the costs associated with this proceeding, and has forced Claimant to bear the entire cost itself. The Tribunal finds that Respondent should pay its share, and, therefore, awards to Claimant half of the costs of the arbitration, *i.e.*, the amount of the ICSID costs and fees that Respondent should have advanced. The Tribunal does not believe it is appropriate to make any other award with respect to costs and fees.

VIII. AWARD

193. On the basis of the foregoing, the Tribunal:

¹⁵⁸ Claimant's Memorial at para. 218.

¹⁵⁹ Respondent's Rejoinder at paras. 183-184.

194. Finds that Respondent has breached its obligations under Article 11 of the BIT by failing to guarantee the observance of the commitments it has entered into with respect to Claimant's investment;
195. Finds that it does not need to resolve Claimant's claim that Respondent's failure to fulfill its alleged extra-contractual promises of payment constituted an additional breach of Article 11 of the BIT because (i) those claims ultimately derive from the same set of facts and commitments that gave rise to the Tribunal's conclusion that Respondent breached Article 11 of the BIT by failing to guarantee the observance of the contractual commitments it has entered into with respect to Claimant and (ii) even if the Tribunal were to find an additional breach of the BIT due to Respondent's alleged failure to fulfill its extra-contractual promises, the finding would not affect the quantum of damages;
196. Finds that it does not need to resolve Claimant's claims that Respondent breached Articles 4(1) and 4(2) of the BIT because (i) such claims ultimately derive from the same set of facts and contractual commitments that gave rise to the Tribunal's conclusion that Respondent breached Article 11 of the BIT by failing to guarantee the observance of the contractual commitments it has entered into with respect to Claimant's investment and (ii) even if the Tribunal were to find an additional breach of Articles 4(1) and 4(2) of the BIT, the finding would not affect the quantum of damages;
197. Awards Claimant US\$ 39,025,950.86 plus interest at the U.S. dollar 30-day LIBOR rate average plus one percentage point beginning on 1 July 1999 until the date of payment;
and
198. Awards Claimant one-half of the amount of US\$ 673,923.28, which is the total amount of the costs of the arbitration.



Donald Francis Donovan

Árbitro

Fecha: 6 de febrero 2012



Pablo García Mexía

Árbitro

Fecha: 2 de Febrero de 2012



Stanimir A. Alexandrov

Presidente

Fecha: 8 Feb. 2012