FINAL AWARD

IN THE MATTER OF AN UNCITRAL ARBITRATION

Between

CLAIMANT

Link-Trading Joint Stock Company
Str. Ghioceilor, 1
2012 Chisinau
Republic of Moldova

And

RESPONDENT

Department for Customs Control
of the Republic of Moldova
Columna Str. 65
2001 Chisinau
Republic of Moldova

A. Factual Background

1. Claimant, Link-Trading Joint Stock Company, is a US-Moldovan joint venture company established under the laws of the Republic of Moldova in July 1996. Its business consisted essentially of the import of consumer products into the Free Economic Zone of Chisinau (hereinafter "the FEZ" or "the Chisinau FEZ") and their resale to retail customers, mainly Moldovan citizens, for their personal use.

2. Claimant registered as a resident in the FEZ as of November 15, 1996. It rented premises in Pavillion No. 1 located in the FEZ and commenced its operations in the beginning of 1997.

3. Under the legislation in effect in Moldova on the date when Claimant registered to become a resident in the FEZ in 1996, (1) Claimant was totally exempt from import duties and value added taxes upon import of its goods into the FEZ and (2) Claimant's retail customers were partially exempt from duties and taxes on import from the FEZ into the customs territory of Moldova of such goods. The partial exemption according to the Budget Law for 1996 was limited to the local currency equivalent of the first USD600 of such goods purchased in any given month.

4. The source of Claimant's exemption on imports into the FEZ was a law regulating the Chisinau FEZ, namely Law No. 625 adopted on November 3, 1995. The source of its customer's USD600 exemption was Annex 11 to the State Budget Law for 1996, adopted on December 14, 1995. The State

Budget Law was referred to in Regulation No. 05/1-07/507 of the Ministry of Finance dated April 11, 1996, which dealt with the imposition of taxes and duties in the FEZ. Article 1(1)(8) of the Regulation provided that :

"Individuals who are not subjects of entrepreneurial activity may take out from the territory of the free enterprise zone on the customs territory of the Republic of Moldova, goods free of customs duties, VAT and excises in the amount and limits set up annually by the Law on State Budget of the Republic of Moldova...."

5. The Budget Law for 1997, adopted on March 21, 1997, reduced the exemption applicable to Claimant's customers from USD600 to USD400. The Budget Law for 1998, adopted on December 27, 1997, further reduced the said exemption to USD250. And then in July 1998, an amendment to the Budget Law for 1998 was introduced by Law No. 96 of July 16, 1998, eliminating the USD250 exemption effective August 8, 1998. A new exemption based upon quantitative quotas for specified categories of consumer products, without regard to the value of the products involved, was established for imports from abroad by physical persons for their own consumption in Moldova, but this exemption was not applicable to purchases made in the FEZ.

6. With a view to implementing the amended Budget Law for 1998, the Respondent, Department for Customs Control of Republic of Moldova, issued a letter no. 583-005 on August 8, 1998 to the Administration of the Chisinau FEZ and, subsequently, issued an Order No. 466 on October 21, 1998 calling for residents of the Chisinau FEZ, including Claimant, to act as collecting agent for the Republic by adding to the price of goods sold to customers for import into the customs territory of Moldova the amount of

customs duties and value added tax due on sales of its products and to remit this amount to the State.

7. Claimant protested, taking the position that this change of the customs and tax treatment of its customers violated governmental guarantees of tax stability which had been given to Claimant for a 10-year period, substantially deprived it of its business, and constituted measures tantamount to an expropriation of its investment without compensation in violation of the provisions of the Bilateral Investment Protection Treaty between the USA and the Republic of Moldova. The Treaty was signed on April 21, 1993 and had become effective on November 25, 1994 (hereinafter "the Treaty"). According to Claimant, this expropriation took place as of August 8, 1998, the date of Respondent's letter no. 583-005. Respondent disagreed with Claimant's position, and asserted that the change in customs and tax treatment was not a breach of any obligation owing to the Claimant but was a normal and proper exercise of the State's regulatory power.

B. Procedural History of the Case

8. On November 27, 1999, somewhat more than a year after the dispute arose, Claimant served a Notice of Arbitration upon Respondent on the basis of the Treaty and in accordance with the UNCITRAL arbitration rules referred to in the Treaty. Upon its constitution pursuant to the UNCITRAL rules (as more fully set forth in the Award on Jurisdiction rendered by this Tribunal on February 16, 2001), the Tribunal by letter of August 3, 2000 invited Claimant to submit its Statement of Claim and Respondent to submit its Statement of Defense.

9. On August 9, 2000, Claimant confirmed that its Notice of Arbitration constitutes its Statement of Claim in this arbitration. In its Notice of Arbitration/Statement of Claim, Claimant sought the following relief:

   [A declaration of] the existence of the right of the company "Link-Trading" to sell goods in conditions of exemption from customs and fiscal tax during the entire prior period of company's activity;

   [A declaration of] the existence of the right of individuals to buy goods from company "Link-Trading" in conditions of exemption from customs and fiscal tax in value of USD600 at import onto the customs territory of the Republic of Moldova;

   [A declaration of] the existence of the violation of these rights by the Department for Customs Control and Customs Service of the FEZ;

   Qualification of these violations as measures tantamount to expropriation; Award of compensation for caused damages and lost profits (equivalent in lei of USD3,458,813.25) from the account of the Department for Customs Control.

10. On August 30, 2000, Respondent filed a Response to the Statement of Claim containing certain objections to jurisdiction as well as arguments on the merits of the dispute, and denying liability.

11. The Tribunal, on October 16, 2000, posed a series of specific questions to both of the parties with respect to jurisdiction and requested responses by November 15, 2000. Claimant responded on November 14. Respondent chose not to respond, despite a reminder letter sent by the Tribunal affording Respondent additional time to do so.

12. By agreement of the parties, the Respondent's jurisdictional objections were considered without an oral hearing as a preliminary matter and, on February 16, 2001, the Tribunal rendered an Award on Jurisdiction, holding that the Tribunal was properly constituted and has jurisdiction over the parties and the subject matter of the dispute before it. The question of the allocation of arbitration costs as between the parties was reserved until the Final Award.

13. Subsequent to the Award on Jurisdiction, the Tribunal requested the parties to submit further arguments and evidentiary materials on the merits of the claim and the quantum of damages by June 15 as for the Claimant and by July 15 as for Respondent, and to indicate by June 1, 2001 as to whether an oral hearing was requested.

14. On May 30, 2001, Claimant confirmed in writing that an oral hearing was not necessary. Respondent did not reply.

15. Claimant requested and received an extension of time to make its further submission until July 15. Respondent was given a similar extension until August 15, 2001. Claimant made its submission on July 12, including an expert opinion on expropriation under international law provided by Mr. Todd Jeffrey Weiler.

16. In its July 12, 2001 submission, Claimant proposed to amend its Request for Relief as follows:

"The issues to be resolved by the Arbitral Tribunal at the request of company 'Link-Trading':

Whether the Republic of Moldova's treatment of the investments of Alai Trading Corporation ("the Investor") constitutes an expropriation for which

compensation is owed under Article III of the US-Moldovian BIT;

Whether the Republic of Moldova's treatment of 'Link-Trading' ("the Investment") constitutes a breach of the international law treatment standards contained within Article II(3) of the US-Moldovian BIT; and

In the event that a breach of the BIT has occurred, what the appropriate amount of compensation should be to remedy such breaches.

Alternatively, [to find that] this Tribunal has authority to determine that such amendment is not necessary because the application of BIT Article II(3) is already contemplated within the claim."

17. Claimant also submitted on this occasion a new evaluation of its alleged damages and lost profits in an amount substantially exceeding the amount originally sought in its Notice of Arbitration/Statement of Claim.

18. On August 2, 2001, Respondent informed the Tribunal that a government commission had appointed a group of experts to study the matter in dispute and make proposals. It requested an extension of three months for its further submission in the arbitration. Claimant objected to such extension. The Tribunal decided to grant an extension but only until September 30, 2001.

19. On September 28, 2001, the Deputy Prime Minister of Moldova wrote to the Tribunal requesting on behalf of Respondent a suspension of proceedings pending completion of negotiations between the parties. Following further exchanges, and by consent of the parties, the Tribunal ordered a suspension of the proceedings until October 19, 2001 for settlement negotiations to take place and further ordered that, in the event that the proceedings resumed

thereafter, Respondent shall make its suspended submission by October 31, 2001.

20. On October 22, 2001, Claimant wrote the Tribunal to inform that, despite the signing of a Protocol No. 2 on October 8, 2001 between Claimant and the governmental commission studying the dispute, which it attached to its letter, no compensation had been received. It requested the resumption of the arbitration.

21. On October 28, 2001, a Moldovan attorney, Mr Mihail Buruiana (unrelated to the arbitrator, Ion Buruiana, appointed by Claimant in this case), appeared on behalf of Respondent and requested an extension of 30 days from October 31 to file Respondent's submission. The Tribunal granted an extension until November 30, 2001.

22. An issue arose as to the validity of Mr. Buruiana's power of attorney. This was resolved to the satisfaction of Claimant and the Tribunal. Respondent was granted one further extension until December 10, 2001 to file its submission, and was advised that no further extensions would be granted.

23. On December 10, 2001, Respondent made its submission, which it characterized as a "Statement of Defense," including an expert opinion of Professor Dr. Hans-Joachim Schramm on the question of expropriation under international law.

24. In its submission, Respondent objected to Claimant's proposed amendments to its Statement of Claim and also raised further jurisdictional arguments.

25. On December 18, 2001, Claimant at its own initiative submitted a Rejoinder to Respondent's submission. In light of this further submission, on January

2, 2002, the Tribunal invited Respondent to submit a reply to the Rejoinder by January 18, 2002, adding that no extensions would be granted and no further submissions would be accepted from either party.

26. On January 9, 2002, the American law firm of Vinson & Elkins wrote to the Tribunal to advise that it had been retained by the Claimant and Claimant's parent company, Alai-Trading. It requested an opportunity to make a further submission on behalf of Claimant and further requested an oral hearing "if the Tribunal determines that such would assist it in its review of the case." The Tribunal responded by referring counsel to the Tribunal's letter of January 2, 2002 closing the evidence in the case. It also recalled the fact, which had been noted by Vinson & Elkins as well, that Claimant had previously declined an oral hearing on the merits. The Tribunal concluded that it did not believe that it would be helpful at this point for it to order a hearing.

27. Respondent made its final submission on January 18, 2002 in accordance with the Tribunal's January 2, 2002 letter.

28. In connection with its deliberations, the Tribunal requested each party to exchange statements of their costs in accordance with the UNCITRAL rules by February 15, 2002 and allowed an opportunity for an exchange of objections by February 28, 2002. Submissions were made by both parties in this regard.

C. Contentions of the Parties

C.1 Claimant's Contentions

29. Claimant's case is predicated on the characterization of the amendment to the 1998 Budget Law and Respondent's implementation of that amendment as being tantamount to an expropriation of Claimant's investment in the Chisinau FEZ for which it is entitled to prompt and adequate compensation under Articles III and X of the Treaty. In its July 12, 2001 submission, Claimant asserted that this amendment also violated the international treatment standards of Article II of the Treaty.

30. In its Statement of Claim, Claimant contends that at the time of its investment in the Chisinau FEZ, Moldovan law guaranteed it for a period of 10 years against adverse change in customs and tax regulations and that the change in the customs and VAT exemptions applicable to its customers violated this obligation and had such an adverse effect upon Claimant's business as to constitute an expropriation of its investment under Articles III and X of the Treaty.

31. In its July 12, 2001 submission, Claimant sought leave to amend its claim in the manner cited in para. 16 hereinabove. Respondent objected to this proposed amendment as untimely and prejudicial.

32. Although Claimant noted that the adverse changes occurred over time, as the exemption ceiling was reduced first from USD600 to USD400 and then from USD400 to USD250, it is Claimant's contention that the alleged expropriation finally occurred when the amended 1998 Budget Law eliminated the exemption altogether and, more specifically, on August 8,

1998, when the tax authorities sought to implement within the FEZ the corresponding provisions of the amended 1998 Budget Law.

33. Claimant relies on several sources of law in support of its alleged entitlement to protection from changes in taxes and customs duties for a 10-year period. First and foremost, Claimant refers to Law No. 625 of November 3, 1995 on the Chisinau FEZ that provides in Article 7 as follows:

"In case of adoption of new legal acts deteriorating the circumstances of activity of residents of the free zone as regards the customs and tax regime foreseen by this Law, residents are entitled to be subject to the law of the Republic of Moldova in force on the date of their registration in the free zone for period of ten years."

34. The customs and tax regimes foreseen by Law No. 625 are contained in its Articles 5 and 6, which read in relevant part as follows:

Article 5. Customs Regime

...

(2) The following goods...shall be exempt from the customs tax:

Goods imported to the Free Zone for ultimate consumption;

Zone-origin goods exported from the Free Zone into the customs territory of the Republic of Moldova;

Zone-origin goods exported from the Free Zone outside the customs territory of the Republic of Moldova;

Any-origin goods exported via the Free Zone outside the customs territory of the Republic of Moldova;

Goods temporarily exported from the Free Zone without sale and returned back, including in another (processed or treated) form.

(4) Goods...imported to the Free Zone and having undergone no substantial treatment or re-cycling and exported into the customs territory of the Republic of Moldova shall be governed by the customs legislation provisions pertaining to the cost of the imported component....

Article 6. Tax Regime

The taxation of the incomes of the Free Zone residents shall be set at 45 percent of the corresponding tax rate existing in the Republic of Moldova.

...

(3) Free Zone residents which have invested a minimum USD250,000 capital equivalent in the Zone development shall be exempt from paying the income tax during 5 years starting from the year quarter following the quarter when the investment has reached the above-mentioned volume.

...

(5) Goods...originating from the Free Zone, shall not be subject to value-added taxation.

(6) The Free Zone Administration shall have the right to impose zonal taxes in accordance with the legislation.

(7) Exempt from VAT and excise duties shall be the following goods...
Goods exported from the Free Zone in conformity with the Customs Regime as envisaged by items b, c, d and e in Article 5(2);
Goods imported to the Free Zone from outside the customs territory of the Republic of Moldova;
Good originating from the customs territory of the Republic of Moldova and imported to the Free Zone for ultimate consumption, except those for sale through retailing.

35. The customs and tax regimes contained in Law No. 625 with respect to the Chisinau FEZ were consistent with the regimes applicable generally to FEZs in Moldova as set forth in the Law on the Free Zones No. 1451-XII of May 25, 1993 to which Claimant also refers.

36. Claimant argues that, since it is uncontested that retail sale of goods is a permitted activity within the FEZ, "ultimate consumption" within the meaning of Article 5.2(a) above must refer to retail sale of goods in the FEZ and buyers of those goods must be deemed to have associated rights to the exemption provided in connection with such sale of goods.

37. It then refers to Article 1.1.8 of Regulation No. 05/1-07/507 of the Ministry of Finance dated April 11, 1996 regarding imposition of taxes in the FEZ, which is cited in relevant part earlier in this decision, but which we repeat here:

"Individuals who are not subjects of entrepreneurial activity may take out from the territory of the free enterprise zone on the customs territory of the Republic of Moldova, goods free of customs duties, VAT and excises in the amount and limits set up annually by the Law on State Budget of the Republic of Moldova...."

38. Finally, Claimant refers to Law No. 998 on Foreign Investments of April 1, 1992 which provides at Article 43(1):

"In case of adoption of new legislation affecting the business of enterprises with foreign investments established before the adoption of such legislation, these enterprises are entitled during a ten year period as from the date of entry into force of the new legislative act to be subject to the legislation of the Republic of Moldova in force on the date of establishment of the enterprise."

39. As regards the measure of its damages, Claimant sought, in its submission of July 12, 2001, leave to amend its original claim in order to seek a higher amount of compensation based on new calculations made by its expert advisors. Respondent objected to such an amendment on the ground that it was untimely and prejudicial at such a late stage in the proceedings to allow Claimant to modify the amount in dispute, particularly when such amount could have been calculated at the outset.

40. Finally, in its July 12, 2001 submission, Claimant sought leave to amend its claim to seek a declaration of the rights of its parent company, as "Investor." Respondent also objected to this amendment on the grounds that it would improperly add a new party to the proceedings.

C.2 Respondent's Contentions

41. Respondent has argued that Claimant's case fails for jurisdictional, procedural and substantive law reasons.

42. As regards jurisdiction, Respondent asserts that Claimant does not have standing to bring this action under the Treaty, since Claimant is a Moldovan and not an American company.

43. Moreover, it alleges that Claimant's US parent company, Alai-Trading, is no longer in existence since March 1, 2000, according to a certificate obtained from the Secretary of State of Delaware, its place of incorporation, and that this affects Claimant's standing to bring the present action under the Treaty.

44. Respondent further asserts that Claimant's action is time-barred by the Moldovan prescription period that it alleges to be one year from the time the dispute arose.

45. On substantive grounds, Respondent argues that no State obligation was undertaken towards Claimant not to change the USD600 exemption from customs duties and value added tax upon import of goods by individuals into the Moldovan customs territory that was in effect in 1996 and that the possibility of such a change was a commercial risk assumed by Claimant at the time of its investment.

46. It argues that the 10-year stability provision in Article 7 of Law No. 625 on the Chisinau FEZ, relied upon by Claimant, is expressly restricted to the Customs Regime and Tax Regime stipulated in that Law, which are set out in Articles 5 and 6 of the Law, and that nothing therein gives an exemption to finished imported goods purchased at retail in the FEZ and imported into the customs territory of Moldova.

47. Respondent argues that Law No. 625 is not the source of the limited exemption afforded to non-residents to make purchases in the FEZ for import into the customs territory, and that such exemption derives solely from the State Budget Law.

48. Respondent further argues that the Regulation No. 05/1-07/507 on which Claimant relies is not a Law, and cannot create rights that do not have their source in a Law. Moreover, it argues that the Regulation in any event confirms that the exemption derives from the Budget Law and that the Budget Law is established on an annual basis.

49. As regards the general 10-year stability provision in the Foreign Investment Law, Respondent points out that Article 43(2) of that Law expressly excludes from the stability provision protection from changes in tax and customs legislation. Article 43(2) reads as follows:

"2. Section 1 does not apply to customs, tax, financial, money-credit, currency and anti-monopoly legislation...."

50. Furthermore, Respondent argues that the amendment to the 1998 Budget Law was a normal regulatory measure, neither unfair by its nature nor arbitrary or discriminatory in its application, and cannot therefore be viewed either as a measure tantamount to expropriation or as a violation of the international treatment standards set forth in Article II of the Treaty.

51. Respondent further argues that Claimant has not carried its burden of proving the causal relationship between the allegedly confiscatory measures of the State and Claimant's alleged damages. Respondent submitted evidence that the Moldovan currency devalued by more than 100% following the Russian financial crisis in August 1998, and argued that this was an equally likely or more probable cause of the setbacks in Claimant's business. It noted that the change in the Budget Law did not prevent Claimant from continuing to conduct its business through most of 1999.

52. Respondent further contests the calculations made by Claimant of its specific losses arguing that they include double counting, speculative amounts, and other amounts which are not properly recoverable even in the event of an expropriation.

53. In conclusion, Respondent requests in its submission of December 13, 2001 that the Tribunal adjudge and declare:

that claimant has shown no prima facie act of expropriation attributable to Moldova, and that the Tribunal does not have jurisdiction to entertain the claim;

further or alternatively, that no act of expropriation has occurred or is attributable to Moldova within the meaning of Article III of the BIT;

further or alternatively, that no breach of the international law treatment standards contained within Article II(3) of the BIT has occurred or is attributable to Moldova;

that the Request by the Claimant be dismissed; and

that the Claimant be required to pay Moldova's costs in this matter and the costs of the Arbitral Tribunal.

D. Discussion of the Issues Raised

54. This is an investment dispute under the Treaty. The Tribunal has already held in its Partial Award on Jurisdiction that it has jurisdiction to determine whether or not a breach of Article X(2) and Article III of the Treaty has occurred and that Claimant has standing to bring this arbitration under the terms of the Treaty. As previously noted, Article VI(8) of the Treaty states that:

"for purposes of an arbitration held under paragraph 3 of this Article [which includes the present UNCITRAL arbitration], any company legally constituted under the applicable law of a Party [Moldova] but that, immediately before the occurrence of the event or events giving rise to the dispute [i.e. August 8 1998] was an investment of companies of the other Party [USA], shall be treated as a company of such other Party."

Therefore, Claimant is treated as an American company for purposes of this arbitration under the Treaty, despite the fact that it is established in the Republic of Moldova.

55. Respondent has raised a new jurisdictional challenge based on evidence that Claimant's parent company, a Delaware company, has ceased to exist as of March 1, 2000. However, we find this fact to be irrelevant, since the critical date for purposes of determining Claimant's standing to sue, as a company controlled by a US investor, is the date on which the expropriation is alleged to have taken place, namely August 8, 1998.

56. In its July 12, 2001 submission, Claimant has sought to amend its request for relief to read as quoted in para. 16 above.

57. In its amended request for relief, Claimant no longer seeks the declaratory relief referred to in the first three paragraphs of its original Statement of Claim, as quoted in para. 9 above.

58. Claimant does seek, however, for the first time a determination that its parent company, Alai Trading, suffered an expropriation under the terms of Article III of the Treaty. Since its parent company is not a party to this arbitration, this Tribunal has no jurisdiction to make any determination as to its rights under the Treaty. In accordance with the terms of the Treaty, had Alai Trading wished to make its own claim in arbitration, it would have had to comply with the procedures set forth in the Treaty for initiating such an arbitration. It has not done so. We consider, however, that this new claim is not intended to be an abandonment of Claimant's own claim of expropriation as set forth in the original Statement and argued in its subsequent submissions.

59. Claimant also seeks to add a new independent claim based upon alleged violation of the international treatment standards of Article II(3) of the Treaty. Article II(3) provides in relevant part as follows:

(a) Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that required by international law.

(b). Neither Party shall in any impair by arbitrary or discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments....

(c). Each Party shall observe any obligation it may have entered into with regard to investments.

As we have already held in our Award on Jurisdiction, our competence in this arbitration is expressly limited to Articles X and III of the Treaty. However, since Article III cross-references to Article II(3), it is within our competence for purposes of Article III to determine whether a violation of the standards of conduct envisaged by Article II(3) has occurred.

60. Finally, Claimant continues to claim for damages and lost profits but increases the amount stated in its original claim. While Claimant does not adequately justify the late recalculation of its claim, in light of the long time period between Claimant's July 12, 2001 submission and Respondent's answer on December 10, 2001 we do not believe that Respondent was prejudiced thereby.

61. There have been some references in the arguments of the parties to contracts concluded by Claimant with authorities in the FEZ with respect to the proposed investment. Claimant has not, however, formulated a claim based upon breach of any of said contracts. Moreover, as has already been noted in the Award on Jurisdiction, this Tribunal is not competent to determine whether the contractual provisions have been respected by the parties thereto, since said contracts create civil law relations and are

governed by their own specific arbitration agreements between the parties thereto.

62. Respondent has argued that Claimant's action should be considered time-barred by virtue of a one-year prescription period applicable to certain civil law claims under Moldovan civil law. Claimant has countered by referring to a 3-year prescription period which it believes is applicable. We consider both such prescription periods to be inapplicable to the present action since this is not an action for breach of contract under Moldovan civil law, but for violation of the State's treaty obligations as defined in the Investment Protection Treaty. The Treaty contains no applicable prescription period.

63. Claimant's case is predicated upon a change of tax and customs regulations allegedly constituting an act of expropriation under the Treaty. It argues that Article X(2) of the Treaty required Respondent to respect the terms of Claimant's investment in the State's tax policy. Article X of the Treaty does indeed permit claims of expropriation to be predicated on tax measures where such measures are found to go beyond normal regulatory action and constitute a direct or indirect taking of a protected investor's investment. Article X provides in relevant part as follows:

"With respect to its tax policies, each Party should strive to accord fairness and equity in the treatment of investment of nationals and companies of the other Party. Nevertheless, the provisions of this Treaty, and in particular Article VI and VII, shall apply to matters of taxation only with respect to the following:
expropriation, pursuant to Article III..."

64. It is clear from paragraph (1) of Article X of the Treaty that not all fiscal measures necessarily constitute an expropriation, although their habitual

effect is to cause the taxpayer to surrender part of his income or property to the State. As a general matter, fiscal measures only become expropriatory when they are found to be an abusive taking. Abuse arises where it is demonstrated that the State has acted unfairly or inequitably towards the investment, where it has adopted measures that are arbitrary or discriminatory in character or in their manner of implementation, or where the measures taken violate an obligation undertaken by the State in regard to the investment.

65. The policy of the Republic of Moldova over a number of years, as reflected in its annual budget laws, has been to reduce the dollar exemption it had originally allowed on duty- and tax-free imports of retail goods into its territory from the FEZ. Respondent has asserted that the 1995 Budget Law had authorized a USD1000 exemption which had been reduced to USD600 prior to Claimant's investment. Although the text of the 1995 Budget Law is not in evidence, Claimant has not challenged this assertion. A pattern of reductions did, however, occur thereafter until August 1998, when the monetary exemption applicable in the FEZ was eliminated and a new system of quantitative exemptions was introduced with respect to goods imported by Moldovan citizens upon return from abroad. The new quantitative exemptions were construed by the Customs Department as not applicable to retail purchases by Moldovan citizens made in the FEZ, on the ground that the FEZ was located within the national borders of the Republic. The new policy was maintained and stated more clearly in subsequent budget laws through 2001.

66. Claimant maintains that the amended 1998 budget law, as interpreted, was an unfair, inequitable, arbitrary or discriminatory taking of its business in violation of Article III and Article II(3) of the Treaty, in that its Moldovan customers could no longer make retail purchases in the FEZ on a tax

exempt basis, while they could import into Moldova the same types of merchandise upon return from travels abroad and benefit from the newly established quantitative exemptions.

67. Putting aside for the moment the question of whether a causal link has been established between the above-mentioned tax measures and the failure of Claimant's business, were the measures taken by the Respondent, unfavorable as they were, of a type that should be considered to be an arbitrary or discriminatory exercise of the State's tax powers vis-à-vis Claimant?

68. Customs policy is a matter that clearly falls within the customary regulatory powers of the state and the burden is on Claimant to establish that there has been an abusive exercise of that power as regards Claimant and that this abusive exercise of power produced consequences tantamount to expropriation of its investment.

69. The changes to the import regime that took place in the present case were contained in annexes to the national budget which, as in most countries, is adopted annually and is subject to annual change. As such, they were changes of general application, and not directed specifically against Claimant.

70. In this connection, we believe that the impact of these changes on Claimant must be analyzed in the context of their impact on other retailers in the FEZ and/or elsewhere in Moldova, since this is the relevant territory with respect to which the Moldovan government exercises its regulatory power.

71. No evidence has been submitted to show that Claimant was treated less favorably than any other retailer within the FEZ 'by virtue of these

regulations. Nor was Claimant treated less favorably in relation to retailers in Moldova located *outside* the FEZ, since there is nothing to indicate that the same customs duties and VAT were not payable with respect to the imported merchandise of such other retailers. Indeed, since Claimant continued to be able to import goods into the FEZ on a duty-free and tax-free basis, it could defer the payment of duties and VAT until final resale, whereas local retailers presumably were obliged to pay these charges upon import. Moreover, Claimant enjoyed special reduced income tax treatment under the regulations pertaining to residents in the FEZ, treatment that was presumably not available to local retailers outside of the FEZ.

72. We therefore conclude that the substance of the tax measures adopted by the Moldovan government, while unfavorable to Claimant, were not dissimilar to the policies of many countries in the world levying duties and taxes on imports into their customs territory and were not inherently abusive, arbitrary or discriminatory towards Claimant. They did not place Claimant in a worse competitive position than any other category or nationality of retailer in Moldova.

73. Tax measures may also become expropriatory without necessarily being arbitrary or discriminatory, when their application violates a specific obligation that the State has previously undertaken in favor of a particular person or class of persons, such as an investor protected under a treaty. Indeed, expropriation under Article III of the Treaty is prohibited when it violates the principles of treatment set out in Article II(3) of the Treaty, including Article II(3)(c) which requires a State Party to *"observe any obligation it may have entered into with regard to investments."*

74. Did, then, the reduction and elimination of the USD600 exemption enjoyed by Claimant's customers at the time when Claimant started business in the

FEZ violate Claimant's rights conferred or created by the Treaty with respect to its investment?

75. Claimant's principal contention in this arbitration, and indeed the basis for the legal analysis of Claimant's expert on expropriation, Mr. Weiler, has been that the change and ultimately the elimination of the exemption originally available to Claimant's customers on their purchases in the FEZ was a violation of an obligation of 10-year tax stability owing to Claimant both under Article 7 of the Law No. 625 on the FEZ and under Article 43(1) of the Law No. 998 on Foreign Investments of April 1, 1992.

76. We are not persuaded by this contention for the following reasons.

77. Article 7 of Law No 625 on the FEZ provides for stability only with respect to the tax exemptions provided for by that Law, i.e. *"the customs and tax regime foreseen by this Law."* That regime is defined in Articles 5 and 6 of Law No. 625 cited in relevant part earlier in this decision.

78. Article 5 (Customs Regime) lists five cases in which goods shall be exempt from customs duties. Four of these cases deal with exports from the FEZ. Claimant has not argued that its goods would fall within any of those cases. (Article 5(2)(b)-(e)). The fifth case deals with *imports* of goods into the FEZ for "ultimate consumption" *(konechnoe potreblenie)*, which might also be translated as "final use." Goods imported into the FEZ for final use are not subject to customs duties on import into the FEZ. Even if one were to interpret "final use" to include retail sale of the goods, there is no basis for reading this provision to mean that, in the event that goods are then exported from the FEZ into the customs territory of Moldova no customs duty would be payable. If this had been intended, such goods would have been covered by an express export exemption as in the other four cases listed.

Article 5(2)(a) speaks only of an exemption on the *import* of goods *into* the FEZ.

79. Moreover, it must be noted that the Article 5(2)(a) exemption is a total exemption. If Claimant's customers were indeed beneficiaries of such an exemption upon bringing goods into the customs territory of Moldova, then they would have been entitled to a full exemption, and not one limited to only USD600.

80. We find further support for this interpretation in the wording of Article 5(4). Here it is made clear that the imported component of goods produced in the FEZ and then exported into the customs territory of Moldova will be subject to the customs legislation pertaining to the cost of the imported component. If goods imported for incorporation into products to be manufactured in the FEZ are subject to duty upon export of the manufactured product to the customs territory, the import and sale for export to the customs territory of finished goods would appear to be an *a fortiori* case.

81. Nor do we find this inconsistent with the uncontested fact that retail business was clearly an authorized activity in the FEZ under Article 3 of the Law. Other incentives existed for a retailer to invest in the FEZ, including the duty-free import of goods to the FEZ provided by Article 5(2)(a) and the favorable income tax treatment for FEZ residents provided under Article 6(1).

82. Article 6 (Tax Regime) defines the VAT and excise duty exemptions applicable in the FEZ. Three cases are identified – two dealing with imports into the FEZ, which are exempted, and one dealing with exempted exports from the FEZ. As regards the case of exports from the FEZ, Article 6(7)(a) provides that exempted goods are those exported from the FEZ in conformity with the Customs Regime as envisaged by items (b), (c), (d) and

(e) in Article 5(2). (Cited *supra*). It may be recalled that none of these items corresponded to the present situation. Claimant maintained that its sales fall under Article 5(2)(a), not Article 5(2)(b)-(e).

83. Claimant heavily relies on Article 1.1.8 of Regulation No. 05/1-07/507 regarding imposition of taxes in the FEZ as proof that the 10-year tax stability in Law No. 625 was intended to extend to the partial exemption enjoyed by its customers on bringing their purchases from the FEZ into the customs territory of Moldova, which it characterized as an "associated right" of Claimant. However, a literal reading of Article 1.1.8, cited earlier in this decision, leads to the opposite conclusion. Article 1.1.8 expressly refers to the Law on the State Budget, not to Law No. 625, as its legislative basis, and states that such customs and VAT exemptions are in an amount and limits set up *annually* by the Budget Law. In light of this language, there were no reasonable grounds for assuming that this partial exemption would not be subject to legislative review and possible modification each year in the context of the annual budget.

84. Claimant also refers the Tribunal to Article 43(1) of the Foreign Investment Law which more generally protects enterprises with foreign investments (regardless of whether or not located in the FEZ) from *"new legal acts that would change the conditions for activity"* of the enterprise during a 10 year period from the creation of the enterprise.

85. However, as Respondent pointed out, Article 43(2) goes on to provide that *"[T]he provisions of paragraph 1 shall not extend to customs, tax, antimonopoly, financial, credit monetary, foreign exchange, as well as the legislation that regulates the insurance of state security, protection of environment, public order, morality and health of the population."* Since we

are here dealing with a tax measure, the Foreign Investment Law stability provision is inapplicable.

86. We therefore conclude that the State had not assumed any specific obligation towards Claimant to maintain unchanged the customs and tax regimes applicable to Claimant's customers for import of goods from the FEZ into the customs territory of the Republic of Moldova.

87. The essence of any claim of expropriation is that there has been a taking of property without prompt and adequate compensation. However, many investment protection treaties and the Treaty which is the basis for the present arbitration extends the notion of a taking to include what has often been referred to as "creeping" or "indirect" expropriation by the State through measures which so substantially interfere with the investor's business activities that they are considered to be "tantamount" to an expropriation. Claimant has the burden of proving the causal link between the measures complained of and the deprivation of its business.

88. Claimant has alleged that the change of its customers' tax treatment led to the failure of its business since it was no longer economically viable for its business to compete in the marketplace. It has alleged that the prices of its merchandise increased by an average rate of 44% as a result of the final elimination of the exemptions enjoyed by its customers.

89. Respondent, however, has asserted that there was a 100% devaluation of the local currency following the Russian financial crisis in August 1998 and that this was a more likely cause for the decline of Respondent's business, which involved the sale of dollar valued imported merchandise.

90. Annex A of Claimant's submission of July 12, 2001 sets out the monthly sales statistics of the venture and the applicable monthly exchange rates over the period from January 1997, when business activity began, until end September 1999. We have noted that, despite Claimant's contention that it was expropriated on August 8, 1998 by virtue of the Respondent's interpretation of the amended 1998 Budget Law eliminating the exemption of its customers as from that date, Claimant's sales actually increased in September 1998 and then continued albeit at a decreasing level through September 1999. We have further noted that the applicable exchange was essentially stable from January through August 1998 and sharply dropped from September 1998 to January 1999 from 4.78 to 8.32 to the dollar, and to 11,01 in September 1999.

91. In light of this, we consider that Claimant has not presented sufficient proof that Claimant's business was expropriated as of August 1998, nor that the cause of the subsequent decline of its business was a direct result of the elimination of its customers' tax exemption as opposed to the devaluation of the Moldovan currency and the resulting decline in its customers' buying power. While one might suppose that the new tax measures contributed to Claimant's losses, that is not enough to constitute expropriation. Otherwise, the concept would be unlimited, since most tax measures have a cost impact on taxpayers. To prove expropriation, Claimant must show that as a direct consequence of the measures complained of Claimant was deprived of its investment. Claimant has not carried its burden of proof of this causal link.

92. In light of our conclusions as set forth above, we do not reach the question of the amount of compensation that might be due in the event of expropriation.

E. COSTS

93. Both parties have sought recovery of the costs of the arbitration and have made corresponding submissions thereon. Article 38 of the UNCITRAL rules states that the Tribunal shall fix the costs of arbitration in its Award and defines the term "costs." According to Article 40 of the UNCITRAL rules, the costs of arbitration, including fees for legal representation and assistance, shall in principle be borne by the unsuccessful party, although the Tribunal may apportion such costs among the parties if it determines that this would be reasonable under the circumstances of the case.

94. In light of our decision that Claimant has failed to prove its claim of violation of the Treaty by the Respondent, the reasonable costs of this arbitration shall be awarded to Respondent. Respondent has made a submission as to its costs on February 15, 2002, which consists of attorney fees of USD138, 352 and expenses of USD1,456.80, legal expert fees of USD2,200, and other expenses of the Respondent of USD2,414, for a total of USD144,422.80.

95. Considering that this arbitration did not involve any hearing and that Respondent's counsel appeared at a late date in the proceedings and was required to make only limited submissions, the Tribunal considers that it would be reasonable to award to Respondent an amount for its counsel fees and expenses of USD20,000. The fees of the legal expert appear to be reasonable at USD2,200. There is no substantiation for Respondent's other expenses, and these expenses are therefore denied. The total amount of party costs awarded to Respondent shall therefore be USD22,200.

96. The Tribunal has received a total amount of USD120,000 solely from Claimant as a security deposit for the Tribunal's fees and disbursements in

this arbitration. At the time of the Award on Jurisdiction, the Tribunal had incurred fees and expenses in the amount of USD40,000, which was paid to the Tribunal by way of an advance. The time incurred by the Tribunal since then has significantly exceeded what the Tribunal reasonably anticipated when the security deposit was set. This was due principally to the unsolicited further submission of Claimant on December 18, 2001 which necessarily required a further responsive pleading from Respondent. This being said, the Tribunal has decided not to award fees and expenses beyond the amount of the security deposit, but to allocate the deposit as follows in full satisfaction of its fees and expenses, to wit:

	Expenses	Fees		Totals
J. M. Hertzfeld, Esq.	USD2,200	USD 51,174	(45%)	USD 53,374
Prof. I. V. Buruiana	USD1,080	USD 31,273	(27.5%)	USD 32,353
Prof. I. S. Zykin	USD3,000	USD 31,273	(27.5%)	USD 34,273
	USD6,280	USD113,720		USD120,000

For these costs the parties are liable jointly and severally. As between the parties they shall ultimately be borne by Claimant. They will be covered out of the advance.

* * *

NOW THEREFORE THE ARBITRAL TRIBUNAL

DECIDES

A. Respondent did not violate Claimant's rights under Articles X and III of the US-Moldova Investment Protection Treaty, including with respect to the international law treatment standards envisaged therein by reference to Article II of the Treaty, by virtue of Respondent's reduction or elimination of the exemption from customs duties and taxes applicable to imports of goods by Claimant's customers from the FEZ onto the customs territory of the Republic of Moldova.

B. This Tribunal has no jurisdiction with respect to Alai-Trading, Claimant's parent company, and makes no determination with respect to the rights or obligations of Alai-Trading.

C. Claimant's claims are dismissed and its request for damages including lost profit is denied.

D. Claimant Link Trading Joint Stock Company is ordered to pay to Respondent Department for Customs Control of the Republic of Moldova compensation for Respondent's reasonable arbitration costs in the amount of USD22,500.

E. Both parties are ordered to pay jointly and severally the costs of the Arbitration Tribunal as follows:

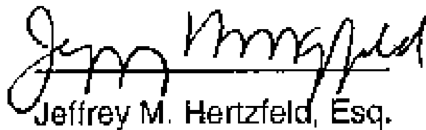
Jeffrey M. Hertzfeld, Esq., Presiding Arbitrator	USD53,374
Professor Ion V. Buruiana, Arbitrator	USD32,353
Professor Ivan S. Zykin, Arbitrator	USD34,273

As between the parties, these costs shall be ultimately borne by Claimant.

Place of Arbitration: Chisinau
Date of Award: April 18TH, 2002

THE ARBITRAL TRIBUNAL

Prof. Ion V. Buruiana
Arbitrator


Jeffrey M. Hertzfeld, Esq.
Chairman

Prof. Ivan S. Zykin
Arbitrator