INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

In the Matter of the Arbitration between

DUKE ENERGY INTERNATIONAL PERU INVESTMENTS NO. 1, LTD.

Claimant

and

REPUBLIC OF PERU

Respondent

ICSID Case No. ARB/03/28

PARTIAL DISSENTING OPINION OF ARBITRATOR DR. GUIDO SANTIAGO TAWIL

I

1. I have concurred with my distinguished colleagues and fellow arbitrators in most of the issues discussed in the Award. Unfortunately, I am unable to join in their conclusions on two issues: (i) the scope of the Tribunal's jurisdiction to construe Peruvian law and to review the correctness of SUNAT's decisions and assessments or of the Tax Court's decisions; and (ii) whether the Depreciation Assessment (as defined in paragraph 130 of the Award) constitutes a breach of the DEI Bermuda LSA. I feel obliged to briefly set down my opinion in relation to these two issues.

II

2. The Award takes the position that the Tribunal's jurisdiction does not include the power to review the correctness of SUNAT's decisions and assessments or of the Tax Court's decisions.[1]

3. While I have agreed that the Tribunal does not sit as the appellate division of the Tax Court, I respectfully dissent on the issue of the scope of the Tribunal's jurisdiction.

4. As the Tribunal stated in its Decision on Jurisdiction,[2] it is not for the Tribunal to determine whether any particular decision of the Tax Court is right or wrong as a matter of Peruvian tax law, but whether such interpretation is consistent with the rights stabilized for DEI Bermuda under its LSA. While the Tribunal does not exercise any authority over SUNAT's or the Tax Court's powers, it has been constituted to determine whether SUNAT's or the Tax Court's decisions in the present case represent a change from the stabilized regime under the DEI Bermuda LSA.

5. While a comparative exercise is reasonably straightforward for legislation and regulations and could suffice where a change is objectively demonstrable, the Award reflects the view that in the absence of proof of a stable pre-existing application or interpretation against

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1 Award, at para. 216.

2 At para. 159, *in fine.*

which the Tribunal can judge subsequent developments, the Tribunal can only evaluate the decision or assessment that is challenged by Claimant against a reasonableness standard.[3]

6. I am unable to agree with this conclusion. In my opinion, in such cases the Tribunal is entitled to depart from a strictly comparative analysis and determine the precise scope of the stabilized regime.

7. While Peruvian courts are the only forum empowered to interpret domestic law and to review administrative decisions in order to reverse or annul them, the Tribunal constitutes the proper contractually-agreed forum to construe Peruvian law in order to determine the scope of the stabilized regime under the DEI Bermuda LSA. In performing such function, the Tribunal's powers to interpret Peruvian law must be construed broadly and, in doing so, it is empowered to depart from the Peruvian courts' view if, in the Tribunal's opinion, such view does not reflect adequately the status of domestic law.

8. The parties have voluntarily decided to entrust that task to the Tribunal, not to Peruvian courts. Thus, in order to determine if the DEI Bermuda LSA has been breached, the actions of SUNAT and the Tax Court subsequent to the entry into force of the DEI Bermuda LSA must be evaluated against the Tribunal's own determination of the meaning and scope of the stabilized regime at the relevant time. The Tribunal's powers in such respect do not differ from those that would have been held by a local court called upon to decide whether the LSA has been breached if such court and not this ICSID Tribunal had been the forum contractually designated to settle the present dispute.

9. Therefore, in my opinion, in applying Peruvian domestic law pursuant to Article 42 of the ICSID Convention, the Tribunal is not limited to an analysis merely of the reasonability of the interpretation or application made by Peru of its own laws and regulations. Much less can the determination of the stabilized regime be made by reference to the reasonability of the interpretation of laws and regulations adopted by Respondent's local

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[3] Award, at para. 223.

courts after execution of the Egenor LSA –i.e. the Tax Court's decision of May 25, 2001– or to constructions elaborated subsequent to SUNAT´s tax assessments, such as the Tax Court's decision of April 23, 2004.

10. As stated above, this does not mean that the Tribunal's jurisdiction to decide this dispute includes the authority to reverse the decisions of the Peruvian courts or administrative agencies. Whatever finding the Tribunal reaches, it cannot exceed the boundaries of its jurisdiction, which is limited to determining whether a violation of the DEI Bermuda LSA has occurred.

11. The jurisdiction of local courts is, thus, distinct from the specific jurisdiction attributed to this Tribunal by the parties' agreement. Each is a distinct venue that serves a particular object and purpose.

12. As it happens in other fields of law, such interaction can give place to some particular but not totally unusual situations. It could well happen (as it has been increasingly recognized in the domain of Administrative Law in certain cases of State liability)[4], for example, that while an administrative decision remains extant in a legal system,[5] it still generates State responsibility and the duty to compensate.

III

13. I must also respectfully disagree with my distinguished colleagues on the decision adopted concerning the Depreciation Assessment.

14. The continuity rule was not in force at the time of the transfer of assets from Electroperú to Egenor and of the execution of both the Egenor LSA and the DEI Bermuda LSA.

15. While Article 105 of Chapter XIII of the Income Tax Law – prior to its 1998 amendment – provided for the application of the continuity rule to asset transfers resulting from

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4 *See* G. S. Tawil, "La Responsabilidad del Estado y de los Magistrados y Funcionarios Judiciales por el Mal Funcionamiento de la Administración de Justicia", Buenos Aires, 1993 (2nd. ed.) at pp. 137/146 concerning State responsibility for judicial errors in cases of decisions that have acquired the status of *res judicata*.

5 Due, as an example, to the impossibility of reversing it based on the lack of remedies available, standing or other limitations. This situation only arises in cases in which, as in the DEI Bermuda LSA, Claimant has an autonomous remedy available to claim State liability.

corporate reorganizations, Article 106 limited the concept of "reorganization" to corporate mergers and divisions, whose precise meaning was to be defined in the implementing regulations. As those implementing regulations had not been issued at the time of the transfer of assets from Electroperú to Egenor, Chapter XIII of the Income Tax Law was not enforceable.[6]

16. In the absence of a legal provision – i.e. the continuity rule or some other provision with similar effect – establishing a specific rate that Egenor was obliged to apply, Egenor was required to apply – as it did – the general depreciation rate provided for in the tax regime. By establishing that Egenor should have applied the special depreciation rate, Peru breached the DEI Bermuda LSA.

17. Even applying the reasonability test referred to at paragraph 302 of the Award –the application of which I do not agree with for the reasons stated in Section II above– I come to the conclusion that the Depreciation Assessment was based on an arbitrary interpretation of Peruvian tax laws.

18. It is an established principle in tax law –to which Peruvian tax law is not foreign- that governmental powers can only be exercised pursuant to certain conditions and limitations. One such limitation is given by the principle *nullum tributum sine lege*. A tax obligation can only arise from a legal provision. Taxpayers cannot be deemed to be responsible for any tax obligation not stated in the law.

19. This legality principle is at the core of the Peruvian legal system. Article 74 of the Peruvian Constitution establishes such principle as follows: "Taxes are created, modified and abrogated, or exoneration is established, exclusively by law or legislative decree in case of delegation of powers, except for fees and rates that are regulated by supreme decree (…)".

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[6] The parties to the present dispute agree that the Tax Court considered that Chapter XIII was not in force at the time the transfer of assets from Electroperú to Egenor took place. *See* Respondent's Rejoinder, para. 194.

20. The constitutional principle of legality has also been codified in the Peruvian Tax Code and in the Private Investment Law.

21. Rule IV of the Peruvian Tax Code provides that "Only by law or legislative decree in case of delegation it is possible to a) create, modify and suppress taxes; indicate the fact giving rise to the tax obligation, its calculation base and percentage; the tax creditor; the tax debtor (…)".[7]

22. The Private Investment Law confirms the principle by stating in its Article 14 that "The constitutional principle of legality in relation to tax issues implies that the creation, modification or elimination of taxes, as well as the granting of exemptions and other tax benefits, determination of taxable matter, persons subject to taxation, tax collectors and tax withholding agents, the applicable rates and the taxable base, should be made by means of a law voted by the Congress of the Republic, in accordance with the provisions set forth herein."[8]

23. The depreciation rate applicable to a company's assets is an essential component of the taxable income, i.e. the tax calculation base under the Income Tax Law. Determination of the tax base depends on the applicable depreciation rate. The lower the depreciation rate is, the higher is the tax base, and *vice versa*. Therefore, the way to determine the depreciation rate cannot be legitimately established by any means other than by the law and its implementing regulations.

24. If the continuity rule was not applicable due to the lack of specific tax legislation (the implementing regulations), it cannot be inferred from principles or legal doctrine. Otherwise, Chapter XIII of the Income Tax Law and the condition therein established in order for such Chapter to enter into force (the issuance of the absent implementing regulations) would be meaningless.[9]

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7 *See* Respondent's Exhibit R-256.

8 *See* Claimant's Exhibit C-9.

9 In its majority opinion, the Tribunal has acknowledged that the Tax Court found that Chapter XIII of the Income Tax Law was not enforceable due to the absence of implementing regulations. However, it finds that conclusion not sound since its Article 106 "*affords the*

25. Due to the constitutional limitation imposed by the legality principle, legal doctrine cannot be held as an autonomous source of tax obligations nor can it step into the shoes of the body in charge of issuing the implementing regulations required under Chapter XIII of the Income Tax Law.[10] As established by Rule VIII, third paragraph, of the Peruvian Tax Code: "In the process of interpretation, no taxes may be created, no sanctions may be established, no exemptions may be granted and no tax provisions may be issued to be applied to entities or situations different from those specified in the law".

26. Based on the foregoing, the Tax Court decision of April 23, 2004, which confirmed that the continuity rule was part of the tax regime at the time that Electroperú transferred assets to Egenor, and on the date of the Egenor LSA (on the basis that it was recognized by legal doctrine –, a source of tax law according to Rule III of the Peruvian Tax Code) violates the constitutional principle of legality stabilized under the DEI Bermuda LSA and does not meet the threshold established by the reasonability test applied by the Trbunal in the Award.

27. Having decided that the continuity rule was neither in force at the relevant time nor stabilized under the Egenor and the DEI Bermuda LSA, it is unnecessary to decide whether the constitution of Egenor qualified as a corporate division for tax purposes.[11]

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executive branch the opportunity to define limitations applicable to the concept of merger and division through regulations, but does not require such regulations for the general concepts to apply." For the majority opinion, a more explicit language would have been required in order to make the enforcement of the rule contingent on the promulgation of regulations (Award, at para. 304). I respectfully disagree with such conclusion. First, article 106 provides: "*The reorganization of companies or corporations occurs only in cases of merger and division, with limitations, and in accordance with the stipulations stated in the regulations*". While it is true that the implementing regulations could have established limitations, the use of "and" following "limitations" indicates that those regulations were not restricted to such purpose. Second, even assuming that the implementing regulations could have just provided for limitations to the general concept, it seems unreasonable to deem a tax rule enforceable without having its precise limits established. Third, following the reasoning explained in para. 24 above, when a certain rule subjects its application "*in accordance with the stipulations stated in its regulations,*" its actual application should be considered contingent on those regulations without need of an express qualification exclusively conditioning its enforcement to their issuance.

10 As a tax law source, legal doctrine may serve as a source of interpretation, but never to enforce a regime that shall be established by law or to define a concept that shall be defined by the implementing regulations. I share the view expressed in the Award that it would be reasonable that depreciation over the useful life of assets should not be changed by the mere fact that ownership thereof has been transferred (Award, para. 302). However, in my view, the issue is not whether the continuity rule is reasonable, but whether such rule existed and was enforceable at the relevant time. If such rule was not established and enforceable when the transfer of assets from Electroperú to Egenor took place it could never have been applied by SUNAT, irrespective of how reasonable or logical such a rule would have been if legally enacted.

11 Notwithstanding so, it should be noted that, pursuant to Article 106 of the Income Tax Law, the Executive was the one empowered to establish the meaning of "division" through the implementing regulations and not the Tax Court. In its April 23, 2004 decision, the Tax Court first held that Chapter XIII of the Income Tax Law was not in force (*see* p. 5 of the Tax Court decision, Spanish original). However, it then filled that gap by applying its own criteria. Through this reasoning, the Tax Court actually enforced the very same Chapter XIII that it had held before was not in force.

28. Due to the majority's finding on liability concerning the Depreciation Rate Assessment claim, it is also unnecessary to enter into further damages considerations in connection with such claim.

Date: July 25, 2008

Dr. Guido Santiago Tawil
Arbitrator