IUSCT (IRAN-US CLAIMS TRIBUNAL)

IUSCT Case No. 439

INTERNATIONAL SYSTEMS & CONTROLS CORPORATION V. THE ISLAMIC REPUBLIC OF IRAN

AWARD (AWARD NO. 256-439-2)

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26 September 1986

Tribunal:
Robert Briner (President)
Charles N. Brower (Appointed by the claimant)
Hamid Bahrami-Ahmadi (Appointed by the respondent)

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Award (Award No. 256-439-2)

I. THE PROCEEDINGS

1. On 18 January 1982, the Claimant, INTERNATIONAL SYSTEMS & CONTROLS CORPORATION ("ISC"), filed a Statement of Claim claiming between U.S.$102 million and U.S.$125 million approximately, plus interest and costs, against the INDUSTRIAL DEVELOPMENT AND RENOVATION ORGANIZATION ("IDRO"), IRAN WOOD AND PAPER INDUSTRIES ("IWPI"), MAZANDARAN WOOD AND PAPER INDUSTRIES ("MWPI") and THE ISLAMIC REPUBLIC OF IRAN ("IRI") (collectively referred to as "the Respondents"). ISC subsequently revised its claim to approximately U.S.$116 million.

2. The Respondents filed their Statement of Defense and Counterclaims on 13 August 1982. The aggregate amount of counterclaims filed totalled U.S.$1.4 billion.

3. A Hearing was held on 20, 21 and 22 January 1986.

II. FACTS AND CONTENTIONS

4. The claims and counterclaims in this Case arise out of four contracts entered into between Stadler Hurter Limited ("SHL"), incorporated in Canada, its subsidiary Stadler Hurter Worldwide ("SHW"), incorporated in Bermuda, and IDRO during 1973 and 1974. These contracts relate to two projects for the design and construction of industrial plants and provision of related equipment for the utilization of forest products in the Gilan and Mazandaran provinces of Iran and related forestation projects.

5. IDRO assigned the management and operation responsibilities for the Gilan Project to IWPI and for the Mazandaran Project to MWPI.

6. The Gilan Project was conceived and designed to be a totally integrated pulp and paper project which would be operated by Iranian personnel and meet specific government objectives, namely, preserve the forests of northern Iran, provide a major source of employment, be a perpetually renewable source of wealth, and reduce Iran's need for foreign exchange. It was to consist of a sawmill, a plywood mill, and a 500 ton per day kraft pulp and paper mill which was to produce liner board, corrugated medium and wrapping paper. It was also to include logging and forestry operations, the latter comprised of nurseries, reforestation plantations and logging roads as well as related infrastructure including a small city of about 5,000 people. The plan was to use hornbeam trees to produce pulp and paper.

7. The pulp and paper complex conceived for Mazandaran differed from the Gilan project as different objectives had to be accommodated. As required by the Government the finished product of the Mazandaran plant had to be saleable primarily in the Iranian economy on the basis of existing

market demand; newsprint was to be one of the products, if feasible; the papermaking was not to produce odors since the Mazandaran region was a resort area; and modern forestry techniques were to be employed to preserve and renew forest resources. Hornbeam trees were also going to be used to produce pulp and paper, including newsprint.

8. For each of the projects, two contracts were signed -- a lump-sum price contract (for work to be performed outside Iran, such as design, management and provision of equipment) and a cost-reimbursable contract (for work to be performed within Iran, including the actual construction). The lump-sum contracts were signed by SHL while the costreimbursable contracts were signed by SHW; all contracts were signed by both IDRO and Technolog -- IDRO's engineering, industrial consultant and "project engineer" for both projects ("the Engineer"). SHL guaranteed the performance of all the obligations of SHW.

9. The price fixed for the lump-sum contract for the Gilan Project was Can.$82,493,000. The Parties could increase the price by mutual agreement. The scope of work under the contract could be extended by an "extra work" or "change in work" ("CIW") order to be made in writing in accordance with a procedure set forth in Article 11 of the lump-sum contract. The lump-sum contract was to be financed by the Canadian Export Development Corporation ("EDC"). Under the contract, payment of the final 5% of the lump-sum amount was contingent on SHL's posting a 5% security bond acceptable to the Buyer for the purpose of assuring that SHL meets its guarantees.

10. The contracts all had similar provisions in respect of the issuance by the Engineer of completion certificates, start-up operations, performance trials and acceptance certificates. Completion certificates were to be issued by IDRO when a section of work was completed in accordance with the contract. Following correction of any minor deficiencies noted in the completion certificate, and performance trials, IDRO was to issue an acceptance certificate for that section of work. The effect of the issuance of an acceptance certificate would be to transfer to the Buyer (IDRO) the risk of loss or damage to the works, to oblige the Buyer to reduce the 5% security and to release the Seller (SHL or SHW) from its obligations regarding the engineering and the performance guarantees. The Seller's workmanship guarantees were to continue for one year following issuance of a completion certificate for a section of works.

11. There were also similar provisions in the contracts as to the liability of the Seller. It was not to be liable to IDRO for any consequential damage and as the Gilan lump-sum contract provided:
Seller's total liability under this Contract for any cause or causes shall be limited to the secured sum outstanding as set forth in Article 9.3....

    Article 9.3 stated as follows:

    Before BUYER pays any amount in excess of 95 per cent of the CONTRACT PRICE, SELLER shall submit to BUYER acceptable evidence of security, such as those stated in Article 9.1 above, for the purpose of assuring that SELLER meets its guarantees. Said security shall be reduced in proportion to the ratio that the value of WORKS or SECTIONS OF WORKS of the FOREIGN DELIVERIES for which ACCEPTANCE CERTIFICATES have been issued bear to the CONTRACT PRICE.

    Article 17.4 in turn provided that:

SELLER shall be liable for any errors and/or omissions with respect to the performance of the engineering services required under the CONTRACT. SELLER's liability therefor shall be limited to the rework of that portion of the engineering as is shown to be in error. This limitation shall not be deemed to override or present a defence to the failure to meet any other guarantees or obligations of SELLER in the Contract.

12. There were also similar provisions in the contracts relating to termination for or without cause as well as for reasons of force majeure.

13. Formal discussions were held between SHL and IDRO as of 1974 and continuing into 1978 on price escalation in view of alleged increases in procurement prices caused by world inflation. SHL and IDRO ultimately signed an agreement on 16 July 1978 in which "IDRO agree[d] to pay SHL its claims related to escalation in the Gilan Contract the sum of CN$9,200,000," effective "upon the approval of the Government of Iran and the appropriation of funds to pay the amount...." The Claimant alleges that IDRO assured it that such approval was a mere formality. Nevertheless, the approval was never given and IDRO never made any payment for price escalation.

14. The Gilan cost-reimbursable contract covering work to be performed in Iran contained no ceiling on the total cost of the contract and was to be financed out of Iranian funds. The Gilan cost-reimbursable contract envisaged that most of the work on site including the construction of physical installations was to be sub-contracted, but under the contract the Seller (in that case SHW) retained ultimate responsibility for performance under the contract.

15. By an agreement of 11 September 1974 the construction of the Gilan plant and the housing units for a price of Rls 3.5 billion was subcontracted to an Iranian company, Gilcon, and the construction was to be completed within 28 months (i.e., 15 January 1977). Delays were subsequently encountered, attributable in part to difficulties in obtaining and importing needed materials and equipment, and in part to the alleged incompetence of the Iranian subcontractor. This ultimately led to the replacement of Gilcon by a Canadian company, Dillingham, in August 1976, by which time (23 months after execution date) Rls 3,265 billion (96% of the original estimate) had been paid with only 17.3% of the work then completed. The assignment of the subcontract to Dillingham coincided with a "Change in Work" order, CIW order No. 1042, which reassigned to SHL the project management functions previously performed by SHW. It fixed the completion date at 19.5 months from the date on which the CIW order came into effect, i.e., 15 May 1978, and stipulated the sum of Can.$12,682,000 as the price for the performance of these CIW order construction management functions. In the event the construction was being delayed beyond the target date, SHL would be entitled to a per diem fee decreasing every month. An additional fee of Can.$11,413 per "start-up" man-month was also to be paid to SHL for man-months expended after issuance or deemed issuance of completion certificates, to pay for correction of deficiencies, assistance in effecting start-up and making necessary modifications, finalizations of accounts and demobilization. Payments made to Dillingham were to be considered as reimbursable costs.

16. After CIW order No. 1042 and the assignment of the plant construction work to Dillingham work proceeded much more satisfactorily, although the new target completion date was not met. Most completion certificates were issued by 16 August 1978 when the Gilan plant was opened and

publicly dedicated. The Claimant alleges that by the end of 1978 completion certificates had been issued for all but two sections of the work, namely the administration building and site services.

17. The Respondents allege, however, that completion certificates were not issued for two additional areas of the Project, namely the forestry division and the townsite. The forestry division work was subcontracted to a Canadian company, Charnell, but certain difficulties encountered with its implementation delayed its completion beyond the original projection and the townsite had not been completed by the Fall of 1978.

18. In addition, the Respondents allege that Dillingham left nearly 1500 deficiencies uncorrected for areas for which completion certificates had been issued.

19. For the Mazandaran Project, the lump-sum contract, covering work performed outside Iran, was fixed at U.S.$142 million while the cost-reimbursable contract was estimated to reach approximately U.S.$200 million. The cost-reimbursable contract is not in dispute here since the materialization of the Mazandaran project did not reach the stage where that contract was in question. Both contracts were signed on 21 December 1974. Unlike the Gilan lump-sum contract, the Mazandaran lump-sum contract contained an escalation clause with a specific formula by which escalation was to be calculated. The contract was initially intended to be financed through Iranian funds, but it was subsequently financed by the Canadian EDC and the German Ausfuhrkredit.

20. The target completion date for the Mazandaran project was 1981, but difficulties were encountered in respect of the pulp and paper mill process and design, and the choice of a subcontractor. Dillingham and an Iranian company, Mana, ultimately were selected jointly as subcontractors for the construction work.

21. In making its proposal which formed the basis of the Mazandaran contract, SHL relied on tests carried out by the Herty Foundation which, according to the Claimant, indicated that both pulp and newsprint could be satisfactorily produced within the constraints prescribed by the Government. Various studies and tests conducted after the contracts had been awarded, however, questioned the feasibility of SHL's proposed processes for making newsprint at Mazandaran, including the use of magnesium sulphite. The studies also indicated the projected high cost that might be incurred in completing the project as designed, and suggested further a need for commercial testing.

22. In 1978 CIW order No. 2000 was signed, which fixed the amount of U.S.$1,097,323 as compensation for costs associated with the delay experienced in converting the Mazandaran project from a cash basis to an export financed basis and to cover costs for certain revisions in the project.

23. Due to conditions then prevailing in Iran in late 1978, SHL and SHW gave notice of force majeure under the Gilan contracts. By a telex of 13 February 1979 SHW notified IWPI of the evacuation of its personnel and indicated its willingness to return to Iran to complete construction work once the situation improved. Most SHL employees left by 5 January 1979; the last SHL employee left Iran on 1 March 1979.

24. Following SHL's departure from Iran, two meetings were held between SHL and IDRO in Tehran in April 1979 and mid-June 1979 with a view to SHL's resumption of work on the projects. No such resumption took place.

25. At the time SHL left Iran, SHL submits that 95% of the work on the Gilan Project had been completed while the Mazandaran Project was 45% completed. SHL contend that it had by then billed under the lump-sum contract including change in work orders and escalation claims Can.$112,050,453 with the total actually paid being Can.$92,659,428. For the Mazandaran lump-sum contract U.S.$61,326,438 had been billed, of which U.S.$52,070,923 was paid.

26. Thus, by the time performance on the various contracts was stopped, the Respondents had disbursed on the lump-sum contracts the equivalent of U.S.$130,831,437. The Claimant asserts that a remaining amount of U.S.$25,737,900 is still owing for work performed under the projects.

27. As a result of financial difficulties, on 31 October 1979 SHL sold its corporate assets including its trade name to a German company, Kloeckner. SHL then became known as Kedzep Limited, and it immediately filed a Proposal in Bankruptcy in the Montreal Superior Court. ISC is also apparently experiencing serious financial difficulties.

28. A major defense to the claim presented in this Case relates to the Respondents' allegation that the Claimant obtained the contracts here at issue by means of bribery and improper payments.

29. The evidence indicates that in August 1972 an agency agreement was signed between SHL and four other persons including an Iranian individual, Shamsedin A. Golestaneh, a former employee of the Iranian Foreign Affairs Ministry and the Prime Minister's office, who then was managing director of an Iranian promotional company, Shatab & Co. Following an investigation conducted by the U.S. Securities and Exchange Commission ("SEC") in 1976, the 1972 agreement was replaced by a new agreement dated 2 May 1977. The 1977 agreement provided that the above four persons were to be paid stipulated compensation in connection with the Gilan and Mazandaran projects for their services, which were identified as: (a) government relations; (b) proposal preparation; (c) assistance during negotiations; and (d) relations with local financial community and extensive support from locations in Geneva, Paris, London and Tehran.

30. Article 6 of the 1977 agency agreement provided that no payment had been nor would be made to Iranian officials. The parties to that agreement also undertook to redraft any provision of the agreement which would be unenforceable according to legal opinion of Quebec counsel which SHL was to seek. An amendment to that agreement was signed on 28 March 1978. The Claimant accordingly alleges that there was no impropriety in the agency payments.

31. The Respondents allege that the commission paid to Mr. Golestaneh was shared with Prince Abdorezza, the brother of the Shah, and Chairman of the Council for the Environment, Mr. Mossadeghi, at one time Director of Planning and Projects of the Ministry of Natural Resources, and Sid Askari, until 1975 the Managing Director of Technolog (the engineer for both projects).

32. As shown in evidence submitted by the Respondents, the SEC determined, based on its investigation, that ISC and SHL had committed themselves to making payments in the sum of Can.$22.3 million to Iranian officials and agents (Can.$14.1 million on the Mazandaran project), of which by June 1977 Can.$11.3 million had been paid.

33. It was also stated in the SEC's investigation that the Gilan contract was obtained by virtue of an artificial reduction of Can.$3 million on the SHL bid, and that this sum was to be recouped through

an escalation agreement.

34. The Respondents have alleged that because of sensitive payments made by SHL, the conclusion of the contracts themselves and the Gilan escalation agreement were obtained by undue influence. The Respondents allege that as a result the contracts should be considered void. They also contend that the contracts would be void for violation of Iranian penal law as well as of public morals and public order. Finally, they argue that the Claimant has no action based on contracts thus improperly obtained by application of the maxim ex turpi causa oritur actio.

35. The Claimant argues that the agency agreement was brought to the notice of the Iranian Prime Minister and a member of Cabinet who informed SHL that the arrangement was not objectionable in the Government's view. In particular, the Claimant asserted that the Ministry of Justice informed ISC by letter dated 15 July 1978 that Prince Abdorezza
had not in the past seven years been an employee of any person acting in an official capacity for or on behalf of the Imperial Government of Iran or any of its departments, agencies or instrumentalities.

36. Affidavits were also submitted by the president of a subsidiary involved and Mr. Golestaneh that no improper payments to Iranian officials had been made out of the funds they had received as commission.

37. As a result of its investigation the SEC filed a civil lawsuit against ISC reflecting, inter alia, the findings set out in paragraph 32 above. The SEC lawsuit ended in the acceptance of a consent decree by ISC's directors; the case consequently never went to trial.

38. The Claimant has denied that there was any impropriety in the agency arrangements and has alleged that the payments made pursuant to the arrangement were quite normal under the business practice in Iran. The Claimant alleges further that the Iranian and Canadian government officials were well aware of the arrangement, and that the payments were in fact ratified by the Iranian government. The Claimant argues that there is no evidence properly before the Tribunal substantiating the Respondents' allegations and has requested the Tribunal to reject as untimely certain documentary evidence relating to that issue submitted by the Respondents on 10 December 1985.

39. Based on the SEC's findings and papers filed in Canadian courts, the Respondents have also alleged that SHL entered into kickback arrangements with North American suppliers of materials for both the Gilan and Mazandaran projects, which led to criminal prosecutions before Canadian courts against the companies concerned. The total of the alleged kickbacks amount to Can.$4,476,494. The Claimant suggests that all the prosecutions were dismissed or withdrawn.

A. The Claims

40. ISC asserts directly or indirectly on behalf of its wholly owned subsidiary SHL a total of five claims for an approximate amount of U.S.$116 million on the ground that the Respondents breached the

Gilan and Mazandaran contracts by failing, despite persistent demands, to pay progress billings as they became due, by refusing, despite SHL's readiness, to authorize resumption of work following the cessation of force majeure conditions in April 1979 and by failing in the light of the circumstances to terminate the contracts in accordance with their termination clauses.

41. Its first claim totalling U.S.$25,737,900 is for amounts owed for work performed under the contracts. For the Gilan Project, ISC claims the sum of U.S.$16,482,345 for approved, unapproved and uninvoiced amounts for work performed under the original Gilan contract (i.e., the lump-sum contract), for work performed under CIW order No. 1042, for work performed under extra work orders and for amounts owed under the Gilan escalation agreement. It claims the sum of U.S.$9,255,555 as amounts due SHL as net receivables for the Mazandaran contract covering approved invoices and uninvoiced amounts, work performed under CIW orders and escalation amounts owing. This claim also relates to the lump-sum contract. ISC contends that the Respondents are liable to pay these amounts under the alternative theories of breach of contract, unjust enrichment or quantum meruit.

42. ISC's second claim is for force majeure costs in the amount of U.S.$4,621,486. According to ISC, SHL incurred costs of evacuation, demobilization of its in-country operations, losses associated with evacuation and maintenance of an office and standby staff. These costs are considered due to SHL as reimbursable costs under the contracts.

43. ISC's third claim is for incidental damages as a result of breach of contract in the amount of U.S.$3,740,656. This claim covers a variety of costs incurred as a result of the disruption of the contracts and the Respondents' failure to authorize a resumption of work. These costs are said to include the storage of equipment scheduled to be delivered to the Mazandaran site, winding down of the company's Montreal operations, and cancellation costs imposed by various suppliers. Many of these costs are said to have occurred after force majeure ended in April 1979.

44. ISC's fourth claim is for lost profits in the sum of U.S.$29,053,445 in respect of the Mazandaran Project and is considered to arise by virtue of the material breach of contract by the Respondents.

45. While all the above claims are indirect claims of ISC on behalf of SHL, the fifth claim, for an amount of U.S.$53 million, is submitted as both a direct and an indirect claim. ISC argues that the Respondents' breaches of the contract and other wrongful acts were the single greatest cause which brought ISC to the brink of bankruptcy and that they were the sole and direct cause of the destruction of SHL, which is now no longer a going concern, its management and technical teams now dispersed, its goodwill destroyed and its name sold.

46. In support of its direct claim, ISC maintains that the Respondents committed an intentional tort by refusing to take action to cure their contractual breaches, authorize a resumption of work or terminate the contract, the foreseeable consequence of the tort being the destruction of SHL. ISC states that the Respondents were put on notice for more than six months that a failure to take action would force SHL into bankruptcy.

47. Alternatively, ISC argues that the destruction of SHL constitutes a "constructive expropriation." It is argued that the Iranian Government deliberately interfered with the projects by requiring SHL to justify continuation of the projects in April 1979 and then by refusing to permit the projects to

continue under the agreed arrangements. ISC contends that SHL was thereby deprived of its substantial property interests in completing the contracts and ISC was deprived of the economic value of its destroyed subsidiary.

B. The Counterclaims

48. The Respondents have asserted nine counterclaims totalling U.S.$1,301,765,966 relating to both the Gilan and Mazandaran projects. In addition, the Respondents have filed four other counterclaims by Iranian entities who were subcontractors on the Gilan project.

49. The counterclaims in respect of the Gilan project are for compensation in respect of cost overruns; costs not approved in an audit report of Ansari and Co.; costs relating to equipment purchases; indemnities payable by insurance companies; forestry damage costs incurred in correcting deficiencies in design and execution of works; expenses incurred under field work orders; expenses in respect of training of personnel; shipping costs; funds of IWPI attached in Montreal; damages caused by work stoppage; inflation costs and lost profits. Most of these counterclaims are based on the cost-reimbursable contract, and total about U.S.$518 million for the Gilan project.

50. In respect of the Mazandaran project, the Respondents counterclaim for the return of all monies paid, for which no consideration was allegedly given. The amount originally claimed totals U.S.$634 million.

51. The Respondents also claim for social security premiums allegedly unpaid.

52. The four Iranian subcontractors who filed Counterclaims are: (a) Sazeman Toseeh Rahhaye Iran, which is claiming Rls 750 million for the breach of an agreement for the lease of road construction machinery; (b) Yassa Construction Company, claiming Rls 148 million for the breach of a contract for site preparations of the Gilan paper plant; (c) Bamanshir Consortium 400, claiming Rls 92 million for the breach of a contract for phase 3 of the site grading; and (d) Gilcon, claiming U.S.$12.8 million for the breach of the 1974 construction contract and its September 1976 amendment. All four counterclaims relate to contracts entered into with SHW. These four counterclaims total approximately U.S.$17 million.

V. REASONS FOR THE AWARD

A. Indirect Claims

53. The Claimant, ISC, to prove its right to bring this claim under the Claims Settlement Declaration, has submitted a certificate of the Secretary of State of the State of Delaware that ISC is incorporated under the laws of the State of Delaware, U.S.A. An affidavit of the corporate secretary attests to the fact that from 1978 until May 1982 more than 99% of all outstanding common shares of ISC were held by shareholders of record with addresses in the U.S., while 96% of all outstanding preferred

shares were held by shareholders of record who had addresses in the U.S. The corporate secretary also attests to the ownership of five individuals, all U.S. citizens, who have directly or indirectly owned 43% of the outstanding common stock of ISC and a total of 23 U.S. individuals and corporations who have owned of record 81% of the outstanding common stock of ISC. The Tribunal is satisfied that ISC is a United States national in accordance with Article VII(1) of the Claims Settlement Declaration.

54. The corporate secretary also attests to the purchase by ISC of 100% of the common stock of SHL, a Canadian corporation, in 1972. The affidavit states that in 1979 SHL sold its name and assumed the name of Kedzep Limited and that at all times until the present it has been owned 100% by ISC. (The Tribunal will continue to refer to the company as SHL for clarity of discussion.) The Tribunal is satisfied that SHL, which was not itself entitled to bring a claim, was owned by ISC in terms of Article VII(2) of the Claims Settlement Declaration.

55. The corporate secretary states that in November 1979 SHL submitted a Proposal in Bankruptcy ("Proposal") to its creditors under Canadian law, but that
[SHL] continues to exist as a corporate entity. It has not been liquidated and following bankruptcy proceedings [SHL] will receive all residual assets and may resume operations.

56. The Proposal, dated 31 October 1979, appointed as Trustee Mr. Paul Bertrand, and was amended on 9 January 1980. The amended Proposal was approved by the Superior Court of Montreal. Paragraph 8 of the amended Proposal states:
[T]he Trustee shall be vested with all the powers of a trustee under Section 14 of the Bankruptcy Act, and in particular shall have the right to incur obligations, borrow money and give security on any of the free property of the Company by mortgage, hypothec, charge, assignment, pledge or otherwise, such obligations and money borrowed to be discharged and repaid with interest out of the property of the Company in priority to the claim of the creditors.

Paragraph 9 provides as follows:

That to secure and guarantee the execution of the foregoing Proposal, the Company does hereby pledge, cede, transfer, assign and convey to the Trustee in trust for and on behalf of the creditors all its property wherever situated and all such property that may be acquired by it or devolve upon it during the term of this Proposal together with such powers in or over or in respect of property as might have been exercised by it for its own benefit, the whole in the manner and to the extent as if the undersigned was a bankrupt and the Trustee herein were vested with its assets as same is defined under Section 47 of the Bankruptcy Act.

57. Mr. Bertrand, in his capacity as Trustee under the Proposal, instituted proceedings in Canadian courts to recover the amounts claimed by SHL in connection with the two Iranian projects. Mr. Bertrand has also acted to freeze assets belonging to the Respondents in Canada pending judgement before Canadian courts. Mr. Bertrand initially opposed the action brought by ISC before this Tribunal without his consent and had contested an action brought by SHL before the Superior Court of Montreal, for the purpose of prosecuting this claim brought before the Tribunal, seeking examination and copying of documents held by Mr. Bertrand. SHL obtained the right of access to the papers in a judgement of Mr. Justice Alphonse Barbeau of 26 August 1983 rendered In the Matter

of the Proposal of Kedzep Limited v. Paul Bertrand, Trustee, SCM 05-010440-830. Subsequently, the Trustee Mr. Bertrand signed a co-operation agreement with ISC. While the details of the agreement have not been submitted to the Tribunal, the Claimant has submitted a letter dated 31 January 1984 from Mr. Bertrand indicating his readiness to co-operate with ISC to prepare its claim before the Tribunal, but without prejudice to his own rights to continue the proceedings instituted in the Montreal Superior Court. Mr. Bertrand in this letter undertakes to desist from the Canadian proceedings only upon receipt of the sums, the fees and the disbursements related to the SHL Proposal. He also undertakes
upon receipt of a sum not less than the sum under seizure at the time of receipt, to give mainlevee of the seizure in Case 500-05-017071-794. Any lesser sum received will be applied on account of the claims made in case number 500-05-017071-794 and the proceedings continued.

58. The Claimant submitted in evidence a copy of a renunciation to the judgement rendered by Mr. Justice Barbeau signed by SHL and Mr. Bertrand to the effect that the aforesaid judgement shall have no effect of whatsoever nature and shall be considered for all legal purposes never to have been rendered. The Claimant also stated at the Hearing that Mr. Bertrand had suspended prosecution of the Canadian proceedings against the Respondents pending the Tribunal's resolution of the claim.

59. The Claimant contends that its claims are those of a U.S. nationa, and that both the direct and indirect claims were owned continuously from the date on which the claims arose in 1978 and 1979 to the date the Claims Settlement Declaration entered into force.

60. As to the Claimant's indirect claims brought on behalf of its subsidiary, SHL, the Respondents contend that the Claimant ceased to "control" SHL when SHL's Proposal in Bankruptcy was filed and ratified in Canada and therefore that ISC cannot present a claim on behalf of SHL pursuant to Article VII(2) of the Claims Settlement Declaration. The Respondents argue that Article VII(2) lays down three conditions to be satisfied in this Case as follows:
i) that the claims should have been owned continuously by U.S. nationals, from the date the claim arose to 19 January 1981;

ii) that when ownership is "indirect", that is to say by virtue of ownership of capital stock, the ownership interest must be sufficient to ensure control of the corporation or entity in which the stock is held; and

iii) that such corporation or entity must not itself be entitled to bring a claim under the Claims Settlement Declaration.

61. According to the Respondents, a fundamental requirement of Article VII(2) is that the beneficial interest in the claim must be owned by a claimant. They argue that the effect of the Proposal under Canadian bankruptcy law was to divest ISC of any further beneficial interest and to vest such beneficial interest in the Trustee for the ultimate benefit of the creditors.

62. The Claimant, on the other hand, argues that the proposal did not deprive SHL or ISC of beneficial ownership of the claim. ISC initially argues that the Tribunal's jurisdiction should be determined by reference to the Claims Settlement Declaration and international law and not by the municipal law

of Canada. In this regard, the Claimant submitted an affidavit by Prof.Burns H. Weston which posits the view that the requirement in Article VII(2) that claims be "owned continuously... by nationals" of the U.S. is a standard formulation of the so-called continuous nationality rule which is included in many claims settlement agreements and is designed to limit the benefits of the claims settlement mechanism to nationals of the countries that are parties to the agreement. Prof. Weston's view is that the concern of Article VII(2) is with nationality and not ownership. It is also argued that in international law and practice the separate nationality or ownership of a trustee is not controlling where the company has a continuing ownership interest in the claim held by the trustee in a fiduciary capacity. As long as the company has some continuing or future interest in a claim, that claim is properly within the jurisdiction of the Tribunal and it does not matter what the precise nature of the interest may be or how it is labelled. SHL, it is concluded, clearly has a "continuing, residual or beneficial ownership in its claims against Iran."

63. Even if Canadian law is applied, however, the Claimant argues that the effect of a proposal is not to vest the Trustee personally with all the rights of ownership of the Company's assets to the complete exclusion of SHL. The Claimant asserts that SHL did not itself relinquish ownership of its claims by filing the Proposal in Bankruptcy, since such an action is not considered to be a liquidation but a reorganization. Since both the Claimant and the Respondents have acknowledged that under Canadian law after the creditors of SHL are paid off all remaining assets, if any, are to be returned to SHL, the Claimant argues that therefore SHL retains a continuing ownership interest in such assets. The argument is that since ISC is the sole shareholder of SHL and the residual beneficiary of any collections by the Trustee, the Trustee in effect holds the assets in trust for SHL and ISC as well as for SHL's creditors. In any case the Claimant argues that no liquidation of the assets has yet taken place, and that any ultimate use of the assets to satisfy SHL's debts will be for SHL's benefit inasmuch as SHL will have been relieved of debt in exchange for its property. Thus the Claimant concludes that SHL retains continuous beneficial ownership in the claim, subject only to the rights of the Trustee.

64. In support of its argument the Claimant has submitted an expert opinion it commissioned from Dr. C.H. Morawetz, in which it is argued that the terms of the amended SHL Proposal vested property in the Trustee under the Proposal only for the purpose of securing creditors' rights under the Proposal and that any residual interest in SHL's property inures to the benefit of the company and the shareholders after the creditors have been satisfied. Dr. Morawetz has also expressed the view that a proposal under Section 32 of the Canadian Bankruptcy Act is a contract between a debtor and its creditors, which contract can be amended at any time by agreement between the proponent and the creditors. A proposal, it is argued, can take a variety of forms and grant varying degrees of authority to the trustee appointed pursuant to the proposal. Under a proposal, the debtor company, it is said, continues to exist as a corporate entity, and unless the terms of the proposal stipulate otherwise, the assets of the debtor remain vested in it and, subject to the provisions of the Proposal, can be freely disposed of by the debtor. Dr. Morawetz has further argued that nothing in the Bankruptcy Act or in Canadian case law indicates that a proposal can transfer absolute ownership in the debtor company's assets to the trustee. He, in fact, likens a trustee under a proposal to a trustee under a will or trust instrument inter vivos. A trustee under a proposal is said to hold and manage the property for the benefit of both the creditors and the debtor company.

65. As to the SHL Proposal itself, Dr. Morawetz expressed the view that while Paragraph 9 of that Proposal appears to grant broad rights and responsibilities to the Trustee, it does not transfer actual

full ownership of those assets to him because there is no absolute vesting of property or assets in the Trustee. The argument continues that once the main purpose of the Proposal -- satisfaction of the claims of creditors -- is met, the Trustee's powers over the handling of the company's assets are at an end, and the remainder reverts to SHL itself. Dr. Morawetz concluded that SHL retains a beneficial ownership interest in its assets, including the Iranian claims.

66. ISC argues further that whatever steps SHL may have taken during its bankruptcy proceedings, ISC in no way relinquished its ownership of its own claim; that it never sold, exchanged, compromised or otherwise transferred any of its claims against Iran, or transferred or ceded any rights to SHL's Trustee; and that ISC did not itself enter into bankruptcy proceedings; and that whatever the effect of bankruptcy proceedings in Canada, they do not affect ISC's claims, which exist independently.

67. The Claimant has argued, finally, that the insolvency of SHL was brought about by the wrongful acts of the Respondents in breaching the contracts. Therefore, it asserts, the Respondents' arguments based on the bankruptcy proceedings are an attempt by the Respondents to use their own wrongful act to deprive the Tribunal of jurisdiction and should not be allowed.

68. For the Respondents, Professor A. Bohemier agrees that under a proposal a debtor usually retains administration and ownership of his assets unless the proposal otherwise provides, and that the debtor and his creditors are entirely at liberty, subject to court approval, to settle the terms of their proposal. In this case, however, Prof. Bohemier states that a "basket proposal" was filed -- a proposal pursuant to which the debtor cedes all his assets to a trustee just as if he were a bankrupt. Since the Superior Court of Montreal approved the amended Proposal, it is to be concluded, he says, that the Trustee, under the clear and unambiguous terms of the amended Proposal, acquired the claims which SHL had against the Iranian corporations. Paragraph 9 of the amended Proposal is said to have expressly provided that the Trustee is vested with all assets of SHL in the same manner as if in a bankruptcy. Since bankruptcy is considered to confer on a trustee all ownership rights to the assets of the bankrupt debtor, such rights were thus considered to have been transferred by the amended Proposal to the Trustee as if SHL were bankrupt. Full and complete effect must be given to the Proposal, which is considered to be a contract between the debtor and a majority of the creditors.

69. Prof. Bohemier agrees with Dr. Morawetz that a proposal like a bankruptcy does not put an end to the corporate existence of the debtor, and that like in a bankruptcy any surplus remaining after creditors have been paid would accrue to the debtor company.

70. The Respondents referred to a decision of the British Columbia Court of Appeal in Henfrey Samson Belair Ltd. v. Wedgewood Village Estates Ltd., 51 B.C.L.R. 389, 51 C.B.R. (N.S.) 285 (1984), reversing Re Skalbania, 48 B.C.L.R. 52, 49 C.B.R. (N.S.) 289 (1983), a decision rendered by the British Columbia Supreme Court in the same case. Chief Justice Nemetz held in that case that the Canadian Bankruptcy Act contains no provision inconsistent with the notion of a proposal vesting property of the debtor in the trustee where the parties so agree, thereby granting the trustee under a proposal the same powers as a trustee in bankruptcy.

71. The Respondents argue accordingly that the rights, powers and authority of the Trustee under the terms of the SHL Proposal are such that he is vested with full ownership rights in and to SHL's assets and has full power and authority over the conduct of its business and affairs, subject only to the

direction of the creditors expressed through their designated inspector and the supervisory authority of the Superior Court of Montreal sitting in bankruptcy.

72. The Claimant, which had initially relied on the Supreme Court decision reversed by the Court of Appeal, distinguishes SHL's proposal from the proposal which was the subject of the Henfry Samson decision. Further, the Claimant, relying on the expert opinion of Dr. Morawetz, states that the decision in Henfry Samson casts no doubt on the fact that once the creditors of SHL have been satisfied any residuary interest in SHL property would inure to the benefit of SHL and its shareholders, and that any conclusion to the contrary would defeat the very purpose of lodging a proposal. The Claimant's view is that to consider the Trustee as being personally vested with all rights of ownership to the company's assets would be inconsistent with the Bankruptcy Act of Canada and the terms of the SHL Proposal.

73. The Respondents also made reference to the judgement of the Superior Court of Montreal rendered by Mr. Justice Alphonse Barbeau of 26 August 1983. The Trustee, Mr Bertrand, is there referred to as having with respect to SHL's assets "all the powers of a trustee to the assets of a bankrupt." The Judge stated that the terms of the Proposal in that case resulted in the transfer to the Trustee of all assets of SHL and granted "to the trustee exclusive ownership of the assets of [SHL], including the right of action against the Iranian corporations." The Claimant argues that the statements were dicta, that the issue of vesting of assets was not at issue in the controversy (over SHL's right to copy documents) that led to the judgment and was not briefed or argued, and that SHL prevailed in the lawsuit, gaining access to the documents held by the Trustee. In any case, the Claimant notes that the judgment has been renounced by SHL and the Trustee and submits that it should not be considered of further force or effect.

74. The question for the Tribunal is whether ISC owned the indirect claims brought before this Tribunal in accordance with Article VII(2) of the Claims Settlement Declaration. Article VII(2) provides:
"Claims of nationals" of Iran or the United States, as the case may be, means claims owned continuously, from the date on which the claims arose to the date on which this Agreement enters into force, by nationals of that State, including claims that are owned indirectly by such nationals through ownership of capital stock or other proprietary interests in juridical persons, provided that the ownership interests of such nationals, collectively, were sufficient at the time the claim arose to control the corporation or other entity, and provided, further, that the corporation or other entity is not itself entitled to bring a claim under the terms of this Agreement.

75. The Claimant here is bringing the claims it owns indirectly on the basis of its ownership and control throughout the relevant period of the capital stock of SHL. The question is whether the insolvency proceedings created a break in the continuity of that ownership. The Claimant contends that the Proposal has not, while the Respondents contend that it has.

76. While it is undisputed that ISC owned SHL from 1972 through 19 January 1981, the argument of the Respondents is that ISC did not own the claims of SHL after filing of the Proposal since they were then owned by the Trustee.

77. The Tribunal does not wish to pronounce on or interpret the domestic laws of Quebec and Canada and in particular on the effect of the Canadian Bankruptcy Act on a proposal. Therefore it will not

venture an excursion into Canadian law on the question. It is, however, compelled to note that both Parties do agree that a proposal
is basically a contract between the debtor and his creditors which gives the debtor as much or as little freedom over his actions as is agreed upon in such contract.

Re Skalbania, 48 B.C.L.R. 52, 49 C.B.R. (N.S.) 289, 297 (1983), reversed on other grounds, 51 B.C.L.R. 389, 51 C.B.R. (N.S.) 285 (1984) (citing Bruce v. Neiff Joseph Land Surveyers Ltd., 23 C.B.R. (N.S.) 258, 269-71 (1977)).

78. Looking therefore to the Proposal as a contract, this Tribunal must determine what the parties (debtor and creditors) agreed to. In so doing, the Tribunal must consider whether the debtor did in fact divest itself under the contract of the ownership of the claims brought before this Tribunal, thereby putting an end to its ownership even if such an ownership could revert in the future.

79. Under the terms of the amended Proposal, it is provided that SHL
does hereby pledge, cede, transfer, assign and convey to the Trustee in trust for and on behalf of the creditors, all its property wherever situated...

Paragraph 9.

80. This wording is unambiguous in that SHL thereby conveyed "all its property" to the Trustee, who then held the same "in trust for and on behalf of the creditors." The Trustee was given the legal ownership of all the company's property wherever situated, the beneficial owners of the said property expressly being the creditors of the company. At that time, therefore, SHL no longer retained any legal or beneficial interest in its claims since all those claims were assigned as part of the property of SHL. The fact that at some time in the future SHL would be entitled to the remaining assets, if any, is irrelevant. By contract, through the Proposal, SHL transferred the ownership of its claims to the Trustee.

81. The Tribunal also notes that any amount awarded in this Case would not accrue to the Claimant to do with it as it likes, but would be transferred to the Trustee to pay off the creditors under the Proposal. Only if there is a surplus after all creditors had been paid, would any residue accrue to the company. A potential future interest is not an existing interest and does not satisfy the requirement of continuous ownership under the Claims Settlement Declaration. It has never been argued, and no evidence has been produced, that Mr. Bertrand, who subsequently owned the claims of SHL, and the creditors on whose behalf he held those claims -- the beneficial owners -- are U.S. nationals.

82. The Tribunal therefore holds that the Claimant, ISC, has failed to prove that it had ownership interests in SHL, which itself could not bring the claims, from the date the claim arose to 19 January 1981 to satisfy the requirements of Article VII(2) of the Claims Settlement Declaration. Although ISC has proved that it was a U.S. national during the relevant period, it has not proved that it continued to own the claims until the end of that period.

83. In reaching this conclusion, the Tribunal has considered various decisions and finds it necessary to distinguish them. In the case of Phelps Dodge Corp. et al. and The Islamic Republic of Iran, Award

No. 217-99-2 (19 March 1986) the claimant, Phelps Dodge, had transferred to OPIC, also named as a claimant, ninety per cent of the beneficial interest of its shareholding in SICAB, but had expressly retained the legal ownership of one hundred per cent of the claim as well as both the legal and beneficial interest in ten per cent of the shareholding interest. Phelps Dodge had therefore not transferred its entire claim to OPIC. Further, that transfer was made on 17 June 1981, which date is after the date the Claims Settlement Declaration entered into force and therefore outside the relevant period for purposes of the Tribunal's jurisdiction. The Tribunal's conclusion in that case was that during the relevant period the claims presented were claims of nationals of the United States and that because Phelps Dodge had retained the beneficial ownership of ten per cent of its investment with respect to which it bore the risk of loss under the insurance contract with OPIC it would have been entitled to receive any excess of the total amount of the insurance payment it had already received from OPIC from an award by the Tribunal. None of these conditions are satisfied in the present Case and thus the Tribunal's decision in Phelps Dodge must be distinguished.

84. The Tribunal also must distinguish the Case of Foremost Tehran Inc. et al. and The Government of the Islamic Republic of Iran et al., Award No. 220-37-1 (11 April 1986). Again in that case, the Tribunal held that OPIC was not a necessary party and struck its name from the case, since in its view the legal title to the entire claim was vested continuously in Foremost during the relevant period, notwithstanding the intervening settlement made with OPIC. There was therefore no interruption of the continuous ownership of the claim since the legal interest remained vested in Foremost throughout the relevant period, as is typical in an insurance contract. In the present Case, there is no such continuous ownership of either the legal or beneficial title to the claim, since that had been transferred to Mr. Bertrand as Trustee.

85. In the case of International Technical Products Corporation and The Islamic Republic of Iran, Award No. 196-302-3 (28 October 1985), there was also no question of a break in the continuous ownership of the claim. The claimant was at all relevant times the beneficial owner of the expropriated property, the Iranian corporation having held the legal title to the property, while after 14 December 1978 the claimant had also become the legal owner of about 89 per cent of the property in question. In the present proceedings the Trustee, Mr. Bertrand, holds all claims and property of SHL in trust for the creditors and not for the Claimant in this Case, the Claimant having neither legal nor beneficial ownership during the relevant period. The issue here presented is thus not one of a present ability of the Claimant to control the claim, but that of his continuous ownership, legal or beneficial, of the claim.

86. In view of the dismissal of the indirect claims, the Tribunal need not examine the issue of the alleged corrupt practices nor decide the question of the influence such practices, if proven, might have on the validity and enforceability of the contracts.

B. Direct Claim

87. The Claimant also brings a direct claim for the loss of value of SHL on the basis that the destruction of SHL constituted either a "constructive expropriation" or an intentional tort. To support its claim for constructive expropriation the Claimant states that following the Revolution in early 1979 new managers were appointed for IDRO, IWPI and MWPI and that these new managers met with SHL to discuss contractual and technical matters in April 1979 and June 1979. The Claimant argues that

despite the detailed status reports on the projects which were prepared by SHL, the repeated assurances from the three agencies that the projects were of critical importance to the Iranian economy and the desire expressed for SHL's return to Iran, the approval of the new government for resumption of work was not forthcoming; however, neither would it terminate the contract. The Claimant contends that IDRO was controlled by the officials of the new government and that that government took steps to interfere with and ultimately destroy SHL's contractual rights. The Claimant argues that the acts of the government are no less an expropriation simply because it did not take the form of decrees or legislation but that the steps taken by the government resulted in the virtually total deprivation to ISC of its investment in its subsidiary so that under international law the government is obliged to compensate it for its loss.

88. To substantiate its theory of an intentional tort the Claimant states that the Respondents by intentionally breaching the contracts committed an intentional act or omission they knew would destroy SHL. These unjustified acts are said to include stopping payments, asking SHL to return for negotiations, but refusing to resume either payments or work. The Claimant argues that by stopping payments without terminating the contracts the Respondents intentionally took acts they knew would force SHL into insolvency and thereby deprive it of all its ptential business gains.

89. The Respondents have argued that the Claimant's alleged loss of its investment is not the natural, proximate or direct result of the Respondents' alleged acts. A delay in payment, it is argued, could not be the natural cause of the bankruptcy of a company since several factors and events not attributable to the Respondents contributed to SHL's destruction. The Respondents also rely on the argument that the damages claimed by ISC cannot be recovered unless it is proven that the Respondents had reason to foresee the alleged loss as a probable result of a breach of the contract at the time the contract was entered into. The Claimant argues, however, that foreseeability as a tort is not necessary since the acts in question constituted an intentional and not a negligent tort.

90. On the issue of constructive expropriation the Respondents maintain that non-payment of invoices and breach of contract cannot amount to expropriation. It is also argued that an indirect expropriation has not been established as a principle of international law. The Respondents have further argued that the claim based on tort is not covered by the Claims Settlement Declaration, and that the reference in Article II(1) to "other measures affecting property rights" is to be construed ejusdem generis with the word "expropriation." Finally, the Respondents contend that shareholders have no right to initiate an action for the loss of value of a company. ISC, it is said, must show that the wrong alleged was not merely an injury suffered by SHL but that it resulted in the breach of some special duty owed to itself and having its origin in circumstances independent of ISC's status as a shareholder.

91. As previously indicated, the Tribunal is satisfied from the evidence submitted by ISC that it was a U.S. national from the date the claims arose in 1978 to 19 January 1981. The Tribunal is satisfied that the claim is owned by U.S. nationals within the terms of Article VII(2).

92. The direct claim is brought by ISC for injury caused to it and is based on alternative theories of constructive expropriation and intentional tort.

93. Article II(1) of the Claims Settlement Declaration provides that the Tribunal has jurisdiction over claims which

arise out of debts, contracts..., expropriation or other measures affecting property rights.

94. The question is whether a claim based on "intentional tort" falls within the concept of "other measures affecting property rights." The Tribunal in the case of Grimm and Government of Iran, Award No. 25-71-1 (22 February 1983), reprinted in 2 Iran-U.S. C.T.R. 78, stated as follows:
under the well-known principle of ejusdem generis the words "other measures" in Article II, paragraph 1, ought to be, especially in the context of "debts and contracts", construed as generically similar to "expropriations"...

95. The Tribunal concurs in this holding. The claim based on intentional tort is therefore dismissed for lack of jurisdiction.

96. As to the alternative claim for constructive expropriation, the Tribunal recognizes that a taking of property may occur even in the absence of a formal nationalization or expropriation if a government has interfered unreasonably with the use of property.

97. In Phelps Dodge Corp., supra, the Tribunal cited with approval (at paragraph 22) an earlier Award which stated as follows:
A deprivation or taking of property may occur under international law through interference by a State in the use of that property or with the enjoyment of its benefits, even where legal title to the property is not affected. [Citations omitted]

While assumption of control over property by a government does not automatically and immediately justify the conclusion that the property has been taken by the government, thus requiring compensation under international law, such a conclusion is warranted whenever events demonstrate that the owner was deprived of fundamental rights of ownership and it appears that this deprivation is not merely ephemeral. The intent of the government is less important than the effects of the measures on the owner, and the form of the measures of control or interference is less important than the reality of the impact.

Tippets, Abbott, McCarthy, Stratton and Tams-Affa Consulting Engineers of Iran et al., Award No. 141-7-2, pp. 10-11 (29 June 1984), reprinted in 6 Iran-U.S. C.T.R. 219, 225.

98. From the above it is to be noted that the owner must at least be deprived of some fundamental rights of ownership and that the deprivation must be not merely ephemeral. The claim for destruction of a business must go beyond a showing of a classical breach of contract. While the tortious action might well relate to the contract, it did not arise out of the contract. The Respondents' failure to renew a contract or their failure to pay a debt cannot be said to amount to expropriation as in any event the Respondents have rights under the contracts to terminate them for cause or without cause upon making stipulated payments. The damage which the Claimant states it suffers approximates damages resulting from tortious conduct rather than from expropriation. Since a claim based on such conduct is not covered by Article II(1) of the Claims Settlement Declaration the Tribunal decides that it lacks jurisdiction over the direct claim brought by ISC.

C. The Counterclaims

99. In Behring International Inc. and Islamic Republic of Iranian Air Force, Award No. ITM/ITL 52-382-3 (10 August 1983), the Tribunal ruled that the withdrawal of claims can have no effect on its jurisdiction over a counterclaim unless the Tribunal were to determine that it had no jurisdiction over the claims as originally filed.

100. In view of the fact that the Tribunal has dismissed both the direct and indirect claims on the ground that it does not have jurisdiction to decide these claims, the counterclaims, which are dependent on jurisdiction of the Tribunal over the claims, are likewise dismissed.

IV. OTHER MATTERS

101. In its Order of 8 November 1985 the Tribunal granted the Respondents permission to file new documentary evidence by 10 December 1985 and the Claimant was authorized to file evidence in rebuttal not later than 6 January 1986. On 10 December 1985 the Respondents filed 18 volumes of brief and documentary evidence.

102. The Claimant in a letter of 30 December 1985 requested the Tribunal to reject the entire filing as being an abuse of the Tribunal's process and as prejudicial to it. In its rebuttal submission of 6 January 1986 the Claimant reiterated its request that the additional filing be rejected since, with one exception relating to the appeal of the Skalbania case, the information submitted was not new evidence but had been either in the Respondents' possession or matters of public record for years. The Tribunal in its Order of 19 December 1985 informed the Parties that it would take a decision regarding the admissibility of the submission at the Hearing.

103. In view of the decision by the Tribunal dismissing both the claims and the counterclaims the issue of the late filing by the Respondents becomes a moot one.

V. COSTS

104. Each Party shall bear its own costs.

VI. AWARD

105. For the foregoing reasons,
THE TRIBUNAL AWARDS AS FOLLOWS:

a) The claims of INTERNATIONAL SYSTEMS & CONTROLS CORPORATION are dismissed for lack of jurisdiction.

b) The counterclaims are also dismissed for lack of jurisdiction.

c) Each Party shall bear its own costs.