13 July 2017

Via Courier

Y.A.B. Dato' Sri Hj. Mohd. Najib Bin Tun Haji Abdul Razak
Prime Minister
Office of the Prime Minister
Main Block, Perdana Putra Building
Federal Government Administrative Centre
62502 Putrajaya, Malaysia

Your Excellency,

Notice of Dispute and Request for Settlement Discussions pursuant to Article X of the 1987 ASEAN Investment Agreement

1. Introduction

We write on behalf of our clients, the duly-recognised heirs to the Sultanate of Sulu and Sabah ("the Sultanate"), and successors-in-interest to Sultan Jamalul Alam Kiram under the 1939 Opinion of Charles F.C. Macaskie, then Deputy Governor and Chief Justice of North Borneo, as administered by the North Borneo Trading Company.

A dispute has arisen between our clients and the Government of Malaysia arising from Malaysia's violations of the 1987 ASEAN Agreement for the Promotion and Protection of Investments signed on 15 December 1987 and which came into force on 02 August 1988 ("the 1987 ASEAN Investment Agreement").[1]

Your Excellency accordingly should consider this letter to constitute a Notice of Dispute and Request for Settlement Discussions under Article X of the 1987 ASEAN Investment Agreement. We summarise the dispute below.

We hope that Malaysia will comply with its obligations under international law (including, but not limited to, Article X of the 1987 ASEAN Investment Agreement) to engage in settlement discussions in good faith. To this effect we propose below a timetable for meaningful negotiations. We respectfully remind Malaysia that it is obligated under international law not to aggravate the dispute,

[1] We are of course aware of the 2009 ASEAN Comprehensive Investment Agreement. We draw your attention to Article XIII(2) of the 1987 ASEAN Investment Agreement, which provides that its provisions in respect of existing investments would continue for ten years after the 1987 ASEAN Investment Agreement's termination.

to preserve the status quo and not to frustrate the negotiation process under the 1987 ASEAN Investment Agreement.

If the dispute cannot be settled within six months of the date of this Notice, then our clients will submit their claims to an international arbitral tribunal pursuant to Article X (2) of the 1987 ASEAN Investment Agreement.

2. Background

This dispute arises out of Malaysia's failure to pay for the true value of our clients' rights in connection with the province of Sabah.

Our clients are the direct heirs to the Sultanate of Sulu and Sabah, and the successors-in-interest to Sultan Jamalul Alam Kiram, signatory to that certain Agreement dated 22 January 1878 between him and Messrs Alfred Dent and Baron Gustavus de Overbeck ("the 1878 Agreement"). Malaysia is the successor-in-interest to Messrs. Dent and Overbeck under the 1878 Agreement.

The essence of the 1878 Agreement was that the Sultan gave Overbeck (acting on behalf of his partner Dent) use of the North Borneo territories in perpetuity in exchange for the annual sum of 5,000 Malay Dollars. This annual payment reflected the *full value* of the territory's uses and produce to the Sultan in 1878. Indeed, it was on the basis of the Sultan's estimate of his income from his North Borneo territory at the time, that Overbeck and the Sultan agreed to set the payment for their arrangement at 5,000 Malay Dollars. The Sultan was thus made whole for the loss of his ability to extract commercial benefit from North Borneo.

The rights and obligations under the 1878 Agreement passed from Dent and Overbeck to the North Borneo Trading Company in 1881. Those rights and obligations in turn passed to the British Crown, under the auspices of the Colony of North Borneo, in 1946.

With the independence of the Malaysian federation on 21 August 1963, Malaysia assumed the role of contractual counterparty for North Borneo (now the Province of Sabah) under the 1878 Agreement previously held by Dent and Overbeck, the North Borneo Trading Company, and then the British Colony of North Borneo. Consistent with the parties' expectations and precedent, Malaysia began rendering annual payments to the heirs of the Sultanate.

In the 1970s, significant hydrocarbons were discovered in and around the territory of North Borneo (now the Province of Sabah). In recent years, those discoveries have been complemented by vast finds of natural gas. Malaysia has extracted hundreds of billions of dollars in oil and gas revenue from the territory to date. Significant hydrocarbon discoveries have become exploitable and extractable over the past few years. Conservative estimates show that hundreds of billions of dollars of reserves remain unexploited.

Pursuant to the 1878 Agreement, the hardship provision in the UNIDROIT Principles, the principles of Shariah law, the international doctrine of *rebus sic stantibus*, and the general precepts of equity and good faith, our clients and their predecessors made numerous attempts to negotiate terms of a more equitable and appropriate arrangement between the parties.

In particular, in 1989, shortly after the 1987 ASEAN Investment Agreement came into force, the Sultanate, with the blessing of the Philippine Administration at that time, reached out to the Government of Malaysia in order to negotiate revised terms to the 1878 Agreement. The Sultanate explicitly floated the concept of formally ceding sovereignty to Malaysia and accepting the termination of the 1878 Agreement in exchange for a lump sum payment. Malaysia did not respond.

In 1999, the Sultanate wrote to Malaysia, again proposing the extinguishment of its sovereignty rights, along with an increase in the annual payment under the 1878 Agreement to US$749 million.

Further attempts, equally unsuccessful, were made to negotiate with the Government of Malaysia over the following 15 years. The sole formal correspondence received from Malaysia constituted cover letters for the annual payments to the heirs of the Sultanate – our clients. Malaysia self-servingly styled these payments "cession monies."

In early 2013, a dissident member of the Sultanate royal family declared himself Sultan (our clients, including Sultan Fuad Kiram, naturally did not recognize the pretender.) The pretender supported an action to take a small force of men across the Sulu Sea to Sabah and stated his intention to "reclaim" the territory on behalf of the Sultanate of Sulu.

Our clients – Sultan Fuad Kiram and the other duly-recognised heirs of the royal family – condemned the recourse to violence and disclaimed his actions.

Nonetheless, in 2013, the Government of Malaysia wrongly used the pretender's actions as a pretext to stop even the paltry annual payments that it had hitherto made – despite the fact that Malaysia had consistently recognised its payment obligation since 1963.

The pretender died later in October 2013.

Earlier this year, our clients made a final demand, by letter to Your Excellency, to negotiate a fair payment. We have received no response to this legitimate request.

3. The Dispute

The Sultanate has repeatedly made demands for a fair payment that reflects the true value of its rights under the 1878 Agreement. Notwithstanding the discovery of massive hydrocarbon reserves, Malaysia has unfairly and arbitrarily failed to respond, let alone accept, those legitimate demands. Further, in

2013, without any explanation or justification, Malaysia abruptly stopped paying the annual payment altogether.

Our clients' request for negotiating a fair annual payment is grounded in the radically changed circumstances of the arrangement brought about by the discovery of natural resources that was neither in the contemplation of the parties when they signed the 1878 Agreement (prior even to the patenting of the internal combustion engine), nor when Malaysia adopted that arrangement (the discovery of hydrocarbons having occurred over a decade later.) Even today, hitherto-unforeseen discoveries and extractions – made viable by developing technologies – contrive to change the circumstances of the arrangement.

Since the discovery of hydrocarbons in the region, our clients have thus been thrust into a position (even when Malaysia does honour its obligations) where they would receive the equivalent of US$1,200 annually in connection with territory that, at today's (relatively low) oil and gas prices, produces approximately *20 million times* that much in annual revenue from petroleum resources.

If ever there were a case for the renegotiation of an arrangement that had become fundamentally unbalanced due to changed circumstances, this is it.

In light of the above, our clients have repeatedly requested that duly-authorised representatives from the Government of Malaysia sit down with them to renegotiate the payment arrangement under the 1878 Agreement along lines that more equitably and correctly reflect the balance of the bargain originally struck between the parties.

Malaysia's repeated and on-going refusal to negotiate in response to our clients' legitimate request for a fair payment and/or its failure to pay any monies at all has resulted in a violation of its obligations in the 1987 ASEAN Investment Agreement, giving rise to this dispute.

4. Malaysia's Violations of the 1987 ASEAN Agreement[2]

The 1987 ASEAN Investment Agreement provides the nationals of a member state with guarantees relating to the protection of investments in another member state.[3] These include the right of the nationals to invoke these guarantees against the host member state before an international arbitral tribunal.

The relevant provisions in the 1987 ASEAN Investment Agreement for the purposes of this dispute include the following:

1. Malaysia's obligation under Article III to accord investments of Philippine nationals "at all times" "fair and equitable treatment" and full protection (Article III (2)). The promise of fair and equitable treatment and full protection is reiterated in Articles IV (2) and IV (1), respectively;

[2] Our clients reserve all rights to bring separate legal proceedings pursuant to the dispute resolution clause of the 1878 Agreement.

[3] Malaysia is of course a party to the 1987 ASEAN Investment Agreement. The Philippines is also a party. Our clients are all citizens of the Philippines.

2. Malaysia's obligation arising from a commitment it may have entered into with regard to an investment of nationals of the Philippines (Article III (3));

3. Malaysia's obligation under Article IV (1) not to impair by unjustified or discriminatory measures the management, maintenance, use, enjoyment, extension, disposition, or liquidation of such investments;

4. Malaysia's obligation that investments of Philippine nationals shall not be subject to expropriation, nationalisation, or any measure equivalent thereto except for public use, or public purpose, or in the public interest, and under due process of law, on a non-discriminatory basis and upon payment of adequate compensation. That such compensation would amount to the market value of the investments affected and be settled and paid without unreasonable delay (Article VI (1));

5. Malaysia further promised to grant Philippine nationals treatment no less favourable than that granted to an investor of the most favoured nation (Article IV (2)).

Without prejudice and without limitation, our clients contend that Malaysia's actions and omissions, taken individually and/or collectively constitute a breach of one or more of the above international law protections in the 1987 ASEAN Investment Agreement.

The above violations are illustrative but not exhaustive. Our clients reserve their rights not only to particularise these examples but also to assert further breaches.

There can be no doubt that our clients, as nationals of the Philippines, benefit from the protections in the 1987 ASEAN Investment Agreement (Article I (1)). Likewise, it is apparent that our clients have a long-standing investment in the territory of Malaysia.

Article I (3) of the 1987 ASEAN Investment Agreement defines the term "investment" to mean every kind of asset, including rights relating to property and claims to money or any performance under contract having a financial value.

Malaysia adopted the arrangement under the 1878 Agreement upon becoming an independent state and reaffirmed it by making annual payments of 5300 Malay Dollars[4] for half a century. In doing so, it expressly recognised our clients' investment, which includes their rights to the annual payment, in its territory.

By refusing to negotiate a fair payment due to our clients and/or by ceasing all payments in 2013, Malaysia has violated the 1987 ASEAN Investment Agreement, including: its obligations to accord fair and equitable treatment at all times; to provide the investment with full protection and security; to

[4] Because of an ambiguity concerning the status of certain islands, the Sultan and the North Borneo Trading Company amended the 1878 Agreement in 1903 to confirm the latter's use of the islands. In consideration for the amendment, the annual payment was increased by 300 Malay Dollars per year. All other terms of the arrangement remained unchanged.

uphold any or all commitments made in relation to the investment, and; to pay market value compensation without delay in the event of an expropriation.

Malaysia undertook a commitment under the 1878 Agreement to pay in perpetuity. As mentioned, the original stipulated rent of 5000 Malay Dollars a year reflected the *full value* of the income derived by the Sultan from the territories at the time.

Thus, as the payment of the rent was based on the value of income, our clients were entitled to payment that reflected the increased income derived from the territory. In this case, the commercial exploitation of hydrocarbons has meant an earning of hundreds of billions of dollars for Malaysia. However, our clients have been deprived of an enhanced and fair payment resulting in a deprivation likewise totalling hundreds of billions of dollars.

Malaysia's failure to agree to an enhanced, fair payment frustrated our clients' legitimate expectations that Malaysia would pay an amount that reflected the value of the territory's produce in perpetuity. Malaysia has violated our clients' legitimate expectations in a manner that is unfair and inequitable, leading to a violation of Articles III (2) and IV (2) of the 1987 ASEAN Investment Agreement. Malaysia has also violated its promise to uphold its obligations in any commitment made to nationals of the Philippines under Article III (2).

Malaysia's failure to render fair payments has destroyed our clients' economic rights and thus constitutes an (unlawful) expropriation of their investment. Malaysia is liable to pay them full and fair compensation immediately and without delay.

It is well established in international investment law that rights arising from a contract or similar arrangement are susceptible to an expropriation in the same way as tangible property. In this case, Malaysia's interference with our clients' rights is tantamount to expropriation; these rights have been wholly impaired, contrary to our clients' reasonable and legitimate expectations. Malaysia's interference results in a right to market-value compensation.

Furthermore, by ceasing the annual payment in 2013, Malaysia purported to terminate the arrangement under the 1878 Agreement and thereby violated our clients' legitimate expectations in a manner that is unfair and inequitable under Articles III (2) and IV (2). In doing so, Malaysia also failed to uphold its commitment to Philippine nationals under Article III (3), impaired the investment by unjustified measures under Article IV (1), and expropriated the investment without paying any compensation under Article VI (1).

Our clients will particularise their claim for compensation in more detail in due course.

5. Proposed Timetable for Settlement Discussions

Pursuant to Article X (1) of the 1987 ASEAN Agreement, our clients respectfully invite the Government of Malaysia to enter into discussions in order amicably to resolve this dispute.

In keeping with the spirit and purpose of this provision, our clients confirm their willingness to participate in good-faith settlement negotiations, through their counsel, with the Government of Malaysia. Please confirm the Government of Malaysia's willingness to do so.

In order to use the six-month window for settlement discussions, we propose the following timetable:

> Within 4 weeks of receiving this Notice (i.e. by ***10 August 2017***), Malaysia will identify the competent authority designated to engage in consultations with us in relation to this dispute.
>
> Within 8 weeks of receiving this Notice (i.e. by ***7 September 2017***), Malaysia's representatives will meet with our clients' representatives in Singapore or another mutually convenient location to explore settlement options. The outcome of the meeting is to be confirmed in unilateral or joint statements by the parties.
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> Within 12 weeks of receiving this Notice (i.e. by ***5 October 2017***), the parties will meet to particularise any settlement avenues. The outcome of the meeting is to be confirmed in unilateral or joint statements.
>
> Within 24 weeks of receiving this Notice (i.e. by ***28 December 2017***), each party will issue a statement in relation to the outcome of the settlement discussions.

The six-month window for settlement discussions will expire on ***9 January 2018.*** If no settlement has been agreed by this point, our clients will submit this dispute (including their claim for compensation) for resolution to an international arbitral tribunal on or after that date. In furtherance of Malaysia's economic and political interests in ASEAN and the international community, we encourage the Government of Malaysia to engage in this opportunity to reach an amicable settlement so as to avoid international arbitration proceedings.

Respectfully,

Paul H Cohen

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