

**INTERNATIONAL CENTRE FOR THE SETTLEMENT OF  
INVESTMENT DISPUTES (ADDITIONAL FACILITY)**

Washington D.C.

Case N° ARB(AF)/00/3

**Waste Management, Inc.  
(Claimant)**

**versus**

**United Mexican States  
(Respondent)**

**AWARD**

Before the Arbitral Tribunal  
constituted under Chapter Eleven  
of the North American Free Trade  
Agreement, and comprised of:

Professor James Crawford, President  
Mr. Benjamin R. Civiletti  
Mr. Eduardo Magallón Gómez

**Secretary of the Tribunal**  
Ms. Gabriela Alvarez Avila

Date of dispatch to the parties: April 30, 2004

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AWARD

**WASTE MANAGEMENT, INC.**  
**Claimant**

**v.**

**UNITED MEXICAN STATES**  
**Respondent**

**AWARD**

**A. PROCEDURAL HISTORY**

1. On 27 September 2000, the Acting Secretary-General of ICSID registered a notice for the institution of arbitration proceedings, lodged by Waste Management Inc. (“Claimant”) under the ICSID Arbitration Additional Facility Rules (“the Rules”) against the United Mexican States (“Respondent”). The Claimant alleged that the Respondent is liable under Articles 1110 and 1105 of NAFTA for the actions of various state organs concerning the Claimant’s investment in an enterprise to provide waste management services to the City of Acapulco in the State of Guerrero.

2. In accordance with Article 1123 of NAFTA and Article 6 of the Rules, the parties proceeded to constitute the Arbitral Tribunal. The Claimant appointed Mr. Benjamin R. Civiletti, a United States national. The Respondent appointed Mr. Guillermo Aguilar Alvarez, a Mexican national. Pursuant to Article 1124(2), the Claimant requested the Secretary-General to appoint the President of the Tribunal. The Secretary-General, following consultations with the parties, appointed Professor James Crawford, an Australian national, to serve as President of the Tribunal. Pursuant to Article 1125 of NAFTA, the Claimant had previously agreed, by letter of 19 June 2000 accompanying its request for arbitration, to the appointment of each individual member of the Tribunal.

3. On 30 April 2001, pursuant to Article 14 of the Rules, the Secretary-General of ICSID informed the parties that all the arbitrators had accepted their appointment and that the Tribunal was deemed to have been constituted, and the

proceeding to have begun, on that date. By that same letter, the Secretary-General informed the parties that Ms. Gabriela Alvarez Avila, Senior Counsel, ICSID, would serve as Secretary of the Tribunal. All subsequent written communications between the Arbitral Tribunal and the parties were made through the ICSID Secretariat.

4. On 1 June 2001, the Respondent informed the Centre that it objected to the competence of the Tribunal. This was the second occasion on which the Claimant had brought proceedings in respect of its claim. In the first proceeding, ICSID Case No. ARB/(AF)/98/2, a Tribunal constituted by Mr. Bernardo M. Cremades (President), Mr. Keith Highet and Mr. Eduardo Siqueiros (hereinafter the “First Tribunal”) rendered an award declining jurisdiction on the ground that the Claimant had not validly waived its right to pursue domestic remedies, a waiver required by NAFTA Article 1121 as a condition precedent to the submission of a claim to arbitration. Moreover this failure could not be remedied by any act of the Claimant, with the result that the Tribunal lacked jurisdiction over the claim.<sup>1</sup> The Respondent argued that the effect of the first unsuccessful proceedings was to debar the Claimant from bringing any further claim with respect to the measure alleged to be a breach of NAFTA.

5. On 8 June 2001, the first session of the Tribunal with the parties was held at the seat of the World Bank in Washington, DC. During the course of the session, the parties acknowledged that the Tribunal had been duly constituted pursuant to Article 1120 of NAFTA and the Rules. An exchange of views took place on the venue of the arbitration and on the procedure for dealing with the Respondent’s objection to jurisdiction based on the previous proceedings, and in particular on the decision of the previous Tribunal.

6. In its Procedural Order No. 1 of 8 June 2001, the Tribunal laid down timetables for written observations on the question of venue and on the preliminary objection. The parties filed their observations on the question of venue on 18 June 2001. On 6 August 2001, the Tribunal gave the parties an opportunity to make further observations on the question of venue in light of the possible relevance of the Panama

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<sup>1</sup> For the Award of 2 June 2000 see 5 ICSID Reports 443.

Convention.<sup>2</sup> The parties filed their further observations on venue on 28 August 2001. Subsequently, by a Decision on Venue of the Arbitration dated 26 September 2001, the Tribunal decided that the venue of the present proceedings would be the same as those of the first proceedings, viz., Washington, DC.<sup>3</sup>

7. Following a communication from the Respondent dated 16 November 2001 which did not, however, amount to a challenge, one of the Arbitrators, Mr. Guillermo Aguilar Alvarez, tendered his resignation from the Tribunal. Pursuant to Article 15(3) of the Rules, the Tribunal accepted his resignation. Pursuant to Article 18(1) of the Rules, Mexico thereupon nominated Mr. Eduardo Magallón Gómez to fill the vacancy so created. The Tribunal was reconstituted on December 14, 2001, following Mr. Magallón's acceptance of his appointment.

8. Pursuant to Procedural Order No. 1, Respondent lodged a Memorial on Jurisdiction of 8 August 2001. Claimant lodged a Counter-Memorial on jurisdiction on 9 October 2001. The hearing initially scheduled for 3 December 2001 having been postponed in order to allow the vacancy on the Tribunal to be filled, the Tribunal convened at the premises of the World Bank, Washington, DC, on 2 February 2002 to hear the parties' oral arguments on jurisdiction. The parties were represented as follows:

Attending on behalf of the Claimant:

Mr. J. Patrick Berry, Baker & Botts LLP  
Mr. Richard King, Baker & Botts LLP  
Ms. Lorena Perez, Baker & Botts LLP

Mr. Jay L. Alexander, Baker & Botts LLP  
Mr. Bob Craig, Assistant General Counsel, Waste Management, Inc.

Attending on behalf of the Respondent:

Mr. Hugo Perezcano Díaz, Lead Counsel, Ministry of Economy,  
Government of Mexico  
Mr. Salvador Behar Lavalle, Ministry of Economy, Government of Mexico  
Ms. Adriana González Arce Brilanti, Ministry of Economy,  
Government of Mexico  
Mr. Cameron Mowatt, Thomas & Partners

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<sup>2</sup> Inter-American Convention on International Commercial Arbitration, Panama City, 30 January 1975, 1438 UNTS 249.

<sup>3</sup> The Tribunal's Decision is reported at 6 ICSID Reports 541.

Mr. Carlos García, Thomas & Partners  
Mr. Robert Deane, Thomas & Partners  
Mr. Stephan E. Becker, Shaw Pittman  
Mr. Sanjay Mullick, Shaw Pittman  
Ms. Brooke Bentley, Shaw Pittman.

The Tribunal heard, on behalf of the Respondent, Mr. Hugo Perezcano Díaz, and on behalf of the Claimant, Mr. Jay Alexander.

9. Representatives of the other two NAFTA parties attended the hearing on 2 February 2002:

Attending on behalf of the United States of America:

Mr. Barton Legum, Chief of the NAFTA Arbitration Division, Office of Legal Adviser, Office of International Claims, Department of State  
Mr. David A. Pawlak, Attorney-Adviser, Office of Legal Adviser, Office of International Claims, Department of State.

Attending on behalf of the Government of Canada:

Mr. Douglas Heath, Embassy of Canada in Washington, DC.

10. In response to certain questions from the Tribunal concerning both the case as argued before the previous Tribunal and the proceedings brought by the Claimant in Mexico, the parties provided certain additional information and argument by letters both dated 19 February 2002.

11. On 28 June 2002, the Secretary of the Tribunal notified to the parties the Tribunal's Decision on Mexico's Preliminary Objection concerning the Previous Proceedings. A copy of the decision is attached as Annex 1. The Tribunal decided that the Claimant was not prevented from bringing its claim and reserved to a later stage the issue of the costs and expenses of the jurisdictional phase of the proceedings.<sup>4</sup> By the same letter, the Secretary of the Tribunal informed the parties that the Tribunal understood that the claim submitted by the Claimant was identical to that previously submitted to arbitration under NAFTA, and that the Memorial submitted as Appendix D to its Request of June 19, 2000 stood as the Claimant's Memorial in the present Arbitration. The Secretary of the Tribunal further invited the parties to consult with a view to agreeing on the time limits for the remaining written pleadings.

12. On the basis of the Claimant's observations of 5 and 13 August 2002 and of the Respondent's observations of 6 and 12 August 2002, and in view of the fact that the parties failed to agree in a schedule for the filing of the remaining pleadings, the Tribunal set up a schedule for the filing of pleadings by the parties, submissions by the NAFTA Parties and fixed a date for a hearing on the merits.

13. By letter of 12 August 2002, the Respondent submitted a request for interpretation and correction of certain translation errors into Spanish regarding the Tribunal's Decision of 26 June 2002, invoking Articles 56 and 57 of the Rules. On 13 August 2002, the Secretary of the Tribunal replied to Mexico, explaining that Articles 56 and 57 were only applicable to awards. The Secretary noted that Mexico's request would, however, be referred to the Tribunal for consideration pursuant to Article 35 of the Rules.

14. On 14 August 2002, the Secretary on behalf of the Tribunal invited the Claimant to file by 23 August 2002 any observations it might have in connection with Mexico's request of 12 August 2002.

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<sup>4</sup> The Tribunal's Decision is reported at 6 ICSID Reports 541.

15. On 22 August 2002, in a further letter to the Secretary-General, Mexico asserted that the Tribunal's Decision should be treated as an award. On 23 August 2002, the Acting Secretary-General responded to Mexico's letter of 22 August 2002, confirming that the term "award" in the ICSID Convention and Rules refers only to the final award which disposes of the case. With respect to the Additional Facility Rules, the Acting Secretary-General noted that these, being based on the Convention, were to the same effect. He further observed that a party could immediately ask the Tribunal to clarify, correct or supplement a preliminary or interim decision and that such question would be a matter for the Tribunal to decide under Article 35 of the Rules.

16. On 23 August 2002, the Claimant replied to the Tribunal's invitation to comment. It supported the Secretariat's interpretation of the term "award" in Articles 56 and 57 of the Rules, and argued that the Mexican request was accordingly inadmissible.

17. In a letter of 30 September 2002, the Secretary incorporated the Tribunal's observations to Mexico's request of 12 August 2002. The Tribunal affirmed that there was no request before it for interpretation or correction in accordance with Articles 56 and 57 of the Rules. It pointed out, however, that it had the power, while still exercising its functions and prior to the closure of the proceedings, to give any necessary interpretation of any of its decisions, to make any necessary supplementary decision, and to correct any error in the translation of a decision. The Tribunal further indicated that it could exercise such powers of its own motion or on the request of a party. The Tribunal, however, rejected Mexico's request, indicating that the two reasons given by Mexico for requesting interpretation were not relevant to the further proceedings before the Tribunal and that the Decision itself was clear. Regarding the correction of the Decision, the Tribunal stated that the points raised by Mexico did not reveal any inaccuracy in the translation of the Decision from English to Spanish or any inconsistency between the two versions.

18. By a letter of 23 September 2002, the Respondent requested an order from the Tribunal requiring disclosure of a series of documents which were said to be "relevant and necessary for the defense of this case". The request concerned two issues which were open at the merits phase, (A) damages and (B) ownership and control of the investment at issue, the Mexican company, Acaverde, S.A. de C.V., which was the actual concessionaire ("Acaverde").

19. By a letter of 30 September 2002, the Claimant noted that it was on the point of delivering to the Respondent's counsel in Washington, DC, a series of documents related to an opinion given by the Claimant's expert witness, Dr. Slottje, indicating that "most, if not all, of the financial information requested by the Respondent regarding the issue of damages will be contained in one form or another in those documents". However, it declined without an order from the Tribunal to provide documents in Category B, indicating that the Respondent appeared to be bringing an additional preliminary objection on the issue of standing. In the Claimant's view, the procedure followed by the First Tribunal had ensured that "all arguments of fact and law relating to jurisdiction" were disclosed; these did not include questions of standing.

20. By a further letter of 30 September 2002, the Respondent stressed that it had at no stage waived any right to raise other objections to the claim. In any event, it noted that the Claimant's ownership and control of Acaverde was relevant to the merits, including, eventually, to the quantum of damages.

21. On 1 October 2002, the Tribunal issued a Procedural Order concerning Disclosure of Documents, giving a certain number of indications regarding disclosure. The Tribunal expressed the view that documents concerning Acaverde's finances and operations in relation to the concession might be sought, provided they were sufficiently identified. The Tribunal further indicated that the Respondent's request for "copies of all the invoices issued in the period 1994-1998" was *prima facie* too burdensome, since it was likely to include large numbers of documents which were not in dispute as such. The Tribunal agreed that documents clarifying the extent of the Claimant's ownership and control of the investment were relevant. Finally, the Tribunal indicated that any remaining issues concerning specific documents could be referred back to the Tribunal by either party for a prompt ruling.

22. After an exchange of correspondence between the Respondent and the Claimant in connection with the production of documents, by a letter of 12 November 2002, the Respondent called on the Tribunal to order that it had access to information regarding Acaverde in possession of Servicios de Tecnología Ambiental, S.A. de C.V.

(“Setasa”).<sup>5</sup> The Respondent explained the reasons for its request of the Claimant’s consent to the hand-over by Setasa of documents that had been provided by a predecessor of the Claimant under cover of a confidentiality agreement, to enable Setasa to assess the value of Acaverde.

23. By a letter of 15 November 2002, the Claimant outlined aspects of the history of its relations with Setasa, underlining that Setasa did not return the documents provided to it and there had been earlier litigation between Setasa and the Claimant regarding Setasa’s compliance with the confidentiality agreement. It offered to disclose directly to the Respondent any responsive documents which were returned to it by Setasa. The Claimant also called on the Tribunal to order immediate disclosure by the Respondent of nine classes of documents previously requested to the Respondent.

24. By a letter of 15 November 2002 to the Tribunal, the Respondent sought directions from the Tribunal as to what it characterized as “the Claimant’s substantial failure to comply with the Tribunal’s order”. In particular, it sought directions as to two classes of documents not disclosed. The first concerned Claimant’s conveyance of its Mexico operations in 1997. The second concerned alleged discrepancies as to the effective date on which the Claimant’s predecessor acquired Acaverde.

25. By a letter of 20 November 2002 to the Tribunal, the Respondent summarized the disclosure so far made by the Claimant. It set out in further detail reasons why the Respondent should be given access to documents in the control of Setasa. It argued that any disclosure request by the Claimant should be entertained only after the deposit of the Counter-Memorial, when it could be considered in the light of the arguments and documents contained in that filing.

26. By letter of 21 November 2002 to the Tribunal, the Claimant commented on the Respondent’s 15 November 2002 requests for orders. As to the 1997 conveyance, it offered to make available to the Respondent a redacted version of the agreement, or to file with the Tribunal an unredacted copy, which the Tribunal could confirm did indeed

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<sup>5</sup> Setasa negotiated with Acaverde’s principal shareholder, Sanifill, for the purchase of Acaverde in 1997 and accordingly received confidential information about the company as part of the due diligence process. It is this information which was the subject of the Respondent’s letter to the Tribunal of 12 November 2002. See further para. 66.

exclude Acaverde from the sale. As to the Respondent's second request, the Claimant noted that the difference between October 1994 and June 1995 in terms of the completed acquisition of Acaverde was irrelevant to standing under NAFTA Chapter 11.

27. By a letter of 21 November 2002 to the Tribunal, the Respondent rejected both proposals the Claimant had made as to the Agreement of 1997. The Respondent further rejected the Claimant's argument regarding the information requested in connection with the Cayman Islands transactions.

28. By a letter of 22 November 2002 to the Tribunal, the Claimant attached a redacted version of the 1997 Agreement.

29. On 25 November 2002, the Respondent requested an extension to file its Counter-Memorial. The Secretary informed the parties by a letter of 26 November 2002, that the Tribunal granted the extension requested by the Respondent and indicated the new schedule for the filing of pleadings.

30. On 27 November 2002, the Tribunal issued Procedural Order No. 2 concerning Disclosure of Documents. The Tribunal indicated that to the extent that documents identified by the Respondent were relevant to the question of ownership or control but the Claimant had neither disclosed them nor explained why they were not available, the Tribunal could draw corresponding inferences. It further stated that the Tribunal did not believe that any additional order was required as to documents pertaining to control over Acaverde in the period 1994-1995. The Tribunal also decided that the 1997 Agreement did not appear to be relevant to the present dispute, and accordingly did not order further disclosure. Regarding the documents in possession of Setasa, the Tribunal found it appropriate that the Claimant disclose promptly to the Respondent all relevant documents that Setasa might provide to the Claimant. The Tribunal asked the Claimant to provide the Tribunal with an explanation of the situation within 7 days of the date of the order.

31. In its Procedural Order No. 2, the Tribunal also addressed the Claimant's request for production of 9 categories of documents. The Tribunal granted in part the Claimant's request, in particular the documents related to Mexico's financial expert

evidence, and denied or found not relevant other categories of documents. The Tribunal directed that the Respondent should disclose the documents concerned at the same time as the Counter-Memorial or at the latest within 7 days of the filing of the Counter-Memorial.

32. The Respondent lodged its Counter-Memorial on the merits on 6 December 2002. On 13 January 2003, the Claimant requested an extension to lodge its Reply. The Secretary informed the parties by a letter of 15 January 2003 that the Tribunal had granted the extension requested by the Claimant and indicated the new schedule for the filing of pleadings, including the filing of submissions by the NAFTA Parties under NAFTA Article 1128.

33. The Claimant filed its Reply on the merits on 22 January 2003. The Respondent filed its Rejoinder on the merits on 7 March 2003.

34. Pursuant to a request of the Tribunal, the parties submitted a joint letter of 12 March 2003 regarding the organization of the hearing on the merits. The parties further expressed their views by a letter submitted by each party on 13 March 2003. The Tribunal, having considered the above correspondence, issued directions regarding the hearing on the merits which were communicated by the Secretary's letter of 14 March 2003.

35. On 19 March 2003, the Government of Canada filed a submission under Article 1128 of NAFTA and the United States of America advised the Tribunal on the same date that it did not intend to make a submission.

36. The hearing on the merits was held from 7 April until 10 April 2003 at the premises of the World Bank in Washington DC to hear the parties' oral arguments and the witnesses and experts called by them. The parties were represented as follows:

Attending on behalf of the Claimant:

Mr. Bob Craig, Assistant General Counsel, Waste Management, Inc.  
Mr. Kemp Sawyers, Baker & Botts LLP  
Mr. J. Patrick Berry, Baker & Botts LLP  
Ms. Clara Poffenberger, Baker & Botts LLP  
Ms. Guillermina Calles, Baker & Botts LLP  
Ms. Lila Pankey, Baker & Botts LLP  
Ms. Sharon Katz, Baker & Botts LLP

Mr. Ulrich Brunnhuber.  
Attending on behalf of the Respondent:

Mr. Hugo Perezcano Díaz, Lead Counsel, Ministry of Economy  
Mr. J. Christopher Thomas QC, Thomas & Partners  
Mr. Cameron Mowatt, Thomas & Partners  
Mr. Stephan E. Becker, Shaw Pittman  
Ms. Adriana González Arce Brilanti, Ministry of Economy,  
Mr. Salvador Behar Lavalle, Ministry of Economy  
Ms. Alejandra Galaxia Treviño Solís, Ministry of Economy  
Mr. Sanjay Mullick, Shaw Pittman  
Mr. Rolando García, Thomas & Partners  
Mr. Carlos García, Thomas & Partners  
Mr. Humberto Guerrero Shaw Pittman.

The following witnesses and experts were heard at the hearing:

*Witnesses of the Claimant:*

Mr. Rodney Proto  
Mr. H. Steven Walton  
Mr. Jaime Eduardo Herrera Gutiérrez de Velasco

*Witnesses of the Respondent:*

Mr. Mario Alcaráz Alarcón

*Experts of the Claimant:*

Dr. Daniel Slottje

*Experts of the Respondent:*

Mr. Carlos de Rivas Ibañez  
Mr. Carlos de Rivas Oest.

37. Representatives of the other two NAFTA parties attended the hearing:

Attending on behalf of the United States of America:

Mr. David A. Pawlak, Office of International Claims, Department of State  
Ms. Jennifer Gehr, Department of Commerce.

Attending on behalf of the Government of Canada:

Mr. Douglas Heath, Embassy of Canada in Washington, DC.

38. Transcripts in English and Spanish of the hearing on the merits were prepared and distributed to the parties and the members of the Tribunal.

39. By letter of 14 April 2003, the Secretary distributed copies of certain questions from the Tribunal to both parties as made at the end of the hearing on the merits. The Secretary also informed the parties, following the Tribunal's instructions, of the schedule for submitting their answers. The parties submitted their answers to the Tribunal's questions on 28 April 2003.

## **B. THE DISPUTE BETWEEN THE PARTIES**

40. The present dispute arises from a concession for the provision of waste disposal services in the Mexican City of Acapulco in the State of Guerrero, one of the component states of Mexico. The agreed terms for this operation were laid down in a Concession Agreement (*Título de Concesion*), the parties to which were the City through its Council (*Ayuntamiento*) ("the City") and Acaverde. Acaverde was a Mexican company created in 1994. It is said at all relevant times to have been a wholly owned subsidiary of the Claimant, Waste Management Inc. ("Waste Management"), a Delaware corporation with substantial interests in municipal waste disposal services in the United States and elsewhere.<sup>6</sup> The question of Waste Management's entitlement to claim under Articles 1116 or 1117 of NAFTA in respect of the present dispute involving Acaverde is an issue in the case. In this section of the Award, the Tribunal will refer to Acaverde as the actual contracting party and provider of services under the Concession Agreement.<sup>7</sup>

41. The Concession Agreement was concluded on 9 February 1995. It was amended in significant respects by a further agreement of 12 May 1995. Under the Concession Agreement as so amended ("the Concession Agreement"), Acaverde undertook to provide on an exclusive basis certain municipal waste disposal and street cleaning services in a specified area of Acapulco. The area concerned, containing approximately 9000 residential and commercial addresses, covered the principal tourist and beachfront area of the City, which is a fraction of the total area of Acapulco, a city of approximately 1.5 million people. Tourism is the most important service industry in Acapulco, and there is no doubt that the waste collection system in the tourist area needed attention.

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<sup>6</sup> USA Waste Services Inc. merged with Acaverde's principal shareholder, Sanifill, in 1996. The merged company was subsequently renamed Waste Management, Inc.

<sup>7</sup> The relationship between Acaverde and its parent companies is discussed at paras. 77-85, below.

42. Clause 15 of the Concession Agreement provided that the City would not grant to any other company or person “any right or concession inconsistent with the rights of the Concessionaire under this Concession Agreement”. Under the Program of Operations, the City undertook to enact “such ordinances and local statutes as may be necessary to forbid manual street sweeping, the collection, transportation, use, recycling or disposal by any person or entity other than the Concessionaire of any Waste generated within the Concession Area”. These ordinances and statutes were to be fully and promptly enforced, both for residential and commercial waste collection. The Parties agreed that the enactment of the relevant ordinances would be a condition precedent to the commencement of operations and that Acaverde could “treat as a default any failure of the City to enforce these ordinances fully”.

43. On 30 June 1995, before Acaverde commenced services under the Concession Agreement, the City passed and subsequently promulgated a Regulation regulating the Rendering of the Public Cleaning Service Concession (“the Cleaning Services Ordinance”). The Cleaning Services Ordinance established exclusivity of waste collection services, prohibited dumping of rubbish in the area and provided for enforcement by way of fines. A schedule of rates was attached.

44. Article 8 of the Cleaning Services Ordinance provided that residents or businesses located in the concession area “must request” the public cleaning service within 90 days of commencement of operations. The Respondent argued that this provision did not correspond to any substantive obligation in the Concession Agreement, and noted that the obligation to pay scheduled rates was not imposed on residents as such. Formally this is true. Only persons who had signed a service contract with Acaverde were obliged to pay, and owners of holiday apartments in the concession area might not have any incentive to do so. Furthermore the terms of service contracts were a matter for agreement; the Ordinance established maximum but not minimum rates and Acaverde could (and did) enter into contracts at less than the scheduled rate. It is true that the Concession Agreement clearly contemplated that Acaverde would enjoy exclusivity within the concession area, and the City would not undermine this exclusivity by granting others the right to collect waste. But this did not necessarily translate into a situation where Acaverde’s market penetration in the concession area was sufficient to maintain its profitability.

45. In addition to providing collection services, Acaverde undertook under the Concession Agreement to build and operate a permanent solid waste landfill for the City as a whole, which would enable the closure of two existing temporary sites. The City would provide a site for the landfill “as [a] gratuitous loan for the term of the concession”. Fees for use of the landfill could be charged, at approved rates, to commercial customers. Pending the construction of the permanent landfill Acaverde would be given, free of charge, access to one of the existing sites.

46. The term of the Concession Agreement was to be 15 years from the date of commencement of services.

47. Under the Concession Agreement, Acaverde undertook to make an initial investment of up to US\$12.8 million. Its charges were to be in accordance with the agreed schedule, which was an integral part of the Concession Agreement and was subject to indexation. In return the City would pay Acaverde a monthly fee for services which, after 1 January 1996 would be NP1 million<sup>8</sup> (approximately equivalent to US\$170,000 at then-current exchange rates), and which was also indexed. Acaverde would pay the City a bonus calculated on the basis of its “success rate” in obtaining payment from customers in the concession area. The bonus payable was only 3% of certain revenues if the success rate was between .80 and .849, but rose to 30% with a success rate above .95. This gave the City some incentive to seek to ensure exclusivity and completeness of coverage. On the other hand it implicitly acknowledged that such coverage would not necessarily be achieved. In fact, the success rate never rose as high as .60, and no bonuses were ever paid to the City under these provisions.

48. Under the Concession Agreement, payments due to Acaverde by the City would bear interest at a specified rate if unpaid after 60 days. The City undertook to negotiate with a development bank established by the federal government of Mexico, Banco Nacional de Obras y Servicios Publicos, S.N.C. (“Banobras”), “an irrevocable, contingent and revolving line [of credit]” to guarantee “all payment obligations” of the City for the term of the Concession Agreement (Article 11).

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<sup>8</sup> “NP” refers to Mexican New Pesos.

49. The Line of Credit Agreement was issued on 9 June 1995. As envisaged by the Concession Agreement, the parties to the Line of Credit Agreement were the Government of the State of Guerrero (“Guerrero”), the City and Banobras. It recited the need to guarantee payment obligations under the Concession Agreement “in the event the City faces temporary cash flow problems that prevent the City to comply with such obligations” (Recitals, cl. III). Despite the reference in Article 11 of the Concession Agreement to “all payment obligations” of the City, the Line of Credit Agreement only covered “an amount equal to six monthly payments agreed to for the services rendered”, i.e. NP6,000,000 (Recitals, cl. XI). Demands for payment under the Line of Credit Agreement could be made by the City or by Acaverde. Disputes under the Line of Credit Agreement were referred to the federal courts of Mexico to the exclusion of “any other jurisdiction that might be available to them by reason of their present or future domiciles” (Clause 14, as translated by the Tribunal).

50. Although the Line of Credit Agreement was clear in limiting the total amount of credit available at any time to NP6 million, Banobras had the right to divert federal payments to Guerrero by way of reimbursement. In this regard Clause 6 provided:

“In the event that one or more requisitions made against the line [of credit] are not paid within 90 days, the Bank will proceed without delay to give effect to the guarantee corresponding to the present and future entitlements

due from federal income to the State Government of Guerrero, thereby recovering the amounts paid to ‘Acaverde, S.A. de C.V.’ against this credit.”<sup>9</sup>

Interpreted literally, this provision was directed at the question of replenishment for Banobras from the federal funds of Guerrero in respect of payments already made to Acaverde and not repaid by the City. It was not expressed in terms of a right of recourse by Acaverde against federal funds in the hands of Guerrero.

51. Before the Tribunal there was some discussion as to Acaverde’s role in the conclusion of the Line of Credit Agreement, and whether it had accepted the limitation of

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<sup>9</sup> Translation by the Tribunal. The original reads:  
“En caso que una o más disposiciones hechas contra la línea no se paguen en el plazo de 90 días, el Banco procederá sin demora a hacer efectiva la garantía correspondiente al las participaciones presentes y futuras que le correspondan en ingresos federales al Gobierno del Estado de Guerrero, recuperando así las cantidades pagadas a ‘Acaverde, S.A. de C.V.’, con cargo a este crédito.”

the Banobras guarantee contained in that Agreement.<sup>10</sup> In the Tribunal's view, although Acaverde may not have played any role in the negotiation or drafting of the Line of Credit Agreement, and although it was no doubt unhappy about the limitation of the guarantee insisted on by Banobras, it nonetheless accepted the resulting situation and went ahead with its investment. In other words, in the Tribunal's view, Acaverde accepted that the Line of Credit Agreement concluded in June 1995 was sufficient to meet the requirements of the amended Concession Agreement.<sup>11</sup>

52. As required by Mexican law, the grant of the Concession for a period of 15 years was approved by Decree of the State Congress in December 1994.<sup>12</sup>

53. Disputes under the Concession Agreement were to be submitted to arbitration in accordance with Clause 17, which provided that:

“Any dispute arising from, or related to, this Concession, shall be submitted to Arbitration by one Arbitrator jointly appointed by the CONCESSIONAIRE and the MUNICIPAL COUNCIL. In the event the parties fail to reach an agreement on such appointment, the Arbitration shall be conducted by three Arbitrators, one of whom shall be an independent expert on Mexican Law. In the latter case, the Arbitrators appointed by the Parties shall jointly select a third Arbitrator, who shall be designated as President.”

The arbitration was to take place in Acapulco under the rules of Conciliation and Arbitration of the National Chamber of Commerce of Mexico City.

54. On 15 August 1995, Acaverde began providing services under the Agreement. Difficulties were encountered almost immediately in enforcing the exclusivity arrangements contained in the Concession Agreement, and there was strong customer resistance to paying for waste disposal services, either at all or at the published

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<sup>10</sup> Mr. Rodney Proto, transcript, 7 April 2003, 102; Mr. Steven Walton, *ibid.*, 282-7. Acaverde's Mexican lawyer, Mr. Jaime Herrera stated that Acaverde did not participate in the drafting of the Line of Credit Agreement and that its suggestions in that regard were rejected by Banobras (Herrera Statement, para. 9; see also Banobras' letter to Sanifill of 19 June 1995). But it is clear that Acaverde, which had agreed to the amended Concession Agreement at Banobras' insistence, had notice of the precise terms of the Line of Credit Agreement when it commenced operations in August 1995: *ibid.*, para. 8.

<sup>11</sup> In the correspondence preceding the Line of Credit Agreement, its limitations are consistently spelled out: e.g. in the letter of the State Delegate, Banobras to Acaverde, 26 May 1995. Subsequently (but before operations commenced), Banobras made it clear that the terms of the Agreement could not be changed: State Delegate, Banobras to Acaverde, 19 June 1995.

<sup>12</sup> Decree No. 127, 15 December 1994, published in the Guerrero *Official Gazette*, 3 January 1995.

rate.<sup>13</sup> Many of those who had previously picked up and/or dumped waste in the concession area on an informal basis were resistant to the new arrangements. The cast of resisters included the pig-farmers (*porcicultores*) who took waste food from restaurants as food for their animals; the “pirates” (*piratas*) who ran unauthorised pick-up trucks looking for (and also dumping) waste, and the hawkers or barrow-men (*carretilleros*) who would do small jobs, including waste disposal, for a tip. Acaverde eventually reached an agreement with the pig-farmers association, but the *piratas* and the *carretilleros* were a continuing source of difficulty.<sup>14</sup> In particular, Acaverde complained that permits issued to the “pirates” allowing them to collect waste in the concession area were not revoked and even continued to be issued. Acaverde also complained that City drivers were picking up waste within the concession area in return for tips.

55. In addition, Acaverde complained at the City’s failure to provide premises for Acaverde’s operations or to enter into the gratuitous loan agreement for the new landfill. Under the Concession Agreement the City was required to provide, through a gratuitous loan, a municipally-owned piece of land for use as a permanent landfill. This would enable the existing open air dumps to be closed. Acaverde complained that the land, though identified and surveyed, was never made available. In lieu of the proposed landfill, Acaverde operated a temporary land-fill, and allowed the City to use it to dump waste collected outside the concession area.<sup>15</sup>

56. Following initial public unrest at the introduction of Acaverde’s services and charges, the Mayor of Acapulco in October 1995 is reported as having requested Acaverde to “make adjustments to fit the Mexican standards”. Mayor Almazán is reported to have said that “the obligation to contract Acaverde’s services will be eliminated in order to remove what was previously interpreted as an imposition”.<sup>16</sup> There is certainly evidence supporting the Mayor’s perception that Acaverde’s concession had been “interpreted as an imposition”. But notwithstanding his statement, neither the Cleaning Services Ordinance nor the Concession Agreement was amended. The Mayor’s statement

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<sup>13</sup> See e.g., Mr. Rodney Proto, transcript, 7 April 2003, 89, lines 7-11.

<sup>14</sup> E.g., letters of Acaverde to the City, 2 September 1996, 13 December 1996.

<sup>15</sup> See Statement by Mr. D. Harich, a civil engineer employed by Waste Management to design the proposed landfill.

<sup>16</sup> “No es obligatorio Acaverde: ROA”, *El Sol de Acapulco*, 13 October 1995, p. 1.

may have added to Acaverde's difficulties, but in the Tribunal's view it did not cause the difficulties, nor did it bring about the failure of the enterprise. Rather it was symptomatic of a public debate about the concession at a difficult time for all concerned.

57. Over time, and with a substantial input of resources, Acaverde built up its client base in the Concession area to approximately 5000 addresses, i.e., about 55% of the total; but it was generally forced to offer discounts in order to attract customers. It also provided considerably more personnel for public street sweeping and collection services than the minimum required by the Concession Agreement. It is clear that the arrangement was not commercially viable, taking into account both the lower than expected proportion of customers serviced and the additional costs incurred.

58. But Acaverde's financial difficulties were greatly exacerbated in that from the beginning there were severe problems in ensuring regular payments from the City under the Concession Agreement. Of 26 invoices presented by Acaverde, the City paid one in full and made partial payments with respect to two.<sup>17</sup> In June 1996 Banobras paid invoices for the 4 months January-April 1996 under the Line of Credit Agreement (but without the indexation element), thereby reducing the City's indebtedness. This was the only payment made under the Line of Credit Agreement. On 23 July 1996, Acaverde requested Banobras to pay the invoice for May 1996, which had not been rejected by the City and was therefore deemed to have been accepted, and it made a series of similar requests for subsequent months. On 2 August 1996, Banobras gave two reasons for denying Acaverde's request: first, what it stated to be the NP5.9 million already paid had not been reimbursed by the City; second, the parties to the Concession Agreement were actively considering modifications to it in response to the City's financial crisis. Banobras' State Delegate wrote:

“Contractually, the Municipality of Acapulco is obliged to refund all amounts [paid under the Line of Credit] within 90 days and, if it fails to do so, the Bank will proceed to use federal contributions made by the Government of the State.

On the other hand, as you know, in the current negotiations between said company and the Municipality of Acapulco, it is considered to make amendments in the Concession Instrument, including the financial part as the main problem to be resolved. This willingness to amend the Concession

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<sup>17</sup> The City made a swap proposal in respect of the 1995 invoices which Acaverde refused, as it was entitled to do.

Instrument was expressed by both parties to the authorities of the Secretariat of Finance and Public Credit and to the Bank, but, to date, there is no final proposal accepted by both.

For the above reasons, I am informing you that it is impossible to pay the bill submitted, until the Municipality refunds to us the amount disbursed and sends us the agreements accepted by your company and the Municipality of Acapulco, which are indispensable elements in order to update the amount of the Line.”

59. Acaverde replied on 6 August 1996. It made the valid point that the amount it had received under the Line of Credit in June 1996 was only NP4.9 million, and that fees and interest charges owed by the City to Banobras as a result of payments to Acaverde should not be counted against it. It also noted that the continuation of its negotiations with the City was no excuse for Banobras not to comply with its obligations under the Line of Credit Agreement. Faced with Banobras’ refusal Acaverde reserved its legal rights:

“our company is forced to terminate the negotiations fostered by your H[onourable] Institution, we will protect our interests and rights contained in said Instrument [Concession Agreement] in the venue and form we deem necessary.”

60. Banobras was in a difficult position. On the one hand the initial Line of Credit was substantially exhausted, and the seizure of the diminished federal grants to the City for the purposes of replenishing it would have been a controversial act locally. The fact that the parties were considering changes to the Concession Agreement was, if not a justification, at any rate an excuse for not considering the exercise of that power for the time being.

61. For its part, the City wrote to Banobras on 11 September 1996, reciting what it claimed were failures on the part of Acaverde to perform its obligations under the Concession Agreement, requesting it not to make further payments under the Line of Credit and threatening it with litigation if it did.

62. The Claimant argued that this letter was a mere excuse by the City to avoid meeting its obligations under the Line of Credit Agreement, that any problems notified to Acaverde were promptly rectified, and that there was no general complaint from the City, at the time, as to the level and quality of the service Acaverde was providing. The

Respondent argued on the contrary that there were persistent problems. This is a matter on which the Tribunal can only reach an impressionistic view. It notes the comment by one witness, who at the relevant time was the City's Secretary of Finance: in his opinion, "Acaverde's service was incomplete, because it only collected garbage from people who had contracts with the company. But *it was efficient for those with contracts.*"<sup>18</sup> There is other evidence to the same effect: the commercial side of Acaverde's operations was efficiently performed, given the constraints upon it.

63. On the other hand, in the Tribunal's view, whatever may have motivated the City's letter to Banobras of 11 September 1996 it did not simply invent a dispute about the level of servicing which had no basis in fact. For a variety of reasons the street sweeping operations conducted by Acaverde were not enough to keep the streets of the concession area consistently clean. Apart from illegal dumping by pirates and the inevitable boundary problems of a partial concession in a large city, there was a persistent problem of "black spots" (*puntos negros*). For much of the period of operations, Acaverde did not collect from addresses which were not contracted; from its point of view this was an attempt to induce residents and businesses to contract with it, and was understandable. But Acaverde's sanitary obligations were not limited to removing trash deposited by its customers. The City had to step in on various occasions to deal with complaints and black spots, and it continued to have to expend resources and manpower on sanitary operations in the tourist zone. Whatever the rights and wrongs of the situation, the fact is that the black spots were a recurring problem. For example on 15 May 1996, Acaverde's General Manager wrote to the City stating that:

"Our company is making its best efforts to keep the concession area clean, so that we are asking for your help to penalize the citizens who throw out garbage in the streets creating black spots throughout the concession area."

64. Thus after September 1996, Banobras could argue that—quite apart from the non-replenishment of the Line of Credit—the City's non-payment of Acaverde's invoices was not the result of the City's financial crisis. Arguably it arose from a dispute between Acaverde and the City over the performance of the Concession Agreement, a dispute which Banobras had no obligation to settle. Whether that position was justified

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<sup>18</sup> Witness statement of Mr. Rogelio Moreno Jarquín, 4 December 2002, para. 8 (emphasis added).

under the Line of Credit Agreement was a question—but at any rate it might help to extricate Banobras from its awkward situation as between Acaverde on one hand and the City on the other.

65. In a letter to the City of 15 November 1996, Banobras defended its payment of NP4.9 million in June on the ground that it was fully justified under the Concession Agreement, and it referred to Acaverde's subsequent demands for payment under the Line of Credit up to September 1996, implying that they might require similar treatment. But in fact it continued to refuse to pay Acaverde's invoices, and it did not seek to have resort to federal funds in Guerrero's hands.

66. By early 1997 the Claimant was seeking to withdraw from Acapulco and to sell its business. On 27 February 1997 Sanifill, principal shareholder of Acaverde's holding company, entered into a 60 day letter of intent with a Mexican company, Setasa, allowing the latter access to Acaverde's financial and operating information on a basis of confidentiality in order to assess the price. Subsequently, on 23 May 1997, a contingent sale agreement was concluded with a price of NP36.6 million (approximately equivalent to US\$4.7 million at the then current exchange rate). In June 1997, however, Sanifill discovered that Setasa was in direct communication with the City, and eventually the sale did not proceed.

67. On 9 October 1997, Hurricane Paulina struck the Acapulco region, causing hundreds of deaths and enormous destruction.

68. By letter of 27 October 1997—with unhappy timing given that the City was still reeling from the hurricane—Acaverde announced that with effect from 12 November 1997 it would suspend the provision of services under the Agreement. The tasks it had performed were immediately assumed by Setasa,<sup>19</sup> which contracted with the City rather than with individual residents.

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<sup>19</sup> In accordance with a request of the City to Setasa, 12 November 1997.

69. Over the 27 months of Acaverde's operations, its invoices to the City totalled more than NP49 million, of which the City itself paid NP2,225,000 and Banobras paid NP4.9 million. Approximately 80% of the total amount invoiced went unpaid.

70. Acaverde brought two sets of proceedings before the Mexican federal courts against Banobras for non-performance of the Line of Credit Agreement. These proceedings were dismissed and Acaverde's appeals were likewise dismissed. Acaverde also commenced arbitration under Clause 17 of the Concession Agreement against the City ("the CANACO arbitration"); this was subsequently discontinued. The domestic Mexican proceedings are examined in detail in paragraphs 118-132 below.

71. On 29 September 1998, while the Mexican proceedings were still pending, Waste Management commenced the first ICSID arbitration, referred to in paragraph 4 above. Indeed it was because those proceedings were pending, and because further proceedings were possible, that Waste Management qualified the terms of its waiver under Article 1121, leading to the dismissal of its claim by the First Tribunal. The present ICSID proceedings were registered on 27 September 2000, by which time Acaverde's claims in the Mexican courts had all been dismissed and the CANACO arbitration had been discontinued without any decision being reached.

72. Despite these developments, Claimant brought precisely the same claim before the present Tribunal as it had in the first ICSID arbitration. In other words, it did not express its claim in terms of a denial of justice through the subsequent Mexican proceedings. By agreement, Claimant's Memorial in the first proceedings was taken to constitute its Memorial in the present proceedings. Nonetheless, and in the Tribunal's view inevitably, attention was paid both to the outcome and to the reasoning behind the Mexican court decisions, as well as to the reasons for Claimant's withdrawal of the domestic arbitration, having regard to their potential relevance to the claim brought under NAFTA Chapter 11 to this Tribunal. In the circumstances the Tribunal proposes to ask whether the facts as disclosed to it involved a breach of NAFTA Articles 1105 or 1110, even though the position may not have been fully captured in Claimant's re-filed Memorial.

## C. THE BASES OF CLAIM UNDER NAFTA

### (1) Overview

73. The Tribunal begins by observing that—unlike many bilateral and regional investment treaties—NAFTA Chapter 11 does not give jurisdiction in respect of breaches of investment contracts such as the Concession Agreement. Nor does it contain an “umbrella clause” committing the host State to comply with its contractual commitments. This does not mean that the Tribunal lacks jurisdiction to take note of or interpret the contract. But such jurisdiction is incidental in character, and it is always necessary for a claimant to assert as its cause of action a claim founded in one of the substantive provisions of NAFTA referred to in Articles 1116 and 1117. Furthermore, while conduct (e.g. an expropriation) may at the same time involve a breach of NAFTA standards and a breach of contract, the two categories are distinct. Even as to Article 1105, while it will be relevant to show that particular conduct of the host State contradicted agreements or understandings reached at the time of the entry of the investment, it is still necessary to prove that this conduct was a breach of the substantive standards embodied in Article 1105. Showing that it was a breach of contract is not enough.<sup>20</sup>

74. The Claimant alleged that the circumstances outlined above disclosed a breach by the Respondent of its duties to United States investors under NAFTA Article 1110 or alternatively under Article 1105(1). It put its damages at more than US\$36,000,000. In addition it sought to recover its demobilization costs resulting from the revocation of the Concession Agreement, which were estimated at US\$630,000. It also sought an award of legal costs.

75. The Respondent did not deny that for the purposes of Chapter 11 of NAFTA the conduct of the City of Acapulco and the State of Guerrero was attributable to it. More difficult issues arise with respect to the conduct of Banobras, which is a development bank partly-owned and substantially controlled by Mexican government agencies. Banobras’ general objective, in the words of the regional director of Banobras

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<sup>20</sup> See further *Compañía de Aguas del Aconquija S.A. & Vivendi Universal v. Argentine Republic* (ICSID Case No. ARB/97/3), Decision on Annulment, (2002) 6 ICSID Reports 340, 365-7 (paras. 95-101), cited with approval by the Tribunal in *SGS Société Générale de Surveillance S.A. v. Islamic Republic of Pakistan*, (ICSID Case No. ARB/01/13), decision of 6 August 2003, (2003) 18 ICSID Rev.-FILJ 307, 352-6 (paras. 147-8). See also *Azinian, Davittian & Baca v. United Mexican States* (ICSID Case No. ARB(AF)/97/2), (1998) 5 ICSID Reports 269, 286 (paras. 81, 83).

in Guerrero, is “to promote and finance activities carried out by the Federal, State, and Municipal Governments of the Country”.<sup>21</sup> From the material available to the Tribunal it is doubtful whether Banobras is an organ of the Mexican State within the meaning of Article 4 of the ILC’s Articles on Responsibility of States for Internationally Wrongful Acts.<sup>22</sup> Shares in Banobras were divided between the public and private sector, with the former holding a minimum of 66%. The mere fact that a separate entity is majority-owned or substantially controlled by the state does not make it *ipso facto* an organ of the state. Nor is it clear that in its dealings with the City and the State in terms of the Line of Credit it was exercising governmental authority within the meaning of Article 5 of those Articles.<sup>23</sup> The Organic Law of 1986 regulating Banobras’ activity confers on it a variety of functions, some clearly public, others less so. A further possibility is that Banobras, though not an organ of Mexico, was acting “under the direction or control of” Guerrero or of the City in refusing to pay Acaverde under the Agreement.<sup>24</sup> again, it is far from clear from the evidence that this was so.<sup>25</sup> For the purposes of the present Award, however, it will be assumed that one way or another the conduct of Banobras was attributable to Mexico for NAFTA purposes.

76. Mexico’s legal defence involved three strands. First, it denied that the Claimant had the status of an investor for the purposes of Chapter 11 on the grounds that the Claimant did not have a direct interest in the investment in Mexico, because Acaverde’s direct shareholder was a company registered in the Cayman Islands, not a NAFTA Party. Secondly, while not denying that there may have been breaches of the Concession Agreement by the City, Mexico denied that these breaches, individually or collectively, rose to the level of conduct in violation of NAFTA Article 1105. Thirdly, it denied that there had been any expropriation, direct or indirect, of the investment, i.e., of Acaverde’s business, contrary to NAFTA Article 1110. The Tribunal will discuss the

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<sup>21</sup> Statement of Mr. Mario Alcaraz Alarcón, para. 3.

<sup>22</sup> Annexed to GA Res. 56/83, 12 December 2001.

<sup>23</sup> The ILC’s commentary describes the notion of a “para-statal” entity as a narrow category: the essential requirement is that the entity must be “empowered by the law of the State to exercise functions of a public character normally exercised by State organs, and the conduct of the entity [which is the subject of the complaint] relates to the exercise of the governmental authority concerned”: Commentary to Article 5, paras. 2 and 7, reproduced in J Crawford, *The International Law Commission’s Articles on State Responsibility* (Cambridge, 2002) 100, 102.

<sup>24</sup> ILC Articles, Art. 8; see the commentary, esp. para. 6, in Crawford, 112-113.

<sup>25</sup> See below, paras. 103, 139 for the Tribunal’s findings on this point.

legal issues in turn, dealing with the facts (and with any factual disputes) as far as necessary for the purpose.

**(2) The status of the Claimant as an “investor”**

77. At the time it was incorporated, Acaverde was owned, through a holding company called AcaVerde Holdings Ltd, by Sun Investment Co., a Cayman Islands company. AcaVerde Holdings Ltd., also a Cayman Islands company, was purchased by Sanifill Inc., a U.S. company (“Sanifill”), at about the time the City initially approved the concession. The sale agreement of 21 December 1994 was contingent upon conclusion of the Concession Agreement and the Line of Credit Agreement. In fact the sale was completed on 27 June 1995. The price paid, in instalments, was US\$5 million, plus the right to certain royalties based on Acaverde’s operations. Subsequently, in August 1996, Sanifill merged with USA Waste Services Inc.; the merged company later adopted the name Waste Management Inc.

78. A number of witnesses presented by the Respondent asserted that the City was not aware at the time the Concession Agreement was negotiated that Acaverde was not owned by Sanifill. The Claimant’s witnesses asserted that they had informed the City of this fact. The Tribunal does not need to resolve the discrepancy. Although the City may not have been aware of the specific financial arrangements between Sun Investments and Sanifill, it was certainly aware that United States interests were involved in the proposed arrangement,<sup>26</sup> as was reported in the local press at the time.<sup>27</sup> The Concession Agreement was signed by Mr. Proto, a senior employee of Sanifill, under a power of attorney granted by Acaverde. As noted, the actual purchase of Acaverde’s stock was contingent upon the conclusion of the Line of Credit Agreement, without which the project would not have gone ahead. By the time Acaverde commenced operations on 15 August 1995, almost all its shares were owned, through Cayman Islands companies, by Sanifill.<sup>28</sup>

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<sup>26</sup> Mr. Walton, transcript, 7 April 2003, 233.

<sup>27</sup> *Novedades* (Acapulco), 30 October 1994, identifying Sanifill Inc. as the prospective concessionaire.

<sup>28</sup> On 30 November 1995, a merger agreement left Sanifill de Mexico, S.A. de C.V., a Mexican company, as the sole successor of the various intermediate holding companies of Acaverde, the ultimate controlling interest of which was in Sanifill.

79. In any event there is no general requirement of *mens rea* or intent in Section A of Chapter 11. The standards are in principle objective: if an investor suffers loss or damage by reason of conduct which amounts to a breach of Articles 1105 or 1110, it is no defence for the Respondent State to argue that it was not aware of the investor's identity or national character. The only question is whether the various requirements of Chapter 11 in this regard are satisfied.

80. Chapter 11 of NAFTA spells out in detail and with evident care the conditions for commencing arbitrations under its provisions. In particular it distinguishes between claims brought by an investor of another Party in its own right and claims brought by an investor on behalf of a local enterprise. The relevant provisions cover the full range of possibilities, including direct and indirect control and ownership. They deal with possible "protection shopping", i.e. with situations where the substantial control or ownership of an enterprise of a Party lies with an investor of a non-party and the enterprise "has no substantial business activities in the territory of the Party under whose law it is constituted or organized".<sup>29</sup> In other words NAFTA addresses situations where the investor is simply an intermediary for interests substantially foreign, and it allows NAFTA protections to be withdrawn in such cases (subject to prior notification and consultation). There is no hint of any concern that investments are held through companies or enterprises of non-NAFTA States, if the beneficial ownership at relevant times is with a NAFTA investor.

81. The scope of protection, and the care with which the relevant provisions were drafted, can be seen from the definitions in Articles 201 and 1139. In accordance with Article 201:

**"enterprise** means any entity constituted or organized under applicable law, whether or not for profit, and whether privately-owned or governmentally-owned, including any corporation, trust, partnership, sole proprietorship, joint venture or other association;

**enterprise of a Party** means an enterprise constituted or organized under the law of a Party;"

Plainly the term "enterprise" includes corporations established under the law of a third State.

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<sup>29</sup> NAFTA, Article 1113(2).

82. Then under Article 1139, which defines certain terms for the purposes of Chapter 11, further definitions are relevant:

“**investment** means:

- (a) an enterprise;
- ...
- (e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise;
- ...

**investment of an investor of a Party** means an investment owned or controlled directly or indirectly by an investor of such Party”.

83. Of course these are only definitions, but they are used consistently in the substantive provisions of Section A of Chapter 11 and in the remedial provisions of Section B. Article 1101 specifies the scope and coverage of Chapter 11:

“1. This Chapter applies to measures adopted or maintained by a Party relating to:

- (a) investors of another Party;
- (b) investments of investors of another Party in the territory of the Party; and
- (c) with respect to Articles 1106 and 1114, all investments in the territory of the Party.”

Thus when Article 1105 specifies the treatment to be accorded to investments of investors of another Party, there is no trace of a requirement that the investment itself have the nationality of that Party either at the time it was acquired or at the time the conduct complained of occurs. Similarly under Article 1110 dealing with expropriation, the protected quantity is “an investment of an investor of another Party” in the territory of the expropriating State. The nationality of the investment (as opposed to that of the investor) is irrelevant. The same is true in respect of claims by investors on their own behalf under Article 1116: it is sufficient that the investor has the nationality of a Party and has suffered loss or damage as a result of action in breach of one of the specified obligations, including Articles 1105 and 1110. The extent of that loss or damage is a matter of quantum, not jurisdiction.

84. Article 1117 deals with the special situation of claims brought by investors on behalf of enterprises established in the host State. But it still allows such claims where

the enterprise is owned or controlled “directly or indirectly”, i.e., through an intermediate holding company which has the nationality of a third State.

85. Where a treaty spells out in detail and with precision the requirements for maintaining a claim, there is no room for implying into the treaty additional requirements, whether based on alleged requirements of general international law in the field of diplomatic protection or otherwise. If the NAFTA Parties had wished to limit their obligations of conduct to enterprises or investments having the nationality of one of the other Parties they could have done so. Similarly they could have restricted claims of loss or damage by reference to the nationality of the corporation which itself suffered direct injury. No such restrictions appear in the text. It is not disputed that at the time the actions said to amount to a breach of NAFTA occurred, Acaverde was an enterprise owned or controlled indirectly by the Claimant, an investor of the United States. The nationality of any intermediate holding companies is irrelevant to the present claim. Thus the first of the Respondent’s arguments must be rejected.

### **(3) The claim for breach of NAFTA Article 1105**

86. The Tribunal turns to the claim for breach of Article 1105(1). This was not the primary basis of claim. Rather the Claimant argued that Article 1105 “provides an alternative and overlapping basis for recovery by Waste Management”, alongside its claim for expropriation under Article 1110.<sup>30</sup> Nonetheless it was an autonomous basis of claim, and it is convenient to deal with it first, before turning to Article 1110.

87. According to the Claimant, the investment was subject to arbitrary acts by the City, Guerrero and Banobras which were capricious, lacking in due process of law and which rendered the investment valueless.<sup>31</sup> Furthermore Acaverde was subjected to a denial of justice at the hands of the City, Guerrero and Banobras, which conspired to obstruct its access to judicial and arbitral forums to resolve claims under the concession: more specifically, these entities “funnelled” the litigation by raising procedural issues to

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<sup>30</sup> Memorial, para. 5.43.

<sup>31</sup> Reply, paras. 4.32-4.33.

delay the merits claims and deny Acaverde the opportunity to obtain timely payment from Banobras, aggravating its bad financial position.<sup>32</sup>

88. In assessing these arguments it is necessary to consider first the interpretation to be given to Article 1105(1), then its application to the facts of the present case.

(i) *The scope and interpretation of Article 1105(1)*

89. Article 1105 is entitled “Minimum Standard of Treatment”. The relevant provision here is paragraph 1, which provides as follows:

“(1) Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security.”

90. On 31 July 2001, the Free Trade Commission, acting under NAFTA Article 1131, issued the following interpretation of Article 1105(1):

“B. Minimum Standard of Treatment in Accordance with  
International Law

1. Article 1105(1) prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to investments of investors of another Party.

2. The concepts of ‘fair and equitable treatment’ and ‘full protection and security’ do not require treatment in addition to or beyond that which is required by the customary international law minimum standard of treatment of aliens.

3. A determination that there has been a breach of another provision of the NAFTA, or of a separate international agreement, does not establish that there has been a breach of Article 1105(1).”

91. The FTC’s interpretation has been extensively discussed in subsequent decisions, in particular the *Mondev*<sup>33</sup> and *ADF* cases.<sup>34</sup> The *Mondev* tribunal found that the FTC interpretation:

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<sup>32</sup> Reply, paras. 4.32, 4.39-4.40.

<sup>33</sup> *Mondev International Limited v. United States of America*, Award of 11 October 2002, 6 ICSID Reports 192.

<sup>34</sup> *ADF Group Inc. v. United States of America*, Award of 9 January 2003, 6 ICSID Reports 470.

- resolves any dispute about whether there was such a thing as a minimum standard of treatment of investment in international law in the affirmative;<sup>35</sup>
- makes clear that the standard of treatment is to be found by reference to international law;<sup>36</sup>
- clarifies that Article 1105 refers to a standard existing under customary law, not standards under other treaties of the NAFTA Parties or other provisions within NAFTA;<sup>37</sup>
- clarifies that the terms “fair and equitable treatment” and “full protection and security” are references to existing elements of customary international law and are not “additive”, that is, they do not add novel elements to that standard;<sup>38</sup> and
- incorporates current international customary law, at least as it stood at the time that NAFTA came into force in 1994, rather than any earlier version of the standard of treatment.<sup>39</sup>

92. This last point was expanded by the tribunal in *ADF*: it recorded the view of the United States, accepted by Canada and Mexico, that the customary international law in Article 1105(1) is not static and that the minimum standard of treatment does evolve, going onto say that “both customary international law and the minimum standard of treatment of aliens it incorporates, are constantly in a process of development.”<sup>40</sup>

93. Both the *Mondev* and *ADF* tribunals rejected any suggestion that the standard of treatment of a foreign investment set by NAFTA is confined to the kind of outrageous treatment referred to in the *Neer* case, i.e. to treatment amounting to an “outrage, to bad faith, to wilful neglect of duty, or to an insufficiency of governmental

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<sup>35</sup> *Mondev International Limited v. United States of America*, Award of 11 October 2002, 6 ICSID Reports 192, 216 (para. 98), 223 (para. 120). See also *ADF*, 527 (para. 178).

<sup>36</sup> *Mondev International Limited v. United States of America*, 216 (para. 98).

<sup>37</sup> *Ibid.*, 223 (para. 121).

<sup>38</sup> *Ibid.*, 223 (para. 122).

<sup>39</sup> *Ibid.*, 224 (para. 125).

<sup>40</sup> *ADF Group Inc. v. United States of America*, Award of 9 January 2003, 6 ICSID Reports 470, 527-8 (para. 179).

action so far short of international standards that every reasonable and impartial man would readily recognize its insufficiency”<sup>41</sup>.

94. The discussion of Article 1105 by the tribunal in *S.D. Myers*, even though before the FTC interpretation, may also be noted. The tribunal considered that a breach of Article 1105 occurs

“only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders. The determination must also take into account any specific rules of international law that are applicable to the case.”<sup>42</sup>

95. In the context of denial of justice arising from decisions of domestic courts, the *Mondev* tribunal formulated the test of the applicable “customary international law minimum standard” under Article 1105(1) in the following terms:

“The test is not whether a particular result is surprising, but whether the shock or surprise occasioned to an impartial tribunal leads, on reflection, to justified concerns as to the judicial propriety of the outcome, bearing in mind on the one hand that international tribunals are not courts of appeal, and on the other hand that Chapter 11 of NAFTA (like other treaties for the protection of investments) is intended to provide a real measure of protection. In the end the question is whether, at an international level and having regard to generally accepted standards of the administration of justice, a tribunal can conclude in the light of all the available facts that the impugned decision was clearly improper and discreditable, with the result that the investment has been subjected to unfair and inequitable treatment.”<sup>43</sup>

96. The *ADF* tribunal, citing *Mondev v. United States*, said of Article 1105 as interpreted by the FTC<sup>44</sup> that “any general requirement to accord ‘fair and equitable treatment’ and ‘full protection and security’ must be disciplined by being based on State

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<sup>41</sup> *USA (L.F. Neer) v. United Mexican States*, 1927, AJIL 555, at 556, cited in *Mondev*, 221 (para. 114).

<sup>42</sup> *S.D. Myers, Inc. v. Government of Canada*, Partial Award, 13 November 2000, para. 263. The majority (Arbitrator Chiasson dissenting) considered that the facts which supported a finding of breach of Article 1102 also established a breach of Article 1105, para. 266.

<sup>43</sup> *Mondev v. United States*, 225-6 (para. 127).

<sup>44</sup> *Ibid.*, 528-31 (paras. 180, 183-4).

practice and judicial or arbitral caselaw or other sources of customary or general international law.”<sup>45</sup> Considering the “general customary international law standard of treatment”, the Tribunal found that:

- the argument that the government procurement provisions were unfair was unconvincing. Performance requirements in governmental procurement were common to all three NAFTA Parties as well as to other States. Thus “the US measures cannot be characterized as idiosyncratic or aberrant and arbitrary”;<sup>46</sup>
- the actions of a government authority in refusing to follow and apply earlier case-law was not in the circumstances of the case “grossly unfair or unreasonable”, nor were ADF’s assumptions about the applicability of that case-law induced by the misrepresentations by authorised officials of government;<sup>47</sup>
- the government agency in question had not acted *ultra vires*, but, in any case, showing an act is *ultra vires* under the internal law of a state “by itself does not necessarily render the measures grossly unfair or inequitable under the customary international law standard of treatment embodied in Article 1105(1)... something more than simple illegality or lack of authority under the domestic law of a State is necessary”;<sup>48</sup>
- the investor’s claim that the United States had breached its duty under customary international law to perform its obligations in good faith in breach of Article 1105 added “only negligible assistance in the task of determining or giving content to a standard of fair and equitable treatment.”<sup>49</sup> However the Tribunal noted in this respect that the investor had not tried to show government actions refusing the request for a waiver of the procurement requirements were “flawed by arbitrariness”. There was no evidence that other companies had been granted the same waivers. The investor did not allege that the contract specifications were tailored so that only a specific US company could comply; nor did the investor show that extraordinary costs or other burdens had been imposed that were not also imposed on other contractors involved in the same project.

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<sup>45</sup> Ibid., 531 (para. 184).

<sup>46</sup> Ibid., 531 (para. 188).

<sup>47</sup> Ibid., 531-2 (para. 189).

<sup>48</sup> Ibid., 532-3 (para. 190).

<sup>49</sup> Ibid., 533 (para. 191).

97. The content of Article 1105 in light of the FTC interpretation was also discussed in *Loewen v. United States* in the specific context of denial of justice.<sup>50</sup> The tribunal said:

“Neither State practice, the decisions of international tribunals nor the opinion of commentators support the view that bad faith or malicious intention is an essential element of unfair and inequitable treatment or denial of justice amounting to a breach of international justice. Manifest injustice in the sense of a lack of due process leading to an outcome which offends a sense of judicial propriety is enough, even if one applies the Interpretation according to its terms.”<sup>51</sup>

The *Loewen* Tribunal also noted that discriminatory violations of municipal law would amount to a manifest injustice according to international law.<sup>52</sup> However, the tribunal held that, where the minimum standards of international law in question in a particular case are raised in respect of a claim of judicial action—that is, a denial of justice—what matters is the *system* of justice and not any individual decision in the course of proceedings. The system must be tried and have failed, and thus in this context the notion of exhaustion of local remedies is incorporated into the substantive standard and is not only a procedural prerequisite to an international claim.<sup>53</sup> For this reason, although the *Loewen* tribunal found that the first instance trial and its verdict were “clearly improper and discreditable” and a breach of the minimum standards of fair and equitable treatment, that did not dispose of the case.<sup>54</sup>

98. The search here is for the Article 1105 standard of review, and it is not necessary to consider the specific results reached in the cases discussed above. But as this survey shows, despite certain differences of emphasis a general standard for Article 1105 is emerging. Taken together, the *S.D. Myers*, *Mondev*, *ADF* and *Loewen* cases suggest that the minimum standard of treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary,

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<sup>50</sup> *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, Award of 26 June 2003 (Case No. ARB(AF)/98/3). For the Tribunal’s discussion of the Article 1105 and the FTC interpretation see *ibid.*, paras. 124-8.

<sup>51</sup> *Ibid.*, para. 132.

<sup>52</sup> *Ibid.*, para. 135.

<sup>53</sup> *Ibid.*, para. 168.

<sup>54</sup> *Ibid.*, para. 137.

grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety—as might be the case with a manifest failure of natural justice in judicial proceedings or a complete lack of transparency and candour in an administrative process. In applying this standard it is relevant that the treatment is in breach of representations made by the host State which were reasonably relied on by the claimant.

99. Evidently the standard is to some extent a flexible one which must be adapted to the circumstances of each case. Accordingly it is to the facts of the present case that the Tribunal turns.

(ii) *The allegations of breach of Article 1105(1)*

100. The Claimant asserted that the failure of Acaverde's enterprise arose from a combination of conduct of local, provincial and federal authorities, together with the failure of Mexican courts and tribunals to provide it any relief. In the first place the Tribunal will consider separately the conduct of each of the various Mexican authorities concerned. Subsequently it will deal with the claim that there was collusion or conspiracy between these authorities.

101. Before turning to the specific facts, the Tribunal notes that an important part of the background to the case was the Mexican financial crisis, which started in December 1994 with a substantial devaluation of the currency and continued for several years. During that period the value of the peso was approximately halved, the rate of inflation reached 38%, and federal revenues to the States and municipalities were greatly affected.<sup>55</sup> The effects on the City were numerous: tourist numbers declined, its financial obligations under the Concession Agreement (which were indexed to inflation) were substantially increased<sup>56</sup> and the federal revenues it received were substantially reduced.

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<sup>55</sup> See William A. Lovett, "Lessons from the Recent Peso Crisis in Mexico", (1996) 4 *Tulane JICL* 143.

<sup>56</sup> The monthly fee increased from NP1 million to NP1.6 million in January 1996.

(a) The conduct of Banobras

102. The only executive entity at federal level of whose conduct Waste Management complained was the development bank, Banobras.<sup>57</sup> Assuming, for the sake of argument, that Banobras' conduct was attributable to Mexico for NAFTA purposes (see above, paragraph 75), nonetheless the Tribunal finds that it did not constitute a breach of Article 1105. Prior to the conclusion of the Line of Credit Agreement in June 1995, Banobras, which had not been a party to the initial negotiations for the Concession Agreement, was in no way obliged to grant the line of credit. Its regional director explained that "lines of credit... guaranteed by the share of the States and Municipalities in federal tax revenue" were not common; in Guerrero, this was the only example and would not be repeated.<sup>58</sup> When it was approached by the City to grant the line of credit, Banobras insisted on various changes to the Concession Agreement. It was within its rights to do so, and the changes were accepted, albeit reluctantly, by Acaverde as a condition of its investment. Whatever hopes Acaverde may have entertained of having a significant part of its income guaranteed by the federal development bank, the fact is that the eventual guarantee was a more limited one, expressed to cover "temporary liquidity problems which the City of Acapulco might experience". On its face it "was not an alternative source [or] mechanism... for the regular payment, to Acaverde, of monthly payments for its services".<sup>59</sup> It was also limited in amount to NP6 million. In other words, it does not appear that Banobras had any obligation to make payments to Acaverde beyond that figure, unless the line of credit was replenished by the City or Banobras was able to divert federal funds in Guerrero's hands in order to replenish the line of credit.

103. It is not necessary for the Tribunal to determine whether, after the Line of Credit Agreement had been concluded, Banobras in all respects complied with its terms. The Agreement provided its own mechanism for determining that question. But it is clear that Banobras did comply at least to some extent, making payments to Acaverde totalling nearly NP5 million. It appears that this amount had not been reimbursed to Banobras by the City at the time Acaverde withdrew from providing services in October 1997. At the same time Banobras discussed with the parties possible changes to their arrangements

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<sup>57</sup> See e.g., Claimant's Memorial, para. 1.1.

<sup>58</sup> Statement of Mr. Mario Alcaraz Alarcón, para. 4.

<sup>59</sup> Ibid., para. 7.

which might be sustainable given the sharp drop in federal revenues to Guerrero and the City and the underlying crisis in public finances. Its role here was that of a concerned intermediary, and the failure of those discussions was not its fault.<sup>60</sup>

104. For these reasons, the Tribunal rejects the claim that Mexico was in breach of Article 1105(1) by reason of the conduct of Banobras.

105. There is a separate issue whether the Mexican courts denied justice to the Claimant through their decisions in the cases brought against Banobras. This is discussed in paragraphs 118-132 below.

(b) The conduct of Guerrero

106. Representatives of the State of Guerrero attended a number of meetings discussing a settlement of the problem, for example in June 1996. According to one witness, State officials offered help with payments to avoid drawing on the line of credit. But the City was unable to pay the share envisaged by these proposals, and the discussions did not reach any conclusion.<sup>61</sup>

107. Although the Claimant asserted that representatives of Guerrero were implicated in the continuing breach of the Concession Agreement, Guerrero was neither a party to the Agreement nor a guarantor. This situation was not affected by the legal requirement that the legislature of Guerrero approve the Concession Agreement, which it did on 15 December 1994. Overall the Tribunal has not been provided with any evidence that supports any specific charge against Guerrero in terms of Article 1105(1) of NAFTA.

(c) The conduct of the City

108. The position with respect to the City is more complex, and there is certainly a case to answer with respect to Article 1105(1).

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<sup>60</sup> See e.g. the letter from the State Representative, Mr. Alcaraz Alarcón to his superior in the Banobras head office, 10 October 1996.

<sup>61</sup> Second Statement of Mr. Alcaraz Alarcón, paras. 4-5.

109. On the information before the Tribunal it is clear that the City failed in a number of respects to fulfil its contractual obligations to Claimant under the Concession Agreement. It did so, most obviously, with respect to the monthly payments, which immediately fell into arrears. In addition Acaverde credibly alleged breaches of the agreement, for example with respect to inadequate enforcement of the 1995 Ordinance and the provision of land for the proposed permanent waste disposal site.

110. On the other hand there are a number of countervailing factors. The City did make at least some attempts to enforce the 1995 Ordinance. It defended proceedings brought against it by local residents challenging the Concession Agreement and the 1995 Ordinance. It made at least some attempts to encourage local residents and business groups to contract with Acaverde. Contrary to the Claimant's allegations, it did bring at least some proceedings against the "pirates" and even against its own employees caught moonlighting in the concession area. It made at least some attempts, through the deployment of inspectors, to enforce the Cleaning Services Ordinance. And some steps were taken, in conjunction with Acaverde, to identify a location for the permanent waste disposal site and to obtain secure title over it. For example, the City brought non-contentious proceedings before an Agrarian Court in Guerrero to give an agreement made with the holders of customary title over the land the status of an order of the Court; on 8 April 1996 the Court granted the order accordingly.<sup>62</sup>

111. Against this background of breaches of contract and allegations of non-performance, two facts are evident. The first is that the Concession Agreement was unpopular with a significant proportion of the residents of the concession area, many of whom were not permanently resident in Acapulco but maintained holiday apartments there. Even the permanent residents were not used to paying separately for waste disposal services. Moreover this problem—acknowledged as a potential difficulty by the Claimant from the outset—was exacerbated by the initial, rather heavy-handed approach of the Claimant in issuing immediate invoices to all area residents, accompanied by threats of legal action in the event of non-payment. As the Tribunal has noted (see paragraph 44 above), the obligation to pay for waste collection services was contingent upon the conclusion of a service agreement, and did not arise under the Cleaning Services

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<sup>62</sup> The land in question was *ejido* land (a form of customary or communal title). The agreement of 5 August 1995 conferred rights of exclusive use of 56 hectares of land for 25 years for use as a sanitary landfill by Acaverde.

Ordinance itself. The Claimant's apparent assumption to the contrary at the early stages of the introduction of the Concession stirred up substantial opposition, leading to public protests and a series of *amparo* actions against the City by residents and business groups. The City defended these actions, not always successfully; for example, confiscated vehicles belonging to several "pirate" collectors had to be released. At least some of the cases of non-compliance with the Concession Agreement of which Claimant complains were the result of these cases and of interim or final orders obtained against the City.

112. The second fact is that the financial plans of the City, and thus of the Claimant, were severely affected by the Mexican financial crisis, which lasted well into 1996 and severely affected the City's capacity to perform its obligations. The City was reduced to offering certain land holdings either to Acaverde in lieu of payment or to Banobras as security for extension of the line of credit.<sup>63</sup> Understandably, neither of them was prepared to accept this, but it is further evidence of the reality of severe financial difficulties.

113. The Tribunal notes that Acaverde itself responded to these early setbacks. It sought to persuade its potential customers to enter into contracts, so that by the end of the period of operations rather more than 50% of residents and enterprises had done so, although in many cases it was necessary to offer substantial discounts (up to 40-50%) on the published rates. It addressed operational complaints and difficulties. It showed flexibility in discussions with the City on a range of matters.<sup>64</sup> It took the initiative in creating a temporary land-fill which appears to have complied with applicable standards, unlike the two existing land-fills.<sup>65</sup> But the fact remains that the weaknesses of the original business plan could not be overcome at a time of financial stringency.

114. The Tribunal does not suggest that financial stringency or public resistance are, as such, excuses for breaches of contractual commitments on the part of a municipality. But NAFTA Chapter 11 is not a forum for the resolution of contractual disputes, and as investment tribunals have repeatedly said, "Investment Treaties are not

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<sup>63</sup> See Mayor Almazán's letter to Banobras, 26 August 1996 and the reply of 4 September 1996.

<sup>64</sup> E.g., letter of Mr. Proto to the Secretary-General of the City, 24 April 1996.

<sup>65</sup> Statement of Mr. D. Harich, paras. 4, 10.

insurance policies against bad business judgments”.<sup>66</sup> The question is whether, having regard to the conduct of the parties concerned and the general circumstances, losses were caused to Waste Management by the City in circumstances amounting to a breach of the minimum standard of treatment embodied in Article 1105, a standard which the Tribunal has summarised in paragraph 98 above.

115. In the Tribunal’s view the evidence before it does not support the conclusion that the City acted in a wholly arbitrary way or in a way that was grossly unfair. It performed part of its contractual obligations, but it was in a situation of genuine difficulty, for the reasons explained above. It sought alternative solutions to the problems both parties faced, without finding them. The most important default was its failure to pay; the Tribunal will discuss in a subsequent section whether such failure, persisted in, could have amounted to a breach of NAFTA Article 1110 because it was tantamount to expropriation, either of the enterprise as a whole or at least of the sums remaining unpaid.<sup>67</sup> For present purposes it is sufficient to say that even the persistent non-payment of debts by a municipality is not to be equated with a violation of Article 1105, provided that it does not amount to an outright and unjustified repudiation of the transaction and provided that some remedy is open to the creditor to address the problem. In the present case the failure to pay can be explained, albeit not excused, by the financial crisis which meant that at key points the City could hardly pay its own payroll. There is no evidence that it was motivated by sectoral or local prejudice.

116. The importance of a remedy, agreed on between the parties, for breaches of the Concession Agreement bears emphasis.<sup>68</sup> It is true that in a general sense the exhaustion of local remedies is a procedural prerequisite for the bringing of an international claim, one which is dispensed with by NAFTA Chapter 11. But the availability of local remedies to an investor faced with contractual breaches is nonetheless relevant to the question whether a standard such as Article 1105(1) have been complied with by the State. Were it not so, Chapter 11 would become a mechanism of equal resort

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<sup>66</sup> *Maffezini v. Spain*, Award, 13 November 2000, 5 ICSID Reports 419, 432 (para. 64), cited in para. 29 of *CMS Gas Transmission Company v. Argentina*, Decision of the Tribunal on Objections to Jurisdiction, 17 July 2003, 42 ILM 788 (2003). See also *Eudoro A. Olguín v. Republic of Paraguay*, ICSID Case No. ARB/98/5, Award, 26 July 2001, 6 ICSID Reports 164, paras. 72-75.

<sup>67</sup> See below, paras. 155-176.

<sup>68</sup> For the terms of Article 17 of the Concession Agreement see para. 53 above.

for debt collection and analogous purposes in respect of all public (including municipal) contracts, which does not seem to be its purpose.

117. For these reasons the Tribunal is not satisfied that the City's breaches of contract rose to the level of breaches of Article 1105(1) of NAFTA.

(d) The Mexican legal proceedings

118. But even if the conduct of the City or Banobras in itself did not violate the Article 1105 standard, the question remains whether the situation presented by their conduct was adequately responded to by the Mexican courts. Both the Concession Agreement and the Line of Credit Agreement made provision for dispute settlement, referring to local arbitration and proceedings before the federal courts of Mexico City respectively. The Claimant tried both avenues, eventually discontinuing the arbitration proceedings and failing in the federal court. It is thus necessary to ask to what extent the decisions of the federal courts or of CANACO either compounded the situation, or constituted a distinct denial of justice, so as to entail a breach of Article 1105(1).<sup>69</sup>

119. Before turning to the relevant legal principles, the course of the three proceedings needs to be described in more detail.

*The arbitration proceedings*

120. By notice of 3 December 1997, Acaverde notified the City that it was commencing arbitration proceedings under Article 17 of the Concession Agreement. On 9 January 1998 the Permanent Commission of Commercial Arbitration of the National Chamber of Commerce (CANACO) was notified. On 4 March 1998 the City objected to the Claimant's notice on procedural grounds, but it subsequently appointed its arbitrator after CANACO had threatened to make a default appointment if it did not. The two party-appointed arbitrators having failed to agree, on 8 September 1998 CANACO was requested to appoint a Chairman of the Tribunal, which it did. On 25 November 1998 the City objected to the jurisdiction of the Tribunal on the ground, *inter alia*, that the Concession Agreement was an administrative act governed by public law and therefore

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<sup>69</sup> Cf. *Azinian, Davitian & Baca v. United Mexican States*, Award of 1 November 1999, 5 ICSID Reports 269, 289 (para. 97).

necessarily subject to the jurisdiction of the contentious administrative courts; it also denied the Claimant's case on the merits.

121. Subsequently the City commenced court proceedings seeking to block the arbitration, using the same arguments.

122. In the light of the City's resistance to the arbitration, CANACO requested an advance of payment of NP2.5 million from each party as a condition of continuing the arbitration. (At then-current exchange rates this was equivalent to approximately US\$275,000.) The City refused to pay this amount, and thus if the arbitration was to proceed it would have had to be wholly funded by Acaverde. On 7 July 1999, counsel for Acaverde wrote to CANACO stating that unspecified "actions of the said Permanent Commission of Arbitration in the above mentioned arbitration trial, as well as the position taken by the Municipality of Acapulco, State of Guerrero, have prevented the continuation of such arbitration procedure". The file was duly returned on 14 September 1999.

123. CANACO is not a State organ, and in any event its sole role was to facilitate the arbitration. Evidence of collusion between CANACO and the City with respect to the conduct of the arbitration or of discrimination against Acaverde on account of its foreign ownership would have been very material, but there is no such evidence before the Tribunal.<sup>70</sup> Although the deposit sought was very large by local standards, the claim was large and the case threatened to be complex. On the evidence presented to the Tribunal, CANACO apparently behaved in a proper and impartial way. For example it rejected a preliminary jurisdictional submission made by the City's lawyers on the grounds that the question of jurisdiction was a matter for the tribunal.<sup>71</sup> Proceedings before the Mexican courts to resolve the issue of arbitrability were never concluded, but it may be inferred from the decisions both of the federal and State courts that they would have enforced the arbitration clause against the City: at any rate the Claimant has not

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<sup>70</sup> The Claimant asserts that CANACO imposed the requirement for deposit of costs "because it was concerned about its own liability in the nullification lawsuit if the arbitration continued". Whether or not its concerns were justified, they were still those of CANACO as a private entity, and there is no sufficient evidence that the judicial process was dilatory or gave unfair advantages to state entities in seeking to avoid domestic arbitration clauses to which they had agreed.

<sup>71</sup> Order of Permanent Arbitration Commission, National Chamber of Commerce of Mexico City, 18 June 1998.

demonstrated the contrary. In the circumstances the Tribunal finds that the discontinuance of the arbitration, a decision made by the Claimant on financial grounds, did not implicate the Respondent in any internationally wrongful act.

*The federal court proceedings*

124. In addition, in January 1997 Acaverde brought proceedings in the Mexican federal court against Banobras under the Line of Credit Agreement in respect of the unpaid invoices of 1996. Subsequently, in July 1998 it brought further proceedings against Banobras in respect of the 1997 invoices. Although Acaverde was not a party to the Line of Credit Agreement, under Mexican law it was entitled to sue as a beneficiary of that Agreement, and its standing to do so was upheld by the courts.

125. In the first proceeding against Banobras, Acaverde claimed more than NP15 million by way of principal plus damages and costs.<sup>72</sup> Guerrero and the City intervened as third parties at Banobras' suit, even though Acaverde made no affirmative claim against them in the proceedings. A challenge to Acaverde's standing having failed, the Tribunal dismissed Acaverde's claim on the ground that it had not proved it had strictly complied with the requirements of the Line of Credit Agreement in terms of demands for payment made on Banobras.<sup>73</sup> Acaverde appealed from this decision. On 11 March 1999, the Federal Tribunal dismissed the appeal, in part relying on the grounds given by the trial court, in part because, at the time the demand was made, Banobras had received from the City notice of a dispute about provision of services by Acaverde.<sup>74</sup> According to the appeal court this was "enough to prove that non-payment of the invoices presented was due to non-performance by Claimant, who is now dissatisfied, and not due to the Municipality's lack of liquidity".<sup>75</sup> An application for *amparo*<sup>76</sup> (a constitutional action) failed on the basis that although the lower court had misinterpreted the Line of Credit Agreement Acaverde had failed to prove the indebtedness.<sup>77</sup>

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<sup>72</sup> H. Juzgado Primero de Distrito en Materia Civil en el Distrito Federal. Juicio Ordinario Mercantil, expediente 12/97, *Acaverde, S. A. de C. V. v. Banco Nacional de Obral y Servicios Públicos, Sociedad Nacional de Crédito*.

<sup>73</sup> Decision of the First Civil District Court of the Federal District, 7 January 1999.

<sup>74</sup> H. Segundo Tribunal Unitario del Primer Circuito. Toca Civil 16/99-II.

<sup>75</sup> Decision of 11 March 1999.

<sup>76</sup> H. Sexto Tribunal Colegiado en Materia Civil del Primer Circuito. Amparo Directo D. C. 5026/99.

<sup>77</sup> Decision of 6 October 1999.

126. The second action,<sup>78</sup> in which Acaverde claimed NP22 million owing in respect of the January-October 1997 invoices, was dismissed on the basis that Banobras, having been notified of the dispute between Acaverde and the City, was entitled not to pay under the Line of Credit until that dispute was resolved.<sup>79</sup> Acaverde's appeal.<sup>80</sup> was dismissed on procedural grounds, on the basis that the dispute related to the Concession Agreement and that Acaverde should first have arbitrated its dispute with the City under Article 17 of the Concession Agreement. The dismissal was stated to be without prejudice to the rights of the Claimant in the proper forum.<sup>81</sup> Again Acaverde brought a constitutional action by way of *amparo* in respect of this decision.<sup>82</sup> It argued that the lower court, in applying the provisions of a 1996 amendment to the Code of Civil Procedure and the Code of Commerce, violated Articles 14 and 16 of the Mexican Constitution which prohibit the retrospective application of laws. The Line of Credit Agreement having been concluded in 1995, Acaverde argued, the 1996 amendment should not have been applied to it. The *amparo* application was rejected by a decision of 20 May 1999. The Court did not accept the City's argument that the application was inadmissible, but it denied the *amparo* claim on the basis that Acaverde had commenced the proceedings relying on the provisions of the law then in force, including the 1996 amendment. The Claimant having failed to challenge a ruling of the lower court to that affect had thereby consented to it: "if... Appellant submitted to the application of legislation currently in force and voluntarily consented to continuing the proceedings thereunder, it is not legally possible to change that on the grounds of that constituting a retroactive application of the Law where the application thereof was consented to from the beginning".

127. The proceedings in the two cases are summarised in Table 1 on the following page.

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<sup>78</sup> H. Juzgado Segundo de Distrito en Materia Civil en el Distrito Federal. Juicio Ordinario Mercantil, expediente 88/98. *Acaverde, S. A. de C. V. v. Banco Nacional de Obras y Servicios Públicos, Sociedad Nacional de Crédito. Institución de Banca de Desarrollo.*

<sup>79</sup> Decision of 12 January 1999.

<sup>80</sup> H. Primer Tribunal Unitario del Primer Circuito. Toca Civil 24/99-I.

<sup>81</sup> Interlocutory Decision, 18 February 1999.

<sup>82</sup> H. Séptimo Tribunal Colegiado en Materia Civil del Primer Circuito. Amparo Directo D. C. 2870/99.

**Table 1****Mexican Judicial Proceedings brought by Acaverde against Banobras**

	<u>First Proceeding</u>	<u>Second Proceeding</u>
Commenced	31 January 1997	11 August 1998
Subject matter	May-December 1996 invoices	January-October 1997 invoices
Amount claimed	Approx NP15 million	Approx NP22 million
First instance decision	<p><b>File 12/97, 7 January 1999</b></p> <p>Claimant's standing upheld but claim dismissed on the grounds that: (a) the Claimant did not prove that the City's non-payment was due to Council's lack of liquidity; (b) the invoices were not submitted in the form required by Line of Credit Agreement, demonstrating the City's acceptance thereof.</p>	<p><b>File 89/98, 12 January 1999</b></p> <p>Interlocutory order dismissing claim on the basis that the dispute related to the Concession Agreement and Acaverde should first have arbitrated its dispute with the City under Article 17 of the Concession Agreement. Case Dismissed without prejudice to the rights of the Claimant in the proper forum.</p>
Appeal	<p><b>Appeal file 16/99-II, 11 March 1999</b></p> <p>Rejected:</p> <p>(a) the Line of Credit can only be used in the event of the debtor's lack of liquidity;</p> <p>(b) Claimant had failed to prove City's receipt and acceptance of invoices;</p> <p>(c) on 13 September 1996 Banobras received formal notice of a dispute between City and Acaverde, establishing that non-payment was due to a dispute about performance, not to City's lack of liquidity</p>	<p><b>Appeal file 24/99-I, 18 February 1999</b></p> <p>Rejected on the ground that it was incorrectly filed.</p> <p>Appeal for reversal rejected on 25 February 1999 on the basis that Acaverde had not invoked the correct remedy of a motion for reconsideration.</p>
Amparo	<p><b>Amparo file 5026/99, 6 October 1999</b></p> <p>Rejected: Although the lower court erred in interpreting the Line of Credit Agreement, Acaverde did not prove City's receipt and acceptance of invoices, its tender of unstamped photocopies not being sufficient for this purpose, in accordance with prior case-law.</p>	<p><b>Amparo file DC 2870/99, 20 May 1999</b></p> <p>Rejected: The Claimant was entitled to invoke Articles 14 and 16 of the Constitution concerning non-retroactivity of the law in relation to the procedural reforms of 1996 (after the Line of Credit Agreement was concluded), but the Claimant had accepted the relevant provisions by conduct in commencing and continuing the suit.</p>

(e) Was there a denial of justice?

128. In asking whether these proceedings involved a denial of justice in terms of Article 1105, two points are fundamental. First, these proceedings were against Banobras

yet the underlying dispute was between the parties to the Concession Agreement, Acaverde and the City. That dispute could not be settled in federal proceedings against a federal agency unless Banobras was a guarantor of the whole of the City's indebtedness under the Concession Agreement. But—and this is the second point—such was not the case. Banobras had quite properly insisted on limiting its obligations under the Line of Credit and Acaverde had accepted that limitation.<sup>83</sup> It is true that Banobras could have sought replenishment of the Line of Credit by diverting federal revenues destined for the City which were in the hands of Guerrero. But in the context of the Mexican financial crisis this was hardly a realistic option, and in any event, it does not appear that Acaverde had any right under the Line of Credit that this be done. Thus the federal proceedings were in any event incapable of resolving Acaverde's most important grievances.

129. Turning to the actual reasons given by the federal courts, the Tribunal would observe that it is not a further court of appeal, nor is Chapter 11 of NAFTA a novel form of *amparo* in respect of the decisions of the federal courts of NAFTA parties. Certain of the decisions appear to have been founded on rather technical grounds, but the notion that the third party beneficiary of a line of credit or guarantee should strictly prove its entitlement is not a parochial or unusual one. Nor was it unreasonable, given the limitations of the Line of Credit Agreement, for the court in the second proceedings to insist that Acaverde comply with the dispute settlement procedure contained in the Concession Agreement, notice of the dispute with the City having been given to Banobras.

130. In any event, and however these cases might have been decided in different legal systems, the Tribunal does not discern in the decisions of the federal courts any denial of justice as that concept has been explained by NAFTA tribunals, notably in the

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<sup>83</sup> See above, para. 51.

*Azinian*,<sup>84</sup> *Mondev*,<sup>85</sup> *ADF*<sup>86</sup> and *Loewen* cases.<sup>87</sup> The Mexican court decisions were not, either *ex facie* or on closer examination, evidently arbitrary, unjust or idiosyncratic. There is no trace of discrimination on account of the foreign ownership of Acaverde, and no evident failure of due process. The decisions were reasoned and were promptly arrived at. Acaverde won on key procedural points, and the dismissal in the second proceedings, in particular, was without prejudice to Acaverde's rights in the appropriate forum.

131. The Claimant argues that litigation strategy adopted by the City itself amounted to a denial of justice and hence a breach of Article 1105. But the City was a litigant, and there is no evidence that it was acting in collusion either with CANACO or the federal courts. It is not unusual for litigants to be difficult and obstructive, and there is nothing here comparable to the abusive remarks of counsel in the *Loewen* case which were tolerated and even condoned by the trial judge, producing a denial of justice.<sup>88</sup> The point is that a *litigant* cannot commit a denial of justice unless its improper strategies are endorsed and acted on by the court, or unless the law gives it some extraordinary privilege which leads to a lack of due process. There is no evidence of either circumstance in the present case.

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<sup>84</sup> In *Azinian* the tribunal also addressed whether the Claimants could have successfully pursued a denial of justice claim. It said: "A denial of justice could be pleaded if the relevant courts refuse to entertain a suit, if they subject it to undue delay, or if they administer justice in a seriously inadequate way.... There is a fourth type of denial of justice, namely the clear and malicious misapplication of the law [which] ... overlaps with the notion of 'pretence of form' to mask a violation of international law." However, in the view of the tribunal, the findings of the Mexican courts could not "possibly be said" to be in any way a denial of justice, *Azinian, Davitian & Baca v. United Mexican States*, Award of 1 November 1999, 5 ICSID Reports 269, 290 (paras. 102-103).

<sup>85</sup> *Mondev International Limited v. United States of America*, Award of 11 October 2002, 6 ICSID Reports 192.

<sup>86</sup> The *ADF* Tribunal, rejecting the investor's submission that a federal administrative body had acted *ultra vires* in its interpretation of the measures in question, the Tribunal said, "...even had the investor made out a *prima facie* basis for its claim, the Tribunal has no authority to review the legal validity and standing of the US measures... under *US internal administrative law*. We do not sit as a court with appellate jurisdiction.... The Tribunal would emphasize, too, that even if the US measures were somehow shown or admitted to be *ultra vires* under the internal law of the United States, that by itself does not necessarily render the measures grossly unfair or inequitable under the customary international law standard of treatment embodied in Article 1105(1).... [S]omething more than simple illegality or lack of authority under the domestic law of a State is necessary to render and act or measure inconsistent with the customary international law requirements of Article 1105(1)...", *ADF Group Inc. v. United States of America*, Award of 9 January 2003, (para. 190). Nor was the authority's refusal to follow prior rulings "grossly unfair or unreasonable" on the facts presented by the investor.

<sup>87</sup> *The Loewen Group, Inc. and Raymond L. Loewen v. United States of America*, Award of 26 June 2003, (ICSID Case No. ARB(AF)/98/3). For the Tribunal's discussion of Article 1105 and the FTC interpretation see *ibid.*, paras. 124-128.

<sup>88</sup> *Ibid.*, paras. 119-123.

132. Of course, as the *Loewen* tribunal said, it is

“the responsibility of the State under international law and, consequently, of the courts of a State, to provide a fair trial of a case to which a foreign investor is a party. It is the responsibility of the courts of a State to ensure that litigation is free from discrimination against a foreign litigant and that the foreign litigant should not become the victim of sectional or local prejudice.”<sup>89</sup>

But neither the decisions themselves nor other evidence before the Tribunal suggest that these proceedings involved discrimination, bias on grounds of sectional or local prejudice, or a clear failure of due process. The CANACO arbitration, which alone held the prospect of complete relief for Acaverde in respect of its claims against the City, was not pursued, and the Tribunal has already held that this fact did not of itself entail a breach of Article 1105. As to the Banobras litigation, Acaverde did exhaust its remedies, but it was not a denial of justice for the federal courts to insist on prior action against the City. This aspect of the claim under Article 1105(1) accordingly fails.

(f) The termination phase

133. On the other hand the relief sought in the Mexican domestic proceedings did not cover the full scope of Claimant’s grievances against the City. Chapter 11 of NAFTA does not require that a party should exhaust local remedies before bringing an international claim: rather it requires a waiver of remaining remedies. There thus remains a question whether conduct attributable to the Respondent, and going beyond the scope of the legal proceedings brought by Acaverde, might constitute a breach of the standard embodied in Article 1105 of NAFTA.

134. Two specific complaints require discussion here. The first concerns the City’s dealings with Setasa, which the Claimant alleged involved a breach of its exclusive rights under the Concession Agreement, if not outright collusion.<sup>90</sup> There is little doubt that Setasa, having been initially involved in discussions with the Claimant,<sup>91</sup> was “waiting in the wings” later that year to take over the operation on a different basis. But there is no evidence that it did so before Acaverde’s withdrawal from the Agreement, and

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<sup>89</sup> *Loewen*, para. 123.

<sup>90</sup> See Claimant’s Memorial, paras. 3.74-3.76.

<sup>91</sup> A 60 day letter of intent was concluded between Sanifill & Setasa on 27 February 1997: see above, para. 66.

in any event whatever civil wrongs may have been committed during the *denouement* of the project, they did not in the Tribunal's opinion either cause or trigger its failure, nor did they independently amount to a breach of the Article 1105 standard.

135. A second and more serious complaint concerns the subsequent attempt by the City to enforce the performance bond given by Acaverde in the amount of NP6 million. This attempt was problematic, especially given the City's own record of non-performance of its obligations under the Concession Agreement. But in fact the City's attempt to collect this money failed, the bond-holder rejecting the claim,<sup>92</sup> and it is not alleged by the Claimant that it suffered any specific losses as a result of this episode.

136. Looking at the matter more generally, the position in this terminal phase can be compared with that in the *ELSI* case, where improper conduct of the local Italian authorities seems to have precipitated the collapse of a failing enterprise, leading to a fire-sale of assets and consequent losses to the investor. A Chamber of the Court held that such conduct did not amount to a breach of the applicable FCN treaty;<sup>93</sup> whether it would have amounted to a breach of NAFTA the Tribunal does not need to inquire. For the key difference here is that there was no actual requisition or any equivalent act triggering the departure of Acaverde. The Claimant was not prevented (as the parent company in the *ELSI* case was arguably prevented) from seeking to conduct an orderly withdrawal from Acapulco. Attempts at a financial settlement or sale of the enterprise failed, but this was not a result of any internationally wrongful act of the Respondent State.

(g) The allegation of conspiracy

137. Thus far the Tribunal has considered the various items of conduct complained of by the Claimant separately and serially. But the Claimant also, in effect, alleged that the various Mexican agencies conspired together to frustrate the concession, and that the sum of this conduct was greater than its various component parts in terms of causing a violation of Article 1105.<sup>94</sup>

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<sup>92</sup> See Statement of J. Herrera, para. 21.

<sup>93</sup> *Case Concerning Elettronica Sicula S.P.A. (ELSI) (United States of America v. Italy)*, 1989 ICJ Reports 15.

<sup>94</sup> See e.g., Claimant's Memorial, para. 3.65.

138. The Tribunal has no doubt that a deliberate conspiracy—that is to say, a conscious combination of various agencies of government without justification to defeat the purposes of an investment agreement—would constitute a breach of Article 1105(1). A basic obligation of the State under Article 1105(1) is to act in good faith and form, and not deliberately to set out to destroy or frustrate the investment by improper means.

139. But such an allegation needs to be proved, and the Claimant has not proved it. For example, the State Delegate of Banobras was said to be responsible for soliciting the City's letter of 11 September 1996 with a view to avoiding payment to Acaverde. He denied this in evidence before the Tribunal,<sup>95</sup> and the Tribunal accepts his denial. But in any event, as already noted, Banobras had no obligation to Acaverde to garnishee funds payable to the City in order to replenish the line of credit. There was a substantial reduction in federal funds being channelled through Guerrero, and in the absence of replenishment the line of credit was nearly exhausted. As the Tribunal has already found, the refusal of Banobras to go further, whether or not it was a breach of contract, was not in itself a breach of Article 1105(1), nor was it converted into such a breach by the federal court decisions. More generally, there are sufficient reasons to explain the collapse of the concession—attributable far more to the City than to Banobras—and there is no need to resort to conspiracy theories, unsupported by solid evidence. A marginal financial plan, predicated on a much more substantial federal guarantee than was eventually agreed, foundered on the rocks of a deteriorating financial climate and a combination of little and large local difficulties. That is not enough to cross the Article 1105(1) threshold.

*(iii) Conclusions as to Article 1105(1)*

140. For these reasons the Tribunal concludes that the claim under Article 1105(1) must fail.

**(4) The claim for expropriation: NAFTA Article 1110**

141. As noted, the Claimant's principal contention was founded not on Article 1105 but on Article 1110. The Claimant argued that Acaverde's entire enterprise in

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<sup>95</sup> Statement of Mr. Mario Alcaraz Alarcón, para. 22 (“Nobody at Banobras had anything to do with the sending of this letter.”); Second Declaration of Mr. Mario Alcaraz Alarcón, paras. 7-8 (“I deny that there was any type of coordination of the actions taken by the City Council and those taken by the Bank... Neither I nor the personnel of the Banobras office for which I was responsible took part in any discussion of [the cancellation of the concession].”).

Acapulco was expropriated by the City, or at any rate by the combined conduct of the City, Guerrero and Banobras, and that this was a breach of Article 1110 of NAFTA. Although the Claimant did not put it in these terms, it could also be argued that the persistent failure of the City to pay the amounts due under the Concession Agreement was tantamount to an expropriation at least of the amount unpaid. In the Tribunal's view the latter claim is encompassed within the former, and is *infra petita*. It is open to the Tribunal to find a breach of Article 1110 in a case where certain facts are relied on to show the wholesale expropriation of an enterprise but the facts establish the expropriation of certain assets only. Accordingly the Tribunal will consider first the standard set by Article 1110, in particular for conduct tantamount to an expropriation, then whether the enterprise as a whole was subjected to conduct in breach of Article 1110, and finally whether (even if there was no wholesale expropriation of the enterprise as such) the facts establish a partial expropriation.

(i) *The Article 1110 standard*

142. So far as relevant, Article 1110 provides that:

“1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ('expropriation'), except:

- (a) for a public purpose;
- (b) on a non-discriminatory basis;
- (c) in accordance with due process of law and Article 1105(1);  
and
- (d) on payment of compensation in accordance with paragraphs 2 through 6.

...

7. This Article does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights, or to the revocation, limitation or creation of intellectual property rights, to the extent that such issuance, revocation, limitation or creation is consistent with Chapter Seventeen (Intellectual Property).

8. For purposes of this Article and for greater certainty, a non-discriminatory measure of general application shall not be considered a measure tantamount to an expropriation of a debt security or loan covered by this Chapter solely on the ground that the measure imposes costs on the debtor that cause it to default on the debt.”

143. It may be noted that Article 1110(1) distinguishes between direct or indirect expropriation on the one hand and measures tantamount to an expropriation on the other. An indirect expropriation is still a taking of property. By contrast where a measure tantamount to an expropriation is alleged, there may have been no actual transfer, taking or loss of property by any person or entity, but rather an effect on property which makes formal distinctions of ownership irrelevant. This is of particular significance in the present case, at least as concerns the enterprise of Acaverde as a whole.

144. Evidently the phrase “take a measure tantamount to nationalization or expropriation of such an investment” in Article 1110(1) was intended to add to the meaning of the prohibition, over and above the reference to indirect expropriation. Indeed there is some indication that it was intended to have a broad meaning, otherwise it is difficult to see why Article 1110(8) was necessary. As a matter of international law a “non-discriminatory measure of general application” in relation to a debt security or loan which imposed costs on the debtor causing it to default would not be considered expropriatory or even potentially so. It is true that paragraph (8) is stated to be “for greater certainty”, but if it was necessary even for certainty’s sake to deal with such a case this suggests that the drafters entertained a broad view of what might be “tantamount to an expropriation”.

145. Thus there is some textual basis for the Claimant’s submission that “the modern definition of ‘expropriation’ must be broad enough to encompass every course of sovereign conduct that unfairly destroys a foreign investor’s contractual rights as an asset”.<sup>96</sup> The Claimant relied on a number of decisions in support of this proposition, and a review of these is first called for.

146. *LETCO v. Liberia*<sup>97</sup> concerned a 1970 concession agreement between LETCO and the Liberian government which gave LETCO, a Liberian company owned by French nationals, the exclusive right to harvest, process, transport and market forest products and to conduct other timber operations within an exclusive exploitation area, in

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<sup>96</sup> Reply, para. 4.23.

<sup>97</sup> *Liberian Eastern Timber Corporation [LETCO] v. Government of the Republic of Liberia* (1986) 2 ICSID Reports 343.

return for certain payments and the performance of other contractual obligations.<sup>98</sup> Following an attempt to renegotiate the agreement, the Liberian Forest Development Authority by a letter of 18 February 1980 reduced the concession area by more than half with immediate effect on the grounds of breaches of the concession agreement by LETCO. After unsuccessfully protesting the actions of the Authority, LETCO suspended its operations in March 1983 and commenced ICSID arbitration proceedings under the agreement. Subsequently Liberia annulled the concession agreement, again citing breaches of the agreement by LETCO. The tribunal found that the Authority's letter of February 1980 communicating the withdrawal of over half the concession area was an effective revocation of the agreement which rendered the concession useless to LETCO, and that the revocation was carried out in breach of the notice and cure provisions of the concession agreement.<sup>99</sup> The tribunal examined LETCO's alleged breaches of the agreement (as set out by Liberia in its correspondence with LETCO), and found the alleged breaches were not supported by the facts before it. Before turning to the assessment of compensation due to LETCO for Liberia's breach of contract, the tribunal considered whether Liberia's actions in reducing the concession area could be justified as an act of nationalisation. It found that any such defence would have failed because the confiscation of the concession area was not for a bona fide public purpose, was discriminatory and was not accompanied by appropriate compensation.<sup>100</sup> It should be stressed that LETCO did not base its claim on expropriation or unfair treatment, nor did the tribunal find Liberia responsible under international law for breach of the concession. The tribunal's discussion of expropriation was in the context of addressing a potential defence by Liberia (which did not appear in the proceedings) to the finding of breach of contract. The award of damages was based on the Liberian law of contract.

147. *Sapphire International Petroleum Ltd. v. National Iranian Oil Company*<sup>101</sup> concerned alleged breaches leading to the unlawful termination of an agreement between the claimant and the National Iranian Oil Company (NIOC) under which the parties would form a joint venture to prospect for and exploit oil in a specified geographical area. The

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<sup>98</sup> Ibid., 359.

<sup>99</sup> Ibid., 363.

<sup>100</sup> Ibid., 366-7.

<sup>101</sup> Arbitral Award, 15 March 1963, 35 ILR 136 (1967). The decision was later set aside by an Iranian court: see 9 ILM 1118 (1970).

relationship between the parties broke down after a only a few months. Sapphire repudiated the agreement on the grounds of NIOC's actions which, it concluded, showed that NIOC did not intend to perform its obligations under the agreement, and commenced arbitration proceedings. As in the *LETCO* case, the arbitration took place pursuant to an arbitration clause in the agreement between the parties. The arbitrator held that NIOC had breached the terms of the concession agreement in a manner which entitled Sapphire to terminate the contract and claim damages.<sup>102</sup>

148. The Claimant argues that the “*Sapphire* decision exemplifies State responsibility for undermining the investor-to-government relations on which a long-term economic development agreement is based” and that “the decision holds a State responsible for such conduct even where neither the State nor any State organ terminates the agreement outright”.<sup>103</sup> While the arbitrator in *Sapphire* discussed in some depth the relevance of the nature of the contract to his finding as to the substantive law applicable to the dispute,<sup>104</sup> the award rests on a finding of breaches of contract by NIOC, a separate agency which was party to the contract and the defendant in the arbitration.

149. Thus both *LETCO* and *Sapphire* were awards for breach of contract, given by tribunals constituted under the arbitration provisions of those contracts. By contrast the present case concerns a claim that Mexico has breached Article 1110(1) by actions tantamount to expropriation. There is no suggestion that the contracts in the present case were “internationalized”. They were contracts between Mexican persons or entities governed by Mexican law and including Mexican dispute settlement provisions. The Claimant relied on statements in the two decisions for the proposition that breach of contract can be characterised as an expropriation. But the two cases are of limited assistance: the statements to that effect, such as they are,<sup>105</sup> were not relevant to the awards of these tribunals.

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<sup>102</sup> 35 ILR 136, 185.

<sup>103</sup> Memorial, para. 5.30.

<sup>104</sup> 35 ILR 136, 170-6. Arbitrator Calvin found that the law of the contract was the rules of law “common to civilized nations” on the basis that the parties had not specified the applicable law in the contract, and the contract was fundamentally different from the ordinary commercial contract envisaged by the rules of private international law because of its long-term and quasi-international character.

<sup>105</sup> The term “expropriation” was not used by the arbitrator in *Sapphire*.

150. Turning to NAFTA itself, the meaning of Article 1110 has been discussed in a series of decisions by NAFTA tribunals.

151. *Pope & Talbot Inc. v. Government of Canada* concerned an alleged regulatory expropriation in terms of the right of access to the United States market. The tribunal held that this right was protected by Article 1105 as part of the “business” in question, but that the Canadian measure was not sufficiently restrictive to amount to a “taking”.<sup>106</sup>

152. The *S.D. Myers* case was also concerned with the distinction between regulation and expropriation, and to that extent is not relevant here. The tribunal defined creeping expropriation as “a lasting removal of the ability of an owner to make use of its economic rights...”.<sup>107</sup> The tribunal accepted that “in legal theory, rights other than property rights may be ‘expropriated’ and that international law makes it appropriate for tribunals to examine the purpose and effect of governmental measures”.<sup>108</sup> The tribunal held that the temporary closure of the border to PCB transports could not be characterised as a measure tantamount to expropriation, rejecting what it characterised as an attempt by the claimant to use the word “tantamount” to extend the meaning of the word “expropriation” beyond the “customary scope of the term... under international law”.<sup>109</sup> It noted that:

“The primary meaning of the word ‘tantamount’ given by the Oxford English Dictionary is ‘equivalent’. Both words require a tribunal to look at the substance of what has occurred and not only at form...”<sup>110</sup>

The tribunal considered that the drafters of the NAFTA intended the phrase “tantamount to expropriation” to cover the concept of “creeping expropriation”.<sup>111</sup> Canada’s actions were

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<sup>106</sup> Interim Award of 26 June 2000, 122 ILR 293, 334-337.

<sup>107</sup> *S.D. Myers, Inc. v. Government of Canada*, Partial Award, 13 November 2000, para. 283, cited in Claimant’s Reply, fn 184; see [http://www.dfait-maecti.gc.ca/tna-nac/disp/SDM\\_archive-en.asp](http://www.dfait-maecti.gc.ca/tna-nac/disp/SDM_archive-en.asp). This was an arbitration conducted under the UNCITRAL Rules.

<sup>108</sup> *Ibid.*, paras. 280-1.

<sup>109</sup> *Ibid.*, para. 285.

<sup>110</sup> *Ibid.*, paras. 285-6, citing *Pope & Talbot, Inc. v. Canada*, Interim Award, 26 June 2000, para. 104.

<sup>111</sup> *S.D. Myers*, para. 286.

not measures “tantamount to expropriation” because Canada realised no benefit from the measure and there was no evidence of a transfer of property or benefit directly to others.<sup>112</sup>

153. *Metalclad Corporation v. United Mexican States* was a claim arising from another municipal concession contract which met fierce local resistance.<sup>113</sup> The claimant alleged that Mexico, through the governments of the State of San Luis Potosi and municipality of Guadalcazar, had breached Articles 1105 and 1110 of the NAFTA by interference in the development and operation of a hazardous waste landfill. Summarising the scope of Article 1110, the tribunal said,

“expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favor of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.”<sup>114</sup>

The tribunal held that Mexico, by tolerating and acquiescing in the actions of the municipal authorities which prevented the operation of the fully constructed landfill, notwithstanding the approval and endorsement of the federal authorities, was responsible for a measure tantamount to expropriation of Metalclad’s investment in breach of Article 1110. Further, it held, the denial by the municipal authority of a construction permit on grounds which were not open to it and which contradicted earlier federal commitments,<sup>115</sup> and the absence of a timely, orderly and substantiated basis for the denial of the municipal permit amounted to an indirect expropriation.<sup>116</sup> The tribunal also considered that the Ecological Decree, setting aside the area as a reserve and thus preventing the land from being used as provided for in the agreement, was an act tantamount to expropriation and a further ground for finding a breach of Article 1110.<sup>117</sup>

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<sup>112</sup> Ibid., para. 287.

<sup>113</sup> *Metalclad Corporation v. United Mexican States*, Award, 30 August 2000, 5 ICSID Reports 209.

<sup>114</sup> Ibid., 230 (para. 103).

<sup>115</sup> The tribunal found that under federal law the municipal authority had the power to issue or refuse construction permits on construction grounds only, and its denial of the permit on ecological grounds was *ultra vires*: *ibid.*, 228 and 230 (paras. 92, 106).

<sup>116</sup> Ibid., 230 (paras. 106-7)

<sup>117</sup> Ibid., 231 (paras. 109, 111).

154. Mexico sought judicial review of the *Metalclad* award in the Supreme Court of British Columbia on various grounds.<sup>118</sup> The Supreme Court upheld Mexico's argument that the tribunal's finding under Article 1105 was in excess of jurisdiction because the tribunal used NAFTA's transparency provisions (extraneous to Chapter 11) as a basis for the interpretation and application of Article 1105.<sup>119</sup> As the tribunal had also based its Article 1110 finding of expropriation, at least in part, on Mexico's failure to act in a transparent manner, this finding was also outside the scope of the submission to arbitration.<sup>120</sup> However, the Supreme Court found that the tribunal's decision that the Ecological Decree was an expropriation was within jurisdiction and not patently unreasonable and that there were no grounds to set it aside.<sup>121</sup> Tysoe J. commented that the tribunal's definition of expropriation for the purposes of Article 1110 was "extremely broad", but held that this was not a reviewable issue under the relevant Canadian legislation.<sup>122</sup>

155. In the present case, for reasons that will appear, the Tribunal does not need to reach final conclusions on the meaning of the phrase "measures tantamount to... expropriation" in Article 1110. Each case has to be looked at it in light of the factual situation and the basis for the measures in question. There is no issue in the present case of "regulatory taking"; rather the question is whether the combined conduct of Mexican public entities had an effect equivalent to the taking of the enterprise, in whole or substantial part. In considering this question it is necessary to distinguish between the measures affecting Acaverde as a whole and those concerning particular contractual rights under the Concession Agreement.

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<sup>118</sup> *United Mexican States v. Metalclad Corporation*, decision of 2 May 2001, 2001 BCSC 664, 5 ICSID Reports 236.

<sup>119</sup> *Ibid.*, 5 ICSID Reports 236, 253 (para. 66).

<sup>120</sup> *Ibid.*, 255 (paras. 78-9).

<sup>121</sup> *Ibid.*, 259-60 (paras. 100, 105).

<sup>122</sup> *Ibid.*, 259 (para. 99)

(ii) *The Article 1110 standard applied to the enterprise*

156. Turning to the impact of the Mexican measures on Acaverde as a whole, the first point is that in the present case there was at no stage any expropriation of physical assets. The assets of Acaverde were sold off in an apparently orderly way at about the time it withdrew from operations under the Concession Agreement.<sup>123</sup>

157. Nor was there any direct or indirect expropriation of the enterprise, Acaverde, as such. As the Tribunal has already held, the reason Waste Management withdrew from Acapulco was not because the enterprise had been seized, or because its activity as a whole had been blocked, for example by the seizure of key items of its property, but because—as a result of contractual defaults, changes of circumstances and the fragility of the underlying business plan—the operation was persistently uneconomic.

158. Thus for present purposes the question is whether there was any conduct tantamount to an expropriation which might trigger NAFTA Article 1110. The Claimant contends that the City's refusal to pay on approved invoices and Banobras' refusal to make payments under the Line of Credit Agreement were confiscatory in effect, and that Acaverde's rights under the concession were rendered valueless by the combination of (a) the City's failure to enforce the exclusivity provisions of the Concession, (b) its frustrating the construction, building and operation of the landfill, and (c) its campaign of obstruction (in cahoots with Guerrero and Banobras) in the face of Acaverde's attempts to resolve the dispute. In short the Claimant argues that these actions and refusals to acts by the City, Guerrero and Banobras taken together resulted in a "creeping" expropriation of the Claimant's investment, in breach of Article 1110.<sup>124</sup>

159. In answering this question it is not necessary for the present Tribunal to resolve the differences in interpretation which arose in the *Metalclad* case as between the NAFTA tribunal and the British Columbia Supreme Court.<sup>125</sup> Leaving aside any question of the breadth of the definition of expropriation given by the *Metalclad* tribunal (at least when considered in isolation from the facts of that case), the present Tribunal does not

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<sup>123</sup> Mr. Rodney Proto, transcript, 7 April 2003, 194.

<sup>124</sup> Memorial, para. 5.8; Reply, para. 4.23.

<sup>125</sup> See paragraphs 153-154 above.

regard the conduct of Mexico in the present case as tantamount to expropriation of the enterprise as such, within the meaning attributed to that term in *Metalclad*. Acaverde at all times had the control and use of its property. It was able to service its customers and earn collection fees from them. It is true that the City failed to make available the promised land for the disposal site—but a failure by a State to provide its own land to an enterprise for some purpose is not converted into an expropriation of the enterprise just because the failure involves a breach of contract. It is also true that the City’s breaches (not remedied by Guerrero and remedied only to a limited extent by Banobras) had the effect of depriving Acaverde of “the reasonably-to-be-expected economic benefit” of the project so far as the monthly fees due from the City were concerned. But that will be true of any serious breach of contract: the loss of benefits or expectations is not a sufficient criterion for an expropriation, even if it is a necessary one.

160. In the Tribunal’s view, an enterprise is not expropriated just because its debts are not paid or other contractual obligations towards it are breached. There was no outright repudiation of the transaction in the present case, and if the City entered into the Concession Agreement on the basis of an over-optimistic assessment of the possibilities, so did Acaverde. It is not the function of Article 1110 to compensate for failed business ventures, absent arbitrary intervention by the State amounting to a virtual taking or sterilising of the enterprise.

161. The nearest the Claimant came to showing an outright repudiation of the enterprise by Mexico was the Mayor’s statement, shortly after the Concession Agreement came into force, to the effect that “the obligation to contract Acaverde’s services will be eliminated in order to remove what was previously interpreted as an imposition”.<sup>126</sup> This of course related only to one aspect of the concession arrangements, although an important aspect. But even if a unilateral and unjustified change in the exclusivity obligation could have amounted to an expropriation, no legislative change was in fact made. The Claimant argued that this statement “effectively repealed the law” but the Tribunal does not agree. The Mayor was not purporting to exercise legislative authority or unilaterally to vary the contract. He was not intervening by taking some extra-legal action, as the Mayor of Palermo did when he intervened in the *ELSI* case. He was saying what ought to be done,

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<sup>126</sup> See paragraph 56 above for the statement and its context.

in his view, to allay public concerns, concerns which did in fact exist at the time. Individual statements of this kind made by local political figures in the heat of public debate may or may not be wise or appropriate, but they are not tantamount to expropriation unless they are acted on in such a way as to negate the rights concerned without any remedy. In fact no action was taken of the kind threatened at the time or later. Even if it had been taken, the Claimant had remedies available to it, under the Concession Agreement and otherwise.

162. For these reasons the Tribunal does not accept that there was an expropriation of Acaverde in this case, or any measure tantamount to the expropriation of Acaverde as an enterprise.

*(iii) Was there conduct tantamount to an expropriation of Acaverde's contractual rights?*

163. This conclusion does not however exhaust the Claimant's case, for the reasons given in paragraph 141 above. Even if the enterprise of Acaverde was not subjected to conduct in breach of Article 1110 when considered as a whole, it is arguable that the persistent refusal or inability of the City to pay sums due under the Concession Agreement involved an expropriation, or at least measures tantamount to an expropriation, of the sums due. As another NAFTA tribunal confirmed in the *Mondev* case, "the protection afforded by the prohibition against expropriation or equivalent treatment in Article 1110 can extend to intangible property interests".<sup>127</sup> The Claimant alleged that the City's failure to pay, persisted in over many months, was a virtual expropriation of its contractual rights amounting to a breach of Article 1110.

164. This issue was raised but not resolved in the *Azinian* case.<sup>128</sup> There the claimants argued that the fundamental non-performance by the city council of a waste management contract with its Mexican subsidiary was a violation of Article 1110, relying on a "wealth of authority treating the repudiation of concession agreements as an

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<sup>127</sup> *Mondev International Limited v. United States of America*, Award of 11 October 2002, 6 ICSID Reports 192, 216 (para. 98).

<sup>128</sup> *Azinian, Davitian & Baca v. United Mexican States*, Award of 1 November 1998, 5 ICSID Reports 269.

expropriation of contractual rights”.<sup>129</sup> The tribunal, having emphasised that proof of a breach of contract did not equate to a breach of NAFTA Chapter 11, responded to this argument in the following terms:

“Labelling is... no substitute for analysis. The words ‘confiscatory,’ ‘destroy contractual rights as an asset,’ or ‘repudiation’ may serve as a way to describe breaches which are to be treated as extraordinary, and therefore as acts of expropriation, but they certainly do not indicate on what basis the critical distinction between expropriation and an ordinary breach of contract is to be made. The egregiousness of any breach is in the eye of the beholder—and that is not satisfactory for present purposes.”<sup>130</sup>

The Tribunal noted however that the repudiation by the council in that case took the form of the actual rescission of the contract for cause, which cause was upheld by the Mexican courts in proceedings not alleged to involve a denial of justice. In the absence of a denial of justice, the Mexican contract had no further existence as a source of rights.<sup>131</sup> That being so, the issue of breach of contract as conduct tantamount to expropriation did not arise: it was “unnecessary to consider issues relating to performance of the Concession Contract”.<sup>132</sup>

165. In the present case, by contrast, the City at no stage purported to invalidate or terminate the Concession Agreement. As the Tribunal has held, it did attempt to perform its obligations in a number of respects. At the same time it is undeniable (and the Respondent hardly sought to deny) that the City was in breach of the Agreement for much of its duration, especially as concerns its failure to pay the monthly fee due. Thus the present case does raise the question whether a persistent and serious breach of a contract by a State organ can constitute expropriation of the right in question, or at least conduct tantamount to expropriation of that right, for the purposes of Article 1110.

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<sup>129</sup> Ibid., 288 (para. 89).

<sup>130</sup> Ibid., 288 (para. 90).

<sup>131</sup> The tribunal stressed that the claimants’ failure to plead denial of justice in respect of the decisions of the Mexican courts was fatal: “if there is no complaint against a determination by a competent court that a contract governed by Mexican law was invalid under Mexican law, there is by definition no contract to be expropriated”: *ibid.*, 290 (para. 100).

<sup>132</sup> *Ibid.*

166. The Claimant relied on several earlier cases as authority for the proposition that contractual non-performance, and in particular the refusal to pay a debt, can constitute an expropriation.

167. *George W. Cook v. United Mexican States*<sup>133</sup> was a decision of the United States-Mexican Claims Commission established under the Convention of 8 September 1923.<sup>134</sup> This was a claim for postal money orders issued in 1913 and 1914 which were not paid by the Mexican postal authorities on presentation. The Commission found for the claimant, dismissing Mexico's submission that the action was time-barred because the right to collect on money orders expired two years after issue. Cook had presented the orders for payment within the two year period, the authorities had refused to pay them, contrary to the governing provisions of Mexican law, and now Mexico could not rely on its own default as a defence to the claim. Commissioner Nielsen, in a statement with which the other two commissioners concurred, said that: "[b]y the failure of the Mexican authorities to pay the money orders in question in conformity with the existing Mexican law when payment was due... Cook was wrongfully deprived at the time of property in the amount [of the postal orders]."<sup>135</sup> It may be noted that the Commission had jurisdiction over the whole class of claims by nationals of one State against the Government of the other State, to be decided "in accordance with the principles of international law, justice and equity". According to Article V of the Convention:

"The High Contracting Parties, being desirous of effecting an equitable settlement of the claims of their respective citizens, thereby affording them just and adequate compensation for their losses or damages, agree that no claim shall be disallowed or rejected by the Commission by the application of the general principle of international law that the legal remedies must be exhausted as a condition precedent to the validity or allowance of any claim."

Thus the Commission's jurisdiction was not dependent upon the qualification of the conduct as expropriatory; nonetheless the Commission did characterise it in those terms.

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<sup>133</sup> *George W. Cook v. United Mexican States*, Opinion of 3 June 1927, 22 *AJIL* 189. See also A.H. Feller, *The Mexican Claims Commissions 1923-1934* (New York, Macmillan, 1935) 179-80.

<sup>134</sup> *United States Treaty Series*, No. 678; 118 *British & Foreign State Papers* 1103.

<sup>135</sup> 22 *AJIL* 189, 191.

168. In the Tribunal's view, the outright refusal by a State to honour a money order or similar instrument payable under its own law may well constitute either an actual expropriation or at least a measure tantamount to an expropriation of the value of the order. There was no suggestion that Cook as the beneficiary of the money order was not entitled to be paid. Like other instruments of similar character the money order was not just an ordinary contract; it was an instrument representing a certain value which the State was *ex facie* committed to pay under its own law.

169. The *Cook* case was, however, relied on in *Singer Sewing Machine Co. v. The Republic of Turkey*<sup>136</sup> for the broader proposition that a government's failure to pay a debt due under a contract is an expropriation of the amount owed—and correspondingly the *Singer* case was relied on by the Claimant before this Tribunal. In that case the American-Turkish Claims Committee held that the Turkish Government's failure to pay for sewing machines it had agreed to purchase could be viewed as either a confiscation of the purchase price of the commodities or the destruction or confiscation of property rights in a contract. According to Nielsen's report, the Committee stated that:

“It cannot be said that the law of nations embraces any ‘Law of Contracts’ such as is found in the domestic jurisprudence of nations. International law does not prescribe rules relative to the forms and legal effect of contracts, but that law may be considered to be concerned with the action authorities of a government may take with respect to contractual rights. It is believed that in the ultimate determination of responsibility under international law, application can properly be given to principles of law with respect to confiscation, and that the confiscation of the property of an alien is violative of international law. If a government agrees to pay money for commodities and fails to make payment, the view may be taken that the purchase price of the commodities has been confiscated, or that the commodities have been confiscated, or that property rights in a contract have been destroyed or confiscated.”<sup>137</sup>

170. The United States-Turkish Exchange of Notes of 24 December 1923, pursuant to which the decision was made, was not limited to claims for expropriation, or indeed to claims for breaches of international law in any sense. The Exchange of Notes provided only that the Committee...

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<sup>136</sup> Reported in F.K. Nielsen, ed., *The American-Turkish Claims Settlement Commission. Opinions and Report* (Washington, Government Printing Office, 1937), 490, cited in Claimant's Memorial, paras. 5.46-5.47.

<sup>137</sup> Nielsen, 491.

“will proceed, with a view to determining the solutions which should be given them, to the examination of the claims presented by either Government within a period of six months from its constitution. The dossiers of the claims must contain the documents establishing the nature, the origin, and the justification of each claim.”<sup>138</sup>

Thus the Committee’s dictum quoted above was not necessary for the purposes of its decision. Moreover it was, in the present Tribunal’s view, far too wide. Taken literally that dictum would appear to eliminate the distinction between breach of contract and breach of treaty entirely.

171. Subsequent authorities have sought to make a distinction between mere failure or refusal to comply with a contract, on the one hand, and conduct which crosses the threshold of taking or expropriation, on the other hand. The Tribunal is sympathetic to the view expressed in *Azinian* that such a distinction is not adequately made by the addition of adjectives (“egregious”, “gross”, “flagrant” or whatever).<sup>139</sup> But *some* distinction must be made: if certain cases of contractual non-performance may amount to expropriation, it must be possible to say, in principle, which ones, otherwise the distinction between contractual and treaty claims disappears.

172. On analysis it appears that the cases fall into a number of groups. First and perhaps best known are the cases where a whole enterprise is terminated or frustrated because its functioning is simply halted by decree or executive act, usually accompanied by other conduct.<sup>140</sup> This was so in many of the oil cases,<sup>141</sup> and in many cases before the Iran-United States Claims Tribunal.<sup>142</sup>

173. Secondly, there are cases where there has been an acknowledged taking of property, and associated contractual rights are affected in consequence. In such cases the bundle of rights requiring to be compensated includes all the associated contractual and

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<sup>138</sup> Text in CI Bevens, *Treaties and other International Agreements of the United States of America 1776-1949* (1974) vol. 11, 1105.

<sup>139</sup> See above, para. 164.

<sup>140</sup> Thus in the *Rudloff* case, the council unilaterally terminated the contract and destroyed the building the Claimant was constructing on the land in question: (1905) 9 RIAA 255, 259.

<sup>141</sup> E.g., *Libyan American Oil Company v. Government of the Libyan Arab Republic*, (1977) 62 ILR 141, 189-90. See also *Revere Copper & Brass, Inc. v. Overseas Private Investment Corporation* (1978) 56 ILR 258.

<sup>142</sup> See the cases reviewed by GH Aldrich, *The Jurisprudence of the Iran-United States Claims Tribunal* (Oxford, Clarendon Press, 1996) ch. 5.

other incorporeal rights,<sup>143</sup> unless these are severable and retain their value in the hands of the claimant notwithstanding the seizure of the related property.

174. Thirdly, there is the much smaller group of cases where the only right affected is incorporeal; these come closest to the present claim of contractual non-performance. *Cook* was such a case, and (if it is properly classified as an instance of expropriation, which is doubtful) so was *Singer Sewing Machine Co. v. The Republic of Turkey*. In such cases, simply to assert that “property rights are created under and by virtue of a contract” is not sufficient.<sup>144</sup> The mere non-performance of a contractual obligation is not to be equated with a taking of property, nor (unless accompanied by other elements) is it tantamount to expropriation. Any private party can fail to perform its contracts, whereas nationalization and expropriation are inherently governmental acts, as is envisaged by the use of the term “measure” in Article 1110(1). It is true that, having regard to the inclusive definition of “measure”,<sup>145</sup> one could envisage conduct tantamount to an expropriation which consisted of acts and omissions not specifically or exclusively governmental. All the same, the normal response by an investor faced with a breach of contract by its governmental counter-party (the breach not taking the form of an exercise of governmental prerogative, such as a legislative decree) is to sue in the appropriate court to remedy the breach. It is only where such access is legally or practically foreclosed that the breach could amount to an definitive denial of the right (i.e., the effective taking of the chose in action) and the protection of Article 1110 be called into play.

175. The Tribunal concludes that it is one thing to expropriate a right under a contract and another to fail to comply with the contract. Non-compliance by a government with contractual obligations is not the same thing as, or equivalent or tantamount to, an expropriation. In the present case the Claimant did not lose its contractual rights, which it was free to pursue before the contractually chosen forum. The law of breach of contract is not secreted in the interstices of Article 1110 of NAFTA. Rather it is necessary to show

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<sup>143</sup> See, e.g., *Starrett Housing Corporation v. Government of the Islamic Republic of Iran* (1987) 16 Iran-US CTR 112, 230-1 (paras. 361-2).

<sup>144</sup> See *Shufeldt Claim*, (1930) 2 RIAA 1083, 1097. This was a case of legislative invalidation of a concession agreement 6 years after its inception.

<sup>145</sup> Article 201 defines “measure” as including “any law, regulation, procedure, requirement or practice”.

an effective repudiation of the right, unredressed by any remedies available to the Claimant, which has the effect of preventing its exercise entirely or to a substantial extent.

176. In the present case, in the Tribunal's view, this has not been shown. The question here is not one of final refusal to pay (combined with effective obstruction and denial of legal remedies); it is one of neglect and failure at the contractual level in the context of a marginal enterprise. That does not pass the test for an expropriatory taking of contractual rights as it emerges from the decisions analysed above.

(iv) *Conclusion as to Article 1110*

177. In the Tribunal's view, it is not the function of the international law of expropriation as reflected in Article 1110 to eliminate the normal commercial risks of a foreign investor,<sup>146</sup> or to place on Mexico the burden of compensating for the failure of a business plan which was, in the circumstances, founded on too narrow a client base and dependent for its success on unsustainable assumptions about customer uptake and contractual performance. A failing enterprise is not expropriated just because debts are not paid or other contractual obligations are not fulfilled. The position may be different if the available legal avenues for redress are blocked or are evidently futile in the face of governmental intransigence. But this was not the case here. The Claimant's decision not to proceed with the CANACO arbitration may have been understandable, but taking into account all the circumstances it did not implicate Mexico in a breach of Article 1110 any more than of Article 1105.<sup>147</sup>

178. For all these reasons, in the Tribunal's view, there was nothing which could be properly described as an expropriation by Mexico of Waste Management's property, assets or investment, or a measure tantamount to such expropriation, within the meaning of NAFTA Article 1110. The Claimant's case on Article 1110, like that on Article 1105, must fail.

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<sup>146</sup> Cf. *Marvin Feldman v. Mexico*, ICSID Case No. ARB(AF)/99/1, Award of 16 December 2002, para. 111.

<sup>147</sup> See above, para. 118-132 for an analysis of the remedies sought by Acaverde in the context of Article 1105.

#### D. THE ISSUE OF COSTS

179. Turning to the question of the costs and expenses of the proceeding, no question arises as to the costs of the first proceeding, which were dealt with by the first Tribunal.<sup>148</sup>

180. In its decision of 26 June 2002, this Tribunal reserved the question of costs on Mexico's preliminary objection, as to which the Claimant was successful.

181. As is now unfortunately common, there were a significant number of interlocutory issues raised by both parties during the proceedings.

182. As to the merits, in the Tribunal's view the proceedings were expeditiously and efficiently conducted by the representatives of both parties.

183. There is no rule in international arbitration that costs follow the event. Equally, however, the Tribunal does not accept that there is any practice in investment arbitration (as there may be, at least *de facto*, in the International Court and in interstate arbitration) that each party should pay its own costs. In the end the question of costs is a matter within the discretion of the Tribunal, having regard both to the outcome of the proceedings and to other relevant factors.

184. In circumstances where the conduct of the City is by no means beyond criticism, the Tribunal concludes that a fair outcome would be an order that each party bear its own legal costs and expenses, and that the costs and expenses of the Tribunal be borne equally between them.

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<sup>148</sup> *Waste Management, Inc. v. United Mexican States*, Award, 2 June 2000, 5 ICSID Reports 443, 461-2.

**AWARD**

For the foregoing reasons, the Tribunal unanimously DECIDES:

- (a) That the claim is admissible under Chapter 11 of NAFTA;
- (b) That the conduct of the Respondent which is the subject of the claim did not involve any breach of Article 1105 or 1110 of NAFTA;
- (c) That Waste Management's claim is accordingly dismissed in its entirety;
- (d) That each Party shall bear its own costs and half of the costs and expenses of these proceedings.

Done at Washington, D.C. in English and Spanish, both versions being equally authoritative.

Professor James Crawford  
President of the Tribunal

Mr. Benjamin R. Civiletti  
Member

Mr. Eduardo Magallón Gómez  
Member