INTERNATIONAL CENTRE FOR SETTLEMENT

OF INVESTMENT DISPUTES

RAILROAD DEVELOPMENT CORPORATION

Claimant

v.

THE REPUBLIC OF GUATEMALA

Respondent

ICSID Case No. ARB/07/23

REBUTTAL REPORT OF ROBERT F. MACSWAIN

Rebuttal Report of Robert F. MacSwain

1. My name is Robert F. MacSwain. I previously provided a report in this proceeding dated May 18, 2009 entitled "Fair Market Valuation of Right of Way, Yard and Station Real Estate Granted in Usufruct to Ferrovías Guatemala." My address and qualifications remain the same as in my initial report.

2. The purpose of this rebuttal report is to revise and restate my prior analysis and valuation of the right-of-way and real estate properties that were granted in usufruct to FVG as of the time immediately prior to the issuance of the Government of Guatemala's *Lesivo* Declaration on August 25, 2006. I will also discuss and respond to certain arguments and criticisms of my initial analysis by Respondent's expert witness, Dr. Pablo T. Spiller, in his statement dated October 4, 2010 entitled "Comments to RDC's Damage Assessment." My report is organized in two sections: **I. Revised Valuation of Long-Term Utility Easements** and **II. Revised Valuation of Station and Station Yard Leases.**

I. <u>Revised Valuation of Long-Term Utility Easements</u>

3. In my original report, I explained that, in my opinion, it is reasonable to expect that, but for the *Lesivo* Declaration, FVG would have continued to earn income through the remaining 42-year term of the usufruct from its four existing long-term utility easement agreements (Planos y Puntos/Gesur, Texaco Guatemala, Zeta Gas and Genor). In his report, Dr. Spiller does not dispute my analysis of and income projections for these easements. Accordingly, I have not made any adjustments to these projections.

4. Dr. Spiller, however, disagrees with my opinion that, in addition to the four utility easements that FVG entered into prior to the *Lesivo* Declaration, it is reasonable to expect that FVG would have entered into additional easement agreements for telecommunications and electric transmission covering both the main lines (Atlantic and Pacific) and rural spur lines. Dr. Spiller also criticizes my assumption that these easement contracts would have been priced at $3,200 per km for the main lines. In Dr. Spiller's opinion, there is not sufficient evidence to support these assumptions.

5. I continue to believe that my assumptions are supportable and quite reasonable. Dr. Spiller's contention that there was no demand for additional utility easements along the right-of-way ignores the fact that, prior to the *Lesivo* Declaration, **555.67 km** of the right-of-way was

already being used for utility transmission. This included not only FVG's four existing utility easement contracts covering a total of 72.82 km, but also the six pre-*lesivo* industrial squatters which covered an additional 482.85 km.[1] This large scale presence of industrial squatters demonstrates that there was, prior to the *Lesivo* Declaration, strong existing demand by utilities to use the right-of-way for transmission purposes. This strong demand has been further confirmed since the *Lesivo* Resolution, as it is my understanding that industrial squatters are now present on essentially the *entire right-of-way*. Attached as **Annex 1** is a map of the right-of-way (main and rural spur lines) granted in usufruct to FVG which identifies the current industrial squatters (power companies EEGSA, INDE, DEORSA and DEOCSA) and where their unauthorized utility poles and power lines are currently located. Annex 3 to the Third Statement of Jorge Senn consists of photographs of industrial squatters that were taken by FVG in February and March 2011. It is quite reasonable to assume that, had the *Lesivo* Declaration not occurred, FVG would have taken steps to either legalize these industrial squatters by entering into long-term easement agreements with them or FVG would have had them evicted and other utilities would have taken their place.

6. Another factor that supports my conclusion that FVG's right-of-way would have engendered significant demand for utility transmission is that most of the right-of-way did *not* have an operating railroad at the time of the *Lesivo* Declaration. Any utility company would confirm that the use of a non-operating railway right-of-way for transmission purposes is superior to an operating right-of-way due to ease of construction, the ease of maintenance and, most importantly, not having to worry about train derailments with concurrent damage to utility poles and pipes. Accordingly, contrary to Dr. Spiller, I believe there is more than sufficient evidence in the record to support my assumption that, absent the *Lesivo* Declaration, there was significant demand by utilities to enter into additional long-term easement contracts with FVG to justify my valuations.

7. Dr. Spiller also questions the $3,200 per km value that I have used for the main line right-of-way easements. The $3,200 per km value was derived from the preliminary agreement FVG negotiated with power line supplier Gesur in 2006 to add 32 km to its existing easement contract that would have averaged over $3,200 per km over the term of the agreement.

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[1] *See* First MacSwain Report § 6.0.

That agreement was never consummated because of the *Lesivo* Resolution.[2] Based on my over 25 years of experience in the railroad real estate business, it is a common and accepted practice that the last agreed upon price for use of a right-of-way "sets the bar" for future valuations. Thus, I remain of the opinion that it is reasonable and proper to use the $3,200 per km valuation that FVG had negotiated with Gesur on the eve of the *Lesivo* Resolution as the basis for valuing future the easement agreements it would have entered into for the main lines of the railway. For the rural spur lines, where utility transmission demand would be lower, I have reduced the valuation to $1,200 per km, or approximately one third of the main line valuation.

8. Besides the $3,200/$1,200 per km pricing, I am also of the strong opinion that the other key financial terms of the utility easements I have projected are reasonable. In my projections, I have assumed that the two utility easement contracts would have been for an initial 20-year term with 5% inflation increases every five (5) years and three (3) five (5)-year renewal options. These terms are based not only on the terms of the easement agreements FVG entered into prior to the *Lesivo* Declaration, but also on my own experience in personally negotiating and executing on behalf of Florida East Coast Railway, Boston & Maine Railroad, Delaware & Hudson Railway, Maine Central Railroad, Canadian National Railway, Canadian Pacific Railroad, Illinois Central Railroad and New York City Transit several long-term rights-of-way easement agreements with AT&T, Sprint, BellSouth, MCI and other utilities. None of the agreements I negotiated were for less than 20 years with 3 to 5-year renewal options and a minimum of 5% inflation increases for each option period, and for a price of less than $5,000 per mile per annum.

9. I have, however, made some adjustments to my original easement valuation analysis to address some of Dr. Spiller's criticisms and also to factor in revised information which has come to my attention since I submitted my original report. First, in my initial report, my right-of-way easement valuations were based upon the main right-of-way (Atlantic and Pacific) totaling 495 km and the rural spur lines totaling 185.40 km. However, I have since learned that the correct total distance of the main right-of-way is 644.04 km and the rural spur lines is 157.72 km, as shown on **Annex 1**.

10. In response to Dr. Spiller's criticism that my original analysis unrealistically assumes that the entire rail network would have been covered by easement agreements in 2007,

[2] *See* Statement of Planos y Puntos/Gesur dated June 17, 2009.

in my revised analysis I have assumed for the main line easements that there would have been a ramp up period from 2007-2012, with 10% occupancy in 2007, 20% occupancy in 2008, 40% occupancy in 2009, 50% occupancy in 2010 and 60% occupancy in 2011, achieving full occupancy in 2012 with a 20% vacancy applied. I believe this is a more than realistic assumption given the fact that, as of 2006, 555.67 km of the main lines were already occupied for electric and gas transmission. Therefore, the main rights-of-way would generate the following cash flow from long term easements:

644.04 kilometers @ $3,200 per kilometer	
<u>Ramp Up</u>	
Year 2007 @ 10% occupancy	$ 412,186 per annum
Year 2008 @ 20% occupancy	$ 824,372 per annum
Year 2009 @ 40% occupancy	$1,648,744 per annum
Year 2010 @ 50% occupancy	$2,060,928 per annum
Year 2011 @ 60% occupancy	$2,473,114 per annum
Begin Year 2012	
Years 1-5	$4,121,856
Less 20% vacancy	$ 824,372
Net Years 1-5	$3,297,484 per annum
Years 6-10	$4,327,948
Less 15% vacancy	$ 649,192
Net Years 6-10	$3,678,756 per annum
Years 11-15	$4,544,346
Less 5% vacancy	$ 227,218
Net Years 11-15	$4,317,128 per annum
Years 16-20	$4,771,564
No vacancy	$ 0
Net Years 16-20	$4,771,564 per annum
Years 21-25 1st Renewal	$5,010,142
No vacancy	$ 0
Net Years 21-25	$5,010,142 per annum
Years 26-30 2nd Renewal	$5,260,649
No vacancy	$ 0
Net Years 26-30	$5,260,649 per annum
Years 31-37 3rd Renewal	$5,523,681

No vacancy	$ 0
Net Years 31-37	$5,523,681 per annum

11. For the rural spur lines, I now assume that utility easements on those lines would not have begun until 2011 rather than 2007, and that there would have been a ramp-up period beginning in 2011 with 10% occupancy in 2011, 20% occupancy in 2012, 40% occupancy in 2013, 50% occupancy in 2014, and 60% occupancy in 2015, with full occupancy in 2016 with 25% vacancy. The rural spur lines would have generated the following income from long-term easements:

157.72 kilometers @ $1,200 per kilometer	
<u>Ramp Up</u>	
Begin Year 2011	
Year 2011 @ 10% occupancy	$ 37,853 per annum
Year 2012 @ 20% occupancy	$ 75,706 per annum
Year 2013 @ 40% occupancy	$151,411 per annum
Year 2014 @ 50% occupancy	$189,264 per annum
Year 2015 @ 60% occupancy	$227,117 per annum
Begin Year 2016	
Years 1-5	$378,528
Less 25% vacancy	$ 94,632
Net Years 1-5	$283,896 per annum
Years 6-10	$397,454
Less 15% vacancy	$ 59,618
Net Years 6-10	$337,836 per annum
Years 11-15	$417,327
Less 5% vacancy	$ 20,866
Net Years 11-15	$396,461 per annum
Years 16-20	$438,193
No vacancy	$ 0
Net Years 16-20	$438,193 per annum
Years 21-25 1st Renewal	$460,103
No vacancy	$ 0
Net Years 21-25	$460,103 per annum

Years 26-32 2nd Renewal	$483,108
No vacancy	$ 0
Net Years 26-32	$483,108 per annum

II. Revised Valuation of Station and Station Yard Leases

12. Dr. Spiller dismisses all of my projected valuations for station and station yard leases that FVG would have entered into absent the *Lesivo* Declaration as too speculative because of an absence of specific documentation supporting my assumptions. Thus, Dr. Spiller is of the opinion that, even in the absence of the *Lesivo* Resolution, FVG would not have been successful in leasing *any* of the station and station yard real estate over the remaining 42-year term of the usufruct.

13. Dr. Spiller's position is difficult to comprehend. As I describe in my initial report, the station and station yard properties granted in usufruct to FVG are located in the center core of the most populated cities, towns and communities in Guatemala. Dr. Spiller's analysis seems to give no credence to *any* commercial leasing activity taking place on these prime location properties at any price over a 42-year period. In other words, Dr. Spiller's position is that, prior to the *Lesivo* Resolution, the 22 analyzed usufruct properties were totally without value; he entirely negates all of the usufruct real estate assets. I do not view such a position to be even remotely reasonable.

14. In my initial analysis, I attempted to value the real estate as conservatively as possible to take into account the obvious uncertainties associated with estimating and projecting valuations 42 years into the future. Nevertheless, to make my projections even more conservative, I have made some additional adjustments to my prior analysis, each of which has the effect of *lowering* most of my previously estimated real estate valuations. In particular, in my revised real estate analysis, I have made the following changes:

(i) I have removed all inflationary increases in rents except for six (6) parcels (Zacapa Retail and Industrial, El Rancho, Gerona Station and Parking Lot and Escuintla);

(ii) For the parcels that have inflationary increases, I have used a very conservative assumption of 10% every five years after the first ten years (2% per annum), except for the Gerona Parking Lot, which has a 10% inflation rent adjustment every five years starting in 2007;

(iii) I have delayed the lease start dates for all properties for an additional five (5) years except for Zacapa Industrial and Gerona Parking Lot; and

(iv) I have removed any projected improvements to the leased properties, so that all projected leases are now based upon unimproved land.

15. Dr. Spiller questions the validity of my projected 10% return on leases of unimproved centrally located land, and, with a few exceptions, no rent increases over 42 years. In reality, 10% is far too low of a return for that risk, because any lending institution granting funds to a tenant on FVG's real estate would have required a subordination to the leasehold. In my several years in real estate lending and developing, the only raw land leases at a less than 10% return were for AAA credits and even then, if subordination were required, the rates of return would be greater than 10%. Thus, using a 10% return in my projections further substantiates how conservative my analysis is.

16. Based on the foregoing, my revised valuations for the station and station yard leases[3] are as follows:

16.1 <u>Gerona Parking Lot</u>

This is the only real estate parcel analysis that remains the same as in my original May 18, 2009 report. My description of the potential use of and demand for the Gerona property provided in paragraph 7.2(g)(2) in the original report is further substantiated by recent photographs that were taken of the area on February 3, 2011, which show several cars being parked on the property during the daytime.[4] These photographs confirm my original assessment that there is high demand for using this property as a parking lot due to its close proximity to the new prosecutor offices which opened in 2006. However, I have not made any changes to my prior valuation in order to maintain the conservative approach to this rebuttal.

Beginning in year 2007 and using a 10% inflationary rent increase every five years, absent the *Lesivo* Declaration, the Gerona Parking Lot would have generated the following annual rents for the five-year terms, through the 42 remaining years of the Usufruct:

Years 1-5	$153,156 per annum
Years 6-10	$168,472 per annum
Years 11-15	$185,319 per annum
Years 16-20	$203,851 per annum

[3] The geographical location of the real estate parcels that I believe would have been leased is shown on **Annex 1** to this report.

[4] **Annex 2**, February 3, 2011 photographs of Gerona Parking Lot area.

Years 21-25	$224,236 per annum
Years 26-30	$246,659 per annum
Years 31-35	$271,325 per annum
Years 36-42	$298,458 per annum

16.2 The next five analyzed properties all continue to contain inflationary increases because of the specific locations, population growth, increasing real estate values and immediate and long-term viability. The inflation rate is a conservative 10% every five years after the first ten years.

a. <u>Zacapa Industrial and Zacapa Retail</u>

My analysis of the Zacapa Industrial and Zacapa Retail properties submitted in my original May 18, 2009 report remains the same (see paragraph 7.2(e)). Without the *Lesivo* Declaration, negotiations with Grupo Unisuper (supermarket) and Maersk (container loading) would have led to completed lease transactions and been the impetus for further retail and industrial development of these properties. Recent photographs of the Zacapa property demonstrate that its size and central location would allow both significant retail and industrial development.[5] The Zacapa location is specifically perfectly located to transload shipments from the Ports of Puerto Barrios and Santo Tomás to be delivered by truck or rail to north and central Guatemala locations.

<u>Zacapa Industrial</u>
Initial report
Land improvements
20% vacancy rates
5% inflation every 10 years
This Report
No land improvements
25% vacancy rates
10% inflation every 5 years after first 10 years
Begin Year 2007
Value = 1,251,043 sf @ $2.40 psf = $3,002,503
10% annual return = $300,250
Begin year 2007

5 **Annex 3,** photographs of Zacapa station and station yard.

Years 1-10	$300,250 per annum
Less 25% vacancy	$225,188 per annum
Years 11-15	$330,275 per annum
Less 25% vacancy	$247,707 per annum
Years 16-20	$363,303 per annum
Less 25% vacancy	$272,477 per annum
Years 21-25	$399,633 per annum
Less 25% vacancy	$299,725 per annum
Years 26-30	$439,596 per annum
Less 25% vacancy	$329,697 per annum
Years 31-35	$483,556 per annum
Less 25% vacancy	$362,667 per annum
Years 36-42	$531,912 per annum
Less 25% vacancy	$398,934 per annum

Zacapa Retail

Initial report

Land improvements
20% vacancy rates
Begin Year 2007
5% inflation every 10 years

This Report

No land improvements
25% vacancy rates
10% inflation every 5 years after first 10 years
Begin Year 2012

Value = 239,580 sf @ $2.80 psf = $670,824
10% annual return = $67,082

Begin year 2012

Years 1-10	$ 67,082 per annum
Less 25% vacancy	$ 50,312 per annum
Years 11-15	$ 73,790 per annum
Less 25% vacancy	$ 55,343 per annum

Years 16-20	$ 81,169 per annum
Less 25% vacancy	$ 60,877 per annum
Years 21-25	$ 89,286 per annum
Less 25% vacancy	$ 66,965 per annum
Years 26-30	$ 98,215 per annum
Less 25% vacancy	$ 73,662 per annum
Years 31-37	$108,037 per annum
Less 25% vacancy	$ 81,028 per annum

b. Gerona Station

As described in my initial report (paragraph 7.2(g)(1)), this is a very well-located property, just one mile from the center of Guatemala City. Significant developer interest for parking and commercial development had occurred prior to the *Lesivo* Decree, but all of the potential developers retracted their interest after the Decree.

Gerona Station	
Initial report	
Land improvements	
20% vacancy rates	
Begin Year 2007	
5% inflation every 10 years	
This Report	
No land improvements	
25% vacancy rates	
10% inflation every 5 years after first 10 years	
Begin Year 2012	
Value = 1,049,832 sf @ $3.00 psf = $3,149,496	
10% annual return = $314,950	
Begin year 2012	
Years 1-10	$314,950 per annum
Less 25% vacancy	$236,212 per annum
Years 11-15	$346,445 per annum
Less 25% vacancy	$259,833 per annum
Years 16-20	$381,090 per annum
Less 25% vacancy	$285,817 per annum

Years 21-25	$419,199 per annum
Less 25% vacancy	$314,398 per annum
Years 26-30	$461,119 per annum
Less 25% vacancy	$345,838 per annum
Years 31-37	$507,231 per annum
Less 25% vacancy	$380,422 per annum

c. El Rancho

My analysis of El Rancho in my initial report (paragraph 7.2(f)) remains the same except the population continues to grow and the need for retail and distribution/warehouse would have continued to exist.

El Rancho	
Initial report	
Land improvements	
20% vacancy rates	
Begin Year 2007	
5% inflation every 10 years	
This Report	
No land improvements	
25% vacancy rates	
10% inflation every 5 years after first 10 years	
Begin Year 2012	
Value = 414,999 sf @ $2.75 psf = $1,141,247	
10% annual return = $114,125	
Begin year 2012	
Years 1-10	$114,125 per annum
Less 25% vacancy	$ 85,594 per annum
Years 11-15	$125,536 per annum
Less 25% vacancy	$ 94,153 per annum
Years 16-20	$138,090 per annum
Less 25% vacancy	$103,568 per annum
Years 21-25	$151,899 per annum
Less 25% vacancy	$113,925 per annum

Years 26-30	$167,090 per annum
Less 25% vacancy	$125,317 per annum
Years 31-37	$183,799 per annum
Less 25% vacancy	$137,849 per annum

d. Escuintla

Escuintla was described in paragraph 7.2(n) of my initial report. The retail opportunities of Escuintla would have continued to be readily available as the population continues to grow.

Escuintla

Initial report

Land improvements
20% vacancy rates
Begin Year 2007
5% inflation every 10 years

This Report

No land improvements
25% vacancy rates
10% inflation every 5 years after first 10 years
Begin Year 2012

Value = 647,499 sf @ $3.25 psf = $2,104,372
10% annual return = $210,437

Begin year 2012

Years 1-10	$210,437 per annum
Less 25% vacancy	$157,828 per annum
Years 11-15	$231,481 per annum
Less 25% vacancy	$173,611 per annum
Years 16-20	$254,629 per annum
Less 25% vacancy	$190,972 per annum
Years 21-25	$280,092 per annum
Less 25% vacancy	$210,069 per annum
Years 26-30	$308,101 per annum
Less 25% vacancy	$231,076 per annum
Years 31-37	$338,911 per annum

Less 25% vacancy	$254,183 per annum

16.3 The properties listed below were analyzed in my initial report. In order to make my valuations of these properties even more conservative, I have revised them so that no inflation is applied and most lease start dates have been moved to a later time frame:

a. Puerto Barrios
Initial report – Start date 2007
This report – Start date 2012
$78,164 per annum for 37 years

b. Bananera
Initial report – Start date 2007
This report – Start date 2012
$10,688 per annum for 37 years

c. Quirigua
Initial report – Start date 2007
This report – Start date 2014
$18,750 per annum for 35 years

d. Gualan Retail
Initial report – Start date 2007
This report – Start date 2014
$8,494 per annum for 35 years

e. Gualan Warehouse
Initial report – Start date 2007
This report – Start date 2012
$17,152 per annum for 37 years

f. Guatemala City
Initial report – Start date 2007, 2% inflation increase every 10 years and 20% vacancy
This report – Start date 2009, no inflation increase and 25% vacancy
$97,879 per annum for 40 years

g. Mazatenango
Initial report – Start date 2007
This report – Start date 2016
$108,884 per annum for 32 years

h. Retalhuleu
Initial report – Start date 2007
This report – Start date 2016
$28,205 per annum for 32 years

i. Tecún Umán
Initial report – Start date 2007, 20% vacancy
This report – Start date 2012, 25% vacancy
$82,687 per annum for 37 years

j. Amatitlan
Initial report – Start date 2007
This report – Start date 2014
$50,156 per annum for 35 years

k. Chiquimula
Initial report – Start date 2007
This report – Start date 2016
$33,906 per annum for 32 years

l. Coatepeque
Initial report – Start date 2012
This report – Start date 2016
$25,438 per annum for 32 years

m. Palin
Initial report – Start date 2012
This report – Start date 2012
$42,000 per annum for 37 years

n. Ipala
Initial report – Start date 2020
This report – Start date 2020
$17,063 per annum for 28 years

o. Anguiatú
Initial report – Start date 2020
This report – Start date 2020
$23,100 per annum for 28 years

p. San Jose
Initial report – Start date 2020
This report – Start date 2020
$112,678 per annum for 28 years

17. In summary, I believe my real estate valuations remain quite reasonable because they have been valued using the following conservative assumptions:

1. Delayed lease start dates for almost all properties;
2. Significant vacancy rates throughout the leasehold terms;

3. Very low real estate per square foot valuations ranging from $1 - $4 despite the good to excellent centralized locations of the properties;
4. No inflation – except for the six noted properties;
5. The six properties with inflation adjustments in rent are at a very conservative 2% per annum**;**
6. No improved real estate; and
7. Low 10% return.

18. One additional adjustment from my original analysis is for the projected FVG income from the Chiquita/COBIGUA lease in Puerto Barrios. The income was increased for 2007-2014 by using a rate of escalation based on FVG's AVERAGE actual experience from 2002 to 2006 (11%). The rent under the COBIGUA lease is based directly on traffic in the port on which FVG has received 2% of the gross revenues (and on which FEGUA is to receive a like amount through 2014). The terms of the agreement specify that, commencing in March, 2015, FVG will receive 4% of COBIGUA's gross revenues through February 2048. After 2014, the COBIGUA income is escalated at the rate used by Dr. Spiller (3.47%). Thus, my adjusted projected income from the COBIGUA lease is as follows:

COBIGUA		
2007	$382,684	
2008	$424,779	
2009	$471,505	
2010	$523,371	
2011	$580,941	
2012	$644,845	
2013	$715,778	
2014	$794,513	
*2015	$1,507,152	*Income escalated @ 3.47% annually per Dr. Spiller's estimate. FVG to receive 4% of COBIGUA gross revenues through February 2048.
2016	$1,701,218	
2017	$1,760,251	
2018	$1,821,331	
2019	$1,884,531	
2020	$1,949,925	
2021	$2,017,587	
2022	$2,087,597	

2023	$2,160,037
2024	$2,234,990
2025	$2,312,544
2026	$2,392,790
2027	$2,475,820
2028	$2,561,731
2029	$2,650,623
2030	$2,742,599
2031	$2,837,767
2032	$2,936,238
2033	$3,038,125
2034	$3,143,548
2035	$3,252,629
2036	$3,365,496
2037	$3,482,278
2038	$3,603,113
2039	$3,728,141
2040	$3,857,508
2041	$3,991,363
2042	$4,129,864
2043	$4,273,170
2044	$4,421,449
2045	$4,574,873
2046	$4,733,621
2047	$4,897,878
2048	$5,067,834

Respectfully submitted,

Robert F MacSwain

Robert F. MacSwain

March 15, 2011