**To:** **Sr. Gregorio Canales**
**Director**
**Dirección General de Inversión Extranjera**
**Secretaría de Economía**
**Insurgentes Sur 1940, piso 8**
**Col. Florida**
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**México**

# NOTICE OF INTENT TO SUBMIT A CLAIM TO ARBITRATION UNDER SECTION B, CHAPTER 11 OF THE NORTH AMERICAN FREE TRADE AGREEMENT

Pursuant to Article 1119 of the North American Free Trade Agreement (NAFTA), notice is hereby given to the United Mexican States (Mexico) that the disputing investors (Claimants) intend to submit to arbitration their claim for damages arising from Mexico's violation of Chapter 11, Articles 1102 and 1110, of NAFTA, as more fully described herein.

This notice of intent is delivered in two languages, English and Spanish. If the two versions conflict, the English version will govern.

## I. Identity of Disputing Investors (Claimants)

Claimants are 17 Texas irrigation districts serving the Rio Grande Valley, which bring this action on their own behalf and of farmers, ranchers, and landowners, who depend upon the irrigation water from the Rio Grande for use on approximately 400,000 acres of agricultural land, 29 independent water rights holders who do not receive their water through any irrigation district, and a water supply company. Claimants hold the fully adjudicated exclusive legal right to withdraw 1,227,596 acre-feet of water annually from the lower Rio Grande River (also known as Rio Bravo). A list of the names and addresses of Claimants, together with a statement of the quantity of water each is legally entitled to receive annually, is attached as Exhibit A.

## II. Provisions of NAFTA That Have Been Violated

The North American Free Trade Agreement (NAFTA), signed by Canada, Mexico, and the United States in 1992, was the first regional or multilateral investment treaty to include a comprehensive investment chapter providing for binding investor-nation arbitration. This investor-nation dispute resolution embodied in Chapter 11 has been hailed as the single most significant legal development which has taken place through the NAFTA. Chapter 11 confers on individual investors the right to bring international legal disputes directly against a host nation, a right that traditionally belonged only to other nation states.

Claimants intend to submit for arbitration their claim that Mexico has violated Chapter 11, Articles 1102 and 1110 of NAFTA. Article 1102, "National Treatment," provides that NAFTA parties shall treat investors of another party no less favorably than they treat their own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments. NAFTA, ch. 11, art. 1102.[1] Article 1110, "Expropriation and Compensation," provides that

[1] Article 1102 states in pertinent part:

> 1. Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
>
> 2. Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
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> 3. The treatment accorded by a Party under paragraphs 1 and 2 means, with respect to a state or province, treatment no less favorable than the most favorable treatment accorded,

NAFTA parties must not expropriate investments, either directly or indirectly, or through a measure tantamount to an expropriation, unless such expropriation is for a public purpose, is non-discriminatory, is in accordance with due process of law and the prescribed international minimum standards of treatment under Article 1105(1), and is accompanied by compensation at fair market value. NAFTA, ch. 11, art. 1110.[2]

## III. Factual Basis for the Claim

From 1992 to 2002, Mexico captured, seized, and diverted to the use of Mexican farmers, an investment (approximately 1,013,056 acre-feet of irrigation water) located in Mexico and owned by Claimants. By diverting Claimants' water to Mexican farmers, Mexico dramatically increased its irrigated agricultural production on the Mexican side of the Rio Grande, while the crops of United States farmers in the Rio Grande Valley shriveled. Mexico thus treated the investments of United States investors less favorably than it treated its own investors with respect to the establishment, acquisition, expansion,

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> in like circumstances, by that state or province to investors, and to investments of investors, of the Party of which it forms a part. . . .

[2] Article 1110 states in pertinent part:

> 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:
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> (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.
>
> 2. Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation"), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.
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> 3. Compensation shall be paid without delay and be fully realizable. . . .

management, conduct, operation, and sale or other disposition of investments in violation of Article 1102 of NAFTA. Mexico also nationalized or expropriated Claimants' investment within Mexico, or took a measure tantamount to nationalization or expropriation of such an investment, unfairly and without compensation and due process in violation of Article 1110 of NAFTA.

1. The Rio Grande River (also known as Rio Bravo) forms more than 1,200 miles of the border between the United States and Mexico, stretching from north of El Paso, Texas to the Gulf of Mexico. The principal sources of the waters of the Rio Grande are the Conchos, San Diego, San Rodrigo, Escondido and Salado Rivers and the Las Vacas Arroyo, all of which rise in Mexico. These six Rio Grande tributaries drain approximately 53,450 square miles of Mexico. The largest and farthest upstream of the tributaries is the Rio Conchos, which flows into the Rio Grande upstream of one of the two international reservoirs on the Rio Grande, Amistad Reservoir. The other international reservoir on the Rio Grande is the Falcon Reservoir; it receives water from the other five tributaries, including the Rio Salado, which is the second largest and runs directly into the Falcon Reservoir.

2. In 1944, the United States and Mexico entered into a treaty "to fix and delimit the rights of the two countries with respect to the waters . . . of the Rio Grande (Rio Bravo) from Fort Quitman, Texas, United States of America, to the Gulf of Mexico, in order to obtain the most complete and satisfactory utilization thereof . . ." Treaty Between the United States of America and Mexico Respecting Utilization of Waters of the Colorado and Tijuana Rivers and of the Rio Grande, Feb. 3, 1944, U.S.-Mexico, TS No. 944. The 1944 Treaty allocated to the United States "[o]ne-third of the flow reaching

the main channel of the Rio Grande (Rio Bravo) from the Conchos, San Diego, San Rodrigo, Escondido and Salado Rivers, provided that this third shall not be less, as an average amount in cycles of five consecutive years, than 350,000 acre-feet (431,721,000 cubic meters) annually . . . .” *Id*. § II, art. 4(B)(c).

3. Under the terms of the 1944 Treaty, the United States and Mexico have constructed two dams and reservoirs to capture the waters of the Rio Grande and make them available for agricultural irrigation and other purposes. The Amistad Reservoir was completed in 1968; the Falcon Reservoir was completed in 1953. Both are jointly managed by the United States and Mexico and are used for the purpose of storing water for irrigation and municipal use in both countries.

4. In the Rio Conchos Basin, Mexico has also constructed seven reservoirs, the last of which was completed in 1993:

- San Gabriel Reservoir was completed on the Florido River in 1981; it holds 0.21 million acre-feet and is used for irrigation.

- Pico de Aguila Reservoir was completed on the Florido River in 1993; it holds 0.045 million acre-feet of water and is used for irrigation.

- La Boquilla Reservoir was completed in 1916 on the Conchos River; it holds 2.34 million acre-feet of water and is used for irrigation and hydroelectricity.

- La Colina Reservoir was completed on the Conchos River in 1927, holds 0.195 acre-feet of water and is used for irrigation and hydroelectricity.

- Francisco I. Madero Reservoir was completed in 1949 on the San Pedro River; it holds 0.28 acre-feet of water and is used for irrigation and sediment control.

- Chihuahua Reservoir was completed on the Chuviscar River in 1960; it holds 0.021 million acre-feet of water and is used for municipal water, irrigation and flood control.

- Luis L. Leon Reservoir was completed on the Conchos River in 1968; it holds 0.29 million acre-feet of water and is used for irrigation and flood control.

5. Since 1992, Mexico has operated these dams and reservoirs to artificially manipulate the flows of the tributaries to the Rio Grande so as to divert the natural flows of those tributaries, one-third of which (a minimum of 350,000 acre-feet per year) is allotted by the 1944 Treaty to the United States (and owned by Claimants), in violation of both the terms of the 1944 Treaty and Chapter 11, Articles 1102 and 1110 of NAFTA. In the 1992-1997 cycle, Mexico delivered only 726,151 acre-feet of water, accumulating a deficit of 1,023,847 acre-feet. During that same time, approximately 4,350,000 acre-feet of excess water was stored in 12 Mexican reservoirs located in the 1944 Treaty tributary basins, after diversions and releases by Mexico to meet its own water demands and another 5,900,000 acre-feet of excess water was stored in the reservoirs through October 1999, all of which could have been released downstream to the Rio Grande to meet the minimum United States allotment under the 1944 Treaty.

Texas Agriculture Commissioner Susan Combs presented satellite photos of Mexican reservoirs and irrigated cropland to State Department officials in the fall of 2003 showing the availability of water that could have been released to the United States under the 1944 Treaty. In the Luis Leon Reservoir alone, excess flood inflows were available during all of 1993, half of 1994, and half the time from fall 1996 to spring 1999, water which could have been released to the United States during the time deficits were being incurred. In fact, from 1992 to October 1999, Mexico kept all of the water that fell above the Luis Leon Reservoir, retaining approximately 5 million acre-feet of extra water that could have been used to erase the deficit.

6. From October 1, 1997 to September 30, 2000, Mexico delivered only 407,088 acre-feet of water to the United States, bringing the total deficit plus current cycle obligation to 1,381,362 acre-feet. On April 6, 2002, the water deficit had reached 1,476,181 acre-feet. Although Mexico was allowed to defer this water debt for one five-year cycle (1997-2002), under Section II, Article 4 of the 1944 Treaty, this entire water debt of 1,476,181 acre-feet became due and payable in October 2002.

7. Claimants are the legal owners of 1,013,056 acre-feet of the irrigation water wrongfully withheld and diverted from the Rio Grande by Mexico. These water rights are a valuable investment, the expropriation and diversion of which has severely damaged the ability of Claimants and the farmers they represent to produce crops. For example, irrigated acreage in Cameron, Hidalgo, and Willacy counties has decreased by about 29 percent, or 103,210 acres, since 1992. The average loss in business activity in the region from 1998 to 2001 was estimated to be US$367.6 million per year. The average irrigation use per year in the Texas portion of the Rio Grande Valley decreased by 563,826 acre-feet since 1992. Between 1992 and 2002, nearly US$1 billion has been lost in decreased business activity and 30,000 jobs have been precluded.

8. Meanwhile, Mexico's imports to the United States through ports of entry in South Texas and Nogales, Arizona of fruits and vegetables have increased dramatically since 1990. Irrigated production of crops in Chihuahua tripled from 1980 to 1999. There has been a decrease in acreage of crops in Chihuahua needing less irrigation and an increase in production of crops like vegetables, fruits, and melons and nuts, which are more profitable but require more water. Total estimated water use for irrigation increased from 1.2 million acre-feet in 1980 to 2.3 million acre-feet in 1997 in Chihuahua.

9. Based on his study, *Alternative Approaches to Estimate the Impact of Irrigation Water Shortages on Rio Grande Valley Agriculture* (May 17, 2002), Dr. John R. C. Robinson estimates the economic values of Claimants' irrigation water in the lower Rio Grande Valley from 1992-2002 at US$350 per acre-foot to US$730 per acre-foot, or a total of US$265,927,200 to US$554,648,160 for the taking of Claimant's water, after accounting for a 25 percent loss through evaporation, diversion losses, and transportation losses (1,013,056 acre-feet of water less 25 percent equals 759,792 acre-feet of water).

10. Mexico has neither offered nor paid fair compensation for the water expropriated, nor for the economic damages resulting from its unequal treatment of United States farmers.

## IV. Arbitration Issues

Claimants intend to submit to arbitration the specific issues of the liability of Mexico for violation of Chapter 11, Articles 1102 and 1110, of NAFTA, and the amount of damages owing to Claimants for the fair market value of the 1,013,056 acre-feet of Claimants' water expropriated by Mexico.

## V. Relief Sought and Approximate Amount of Damages Claimed

Claimants will request the following approximate damages:

1. Fair compensation for the 1,013,056 acre-feet of water expropriated by Mexico, in the approximate amount of US$265,927,200 to US$554,648,160; or, in the alternative,

2. Economic losses resulting from Mexico's less favorable treatment of Claimants and their investments, in the approximate amount of US$554,648,160; and

3. Interest on such sums from October 2002 until the date of payment; and

4. Costs of attorneys, consultants, the arbitration panel, and such other losses and expenses as are legally allowable.

The law firm of Marzulla & Marzulla is authorized to receive correspondence related to this matter on behalf of Claimants. We would be happy to meet with you and to discuss any questions that you may have in this regard.

Respectfully submitted,

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