

**INTERNATIONAL CENTER FOR
SETTLEMENT OF INVESTMENT DISPUTES
ADDITIONAL FACILITY**

WASTE MANAGEMENT, INC.

Claimant

v.

THE GOVERNMENT OF THE UNITED MEXICAN STATES

Respondent

ICSID Case # ARB (AF)/00/3

POST-HEARING SUBMISSION

SUBMITTED BY

WASTE MANAGEMENT, INC.

Claimant

1. Analyze the similarities and differences between the claims brought before the courts in Mexico, specifically concerning damages; and compare them to the claims presented in the CANACO arbitration and the two proceedings before ICSID.

Banobras Litigation. Two separate breach of contract actions were instituted by Acaverde against Banobras in the Mexican courts. Banobras I was filed in January 1997 and sought over N\$ 15 million in damages, which represented the value of unpaid invoices from May through December 1996. Banobras II was filed in July 1998 and sought over N\$ 21 million in damages, which represented the value of unpaid invoices from January through October 1997. Because both lawsuits were based on the refusal by Banobras to honor its contractual obligations to Acaverde as a third-party beneficiary under the Line of Credit Agreement, the lawsuits were filed against Banobras, not the City. There was no decision on the merits in either Banobras I or Banobras II. However, any decision on the merits in either case would only have addressed Banobras' obligations to Acaverde under the Line of Credit Agreement and would not have addressed the City's obligations to Acaverde under the Concession.

CANACO Arbitration. The CANACO arbitration was instituted by Acaverde against the City in January 1998. Acaverde sought damages for the City's material and substantial breach of various obligations under the Concession. Four different claims for damages were asserted. First, Acaverde sought payment of N\$ 149.4 million, which was calculated pursuant to the penalty clause of Article 10 of the Concession. Second, Acaverde sought payment of approximately N\$ 11 million, representing the difference between actual amounts collected from private customers and the amount Acaverde would have collected had the collection rate equaled 60%. Third, Acaverde sought payment for approximately N\$ 71 million, representing payments related to fixed assets. Fourth, Acaverde sought approximately N\$ 15 million, representing payments related to intangible assets. As discussed in the response to question number 3 below, the damages in the third and fourth categories above are alternatives to the other damages sought. *See* Concession, Article 10.

ICSID Proceedings. Unlike the narrow breach of contract claims brought in the judicial actions against Banobras or the CANACO arbitration against the City, the claims in both NAFTA proceedings involve allegations that the Mexican Governments violated applicable provisions of international law – namely, Articles 1105 and 1110 of NAFTA. As concisely explained by Keith Highet in his dissent in Waste Management I:

[T]he claims advanced by Waste Management here differ from the claims asserted against Banobras and Acapulco in the local Mexican actions. Claimant's claims under Articles 1110 and 1105 of NAFTA are broader than—and proceed on a plane different from—the claims advanced in either the Banobras lawsuits or the Acapulco arbitration. Not only did they involve numerous additional elements; they also proceed on a distinct and separate judicial plane, since a “creeping expropriation” is comprised of a number of elements, no one of which can—separately—constitute the international wrong. These constituent elements include non-payment, non-reimbursement, cancellation, denial of judicial access, actual practice to exclude, non-confirming treatment, inconsistent legal blocks, and so forth.¹

¹ Dissenting Opinion, ¶ 17 (footnotes omitted). *See also* Mr. Highet's comments in ¶ 7 (“[C]laims relating to Mexican remedies for Mexican wrongs are not the same as claims for NAFTA remedies for NAFTA wrongs.” (footnote omitted)); and ¶ 28 (“The causes of action are different: local commercial claims in the Mexican tribunals, and international treaty claims before this Tribunal.”).

Because the claims in the domestic and ICSID proceedings are different, the damages sought by Claimant are also different. Under NAFTA, an investor is entitled to recover the fair market value of the expropriated investment.

In the NAFTA proceeding, Claimant set forth two alternative methods of calculating its damages. Both are designed to eliminate the diminution in value of Claimant's investment directly caused by Respondent's breaches of Articles 1105 and 1110. The first method calculates the fair market value of the expropriated investment by considering, *inter alia*, profits Claimant would have generated "but for" Respondent's breaches of NAFTA. The second method assumes that the penalty clause formula set forth in the Concession reflects the parties' estimate of the value of Claimant's economic interests under the Concession. Unlike the penalty claim asserted in the CANACO arbitration, however, Claimant is not limited in the NAFTA proceedings to using Acaverde's actual revenues for 1997 because the amount of actual revenues had been arbitrarily reduced by, among other things, the City's systematic failure to enforce Acaverde's rights to exclusivity and the published rates.

In summary, the damage claims brought in the domestic proceedings are completely different from the damage claims before ICSID. This results because Claimant sought contractual damages in the domestic proceedings and is seeking damages for the fair market value of its investment in the ICSID proceedings.

2. Comment on the cost of the CANACO arbitration, because from the documentary evidence provided, both parties complained about the amount that CANACO sought to charge them.

Within months of being sued by the City of Acapulco, CANACO effectively ended the domestic arbitration by imposing an excessive and unreasonable demand for advance payment of arbitration fees (more than three times the standard fee), knowing that the City of Acapulco had already declared its inability to pay.

The CANACO arbitration was commenced in January 1998. Immediately, the City claimed that it lacked the funds necessary to defend itself. In its November 25, 1998 filing, the City reiterated its previous objections to the arbitration and asserted as its sixth affirmative defense "the lack of budgetary resources available to the Municipality to defray the expenses of the arbitration." Exhibit G-40, p.17 (courtesy translation).

In September 1998, the City filed a lawsuit (discussed in detail in response to Question #3 below) seeking a nullification of the arbitration and damages from Acaverde and CANACO if the arbitration moved forward. In March 1999, the commercial court in Guerrero ruled that it had jurisdiction to consider the City's nullification claim. On April 21, 1999, three weeks after learning that the court would entertain the City's nullification lawsuit, CANACO ordered the payment of N\$ 2.5 million per party (N\$ 5 million total) to continue the arbitration. MX 0612, Tab 1.

CANACO's customary fee schedule is determined by a formula based largely on the total amount in controversy. In the CANACO arbitration, Acaverde presented claims for damages that were, on their face, alternative under the language of Article 10 of the Concession. MX 565-571, Tab 2. However, even if one added all of these claims together, which Claimant does not concede should be done, and uses the resulting total of N\$ 246 million as the amount in

controversy, the total fee CANACO should have assessed is approximately N\$ 1.6 million (or N\$ 800,000 per party), not N\$ 5 million.² Accordingly, Acaverde and the City were required to pay more than three times CANACO's established rate just to continue the arbitration. This is consistent with Mr. Herrera's testimony that CANACO's demand for fees was unreasonably excessive. Hearing Transcript, p. 402.³

Acaverde objected to CANACO's proposal on April 28, 1999 on the grounds that the fees were exorbitant and greatly exceeded the customary fees imposed by CANACO. MX 0613, Tab 4. One month later, on June 29, 1999, Acaverde withdrew from the arbitration. MX 0624, Tab 5. CANACO imposed these exorbitant costs because it was concerned about its own liability in the nullification lawsuit if the arbitration continued. CANACO also imposed these exorbitant fees knowing full well that the City had not paid and would not pay a single centavo to defray them.

3. Inform the Tribunal about the nullification proceeding in connection with the arbitration clause. Indicate the references in documents produced or otherwise indicate the outcome of the proceeding.

The City filed a complaint against Acaverde and CANACO in the commercial court in the State of Guerrero on September 4, 1998. The City sought a declaration that the arbitration clause of the Concession Title was null and void and that the ongoing arbitration was similarly null and void. In addition, the City sought damages from both Acaverde and CANACO if the arbitration was continued. Exhibit G-39, pp. 1-2. Acaverde filed a demurrer to the court's exercise of jurisdiction on the ground that the City's complaint should be considered in federal court, not state court, because the Concession was an administrative instrument, not a commercial instrument. Tab 6. Acaverde's demurrer thus tracked the argument of the Mexican Governments in Banobras II that the litigation should be dismissed because the Concession was an administrative act.

In a March 29, 1999 decision, the court rejected Acaverde's demurrer on the ground that the dispute was commercial and not administrative in nature. *See* Opinion, Tab 7. In response, Acaverde filed an interlocutory appeal on April 9, 1999. Tab 8. The appellate court of the State of Guerrero upheld the commercial court's ruling in a decision issued on August 6, 1999. (An almost illegible copy of the opinion is attached at Tab 9)

It should be emphasized that the only decision made by the commercial court (and upheld

² These rates are calculated using CANACO's web site at www.arbitrajecanaco.com.mx/frameset.htm. If one inputs the amount in controversy as N\$ 246 million and the number of arbitrators as 3, the web site calculates CANACO's total costs under today's rates at N\$ 1,650,648, which is 32% of the total amount imposed on the parties in April 1999. A copy of the web site calculation is attached at Tab 3.

³ Respondent argued during the hearing that it is not unusual for one party to pay the entire amount of fees if the other party refuses to pay. Hearing Transcript, p. 756: 13-20 ("it's not unusual in commercial arbitration for one of the parties to refuse to pay [T]he rules of the National Chamber of Commerce and the ICC Arbitration Rules provide that in the event that a party doesn't pay this amount, it will be covered by the other party. That's normal.") Indeed, an arbitration can be suspended if one party refuses to pay, unless the other party advances 100% of the total arbitration costs. *See e.g.*, Article 30 of the ICC Rules of Arbitration. When it issued its demand for advance costs in April 1999, CANACO knew that the City had already taken the position that it was unable to pay its share. Thus, CANACO knew that Acaverde would have to pay the entire amount of N\$ 5 million – or more than six times the standard per party rate – to continue the arbitration.

by the appellate court) was that the commercial court had jurisdiction to entertain the City's lawsuit. No decision was ever made on the merits (*i.e.*, whether the arbitration clause was null and void). Nothing happened in the nullification lawsuit after the appellate court ruling because six weeks before that ruling, Acaverde withdrew from the CANACO arbitration. Thus, the City got exactly what it set out to get by filing the nullification lawsuit in the first place.

4. In connection with the obligation to enforce the Ordinances which were relevant to the Concession, please indicate:

4.1. Who were the individuals responsible for enforcing the Ordinances?

The City of Acapulco was solely responsible for enforcing the July 1995 Ordinances regarding exclusivity (Article 16) and the requirement to use Acaverde's services and pay the published rates (Articles 8 and 9). This responsibility was derived from Mexican law, the Concession and the July 1995 Ordinances.

Under Article 61 of the Framework Law of Municipalities of the State of Guerrero, a municipality is obligated "to comply and to enforce ... the laws of the State as well as ensure strict compliance with the municipal regulations and ordinances." MX 0149. Tab 10. The Concession obligated the *Ayuntamiento* to take such "action as necessary to secure effective and prompt enforcement" of the laws regarding exclusivity. Concession, Annex A, Clauses II.1.d and II.2.d. Lastly, Article 3 of the July Ordinances required the *Ayuntamiento*, through the Department of Municipal Services, to exercise oversight and control over the provision of public sanitation services. Accordingly, the *Ayuntamiento* was clearly responsible for enforcing the July 1995 Ordinances.⁴

4.1.1 According to Article 3 of the Ordinances, indicate the authority within the Ayuntamiento who had the power to enforce the Ordinances.

Because the July 1995 Ordinances were part of the municipal law of Acapulco, any city official empowered to enforce the law (*e.g.*, a member of the police department) was generally empowered to enforce the July 1995 Ordinances. In addition, Article 21 of the July 1995 Ordinances specifically placed responsibility on the Mayor of Acapulco, the Director of Municipal Public Services, inspectors within the Department of Municipal Public Services and qualified judges (to whom violators shall be turned over) to enforce the Ordinances and apply the sanctions set forth in Articles 22-25.

Accordingly, Acaverde's numerous complaints concerning unauthorized waste collectors (Exhibits D-21, D-26, D-27), City trucks (Exhibit D-20) and the failure of residents and businesses to use and pay for Acaverde's services (Exhibit D-25) were directed to the Mayor and/or the Director of Municipal Public Services. Unfortunately for Acaverde, the individuals authorized to enforce the Ordinances failed to enforce and, in the case of the Mayor, effectively revoked the Ordinances.⁵

⁴ As a private business, Acaverde obviously had no authority to fine or otherwise sanction residents, businesses or unauthorized waste collectors for violations of the July 1995 Ordinances.

⁵ Acaverde even provided the City with: (a) a list of municipal departments that could provide support in fining unauthorized waste collectors; and (b) the legal grounds upon which fines should be imposed. Tab 11 (originally attached as part of Exhibit D-21).

4.1.2. Comment on Article 4 of the Ordinances in light of Annex A of the Concession, clause III.2.b, which was amended on May 12, 1995.

Article 4 of the July 1995 Ordinances required the Department of Municipal Public Services to designate three inspectors who were responsible for: (a) enforcing the Ordinances; and (b) designing and executing (in cooperation with Acaverde) public education programs concerning trash management. As stated in Annex A, Clause III.2.b, the *Ayuntamiento* was "exclusively responsible" for appointing these inspectors, who were employed by the City (Department of Municipal Public Services).⁶ The Article 4 inspectors were not hired by Acaverde, and Acaverde had no authority to fire the inspectors. Acaverde only had the ability to request (in writing) changes regarding the inspectors; the *Ayuntamiento* retained the exclusive right to act on any such request.⁷ Concession, Annex A, Clause III.2.b.

4.2. Article 8 of the Concession indicates that labor responsibility, that is the relationship between employer and employee, rests upon the Concessionaire and not upon the *Ayuntamiento*. Who gave orders to the three inspectors who were in charge of enforcing the ordinances: the *Ayuntamiento*, the Concessionaire or both?

Article 8 of the Concession indemnified the *Ayuntamiento* from liability arising out of labor disputes between Acaverde and company employees. Article 8 applies only to staff hired by Acaverde. Thus, this provision does not apply to the inspectors designated and hired by the Department of Municipal Public Services.

The Article 4 inspectors took their orders from the City, and Acaverde had no ability to order the inspectors to do anything. Acaverde could only request that the Mayor or Director of Municipal Public Services instruct its officers to enforce the Ordinances. See e.g., letter dated January 11, 1996 to Rogelio de la O Almazán (originally part of Exhibit D-25 and attached hereto as Tab 12). Acaverde routinely informed inspectors about specific unauthorized waste collection activity, but it was up to the inspectors (and the other individuals empowered under Article 21) to issue fines and/or other sanctions. Acaverde never enjoyed exclusivity or the benefits of Articles 8 and 9 because neither the inspectors nor other city officials issued fines for violations of the Ordinances.⁸

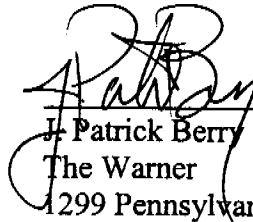
⁶ The February 1995 version of the Concession stated that the "*Ayuntamiento*, jointly with the Concessionaire and at the cost of the latter, shall appoint three persons as inspectors of the service under Concession." MX 0026. The language of Annex A, Clause III.2.b was modified in May 1995 to clarify that the *Ayuntamiento* was "exclusively responsible" for appointing the inspectors.

⁷ Although Acaverde paid the City for the salaries of the inspectors (as required by Annex A, Clause III.2.b of the Concession), the inspectors worked for the Department of Municipal Public Services and were paid by the City at all times. Francisco Larequi Statement (Exhibit A-5), ¶ 9.

⁸ James Herak Statement (Exhibit A-4), ¶ 7 ("the inspectors did not make any significant effort to enforce the exclusivity provisions"); Rod Proto Statement (Exhibit A-3), ¶ 14; Francisco Larequi Statement (Exhibit A-5), ¶ 9; Joseph Coradetti Statement (Exhibit A-6), ¶ 9.

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Respectfully submitted,



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