BEFORE THE HONORABLE TRIBUNAL ESTABLISHED PURSUANT CHAPTER ELEVEN OF THE NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)

ROBERT AZINIAN, KENNETH DAVITIAN AND ELLEN BACA, CLAIMANTS

VS.

THE UNITED MEXICAN STATES, RESPONDENT

POST-HEARING SUBMISSION

COUNSEL FOR THE RESPONDENT:
Hugo Perezcano Díaz

ASSISTED BY:

Secretaría de Comercio y Fomento Industrial
Carla Tochijara Vargas
Fernando Reséndiz Wong

Thomas & Davis
Christopher Thomas
J. Cameron Mowatt
Máximo Romero Jiménez
Alejandro Posadas Urtusuástegui
Katharina Byrne
Carlos G. García

Shaw Pittman
Stephan E. Becker
Nancy A. Fischer

1. Pursuant to the Tribunal's request, the Respondent hereby submits this Post-Hearing Submission. Part I summarizes the evidence presented during the written and oral proceedings. Part II addresses certain issues of Mexican domestic law that are highly relevant to this proceeding and in which the Tribunal expressed interest during the Oral Procedure. Part III discusses the scope of the Tribunal's jurisdiction. Part IV contains conclusions and the relief requested.

PART I: SUMMARY OF THE EVIDENCE

1. *The Evidence of Poor Performance*

2. The evidence is overwhelming that the Claimants' enterprise[1] was unable to perform the concession.

3. First, it breached its obligation to introduce five new state-of-the-art trucks into service as of December 13, 1993, a breach that was never cured. In fact, this breach was compounded when DESONA failed to introduce another seven such trucks into service on March 1, 1994.

4. Second, the uncontroverted evidence is that throughout the life of the concession the municipality continued to pay the workers' salaries and the equipment expenses for the collection of solid waste in all sectors of the municipality, including the sector for which DESONA assumed responsibility (Satélite)[2].

5. Third, the State (and subsequently the municipality) continued to pay the lease, the workers' salaries, and the rental costs of the earth-moving equipment at the Rincón Verde landfill. The two checks put to Mr. Piazzessi in an attempt to challenge his testimony that DESONA did not pay rent for the landfill were expressly qualified by the Claimants' counsel when asked whether or not he was introducing them as proof of payment[3].

6. In short, although the testimony at the hearing generally focused on DESONA's failure to introduce the trucks, there were other significant failures to perform the concession[4].

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1. For the purposes of this submission, the Respondent will describe the enterprise as DESONA. This is purely for ease of reference. The Respondent reaffirms the arguments made in respect to the different versions of DESONA and notes in particular that at the material time of the signing of the concession contract, the concession was held by DESONA I although the contract of concession was allegedly signed by DESONA B.

2. Counter-memorial, Annex III (Volume III), Tab E, Declaration of Francesco Piazzessi at paragraphs 26 and 38. See also the oral testimony of Mr.Piassezzi, Hearing Transcript dated Wednesday, June 23, 1999 at pages 102 (lines 14-18), 105 (lines 6-11) and pages 120-123.

3. The Tribunal will recall that after the checks were put to Mr. Piazzessi, when asked by Mr. Civiletti what the Claimants' position on the checks was, counsel declined to tender them as proof of payment, instead informing the Tribunal that Mr. Goldenstein would so testify if called upon to testify. See Hearing Transcript dated Wednesday, June 23, 1999 at page 138.

4. As noted in the closing argument, Mr. Azinian's letter dated February 15, 1994 to the Municipal President, in which he sought to set out why DESONA was complying with the concession, is evidence that the Claimants were well aware of the failures in performance. There would be no need to write a letter attempting to convince the *Ayuntamiento* of the company's compliance (note that "compliance" is now described in the Reply as "substantial"

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7. Notwithstanding Mr. Proctor's written testimony, BFI did not fulfil the commitment he said that he gave to the prior municipal administration that BFI would provide the capital and operational and technical expertise necessary for the concession[5]. For reasons that remain unclear, the proposed BFI-DESONA joint venture never materialized[6].

2. *The Company's Lack of Financial Capacity*

8. Contrary to Mr. Goldenstein's claims that the company was well-financed, the evidence is overwhelming that DESONA lacked the necessary finances to perform the concession:

a) Notwithstanding its claims of vast experience, Global had only been incorporated as of March of 1991. Moreover, Global entered bankruptcy some five months before Mr. Goldenstein appeared before the *Ayuntamiento* to describe its role in the proposed consortium; the bankruptcy occurred less than 18 months after the company's incorporation[7];

b) One year later, on November 11, 1993, just days before the concession was to enter into force, DESONA still did not have any trucks ready to introduce into service. Mr. Azinian's fax to Mr. Proctor showed that as of that date, DESONA required a loan from BFI to acquire the two front-loaders that it had arranged to purchase from Northside Steel Fabricators (Witke)[8];

c) When the Claimants and Mr. Goldenstein entered into the agreements with BFI on November 18, 1993, for only 100,000 U.S. dollars of its own funds and a 100,000 dollar loan from Western Wastes Industries, BFI was able to secure (what it thought would be) an exclusive right to negotiate a joint venture with DESONA for the Naucalpan project[9]. As Mr. Proctor admitted, this was a very small amount of money for a company of BFI's size[10];

d) The evidence shows that by the end of December 1993, Mr. Bryan Stirrat contacted the senior executives of Regional Waste Disposal Company to see if they were interested in investing in DESONA. Mr. Stirrat's attempt to characterize his efforts as aimed at finding investors to "take the show on the road" rather than to shore up the Naucalpan concession was not credible; his testimony was contradicted by documents created at the time and by the testimony of Mr. Hodge[11];

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as opposed to "full" compliance), unless DESONA was concerned that the concession was in jeopardy. See Counter-memorial, Annex VI (Volume I), Exhibit 8.

5. Reply, Section V, Tab 7, Affidavit of Ronald Proctor, pages 3-4.

6. Under questioning from Mr. Paulsson, Mr. Proctor was unable to specify what it was that DESONA actually brought to the performance of the concession. Oral testimony of Ronald E. Proctor, Hearing Transcript dated Monday, June 21, 1999 at pages 267-270.

7. Hearing Brief A,Tab 1. See also Respondent's June 8, 1998 Motion, Exhibit 2.

8. Hearing Brief B, Tab 2.

9. Hearing Brief A, Tab 8. See also Claimant's Reply to the Respondent's Motion for Directions dated May 18, 1998.

10. Oral Testimony of Ronald E. Proctor in Hearing Transcript dated Monday, June 21, 1999 at pages 166-168.

11. Mr. Stirrat's evidence is contradicted by the fact that: (1) Mr. Hodges' letter of August 19, 1994 dealt with the Naucalpan project only. See Counter-memorial, Annex III (Volume I), Tab B, Declaration of James Hodge, Exhibit A. (2) Mr. Maphis, who the Tribunal can only infer, received the information about the project from Mr. Carolan, wrote notes that were concerned with the Naucalpan project only. See Counter-memorial, Annex III

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e) Five weeks after the signing of the November 18, 1993 DESONA-BFI agreement, confidential BFI information analyzing the Naucalpan project was faxed to Mr. Stirrat's office and then passed on to Mr. Carolan. It is evident that Mr. Carolan then disclosed the information to at least Mr. Maphis in an effort to solicit his interest in taking over the project[12];

f) Mr. Hodge's comment in his subsequent letter that DESONA was looking for capital "on a seemingly desperate basis"[13] is echoed by the Maphis file note which states that "they are clearly over their head in terms of technical and financial capability and my feeling in talks with Mike Carolan is that they want out"[14];

9. Thus, compelling direct and circumstantial documentary and testimonial evidence proves that DESONA was undercapitalized and unable therefore to perform financially.

10. Although the matter was not canvassed at the hearing, Dr. Dávalos testifies that during the Mexican court proceedings, DESONA was called upon to produce evidence of its financial capacity to perform the concession. His uncontradicted evidence is that it failed to do so. In contrast, the *Ayuntamiento* tendered extensive evidence of its continued expenditures and the concessionaire's lack of financial capacity[15].

11. It warrants noting that although Mr. Proctor claims that he informed officials of the prior administration of BFI's commitment to perform the concession[16], if this occurred, it was neither disclosed publicly nor to the subsequent Jacob administration[17]. At *no* time did DESONA inform the *Ayuntamiento* or the courts that it had the financial backing of BFI or any other experienced and financially capable waste management company[18].

3. *Misstatements and Misrepresentations*

12. There is ample evidence of misstatements and misrepresentations by the Claimants. The leading example was the Claimants' misrepresentation ascribing 40 years of experience to Global Waste Industries[19]. The Tribunal can reasonably infer that this misrepresentation, made

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(Volume I), Tab C, Declaration of J. Cameron Mowatt, Exhibits S, U and V. This documentary evidence is fully consistent with Mr. Hodge's testimony that he had been invited to inspect DESONA's operation and consider investing in it.

12. For example, see Counter-memorial, Annex III (Volume I), Tab C, Declaration of J. Cameron Mowatt, Exhibit S.

13. Mr. Hodges' letter of August 19, 1994, page 1 at paragraph 2. Refer to Counter-memorial, Annex III (Volume I), Tab B, Declaration of James Hodge, Exhibit A.

14. Mr. Maphis' letter dated March 7, 1994 at page 2. Refer to Counter-memorial, Annex III (Volume I), Tab C, Declaration of J. Cameron Mowatt, Exhibit S.

15. Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, paragraphs 36-43.

16. See Reply, Section V, Tab 7, Affidavit of Ronald Proctor, pages 3-4. See also oral testimony of Ronald E. Proctor in Hearing Transcript dated Monday, June 21, 1999 at pages 222-223.

17. See oral testimony of Ariel Goldenstein in Hearing Transcript dated Monday, June 21, 1999 at pages 321-322.

18. See oral testimony of Ariel Goldenstein in Hearing Transcript dated Monday, June 21, 1999 at pages 321-322.

19. See, for example, DESONA's Company profile submitted in the Rejoinder, Annex Three, the representations made to the *Ayuntamiento* on November 4, 1994 submitted in the Counter-memorial, Annex VI,

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directly by the Claimants or repeated by others with their knowledge and acquiescence, was intended to mislead the two decision-makers, the *Ayuntamiento* and the State Congress, as to the Claimants' true experience and financial capacity. This was done in order to induce them to grant the concession to what turned out to be an enterprise owned exclusively by the Global "principals"[20].

13. Mr. Goldenstein admitted under cross-examination that although the approvals of the *Ayuntamiento* and the Congress were essential in order for the concession to be granted to DESONA, he did not consider it to be his responsibility to inform either of them of the truth about the Claimants' inexperience and Global Waste's bankruptcy[21]. He also did not view it as his duty to correct plainly incorrect statements made by municipal officials about the Claimants' experience and Global's financial capacity[22].

14. This pattern of misrepresentation continued in the concession's performance. For example:

a) Mr. Goldenstein's application to obtain federal import permits for the 10 new trucks included a false bill of sale purporting to show that on February 25, 1994 American Waste Removal ("AWR") (Mr. Davitian's former company by then owned by Ellen Baca[23]) sold the trucks to DESONA. The evidence demonstrates conclusively that this sale did not occur. BFI's subsidiary, Latin American Environmental Services Ltd. offered the same 10 trucks for sale to DESONA some two weeks later on March 9, 1994. Under cross-examination, Mr. Goldenstein admitted that AWR did not own the trucks that it purported to sell to DESONA and that as of March 9, 1994, they had not been purchased[24].

b) It is also evident that the AWR bill of sale understated the value of the trucks by nearly 300,000 dollars. The Tribunal can reasonably infer that this was an attempt to undervalue

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Exhibit 3, and representations made to the State Congress as set out in the Rejoinder, Annex One, page 4 at paragraph 17.

20. The claim of over 40 year's experience was repeated by a municipal official and by Mr. Goldenstein before the State Congress. See Rejoinder, Annex One, page 4 at paragraph 17. It was also contained in a letter alleged to have been written by the former mayor, Mario Ruiz de Chávez to his successor, Enrique Jacob, in March of 1994 *after* the *Ayuntamiento* decided to commence nullification proceedings. See the Claimant's Response to Respondents' Request for Documents, annexed to the section entitled "Observations". This letter contradicts the Claimants' contention that officials knew about Global's fate and the Claimants' inexperience. In reference to the representation of 40 years of experience by the DESONA principals, Mr. St. Louis excuses the misrepresentations by stating: "Now I have to confess to you that that obviously is puffing". See Hearing Transcript dated Thursday, June 24, 1999 at page 62, lines 14 and 15.

21. See oral testimony of Ariel Goldenstein, Hearing Transcript dated Monday, June 21, 1999 at pages 298-301.

22. See oral testimony of Ariel Goldenstein, Hearing Transcript dated Monday, June 21, 1999 at pages 296-301.

23. Who, according to her matrimonial settlement dated July 22, 1993, was assigned Mr. Davitian's interest in AWR. See Hearing Brief B, Tab 19.

24. Oral testimony of Ariel Goldenstein, Hearing Transcript at pages 283-286.

the goods in order to reduce the amount of customs duties that would be payable in the event that the goods were imported under the federal permits[25].

15. This propensity for misrepresentation by word or conduct was exhibited in other contexts. For example:

a) During 1992-1993, the Claimants did not see fit to inform their fellow consortium members of Global's deteriorating financial condition[26]. In fact, Global's failure to provide financial information to Sunlaw was one of the reasons why Sunlaw's President chose to distance his company from Global in January of 1993[27].

b) The Claimants had Bryan Stirrat accompany them to the June 1, 1994 Cabildo meeting at which they requested the reinstatement of the concession without informing him of the fact that 10 days earlier they had secretly sold all of DESONA's assets to a subsidiary of Sanifill[28]. Mr. Stirrat admitted under cross-examination that he was unaware of that fact and that the Claimants had not seen fit to pay him for any of his company's contributions to the project from the proceeds of the sale[29].

c) DESONA used BFI's loan to pay for the two front-loaders purchased from Witke but did not repay BFI when it sold those assets to Sanifill six months later. Mr. Proctor admitted under cross examination that he was unaware of the sale of the two trucks until late 1994[30], when he read about it in Waste Age magazine and recommended to his superior, Mr. Page, that BFI take legal action against Messrs. Azinian, Davitian and Goldenstein[31].

d) As Dr. Palacios has testified, he entered into a business venture with Mr. Goldenstein and incorporated DESONA I on the understanding that DESONA I would be the concession holder for the Naucalpan Project[32]. Believing that he was participating in the concession, Dr. Palacios contributed cash in the amount of 225,000 dollars and 60 metal garbage containers to DESONA I for use in the concession[33]. On the basis of Mr. Goldenstein's

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25. The difference is 277,250.00 dollars. See Hearing Brief B, Tab 16 where an invoice from American Waste Removal lists the value of the trucks at 464, 400.00 dollars. Compare this with an order confirmation letter from McNeilus Truck and Manufacturing Co. listing the cost of the same trucks, as evidenced by the same serial numbers, as 741, 650.00 dollars. See Hearing Brief A, Tab 19 and also the Memorial, Volume II, Section 4, Exhibit 15. See oral testimony of Ariel Goldenstein, Hearing Transcript dated Monday, June 21, 1999 at pages 276-287.

26. This is evidenced by the letter from Robert Danziger to Robert Azinian dated January 20, 1993. See Hearing Brief A, Tab 4 or Counter-memorial, Annex III (Volume I), Tab A, Declaration of Raul Romo Velázquez, Exhibit 2. Further evidence is provided by the fact that *none* of the three witnesses from BAS, BFI, and Witke was aware of Global's bankruptcy at the time. For example, see oral testimony of Ronald E. Proctor in Hearing Transcript dated Monday, June 21, 1999 at pages169-171 and the oral testimony of Basil Carter in Hearing Transcript dated Tuesday, June 22, 1999 at pages 97-99. Mr. Stirrat could only recall becoming aware of this sometime in 1992, refer to oral testimony of Bryan Stirrat in Hearing Transcript dated Monday, June 21, 1999 at page 41. Mr. Stirrat further professed to be untroubled by it, in his words "It had no impact on my work," see oral testimony of Bryan Stirrat in Hearing Transcript dated Monday, June 21, 1999 at page 40.

27. A second reason for Sunlaw's distancing was Global's unauthorized disclosure of Sunlaw's confidential information to its competitors. See Hearing Brief A, Tab 4 or Counter-memorial, Annex III (Volume I), Tab A, Declaration of Raul Romo Velázquez, Exhibit 2.

28. Hearing Brief A, Tab 17.

29. Oral Testimony of Bryan Stirrat in Hearing Transcript dated Monday, June 21, 1999 at pages 105-109.

30. Oral testimony of Ronald E. Proctor in Hearing Transcript dated Monday, June 21, 1999 at page 174.

31. Hearing Brief B, Tab 15.

32. Counter-memorial, Annex III (Volume III), Tab H, Declaration of Oscar Palacios Gómez at paragraphs 9-10.

33. Counter-memorial, Annex III (Volume III), Tab H, Declaration of Oscar Palacios Gómez at paragraph 11.

representations, he expected that once the concession was approved by the State Legislature, Mr. Goldenstein and his colleagues would contribute their share of money[34]. They never did and, in the end, Dr. Palacios was left without the benefit of his investment and DESONA B converted both the money and the metal containers that he contributed to DESONA I to its own use.

16. This conduct continued in this proceeding:

a) The Claimants asserted that Messrs. Azinian, Davitian and Goldenstein each owned 33% of Global[35]. This was contradicted by Mr. Goldenstein's sworn statement to the United States Bankruptcy Court[36].

b) The Memorial pleaded that the new trucks depicted in the photograph on page 60 of Section III had actually begun to be substituted for the old municipal trucks[37]. Mr. Goldenstein admitted in cross-examination that this never occurred[38].

c) During the hearing, the Claimants' sought to introduce two unidentified checks as evidence of proof of payment of the Rincón Verde landfill lease. When the checks were shown to have been endorsed back to an employee/associate of DESONA (in other words, on their face, they were paid to persons involved in the ejido that controlled the landfill and then endorsed back to DESONA), this contention was abandoned by counsel[39].

d) Only just before the hearing did the Claimants admit that they had sold the assets of DESONA, including its commercial service contracts, for $500,000 shortly after the concession was nullified in 1994[40].

17. In the Respondent's submission, the Claimants' testimony is unreliable in material respects and their depiction of crucial events, and assertions of damages, are not credible.

PART II: MEXICAN LAW ISSUES

18. Given the Reply's failure to address the evidence of Dr. Dávalos concerning the domestic legal proceedings invoked by the Claimants' enterprise and the Claimants' decision not to call Dr. Dávalos for cross-examination, the hearing did not review the Mexican law issues in detail. However, an understanding of those issues is relevant to the discussion of the Tribunal's jurisdiction in Part III below.

19. The concession was a juridical act regulated by Mexican law as to, *inter alia*, its nature, effect and methods of termination. The Respondent submitted with its Counter-memorial an

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34. Counter-memorial, Annex III (Volume III), Tab H, Declaration of Oscar Palacios Gómez at paragraph 11.

35. Claimant's Response to Production of Documents, Section 2, Page 2 at paragraph 1.

36. Hearing Brief A, Tab 1. See also Respondent's June 8, 1998 Motion, Exhibit 2.

37. Memorial, Volume I, Section 3 at page 60.

38. Oral testimony of Ariel Goldenstein, Hearing Transcript dated Monday, June 21, 1999 at pages 288-290 and see also Hearing Transcript dated Tuesday, June 22, 1994 at pages 115-117.

39. The Tribunal will recall that after the checks were put to Mr. Piazzessi, when asked by Mr. Civiletti what the Claimants' position on the checks was, counsel declined to tender them as proof of payment, instead informing the Tribunal that Mr. Goldenstein would so testify if called upon to testify. In the words of Mr. St. Louis, "If Mr. Goldenstein were called to testify, he would testify that money was demanded from him from the Ahido (sic) for rent, and he made those payments". See Hearing Transcript dated Wednesday, June 23, 1999 at page 138.

40. Hearing Brief A, Tab 17.

expert report on the legal regime governing public service concessions[41]. The Claimants simply ignored this issue. They did not submit an expert report with their Memorial or Reply, nor did they comment upon the Respondent's expert report. The Tribunal should give full weight to the expert opinion proffered by the Respondent.

20. Public services are destined to satisfying basic public needs in a regular, continuous and uniform manner. The provision of such services originally falls upon the State. However, the Mexican Constitution allows for such services to be performed by the private sector by way of a concession, when it is in the public interest because the State lacks the necessary economic or technical capacity to provide the service efficiently. Thus, this delegation of State responsibility is justified only if the concessionaire has the financial, technical and legal capacity to surpass the State in the performance of the service. For such reason, concessions are *intuitu pærsone* instruments, that is, instruments granted to a specific person on the basis of that person's particular characteristics and capabilities which enable him to surpass the State in providing the public service. Otherwise, there is no basis for granting a concession.

21. In accordance with Mexican law, concessions may be extinguished in several different ways, two of which are nullification and rescission. Nullification occurs when it is determined that there are defects rendering a concession illegitimate, that is, defects regarding essential aspects for its valid and effective existence. Administrative rescission occurs when there is noncompliance with the object of the concession. Nullification destroys the concession; administrative rescission terminates it as of the date that termination has been so declared.

22. In the instant case, after a detailed analysis undertaken by Dr. Dávalos, the *Ayuntamiento* determined the existence of 27 irregularities which formed the basis of the nullification of the concession "due to error" in its granting[42]. The Claimants' enterprise chose not to respond to the *Ayuntamiento's* determination and instead opted to resort to the local courts. DESONA having elected not to provide any response, the *Ayuntamiento* annulled the concession pursuant to Article 167 of the Municipal Organic Act.

23. There was some discussion during the hearing about the "four days" that DESONA was allegedly given to respond to the *Ayuntamiento*. It is more accurate to state that the company was given seven calendar days, not four business days to respond. In all three NAFTA Parties' legal systems, parties can be called upon to respond to matters on an expedited basis. It is not uncommon in Canada and the United States, for example, to have to respond to an injunction application in two business days. In the case of DESONA, at the March 10, 1994 meeting held at the Municipal offices, DESONA was provided with an opportunity to respond to the 27 irregularities. As no explanation was given, DESONA was given seven calendar days in which to present its position and adduce evidence in support thereof[43]. It declined to do so, instead invoking the assistance of the local courts.

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41. Expert Report on the legal regime for the granting of a public service concession in Mexico, submitted by the Instituto de Investigaciones Jurídicas de la Universidad Autónoma de México (Institute for Legal Research of the Autonomous University of Mexico), as requested by the Secretaría de Comercio y Fomento Industrial (Secretariat for Commerce and Industrial Development). Counter-memorial, Annex IV.

42. Counter-memorial, Annex VI, Exhibit 9, *Cabildo* meeting minutes dated March 21, 1994 listing the 27 irregularities found by Lic. Dávalos.

43. See the Counter-memorial, Annex III (Volume II, Declaration of Lic. Dávalos at paragraphs 25 and 26.

24. The Mexican local and federal courts —the Third Regional Chamber of the Administrative Tribunal of the State of Mexico in the first instance[44], the Superior Chamber of the Administrative Tribunal of the State of Mexico on appeal[45], and the First Administrative and Criminal Court of the Second Circuit (federal) in an *amparo* proceeding[46]— confirmed the *Ayuntamiento*'s decision. The courts confirmed that the matter pertained to a concession (an administrative act governed by public law and not a simple bilateral contract) and that the actions of the *Ayuntamiento* were strictly in accord with the law, including granting the fundamental rights to a hearing, justice and due process[47].

25. The Superior Chamber analyzed each of the 27 irregularities identified by the *Ayuntamiento*. It determined that 9 of them constituted a basis for nullification. Of the remaining 18, it noted that 7 referred to noncompliance with the contract —including, for example, the failure to substitute the municipal fleet of trucks with new and modern equipment— and that they could lead to its rescission, but not to its nullification[48].

26. Similarly, of particular interest to this Tribunal in light of the questions to counsel, is the Federal Circuit Court's decision which noted DESONA's "obvious omission" in not rebutting "the fundamental part of the decision rendered [by the Superior Chamber]"[49], namely, the 9 of the 27 irregularities which formed the basis for the annulment of the concession and which were upheld by the Superior Chamber.

27. From the perspective of international law, therefore, the actions of the *Ayuntamiento* must be analyzed within the context of Mexican law.

28. Article 167 of the Municipal Organic Act[50] requires the annulment of concessions in certain circumstances, with a prior hearing of the interested parties, in a way that enables them to defend their rights and interests and to present the corresponding evidence. The law does not provide for a specific time frame for this.

29. The Mexican courts expressly considered this issue in response to DESONA's claims that it had been denied the right to a hearing, that the *Ayuntamiento* had acted without any justification and legal basis, and that it had taken justice into its own hands. As has already been noted, the courts confirmed that the means by which the *Ayuntamiento* initiated and concluded

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44. Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 16.

45. Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 17.

46. Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 18.

47. Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos at paragraph 51 and Exhibit 17.

48. Regarding the remaining issues, it was decided that they could also not form the basis for the nullification of the concession —for example, because statutory provisions prevail over certain contractual ones, the concession being an instrument governed by public law, and for the same reason, such statutory provisions would remedy the omission in the contract of certain other requirements.

49. Decision of the First Administrative and Criminal Court of the Second Circuit (federal) in an *amparo* proceeding dated May 18, 1994, as cited in the Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 18 at page 41 in the Spanish original.

50. "Article 167.- Any agreement, concession, permit or authorization granted by an authority or public official without jurisdiction to grant it, or issued due to error, misrepresentation or duress, that affects or limits the municipality's rights regarding its public property or any other matter, shall be administratively nullified by the *Ayuntamiento*, after hearing the interested parties."

the nullification process were undertaken in strict observance of the right to a hearing and in full compliance with the law[51].

30. In particular, the Federal Circuit Court noted that "it is true that [the law] does not provide for a proceeding with specified time periods regarding the right to be heard, but it is also true that the claimant [DESONA] cannot complain that this right was not observed in its benefit, since it is obvious that during the procedure that concluded in the nullification of the concession, the claimant company was granted the opportunity to offer evidence and argue in its defense. Thus the constitutional obligation was met"[52]. It added that DESONA failed to challenge the existence of the 9 of the 27 irregularities that properly formed the basis of the nullification.

PART III: JURISDICTIONAL ISSUES

31. As discussed in Part Two of the Respondent's Rejoinder, the Tribunal has the jurisdiction to determine only whether there has been a breach of the obligations contained in Section A of NAFTA Chapter Eleven. This contrasts with the situation in many other types of international arbitration proceedings, where the arbitrators have been vested with jurisdiction to resolve all issues arising under a contract on a *de novo* basis[53].

32. The Tribunal's jurisdiction does not arise from a contractual agreement between the Claimants and the Mexican federal government; rather, it derives from an international agreement between the governments of Mexico, the United States and Canada, under which each Party agreed to ensure non-discrimination and treatment in accordance with international law to investors of the other Parties. The NAFTA was not intended to provide a mechanism for enforcement of all contractual obligations entered into by all levels of government, and it does not authorize a tribunal to rule on the interpretation of contracts or other issues of domestic law as if it were a domestic court.

33. Put another way, the Mexican federal government does not stand directly "in the shoes" of the municipality for purposes of this arbitration and cannot be sued for "breach of contract" under the NAFTA. The Respondent is responsible for ensuring that the Claimants received fair, equitable and non-discriminatory treatment in accordance with international law —not for ensuring that a concession granted by a Mexican municipality to a Mexican company incorporated by U.S. and Argentinean nationals would never be terminated under domestic administrative law.

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51. Decision of the Superior Chamber of the Administrative Tribunal of the State of Mexico as cited in the Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 17. The Court added that "Ariel Darío Goldenstein, in his position as General Manager of Desechos Sólidos de Naucalpan, S.A. de C.V., voluntarily submitted to the concession's administrative nullification procedure by appearing on March 10th of the current year [1994] at the hearing that was granted, thereby consenting and remedying the supposed limitations that could have existed, even though no such limitations really exist, regarding the timeframe, methods and procedures of the proceedings, "

52. May 18, 1995 decision of the First Administrative and Criminal Court of the Second Circuit (federal) in the *amparo* proceeding. See Counter-memorial, Annex III (Volume II), Declaration of Lic. Dávalos, Exhibit 18 at pages 37 to 38

53. See, for example, *AGIP SPA v. The Government of the People's Republic of the Congo*, 1 ICSID Reports 306, 313 (Award, November 30, 1979) and *Benvenuti & Bonfant v. Congo*, 1 ICSID Reports 330, 340-341, 349 (Award, August 15, 1980) noted in the Rejoinder, Part Two (A) at paragraph 27.

34. Accordingly, this Tribunal must review the *totality* of the treatment of the Claimants (and their enterprise) by the Mexican executive and judicial authorities, including the availability of judicial remedies and the conduct of the Mexican courts[54]. In making this review, the Tribunal must apply the standards established by NAFTA Articles 1105 and 1110, namely:

a) Were the Claimants and their investment (assuming the Tribunal determines that DESONA B was a legitimate entity that validly held the concession, and that the Claimants have properly brought a claim on its behalf under Article 1117) accorded "treatment in accordance with international law, including fair and equitable treatment and full protection and security"?

b) Has Mexico "directly or indirectly nationalize[d] or expropriate[d] [DESONA B] or take[n] a measure tantamount to nationalization or expropriation"?

35. The limited jurisdiction conferred by Chapter Eleven reflects the fact that the NAFTA Parties intended the dispute settlement procedure to be used on a limited and extraordinary basis, for violations of international law, and not for routine breach of contract claims. It also limits the possibility that tribunals will rule on issues of domestic law in a manner that might conflict with the decisions of the domestic courts of the Parties.

1. *The Relationship Between Article 1121 and Domestic Legal Proceedings*

36. On June 23rd, the Tribunal requested the parties' views as to the extent of its jurisdiction to hear a claim by investors where their enterprise had resorted to the local courts and had failed to obtain relief there. Specifically, the question was whether, if the domestic courts considered the matter and ruled against the enterprise (even if the relief requested was for declaratory or injunctive relief and not for damages), there was a residual jurisdiction vested in the Tribunal to review the issue under Chapter Eleven.

37. The Respondent's position remains the same as expressed in its pleadings. It agrees that Article 1121 addresses the availability of the forum and bars consecutive or simultaneous damages claims in the domestic courts (or in other dispute settlement proceedings such as arbitration) and the NAFTA. However, it disagrees with the Claimants regarding the effect of proceedings for declaratory or injunctive relief on a subsequent NAFTA claim for damages.

38. In the Respondent's view, the effect of the domestic courts' upholding of the concession's nullification is dispositive; unless the Claimants can point to a NAFTA breach, this Tribunal has no jurisdiction to review the courts' determinations of a Party's law.

2. *Comments on Tribunal's Questions Regarding Effect to Be Given Decisions of Domestic Courts*

39. During the closing submissions by the Claimants' counsel, the Tribunal again asked what effect should be given by a NAFTA arbitration tribunal to the decisions of domestic courts on issues of domestic law.

40. To stimulate discussion of this issue, President Paulsson posed the following hypothetical, and asked the Claimants to comment upon the options available to the investor:

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54. The Respondent considers that, although the NAFTA does not require the exhaustion of local remedies, the availability of such remedies will in many cases, such as this, be highly relevant in determining whether there has been a violation of Article 1105.

> Let's assume that a Canadian investor contracts with an American city to build a rapid transit system on a concessionary basis. It's a project financed (sic). You need a long-term contract under which rates will provide a return on capital. Hence the importance to the investor of reliance on a fairly long-term concession agreement.
>
> Things can turn a bit sour for any number of reasons, and the city decides to review the concessional agreement and comes to the conclusion that it was null and void for misrepresentation, and failing that, has been neglected by the concessionaire in such a substantial way that the city is entitled the rescind the concession agreement as an alternative basis of their decision. So this decision is now rendered... The concession agreement contains a submission to the U.S. courts. It doesn't say exclusive. It says the parties submit to the jurisdiction of U.S. courts, and obviously, we assume that both the grounds for nullification and rescission are debatable.
>
> Now, the Canadian investor looks at NAFTA, looks at its concession agreement and looks at what the city council has done, and considers its options. And I want you to tell me what you think those options are if we have in the mind that the Canadian investor ultimately wants to be sure that it doesn't lose rights under NAFTA because, on balance, it would rather ultimately have its case heard by an international tribunal rather than by U.S. courts, bear that thought in mind[55].

41. Counsel answered that he would recommend that the Canadian company initiate an action for injunctive relief only, so that it would preserve its ability to bring a NAFTA claim. This led to questions regarding what would happen if the U.S. courts, in dealing with the requested injunctive relief, were to decide the merits before a NAFTA tribunal reached those issues[56].

42. The Claimants responded by arguing that decisions of domestic courts should not be given *res judicata* effect. In the Respondent's view, this response misses the point. The role of a NAFTA tribunal is not to interpret and apply the contract, or to otherwise apply domestic law like a domestic court. Its role is to determine solely whether there has been a violation of NAFTA Chapter Eleven.

43. Consequently, in the President's example the Canadian investor should invoke Chapter Eleven only if it considered that the United States had contravened the NAFTA, and not simply to resolve a dispute over whether the municipality had breached the concession contract. Whether or not the contract was properly nullified is an issue of domestic law, to be resolved in the domestic courts (given that the domestic proceedings could reach a much broader scope of

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55. See Hearing Transcript dated Thursday, June 24, 1999 at pages 36-38.

56. President Paulsson stated: "They turn to you and say, 'I can go to court in America. It says so. I have submitted and the city has submitted to the jurisdiction of the U.S. courts.' So why don't I have —what if I do that? What if I go to the U.S. courts, all of the way up to the Supreme Court, as far as I can go, is there any risk that having done so and then hearing from the U.S. courts that they don't find that there was anything wrong with the decision, therefore, the nullification or the rescission, one or the other, is upheld, isn't there a risk that I am then precluded, irrespective of the fact that internationally I might be making a claim as the Canadian shareholder in the investment field?"

Mr. Civiletti added: "Well, the next step in what you acknowledge to be an argument that has some merit is, if the declaratory claim or injunctive claim involves a decisional issue, which is at the heart of a later NAFTA claim for damages, and it's been resolved adversely to the Claimant, under the same argument or inference, could one argue that the claim for damages, which is based on the same issues that have been decided in the declaratory action by the domestic court, the NAFTA claim is successive, NAFTA claim is also [sentence interrupted]". See Hearing Transcript dated Thursday, June 24, 1994 at pages 39-48.

legal issues, it would normally be more advantageous for the Canadian company to pursue domestic proceedings rather than pursuing NAFTA arbitration).

44. If the Canadian company made investments to perform the concession contract, and the state government had then enacted legislation invalidating the contract on the basis that the contractor was Canadian, and refused to pay the Canadian investor fair compensation for its investment, the Canadian investor might wish to assert that its investment had been expropriated in violation of NAFTA Article 1110, and/or that it had been denied national treatment in violation of Article 1102. Alternatively, the Canadian investor might seek to have the legislation declared unconstitutional by the U.S. courts on the basis that it was inconsistent with the Fifth Amendment and the Commerce Clause[57]. If the investor sought money damages in the U.S. courts, it would be precluded from NAFTA arbitration.

45. If the investor sought injunctive relief only in the U.S. courts, and the courts ruled that the municipality's action was lawful and constitutional, a NAFTA tribunal could conceivably determine that the legislation under which the municipality acted was nonetheless inconsistent with Article 1110 (expropriation) and Article 1102 (national treatment) of the NAFTA. Because the governments of the NAFTA Parties intended the obligations imposed by NAFTA Chapter Eleven to be consistent with the obligations already imposed by their respective domestic laws, this outcome would be unlikely.

46. If it was argued successfully that NAFTA tribunals have a broad jurisdiction to act in place of domestic courts in resolving contract disputes and other issues of domestic law, such tribunals could issue rulings inconsistent with domestic jurisprudence and the decisions of the domestic courts. The limiting language of Articles 1116 and 1117 shows that that the Parties did not intend this to occur. Were such a result to obtain through a strained interpretation of Articles 1116 and 1117, as a policy matter, the Respondent considers that the result would be unacceptable to all three Parties.

3. *A Tribunal's Jurisdiction vis-a-vis Determinations of Domestic Law by the Domestic Courts*

47. On June 24th, during the closing arguments, Messrs. Paulsson and Civiletti posed another question going to the Tribunal's jurisdiction. Specifically, both asked the Respondent whether there were any circumstances under which the Tribunal should be allowed to examine whether the Mexican authorities, either executive or judicial, had properly applied Mexican domestic law. Their questions were as follows:

> PRESIDENT PAULSSON: ...Do you consider that there are circumstances when a NAFTA Tribunal could rule on whether Article 167... ha[s] been correctly applied, or do you consider that

57. The Fifth Amendment ("nor shall private property be taken for public use, without just compensation") imposes an obligation on the U.S. government analogous to that of NAFTA Article 1110. The Commerce Clause, contained in Article I, Section 8 of the Constitution, vests the U.S. Congress with the authority to regulate interstate and foreign commerce, and has been interpreted to prohibit the states from enacting laws that discriminate against foreign commerce (analogous to the obligation of national treatment imposed by NAFTA Article 1102). See, for example, *National Foreign Trade Council v. Natsios and Anderson, No. 98-2304* (1st Cir. June 22, 1999) (Massachusetts law prohibiting government procurement from companies doing business in Burma held violation of Commerce Clause, as well as of Supremacy Clause and of federal government's exclusive power to conduct foreign affairs); *Tupman Thurlow Co. v. Moss*, 252 F. Supp. 641 (M.D. Tenn. 1966) (state law imposing special labeling requirements on imported meat held violation of Commerce Clause).

there are no circumstances when a NAFTA Tribunal could make a determination as to whether or not Article 167 has been correctly applied by Mexican authorities, executive or judicial?

MR. CIVILETTI: Is it your position that the NAFTA Tribunal, once that has been determined by a domestic court or courts, cannot then review the determination of the grounds for nullity, whether they're one or 27 or nine, under any circumstances?

48. The Respondent is of the view that a NAFTA tribunal would have a jurisdiction in the unlikely event that a NAFTA breach was committed by the executive or the judiciary in a domestic judicial proceeding.

49. For example, on the facts present in the case at bar, suppose that having invoked the assistance of the Mexican courts, the court permitted the municipality to adduce evidence to support its decision to nullify but refused the company the same opportunity, and then upheld the nullification on the basis of the evidence adduced by the municipality.

50. Such action might give rise to a NAFTA claim because, in breach of the *audi alteram partem* rule, the court did not accord the complainant an opportunity to make its case; this would be a potential breach of the rules of natural justice, therefore implicating NAFTA Article 1105. In this example, it would be the court's failure to accord the Claimants' enterprise a fair hearing rather than the nullification *per se* that would provide the basis for the NAFTA claim.

51. In addition, it is conceivable, albeit remote, that a domestic court could depart from the conventional understanding of the substantive domestic law to such an extent as to raise a question as to whether there was a denial of justice.

52. Even in that type of case, however, the NAFTA tribunal would not sit in review of the domestic court's decision *per se*. Instead, the tribunal's task would be to determine whether the court's actions were so unfair and unreasonable as to constitute a violation of the minimum standards established by international law[58].

53. In considering whether to embark upon such an inquiry, however, a NAFTA tribunal would have to give serious consideration to the following issues:

a) It is well established in international law that international arbitral tribunals are not courts of review of the decisions of national courts. There would have to be extraordinary grounds for engaging in such a review.

b) International arbitral tribunals have repeatedly found that of the various arms of the State (the Executive, the Legislature, and so on) the decisions of a nation's judiciary are to be accorded the most deference.

c) A corollary to this is the recognition that the domestic courts are the most qualified of all bodies to determine the lawfulness of actions under domestic law. Conversely, international tribunals, which do not have the expertise or experience of the local courts, are not as well qualified to review the courts' decisions.

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58. In other words, the tribunal would not substitute its own judgment for that of the governmental agency and the courts, but rather would determine whether the conduct of the governmental and judicial authorities in reaching their decisions violated international law.

d) A NAFTA tribunal would also be guided in the inquiry by whether an appeal of the impugned decision was taken. The upholding of the court of first instance by a court of appeal would give rise to a strong presumption of regularity.

e) If a NAFTA tribunal considered that there *was* a basis for reviewing the court's decision, it would have to have the necessary evidence before it. This would require evidence from qualified experts on the domestic law who would testify as to the matters at issue.

f) Assuming that such evidence was received, the NAFTA tribunal would have to be satisfied that there was clear and convincing evidence of a serious departure from the domestic law in order to justify a finding that the court's decision led to a NAFTA breach. In this regard, even a determination that the domestic court had erred would be insufficient to justify intervention; the tribunal would have to be satisfied that the domestic court erred in such a fundamental way as to constitute a denial of justice or otherwise have committed a breach of the NAFTA.

54. The more that the domestic courts scrutinized the matter and the higher the final such court stood in the domestic judicial hierarchy, the less likely that a NAFTA tribunal could find it appropriate to review the national determination. It would be a truly extraordinary act for a NAFTA tribunal to hold that a court of appeal or Supreme Court of any of the NAFTA Parties had countenanced an act that attracted NAFTA liability, either because of its alleged failure to correct a NAFTA breach or because the court itself engaged in such a breach.

55. Such a remote possibility is, of course, not present on the facts of this instant case. To the contrary, the Claimants have not complained of any Mexican law. They have also expressly conceded that they do not allege that there was a denial of justice by the Mexican courts, and they do not challenge the correctness of the courts' decisions.

56. Nor have the Claimants offered proof of the applicable Mexican law or any expert evidence or even a suggestion as to how the Mexican law —and in particular Article 167, the State law on nullification of concessions— should have been applied. They have simply cited the language of the concession contract as though it existed in a legal vacuum.

57. The Respondent has pointed out that the decisions rendered by the Mexican courts contain legal and factual elements that are highly relevant to the present proceeding. It has also submitted that the NAFTA does not empower the tribunals established under Chapter Eleven to act as courts of appeal for decisions rendered by municipal courts. Both the commentary of qualified publicists and the decisions of previous international arbitral tribunals confirm this position.[59]

58. Consequently, the decisions of domestic tribunals should be accorded full respect, except in the most extraordinary circumstances, which in any event are not present in this case.

PART IV: CONCLUSIONS AND RELIEF REQUESTED

59. From the beginning, the Claimants have asserted that their claim is based upon a breach of contract. As the authorities and commentaries cited in the Counter-memorial and Rejoinder demonstrate, the mere breach of a contract between an enterprise and a local government of a State cannot be elevated to the level of an international wrong which attracts liability on the part of the State.

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59. See Counter-memorial, Part III, Legal Submissions at paragraphs 232-235.

60. Moreover, the facts demonstrate that the present claim is not even a credible breach of contract claim, let alone a serious international claim. On basic principles of law commonly applied in the major legal systems of the world, it is manifestly clear that the nullification of the contract was completely justified, and that the Claimants were extended a fair and reasonable opportunity to respond to the *Ayuntamiento* and to appeal the nullification.

61. The Claim does not contain any elements that could elevate it to the international plane, such that the principles of state responsibility on the part of Mexico could be engaged. In addition, the numerous misrepresentations and misstatements of the Claimants (including in the presentation of evidence to the Tribunal) demonstrate a lack of good faith. For these reasons, the Claim should be dismissed with costs awarded to the Respondent.

62. The Respondent seeks the award of its costs at a minimum:

i) its share of the fees assessed by the ICSID for the conduct of this proceeding; and

ii) the fees paid by it to its valuation expert to respond to the allegations of the Claimants regarding their damages. Reimbursement of the costs of the valuation expert are justified, *inter alia*, by the Claimants' failure to disclose in a timely fashion that they had previously sold DESONA's assets and business to Sanifill and the amount they received therefor.

63. The Respondent believes it is also justified in requesting reimbursement of the costs of legal representation, and is prepared to submit information on those costs for consideration by the Tribunal should it so request.

All of which is respectfully submitted

(signature)

Hugo Perezcano Díaz
General Counsel for Trade Negotiations
Secretariat of Trade and Industrial
Development