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

ROBERT AZINIAN AND OTHERS
CLAIMANTS

VS.

THE UNITED MEXICAN STATES
RESPONDENT

COUNTER MEMORIAL

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The Respondent's Counter-memorial will be divided into four parts and six annexes:

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PART III. Legal Submissions
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Witnesses:

A. Mr. Raul Romo Velázquez
B. Mr. James Hodge
C. Mr. J. Cameron Mowatt
D. Dr. Carlos Felipe Dávalos
E. Mr. Francesco Piazzessi
F. Patrícía Tejeda
G. Mr. Emilio Sánchez
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COUNTER-MEMORIAL OF THE UNITED MEXICAN STATES

PART I: INTRODUCTION

1. The Respondent submits that the Claimants do not have valid grounds for bringing these proceedings under the North American Free Trade Agreement ("NAFTA"). As the Tribunal will see, all legal rights of the Claimants with respect to their failed attempt to operate the waste disposal concession in the Municipality of Naucalpan de Juárez, State of Mexico, were fully and fairly determined under the Mexican legal system. Disgruntled with this result, the Claimants have brought this action in an attempt to use this Arbitration Tribunal as a court of appeal to review those determinations.

2. The Respondent's Counter-memorial will begin by bringing certain facts omitted by the Claimants to the attention of the Tribunal. They are highly material and, once appreciated by the Tribunal, will assist it in understanding why the concession was nullified. The Counter-memorial will then explain the events leading up to and following the concession's nullification. Thereafter, it will set out additional facts relevant to the disposition of this matter. The admissions and denials of the facts alleged by the Claimants required by Article 38 (3) of the Arbitration (Additional Facility) Rules are contained in Annex 1.

3. For ease of reference, the Respondent includes Mr. Ariel Goldenstein when using the term "Claimants". This is not in any way to be taken to be an admission that Mr. Goldenstein has any legal right to assert any claim in this or other proceeding under the NAFTA. Rather, it is because Mr. Goldenstein has assumed the role of a "quasi-claimant" in that he has purportedly assigned his interest in Desechos Sólidos de Naucalpan, S.A. de C.V. ("DESONA") to Mr. Robert Azinian in the hope that, were damages awarded, Mr. Azinian could recover on his behalf. This, it will be argued, is a patently untenable attempt to circumvent the eligibility strictures of NAFTA Articles 1116 and 1117.

4. Although, as a matter of law, he cannot qualify to make a NAFTA claim, Mr. Goldenstein has been the most active of the former principals of DESONA in participating in this proceeding. The Tribunal will recall that it was Mr. Goldenstein, not the Claimants, who swore under threat of prosecution for perjury that the statements that he made in response to the Respondent's request for particulars, for example, were true. Since Mr. Goldenstein played a central role in the events in dispute, purely for convenience sake, he will be included in the term "Claimants".

5. On the other hand, the Respondent notes that the Claimant Ellen Baca seems to have had little to do with any of the events in question and is present only because, as part of a matrimonial settlement, she purportedly received what are claimed to be Mr. Kenneth Davitian's shares in the version of DESONA that allegedly entered into the concession contract.

6. It is important to note that there is confusion with respect to the identity of DESONA. The different versions of DESONA will be addressed in Section C, Additional Facts. For present purposes, when the term Global/DESONA is used, it refers to an entity run by the individuals who ostensibly owned Global Waste Industries, Inc., and who ended up incorporating a company that signed the concession contract (DESONA B) even though the concession was held by DESONA I at the time.

PART II: STATEMENT OF FACTS

A. Omitted Facts

7. The Memorial omits to address certain fundamental facts which are dispositive of the claim.

The Fate of the Consortium

8. The Memorial discusses the origins and theory of the Integral Solution Project, but the Tribunal is given no sense of what actually transpired. The implication is that the project as originally conceived and presented to the *Ayuntamiento* (the Municipal Council) and approved by it on November 4, 1992, is what was actually implemented. As shall be seen below, this is far from the truth.

9. The Integral Solution Project, as presented to the *Ayuntamiento*, was to be performed by a consortium of companies: Global Waste Industries, Inc. (Global), Bryan A. Stirrat & Associates (BAS), Sunlaw Energy Corporation (Sunlaw) and México Diesel Electro-Motive S.A. de C.V. (México Diesel) (the latter affiliated itself with Sunlaw to set up a Mexican corporation — Sunlaw de México, S.A. de C.V. —to participate in the project).

10. The Claimants, the Tribunal will see, represented themselves as shareholders and officers of Global[1]. Evidence of Mr. Goldenstein's making shows, however, that although he was vice-president of Global, neither he nor Mr. Azinian had *any* shareholding interest in Global. Mr. Davitian did; however, he owned only 15% of the shares of the company. Moreover, although Mr. Azinian was held out as being the President of Global[2], in fact he did not occupy any position with the company[3].

11. For present purposes, it is sufficient to note that Messrs. Azinian and Goldenstein both held themselves out as owners of Global, and the former as the company's President. For that reason, they will be described as the "ostensible owners" of Global. They, apparently together with Mr. Davitian, formed one of the versions of DESONA. This will be addressed further below.

12. The Memorial refers to, and includes as an exhibit, the Memorandum of Understanding (MOU) signed by Global, Sunlaw and BAS on November 3, 1992, the day before the concession was granted. The evidence of Mr. Raúl Romo of Sunlaw de México, S.A. de C.V.(Sunlaw de México) is that Sunlaw did indeed sign the MOU setting out how the consortium would operate,

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1. In the response to the Respondent's request for particulars, it was stated that each of Mr. Azinian, Mr. Davitian and Mr. Goldenstein held a 33% shareholding interest in Global.
2. In the Spanish "company profile" of Global Waste Industries prepared by the Claimants, Mr. Azinian was described as "President" of Global. See Exhibit 1.
3. See Statement of Financial Affairs for Global Waste Industries, Inc., sworn by Mr. Goldenstein and filed in the United States Bankruptcy Court, June 11, 1992, in Exhibit 2 of Respondent's Motion for Directions to Answer Request for Particulars and Produce Documents, June 8, 1998 (hereinafter Respondent's June 8, 1998 Motion).

but by January 20, 1993 (only two months after signing it), Sunlaw informed Global that it would not participate with Global on the basis of that agreement.

13. Sunlaw's President, Mr. Robert Danziger, held a meeting with Mr. Azinian and Mr. Davitian on January 19, 1993. In his letter to Mr. Azinian written the next day, Mr. Danziger reiterated Sunlaw's objections to forming a relationship with Global on the basis contemplated by the November 3rd MOU, informing Mr. Azinian that:

> "Reference is... made to the Memorandum of Understanding dated 3 November 1992. As it is now clear that at least three material terms of the Memorandum cannot be satisfied, the position stated below replaces and supercedes the Memorandum.
>
> Please note that Sunlaw strongly objects to Global's failure to deliver documents, data and other information in a timely way despite repeated requests; failure to disclose material financial and trade information; and, unauthorized disclosure to competitors of highly sensitive and confidential data considered proprietary by Sunlaw and marked as confidential in transmission to Global. In addition, very serious communication problems require that alternative approaches for moving forward be implemented."[4] [Emphasis added]

14. It is evident from these paragraphs that Sunlaw was disturbed by Global's behavior in the two months following the MOU's signing. Mr. Danziger went on to set out Sunlaw's position:

> "It is Sunlaw's position that it is now Global/Desona's responsibility to complete it's [sic] deal with the Municipality of Naucalpan and to comply with all Federal, State and Local requirements. Selection of Global/Desona for the waste collection and recycling is solely the province of Naucalpan, and we will not interfere in that process. You have represented to us that your position with Naucalpan is secure, and we have no reason at this time [to] believe otherwise, although we do understand that negotiations are continuing, contracts are not signed, Federal approvals have not yet been obtained, and that performance bonds need to be provided by Desona shortly. It is in everyone's best interest that you complete these things quickly."[5] [Emphasis added]

15. In place of the MOU, Mr. Danziger stated that Sunlaw would not align itself closely with Global/DESONA:

> "Global/Desona and Naucalpan will be responsible for negotiating with CFE [the Federal Energy Authorities] or any other party for payment of the services to be rendered by Global/Desona. If Sunlaw is asked to receive funds from CFE or any other party on behalf of, or for the benefit of Global/Desona, Sunlaw will use its best efforts to do so, subject to all requirements of our financiers, lenders and equity investors as well as Mexican and United States laws."[6]

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4. Letter from Mr. Danziger to Mr. Azinian, dated January 20, 1993, Exhibit 2 in the witness statement of Mr. Raúl Romo.
5. Ibid.
6. Ibid.

16. By its own terms, this letter was copied to Mr. Bryan Stirrat, and Mr. Danziger sent another copy to Mr. Romo.

17. After January 20, 1993, therefore, according to the evidence of Mr. Romo, Mr. Danziger's partner in the energy project, the energy generation part of the project proceeded on a separate track from the garbage collection track. Throughout the period leading up to the end of October of 1993, just before DESONA B signed the concession contract, Sunlaw de México had some dealings with the municipal officials, but dealt mainly with federal energy officials. It had virtually no dealings with Global/DESONA itself for the reasons stated in Mr. Danziger's letter[7].

18. Mr. Romo testifies that in March of 1993, Sunlaw was informed by Mr. Abel Duarte, the General Director of Economic Development, that it had erred in estimating the electricity consumption figures. Instead of being able to consume 200 megawatts, the municipality could consume only 15 to 20 megawatts. This made the project simply not economically feasible. Over the next months, Mr. Duarte sought to broaden the geographical scope of the project by approaching other neighboring municipalities in the hope that they would be interested in consuming the energy that would be generated[8].

19. In addition, Sunlaw de México found that the biogas generated by the Rincón Verde landfill would not provide a rich enough fuel supply for the electricity plant. It would have to be complemented by up to 90% natural gas. This would involve the construction of a natural gas pipeline to the landfill where the plant would be located, with a corresponding increase in cost[9].

20. By the end of October of 1993, it was clear that the deficit in the anticipated electricity demand was not going to be made up and the electricity project —which Mr. Romo points out was intended to pay for the rest of the solid waste project, including the purchase of the state-of-the-art garbage trucks — was not economically feasible. Thus, he testifies that at that point, Sunlaw de México lost interest in the project[10].

21. Mr. Romo testifies that the inclusion of the electrical generating phase in the concession contract that Global/DESONA signed made no sense because the underlying financial projections would not work, and there was no possibility that it would actually be implemented. He believes that any other power company that examined the project would arrive at the same conclusion[11].

22. This explains why the Memorial devotes considerable space to describing the Integral Solution Project but omits to explain why the lead company, Sunlaw de México, which had the technical expertise and the access to the capital necessary for the project, disappeared from the scene and did not appear as part of the concessionaire. Of course, since Sunlaw de México was supposed to finance the whole project, its absence from the final contract highlights one of the fundamental problems that Global/DESONA faced in performing the concession contract:

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7. Witness statement of Mr. Raúl Romo.
8. Ibid.
9. Ibid.
10. Ibid.
11. Ibid.

namely, finding the funds to pay for the state-of-the-art trucks and equipment that it promised to provide.

23. To the extent that the Memorial adduces evidence regarding the energy generation part of the concession as originally conceived, that evidence has been taken from documents prepared by Sunlaw de México or one of its two parent companies and passed off, implying falsely that it was material produced by Global/DESONA.

24. With respect to the other intended member of the consortium, Bryan A. Stirrat & Associates (BAS), the Respondent has been unable to precisely identify the nature of its participation in the project. It is clear that BAS continued to do business with Global even though Mr. Stirrat was apparently copied with Mr. Danziger's letter of January 20, 1993. Mr. Stirrat also attended key meetings such as the June 1, 1994 meeting of the *Cabildo* at which DESONA defended its performance of the concession.

25. It has been represented to the Tribunal both by the Claimants and by Mr. Stirrat himself that BAS was a mere subcontractor to Global/DESONA and that it is owed monies for services it rendered[12].

26. The Respondent's investigation of the claim yielded evidence that the relationship between Mr. Stirrat and Global/DESONA was much closer than that represented to the Tribunal. First, the evidence of Mr. Jim Hodge, formerly of the Washington State-based company, Regional Disposal Company (RDC), is that in late December of 1993, one month after the concession entered into force, he was contacted by an employee of BAS to inquire as to his company's interest in investing in Global/DESONA. In fact, in early January of 1994, he and his superior visited Naucalpan to inspect Global/DESONA's operations. They were accompanied by Mr. Stirrat himself[13].

27. Secondly, in early 1994 after RDC declined to invest in DESONA, Mr. Stirrat arranged for a broker, Mr. Mike Carolan, to try to attract investors to Global/DESONA. One of the people contacted by Mr. Carolan was Mr. Sam Maphis of Boulder, Colorado. From the file provided to the Respondent by Mr. Maphis, it is clear that he understood that Mr. Stirrat was an owner of Global/DESONA, not a subcontractor[14].

28. Mr. Stirrat originally volunteered to answer written questions put to him by the Respondent. To obtain further information on this issue, therefore, the Respondent sent detailed questions to Mr. Stirrat on July 1, 1998, inquiring *inter alia*, as to the extent if any of his ownership interest in DESONA.[15] After repeated inquiries as to whether he intended to respond, on September 24, 1998, Mr. Stirrat sent a letter to counsel declining to answer the questions posed to him[16].

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12. See the Memorial, Section 6, p. 1.
13. Witness statement of Mr. Jim Hodge.
14. Witness statement of Mr. J. Cameron Mowatt.
15. Ibid.
16. Ibid.

29. The Respondent intends to address Mr. Stirrat's activities further in the Oral Procedure phase of this proceeding.

The Fundamental Misrepresentations to the Ayuntamiento

30. For obvious reasons, the Memorial repeatedly attempts to distance Global/DESONA and Mr. Goldenstein from the statements that he made to induce the *Ayuntamiento* to grant the concession. It is argued that his representations (and others made at the November 4, 1992 meeting) are not relevant because some of them were not reflected in the contract that purported to memorialize the concession. However, the municipal administration that nullified the concession concluded that there were major misrepresentations made to the *Ayuntamiento*.

31. Although Global/DESONA was summoned to a hearing in order to provide explanations and proof to the contrary in response to the *Ayuntamiento's* findings, it failed to do so. Global/DESONA was given an opportunity to reply in writing following the hearing. In its reply, Global/DESONA focused on the purported inability of the *Ayuntamiento* to nullify the concession, but did not address the *Ayuntamiento's* findings.

32. The Memorial omits to note the fact that in its initial solicitation of the solid waste disposal concession to the municipality and in its presentation to the *Ayuntamiento* in November 1992, Global misrepresented the true state of its experience and its complete lack of financial capacity. Some of the major misrepresentations include the following:

a) Global prepared a company profile in Spanish stating that it had "more than 40 years of experience" and was "considered to be a leading company in the industry"[17]. These statements were false. A search of the California State Public Registry shows that far from having the experience that it claimed, the company had been incorporated only six months before the statements were made and only sixteen months before the Claimants appeared before the *Ayuntamiento*[18]. Moreover, of its principals, only Mr. Davitian had any experience and he did not have more than 40 years of experience that could be imputed to the company.

b) Global petitioned itself into bankruptcy in the United States Court of Bankruptcy on May 28, 1992[19], some six months *before* Mr. Goldenstein appeared before the *Ayuntamiento* and outlined his company's plans for delivering new trucks and other equipment, closing and sealing the Rincón Verde landfill and turning it into a recreational park, and making an investment of 60,000,000 new pesos (20 million U.S. dollars)[20]. Global's total annual income according to Mr.

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17. See Exhibit 1.
18. See Exhibit 2.
19. See the bankruptcy records of Global Waste Industries, Inc. in Exhibit 1 of the Respondent's June 8, 1998 Motion.
20. See Exhibit 3, the minutes of the *Cabildo* session of November 4, 1992;

Goldenstein's sworn testimony in the bankruptcy proceedings was 30,000 dollars[21].

c) Throughout the period leading up to the presentation to the *Ayuntamiento*, in written communications with the municipality and in the company profile, as noted earlier, Mr. Azinian held himself out as President of Global[22]. However, in the company's Statement of Financial Affairs filed in the company's U.S. bankruptcy proceeding, Mr. Goldenstein swore that Mr. Davitian, not Mr. Azinian, was President[23].

d) In fact, neither Mr. Azinian nor Mr. Goldenstein had *any* experience in the garbage business. Mr. Azinian had operated diverse businesses such as Da Azini, Inc., Two Roberts Shoe Co., RA RA RA Shoe Inc. Corp., Black Knight Production, Inc., and American Mall Management, and in the late 1980's, prior to declaring personal bankruptcy in late December of 1990, held a one-half interest in a gas station[24].

e) Mr. Azinian had a history of lawsuits against him at: least 34 in the greater Los Angeles area at the time that the concession was granted. Most involved breach of contract or misrepresentation claims. For example, in 1989, Mitsui Manufacturers Bank sued him in Los Angeles Superior Court for breach of contract and obtained a judgment against him for 250,300 dollars[25].

f) Mr. Davitian also had a history of unsuccessful business dealings and lawsuits against him. Like the suits against Mr. Azinian, these lawsuits involved breach of contract and misrepresentation claims. The Respondent has been able to identify 9 default judgments against Mr. Davitian[26].

g) Mr. Goldenstein's business experience was limited to the ownership of a restaurant in Los Angeles known as "Johnny Rockets"[27].

The Legal Proceedings in the Mexican Courts

33. Mr. Azinian cryptically comments at the end of his witness statement as follows:

"We tried to get an injunction from a local administrative court who would not act at all. I understand that we lost our injunction efforts because we should have responded to the

21. See the bankruptcy records of Global Waste Industries, Inc. in Exhibit 1 of the Respondent's June 8, 1998 Motion.
22. See Exhibit 6 of the Respondent's June 8, 1998 Motion.
23. See Exhibit 2 of the Respondent's June 8, 1998 Motion.
24. See Exhibit 4 of the Respondent's June 8, 1998 Motion.
25. Mitsui Manufacturers Bank v. Robert Azinian, Los Angeles Superior Court, File Number 707381C, judgment date 08/09/89. See Exhibit 4 of the Respondent's June 8, 1998 Motion.
26. See Exhibit 5 of Respondent's June 8, 1998 Motion.
27. See Exhibit 4.

trumped up charges within four days. I further understand that we never had a 'day in court' about our damages for loss of the contract."[28]

34. Similarly, although the Memorial makes a very brief reference to domestic legal proceedings, it does not do justice to what actually transpired after the nullification process was initiated. After receiving notice of the 27 irregularities from the *Ayuntamiento*, Global/DESONA immediately commenced suit in the State Administrative Tribunal challenging the decision to commence nullification proceedings.

35. The evidence of the external legal consultant retained by the municipality, Dr. Carlos Felipe Dávalos Mejía, shows that when called upon to defend its actions, the municipality did so. He both advised the municipality on the nullification of the concession and defended it in the subsequent legal proceedings[29].

36. Dr. Dávalos notes that while he adduced extensive evidence in defense of the municipality's actions, Global/DESONA did not. He introduced three expert reports, including one on the financial expenditures that the municipality was forced to make while the concession was being operated by Global/DESONA. Global/DESONA's "expert's report" was *a single page* which purported to set out the company's expenditures. Not surprisingly, the State Administrative Tribunal found it to be incomplete[30].

37. Dr. Dávalos also testifies that after the nullification was upheld, DESONA appealed to the Superior Chamber of the State Administrative Tribunal. Once again, the Superior Chamber ruled in favor of the municipality. This time the nullification was upheld on the basis of 9 of the 27 irregularities, the Superior Chamber holding that *the first of the 9 irregularities identified* was sufficient to support the nullification[31].

38. He testifies further that DESONA then brought a constitutional *amparo* challenge before a Federal Circuit Court. After extensive consideration of the matter, that court also found that the municipality was fully justified in its action[32].

B. Events Leading Up to and Following Nullification

The Concession

39. As pleaded by the Claimants, a concession was granted by the municipal administration of Naucalpan led by Municipal President Mario Ruiz de Chávez.

40. The concession was granted by the *Ayuntamiento* on November 4, 1992. The concession involved the collection and recycling of municipal waste; the remediation and closure of the existing landfill, Rincón Verde, and the development of a sports park on the site upon closure;

28. Witness statement of Mr. Azinian at page 5 and 6.
29. See witness statement of Dr. Carlos Dávalos.
30. Ibid.
31. Superior Chamber's decision dated November 17, 1994. See Exhibit 31.
32. Federal Circuit Court's decision dated May 18, 1995. See Exhibit 33.

the development of a new landfill at Corral del Indio; and the construction of an electrical power plant and generation of electricity using bio-gas produced at the landfills.

41. In essence, the concession was approved under the following terms: the concession would be operated by a consortium of four companies: Global Waste Industries, Inc., Sunlaw Energy Corporation, México Diesel Electro-Motive, S.A. de C.V. and Bryan A. Stirrat & Associates. The project would be fully funded by the consortium which would, nonetheless, hold only 90% of the capital stock, as the Municipality would hold title to the remaining 10%, with no investment on its part. The 90% participation held by the consortium was to be comprised of 45% U.S. capital and 45% Mexican capital[33].

42. Since it was intended that the concession would last for a period of 15 years, it was necessary to seek the approval of the State Legislature. Approval was granted on August 16, 1993.

43. Negotiations over the contract that was to memorialize the terms of the concession then took place. The results of the negotiations purported to memorialize the terms of the concession.

44. The contract was signed by Mr. Azinian and Mr. Goldenstein for Global/DESONA and Municipal President Ruiz de Chávez and Municipal Secretary Chávez Tello for the municipality.

45. The concession contract entered into force on November 15, 1993.

The Concession Contract's Performance

46. On or about December 23, 1993, prior to officially taking office, the incoming General Director of Economic Development, Mr. Francesco Piazzesi di Villamosa, and the newly elected Municipal President, Enrique Jacob Rocha, met with Global/DESONA to review the initial implementation of the concession contract. Mr. Piazzesi testifies that he was enthusiastic about the prospect of the improved service that Global/DESONA was to provide under the concession[34].

47. Mr. Piazzesi's evidence is that at the first meeting, held approximately one month after Global/DESONA purportedly began performance under the concession, he informed the Global/DESONA representatives that the people of the municipality were not happy with the first month of Global/DESONA's public waste collection service. According to Mr. Piazzesi, "it appeared to us that Global/DESONA was concentrating on developing fee paying commercial and industrial accounts and was ignoring its duty to provide the public waste collection service"[35].

48. By the end of December of 1993, before the new administration even took office, Global/DESONA had already failed to comply with the requirement to introduce seven state-of-the-art trucks for use in the public waste collection service. Global/DESONA had

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33. November 4, 1992 *Cabildo* session. See Exhibit 3.
34. Witness statement of Mr. Francesco Piazzesi.
35. Ibid.

introduced only two trucks of its own into circulation which were devoted to servicing the industrial and commercial areas of the municipality for which it charged fees for collection[36].

49. In order to try to meet its contractual obligations, therefore, in December of 1993 and throughout the period leading up to the concession's nullification, Global/DESONA used the municipality's aging fleet of trucks, its fuel, and its workers — all at the municipality's expense[37].

50. Mr. Piazzesi testifies that Mr. Goldenstein told him that the trucks necessary to perform the concession were on order from the United States and that they would put them to work as soon as possible[38].

51. On December 31, 1993, Naucalpan's Municipal President Ruiz de Chávez's three year administration ended.

52. On January 1, 1994, the NAFTA entered into force. On the same day, the new Municipal Government took office.

53. The evidence of Mr. Jim Hodge, the former Senior Vice President of the Seattle, Washington-based company, RDC, is that in early January of 1994, he and RDC's owner, Mr. Warren Razore, visited Naucalpan at Global/DESONA's request. The request was made to him through Mr. Dave Luneke, an employee of Bryan A. Stirrat & Associates[39].

54. BAS approached RDC to see if it was interested in investing in Global/DESONA. Messrs. Hodge and Razore were accompanied on their visit to Naucalpan by Mr. Stirrat. Mr. Hodge testifies that it took them very little time to see that Global/DESONA was incapable of performing the concession. The company's "dispatch center", for example, was being operated out of a small house and there were very few employees. Hodge and Razore formed the opinion that the principals of Global/DESONA were very inexperienced and out of their depth[40].

55. In a letter to a Mexican waste disposal operator written on August 19, 1994, attached to his witness statement as Exhibit 1, Mr. Hodge recalled the visit:

> "...Warren Razore, the owner of our company, and myself, at DESONA's request, spent some time with them in Mexico in early January 1994. <u>During the course of those discussions it was apparent that 1) they were looking for additional capital on a seemingly desperate basis, and 2) it was apparent to us that they were not capable of fulfilling their commitments to the municipality of Naucalpan. A substantial part of our determination to not proceed further with DESONA was based on our perception of their overall corporate operational capacity, and we felt that they were behind in their obligations to Naucalpan.</u>

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36. Ibid.
37. Ibid.
38. Ibid.
39. Witness statement of Mr. Jim Hodge.
40. Ibid.

As far as we were concerned, that was the end of the matter for us until you and I discussed the present circumstances, and you had informed me that Naucalpan was compelled to terminate their concession with DESONA.

Ernesto, we feel that the entire DESONA incident was a mistake and this history could potentially harm subsequent well-planned and well-financed solid waste projects. Therefore we feel it is imperative that we make sure that the record is straight, not only with the various governmental agencies in Mexico, but also with the United States governmental agencies (due to NAFTA and the environmental side agreements)."[41] [Emphasis added]

56. Thus, it was evident to an independent third party as early as the beginning of January of 1994, that Global/DESONA was incapable of performing the concession.

57. In January of 1994, Global/DESONA invoiced the municipality. Mr. Piazzesi testifies that the municipality refused to pay the invoice because Global/DESONA was not providing the waste collection service as required by the concession contract, and the municipality was still paying the salaries of all the municipal workers as well as for its fleet of trucks (and the fueling thereof). In general, it was not satisfied with Global/DESONA's performance[42].

58. Mr. Piazzesi testifies that, in essence, Global/DESONA wanted the municipality to pay twice; it had to pay for its own trucks, workers, and fuel, yet Global/DESONA expected to be paid a service fee for the activity performed by the municipality's own trucks and workers[43].

59. The municipality's external legal counsel, Dr. Dávalos, testifies that he later provided expert evidence of the municipality's continued expenditures to the State Administrative Tribunal when Global/DESONA appealed the concession's nullification by the *Ayuntamiento*. A financial expert reviewed the municipality's financial accounts and testified that there had been no diminishment in its expenditures. The Tribunal accepted this testimony[44].

60. Mr. Piazzesi testifies that in January of 1994, he was repeatedly instructed by Municipal President Jacob to contact Messrs. Goldenstein and Azinian to discuss the waste service issue. He says that he had at least seven meetings with them in January and February of 1994, and that they continually promised they would comply with the concession contract and the operation program. However, with the garbage situation worsening rather than improving, public pressure upon the administration was mounting, and officials did not see any sign of progress.

61. Mr. Piazzesi notes that some 300 tons of garbage a day were piling up in the municipality's streets and public areas. He also testifies that although Global/DESONA claims that the garbage crisis that was unfolding in the residential areas could not be attributed to the company because it was not yet responsible for those sectors, this was not in fact the case. In fact, Global/DESONA was using the municipality's trucks and diverting them to its needs and as

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41. Ibid.
42. Witness statement of Mr. Francesco Piazzesi.
43. Ibid.
44. Expert report of Alberto Villarruel Briones dated June 14, 1994. See Exhibit 26.

a result the rest of the municipality was suffering because there were few trucks left to collect garbage in those districts[45].

62. Residents began to protest about the garbage accumulating in public areas. For example, in January some citizens groups went to the Municipal offices and dumped waste in the hallways in protest. Faced with the mounting public pressure, the municipality did not have the resources on hand to solve the problem. Mr. Piazzesi testifies that the municipal government was relying upon Global/DESONA to provide the service and the municipal resources were not enough to collect the growing waste build-up[46].

63. According to Mr. Piazzesi, by mid-January it was becoming clear that Global/DESONA was having problems obtaining the state-of-the-art trucks it had promised to provide both in the November 4, 1992 *Cabildo* session in which the concession was awarded to the DESONA's consortium, and in the concession contract formalizing the concession that was signed on November 15, 1993. In mid-January of 1994, Global/DESONA informed Mr. Piazzesi that they were having problems importing 17 trucks and requested his help. He suggested buying the trucks in Mexico and offered assistance in obtaining a loan from BANOBRAS, a Mexican government-owned development bank, to acquire them. However, the Global/DESONA principals rejected this idea, arguing that BANOBRAS would demand that they acquire Mexican trucks, and that new Mexican garbage trucks were not "state-of-the-art" technology[47]. In fact, Mr. Piazzesi notes that Mercedes Benz, among other companies, manufactures garbage trucks in Mexico. (After the public service reverted back to the municipality upon nullification of the concession, the *Ayuntamiento* acquired Mercedes Benz trucks to continue providing the service on its own[48].)

The Municipality Develops Serious Doubts about Global/DESONA

64. According to Mr. Piazzesi, on February 9, 1994, Global/DESONA again invoiced the municipality. The *Ayuntamiento* again objected to paying the invoice because the municipal government was still paying for the garbage trucks, fuel and the salaries for workers and technicians. While it continued to make the same expenditures as it had prior to the concession contract's entry into force, the public waste problem was worsening and the officials had not seen an adequate response from Global/DESONA. Mr. Piazzesi testifies that he told Global/DESONA that they should be paying the additional expenses being incurred by the municipality[49].

65. The worsening waste disposal problem and the administration's dealings with Global/DESONA led officials to have serious concerns about Global/DESONA's professionalism, financial capacity and its willingness to comply with its obligations under the concession. Mr. Piazzesi was instructed by the Municipal President to try to obtain relevant

45. Witness statement of Mr. Francesco Piazzesi.
46. Ibid.
47. Ibid.
48. Ibid.
49. Ibid.

information about Global/DESONA, Global Waste Industries, and the Global/DESONA representatives themselves[50].

66. Mr. Piazzesi's investigations revealed that the principals of Global/DESONA had made several misrepresentations about their U.S. company, Global, to municipal officials and at the session of the *Cabildo* which approved the grant of the concession on November 4, 1992. Moreover, Mr. Piazzesi formed the opinion that Messrs. Goldenstein and Azinian wholly lacked the technical, administrative and financial expertise required for the concession and that only Mr. Davitian had any experience in the garbage industry at all. He also discovered that both Global and Mr. Azinian had commenced corporate and personal bankruptcy proceedings respectively less than two years before the concession was awarded to Global/DESONA.

67. Mr. Piazzesi also spoke to persons who had had unfortunate experiences in their dealings with the principals of Global/DESONA, including Eduardo and Emilio Sánchez ("the Sánchez brothers"), Mr. Romo of Sunlaw de México, and Dr. Oscar Palacios, a shareholder in DESONA I[51]. (Evidence of each of the Sánchez brothers and Dr. Palacios' dealings with Messrs. Goldenstein, Azinian and Davitian is provided below.)

Outside Legal Counsel Is Retained

68. On or about February 9, 1994, Mr. Carlos Alfaro, the General Director of Municipal President Jacob's Technical Office, contacted Dr. Dávalos of the Mexico City law firm, Dávalos y Associados, S.C. to arrange a meeting between Dr. Dávalos and Messrs. Jacob and Piazzesi to discuss the Global/DESONA problem. Dr. Dávalos was asked to prepare an analysis of the circumstances surrounding the awarding of the concession to Global/DESONA. He was also asked to advise the municipality of its legal rights and obligations.

The Used Trucks Import Problem

69. Given that Global/DESONA was having problems importing the trucks from the United States, in early February of 1994, Mr. Piazzesi contacted the Secretariat of Commerce and Industrial Development (SECOFI) to request its help in facilitating the importation process. At that time, Mr. Piazzesi testifies, he did not know that Global/DESONA intended to import used, rather than new trucks.

70. By letter dated February 10, 1994, the Director General of Industrial Promotion for SECOFI, Mr. Manuel Fernández Pérez, replied to the municipality's request for assistance regarding the importation of the trucks.

71. Mr. Fernández informed Municipal President Jacob that the trucks the company sought to import were as follows:

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50. Ibid.
51. Ibid.

"...new and used waste cleaning equipment the first importation petition consisting of 17 used waste collecting trucks (10 Volvo White Expeditor trucks; 5 Ford L8000 trucks, and 2 Volvo White Roll-Offs) models 1981 to 1988 with a total cost of $357,700 dollars..."[52]

72. Mr. Piazzesi testifies that Mr. Jacob instructed him to contact the SECOFI officials to find out what the problem was. He spoke with Mr. Fernández who explained that the trucks that Global/DESONA wished to import were very old and that Mexican federal law restricted the importation of used trucks[53].

73. Mr. Piazzesi then confronted Messrs. Goldenstein and Azinian and informed them of the problem. The Tribunal will recall that Global/DESONA had committed to acquiring state-of-the-art trucks and, purportedly for this reason, had declined to purchase Mexican-made trucks.

74. Mr. Piazzesi testifies that the Global/DESONA principals claimed that the used trucks were "state-of-the-art" for the purposes of the concession, and that they required those trucks and only those trucks. He testifies further that they "could never explain to me why those were the only trucks they needed or why thirteen year old trucks were more 'state-of-the-art' than new Mexican trucks" [54].

The Attempt to Transfer Shares Informally

75. Around this time, Global/DESONA forwarded some share certificates that they said represented the municipality's 10% interest in the company. Under the terms of the concession contract, this should have been done by December 15, 1993. By letter dated February 14, 1994 Mr. Piazzesi forwarded the share certificates to the municipality's General Counsel, Sergio Maldonado[55]. He also enclosed a copy of Global/DESONA letter dated February 9, 1994 presenting the shares to the municipality. Mr. Piazzesi informed Mr. Maldonado that the shares were provided extemporaneously and he believed that the value of the shares did not correspond to the current capital stock of the company. He added that his office had no authority to keep the shares[56].

Global/DESONA's Failure to take Responsibility for the Landfill

76. Shortly after the Municipal officials discovered that Global/DESONA was proposing to employ used trucks, that Mr. Piazzesi and other officials considered could not reasonably be described as "state-of-the-art"[57], they were surprised to find that the municipality was also about to be assigned full responsibility for the Rincón Verde landfill. By letter dated February 15,

52. Letter from Mr. Manuel Fernández Pérez to Enrique Jacob-Rocha, dated February 10, 1994. See Exhibit 5.
53. Witness statement of Mr. Francesco Piazzesi.
54. Ibid.
55. Letter from Mr. Francesco Piazzesi to Sergio Maldonado, February 14, 1994. See Exhibit 6.
56. Ibid.
57. The Municipality later adduced the evidence of an expert in the domestic legal proceedings to the effect that the trucks that DESONA wished to import were not state-of-the-art. See Exhibit 27, expert report of Mr. Ángel Torralva. DESONA did not adduce any evidence to contradict this.

1994, Pablo Pérez Gavilán, Director General of the State Secretariat of Ecology, informed Mr. Jacob that effective February 28, 1994, the State Secretariat of Ecology would be transferring the operation of the landfill to the municipal government[58].

77. Mr. Piazzesi testifies that, like the used trucks issue, this announcement came as somewhat of a surprise to municipal officials. They thought the landfill was already being administered by Global/DESONA because the concession contract required it to assume all responsibility for the landfill on December 1, 1993[59].

78. In fact, the State Secretariat of Ecology had been operating the Rincón Verde landfill (and twelve other landfills within the State of Mexico), pursuant to the Metropolitan Solid Waste Program, that was jointly carried out with the Department of the Federal District (the government agency then in charge of administrating the Federal District). Operations involved final disposition of solid waste, and included operation of heavy duty machinery and dump trucks (which the Secretariat leased at its own cost); extraction of *tepetate* (a special kind of soil) which it used to cover up waste; construction of drains and bio-gas wells; and dealing with the pepenádores (the workers who separate waste and recycle it) who work at landfills. The personnel involved in the operation of the landfill were hired and paid by the State Secretariat. Ecological control over the landfill was also exercised by the State Secretariat[60].

79. Mr. Piazzesi contacted Mr. Goldenstein and found that Global/DESONA had been charging a fee to independent waste collection trucks for dumping at Rincón Verde, that the company was not declaring this income, and that it had not informed the municipality of these fees. The municipality was concerned about this because, although the concession contract gave Global/DESONA the right to collect fees, this had to be done in accordance with the relevant municipal regulations. In addition, Global/DESONA had not provided the necessary personnel or equipment to the landfill. There was one representative from BAS at the landfill but he was not there on a full time basis and Global/DESONA was controlling access to it, otherwise, the landfill was being operated by State employees[61].

80. Mr. Piazzesi's evidence is corroborated by that of Mr. Hodge. His testimony is that when he visited Naucalpan, there was only one BAS technician at Rincón Verde and he did not appear to have the necessary support from Global/DESONA to undertake BAS's plans[62].

81. In summary, since December 1, 1993, Rincón Verde had been a source of income for Global/DESONA but it had not assumed any meaningful responsibility in regard to the landfill's operation[63].

82. Mr. Piazzesi testifies that he received a large volume of manuals, documents, forms and other materials from Ms. Tejeda of the State Secretariat of Ecology. He called Mr. Goldenstein

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58. Letter from Dr. Pablo Pérez Gavilán to Mr. Enrique Jacob-Rocha, February 15, 1994. See Exhibit 7.
59. Witness statement of Mr. Francesco Piazzesi.
60. Witness statement of Ms. Patricia Tejeda.
61. Witness statement of Mr. Francesco Piazzesi.
62. Witness statement of Mr. Jim Hodge.
63. Witness statement of Mr. Francesco Piazzesi and Ms. Patricia Tejeda.

who assured him that Global/DESONA would take care of everything and that it would pick up the large volume of materials. He testifies that Global/DESONA did not do so[64].

83. In a letter dated February 15, 1994, Mr. Azinian sent Municipal President Jacob a financial pledge to guarantee the company's performance under the concession (as set out in clause eighteen of the concession contract this pledge was to be provided 90 days after the November 15, 1993 signing of the concession contract)[65].

The Ayuntamiento Considers Dr. Davalos' Legal Advice

84. On February 23, 1994, Dr. Dávalos advised the municipality that it had valid grounds for nullifying the concession. The basis for his advice is described at length in his witness statement.

85. The *Ayuntamiento* identified what it considered to be 27 irregularities with respect to the awarding of the concession to DESONA's consortium and the performance of the concession by Global/DESONA[66].

86. On March 7, 1994, the *Ayuntamiento* of Naucalpan met in *Cabildo* session to consider the waste situation. The minutes of the meeting record:

> "...Mr. Enrique Jacob Rocha, Constitutional Municipal President, addresses the meeting... we have received a number of complaints about the poor waste services, and thus we face a serious situation that should be resolved as soon as possible to prevent more serious consequences. He stated also that based on this, they decided to study the way in which the company has provided the concession services, including the company's operation, administration and legal organization. [The Municipal President] provided the Municipal officials with an executive summary of the current situation. In addition to mentioning that the service was completely inadequate, the Municipal President explained that they have found a number of irregularities in the concession. The main ones deal with the legal capacity and standing of the concessionaire. This was probably the result of the difficulties faced to implement the complex concession procedure. Unfortunately they have found violations of public law provisions, in particular of the Municipal Organic Act and of federal provisions."[67]

87. The Municipal President therefore requested the *Ayuntamiento* to consider two proposals:

> "...first, to initiate an appropriate administrative procedure. The *Primer Sindico* of the *Ayuntamiento* should notify the concessionaire, Desechos Sólidos de Naucalpan, S.A. de C.V. in strict compliance with the law, in order to inform it of the irregularities found by the municipality with regard to the company's capacity and standing, as provided by the Mexican Constitution, the State Constitution, the Municipal Organic Act, and other applicable provisions. He should also be informed of the violations of public law provisions found, in particular of violations of Articles 37, 132, 137 or 167 of the

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64. Ibid.
65. Letter from Mr. Azinian to Municipal President Jacob Rocha dated February 15, 1994. See Exhibit 8.
66. *Cabildo* meeting minutes dated March 21, 1994. See Exhibit 9.
67. Minutes of the *Cabildo* session March 7, 1994. See Exhibit 10.

Municipal Organic Act. The Municipal findings should be disclosed to the company in a hearing, in which a date should be established for the company to respond and submit evidence in defense. And second, to grant Mr. Ignacio Espinoza Castillo, *Primer Síndico*, as the legal representative of the *Ayuntamiento*, all necessary powers to conduct, in view of the seriousness of the problem, the following acts: a) to determine precisely which provisions of law have been violated; b) to notify DESONA in strict compliance with the law… c) to prepare an administrative report of the hearing, in which the irregularities found by the *Ayuntamiento* are disclosed to the concessionaire, and the concessionaire is informed that if it fails to file a response and evidence on the deadline established, it will lose its right to do so. And if the company does not appear at the information hearing, the *Síndico* notifies it and serves a copy of the resolution establishing the deadline to respond and informing it will lose its right to respond if it does not comply with this filing date. The *Síndico* will then inform the *Ayuntamiento*, who will issue a resolution on this matter, according to its own powers."[68]

88. The Municipal President's proposals were approved by unanimous vote[69], on March 7, 1994.

Another Third Party Examines Global/DESONA's Situation

89. On the same day as the Municipal President proposed that the *Ayuntamiento* commence the nullification process, March 7, 1994, Mr. Sam Maphis of Maphis International Ltd., of Boulder, Colorado, prepared a note to a potential investor in Global/DESONA, Mr. William Birman Feldman. In the note, Mr. Maphis recounted that:

> "On March 4-5 [of 1994], Maphis met with Mike Carolan, who represents the 3 principal owners of DESONA."[70]

90. Mr. Maphis then stated there may be a business opportunity for them to take over the concession if they so desired. He identified the owners of Global/DESONA as:

- Robert Azinian, President;
- Ariel Goldenstein (Mr. Maphis described Messrs. Azinian and Goldenstein as "Argentineans who now live in Mexico and are former restaurant owners in L.A., who have no waste experience");
- Kenneth Davitian, "who has a hauling company in L.A., San Jose and Malibu"; and
- Bryan A. Stirrat, "who is an engineering company principal from L.A."

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68. Ibid.
69. Ibid.
70. Letter from Mr. Sam Maphis to Mr. William Birman dated March 7, 1994, attached as Exhibit 5 to the witness statement of Mr. J. Cameron Mowatt.

91. It should be noted that Global/DESONA's and BAS's retention of Mr. Carolan followed the company's discussions in early January of 1994 with RDC where the Global/DESONA principals and Mr. Stirrat tried unsuccessfully to convince RDC to invest in the company.

92. Mr. Maphis' conclusion in the memorandum to Mr. Birman was that DESONA was not capable of performing the concession at that time. Specifically, he noted that:

> "DESONA is obviously over their head in technical and operational expertise and are heavily under-capitalized —my feeling in discussions with Mike Carolan is that they want out."[71]

Formal Notice of the Defects is Given to DESONA

93. Mr. Piazzesi, the responsible official, repeatedly informed the Claimants that Global/DESONA's performance of the concession was inadequate. In addition, on March 8, 1994, Global/DESONA was formally notified by Mr. Ignacio Espinoza, *Primer Síndico* of the municipality, of the initiation of an administrative law procedure to review the concession[72]. The notice established March 10, 1994 as the date for a meeting in the *Primer Sindico's* office to personally inform Global/DESONA of the irregularities and violations found by the *Ayuntamiento*. The notice was hand delivered to Mr. Davitian, who identified himself as a shareholder and Mr. Edgar Lozada. The latter read it, and informed Davitian of its content. Also present was Mr. Carolan, the broker who had been retained to assist Global/DESONA in selling the company.

94. In the March 10, 1994 hearing, Global/DESONA was informed of the nullification process and provided with a document setting out the 27 irregularities as well as a copy of the *Ayuntamiento*'s decision dated March 7, 1994.

95. Global/DESONA provided its response to the *Ayuntamiento* on March 16, 1994. However, the company fail to address the irregularities found and instead had initiated a claim before the State Administrative Tribunal requesting the nullification of all acts of the *Ayuntamiento* arising out of, and including, the March 7, 1994 resolution.

96. In its response, Global/DESONA also alleged that, *inter alia*:

- the *Ayuntamiento* and the company had entered into a concession contract on November 15, 1993 setting out the rights and obligations for both parties;
- the parties had agreed in clause 34 of the contract that in celebrating the contract, there had been no error or any other cause of nullity;
- clause 32 established that the parties waived the jurisdiction of the courts of their legal domiciles, and agreed to subject themselves to the jurisdiction of the courts of the State of Mexico;

71. Ibid.
72. Notice dated March 8, 1994 to Desechos Sólidos de Naucalpan, S.A. de C.V. See Exhibit 11.

- they agree to consult in order to solve their differences before taking the matter to the courts;

- the *Ayuntamiento* had not quoted the provisions that had been violated by the concessionaire, the provisions establishing the initiation of the administrative procedure, or the provisions under which the concessionaire had been notified; and

- the *Ayuntamiento* could not claim that it entered the contract on the basis of an error of fact or law because of the principle that 'no one can claim in his favor his own mistakes[73].

The Concession Is Nullified

97. On March 21, 1994, after reviewing Global/DESONA's response of March 16, 1994, the *Ayuntamiento* unanimously resolved to nullify the concession[74].

98. By letter dated March 22, 1994, the *Primer Síndico*, Mr. Ignacio Espinoza, requested that the Municipal General Director of Public Services participate in a procedure to enforce the March 21, 1994 decision regarding the municipality's repossession of the Rincón Verde landfill, so that he could identify the municipal government's property[75]. Mr. Ignacio Espinoza sent similar letters to the Municipal Treasurer and to the Director General for Public Security and Firemen Corps Police Director General. He asked the Treasurer to appoint an official to take over the collection of fees at the Rincón Verde landfill beginning the next day, and requested that the Municipal Police Director implement a general protection operation for the repossession action[76].

99. On March 23, 1994, the *Ayuntamiento* notified Global/DESONA that the concession had been nullified[77]. Mr. Goldenstein received and signed the notice at 9:00 A.M. At 11:00 A.M. the municipality took possession of the Rincón Verde landfill. The report noted that Global/DESONA retrieved all of its equipment, including the money in the cash register in the amount of 1,835 new pesos[78].

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73. Desona's March 16, 1994 response to the *Ayuntamiento*. See Exhibit 12.
74. Minutes of the *Cabildo* session, March 21, 1994. See Exhibit 9.
75. Letter from Municipal *Primer Síndico Procurador*, Ignacio Espinoza, to Municipal Director General of Public Services, Esteban Espinoza, March 22, 1994. See Exhibit 13.
76. Letter from Municipal *Primer Síndico Procurador*, Ignacio Espinoza, to Municipal Treasurer, Dr. Jorge Laris, March 22, 1994; and letter from Municipal *Primer Síndico Procurador*, Ignacio Espinoza, to the Director General of Public Security and Firemen Corps, Enrique Ramírez, March 22, 1994. See Exhibit 14.
77. Notice of nullification of concession to DESONA, March 23, 1994. See Exhibit 15.
78. Report concerning the repossession of the Rincón Verde landfill, March 23, 1994. See Exhibit 16.

The State Administrative Tribunal Proceedings

100. As noted above, on March 15, 1994, Global/DESONA responded to the nullification process by filing a claim with the State Administrative Tribunal challenging the *Cabildo's* decisions dated March 7 and March 10, 1994. Specifically, Global/DESONA challenged:

> "... a) From the Honorable *Cabildo* of the Constitutional *Ayuntamiento* of Naucalpan de Juárez, the resolution dated March 7, 1994, regarding the concession for the collection, transport, recycling, use and final disposal of the solid waste public service, as well as all the factual or legal consequences deriving from this act, such as, the administrative resolution terminating the contract...
>
> b) From the *Primer Síndico,* his acts pursuant to the March 7 resolution: 1) the findings of alleged violations by my client; 2) the notification of these violations to my client; 3) initiation of an 'administrative procedure' to notify these violations to my client; 4) establishing a "four day" deadline within this unlawful administrative procedure, in order for my client to respond to the allegations made and submit evidence; 5) illegally notifying my client that in case it did not respond before the unlawful deadline, it would lose all its rights and the concession would revert to the municipality; 6) unlawfully requiring my client to provide accounting documents, as if the procedure was a judicial procedure; 7) any consequence that could arise from these acts; 8) the March 10 resolution by the *Primer Síndico* himself that 'the time given to the company is enough and sufficient to respond to the issues hereby notified ...."[79]

101. On March 25, 1994, the State Administrative Tribunal accepted jurisdiction over Global/DESONA 's challenge.

102. On April 11, 1994, Global/DESONA submitted an amended complaint to include the *Ayuntamiento's* March 21, 1994 decision nullifying the concession. The complaint reaffirmed, the earlier allegations against the procedure followed to nullify the concession, and asked the Tribunal to declare the nullity of the acts challenged and to restore the waste concession to the company. It argued that:

a) The *Ayuntamiento* did not have powers to nullify the concession. Clause 32 of the concession contract established that the parties would submit any dispute *Ayuntamiento* that required a judicial decision to the courts of the State of Mexico. The *Ayuntamiento* initiated an illegal procedure where it acted as judge and party, instead of following a judicial procedure before the appropriate tribunals.

b) The *Ayuntamiento* violated the necessary formalities of law. The *Ayuntamiento* did not comply with the formalities of the concession contract, such as the parties' agreement in clause 34 not to invoke the nullity of the concession contract due to error.

79. Complaint by DESONA filed with the State Administrative Tribunal for the State of Mexico on March 15, 1994. See Exhibit 17.

c) The *Ayuntamiento* violated Articles 14, 16 and 17 of the Constitution by initiating a procedure against the company where the government authority acted simultaneously as party and judge. The municipality took justice on its own hands in violation of the Mexican Constitution.

d) The *Ayuntamiento* had to follow the provisions of the Civil Code regarding contractual error instead of deciding to nullify the concession. In addition, the Civil Code establishes that the validity and fulfillment of contracts cannot rest in the decision of one of the contracting parties, i.e., the *Ayuntamiento* of Naucalpan.

e) The *Ayuntamiento* violated the principle of fairness and equality between parties that shall prevail in a dispute[80].

103. Regarding the 27 irregularities upon which the *Ayuntamiento* based its decision to nullify the concession contract, Global/DESONA repeatedly argued that the *Ayuntamiento* was aware of the facts, and thus there had been no error; that even if there had been an error, the *Ayuntamiento* could not use its own errors to its advantage; that it had waived its right to allege an error; that there was legally no error in law; and that, in any event, the time within which an error could be legally challenged had elapsed. Global/DESONA also presented arguments as to why each of the 27 irregularities were not a valid basis for nullification:

a) With regard to the fact that the consortium did not form part of the company, as per the representations made to the *Cabildo* on November 4, 1992, counsel for DESONA stated that the company simply agreed to associate with such companies, which was different from having them as shareholders.

b) Regarding the allegation that instructions had been given to the notary prior to the November 4, 1992 *Cabildo* session to incorporate the company in a manner different to what was later that day represented, counsel for DESONA argued that the *Ayuntamiento* had failed to produce evidence of that.

c) With respect to the failure to replace the existing municipal vehicles with new and modern equipment, and the attempt to import used vehicles, counsel for DESONA stated that this was mere speculation and that in any event a breach of contract could not be considered an error.

d) Regarding the failure to create 200 new jobs, counsel for DESONA argued that when the *Ayuntamiento* ceased to provide the public service upon its contracting DESONA for such purpose, 200 municipal employees were left unemployed and were rehired by the latter, thus generating the 200 jobs.

e) Concerning the failure to make the promised construction, counsel for DESONA argued that it required several years and only three months had elapsed since the concession contract had been signed. In any event, should DESONA fail to

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80. DESONA's Amended Complaint, dated April 11, 1994. See Exhibit 18.

comply, that would be the basis for the rescission of the contract, not its nullification.

f) Counsel for DESONA claimed that the allegations of the *Ayuntamiento* regarding obligations concerning the *Ejido de San Mateo Nopala* were false, since the company had only surrogated in the *Ayuntamiento*'s rights and had not undertaken any obligations in that respect in the concession contract.

g) With respect to the notorious inability to provide the service efficiently, with stability and on a regular basis, counsel for DESONA stated that it could not be presumed that the company would not be able to comply with its obligations under the concession contract, that the *Ayuntamiento*'s allegation constituted a mere guess which, in any event, existed at the time the State legislature authorized the contract.

h) Concerning violations of the *Ley General de Población*, the allegations were illogical and untimely given that more than a year had passed since the *Ayuntamiento* first saw the deed of incorporation.

i) Counsel for DESONA claimed it was false that the concession contract was based on a law that was no longer in effect at the time it was signed, since the contract was entered into on November 4, 1992, although it was formalized on November 15, 1993 because it required prior authorization by the State Legislature.

j) Respecting the obligation to effect payments to DESONA for the waste collection service and to transfer municipal assets, regardless of the original assurances that the municipality would not be required to make any investments, counsel for DESONA argued that it had been a bilateral agreement between two legally competent persons in addition to the *Ayuntamiento*'s affecting assets that would otherwise remain idle.

k) As regards the inability to generate electricity from bio-gas, counsel for DESONA argued that should that come to happen, it would constitute a breach of contract, not an error.

l) Counsel for DESONA stated that laws in force did not prohibit the acquisition of the electrical power by the State enterprise that held the monopoly in this area.

m) Concerning the subrogation of rights between the *Ayuntamiento* and the *ejidatarios* without the latter's consent, counsel for DESONA argued that the Rincón Verde landfill had never been subleased by DESONA and, in any event, such subrogation was not prohibited by law.

n) With respect to subrogation of rights concerning the operation and remediation of Rincón Verde emanating from the agreement between the *Ayuntamiento* and the State Secretariat of Ecology, counsel for DESONA stated that his client had not been a party to that agreement and that such subrogation was not prohibited by law.

o) As regards the lack of authorization to impose access fees for Rincón Verde, counsel for the claimant argued that such right had been granted exclusively to DESONA, according to the terms of the contract.

p) Finally, in respect of the failure to register in the Suppliers Registry of the State, counsel for DESONA argued that it was not a legal requirement and, if it was, it could be remedied[81].

104. On April 11, 1994, the State Administrative Tribunal accepted Global/DESONA 's complaint for filing[82].

105. On April 27, 1994, the Municipality filed its response to Global/DESONA 's amended complaint. Its forty-page response addressed every allegation. The Municipality began by clarifying some of the issues raised in the complaint:

> "1. The Municipality's act challenged by the complainant was based on the fact that the Municipality relied on an error, either an error in fact or an error in law, and in an error induced by misrepresentations (Civil Code of the State of Mexico).
>
> 2. The Municipality did not act arbitrarily when it invoked the error as a basis for administrative nullification. It acted in strict compliance with the law that governs such acts, the Municipal Organic Act of the State of Mexico, provides in Article 167 that:
>
> > 'The agreements, concessions, permits or authorizations granted by municipal authorities or officials that lack powers to issue them, or that were issued based on error, misrepresentations or duress, and that affect or restrict the rights of the Municipality over its public property, or any other rights, would be nullified through an administrative procedure by the *Ayuntamiento*, following a hearing with the interested party.' [Emphasis in the original]
>
> 3. Notwithstanding that claimant's counsel repeatedly submits that there is "no error in law", Article 1642 of the Civil Code of the State of Mexico provides that:
>
> > 'An error in law or in fact invalidates the concession when it affects the fundamental intention of any of the contracting parties…' [Emphasis in the original]
>
> 7. Finally, for the benefit of the complainant and of the main issues raised in this legal proceeding, it is important to repeat that the challenged act of nullification of the concession was not directed against a private law concession contract, but against an administrative act of concession. These are two distinct acts. Further evidence of this is the fact that the complaint was filed with the State Administrative Tribunal, that pursuant to Article 3 of the Administrative Law for the State of Mexico has jurisdiction in administrative disputes between Municipalities and citizens, when the former acts as an authority. This Article is reproduced for the sake of clarity:

81. Ibid.
82. Decision of the State Administrative Tribunal, April 11, 1994. See Exhibit 19.

'Article 3: The State Administrative Tribunal is established to resolve administrative and fiscal disputes between the State Public Administration, the Municipalities and Semi-Autonomous Government Agencies, that exercise authority, and private citizens, as well as to address responsibility issues pertaining to government officials.' [Emphasis in the original]

In fact, through the concession contract, the Municipality granted the necessary powers so that the Claimant company could provide a public service that was within the *Ayuntamiento's* exclusive jurisdiction...

Finally, as is well known in the legal profession, administrative acts can be nullified if the legal criteria for that purpose are met. Only the same authority that issued the act can nullify it. This provision is established in Article 167 of the Municipal Organic Act and simply reflects a basic principle of Administrative Law..."[83]

106. On May 10, 1994, Global/DESONA filed a submission arguing that it had entered into a contract with the *Ayuntamiento,* and the dispute was therefore a matter of private law and the *Ayuntamiento* was not entitled to nullify the concession under Article 167 of the Municipal Organic Act. (The courts later rejected these arguments and concluded that the "contract" was in fact an administrative concession concerning a public service that was subject to Article 167 of the Municipal Organic Act.)

107. Meanwhile, on May 14, 1994, the Municipality entered into an agreement to purchase 25 new Mercedes Benz garbage trucks manufactured in Mexico. Mr. Piazzesi testifies that when the concession was nullified, consideration was given to putting the concession out to tender. However, it was concluded that this would be too time-consuming given the build-up of garbage and that the Municipality should instead arrange the necessary financing to purchase new trucks and resume the garbage collection service itself[84].

The Cabildo Session of June 1, 1994

108. During May of 1994, while the Tribunal proceedings were underway, Global/DESONA requested an unofficial meeting with the Municipal President to discuss the concession. Mr. Jacob declined to discuss the matter unofficially, but, at the request of Mr. Azinian, agreed to allow the Global/DESONA principals to make a presentation before the full *Cabildo*[85] (Exhibit 21 contains a videotape and extracts of the transcript of the session).

109. Shortly before the June 1, 1994 *Cabildo* session, the Sánchez brothers and Dr. Oscar Palacios were asked if they would like to attend the session. They agreed.

110. In that hearing, Mr. Goldenstein and Mr. Stirrat made presentations on behalf of Global/DESONA. Thereafter, they were questioned by the members of the *Ayuntamiento*.

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83. Response by the *Ayuntamiento* to Global/DESONA 's complaint, April 27, 1994. See Exhibit 20.
84. Witness statement of Mr. Francesco Piazzesi.
85. Ibid.

111. At the end of the meeting, Ms. Gloria Myers, the landlord of the premises where Global/DESONA had their offices, complained that Global/DESONA had never paid the lease[86].

112. The Tribunal will recall that in their pleadings and their response to the Respondent's request for particulars, Global/DESONA claimed to have paid for the municipal delegation's visit to Los Angeles in January of 1992[87]. Mr. Eduardo Sánchez told the *Ayuntamiento* that he and his brother had introduced Global to the Municipality and that the Global principals had defrauded his brother Emilio[88].

113. The evidence of Mr. Emilio Sánchez is that, together with his brother Eduardo, he was introduced to the Global principals and in turn introduced them to the municipality. Mr. Sánchez testifies that it was he, not the Global/DESONA principals, who paid for the airfare and hotel accommodations of the municipal officials. He did so at the Global/DESONA principals' request and upon their promise to reimburse him. They never did so[89].

114. Mr. Sánchez has attached the relevant credit card statements to his witness statement[90].

115. Counsel for Dr. Oscar Palacios told the *Ayuntamiento* that Dr. Palacios had given money to Mr. Goldenstein to develop DESONA I, in which both he and Mr. Goldenstein were shareholders. Mr. Goldenstein had told Dr. Palacios that DESONA I would hold the concession[91]. While Mr. Goldenstein had requested that the concession be transferred from Global/DESONA to DESONA I and this was authorized by the former administration on May 3, 1993, on November 16, 1993 the concession was transferred back to Global/DESONA, upon Mr. Goldenstein's request. Dr. Palacios told the *Ayuntamiento* that he would be filing a criminal complaint against Mr. Goldenstein because he had defrauded him of his money. The criminal complaint was filed after the meeting[92].

116. Upon reviewing the videotape, the Tribunal will see that when Mr. Goldenstein realized that the Sánchez brothers and Dr. Palacios were present, he abruptly left the meeting. Given his dealings with them, the reasons for his hasty departure are obvious; however, with respect to Dr. Palacios, they will be explained more fully below in the Additional Facts section.

The Tribunal Proceedings Continue

117. On June 6, 1994, counsel for the Municipality sought to adduce evidence in the State Administrative Tribunal proceeding of what transpired at the June 1, 1994 *Cabildo* session, noting that the members of citizen's groups:

86. See Exhibit 21. June 1, 1994 *Cabildo* meeting minutes.
87. See Claimants' response to the Respondent's request for particulars, p. 2-3. See also Section 2 of Desona's Memorial.
88. See witness statement of Mr. Emilio Sánchez.
89 Ibid.
90. See Exhibit 4 to Mr. Emilio Sánchez's witness statement.
91. See Exhibit 21. June 1, 1994 *Cabildo* meeting minutes.
92. Witness statement of Dr. Oscar Palacios.

"raised some questions before DESONA's legal representative, that the Municipality ignored, such as: that DESONA had not paid the lease of its offices, that in fact, the company was no longer at the address of Gustavo Baz 85; that the company had committed fraud against several persons based on the promise to make them shareholders, etc. When he heard those questions, Mr. Goldenstein abruptly left the meeting without giving any explanation, notwithstanding that he was told that the meeting had been held only because DESONA itself had requested it. This attitude is further evidence that the company has always conducted itself in bad faith and disdain for the Mexican authorities. It also shows that the company does not in fact exist, and that is why it has refused to consent to an on-site inspection of DESONA's offices requested by the defendants."[93]

118. Counsel for the Municipality offered the minutes of a *Cabildo* session as evidence in the proceeding. He further requested that the Tribunal verify whether there was an operating business at the company's address and if not, to ask when it left[94].

119. On June 14, 1994, the Municipality filed another submission regarding the evidence that it had offered on June 6, 1994 that was not known prior to the June 1, 1994 *Cabildo* session[95]. The evidence included a number of letters written by citizens' groups to the Municipal President in support of the concession's nullification and a criminal complaint by Dr. Palacios, the DESONA I shareholder, where he alleged that he had been defrauded by Mr. Goldenstein[96].

120. Counsel for the Municipality also presented a letter dated March 28, 1994 from Dr. Palacios to Mr. Goldenstein calling for a shareholder's meeting of DESONA I, and minutes of the meeting of DESONA I dated March 30, 1994. This shareholder's meeting was called to ask

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93. Submission by the Municipality to the Third Regional Chamber of the State Administrative Tribunal, June 6, 1994. See Exhibit 22.

94. The Tribunal ordered an official of the Tribunal to conduct the verification requested. The verification was conducted on May 13, 1994. On that same date, DESONA's counsel challenged the verification order as being irrelevant in the controversy. The Court rejected the challenge stating that the verification had already been conducted.

95. Submission by the Municipality to theThird Regional Chamber of the State Administrative Tribunal, June 14, 1994. See Exhibit 23.

96. The criminal complaint was submitted on June 2, 1994. In the complaint, Dr. Palacios stated that, *inter alia:*

a) He had met Mr. Goldenstein in January 1993. Mr. Goldenstein invited him to engage in a business that would produce incredible profits if they were able to obtain the waste services concession from the Municipality of Naucalpan. The waste of all the Municipality would be transformed into energy with an American scientific process and sold;

b) On March 3, 1993, they incorporated Desechos Sólidos I de Naucalpan [DESONA I]. The shareholders were Mr. Goldenstein with 3,500 shares and Mr. Palacios with 1,500 shares, for a total of 5,000 shares;

c) Mr. Palacios deposited 185,000 new pesos to a bank account. Mr. Palacios and Mr. Goldenstein had agreed to use the money for the development of the company, in particular, to construct waste bins and develop the waste collection system;

d) Mr. Palacios requested Mr. Goldenstein to return his money. The last time was at the June 1, 1994 *Cabildo* session where he claimed his money back in the presence of Mr. Palacios' accountant. Mr. Goldenstein refused to answer and asked Mr. Palacios to proceed as he wished because he was a foreigner and there was nothing that could be done against him.

See Exhibit 24.

that Mr. Goldenstein give an account of the company's operations. As set out in the Minutes of the March 30, 1994 meeting, Mr. Goldenstein informed Dr. Palacios that the company had not operated since its incorporation, that he had been unable to prepare a report, and that he would call a meeting to provide the report required by law. In addition, he was unable to set a date for the next meeting.

121. On June 14, 1994, the Municipality submitted allegations to the State Administrative Tribunal. It asserted that the acts challenged were not illegal, because they complied with federal constitutional requirements; specifically, they were properly reasoned, respected legal rights and due process, and were issued pursuant to the applicable legal provisions. Further, the acts challenged were undertaken to prevent violations of the peoples' right to health, as provided by Article 4 of the Mexican Constitution[97].

122. The Municipality further argued that it had acted on legal grounds, *inter alia*:

a) In February of 1994, a number of citizen's groups and residents came to the Municipal offices to complain about the waste services provided by Global/DESONA.

b) On January 11, 1994, the Municipality received a letter from Mexican Customs advising that Global/DESONA was now able to import two trucks that were waiting at the Customs storehouse in Mexico City. The Municipality realized that two months after signing the concession contract, Global/DESONA had only imported two trucks, and that the company could only then begin providing the Municipal waste collection service.

c) On February 10, 1994, the Municipality received a letter from the SECOFI General Office for Industrial Development informing it that Global/DESONA had requested that the federal authority issue an import permit for the importation of 17 trucks worth 357,700 dollars in total. The request was made on the basis that the company was providing waste services in partnership with the Municipality. The Municipality realized that the company intended to import used trucks and had wrongly informed SECOFI that it had entered into a partnership arrangement with the Municipality.

d) On February 15, 1994, the Municipality received a letter from the State Ecology Secretariat informing it that on February 28, 1994 the State would stop paying for the machinery used at the Rincón Verde landfill. The Municipality realized that the concessionaire had not paid for the equipment and that beginning in March of 1994, the Municipality would have to pay for it itself[98].

e) Based on these facts and a number of complaints received against the waste services provided by Global/DESONA , the Municipality conducted an

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97. Submission of arguments by the Municipality to the Third Regional Chamber of the State Administrative Tribunal, June 14, 1994. See Exhibit 25.

98. See witness statement of Patricia Tejeda.

investigation on the operation, administration and legal status of the company. The issue was discussed in several *Cabildo* sessions and on March 7, 1994, the *Ayuntamiento* ordered the *Primer Síndico* to initiate an administrative procedure to inform the company of the irregularities found and to act accordingly. The next day, thirty-two residents' organizations expressed their support for the *Ayuntamiento 's* decision of March 7, 1994.

f) The investigation revealed a number of irregularities, not only in the way the service was provided, but also regarding the legal status, and the financial, technical and organizational capacity of the concessionaire. These contrasted with the company's representation at the November 4, 1992 *Cabildo* session which it made in order to secure the concession. The Municipality concluded that the former administration had awarded the concession on the basis of Global/DESONA 's misrepresentations, including as to its financial and organizational capacity. The Municipality found that, *inter alia*:

i) Contrary to its representations, the company did not have experience in the waste business or any other business. For example, Global/DESONA's Manager, Mr. Goldenstein, was 26 years old on November 4, 1992. He was unable to import two trucks until the Municipality helped him, not only with the importation procedure, but with the payment of the import duties;

ii) Contrary to its representations, the company was not financially or technically capable of undertaking the business. The company invested only around 15,000 dollars and was unable to pay the duties for the imported trucks;

iii) Contrary to its representations, the company's stock was not owned by, nor was the Board of Directors comprised of, a group of experienced foreign companies;

iv) Contrary to its representations, the company used only two ten year old rebuilt trucks, when it had promised modern trucks. In addition, the company was poorly organized, had no corporate objectives or structure;

v) Contrary to the company's representations, the Municipality did not save money or reduce its waste service expenses to zero, but instead had increased its expenses and fiscal budget for that area. In addition, it lost the revenues generated by the Rincón Verde landfill;

vi) The Municipality had serious doubts not only about the legal status of the company, but also of its viability. First, the *Ayuntamiento* had in its possession two deeds of incorporation for the same company, with the same date and registration number, but with different shareholders. Second, the landlord of the place where the company had its offices complained to the Municipality that the concessionaire had not paid a

single month of rent. The landlord claimed that on March 23, 1994 the company simply disappeared: it had no offices or workers anywhere in Naucalpan;

vii) The company had charged unauthorized fees for landfill services, without providing invoices and without paying the owners of the *Ejido San Mateo Nopalá* the proper fees. This constituted tax evasion;

viii) Global/DESONA had transferred the concession to another company named DESONA I. Thus, on November 15, 1993 the company had no legal standing to sign the concession contract;

ix) In conclusion, the Municipality awarded the concession on the strength of the company's misrepresentations. The company did not have the capacity to comply with its obligations. The company obtained the concession with total disregard for the peoples' health;

x) Global/DESONA never provided evidence to explain the irregularities. The Municipality would have expected the company to provide documents such as the list of employees, an explanation by the notary on the existence of two almost exact deeds of incorporation, invoices of acquisition of equipment to be imported, proof of the investment of the shareholders, the minutes of the shareholder meetings to show its association with experienced international companies, etc. In contrast, in a four page response dated March 16, 1994 to the *Ayuntamiento's* notification of the irregularities dated March 10, 1994, the concessionaire protested the notification of the irregularities and in strong language informed the municipal authority that it had filed a complaint before the State Administrative Tribunal requesting the nullification of all municipal acts arising out of the decision of March 7, 1994;

xi) Thus, Global/DESONA's attitude was further evidence leading the Municipality to conclude that it had to nullify the concession in order to prevent a serious threat to the peoples' health. Indeed, the Municipality has a legal duty, emanating from the Mexican Constitution, to protect the health of its citizens. Given the complete absence of a regular waste collection service, the Municipality would have acted unconstitutionally and irresponsibly had it not reverted the public service, knowing of the serious irregularities, all relating to an obvious lack financial, technical and corporate capacity; and

xii) Global/DESONA, in its documents submitted to the *Ayuntamiento* and the Tribunal, noted that the Municipality decided to initiate the administrative procedure due to the irregularities that the company was advised of.

These irregularities have never been contested nor contradicted by the company, and most of the time have not been addressed[99].

123. Dr. Dávalos therefore requested that the Tribunal dismiss the complaint and confirm the legality of the acts challenged by Global/DESONA .

Evidence of the Municipality's Continued Expenditures

124. On June 14, 1994, Alberto Villarruel Briones, the defendant's accounting expert, submitted his report to the Tribunal. The accountant's conclusions were as follows:

> "1) Based on this report, we conclude that the *Ayuntamiento* of Naucalpan de Juárez did not stop incurring any expense related to the cleaning and waste services during the November 1993-March 1994 period. The *Ayuntamiento* continued paying, *inter alia*, the salaries and employment benefits of the personnel, the maintenance costs of the vehicles, gasoline expenses, and the lease of the Rincón Verde landfill.
>
> 2) Further, in February and March of 1994 expenses for vehicle rent increased in the amount of N$119,908 (one thousand nineteen, nine hundred and eight new pesos) and on May 14, 1994, they increased again because of payment made for 25 new Mercedes Benz vehicles. The transactions had not closed when this report was finished.
>
> 3) Thus, in summary, there was no reduction in the expenses of the Municipality for waste services during the period of the report in comparison with other months. We therefore conclude that no third party could have incurred expenses for that same service.
>
> 4) In our analysis, a company needed at least a working capital of N$9,000,000 (nine million new pesos 00/100 N.C.) to be able to cover expenses to operate five months in the *Ayuntamiento* of Naucalpan.
>
> 5) We were informed by the Municipality that the company Desechos Sólidos de Naucalpan, S.A. de C.V. had two used trucks to collect waste, leased a house, hired one assistant, one cashier for the Rincón Verde landfill and two truck drivers. Thus we concluded that the company's daily expenses could not be in excess of N$2,000 (two thousand new pesos 00/100 N.C.). By information provided by the Municipality we knew that the company obtained approximately N$8,000.00 (eight thousand new pesos 00/100 N.C.) for fees charged to public and private trucks using the landfill. On March 23, 1994, the day the Rincón Verde landfill returned to the Municipality, the amount of N$1,835.00 (one thousand eight hundred and thirty five 00/100 N.C.) was handed in by the cashier for fees that day. The landfill had operated only from 6:00 A.M. to 10:00 A.M. In normal conditions, the fees for the whole day would have amounted to N$8,000.00.
>
> Thus we conclude that the company DESONA obtained a daily revenue for the Rincón Verde landfill of N$6,000.00 (six thousand new pesos 00/100 N.C.) ..." [100]

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99. Submission of the Municipality, June 14, 1994. See Exhibit 25.
100. Report of Defendant's expert Alberto Villarruel Briones (June 14, 1994). See Exhibit 26.

125. Ángel Torralva Millares, another expert for the *Ayuntamiento*, concluded with regard to the concession's administration and the equipment used by Global/DESONA that:

a) "Given that the proper and essential way to initiate any comprehensive and integral waste collection and disposal program is by designing adequate and complete zones and routes and, as demonstrated by all the elements of this report, such a design did not exist, we may conclude that Desechos Sólidos de Naucalpan, S.A. de .C.V. completely lacked, and continues to lack any plans whatsoever, as well as state-of -the-art technology or any other technology. Moreover, the company was apparently trying to consolidate a project through continual *ad hoc* improvisations and financing obtained from revenue of "Rincón Verde" landfill or other sources;

b) in the undersigned's opinion, the concessionaire offered a great number of decisive elements and factors... but the proposed solutions were obviously inappropriate and revealed its lack of experience and technical capacity. The few things that Desechos Sólidos de Naucalpan, S.A. de C.V. managed to perform, could have been performed by any other company that began from "zero" in the waste services industry, both in its experiences and technical resources, as well as its corporate and financial capabilities;

c) As demonstrated by the aforementioned elements, Desechos Sólidos de Naucalpan, S.A. de C.V. clearly did not use, nor did it have the capacity to use, state-of-the-art technology, to provide the service that it was contracted to, to the extent that it provided it in a grotesque manner (old vehicles; minimal amount of workers; minimal financial and material resources; absence of planning and development of sectors; and minimal controls, except for charging fees at the Rincón Verde landfill, etc.);

d) ...the material and equipment resources; specifically the trucks used by Desechos Sólidos de Naucalpan, S.A. de C.V. can in no way to be considered state-of-the-art; since, as has been shown, they are obsolete, reconstructed and trucks that have been disposed of. Further, they were insufficient and inadequate to service the areas in which they were operating;

e) Desechos Sólidos de Naucalpan, S.A. de C.V.'s calculations are erroneous and far from reality, because in order to provide the service adequately, it should have contemplated at least 50% additional suitable vehicles, not only to provide the mechanical failures, maintenance and unexpected events, but also to provide a complete service from the users' standpoint;

f) Desechos Sólidos de Naucalpan, S.A. de C.V. did not comply, nor was it in any position to comply with any of the commitments made on November 4, 1992, during the time the system operated;

g) ...the investment required to provide the service that was contracted far exceeds that made by Desechos Sólidos de Naucalpan, S.A. de C.V. The lack of experience it showed in this area was obvious. The minimal investment directed towards the project is simply inadmissible and unthinkable".[101] [Emphasis added in the original]

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101. Expert Report of Ángel Torralva Millares offered by the defendant before the Third Regional Chamber of the State Administrative Tribunal, June 14, 1994, p. 15. See Exhibit 27.

126. On June 14, 1994 the State Administrative Tribunal held its hearing. The Tribunal rejected the late evidence sought to be offered by the Municipality (the letters of support from citizen's groups, the criminal complaint, and the minutes of the shareholder's meeting of DESONA I) as inadmissible. The Tribunal ruled the evidence was not relevant[102].

The Decision of the State Administrative Tribunal

127. On July 4, 1994 the State Administrative Tribunal rendered its judgment. It held that Global/DESONA had failed to prove its allegation that the Municipality had acted improperly and found that Global/DESONA had neither the technical nor the financial resources necessary to fulfill its commitments under the concession. The Tribunal's decision stated, *inter alia*:

> "... when issuing a decision, the authorities shall comply with the right to a prior hearing. The *Ayuntamiento* de Naucalpan de Juárez, State of Mexico, complied with this obligation, because, as declared by the claimant, it was called to offer evidence and argue in his defense. The claimant also argues that the appropriate procedure for the Municipality was to bring the claim before the courts. This argument is rejected because in such a case, at issue would be a private contract between private parties, which is not the case [here]. At issue [here] is a concession of a public service. In other words, this is a discretionary administrative act by which the Municipality empowers a private person to establish and exploit the service in accordance with the limits and conditions established by law. Thus, as an essential requirement, the Administration must act as an authority because the *Ayuntamiento* is obliged to provide the public services pursuant to Article 126 of the Municipal Organic Act for the State of Mexico...
>
> [T]he Municipality that issued the act subject to challenge stated the legal basis for the nullification of the concession and the reasons why the Municipality applied the provisions to this particular case. The Tribunal finds a proper relation between the reasons to nullify and the provisions of law quoted in the acts subject to challenge. The Tribunal rejects the claimant's argument that they lacked a legal basis because the claimant was unable to identify how the defendant failed to observe these principles...
>
> [P]ursuant to article 167 of the Municipal Organic Act of the State of Mexico... *Ayuntamientos* have the power to implement an administrative procedure to nullify a concession that harms the Municipality's rights, subject to previously hearing the interested parties...
>
> The concession must be awarded to individuals or corporations with the technical and economic capacity to provide the public service efficiently. Thus, the concessionaire is obliged to have the necessary technology and economic capacity. The concessionaire needs to have the resources to acquire the technology. This is an essential element to fulfill the purpose of awarding a public service concession. In the instant case, the conditions that the concessionaire must meet are established in the concession contract...
>
> BE IT RESOLVED
>
> FIRST.- The claimant failed to prove its case.

102. Tribunal decision on admissibility of the Municipality's additional evidence, June 14, 1994. See Exhibit 28.

SECOND.- The validity of the acts dated March seven and twenty one, nineteen ninety four, whereby the nullification proceeding of the concession granted to Desechos Sólidos de Naucalpan, S.A. de C.V. by the Honorable *Ayuntamiento* of Naucalpan de Juárez, State of Mexico is initiated, and the concession nullified, is hereby recognized.

THIRD.- The validity of the reversion of the concession for the public service consisting of cleaning, collection, transportation, recycling, profit and final disposal of solid waste and its execution, is hereby recognized..."[103]

The Appeal to the Superior Chamber of the State Administrative Tribunal

128. On July 13, 1994, Global/DESONA appealed the decision of the State Administrative Tribunal to the Superior Chamber of the State Administrative Tribunal[104].

129. On November 17, 1994, Global/DESONA's appeal was dismissed and the validity of the *Ayuntamiento's* resolutions of March 7 and 21 of 1994 were upheld. It was concluded that there was a basis for the nullification of the concession. The Superior Chamber modified the lower Tribunal's ruling to sustain the decision on 9 of the 27 irregularities invoked by the Municipality. The Superior Chamber narrowed the issue to Global/DESONA's misrepresentations regarding the capital, investment and structure of the company. It also rejected Global/DESONA's arguments that it was denied a hearing and that the nullification of the concession was unlawful because it violated the contractual provisions. The Superior Chamber stated:

> The first six claims submitted by the appellant company, that the decision dated July 4, 1994 violates Articles 14, 16, and 17 of the Mexican Constitution, 126 of the State's Municipal Organic Act and Articles 1622 and 1626 of the State Civil Code are reviewed together and dismissed for the following reasons:
>
> i) The resolutions dated March 7 and 21, 1994, subject to challenge in this administrative law litigation were issued in strict compliance with Article 14 of the Federal Constitution. The Municipality's *Primer Síndico*, following the directions of the *Ayuntamiento*, provided the representative of DESONA with the constitutional right to a hearing. In this hearing, the representative was able to declare what he considered to favor his client's interests and to provide the evidence he deemed necessary. This was part of the administrative procedure initiated to nullify the concession awarded for the collection, recycling, processing, and final disposal of solid wastes for residential, commercial and industrial areas. It is important to note that Mr. Ariel Goldenstein, General Manager of DESONA, voluntarily participated in the administrative nullity procedure, and by appearing at the hearing that was held on March 10, 1994, he consented to and cured any limitations that may have arisen with respect to the time limits, methods and procedures, although no such limitations arose. A correct interpretation of the second paragraph of Article 14 of the Federal Constitution leads to the understanding that it is not necessary to engage in a proceeding before a judicial tribunal in order to satisfy the right to a hearing. It is

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103. Decision of the State Administrative Court, July 4, 1994, pp. 4-6. See Exhibit 29.

104. DESONA's appeal to the Superior Chamber of the State Administrative Court, July 13, 1994. See Exhibit 30.

sufficient that the *Ayuntamiento* and the Municipal *Síndico* initiate an administrative proceeding and allow the claimant to submit arguments and offer evidence in its defense, as required by Article 167 of the State's Municipal Organic Act. This Article establishes that a concession awarded by the Municipality on the basis of a fundamental error, misrepresentation or duress, that affects or restricts the Municipality's rights, can be nullified in an administrative law procedure by the *Ayuntamiento,* after hearing the parties with an interest in the matter.

ii) The resolutions dated March 7 and 21, 1994 fully complied with Article 16 of the Constitution. The *Ayuntamiento* through its *Primer Síndico* conducted the nullification procedure of the administrative concession pursuant to the provisions cited in the first consideration of the resolution dated March 21, 1994. In particular, Article 167 of the State's Municipal Organic Act is relevant. The jurisdiction of the *Ayuntamiento* and the *Primer Síndico* to conduct the administrative nullity procedure and issue a resolution is unquestionable because it involves an administrative concession through which the Municipality of Naucalpan granted DESONA the right to provide the public waste collection service in the community, in accordance with Articles 126 and 128 of the Municipal Organic Act. The municipal authority's jurisdiction is not voided by Clause 32 of the concession contract dated November 15, 1993 which establishes that the parties will submit to the State Courts any claims regarding the interpretation, compliance with and enforcement of the obligations contained therein, because this is not an issue concerning the interpretation, observance or enforcement of the contract, but rather the nullification of the concession under administrative law due to an error upon having been awarded, which is governed by Article 167 of the State's Municipal Organic Act.

iii) The Superior Administrative Tribunal therefore admitted 9 of the 27 irregularities identified by the *Ayuntamiento*; namely, the irregularities set out in numerals 1, 3, 5, 6, 12, 13, 15 and 18. The irregularities set out in numbers 4, 7 through 11, 14, 16, 17, and 19 through 27 were excluded[105].

130. Those nine irregularities are as follows:

"There is misrepresentation inducing the Municipality to Consent to the Awarding of the Concession as a result of the following circumstances.

[Irregularity #1] "Those seeking the concession stated that during the November 4, 1992 *Cabildo* session ...the companies: Bryan A. Stirrat & Associates, Global Waste Industries, Inc. Sunlaw Energy Corporation and México Diesel Electro Motive, S.A. de C.V. (sic) would join together to unite their technical, industrial and financial experience, which they previously stated before the *Cabildo* session was the equivalent of 40 years in order to incorporate the company, Desechos Solidos de Naucalpan, S.A. de C.V.; however upon incorporating the company with deed of incorporation number 6,477, dated November 4, 1992.... it was revealed that this company was solely comprised of individuals and that none of them appeared as a representative of the companies

105. Appeal Decision of the Superior Administrative Tribunal of the State of Mexico, November 17, 1994. See Exhibit 31.

mentioned above. Therefore, there was misrepresentation regarding both the company's technical capacity and the incorporation of the company with individual persons and not companies."

[Irregularity #2] "Another factor influencing the *Ayuntamiento's* consent to award the concession was the understanding, as presented by the company's representatives, that 45% of the company's capital would be held by the American companies noted above, the other 45% would be held by a Mexican group that would be comprised of the noted Mexican company, among others and the remaining 10% would be held by the Municipality. However, Desechos Solidos de Naucalpan, S.A. de C.V's deed of incorporation, numbered 6,477, shows that none of these promises were complied with, given that the partners of the company were all individuals and 80% of the corporate capital was held by foreign individuals; moreover, the Municipality was not listed in the incorporation documents of this company. As a result of these misrepresentations, the *Cabildo* believed that the Concessionaire would be formed differently than that which actually materialized with respect to the shareholders and their respective participation."

[Irregularity #3] "In both the November 4, 1992 *Cabildo* session and the concession contract signed on November 15, 1993, those seeking the concession promised the Municipality a 10% interest in the concessionaire's company without having to invest any money. However, these documents did not stipulate whether this 10% interest would be given by the shareholders or whether it would be issued upon incorporation. This 10% interest was never received by the *Ayuntamiento*. Instead, on February 9, 1994, significantly later than the date upon which the shares should have been provided, the concessionaire submitted to the these offices five share certificates for 24,000 new pesos each. However, the procedure undertaken in issuing the shares did not comply with the legal requirements set out in the General Law for Corporations . Therefore, this Ayuntamiento did not appear as a founding shareholder in the company and moreover the shares should have been transferred through purchase and sale or through assignment, which requires that both a deposit in the amount of 20% of the share's value for the tax on dividends and a consent agreement from the parties, a consent which the Municipality had not issued. Therefore this commitment has not been complied with. As a result, the Ayuntamiento cannot agree that these conditions have been met. The *Ayuntamiento* cannot authorize procedures undertaken in violation of the law and, as a result, the *Ayuntamiento* was not a founding shareholder in the company.... it can be concluded, that the promise made by the concessionaire to the Municipality that it would participate with a 10% interest, upon not being legally valid was a misrepresentation, under the terms set out above. Therefore, the undertaking to issue a 10% interest to the *Ayuntamiento* was a misrepresentation and the manner in which it was eventually undertaken constituted an error in law.

[Irregularity #5] "The text of the decision passed in the November 4, 1992 *Cabildo* session, where it was agreed to award the concession to Desechos Solidos de Naucalpan, S.A. de C.V. noted that the session commenced at 12:30 p.m. and concluded at 10:45 p.m. The decision also noted that, among others, Mr. Ariel Goldenstein, a founding shareholder of the above noted company, was in attendance.... the text of the deed of incorporation reveals that the notary public formalized the deed on the same November 4, 1992. Therefore, it can be deduced that the deed of incorporation was prepared in accordance with instructions given by the shareholders before 12:30 p.m. that same day, because thereafter they were in the *Cabildo* chambers until late in the evening. Consequently, the Desechos Solidos de Naucalpan, S.A. de C.V. principals, including

Mr. Goldenstein, knew from the very start of the *Cabildo* session that the company they presented to the *Cabildo* would not be incorporated with the proposed United States and Mexican companies, because they had already instructed the notary to incorporate the company in a manner that was completely different from what they would be presenting to the *Cabildo*. The name and backgrounds of these companies as presented by Mr. Goldenstein, were found to be misrepresentations that led the *Cabildo* to award the concession, which therefore constituted an error in its awarding. ... the shareholders had time before the Cabildo session to prepare the deed of incorporation for two different companies but with the same name, notary number and date.

[Irregularity #6] In effect there is misrepresentation, by virtue of the fact that the Municipal files contain two deeds of incorporation for two different versions of Desechos Solidos de Naucalpan, S.A. de C.V.. Both versions of Desechos Solidos de Naucalpan, S.A. de C.V. have the same date, notary number and notary volume. However, these documents differed with respect to the shareholders, the capital distribution, the members of the administrative board and the commissioner. One of the documents of incorporation numbered 6,477, volume 167, presented to the Municipality in November of 1992, sets out the shareholders, their respective interests and the corporate officials as follows....

[DESONA A]		
Shareholder	**Shares**	**Capital**
Robert Azinian	2,700	27,000.00
Ariel Dario Goldenstein	1,300	13,000.00
José Humberto Pulido García	500	5,000.00
Epifano López Martínez	500	5,000.00
TOTAL	5,000	50,000.00
President	Robert Azinian	
Secretary	Ariel Dario Goldenstein	
Treasurer	José Humberto Pulido García	
Commissioner	Ma. Del Pillar Villanueva Jaso	

However, the deed of incorporation that the Municipality obtained from the Public Registry for Property and Commerce in February of 1994 also had the same document number 6,477 and volume number 167, noted that the shareholders, capital interest and company officials were as follows:

[DESONA B]		
Shareholder	**Shares**	**Capital**
Robert Azinian	2,700	27,000.00
Ariel Dario Goldenstein	1,300	13,000.00
Kenneth Davitian	1,000	10,000.00
TOTAL	5,000	50,000.00
President	Robert Azinian	
Secretary	Ariel Dario Goldenstein	
Treasurer	Kenneth Davitian	
Commissioner	Samuel Sritman	

The above leads to the conclusion, that there was a clear intention by those seeking the concession to misrepresent the facts to the Municipality with the sole objective of obtaining the Concession which was the object of this decision. Similarly, due to this anomaly the Ayuntamiento does not have the legal certainty that is required in Mexican law and, both due to the contracting person's status but fundamentally due to the fact that this is such an important public service.

[Irregularity #12] The misrepresentations that influenced the Municipality's consent to award the concession, is clearly manifested in Desechos Solidos de Naucalpan,. S.A. de C.V. incapacity in providing the solid waste collection, transportation and disposal service which has been evident since they started operating. Desechos Solidos de Naucalpan, S.A. de C.V. repeatedly emphasized that it had the capacity to provide the service efficiently and consistently. and made statements to support their promises which were in fact preconditions for the awarding of the concession.

There is an error in law in the consent to award the concession, due to the following circumstances:

[Irregularity #13] Compared to what was promised in the *Cabildo* session, the deed of incorporation, number 6,477, clearly provides that the corresponding Notary Public trusted that Mr. Robert Azinian and Mr. Ariel Goldenstein (as well as Mr. Kenneth Davitian in the second version of document number 6,477 in point 6 and those relating thereto) were of the foreign nationality and were passing through the Notary's city. However, they did not provide evidence of their capacity to appear as shareholders in the deed of incorporation. In accordance with the General Law on Residents they must have the express authorization of the Secretariat of Governance.... moreover as the founding shareholders failed to obtain the necessary legal standing to incorporate a company in Mexico, the *Ayuntamiento* was left in an obvious precarious legal situation, given that there was the permanent risk that the company that entered into agreement could be nullified thereby leaving the *Ayuntamiento* and the community vulnerable to any damages and injury that may ensue.

[Irregularity #15] In the November 4, 1992 *Cabildo* session, Desechos Solidos de Naucalpan, S.A. de C.V. promised... that one of the benefits to the Municipality with the Concession would be that it would not have to invest any capital. However, clauses Twenty-two and Twenty-three of the Concession Contract show that the Municipality committed itself to provide certain amounts of money to the Concessionaire for the provision of the public service. Similarly, the contract provides for the transfer of the Municipality's vehicle fleet and sanitation equipment to provide the service awarded in the concession thereby disposing of Municipal public goods to the Municipality's detriment. This ceding of Municipal goods was not discussed in the November 4, 1992 *Cabildo* session. Moreover, this is in violation of article 31(paragraph 26) of the Organic Municipal Law of the State of Mexico....Therefore, this was an error in law which vitiates the Concession.

[Irregularity #18] Similarly, there exists an error in law in the Ayuntamiento itself because upon exercising of the powers which the State Legislature conferred upon it, the Ayuntamiento entered into the Concession Contract, and upon agreeing to the other condition in the same, because upon transferring the municipal goods to the

Concessionaire, such as the Municipal vehicles, the sanitation equipment and the property rights over Rincón Verde, such transfers required the specific prior authorization of the State Legislature, as set out in Article 31… of the Municipal Organic Law of the State of Mexico, which was in force on the date the Concession Contract was entered into."

The Federal Circuit Court

131. On December 10, 1994, Global/DESONA filed an *amparo* challenge against the November 17, 1994, decision of the Superior Chamber of the State Administrative Tribunal[106].

132. On May 18, 1995, the Federal Circuit Court unanimously denied the requested *amparo*. The validity of the decisions of March 7 and 21 of 1994 were affirmed, as was the *Ayuntamiento's* administrative procedure for the nullification of the concession. The Federal Circuit Court concluded that Global/DESONA had manifestly omitted to challenge the central part of the decision of the Superior Chamber of the State Administrative Tribunal, namely the validity of 9 of the 27 irregularities that gave rise to the nullification of the concession which had been specifically analyzed by the Superior Chamber leading it to conclude that, in awarding the administrative concession, there had been errors and elements that vitiated the *Ayuntamiento*'s consent, and thus upheld the decision of March 7 and 21, 1994.[107]

Summary of Court Proceedings

133. The Tribunal can see that the nullification was challenged by Global/DESONA in three legal proceedings. In each instance, Global/DESONA lost. Dr. Dávalos testifies that Global/DESONA had ample opportunity to adduce evidence in support of its position. It failed to do so. On the other hand, the Municipality did file substantial evidence to support its action. The three courts accepted the evidence supporting the Municipality's actions.

134. The Tribunal can see that Global/DESONA was also afforded an opportunity to make its case to the *Ayuntamiento*. In doing so, it encountered Dr. Palacios, the aggrieved shareholder in DESONA I. The Respondent will now attempt to explain the complex relationship between the different versions of DESONA.

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106. See Exhibit 32. In sum, in addition to some minor allegations, including that the Municipal President lacked the capacity to nullify the concession, Global/DESONA's *amparo* claim primarily argued that its rights had been violated because: (i) the Municipality had undertaken the administrative nullification of the concession without any basis and both the State Administrative Tribunal and the Superior Chamber had not given its reasons (ii) the Municipality had cancelled a contract without having followed the procedure established in law to rescind a contract, and (iii) the State Administrative Tribunal and the Superior Chamber had not analyzed all the evidence and claims presented by Global/DESONA.

107. Decision of the First Collegiate Court for Criminal and Administrative Matters of the Second Circuit, dated May 18, 1995. See Exhibit 33.

C. Additional Relevant Facts

The Four Versions of DESONA

135. As the Tribunal has seen, the confusion between the Claimants' creation of two almost identical versions of the company, DESONA A and B, was one of the bases for the Mexican Courts' decision to uphold the nullification. In addition, the *Ayuntamiento* cited the failure to incorporate the 'DESONA Consortium' as an irregularity. Finally, DESONA I's role in the events leading up to the conclusion of the concession contract is explained by Dr. Palacios in his witness statement.

136. From the beginning of this proceeding, the Respondent has raised questions about the nature of the alleged investment and the Claimants' purported interests therein. The Tribunal will recall that there have been four versions of DESONA:

- the first, which the Respondent designated as DESONA A for ease of reference (and whose deed of incorporation listed two Mexican nationals as shareholders, Mr. José Humberto Pulido García and Mr. Epifanio López Martínez, together with Mr. Azinian and Mr. Goldenstein);

- the second, which the Respondent designated as DESONA B (and whose deed of incorporation listed only Mr. Azinian, Mr. Davitian and Mr. Goldenstein as shareholders);

- the third, DESONA I (a company incorporated on March 3, 1993 whose shareholders were Mr. Goldenstein and Dr. Oscar Palacios); and

- a fourth version, which in fact was never created, was described in the November 4, 1992 *Cabildo* minutes as a consortium of four companies.

137. Since corporate documents for the fourth version were apparently never produced, the Respondent will not address it further other than to note that at the *Cabildo* session of November 4, 1992, it was represented that "four companies have associated… to incorporate a Mexican enterprise called DESONA, S.A. de C.V., which means Desechos Sólidos de Naucalpan…" Thus, the concession would be operated by four companies[108]. DESONA was described as being a company whose capital stock would be distributed as follows: 45% U.S. interest; 45% Mexican interest; and 10% interest of the Municipality. It is evident that neither DESONA A, DESONA B, nor DESONA I corresponded to the shareholding that was described to the *Ayuntamiento*.

138. It should be noted that the Claimants did not add the letters 'A' and 'B' to DESONA's deeds of incorporation. The Respondent did so in its original motion in order to distinguish between the two different versions of the company's shareholders. The corporate name, the deed number and the notarial seal were otherwise identical.

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108. Minutes of the *Cabildo* session of November 4, 1992. See Exhibit 3.

139. After the First Session of the Tribunal, the Respondent filed a Motion seeking directions from the Tribunal that the Claimants establish their standing and clarify the basis for their claim. The Tribunal received the motion, and a reply from the Claimants, and decided to defer the consideration of the motion's merits until later in the proceeding.

140. The Tribunal will recall that the Respondent requested further information regarding the three versions of DESONA and transactions relating to their share capital. The Respondent has attempted to make sense of the evidence that it has received. However, the Tribunal will see that the Claimants' account of the various transactions simply does not make sense.

141. It is established that two versions of the deeds of DESONA were drafted by Notary Public #7 of Cuautitlán Izcalli on November 4, 1992, just prior to the *Cabildo* meeting at which the concession was granted to "DESONA". Neither one was perfected according to Mexican law. The deed of incorporation would have to be registered at the local Public Registry and then finally authorized by the Notary Public. This was not done until November, 26, 1993, one year later.

DESONA A

142. DESONA A originally issued shares to two Mexican businessmen, José Humberto Pulido G. (initially holding 500 shares) and Epifanio López Martínez (initially holding 500 shares), in addition to Mr. Azinian (with 2700 shares) and Mr. Goldenstein (with 1300 shares). The Claimants assert that DESONA A was simply abandoned because the two Mexicans did not subscribe to their shares[109].

143. However, the Respondent has obtained a document prepared by Mr. Goldenstein on August 12, 1993, in which he set out the January through July financial situation for DESONA A[110]. It contains balance sheets prepared by the accounting firm Dinamica Contabe, S.C. The Tribunal will see that both Mr. Pulido and Mr. López are listed as shareholders, while Mr. Davitian is not listed as a shareholder. It further indicates that the original capital contributions were subscribed (including by the two Mexican shareholders), and that Mr. Pulido made substantial additional capital contributions —at least in relation to the other shareholders. This document of Mr. Goldenstein's own making therefore contradicts the Claimants' account of DESONA A.

144. Oddly, the balance sheets in Mr. Goldenstein's August 12th financial report for DESONA A list DESONA I as a creditor, even though DESONA I at that time held the concession.

DESONA I

145. It is established that DESONA I was incorporated by Mr. Goldenstein (holding 3500 shares) and Dr. Oscar Palacios (holding 1500 shares) on March 3, 1993. On April 22, Mr.

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109. Claimant's reply to the Mexican Government's Motion for Directions dated November 5, 1997.
110. Financial Report on DESONA, dated August 12, 1993. See Exhibit 34.

Goldenstein formally requested the *Ayuntamiento* to assign the concession to DESONA I[111] and on May 3, 1993, it obliged.

146. Dr. Palacios testifies that Mr. Goldenstein promised him that DESONA I would be the concession holder. They agreed that Dr. Palacios (on behalf of EPYCSA S.A. de C.V., a Mexican group that he directed) would contribute cash and manufacture metal garbage containers for use in the concession. Once the concession was approved by the State Legislature, Mr. Goldenstein and his colleagues would contribute their share of money[112].

147. Mr. Goldenstein told Dr. Palacios to deposit the funds in a BANAMEX S.A. account number 520786-5. Dr. Palacios testifies that he deposited funds into the account on several occasions and set about manufacturing the metal garbage containers[113].

The State of Affairs as of April 1993

148. As of April 1993, according to the evidence generated by the Claimants, there were three versions of DESONA: DESONA A, which according to Mr. Goldenstein's own financial records was the operative version of DESONA (although the necessary steps to complete the company's registration had not been effected), DESONA I, which had just been incorporated and was about to take the assignment of the concession, and DESONA B, the deed for which had apparently been drafted but which was evidently not operative at all.

The April 19th Shareholders Meeting

149. Although DESONA A and DESONA I were the two of the three versions that were being "operated" at this time, the Claimants have produced minutes of a shareholders meeting purportedly held on April 19, 1993 at which they claim that they scrutinized the share capital of DESONA. According to the minutes, Mr. Davitian certified that the total shares issued were represented and that owners of such shares were, Mr. Azinian (2700), Mr. Goldenstein (1300), and 1000 for himself[114].

150. This, of course, is contradicted by Mr. Goldenstein's subsequent August 12th financial statement for DESONA, which included a balance sheet for the month in which this meeting is claimed to have occurred. Further, DESONA I was already in existence and was to hold the concession, so it is unclear why DESONA (either A or B) would have a meeting to discuss performance of the concession —particularly when Mr. Goldenstein, only three days later, requested that the concession be transferred to DESONA I. Finally, Dr. Palacios, who on Mr. Goldenstein's own evidence was an incorporating shareholder of DESONA I, was described in the minutes as a "special guest" —a peculiar term in the context of a shareholders meeting.

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111. Letter from Mr. Goldenstein requesting assignment of the concession from Desona A to Desona I dated April 22, 1993. See Exhibit 35.
112. Witness statement of Dr. Oscar Palacios.
113. Ibid.
114. Declaration of Ariel Goldenstein, dated October 28, 1997, p. 1.

The Awarding of the Concession

151. The State Legislature committee considered the awarding of the concession for a period of fifteen years during its sessions held on July 22 and 24 of 1993. The Legislature eventually authorized the awarding of the concession for fifteen years to "DESONA". Oddly, the documents submitted by the Global/Desona principals refer to both DESONA B and DESONA I. In fact, the deed of incorporation and the draft Title of Concession (which informed the Legislature how the concession contract would operate) are two documents which specifically refer to DESONA I[115]. Nevertheless, in the end, it was "DESONA" that was authorized the concession apparently due to a typographical error which omitted to include the number "I" in an otherwise identical corporate name.[116]

Events After the State's Approval

152. The draft title of concession before the State Congress required that the concessionaire associate with Sunlaw de México and BAS immediately upon the concession being approved, and to initiate operations 90 days thereafter.

153. Dr. Palacios' testimony is that after the State Legislature approved the concession he pressed Mr. Goldenstein to make his promised contribution. Although Mr. Goldenstein promised to do so, he never did[117].

154. Instead, Mr. Goldenstein proceeded to negotiate the concession contract with Mr. Chávez Tello, the Municipal Secretary. The concession contract was signed, not on behalf of DESONA I, but rather on behalf of DESONA B whose deed of incorporation was subsequently registered in the State Public Registry of Property and Commerce on November 23, 1993.

155. On the date of the contract's signing, it was DESONA I, not DESONA B, that held the concession.

156. On November 26, 1993, Mr. Goldenstein *—acting on behalf of DESONA B rather than the then-concession-holder, DESONA I—* requested that the concession be transferred from DESONA I to DESONA B[118]. The Tribunal should note that this occurred eleven days after the ostensible "signing" of the concession contract.

157. The Claimants' response to the Respondent's request for clarification as to the status of DESONA I was terse and uninstructive. Nonetheless, it is apparent that 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. Hence Dr. Palacios subsequently filed a criminal complaint for fraud against Mr. Goldenstein.

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115. The draft Title of Concession. See Exhibit 36.

116. Apparently the error stems from the fact title of Concessión refers to "Desechos Sólidos de Naulcalpan S.A. de C.V." as a concessionaire even though it clearly refers to the incorporation deed of DESONA I, when describing it.

117. Witness Statement of Dr. Oscar Palacios.

118. See Exhibit 37.

DESONA B

158. The Claimants have provided the share certificates that they claim represent their interests in DESONA B[119].

159. The Tribunal will see that the certificates are dated November 15, 1993, the date of the ostensible signing of the concession contract. This date has further significance for reasons that will be explained below.

160. The certificates are numbered in the upper left hand corner, commencing with #52. Certificates #1-51 have not been produced, so it is not known what names were inscribed on them. Each certificate that has been produced represents 100 shares. The certificates were issued as follows:

- Certificates #52-73: Robert Azinian, totaling 2200 shares.
- Certificates #87-96: Ellen Baca, totaling 1000 shares.
- Certificates #97-101: H. Ayuntamiento de Naucalpan de Juázez, totaling 500 shares.

161. This adds up to 3700 shares. The 5100 shares represented by certificates #1-51, and the 1300 shares represented by certificates #74-86, are unaccounted for. Even assuming that Mr. Goldenstein was issued 1300 shares, as the Claimants assert, the 5100 shares that were represented by certificates #1-51 are unaccounted for. It could be inferred that those shares were issued to Mexican investors, such as Mr. Pulido, Mr. López, and perhaps Dr. Palacios.

162. It is important to note that, as of the date of the shares' issuance, November 15, 1993, Ms. Baca is now listed as a shareholder in place of Mr. Davitian.

163. The reasons why November 15th is a critical date is that only three days later, Messrs. Azinian, *Davitian*, and Goldenstein signed a Security and Guaranty Agreement with BFI to secure a loan for 100,000 dollars[120].

164. The Agreement's recitals in Clause I note that "The Guarantors Robert Azinian, Ariel Dario Goldenstein *and Kenneth Davitian* are currently the legal and beneficial owners respectively of fifty-four percent (54%), twenty-six percent (26%) *and twenty percent (20%) of the issued and outstanding shares* of Desechos Solidos de Naucalpan (DESONA)".

165. This recital is inconsistent with several other facts. First, according to the share certificates provided to the Respondent, only three days earlier, Mr. Davitian's shares were issued to Ms. Baca.

119. Claimants' reply to the Mexican Government's Motion for Directions dated November 5, 1997.
120. Ibid.

166. Second, Mr. Azinian's pledge of 750 shares to BFI as a Guarantor demonstrates another inconsistency: the Tribunal will note that he has tendered as evidence of his shareholding 100% of the shares that he initially held. Yet he claims that BFI has demanded payment of its loan. It seems inconceivable that BFI would have returned its security to Mr. Azinian prior to repayment.

167. The Respondent has obtained another balance sheet for "DESONA" as of October 31, 1993.[121] The balance is very similar to those contained in the August 12 financial report, and was prepared by the same accounting firm. In particular, like the balance sheet for DESONA as of July 31, 1993, it shows DESONA I as a creditor.

168. The balance sheet shows that an additional subscription of Capital was made by EPYCSA (the Mexican group directed by Dr. Palacios), thereby indicating that EPYCSA was a shareholder.

169. It therefore, appears that, unbeknownst to Dr. Palacios, his financial contribution to DESONA I was recorded on the books of DESONA A as a capital contribution by EPYCSA.[122]

170. It should be noted that it was not until this time that the Claimants actually took steps to formalize one of the versions of DESONA A or B, which was apparently done because of a requirement in the BFI agreement that DESONA be incorporated. The Tribunal will see that the deed of incorporation for DESONA B is actually registered on November 23rd, and then finally certified by the Notary Public on November 26th.

The December 15th Shareholders Meeting

171. The Claimants have tendered minutes of their December 15th shareholders meeting in which the assignment of Mr. Davitian's shares is reported as being authorized.

172. As in the April 19th minutes, there is a section in which the existing shareholders are scrutinized and Mr. Davitian is said to still hold his allotment of 1000 shares.

173. The problem for the Claimants is that according to the certificates provided by them in this proceeding, Ms. Baca had already received her shares one month before. Yet it is at this meeting that Mr. Davitian allegedly requests the transfer of his shares to Ms. Baca.

174. It is not possible for the Claimants to argue that this meeting merely ratified that which was done one month earlier because, as the December 15th meeting's minutes state, Mr. Azinian was authorized "to issue new stock certificates under the name of Ellen Marie Baca and cancel the ones under Mr. Kenneth Davitian (sic) name".

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121. See Exhibit 38.
122 This financial contribution was later withdrawn from the capital stock contributions and considered as a creditor.

Summary

175. The intended grant of the concession to the DESONA consortium, the Claimant's provision of the deed for DESONA A to the Municipality, the concession's assignment to DESONA I, the Claimants' replacement of DESONA A with DESONA B, and the assignment from DESONA I to DESONA B after the concession contract was allegedly signed by DESONA B, were among the irregularities cited by the *Ayuntamiento* when it decided to nullify the concession and in the subsequent Tribunal proceeding[123].

176. The Respondent submits that the documents supplied by the Claimants are representative of their conduct throughout the entire affair. They are contradictory, unreliable, and therefore cannot be accepted as proof of the facts alleged by the Claimants.

177. For the convenience of the Tribunal, a diagram illustrating the composition of the four versions of "DESONA" follows.

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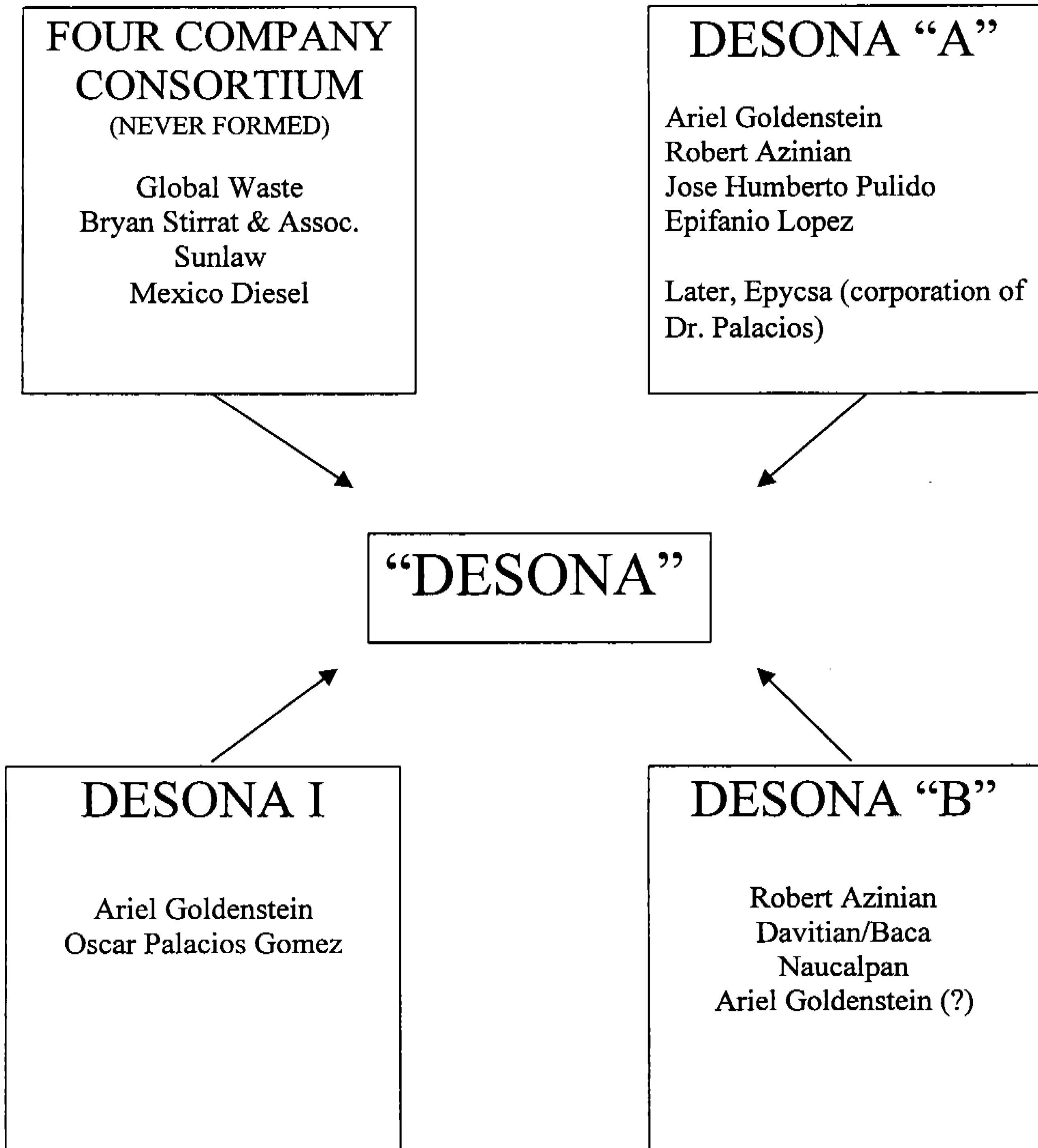
123. The Superior Chamber of the State Administrative Tribunal held that the existence of two conflicting deeds of incorporation was evidence of "the possible intention to confuse the Municipal Authorities and not comply with the commitments made in the *Cabildo* session" on November 4, 1992. This was upheld by the Federal Circuit Court. See Superior Chamber's decision dated November 17, 1994 in Exhibit 31; Federal Circuit Court decision dated May 18, 1995 in Exhibit 33.

THE FOUR VERSIONS OF "DESONA"
Shareholders



PART III: LEGAL SUBMISSIONS

A. Interpreting The NAFTA — Applicable Principles: Article 102

178. The governing rule of the interpretation and application of the NAFTA as a whole is set out in Article 102:

> "The Parties shall interpret and apply the provisions of this Agreement in the light of its objectives set out in paragraph 1 and in accordance with applicable rules of international law."

179. The interpretation of Chapter Eleven is governed by the actual terms of the NAFTA, taken in context, as well as the "applicable rules of international law". The latter include Article 31 of the Vienna Convention on the Law of Treaties[124].

180. In the case of *In the Matter of Tariffs Applied by Canada to Certain U.S.–Origin Agricultural Products*, the Panel interpreted this to mean that it should commence its inquiry by identifying the "plain and ordinary meaning of the words used" in the Agreement; such identification would consider "the meaning actually to be attributed to words and phrases looking at the text as a whole and examining the context in which the words appear"[125].

181. International agreements express the common intention of the Parties. It necessarily follows that the objective of treaty interpretation is to ensure that the Agreement is interpreted and applied in a manner that gives effect to that common intention[126]. The principle of good faith in interpreting an international agreement underlies the concept that the interpretation should not lead to results that are manifestly absurd or unreasonable.

B. Preliminary Issues

1. The Entire Claim is Based on Misrepresentations

182. Chapter Eleven was a development of historical significance in the treaty relations between the three North American nations. The Parties to the NAFTA agreed to offer the protections contained in Section A of the Chapter to each other's investors.

183. The Parties assumed that Chapter Eleven would be invoked by investors with good faith claims. In the Respondent's view, tribunals have a duty to ensure that frivolous or vexatious claims are dealt with in an appropriate fashion to avoid abuse of the arbitration process and unnecessary diversion of government resources. This is such a claim.

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124. In the Matter of Tariffs Applied by Canada to Certain U.S.-Origin Agricultural Products, 1 T.T.R. (2d) 975 at paragraph 119.
125. Ibid. at paragraph 120.
126. Lord McNair, The Law of Treaties, (Oxford: Clarendon Press, 1961) at page 365.

184. The evidence taken from U.S. court filings and other documents of the Claimants' making shows that the concession was obtained through an extraordinary set of misrepresentations and material omissions calculated to mislead the Municipality.

185. The evidence also shows that one of the Claimants, Robert Mr. Azinian, was a bankrupt at the time that the concession was granted. This was not disclosed to the *Ayuntamiento*.

186. Mr. Azinian was continuously held out to the Municipality as the President of Global Waste Industries, Inc. The sworn statement of his colleague, Ariel Goldenstein, in Global's U.S. bankruptcy proceeding, however, contradicts this representation. In listing the shareholders and officers of Global to the United States Court, Mr. Goldenstein did not include Mr. Azinian at all.

187. In fact, *none* of Mr. Azinian, Mr. Davitian, and Mr. Goldenstein had the interest in Global that they represented to the Respondent and to the Tribunal in their response to the Respondent's request for particulars.

188. Further, in its Spanish language "company profile", Global was represented as having 40 years of experience. Yet it had only been incorporated on March 1, 1991, some nineteen months before it appeared before the *Ayuntamiento* to seek the grant of the concession.

189. Moreover, at the time that Global appeared before the *Ayuntamiento,* it was already well into its own corporate bankruptcy proceeding. This fact, which obviously would have affected the decision of the *Ayuntamiento* (in that the company was supposed to be financially capable and able to make the investments that it told the *Ayuntamiento* it would make), was never disclosed to the official body of the Municipality that, under Mexican law, had the authority to grant the concession.

190. Global's sum total of revenue for 1991-92, according to Mr. Goldenstein's sworn statement in the bankruptcy proceeding, was 30,000 U.S. dollars. Mr. Goldenstein knew at the time that he presented Global's plans to the *Ayuntamiento* that it had no capability to make the kind of investment that he was describing.

191. It was not disclosed to the *Ayuntamiento* that Mr. Azinian and Mr. Goldenstein had no personal experience whatsoever in the waste disposal business, nor that Mr. Davitian's track record in the business was poor.

192. The Respondent submits that on these grounds alone, the Claim should be deemed wholly lacking in basis. It should be dismissed without the need for further steps in this proceeding.

2. There Was No Investment Within the Meaning of the NAFTA

193. It is submitted that the Tribunal must also carefully examine the nature of the investment that has been claimed to have been expropriated and the Claimants' relation thereto. As the Tribunal noted in its decision on standing, the Claim being advanced by the investors in this case is in their personal right and not on behalf of the enterprise itself in which they allegedly invested.

194. There are two related issues here. First, there is the Claimant's failure to present even minimally credible evidence that they actually made a commitment of capital or other resources in relation to the concession agreement. Second, there is the question of whether the company in which the Claimants made their purported investment – DESONA B—actually was the concession-holder.

195. NAFTA Article 1139 sets out the forms of investment recognized by the Parties as protected by the Agreement. In each case, the investor must demonstrate to the Tribunal's satisfaction the precise nature of his or her investment. The Claimants assert that the following sections of the definition of investment apply in this case:

> "investment means:
>
> (a) an enterprise;
>
> (b) an equity security of an enterprise…
>
> (d) a loan to an enterprise…
>
> (ii) where the original maturity of the loan is at least three years,
>
> (e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise…
>
> (h) interests arising from the commitment of capital or other resources in the territory of a Party to economic activity in such territory, such as under
>
> (i) contracts involving the presence of an investor's property in the territory of the Party, including turnkey or construction contracts, or concessions, or
>
> (ii) contracts where remuneration depends substantially on the production, revenues or profits of an enterprise…"[127]

a. The Claimants Have Not Shown they Committed any Capital

196. The Tribunal will recall that, while the Claimants have asserted that they contributed "hundreds of thousands of dollars," they have not substantiated any of those claims —despite repeated requests for supporting documentation from the Respondent.

197. Article 1139 includes within the definition of investment "*interests arising from the commitment of capital or other resources* in the territory of a Party to economic activity in such territory, such as under… concessions". As such, the concession itself is not an investment —only interests arising from the commitment of capital or other resources relating to the concession are investments.

198. Article 1139 expressly *excludes* from the definition of investment "claims to money that arise solely from commercial contracts for the sale of goods or services by a national or

127. Memorial, Section 5, page 2.

enterprise in the territory of a Party to an enterprise in the territory of another Party, or... any other claims to money that do not involve the kinds of interests set out in subparagraphs (a) through (h)".

199. In order for an investment to be governed by the Chapter Eleven of the NAFTA, there must have been an actual commitment of capital or other resources within Mexico that was lost because of action taken by the Respondent which the Tribunal concludes has contravened the investment protections of the NAFTA.

200. Moreover, the Claimants did not have a personal interest in the concession. As a matter of law, that interest was held by one of the various versions of DESONA. The Tribunal is directed by Article 1139 to consider therefore what interests arose in the commitment of capital or other resources by the Claimants relating to the concession. Put succinctly, what capital or other resources did the Claimants actually invest in Mexico?

201. The evidence shows that one of the reasons why the concession was nullified was because, notwithstanding their representations of considerable corporate experience and financial capacity, DESONA lacked the capital needed to carry out the concession. Evidence of this is provided:

a) by Mr. Piazzesi's evidence and the *Ayuntamiento*'s findings;

b) by two independent third parties, Mr. Jim Hodge and Mr. Sam Maphis, both of whom examined the concession in early 1994 (Mr. Hodge in January and Mr. Maphis in early March) and concluded that DESONA lacked the financial (and managerial) capability to perform the contract; and

c) by the fact that DESONA's evidence of expenditures which was put before the State Administrative Tribunal —consisting of a single page— was found to be incomplete.

202. In other words, there is little evidence of *any* personal resources committed to the investment because the Claimants were *incapable* of committing capital or other resources to economic activity in Mexico. The Tribunal will also recall that not only was Global in bankruptcy prior to obtaining the concession, but that Mr. Azinian himself was in personal bankruptcy at that time.

203. What little expenditure the Claimants claimed they have made (for example, the expenses for the local officials' visit to Los Angeles) turned out to be mostly paid for by Emilio Sánchez. Similarly, the evidence is that the garbage containers that the Claimants make much of providing to the municipality were supplied mainly by Dr. Palacios, not the Claimants. Finally, the two trucks that the Claimants seem to have supplied apparently were sold by them to another waste company, once owned by Sanifill, called "King Kong."

204. Most importantly, the best evidence available —Mr. Goldenstein's financial report of August 12, 1993— shows Mr. Azinian as having subscribed to a capital contribution of 27,000 pesos (roughly 9,000 dollars); there is nonetheless no independent evidence that he acutally paid in that money. Mr. Davitian is not shown as a shareholder, but is listed as *owing* 2,500 pesos to

the company. All evidence indicates that persons other than the Claimants contributed capital to the company and owned—or believed they owned—a majority of its shares.

b. The Claimants Have Not Shown they Made an Investment in an Enterprise, or in Shares Thereof, nor that they Were Entitled To Share in Income or Profits Therefrom

205. The expert evidence is that under Mexican law, public services are of the exclusive competence of the public administration (whether federal, state or municipal). No private party has a pre-existing right to provide such services. Government agencies may, however, award concessions for the provision of certain public services, where they lack the necessary resources to provide the service adequately and most efficiently, or where their resources would be better utilized in other areas.

206. A concession does not imply privatization of the service; it remains a public service under the responsibility and oversight of the corresponding government agency. It only involves the delegation of certain activities on a temporary basis. In granting a concession, the public administration does not relinquish or abandon its duties; it is still responsible for the performance of such activities, which remain within its competence.

207. The underlying principle in granting a concession is that the concessionaire will surpass the government agency's capabilities in performing the public service (otherwise, it would be illogical to grant the concession). The concessionaire needs to have the necessary legal, technical, financial and moral capacity to provide the public service in a general, uniform, continuous, and permanent manner.

208. For these reasons, concessions are granted on a strictly personal basis, that is, they are awarded to the concessionaire, and none other. Concessions are awarded for purposes of performance by the concessionaire, given its capabilities to provide the public service in question. As a matter of Mexican law, concessions are, therefore, non-tradeable; the concessionaire may not freely transfer it without the consent of the governmental authority. Indeed, the Tribunal has seen that the confusion between the various versions of DESONA was one of the grounds on which the courts upheld the concession's nullification[128].

128. See expert report of the *Instituto de Investigaciones Jurídicas*.

(1) The Concession Was Never Properly Assigned to the Version of DESONA that Claimants Purport to Own

209. As discussed in detail above in Part II, C (Additional Relevant Facts), the Claimants engaged in a "shell game" with the various corporate forms held out on "DESONA." They have not established that the corporation they purport to own—DESONA B—was assigned properly within the Concession Contract, following the State's approval of the concession.

(2) The Claimants Were Unable To Perform under the Concession

210. Given the Claimants' technical and economic background, specifically, their personal financial situations and that of Global, as well as their lack of expertise in this area, it is obvious that, as events transpired, they were unable to perform under the concession at the time that it was awarded, when the concession contract was signed or any later stage. Messrs. Azinian, Goldenstein and Davitian not only obtained the concession through gross misrepresentations; they proved to be wholly incapable of substituting for the *Ayuntamiento* in the provision of the public services, let alone surpassing it, notwithstanding the scarce resources of the *Ayuntamiento*. Indeed, the *Ayuntamiento* later resumed the provision of the public service on its own.

211. The nature of the concession precluded the concessionaire from transferring it to a third party without consent. It was directly responsible for performance and thereby accountable to the *Ayuntamiento*.

212. Because of the irregularities surrounding the different versions of DESONA in relation to the awarding of the concession and the inability of the ostensible concessionaire to perform under the concession, the validity to a claim concerning the existence under the NAFTA of an enterprise, an equity security of such enterprise or an interest in an enterprise that entitles the owner to share in income or profits arising therefrom, cannot be sustained.

c. The Claimants Have Not Shown That Any of Them Made a Loan to an Enterprise

213. The Claimants allege to have made investments in the form of a "loan to an enterprise… where the original maturity of the loan is at least three years." Yet, they have failed to provide any evidence of this. Indeed, the Memorial contains no reference to any such loans. Although the Claimants allege to have jointly and severally borrowed money and to be obligated in amounts in excess of 1.6 million dollars, there is no evidence that they loaned such monies to an enterprise in Mexico. Accordingly, this contention should be rejected.

214. Thus, the Respondent submits that the Claimants, having offered no evidence of an actual investment within the meaning of Article 1139, cannot be allowed to maintain their claim.

3. Additional Issues Concerning The Standing of the Purported Investors

215. In addition to the Respondent's objections about the Claim in general, it wishes to make certain observations on the problems of standing of some individual Claimants.

Mr. Davitian

216. The Tribunal will recall that the Respondent raised the issue of Mr. Davitian's standing previously and the Tribunal deferred consideration of the point until later in the proceeding. In the Respondent's respectful submission, the Claimants have been unable to advance a convincing legal basis for Mr. Davitian's standing.

217. Although it is asserted that he was an investor in one of the versions of DESONA, (DESONA B), there is evidence of Mr. Goldenstein's making (a year-to-date financial report on DESONA dated 12 August 1993) which does not list Mr. Davitian as a shareholder at all (the financial statements as of July 31, 1993 list Mr. Davitian under "additional capital contributions", he is shown as owing 2,500 pesos). Therefore, it is not clear that Mr. Davitian ever had an interest in any version of DESONA.

218. Even if he did have an interest, Mr. Davitian assigned it to his former wife, Ms. Baca, as part of a divorce settlement and Ms. Baca would now stand in his place as a Claimant. This is the only investment interest of Mr. Davitian (if he ever did in fact have it) that could be recognized by the NAFTA.

219. The Memorial and Mr. Davitian's statement assert that although he is no longer a shareholder, he still had an expectation of profit in the company's endeavors. However, as Article 1139 shows, the NAFTA's definition of "investor" does not extend to employees. While Mr. Davitian may once have been "an investor ... that seeks to make, is making or has made an investment", upon assigning his interest to Ms. Baca, Mr. Davitian lost any entitlement he may have had to assert a claim under Chapter Eleven. The simple legal fact is that, at the time the claim was filed, he had no interest in any of the different versions of DESONA that would confer standing on him for the purposes of this proceeding.

Ellen Baca

220. Ms. Baca's claim is based exclusively on whatever had been Mr. Davitian's interest, if there was any, in the investment. If Mr. Davitian was not a shareholder in the investment —as indicated by the financial report prepared by Mr. Goldenstein— he had no ownership interest to transfer to Ms. Baca. She therefore would also lack standing to assert a claim.

The Purported Assignment of Mr. Goldenstein's Interest to Mr. Azinian

221. The Respondent has already objected to the attempt to vest Mr. Azinian with the right to assert a claim on behalf of Mr. Goldenstein, who is not a national of a NAFTA country, and it reiterates that objection. Even if Mr. Azinian had standing to assert a claim on his own behalf

—which he does not— the attempted assignment cannot be employed to indirectly give standing to Mr. Goldenstein.

222. The NAFTA Parties conferred the right to assert a Chapter Eleven claim upon nationals of the Parties only. Article 1139 states in this regard that the term "investor of a Party" means in respect of a natural person "a *national*...of such Party". Nothing in the Agreement allows a non-national to assign his shares to a national so that his claim can be asserted by that person.

223. Allowing Mr. Azinian to assert Mr. Goldenstein's claim by virtue of a purported assignment of the latter's shares in DESONA to him would negate the Parties' clear intention to limit the right to assert a Chapter Eleven claim to their respective nationals.

C. The Respondent's Answer to the Specific Claims

224. The Claimant's Memorial is based upon two specific sets of claims:

a) Article 1105: the alleged failure to accord the Claimant treatment in accordance with international law, including fair and equitable treatment and full protection and security; and

b) Article 1110: the alleged expropriation of the investment, by direct and indirect acts or by measures tantamount to expropriation.

1. The Domestic Legal Proceedings and Their Relevance to This Proceeding

225. One of the factors that may prove there has been an expropriation of contractual rights is the lack of a domestic legal remedy[129]. The absence of domestic legal remedies could conceivably be relevant in a consideration of the fair and equitable treatment standard.

226. The Claimants seek to have the Tribunal ignore the three domestic legal proceedings. Yet the proceedings were initiated in the name of DESONA, the purported investment of these individuals. Further, the Claimants themselves state that "DESONA's management" —that is, the Claimants themselves— sought domestic legal relief "without success"[130].

227. In the Respondent's submission, the domestic legal proceedings add important factual and legal elements to this proceeding. The Claimants had their day in court three times and lost three times.

228. The Respondent does not contend that by virtue of DESONA's having prosecuted two different legal proceedings (and one appeal), NAFTA Article 1121 foreclosed the Claimants' right to invoke Section B.

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129. See the Restatement (Third) of Foreign Relations Law of the United States at Section 712..

130. Memorial at p. 52.

229. However, the Courts' findings of fact and legal conclusions are directly relevant in this arbitration. The Claimants face a situation where the act complained of was reviewed and upheld by three different courts. Yet the Claimants do not allege (nor can they adduce any evidence to support a claim) that there was a failure by the Respondent's judiciary to fairly hear and resolve their enterprise's legal claim.

230. The domestic legal proceedings are highly relevant to this proceeding for five reasons:

- First, the Tribunal can see that there was an appropriate domestic forum to hear the claim of unlawful termination.
- Second, the Tribunal can see from Dr. Davalos' witness statement that DESONA did *not* adduce any evidence in response to the voluminous evidence adduced by the Municipality to support its decision to nullify the concession.
- Third, the Claimants devote a considerable amount of their Memorial to attempting to reargue the enterprise's case against the 27 irregularities.
- Fourth, the Tribunal can see that the 27 irregularities identified in the nullification procedure were each challenged and considered by the domestic courts.
- Fifth, the Tribunal can see that, after considering the matter, the courts confirmed the concession's nullification. This is evidence of the reasonableness of the municipality's action and that its motivation in taking action was proper.

231. Thus, bald assertions such as that made at page 12 of Section 5 of the Memorial, where it is contended that "DESONA was not in breach of its obligations under the concession Contract and was fully capable of performing those obligations", simply lack credibility. The Claimants are unable to assert that the courts failed to provide an adequate and fair hearing of the merits of their complaint and accordingly, this claim should be dismissed.

232. In addition to the five reasons set out above, the Tribunal will recall the well-established principle of international arbitration, namely, that international arbitral tribunals do not sit as appellate courts of review for the decisions of national courts. The decisions of the national judiciary are to be accorded deference and respect and findings of fact and law are to be left untouched except in the most extraordinary of cases.

233. Judge Tanaka addressed this principle in detail in the *Barcelona Traction* case[131]:

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131. Judge Fitzmaurice made the following comment regarding the significance of separate opinions of international tribunal:

> "Although these comments [separate opinions] can only be in the nature of *obiter dicta*, and cannot have the authority of a judgment, yet since specific legislative action with direct binding effect is not at present possible in the international legal field, judicial pronouncements of one kind or another constitute the principal method by which the law can find some concrete measure of clarification and development. I agree with the late Judge Sir Hersch

Footnote continued on next page

"It is to be noted that the various complaints raised by the Belgian Government are mainly concerned with the interpretation of municipal law, namely provisions of the Spanish commercial code and civil procedure code in the matter of bankruptcy, and provisions of Spanish private international law on the jurisdiction of Spanish Courts concerning bankruptcy. Questions relating to these matters are of an extremely complicated and technical nature: they are highly controversial and it is not easy to decide which solution is right and which wrong. Even if one correct solution could be reached, and if other contrary solutions could be decided to be wrong, we cannot assert that incorrect decisions constitute in themselves a denial of justice and involve international responsibility.

In short, since these issues are of a technical nature, the possible error committed by judges in their decisions cannot involve the responsibility of a State. That the above-mentioned doctrine precludes such an error from being a constituent element in a denial of justice as an internationally wrongful act is not difficult to understand from the other viewpoints also. The reason for this is that these issues are of a municipal law nature and therefore, their interpretation does not belong to the realm of international law. If an international tribunal were to take up these issues and examine the regularity of the decisions of municipal courts, the international tribunal would turn out to be a '*cour de cassation*', the highest court in the municipal law system. An international tribunal, on the contrary, belongs to quite a different order; it is called upon to deal with international affairs, not municipal affairs. Now, as we have seen above, the actions and omissions complained of by the Belgian Government, so far as they are concerned with incorrectness of interpretation and application of municipal law, cannot constitute a denial of justice. This means that in itself the incorrectness of a judgment of a municipal court does not have an international character[132]."

234. Louis B. Sohn and R.R. Baxter, then of the Board of Editors of the *American Journal of International Law*, wrote that: "In order to avoid putting an international tribunal in the position of a court of appeal from the courts of the State which is a party to the agreement, a 'clear' departure from the proper law of the contract is requisite to the establishment of responsibility"[133]. They added further: "...the courts and other agencies of the State party to the agreement are, if acting in good faith, presumptively the soundest interpreters of the law of that State"[134].

235. The Claimants are seeking to have this Tribunal sit as a court of review of Mexican municipal law to resolve issues that do not involve international law. The NAFTA does not grant the Tribunal the jurisdiction to make such a review.

Footnote continued from previous page

> Lauterpacht that it is incumbent on international tribunals to bear in mind this consideration, which places them in a different position from domestic tribunals as regards with —or at least commenting on— points that lie outside the strict *ratio decidendi* of the case."

Separate Opinion of Judge Fitzmaurice, *Barcelona Traction, Light and Power Company, Ltd.*

132. Separate Opinion of Judge Tanaka, *Barcelona Traction*, 1970 ICJ at 157-58.

133. Sohn and Baxter, "Responsibilities of States for Injuries to the Economic Interests of Aliens," in 55 *American Journal of International Law* 545, 571 (July 1961).

134. Ibid.

236. Further, there is no evidence that any of the courts to which the Claimant applied for relief committed an act or omission which constituted a denial of justice or other wrong for which the Respondent might incur responsibility under international law.

237. In general, a denial of justice in civil proceedings includes the following:

a) denial of court access;

b) unreasonable delay in administrative justice; and

c) irregularities in the conduct of the proceedings[135].

238. Clearly, there has been no breach of the procedural requirement as to free court access. DESONA was able to have its claim heard three times, twice at the State level and once at the federal level.

239. There is no evidence of unreasonable delay. In fact, the time from which DESONA first filed its claim with the State Administrative Tribunal (March 1994) until final disposition of the matter by the Federal Circuit Court (May 1995) took only 14 months.

240. The Claimant has not adduced any evidence of any irregularities in the conduct of proceedings at the three court levels. On the contrary, Dr. Dávalos' evidence shows that all correct procedures were observed and that there was no bias on the part of any of the judges against the Claimant. In fact, the principal claim raised by the Claimants before the domestic courts concerned whether the each of the authorities involved in the decision-making process (the *Ayuntamiento*, the State Administrative Tribunal and, ultimately, the Superior Chamber of the State Administrative Tribunal) had acted in accordance with fundamental rights embedded in the Mexican Constitution, namely: the right to be heard; the observance of due process; the obligation of authorities to set forth the rationale for their acts and cite applicable law; and the prohibition of taking justice into one's own hands. Each of the courts confirmed that these principles had been fully observed throughout the nullification and judicial proceedings.

241. In this regard, the Respondent observes that the State Administrative Tribunal made rulings against the Municipality (in declining to accept additional evidence of Dr. Palacios' criminal complaint against Mr. Goldenstein, for example). There is no evidence of a denial of justice.

242. The fact that the Respondent was <u>not</u> required to make radical changes to its judicial system as a condition of its participation in NAFTA gives rise to a presumption of compliance with international law. In the NAFTA, the Respondent, Canada and the United States agreed to certain changes to their domestic legal systems, but only in respect of specific amendments to laws as identified in the NAFTA[136].

135. *The International Responsibility of States for Denial of Justice,* Alwyn V. Freemen (1938) Reprinted 1970.

136. See, for example, Annex 1904.15, which deals with required amendments to the national anti-dumping and countervailing duty laws of Mexico, Canada and the United States.

243. The judgments of the three courts also do not give rise to an international wrong on the part of the Respondent. Moreover, insofar as they are concerned with the correct interpretation and application of municipal law, they cannot have an international character except in limited circumstances.

244. There is no evidence, direct or circumstantial, of bad faith on the part of the Respondent's judiciary in any of the proceedings. In his judgment in *Barcelona Traction*, Judge Tanaka held that there had to be "*objective facts* constituting collusion, corruption, and flagrant abuse of judicial procedure, in order to enable the International Court of Justice to make a finding of bad faith. Furthermore, bad faith could not be presumed"[137].

245. On these grounds alone, there is no basis for the Claim. That being said, the Respondent will also show that no breach of Articles 1105 and 1110 can be sustained.

2. Article 1105: Fair and Equitable Treatment and Full Protection and Security.

246. Article 1105 provides:

> "Each Party shall accord to investments of investors of another Party treatment in accordance with international law, including fair and equitable treatment and full protection and security."

247. The minimum standard of treatment incorporated in this Article is treatment "in accordance with international law". This standard of treatment can be divided into two express components, fair and equitable treatment and full protection and security, and one residual component, other standards of treatment mandated by international law.

a. Fair and Equitable Treatment

248. The phrase "fair and equitable treatment" is not defined in the NAFTA.

249. In accordance with Article 31 of the *Vienna Convention*, the phrase must be interpreted in good faith in accordance with its ordinary meaning, in its context, and in the light of its object and purpose.

250. The ordinary meaning of the word "fair" is "just, unbiased, equitable; in accordance with the rules" and the ordinary meaning of the word "equitable" is "fair and just"[138].

251. The meaning of "fair and equitable treatment" is clearer when viewed in its context. The qualifying words "in accordance with international law" in Article 1105(1) signify that the drafters' intention was to incorporate the public international law meaning of "fair and equitable

137. Case concerning the Barcelona Traction, Light and Power Company, Limited (Belgium v. Spain), second phase, separate opinion of Judge Tanaka, February 5, 1970, at page 160.
138. The Concise Oxford Dictionary of Current English (8th Edition).

treatment". Although the phrase is widely employed in bilateral investment treaties, there is no agreement as to the phrase's precise meaning. Interpretations include:

- The Claimants were not denied fair and equitable treatment. All actions of the Respondent in this matter, when assessed in the light of all relevant facts and circumstances, were taken in good faith and reasonable, without abuse, arbitrariness or discrimination.

- It is beyond dispute that the three principals of DESONA B grossly misrepresented: (i) their relationship to Global and (ii) their own personal and the company's experience and financial capability to the *Ayuntamiento.*

- Six months *before* the concession was granted, Global was in bankruptcy. This was not disclosed to the *Ayuntamiento*.

252. At the November 4, 1992 meeting, Mr. Goldenstein outlined grandiose plans. In retrospect, it is now obvious that Global never had the financial capability to implement such plans.

253. When the concession entered into force and performance problems arose, they stemmed from the fact DESONA lacked the capital to purchase state-of-the-art trucks, pay import duties, hire staff, pay the existing staff of the municipality who were to be transferred to it, pay for fuel, and so on. It was trying to finance the concession "on the fly."

254. In this regard, the Memorial admits that the DESONA principals *knew* they did not have the resources to perform the public collection and residential service nor could they afford to buy the trucks. They knew this *before* they signed the contract.

255. When the new administration found out about these facts after DESONA showed it could not meet certain key obligations, in view of the mounting "waste crisis," to use DESONA's words, it acted responsibly in nullifying the concession. Indeed, having learned of the misrepresentations by the DESONA principals, it was under a legal obligation to nullify the concession. The Municipality's actions were fully justified. The Tribunal should take note of Mr. Hodge's independent evidence that he observed in early January 1994 that DESONA was "seemingly desperate for capital".

256. Its decision was subsequently upheld by the courts.

b. Full Protection and Security

257. The phrase "full protection and security" is not defined in the NAFTA. In accordance with Article 31 of the *Vienna Convention*, the phrase must be interpreted in good faith in accordance with its ordinary meaning[139], in its context, and in the light of its object and purpose.

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139. The ordinary meaning of the word "protect" is "keep safe, defend, guard" and the ordinary meaning of the word "security" is "a secure condition, a thing that guards or guarantees". *The Concise Oxford Dictionary of Current English* (8th Edition).

258. As in the case of "fair and equitable treatment", the qualifying words "in accordance with international law" in Article 1105(1) signify that the drafters intended to incorporate the public international law meaning of "full protection and security".

259. Under public international law principles, the obligation to provide "full protection and security" does not make the state absolutely liable for injuries inflicted upon the foreign property[140]. In *Asian Agricultural Products Ltd. v. Republic of Sri Lanka (AAPL)*, the ICSID Tribunal stated:

> "The Arbitral Tribunal is not aware of any case in which the obligation assumed by the host state to provide nationals of the other Contracting State with "full protection and security" was construed as an absolute obligation which guarantees that no damages will be suffered..."[141]

260. A state which exercises due diligence, even where the foreign property has suffered injury, will have discharged its obligation to provide full protection and security. A state complies with its due diligence obligation where it acts reasonably in the protection of foreign property[142].

261. It is manifestly clear that there are no facts present in the instant case to sustain a claim that the Respondent failed to accord full protection and security to DESONA.

c. Other Standards of Treatment Accorded by International Law

262. The minimum standard of treatment incorporated in Article 1105(1) includes all other standards of treatment afforded by customary international law.

263. The Claimants have not articulated any claim that DESONA was denied treatment in accordance with any other minimum standard established by international law.

3. Terminating a Concession for Poor Performance Does not Amount to an Expropriation

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140. Brownlie, in *System of the Law of Nations: State Responsibility (Part I)* (Oxford: Clarendon Press, 1983) at 171 (hereinafter, *System of the Law of Nations*) rejects the absolute liability theory:

> "[N]o state has been prepared to accept such a standard of liability as guarantor. Even capital-exporting states, such as the United States, were appreciative of the difficulties which face states coping with severe internal crises. In short, the theory of absolute liability was not mirrored in the practice of states".

141. *Asian Agricultural Products Ltd. v. Republic of Sri Lanka* (I.C.S.I.D.), (1991) 30 ILM 580 at 599-600. This rule follows the judgment of the International Court of Justice in *Case Concerning Elettronica Sicula S.p.A (ELSI)* (United States v. Italy), 1989 ICJ 15. In *ELSI*, the ICJ had to determine whether the term "most constant protection and security" contained in a Treaty of Friendship, Commerce and Navigation between Italy and the United States made Italy absolutely liable for any damage occurring to the property of the Raytheon Corporation. The ICJ rejected such an interpretation finding instead that:
"The reference in Article V ["most constant protection and security"] cannot be construed as the giving of a warranty that property shall never in any circumstances be occupied or disturbed."

142. Lillich, *op. cit.* at page 232.

264. Insofar as expropriation is concerned, the issue is whether the Respondent's decision to nullify the concession held by one of the versions of DESONA, a concession that was manifestly obtained by gross misrepresentation, whose nullification occurred after a failure to perform the contract of concession, with informal and formal notice given to the contractor following administrative practice, all of which was subsequently upheld by three different domestic courts, constitutes an expropriation under NAFTA Article 1110.

265. It is well-established in international law that a state's decision to terminate a concession on the grounds that the concessionaire has failed to perform it adequately does not constitute an expropriation.

266. The Claimants cite Section 712(2) of the Restatement (Third) of Foreign Relations Law of the United States which states:

> "A state is responsible under international law for injury resulting from…
>
> (2) a repudiation or breach by the state of a contract with a national of another state
>
> (a) where the repudiation or breach is (i) discriminatory; or (ii) motivated by noncommercial considerations, and compensatory damages are not paid; or
>
> (b) where the foreign national is not given an adequate forum to determine his claim of repudiation or breach or is not compensated for any repudiation or breach determined to have occurred."

267. In the Respondent's submission, this section of the *Restatement* is generally consistent with the approach taken by international tribunals. The Tribunal will note that the *Restatement* does not hold that all contract terminations by a state constitute expropriations. Rather, it contains important provisos necessary to establish an expropriation. These are not present on the facts of this case.

268. One of the indicia of an expropriation is the absence of domestic legal remedies. As seen above, that indicator is absent in this case.

269. A second indicator is evidence of discrimination. On the facts of this case, there is no evidence whatsoever to support the contention that the municipality acted discriminatorily. The evidence is overwhelming that Global/DESONA lacked the capacity to perform the concession and that its principals grossly misled the *Ayuntamiento* as to their experience and that of the company they have claimed to have controlled, Global Waste Industries.

270. A third indicator of expropriation is noncommercial motivation: Was the contract's termination motivated by concerns about poor or non-performance of key obligations and material misrepresentation, or for extrinsic non-commercial considerations?

271. It is submitted that the evidence of material —indeed fraudulent— misrepresentation is overwhelming. As for the failure to perform, as the waste piled up in public places and DESONA tried to convince Municipal officials that thirteen-year-old rebuilt garbage trucks were "state-of-the-art", the officials concluded that non-performance was going to remain a problem.

272. The officials' view was shared by two independent parties, Mr. Hodge and Mr. Maphis.

273. The officials' doubts were given further substance by their discovering the truth about Global's bankruptcy and the misrepresentations that had been made to the former *Ayuntamiento.*

274. The court proceedings all rejected DESONA's claim and upheld the municipality's actions as justified by the company's material misrepresentations and its inadequate performance of the concession.

275. DESONA sought, and was granted, a hearing before the *Ayuntamiento.* Mr. Goldenstein abruptly left the meeting when the Sánchez brothers and Dr. Palacios were permitted to make statements to the council.

276. The Claimants allege further that the termination was not motivated by concerns over performance, but rather a desire to assign the concession to a Mexican company, Tribasa.

277. Mr. Piazzesi's testimony is that, contrary to the Memorial's speculation that the Mexican company, Tribasa, was to have profited from the nullification by stepping into DESONA's place, after its experience with DESONA and given the urgency of the problem, the municipality decided to borrow funds to acquire new trucks and has maintained a publicly provided service ever since it nullified the concession. Thus, no other private firm benefited from the decision to nullify the concession.

278. DESONA entered into the contract of concession fully aware of the fact that the source of the income for its operations was insufficient to sustain the expenditures that it had to make under the contract.

279. DESONA was unable to provide the trucks that it represented it would provide and according to the schedule that was set out in the concession annex.

280. Its need for financing was evidenced by the fact that the three principals entered into the BFI agreement representing that they owned 100% of the shares of the company when by virtue of the concession they were obliged to set aside 10% of the shares.

281. There was nothing expropriatory in the Respondent's conduct

Relief Requested

282. In these circumstances, the Respondent requests that the Claim be dismissed with an award of costs payable to the Respondent.

PART IV: DEFENSE TO THE CLAIM FOR DAMAGES

A. Introduction

283. The Claimants have failed to meet the burden of proof in asserting their claim for damages. They have failed to produce any documentary evidence in support of their revenue and cost projections relied on by their expert witnesses. Similarly, they have neglected or refused to provide any documentary support for the expenditure they claim to have incurred or their claims that they have invested "hundreds of thousands of dollars" in DESONA. Indeed, the only documentary evidence that has been adduced in this proceeding shows that the expenditure the Claimants say they incurred was actually incurred by others – Mr. Sanchez as to the sum of 10,000 dollars for the air fare and hotel expenses of the delegation that visited Los Angeles in January, 1992 and Dr. Palacios as to the sum of 300,000 dollars for cash and steel containers that he contributed as his investment in DESONA I.

284. There is no cogent evidence of the fair market value of DESONA. The Ernst & Young ("E & Y") "Summary of Value Indicators" (the "E & Y report") is not expert opinion evidence of value. According to its own terms (and its numerous limiting caveats) it is nothing more than a discussion paper as to what DESONA might be worth if the assumed facts – the revenue and cost projections supplied by Mr. Goldenstein – were true. However, these assumed facts are not in evidence. The "limited scope analysis" prepared by Richard R. Carvell (the "Carvell report"), which is based on the E & Y report and the same assumed facts, suffers from the same fatal flaw. Likewise, the Sanifill conditional offer to purchase DESONA lacks cogency because the revenue and cost projections upon which it is premised are not disclosed. As will be demonstrated below, the evidence shows that the revenue and cost projections Mr. Goldenstein supplied to E & Y and Carvell (and, one assumes, to Sanifill) are wholly unsupportable.

285. Mr. Goldenstein's revenue and cost projections are not supported by the evidence. Upon reviewing the evidence as a whole it can be seen that:

a) the projection that DESONA would have achieved 100% market penetration in the industrial and commercial sectors (and would have done so within one year) fails to pay any regard to the fact that there were 200 waste collection operators in Naucalpan at the material times.

b) the projection that DESONA would have performed its residential waste collection obligations on a break even basis is contradicted by the fact that DESONA was only being paid an amount equal to the Municipality's annual waste collection budget which, the Claimants allege and the Respondent admits, was insufficient to purchase any new equipment, let alone the 70 state-of-the-art trucks that DESONA undertook to supply in the first year of the contract;

c) the projection that DESONA would have earned 8.4 million dollars in annual revenue against expenses of 71% of revenue from operating the landfill fails to take into account that the fact that:

i) the concession contract contemplates that landfill tipping fees will be established on a cost recovery basis;

ii) applicable municipal law requires that landfill dumping fees would require the express approval of the *Ayuntamiento,* and

iii) the great majority of the dumping fees would have been payable by DESONA itself, if, according to Mr. Goldenstein's purported expectations, it were to become the depositor of 100% of Naucalpan's industrial and commercial waste.

d) the projection that DESONA would have earned over 7 million dollars in annual revenue against expenses of 65% of revenue for the sale of recyclable materials fails to take into account that the Rincón Verde landfill (like most others in Mexico) is the home and livelihood of a society of *pepenádores* who traditionally have collected and sold all of the reusable material entering the landfill, a fact the Claimants themselves acknowledge in a draft business plan that states they expect no profit on recycling activities.

286. Sanifill's conditional offer to purchase DESONA is not cogent evidence of DESONA's fair market value. The evidence shows that Sanifill actually purchased DESONA's industrial and commercial waste collection operation which had operated in a subsidiary known as King Kong, S.A. de C.V., which company continues to operate in Naucalpan, although apparently now under new ownership. The Respondent submits that the purchase price of DESONA's industrial and commercial waste collection operations, which was not divulged by the Claimants in the Memorial or in response to the Respondent's Motion for Directions would demonstrate that Sanifills conditional offer does not reflect fair market value as at the date of expropriation.

287. Arbitral tribunals in international proceedings have been reluctant to use the discounted cash flow ("DFC") method of assessing going concern value for companies that are not a going concern or that have been in business for less than two years. In the circumstances of this case— where the Claimants have refused to produce the business records which demonstrate their actual business revenues and expenses— the DCF method is even less appropriate. The Tribunal should look to an alternate method of assessing DESONA's fair market value, such as net asset value. Regrettably, the Claimants have also refused to disclose information that would allow the Respondent or the Tribunal to sensibly make such an assessment. The Respondent thus submits that the claim for damages should be dismissed.

B. Failure to Meet the Burden of Proof

288. The Claimants allege that they have invested "hundreds of thousands of dollars" in DESONA. They also contend that the fair market value of DESONA, immediately prior to the nullification of the concession, was 19.46 million dollars.

Alleged "Pre-Nullification" Investment

289. The only documentary evidence the Claimants have adduced in support of their allegation that they made a direct financial investment is a Guaranty and Security Agreement in favor of

BFI, purportedly to secure a loan of 100,000 dollars to DESONA; four check stubs totaling 100,000 dollars, drawn on the account of Western Waste Management ("Western Waste"), that do not disclose the name of the payees; and a series of fee accounts totaling765,970 dollars, issued to DESONA by BAS, that do not disclose any details of the services allegedly rendered.

290. Significantly, notwithstanding the Respondent's repeated requests to produce receipts for expenses allegedly incurred, documentary proof of money or goods contributed to DESONA, and written evidence of personal liability for sums allegedly owing to BAS and Western Waste, the Claimants have neglected or refused to produce a single cancelled check, deposit slip, bank statement, credit card statement, invoice, receipt, tax return, financial statement, ledger, guaranty agreement, demand letter, or any other document containing proof that any of the Claimants spent money or incurred expenses or liabilities in connection with DESONA or the concession. The one set of invoices produced by BAS are of a dubious nature given the relationship between Mr. Stirrat, BAS, and the Claimants.

291. The Respondent refers to its Request for Particulars and Request for Production of Documents issued on April 1, 1998 and to its Motion for Directions issued on June 8, 1998. The Tribunal will recall that:

a) In response to the Respondent's request for documentary proof of the expenses the Claimants claim to have incurred in connection with the January 1992 visit to Los Angeles of an eleven-member delegation from the Municipality (and the rest of the Claimants' so-called "pre-nullification investment"), the Claimants, having stated that in the Memorial that these were among financial records that are "too voluminous to produce", declined to comply on the grounds that such documents "may be in storage and may be in Mexico."[143]

b) In fact, documentary evidence adduced by the Respondent clearly shows that the majority of the expenses connected with the Los Angeles trip were borne by Emilio Sánchez on the Claimants' unfulfilled promise that he would be reimbursed.

c) In response to the Respondent's request to produce DESONA's basic accounting records – such as financial statements, tax returns and daily journal for 1993 and 1994 – to enable to Respondent to assess the value or DESONA in accordance with its actual financial performance, the Claimants declined to comply stating "these are collateral issues only and are difficult if not impossible to locate or reconstruct."[144]

d) In response to the Respondent's request for particulars of the money that each of Mr. Azinian, Mr. Davitian and Mr. Goldenstein invested in the concession project and the manner in which such investment occurred, the Claimants complained,

143. See Motion for Directions dated June 9, 1998, paragraphs 23 to 31.
144. Ibid, paragraphs 33 and 34.

inter alia, that the request was for "irrelevant material that is not an issue before the tribunal and is burdensome and oppressive in nature".[145]

e) In fact, documentary evidence adduced by the Respondent clearly shows that Dr. Oscar Palacios invested money and goods (steel waste containers) having a total value exceeding 300,000 dollars in the concession project – then held by DESONA I – but that the Claimants failed to make their pro-rata contribution of capital, or any contribution, when called upon to do so after the grant of concession was ratified by the State Legislature.

292. In the result, the only documentary evidence indicating that expenses were incurred or money (or money's worth) was invested in any of the versions of DESONA or in the concession project comes from two Mexican citizens, Mr. Sanchez and Dr. Palacios, both of whom complain that they have been cheated by the Claimants. It is proper for the Tribunal to infer, in the face of the Claimants' refusal to produce documentary evidence, that the Claimants' allegations that they incurred expenses and invested money or (money's worth) in DESONA or the concession are false and unsupportable. In any event, in these circumstances, it would be proper for the Tribunal to find that the Claimants have failed to meet the burden of proving that they made any "pre-nullification investment" or that any of them contributed any capital that qualifies as an "investment" within the meaning of that term in Article 1139 of the NAFTA.

Alleged Guarantee of DESONA's Debt to BFI

293. As to the Claimant's allegation that they (excluding Ms. Baca) are indebted to BFI in the sum of 350,000 dollars (plus interest) for personal guarantees of loans to DESONA, the Respondents note that:

a) the only documentary evidence submitted by the Claimants indicates that they personally guaranteed a loan of 100,000 dollars from BFI to DESONA and that they purported to pledge 15% of the share capital in DESONA as additional security for the loan;

b) there is no documentary evidence indicating that funds were advanced to DESONA, that the funds advanced (if any) were expended in connection with the concession, that the funds advanced (if any) were never repaid, that BFI has demanded payment of the amount the Claimants allege is, or that any amount is actually due and owing by the Claimants to BFI;

c) BFI has declined to answer the inquiries of counsel for the Respondents as to amounts advanced, amounts owing, details of any settlement reached between BFI and the Claimants, or the disposition of any DESONA shares pledged as additional security for the primary debt.[146]

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145. Ibid, paragraphs 47 and 51.
146. See Affidavit of Mr. J. Cameron Mowatt, paragraphs 2 to 11.

294. In view of the Claimants' failure to supply proper details and documentary support of their alleged debt to BFI and the disposition of funds (if any) that DESONA received from BFI, it would be proper for the Tribunal to infer that the Claimants' allegation that they are personally indebted to BFI in the sum of 736,251 dollars (inclusive of interest) is unsupportable. In any event, in these circumstances, it would be proper for the Tribunal to find that the Claimants have failed to meet the burden of proving that they are liable to pay any amount, pursuant to personal guarantees they gave to BFI, that qualifies as an "investment" within the meaning of that term in Article 1139 of the NAFTA.

Alleged Guarantee of DESONA's Debt to Western Waste Industries

295. As to the Claimants' allegation that they (excluding Ms. Baca) are personally indebted to Western Waste in the principal sum of 100,000 dollars, the Respondent notes that:

a) notwithstanding the Claimants' testimony that they "signed personal guarantees" in favor of BFI and Western Waste, their response to the Respondent's request for particulars states that their liability arises only upon Mr. Azinian's oral undertaking to be personally liable to repay a loan for which no documentary evidence has been adduced other than check stubs that do not identify the payee;[147]

b) the Claimants' alleged personal guarantees (made orally on their behalf by Azinian) do not satisfy the requirement of Section 1624 ("Statute of Frauds") of the California Civil Code for a written memorandum signed by the party to be charged[148];

c) there is no documentary evidence indicating that funds were advanced to DESONA, that the funds advanced (if any) were expended in connection with the concession, that the funds advanced (if any) were not repaid, or that Western Waste has demanded payment from the Claimants or any of them;

296. In view of the Claimants' failure to supply proper details and documentary support of their alleged debt to Western Waste and the disposition of funds (if any) that DESONA received from Western Waste, it would be proper for the Tribunal to infer that the Claimants' allegation that they (excluding Baca) are personally indebted to Western Waste in the sum of 100,000 dollars (or any sum) is unsupportable. In any event, in these circumstances, it would be proper for the Tribunal to find that the Claimants have failed to meet the burden of proving that they are liable to pay any amount, pursuant alleged personal guarantees they gave to Western Waste, that qualifies as an "investment" within the meaning of that term in Article 1139 of the NAFTA.

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147. Claimants' response to Request for Particulars. See Exhibit 17.

148. Section 1624 of the California Civil Code contains the 'Statute of Frauds' requirement that certain types of contracts be evidenced in writing, among them Contracts of Guaranty.

Alleged Guarantee of DESONA's Debt to BAS

297. As to the Claimants' allegation that they are indebted to BAS in the sum of765,970 dollars, the Respondent notes that:

a) all of the BAS invoices (the single invoice exhibited in the Memorial and the individual invoices produced at the Respondents request) are addressed to DESONA, not the Claimants;

b) there is no written memorandum signed by the party to be charged or other any other documentary evidence indicating that the Claimants agreed to be personally liable for DESONA's debt to BAS;

c) Mr. Stirrat, after offering to answer written questions submitted by the Respondent, announced at the eleventh hour that he believes his affidavit adequately addresses the matters raised in the Respondents written questions and that he "never intended to become a shareholder nor acquire any interest in DESONA"[149];

298. Among the questions Mr. Stirrat was asked to answer were the following:

a) Did you and/or Stirrat & Associates ever have any formal or informal agreement with DESONA, or any of its principals, to hold a direct or indirect ownership interest in DESONA or in the concession itself?

b) Did you and/or Stirrat & Associates ever expect to receive a share of the earnings, profits or other revenues of DESONA, or of the concession itself? If so, please provide details.

c) Is there a written agreement between Stirrat & Associates and DESONA (or Global, or any of its principals) concerning payment for services rendered by your company in connection with the concession ? If so, please provide a copy.

d) If the agreement was oral, what were its terms?

e) Is there a written agreement between Stirrat & Associates and Azinian, Goldenstein and Davitian requiring Azinian, Goldenstein and Davitian to personally guarantee any debts of DESONA to Stirrat & Associates?

f) If their agreement to do so was oral, what were the terms of such agreement?

g) Has Stirrat & Associates made any demand or taken legal action to enforce any debt, covenant, or other obligation owed to it by DESONA, or Global, or Azinian, Davitian, and/or Goldenstein?

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149. See Affidavit of Mr. J. Cameron Mowatt, Exhibits "I" and "L."

h) Your statement indicates that Stirrat & Associates first began to provide services in July 1992. Did Stirrat & Associates expect to be paid by DESONA (or Azinian, Goldenstein or Davitian) for work done in the event that the concession was not ultimately awarded to DESONA?

i) Do you or Stirrat & Associates have any financial interest in the outcome of this litigation other than payment of the outstanding account for services rendered in connection with the concession? If so, please explain[150].

299. The evidence of Mr. Hodge, and documents provided by Mr. Maphis,[151] indicate that Mr. Stirrat had a financial interest in DESONA or, if not, that he intended to acquire an interest in an enterprise that would have a direct financial interest in the concession.

300. In the view of the Claimants' failure to adduce documentary evidence supporting their contention that they are personally liable to BAS, and in view of Mr. Stirrat's refusal to answer questions concerning BAS's contractual and other relations with DESONA and the Claimants, and in view of Mr. Stirrat's apparently misleading response to the Respondent's inquiry as to whether he or BAS had or expected to have a financial interest in DESONA, the concession or the profits of the concession, it would be proper for the Tribunal to infer that the Claimants' allegation that they are personally liable for services rendered to DESONA by BAS is unsupportable. In any event, it would be proper for the Tribunal to find that the Claimants have not discharged the burden of proving that they are personally liable to BAS for the amount claimed (or any amount) or that such liability falls within the definition of "investment" under Article 1139 of the NAFTA.

C. Failure to Adduce Cogent Evidence of DESONA's Fair Market Value

301. In order for expert opinion evidence to be admissible and have probative value it must consist of an opinion, within the witness' scope of expertise, based on:

a) facts within the expert's knowledge by reason for his or her expertise in a particular subject;

b) facts that the expert has determined through independent inquiry and application of his or her expertise in a particular subject; or

c) facts that are established in evidence in the proceeding.

302. Neither the E & Y report nor the Carvell report meet this test for the simple reason that the primary factual assumptions as to projected revenue and costs that they rely on were supplied by DESONA management. These facts were not independently verified by E & Y or Mr. Carvell, nor have they been adduced in evidence in this proceedings. Simply put, there is <u>no</u> proper factual foundation for either opinion.[152]

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150. Ibid. Exhibit "K"
151. See Affidavit of Mr. J. Cameron Mowatt, Exhibits "S" and "T".
152. With regard to the inadequacy of the E&Y report, see Expert Report of David A. Schwickerath, Annex V.

303. It is clear that neither E & Y or Mr. Carvell independently examined DESONA's actual costs and revenues during the period that it provided industrial and commercial waste collection services in Naucalpan, nor did either of them investigate the market conditions in Mexico to assess costs that DESONA could be expected to incur. Instead, their opinions are purely hypothetical, based solely upon assumed facts which have been fed to them by Mr. Goldenstein.[153] Indeed, it is evident that E & Y invited Mr. Goldenstein to "fill in the blanks" in their spreadsheets.[154] As will be discussed in some detail below, the evidence in this proceeding shows that the revenue and cost projections that Mr. Goldenstein instructed E & Y and Mr. Carvell to assume are wholly unsupportable .

304. In view of the Claimant's refusal to provide its experts with its basic accounting records and its refusal to provide such records to the Respondent after being requested to produce such documents so that the Respondent could make its own assessment of fair market value based on DESONA's actual revenues and operating costs, it would be proper for the Tribunal to infer that DESONA's business records do not support the assumptions that Mr. Goldenstein instructed E & Y and Mr. Carvell to rely on.

D. DESONA's Revenue and Cost Projections are Refuted by the Evidence

Industrial and Commercial Waste Collection Revenues

305. It is evident from reviewing the documents supplied by E & Y in response to the Respondent's request for production of documents that, not only did Mr. Goldenstein "fill in the blanks" on the E & Y spreadsheets, he instructed E & Y to assume that, by January 1, 1995, DESONA would have captured 100% of the industrial and commercial waste collection market in Naucalpan.[155] This assumption is unrealistic for the following reasons:

a) there were over 200 independent waste collection operators in Naucalpan at the material time;[156]

b) it is completely at odds with DESONA's actual operating capacity which, the evidence shows, consisted of only two front load garbage trucks that DESONA was able to import after the Municipality paid the applicable import duties.

306. DESONA's draft business plan indicates that the Claimants anticipated achieving 75% market penetration with two years. Although still questionably optimistic, this is considerably less than the 100% predicted by Mr. Goldenstein.

153. See Memorandum from Mr. Ariel Goldenstein to Tony Aaron dated 8 July 1994. See Exhibit 39.
154. Memorandum from J.R. Ahn to Mr. Ariel Goldenstein dated 9 July 1994. See Exhibit 40.
155. See Exhibit 39. 8 July 1994 Memorandum from Mr. Goldenstein to Aaron.
156. Witness Statement of Mr. Francesco Piazzesi.

Residential Waste Collection Revenues

307. As to residential waste collection revenues, the E & Y report acknowledges that there would be a loss.[157] The fact is that DESONA was only being paid the Municipality's annual waste collection budget which, the Claimants allege and the Respondent admits, was insufficient to pay for any new equipment let alone the 70 "state-of-the-art" garbage trucks that DESONA was obliged to supply. Accordingly, it is obvious that the residential waste collection would be operated at a loss until the cost of the new trucks was fully absorbed.

308. Judging from the cost of the trucks that the Claimants ordered from McNellus the day after the Municipality nullified the concession contract, an additional expense of approximately 5 million dollars would have been incurred. According to the Claimants, these trucks cost between 60,000 and 80,000 dollars per unit.[158] At an average price of 70,000 dollars the acquisition of 70 state-of-the-art trucks, would have resulted in additional expenditures of 4.9 million dollars (plus duty and delivery costs) in the first year of the contract.

Landfill Revenues

309. As to landfill revenues, it is to be noted that:

a) the concession contract contemplates that the landfill tipping fee would be established on a cost recovery basis;[159]

b) applicable municipal law requires that landfill tipping fees have the express approval of the *Ayuntamiento*;[160] and

c) the vast majority of the tipping fees would have been payable by DESONA if, in accord with Mr. Goldenstein's purported expectations, it became the depositor of 100% of Naucalpan's industrial and commercial waste.

310. It can thus be seen that any "profit" to be derived from landfill operations would depend entirely on the willingness of the *Ayuntamiento* to allow a fee structure that would generate revenue in excess of DESONA's costs. Moreover, and most importantly, DESONA would be responsible for paying tipping fees out of its revenue for commercial and industrial waste collection services. These charges also had to be approved by the *Ayuntamiento* in accordance with the terms of the concession contract and applicable municipal law. Accordingly, the amount would either appear as an additional cost in the industrial and commercial waste collection business, or as a reduction in revenue in the operation of the landfill. In any case, the

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157. E&Y, in its list of "assumptions," notes that "Desona will provide this service as a goodwill gesture". See Exhibit 40.

158. See the Claimants' Response to the Respondents ' Request for Particulars (undated) at page 9, ref: "Section 3, page 60".

159. See Operations Program, Memorial, Section 3, page 40 (English version).

160. Article 53 of the Regulation for Operation and Disposal of Solid Waste in the Municipality of Naucalpan, State of Mexico (published in the Municipality Gazette dated 15 December 1992) states that: "the concessionaire in the handling of waste will collect the fees authorized by the *Ayuntamiento* for the services that it provides".

figure that E & Y was instructed to adopt is grossly exaggerated. The truth can be found in DESONA's draft business plan which provides in part as follows:

> "The revenues from the landfills will be kept by the operator, DESONA. However, residential refuse collected by the vehicles of DESONA for all residents of Naucalpan will not have any tariff. That is, the residents will dump free in the landfill. Additional revenues from commercial, industrial, and others will belong to DESONA. It is anticipated that a mutual agreement with the Municipality will be required to establish a rate schedule. The rate schedule will be based on documented cost of operations, including closure, post-closure, leachate treatment, and other environmental needs. The study should present that." [Emphasis added][161]

Recycling Revenues

311. As to the assumption that DESONA would have enjoyed 7 million dollars in annual revenue from recycling (against expenses of 40% of revenue) it is instructive to refer again to DESONA's draft business plan which states the following:

> "The landfill operations were assumed by DESONA in December of 1993. The existing practices and operations are being continued. It is practically impossible to change the operations without first addressing the issue of Pepenadores. The Pepenadores Union and DESONA have carried on discussions and are in agreement in general direction for this operation. DESONA will construct a Materials Recovery Facility (MRF). The MRF will employ Pepenadores for sorting through refuse and recycling that which can be pulled out. They will be doing essentially the same activity that they did on the surface of the landfill. However, now these activities will be carried out in a facility which will be maintained from a health and safety standpoint. It will be under roof. It is hoped that the sanitary conditions will have a positive effect on the Pepenadores. A Day Care Center is also planned to allow the children to be taken care of rather than running loose on the landfill as they currently do. All of the refuse will be diverted through the MRF area. That which has no salvageable component may go directly to the landfill after being waved on by a member of the Pepenadores Union. There will be no attempt to reduce the supply of waste to the MRF. The residual of the operation will then be transported to the landfill for proper disposal. The Pepenadores will receive, as they do today, all the proceeds from the operation. However, it is hoped that DESONA will provide some assistance in perhaps obtaining better pricing for the recycled materials." [Emphasis added][162]

312. It is clear, beyond doubt, that DESONA expected the recycling operation would be revenue neutral. This is completely in accord with the reality of the fact that the *Pepenadores*, who have resided at the landfill and have relied on it as their sole source of income throughout its entire existence, would have to be accommodated by any new landfill operator.

Bio-Gas Generation or Co-Generation Revenues

313. The concession contract provides for possibility of establishing either electricity generating plant fueled solely by methane gas generated by the landfill (the bio-gas plant) or a plant which would generate electricity utilizing a combination of methane gas and natural gas supplied by pipeline (a co-generation plant). In the latter case there was provision for

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161. See Affidavit of Mr. J. Cameron Mowatt, Exhibit "V", page V-2.
162. Ibid, page II-3.

contribution of a portion of the sale proceeds of the electricity to pay for the Municipality's waste collection and disposal services, as originally intended when the concession was approved by the *Ayuntamiento* in November, 1992.

314. Known to Mr. Goldenstein and the other Claimants, Sunlaw de México concluded after extensive study that it was not technically or economically feasible to establish a bio-gas generating facility at the landfill nor, then or for the foreseeable future, was it economically feasible to establish a co-generation facility.

315. The Respondent thus submits that Mr. Goldenstein's revenue projections in connection with phase 4A and phase 4B have no realistic basis for fact.

E. The Sanifill Offer – Lack of Probative Value

316. The Claimants purport to rely on a conditional offer to purchase DESONA that was made by Sanifill on May 17, 1994 as evidence of DESONA's fair market value. The offer is conditional upon DESONA resurrecting its relationship with the Municipality and upon Sanifill conducting a satisfactory "due diligence" investigation.

317. The Respondent has adduced evidence that Sanifill actually purchased DESONA's industrial and commercial waste collection operation which it operated through a company known as King Kong S.A. de C.V. ("King Kong") until recently. The Respondent's evidence further indicates that King Kong continues to provide industrial and commercial waste collection services in Naucalpan.[163]

318. In its motion for directions dated June 8, 1998, the Respondent asked the Tribunal to direct the Claimants to disclose the details of the sale to Sanifill. Although the Tribunal elected not to issue further directions, stating that each party was responsible for the content of its pleadings, it is submitted that the Claimant has willfully concealed the fact that it recovered all or part of the value of the business it established in Naucalpan upon selling its equipment and customer contracts to Sanifill.[164]

319. The Respondent submits that the Claimants' failure to disclose the terms of sale of DESONA's industrial and commercial operations to Sanifill (let alone its failure to mention the existence of the transaction in the Memorial) should be treated with great suspicion. Equally, the failure of the Claimants to include in the evidence the representations made to Sanifill in eliciting the offer to purchase should be treated with suspicion. Clearly, if Sanifill was operating under the same revenue and cost projections that were given to E & Y and Mr. Carvell, the offer would be meaningless and have no probative value.

F. Method of Valuation

320. Other than stating that "valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine

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163. See the witness statement of Francesco Piazzesi, paragraph 78.

164. See Motion for directions dated June 8, 1998, paragraphs 71 to 74.

fair market value", Article 1110 does not dictate the method by which "fair market value" shall be determined. The Respondent submits that "fair market value" is to be determined according to the most appropriate method of valuation and does not necessarily mean that the expropriated enterprise will be valued as a going concern as the Claimants insists, particularly where the Claimants have refused to divulge any financial information for the four month period that it operated under the concession contract or the additional period that it carried on an industrial and commercial waste collection business after the concession was nullified.

321. "Fair market value" is the "the price that a willing buyer would have paid to a willing seller for the asset on the date of the taking in circumstances in which each had good information, each desired to maximize his financial gain, and neither was under duress or threat".[165]

322. A summary of the methods used in recent ICSID and Iran-U.S. Claims Tribunal cases suggests that there are four basic valuation methods: (i) the book value method, (ii) the replacement value method, (iii) the liquidation value method, and (iv) the discounted cash flow ("DCF") method.[166]

DCF Method Is Inappropriate Where The Investment Is Not A Going Concern

323. The E & Y report and the Carvell report rely primarily on a discounted cash flow ("DCF") model to assess fair market value. The DCF method of valuation values an income-producing asset by estimating the cash flow that the asset would be expected to generate over the course of its life, and then discounting that cash flow by a factor that reflects the time value of money and the risk associated with the cash flow.

324. Since the DCF method of valuation is based on a calculation of all anticipated profits that the expropriated enterprise could have earned over its lifetime, it is appropriate only where the asset being valued was a "going concern" at the time of expropriation. Where it was not, an alternative method that more accurately yields the real "fair market value" of the asset is

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165. Friedman, P.D., and Wong, E., "Measuring Damages for the Deprivation of Income-Producing Assets: ICSID Case Studies" 6:2 ICSID Review – Foreign Investment Law Journal 400 (1991) at 404. See also, *Starrett Housing Corp. v. Iran,* Award No. 314-24-1, 16 Iran-U.S. C.T.R. 112 (1987), Final Award at paragraph 277.

166. Friedman, P.D., and Wong, E., "Measuring Damages for the Deprivation of Income-Producing Assets: ICSID Case Studies" 6:2 ICSID Review – Foreign Investment Law Journal 400 (1991) at 405. The authors suggest that the liquidation value method may be a specific application of the DCF method:
If an owner of an unprofitable enterprise could realize a greater sum from the sale of the individual assets comprising the enterprise than in its continued operation, assuming rational economic behavior, such owner would liquidate rather than continue to operate the enterprise. The cash flow which such an enterprise could be expected to generate would therefore simply be the price of each asset comprising the enterprise when sold off. No discount rate would need to be applied to the cash flow since one would assume that the sale of assets would take place in the immediate future (pages 406-7).
See also J.A. Westberg, *International Transactions and Claims Involving Government Parties: Case Law of the Iran-United States Claims Tribunal,* (Washington, D.C.: International Law Institute, 1991), page 211, fn.2.

appropriate.[167]

325. Both ICSID and Iran-U.S. Claims Tribunal panels have refused to apply the DCF method of valuation where they found that the expropriated enterprise was not a going concern and, therefore did not have a reasonable expectation of future profits which could be discounted using the DCF method of valuation. Criteria which indicate that the enterprise is not a going concern have included the following:

a) its appearing never to have gone into operation;[168]

b) its having only generated revenues for less than one year and having a project that was "in its infancy"[169];

c) its having only "the briefest past record of profitability";[170] and

d) its having a factory, which was neither fully equipped nor fully operational, such that any estimation of future profits, would be "highly speculative".[171]

326. One of the lengthiest discussions about whether compensation for expropriation should be based on a projected stream of future profits was in respect of a company formed to undertake shrimp farming which was destroyed as a result of a counter-insurgency operation by government forces. An ICSID Tribunal refused to award the owner of shares in the destroyed company compensation for either goodwill or loss of future profits, as neither "could be reasonably established with a sufficient degree of certainty".[172]

327. The Tribunal found that in order for there to be goodwill, there must be a presence in the market for at least two or three years. This was the minimum period needed in order to establish continuing business connections. Also during that period expenses would be incurred in

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167. S.K. Khalilian, supra. See also Gann P.B., "Compensation Standard for Expropriation", 23 *Columbia Journal of Transnational Law* 615 (1985) at 618-619 for a recitation, from R. Smith, "The United States Government Perspective on Expropriation and Investment in Developing Countries", 9 J. Transnatl L. 519-520 (1976), of the U.S. Department of State's perspective on the valuation of expropriated property, including its recognition, at page 618, that, "There may be circumstances in which application of this [going-concern - i.e. DCF] method is impracticable, or where it might operate unfairly - for example, where an investment has a limited history of operating results...." This perspective is also discussed in *Sola Tiles v. Government of the Islamic Republic of Iran*, 83 I.L.R. 460 (1987) at fn.18.

168. *Benevenuti et Bonfant v. People's Republic of the Congo*, 21 I.L.M. 740 (1980) at paras. 4.86-4.94. See also P.D. Friedland and E. Wong, supra at pages 408-411.

169. *Southern Pacific Properties (Middle East) Limited v. Arab Republic of Egypt*, 8:2 ICSID Review – Foreign Investment Law Journal 3328 (1993) at paragraphs 187-8.

170. *Sola Tiles v. Government of the Islamic Republic of Iran*, 83 I.L.R. 460 (1987) at paragraph 64.

171. *Phelps Dodge Corp. and Overseas Private Investment Corp. v. Government of the Islamic Republic of Iran*, 10 Iran-U.S. C.T.R. 121 (1986) at paragraph 30.

172. *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka*, 6:2 ICSID Review - Foreign Investment Law Journal 526 (1990) at paragraph 106, and generally, paragraphs 87-108. See also P.D. Friedman and E. Wong, Measuring Damages for the Deprivation of Income-Producing Assets: ICSID Case Studies, 6:2 ICSID Review - Foreign Investment Law Journal 400 (1991) at 419-421.

supporting management's efforts devoted to create and develop the marketing network of the company's products.

328. The possible existence of valuable "goodwill" becomes even more difficult to sustain with regard to a company, not only newly formed and with no record of profits, but also incurring losses and under-capitalized.

329. In *Asian Agricultural Products Ltd.*, the fact that the lost company had exported for the first time only two shipments of product to Japan before its farm was destroyed, did not sufficiently demonstrate in the Tribunal's opinion "a certain ability to earn revenues" in a manner that would justify considering it able to keep itself commercially viable as a source of reliable supply in the Japanese market.[173]

330. Furthermore, according to a well established rule of international law, the assessment of prospective profits required proof that:

> "they were reasonably anticipated; and that the profits anticipated were probable and not merely possible".[174]

Appropriate Valuation Criteria for DESONA

331. In this case, DESONA purported to carry on business, (i) as an industrial and commercial waste collection operator from November 17, 1993 until the date that it sold its industrial and commercial waste collection business to Sanifill; (ii) as a landfill operator from December 1, 1993 until March 21, 1994 when the concession was nullified; and (iii) as residential/public facility waste collection operator from December 15, 1993 until March 21, 1994.

332. As explained in detail above, the Claimants have refused to produce DESONA's basic accounting records – financial statements, tax returns, daily journal, and so on – making it impossible for the Respondent, or the Tribunal, to make any sort of reasonable assessment of DESONA's value (or potential value) as a going concern. Instead, the Tribunal is asked to find that DESONA had a fair market value of 19.46 million dollars, being the median of the various figures postulated by E & Y and Mr. Carvell that have been divined from revenue and cost projections that are inconsistent with the facts. The magnitude of the sum claimed defies common sense when taking into consideration the facts that:

a) DESONA was a start up company comprised of three individuals, two of whom had a history of business failures and only one of whom had any experience in the waste collection business;

b) it is evident (or can properly be inferred) that the Claimants did not make any significant capital investment in DESONA or the concession

173. *Asian Agricultural Products Ltd. (AAPL) v. Republic of Sri Lanka*, 6:2 ICSID Review - Foreign Investment Law Journal 526 (1990) at paragraphs 102-105.

174. Marjorie Whiteman, *Damages in International Law*, volume II (1937), page 1837.

c) DESONA did not have the capital (or access to capital) it needed to purchase the-70-state-of-the-art waste collection trucks it was obliged to supply under the concession contract, or to finance its day to day operations;

d) as at the date of alleged expropriation, DESONA was significantly in breach of its obligations under the concession contract, having failed:

    i) to supply 14 waste collection trucks that were then due to have been put in service;

    ii) to pay the wages of the municipal employees and the cost of operating municipal trucks that were transferred to DESONA to perform residential and public waste collection services;

    iii) to pay the costs of operating the landfill and rent due under the lease for the landfill.

333. The Respondent submits that, in the circumstances of this case, it would be appropriate to assess fair market value according to criteria other than going concern value. The possibilities include net asset value or "book value", a figure that in this case might approximate the Claimant's financial investment in DESONA. However, the Claimants have refused to adduce documentary evidence that would assist the Respondent, or the Tribunal, to assess DESONA's net asset value, or the amount of money (or money's worth), if any, that the Claimants contributed to DESONA. Rather, as noted above, the only evidence of specific expenses incurred or amounts of capital contributed comes from two Mexican citizens, Mr. Sanchez and Dr. Palacios. Indeed, Dr. Palicios testifies that the Claimants failed to make their capital contribution when called upon to make their promised pro-rata contribution to DESONA I after the State Legislature ratified the award of concession.

334. The Respondent respectfully submits that the Claimants, by their failure to adduce proper evidence of their alleged capital contributions, and by their refusal to produce DESONA's business records, have created a conundrum—they have prevented the Tribunal from undertaking a proper assessment of DESONA as a going concern, or from making a realistic assessment of its net asset value or, for that matter, its liquidation value. In all of the circumstances it is proper for the Tribunal to infer that DESONA's fair market value, whether assessed according to discounted cash flow, net asset value, liquidation value or by any other criterion, is negligible and any award of compensation for the alleged expropriation of DESONA should be assessed accordingly.

335. The Respondent further submits that the Claimant's damages, if any, or the fair market value of DESONA which they claim has been expropriated, should be reduced by the amount that Sanifill paid to acquire DESONA's industrial and commercial waste collection operations.