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Note: For the Decision of the British Columbia Supreme Court setting aside this award, United Mexican States v. Metalclad Corp., May 2, 2001, go to www.naftalaw.org.

IV. THE TRIBUNAL’S DECISION

[...]

3. NAFTA, Article 1110: Expropriation

40“NAFTA, Art. 1110 provides that '[n]o party shall directly or indirectly ... expropriate an investment ... or take a measure tantamount to ... expropriation ... except: (a) for a public purpose; (b) on a non-discriminatory basis; (c) in accordance with due process of law and Article 1105(1); and (d) on payment of compensation ....’ ‘A measure’ is defined in Article. 201(1) as including ‘any law, regulation procedure, requirement or practice’.

41“Thus, expropriation under NAFTA includes not only open, deliberate and acknowledged takings of property, such as outright seizure or formal or obligatory transfer of title in favour of the host State, but also covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host State.

42“By permitting or tolerating the conduct of Guadalcazar in relation to Metalclad which the Tribunal has already held amounts to unfair and inequitable treatment breaching Art. 1105 and by thus participating or acquiescing in the denial to Metalclad of the right to operate the landfill, notwithstanding the fact that the project was fully approved and endorsed by the federal government, Mexico must be held to have taken a measure tantamount to expropriation in violation of NAFTA, Art. 1110(1).

43“The Tribunal holds that the exclusive authority for siting and permitting a hazardous waste landfill resides with the Mexican federal government. This finding is consistent with the testimony of the Secretary of SEMARNAP and, as stated above, is consistent with the express language of the LGEEPA.

44“As determined earlier (see above, para. 30), the Municipality denied the local construction permit in part because of the Municipality's perception of the adverse environmental effects of the hazardous waste landfill and the geological unsuitability of the landfill site. In so doing, the Municipality acted outside its authority. As stated above, the Municipality's denial of the construction permit without any basis in the proposed physical construction or any defect in the site, and extended by its subsequent administrative and judicial actions regarding the Convenio, effectively and unlawfully prevented the Claimant's operation of the landfill.

45“These measures, taken together with the representations of the Mexican federal government, on which Metalclad relied, and the absence of a timely, orderly or substantive basis for the denial by the Municipality of the local construction permit, amount to an indirect expropriation.
46” The present case resembles in a number of pertinent respects that of Biloune, et al. v. Ghana Investment Centre, et al., 95 I.L.R.183, 207-210 (1993)\(^8\) (Judge Schwebel, President; Wallace and Leigh, Arbitrators). In that case, a private investor was renovating and expanding a resort restaurant in Ghana. As with Metalclad, the investor, basing itself on the representations of a government affiliated entity, began construction before applying for a building permit. As with Metalclad, a stop work order was issued after a substantial amount of work had been completed. The order was based on the absence of a building permit. An application was submitted, but although it was not expressly denied, a permit was never issued. The Tribunal found that an indirect expropriation had taken place because the totality of the circumstances had the effect of causing the irreparable cessation of work on the project. The Tribunal paid particular regard to the investor's justified reliance on the government's representations regarding the permit, the fact that government authorities knew of the construction for more than one year before issuing the stop work order, the fact that permits had not been required for other projects and the fact that no procedure was in place for dealing with building permit applications. Although the decision in Biloune does not bind this Tribunal, it is a persuasive authority and the Tribunal is in agreement with its analysis and its conclusion.

47” Although not strictly necessary for its conclusion, the Tribunal also identifies as a further ground for a finding of expropriation the Ecological Decree issued by the Governor of SLP on 20 September 1997. This Decree covers an area of 188,758 hectares within the 'Real de Guadalcazar' that includes the landfill site, and created therein an ecological preserve. This Decree had the effect of barring forever the operation of the landfill.

48” The Tribunal is not persuaded by Mexico's representation to the contrary. The Ninth Article, for instance, forbids any work inconsistent with the Ecological Decree's management program. The management program is defined by the Fifth Article as one of diagnosing the ecological problems of the cacti reserve and of ensuring its ecological preservation. In addition, the Fourteenth Article of the Decree forbids any conduct that might involve the discharge of polluting agents on the reserve soil, subsoil, running water or water deposits and prohibits the undertaking of any potentially polluting activities. The Fifteenth Article of the Ecological Decree also forbids any activity requiring permits or licenses unless such activity is related to the exploration, extraction or utilization of natural resources.

49” The Tribunal need not decide or consider the motivation or intent of the adoption of the Ecological Decree. Indeed, a finding of expropriation on the basis of the Ecological Decree is not essential to the Tribunal's finding of a violation of NAFTA, Art. 1110. However, the Tribunal considers that the implementation of the Ecological Decree would, in and of itself, constitute an act tantamount to expropriation.

50” In conclusion, the Tribunal holds that Mexico has indirectly expropriated Metalclad's investment without providing compensation to Metalclad for the expropriation. Mexico has violated Art. 1110 of the NAFTA.”

IV. QUANTIFICATION OF DAMAGES OR COMPENSATION

1. Basic Elements of Valuation

51” In this instance, the damages arising under NAFTA, Art. 1105 and the compensation due under NAFTA, Art. 1110 would be the same since both situations involve the complete frustration of the operation of the landfill and negate the possibility of any meaningful return on Metalclad's investment. In other words, Metalclad has completely lost its investment.

52” Metalclad has proposed two alternative methods for calculating damages: the first is to use a discounted cash flow analysis of future profits to establish the fair market value of the investment (approximately $90 million); the second is to value Metalclad's actual investment in the landfill (approximately $20-25 million).

53” Metalclad also seeks an additional $20-25 million for the negative impact the circumstances are alleged to have had on its other business operations. The Tribunal disallows this additional claim because a variety of factors, not necessarily related to the La Pedrera development, have affected Metalclad's share price. The causal relationship between Mexico's actions and the reduction in value of Metalclad's other business operations are too remote and uncertain to support this claim. This element of damage is, therefore, left aside.
54”“Mexico asserts that a discounted cash flow analysis is inappropriate where the expropriated entity is not a going concern. Mexico offers an alternative calculation of fair market value based on COTERIN's 'market capitalization'. Mexico's 'market capitalization' calculations show a loss to Metalclad of $13-15 million.

55”“Mexico also suggests a direct investment value approach to damages. Mexico estimates Metalclad's direct investment value, or loss, to be approximately $3-4 million.

56”“NAFTA, Art. 1135(1) (a), provides for the award of monetary damages and applicable interest where a Party is found to have violated a Chapter Eleven provision. With respect to expropriation, NAFTA, Art. 1110(2), specifically requires compensation to be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place. This paragraph further states that 'the valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value'.

57”“Normally, the fair market value of a going concern which has a history of profitable operation may be based on an estimate of future profits subject to a discounted cash flow analysis. Benvenuti and Bonfant Srl v. The Government of the People's Republic of Congo, 1 ICSID Reports 330; 21 I.L.M.

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58”“However, where the enterprise has not operated for a sufficiently long time to establish a performance record or where it has failed to make a profit, future profits cannot be used to determine going concern or fair market value ....

59”“The Tribunal agrees with Mexico that a discounted cash flow analysis is inappropriate in the present case because the landfill was never operative and any award based on future profits would be wholly speculative.

60”“Rather, the Tribunal agrees with the parties that fair market value is best arrived at in this case by reference to Metalclad's actual investment in the project....

61”“Metalclad asserts that it invested $20,474,528.00 in the landfill project, basing its value on its United States Federal Income Tax Returns and Auditors' Workpapers of Capitalized Costs for the Landfill .... The calculations include landfill costs Metalclad claims to have incurred from 1991 through 1996 for expenses categorized as the COTERIN acquisition, personnel, insurance, travel and living, telephone, accounting and legal, consulting, interest, office, property, plant and equipment, including $328,167.00 for 'other'.(....)

62”“The Tribunal agrees, however, with Mexico's position that costs incurred prior to the year in which Metalclad purchased COTERIN are too far removed from the investment for which damages are claimed. The Tribunal will reduce the Award by the amount of the costs claimed for 1991 and 1992.(....)