

*This case summary was prepared in the course of research for
[S Ripinsky with K Williams, Damages in International Investment Law \(BIICL, 2008\)](#)*

Case summary

Técnicas Medioambientales Tecmed, S.A.

v

Mexico

Year of the award: 2003

Forum: ICSID

Applicable investment treaty: Mexico – Spain BIT (signed 1995, in force 1996)

Arbitrators	Timeline of the dispute
Mr. Horacio Grigera Naón – President Prof. José Carlos Fernández Rozas Mr. Carlos Bernal Vereza	28 July 2000 – request for arbitration 13 March 2001 – arbitral tribunal constituted 29 May 2003 – arbitral award

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I. Executive Summary

Tecmed, a Spanish company with two Mexican subsidiaries, brought a claim against Mexico alleging several violations of the Spain-Mexico BIT. These violations concerned Tecmed's investment in a waste landfill acquired in 1996. Tecmed alleged to have lost the landfill in 1998 as a result of the non-renewal, by Mexican authorities, of a license necessary to operate the landfill. Tecmed argued that as a result of this arbitrary and non-substantiated decision of Mexico, the investment was completely lost, as it ceased to represent any economic value as an on going business. This, in Tecmed's view, constituted expropriation. Tecmed also alleged a number of other BIT violations, in particular, of BIT rules on fair and equitable treatment and on full protection and security.

The Tribunal found that Mexico's actions indeed constituted expropriation and also violated its 'fair and equitable treatment' obligation. The rest of Tecmed's claims were rejected.

Tecmed requested a compensation for expropriation of US\$52 million based on its discounted cash flow (DCF) analysis. The Tribunal rejected Tecmed's DCF approach, as based on insufficient historical data, and instead calculated the damages on the basis of actual expenses incurred by Tecmed throughout the existence of the investment (its acquisition and subsequent development). It added a measure of profits lost by Tecmed as a result of expropriation, with the compensation totaling US\$5.5 million. The Tribunal added 6% compounded interest on this amount, to be calculated from the date of expropriation until the date of payment.

II. Factual Background and Claims of the Investor

Técnicas Medioambientales Tecmed, S.A. (the Claimant) is a company incorporated in Spain. Through two of its Mexican subsidiaries – Tecmed and Cytrar¹ – the Claimant acquired, at a public auction held in Mexico in 1996, property, buildings, facilities and other assets relating a controlled landfill of hazardous industrial waste.

A license was required to operate the landfill. In 1996, such a license was granted to Tecmed by INE,² in substitution of the previous license of indefinite duration. The new license had to be extended every year. It was so extended until November 1998. By its Resolution adopted in November 1998, INE rejected Tecmed's request to renew the permit to operate the landfill. Certain minor breaches in the mode of landfill operation were indicated by an INE as grounds for refusal.

According to the Claimant, the refusal to renew the license (the measure at issue) was largely due to political circumstances, i.e., the change of administration in the Municipality of Hermosillo, in which the landfill was physically located, rather than to legal considerations. According to the Claimant, the new authorities of Hermosillo

¹ For convenience, all of these entities are hereinafter referred to as 'Tecmed'.

² Hazardous Materials, Waste and Activities Division of the National Ecology Institute of Mexico, an agency of the Mexican Federal Government within the Ministry of the Environment, Natural Resources and Fisheries.

encouraged a movement of citizens against the landfill, which sought the withdrawal or non-renewal of the landfill's operating permit and its closedown, due to the landfill's proximity to the city. The Claimant argued that INE's refusal to extend the authorization to operate the landfill was arbitrary.

The Claimant contended that the INE's refusal to renew the landfill's operating permit constituted:

1. an expropriation of its investment, without any compensation or justification thereof;
2. a violation of the BIT provision regarding fair and equitable treatment;
3. a violation of the BIT provision according full protection and security to foreign investors and of certain other BIT provisions.

According to the Claimant, the measure at issue led to a complete loss of the profits and income from the economic and commercial operation of the landfill as an on going business. It entailed the impossibility of recovering the cost incurred in the acquisition of assets for the landfill, its adaptation and preparation. The claimed heads of damages included:

- constructions relating to the landfill;
- lost profits and business opportunities;
- the impossibility of performing contracts entered into with entities producing industrial waste, thus leading to termination of such contracts and to possible claims relating thereto; and
- the injury caused to the Claimant and to its subsidiaries in Mexico due to the adverse effect on its image in that country, with the consequent negative impact on the Claimant's capacity to expand and develop its activities in Mexico. (para.45).

Mexico denied all claims.

III. Findings on Merits

A. Expropriation

The Claimant maintained that the non-renewal of the permit to operate the landfill was an arbitrary decision which effectively meant the expropriation of the Claimant's investment and caused damage to the Claimant, as the latter was deprived of all benefits and economic use of its investment.

The Tribunal analyzed in detail the facts of the case and made the following main points. First, the INE's decision meant that the landfill would be closed permanently and irrevocably. Since the landfill could not be used for a different purpose, it lost its value.³ Secondly, the Tribunal found that the Mexican authorities did not keep a reasonable proportionality between the interest protected (the environment) and the

³ The Tribunal noted, also citing the *Santa Elena* arbitral award, that regulatory administrative actions *per se* are not excluded from the scope of the BIT, even if they are beneficial to the society as a whole – such as environmental protection measures (para. 121).

protection of the investor's rights (Tecmed was actually deprived of operating the landfill and lost thereby its investment). In this regard, the Tribunal considered the following facts:

- although Tecmed had committed breaches of certain environmental regulations, they were not the true reason for the non-renewal of the license (the true reasons, as established by the Tribunal, related to social and political circumstances and the pressure exerted on authorities by such circumstances to remove the landfill away from the city);
- Tecmed had agreed to relocate the landfill and was waiting for new land that the Mexican authorities would provide.

In light of these facts, the Tribunal concluded that the INE's decision not to renew the license was a *de facto* indirect expropriation, i.e., the investment was permanently deprived of economic value and could not be exploited, despite the fact that the legal ownership of assets concerned did not pass to third parties or to the Mexican government. By expropriating Tecmed's investment and not paying an adequate compensation, Mexico violated Article 5 of the BIT.

B. Fair and Equitable Treatment

Under the BIT, each Party agreed to accord to investments of investor of another party 'fair and equitable treatment according to international law' (FET standard). The Tribunal considered the FET standard in light of the principle of good faith and interpreted it to require State's conduct to be consistent, without ambiguities and transparent in relation to the foreign investor, so as not to prejudge its fair expectations at the time of making an investment. (paras. 154, 157)

On the basis of its factual analysis, the Tribunal concluded that INE's actions were contradictory, ambiguous and uncertain and, therefore, prejudicial to the investor (para. 172). In particular, Mexican authorities acted in a contradictory way by, on the one hand, reassuring Tecmed that it could operate the landfill until the relocation was conducted and that new land would be provided together with licenses to operate the new landfill, and, on the other hand, denying the renewal of the license. The Tribunal also mentioned other instances of Mexico's wrongful conduct and thus found Mexico in violation of its FET obligation.

C. Full Protection and Security / Other Claims

The Tribunal dismissed Tecmed's claims relating to the BIT 'full protection and security' obligation and all of its other claims.

IV. Findings on Damages

A. Law Applicable to Determination of Damages

The BIT establishes the standard of compensation (see below) but for valuation criteria, it refers to the “laws in force applicable in the territory of the Contracting Party receiving the investment” (Article 5.2 of the BIT). So, international law and domestic law apply concurrently.

The Tribunal cited the apparently most relevant article of the Mexican Law on Expropriation, which provides that the compensation shall indemnify for the commercial value of the expropriated property, which in the case of real property shall not be less than the tax value. As Mexican law did not set out more specific valuation criteria, the Tribunal did not use it in its valuation exercise.

B. Restitution in kind

The Claimant’s primary claim was for compensation; secondarily, the Claimant sought restitution in kind. Taking into account that the in-kind restitution claim was secondary and that the Claimant himself considered such restitution “absolutely impossible”, the Tribunal decided not to consider the admissibility of the restitution in kind and held monetary compensation to be an “adequate satisfaction of the Claimant’s claim”. (para.183)

C. Standard of Compensation

Article 5.2 of the BIT provides that in the event of expropriation:

‘Compensation shall be equivalent to the *fair market value* of the expropriated investment *immediately before the time when the expropriation took place*, was decided, announced or made known to the public (...) valuation criteria shall be determined pursuant to the laws in force applicable in the territory of the Contracting Party receiving the investment.’ (emphasis added)

The lost investment was defined by the Tribunal as an integrated unit comprising tangible and intangible assets, including any permits or licenses to operate it as a hazardous waste landfill. The Tribunal then pursued the task of determining the market value of this unit. (para.189)

The Tribunal determined that market value of the landfill shall be the total compensation for *both* violations to the BIT found by the Tribunal (para. 188). That is, it decided that it would not be appropriate to award separate compensations for two distinct violations of the BIT (expropriation and the FET standard).

D. Burden of Proof

The Tribunal stated that the burden to prove the investment’s market value is on the Claimant. Such burden shifts to the Respondent if the Claimant submits evidence that *prima facie* supports its allegation. The Tribunal added that “any difficulty in determining the compensation does not prevent the assessment of such compensation where the existence of damage is certain”. (para.190)

E. Valuation Method and Heads of Damages

The Tribunal stated that market value could be defined as the “fair value of the transaction on an arms’ length basis, where both parties to the transaction have knowledge of the applicable circumstances”. A price determined through a public tender could be an efficient indicator of the market value. However, the Tribunal decided not to use this method to determine the landfill’s market value at time of expropriation in 1998 because at that time there was no ‘market supported by a sufficient number of similar transactions’ that could be used as a guide. (para.191)

Parties presented sharply contrasting estimates of damages. Tecmed used the discounted cash flow (DCF) analysis of the landfill’s operation, and on this basis claimed US\$52 million plus interest. In addition, Tecmed asked the Tribunal to award compensation for damage to its reputation.

Mexico objected to Tecmed’s DCF analysis because of the very short term during which the landfill operated as an on going business (a little more than two years) and the according lack of sufficient historical data to prepare the reliable estimates. According to Mexico, in such a situation, the DCF analysis was highly speculative. Additionally, Mexico disagreed with a number of assumptions made in the Tecmed’s DCF calculation, including cost estimates and the discount rate (in an alternative DCF valuation offered by Mexico, damages totaled between US\$1.8 and US\$2.1 million, depending on the assumptions used). Instead of using the DCF analysis, Mexico suggested calculating damages on the basis of Tecmed’s actual expenses in making the investment.

The Tribunal expressed doubts as to the reliability of Tecmed’s DCF analysis. In particular, it noted a large difference in the amount paid by Tecmed for assets related to the landfill (US\$4 million) and the relief sought by Tecmed (US\$52 million). For the Tribunal, this disparity, as well as an even larger disparity between the alternative DCF calculations presented by the two parties) seemed to be an indication that the investor’s estimate was inflated. (para.186)

The Tribunal decided that the DCF analysis was not an appropriate valuation method because a little more than two years of business operation was an insufficient historical period from which reliable projection could not be derived. Important in this regard were the ‘protracted’ fifteen-year life of the investment, and the fact that the project’s future revenues were contingent on future investment expansions which were difficult to predict. (para.186)

Having rejected the DCF method, the Tribunal determined that the market value of the lost investment consisted, on the date of expropriation (November 1998), of the following elements (paras.191-195):

- 1) the tender price paid by Tecmed for the landfill-related assets in 1996 (US\$4 million);
- 2) Investments made by Tecmed in 1996-98 to improve the facility (US\$439,000);⁴

⁴ Tecmed claimed almost US\$2 million but the Tribunal decided that this figure was not supported by any documentary evidence.

- 3) Lost profits for two subsequent years of operation determined by the Tribunal to be US\$1.09 million (without explanation of how the Tribunal arrived at this figure).⁵

The Tribunal rejected the request to compensate the alleged damage to Tecmed's reputation because of the lack of evidence demonstrating that Tecmed's reputation was affected by wrongful actions of Mexico. In other words, no causal link between the breach and the damage was established. In addition, the Tribunal did not find that the adverse press coverage for Tecmed of the events regarding the landfill was attributable to Mexico. (para.198)

All in all, the Tribunal awarded Tecmed the damages of US\$5.5 million.

F. Interest

Tecmed requested compound interest at a rate of 6%. Noting the absence of specific objections on this point on the part of Mexico, the Tribunal awarded the requested interest from the date of expropriation 'until the effective and full payment by the Respondent of all amounts payable by the Respondent to the Claimant under this award.' (para.197)

On the issue of whether interest should be compound or simple, the Tribunal noted that compound interest has been accepted in a number of arbitral awards, and has cited the *Middle East Cement* case where it had been said that '...compound (as opposed to simple) interest is at present deemed appropriate as the standard of international law in [...] expropriation cases.'⁶

G. Legal Costs

The Tribunal determined that each party would bear its own costs, expenses and legal counsel fees and that the costs incurred by the Arbitral Tribunal and ICSID would be shared equally between the Claimant and the Respondent. In support of this decision, the Tribunal referred to the fact that Tecmed was successful only with respect to some of its claims and that Mexico's defenses were also admitted only partially.

V. Implications/Initial Analysis

- No "double recovery". In cases where there are several breaches of the investment treaty by a State, an investor does not receive a separate compensation for each violation. In this case, compensation for expropriation (market value of the lost investment) covered other breaches as well.

⁵ The Tribunal limited the calculation of lost profits to two additional years of operation because within this time-period the landfill would have had to be relocated, due to community pressure.

⁶ Award in ICSID case ARB/99/6 *Middle East Cement Shipping and Handling Co.S.A v Arab Republic of Egypt*, 12 April 2002, 174 , p. 42.

- The approach taken by the Tribunal towards the **burden of proof** in relation to damages (the investor has to establish a *prima facie* case and after that the burden shifts to the State) accords well with international legal authorities, although it does little to solve the common problem of competing quantum experts.⁷
- The Tribunal suggested that where the damage cannot be assessed exactly (but where it is obvious that the damage exists), an **approximate assessment** would do.
- **DCF valuation method** is running the risk of being rejected when an investment, although an ongoing business, has an insufficiently long history of operation, i.e., insufficient data to make future economic predictions. What would constitute a ‘sufficiently long’ history of operation remains to be decided on a case-by-case basis.
- The Tribunal recognized that the **value of the investment** exceeded the sum total of the invested amounts and added an additional compensation for two years of **lost profits**. This does not appear to be a theoretically correct model for calculating the ‘fair market value’ of an investment. The added amount resembles compensation for the ‘loss of opportunity’.
- In principle, **damage to reputation** is recoverable but the claimant has to prove the damage, as well as the causal link between the violation of the agreement by the State and the damage.

⁷ J. Coe Jr., N. Rubins, ‘Regulatory Expropriation and the *Tecmed* case: Context and Contributions’, in T. Weiler (ed.), *International Investment Law and Arbitration: Leading Cases from the ICSID, NAFTA, Bilateral Treaties and Customary International Law* (Cameron May, 2005), 597-667, at 658.