Tecnicas Medioambietales Tecmed S.A. v The United Mexican States, ICSID Case No. ARB(AF)/00/2, Award

Summary: Tecmed claimed in respect of its loss of a landfill due to the Mexican authorities' non-renewal of the licence necessary to operate the landfill. Tecmed claimed that this was due to political considerations. It claimed in respect of *inter alia* a violation of the fair and equitable treatment under the Mexico-Spain BIT.

International Centre for Settlement of Investment Disputes

TECNICAS MEDIOAMBIENTALES TECMED S.A.

v.

THE UNITED MEXICAN STATES

CASE No. ARB (AF)/00/2

AWARD

President: **Dr. Horacio A. GRIGERA NAON**

Co-arbitrators: **Prof. José Carlos FERNANDEZ ROZAS**
Mr. Carlos BERNAL VEREA

Secretary to the Tribunal: **Ms. Gabriela ALVAREZ AVILA**

Date of dispatch to the parties: May 29, 2003

II. Fair and Equitable Treatment

152. According to Article 4(1) of the Agreement:

Each Contracting Party will guarantee in its territory fair and equitable treatment, according to International Law, for the investments made by investors of the other Contracting Party.

153. The Arbitral Tribunal finds that the commitment of fair and equitable treatment included in Article 4(1) of the Agreement is an expression and part of the *bona fide* principle recognized in international law,[189] although bad faith from the State is not required for its violation:

To the modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In particular, a State may treat foreign investment unfairly and inequitably without necessarily acting in bad faith.[190]

154. The Arbitral Tribunal considers that this provision of the Agreement, in light of the good faith principle established by international law, requires the Contracting Parties to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the State that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation. In fact, failure by the host State to comply with such pattern of conduct with respect to the foreign investor or its investments affects the investor's ability to measure the treatment and protection awarded by the host State and to determine whether the actions of the host State conform to the fair and equitable treatment principle. Therefore, compliance by the host State with such pattern of conduct is closely related to the above-mentioned principle, to the actual chances of enforcing such principle, and to excluding the possibility that state action be characterized as arbitrary; i.e. as presenting insufficiencies that would

[189] I. Brownlie, Principles of Public International Law, Oxford, 5th. Edition (1989), p. 19. It is understood that the fair and equitable treatment principle included in international agreements for the protection of foreign investments expresses "...the international law requirements of due process, economic rights, obligations of good faith and natural justice" : arbitration case *S.D. Myers, Inc.v. Government of Canada,* partial award of November 13, 2000; 134, p. 29 ; www.naftalaw.org.

[190] ICSID Arbitration no. ARB(AF)/99/2, *Mondev International Ltd v United States of America*, p.40, 116, October 11, 2002, www.naftalaw.org.

be recognized "…by any reasonable and impartial man,"[191] or, although not in violation of specific regulations, as being contrary to the law because:

...(it) shocks, or at least surprises, a sense of juridical propriety.[192]

155. The Arbitral Tribunal understands that the scope of the undertaking of fair and equitable treatment under Article 4(1) of the Agreement described above is that resulting from an autonomous interpretation, taking into account the text of Article 4(1) of the Agreement according to its ordinary meaning (Article 31(1) of the Vienna Convention), or from international law and the good faith principle, on the basis of which the scope of the obligation assumed under the Agreement and the actions related to compliance therewith are to be assessed.

156. If the above were not its intended scope, Article 4(1) of the Agreement would be deprived of any semantic content or practical utility of its own, which would surely be against the intention of the Contracting Parties upon executing and ratifying the Agreement since, by including this provision in the Agreement, the parties intended to strengthen and increase the security and trust of foreign investors that invest in the member States, thus maximizing the use of the economic resources of each Contracting Party by facilitating the economic contributions of their economic operators. This is the goal of such undertaking in light of the Agreement's preambular paragraphs which express the will and intention of the member States to "...intensify economic cooperation for the benefit of both countries..." and the resolve of the member States, within such framework, "....to create favorable conditions for investments made by each of the Contracting Parties in the territory of the other ...".

157. Upon making its investment, the fair expectations of the Claimant were that the Mexican laws applicable to such investment, as well as the supervision, control, prevention and punitive powers granted to the authorities in charge of managing such system, would be used for the purpose of assuring compliance with environmental protection, human health and ecological balance goals underlying such laws.

158. The evidence submitted reveals that when the authorities of the Municipality of Hermosillo, in the state of Sonora, of SEMARNAP and INE, perceived that the political problems mentioned above, closely related to the community opposition already described, made it necessary to relocate Cytrar's activities in the Landfill to a place outside Hermosillo, Cytrar, with Tecmed's support, agreed that its publicly known relocation proposal would become a commitment of Cytrar and of the Mexican federal, state and municipal authorities. Such evidence also shows that although Cytrar accepted or agreed to such relocation, it made it conditional upon having a new site to carry out its technical and business activities and that it expressed this condition before the Mexican authorities on several occasions. In its note dated June 25, 1998, to the President of INE, Cytrar defines the distribution of duties and obligations related to the relocation as follows:

[191] *Neer v. México* case, (1926) R.I.A.A. iv. 60.
[192] International Court of Justice Case: *Elettronica Sicula S.p.A. (ELSI) (United States of America v. Italy*), 128, p. 65, July 20, 1989, ICJ, General List No. 76.

....[Cytrar] will accept its relocation and, to that end, the municipal and state authorities will be in charge of finding, acquiring and delivering a new site, and they will also be in charge of carrying out any and all pertinent studies and of granting the related permits and licenses.[193]

159. There is no proof that INE or the state and municipal authorities challenged the distribution of the relocation obligations. Such allocation was only changed to the extent that Cytrar offered to assume a significant portion of the financial cost of the relocation. At no time, from the time the authorities communicated to the public the relocation of the Landfill to the date of the Resolution, did such authorities or IMADES express any disagreement as to conditioning the operation of the Landfill by Cytrar to the relocation of such operations to a different place, nor did they deny that the relocation was the result of an agreement with Cytrar on the basis of conditions agreed upon between Cytrar and such authorities. Dr. Cristina Cortinas Nava, INE's General Director of Hazardous Materials, Waste and Activities recognized this as follows:

.....I recognize that the company stated that the relocation would take place after finding a new site. Therefore, the company expected to continue operating the Landfill at its current site until then. [...] I recognize that, and if you ask me why, then, at the time I made the decision that implied an interruption of the continuity sought by the company, why did I do it? [....] my answer is that it was because the circumstances in November were such that I am sure that if I had renewed the permit I would not have been able to guarantee to the company the continuity of its operations there. Because there were many objections to the continuity of the company's operations there.[194]

160. Cytrar may have understood in good faith that its operations at Las Víboras under the Permit would continue for a reasonable time until effective relocation. Although it is true that the relocation agreement has not been memorialized in an instrument signed by all the parties involved, the evidence submitted leads to the conclusion that there was such an agreement, as evidenced by the joint declaration of SEMARNAP, the Government of the state of Sonora and the Honorable Municipality of Hermosillo to that effect. Section 4 of such declaration states that "…the current landfill operated by CYTRAR shall be closed as soon as the new facilities are ready to operate".[195] On the other hand, the Resolution[196] itself stated that:

Furthermore, CYTRAR S.A. de C.V. agreed with the different levels of the federal, state and municipal government that the landfill would be relocated and made this agreement public.

There is no doubt that the agreement commenced to be performed, as evidenced by the joint visits of Cytrar and IMADES to sites that were possible locations for the relocated landfill. There is no evidence stating or suggesting that the parties to such agreement agreed that external factors stemming from community pressure —which the Mexican authorities were fully aware of upon reaching the agreement— would cause the closing of Cytrar's business

[193] Document A49. The relocation commitment project between the Mexican authorities and Cytrar referred to by the Respondent in the Counter-memorial, n. 324-329, pp. 93-94, which reportedly gives rise to a change in the allocation of obligations described above, has never been executed and was still subject to comments as of January 13, 1999. Therefore, such commitment cannot be taken into account to measure the allocation of the relocation obligations assumed by the parties in the stage prior to the issuance of the Resolution.
[194] Hearing held from May 20 to May 24, 2002; transcript of the session of May 21, 2002, pp. 77-77 overleaf.
[195] Document A88.
[196] Document A59.

at the Landfill without complying with the prior relocation of this business to another place. The incidental statements as to the Landfill's relocation in the correspondence exchanged between INE and Cytrar or Tecmed, and that constitute the immediate precedents of the Resolution, cannot be considered to be a clear and unequivocal expression of the will of the Mexican authorities to change their position as to the extension of the Permit so long as Cytrar's business was not relocated, nor can it be considered an explicit, transparent and clear warning addressed to Cytrar from the Mexican authorities that rejected conditioning the revocation of the Permit to the relocation of Cytrar's operations at the Landfill to another place, a rejection that should not have been expressed only by INE, but also by the other authorities responsible for deciding on the Landfill's relocation; i.e. the Municipality of Hermosillo, the Government of Sonora and SEMARNAP. The conclusion is that Cytrar may have reasonably trusted, on the basis of existing agreements and of the good faith principle, that the Permit would continue in full force and effect until the effective relocation date.

161. As stated above, on July 15, 1998, in a letter sent to the General Director of Hazardous Materials, Waste and Activities of INE, Dr. Cristina Cortinas Nava, Cytrar presented a number of proposals related to the expansion of cell Nº 2 and the construction of cell Nº 3 to address the company's commitments while the process to relocate its operations to a different site was carried out.[197] In spite of the urgency of the case and of the letter that Cytrar had sent to INE's President on June 25, 1998, reporting the need to increase the Landfill's capacity for those very reasons,[198] and reiterating Cytrar's commitment to relocate subject to the conditions expressed therein, INE took about three months to issue its reply to Cytrar. In its response, included in an official communication sent to Cytrar on October 23, 1998,[199] i.e. scarcely more than one month before the expiration of the Permit's term and when Cytrar had already requested the Permit's renewal in a letter sent to INE on October 19, 1998,[200] INE did not express the existence of any irregularity committed by Cytrar in the Landfill's operation or of any default by Cytrar of the conditions under which the Permit was granted that, in the opinion of INE, might jeopardize the Permit's renewal or its limited extension for a reasonable time so as to permit the relocation as proposed by Cytrar. INE could not have been unaware at the time of the existence of irregularities or infringements related to the expansion of cell Nº 2. The expansions seemed to be the biggest concern of the sectors that opposed the Landfill, as their interpretation was that the expansions, which had been communicated by PROFEPA to INE by means of an official communication received by INE on September 14, 1998,[201] were *sine die* the cause for the delay in closing the Landfill. As INE only stated that it would evaluate the request for the expansion of cell Nº 2 and construction of cell Nº 3 upon considering renewal of the Permit, without warning Cytrar of any breach or irregularity in the expansion of the Landfill's capacity that, in the opinion of INE, jeopardized the renewal of the Permit, INE significantly affected Cytrar's ability to cure such defaults or irregularities in due time and prevent the denial of the Permit's renewal upon its expiration. Although INE, in its official

[197] Letter sent to Dr. Cristina Cortinas Nava, document A50.
[198] Letter sent to Enrique Provencio, document A49.
[199] Official communication no. DOO-800/005262 of October 23, 1998, document A51.
[200] Cytrar's letter to Dr. Cristina Cortinas Nava, document A52.
[201] Document D133.

communication addressed to Cytrar on November 13, 1998,[202] in reply to the note sent by Cytrar on October 19, 1998, whereby it requested the renewal of the Permit, refers to these and other infringements, only six days before expiration of the Permit, it seems evident that, at that time, any meaningful effort to cure such infringement and prevent a denial of the permit's renewal was not feasible.

162. INE did not report, in clear and express terms, to Cytrar or Tecmed, before issuing the Resolution, its position as to the effect of these infringements on the renewal of the Permit. As a consequence, it prevented Cytrar from being able to express its position as to such issue and to agree with INE about the measures required to cure the defaults that INE considered significant when it denied the renewal without allowing a reasonable time to relocate Cytrar to another site. Providing an opportunity to Cytrar was reasonable and equitable, since at all times the parties considered that Cytrar would relocate the Landfill to another place, and such relocation and the necessity for the Landfill to continue operating at Las Víboras until the effective relocation, was the purpose of the recent correspondence exchanged between the parties. There was no disagreement that relocation could not be immediate and that it would require continued efforts, probably for many months, even for more than a year. There are clear inconsistencies or contradictions in the attitude of INE, which, on the one hand, did not challenge the technical capacity and operating qualifications of Cytrar upon entrusting it with the operation of a hazardous waste landfill that would be relocated to another site and that would operate under the more ambitious conditions —and surely with more responsibilities for the operator— of a Comprehensive Center for the Management of Industrial Waste, or CIMARI, and that, on the other hand, did not warn Cytrar about the curable defaults in its operations at Las Víboras sufficiently in advance so as to avoid the denial of the Permit's renewal. As shown, such defaults have not endangered public health, ecological balance or the environment. It should be noted that, although the official communication sent by INE to Cytrar on November 13, 1998, refers to an alleged violation by Cytrar of the specific condition 1.12 of the Permit, under which "....the presentation of repeated and justified complaints against the company or the occurrence of events due to problems in the Landfill's operation that may endanger public health...." (without going any deeper into this subject or expressly mentioning such events) are sufficient events to «*cancel*» the Permit (not to *deny its renewal*), such condition was not invoked among the grounds of the Resolution. After analyzing such inconsistencies, it may be concluded that the contradictions and lack of transparency in INE's attitudes vis-à-vis Cytrar, and the absence of clear signs from INE, did not permit Cytrar to adopt a behavior to prevent the non-renewal of the Permit, or that might at least guarantee the continuity of the permit for the period required to relocate the Landfill to a new site.

163. If INE's position was that relocation was to take place within a given period —which, as stated above, according to the Mexican authorities, should be about twelve months—[203] after the expiration of which the Permit would not be renewed, it would be reasonable to expect such situation to be reported to or agreed upon by Cytrar. Certainly, it is surprising that INE did not unequivocally and clearly specify the deadlines, terms and conditions that would apply to the relocation, as requested by the authorities of the Municipality of

[202] Document A53.
[203] Communication of the Mayor of the Municipality of Hermosillo, document D113.

Hermosillo a day before the Permit's expiration,[204] even when Cytrar and Tecmed had agreed to relocate Cytrar's business to any site selected by the Mexican authorities and regardless of the note sent by Tecmed to INE on November 17, 1998, in which Tecmed clearly requests the execution of an agreement with INE and the Mexican federal, state and municipal authorities containing a certain and specific relocation schedule.[205] There are also express inconsistencies between, on the one hand, the absence of such specifications and a notice to Cytrar warning it to agree to or abide by such conditions and, on the other hand, the use of the denial to renew the Permit as a factor to pressure Cytrar to relocate, as declared by INE's General Director of Hazardous Materials, Waste and Activities, who authored the Resolution:

> .....for them [the local authorities] if I continued renewing the Permit, that would [sic] extend ... For as long as the company could continue receiving waste, it would not assume a full commitment to perform the studies required to relocate the site ...[206]

This statement reveals the two goals pursued by INE upon issuing the Resolution. On the one hand it denies the renewal of Cytrar's Permit without any compensation whatsoever for the loss of the financial and commercial value of the investment. On the other hand, this denial is described as a means to pressure Cytrar and force it to assume a similar operation in another site, bearing the costs and risks of a new business, mainly because by adopting such course of action, INE expected to overcome the social and political difficulties directly related to the Landfill's relocation. Under such circumstances, such pressure involves forms of coercion that may be considered inconsistent with the fair and equitable treatment to be given to international investments under Article 4(1) of the Agreement and objectionable from the perspective of international law.[207]

164. If, on the other hand, INE's position was —as has actually been established— to close the Landfill inevitably, with or without relocation, INE should have expressed such position clearly. Regardless of the hypothesis contemplated, the decisive factor —for which Cytrar was not responsible— was the Landfill's location at the Las Víboras site and its proximity to Hermosillo's urban center, which was in violation of Mexican regulations and a source of community opposition and political unrest, but which was not —as confirmed by Mexican authorities— against the legitimacy of the Landfill's operation under Mexican law. If the inevitable consequence of this situation, evaluated by the Mexican authorities, was the refusal to renew the Permit and the closing of the site, such determination, from the Agreement's standpoint, should have been accompanied, as has already been decided, by the payment of the appropriate compensation. The lack of transparency in INE's behavior and intention throughout the process that led to the Resolution, which does not reflect in full the reasons that led to the non-renewal of the Permit, cover up the final and real

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[204] Communication sent to INE's President by the Mayor of the Municipality of Hermosillo on November 18, 1998, in which the Mayor requests "the execution of a landfill relocation agreement between the Federation, the State, the Municipality and the company. A detailed, signed, legal agreement containing a schedule and fixed dates." Document D157.

[205] Document A 91.

[206] Hearing held from May 20 to May 24, 2002; transcript of the session held on May 21, 2002, p. 72.

[207] D.F.Vagts, Coercion and Foreign Investment Rearrangements, 72. The American Journal of International Law , pp. 17 *et seq*., specially p. 28 (1978) : "…the threat of cancellation of the right to do business might well be considered coercion."

consequence of such actions and of the Resolution: the definitive closing of the activities at the Las Víboras landfill without any compensation whatsoever, whether Cytrar agreed or not, in spite of the expectations created, and without considering ways enabling it to neutralize or mitigate the negative economic effect of such closing by continuing with its economic and business activities at a different place. Within the general context of the circumstances mentioned above, the ambiguity of INE's actions was even greater when it resorted to the non-renewal of the Permit to overcome obstacles not related to the preservation of health and the environment although, according to the evidence submitted, the protection of public health and the environment is where INE's preventive function should be focused. To the question about the factors or parameters that INE should take into account to decide on the renewal of authorizations such as the Permit, witness Dr. Cristina Cortina Navas answered:

> Provisions can have two different purposes: to evaluate environmental performance and to assess the management of companies. Thus, you will distinguish, among the conditions established, such conditions that allowed for the evaluation of the former and the conditions that allowed for the assessment of the latter. As regards management, there were a series of instruments, reports, records and issues that the company had to take care of. In turn, performance involved providing sufficient security that there would not be escapes, leaks or accidents during hazardous waste management, including transportation and storage. Any of these issues could be verified, and, in fact, before issuing any resolution we tried to gather all the elements necessary to be able to pass judgment on whether or not such purposes had been fulfilled.[208]

The refusal to renew the Permit in this case was actually used to permanently close down a site whose operation had become a nuisance due to political reasons relating to the community's opposition expressed in a variety of forms, regardless of the company in charge of the operation and regardless of whether or not it was being properly operated.

165. The Arbitral Tribunal considers that INE's behavior described above with respect to Cytrar, which had a material adverse effect on Cytrar's ability to get to know clearly the real circumstances on which the maintenance or validity of the Permit depended —it must be recalled that Cytrar could not operate without this Permit— is not an unprecedented action. INE's denial to renew the Permit belongs to the wider framework of the general conduct taken by INE towards Cytrar, Tecmed and, ultimately, the Claimant's investment.

166. The Arbitral Tribunal finds that INE's behavior, as analyzed in paragraphs 153-164 above and because of the "deficiencies" explained therein, conflicts with what a reasonable and unbiased observer would consider fair and equitable, and that this amounts to a violation of Article 4(1) of the Agreement. The Arbitral Tribunal also finds that such a behavior can be related, in terms of its prejudicial consequences, to the consequences of the Resolution; and that only after the Resolution was issued could the Claimant fully realize the breach of the Agreement incurred by such behavior and the resulting damage. Consequently, the Claimant's claims in connection with such behavior satisfy the requirements for admissibility contemplated in Title II(4) and (5) of the Appendix to the Agreement.

[208] *Ibidem*, pp. 68-68 overleaf

167. Notwithstanding the above, the Arbitral Tribunal considers it equally appropriate to place this behavior within the context of INE's prior conduct on the basis of the abundant arguments and evidence presented by the Parties in connection with such prior conduct and in view of the undeniable fact that the legal relationship between INE and Cytrar or Tecmed associated with the Landfill is one and only one, starting with the initial procedures in connection with the authorization to operate the Landfill and finishing with the Resolution —the immediate cause for the damage sustained by the Claimant. This conduct should also be analyzed in light of the fact that throughout a relationship of such nature, necessarily prolonged in time, the Claimant was entitled to expect that the government's actions would be free from any ambiguity that might affect the early assessment made by the foreign investor of its real legal situation or the situation affecting its investment and the actions the investor should take to act accordingly.

168. As a result of the judicial sale of the Landfill's assets, Tecmed and the Municipality of Hermosillo request from INE the "change of name" or the facilitation of such change, which, according to the administrative practice up to date, at least in connection with the Landfill, entailed the replacement of the holder of the permits necessary for the operation of the landfill at Las Víboras by such holder's successors. There is no evidence that INE has responded to such communications stating that Cytrar had actually to request a new permit, which may differ from the existing one, instead of requesting the replacement of the old holder with a new one; and no convincing evidence has been offered to support the Respondent's allegations as to the fact that, from the beginning, INE's officers instructed Cytrar to obtain a new "operating license" because, for example, as stated by the Respondent, the nature of the operation undertaken by Cytrar and the consequent expansion of the Landfill's installed capacity would so require it.[209] Among others, in the note dated June 5, 1996, sent to INE by Tecmed together with the MRP Form, containing information that INE should evaluate in connection with the individual or entity that was to be in charge of a hazardous waste landfill operation, Tecmed specifically requested from INE "...the change of the name appearing in the permit granted by INE to the new company for such purpose, CYTRAR S.A. de C.V.". Attached as Annex "A" to such presentation and Form, are the Establishment License granted on December 7, 1988, and the permit to operate the already existing Controlled Landfill, dated May 4, 1994, together with its expansion of August 25, 1994.[210]

169. Thus, there was no possible margin for error with respect to the request made by Tecmed and Cytrar with the support of the Municipality of Hermosillo in connection with the existing licenses or permits by virtue of which the Landfill had operated and was still operating. Considering such very clear requests, there is no evidence that INE had warned Cytrar that such requests could only be interpreted as petitions to be included in INE's listing of companies that would qualify for the operation of CIMARIS or Comprehensive Centers for Industrial Waste Management —to which the witness Jorge Sánchez Gómez, the INE's General Director of Hazardous Materials, Waste and Activities at that time[211] had made reference— or evidence of practices, resolutions or administrative regulations or legal

[209] Counter-memorial, 127, pp. 34-35
[210] Document D46
[211] Hearing held from May 20 to May 24, 2002. Transcript of the session of May 23, 2002, p. 57.

provisions leading to such sole and exclusive interpretation. On September 24, 1996, INE sent Cytrar an official communication signed by Jorge Sánchez Gómez, whereby Cytrar was informed that "In view of the request filed by the company Promotora e Inmobiliaria del Municipio de Hermosillo, OPD to change its name to Cytrar S.A. de C.V.," and considering that according to the recommendations of INE's "...Legal Affairs Department …" Cytrar had furnished "...the documents required by this General Office and had fulfilled all legal requirements that, in such Department´s understanding, are essential *for carrying out the necessary procedure,"*[212] Cytrar "... for all legal and administrative purposes..." had been "duly registered in this General Office under my charge".[213] It is not surprising that from this communication, Cytrar interpreted that INE had changed the corporate name appearing on the permits to operate the Landfill, as requested by Cytrar, Tecmed and the Municipality of Hermosillo.

170. Subsequently, it is no wonder to see Cytrar surprised when after Cytrar had been operating the Landfill under the existing permit dated May 4, 1994, in its capacity as new company authorized under the permit pursuant to INE's official communication dated September 24, 1996, as Cytrar was entitled to believe in good faith, INE demanded Cytrar to return such communication to be replaced by another, with the same date and an almost identical text, except for an annex whereby Cytrar was granted a permit to operate the Las Víboras landfill, dated November 11, 1996.[214] Such permit, in addition to terminating the prior permit dated May 4, 1994, in which Cytrar had requested the change of name, differed from the last one in some material respects. The most outstanding difference, which would only be appreciated upon refusal to renew the Permit in 1998, was that the permit of May 1994 had an indefinite duration and the permit of November 1996 had a term of one year that could be extended. As highlighted by the witness Jorge Sánchez Gómez, the purpose behind the annual renewal of permits was to facilitate INE's actions to put an end to the operations carried out by companies that, in INE's understanding, did not adjust their actions to the applicable legal provisions**;** the INE could refuse the extension or refuse to renew such permits at the end of each year. According to the witness, this allowed INE to dispense with the more cumbersome procedure —of uncertain success— of obtaining the revocation of the permit by PROFEPA, which required that a case be opened and that the party subject to sanctions be given the opportunity to express its argumentations and defenses:

….apparently, there is an alternative: that the agency that had to enforce the law; in this case, PROFEPA, carried out the execution. However, it was very difficult to have a company's registration withdrawn if there were no elements that would clearly allow verification of a breach. Revocation of permits is a very complicated procedure.....[215]

To emphasize INE's discretionary powers as to the continuation of Cytrar's operation of the Landfill and in accordance with INE's policy of facilitating the possibility of putting an end to such operation without having to start the proceeding to withdraw the permit, when

[212] Emphasis added by the Arbitral Tribunal
[213] Document A42
[214] Documents A43 and A44
[215] Hearing held from May 20 to May 24, 2002. Declaration of Jorge Sánchez Gómez, transcript for the session of May 23, 2002, p. 53 overleaf.

the Permit was granted —on November 19, 1997— it was determined that this Permit, instead of being "subject to extension" (as the previous permit stated), was subject to "renewal" upon request of the interested party. That is to say, it required a new permit at the end of each year, instead of extending its validity at the end of such period. In the words of the witness Jorge Sánchez Gómez:

...the notion of renewal is much easier to handle for the purpose of refusing a permit to a company that is not complying with the requirements.[216]

171. If the indefinite-duration permit dated May 4, 1994 had been transferred to Cytrar as requested to INE by Cytrar, Tecmed and the Municipality of Hermosillo, INE would not have been able to put an end to Cytrar's operation of the Landfill by means of the Resolution and the only remedy available for that purpose would have been the revocation of the Permit by PROFEPA. But such revocation would probably have not been successful on the basis of the infringements of the Permit used to justify the Resolution, which were not even considered by PROFEPA as deserving any sanction other than a fine. To sum up, INE unilaterally transformed a previous administrative act, which, as such, was presumed to be legitimate, had immediate effects and could only be interpreted in good faith as having accepted Cytrar's petition to be the transferee of the existing permits for the operation of the Landfill. The objective consequence of such transformation was to grant Cytrar a permit to operate the Landfill, which reduced Cytrar's entitlement to question actions that deprived it of the Permit or that had such effect. Subsequently, INE —also unilaterally— classified the petition as a request to be registered in a listing that Cytrar was not aware of, and regarding which, in any case, Cytrar had shown no interest. The same objective consequence is to be attributed to the transformation as from November 19, 1997, of Cytrar's permit to operate the Landfill, from a permit that was subject to extension to a permit that was subject to renewal.

172. The contradiction and uncertainty inherent in INE's actions as to Cytrar and Tecmed is evidenced, then, both in the initial stage of the processing of the necessary permits to operate the Landfill and when INE decided to put an end to such operation by means of the Resolution. Such actions belong to one and the same course of conduct characterized by its ambiguity and uncertainty which are prejudicial to the investor in terms of its advance assessment of the legal situation surrounding its investment and the planning of its business activity and its adjustment to preserve its rights. Such ambiguity and uncertainty are also present in the last stage of the relationship, analyzed under paragraphs 153-164 above, which led to the Resolution, and added their harmful effects to the damage resulting from the denial to grant the Permit. Although INE's initial behavior was before the effective date of the Agreement and the Arbitral Tribunal will not pass judgment on whether at that stage such conduct, considered in isolation, amounted to a breach of the provisions thereof before its entry into force, it cannot be ignored, in light of the good faith principle (Articles 18 and 26 of the Vienna Convention), that the conduct of the Respondent between the date of execution of the Agreement (in view of the Respondent's determination to ratify it subsequently) and the effective date thereof, is incompatible with the imperative rules deriving from Article 4(1) of the Agreement as to fair and equitable treatment. This is

[216] Transcript of the session of May 23, 2002, p. 59 overleaf.

particularly so since, according to Article 2(2) of the Agreement, it is applicable to investments made before its entry into force, a circumstance to be certainly considered when analyzing the conduct attributable to the Respondent that took place before that time but after the Respondent having executed the Agreement. INE's contradictory and ambiguous conduct at the beginning of the relationship between INE, Cytrar and Tecmed before the entry into force of the Agreement has the same deficiencies as those encountered in such conduct during the last stage of the relationship, immediately preceding the Resolution. Thus, INE's conduct during such time is added to the prejudicial effects of its conduct during the last stage, which breached Article 4(1) of the Agreement.

173. Briefly, INE's described behavior frustrated Cytrar's fair expectations upon which Cytrar's actions were based and upon the basis of which the Claimant's investment was made, or negatively affected the generation of clear guidelines that would allow the Claimant or Cytrar to direct its actions or behavior to prevent the non-renewal of the Permit, or weakened its position to enforce rights or explore ways to maintain the Permit. During the term immediately preceding the Resolution, INE did not enter into any form of dialogue through which Cytrar or Tecmed would become aware of INE's position with regard to the possible non-renewal of the Permit and the deficiencies attributed to Cytrar's behavior —including those attributed in the process of relocation of operations— which would be the grounds for such a drastic measure and, thus, Cytrar or Tecmed did not have the opportunity, prior to the Resolution, to inform of, in turn, their position or provide an explanation with respect to such deficiencies, or the way to solve such deficiencies to avoid the denial of renewal and, ultimately, the deprivation of the Claimant's investment. Despite Cytrar's good faith expectation that the Permit's total or partial renewal would be granted to maintain Cytrar's operation of the Landfill effective until the relocation to a new site had been completed, INE did not consider Cytrar's proposals in that regard and not only did it deny the renewal of the Permit although the relocation had not yet taken place, but it also did so in the understanding that this would lead Cytrar to relocate.

174. Such behavior on the part of INE, which is attributable to the Respondent, results in losses and damage[217] for the investor and the investment pursuant to Title II(4) of the Appendix to the Agreement coinciding both as to essence and time with those derived from the Resolution, whether such behavior is considered generically or only as to the stages mentioned and analyzed by the Arbitral Tribunal in paragraphs 153-164 above. The Respondent's behavior in such stages amounts, in itself, to a violation of the duty to accord fair and equitable treatment to the Claimant's investment as set forth in Article 4(1) of the Agreement and such behavior constitutes sufficient basis for the Claimant's claims founded on such violation to be admissible, given the time at which the damage occurred and the time when the damage and the violation of the Agreement were necessarily perceived by the Claimant (on the date of issuance of the Resolution), pursuant to Title II(4) and (5) of the Appendix to the Agreement.

III. Full Protection and Security and Other Guarantees under the Agreement

[217] "Damage" is not limited to the economic loss or detriment and shall be interpreted in a broad sense (J. Crawford, The International Law Commission's Articles on State Responsibility, 29-31 (Cambridge University Press, 2002).