



International Arbitration Case Law

Academic Directors: Ignacio Torterola
Loukas Mistelis*

SAUR INTERNATIONAL SA V. REPUBLIC OF ARGENTINA (ICSID CASE NO. ARB/04/4)

ARBITRAL AWARD

Case Report by Marine de Bailleul **
Edited by Loukas Mistelis***

In a decision rendered on May 22, 2014, the International Center for Settlement of Investment Disputes addressed an original issue: the determination of the value of the Claimant's investment, corresponding to the compensation amount that the Claimant is entitled to receive, because of the violation by the Republic of Argentina of several principles established by the Agreement between France and Argentina for the mutual promotion and protection of investments.

Main Issues:	Jurisdiction – competence of the arbitral tribunal; treaty obligations – international law standard – full protection and security; treaty obligations – international law standard – fair and equitable treatment; damages – determination of value of compensation.
Tribunal:	Professor Juan Fernandez-Armesto, Professor Bernard Hanotiau, Professor Christian Tomuschat.
Claimant's counsel:	Mr. Philippe Pinsolle, Quinn Emanuel Urquhart & Sullivan, LLP, Mr. Fernando Mantilla-Serrano, Latham & Watkins, Prof. Emmanuel Gaillard, Shearman & Sterling, LLP.
Defendant's Counsel:	Dr. Angelina Maria Esther Abbona, National Treasure, Buenos Aires, Argentina.

* Directors can be reached by email at ignacio.torterola@internationalarbitrationcaselaw.com and loukas.mistelis@internationalarbitrationcaselaw.com

** Marine de Bailleul is a French attorney admitted to practice in New York State. She holds an LL.M. in International Business Law and Arbitration from American University and a French Master's degree in Business and Corporate Law. She can be reached at marine.debailleul@gmail.com.

*** Loukas Mistelis is co-Director of International Arbitration Case Law (IACL).

Digest

1. *Procedural History*

On November 17, 2003, SAUR International S.A. (“Sauri” or “Claimant”) introduced arbitral proceedings before the International Center for Settlement of Investment Disputes (“ICSID”), against the Republic of Argentina (“Respondent”), to obtain compensation for the damage sustained because of the non-respect by the Respondent of the principles established by the Agreement between France and Argentina for the mutual promotion and protection of investments (“APPI”). Two aspects compose the loss suffered by Claimant: the damage sustained to his investment in shares, and the damage sustained to his investment for technical support.

On November 10 and 11, 2005, the hearing relating to the competence of the Arbitral Tribunal took place in Washington, D.C., head office of the ICSID. At this occasion, the Respondent raised several exceptions to the competence and to the jurisdiction of the Arbitral Tribunal (which will be examined later).

From November 14 to 18, 2011, the Tribunal rendered its hearing on the substance of the dispute, in Washington, D.C. The Arbitral Tribunal recognized the existence of measures of expropriation and nationalization, which were used by the Respondent while dealing with the investments, resulting in the dispossession of its investment by the Claimant. In addition, the Tribunal affirmed that the Republic of Argentina did not respect the fair and equitable treatment standard while dealing with Sauri’s investments.

On October 15, 2012, Sauri presented its memorandum demanding compensation for the damages suffered. On June 14, 2013, the Republic of Argentina presented a memorandum in reply to the damages and its counter-claims.

On June 17 and 18, 2013, the hearing relating to the damage endured was held in Washington, D.C., at the head office of the ICSID.

On May 22, 2014, the Arbitral Tribunal, proving the Claimant right, rendered a decision rejecting the reopening of the arbitral proceedings.

2. *Facts of the Case*

The Claimant to the present arbitration, Sauri, created in 1994, is the wholly owned subsidiary and gathers the totality of the international activities of the company “Société d’Aménagement Urbain et Rural, S.A.,” specialized in water production, water treatment, water distribution and sanitization.

Sauri participated to a call for tender issued by the Province of Mendoza in 1997, in order to privatize by a partial divestiture of shares the Argentinian company Obras Sanitarias Mendoza (“OSM”), appointed to hold the private contract to render the public service of production and distribution of drinkable water and treatment of industrial waste within the area of Mendoza.

After Sauri win the bid, OSM and the Province of Mendoza signed a concession contract, naming OSM as the agent of the public service provision for drinkable water and draining of sewerage systems.

Sauri realized an investment by two means:

- On the one hand, by the acquisition of 12,08 % of the capital of OSM, by paying US \$72,4 million;
- On the other hand, by the conclusion of a contract to provide technical support, naming Sauri as the technical operator in charge of performing activities related to management on behalf of OSM, in exchange of remuneration equivalent to 3% of the turnover of OSM.

The Respondent, the Republic of Argentina, is a party to the present arbitration because of the involvement of one of its provinces, Mendoza.

Even though both the concession contract and technical support contract have been correctly executed during the first years, the financial crises in 2002 had a great impact on their application. After suffering important losses, OSM requested that the price of water be raised. The Province of Mendoza was under the obligation to take emergency measures to face this newly challenged financial situation.

On November 17, 2003, Sauri introduced the present arbitration request before the ICSID, claiming that the Province of Mendoza had violated the principles established by the APPI.

On May 17, 2007, the Province of Mendoza and OSM concluded the Segunda Carta de Entendimiento, agreement establishing a methodology to determine the changes in fees. The parties agreed to raise the going rate by 19,7%.

The Governor of the Mendoza Province carried out an administrative intervention with OSM (“la Intervención”), with the aim of “reestablishing the

adequacy of the conditions of the provision of service, and assuring its continuity.” Said intervention was for an initial duration of 180 days, and had been renewed for 180 additional days by the executive power.

On July 12, 2010, the concession contract was terminated by the Governor, because of the non-compliance to its obligations by the dealer, OSM. (This violation will be further explained in Part III).

During the negotiations, the arbitration was suspended. However, the arbitral proceedings were reopened when Argentina failed to comply with the principles established by the APPI, failure constituted by the non-respect of the Segunda Carta de Entendimiento, by the Intervención with OSM, as well as by the immediate termination of the technical support contract.

The present arbitration is unusual. The very purpose of this Award is to quantify, by referring to a method of calculating subject to verification by the Tribunal, the compensation claimed by Sauri, investor affected by the expropriation committed by the Republic of Argentina, and thus entitled to receive full reparation for the damages suffered.

3. *Legal Issues Discussed in the Award*

(a) Exceptions of competence of the Tribunal

The Republic of Argentina claims that the Claimant has presented its allegation of violation of the principle of fair and equitable treatment in a subsidiary manner to the claim relating to expropriation. In this regard, said allegation is only of declaratory nature: “In the second place, if the Tribunal were to decide that there was no expropriation, to order the Republic of Argentina to compensate Sauri for an amount of US \$143,9 million, to account for its violations of the obligations of fair and equitable treatment and full protection and security.” Therefore, the Respondent found that the Arbitral Tribunal should not award the Defendant any damages for the violation of the principle of fair and equitable treatment.

In addition, Argentina argues that no compensation should be awarded to Sauri for the losses sustained subsequently to the Segunda Carta de Entendimiento. Instead, only injuries suffered prior to the date of entry into force of such contract should be compensated.

Lastly, the Respondent claims that the Tribunal exceeded its powers and rendered a decision *ultra petita*, by allocating to Claimant an amount of

compensation greater than which was sought. The Tribunal found that there was a direct expropriation by Argentina of the investments; whereas the Claimant had initially declared being victim of an indirect expropriation only.

The Arbitral Tribunal rejected the allegations of the Respondent, by deciding that:

- The demand, even if subsidiary in nature, was later modified by Sauri in its counter-claim, by raising to the same level the compensation relating to the violation of the principle of fair and equitable treatment, constituting the principal claim, and the two other alleged violations of the APPI.
- The Claimant did not waive its right to receive compensation for any losses sustained subsequently to the Segunda Carta de Entendimiento. Instead, Sauri affirmed that it is entitled to be awarded damages for the injuries suffered even after the effective date of such agreement, stating that “it would be necessary to reopen the debates on this precise question.”
- “The Republic of Argentina has adopted a series of measures which amount to expropriation, resulting to a dispossession of Sauri of its investment in the company OSM.” The Tribunal recognized the existence of a direct expropriation only, as alleged by the Claimant, and denied the existence of any indirect expropriation, as claimed by Respondent.

To sum up, the Arbitral Tribunal found that it acted within the scope of its competence and therefore did not clearly exceed its powers.

(b) Positions of the parties

Sauri argues that the Argentinian Republic failed to respect the principle of fair and equitable treatment, the principle of expropriation, as well as the principle of full protection and security regarding the investments. As such, the Claimant requests the Arbitral Tribunal to condemn Argentina to pay an amount of US \$40,225 million in damages. (It is relevant to note that this demand for compensation, which initially amounted to US \$143,9 million, has been considerably revised downwards).

Argentina requested that the Arbitral Tribunal reject each and every claim brought by Claimant, and condemn Claimant to the payment of all costs resulting from the present arbitration proceedings, pursuant to the terms of the convention established by the Republic of Argentina.

The Arbitral Tribunal reaffirmed its competence to hear the dispute and decided that only the principle of fair and equitable treatment and the principle of expropriation had been violated by the Respondent. However, the Tribunal found that Argentina had respected its obligation of full protection and security. Indeed, the Intervención was undertaken lawfully, in accordance with its legal dispositions, without harassment or threats of any sort.

(c) *Determination of the compensation*

Sauri argues that it is entitled to receive compensation for the violations committed by the Republic of Argentina: the Respondent not only has adopted measures of expropriation and nationalization, providing for a transfer of the concession contract to a new agent (direct expropriation), but also has failed to grant a fair and equitable treatment to the investment, by deciding to raise the rates and by purposefully postponing the entry into force of the Segunda Carta de Entendimiento.

Sauri sustains that the expropriation should be compensated in an amount of equal value than the investment in the shares of the company OSM (“Investment in shares”), and of the investment in accessory rights, in technical assistance and support (“Investment for technical support”). Also, the violation of the principle of fair and equitable treatment must be taken into account in determining the amount of damages to be paid.

These two above-mentioned types of investment, which constitute the core of the decision, will be discussed separately.

(i) *Value of the investment in shares*

In order to determine the amount of compensation due for the loss in value of Sauri’s investment in OSM, the Claimant based its reasoning on a hypothetical scenario “As if,” supposing that the violations of the APPI were never committed. This method allows to obtain the value that would have reached OSM at the date the Segunda Carta de Entendimiento should have become effective.

The expert for the Claimant undertook a valuation to determine the value of the investment in shares, by calculating the value of OSM using a discounted cash flow model actualized since the date at which the Segunda Carta de Entendimiento should have come into force, i.e., September 17, 2007, until the end of the concession in 2023. The Claimant adopted a discount rate of 6%. After

the expert's calculation, Sauri found that the loss it suffered, which corresponds to the value of its investment in shares, amounts to US \$20 907 000.

The Respondent rejected this valuation methodology, arguing that it is inappropriate, inasmuch as it does not exclude the compensations that OSM, and eventually Sauri, could be awarded by the tribunals of first instance of the Argentinian justice system, resulting in a double recovery for the same offense.

In addition, the Republic of Argentina criticized the effective date of the Segunda Carta de Entendimiento suggested by Claimant, arguing that such date is in January of 2008.

Finally, Argentina contends that the data used by the Claimant's expert are ex post data, which would not have been known in September of 2007 if the discount cash flow model had been done at this time.

After verifying the correctness of all the figures and hypothesis on which are based the valuation methodologies, the Arbitral Tribunal recognized the necessity of granting a compensation for damages based on a projection model of the value of the investment, should the violations of the APPI would not have been committed. Therefore, the Tribunal has rejected the allegations of the Republic of Argentina criticizing the valuation methodology introduced by Sauri.

As for the valuation date, the Tribunal has again ruled in favor of the Claimant, deciding that such date corresponds to the date the Segunda Carta de Entendimiento should have become effective, should the Respondent had not violated its obligations, i.e., September 17, 2007.

Similarly, the Tribunal joined Sauri in its position adopting a discount rate of 6%. By introducing the principle of free will of the parties, the Tribunal pointed out that in the present arbitration proceedings, Sauri and Argentina are free to agree upon a discount rate in a contractual provision. In the case before us, the parties negotiated the terms of the Segunda Carta de Entendimiento, establishing a reasonable discount rate of 6% in the agreement. This rate binds the parties.

However, the Arbitral Tribunal lined itself to the Respondent on a very particular point: the possibility for Sauri to receive a double compensation for the same offense, by requesting damages with other Argentinian tribunals. A true risk exists that both the Arbitral Tribunal and an Argentinian jurisdiction deliver a sentence on the same case.

To conclude, the Tribunal prove the Claimant right and determined that the value of Sauri's investment in shares in OSM amounts to US \$20 643 021 on September 17, 2007, that is, slightly below the amount of US \$20 907 000 claimed by Sauri.

(ii) Value of the investment for technical support

The second loss suffered by Sauri because of the breach of the APPI by Respondent ensues from the investment for technical support, Sauri being the technical operator of OSM.

The Claimant demands to receive compensation up to the revenues that he would have received in accordance with the contract for technical support, which was automatically terminated with the end of the concession contract.

The Republic of Argentina is opposed to all compensation by virtue of the concession contract, because according to Respondent, the Arbitral Tribunal does not have competence to hear the claim. Argentina justifies its position by the following objections as to the competence of the Tribunal:

- The existence of a jurisdiction clause naming the International Court of Arbitration of the International Chamber of Commerce, based in Geneva, as the competent authority;
- The fact that the technical support contract binds Sauri and OSM only, since it was exclusively concluded between these two entities, and does not concern Argentina.

The exceptions to the competence of the Tribunal alleged by the Argentinian Republic are groundless and inappropriate. The Arbitral Tribunal recognized its competence to hear the dispute and to determine the damages to be paid. The Tribunal affirmed the existence of a causal link between the violation of the provisions of the APPI by Argentina and the loss suffered by Sauri. The cause is constituted by the failure to respect the Segunda Carta de Entendimiento (giving rise to an unfair and inequitable treatment), together with the unlawful termination of the concession contract (giving cause for expropriation), and the effect is constituted by the hardship of a cash flow to Sauri arising from its investment for technical support.

As a consequence, Sauri was indeed expropriated and dispossessed of its investment in technical assistance, and for this reason, is entitled to receive

compensation in the amount of benefits that it stopped receiving by way of the contract.

After determining the existence of this causal relation, the Tribunal looked into the method of calculation of the value of the investment for technical assistance introduced by Sauri's expert.

The Claimant suggests calculating 3% of the revenues of OSM, obtaining by this way the revenues received as a technical operator, and to convert this amount to current value on September 17, 2007. The result obtained, US \$19 348 000, corresponds to the amount of receipts that Sauri failed to receive, that is to say, the value of the technical support agreement, and the compensation that should be paid for the loss.

The Respondent contends that the technical support agreement was concluded for a duration of five years, and was automatically canceled when the concession contract was terminated by the parties. According to Argentina, there was nothing in the contract or in the circumstances and behavior of the parties that suggested the parties would renew the agreement.

The Arbitral Tribunal settled the dispute by deciding the following: the validity of the technical support contract is supposed to be extended five year by five year, until the termination of the concession contract, as it is expressly provided for in article 6.1 of the technical support agreement, which states: "The present contract is concluded for a duration of five years (...) it will be renewed automatically for periods of five years until the termination of the concession contract, except as otherwise expressly provided by OSM at least 360 days before the maturity date of each period." The Tribunal concluded that it was neither legally well-founded, nor actually foreseeable or plausible, to believe that Sauri would not hope for a renewal of said contract. Indeed, Sauri has no reason to give up its right to receive the incomes ensuing from its investment in OSM.

After calculations, the Tribunal found that the total value of the incomes that Sauri was prevented to receive because of the wrongful termination of the contract for technical support amounts to US \$19 347 090.

By way of conclusion, by the present arbitral award, the Tribunal acceded to almost all of the claims introduced by Sauri. It found that Argentina had breached the principles established by the APPI and therefore was ordered to pay US \$39 990 111 for damages to Sauri's investment. According to the Tribunal, this amount is reasonable: it represents half of the amount that Sauri invested in

the project 15 years ago, project that generated almost no revenues, and represents the quarter of the compensation amount initially demanded by Sauri.

4. *Costs*

Since it agreed with Claimant on the issue of competence and on the violations of the APPI by Argentina, the Tribunal determined that the procedural costs must be supported by the Republic of Argentina, up to US \$686 500, as well as the defense-related costs (legal fees and accounting fees), for an amount of 1 486 975,13 euros.

5. *Decision*

The Arbitral Tribunal unanimously adopted the following decisions:

“ 1. The Tribunal condemns the Republic of Argentina to pay a compensation of US \$39 990 111 to Sauri.

2. The Tribunal condemns the Republic of Argentina to pay the interests on the principal amount of US \$39 990 111, payable since September 17, 2007, until the date of the present award, calculated according to an annual rate of 6% and compounded yearly.

3. The Tribunal orders the Republic of Argentina to reimburse US \$686 500 and 1 486 975 euros for the costs and legal fees which were borne by Sauri.

4. The Tribunal condemns the Republic of Argentina to pay the interests on the principal amount of US \$40 676 611 and of 1 486 975 euros, payable since the date of the present award, calculated according to an annual rate of 6% and compounded yearly.

5. The Tribunal rejects all other claim not contained in the above-mentioned condemnations.”