



School of International Arbitration

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International Arbitration Case Law

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IMPREGILO S.P.A.

V.

ARGENTINE REPUBLIC

(ICSID CASE NO. ARB/07/17),

AWARD

Case Report by Bingen Amezaga**

Edited by Natasha Dupont***

In an award rendered on June 21, 2011, the Arbitral Tribunal rejected Respondent's objections to the jurisdiction of the Centre and the competence of the Tribunal, and after dismissing Impregilo's claims of expropriation, declared that Argentine had breached the fair and equitable treatment standard established in Article 2.2 of the Italy-Argentine BIT. Professor Stern and Judge Brower each signed a concurring and dissenting opinion ("CDO").

Tribunal: Judge Hans Danelius (President), Professor Brigitte Stern and Judge Charles N. Brower.

Claimant's Counsel: Mr. R. Doak Bishop, Mr. Craig S. Miles, Mr. Roberto Aguirre Luzi, Ms. Silvia Marchilli, Mr. David Weiss, Mr. Joost Pauwelyn of King & Spalding LLP.

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Digest

1. Facts of the Case

In 1996, the Province of Buenos Aires (the "Province") decided to privatize its water and sewerage services and organized a bidding process for the concessions to be issued for the various areas of the Province.

Impregilo S.p.A. ("Impregilo"), an Italian corporation, formed a consortium with other companies to participate in the bidding process and was awarded one of the concession areas (the "Area"). Impregilo and its partners had to incorporate an Argentinean company to execute the Concession Contract (the "Contract"), and develop the activities related to the concession; therefore they incorporated the Argentinean company AGBA.

On December 7, 1999 the Province and AGBA executed the Contract, according to which AGBA acquired, for a period of thirty years, the exclusive right to collect, treat, transport, distribute and commercialize drinking water, as well as collect, treat, dispose and potentially reuse or commercialize sewage, including industrial sewage in the Area.

In consideration for the concession, AGBA made an initial payment of US\$1,260,000 to the Province, and obligated itself to maintain and renew the facilities and in particular, to comply with the Service Optimization and Expansion Program ("POES"), which consisted of six consecutive "Five Years Plans" establishing quantitative and qualitative goals to be attained by the Concessionaire. On the other hand, the Contract provided that AGBA has the right to be paid a tariff for the service, which, according to Article 12.1.1, should "cover all operating expenses, maintenance expenses and service amortization" as well as "provide a reasonable return on the Concessionaire's investment subject to efficient management and operation by the Concessionaire and strict compliance with the applicable service quality and expansion goals."

On January 3, 2000 AGBA took possession of the concession, and the first Five Year Plan was approved by the State Regulator "Organismo Regulador de Aguas Bonaerense" ("ORAB") on January 31, 2001.

On May 2001, in view of the considerable difficulties to collect payment from customers, Impregilo sent a letter to the Minister of Public Work and Services of the Province (the "Minister") requesting analysis of appropriate solutions, and asking for the temporary suspension of the expansion goals set in the POES.

The Minister rejected the principle of the request, asserting that the issue of the rate of non-collection was a business risk assumed by AGBA, but agreed to set up a working commission to analyze possible contractual modifications.

The economic crisis hit Argentina in 2001, worsening the tariff collections problem of Impregilo and at the same time provoking the implementation of several urgency measures by the Argentine Government which also affected Impregilo's business. Those measures were, in particular, the "pesification" at parity level of utilities' contracts, the freezing of public services tariffs (implemented by ORAB in the Contract on January 11, 2002) and a Decree authorizing a new regulatory framework for water services.

ORAB also issued Resolution N° 14/02 that prevented AGBA from billing work charges, and on August 27, 2002, suspended AGBA's right to interrupt water service to customers who had not paid their bills.

On numerous occasions from mid 2001 to 2005, AGBA insisted before ORAB and other Government entities on renegotiation of the Contract in order to restore the concession's economic equilibrium. AGBA also challenged the Decree implementing the new regulatory framework for water services in the Province.

On December 2002, ORAB decided that AGBA had met the service expansion and quality goals of the first year of the concession, and granted AGBA's request for suspension of the POES obligations in the second concession year, but the parties failed to reach any agreement concerning the renegotiation of the Contract.

On July 10, 2006, following a report on the performance of the concession's holders concluding that AGBA had violated several of its obligations under the Contract and the POES, the new regulatory authority, OCABA, fined AGBA. The next day, the Province Governor terminated the Contract, and two days later, AGBA's concession was transferred to a company controlled by the State named ABSA.

On July 25, 2007, the ICSID registered the request for arbitration filed by Impregilo against Argentine under the n° ARB/07/17.

2. *Legal Issues Discussed in the Decision*

a) Issues of Jurisdiction

i. Jurisdiction Requirements under the BIT and Most Favored Nation ("MFN") Clause (§§ 79-109; see also CDO of Professor Stern)

The first objection to the jurisdiction of the Tribunal by Argentina was that Impregilo did not comply with the requirements set forth in Article 8(2) and 8(3) of the BIT, which requires investors to submit their dispute to domestic courts for 18 months before filing international arbitration proceedings.

The Arbitral Tribunal concluded that said provisions should be interpreted as containing a jurisdictional requirement that had to be fulfilled before submitting the dispute to international arbitration, and "Impregilo not having fulfilled this requirement, the Tribunal cannot find jurisdiction on the basis of Article 8(3) of the BIT." (§ 94)

However, after reaching that conclusion, the majority considered whether the MFN clause in Article 3(1) of the BIT allowed Impregilo to rely on the provision of Article VII of the Argentine-US BIT, which provides that investors have the choice to submit the dispute to domestic courts or, after six months from the date on which the dispute arose, to international arbitration..

The majority noted that, "the term 'treatment' in the MFN clause is in itself wide enough to be applicable also to procedural matters such as dispute settlement. Moreover, the wording 'all other matters regulated by this Agreement' is certainly wide enough to cover the dispute settlement rules," (§ 99) and rejected Argentine's argument that the application of the *ejusdem generis* principle would limit the application of the MFN clause only to matters similar to "investments."

As regards to Argentine's argument that resorting to domestic courts cannot be deemed as something unfavorable for investors, the majority reasoned that, "what should be considered is whether a choice between domestic proceedings and international arbitration, is more favorable to the investor than compulsory domestic proceedings before access is opened to arbitration" and concluded that "a system that gives a choice is more favorable to the investor than a system that gives no choice." (§ 101)

Finally, even if admitting that "these issues remain controversial and that the predominating jurisprudence which has developed is in no way universally accepted", the majority considered that "in cases where the MFN clause has referred to 'all matters' or 'any matter' regulated in the BIT, there has been near unanimity in finding that the clause covered the dispute settlement rules." (§ 108)¹

The majority therefore concluded that Impregilo was entitled to rely on the Article VII of the Argentine-US BIT, and that "the case cannot be dismissed for non-observance of the requirements in Article 8(2) and (3) of the BIT." (§ 108)

Professor Stern dissented from the majority in this aspect and stated that the MFN clause cannot be used to create the arbitral tribunal jurisdiction.

In her Concurring and Dissenting Opinion, acknowledging the apparent predominance of awards applying the MFN clause to dispute resolution but

¹ The majority quoted in particular the jurisdiction decisions in *Maffezini v. Spain*, *Gas Natural v. Argentina*, *Suez v. Argentine Republic*, *Vivendi v. Argentina* and *Camuzzi v. Argentine Republic*.

noting a more even split among arbitrators, and emphasizing the non-binding character of the former decisions, Professor Stern pointed out that Article 3 of the BIT and Article VII of the Argentine-US BIT relied on completely different and incompatible procedures, and that consequently, "the concrete result is not to grant Impregilo the most favorable existing dispute settlement mechanism, which is the purported objective of MFN clauses, but it is to grant it a *sui generis* mechanism that was constructed by the reasoning of the arbitrators forming the majority and was envisaged neither in the basic treaty nor in the third-party treaty."(CDO of Professor Stern ¶12)

Professor Stern took the opportunity to express why, in her view, MFN clauses should not import a dispute settlement mechanism from a third-party treaty into the BIT, unless the contrary is expressly provided.

Rather than adopting the reasoning of other Tribunals that arrived at the same conclusion (clause "specifically negotiated" (*Plama, Tza Yap Shum v. Peru*), distinction between substantive matters and procedural matters (*Telenor Mobile v. Hungary*), distinction in the MFN clause between investment and investors (*RosInvestCo v. Russian Federation*)), Professor Stern proposed to base the analysis on a distinction between the qualifying conditions for access to rights and the rights themselves. A MFN clause can only concern the rights that an investor can enjoy, but it cannot modify the fundamental conditions for the enjoyment of such rights. As the other qualifying conditions to access to jurisdiction (*rationae personae, rationae materiae and rationae temporis*) were not affected by MFN clauses, then the condition *rationae voluntatis* should not be impacted either.

ii. *Indirect claims and the risk of double recovery* (¶¶ 137-139)

The Tribunal had to resolve the argument of Argentina that Impregilo's claims were in fact indirect claims of a separate company, AGBA, relating exclusively to the execution of the Contract.

The Tribunal started by noting that the formation of the Argentine company AGBA was a requirement of the bidding rules imposed by Argentina. Then, the Tribunal reasoned that since the Article 1(1)(b) of the BIT protected Impregilo's shares in AGBA, if AGBA was subjected to expropriation or unfair treatment, such illegal actions would thus affect Impregilo's rights as an investor under the BIT. The Tribunal relied on the substantial case law showing that claims presented by shareholders enjoy protection under the BIT, and dismissed the objection.

Regarding the risk of double recovery, the Tribunal recognized that if compensation were granted at the domestic level, this would affect Impregilo's claims under the BIT and conversely, any compensation obtained by Impregilo under the BIT would affect the domestic claims of AGBA.

iii. Contractual claims and clauses of choice of jurisdiction (¶¶ 173-189)

After noting that it was AGBA which executed the Contract and not Impregilo, the Tribunal rejected that the choice of jurisdiction clause in the Contract could be considered to exclude recourse to arbitration under the BIT in cases of a dispute about acts which might constitute breaches of both the Contract and the BIT.

The Tribunal admitted that some of Impregilo's claims concerned mere contractual issues, while also considered that Impregilo's claims of expropriation, unfair treatment and discrimination were beyond contractual breaches, even if shared the same factual basis.

The Tribunal thus partially upheld Argentine's jurisdictional objection, but only regarding the contractual breaches which do not, at the same time, involve violations of Argentine's obligations to investors under the BIT.

b) Merits

i. Expropriation (¶¶ 268-283; See also Judge Brower CDO, ¶¶ 17-34)

The Tribunal stated that expropriation should be distinguished from less far-reaching measures which regulate or restrict the right to use property, while acknowledging the existence of borderline cases which amount to the deprivation of property (indirect expropriation and creeping expropriation).

The Tribunal concluded that, although they affected AGBA's rights, none of Argentine's acts amounted to a loss of the concession or a loss of property rights. The loss only occurred when the Province terminated the concession.

Notwithstanding any Argentine goal to transfer water and sewerage services to public entities, in the Tribunal's view, what was decisive on the issue of whether an expropriation occurred was whether the reasons given by the Province for the termination constituted legally valid grounds for termination according to the Contract. The Tribunal observed in this respect that the reasons given by the Province for the termination were extensive and specific, and revealed that AGBA considerably failed to carry out its undertakings. The Tribunal considered these findings sufficient to exclude the termination as an act of expropriation

Judge Brower dissented from the majority. In his view, the award wrongly disregarded the possibility of an indirect expropriation, and also failed to address as expropriatory other acts and omissions of Argentine that cumulatively diminished AGBA's value.

ii. Fair and Equitable Treatment (¶¶ 284-331; See also Judge Brower CDO, ¶¶ 2-16)

The Tribunal affirmed the distinction between legitimate expectations under international law and contractual rights, and concluded that, in so far as the Province's acts are exclusively contractual, they cannot amount to a violation of the fair treatment standard based on the theory of legitimate expectations.

Subsequently, the Tribunal analyzed whether the Province's acts in relation to the Contract not only constituted a breach of such contract but were, at the same time, a misuse of Argentine's sovereign power. The Tribunal did not find that the Province's acts implicated the misuse of public power and decided that they could not invoke Argentine's responsibility under the BIT.

Thereafter, the Tribunal analyzed Argentine's acts other than those performed by the Province as a party to the Contract, and in particular the emergency legislation that pesified utilities' contracts at parity level and froze tariffs, and the new regulatory framework enacted by the Decree in 2003.

The Tribunal noted that AGBA had no guarantee that the exchange rate would remain the same, or that the contractual framework would be maintained. However, as those measures altered the economic balance guaranteed by Article 12.1.1 of the Contract, Argentine was under the obligation of restore the economic equilibrium, which it failed to do, notwithstanding Impregilo's numerous requests. The Tribunal concluded that by failing to restore a reasonable equilibrium in the concession, Argentine aggravated Impregilo's situation to such an extent as to constitute a breach of its duty under the BIT to afford fair and equitable treatment to Impregilo's investment.

Judge Brower considers that Argentine not only breached its fair and equitable treatment obligations by the reasons explained by the majority but that the Republic also violated those obligations through many other contractual violations which in his view frustrated Claimant's expectations and arbitrarily disrupted the Contract balance.

iii. State of Necessity (¶¶ 336-360)

The Tribunal examined Argentine's necessity plea under the standard set by customary international law, and in particular by the International Law Commission's Articles on Responsibility of States for Internationally Wrongful Acts ("ILC Articles").

After admitting that Argentine's economic crisis constituted "grave and imminent peril" to the State's essential interests within the meaning of the ILC Articles, the Tribunal considered whether the other criteria set by the ILC Articles were fulfilled. (¶ 250)

The Tribunal rejected Impregilo's argument that its own interest as an Italian legal entity must be taken into account in the balancing required under ILC Article 25, paragraph 1(b), since the interests of a small number of Contracting State's nationals or legal entities not qualify as an "essential interest" of that State.

Then, the Tribunal examined the requirement of ILC Article 25, paragraph 2(b) according to which, if the State concerned has contributed to the situation of necessity, the application of the necessity defense will be excluded. Regarding this requirement, the Tribunal affirmed that the State's contribution does not need to be specifically intended or planned but also can be the consequence of well-intended but ill-conceived policies.

As for the level of contribution required, the Tribunal referred to the Commentary of the ILC Articles according to which the contribution should be substantial and not merely incidental. On this point, the Tribunal concluded that even if other elements affected the economy of Argentine, Argentine's own economic policies over several years before the crisis rendered the economy of the country vulnerable to exogenous shocks and pressures, and impacted adversely the sustainability of its economic model on the national and local levels.

The Tribunal therefore found that Argentine contributed significantly to its "situation of necessity" and thus, did not satisfied the conditions set forth in ILC Article 25, excluding the application of the state of necessity defense.

Professor Stern considers that the substantial contribution of the Argentine authorities to the crisis has not been satisfactorily proven, but since the violation of the fair and equitable treatment's obligations continued after the crisis, she concurs with the decision on the merits.

iv. Compensation (¶¶ 361-381, see also Judge Brower CDO, ¶¶ 35-38)

The Tribunal proposed to implement the principle of reparation derived from the *Chorzow Factory* case, and in consequence, to re-establish the situation in which, with all probability, Impregilo would have been, had Argentine's violations of the BIT not occurred.

After considering all the circumstances, and in particular, the fact that the concession covered a very poor area with significant rates of non-collectability, the difficulties experienced by AGBA at the beginning of the concession period, and the need for substantial investments from the side of the investor, the Tribunal concluded that it was not sufficiently established that, even in the absence of the illegal acts of Argentine, the concession would have been profitable for AGBA.

Therefore, the Tribunal considered inappropriate to calculate damages on the basis of cost or asset-based method, or an income method, preferring to perform a reasonable estimation of the loss.

The Tribunal finally decided that Argentine should compensate Impregilo only on the amounts that Impregilo invested in the concession.

Judge Brower did not approve the premise of the “shared responsibility” applied by the majority and considers that the value of the investment should be determined by using the Discounted Cash Flow method, which is customarily applied to ventures that are “going concerns.”

v. Interest (¶¶ 382-384, see also Judge Brower CDO ¶¶ 39-40)

Regarding the starting point to calculate the interest, the Tribunal stated that there was not a precise point in time when the unfair treatment took place. The Tribunal then chose the date of the Contract’s termination as the starting point for Argentine’s duty to pay interest, since there can be no doubt that by this date its breaches of the BIT had culminated.

Judge Brower dissented from the majority by pointing out that the acts which were designated by the majority as the basis to decide that Argentine had violate its fair and equitable treatment obligations, took place in 2002 (“pesification”), and 2003 (New Regulatory Framework), so the award should have compensated Claimant for those three “lost” years by including them in its interest calculation.

3. Decision

The Tribunal dismissed Respondent’s objections to the jurisdiction of the Centre and the competence of the Tribunal save for the claims that were merely contractual.

On the merits, after dismissing Impregilo’s claims of expropriation, the Tribunal declared that Argentine violated the BIT by failing to treat Impregilo’s investment in a fair and equitable manner. The Tribunal considered unnecessary to determine whether Respondent impaired Impregilo’s investment by unjustified and discriminatory measures, or failed to grant full protection and security to the investment.

Finally, the Tribunal decided that Argentine should compensate Impregilo for the damages it has suffered in the amount of US\$21,294,000 and interest on that amount, compounded annually, at the rate of 6 % from the date of the termination of the Contract by the Province.