INTERNATIONAL CENTRE FOR THE SETTLEMENT
OF INVESTMENT DISPUTES

ICSID CASE No. ARB/10/23

TECO GUATEMALA HOLDINGS LLC

CLAIMANT

V.

REPUBLIC OF GUATEMALA

RESPONDENT

MEMORIAL ON OBJECTIONS TO JURISDICTION AND ADMISSIBILITY AND COUNTER-MEMORIAL ON THE MERITS

24 JANUARY 2012

The Republic of Guatemala (***Guatemala***) presents its Memorial on Objections to Jurisdiction and Admissibility and Counter-Memorial (***Memorial on Objections and Counter-Memorial***) in accordance with point 13 of the Minutes of the First Session of the Tribunal, and the Parties' agreement that the parties confirmed for the Tribunal via e-mail of the Secretariat of the Tribunal of October 31, 2011. This Memorial of Objections and Counter-Memorial respond to the Memorial of TECO Guatemala Holdings, LLC (***TGH*** or the ***Claimant***) of September 23, 2011 (***Claimant's Memorial***).

Guatemala uses the acronym "TGH" to refer to the Claimant and not "TECO" as the Claimant did in its Memorial,[1] so as to avoid confusing the Claimant with other companies in the TECO group that are currently, or were previously, part of the corporate structure of this investment. It is curious that TGH preferred to use the reference "TECO" in its Memorial when in its Notice of Arbitration it elected to use "TGH." This change creates confusion regarding the identities of the group's companies and the transfer of allegedly legitimate expectations between them. TGH attempts to benefit from any such expectations even though TGH did not exist at the time of EEGSA's privatization in 1998 and did not come into existence until 2005, as explained below.[2] Guatemala uses the term "Teco" to refer to the other companies of the holding group that are distinct from TGH.

Guatemala attaches to this Memorial on Objections and Counter-Memorial the witness statements of Mr. Carlos Colóm and Enrique Moller, and Messrs. Alejandro Arnau, Mariana Álvarez Guerrero and Leandro Torres of Mercados Energéticos S.A. In addition, it attaches the expert reports of Mr. Mario Damonte and of Messrs. Manuel Abdala and Marcelo Schoeters and of Dr. Juán Luis Aguilar Salguero. Finally, Guatemala attaches 9 appendixes, 162 exhibits numbered R-1 to R-162, and 17 doctrinal and jurisprudential exhibits numbered R-1 to R-17.

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1 Claimant's Memorial, para. 1.

2 See Section IV.C below.

This Memorial on Objections and Counter-Memorial has been written in Spanish and translated to English. Any discrepancy between the English and Spanish versions should be resolved with reference to its official version in the Spanish language.

I. INTRODUCTION

1. The claim asserted by TGH is a mere regulatory complaint under Guatemalan law, disguised as a claim under the CAFTA-DR (the ***Treaty***). This disguise is not convincing.

2. TGH's claim is that, in setting the electricity distribution tariffs for the 2008-2013 period for Empresa Eléctrica de Guatemala S.A. (***EEGSA***), the electricity regulator in Guatemala (the ***CNEE***) did not properly apply the Guatemalan regulatory framework. Since that regulatory framework provided the basis for its original investment, TGH claims that such allegedly defective application by the regulator frustrated its expectations as a shareholder in EEGSA. This is TGH's claim.

3. As stated in the case of *Azinian v. Mexico*, "*labelling is no substitute for analysis.*"[3] A simple analysis of the facts presented demonstrates that TGH has submitted to this Tribunal a simple dispute of a regulatory nature concerning different interpretations of certain procedural issues related to the review of tariffs established by the General Electricity Law (the ***LGE***) and the Regulations of the General Electricity Law (the ***RLGE***).[4]

4. TGH wants this Tribunal to decide on the proper interpretation of the regulations: the one that TGH shares with EEGSA on one hand, or that of the CNEE on the other. This is evidenced by the title of the section of the Claimant's Memorial in

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3 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2), Award, 1 November 1999, **Exhibit RL-2**, para. 90.

4 General Electricity Law, Decree No. 93-96 of the Congress of the Republic, 16 October 1996 (***LGE***), attached to the Memorial as **Exhibit R-8**; Regulation of the General Electricity Law, 21 March 1997 and its modifications (***RLGE***), **Exhibit R-36**.

which TGH explains how Guatemala supposedly breached the minimum standard of treatment pursuant to Article 10.5 of the Treaty. Here, TGH states:

> Guatemala breached its Treaty obligation to accord TECO's investment fair and equitable treatment when it arbitrarily and in complete disregard of its legal framework ignored the Expert Commission's report and set the tariffs on the basis of its own study.[5]

5. In other words, TGH plainly and simply tries to have an ICSID Tribunal – which was constituted on the basis of an international treaty and which must judge the international responsibility of the Republic of Guatemala – decide whether a tariff review procedure has been properly followed. This is an eminently regulatory issue of Guatemalan domestic law. An issue that, furthermore, has already been raised by EEGSA before the regulatory body with jurisdiction (the CNEE) and before the highest level of the Guatemalan courts – the Constitutional Court.

6. Despite confirmation from the Guatemalan courts that the CNEE did indeed properly apply the Guatemalan regulatory framework, TGH asks this Tribunal to ignore the conclusions of the regulator and of the local courts. It asks, among other things, that this Tribunal repeat the entire tariff review, complaining that Guatemala breached the Treaty when in 2008 it approved a Value-Added for Distribution (***VAD***) for EEGSA − the component of the electricity distribution tariff that must be paid to the distributor for its costs − that was "unlawful and unjustifiably low."[6]

7. This is not a task for an international tribunal, which is responsible for judging the international responsibility of a State but is not competent to rule on the simple interpretation of domestic regulatory provisions. Much less can it request that such a tribunal determine the correct VAD or the proper tariff for EEGSA. First of all, these are matters for the regulator, the CNEE, and, secondly, for the control

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5 Claimant's Memorial, title of Section III.C.

6 *Ibid.*, title of Section II.F.7.

of the Guatemalan courts and tribunals. Therefore, TGH's claim is not justiciable by this Tribunal.

8. It is a basic principle of international law that a disagreement over the interpretation and application of domestic law does not automatically become an international dispute. As the International Court of Justice stated in its decision in the *Case Concerning Ahmadou Sadio Diallo*:

> The Court recalls that it is for each State, in the first instance, to interpret its own domestic law. The Court does not, in principle, have the power to substitute its own interpretation for that of the national authorities, especially when that interpretation is given by the highest national courts.[7]

9. This reasoning equally applies to disputes related to investment treaties. In the case of *Encana v. Ecuador*, the tribunal stated:

> […] But there is nonetheless a difference between a questionable position taken by the executive in relation to a matter governed by the local law and a definitive determination contrary to law. In terms of the [treaty] the executive is entitled to take a position in relation to claims put forth by individuals, even if that position may turn out to be wrong in law, provided it does so in good faith and stands ready to defend its position before the courts. Like private parties, governments do not repudiate obligations merely by contesting their existence […].[8]

10. Furthermore, the tribunal in *SD Myers v. Canada* established the basic rules in relation to the minimum standard of treatment:

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7 *Case Concerning Ahmadou Sadio Diallo (Republic of Guinea v. Democratic Republic of the Congo)* Decision, 10 November 2010, **Exhibit RL-15**, para. 70. The Court continues: "Exceptionally, where a State puts forward a manifestly incorrect interpretation of its domestic law, particularly for the purpose of gaining an advantage in a pending case, it is for the Court to adopt what it finds to be the proper interpretation."

8 *EnCana Corporation v. Republic of Ecuador* (LCIA Case No. UN3481, UNCITRAL Rules) Award, 3 February 2006, **Exhibit RL-9**, para. 194 (Emphasis added).

> [The] tribunal does not have an open–ended mandate to second–guess government decision–making. Governments […] may appear to have made mistakes, to have misjudged the facts, […] The ordinary remedy, if there were one, for errors in modern governments is through internal political and legal processes, […]. The Tribunal considers that a breach of Article 1105 [minimum standard of treatment] occurs only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders […].[9]

11. These rules were directly applied by the tribunal in *Saluka v. Czech Republic*:

> The Treaty cannot be interpreted so as to penalise each and every breach by the Government of the rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State.[10]

12. The tribunal ruled in the same manner in the case of *Glamis Gold v. United States*:

> [T]he Tribunal first notes that it is not for an international tribunal to delve into the details of and justifications for domestic law. […] the proper venue for its challenge was domestic court. […] It is not the role of this Tribunal, or any international tribunal, to supplant its own judgment of underlying factual material and support for that of a qualified domestic agency.[11]

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9 *SD Myers Inc v. Canada* (UNCITRAL Case) First partial award, 13 November 2000, **Exhibit CL-41**, paras. 261 and 263 (Emphasis added).

10 *Saluka Investments B.V. v. Czech Republic* (UNCITRAL Case) Partial award, 17 March 2006, **Exhibit CL-42**, para. 442.

11 *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit CL-23**, paras. 762, 779.

13. In the 2008 EEGSA tariff review process, the CNEE applied the same basic principles provided for in the LGE and the RLGE, under which TECO made its investment. Naturally, the CNEE acted as the regulator and implemented this procedure based on its interpretation of the regulatory framework, in accordance with its jurisdiction. TGH may disagree with this interpretation. It is common for a regulated company to be in disagreement with decisions made by the regulator. These disagreements are put before local courts and tribunals. The mere interpretation of a regulatory framework is a matter of domestic law.

14. EEGSA and TGH clearly understood this when they resorted to the courts in Guatemala to challenge the same regulatory decisions about which TGH complains in this arbitration. On that occasion, EEGSA and TGH took their claim up to the Constitutional Court, the highest court of Guatemala and the body that safeguards the interpretation of the Constitution and the laws.

15. The Constitutional Court decided on the contested points of the tariff procedure and ruled in favor of the CNEE. Having obtained well-founded decisions from the Constitutional Court that rejected its claims, TGH now, under the guise of a claim based on the Treaty, wants this Tribunal to become a court of *last instance* in the matter. This is not the function of this Tribunal. As the tribunal observed in *Azinian v. Mexico*:

> The possibility of holding a State internationally liable […] does not, however, entitle a claimant to seek international review of the national court decisions as though the international jurisdiction seised has plenary appellate jurisdiction.[12]

16. This was confirmed by the tribunal in *Generation Ukraine v. Ukraine* with respect to the application of regulatory provisions of Ukrainian law, in highly technical matters, by the local authorities:

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12 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2), Award, 1 November 1999, **Exhibit RL-2**, para. 90.

> […] This Tribunal does not exercise the function of an administrative review body to ensure that municipal agencies perform their tasks diligently, conscientiously or efficiently. That function is within the proper domain of domestic courts and tribunals that are cognisant of the minutiae of the applicable regulatory regime. […] the only possibility in this case for the series of complaints relating to highly technical matters of Ukrainian planning law to be transformed into a BIT violation would have been for the Claimant to be denied justice before the Ukrainian courts in a *bona fide* attempt to resolve these technical matters.[13]

17. Only if the Guatemalan justice system had denied justice to EEGSA/TGH could a valid international claim come to exist.[14] But TGH does not claim denial of justice. Nor could it, because at no time was justice denied by the Guatemalan courts.

18. TGH naturally attempts to raise the language of its claim, aware that the facts do not justify a claim under the Treaty. It claims that the position that a domestic regulator takes within the scope of its jurisdiction is an "alter[ation of] the legal and business environment,"[15] simply because the regulated entity disagrees with the regulator's position. But, as indicated previously, this is an implausible proposition. If one were to accept this thesis, any country that has attracted foreign investors to its regulated sectors would be forced to defend itself in an international investment arbitration whenever the investors disagree with a regulatory decision or with the decisions of its domestic courts regarding the proper interpretation of those regulations. Fortunately, this Pandora's Box has not been opened. International case law has consistently rejected these types of arguments.[16]

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13 *Generation Ukraine, Inc. v. Ukraine* (ICSID Case No. ARB/00/9) Award, 15 September 2003, **Exhibit CL-26**, paras. 20.33.

14 E.g., *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, 1 November 1999, **Exhibit RL-2**, paras. 82-84, 87, 96-97, 100.

15 E.g., Claimant's Memorial, para. 270.

16 See Sections II.A.2 and IV.A below.

19. TGH also tries to suggest that the amendment of a provision of the Regulations, Article 98, could constitute a fundamental alteration of the legal framework. TGH tries to compare this regulatory modification (which is completely legitimate) to what occurred in cases related to the Argentine emergency legislation, in which the tariff regimes of public utilities were completely abolished and concessions and licenses were forcibly renegotiated. The absurdity of this comparison alone reflects how far this case is from the *Argentine cases.*

20. Here, the tariff regime has not been abolished by law or altered in a way that would derogate or suppress the rights of EEGSA concerning the setting of tariffs. In fact, the amendment to Article 98, which appears to offend TGH, occurred in 2007 (although its immediate precedent was in 2003) and passed by EEGSA (and TGH) apparently unnoticed until the beginning of this arbitration. There was no questioning, formal or informal, of this regulatory provision. This is clear proof of the opportunistic character of the complaint that TGH now presents.

21. While, for the above reasons, it does not fall to this Tribunal to examine the tariff review process for the 2008-2013 period, there are certain facts in this arbitration that merit special consideration. One example reveals that EEGSA tried to impose its will upon the CNEE during the tariff review process that is the subject of this arbitration.

22. On April 22, 2008, while the review process was fully underway, the CNEE Board of Directors received a visit from Mr. Gonzalo Pérez, President of EEGSA, who resided in Mexico and, until then, had no direct involvement in the tariff review process. Mr. Pérez's request for a meeting drew the attention of the CNEE Board of Directors. At that meeting, Mr. Pérez gave the CNEE Directors a presentation. In the presentation, EEGSA proposed replacing the VAD increases of 100 percent or more, which were requested in its own tariff studies that were currently underway, with an increase of just 10 percent.

23. TGH seeks to paint this "offer," made in person by EEGSA President, Mr. Gonzalo Pérez, as a legitimate and transparent possibility. It was so transparent

that the offer was made at an in-person meeting with no pre-established agenda, by means of a single copy of a document, without letterhead, with no e-mail of introduction or follow-up, and with no mention of the real names of the people and companies involved.

24. TGH anticipates this fact (since it knew that this issue was discussed in the parallel arbitration filed by its co-shareholder, Iberdrola) and discusses secondary matters in its attempt to justify the legality of this proposal. However, TGH avoids explaining the truly relevant issue surrounding it: why would EEGSA have made an offer of this magnitude if it truly believed that the study that its consultant had prepared complied with the regulatory framework? EEGSA is not a charitable institution and, if its consultant's tariff study had been credible, there would have been no reason (or justification to its own shareholders) for offering, as Mr. Pérez did, a 90% (!) discount in the tariffs that were to be valid for the next five years.

25. Mr. Pérez left the meeting empty-handed. This was because the CNEE insisted on upholding the Rule of Law and the proper and legitimate technical application of the regulatory framework. Curiously, Mr. Pérez has not been called by TGH to testify in this arbitration nor was he summoned to testify in the arbitration filed by Iberdrola.

26. This is the story of this tariff review process: EEGSA sought to manipulate the regulatory framework in its favor in every way possible, and the CNEE had to deal with these manipulative attempts by making the regulatory framework prevail.

27. Thus, for example, EEGSA refused to make its reports auditable and refused to submit information to support the costs it claimed, intentionally preventing the CNEE from performing its role as supervisor and guarantor of compliance with the LGE.

28. Likewise, EEGSA sought to obtain remuneration based on the gross value of its assets; EEGSA argued that the process to set EEGSA's New Replacement Value (***VNR***) required an assumption that each asset in its network was brand new, despite the fact that this not only violated the LGE and the formula set forth in the Terms of Reference, but also basic principles of regulatory economics that determine that the return is always calculated based on the investment, net of accumulated depreciation.

29. In an excess of prudence, Guatemala has made a great effort to refute each and every false technical and factual issue upon which TGH rests. Guatemala does so to prove that it has acted in good faith and according to technical criteria throughout the tariff review process. It also does this to demonstrate that the CNEE refused to be intimidated into accepting a tariff study that could not be verified according to its regulatory obligations.

30. However, in the words of the *Glamis* decision, it does not fall to this international Tribunal to examine the whys and wherefores of domestic law. Nor does it correspond to this Tribunal to substitute the decision of the competent national agency (the CNEE), regarding an extensive technical case, with its own decision. Especially not when the validity of said agency's decision has been upheld by the country's highest court, the Constitutional Court.

31. Finally, it is necessary to point out TGH's sensationalist strategy of accusing the CNEE and the Constitutional Court of engaging in conduct guided by political influences during EEGSA's tariff review.[17] Given the seriousness of these allegations, one would expect that some proof or support be given. However, TGH presents no evidence; it simply wants the Tribunal to accept its mere speculations. In addition, since TGH does not claim a denial of justice, it is not clear what it wishes to achieve with these assertions.

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17 E.g., Claimant's Memorial, paras. 228, 259, 212, 277, 280.

32. If it occurred to anyone to attempt to "politically" influence the Constitutional Court, it was EEGSA's foreign shareholders themselves, including TGH. In early 2010, these shareholders considered the possibility of pressuring the Constitutional Court with respect to a potential appeal concerning the scope of Article 98 of the RLGE:

> We have concluded that the challenge is feasible. We are already working on arguments, and we suggest the participation of 3 politically powerful attorneys in order to obtain a favorable decision.[18]

33. The reality is that neither the CNEE nor the Constitutional Court act under political influence. Guatemala cannot be put in the logical impossibility of proving a negative fact based on mere conspiracy theories.

34. Suffice it to say, TGH's claims are completely inconsistent with the level of foreign investment recorded in the Guatemalan electricity sector in recent years. Also unjust is TGH's criticism of the Constitutional Court, a body that has ruled against the National Government on repeated occasions and has ordered favorable tariff increases to EEGSA, even after the approval of the tariff schedule that is the subject of this arbitration.

35. The unjust and abusive nature of TGH's claim is also clear if one considers the sale of its share in EEGSA on October 21, 2010, just one day after initiating this Arbitration. In its Notice of Arbitration of October 21, 2010, TGH said that EEGSA's "long-term sustainability" was "jeopardize[d]" and that this "severely undermined [its] operational viability."[19] Also, in its Notice of Intent to Submit a Claim to Arbitration filed against Guatemala on 9 January 2009, TGH claimed that its investment in Guatemala was "severely jeopardize[d]."[20] However, the day after launching this arbitration, TGH received an amount close to US$ 121.5

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18 Presentation of the 2009 DECA II Administration, **Exhibit R-107**, p. 17 of the PDF.

19 Notice of Arbitration, para. 69.

20 Notice of Intent, Exhibit 3 of the Notice of Arbitration, para. 28.

million for its shares in EEGSA, in accordance with the valuation prepared by its own financial advisor for the sale of these shares, Citibank.[21]

36. Furthermore, in the sale process, EEGSA's foreign shareholders presented this company to the buyer in September 2010 as:

> One of the best and most solid companies in the country.[22]

37. EEGSA was therefore neither unviable nor severely undermined nor was it severely jeopardized. Nor, as TGH tells this Tribunal in the Memorial, was the VAD approved by the CNEE in 2008 "economically devastating."[23] Quite the contrary, in TGH's own words (through the holding company): EEGSA was one of Guatemala's best and most solid companies.

38. The reality is that TGH launched this arbitration once it knew that it was going to receive tens of millions of dollars for its share in EEGSA, in order to obtain the benefit of double compensation (*double recovery*). It is clear from its decision to wait more than two years from the time that the allegedly unlawful events occurred and nearly 22 months from the Notice of Intent. Nothing would explain this delay except that it is aware of the merely opportunistic and speculative nature of its claim. With the sale, TGH knew that it would lose its investor status under the Treaty, and so it presumably decided that it did not have much to lose by trying to get a double compensation by suing Guatemala in this arbitration.

39. In order to do so, TGH points out that its sale was motivated by the alleged adverse measures of the CNEE. However, its declared motive was the TECO group's strategic and commercial approach of focusing on its power generation assets in Guatemala, as it explained to the market following the sale:

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21 Letter from Citibank to Board of Directors of Teco Energy, Inc., 14 October 2010, **Exhibit R-128**, pg. 7 (C-1-01) sheets 7 y 8.

22 Deca II – Management Presentation, September 2010, **Exhibit R-127**, pg. 22.

23 Claimant's Memorial, title of Section II.F.7.

> We have been very clear with our investors that TECO's principal strategy is in the business of public services; deriving good value from our non-regulated businesses. This transaction is consistent with said strategic focus.[24]
>
> The sale of our interest in DECA II last week provides cash that we can use to retire TECO Energy debt and to invest in our utility operations. We look forward to the continued good operations and strong earnings and cash flow from our two power plants in Guatemala.[25]

40. With this history, the lack of credibility of TGH's claim is obvious.

41. With respect to the CNEE, the best evidence of this body's reputation, despite TGH's opportunistic criticism, lies in the fact that, in the last three years, record investments have been made in the electricity sector in excess of US$ 2,500 million.[26] For example:

    (a) Two experienced foreign investors (the Colombian company Empresas Públicas de Medellín[27] and the British investment group Actis)[28] jointly invested some US$ 1,100 million in 2010 in purchasing the shares of the country's three largest electricity distributors—EEGSA, Deorsa and Deocsa—all of which are subject to regulation by the CNEE, and which collectively represent 93 percent of the country's electricity distribution

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24 Teco Press Release: "TECO Guatemala Holdings LLC sells its interest in Guatemalan electric distribution company," 21 October 2010, **Exhibit R-162**.

25 Teco Press Release: "TECO Energy reports third quarter results," 28 October 2010, **Exhibit R-134**, p. 1.

26 "Energy Sector attracts investments," *Prensa Libre*, 2 July 2010, **Exhibit R-102**.

27 Explanatory note on the sale of Iberdrola investments in Guatemala, 12 November 2010, **Exhibit R-138**, para. 12.

28 Actis Press Release, "Actis acquires majority stake in Guatemala's largest electricity network from Gas Natural Fenosa," 20 May 2011, **Exhibit R-138.**

market.[29] The three companies will have their tariff review processes in 2012 and 2013;

(b) An American consortium comprising the company Ashmore Energy International will invest some US$700 million in the largest electricity generation projects in Central America;[30] and

(c) A consortium led by the Colombian company Empresa de Energía Eléctrica de Bogotá will invest more than US$400 million in expanding the transmission system.[31]

42. The investors themselves have emphasized the legal security and investment opportunities in Guatemala today:

- The President of Ashmore Energy stated:

> This investment in energy infrastructure highlights the commitment of AEI with Guatemala and the central-american region and demonstrates the company's confidence in the legal and regulatory framework of the electricity sector [in Guatemala].[32]

- In 2010, upon investing in EEGSA, the EPM General Manager stated:

> It brings much satisfaction to be able to take part in this negotiation for electricity in Guatemala because it's something we've been pursuing for quite some time.
>
> Guatemala [possesses] highly significant institutional strength.[33]

- Michael Till, co-director of Infrastructure of the Actis Group said:

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29 Statement of the witness Mr. Carlos Eduardo Colom Bickford, President of the CNEE of Guatemala, 24 January 2012 (***Colom***), **Appendix RWS-1**, para. 31.

30 *Ibid*., para. 173.

31 *Ibid.*

32 "Construction of a US$ 700 million carbon plant begins in Guatemala," *Revista Summa*, http://www.revistasumma.com/negocios/3271-inicia-construccion-de-planta-de-carbon-por-us$700-millones-en-guatemala.html, May 14 2010, **Exhibit R-119**.

33 "We carry no flag, we respect roots," *Prensa Libre*, October 23, 2010, **Exhibit R-192**.

> This investment reflects our confidence in this country, which has key ingredients for investment, such as legal certainty. It is a market with an important growth.[34]

43. In light of all this, there are only two possibilities: either these investors are negligently investing in a sector in which the regulatory framework is politically manipulated in a country with a Constitutional Court that is susceptible to political influence, as TGH claims, or what the Claimant says regarding this alleged manipulation is completely false.

44. There is no doubt. Guatemala is not a country that is hostile to foreign investments. Nor is the regulator of the electricity sector, the CNEE, hostile to foreign investments. Perhaps the statement that best reveals the fallacy of the Claimant's allegations before to this Tribunal comes from TGH itself. When consulted in July 2010 regarding a recent extension of its contracts in the generation sector, Mr. Víctor Urrutia, Manager of Teco Guatemala, stated:

> Teco Energy decided to go for the extension [of the contract] because 'we continue to believe [that Guatemala is] a market where there are clear rules and certainty.'[35]

45. The electricity regulatory framework in Guatemala provides legal certainty and security and the regulator applies it correctly. For reasons of procedural strategy, TGH now chooses to say the opposite.

46. This Memorial on Objections and Counter-Memorial has the following structure:

(a) Section II below examines how TGH has not filed a valid nor admissible international claim and how the tribunal does not have jurisdiction;

(b) Section III studies the facts and corrects the many inaccuracies and errors in TGH's accounting of the facts;

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34 "Británica Actis acquires Guatemala's Deorsa and Deocsa for US$ 449 million", *Revista Summa*, http://www.revistasumma.com/negocios/12242-britanica-actis-adquiere-por-us$449-millones-a-deorsa-y-deocsa-de-guatemala.html, May 20, 2011, **Exhibit R-139**.

35 "Price reduction in Tampa contract", *Prensa Libre*, July 12, 2010, **Exhibit R- 105**.

(c) Section IV demonstrates how TGH's claim that Guatemala breached the international minimum standard of treatment of the Treaty lacks merit; and

(d) Section V shows how, even if Guatemala had breached the Treaty, which it did not, TGH has not suffered any financial damage.

II. TGH DOES NOT PRESENT A VALID OR ADMISSIBLE CLAIM, THEREFORE, THE TRIBUNAL LACKS JURISDICTION

A. TGH RAISES A MERE REGULATORY DISAGREEMENT THAT CANNOT GIVE RISE TO AN INTERNATIONAL CLAIM

47. Before analyzing TGH's factual and legal arguments in detail, it is necessary to address a preliminary question that demonstrates the flaws in its reasoning and undermines its claim. TGH's claims are based on its disagreement with the manner in which the regulator of the Guatemalan electricity sector (the CNEE) interpreted and applied the regulatory framework to the five-year tariff review process of EEGSA's tariffs for the period of 2008-2013. TGH does not complain of a legislative change that would have altered the fundamental rules set out in the LGE; its only complaint in this regard refers to a minor reform of the RLGE Article 98 which was not objected to at the time. Moreover, although TGH disagrees with the decisions of the Constitutional Court, it has not claimed that the conduct of the Guatemalan courts has, in itself, violated the treaty. The dispute submitted to this Tribunal is nothing but a disagreement of a regulatory nature under Guatemalan law, related to how the local regulatory framework should be interpreted and applied – an issue that the Guatemalan courts have already considered and decided in favor of the CNEE.

48. International jurisprudence dealing with similar claims has rejected the proposition that disputes of this nature could give rise to a violation of an investment protection treaty. A regulatory body for a public service, such as the CNEE, has the right and the responsibility to take a stance regarding issues within its competence, subject to review by the local courts, which have the final word on matters relating to the interpretation of the regulatory framework. Even if the

CNEE's interpretation of the regulatory framework were questionable or erroneous (which it is not in this case), this can by no means automatically constitute a violation of international law leading to a finding of the State's international responsibility. Otherwise, any regulatory decision involving a foreign investor would be subject to a claim before an international tribunal.

49. That an investor disagrees with the manner in which a rule of domestic law is applied does not provide grounds for a claim of violation of international investment protection standards. At most, it gives rise to a regulatory and contractual dispute under domestic law, over which the local courts are the competent bodies to remedy any possible irregularity. Accordingly, a matter of this nature must be submitted and decided by the competent domestic courts; TGH and EEGSA understood this when they resorted to the Guatemalan justice system, which has already ruled on the issues that TGH brings before this Tribunal.

50. This ICSID Tribunal cannot play the role of an appellate court of third or fourth instance for regulatory matters in Guatemala. TGH would have a valid claim only if the Guatemalan justice system had not been available to hear its claims, or if the local courts had acted in such a deficient manner as to deny justice to EEGSA and TGH. None of this has occurred and TGH does not even assert a claim in this regard: TGH does not even assert a claim of denial of justice.

51. Therefore, TGH has failed to bring a valid international claim. This has consequences related to jurisdiction and admissibility, as well as the substance of TGH's claims. Section II addresses matters related to jurisdiction and admissibility, while substantive matters are analyzed in Section III below. Prior to doing so, however, we examine the nature of TGH's claim in further detail.

1. TGH submits a mere regulatory disagreement

a. The substance of TGH's claim is the CNEE's interpretation of the Expert Commission's role and the CNEE's prerogative to approve tariff studies

52. The substance of TGH's claim is summarized in Section III.C of Claimant's Memorial, where TGH attempts to explain how Guatemala allegedly violated the international minimum standard of treatment. The title of this section is indicative. It reads:

> Guatemala Breached Its Treaty Obligation To Accord TECO's Investment Fair and Equitable Treatment When It Arbitrarily And In Complete Disregard Of Its Legal Framework Ignored The Expert Commission's Report And Set The Tariffs On The Basis Of Its Own Study.[36]

53. TGH is wrong: Guatemala, through the CNEE (the regulatory body in matters concerning electricity tariffs), did not act either arbitrarily or in violation of the regulatory framework. It is important, nonetheless, to identify the true nature of TGH's claim. In this regard, the very words employed by TGH reveal that, in fact, its claim refers to a mere disagreement with the actions of the CNEE during EEGSA's tariff review process. In particular, TGH disagrees with the CNEE's interpretation of the Expert Commission's role under LGE Article 75 and of its own powers in matters concerning the approval of tariff studies used in the determination of the five-year tariffs.

54. This is clear from a reading of the first paragraph of Section III.C, which summarizes TGH's claim in the following manner: "[t]he CNEE thus arbitrarily and unlawfully imposed its own VAD, rather than the VAD that it was required to apply according to the law;" and "[i]n so doing, the CNEE deliberately ignored both the Expert Commission's Report and Bates White's revised tariff study, and instead relied on its own commissioned study;" "[t]he result was a VAD that did not provide EEGSA's foreign investors with a rate of return within the range

36 Claimant's Memorial, title of Section III.C.

guaranteed by the LGE." TGH then concludes that "[b]oth the process and the result of the tariff review were unlawful and arbitrary, and contravened TECO's legitimate expectations."[37]

55. In other words, this dispute relates to a disagreement between TGH (and EEGSA) and the CNEE with respect to:

(a) The CNEE's authority under the regulatory framework to approve the independent tariff study prepared by a prequalified consultant commissioned by the CNEE, rather than the study prepared by the distributor's consultant;
(b) The role of the Expert Commission and the binding character (or lack thereof) of its opinion, as well as the scope of the Expert Commission's powers with respect to the approval of the tariff study; and
(c) The calculation of the VAD and the rate of return, and whether the tariff adopted by the CNEE yielded sufficient earnings for EEGSA and TGH.

56. These questions relate to the interpretation and application of the regulatory framework to EEGSA's 2008 tariff review, and, in particular, to the VAD calculation. It is important to note that, according to the LGE and the RLGE, the CNEE is the party responsible for complying with and enforcing the regulatory framework:

> **Article 4 (LGE)**
>
> The [CNEE] is established […] The Commission shall have functional independence in exercising its powers and the following functions:
>
> a) Compliance with and enforcement of this law and its regulations […][38]
>
> **Article 3 (RLGE)**

37 *Ibid.*, para. 259.

38 LGE, **Exhibit R-8**, art. 4(a).

> **Entities Responsible for their Application.** The Ministry of Energy and Mines is the State agency responsible for applying the General Law of Electricity and these Regulations, through the competent entity and the [CNEE], except in those matters of the exclusive competence of the Commission, as established in the Law and these Regulations.[39]

57. This also includes the responsibility to "[d]efin[e] the transmission and distribution tariffs […] as well as the methodology for calculation of the same"[40] and to conduct the tariff review process, including the calculation of the VAD.[41]

58. Accordingly, it was for the CNEE, as the competent regulatory body, to interpret and apply the regulatory framework to the best of its knowledge and understanding with respect to the issues raised by TGH; this the CNEE has done. It was then for the Guatemalan courts to decide whether the CNEE was right or wrong, which they have done, ruling in favor of the CNEE. TGH therefore submits to this Tribunal a dispute regarding the CNEE's conduct in the exercise of its regulatory functions. This dispute has already been decided by the Guatemalan courts.

59. TGH refers to the 2007 reform of RLGE Article 98. TGH, however, does not complain about the reform itself, but rather, about the manner in which the CNEE interpreted and applied the RLGE. With respect to the 2008 reform incorporating RLGE Article 98 *bis*, TGH admits that this article was not applied; it therefore could not have caused TGH any harm. As for the decisions of the Constitutional Court, TGH disagrees with them and argues that they were influenced by political considerations. This allegation, however, is based on nothing but the opinion of TGH's legal expert, Professor Alegría, who provides no evidence in support of his assertions. These issues, as well as TGH's other allegations, are discussed in further detail in the sequence.

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39 RLGE, **Exhibit R-36**, art. 3.

40 LGE, **Exhibit R-8**, art. 4(c).

41 *E.g.*, LGE, **Exhibit R-8**, arts. 61 and 71.

b. The Terms of Reference

60. The publication of the Terms of Reference by the CNEE is the first step in the five-year review of Guatemala's electricity distribution tariffs.[42] TGH complains that the CNEE "issued Terms of Reference that contravened the law."[43] The CNEE's power and responsibility to formulate the Terms of Reference is made clear in the following provisions:

(a) LGE Article 4(c): The CNEE is responsible for "[d]efining the transmission and distribution tariffs subject to regulation in accordance with this law, as well as the methodology for calculation of the same";

(b) LGE Article 74: "The terms of reference of the study(ies) of the VAD shall be drawn up by the Commission";

(c) LGE Article 77: "The methodology for determination of the tariffs shall be revised by the Commission every five (5) years [...]";[44]

(d) RLGE Article 98: "Every five years, […] the Commission shall deliver to the Distributors the terms of reference for the studies […]"[45]

61. TGH disagrees with the manner in which the CNEE interpreted and applied the RLGE, particularly with respect to the role of the Terms of Reference in the tariff review process. Apart from the fact that TGH is wrong in claiming that the 2008 Terms of Reference adopted by the CNEE (the ***Terms of Reference***) contravened the law, it must be noted that this disagreement concerns a mere regulatory issue under Guatemalan law. EEGSA and TGH themselves understood it as such when they challenged the Terms of Reference before the Guatemalan courts and obtained a provisional *amparo*.[46] This *amparo* was rendered moot by a

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42 See Section III.B.2.

43 Claimant's Memorial, title of Section II.F.2.

44 LGE, **Exhibit R-8**, arts. 4(c), 74 and 77.

45 RLGE, **Exhibit R-36**, art. 98.

46 Claimant's Memorial, paras. 103-104.

subsequent agreement between EEGSA and the CNEE on the content of the Terms of Reference.[47] TGH, however, continues to raise this claim.[48] As previously noted, this claim relates to a mere disagreement regarding the interpretation and application of the regulatory framework; this responsibility falls within the competence of the CNEE, which must act in way it deems legally correct, regardless of whether this is to the liking of a distributor such as EEGSA.

c. Supervision of the Bates White study

62. The tariff review process involves the preparation of a tariff study used to calculate the VAD. The distributors are required to commission such a study from a consultant prequalified by the CNEE, and the latter supervises the progress of the study and determines whether it meets the relevant criteria.[49] TGH alleges that the CNEE "[f]ailed to constructively engage with EEGSA" during this process.[50] However, it was EEGSA and its consultant, Bates White, who did everything possible to prevent the CNEE from exercising its supervisory powers, as explained below.[51]

63. What matters here is that TGH refers to a mere disagreement over how the CNEE interpreted and exercised its functions, including the "right to supervise progress of" the Bates White Study, its responsibility to revise "the studies performed and may make comments on the same" and "decide on the acceptance or rejection of the studies performed."[52] As the responsible regulatory body, the CNEE had a duty to supervise the progress of the Bates White study as it deemed most appropriate according to the relevant rules, and to make the necessary determinations regarding, for example, the admissibility of said study. The issue of whether the CNEE correctly interpreted and applied its powers with regard to

47 *Ibid.*, paras. 106-107.

48 *Ibid.*, para. 266.

49 LGE, **Exhibit R-8**, art. 74.

50 Claimant's Memorial, title of Section II.F.3.

51 See Section III.F.6.

52 LGE, **Exhibit R-8**, arts. 74 and 75; RLGE, **Annex R-36**, art. 98.

this process is a purely regulatory question governed by Guatemalan law, and subject to the control of local courts.

d. Role of the Expert Commission

64. Once the distributor's consultant submits its study to the CNEE, the rules prescribe that an expert commission shall pronounce itself on the discrepancies that exist between the CNEE and the distributor. The core of TGH's claim concerns the role of this expert commission. TGH complains that the CNEE considered the Expert Commission's report to be a non-binding technical opinion, which by its nature did not require the CNEE to accept the revisions to the Bates White study. Further, TGH disagrees with the CNEE's view that it was not the function of the Expert Commission to approve such a revised study.[53] As explained below, TGH's claim has no basis.[54] The CNEE, as the regulatory body responsible for enforcing and applying the law, has the authority and responsibility to approve the tariffs; this requires the CNEE to ensure that the approved tariffs and the VAD meet the requirements set forth in the law and regulations.[55] Nothing in the LGE confers a similar power on the Expert Commission.

65. In any case, as noted already, TGH's claims concern the interpretation and application of the regulatory framework, which is a matter within the responsibility of the CNEE. TGH's disagreement regarding the manner in which the CNEE performed this task amounts to a mere regulatory dispute, to be decided pursuant to Guatemalan law by Guatemala's courts. This has in fact occurred in EEGSA's and TGH's prior recourses to the Guatemalan courts, which the Constitutional Court decided in favor of the CNEE.

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53 Claimant's Memorial, Section II.F.5.

54 See section III.B.2 and IV.B. below.

55 LGE, **Exhibit R-8**, arts. 61 and 71; RLGE, **Exhibit R-36**, arts. 3, 82, 99.

e. The VAD approved by the CNEE

66. TGH also complains about the outcome of the tariff review, being the VAD approved by the CNEE, which according to TGH was "unlawful and unjustifiably low."[56] This is incorrect. As explained below,[57] the CNEE established the VAD and the tariffs using technical criteria, based on a tariff study conducted by a prequalified independent consultant. This was carried out according to the procedure and principles set forth in the LGE and the RLGE, and following the Terms of Reference.

67. In any event, it is clear that TGH has in effect requested this Tribunal to redo the 2008 tariff review, and recalculate the VAD, in order to determine whether it was too low and in violation of the regulation. This is not the role of this Tribunal. The disagreement between the CNEE and EEGSA/TGH is regulatory in nature; it concerns the proper application of the regulatory framework and, at most, is a matter for the Guatemalan courts. EEGSA always had and continues to have the right to a fair and adequate tariff in accordance with the regulatory framework, as was categorically reaffirmed by the Constitutional Court in its 18 November 2009 decision:

> The [CNEE]'s role of fixing the tariff schemes is a legitimate power granted by the General Electricity Law with which it fulfills a State function, and regulated in Articles 60, 61, 71 and 73 of the abovementioned law, which should moderate any excess in the exercise of discretion, since it refers to verifiable criteria in requiring that those tariffs " be compatible with standard distribution costs of efficient companies", structured "to promote equal treatment of consumers and the sector's economic efficiency", that "the Value-Added Distribution shall be related to the average capital and operations costs of a distribution network of an efficient company", and, likewise, that the "cost of operation and maintenance shall correspond to an efficient management of the reference distribution

56 Claimant's Memorial, title of Section II.F.7.

57 See section III.F.14.

> network". It is estimated that fixing of tariffs, when the report by the Experts' Commission has not been accepted as valid to guide this policy, cannot be, within its discretion, harmful or unreasonably arbitrary, having the indicators of efficient operators as a reference, as the one conditioned in Article 2 of the transitory dispositions of the Law, which made reference to the "values used in other countries applying a similar methodology".[58]

68. Whether EEGSA's VAD and tariff for 2008-2013 are appropriate is an issue to be determined by the CNEE and reviewed by the competent Guatemalan courts, and not by this Tribunal.

f. The reform of RLGE Article 98

69. RLGE Article 98 was amended in 2007. Until that point, that article provided that if the distributor did not submit tariff studies for the calculation of the VAD, or failed to correct them as required by the CNEE, "it may not modify its tariffs and the tariffs in effect at the time of the termination of the effective term of such tariffs shall continue to apply."[59] This provision could create a perverse incentive for distributors to not cooperate in the tariff review process in order to maintain tariffs that were more favorable than those resulting from an eventual review. In light of this, that rule was amended in 2007, establishing that in said scenario "the Commission shall be empowered to issue and publish the corresponding tariff schedule, based on an independent tariff study conducted by the Commission or on the basis of corrections to the studies begun by the distributor."[60] This reform was better aligned with the CNEE's regulatory authority to determine and fix the tariffs, and the principle under the LGE that tariffs must reflect the efficient costs

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58 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November, 18 2009, **Exhibit R-105**, pgs. 32-33 (Emphasis added).

59 Regulations of the General Electricity Law, March 21, 1997 (hereinafter ***RLGE-excerpts***), **Exhibit R-12**, art. 98.

60 Government Resolution No. 68-2007, March 2, 2007, published in the *Diario de Centro América* on March 5, 2007, **Exhibit R-35**, art. 21 (Emphasis added).

of distributors. In addition, the reform harmonized RLGE Article 98 with Article 99, which had been amended in 2003.[61]

70. In fact, RLGE Article 99 had been similarly modified in 2003, providing that when "a Distributor ends up without a tariff schedule, the National Electric Energy Commission shall immediately issue and put into effect a tariff schedule."[62] Notably, at no time in 2003 or later, did EEGSA or any other distributor challenge the CNEE's power to unilaterally establish tariff schedules.

71. TGH refers to the 2007 reform of RLGE Article 98 as if the reform had caused damage to TGH.[63] However, TGH later clarifies that, in reality, its complaint refers to the fact that "the CNEE erroneously construed amended RLGE Article 98."[64] Thus, TGH does not raise a claim against the reform of Article 98 itself; following TGH's reasoning, had the CNEE correctly applied Article 98, there would have been no harm to EEGSA or TGH. The question, therefore, is how Article 98 should be interpreted and applied, an issue with respect to which the CNEE, as the regulator and the body responsible for the enforcement of the regulatory framework, was entitled to make a decision. This is therefore a mere regulatory dispute under Guatemalan law, and such dispute has already been decided by the Guatemalan courts in favor of the position adopted by the CNEE.

72. In any case, the 2007 reform of RLGE Article 98 could not have caused injury to TGH. It was, by definition, a reform of the RLGE, which could not result in a modification of the rules contained in the LGE. TGH claims that the reform is unconstitutional because it contradicts the LGE.[65] This argument, though incorrect, precisely demonstrates that the reform did not alter the rules contained in the LGE: they are still valid and, per the principle of hierarchy of rules, they

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61 See Section III.E.

62 Governmental Resolution No. 787-2003, December 5, 2003, published in the Diario de Centro América on 16 January 2004, **Exhibit R-30**.

63 Claimant's Memorial, paras. 84-93.

64 Claimant's Memorial, para. 192; see also Claimant's Memorial, paras. 93 and 272.

65 *Ibid.*, paras. 90-92, 192, 264.

continue to prevail over the RLGE. Even if TGH's allegations had any basis, it would be for the Guatemalan courts, not this international tribunal, to ensure that the principles contained in the LGE prevail over any RLGE rules to the contrary, and that the CNEE does not interpret the RLGE in a manner contrary to the LGE. It is notable that the constitutionality of the reform in question was never challenged either by EEGSA or the other distributors.

73. In sum, the 2007 reform of RLGE Article 98 improved the RLGE in that it clarified the principle contained in the LGE under which the CNEE has the obligation to ensure that the distribution tariffs comply with the regulatory framework. EEGSA expressly accepted that this type of reform would apply to it. The Authorization Contracts, which govern EEGSA's operations and provision of electric distribution services, establish in clause 20 that EEGSA:

> [A]grees to comply with all the provisions set forth in the Law of General Electricity and its Regulations, or modifications they suffer as well as the other regulations and provisions that generally apply […][66]

74. In 2008, the RLGE was amended once again through the addition of the new Article 98 *bis*.[67] This article fills a gap in the regulation by providing a method for the appointment of the third member of the Expert Commission in the event that the parties, i.e., the CNEE and the distributor, are not able to reach agreement regarding such appointment. It provided that the Ministry of Energy and Mines would make the appointment from among the candidates suggested by the parties who met the pre-requisite of independence from the parties. As TGH recognizes,[68] this provision was never applied to EEGSA and therefore could not have caused TGH any harm.

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66 Authorization Agreement for the departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, May 15, 1998, **Exhibit R-17**, clause 20; Final Electricity Authorziation Agreement for the Departments of Chimaltenango, Santa Rosa and Jalapa, February 2, 1999, **Exhibit R-20,** clause 20.

67 Ministry of Energy and Mines Governmental Accord No. 145-2008, May 19, 2008, **Exhibit R-72**.

68 Claimant's Memorial, para. 135.

g. Actions of the Guatemalan courts

75. EEGSA submitted the above regulatory disputes to the Guatemalan courts. The proceedings commenced by EEGSA ultimately led to two decisions by the Constitutional Court, dated 18 November 2009 and 24 February 2010.[69]

76. TGH claims that such decisions are wrong and appear to have been politically influenced.[70] Notwithstanding the severity of such allegation, TGH has provided no evidence in support of its allegations of political influence; it cites only the unsupported opinion of its legal expert, Mr. Alegría.[71]

77. TGH's only real complaint is that the Constitutional Court made a mistake. It raises no allegation of denial of justice. It asks this Tribunal to correct the alleged errors of the Constitutional Court, as if it were an appellate court of third or fourth instance in matters governed by Guatemalan law. This cannot be the role of this Tribunal.

h. Conclusion: TGH raises a mere regulatory disagreement, already resolved by the Guatemalan justice system

78. In sum, TGH has presented to this Tribunal a disagreement regarding the manner in which the CNEE performed its functions of interpreting and applying the regulation during EEGSA's 2008 tariff review. The main questions are the role of the Expert Commission and the CNEE's duties regarding the approval of the VAD and the tariffs. This dispute – which is a dispute under Guatemalan law – has already been decided by the Guatemalan judicial system, through the decisions of its highest court, the Constitutional Court. TGH does not allege that the Guatemalan courts have committed a denial of justice. TGH practically requires this Tribunal to redo the tariff review and the determination of the VAD.

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69 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-105**; Decision of the Constitutional Court, Case File 3831-2009, February 25, 2010, **Exhibit R-111**.

70 Claimant's Memorial, paras. 212-218 and 275-277.

71 *Ibid.*, paras. 212, 275, 277.

As is discussed below, a claim such as the one raised by TGH does not constitute a valid claim pursuant to an investment protection treaty.

2. TGH has failed to submit a valid international claim

a. This Tribunal cannot act as an appellate or an amparo court with respect to issues of Guatemalan law

79. As noted above, TGH asks this Tribunal to act as an appellate court of third or fourth instance in matters governed by Guatemalan law. However, this Tribunal cannot and should not play this role.

80. As stated by the tribunal in *ADF v. United States*, where the issue was whether a public authority had correctly applied the relevant U.S. regulations to a project involving the construction of a highway:

> […] More important for present purposes, however, is that even had the Investor made out a *prima facie* basis for its claim, the Tribunal has no authority to review the legal validity and standing of the U.S. measures here in question under *U.S. internal administrative law*. We do not sit as a court with appellate jurisdiction with respect to the U.S. measures.[72]

81. The tribunal in *Azinian v. Mexico* ruled in a similar fashion:

> The possibility of holding a State internationally liable […] does not, however, entitle a claimant to seek international review of the national court decisions as though the international jurisdiction seised has plenary appellate jurisdiction.[73]

82. In the same manner, the tribunal in *Waste Management v. Mexico* refused to act as a court of appeals or *amparo*:

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72 *ADF Group Inc. v. United States of America* (ICSID Case No. ARB(AF)/00/1) Award, January 9, 2003, **Exhibit CL-4**, para. 190.

73 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, November 1, 1999, **Exhibit RL-2**, para. 99.

> [T]he Tribunal would observe that it is not a further court of appeal, nor is Chapter 11 of NAFTA a novel form of *amparo* in respect of the decisions of the federal courts of NAFTA parties.[74]

83. When a claimant brings an international claim regarding the legality of certain measures under local law, it asks the international tribunal to act as a local appellate court, which is not its role and falls outside its jurisdiction.

b. Jurisprudence refuses to allow these types of disputes to give rise to a violation of an investment protection treaty

84. The existing case law unanimously holds that mere regulatory disputes (or contractual disputes) cannot give rise to violations of investment treaties.

85. This was the conclusion of the tribunal in *Saluka v. Czech Republic* with respect to a dispute regarding regulatory measures taken by the regulator of the Czech Republic's financial services sector. The tribunal in *Saluka* rejected the fair and equitable treatment claim with the following words:

> […] The Treaty cannot be interpreted so as to penalise each and every breach by the Government of the rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State.
>
> As the tribunal in *ADF Group Inc.* has stated with regard to the "fair and equitable treatment" standard contained in Article 1105(1) NAFTA:
>
> something more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the customary international law requirements….
>
> Quite similarly, the *Loewen* tribunal stated in the same legal context that:
>
> whether the conduct [of the host State] amounted to a breach of municipal law as well as international law is

74 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, April 30, 2004, **Exhibit CL-46**, para. 129.

> not for us to determine. A NAFTA claim cannot be converted into an appeal against decisions of [the host State].[75]

86. The tribunal ruled in a similar manner in *EnCana v. Ecuador*, in which the claimant argued that its investment had been expropriated as a result of certain decisions of the Ecuadorian tax authorities to reject certain tax refunds. The tribunal assumed that the claimant's allegations with respect to its right to tax refunds were well-founded, but stated:

> [...] there is nonetheless a difference between a questionable position taken by the executive in relation to a matter governed by the local law and a definitive determination contrary to law. In terms of the BIT the executive is entitled to take a position in relation to claims put forward by individuals, even if that position may turn out to be wrong in law, provided it does so in good faith and stands ready to defend its position before the courts. Like private parties, governments do not repudiate obligations merely by contesting their existence.[76]

87. The tribunal in *Generation Ukraine v. Ukraine* made a similar ruling in the context of a expropriation claim related to a series of regulatory actions undertaken by the municipality of Kiev:

> […] This Tribunal does not exercise the function of an administrative review body to ensure that municipal agencies perform their tasks diligently, conscientiously or efficiently. That function is within the proper domain of domestic courts and tribunals that are cognisant of the minutiae of the applicable regulatory regime. […] the only possibility in this case for the series of complaints relating to highly technical matters of Ukrainian planning law to be transformed into a BIT violation would have been for the Claimant to be

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75 *Saluka Investments B.V. v. Czech Republic* (UNCITRAL case), Partial Award, March 17, 2006, **Exhibit CL-42**, paras. 442-443.

76 *EnCana Corporation v. Republic of Ecuador* (LCIA Case No. UN3481, UNCITRAL Rules) Award, February 3, 2006, **Exhibit RL-9**, para. 194 (Emphasis added).

> denied justice before the Ukrainian courts in a *bona fide* attempt to resolve these technical matters.[77]

88. As stated by the *Waste Management* tribunal in the context of a concession for waste treatment services:

> […] In the present case the Claimant did not lose its contractual rights, which it was free to pursue before the contractually chosen forum. The law of breach of contract is not secreted in the interstices of Article 1110 of NAFTA. Rather it is necessary to show an effective repudiation of the right, unredressed by any remedies available to the Claimant, which has the effect of preventing its exercise entirely or to a substantial extent.[78]

89. Faced with purported regulatory (or contractual) violations, the investor has not lost its rights, or the rights it claims to have. No legislative or regulatory change has taken place that could substantially modify, suppress, abolish or repudiate said rights.

90. A regulatory body such as the CNEE not only has the right, but the duty, to take a position on disputed matters under local law relating to the exercise of its functions, including the rights of a specific entity subject to the relevant regulations. This can give rise to a dispute between the entity in question and the regulator regarding the scope of the former's rights. In such circumstances, it is not the allegedly irregular conduct of the regulator that could give rise to a Treaty claim, but rather the treatment that the entity in question has received in the local justice system (denial of justice).

91. For example, in *Azinian,* the claimants disputed certain actions of the City of Naucalpan de Juárez in Mexico in the context of an administrative process in which the investors' compliance with the terms of a concession for waste

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77 *Generation Ukraine, Inc. v. Ukraine* (ICSID Case No. ARB/00/9) Award, September 15, 2003, **Exhibit RL-6** para. 20.33.

78 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, April 30, 2004, **Exhibit CL-46**, para. 175.

collection and disposal was reviewed, and which resulted in the cancellation of the concession. The claimants alleged that the actions of the City constituted a violation of the investment protections of Chapter 11 of the NAFTA. The tribunal stated:

> Arbitral jurisdiction under Section B is limited not only as to the persons who may invoke it (they must be nationals of a State signatory to NAFTA), but also as to subject matter: claims may not be submitted to investor-state arbitration under Chapter Eleven unless they are founded upon the violation of an obligation established in Section A.
>
> To put it another way, a foreign investor entitled in principle to protection under NAFTA may enter into contractual relations with a public authority, and may suffer a breach by that authority, and *still not be in a position to state a claim under NAFTA*. It is a fact of life everywhere that individuals may be disappointed in their dealings with public authorities, and disappointed yet again when national courts reject their complaints. It may safely be assumed that many Mexican parties can be found who had business dealings with governmental entities which were not to their satisfaction; Mexico is unlikely to be different from other countries in this respect. NAFTA was not intended to provide foreign investors with blanket protection from this kind of disappointment, and nothing in its terms so provides.
>
> It therefore would not be sufficient for the Claimants to convince the present Arbitral Tribunal that the actions or motivations of the Naucalpan Ayuntamiento are to be disapproved, or that the reasons given by the Mexican courts in their three judgments are unpersuasive. Such considerations are unavailing unless the Claimants can point to a violation of an obligation established in Section A of Chapter Eleven attributable to the Government of Mexico.
>
> […]
>
> The problem is that the Claimants' fundamental complaint is that they are the victims of a breach of the Concession Contract. NAFTA does not, however, allow

investors to seek international arbitration for mere contractual breaches. Indeed, NAFTA cannot possibly be read to create such a regime, which would have elevated a multitude of ordinary transactions with public authorities into potential international disputes. *The Claimants simply could not prevail merely by persuading the Arbitral Tribunal that the Ayuntamiento of Naucalpan breached the Concession Contract*.

[…]

From this perspective, the problem may be put quite simply. The Ayuntamiento believed it had grounds for holding the Concession Contract to be invalid under Mexican law governing public service concessions. At DESONA's initiative, these grounds were tested by three levels of Mexican courts, and in each case were found to be extant. How can it be said that Mexico breached NAFTA when the Ayuntamiento of Naucalpan purported to declare the invalidity of a Concession Contract which by its terms was subject to Mexican law, and to the jurisdiction of the Mexican courts, and the courts of Mexico then agreed with the Ayuntamiento's determination? […]

With the question thus framed, it becomes evident that for the Claimants to prevail it is not enough that the Arbitral Tribunal disagree with the determination of the Ayuntamiento. A governmental authority surely cannot be faulted for acting in a manner validated by its courts *unless the courts themselves are disavowed at the international level*. As the Mexican courts found that the Ayuntamiento's decision to nullify the Concession Contract was consistent with the Mexican law governing the validity of public service concessions, the question is whether the Mexican court decisions themselves breached Mexico's obligations under Chapter Eleven.

[…]

But the Claimants have raised no complaints against the Mexican courts; they do not allege a denial of justice. Without exception, they have directed their many complaints against the Ayuntamiento of Naucalpan.

> The Arbitral Tribunal finds that this circumstance is fatal to the claim […].[79]

92. In other words, according to the tribunal in *Azinian*, there is no valid Treaty claim if the investor's only complaint is that the regulator might have committed certain irregularities in its ordinary dealings with the regulated entities. The investor must instead claim that the courts charged with hearing the case have denied it justice.

93. The tribunal in *Feldman v. Mexico* reached a similar conclusion in a case in which the investor argued that certain disagreements between it and the Mexican tax authorities involving its cigarette sale business constituted an expropriation.[80] The tribunal noted that the "[c]laimant, through the Respondent's actions is no longer able to engage in his business of purchasing Mexican cigarettes and exporting them,"[81] and that:

> [I]t is undeniable that the Claimant has experienced great difficulties in dealing with SHCP officials, and in some respects has been treated in a less than reasonable manner, but that treatment under the circumstances of this case does not rise to the level of a violation of international law under Article 1110.[82]

94. Therefore, despite the difficulties and the unreasonable actions of the Mexican fiscal authorities, the tribunal could not conclude that a treaty violation had taken place because the questions at issue were a matter of domestic law for which the local tribunals were competent and had been available to decide.

> Formal administrative procedures and the courts, according to the record, were at all times available to him, and have not been challenged here as being

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79 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, November 1, 1999, **Exhibit RL-2**, paras. 82-84, 87, 96-97, 100 (Emphasis in italics in the original; underlined emphasis added).

80 *Marvin Feldman v. México* (ICSID Case No. ARB(AF)/99/1) Final Award, December 16, 2002, **Exhibit RL-5**.

81 *Ibid*, para. 109.

82 *Ibid*, para. 113.

> inconsistent with Mexico's international law obligations.
>
> […]
>
> Given as noted earlier that Mexican courts and administrative procedures at all relevant times have been open to the Claimant, […] there appears to have been no denial of due process or denial of justice there as would rise to the level of a violation of international law.[83]

95. *Parkerings v. Lithuania* is also relevant. In *Parkerings*, the claimant argued that a municipality had committed certain irregularities in the process of verifying the investor's compliance with the terms of a contract and in the subsequent termination of that contract. The tribunal found that the irregularities in question did not constitute a violation of the fair and equitable standard of treatment:

> Fair and equitable treatment is denied when the investor is treated in such an unjust or arbitrary manner that the treatment is unacceptable from an international law point of view. Indeed, many tribunals have stated that not every breach of an agreement or of domestic law amounts to a violation of a treaty. For instance, in the *Saluka v. Poland* case, the Tribunal stated:
>
> The Treaty cannot be interpreted so as to penalise each and every breach by the Government of the rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State. […] something more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the customary international law requirements […].
>
> Under certain limited circumstances, a substantial breach of a contract could constitute a violation of a treaty. So far, case law has offered very few illustrations of such a situation. In most cases, a preliminary determination by a competent court as to whether the contract was breached under municipal law

83 *Ibid*, paras. 134 and 140.

is necessary. This preliminary determination is even more necessary if the parties to the contract have agreed on a specific forum for all disputes arising out of the contract. For the avoidance of doubt, the requirement is not dependent upon the parties to the contract being the same as the parties to the arbitration.

However, if the contracting-party is denied access to domestic courts, and thus denied opportunity to obtain redress of the injury and to complain about those contractual breaches, then an arbitral tribunal is in position, on the basis of the BIT, to decide whether this lack of remedies had consequences on the investment and thus whether a violation of international law occurred. In other words, as a general rule, a tribunal whose jurisdiction is based solely on a BIT will decide over the "treatment" that the alleged breach of contract has received in the domestic context, rather than over the existence of a breach as such.

In the case at hand, there is no doubt that BP had access to the Lithuanian Courts. […]

[E]ven supposing that the Agreement has been wrongfully terminated, the Claimant failed to show that the right of BP to complain of the breach of the Agreement has been denied by the Republic of Lithuania and thus that its own investment was actually not accorded, by the Respondent, an equitable and reasonable treatment in such circumstances.

Given the above circumstances, the Arbitral Tribunal cannot reach the conclusion that Article III of the BIT was breached.

[…]

[…] The acts and omissions of the Municipality of Vilnius, in particular any failure to advise or warn the claimant of likely or possible changes to Lithuanian law, may be breaches of the Agreement but that does not mean they are inconsistent with the Treaty.[84]

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84 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No. ARB/05/8) Award, September 11, 2007, **Exhibit RL-10**, paras. 315-320 and 345 (Emphasis in italics in the original; underlined emphasis added).

96. In the present case, TGH does not argue that the treatment accorded by the Guatemalan judiciary violates the Treaty;[85] its complaint instead concerns the CNEE's conduct. As stated in *Parkerings*, this does not give rise to a Treaty violation.

97. The fact that a regulatory authority takes a position that is at odds with the regulated entity does not, in and of itself, mean that the State as such has treated the investor in a manner contrary to international law. According to TGH, any difference of opinion between the investor and the CNEE and the local courts regarding the interpretation of the regulatory framework would give rise to a violation of the Treaty. This is an extreme position. If such position were correct, any state that receives foreign investors in its regulated sectors would be exposed to a claim under an investment protection treaty every time an investor disagreed with the position adopted by the state's regulatory authorities.

B. THIS TRIBUNAL LACKS JURISDICTION AND THE CLAIM BROUGHT BY TGH IS INADMISSIBLE.

98. The consequence of the discussion above in Section A, is that this Tribunal lacks jurisdiction and the claim, as presented, is inadmissible:

(a) The Tribunal does not have jurisdiction *ratione materiae*. TGH has not submitted a dispute over matters regulated by the Treaty, as established by Treaty Article 10.16.1, but rather a merely regulatory dispute; and

(b) TGH does not claim denial of justice, the only claim which this Tribunal could have heard.

1. The Tribunal has no jurisdiction *ratione materiae*

99. In accordance with Article 10.16.1(a)(i)(A) of the Treaty, Guatemala has consented to submit to arbitration disputes brought by U.S. investors involving "a

[85] See Section II.A.1.g above.

claim […] that the respondent has breached […] an obligation under Section A" of the Treaty. This is the provision invoked by TGH in submitting the present dispute to this Tribunal.[86] Under this provision, Guatemala's consent does not refer to just any type of claim. Rather, it refers to only those claims concerning a violation by the Guatemalan State of investment protections established by the Treaty.

100. In this regard, it is common knowledge that international tribunals must examine the fundamental bases of claims brought under investment protection treaties to determine whether the dispute qualifies as an international claim. The claimant's characterization of its claims as international claims is not enough.

101. As the tribunal in *Azinian* stated, in refusing to accept without more the claimant's characterization of certain acts as "confiscatory" or as "destroy[ing] contractual rights as an asset,": "Labeling is, however, no substitute for analysis."[87]

102. In a similar vein, the tribunal in *Pantechniki v. Albania* noted, with reference to relevant precedents, that:

> This is a matter of capital importance. It is common ground that the relevant test is the one expressed by the America-Venezuela Mixed Commission in the *Woodruff* case (1903): whether or not "the fundamental basis of a claim" sought to be brought before the international forum is autonomous of claims to be heard elsewhere. This test was revitalised by the ICSID *Vivendi* annulment decision in 2002. It has been confirmed and applied in many subsequent cases.[88]

103. As the tribunal in *UPS v. Canada* also correctly stated:

> [A] claimant's party mere assertion that a dispute is within the Tribunal's jurisdiction is not conclusive. It is

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86 Notice of Arbitration, para. 27.

87 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, November 1, 1999, **Exhibit RL-2**, para. 90.

88 *Pantechniki S.A. Contractors & Engineers v. Republic of Albania* (ICSID Case No. ARB/07/21) Award, July 30, 2009, **Exhibit RL-12,** para. 61.

> the Tribunal that must decide. The formulation also importantly recognizes that the Tribunal must address itself to the particular jurisdictional provisions invoked. There is a contrast, for instance, between a relatively general grant of jurisdiction over "investment disputes" and the more particularised grant in article 1116 which is to be read with the provisions to which it refers and which are invoked by UPS. […]
>
> The International Court of Justice in the *Case concerning Oil Platforms* (Islamic Republic of Iran v United States of America) 1996 ICJ Reports 803, para. 16 states the test in this manner:
>
> > [The Court] must ascertain whether the violations of the Treaty… pleaded by Iran do or do not fall within the provisions of the Treaty and whether, as a consequence, the dispute is one which the Court has jurisdiction *ratione materiae* to entertain, pursuant to Article XXI, paragraph 2.
>
> That paragraph gave the Court jurisdiction over any dispute between the Parties about "the interpretation or application" of the Treaty.
>
> […]
>
> Accordingly, the Tribunal's task is to discover the meaning and particularly the scope of the provisions which UPS invokes as conferring jurisdiction. Do the facts alleged by UPS fall within those provisions; are the facts capable, once proved, of constitution breaches of the obligations they state?[89]

104. Therefore, the mere assertion that TGH's claim lies within this Tribunal's jurisdiction is not sufficient. The essential or fundamental basis of the claim (which is nothing more than TGH's dispute over the CNEE's application of rules relating to the tariff review process) must be analyzed to determine whether this gives rise to a Treaty claim.

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89 *United Parcel Service of America, Inc. v. Canada* (UNCITRAL case) Decision on Jurisdiction, November 22, 2002, **Exhibit RL-4**, paras. 34, 35, 37.

105. TGH focuses on "labeling" its claims as being based on the Treaty. It does so by resorting to borrowed phrases regarding the alleged "arbitrary," "illegitimate," "abusive," and "politically motivated" actions adopted by the CNEE, as if this were sufficient to give rise to a Treaty claim.[90] However, TGH cannot expect that the use of such terms is enough to turn its claim into a Treaty claim.

106. As has been held in case law, the fundamental basis of the claim presented must be examined. Once such examination is conducted, as already noted,[91] it becomes evident that the facts presented by TGH simply concern a disagreement between a regulator and the regulated entity, and do not constitute a dispute under the Treaty.

107. This type of analysis was conducted, for example, by the tribunal in *Azinian*. The relevant analysis is contained in the section of the award titled "[v]alidity of the claim under NAFTA,"[92] where the tribunal examines whether the claim satisfies the requirements of NAFTA's Article 1116, which provides:

> An investor of a Party may submit to arbitration under this Section a claim that another Party has breached an obligation under […] Section A [substantive protections].

108. In this regard, the *Azinian* tribunal noted that "claims may not be submitted to investor-state arbitration under Chapter Eleven unless they are founded upon the violation of an obligation established in Section A,"[93] that is, claims based on NAFTA's substantive investment protections.

109. The relevant Treaty provision in the present case is identical to the NAFTA provision examined by the tribunal in *Azinian*. Accordingly, in the words of *Azinian*, the present Tribunal must first determine, as a jurisdictional question, the

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90 See, *e.g.*, Claimant's Memorial, paras. 228, 259, 263, 272 and title of Section III.C.

91 See Section II.A.1 above.

92 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, November 1, 1999, **Exhibit RL-2**, title of Section VI.6.

93 *Ibid.*, para. 82, referring to NAFTA article 1116.

"[v]alidity of the claim under" the Treaty, because "claims may not be submitted to investor-state arbitration under" Chapter 10 of the Treaty "unless they are founded upon the violation of an obligation established in Section A" of the Treaty.

110. In this context the question is: Has TGH presented a valid claim under the Treaty by simply arguing that the CNEE has allegedly misinterpreted and misapplied the relevant rules in the tariff review process for EEGSA, when, moreover, Guatemala's Constitutional Court has ruled in favor of the position adopted by the CNEE? According to case law examined above,[94] the answer is no. In this context, TGH must claim and prove denial of justice.

111. This was clearly stated, for example, by the tribunal in *Azinian*, which was cited above but is worth repeating:

> […] It is a fact of life everywhere that individuals may be disappointed in their dealings with public authorities, and disappointed yet again when national courts reject their complaints. It may safely be assumed that many *Mexican* parties can be found who had business dealings with governmental entities which were not to their satisfaction; Mexico is unlikely to be different from other countries in this respect. NAFTA was not intended to provide foreign investors with blanket protection from this kind of disappointment, and nothing in its terms so provides.
>
> […]
>
> A governmental authority surely cannot be faulted for acting in a manner validated by its courts *unless the courts themselves are disavowed at the international level.*[95]

112. Thus, when a regulatory body makes a decision which falls within its powers and responsibilities it cannot be found to have violated an investment protection treaty

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94 See section II.A.2, above.

95 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, November 1, 1999, **Exhibit RL-2**, paras. 83 and 97 (Emphasis in italics in the original, underlined emphasis added).

– no matter how erroneous that decision is. This is particularly the case when the local courts, acting within their competence, have already decided on the matter. In this scenario, a state can only be found to be responsible under international law for the actions of its courts, that is, for denial of justice, a claim that TGH has not made in this case as explained below.

2. The disagreement has been resolved by the local courts which did not deny justice to TGH, a claim which is not, in any event, made by TGH

a. The only claim that TGH could have submitted to this Tribunal is a claim of denial of justice

113. In a case such as the present one, concerning an investor's mere disagreement with the actions of an administrative body that has already been examined by the local judicial bodies, the only hypothetical Treaty claim that could have been brought is denial of justice by the local courts. The issue is very simple: when these types of disagreements between the regulatory authority and the regulated entities arise, something that is not unusual in any given State, what the State must ensure is that its courts – the competent bodies to resolve such disputes – are available, provide due process, and do not issue arbitrary decisions. When this occurs, the State cannot be held responsible for the actions of a regulatory authority, since another branch of the government, being the judiciary, has been called to intervene and has issued a decision on the matter. A State is internationally responsible only when this process fails.

114. In other words, Guatemala cannot be held responsible under the Treaty and international law solely on the basis of whether an entity such as the CNEE has acted rightly or wrongly in the exercise of its functions. This would disregard a fundamental aspect of this case, that is, EEGSA's and TGH's decision to resort to the Guatemalan courts and the rulings of the latter. This Tribunal is called upon to judge the conduct of the State, which necessarily and primarily includes the actions of its courts, and not merely the actions of an administrative body whose conduct has precisely been subject to the consideration of said courts. Therefore,

Guatemala's international responsibility must be determined on the basis of whether the Guatemalan courts have given EEGSA and TGH the opportunity to present their case regarding the CNEE's actions, and whether the decisions rendered thereafter are in accordance with basic standards of justice.

115. TGH, nonetheless, focuses its arguments on the actions of the CNEE. In its brief of over 300 paragraphs, TGH references the Constitutional Court decisions rendered on 18 November 2009 and 24 February 2010, which favored the position adopted by the CNEE, in only one paragraph of the legal section,[96] and in not more than nine paragraphs of the factual section of the Memorial.[97] In those paragraphs, TGH, relying on the expert opinion of Professor Alegría, simply states that "the Court's decision was wrong," or is "incorrect," or that "[t]he Court wrongly rules that […] the Expert Commission's decision was not binding."[98] It also says that the resolution of the Court "appears to have been influenced by political considerations,"[99] but does not provide further details and evidence in support of this allegation. Thus, in the absence of arguments and proof that the Constitutional Court denied justice to EEGSA and TGH, which is not surprising since there has been no denial of justice, TGH has failed to present a valid claim that Guatemala has violated the Treaty.

116. This is how international tribunals have decided when faced with matters similar to those presented by TGH. If TGH wants Guatemala to be found responsible as a State under international law, it must demonstrate what the Guatemala courts – which were called upon by EEGSA to intervene in the dispute and which eventually ruled in favor of the position adopted by the CNEE – have done wrong. As held by the tribunal in *Azinian,* "[a] governmental authority surely

96 Claimant's Memorial, para. 277.

97 *Ibid.*, paras. 211-219.

98 *Ibid.*, paras. 212, 213, 218.

99 *Ibid.*, para. 212.

cannot be faulted for acting in a manner validated by its courts *unless the courts themselves are disavowed at the international level*."[100]

117. This requires more than simply disagreeing with the courts' decisions; it requires proof that the courts have acted in violation of international law (e.g., in a clearly arbitrary manner and without respect for due process, that is, denying justice). TGH cannot leave this question aside and instead simply state, without providing any evidence whatsoever, that the Constitutional Court made a mistake or was politically influenced. This is particularly problematic in light of the fact that TGH focuses its arguments on the CNEE's purported errors, which were submitted to the review of the courts. It must be concluded that this focus on a particular aspect of the conduct of Guatemala, i.e., the acts of the CNEE, has been intentionally adopted with a view to avoiding discussion of the unfavorable decisions of the local courts. TGH cannot proceed in this manner given that it is Guatemala's conduct that is at issue and this clearly (and importantly) includes the actions of its courts.

118. To be clear, what TGH should have argued but has not is denial of justice. As held by the tribunal in *Azinian* "[a] governmental authority surely cannot be faulted for acting in a manner validated by its courts *unless the courts themselves are disavowed at the international level.*"[101]

b. TGH does not argue that the Guatemalan courts have committed a denial of justice, and in any case no denial of justice has taken place

119. Given the regulatory nature of their disagreement with the CNEE, EEGSA and TGH correctly resorted to the local courts to attempt to enforce their interpretation of the regulatory and contractual framework. The decisions of the local courts have been both favorable and unfavorable to EEGSA and TGH, but in no case have EEGSA and TGH been deprived of access to the courts. Moreover, TGH has

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100 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, 1 November 1999, **Exhibit RL-2**, para. 97 (Emphasis in original).

101 *Ibid.*, para. 97 (Emphasis in original).

not suggested that the unfavorable decisions resulted in a denial of justice pursuant to international law.

120. In *Pantechniki*, the tribunal explained that denial of justice is not an error in the interpretation of local law, but rather an error that "no competent judge could reasonably have made," in other words, that the State did not provide "even a minimally adequate justice system."[102] In *Jan de Nul v. Egypt*, the tribunal stated, in a similar manner, that:

> It is not the role of a tribunal constituted on the basis of a BIT to act as a court of appeal for national courts. The task of the Tribunal is rather to determine whether the Judgment is "*clearly improper and discreditable*" in the words of the *Mondev* tribunal.[103]

121. In *Mondev v. United States*, the tribunal ruled that "it is not the function of NAFTA tribunals to act as courts of appeal […] the question is whether […] the impugned decision was clearly improper and discreditable […]."[104]

122. In his most recent study regarding denial of justice, Jan Paulsson explains that a misapplication of domestic law by national judges does not constitute denial of justice:

> The general rule is that the final word as to the meaning of national law should be left with the national judiciary. […] De Visscher put it as follows:
>
> The mere violation of internal law may never justify an international claim on denial of justice. It may be that the defectiveness of internal law, the refusal to apply it, or its wrongful application by judges, constitute elements of proof of a denial of justice, in the international understanding of the expression; but in

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102 *Pantechniki S.A. Contractors & Engineers v. Republic of Albania* (ICSID Case No. ARB/07/21) Award, July 30, 2009, **Exhibit RL-12**, para. 94.

103 *Jan de Nul N.V. & Dredging International N.V. v. Arab Republic of Egypt* (ICSID Case No. ARB/04/13) Award, November 6, 2008, **Exhibit RL-11**, para. 209.

104 *Mondev International Ltd. v. Estados Unidos* (ICSID Case No. ARB(AF)/99/2) Award, October 11, 2002, **Exhibit CL-31**, paras. 126-127.

and of themselves they never constitute this denial. In sum: Errare humanum est: error in good faith excludes responsibility.

[…]

The erroneous application of national law cannot, in itself, be an international denial of justice. Unless somehow qualified by international law, rights created under national law are limited by national law, including the principle that by operation of the fundamental rule of *res judicata* a determination by a court of final appeal is definitive. So even if an instance of municipal *mal jugé* is given weight by international adjudicators when determining that there has been a denial of justice, on the footing that rights created under national law have been so blatantly disregarded as to compel conviction with respect to violation of international standards as proscribing discrimination, bias, undue influence, or the like, it remains the case that the international wrong is not the misapplication of national law.

[…]

[T]o declare that judgments under national law are rationally unsustainable may expose the international jurisdiction to the criticism that it does not have an adequate intellectual foundation in the relevant national law.

It may seem that this discussion seriously undercuts the conclusion of the previous section (the general rule of non-revision) as well as the title of the present one. What needs to be understood is that even if in extreme cases the substantive quality of a judgment may lead to a finding of denial of justice, the objective of the international adjudicator is *never* to conduct a substantive review.[105]

105 J. Paulsson, "Denial of Justice in International Law" (2005) Cambridge University Press, **Exhibit RL-8**, pgs. 73, 81, 83-84 (Emphasis in original).

123. TGH has made no such allegations. As noted above, TGH makes practically no mention of the actions of the Guatemalan courts in the legal section of the Memorial.[106]

124. It is no surprise that TGH has not made these types of allegations. In its decisions issued on 18 November 2009 and 24 February 2010, the Constitutional Court ruled on the claims brought by EEGSA and TGH after granting the parties a full opportunity to present their arguments both written and orally.[107] Its decisions are, moreover, fully reasoned and well-founded.

125. In its decision of 18 November 2009,[108] the Constitutional Court, by a majority of its members, ruled on the nature of the Expert Commission's pronouncement, on the CNEE's power to approve the independent study of the consultant commissioned by the CNEE, and on the CNEE's power to adopt the tariff schedules based on such study. These issues are also the core of TGH's claim before this Tribunal. In sum, the Court decided as follows:

(a) The CNEE is the only entity empowered to approve the tariffs and is not authorized to delegate this function;[109]

(b) In cases where there are discrepancies between the VAD study submitted by the distributor and the Terms of Reference issued by the CNEE, the function of the Expert Commission is only to issue a pronouncement;[110]

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106 See section II.A.1.g, above.

107 See Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-105**, pgs. 13-15; Decision of the Constitutional Court, Case File 3831-2009, February 24, 2010, **Exhibit R-110**, pgs. 13-16.

108 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-105**.

109 *Ibid*., pgs. 30-32.

110 *Ibid*, pgs. 23-26.

(c) Once it has issued its pronouncement, the legal framework does not establish any additional functions for the Expert Commission; [111]

(d) In accordance with the advisory nature of expert opinions under Guatemalan law and given the CNEE's responsibility to adopt the tariffs, the Expert Commission's pronouncement cannot be binding in nature; [112] and

(e) Finally, the Court affirmed the regulatory nature of the CNEE's function to approve the tariffs, which must reflect the criteria fixed by law, in particular with respect to costs, including the cost of capital. The Court clarified, however, that this issue was not submitted to the courts. [113]

126. In turn, in its decision of February 24, 2010, the Constitutional Court found that:

(a) The relevant legislation does not grant the Expert Commission any function other than to issue a pronouncement on the discrepancies between the CNEE and the distributor;[114]

(b) The dissolution of the Expert Commission, once its pronouncement had already been issued, could not have caused harm to EEGSA;[115] and

(c) Given the advisory nature of expert pronouncements under Guatemalan law and the indelegable nature of the CNEE's duties and responsibilities regarding adoption of the tariffs, according to the

111 *Ibid*, pg. 25.

112 *Ibid*, pgs. 23 and 31-32.

113 *Ibid*, pgs. 32-33.

114 Decision of the Constitutional Court, Consolidated Case Files 3831-2009, February 24, 2010, **Exhibit R-110**, pgs. 31-32.

115 *Ibid*, pg. 32.

principles of legality and organization of the public administration, the pronouncement of the Expert Commission cannot be binding.[116]

127. Therefore, the matters at issue were examined at length and the decisions issued are well-reasoned. What TGH now claims is that the Constitutional Court was mistaken. In other words, the Court's decisions were not to its liking. While TGH may disagree with the decisions, this does not constitute a denial of justice. TGH is aware of this and does not argue denial of justice.

128. Having no credible basis to claim denial of justice, TGH nonetheless seeks to cast doubt on the integrity of the Guatemalan judiciary by citing in a footnote to the Memorial reports issued by non-governmental organizations expressing criticisms in this regard.[117] These reports do not support TGH's allegations.[118] The truth is that the Constitutional Court has not hesitated in supporting tariff increases for EEGSA even when these results were unpopular, [119] and has repeatedly demonstrated its independence from political power.[120]

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116 *Ibid*, pgs. 32-34.

117 Claimant's Memorial, footnote 1057.

118 The report of the International Commission of Jurists (**Exhibit CL-90**) bases its findings on a case concerning the candidacy of General Efrain Rios Montt to the Presidency of the Republic that was decided by the Constitutional Court in office between 2001-2006, which had a different composition from the Court deciding the *amparos* brought by EEGSA. It is also important to note that the Court in office during the period 2006-2011 overturned this ruling and withdrew this precedent from case law (Decision of the Constitutional Court, Case File 2395-2006, October 10, 2006, **Exhibit R-32**, pg. 7). On the other hand, the report issued by Transparency International (**Exhibit CL-100**) does not deal with the Constitutional Court, but rather the courts of ordinary jurisdiction. The report also refers to the situation prior to 2005, which has changed as of the creation of the International Commission Against Impunity in Guatemala (CICIG) in 2007. International Commission Against Impunity in Guatemala, "Two Years of Work: a Commitment to Justice", **Exhibit R-159**.

119 In 2010, for example, the Constitutional Court sustained the implementation of tariff increases in favor of EEGSA, which were fiercely opposed by the Human Rights Ombudsman of Guatemala. Decision of the Constitutional Court, Consolidated Case Files 719-2010, 721-2010, 722-2010, 723-2010, and 724-2010, March 3, 2010, **Exhibit R-113**, pgs. 4-6.

120 Also in 2010, for example, the Constitutional Court ordered the removal of the Minister of Education, Mr. Bienvenido Argueta, one of the most influential ministers of the Government, Decision of the Constitutional Court, Case File 4255-2009, February 25, 2010, **Exhibit R-111**, pg. 9, and ordered the removal of the Prosecutor General of the Republic and Director of the "Ministerio Publico", Conrado Reyes, a few days after his appointment by the then President Alvaro Colom. Decision of the Constitutional Court, Consolidated Case Files 1477, 1478, 1488,

C. CONCLUSION: TGH DOES NOT PRESENT A VALID OR ADMISSIBLE INTERNATIONAL CLAIM, THIS TRIBUNAL LACKS JURISDICTION, AND THEREFORE SHOULD NOT PROCEED TO THE *MERITS* OF THIS MATTER

129. TGH has limited itself to submitting before this Tribunal a disagreement with the CNEE concerning the interpretation and application of Guatemala's regulatory framework to EEGSA's 2008-2013 tariff review process; such disagreement, moreover, has already been decided by the Guatemalan courts in favor of the CNEE. This does not constitute a valid international claim. A regulatory authority does not violate an investment protection treaty every time that, in the exercise of its powers, it makes a decision with which the regulated entities disagree. This is particularly the case when the domestic courts have examined the matter and ruled in favor of the regulator. Nor do decisions of local courts that are not to the liking of a foreign investor violate an investment protection treaty. In such circumstances, an investor must claim denial of justice, and TGH has not done so.

130. This Tribunal cannot act as an appellate court of third or fourth instance in matters of Guatemalan law, and much less redo the tariff review and the determination of EEGSA's VAD as if it were the regulator of Guatemala's electric distribution services. This is excluded by the Treaty when it states that a U.S. investor "may submit to arbitration [...] a claim that the respondent has breached an obligation under" the Treaty.[121]

131. In short, TGH has failed to present a valid or admissible international claim, and thus this Tribunal has no jurisdiction. Accordingly, it should not proceed to review the merits of this matter.

1602, 1630-2012, June 10, 2010, **Exhibit R-120**, pg. 11. Further, it was the Constitutional Court which recently rejected the candidacy for President of the Republic of Sandra Torres, wife of the then President Alvaro Colom. Decision of the Constitutional Court, Case 2906-2011, August 8, 2011, **Exhibit R -141**, pg. 62.

121 CAFTA-DR, art. 10.16.

III. THE FACTS

A. THE REPUBLIC OF GUATEMALA

132. The Republic of Guatemala is a Central American nation located south of Mexico and north of Honduras and El Salvador, with a surface area of 108,889 km^2 and a population of 14.7 million inhabitants.

133. During the second part of the 20th century, Guatemala suffered a bloody civil war for 36 years as the nation alternated between military and civilian rule. It was not until 1996 that Guatemala could finally put an end to that war by signing the peace agreement between the Government and the Guatemalan National Revolutionary Unit (URNG).[122]

134. At that point, the Government of Guatemala decided to take advantage of the opportunity afforded by the peace agreement to reverse the institutional and social ills throughout the country. To that end, the Government instituted a series of structural reforms to modernize its legal and institutional framework; such reforms placed Guatemala among the ten countries adopting the most reforms worldwide.[123] In addition, the Government implemented a social development project, with the primary objective of reducing the poverty level by restructuring public spending, reducing resources dedicated to defense, and increasing social investment.[124] Through that reform process, Guatemala achieved: (i) greater institutional transparency; (ii) improved management of public finances; (iii) a substantial increase in social expenditure,[125] which prior to the reform was one of the lowest in Latin America; (iv) greater access to education in the most marginalized regions; (v) the implementation of new child nutrition programs;

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122 Agreement for Firm and Lasting Peace signed between the Republic of Guatemala and the National Revolutionary Unit of Guatemala (URNG), December 29, 1996, **Exhibit R-10**.

123 World Bank, Central America Department, Poverty Reduction and Economic Management Unit, Latin America and Caribbean Region, "Guatemala, Evaluation of Poverty," March 18, 2009, **Exhibit R-101**, pg. 105.

124 *Ibid.*, pg. vii.

125 Between 5 and 6 percent of GDP between 2004 and 2006. *Ibid.*, pg. 4.

(vi) a generation of constant economic growth; and (vi) the promotion of economic competitiveness.[126] Since 1996, economic management has remained solid, including a low fiscal deficit with inflation constantly declining.[127]

135. Successive government policies have sought to modernize infrastructure throughout the country. These policies placed special emphasis on the energy and telecommunications sectors, in order to provide the population with high-quality services at reasonable tariffs. At times, these policies have been paired with subsidies and social tariff policies financed directly by the State.[128]

136. As a result of this development policy, and its respect for the legal and institutional framework, Guatemala has successfully attracted significant levels of foreign direct investment, as illustrated in the following chart: [129]

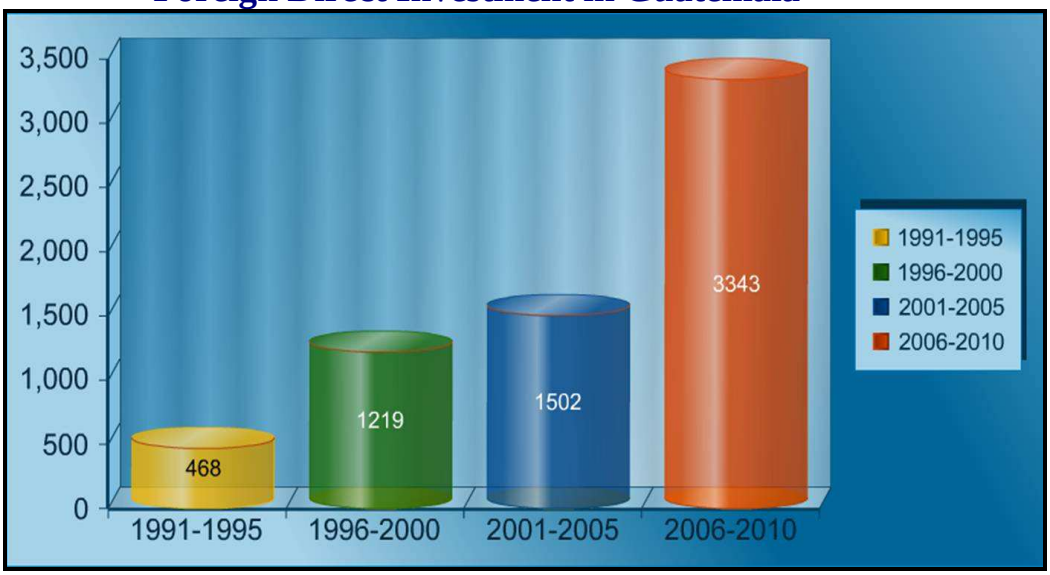
126 *Ibid.*, pgs. 4-5.

127 *Ibid.*

128 See, for example, "State profits will be directed towards a subsidy," *Prensa Libre*, July 3, 2010, **Exhibit R-124** ("With the utilities that correspond to the State, due to its shareholder participation in EEGSA, the biggest part of extraordinary subsidy for the electrical energy shall be covered. The subsidy ascends to Q127 million for the non-social Tariff of the quarter from May to July."); Government Resolution No. 188-2010, July 2, 2010, **Exhibit R-122;** Social Tariff Act, Decree 96-2000, December 29, 2000, published in *Diario de Centro América* No. 68 on January 2, 2001, **Exhibit C-52**.

129 Economic Commission for Latin America and the Caribbean, "Foreign Direct Investment in Latin America and the Caribbean 2009," May 2010, **Exhibit R-115**, pgs. 36 and 75; Economic Commission for Latin America and the Caribbean, "Foreign Direct Investment in Latin America and the Caribbean 2010" May 2011, **Exhibit-R-137**, pgs. 33 and 65; World Bank, Foreign Direct Investment, net inflows, http://www.eclac.org/publicaciones/xml/0/43290/2011-138-LIEI_2010-WEB_INGLES.pdf, 2011, Exhibit-**R-136**.

Foreign Direct Investment in Guatemala



Total investment by period indicated in millions of US dollars

137. Despite the global financial crisis, Guatemala continues to be among the Central American nations with the greatest flow of foreign direct investment.[130] It must be noted that Guatemala, unlike other countries in the region, does not form part of the group of countries known as the Bolivarian Alliance for the Americas (ALBA), nor has it adopted any policy to nationalize foreign investments. Rather, Guatemala continues to attract private-sector investment projects. In recent years the Guatemalan electricity sector itself has received an unprecedented flow of foreign capital investment.[131]

B. THE PRIVATIZATION OF THE ELECTRICITY SECTOR IN GUATEMALA

138. The parties generally agree on the reasons that motivated the privatization of the electricity sector. Nonetheless, in its Claimant's Memorial, TGH provides a distorted and baseless description of the regulatory framework within which Teco made its investments, and of its legitimate expectations when investing in

130 Economic Commission for Latin America and the Caribbean, "Foreign Direct Investment in Latin America and the Caribbean 2009," May 2010, **Exhibit R-115**, pg. 12.

131 Colom, **Appendix RWS-1**, para. 50, paras. 162-165.

Guatemala.[132] In particular, TGH completely ignores the distribution of powers among different agents in the electricity sector pursuant to the regulatory framework, and it distorts the model company system. In this section, Guatemala briefly describes the privatization process of the Guatemalan electricity sector, and provides a description of that framework.

1. The origin of the project to privatize the electricity sector in Guatemala

139. During the second half of the nineties, within the context of the institutional and social reforms described in Section I.A, above, Guatemala decided to privatize certain sectors controlled by the State, including the electricity sector,[133] to limit public spending and to finance the social development policies being promoted.[134]

140. Since 1959, electricity generation, transportation and distribution activities in Guatemala had been under the quasi-monopolistic control of a public agency, the National Electricity Institute (***INDE***). In the middle of the nineties, however, the INDE lacked the resources to make the investments in generation, transportation and distribution necessary to supply the growing demand for electricity. One of the principal reasons for the lack of resources was that the electricity tariff was set at the discretion of the President of the Nation, and did not reflect the costs of the service, but rather the political will of the Government.[135]

141. The lack of State resources to offset costs not covered by users left the INDE without the means to attend the growing demand for electricity. In that context, in 1991, the Government began considering the possibility of de-monopolizing and decentralizing the electricity sector.[136] Thus in 1993, the United States Agency

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132 Claimant's Memorial, sections II.B and C.

133 The communications, highway, railway and mail sectors, among others, were also privatized.

134 Government Resolution No. 865-97, December 18, 1997, **Exhibit C-23**, second whereas.

135 Claimant's Memorial, para. 12; Statement of Witness Enrique Moller Hernández, January 24, 2012 (hereinafter ***Moller***), **Appendix RWS-2**, para. 6.The INDE proposed the electricity tariff.

136 Moller, **Appendix RWS-2**, para. 6.

for International Development (USAID) commissioned expert Chilean engineers, Sebastián Bernstein and Jean Jacques Descazeaux, to prepare a diagnostic study and proposal to reform the sector.[137] That study recommended that the electricity sector be restructured, as efficiency would be improved through the participation of the private sector in its development and operation.[138]

142. Following these recommendations, the Government modified the INDE law in December 1994 in order to de-monopolize the sector and allow private agents to compete with the state company.[139] Likewise, Article 50 of the INDE reform law stipulated that within a maximum period of six months, an overall proposal for reform would be presented to the Congress.[140]

143. Pursuant to that legal directive, several draft laws were presented, which were discussed by the Congressional Committee of Energy and Mining. To prepare the text of the electricity law and its regulation, Guatemala relied on the advice of Synex, well-known Chilean consultants, whose team included Sebastián Bernstein, who had already advised the Government regarding the de-monopolization of the sector.[141] When preparing the draft law, which was based to a large degree on the Chilean model, the regulatory models of the electricity sector in Great Britain and in Argentina were also considered.[142] We note that the legal expert in Guatemalan law, Juan Luis Aguilar Salguero, was hired by USAID

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137 JS Bernstein and JJ Descazeaux, "Restructuring the Power Sector in Guatemala: Analysis of Decentralization and Private Participation Mechanisms: Final Report", June 1993, **Exhibit R-3**, pg. 1.

138 *Ibid.*, **Exhibit R-3**, pgs. 4-5.

139 Organic Act of the National Electrification Institute, Congressional Decree 64-94, December 7, 1994, published in Diario de Centro América No. 86 on February 20, 1995, **Exhibit R-4**. INDE was in turn created by Decree-Law 1287 of 1959, **Exhibit R-1**.

140 Moller, **Appendix RWS-2** para. 8; Organic Act of the National Electrification Institute, Congressional Decree 64-94, December 7, 1994, published in Diario de Centro América No. 86 on February 20, 1995, **Exhibit R-4**, art. 50.

141 USAID, Draft General Electricity Act and its RLGE: Final Draft, April 4, 1995, **Exhibit R-6**, preamble.

142 Moller, **Appendix RWS-2**, para. 9; Service Agreement Between EEGSA and the State of Guatemala, September 10, 1998, **Exhibit R-19**.

to advise Mr. Bernstein on Guatemalan law, and therefore was directly involved in the regulatory reform.[143]

144. As is explained by Enrique Moller Hernández, current director of the CNEE and member of the team in charge of the electricity sector reform project, one of the principal objectives of the law was to place the determination of tariffs in the hands of a technical body that would work autonomously and independently of the Political Branch.[144] It was therefore necessary to establish a mechanism to limit political influence over the designation of the members who would form the technical body. Given the prestige of the university sector in Guatemala (in particular the University of San Carlos for its participation in the reform projects underway in Guatemala), it was proposed that the university sector be involved in appointing the board of directors of the entity. It was also decided that the agents in the wholesale market (that is, the private agents in the sector and, in particular, the distributors, such as EEGSA) and the Ministry of Energy and Mines (***MEM***) be involved in appointing the board of directors. Thus, the MEM, the provosts of the universities and the market agents would propose a shortlist to the Executive, who would select one member from each sector, to form the Board of Directors of the regulatory body.[145]

145. In order to establish objective tariffs based on technical and economic criteria, a proposal was made for regulations based on the "efficient company" model that had been implemented in Chile in the eighties and later implemented with certain variations, in different countries such as Argentina, Brazil, Ecuador, El Salvador, Nicaragua, Peru and the Dominican Republic.[146]

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143 Informe del experto Dr. Juán Luis Aguilar Salguero, 24 de enero de 2012 (en adelante ***Aguilar***), **Apéndice RER-3**, párrs. 5.

144 Moller, **Appendix RWS-2**, para. 13.

145 *Ibid.*, para. 19.

146 M Abdala and M Schoeters "Damages and Economic Regulation Opinion in TECO Guatemala Holdings, LLC v. Republic of Guatemala", January 24, 2012 (hereinafter ***M Abdala and M Schoeters***), **Appendix RER-1**, paras. 104-110.

146. In order to limit excessive profits and ensure efficiencies, the "efficient" or "model" company system utilizes a theoretical company that seeks to replicate how a regulated company should function within an efficient operational and investment framework.[147] The tariffs thus reflect only the costs of an efficient company. If the distributor is more efficient than the model company, that distributor is ensured a greater return on its investment. All inefficiencies on its part, on the other hand, reduce its return margin.[148] Under this logic, Guatemala expected that, as successive tariff reviews were performed, the tariffs would fall in real terms.[149] That was particularly true of the area under concession, which is a geographically small area with the highest population and industrial density in Guatemala.[150]

2. The General Electricity Law and its Regulations

147. Having reviewed the proposals and the model company approach, on September 19, 1996, the Congressional Committee of Energy and Mines approved the draft electricity law project in discussion.

148. Based on this report, the General Electricity Law (the ***LGE***) was approved by Congress on October 16, 1996, with certain amendments aimed at strengthening the CNEE's independence.[151] The Regulation of the LGE (the ***RLGE***) was approved some months later, on March 21, 1997. In the next section we refer to the terms of the regulatory framework existing at the time when Teco decided to invest in Guatemala. The modifications to the RLGE are analyzed in further detail in Section III.E.

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147 Expert Opinion of Mario Damonte, January 24, 2012 (hereinafter Damonte), **Appendix RER-2**, paras. 23-26; Colom, **Appendix RWS-1**, para. 50.

148 M Abdala and M Schoeters, **Appendix RER-1**, paras 116 and 120; Damonte, **Appendix RER-2**, para. 25.

149 Damonte, **Appendix RER-2**, para 26.

150 Colom, **Appendix RWS-1**, para. 34.

151 LGE, **Exhibit R-8**. For example, in article 4 of the LGE it was added that the CNEE, besides being a technical body, would enjoy functional independence in the exercise of its powers, Diary of the Congress of the Republic, October 16, 1996, **Exhibit R-9**, pg. 112. See para. 155 below.

a. The regulatory agency of the electricity sector: the National Electric Energy Commission

149. As was explained by the Congressional Committee of Energy and Mining when it approved the draft LGE, the objective was to create a regulatory entity that would determine tariffs in accordance with clear and generally applicable legal precepts.[152] This implied a radical change with respect to the prior system, in which there was no regulatory agency and tariffs were defined by the President of the Republic based on his own criteria. The creation of a regulatory agency and the rules that governed its conduct were stipulated in the LGE and the RLGE.

150. Within that context, Chapter II of the LGE created the CNEE and granted it the functions of a regulatory agency for electricity generation, transportation, distribution and sales activities.[153] As was explained by the legislature in the LGE's preamble, the principal objective of instituting a regulator was to create a technical, independent and qualified body that would be representative of all interested agents in the electricity sector:

> **WHEREAS**
>
> It is necessary to establish the basic legal regulations to allow activity in the various sectors of the electrical system, seeking its optimal operation, which makes it imperative to establish a qualified technical Commission, chosen from among those proposed by the national sectors that are most interested in the electrical subsector's development.[154]

151. The application of these principles rested on the idea that the regulatory body should have the independence necessary to carry out its duties. Thus, the LGE stressed this attribute in the very article that created the CNEE, Article 4, and it repeated it in Article 29 of the RLGE:

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152 Congressional Committee of Energy and Mining, approval of the General Electricity Law Draft, September 29, 1996, **Exhibit C-15**, pg. 2.

153 LGE, **Exhibit R-8**, art. 4.

154 LGE, **Exhibit R-8**, last whereas (Emphasis added).

> Art. 4 – LGE: "The Commission shall have functional independence in exercising its powers […]".[155].
>
> Art. 29 – RGLE: "The Commission shall have functional independence, its own budget and exclusive funds […]".[156]

152. It is worth noting that the draft of the LGE as submitted to Congress established the CNEE as a body fully dependent on the MEM.[157] However, in the final approval of the LGE, through an amendment proposed by the Congressional Committee of Energy and Mining, the CNEE was assured by law "functional independence to exercise its powers and the following functions […]", which strengthened the independence of the CNEE and its directors.[158]

153. The LGE and the RLGE contain several other provisions to ensure the objectives set forth in the LGE's Preamble are implemented. First, to ensure the technical character of the CNEE, the LGE requires that its Board of Directors be comprised of university professionals of recognized prestige, specializing in the subject of electricity.[159]

154. Second, in order to ensure the independence of the directors of the CNEE, the LGE requires that all interested agents of the electricity sector be involved in selecting directors. Thus the CNEE is comprised of three directors named by the Executive but chosen from among three shortlists of candidates proposed by:[160]

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155 LGE, **Exhibit R-8**, art. 4; Diary of the Congress of the Republic, October 16, 1996, **Exhibit R-9**, pg. 112 (Emphasis added).

156 RLGE, **Exhibit R-36**, art. 29 (Emphasis added).

157 Diary of the Congress of the Republic, October 16, 1996, **Exhibit R-9**, pg. 69 ("The National Electricity Commission ('the Commission') is hereby created as a technical entity of the Ministry […]").

158 *Ibid.*, **Exhibit R-9**, pg. 112; LGE, **Exhibit R-8**, art. 4.

159 LGE, **Exhibit R-8**, art. 5.

160 *Ibid.*, **Exhibit R-8**, art. 5; RLGE, **Exhibit R-36**, art. 30; Diario del Congreso de la República, October 16, 1996, **Exhibit R-9**, pgs. 112-113; Colom**, Appendix RWS-1,** para. 19.

- the national universities;[161]
- the MEM; and
- wholesale market agents, including electricity distributors (among them, EEGSA).[162]

155. Although each sector has full freedom to choose its candidate for Director, it may not select a candidate with any relation to regulated electricity companies.[163] Once the sectors have presented their shortlists of candidates, the Executive names one Director from each shortlist via Government Resolution. Therefore, although the Executive names the members, it may select only from among the candidates proposed by the sectors. This selection process, coupled with the technical prerequisites to be Director, ensures that the CNEE has no relationship with or political dependency on the Government, as the majority of the Board members are proposed by sectors alien to it. Notably, TGH neither describes the selection of the regulatory body, nor the distributors' participation in that selection.

156. The LGE establishes that the Directors must employ "independence of judgment", for which they are personally liable:

> The Commission's resolutions shall be adopted by a majority of its members, who shall perform their duties with absolute independence of judgment and under their sole responsibility.[164]

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161 For the decision on the selection from the shortlist to be valid, participation is required by at least one-half plus one of the provosts. RLGE, **Exhibit R-36**, art. 30(d).

162 "The wholesale market agents will be represented by four people appointed by each one of the organizations accredited by the Ministry, [including] generators, transporters, marketers, and distributors." RLGE, **Exhibit R-36**, art. 30(e).

163 LGE, **Exhibit R-8**, art. 5.

164 *Ibid.* (Emphasis added).

157. Finally, the LGE stipulates that the Board of Directors be named every five years.[165] As a result, their terms of office do not coincide with that of the President of the Republic, who is elected every four years.

158. Finally, to ensure that the CNEE could exercise its technical functions independently from the political powers of the day, the LGE and the RLGE granted the CNEE financial independence, authorizing it to determine its "own budget and funds."[166] Such funds are generated by fees paid by electricity distributors based on their monthly sales.

159. These factors – the CNEE's independence from the executive branch, its technical nature, and distributor representation among its Board – guaranteed investors that tariff reviews would be depoliticized. Contrary to TGH's allegations, such depoliticization was not achieved by conferring distributors with the power to set tariffs.[167] As explained in detail in the next section, the CNEE has the obligation to determine the methodology and to ultimately define tariffs.

b. The role of the CNEE in the process of setting distribution tariffs

160. As TGH itself acknowledges, the LGE attributes the following functions to the CNEE:

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165 *Ibid.*, art. 5; Political Constitution of the Republic of Guatemala, June 3, 1985, **Exhibit C-**, arts. 157, 184, 251, 252, 254 (Members of Congress, the President and the Vice President, the Prosecutor General of the Nation, the Attorney General of the Nation and the Municipal Government).

166 LGE Article 4 and RLGE Article 29 establish:

> Art. 4 – LGE: "The [CNEE] shall have its own budget and funds, which it shall apply to financing its ends. The Commission's revenues shall be derived from applying a rate to the monthly electricity sales of each electric distribution company"
>
> Art. 29 – RLGE: "The [CNEE] shall have functional independence, its own budget and exclusive funds […]"

LGE, **Exhibit R-8**, art. 4; RLGE, **Exhibit R-36**, art. 29.

167 Aguilar, **Appendix RER-3**, para. 10.

> Defining the transmission and distribution tariffs subject to regulation in accordance with this law, as well as the methodology for calculation of the same.[168]

161. For its part, Article 61 establishes as follows:

> The tariffs to users of the Final Distribution Service shall be determined by the [CNEE] by adding the power and energy acquisition cost components, freely agreed upon among generators and distributors and referenced to the inlet to the distribution network with the components of efficient costs of distribution to which the preceding article refers. [169]

162. As is well-established in LGE Article 4(c), the definition of the methodology and the tariffs cannot be arbitrary, but rather must be performed in accordance with the guidelines established by the law itself. These guidelines are defined by LGE Articles 61 and 71, under which the CNEE has the obligation to guarantee that the tariff reflects:

- the acquisition cost of energy and power acquired by the distributors based on freely negotiated prices; and
- the cost of capital and the operating costs of an efficient company, or Value-Added for Distribution (***VAD***).[170]

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168 LGE, **Exhibit R-8**, art. 4(c) (Emphasis added).

169 Ibid., **Exhibit R-8**, art. 61 (Emphasis added). Article 29 of the RLGE confirms this authority, establishing:

> [The function of the CNEE] shall be to determine the prices and quality of the provision of the services of transportation and distribution of electricity […]

RLGE, **Exhibit R-36**, art. 29.

170 Article 61 establishes:

> The tariffs to users of the Final Distribution Service shall be determined by the Commission by adding the power and energy acquisition cost components, freely agreed upon among generators and distributors and referenced to the inlet to the

163. The methodology for calculating tariffs is established under the Terms of Reference, which is prepared by the CNEE every five years, for each tariff revision.[171] Thus, LGE Article 74 provides:

> The terms of reference of the study(ies) of the VAD shall be drawn up by the Commission […][172].

> distribution network with the components of efficient costs of distribution to which the preceding article refers. The tariffs shall be structured so as to promote equality of treatment among consumers and the economic efficiency of the sector.

Article 71, for its part, establishes:

> The tariffs to end consumers for the final distribution service, in their components of power and energy, shall be calculated by the Commission as the sum of the weighted price of all the distributor purchases, referenced to the inlet to the distribution network, and the Valued-Added for Distribution (Valor Agregado de Distribución - VAD).
>
> [...]
>
> The VAD is the average cost of capital and operation of the distribution network of a benchmark efficient company operating in a given density area.

LGE, **Exhibit R-8**, arts. 61 and 71.

RLGE Articles 29 and 82 in turn establish:

> **Article 29. Functions.** The National Electric Energy Commission, hereafter the Commission, shall be a technical agency of the Ministry. The Commission shall have functional independence, its own budget and exclusive funds, the function of which shall be to determine the prices and quality of the provision of the services of transportation and distribution of electricity subject to authorization, control and ensure the competitive conditions in the Wholesale Market, and all the other responsibilities assigned to it by the Law and these Regulations.
>
> [...]
>
> **Article 82. Supply Costs.** The supply costs for the calculation of the Base Tariffs and per voltage level, shall be approved by the Commission by way of Resolution, and shall be based on the structure of an efficient company.

RLGE, **Exhibit R-36**, arts. 29 and 82 (Bold emphasis in original).

171 Colom, **Appendix RWS-1**, para. 38.

172 LGE, **Exhibit R-8**, art. 74 (Emphasis added).

164. As indicated by Mr. Bernstein (the expert named by USAID for the reform of the sector) in a study on the tariff revision process:

> The VAD are calculated by the Distributors through a study requested from a consultant company pre-qualified by CNEE, that shall comply with the methodology established by the Commission in the reference terms of said studies […][173].

165. The LGE specifically defines the costs that must be approved by the CNEE in order to determine the tariffs: only those "standard distribution costs of efficient companies". [174] The RLGE specifically defines which costs must not be recognized and grants the CNEE the discretion to reject any costs that it considers inappropriate or excessive. Thus, RLGE Article 83 establishes:

> **Unrecognized Costs.** The following shall not be included as supply costs for the calculation of the Base Tariffs: financial costs, equipment depreciation, costs related to generation assets owned by the Distributor, costs associated with the public lighting installations, loads due to excess demand over the demand contracted, established in the Specific Regulations of the Wholesale Market Administrator, any payment that is additional to the capacity agreed in the capacity purchase contracts and other costs that, in the opinion of the Commission, are excessive or do not correspond to the exercise of the activity.[175]

166. Therefore, it is up to the CNEE to ensure that the tariffs paid by consumers only reflect (i) efficient costs; (ii) costs that are not excessive; and (iii) costs related to the distribution of electricity. Conveniently TGH also chooses to ignore these essential powers granted to the CNEE through the regulatory framework. LGE Article 76 is clear in requiring the CNEE to structure distribution tariffs and that:

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173 JS Bernstein "Some Methodological Aspects to Consider in the Terms of Reference for the Value-Added for Distribution Study", May 2002, **Exhibit R-23**, pg. 2 (Emphasis added).

174 LGE, **Exhibit R-8**, art. 60 (Emphasis added); see also RLGE, **Exhibit R-36**, art. 84.

175 RLGE, **Exhibit R-36**, art. 83 (Bold emphasis in original, underlined emphasis added).

> These tariffs should strictly reflect the economic costo of acquiring and distributing electrical energy.[176]

167. This means that the CNEE, as the entity responsible for approving tariffs, should ensure that they reflect a suitable VAD (the economic cost of distributing electric energy). Conveniently, TGH also chooses not to mention these essential powers authorized to the regulator by the regulatory framework.

168. In order to establish a methodology and tariff based on technical criteria, the CNEE is free to contract external studies and consultants as it deems necessary. Thus, LGE Article 5 establishes:

> The [CNEE] may commission professional advice, opinions and expert reports needed for the discharge of its functions. [177]

169. For its part, RLGE Article 32 establishes:

> The budget shall be used by the Commission for its operation, the contracting of studies, technical advice and the preparation of the documents foreseen in these Regulation.[178]

170. The authority to contract external consultants allows the CNEE to obtain technical and third-party support to determine the methodology and tariff.[179] As Mr. Bernstein stated in 2002:

> In order to exercise its control functions, CNEE shall be able to carry out a critical analysis of every step of the study commissioned by the Distributors, which implies, in practice, to carry out of an independent study, but implementing the same methodology.[180]

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176 LGE, **Anexo R-8**, art. 76.

177 *Ibid.*, art. 5.

178 RLGE, **Exhibit R-36**, art. 32.

179 Colom, **Appendix RWS-1**, paras. 39.

180 JS Bernstein "Some Methodological Aspects to Consider in the Terms of Reference for the Value-Added for Distribution Study", May 2002, **Exhibit R-23**, pg. 2.

171. Despite the clear terms of the LGE and the RLGE, TGH attempts to confine the CNEE to the mere role of "supervisor" of the progress of the tariff study prepared by the company consultant.[181] That interpretation, however, is directly incompatible with the letter of the law. The CNEE is the regulatory entity that is specifically empowered to determine tariffs and therefore also to define and approve the VAD.[182] Even though the distributor directly participates in the tariff review process, it is clear that it is not, and could not be, on equal footing with the CNEE.

c. The Constitutional Court of Guatemala has confirmed the scope of the authority of the CNEE as established by the LGE

172. The Constitutional Court, the highest court of the Guatemalan judicial system and the maximum authority for the interpretation of its law, analyzed the CNEE's authority under the LGE in its decisions of November 18, 2009 and February 24, 2010. The aforementioned decisions responded to two *amparo* actions initiated by EEGSA in Guatemala. The Court held that:

(a) The CNEE is a body integrated pursuant to a company's plural appointment system with the powers to determine tariffs and their calculation methodology,[183] and is responsible for the approval of tariffs;[184]

(b) The setting of tariffs and the methodology for its calculation, constitutes not only a power, but also an obligation, for which the CNEE is responsible according to the law; it cannot be delegated to any entity or

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181 Claimant's Memorial, para. 40. This same fallacious argument was used by EEGSA during the tariff review process in 2008: see, e.g., Letter from Miguel Francisco Calleja to Carlos Colom Bickford, February 19, 2008, **Exhibit R-57**, pgs. 2-4.

182 Aguilar, **Apéndice RER-3**, párrs. 10, 46-58.

183 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-110**, pg. 34.

184 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-105**, pg. 31.

body, given that such act would be contrary to the principles of legality and public function;[185] and

(c) Neither the LGE nor the Regulation provide any additional function to the Expert Commission once it has issued its pronouncement.[186]

173. Thus, the Constitutional Court confirmed that the CNEE was empowered by the LGE to determine the applicable methodology as well as the final tariffs, and that such powers could not be delegated.

d. The procedure for determining electricity distribution tariffs

174. The RLGE establishes that tariffs must be established at the start of every five-year tariff period, and that they will remain in effect for the entirety of that period.[187] The LGE considers these five-year periods to be an efficient cycle with which to conduct the tariff reviews.

175. The RLGE further establishes that in the course of these tariff periods, there should be periodical adjustments, which currently are semi-annual and quarterly.[188] The tariff review process is detailed in Chapter III of the LGE and in RLGE Articles 97 to 99. The process commences with the approval of the Terms of Reference by the CNEE.

(i) The determination of the Terms of Reference for preparing the tariff study

176. As mentioned in the prior section, the CNEE is responsible for defining the methodology under which the tariffs will be calculated.[189] That methodology is

185 *Ibid.*, pg. 29; Decision of the Constitutional Court, Case File 3831-2009, February 24, 2010, **Exhibit R-110**, pg. 34.

186 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November 18, 2009, **Exhibit R-105**, pg. 25; Decision of the Constitutional Court, Case File 3831-2009, February 24, 2010, **Exhibit R-110**, pgs. 15-16.

187 RLGE, **Exhibit R-36**, art. 84.

188 *Ibid.*, art. 86.

189 LGE, **Exhibit R-8**, art. 74.

set forth in the Terms of Reference, issued through an administrative resolution by the CNEE.[190] The Terms of Reference is the technical guide that establishes how the VAD must be calculated. In the words of Mr. Carlos Colom, President of the CNEE:

> The ToR establish, in conformity with the Electricity Law and RLGE, the content and scope of the tariff studies, prepared by both the distributor and the CNEE.[191]

177. In other words, the Terms of Reference establish how the "model" company is to be defined, and how to determine the cost of capital and the operating costs of that company (the VAD).

178. Once established, the CNEE communicates the Terms of Reference via resolution to the distributors, at least eleven months prior to the date that the tariffs are to take effect.[192] The distributor may oppose the resolution, administratively or judicially, if it believes that the Terms of Reference violate the LGE or the RLGE.[193] As is logical, once the matter is judicially settled, the content of the Terms of Reference is fixed and may not be later reopened or amended except by agreement of the parties.

(ii) Summary of the methodology for calculating the VAD according to the LGE

179. The LGE establishes that electricity distribution tariffs for regulated users (consumers with demand below 100 kW) must be comprised of: (i) the average price of all energy purchases by the distributor; (ii) distribution losses; and (iii)

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190 *Ibid.*, art. 77.

191 Colom, **Appendix RWS-1**, para. 38.

192 RLGE-excerpts, **Exhibit R-12**, art. 98; RLGE, **Exhibit R-36**, art. 98. The RLGE currently establishes a minimum of twelve months. See Section II.E.3 below.

193 RLGE-excerpts, **Exhibit R-12**, art. 149; RLGE, **Exhibit R-36**, art. 149. The RLGE currently establishes that the available opposition mechanism is vacatur. See Section II.E.3 below.

the cost of capital, operation and maintenance associated with the distribution, expressed per unit of transmitted power − the VAD.[194]

180. The first tariff component is transferred entirely to the consumer through a mechanism called "*pass-through*," and therefore does not represent a source of income for the distributor.[195] The third component, the VAD, on the other hand, represents the compensation to the distributor, and also includes operating and maintenance costs (the cost of capital). The calculation of the cost of capital in 2008, the element at the heart of the present dispute, is the focus of this Section.

181. The cost of capital is comprised of two elements: (i) amortization of the capital invested by the distributor; and (ii) the return on that capital.[196] Under the LGE, the amortization and return are not calculated on the capital actually invested by the distributor, but rather on the basis of the capital of an efficient model company:

> The VAD is the average cost of capital and operation of the distribution network of a <u>benchmark efficient</u> company […][197]

182. The calculation of that capital base is therefore crucial. If the capital base is inefficient and therefore overvalued, the investor is compensated for investments that it did not make, nor will not make, given that there are no mandatory investment plans under the Guatemalan regulatory system. Therefore, not only will the consumer be paying for a service that he does not nor will not receive, but the distributor will also have no incentive to make improvements to the service.

183. According to Guatemalan regulations, to determine the capital base of the model company, the distributor's consultant must construct the network that most efficiently provides electricity service in the covered distribution area, in

194 Colom, **Appendix RWS-1**, para. 36. The tariff also includes transportation costs.

195 *Ibid.*

196 Damonte, **Appendix RER-2**, para. 64.

197 LGE, **Exhibit R-8**, art. 71 (Emphasis added).

accordance with the guidelines established by the Terms of Reference. That is, the consultant must establish the installations and operating processes necessary to efficiently provide service for the estimated demand, taking into account new technologies available.[198] Such installations are known as construction units.[199] By way of example, a construction unit is one kilometer of aerial network, one transformer or one pole.[200]

184. Once the construction units are identified, they must be optimized, that is, only those units that are economically justified (in terms of quantity and cost) can be selected to construct the capital base. Under the terms of the LGE:

> The investment annuity shall be calculated based on the New Replacement Value of the optimally designed facilities […] The concept of economically adapted installation involves recognizing in the New Replacement Value only those facilities or parts of facilities that are economically justified to provide the required service.[201]

185. Thus, for example, the consultant must determine whether it is more efficient to use reinforced concrete or wooden poles, whether transformers with greater or weaker power should be installed, etc. Likewise, the optimal number of each one of these units must be determined; for example, determining whether 100 transformers are needed to cover the area, or whether 80 are sufficient. Thus, with

198 There are two methods for building the model company. Under the *Bottom Up* method, used in Guatemala, an entirely new network is created that is capable of covering the demand in a specific geographic region (with minimum to no reference to the actual company), taking into account the energy entry points into the actual distribution area. The *Top Down* method starts with the existing network and adjusts the assets to achieve the greatest efficiency possible. Damonte, **Appendix RER-2**, para. 32-36; M Abdala and M Schoeters, **Appendix RER-1**, párr. 121.

199 A construction unit is comprised of a set of building blocks. Each building block is comprised of materials configured in a pre-established way to that comprise an assembly unit, which facilitate the design of electricity distribution installations simply, orderly, and uniformly.

200 Damonte, **Appendix RER-2**, Chapter 3.3.1.

201 LGE, **Exhibit R-8**, art. 67 (Emphasis added).

the assistance of computer and electricity distribution engineering models, the capital base of the model company is determined.[202]

186. Once the efficient and optimized capital base has been determined, that capital base must be valued. In practice, there are different methods to value the capital base. The LGE values assets by using the VNR or new replacement value method.

187. As explained by Mr. Mario Damonte, unlike the traditional accounting model for valuing assets (which takes the acquisition cost of the assets and adjusts them for inflation) or the reinstatement system (which takes the market value of the assets), the VNR method values the asset at its replacement value. The replacement value is the market price of the available asset that best (more efficiently in terms of technology and price) performs the function of the asset in question. Thus, the replacement method (unlike the reinstatement method) not only reflects the current value of the asset or capital base, but also includes the efficiencies of the new technologies available in the market.[203]

188. The VNR method was defined by the LGE Article 67 under the following terms:

> The New Replacement Value is the cost involved in building the works and physical assets of the authorization[204] with the technology available on the market to provide the same service.[205]

189. Once the value of the optimized asset base is defined, this value is used to calculate the investor's compensation. For this, the value of the VNR is included in a formula (FRC) that is used to calculate the investor's cost of capital,[206] which includes:

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202 Damonte, **Appendix RER-2**, Chapter 3.3.1.

203 Damonte, **Appendix RER-2**, paras. 49-50; see also JA Lesser and LR Giacchino, *Fundamentals of Energy Regulation* (1st ed. 2007) (excerpt), **Exhibit R-34**, pgs. 100-101.

204 Authorization is used here as the distribution area for which the distributor is responsible.

205 LGE, **Exhibit R-8**, art. 67.

206 M Abdala and M Schoeters, **Appendix RER-1**, Chapter 3.5.2. LGE, **Exhibit R-8**, art. 73:

(a) depreciation, which allows the investor to recover the capital invested by establishing a reserve fund that can eventually be used to replace the asset once its useful life has expired.[207] This value is calculated based on the gross value of the capital base; and

(b) the return, which compensates the investor for the opportunity cost of its capital, through profit, which is calculated on the net or depreciated value of the capital base.[208] According to the LGE the rate of return is defined by the regulator but must be between 7% and 13% in real terms.

190. Contrary to what was argued by TGH[209] and by EEGSA in the 2008 tariff review, and as confirmed subsequently by the Expert Commission and even the TGH's expert Kaczmarek[210], the return is not calculated on the VNR, but rather on the VNR net of depreciation. If not, the investor would be compensated on the capital already recovered, which is contrary to the basic principles of economic theory.[211]

> The cost of capital […] shall be calculated as the constant annuity of cost of capital corresponding to the New Replacement Value of an economically designed distribution network. The annuity shall be calculated on the basis of the typical useful life of distribution facilities and the discount rate that is used in the calculation of the tariffs […]

(Emphasis added).

207 If the investor reinvests this money, it goes toward an increase in the compensable capital base.

208 Damonte, **Appendix RER-2**, para. 64.

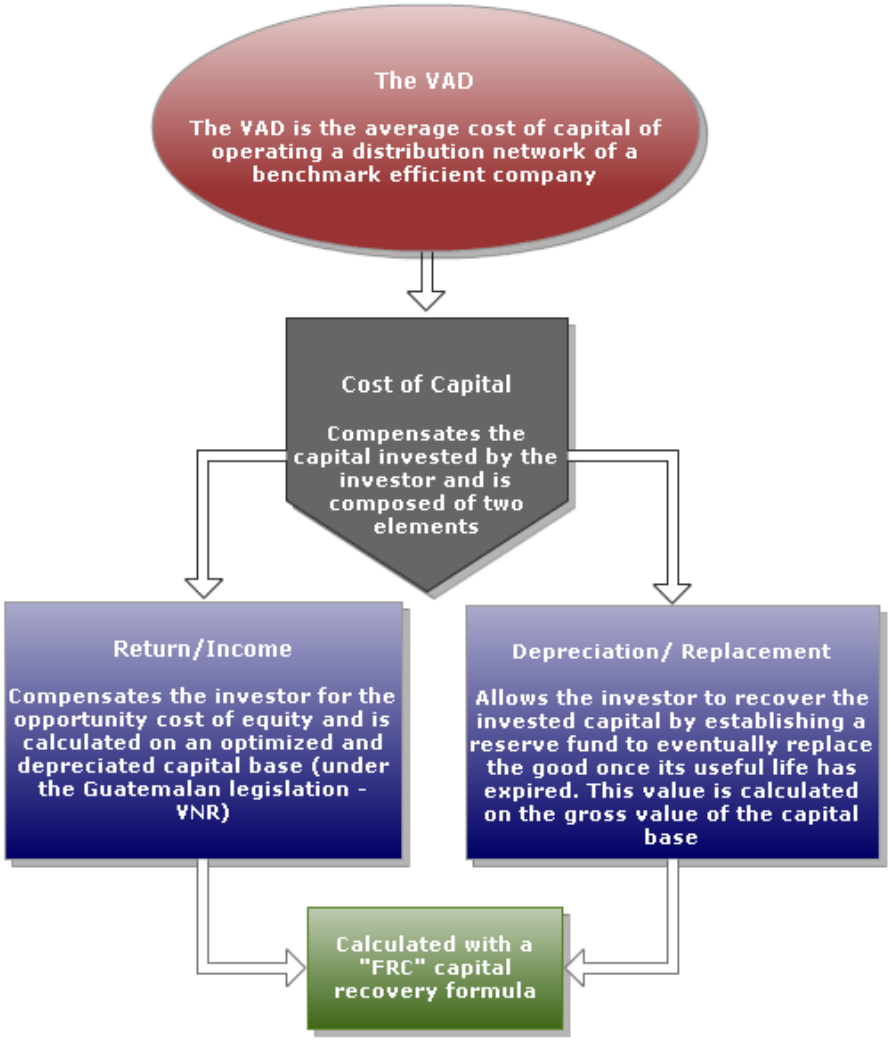
209 Claimant's Memorial, para. 35.

210 See section III.F.10.c below. This had also been the focus for the 2003 tariff review 2003; see Kaczmarek, **Appendix CER-2**, paras. 89-90.

211 AE Kahn, *The Economics of Regulation, Principles and Institutions* (1996) Vol. 1 (excerpt), **Exhibit R-7**, pg. 32.

> The return to capital, in other words, has two parts: the return *of* the money capital invested over the estimated economic life of the investment and the return (interest and net profit) *on* the portion of the investment that remains outstanding. The two are arithmetically linked, since according to the usual (but not universal) regulatory practice the size of the net investment, on which a return is permitted, depends at any given time on the aggregate amount of depreciation expense allowed in the previous years—that is, the amount of investment that

191. The following graphic illustrates these elements:



> remains depends on how much of it has been recouped by annual depreciation charges previously.

Likewise, when describing the costs to be recovered by the investor, TGH's witness, Mr. Giacchino, explains in his book Fundamentals of Energy Regulation:

> The cost of doing business will also include a fair return on the firm's undepreciated capital investment, which is called the rate base, including interest payments on short- and long-term debt and a return on equity capital.

JA Lesser and LR Giacchino, *Fundamentals of Energy Regulation* (1st ed. 2007) (excerpt), **Exhibit R-34**, pg. 68; Damonte, **Appendix RER-2**, para. 65.

(iii)The VAD calculated by the distributor expert

192. Once the methodology is established in the Terms of Reference, the LGE stipulates that each distributor must contract a prequalified engineering firm to conduct a tariff study to calculate the VAD.[212]

193. It is worth noting that different countries have adopted different approaches with respect to who should prepare the tariff study (the distributor or the regulator) and there is no clearly predominant position in this regard. Although in some countries the distributor prepares the study, there is a consensus that the regulator must always commission an independent expert to prepare a parallel study to review the distributor's study, and make objections and modifications thereto. The weight assigned to each study varies. For example, in Chile two studies are prepared; in case of a disagreement their results are weighted, assigning 2/3 of the value to the regulator's study, and 1/3 to the distributor's study.[213] In Peru, on the other hand, the distributor performs its study, which the regulator audits with its independent study;[214] both studies are then subjected to a public hearing.[215]

194. Under Guatemala's LGE, the distributor performs the study, and the regulator has the right to comment on, approve, or reject the study. This task is delegated to the distributor principally because the distributor is better positioned to access the information and documentation necessary to perform the study.[216] This mechanism prevents the regulator from directly intervening in the company to

212 LGE, **Exhibit R-8**, art. 74.

213 General Electricity Services Act DFL No. 1/1982, amended by Law 20,018 of 2006, September 13, 1982 **Exhibit R-2**, art. 107.

214 Law for transparency and simplification of the regulatory procedures for tariffs, Law No. 27838, published in the Diario Oficial El Peruano on October 4, 20002, **Exhibit R-24**, art. 7.

215 Law of Electrical Concessions, Law Decree No. 25844, published in the Dairio Oficial El Peruano on November 19, 2002, **Exhibit R-26**, arts. 67 and 68.

216 Colom, **Exhibit RWS-1**, para. 51.

gather the information that would be necessary if the regulator were the one to perform the VAD study.[217]

195. Under the RLGE, the CNEE prepares a list of prequalified consultant firms that may perform the VAD study.[218] To qualify those consulting companies, the CNEE invites firms to present their qualifications and selects the firms it believes to be the most technically suitable to perform the task.[219]

196. The distributor then selects its consultant from the list of prequalified consultants and the consultant prepares the tariff study. That consultant must calculate the different components of the VAD using the methodology established by the CNEE in the Terms of Reference that were approved to that end.[220]

197. The distributor must present the consultant's study to the CNEE three months before[221] the new tariffs take effect, or eight months after the Terms of Reference are issued.[222]

(iv) Supervision of the distributor's tariff study by the CNEE

198. Under the LGE, the CNEE has the obligation to supervise the preparation of the distributor's study.[223] The LGE establishes that once the tariff study is received, the CNEE "shall review the studies performed" and may "make comments on the same."[224]

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217 *Ibid.*

218 RLGE, **Exhibit R-36**, art. 97.

219 Colom, **Appendix RWS-1**, paras. 57-60; Claimant's Memorial, para. 72.

220 RLGE, **Exhibit R-36**, art. 98.

221 RLGE-excerpts, **Exhibit R-12**, art. 98; RLGE, **Exhibit R-36**, art. 98. In the current version of the RLGE there are four months before the new tariffs take effect. See para. 230 below.

222 RLGE-excerpts, **Exhibit R-12**, art. 98; RLGE, **Exhibit R-36**, art. 98.

223 LGE, **Exhibit R-8**, art. 74.

224 *Ibid.*, **Exhibit R-8**, art. 75.

199. In order to supervise the studies, the CNEE may hire its own external consultants to help determine the legitimacy of the consultant's study.[225] In practice, the CNEE hires its consultant among those previously prequalified for the distributor's study.[226]

200. Hiring a prequalified consultant ensures that the CNEE will have the independent technical advice necessary to fulfill its supervisory obligations established in the LGE.[227] The technical advice to the CNEE also guarantees the distributor that the CNEE's comments have technical foundation.[228] The foregoing also allows the CNEE to adequately defend the final tariffs in case of a challenge by third parties.

201. The CNEE and its consultants must analyze whether the distributor's consultant's study complies with the Terms of Reference. This includes ensuring that the distributor has (i) presented the required documentation; (ii) justified its costs; (iii) applied the correct formulas; (iv) and correctly projected user demand. The CNEE thereby ensures that the study presented constitutes a reliable and reasonable foundation for determining the tariffs.[229] As explained by Mr. Colom, the CNEE was required:

> To review the distributor's study, its calculations, and all information requested and required by Article 98 RLGE, the justifications for each cost item, the relevant adjustment formulas, and the respective supporting report. This permits the CNEE to analyze and monitor the distributor's calculations and models and thus validate the foundation of the distributor's study. It is further essential so that the CNEE can follow the technical reasoning used by the distributor in its models

225 RLGE-excerpts, **Exhibit R-12**, arts. 32 and 98; RLGE, **Exhibit R-36**, arts. 32 and 98. In the reform to the RLGE that took place in 2007, the obligation of the CNEE to have a parallel study independent of the distributor was also established (until that, that was optional for the CNEE), which task the CNEE also assigns to its outside consultants. See section III.E.2 below.

226 Colom, **Appendix RWS-1**, para. 42.

227 *Ibid.*

228 *Ibid.*

229 Damonte, **Appendix RER-2**, para. 94.

> and verify that the calculations used are consistent with the ToR and can thus provide a sound basis for the new tariffs set by the CNEE.[230]

202. In order for the CNEE to perform its legal function, it is absolutely necessary that the consultant's study is capable of being audited, understood and analyzed by third parties who have not participated in its preparation, such as the CNEE and its advisors.[231] In other words, the calculations in the consultant's study must be capable of being replicated or corroborated.[232] For this, the electronic models must be interconnected (*linked*) so it is possible to emulate the results and perform sensitivity analyses, that is, to automatically update the study results when information is inputted into the model.[233] A study that does not take these technical considerations into account cannot be approved by the CNEE, as it exposes its directors to personal liability[234] and the tariffs to future challenges by third parties.

(v) Acceptance or rejection of the consultant's study

203. Once the tariff study is submitted, the RLGE gives the CNEE the right to "approve" or "reject" the tariff study if it believes it does not comply with the Terms of Reference:

> Three months prior to the initial effective date of the new tariffs, each Distributor shall deliver to the [CNEE] the tariff study which must include the resulting tariff

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230 Colom, **Appendix RWS-1**, para. 43.

231 Damonte, **Appendix RER-2**, para. 94; LGE, **Exhibit R-8**, art. 74 ; Colom, **Appendix RWS-1**, para. 43.

232 Damonte, **Appendix RER-2**, Chapter 4.1.1; Terms of Reference for Conducting the Valued Added for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 88-2002, October 23, 2002, **Exhibit R-25**, section A.6; Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, art. 1.6.4.

233 Damonte, **Appendix RER-2**, chapter 4.1.1; Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, arts. 1.6.4, 10.4 and 10.5; CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pg. 2.

234 LGE, **Exhibit R-8**, art. 5.

> schedules and the respective adjustment formulas, as well as the respective supporting report; the [CNEE] within a term of one month, shall approve or reject the studies performed by the consultants, submitting the comments it deems appropriate.[235]

(vi) The corrections to be made by the distributor

204. If the CNEE, with the aid of its consultants, determines that the consultant's tariff study departs from the Terms of Reference or contains errors, it makes comments to the study. The distributor shall implement the corrections and resubmit the study to the CNEE within a period of fifteen days. The second paragraph of RLGE Article 98 specifically establishes:

> The Distributor, through the consultant companies, shall analyze the observations, implement the corrections to the tariffs and their adjustment formulas and shall send the corrected study to the Commission within the term of fifteen days after receiving the comments […] Once the tariff studies are presented or the corrections are made, the definitive tariffs shall be published […].[236]

205. Contrary to what is claimed by TGH, Article 98 establishes an obligation, not a right, to incorporate the corrections to conform to the Terms of Reference. Therefore, TGH's position that the distributor's consultant may "reject" the CNEE's comments lacks legal foundation, as evidenced by the lack of support cited by TGH.[237]

e. The Expert Commission only pronounces itself on whether the distributor's study adequately follows the Terms of Reference

206. Once the distributor submits the corrected tariff study, LGE Article 75 establishes that, if the discrepancies between the CNEE and the distributor persist, the parties

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235 RLGE-excerpts, **Exhibit R-12**, art. 98 (Emphasis added); RLGE, **Exhibit R-36**, art. 98 (Emphasis added). In the current version of the RLGE there are four months before the new tariffs take effect. See para. 272 below.

236 *Ibid.* (Emphasis added); RLGE, **Exhibit R-36**, art. 98 (Emphasis added).

237 Claimant's Memorial, paras. 41-42 and 106.

will agree to call an Expert Commission. Article 75 is the only article in the LGE that describes the function of the Expert Commission, and it stipulates the following:

> In case of discrepancies submitted in writing, the [CNEE] and the distributors shall agree on the appointment of an Expert Commission made of three members, one appointed by each party and the third by mutual agreement. The Expert Commission shall pronounce itself on the discrepancies in a period of 60 days counted from its appointment.[238]

207. Two fundamental aspects of Article 75 must be analyzed. The first is the meaning of the term "discrepancies" and the second is what is meant by "the Expert Commission will "pronounce itself" [*se pronunciará*]. Given that RLGE Article 98 establishes an obligation to "incorporate" the corrections required by the CNEE, the discrepancies before the Expert Commission concern whether the distributor (i) implemented the corrections; and (ii) the corrections were properly implemented.

208. To claim that a discrepancy arises when the consultant rejects the CNEE's comments, as in when it refuses to apply the Terms of Reference, would allow the consultant to unilaterally amend those Terms. As previously explained, the distributor has the right to challenge the Terms of Reference administratively or judicially after their issuance, but once they are finalized, they can only be modified with the agreement of the CNEE.[239] Absent agreement of the CNEE, the approved version of the Terms of Reference must be applied, both by the consultant and by the Expert Commission.

209. Therefore, pronouncements by the Expert Commission regarding the content of the Terms of Reference, including the methodology to calculate the VAD; the approval or rejection of the distributor's study; and/or the approval of the tariffs, are excluded from its scope of competence.

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238 LGE, **Exhibit R-8**, art. 75 (Emphasis added).

239 See para 178 above; Colom, **Appendix RWS-1**, para. 40.

210. If the Expert Commission is of the opinion that the CNEE's comments have not been incorporated such that the study complies with the Terms of Reference, the CNEE has the right to reject the distributor's study in fixing the tariff schedule.[240] On the other hand, if the Expert Commission determines that the CNEE's comments are unjustified, its pronouncement would be one of the elements which the CNEE should take into account when establishing the new tariff schedule.[241] Finally, if the Expert Commission (a private and temporary entity) exceeds its authorities, its pronouncement or the parts thereof that exceed the entity's powers may not be adopted by the CNEE because they violate the LGE and the RLGE.

211. With respect to the meaning of "pronounce itself on the discrepancies," Guatemala would like to clarify that TGH's translation to English of "*se pronunciará*" as "*shall rule*" is not only incorrect but also biased. The correct translation of the reflexive form "*pronunciarse*" is "to pronounce oneself"[242] or "to declare oneself"[243] or "to give one's opinion on" (e.g. in favor of or against a proposal).[244] Based on its erroneous translation, TGH and its Professor Alegría manipulate the term "*se pronunciará*" used in Article 75 to argue that the Expert Commission's report would be binding. That is incorrect. The Expert Commission pronounces as an *ad hoc* panel of experts, on matters put forth for its consideration. The pronouncement of the experts is neither a "*ruling*" nor does it "*resolve*" the case as a decision by a judicial body would.[245] Inasmuch as it is a pronouncement of "experts," it serves to inform the decision of the body that is legally mandated to set tariffs, the CNEE. This is so because, as explained above,

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240 RLGE, **Exhibit R-36**, art. 98; Colom, **Appendix RWS-1**, paras. 47-48.

241 In Sections III.B.2.e and IV.B.1 we refer to the legal nature of the opinion of the Expert Commission. Colom, **Appendix RWS-1**, para. 48.

242 This is the most literal translation of the term.

243 See Merriam-Webster Dictionary, http://www.merriam-webster.com/spanish/pronunciar, **Exhibit R-157**.

244 Larousse Spanish-English, English Spanish Dictionary, **Exhibit R-5**, pg. 514.

245 The binding or nonbinding nature of the opinion of the Expert Commission is discussed in detail in Section III.B.2.e and IV.B.1 below.

the Expert Commission only hears the discrepancies at issue.[246] With that pronouncement, the CNEE considers the entirety of the tariff study and it proceeds to set the tariffs.

212. Even more importantly, it is not necessary to review the use of the expression "*se pronunciará*" to establish its meaning under Article 75, as TGH does. It is sufficient to analyze the context of Article 75 itself, in which it is clear that the LGE assigns an expert body (the Expert Commission) the task of issuing a report or pronouncement. The Constitutional Court, the supreme authority for the interpretation of laws in Guatemala, had the opportunity to analyze this issue and clearly decided the force of the pronouncement of the Expert Commission in Article 75 under Guatemalan law. In the words of the Court:

> Expertise, as being wisdom, practice, experience or ability in science and art, has traditionally served as an auxiliary resorted to by authorities when make a decision regarding a certain matter […] It follows, that the authority is not obligated to abide by the expert opinion; particularly when, in any reasonable case, it has the power to resolve the matter; thereby forming its own judgment based on the facts or information gained from exercising competence and other aspects that contribute to a determination of the facts.[247]
>
> […] To claim that the Expert Commission could have the function to decisively resolve conflicts and recognizing its competence in issuing a binding decision is contrary to the legality principle […] Following a strict compliance with the General Law of Electricity, the National Commission of Electric Energy has the authority to approve tariff schedules, never an expert commission whose nature has been considered.[248]

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246 Aguilar, **Appendix RER-3**, paras. 10, 46-58.

247 Constitutional Court, Consolidated Cases Nos. 1836-1846-2009, November 18, 2009, **Exhibit R-105**, pg. 28 (Emphasis added).

248 *Ibid*., pg. 31 (Emphasis added). Carlos Bastos himself, President of the Expert Commission named for EEGSA's tariff study in 2008 explained during the Hearing in *Iberdrola*:

213. In any case, the authority conferred on the Expert Commission to issue a pronouncement on discrepancies in no way authorizes the experts to replace the CNEE in determining the methodology, or in approving or rejecting costs, or the tariff study in general.

3. The public auction to sell shares in EEGSA

214. Once the regulatory framework applicable for the distribution sector was established, Guatemala was ready to launch the privatization process.

215. The reform of the electricity sector prepared for the sale of shares of three public companies providing distribution services, which together served roughly 62 percent of the population of the Republic of Guatemala. In addition to EEGSA, this included the two companies into which the INDE's distribution area was divided: Distribuidora de Electricidad de Oriente, S.A. (***Deorsa***) and Distribuidora de Electricidad de Occidente, S.A. (***Deocsa***).

216. With respect to EEGSA, on December 17, 1997, the Government authorized the sale of 80 percent of its shares through an international public offering.[249]

4. Setting the tariff schedule in 1998

217. Prior to selling EEGSA's shares, Guatemala heeded the advice of its financial advisors, Salomon Smith Barney, and eliminated the tariff subsidies and established tariffs for the first five-year tariff period (1998-2003).[250] Guatemala clarified to the future buyers the tariffs that would be in effect for the first tariff

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> MR. BASTOS: The truth is that the mistake comes from saying 'arbitration' instead of 'expert evaluation' In reality our work was not an arbitration; it was an expert evaluation.

Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 650:8-11.

249 Government Resolution No. 865-97, December 17, 1997, **Exhibit C-23**. Likewise, on December 22, 1998, the Government ordered the sale of 80 percent of the shares of Deorsa and Deocsa through the international public offering mechanism.

250 Salomon Smith Barney, "Preliminary Report by the Financial and Technical Consultant", January 28, 1998, **Exhibit C-25**, pg. 4.

period, minimizing uncertainties that could affect the sale price of the shares and investors' expectations.

218. Thus, in May 1997, Guatemala commissioned Synex, the Chilean consultants who provided advice on the reform of the sector, to prepare the 1998-2003 tariff study.[251] This project was performed under the auspices of the World Bank.[252]

219. The LGE established that the first tariff review could use reference values of a comparable country.[253] Therefore, the first tariff was calculated based on values of El Salvador, a country with economic and electricity characteristics similar to those of Guatemala and a regulatory system similar to the one established by the LGE.[254] As Synex explained:

> In accordance with the transitory provisions of the Law, the fist assessment of VAD may be based on reference values adjusted according to the economic and electric power reality of Guatemala. To this effect, it was considered appropriate to use as reference values the determined VAD used in El Salvador in the first half of 1996, as the economic and electric power similarity between the two countries is high. On the one hand, the GDP per capita of both countries, although not identical, is similar, reflecting the economic realities that are very similar. On the other hand, the electric power systems of El Salvador and Guatemala have similar characteristics, as both countries show a resemblance in geographical realities. Both factors, plus the fact that the realities of Ghana and Chile do not adequately reflect the reality of Guatemala, led the

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251 Synex, Determination of Electric Rates at Generation Levels – Transmission and Distribution in Guatemala", May 27, 1997, **Exhibit R-13**.

252 *Ibid.*

253 LGE, **Exhibit R-8**, art. 2; *see also* Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, pg. 63 (EEGSA recognizing that for "the first determination of tariffs, to take place in May 1998, the [CNEE] may use values for the VAD derived from other countries, which apply similar methodologies (as is the case in Chile, Peru, El Salvador, for example)." As therein established, the VAD was actually set July 17, 1998).

254 World Bank, "Synex Tariff Report: Determination of Electric Rates at Generation Levels – Transmission and Distribution in Guatemala", May 27, 1997, **Exhibit R-13**, section 3.1.

> consultant to consider the specific VAD in El Salvador as reference values.[255]

220. However, El Salvador was only taken as a reference. The Synex consultants were aware of the differences between the two countries, and therefore adjusted the El Salvador parameters to the reality of the Guatemalan electricity sector:[256]

> The distribution costs applicable in Guatemala were determined based on a study of efficient Distribution Added Values – VAD – undertaken in 1996 by SYNEX in El Salvador, to which coefficients were applied that represent the cost differences in equipment, materials and labor for the two countries. It must be recalled that the VAD found for El Salvador does not represent the true condition of companies in that country, but only the efficient costs of performing the distribution activity. Consequently, the VADs calculated for Guatemala do not transfer to the tariffs any inefficiencies that the electric companies have at that time.[257]

221. Therefore, TGH's argument that "the choice of El Salvador, however, was a poor one and resulted in distorted tariffs, because distribution companies in El Salvador generally are not comparable to those in Guatemala"[258] is baseless. In chapter three of its report, Synex included a detailed description of each of the parameters applied and the adjustments made to calculate a VAD adequate for Guatemala. In particular, TGH argues that the inability to use El Salvador as a reference arises "among other things, [from] the different densities of EEGSA's distribution

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255 *Ibid.*, section 3.1 (Emphasis added).

256 Chapter 3 of the Synex report provides a detailed explanation of each one of the elements taken into account to calculate the VAD applicable from 1998. World Bank, "Synex Tariff Report: Determination of Electric Rates at Generation Levels – Transmission and Distribution in Guatemala", May 27, 1997, **Exhibit R-13**.

257 World Bank, "Synex Tariff Report: Determination of Electric Rates at Generation Levels – Transmission and Distribution in Guatemala", May 27, 1997, **Exhibit R-13**, Presentation and Executive Summary, pg. 6.

258 Claimant's Memorial, para. 67; Statement of Witness Leonardo Giacchino, September 23, 2011 (hereinafter ***Giacchino***) **Appendix CWS-4**, para. 5 and note 3.

territory and [that of] El Salvador."[259] However, the consultants analyzed the density factor to ensure that the necessary adjustments were made in calculating the VAD.[260] Other parameters, such as investment and operating costs, were also adjusted to take into account local value.

222. The resulting final tariffs implied a significant increase in residential rates (169 percent) and a lesser increase for industrial customers (13 percent). Although the increases to residential consumers were significant, Synex recommended their application in order to comply with the LGE's mandate that tariffs reflect costs and not generate distortions.[261] To alleviate their impact, the consultants suggested that increases for certain categories of customers be scaled in over two years, but that the increases should be published immediately.[262]

223. Contrary to TGH's allegations,[263] Guatemala did not set low tariffs in order to avoid the political risk of the tariff increase. Rather, Guatemala accepted the recommendations made by Synex and World Bank study to apply the entire tariff increase prior to the sale of the EEGSA shares to Teco. TGH does not cite, nor can it cite, a single reference (other than its own witnesses[264]) that even suggests that Guatemala implemented lower tariffs than those technically applicable according to the World Bank study. TGH's arguments with respect to the 1998 tariff review must therefore be discarded.

224. Finally, it is noteworthy to mention that throughout this process of setting tariffs, the prevailing principle was that determination of tariffs be subject to strictly technical criteria. The former was true even though, by increasing the tariff

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259 Claimant's Memorial, para. 67; Damonte, **Appendix RER-2**, paras. 231-234,

260 World Bank, "Synex Tariff Report: Determination of Electric Rates at Generation Levels – Transmission and Distribution in Guatemala", May 27, 1997, **Exhibit R-13**, Section 3.1.1.

261 *Ibid.*, Presentation and Executive Summary, pgs. 7-8.

262 *Ibid.*, Presentation and Executive Summary, pg. 8.

263 Kaczmarek, **Appendix CER-2**, para. 11.

264 Claimant's Memorial, para. 67.

artificially, Guatemala could have obtained short-term benefits, such as a higher price for the privatization of EEGSA.[265] Far from that, the tariffs set by Synex were faithfully implemented, respecting the principle enshrined in the LGE that tariffs should strictly reflect the costs of the system.

5. Promotion of the investment and the expectations generated in Teco

225. As TGH describes in its Claimant's Memorial,[266] Guatemala began promoting the privatization of EEGSA in April 1998. Several documents were prepared during the promotion process, including an Informational Sales Memorandum and the Terms of Reference for the national and international public offering, which reflected, among other things, the provisions of the legal and regulatory framework described in Section I.B, above.[267] In particular, Guatemala stressed that the tariffs would not be calculated on the basis of the actual costs of the distributor but rather on the theoretical costs of a "highly efficient model company".[268]

226. Further, the Information Sales Memorandum, prepared by Salomon Smith Barney, clearly explained to investors that the CNEE was a functionally and financially independent technical arm of the MEM (which regulated and supervised the sector), which had the power to set the tariffs:

> The Law further created the National Electric Electricity Commission […] to regulate and oversee the electricity sector. Among other duties, the Commission

265 Moller, **Exhibit RWS-2**, para. 28.

266 Claimant's Memorial, pgs. 49-52.

267 EEGSA, "Selection Terms for the Financial Advisor", 1997, **Exhibit R-11**; EEGSA, "Internal Memorandum: Financial Advisor Qualification", December 5, 1997, **Exhibit R-14**; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**; Salomon Smith Barney, "Preliminary Report by the Financial and Technical Consultant", January 28, 1998, **Exhibit C-25**; EEGSA, "Terms of Reference for a national and international public tender for the sale of a strategic packaged within the social capitalization process and sale of state-owned shares in EEGSA", April 1998, **Exhibit R-15**; EEGSA Road show Presentation, May 1998, **Exhibit C-25**.

268 Claimant's Memorial, para. 53, third section.

> is responsible for […] (iv) setting the tariffs specified by law[269].

227. Likewise, Guatemala stressed the growth possibilities in the distribution area and the possible synergies with other activities.[270]

228. According to the procedure for the public offering of EEGSA's shares, the interested companies could ask questions and request clarifications on the applicable regulatory framework. Teco did not consider it necessary to ask any questions or make any remarks regarding the role of the regulator and/or its powers and authorities.[271] Nor did TGH ask any questions regarding the role of the Expert Commission, the nature of its pronouncement, or the procedure to be followed after the pronouncement was issued.[272]

a. Teco's decision to invest in EEGSA

229. At the time it decided to invest, Teco had access to the legal framework plus the promotional material described above. In summary, at the time when Teco, Electricidade de Portugal and Iberdrola (the ***Consortium***) analyzed the possibility of investing in EEGSA, the regulatory framework had the following essential characteristics:[273]

- The CNEE was an entity that acted independently from the Government;

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269 Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, pgs. 54-55.

270 Claimant's Memorial, para. 55.

271 Guatemala requested that TGH produce material generated in the context of EEGSA's due diligence. It appears that the Consortium did not pose any questions in that context. *See* document requests from Guatemala dated November 7 and 28, 2011 and answers from TGH dated November 18 and 28.

272 Despite all of this, now TGH now seeks to base its claim against Guatemala on the alleged binding nature of Expert Commission opinion (Claimant's Memorial, para. 270). As we will explain below, that is contrary to the text and spirit of the LGE, as has been confirmed by the highest court of Guatemala at the specific request of EEGSA (see Section IV.B.5 below).

273 TGH argues that "In addition to analyzing the new legal and regulatory framework established by Guatemala for its electricity sector, TECO performed extensive due diligence." Claimant's Memorial, para. 59.

- The CNEE would define the tariff calculation methodology;[274]

- The CNEE would review that methodology every five years;[275]

- The CNEE would prepare the Terms of Reference for the calculation of the VAD, which could be challenged by the distributors administratively and then judicially;[276]

- The CNEE would define the electricity distribution tariffs according to the terms of the LGE, which would reflect the costs of an efficient company;[277]

- The CNEE would hire professional consultants to assist it in the performance of its functions, especially for the definition of the tariffs;[278]

- The CNEE would prequalify consultants to prepare the VAD studies;[279]

- The CNEE would supervise and comment on the VAD tariff study prepared by the distributor;[280]

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274 LGE, **Exhibit R-8**, arts. 4(c) and 61; RLGE, **Exhibit R-36**, art. 97; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, arts. 4(c), 61 and 77 and Appendix B, art. 29.

275 LGE, **Exhibit R-8**, art. 77; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, art. 77 and Appendix B, art. 95.

276 LGE, **Exhibit R-8**, art. 74; RLGE-excerpts, **Exhibit R-12**, art. 98; RLGE, **Exhibit R-36**, art. 98; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, art. 74 and Appendix B, art. 98.

277 LGE, **Exhibit R-8**, arts. 71 and 61; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, art. 71 and Appendix B, art. 84.

278 *Ibid.*, art. 5; RLGE, **Exhibit R-36**, art. 32; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix B, art. 32.

279 RLGE, **Exhibit R-36**, art. 97; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, art. 74 and Appendix B, art. 97.

- The distributor would be obliged to incorporate the corrections so that its consultant's tariff study would conform to the Terms of Reference;[281]

- The Expert Commission would pronounce itself [*se pronunciará*] on the conformity of the distributor's study with the Terms of Reference, when the CNEE rejected the study or discrepancies persisted:

- The CNEE would approve or reject the VAD tariff study prepared by the distributor taking into account the pronouncement of the Expert Commission;[282]

- Once the study was approved by the CNEE, the CNEE itself would define the tariffs;

- The tariffs defined by the CNEE would be applicable for five years;[283] and

- The distributor would have to comply with all of the obligations under the LGE and the RLGE, including future amendments.[284]

230. Teco made its investment in EEGSA based on these expectations. It must be clarified, however, that Teco's main interest in EEGSA was the potential for synergies with its other electricity generation investments in Guatemala. As Teco explained in its July 1998 Board of Directors report, participating in the electricity distribution business in Guatemala through EEGSA was for Teco:

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280 LGE, **Exhibit R-8**, arts. 74 and 75; Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix A, arts. 74 and 75.

281 Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, Appendix B, art. 98.

282 LGE, **Exhibit R-8**, art. 77; RLGE-excerpts, **Exhibit R-12**, art. 98.

283 Salomon Smith Barney, "EEGSA: Sales Memorandum, 1998, **Exhibit R-16**, Appendix A, art. 78 and Appendix B, art. 98.

284 Authorization Agreements for the departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, May 15, 1998, **Exhibit R-17**, clause 20.

> […] of particular strategic importance […] because TPS [had] existing investments in power generation in this country.[285]

231. As Teco's witness Mr. Gillette, the former president of Teco Guatemala, explains:

> '[b]ecause our two power plants in Guatemala were supplying or were under construction and planned to supply all of their power to EEGSA, placing EEGSA in private hands provided increased security for those investments […]'[286].

232. Similar reasons were stated in the Board of Directors' July 1998 recommendation:

> **Conclusion and Recommendation**
>
> TPS recommends board approval for TPS participation in the EEGSA privatization bid. The purchase of this ownership interest in EEGSA would enhance our ability to vertically integrate our position in Guatemala and provide added protection to our existing projects there. It would also position TPS to have a stake in the distribution and generation of electricity as well as other end-use businesses, not only in Guatemala but in all of Central America as electrical integration in the region evolves. In addition, the Project itself provides very significant long-term earnings through the potential opportunities for both cost-cutting and growth, which can potentially enhance our returns. This one-time opportunity to acquire the EEGSA distribution

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285 Teco Energy, Inc. Action Regarding the Privatization of an Electric Utility in Guatemala, Board Book Write-up, July 1998, **Exhibit C-32**, pg. 7-2. EEGSA was not Teco's first investment in Guatemala. Earlier, Teco had invested in two power plant projects in Guatemala: the Alborada and San Jose power plants. See Claimant's Memorial, para. 56.

286 *Ibid*., **Exhibit C-32**; Statement of Witness Gordon Gillette, September 23, 2011 (hereinafter ***Gillette***), **Appendix CWS-5**, para. 9; EEGSA "EEGSA Privatization, Management Presentation", July 9, 1998, **Exhibit R-**161, pg. 27 of the PDF ("EEGSA Privatization Opportunity [provides] […] additional protection for existing investments"). As indicated in the Memorandum of Sale, until 1997, EEGSA's power demand was primarily supplied by private generators, of which, Teco was one of the most important ones. Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, pg. 30. EESGA had fixed-term contracts with these companies, including Teco's subsidiaries. Salomon Smith Barney, "EEGSA: Memorandum of Sale", May 1998, **Exhibit R-16**, pgs. 48-49. Teco Energy, Inc. Action Regarding the Privatization of an Electric Utility in Guatemala, Board Book Write-up, July 1998, **Exhibit C-32**, pg. 7-1 ("TPS currently has one power plant in operation in Guatemala […] and one under construction […] each of which has a long term power purchase agreement in place with EEGSA").

> company is a positive fit with the long-term strategies of TECO Energy.[287]

233. Therefore, Teco principally regarded its possible investment in EEGSA in terms of the possible synergies between EEGSA and its existing investments in power generation assets in Guatemala. Although EEGSA in and of itself was an additional justification for the investment, Teco hoped that EEGSA would yield benefits in the long-term.[288] Contrary to the allegations by Teco,[289] there was no expectation whatsoever of substantial tariff increases to achieve an increase in profit.[290] That increase in profit, according to Teco's Board of Directors itself, would be achieved over the long-term, and only if EEGSA managed to reduce its costs and grow. More importantly, because of a document submitted by TGH in response to a discovery request, Guatemala has shown that in the Claimant's pre-investment projections, it neither considered necessary, nor did it project, a significant increase in tariff reviews for the years 2003, 2008, and 2013; instead,

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287 Teco Energy, Inc. Action Regarding the Privatization of an Electric Utility in Guatemala, Board Book Write-up, July 1998, **Exhibit C-32**, pg. 7-8 (Bold emphasis in original, underlined emphasis added).

288 The hierarchy in its order of priorities even figures into this Arbitration:

> In addition to EEGSA's synergies with TECO's other investments in Guatemala, Mr. Gillette testifies that the investment opportunity was attractive 'in its own right as well'.

See Claimant's Memorial, para. 57 (Emphasis added). Mr. Gillette for his part states:

> The investment opportunity was attractive not only for its synergies with our other Guatemalan investment […]

Gillete, **Exhibit CWS-5**, para. 10 (Emphasis added).

289 Claimant's Memorial, para. 71.

290 Valuation Model of Dresdner Kleinwort Benson, **Exhibit R-160**, pg. 43, section c, Tariff calculation variable (A3-09.pdf or TGH-551).

the Claimant projected that the tariff would decrease in real terms, in line with what was anticipated under the RLGE..[291]

6. The process of selling the EEGSA shares

a. The Authorization Agreement

234. In parallel with the process of selecting the investor and preparing the transfer of the shares in EEGSA, the MEM and EEGSA signed a first authorization agreement on May 15, 1998, by which EEGSA was given the right to distribute electricity in the departments of Guatemala City, Sacatepéquez and Escuintla for a period of 50 years (***Authorization Agreement I***).[292] Then, on February 2, 1999, based on a second authorization agreement, EEGSA was authorized to provide services in the cities of Chimaltenango, Santa Rosa and Jalapa for the same period (***Authorization Agreement II***, and together with Authorization Agreement I, the ***Agreements***).[293] The Agreements included all legal and regulatory terms in effect at that date, which were described in Section I.B, above. Likewise, the Agreement stipulated the obligation of the successful bidder to comply with all of the terms of the LGE, the RLGE or such modifications as they might undergo. Therefore, at the time of investment, Teco's expectations explicitly included the possibility of modifications to the regulatory framework.[294]

b. The Consortium's offer

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291 This reduction likely is due to the implementation of the X Factor for efficiency, provided for the RLGE, art. 92.

292 Authorization Agreements for the departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, May 15, 1998, **Exhibit R-17**, clause 5.

293 Final Electricity Authorization Agreement for the Departments of Chimaltenango, Santa Rosa and Jalapa, February 2, 1999, **Exhibit R-20**, clause 5.

294 Authorization Agreements for the departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, May 15, 1998, **Exhibit R-17**, clause 20:

> **TWENTIETH. LAWS, JURISDICTION AND INTERPRETATION**. The AWARDEE agrees to comply with all the provisions set forth in the Law of General Electricity and its Regulations, or modifications they suffer and the other regulations and provisions that generally apply […].

(Bold emphasis in original, underlined emphasis added).

235. Based on the business as presented, the Consortium decided to make an offer to acquire 80 percent of EEGSA. The Consortium offered US $520 million.

236. TGH's expert, Mr. Kaczmarek, states that the price offered was much greater than the book value of the company. Kaczmarek believes that the market price was elevated due to the model company system adopted by Guatemala, which would allow income to be received above the value of its assets.[295] Mr. Kaczmarek, however, does not provide (and cannot provide) any proof contemporaneous to Teco's investment in EEGSA to sustain the claim that the offered price was established as a function of the model company system. Moreover, his analysis is false.

237. First, if the analysis of Mr. Kaczmarek were valid, this would mean the model company system would allow a state to "inflate" the sales price of a company, promising income unrelated to the service that the company was capable of providing. Thus, customers would not be paying for the service provided, but rather their tariff would be repaying (such as in a loan) the amount offered by the investor to the state. This is clearly not, nor could it be, the logic on which the model company system is based. As previously explained, the model company system is a system designed precisely to control possible tariff excesses resulting from the monopolistic position of the investor, in order to reduce costs and to encourage the efficiency of the actual company. As Mr. Damonte explains:

> [I]t is not true that the strategy chosen by Guatemala (Price Cap based on Model Company) results in a higher value of the distribution company and therefore in higher rates for consumers in Guatemala, but quite the opposite. The scheme chosen by Guatemala is considered as a modern and efficient system, chosen by most countries of South America and Central America, thanks to which they not only get lower rates on its first application, but also, by encouraging companies to be more efficient each

295 Kaczmarek, **Appendix CER-2**, para. 62.

> year, in order to obtain higher rates of profitability, they generate a reduction of costs which, at successive tariff settings, will lead to lower tariffs for the consumers.[296]

238. Second, as previously explained, Teco's decision to invest was not only based on the business potential of EEGSA, but also on its synergies with Teco's other investments in electricity generation and other businesses in Central America. Therefore, it is reasonable to assume that these considerations were included in the price offered.

239. Third, Teco valued, or should have valued, the business based on a tariff forecast grounded in the tariffs established in 1998. From there, Teco could only expect a reduction in the unitary VAD in real terms, as shown by its own pre-investment projections, given that the model company would become ever more efficient.[297]

240. Finally, and most important of all, the price paid by Teco has no relevance to this case, given that it is a risk assumed completely by the investor. To be clear: consumers cannot be penalized for an excessive price paid by the investor. If this were so, all investors would have an incentive to unjustifiably increase their offers and recover that amount, plus a return on it, through the tariff.

241. The offer by the Consortium was selected because it was the highest and the public tender process closed with the signing of a Stock Purchase and Sale Agreement under which Distribución Eléctrica Centroamericana S.A. (***DECA I***) (the vehicle company of the successful bidding consortium, of which TGH held 49 percent) acquired 80 percent of EEGSA's shares.[298] In parallel with the share

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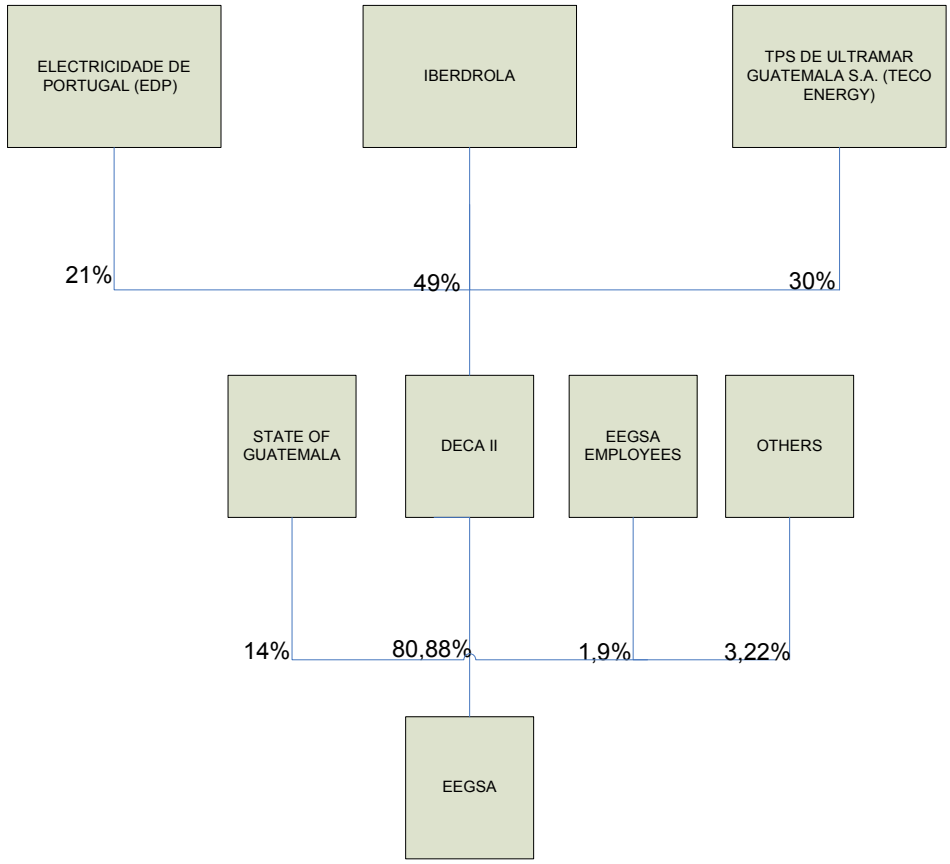
296 Damonte, **Appendix RER-2**, para. 31, paras. 39-43 and Chapter 7.1. As already explained by Damonte, depending on the type of optimization used, the difference between the actual and optimized network can fluctuate between 5 and 30 percent.

297 Valuation Model of Dresdner Kleinwort Benson, **Exhibit R-160**, pg. 43, section c, Tariff calculation variable (A3-09.pdf or TGH-551).

298 Stock Purchase and Sale Agreement between the State of Guatemala and DECA, S.A., September 11, 1998, **Exhibit C-38**. In parallel with the sale of EEGSA's shares, a public auction was also held for the sale of 80 percent of the shares of Deorsa and Deocsa. The sale process for Deorsa and Deocsa shares took place some months after EEGSA's, and it was not materially different from it. As a result of this process, 80 percent of the shares of both companies were acquired by

purchase, the shareholders of DECA I established a second entity named Distribución Eléctrica Centroamericana Dos, S.A. (***DECA II***), and then merged Deca I on April 13, 1999 with EEGSA and transferred its shareholdings in EEGSA to Deca II. As a result of the merger, DECA II became the holding company of the Consortium through which they controlled 80.8 percent of the shares of EEGSA. Of the remaining 19.2 percent of EEGSA's shares, 14 percent remained in the hands of the Guatemalan State, and 5.12 percent in the hands of private investors. The capital structure, therefore, was constituted as follows:



one Spanish investor, the electricity multinational Unión Fenosa Acción y Desarrollo Exterior, S.A. (***Unión Fenosa***). The remaining 20 percent of the shares of both companies was reserved for INDE, which subsequently sold part of those shares to minority shareholders.

C. THE FIRST FIVE YEARS OF EEGSA

1. The restructuring of EEGSA's operations

242. Shortly after starting operations under the Agreements, the Consortium decided to restructure EEGSA's business and transfer part of EEGSA's assets to recently-created related companies. Thus, on October 6, 1999, EEGSA and a subsidiary company, Crediegsa, S.A. (***Crediegsa***) established Transportista Eléctrica Centroamericana, S.A. (***Trelec***) to perform electricity transportation activities and manage activities for the transport of power and related electricity, originally performed by EEGSA. For this, EEGSA transferred the infrastructure related to its transportation network to Trelec.[299] From that restructuring, the assets transferred to Trelec are compensated independently through the corresponding toll on the transportation network.

243. Similarly, in the years after the acquisition of EEGSA, the Consortium decided to transfer many of the services that EEGSA initially provided to itself and to other companies, to subsidiary companies of the Consortium members, established to that end.[300] Guatemala notes that TGH decided not to inform the Tribunal of the

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299 Public Deed No. 41 authorized by the Notary Laura Vargas Florido, April 14, 2000, **Exhibit R-22**; Audited Financial Statements of 2009, December 31, 2009, **Exhibit R-106**, pg. 10, note 1, subsection (d).

300 On November 5, 1998, shortly after the Consortium's acquisition of EEGSA's shares, EEGSA and Crediegsa established Comercializadora Eléctrica de Guatemala, S.A. (***Comeegsa***), the company that would sell electricity and provide advisory services in the electricity sector. On August 31, 1999, EEGSA y Crediegsa established Enérgica, for the purpose of providing engineering, design, assembly, construction, implementation and maintenance services for electricity networks and conduits to, among others, EEGSA. Similarly, on June 15, 2006, EEGSA and Crediegsa established Inmobiliaria y Desarrolladora Empresarial de América, S.A. (***Ideamsa***), in order to handle real estate activities for the group. On September 23, 2004, DECA II, EEGSA and Crediegsa established Inversiones Eléctricas de Centroamerica, S.A. (***Invelca***), to which EEGSA contributed the shares that it held in Crediegsa, Trelec, Comegsa and Enérgica, establishing it as a holding company for the related companies. Subsequently, EEGSA transferred the shares derived from those contributions to its shareholders in the same proportions as their participations in EEGSA for the payment of future capitalizations. As a result of this final transfer of shares, 99.99 percent of the shares issued by Crediegsa were transferred to Invelca; 98 percent the shares issued by Comeegsa were transferred to Invelca, and the remaining 2 percent to Crediegsa; 85% of the shares issued by Enérgica were likewise transferred to Invelca, the 15% of remaining shares remained the property of Crediesa; 99.9% of the shares issued by Trelec were subsequently transferred to Invelca. Therefore, as a result of the creation of subsidiaries and companies described, EEGSA and Invelca now function as two related companies (both have the same

dismemberment of EEGSA's business. Nonetheless, an analysis of the return on the initial investment should clearly take into account the effect of that restructuring and the financial impact of such companies.

2. The economic performance of EEGSA in the first five years

244. In parallel with the restructuring of its business, EEGSA started operations according to the terms of the Agreements. As was indicated during the privatization process, the tariffs set in 1998 applied to the five-year period, with certain periodic adjustments for inflation.

245. In its Claimant's Memorial, TGH alleges that despite its growth, and despite having reduced costs and losses, EEGSA "did not prosper financially" during this first five-year period.[301] TGH argues that such lack of prosperity was due to the increase in the price of oil, the devaluation of the currency in 1999, and the "low" tariffs established in 1998.[302] However, as was already explained, the tariffs set in 1998 were based on a technical study performed by Synex under the auspices of the World Bank, and they were known by Teco before investing.[303] Additionally, the increases in the price of petroleum and the devaluation of the currency were compensated by the periodic adjustments within each tariff period, according to the mechanisms under the regulatory framework.[304]

246. According to TGH, in 1999 and 2000, EEGSA was still generating negative cash flows and in 2001 negative net profits.[305] According to Mr. Kaczmarek, the return

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owners). A significant part of the activities that EEGSA previously provided itself is now provided by the subsidiaries of Invelca, which means that EEGSA does not receive any profit from the gains that Invelca or its subsidiaries might obtain based on those businesses. We attach a graph with the corporate structure in **Appendix IV**. Note 6 of the Audited Financial Statements of EEGSA for 2009 describe the amount of the billing between companies. Audited Financial Statements of 2009, December 31, 2009, **Exhibit R-106**, pgs. 20-21.

301 Claimant's Memorial, paras. 68-69.

302 Claimant's Memorial, para. 69.

303 See Section III.B.4 above.

304 RLGE, **Exhibit R-36**, arts. 79, 86, 87, 88.

305 Claimant's Memorial, para. 69.

on investment realized during the first five-year period was between 4 and 6 percent, which would be below the 7 percent guaranteed by the LGE.[306] On that basis, Mr. Kaczmarek concludes that the tariffs set in 1998 were set at a very low level.[307] These arguments lack legal support, but above all, they lack economic support.

247. First, investments in infrastructure are long-term investments that require a significant initial investment to be recovered over the term of the agreement. That is even truer in the case of investments of privatized state companies to overcome chronic inefficiencies and insufficient investments. At the time of its decision to invest in EEGSA, the Board of Directors of Teco itself indicated that the expected return would be long-term.[308] To claim that a recently privatized public service company could generate profit in the first or second year of operation is completely unreasonable.

248. Second, Mr. Kaczmarek makes his return analysis based on the initial capital (price paid) and subsequent investments.[309] As previously explained, the LGE does not recognize the return on the actual investment nor the price paid, but rather on the capital base of the model company. Further, because it is a long-term investment, the return of 7 percent to 13 percent mentioned in the LGE must be analyzed over the concession period, and not merely a single five-year period. Furthermore, in his analysis, Mr. Kaczmarek completely ignores the restructuring of EEGSA's business, including the transfer of part of the transportation infrastructure and operations from EEGSA to Trelec.[310]

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306 Kaczmarek, **Appendix CER-2**, para. 96. We note that in Claimant's Memorial, TGH incorrectly reports its expert's conclusions, which refer to 3 and 4 percent instead of 4 and 6 percent. Claimant's Memorial, para. 69.

307 Giacchino, **Appendix CWS-4**, para. 5; Claimant's Memorial, para. 69.

308 Teco Energy, Inc. Action Regarding the Privatization of an Electric Utility in Guatemala, Board Book Write-up, July 1998, **Exhibit C-32**, pgs. 7-8, "Conclusion and Recommendation".

309 Kaczmarek, **Appendix CER-2,** paras. 95-96.

310 M Abdala and M Schoeters, **Appendix RER-1**, para. 87.

249. Finally, despite the alleged financial problems, TGH concedes that in the first five-year period it received over US$ 2 million in dividends for its 24 percent interest in the company.[311] Indeed, as indicated by Mr. Kaczmarek, in that period, EEGSA distributed dividends of some US$ 9 million.[312] Given the characteristics of the investment, these represent excellent results for the first years of a 50-year agreement. As properly stated in Teco's Board of Directors Minutes in January 2000 (contradicting the statement by Mr. Kaczmarek), "EEGSA's overall income was higher than plan[ned]."[313]

D. THE 2003-2008 TARIFF REVIEW

250. Under LGE Article 77, the tariffs for the second five-year period were to be set by mid-January 2003. For the second tariff review, the CNEE hired the Chilean consultant Sebastián Bernstein, one of the contributors to both the regulatory framework and the first tariff review, to prepare the methodology to use for the Terms of Reference for EEGSA, Deorsa, and Deocsa.[314]

251. Of particular importance, Bernstein in his report explained that, in order to adequately supervise that study, the CNEE would need to hire its own expert to perform a study in parallel with that of the distributor. As Mr. Bernstein stated:

> The VAD is calculated by the Distributors through a study requested from a consultant company pre-qualified by CNEE, which shall comply with the methodology established by the [CNEE] in the Terms of Reference of said studies (Art. 74 of the Law). However, [the] CNEE may raise comments on the obtained values and, if the discrepancies persist, an Expert Committee, composed of 3 members (Art 75. of the Law) will be established. <u>In order to exercise its</u>

311 Claimant's Memorial, para. 69.

312 Kaczmarek, **Appendix CER-2,** para. 94.

313 TECO Power Services Corp., Activities of Distribution Companies, Board of Directors Minutes Book, January 2000, **Exhibit C-47**, pg. 2-36.

314 JS Bernstein, "Some Methodological Aspects to Consider in the Terms of Reference for the Value-Added for Distribution Study," May 2002, **Exhibit R-23**.

> control functions, the CNEE shall be empowered to carry out a critical analysis of every step of the study commissioned by the Distributors, which implies, in practice, the commissioning of an independent study, which implements the same methodology.[315]

252. This same recommendation was also outlined by Leonardo Giacchino (EEGSA's consultant in the 2003 and 2008 tariff reviews, and witness in this Arbitration). Only a short time before, in 2000, he published an article explaining the need for regulators to hire external experts in order to eliminate problems that might arise in tariff reviews:

> The regulated tariff review caused most of the problems with the new regulatory frameworks to become apparent. Regulators and regulated utilities had difficulty agreeing on certain details, such as values of regulated assets, recalculation of original tariffs, the value of the efficiency factor in price cap regimes, and the improvement in quality of service.
>
> Each of these issues will continue to cause friction, especially in countries that have not yet had tariff reviews (eg, Mexico, El Salvador, Guatemala and Panama). To simplify the tariff review, each country should make its regulatory decisions more transparent. Some are already working toward this goal, developing measures such as regulatory accounting, service quality standards, and reports by outside experts[316].

253. With respect to the Terms of Reference, Mr. Bernstein mentioned the clear benefits of comparing the results of the distributor's study to that of the regulator:

> [T]o establish the terms of reference and calculation methodology precisely enough as to a) appropriately reflect the concepts of VAD contained in the Law and its Regulations, avoiding imprecisions that may be used to exaggerate the distribution costs, b) be able to compare the numeric intermediate and final results

315 *Ibid.*, pg. 2 (Emphasis added).

316 L Giacchino, et al., "Key regulatory concerns in Latin America energy, telecoms and water sectors in Latin America" (2000) Privatization International: Utility Regulation 2000 Series, Volume 2 Latin America, **Exhibit R-21,** pg. 1 (Emphasis added).

> reached in the studies of the Distributors and of the Regulator, and be able to establish the causes of those differences […][317].

254. All of Mr. Bernstein's recommendations derived from recent experiences with tariff reviews in countries such as Peru (2001), Uruguay (2001-2002) and El Salvador (2002), in which Mr. Bernstein had participated directly.[318] Among other recommendations, Mr. Bernstein advised the CNEE that the Terms of Reference require that costs be justified with comparables from at least two other countries:

> Finally, it is appropriate to establish in the [Terms of Reference] that the consultants shall compare the costs of the components that form part of the VNR [New Replacement Value] with values of at least two countries in the continent that apply similar regulatory concepts.[319]

255. Following the recommendations of Mr. Bernstein, the CNEE hired outside consultants. On this occasion, the support from the external consultant was limited to an analysis of the stage reports in the tariff study; despite the recommendations of Mr. Bernstein, the consultant did not analyze the distributor's tariff study in full nor did he conduct a parallel study.[320]

256. For its part, EEGSA hired Leonardo Giacchino's team from NERA Economic Consulting (***NERA***) to prepare its tariff study. EEGSA also had assistance from the Argentine consulting firm Sigla S.A. / Electrotek (***Sigla***), which prepared the Load Characterization study, an important component of the tariff study. EEGSA's decision to select Giacchino was not surprising given that he had previously worked with the Iberdrola Group (the operator of the Consortium) on tariff reviews of companies in which it was the controlling shareholder, including

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317 JS Bernstein "Some Methodological Aspects to Consider in the Terms of Reference for the Value-Added for Distribution Study," May 2002, **Exhibit R-23**, pg. 2 (Emphasis added).

318 *Ibid.*, **Exhibit R-23**, pg. 3.

319 *Ibid.*, **Exhibit R-23**, pg. 7 (Emphasis added).

320 Colom, **Appendix RWS-1**, para. 49.

Compañía de Electricidade do Estado da Bahia (***Coelba***) of Brazil and Electricidad de la Paz (***Electropaz***) of Bolivia.[321]

257. As Mr. Bernstein had warned, without an expert to conduct an independent study during the 2003-2008 period, the CNEE was significantly limited in its supervision of NERA's stage reports. Although the CNEE could make certain comments on the study, it did not have a "benchmark" or reference against which it could compare the results of the study. Likewise, the CNEE was unable to fully review the voluminous information to justify the reference prices included in the VNR.[322]

258. This tariff review resulted in an increase in EEGSA's VAD, which for low voltage increased from US$6.63/kW-month to US$7.48/kW-month (an increase of 12.83 percent) and in medium voltage increased from US$5.10/kw-month to US$8.71/kW-month (an increase of 70.78 percent). Notably, this review used the SER *top-down approach* system, applying actual data from the company to construct the model company, which was adjusted for efficiency.[323]

259. As explained by Mr. Damonte, this tariff review resulted in very disproportionate values for EEGSA as compared to the average throughout Latin America.[324]

E. MODIFICATION OF THE RLGE

260. In its Claimant's Memorial, TGH claims that, in 2007, Guatemala modified RLGE Article 98 unconstitutionally and in violation of the text and objective of the LGE, to allow the CNEE to use its own tariff study to calculate the VAD.[325]

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321 Giacchino, **Appendix CWS-4**, Annex A, pgs. 7, 9, 16; Ernst & Young, "Iberdrola, Auditing Report", February 23, 2010, **Exhibit R-109** pgs. 85-86; Iberdrola, "Corporativa: Group's Websites", last visit July 1, 2010, **Exhibit R-121**, (listing Electropaz, Coelba, and EEGSA among its six corporate entities in Latin America).

322 Colom, **Appendix RWS-1**, para. 49.

323 Kaczmarek, **Appendix CER-2**, para. 98.

324 Damonte, **Appendix RER-2**, párr. 251.

325 Claimant's Memorial, para. 84.

That is incorrect. Contrary to TGH's claim, the reform process was not politically conceived to interfere with the 2007 tariff review. The reform of the RLGE commenced in 2003 and affected various aspects of the regulations. Each of the modifications was justified and in full accordance with the LGE.

1. The need to reform the RLGE was foreseeable and accepted by EEGSA

261. First, reforms to electricity regulations are not unusual occurrences in Latin America. Similar to Guatemala, the majority of countries in the region have implemented new electricity regimes within the last twenty years. As authorities gain regulatory experience, subsequent reforms to harmonize regulatory texts and fill legal gaps are normal.[326]

262. In this regard, the Agreements themselves anticipated that such modifications to regulatory framework would take place and that EEGSA would be obliged to adhere to them:

> [EEGSA] agrees to comply with all the provisions set forth in the Law of General Electricity and its Regulations, or <u>modifications they suffer and the other regulations and provisions that generally apply</u> […][327]

263. EEGSA therefore invested not only accepting that such legislative and regulatory modifications were permissible, but also that they would have to abide by them.

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326 Chile, for example, in 2004 made a substantial modification to its General Electricity Act and its Regulation. Peru is another example of a country in the region which, since passing its electricity law in 1992, has implemented successive reforms to it and created related norms, such as the Law Creating the Supervisory Body for Investment in Energy – OSINERG – (1996); the Antitrust Act and Anti-Oligopoly Act in the Electricity Sector (1997); Law that establishes the obligation to submit, among other things, an Environmental Impact Study in the cases of thermoelectric generation activities whose power exceeds 10 MW (1997); Law that amends different articles of the Electricity Concessions Act (1999), Law Promoting Hydroelectric Plant Concessions (2001).

327 Final Electricity Distribution Authorization Agreement for the Departments of Guatemala, Sacatepéquez and Escuintla, May 15, 1998, **Exhibit R-17**, clause 20 (Emphasis added); Final Electricity Distribution Authorization Agreement for the Departments of Chimaltenango, Santa Rosa and Jalapa, February 2, 1999, **Exhibit R-20**, clause 20 (Emphasis added).

2. Genesis: the reform to RLGE Article 99

264. With several years of the RLGE in place and the experience of the 2003 tariff review behind it, the MEM believed that certain issues could be improved and clarified. Thus on December 5, 2003, Government Resolution No. 787-2003 was approved, making some modifications to Articles 98 and 99 of the RLGE.[328]

265. The first objective of the modification was to resolve some problems related to the tariff review timeframe; these periods were established under the premise that the review processes for all distributors would occur simultaneously (Articles 98 and 99, first paragraph), which did not conform with reality.

266. The second objective of the modification was to resolve instances in which the distributor did not have a tariff schedule after its prior tariff schedule had expired.[329] Until this point, such a situation was indirectly governed by RLGE Article 98, under which a distributor without approved tariffs would continue to apply the previous tariffs (with adjustment formulas) until new tariffs were published.

267. Nonetheless, this violated the principle of the model company as established by the LGE, which required that new, efficient tariffs be determined every five years. Under the original drafting of RLGE Article 98, if the previous tariff study was more favorable than a new tariff study, the distributor could decide not to cooperate in the tariff review process and thereby extend, *sine die*, the application of the current tariffs to the detriment of consumers. As has already been explained, under the model company regulatory system, the tariffs were expected to reduce over time as demand increased and the model company improved in efficiency. Indeed, this was the case under the Chilean model, which is a similar

328 Government Resolution No. 787-2003, December 5, 2003, published in Diario de Centro América on January 16, 2004, **Exhibit R-30**.

329 Expert Alegria's argument that there are no known cases in which no consultant's study was presented is incorrect. The municipal companies often decide not to present tariff studies, additionally, the CNEE has to determine the tariffs based on its own studies. Claimant's Memorial, para. 89; Statement of Witness Rodolfo Alegria, September 22, 2011 (hereinafter ***Alegria***), **Appendix CER-1**, para. 38.

model to the Guatemalan model.[330] Thus, continued application of old tariffs could harm consumers.

268. Faced with this scenario, the last paragraph of Article 99 was amended to allow the CNEE to issue and implement a tariff schedule immediately. The 2003 reform added the final paragraph of Article 99. The chart below shows the changes from one version to the other:

ART. 99 – ORIGINAL VERSION 1997[331]	ART. 99 – 2003 REFORM[332]
Article 99. Application of the Tariffs. Once the tariff study referred to in the previous articles has been approved, the Commission shall set the definitive tariff studies within a term not greater than one month from the date on which the definitive study was approved […] If the Commission has not published the new tariffs, the same may be adjusted by the distributors based on the effective adjustment formulas, save for what is set forth in the last paragraph of the previous article. The tariffs shall apply from the 1 of May immediately following the date of approval by the Commission.	**Article 99. Application of the Tariffs.** Once the tariff study referred to in the previous articles has been approved, the Commission shall proceed to set the definitive tariffs as of the date on which the definitive study was approved […] If the Commission does not publish the new tariffs, the tariffs of the previous tariff schedule shall continue to apply, including their adjustment formulas […] At no time shall electricity distribution to end-users be carried out without a valid tariff schedule being in force. If a Distributor ends up without a tariff schedule, the National Electric Energy [CNEE] shall immediately issue and make effective a tariff schedule with a view to complying with the aforementioned principle.

269. Thus Article 99 anticipated the consequences of the two possible scenarios. First, where the new tariff schedule was unpublished because of the CNEE's error (second paragraph of the new Article 99), for which the original solution

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330 The National Energy Commission of Chile explained the reason for this decreasing trend in tariffs in the following terms:

> The main reason that explains this variation lies in the greater efficiency acquired by the distributing companies as demand increases, produced by the economies of scale and density, efficiency that is transferred to the tariffs.

Press releases from the National Energy Commission of Chile, November 15, 2000 and November 27, 2008, **Exhibit R-152**.

331 RLGE-excerpts, **Exhibit R-12**, art. 99.

332 RLGE, **Exhibit R-36**, art. 99.

remained and the distributor could continue to apply tariffs from the prior tariff period. Second, where the new tariff schedule was not published because of the distributor's error (third paragraph of the new Article 99), in which case it was up to the CNEE to implement a new tariff schedule.

270. One fundamental point must be stressed: neither EEGSA nor its shareholders objected, formally or informally, to the modification of RLGE Article 99 in 2003.

3. The 2007 modification to the RLGE

271. In March 2007, the then-presiding Board of Directors of the CNEE amended several articles of the RLGE. Contrary to TGH's claim, this was not a "politicized" reform to interfere with the EEGSA's next tariff review. The draft of that reform dated back to 2005, under the direction of the National Program on Competitiveness (Pronacom), a public entity whose mission, among others, was to foster policies to improve productive investment in Guatemala. At that time, a process for legislative reform of the electricity sector was instituted so as to increase its competitiveness by generating renewable sources of energy and utilizing more efficient fuels.[333] The reforms also sought to fill in legal gaps and harmonize terms in the regulatory framework. Such changes to the regulatory framework included (i) an amendment to the provision establishing that end users provide certain guarantees to pay bills owed to distributors; and (ii) an adjustment of the service connection period.[334] Several amendments related to the periodic tariff studies were incorporated into Article 98.

272. First, it was necessary to extend the time allocated for tariff reviews, as the original timeframe had proved to be too short to allow for an efficient yet rigorous process, including adequate supervision by the CNEE. Thus, the entire process was extended: the Terms of Reference were distributed to the distributors twelve

333 Government Resolution 68-2007, March 2, 2007, published in Diario de Centroamérica on March 5, 2007, **Exhibit R-35**, Preamble.

334 Government Resolution 68-2007, March 2, 2007, published in Diario de Centroamérica on March 5, 2007, **Exhibit R-35**, arts. 1, 15 and 19.

months prior to the approval of the tariff schedule (as opposed to eleven months under the original RLGE) and all other timeframes were extended by one month.[335]

273. Secondly, the second paragraph of Article 98 was amended to add that the distributor was to submit "the justification for each cost line item to be included" in the tariffs.[336] Nonetheless, the obligation to justify all costs included in the tariff study already existed in the LGE and the prior RLGE, as the CNEE was only to approve efficient costs (LGE Article 60) on the basis of the costs presented by the distributor (RLGE Articles 82 and 83). However, because EEGSA had resisted the requirement to justify all costs in its prior tariff review,[337] the CNEE decided to explicitly establish such requirement in its modification of the RLGE, to avoid future disputes regarding this basic issue, and permit the CNEE to adequately supervise the review. This clarification was also in line with international regulatory trends.

274. Further, the wording of that same paragraph was corrected, replacing the text "shall approve or reject the studies performed by the consultants"[338] with "shall decide on the acceptance or rejection of the studies performed by the consultants."[339] With this change, the CNEE continued to have, as established

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335 RLGE, **Exhibit R-36**, art. 98.

336 RLGE, **Exhibit R-36**, art. 98.

337 Letter from Roberto Urdiales (CNEE) to Miguel Francisco Calleja (EEGSA) and Leonardo Giacchino (NERA-SEMELEC), June 16, 2003, **Exhibit C-66** ("Some costs were not yet provided by EEGSA, and therefore, in certain cases, they have been established by extrapolation and in others, when it has not been possible, they were provisionally left with value zero[…]"). Letter from Roberto Urdiales (CNEE) to Miguel Francisco Calleja (EEGSA) and Leonardo Giacchino (NERA-SEMELEC), July 4, 2003, **Exhibit R-27** ("The consulting company has found that the consulting expenses incurred by the Distributor have been efficient without specifying verifiable references as to the efficiency criteria used. The consulting company highlights in the section of consulting services costs the consulting expenses incurred by SAP […] The total costs for the Facilities of EEGSA have been paid up, without any support of the adequacy of the facilities (size and features) for the performance of the relevant activities, pursuant to the base criteria of achieving the highest efficiency level […]").

338 RLGE-Extracts, **Exhibit R-12**, art. 98.

339 RLGE, **Exhibit R-36**, art. 98.

under the original RLGE, the authority to reject a study that did not comply with the Terms of Reference.

275. Third, the wording of the third paragraph establishing that the distributor "shall […] implement the corrections to the tariffs and their adjustment formulas"[340] in accordance with the CNEE's comments was changed to "implement the corrections to the studies."[341] The prior wording was not appropriate, as the subject of analysis was the distributor's tariff study, not the tariffs themselves. Nonetheless, the original obligation to incorporate the CNEE's comments remained unchanged.

276. Fourth, the fourth paragraph was modified to provide that, in case of differences regarding in the appointment of the third expert to the Expert Commission, the CNEE and the distributor would resolve these between them.[342] No other modification was made with respect to the authority or role of the Expert Commission.

277. Fifth, the fifth paragraph was modified to make Article 98 consistent with Article 99, which had been modified in the last reform of 2003.[343] As was previously explained, Article 99 established that the CNEE should immediately "issue and make effective" a tariff schedule if the distributor did not have one. However, after the 2003 reform, Article 98 was inconsistent with the Article 99 reform, as it still established that the prior tariff schedule would continue to apply if the distributor did not submit its study or the necessary corrections.

278. As previously explained, the continued application of the prior tariff schedule could create perverse incentives for distributors. Therefore, in order to ensure that Articles 98 and 99 are fully consistent, Article 98 was changed to "oblige" the

340 RLGE-Extracts, **Exhibit R-12**, art. 98.

341 RLGE, **Exhibit R-36**, art. 98.

342 *Ibid.*

343 *Ibid.*, art. 98. Government Resolution No. 787-2003, December 5, 2003, published in Diario de Centro América on January 16, 2004, **Exhibit R-30**, art. 99.

CNEE to "emit and publish" the tariff schedule if the distributor did not submit its study, or did not correct it in accordance with the CNEE's comments, as established under Article 99.[344]

279. In this sense, TGH and its legal expert have acknowledged that, prior to the reform of Article 98, the RLGE implicated an "undesirable result," as it created perverse incentives for distributors.[345] Despite this, they argue that such a problem was not insurmountable given the CNEE's authority to impose fines to generate a "significant financial incentive" to ensure that the distributor cooperated.[346] This argument fails to address the negative impact that a deviation from the Terms of Reference or the timeframes has on the regulatory system (inefficient tariffs, harm to the consumer). This affects the very same principles underlying the system established in the LGE, which can in no way be remedied with the imposition of a fine. Furthermore, given the magnitude of capital involved in a tariff review, the proposed fines will not generate a sufficient disincentive to alter the distributor's conduct.

280. The new Article 98 was also amended to require the CNEE to hire its own prequalified expert to conduct an independent tariff study.[347] The CNEE previously had the right to hire an outside consultant to prepare its independent study. However, it was deemed more appropriate to impose this as an obligation of the CNEE so as to not leave it to the discretion of the CNEE's Directors. This reflected the recommendation provided by Sebastián Bernstein in 2002, when he stated it necessary for the CNEE to hire an outside consultant to perform an independent backup study. This independent study would enable the CNEE to diligently supervise and minimize the asymmetry of information. Furthermore, as was previously explained, having adequate technical support would reduce the

344 RLGE, **Exhibit R-36**, arts. 98 and 99.

345 Claimant's Memorial, para. 89; Alegria, **Appendix CER-1**, paras. 38-40.

346 Claimant's Memorial, para. 89; Alegría, **Appendix CER-1**, para. 38.

347 RLGE, **Exhibit R-36**, art. 98.

risk of a successful challenge to the newly fixed tariffs,[348] and protect the rights of users and distribution companies to be able to review the new tariffs on a technical and objective basis.

281. This modification was also based on the CNEE's experience during the 2003-2008 EEGSA tariff review, during which the CNEE was unable to adequately validate and compare results submitted by the distributor. At that time, due to a lack of internal resources and outside advisory services, many elements of the EEGSA tariff study—which would have been rightfully challenged by the CNEE—were never objected to. Some of these elements were as obvious as the payment of the operator's fee in the amount of US$4.889 million,[349] even when the bidding documents and the Operating Contract clearly indicated that such a fee would be incorporated in the tariffs only during the first five-year period.[350] Thus the new wording of Article 98 guaranteed that the CNEE would have an opportunity to conduct its own independent study separate from the one prepared by the distributor. This would provide the CNEE with an independent technical reference as a basis upon which it could accurately correct the distributor's study on its own, if possible. If this were not possible, the CNEE could use the independent study to determine the proper tariffs.

282. The different versions of Article 98 are demonstrated in the chart below:

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348 See para. 200 above.

349 National Economic Research Associates, "Operation and Management Costs and Commercialization Costs," Report Prepared for EEGSA, May 7, 2003, revised July 20, 2003, submitted July 30, 2003, **Exhibit R-29**, pgs. 90-92.

350 EEGSA, "Terms of Reference for a national and international public tender for the sale of a strategic package within the social capitalization process and sale of state-owned shares in EEGSA, April 1998, **Exhibit R-15**, art. 3.1.9; Operating Agreement between EEGSA and Iberdrola Energía S.A. for the provision of technical assistance and transfer of Management "know how," and operation of activities related to electricity distribution, transmission and sales, August 21, 1998, **Exhibit R-18**, clauses 2 and 4.

ARTICLE 98 PRIOR TO THE 2007 REFORM[351]	ARTICLE 98 FOLLOWING THE 2007 REFORM[352]	ARTICLE 99 IN FORCE IN 2007[353]
Article 98. Periodicity of the Tariff Studies. Every five years, eleven months before the initial effective date of the tariffs, the Commission shall deliver to the Distributors the terms of reference for the studies that shall be commissioned from the specialized consulting companies prequalified by the Commission. Three months prior to the initial effective date of the new tariffs, each Distributor shall deliver to the Commission the tariff study which must include the resulting tariff schedules and the respective adjustment formulas, as well as the respective supporting report; the Commission, within a term of one month, shall approve or reject the studies performed by the consultants, submitting the comments it deems pertinent. The Distributor, through the consultant companies, shall analyze the observations, implement the corrections to the tariffs and their adjustment formulas and shall send the corrected study to the Commission […] The cost of this contracting shall be covered by the Commission and the Distributor in equal parts. Until the distributor delivers the tariff studies, or until it performs the corrections to same, according to what is stipulated in the previous paragraphs, it may not modify its tariffs and it shall continue applying the effective tariffs at	Article 98. Periodicity of the Tariff Studies. Every five years, twelve months before the initial effective date of the tariffs, the Commission shall deliver to the Distributors the terms of reference for the studies that shall be the basis for the hiring of the specialized consulting companies prequalified by the Commission. Four months prior to the initial effective date of the new tariffs, the Distributor shall deliver to the Commission the tariff study which must include the resulting tariff schedules, the justification for each cost line item to be included and the respective adjustment formulas, as well as the respective supporting report; the Commission, within a term of two months, shall decide on the acceptance or rejection of the studies performed by the consultants, making the comments it deems pertinent. The Distributor, through the consultant company, shall analyze the observations, implement the corrections to the studies and send them to the Commission […] The cost of contracting the third member of the Expert Commission shall be borne by the Commission and the Distributor in equal parts. In case of the Distributor's failure to send the studies or	Article 99. Application of the Tariffs. Once the tariff study referred to in the previous articles has been approved, the Commission shall proceed to set the definitive tariffs as of the date on which the definitive study was approved […] If the Commission does not publish the new tariffs, the tariffs of the previous tariff schedule shall continue to apply, including their adjustment formulas […] At no time shall electricity distribution to end-users be carried out without a valid tariff schedule being in force. If a Distributor ends up without a tariff schedule, the National Electric Energy Commission shall immediately issue and make effective a tariff schedule with a view to complying with the aforementioned principle.

351 RLGE-Extracts, **Exhibit R-12**, art. 98. Government Resolution No. 787-2003, December 5, 2003, published in Diario de Centro América on January 16, 2004, **Exhibit R-30**, art. 98

352 RLGE, **Exhibit R-36**, art. 98.

353 RLGE, **Exhibit R-36**, art. 98.

the time of the termination of the effective term of such tariffs.	the corrections to same, the Commission shall be empowered to issue and publish the corresponding tariff schedule, based on an independent tariff study conducted by the Commission or on the basis of corrections to the studies begun by the distributor.	

283. As was the case with the 2003 reform, at no point did EEGSA or its shareholders (or other distributors) ever object, formally or informally, to the RLGE modifications. Nor did they raise any objections to the constitutionality of amended Article 98. In fact, DECA II did not even consider challenging the reform until 2010, after the present dispute had already started. It was at this point that DECA II decided it would use its "political influence" in order to seek to obtain a "favorable" decision from the judiciary, as reflected in DECA II's Management Presentation:

> We have concluded that the challenge is feasible. We are already working on arguments, and we suggest the participation of 3 politically powerful attorneys in order to obtain a favorable decision.[354]

284. Its reference to political influence to obtain a favorable outcome leaves no doubt: TGH's argument and its form of conduct are not based on the law. This demonstrates that TGH's claims are not only groundless, but also opportunistic.

285. Finally, we must analyze the claim by TGH's witness, Mr. Calleja, stating that EEGSA "seriously" considered challenging the Article 98 reform, but did not do so out of fear of reprisals by the CNEE during its tariff review.[355] This claim is completely unfounded. Mr. Calleja does not provide any internal

354 Management Presentation by DECA II 2009, January 14, 2010, **Exhibit R-107**, (slide "Constitutional Court – Vad") (Emphasis added).

355 Statement of witness Miguel Francisco Calleja, September 22, 2011 (hereinafter ***Calleja***), **Appendix CWS-3**, para. 13. See also Statement of Witness Luis Maté, September 21, 2011 (hereinafter ***Maté***), **Appendix CWS-6**, para. 6.

contemporaneous documentation containing any discussion or decision not to challenge a measure, which, according to TGH's recent arguments, significantly altered the legal framework applicable to its investment. Further, despite having referred to the RLGE reforms in his witness statement in the Iberdrola arbitration, Mr. Calleja did not mention at that time that EEGSA had considered challenging these reforms in any respect.[356] Given the potential liability involved, one would expect that, at the very least, TGH's directors would discuss a waiver of such a right. Likewise, this argument is inconsistent with the challenge, and even the request for injunctive relief, that EEGSA presented shortly after the release of the first version of the Terms of Reference for the 2008 tariff review. If, in fact, EEGSA feared reprisals by the CNEE, it certainly would not have attempted (as it did) to halt the tariff review under way in 2008.

F. THE TARIFF REVIEW OF THE 2008-2013 PERIOD

1. The prequalification by the CNEE of consultant firms for the performance of tariff studies

286. EEGSA's existing tariff schedule expired at the end of July 2008, while Deorsa's and Deocsa's expired at the end of January 2009. According to LGE Article 74, the CNEE was required to prequalify experts who were able to assist both the distributors and the CNEE in the preparation of the tariff review studies.[357]

287. On April 11, 2007,[358] the CNEE contacted engineering firms interested in joining the list of consultant firms qualified to perform the tariff studies. Of the nine firms

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356 Mr. Calleja does not only not mention such an intention, but he states that, at that time, they believed that such a reform would not apply to EEGSA, which is incompatible with their position today that there existed an intention to challenge the reform. *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statements of Miguel Francisco Calleja, October 14, 2009 and September 25, 2010, **Exhibit R-150**, paras. 10-12. In his second declaration presented in that arbitration, Mr. Calleja also fails to refer to such intention. *Ibid.* , **Exhibit R-150**.

357 Colom, **Appendix RWS-1**, paras 39 and 57-60.

358 Terms of Reference for Consultant Firms in Conducting Studies to Calculate the Value Added for Distribution – VAD – in Guatemala's Electricity Distribution Companies, Government Resolution 51-2007, April 11, 2007, **Exhibit R-37**.

that submitted a bid, six were prequalified in light of their experience in the electricity sector and of particular importance, their experience in tariff reviews based on the model company system.[359] These firms included PA Consulting Services S.A. (Argentina), Quantum S.A. (Argentina) (***Quantum***),[360] Mercados Energéticos S.A. Argentina (***Mercados Energéticos***), Synex Ingenieros Consultores Ltda. (Chile) (***Synex***), Bates White LLC (United States) (***Bates White***), and the consortium of Sigla S.A./Electrotek (Argentina) (***Sigla***).[361]

288. Both the distributors and the CNEE were free to hire any of these prequalified firms in preparation of their VAD tariff studies for the 2008-2013 tariff review.

2. Definition of the methodology: the Original Terms of Reference

289. As the CNEE prequalified these consulting firms it also worked on preparing the Terms of Reference for EEGSA's tariff review. According to the RLGE as amended in 2007, the Terms of Reference were to be published at least twelve months prior to the date on which the company's new tariff schedule would enter into force (August 1, 2008).[362] In preparing the Terms of Reference, members of the CNEE visited regulatory bodies in Chile, Peru, and Argentina, in order to discuss their experience with this type of review. Following those visits, the CNEE decided to hire Edwin Quintanilla Acosta and Miguel Révolo.[363] These consultants were, respectively, the General Manager and Manager of Regulation

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359 Colom, **Appendix RWS-1**, paras 59-60.

360 Deorsa and Deocsa chose Quantum to perform their VAD study.

361 Approving the firms prequalified to perform the VAD studies, CNEE Resolution 55-2007, June 21, 2007, **Exhibit C-117**.

362 Colom, **Appendix RWS-1**, para. 37. For distributors Deocsa and Dorsa, the tariff reviews commenced in January 2008 and their tariff schedules had to be approved in January 2009.

363 Edwin Quintanilla Acosta has a Ph.D in Management Science (Excellent Cum Laude) having graduated from ESADE-Spain, and serving as professor in the Master's in Economics and Public Service Regulation program at the University of Barcelona, Spain. Mr. Quintanilla and Mr. Révolo have more than 10 years of experience in analyzing and approving tariff studies in Peru, where there exist around 20 electricity distributors, among them, EDELNOR, controlled by ENDESA (ENDESA is the largest electricity company in Spain and the largest private electricity company in Ibero-America). See Curriculums Vitae of Edwin Quintanilla Acosta and Miguel Juan Révolo Acevedo, **Exhibit R-155**.

and Electricity Distribution of the agency tasked with regulating and supervising the electricity, hydrocarbon, natural gas, and mining operations in Peru.[364] Both Mr. Acosta and Mr. Révolo had recently participated in the tariff review processes in their own country. In addition, the CNEE also hired Alfredo Campos as an independent consultant; Mr. Campos is an Argentine electromechanical engineer with experience in the Latin American electricity sector. Together, these three consultants were to provide the CNEE with technical advice on preparing the methodology corresponding to the VAD calculation,[365] which would be published in the Terms of Reference. The consultants were to review the Terms of Reference to ensure their compliance with standards established under the LGE and RLGE, as well as analyze regulatory practices of other countries.[366]

290. Based on their assessment, the CNEE established the Terms of Reference and communicated them through official letter CNEE-13680-2007, dated April 30, 2007 (the ***Original Terms of Reference***), 14 months prior to the date on which the new tariff schedule would take effect.[367]

3. The CNEE strengthened the technical capabilities of the Tariff Division

291. Once the Terms of Reference were published, the mandate of the then-existing CNEE Board came to an end. A new Board of Directors was named in May 2007, in accordance with the mechanism for selection provided in the LGE and the RLGE.

292. The three Directors subsequently selected were well-known and possessed a high degree of technical experience within the electricity sector. Specifically, this new

364 Supervisory Agency for the Investment of Energy (OSINERGMIN).

365 Colom, **Appendix RWS-1**, para 61.

366 See Curriculum Vitae of Alfredo Daniel Campos, **Exhibit R-155**.

367 Terms of Reference for Conducting Studies to Calculate the Value Added for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 13680-2007, April 30, 2007, **Exhibit R-38**.

Board of Directors was comprised of engineers Enrique Moller, Carlos Colom Bickford, and Cesar Augusto Fernández.

293. Enrique Moller was nominated by agents of the Wholesale Market, including distributors.[368] Mr. Moller has more than thirty years of experience in Guatemala's electricity sector, having been, among other things, the General Director of Energy at MEM, a member of the INDE Board of Directors, as well as a member of the EEGSA Board of Directors during the time that the company was under state control. Mr. Moller was appointed president of CNEE's first Board of Directors in 1997. It is important to note that Mr. Moller had in-depth knowledge of the legal regime and its scope, as he participated in the creation of that same legal framework.

294. Carlos Colom Bickford was nominated by the MEM and appointed as president of the CNEE. Mr. Colom is a mechanical engineer with much experience in the electricity sector, having been educated both in Guatemala and in the United States.[369] Before being named director of the CNEE, Colom acted as General Manger of INDE,[370] a public company that, following certain sector reforms, was charged with supplying electricity throughout Guatemala.[371]

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368 IBERDROLA, which indirectly acts among the Wholesale Market agents through EEGSA, Trelec, Comesgsa, which participate as distributor, transporter, and seller, respectively. Moller, **Appendix RWS-2**, para. 31.

369 Colom studied mechanical engineering at Universidad del Valle de Guatemala. He then completed a Master's degree in Project Management with an average GPA of 3.9 out of 4.0 at the McCormick School of Engineering in Chicago – United States. Colom, **Appendix RWS-1**, para 4.

370 Colom, **Appendix RWS-1**, para. 10.

371 TGH has pointed to the relationship between Mr. Colom with the outgoing President of Guatemala, Álvaro Colom. The reference they omit (1) that Mr. Colom was named President of the CNEE in May 2007, several months before Alvaro Colom was elected President of Guatemala; and (ii) that the designation of Mr. Colom before the CNEE was carried out by President Oscar Berger, principle political rival of President Álvaro Colom and the person who would defeat him in the presidential elections of 2003. See Colom, **Appendix RWS-1**, para. 22.

295. César Fernández was nominated by the universities.[372] As part of his academic background, Mr. Fernandez has served as Dean of the Engineering School of the Universidad de San Carlos in Guatemala, of which he was also the first Director of the Center for Superior Studies of Energy and Mines. He has also acted as Dean of the Universidad del Valle de Guatemala, as well as professor at the Universidad de San Carlos in Guatemala, Universidad de Rafael Landivar, Universidad del Valle de Guatemala, and the Universidad del Istmo de Guatemala. Furthermore, Mr. Fernandez also served as Minister of Energy and Mines from 1992 to 1993, President of Guatemala's Association of Engineers, and Member of the National Board of Science and Technology.

296. Immediately after taking office, the new Board of Directors set out to overhaul the CNEE's Tariff Division structure, to supply the personnel and infrastructure necessary to perform high-quality technical work. In the opinion of the new Board, the resources previously allotted to this Division were insufficient to meet the obligations imposed upon the CNEE by the LGE. As explained by Mr. Colom:

> [A]t the start of our tenure, the Division had six professional employees and one assistant, who were tasked with work related to the five-year tariff review of all the country's electricity distribution companies, with the quarterly, bi-annual and annual adjustments, and with other duties such as the analysis of distributors' electricity purchase and sales data for subsequent adjustments and the assessment of transmission network usage charges. On our arrival, we were informed that the Division conducted the distributor's tariff reviews as a "task force," matched to the pending task. However, given its limited staff and resources, the Division could not specialize and had difficulties in fulfilling the obligations the Electricity

372 When appointed Director in 2007, Fernández remained in his current position because in 2004, he was appointed Director from a list proposed by the universities to replace the prior Board of Directors (which had been removed by the Constitutional Court) to complete its term of office through 2007. Moller, **Appendix RWS-2**, para. 31.

> Law imposed on the CNEE for the tariff review process.[373]

297. To that end, the CNEE decided to expand the Tariff Division's personnel base and create two Departments and one Unit, with use of their own staff. First, they created the Department of Tariff Adjustments comprised of six (seven today) professionals, all of whom are in charge of reviewing and performing analyses for the quarterly, semiannual, and annual adjustments to the electricity distribution tariffs, as well as conducting studies to calculate compensation for the transportation network in Guatemala. Second, the Department of Tariff Studies was charged with analyzing the stage reports that each distributor submits when it performs its five-year tariff study, as well as coordinating, reviewing, and following up on the tasks performed by outside consultants who assist with the process. This department is comprised of five professionals and three technicians, all of whom analyze the distribution network, perform field audits, and conduct supervisory activities. At the same time, they coordinate the execution of the parallel tariff study. Third, the Uniform System of Accounts Unit was comprised of two professionals in charge of analyzing financial and technical information submitted by the distributors.[374]

298. At this point, the CNEE had a minimum of 16 professionals working full-time on tariff matters (compared to the six professionals performing a variety of tasks under the previous management).[375] This new internal structure ensured that the CNEE would have all of the resources needed to correctly perform its functions, thereby minimizing the risks of having an asymmetry of information or inadequate resources.

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373 Colom, **Appendix RWS-1**, para 25.

374 *Ibid.*, para. 26.

375 *Ibid.*, paras. 25-26.

4. The determination of the Final Terms of Reference

299. Once the Tariff Division was upgraded, the new CNEE Board of Directors analyzed the Terms of Reference for EEGSA's tariff review, as communicated to EEGSA through official letter CNEE-13680-2007. EEGSA, in the exercise of its right to object to the Terms of Reference, initiated an administrative challenge. Thereafter, it brought a challenge before the courts via *amparo*, at which point the tariff review process had to be suspended.[376]

(i) EEGSA used its *amparo* against the Terms of Reference as a tool to pressure the CNEE into granting concessions – all the while objecting to the very same provisions that EEGSA had previously accepted in a prior tariff review

300. In its Claimant's Memorial, TGH alleges that it was forced to object to the Terms of Reference because they radically departed from those used in the prior tariff review, alleging that the CNEE subsequently granted itself "wide latitude"[377] such as the right to refuse acceptance of the distributor's study.[378]

301. That is not correct. EEGSA (and TGH) accepted, without objection, these same provisions in the Terms of Reference of the prior 2002 tariff review. In fact, the Terms of Reference of the 2002 tariff review grant the CNEE an equal or greater degree of control over EEGSA's tariff study, even using the same language for such Terms. The following comparison is conclusive:

376 *Ibid.*, para. 62.

377 Claimant's Memorial, paras. 96-100.

378 *Ibid.*, paras. 97-99.

TGH's Criticism of the Original Terms of Reference	Original Terms of Reference, April 2007, objected to by EEGSA[379]	2002 Terms of Reference, no objection[380]
"Article 1.7.4 [violates] LGE Article 75 and RGLE Article 98" (Claimant's Memorial paras. 97, 98)	1.7.4. If any Stage Report fails to meet the aforementioned premises, [the] CNEE has the legal power to require additional information and to suspend the receipt of any subsequent development of the Study if, at its exclusive explicitly stated judgment, duly reasoned and supported, it is being performed in disregard, ignorance or noncompliance with the [Terms of Reference]. 1.7.4. If the CNEE detects deviations from the theoretical, methodological, or procedural guidelines determined in the Terms of Reference, it shall object to the continuation of the Study. 1.7.4. In that case, the Distributor must redo the pertinent tasks to amend the objection as instructed and in the term established by the CNEE.	A.6.2. [Upon receiving the reports], the CNEE shall have the legal authority to require any additional information and suspend any further development of the STUDY if, in its own explicit, sufficiently grounded, reasoned and detailed opinion, said STUDY were being conducted in disregard of, departure from, or breach of these [Terms of Reference]. A.6.3. Where the CNEE has detected a departure from the theoretical, methodological, or procedural guidelines set forth in these ToR, the CNEE shall object to the continuation of the STUDY. […] A.6.4. In the event that the intermediate results should be objected to by the CNEE, the CONSULTANT shall redo any such works as appropriate in order to remedy said objection, as directed and within the term established by the CNEE.

379 Terms of Reference for Conducting Studies to Calculate the Value Added for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 13680-2007, April 30, 2007, **Exhibit R-38**, arts. 1.7.4. and 1.9 (Emphasis added).

380 Terms of Reference for Conducting the Valued Added for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 88-2002, October 23, 2002, **Exhibit R-25**, section A.6 (Emphasis added).

As explained by Professor Alegría, Article 1.9, like Article 1.7.4, accordingly was unlawful because the CNEE had no right under the law to intervene in or to influence, much less to ignore, the consultant's study just because it disagreed with it. (Claimant's Memorial, para. 99)	1.9. the Study shall be filed together with the entire set of Stage Reports. Should any such Report be missing, the CNEE shall so notify the Distributor and, for the purposes of Section 98 of the Rules, the Study shall be deemed not to have been delivered until such time as the missing information is presented. Accordingly, submission of the Stage Reports shall not trigger the time limits referred to in Section 98 of the Rules.	A.6.7. These [Terms of Reference] prescribe that the Tariff Study that the DISTRIBUTOR must submit to the CNEE for consideration shall consist of the full set of Reports and Results herein established. Should any of these elements be missing, the [CNEE's Technical Committee] shall inform the DISTRIBUTOR of this situation and, for as long as the missing information has not been received, the CNEE shall consider that, for the purposes of Section 98 of the RULES, the Tariff Study has not been yet submitted to the CNEE for consideration. Consequently, partial delivery of Reports or Results may be considered for informational purposes, but shall not affect the running of the terms set forth in Section 98 of the RULES.
	1.9. The CNEE may also consider the Study as not received if, in its own judgment, the results requested in the [Terms of Reference] were not included, such that the Study may be deemed to be incomplete, or to provide a partial or distorted portrayal.	A.6.8. The CNEE may also consider the Tariff Study as not received if, in its own opinion and the opinion of the [CNEE's Technical Committee], the aforementioned Reports and Spreadsheets should have omitted the results required under these [Terms of Reference], so that it may be held that the Tariff Study is incomplete or presents a partial or biased opinion.

302. As can be seen in the chart above, in the 2002 tariff review, the CNEE already had the power to reject the tariff study if it failed to conform to the Terms of Reference. The CNEE also had a right in the 2002 tariff review to suspend the process if the study departed from the Terms of Reference. Furthermore, in its *amparo*, EEGSA set forth strong accusations regarding the CNEE's alleged "abuse of power" in defining the useful life of facilities as 30 years (Section 6.5). However, this is exactly the same period adopted in the 2002 Terms of Reference (Section D.4.2), to which EEGSA never objected.[381] In short, it is evident that the

381 Writ of Amparo by EEGSA against the Terms of Reference, Amparo C2- 2007-4329, May 29, 2007, **Exhibit C-112**, pg. 21; Terms of Reference for Conducting the Study to Calculate the Value Added for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 13680-2007, April 30, 2007, **Exhibit R-38**, section 6.5; Terms of Reference for Conducting the Valued Added

provisions of the Original Terms of Reference in no way granted the CNEE any additional powers to those previously accepted by EEGSA and TGH in the 2002 tariff review.[382]

303. But there is more. EEGSA's *amparo* ignored basic principles of the LGE, making it clear that in reality, EEGSA was challenging the fundamental bases of the regulatory framework under which Teco invested in 1998. These challenges come, in part, from the consultant firm Bates White, which as part of its service offer prepared a report for EEGSA comparing the Terms of Reference with what Bates White considered to be "best practices for tariff reviews."[383]

304. For example, EEGSA indicated that the consultant should prepare the tariff study "using the technical and methodological criteria it deems adequate and reasonable to perform the work asked of it."[384] This ignored the CNEE's legal right to establish the methodology and to declare the study "admissible or inadmissible" (as stated in the original language of the RLGE as "accept or reject") if not in accordance with the Terms of Reference.[385] As previously explained in Section I.F.2, according to the LGE, the consultant must prepare its tariff study by following the methodological guidelines established in the Terms of Reference, applying information provided by its distributor. EEGSA's interpretation, however, gave the distributor and its consultant the power to "determine" the Terms of Reference themselves, thereby distorting the balance of power granted by the LGE to the CNEE, the distributor, and the distributor's consultant.

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for Distribution for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 88-2002, October 23, 2002, **Exhibit R-25**, section D.4.2.

382 Claimant's Memorial, paras. 97-99.

383 Email from Guillermo Israilevich to Fernando Oroxom, attaching the Evaluation of the Terms of Reference Methodology, June 29, 2007, **Exhibit R-39**.

384 Writ of Amparo by EEGSA against the Terms of Reference, Amparo C2- 2007-4329, May 29, 2007**, Exhibit C-112**, pg. 8 (Emphasis added).

385 RLGE, **Exhibit R-36**, art. 98; LGE **Exhibit R-8**, arts. 4(c), 77, 78 (the CNEE is the only entity that reviews the methodology used to determine tariffs).

305. Thus, the main arguments presented in EEGSA's *amparo* were neither technical nor methodological in nature. These were legal challenges submitted to gain judicial authorization for EEGSA to depart, at its own discretion, from the Terms of Reference after the tariff review process was under way (as it eventually did in 2008). Nonetheless, as a result of the *amparo*, the Guatemalan courts ordered a preliminary stay on the application of the Terms of Reference pending a resolution on the merits, which it had yet to examine.[386]

b. Without waiving any of its rights, the CNEE agreed to make certain modifications to the Terms of Reference so as to prevent a delay in the review process under way

306. As explained by Mr. Colom, the new Board of Directors of the CNEE evaluated the situation and decided to revise the Terms of Reference in order to proceed with the tariff review. Otherwise, the court's stay on the Original Terms of Reference would have effectively suspended the entire tariff review until the court issued its final decision on the merits. This process could take several months and would prevent the CNEE from determining the new tariff schedule until then.[387]

307. In order to carefully revise the Terms of Reference duly prepared by the previous Directors, the CNEE hired engineers Alejandro Arnau and Jean Riubrugent, of the prequalified consultant firm Mercados Energéticos, to provide specialized external advice to the Tariff Division. Based on an analysis that weighed the advantages and disadvantages of modifying the Terms of Reference, the CNEE decided to incorporate certain modifications requested by EEGSA that did not affect the principles underlying the LGE.

308. First, the CNEE established that, in determining whether submissions complied with the RLGE timeframes, the submission of the entire tariff study, rather than the stage reports, was determinative.

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386 Writ of Amparo by EEGSA against the Terms of Reference, Amparo C2- 2007-4329, May 29, 2007**, Exhibit C-112**.

387 Colom, **Appendix RWS-1**, para. 66.

309. Second, the public hearing phase was eliminated because, although the CNEE believed it to be solid, transparent regulatory practice, it was never stipulated in the LGE or the RLGE. Ultimately, the CNEE felt it was preferable to concede to EEGSA's objection in order to prevent the tariff review from being delayed any further.[388]

310. Third, the capital recovery formula was modified, per the suggestion of Mr. Leonardo Giacchino (at that time a consultant with NERA), from a constant capital method to a constant depreciation method.[389] For purposes of this tariff review, the assets of the distributors (EEGSA, Deorsa and Deocsa) were considered to be 50 percent depreciated.[390]

311. Fourth, an addendum was added to Article 1.5 of the Terms of Reference, establishing the obligation of the consultant firm to maintain professional judgment independent from the distributor that hired it.[391]

312. Fifth, the CNEE eliminated a reference in Article 1.9 that provided that the study would be considered "not received" if the consultant omitted the "requested results." However, the provision requiring consultants to implement the CNEE's corrections was confirmed. Thus, the text of the article was worded as follows:

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388 Letter from Miguel Francisco Calleja to José Toledo Ordoñez, May 11, 2007, **Exhibit C-108**, pg. 5.

389 G Berchesi and L Giacchino, National Economic Research Associates, "Phase E Report: Value-Added for Distribution and Balance of Power and Energy", June 27, 2003, revised on July 30, 2003, **Exhibit C-75**, pg. 7:

> A second alternative is using the useful lives to calculate replacement in a linear form. This formula is commonly applied in a great majority of countries (US, UK, Australia, etc.) in cases in which the asset base increases with time..

390 CNEE Resolution 5-2008, January 17, 2008, January 17, 2008, **Exhibit R-54**, art. 8.3.

391 The addendum to Article 1.5 of the Terms of Reference reads as follows:

> […]The Consultant Firm must have independence of judgment in preparing the Study. […].

Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**.

> The Distributor shall analyze said observations, make any corrections it deems appropriate and send the corrected final report of the study to the CNEE within fifteen (15) days of receiving the observations."[392]

313. TGH argues that the text "it deems appropriate" means that the consultant did not have an obligation to incorporate the corrections. This is incorrect. It is clear that within the context of the review, this phrase means that, following comments to the study (for example: that it is not auditable and does not contain the reference price), the consultant would carry out the necessary steps to address such a comment. In other words, the consultant is free to decide on the "appropriate" manner in which the measures should be implemented, but the consultant cannot decide unilaterally whether or not it will implement such measures. That is the only interpretation compatible with RLGE Article 98, which establishes that the consultant "make the corrections to the studies,"[393] with LGE Article 75 and with the CNEE's function to monitor the studies, including the authority to order corrections. Even if the language of Article 1.8 gives rise to any doubt, the Terms of Reference establishes that in case of a conflict between the Terms of Reference and the RLGE, the latter prevails.[394]

314. Finally, Article 1.10 was incorporated as an exception pursuant to which EEGSA could depart from the Terms of Reference provided that there was a justified

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392 Addendum to the Terms of Reference for the Performance of the Value-Added for Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, October 11, 2007, **Exhibit R-44**, art. 1.8.

393 Colom, **Appendix RWS-1**, 44; RLGE, **Exhibit R-36**, art. 98 ("The Distributor, through the consultant company, shall analyze the observations, implement the corrections to the studies and send them to the Commission within the term of fifteen days after receiving the observations.").

394 Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, art. 1.10.

> These terms of reference do not constitute a legal or regulatory amendment, therefore in the event of a conflict between any of the provisions of these terms of reference and the Law or the Regulation the latter's provisions shall prevail, applying the principle of legal hierarchy in all cases. Likewise, any omission in these terms of reference, related to aspects defined in the Law and the Regulation on the subject of tariffs shall be construed as included in the [Terms of Reference].

reason for doing so, which needed to be explained by the CNEE's consultant. The justification would allow the CNEE to analyze the matter and decide whether the departure was reasonable and therefore acceptable or not, for the purposes of modifying the Terms of Reference.

315. The wording of Article 1.10 caused some disagreement between EEGSA and the CNEE. As explained by Mr. Colom, EEGSA sought to provide consultants with the discretion to decide whether or not to follow the Terms of Reference,[395] whereas the CNEE was neither willing nor legally capable of renouncing its specifically-conferred legal powers. The contrast between EEGSA's proposal and the text ultimately approved by the CNEE conclusively establishes the scope of Article 1.10:

Article 1.10 of the Terms of Reference

Proposed by EEGSA[396]	Approved Text[397]
These [Terms of Reference] set forth general guidelines to be followed by the distributor and the consultant in each of the Stages and/or studies that have been described and defined. Consequently, the consultant may change, in a justified manner, the methodologies presented in each of the studies to be performed, based on its knowledge and experience.	These ToR set forth the guidelines to follow in preparation of the Study, and for each one of its Stages and/or described and defined studies. If there are changes in the methodologies set forth in the Study Reports, those must be fully justified, and CNEE shall make such observations regarding the changes as it deems necessary, **confirming that they are consistent with the guidelines for the Study.**

395 Colom, **Appendix RWS-1**, paras. 69-71 and 107-109. Letter from Miguel Francisco Calleja to José Toledo Ordoñez, May 11, 2007, **Exhibit C-108**, pg. 5.

396 Letter from Miguel Francisco Calleja to José Toledo Ordoñez, May 11, 2007, **Exhibit C-108**, pg. 5.

397 Addendum to the Terms of Reference for the Performance of the Distribution Value-Added Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, October 11, 2007, **Exhibit R-44**, art. 1.10.

316. As explained by Mr. Colom, the final text of Article 1.10 reflected the following:

(a) *First*, the CNEE rejected the text whereby EEGSA proposed that such guidelines were meant to be "general." The clear intention of Article 1.10, as seen in the approved text, is that the Terms of Reference serve as guidelines "to follow" as a mandatory requirement for consultant firms (unless the CNEE authorizes a departure from the terms);

(b) *Second*, the CNEE eliminated EEGSA's proposal to give the consultant firm the right to change the methodology on its own without prior consultation. The provision "consultant may vary" was replaced with the more limited "if there are changes," which clearly denotes the exceptional nature of such changes;

(c) *Third*, in the event that the consultant firm were to propose a variation of the Terms of Reference, such proposal must be "fully justified," as opposed to being simply "justified," thereby establishing a higher standard; and

(d) *Fourth*, most importantly, the CNEE was to verify <u>through its comments</u> that any methodological variations were consistent with the guidelines contained in the Terms of Reference.[398] This confirmed the CNEE's exclusive power to define the methodology.

317. In order to avoid any subsequent doubt or conflict, Article 1.10 was accompanied by a statement that: (i) confirmed the CNEE's right to verify the consistency of any changes made to the Terms of Reference; and (ii) included a principle of hierarchy under which the terms of law would take precedent in the event of any conflict. Thus, Article 1.10 of the final Terms of Reference therefore established the following:

398 Colom, **Appendix RWS-1**, para. 71.

> These [Terms of Reference] show the guidelines to follow in performing the Study and for each one of its described and defined Stages and/or studies. Should there be any variations in the methodologies presented in the Study' Reports, they must be fully justified, the CNEE will make the observations it deems necessary concerning the variations, verifying their coherence with the Study's guidelines.
>
> These terms of reference do not constitute a legal or regulatory amendment, therefore in the event of a conflict between any of the provisions of these terms of reference and the [LGE] or the Regulation the latter's provisions shall prevail, applying the principle of legal hierarchy in all cases. Likewise, any omission in these terms of reference, related to aspects defined in the [LGE] and the Regulation on the subject of tariffs shall be construed as included in the [Terms of Reference].[399]

318. Once EEGSA withdrew its *amparo* in August 2007, the Terms of Reference became final.

5. The hiring of technical consultants prequalified by the CNEE and EEGSA

319. In order to prepare their respective tariff studies, both EEGSA and the CNEE selected their consultants from the list of prequalified consultant firms. EEGSA requested proposals from Bates White, PA Consulting Services, S.A., Quantum, Mercados Energéticos, Synex and Sigla (who previously worked for EEGSA in preparation of the tariff study corresponding to its 2003-2008 tariff review).[400] From these proposals, EEGSA selected Bates White,[401] whose partner, Leonardo Giacchino, had previously prepared EEGSA's tariff study during the 2003-2008 tariff review while working for NERA. As previously indicated, Mr. Giacchino

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399 Terms of Reference for the Performance of the Distribution Value-Added Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, art. 1.10 (Emphasis added).

400 See para 256 above.

401 Contract between EEGSA and Bates White LLC for performance of the 2008-2013 Tariff Study, January 23, 2008, **Exhibit R-55**.

had recently advised Iberdrola, EEGSA's Consortium operator, in tariff reviews for its subsidiaries in Bolivia and Brazil.[402]

320. For its part, the CNEE issued an international public tender for bids seeking an independent consultant who would assist in the EEGSA, Deorsa, and Deocsa tariff reviews.[403] The tasks of the CNEE's independent consultant would consist of: (i) providing support to the CNEE in evaluating the tariff studies submitted by the distributors; and (ii) preparing independent tariff studies for the CNEE as established in RLGE Article 98.

321. Given that Bates White, Quantum, and PA Consulting Services were currently contracted to conduct studies for the distributors, the CNEE analyzed offers proposed by Sigla (which was previously invited by EEGSA to bid) and by the Mercados Energéticos-Synex consulting consortium.[404]

322. After analyzing their financial proposals and professional experience, the CNEE Board of Directors chose Sigla to perform the task at hand.[405] Sigla's engineer, Eduardo Redolfi, with 39 years of experience in Latin America's electricity sector, would conduct the tariff studies.[406] The consultant Sigla had performed or provided advisory services for over 30 studies to calculate VAD components throughout the region between 1998 and 2007, the majority of which were conducted under the model company approach.[407] Moreover, Sigla had assisted EEGSA during its 2003-2008 tariff review. With respect to this engagement,

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402 Among others, Giacchino had advised Iberdrola's electricity companies, Coelba del Brasil and Electropaz de Bolivia, in 2002 and 2004; Giacchino, **Appendix CWS-4**, Annex A, pgs. 7, 9, 16; Ernst & Young, "Iberdrola, Auditing Report", February 23, 2010, **Exhibit R-109** pgs. 85-86; berdrola, "Corporate: Group's Websites, last visited July 1, 2010, **Exhibit R-121**, (listing Electropaz, Coelba, and EEGSA among its six corporate entities in Latin America).

403 CNEE Resolution 116-2007, July 27, 2007, **Exhibit R-40**.

404 Colom, **Appendix RWS-1**, para. 80.

405 CNEE Resolution 150-2007, October 26, 2007, **Exhibit R-46**.

406 Sigla S.A. – Electrotek S.A, Technical Offer to Participate in the Supervision of Load Characterization Studies (EEC) and the Components of the Distribution Value-Added (EVAD), October 15, 2007, **Exhibit R-45**, pgs. 246 and 257-258.

407 *Ibid.*, pgs. 81-85.

EEGSA stated that it was "satisfied with the work performed" by Sigla, as expressed in a 2005 letter to Sigla from Miguel Calleja, EEGSA's then Planning, Control and Regulations Manager (TGH's witness in this Arbitration).[408]

323. Similarly, the CNEE received advisory services from Alejandro Arnau and, to a lesser degree, Jean Riubrugent, of Mercados Energéticos, both of whom had provided advice regarding the Terms of Reference. These consultants assisted the CNEE by analyzing various sections of the Bates White tariff study, as well as Sigla's study. The CNEE thereby ensured that it had the technical resources necessary to avoid repeating its experience during the 2003-2008 tariff review, in which the lack of outside technical advice limited its ability to review the distributor's study. As explained by Mr. Colom:

> It was important for us to have an outside team in addition to Sigla in order to ensure the quality of our supervision over the independent studies conducted by Sigla and Bates White.[409]

324. As previously explained, the hiring of an external consultant at the start of the tariff review was provided for in the LGE, and was necessary for the CNEE to adequately supervise EEGSA's study. Such a hiring was not, as TGH and its legal expert argue, "unlawful," as it remained unknown whether the EEGSA report would comply with legal requirements.[410] Had the CNEE waited until the end of the tariff review to conduct its own study, it is clear that (i) the CNEE would not be able to supervise EEGSA's study; and (ii) the CNEE would not have sufficient time to complete a parallel study in the event that EEGSA's study was deemed unacceptable.

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408 *Ibid.*, pgs. 46-47, (attaching letter from Miguel Francisco Calleja, Manager of Planning and Control, to Luis Sbertoli, President of Sigla, October 13, 2005).

409 Colom, **Appendix RWS-1**, para. 83.

410 Claimant's Memorial, para. 111; Alegría, **Appendix CER-1**, para 69.

6. The study Bates White prepared for EEGSA

325. In its Memorial, TGH repeatedly alleges that the CNEE did not cooperate with EEGSA or EEGSA's consultant during the tariff review.[411] Such arguments are false. It was EEGSA that failed to submit requested information, asked for repeated extensions on the submission of its stage reports (which were granted), systematically refused to implement the directives contained in the Terms of Reference, and refused to present information in an auditable format.

a. The stage reports

326. In accordance with the Terms of Reference, Bates White was to submit nine preliminary stage reports before presenting its complete tariff study.[412] As established in LGE Article 75, this process would allow the CNEE to supervise the progress of the study, as well as promptly correct any departures from the Terms of Reference that it encountered.[413] This mechanism was designed to improve the predictability and speed of the tariff review.[414] With this same purpose in mind, the CNEE held a meeting with EEGSA, EEGSA's consultant, and Sigla to discuss matters relating to the tariff study on November 21, 2007, several weeks before the due date for the Stage A report.[415]

327. In view of the complexity of the process, the CNEE granted EEGSA all of the extensions required to submit six of the nine stage reports.[416] Despite the CNEE's

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411 Claimant's Memorial, section II.F.3.

412 Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, art. 1.4.

413 Colom, **Appendix RWS-1**, paras. 41 and 84. It should be noted that EEGSA systematically opposed the submission of phase reports and insisted that only one final study be submitted. However, the phase reports were preserved in the final Terms of Reference, given that it was vital for the CNEE to analyze the phase tariff studies on an ongoing basis so as to conduct a more efficient review.

414 *Ibid*, para. 41.

415 As Colom has indicated and contrary to TGH's assertions (Claimant's Memorial, para. 112), it is not true that EEGSA had not received a response to its proposal at said meeting. To the contrary, intense discussion on that very issue took place. *Ibid.*, para. 85.

416 *Ibid.*, para. 86 (see table).

cooperative attitude, EEGSA refused, from the start, to submit the information required of it.[417] The submission of documentation prior to the delivery of the stage reports was established in the Terms of Reference.[418] This prior submission of documentation was essential not only for the CNEE's analysis of the distributor's study, but also to allow Sigla to prepare its parallel study.

328. EEGSA's uncooperative attitude is easily illustrated in a letter written by EEGSA, dated September, 17, 2007, in response to the CNEE's request for information:

> In response to your official letter CNEE-14425-2007, DMT-Notas-424, attached, I send you the Geo-referential Information and the information about the Distribution Network of EEGSA […]
> LV lines length. Not available. […]
> Average length between posts urban …not available
> Average length between posts rural … not available
> Number of posts urban LV…not available
> Number of posts rural LV…not available […]
> Average length operable urban section…not available
> Average length operable rural section…not available
> Average length between urban posts…not available
> Average length between rural posts…not available
> Number of urban posts…not available
> Number of rural posts…not available
> Number of junctions per km…not available
> Number of connected customers…not available
> Average length LV feeder …not available
> Number of terminals…not available
> Number of junctions…not available […]

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417 The CNEE requested that EEGSA send information that would constitute the *input* on which it could perform the Tariff Study, however, EEGSA ignored such requests and either did not deliver, only partially delivered, or delivered the information in an unseasonable manner. In his witness statement, Colom explains these failures in detail. See, e.g., Letters from CNEE to EEGSA, **Exhibits R-41, R-43, R-47, R-48, R-49**; for more examples and details see **Appendix R-III**.

418 Addendum to the Terms of Reference for the Performance of the Distribution Value-Added Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, October 11, 2007, **Exhibit R-44** ("**1.6.5.** […] The Distributor shall deliver to CNEE, prior to each stage report, the base information that it passes on to the consultant for the preparation of each phase of the study, on the date on which same is transferred to the consultant.") (Bold emphasis in original, underlined emphasis added).

High-voltage injection point Not available[419]

329. Despite the difficulties relating to this exchange of information, EEGSA eventually delivered the stage reports to the CNEE. As established in the Terms of Reference, the CNEE, together with its consultants, reviewed EEGSA's stage reports and made comments thereto. Contrary to what TGH claims in its Claimant's Memorial, these comments were duly reasoned, as explained in each one of the letters sent to EEGSA.[420]

b. The Bates White tariff study of March 31, 2008

330. Once the CNEE made comments on the stage reports, it was up to the EEGSA expert to "implement" the corrections[421] and deliver its final study. However, the EEGSA's supposedly "final" study of March 31, 2008 did not contain a majority of the corrections as requested by the CNEE (hereinafter the "March 31 study").[422]

331. The VNR (capital base) resulting from the March 31, 2008 study was US$1.695 billion.[423] This value was almost three times greater than the US$583.68 million calculated in 2003 by the same consultant, Mr. Giacchino, and it implied an increase in VAD of 245 percent when compared with the 2007 study.[424] This increase in VAD thus represented an increase of almost three times in terms of

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419 Letter from Carlos Fernando Rodas to Carlos Colom Bickford (GAC-P&N-C-338-2007), September 17, 2007, **Exhibit R-42** (Emphasis added).

420 Letter from Carlos Colom Bickford to Luis Maté (Phase B), February 8, 2008, **Exhibit R-56**; Letter from Carlos Colom Bickford to Luis Maté (Phase A), February 12, 2008, **Exhibit C-161**; Letter from Carlos Colom Bickford to Luis Maté (Phase C), March 14, 2008, **Exhibit C-169**; Letter from Carlos Colom Bickford to Luis Maté (Phase D), March 14, 2008, **Exhibit C-170**; Letter from Carlos Colom Bickford to Luis Maté (Phase E), March 25, 2008, **Exhibit C-176**; Letter from Carlos Colom Bickford to Luis Maté (Phase F), March 25, 2008, **Exhibit C-175**.

421 RLGE, **Exhibit R-36**, art 98.

422 Colom, **Appendix RWS-1**, paras. 96-100.

423 *Ibid*, **Appendix RWS-1**, para. 96.

424 L Giacchino, National Economic Research Associates, "Phase C Report: Expansion process and Calculation of Capital Component," June 17, 2003, revised July 17, 2003, submitted July 30, 2003, **Exhibit R-28**, pgs. 1 and 10.

distribution charges to consumers. It was clear that, in order to justify to consumers an increase of such magnitude, the CNEE needed to have all elements of support. This was especially true when, as was stated by the then consultants Mercados Energéticos, these values were highly disproportionate when compared to other companies with similar characteristics:

> As can be observed, the differences are important even comparing with Luz del Sur which is the company that distributes electricity in the south of Lima. In case of CAESS and DELSUR, they are indeed smaller companies than EEGSA, however the existing differences in VNR [New replacement value] are in the magnitude of 10 times, while the physical information does not show said difference.[425]

332. Nonetheless, the information submitted by Bates White was not auditable, as it did not provide sufficient technical and documentary support for an appropriate and objective review of the basis of the tariffs. All this was despite the clear instructions provided in the Terms of Reference and the comments made by the CNEE on the stage reports.[426] The model company that serves to determine tariffs is constructed on Excel computer models. In order for a third party to confirm the results of the model, there must be traceability. In other words, it must be possible to follow the calculations step-by-step. For this to occur, the model's cells must be linked and there cannot be "pasted" values. Instead, these values must be derived from formulas that allow the auditor to repeat such calculations and conduct a sensitivity analysis.[427] The model submitted on March 31 did not permit replication of calculations, nor a sensitivity analysis, which violated Terms of Reference sections 1.5(3) and 1.6.4.

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425 Mercados Energéticos, "Comments to eGAS Network Optimizing Study," January 2008, **Exhibit R-52**, pg. 6 (Emphasis added).

426 CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pgs. 2-3.

427 See Damonte, **Appendix RER-2**. These comments were sent to EEGSA again through CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pgs. 2-3.

333. Furthermore, according to the Terms of Reference, EEGSA had to justify the efficiency of costs incorporated into its model, providing at least two national comparable examples and one international one. It also had to organize such information into a systematized database that would allow for easy review.[428] Additionally, the consultant was to present a comparative analysis to other similarly-sized companies (*benchmarking study*), validating the efficiency of costs in comparison to these other companies.[429] Despite the CNEE's comment regarding TGH's failure to justify costs in the stage reports, the March 31 study was similarly presented without providing the required justifications.[430]

334. In analyzing the study, the CNEE verified that a substantial increase in the VNR was due in large part to the use of construction units that were not optimal, both in terms of quality and quantity.[431] A detailed analysis of these matters is presented in paragraphs 402-410 below.

335. Facing these deficiencies, the March 31 tariff study was again commented on by the CNEE (with the advice of its consultants) and declared inadmissible, as it failed to conform to the Terms of Reference.[432]

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428 Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, arts. 3.2-3.3.3.

429 *Ibid.*, art. 7.5.3.1. The same establish that:

> A model company structure should be designed whose large functional divisions correspond to those necessary to achieve a maximum level of efficiency, as set out in section 7.5.2. To this end, their costs should be validated through a comparative analysis with other companies of a similar magnitude acting in an equivalent manner to that of the Distributor, using recent information obtained from recognized institutions or agencies of prestige.

(Emphasis added).

430 CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pg. 6.

431 *Ibid.*, **Exhibit R-63**, pgs. 8-9; Damonte, **Appendix RER-2**, para 6.

432 CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pg. 2. We note that TGH objects to the speed with which CNEE's comments were prepared (in only 10 days despite having two months). Claimant's Memorial, para 119. Importantly, the CNEE, having worked intensely on the phase reports, had previously analyzed the Bates White report in detail, which allowed it to

c. EEGSA tried to secure new tariffs outside the regulatory framework in disregard of its tariff study, which was considered unreliable.

336. Shortly after the CNEE submitted its comments to the March 31 study, it received a call from the secretary of the General Manager of EEGSA requesting a meeting between the CNEE's Directors and the President of EEGSA's Board of Directors (also President of Iberdrola for Latin America), Mr. Gonzalo Pérez, who was based in Mexico. As explained by Mr. Colom, although it was usual to hold meetings with EEGSA executives, this meeting was noteworthy given that Mr. Perez had not been involved in the EEGSA tariff review process until that moment, and also because EEGSA did not provide a reason for the meeting.[433]

337. During this meeting, which took place on April 22, 2008, Mr. Pérez issued a presentation wherein he explained that Mr. Giacchino's tariff proposal for the upcoming May 5th tariff study would yield an "**an estimated compensation increase of 100**.[434]" In this context, Mr. Pérez's presentation contained a "propuesta" to be applied by "disregarding the study" that would reduce the increase from 100 percent to 10 percent.[435] This increase could also be implemented, according to Mr. Pérez, without an increase in tariffs:[436]

> Consequently, the **Distributor would collect from users** (2007) almost the same (USD3,000), but would obtain a 10% increase in the revenues from its investment as it has already finished collecting the portion of the tariff it receives to compensate for generation costs (a 10% increase with respect to the 100% increase proposed by the consultant). **USD175,000 compared to USD160,000 (2007).**

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reformulate its comments on the uncorrected points in a short time. Moreover, EEGSA failed to include almost all of CNEE's comments and therefore, the work required was minimal.

433 Colom, **Appendix RWS-1**, para 101.

434 Presentation on Tariff Study Income Requirements, **Exhibit R-65**, pg. 8 (Bold emphasis in original, underlined emphasis added).

435 *Ibid*, **Exhibit R-65**, pgs. 12-13; Colom, **Appendix RWS-1**, para. 102.

436 Presentation on Tariff Study Income Requirements, April 22, 2008, **Exhibit R-65**, pg. 12.

> […]
>
> **THE DISTRIBUTOR WOULD OFFER SUCH PROPOSAL TO THE CNEE AS A REDUCTION TO THE PROPOSAL MADE BY THE CONSULTANT AND IN DISREGARD OF THE STUDY.**
>
> Given that it is impossible to adapt the study concept-by-concept in order to obtain this level of income while complying with the Law.[437]

338. In other words, while its March 31 study requested a VAD increase of 245 percent in comparison to 2007, EEGSA was now content with an increase of only 10 percent and agrred to "disregard the study" (a reduction of US$326 million per year).[438]

339. In its Memorial, TGH affirms that Mr. Pérez's proposal originated at a lunch during which Mr. Moller asked Luis Maté, General Manager of EEGSA, whether EEGSA would accept a VAD increase of 5 percent over the present one. According to Mr. Maté, based on that proposal, EEGSA prepared a counterproposal including an increase in VAD without an increase in tariffs.[439] As explained by Mr. Moller, this is simply false.[440] Although he had lunch with Mr. Maté on several occasions (always at the invitation of Mr. Maté), Mr. Moller never made this alleged proposal. Such a proposal would imply not only a violation of the LGE, but would also frustrate the internal efforts by him and his colleagues to ensure adequate technical support for the tariff review process (among them, the modernization and expansion of the Tariff Division).[441] Furthermore, had such a proposal existed, it would have been discussed internally

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437 *Ibid.*, pgs. 12-13 (Bold emphasis in original, underlined emphasis added).

438 Colom, **Appendix RWS-1**, para. 103.

439 Claimant's Memorial, paras. 120-121; Maté, **Appendix CWS-6**, para. 21.

440 Moller, **Appendix RWS-2**, para. 37.

441 *Ibid.*, para. 38.

at EEGSA, TGH, or Iberdrola prior to its implementation. TGH has not provided any evidence of its allegations.

340. Nor does TGH explain why this proposal was made in person, during a meeting with no pre-established agenda, no introductory or follow-up email, through a single document without letterhead, and without any mention of the actual names of the individuals or companies involved (referring only to "Distributor" and "Consultant"). TGH's claim that this document was delivered in electronic format[442] is not only false (note that TGH failed to provide evidence in support of this claim), but TGH submitted the same version of the document that Guatemala submitted in the Iberdrola arbitration.[443]

341. It is worth wondering how Mr. Pérez could justify such a gratuitous waiver of a large portion of its income to TGH, if the value estimated by its consultant truly reflected a technically fair and efficient value of the VAD.

342. The answer is clear. As explained by Mr. Colom, Mr. Pérez stated that the Bates White report was "good for nothing."[444] In fact, the presentation submitted by TGH is the same version that remained in the CNEE's possession (and that Guatemala presented in the Iberdrola arbitration), which contains a handwritten note by Mr. Colom, in which he records Mr. Pérez's statements:

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442 Claimant's Memorial, para. 121 ("At the end of the meeting, the CNEE's directors said that they would analyze the presentation, which EEGSA provided in electronic format."). In support of this statement, TGH quotes the statement by Maté (para. 23), who however did not state the foregoing.: "At the end of the meeting, the CNEE Directors thanked us and said they would analyze the presentation and would send us a response to our proposal." Maté, **Appendix CWS-6**, para. 23; Colom, **Appendix RWS-1**, paras. 102-103.

443 TGH's objectionable attitude is also evidenced in the fact that, contrary to what has occurred in this arbitration, neither Mr. Maté nor Mr. Calleja referred to this irregular situation in their first declarations as Iberdrola's witnesses. Once Guatemala shared these facts and submitted the proposal received from Mr. Pérez in that arbitration, these witnesses referred to the irregular offer by Mr. Pérez. *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statements of Luis Mate, October 14, 2009 and September 23, 2010, **Exhibit R-149**; *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statements of Miguel Francisco Calleja, October 14, 2009 and September 25, 2010, **Exhibit R-150**.

444 Colom, **Appendix RWS-1**, para 103.

EEGSA: (the study prepared by the EEGSA's consultant was useless).[445]

343. Mr. Pérez's visit can only be interpreted in one way: the offer to reduce the VAD tariff was not an act of charity by Iberdrola, but rather demonstrated that the values advanced by the Consortium's consultant were not real, and instead functioned as a tool for negotiating the tariff.[446] The CNEE's Directors were thus placed in a very inappropriate situation, given that the proposal for a tariff negotiation or "a negotiated settlement" was outside of their authority and outside of the LGE provisions. For this reason, the proposal was ignored and not given further consideration.[447]

d. The May 5 tariff study

344. On May 5, 2008, Bates White, through Leonardo Giacchino, submitted its reply to the comments on the March 31 study (hereinafter the "May 5 Study").[448] That study reflected only 40 of the 125 corrections ordered by the CNEE through its comments. Among the corrections not implemented were: models remained inauditable, the justification of efficient prices failed to contain national and international comparables, benchmarking, or a systematized database, and the construction units continued to be non-optimal.[449]

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445 See handwritten note on Presentation on Tariff Study Income Requirements, April 22, 2008 **Exhibit R-65**, pg. 8; Colom, **Appendix RWS-1**, para 103. This document is the copy of the presentation that remained with CNEE, and which was presented by Guatemala in the arbitration commenced by Iberdrola. Guatemala understands that a copy of this document was submitted by Iberdrola to TGH in the context of an agreement to exchange information, an agreement that TGH has refused to submit to Guatemala in this arbitration.

446 Guatemala notes that in the arbitration commenced by Iberdrola, Mr. Pérez was not presented as a witness in this arbitration (nor were reasons given for not presenting him), despite the fact that he continued to work for Iberdrola. TGH preferred to channel its responses to this incident though two other witnesses, also employees of Iberdrola, Messrs. Maté and Calleja.

447 Colom, **Appendix RWS-1**, para 104.

448 Letter from Leonardo Giacchino to Mr. Carlos Colom Bickford and Mr. Miguel Francisco Calleja, May 5, 2008, **Exhibit R-68**; Colom, Appendix RWS-1, para. 105.

449 See section III.F.9 below.

345. Bates White justified its failure to correct 85 of the 125 comments with an inaccurate interpretation of Articles 1.5 and 1.10 of the Terms of Reference.[450] As previously explained (para. 311 above), the Terms of Reference required the consultant to "have independence of judgment" (Article 1.5). However, such independence was with respect to the distributor and not, as Bates White claimed, with respect to the Terms of Reference. The Terms of Reference are the action plan for the distributor and its consultant; under the Bates White interpretation of this article, there would be no reason for the Terms of Reference to exist. The following extract evidences the consultant's position with regard to this standard:

> This consultant followed the guidelines included in the [Terms of Reference] but used its own independent criteria when certain language in the [Terms of Reference] showed deviations from Guatemalan reality, errors or omissions, lack of consistency with precedent from the CNEE itself and deviations from the best international regulatory practices. […] In such cases, this consultant applied their own independent criteria in order to justify the submitted solutions […][451]

346. Furthermore, Bates White made repeated use of Article 1.10 which, as previously explained, allows a consultant to include certain "variations" in the methodology, provided these are justified and agreed to by the CNEE itself. The use of these articles was only permitted in exceptional cases since the distributor previously had the opportunity to challenge the Terms of Reference (as EEGSA had in this case). Furthermore, Article 1.10 establishes that all changes to the Terms of Reference require consent from the CNEE, the only entity authorized by the LGE to establish and modify the methodology.[452]

347. This interpretation is also the only one consistent with RLGE Article 98, which establishes that a consultant must "implement the corrections" required by the

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450 Colom, **Appendix RWS-1**, para. 108.

451 Letter from Leonardo Giacchino to Engineer Carlos Colom Bickford and Miguel Francisco Calleja, May 5, 2008, **Exhibit R-68**, pgs. 1-2.

452 Colom, **Appendix RWS-1**, para. 109.

regulator. An interpretation of the Terms of Reference that allows a consultant to unilaterally depart from them is illegal, because it is contrary to the CNEE's function to define the methodology for calculating the tariff, which is exclusively assigned to the CNEE by the LGE. Despite this, Bates White invoked these articles during its tariff review in order to depart from the methodology a total of 423 times![453] It even invoked the articles in order to justify its failure to present information in an auditable format. It is clear that such abuse neutralized the basic purpose of the Terms of Reference to be applied.

348. The incorporation of only 40 of the CNEE's 125 comments into the May 5 study resulted in a VNR reduction of 23 percent (equivalent to US$395 million) compared to that of March 31.[454] Such a reduction speaks volumes as to the validity of the figures in the first tariff study. TGH tries to justify such reduction by pointing to its exclusion of underground networks (much more expensive than aerial networks, they are also nonexistent in EEGSA's actual present network[455]) allegedly included in the first study by agreement with the CNEE.[456] Not only did such agreement not exist, as shown by TGH's lack of evidence, but it could never have existed because the LGE expressly prohibits charging for underground lines in the tariff.[457]

349. The new value was still far greater than the one proposed by Mr. Pérez during his earlier visit to the CNEE. In a few days, the VAD increase was not of 100 percent compared to 2007, as Mr. Pérez "threatened," but rather 184 percent.[458] It is thus clear that the CNEE's rejection of EEGSA's proposal had an inflammatory effect.

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453 Extracts from the Phase Reports wherein Bates White invokes Articles 1.5 and 1.10 of the Terms of Reference, **Appendix II**.

454 Claimant's Memorial, para. 122.

455 See below, Section III.F.9.d(i).

456 Claimant's Memorial, para. 122; Giacchino, **Appendix CWS-4**, para. 30.

457 LGE, **Exhibit R-8**, art. 52.

458 Colom, **Appendix RWS-1**, para. 105.

350. Faced with this situation, it was evident that the CNEE could not accept the Bates White tariff study.

7. The procedure before the Expert Commission

a. The calling of the Expert Commission

351. On May 15, 2008, in light of the rejection of Bates White's tariff study for its failure to conform to the Terms of Reference, the CNEE called for the establishment of the Expert Commission via Resolution 96-2008, to which its discrepancies with EEGSA would be referred, as established under LGE Article 75.[459] The role of the Expert Commission, as clearly set forth in the text of the Resolution, was limited to determining whether the Terms of Reference had been properly applied in the distributor's study:

> [V]erifying the correct application of the Terms of Reference (TdR) of the Distribution Value Added Study approved by the National Electric Energy Commission.[460]

352. The LGE at that time did not require that the party-appointed members of the Expert Commission be independent or impartial. Therefore, EEGSA immediately informed the CNEE that Mr. Leonardo Giacchino himself, author of the tariff study under review, would be its representative on the Expert Commission.[461] The

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459 CNEE Resolution 96-2008, May 15, 2008, **Exhibit R-71**. EEGSA, and now TGH, complained to the CNEE in this letter, indicating that Resolution 96-2008, which had ordered the formation of the Expert Commission, had included "additional discrepancies" that the distributor had not previously been able to study. This is not true. While some of the titles of the discrepancies named in Resolution 96-2008 had changed, nearly all of the discrepancies were already the subject of previous communications from the CNEE. See e.g., CNEE Resolution 63-2008, April 11, 2008 **Exhibit R-63**; Letter from Letter from Carlos Colom Bickford to Luis Maté (Phase C), March 14, 2008, **Exhibit C-169**, pgs. 3-8. New issues arose involving a few minor discrepancies due to the CNEE's repeated revision of a the highly flawed study. Further, what TGH fails to say (which its witness Mr. Calleja does indeed recognize) is that the parties agreed that the Expert Commission would consider both the discrepancies indicated by the CNEE in Resolution 96-2008 and the May 23 response from Bates White. Therefore, even if there had been a legitimate complaint regarding the discrepancies identified by the CNEE to be submitted to the Expert Commission (which there was not), it likewise would not have caused EEGSA any damage.

460 CNEE Resolution 96-2008, May 15, 2008, **Exhibit R-71**, pg. 3.

461 Colom, **Appendix RWS-1**, para. 116.

CNEE, for its part, appointed Jean Riubrugent who had advised it in specific matters of the analysis prepared by Sigla, as previously explained.[462] Such appointments (especially that of EEGSA, whose appointee had prepared the study that was the subject of the discrepancies), demonstrated that no one considered that this Commission was to be independent or impartial.

b. Modification of Article 98 Bis

353. Once both parties appointed their respective representatives to the Expert Commission, the parties were to agree on the appointment of the third expert, who would preside over the Expert Commission. In their first exchanges, however, the parties were unable to agree on the third member. Curiously, despite the need to include engineering and economics experts from the electricity sector, EEGSA proposed Roberto Aguirre Luzi and Arif Hyder Ali, two attorneys specializing in international investment arbitration practicing in the United States with the firms King & Spalding and Crowell & Moring, respectively, who clearly did not have the knowledge or experience required to study technical discrepancies related to the VAD calculations submitted to the Expert Commission. More striking still, Crowell & Moring was one of Bates White's largest clients.[463] The CNEE did not accept these candidates. EEGSA also proposed Mr. José Luis Aburto Ávila and Carlos Herrera Descalzi, but the CNEE also did not consider them sufficiently specialized in the subject. The CNEE, for its part, proposed engineers specializing in the electricity sector, including Carmenza Chahin, Rafael Moscote, Alejandro Sruoga and José Miranda Abdo. EEGSA, however, rejected these candidates.[464]

354. Faced with this situation, the CNEE board became concerned as it became apparent that, due to a lacuna in the RLGE, the procedure would be blocked indefinitely if the parties were unable to agree on the third member of the Expert

462 *Ibid.*, para. 117.

463 Matthew E. Raiff, a founder member of Bates White, oversees various matters for the firm's most important clients, including Crowell & Moring LLP. Profile of Matthew E. Raiff, PhD, Partner of Bates White, http://www.bateswhite.com/professionals.php?PeopleID=54, **Exhibit R-156**.

464 Colom, **Appendix RWS-1**, para. 118.

Commission.[465] To avoid this situation, the CNEE proposed the incorporation of RLGE Article 98 bis to allow the tariff review to progress and establish tariffs on time.[466] Under this reform, the parties were to agree on a third expert within a period of three days, after which time the MEM would appoint that expert from among the candidates proposed by both parties.

355. In face of EEGSA's rejection of the solution offered, the CNEE agreed not to apply Article 98 bis to the review in progress (as TGH acknowledges).[467] Fortunately, a few days later, the parties succeed in unlocking this process by agreeing on the third member, nominating Mr. Carlos Bastos, of Argentine nationality.[468]

356. All in all, the raft of issues raised by TGH in its Claimant's Memorial regarding Article 98 bis, which caused it no harm, is groundless and seeks to confuse the Tribunal. As Mr. Colom explains, contrary to TGH's allegations,[469] behind this modification there were only practical motives and concern on the part of the CNEE to implement the new tariff schedule within the legal timeframe, a schedule that was running the risk of remaining stalled as a result of the regulatory gap:

> In any case, our intention in requesting the RGLE reform was not to prejudice EEGSA, but rather to devise a practical solution to advance the process of

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465 *Ibid.*, para. 119.

466 According to this amendment, for the third member of the Expert Commission to be nominated, both the CNEE and the distributor must propose three candidates, who must meet certain requirements, including: being electric power specialists of recognized reputation, without any associations with entities or companies in the electricity sector in Guatemala within the previous five years. If, after three days from the date that the candidates were presented, the parties do not agree on one of them, it falls to the MEM to select the third member from among those proposed by the parties. This measure guarantees a certain degree of collaboration and cooperation in the process and would avoid any maneuvers that could stall the procedure, while also guaranteeing that the candidates are independent and meet the minimum requirements for suitability and experience to carry out the tasks with which they are charged.

467 Claimant's Memorial, para. 135; Colom, **Appendix RWS-1**, para. 121.

468 Colom, **Appendix RWS-1**, para. 121.

469 Claimant's Memorial, paras. 133-135.

appointing the third member to the Expert Commission.[470]

357. It is worth nothing that, at the time the parties inquired about his interest in joining the Expert Commission, Mr. Carlos Bastos disclosed that EEGSA was his client, having worked for that company in connection with the Guatemalan wholesale electricity market in the past.[471] It is clear that, under such circumstances, the CNEE would never have agreed to his appointment with an understanding that the pronouncement of the Expert Commission could be binding.

c. The CNEE could not accept (and did not accept) Rule 12 because it violated the exclusive authority assigned it by the LGE

358. In tandem with the discussions between CNEE and EEGSA representatives regarding its third member, the parties discussed the possibility of adopting operating rules to structure the work of the Expert Commission. The original idea was to issue a regulation in accordance with LGE Article 77.[472] Not only did the LGE and RLGE fail to establish a mechanism to create the Expert Commission, it also lacked instructions on how the Expert Commission was to carry out its work. Furthermore, it was the first time in the history of the CNEE that this body was created and, therefore, there were no precedents to guide its operation.

359. In its Claimant's Memorial, TGH states that the parties reached an agreement on these rules and, in particular, on the so-called "Rule 12."[473] This rule stipulated that, once the Expert Commission issued its pronouncement, the distributor's consultant would adjust the tariff study to incorporate the pronouncement, and the Expert Commission itself would review the adjustment to confirm the

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470 Colom, **Appendix RWS-1**, para. 120.

471 Statement of Witness Carlos Bastos, September 21, 2011 (hereinafter ***Bastos***), **Appendix CWS-1**, para. 10.

472 Colom, **Appendix RWS-1**, para. 123.

473 Claimant's Memorial, para. 137.

pronouncement was correctly incorporated. It must be made clear that TGH's assertions regarding the CNEE's supposed acceptance of Rule 12 are absolutely false. Although the parties agreed in principle on most of the operating rules, it was precisely the disagreement on Rule 12 that prevented the parties from formalizing any final agreement on those rules. As explained below, the primary reason for the CNEE's objection to Rule 12 was that it affected essential powers of the CNEE and breached the procedure established in the LGE and RLGE, which did not provide for any additional action or duty on the part of the Expert Commission after issuing its pronouncement on the discrepancies.

(i) The exchange of drafts between the CNEE and EEGSA regarding the operating rules

360. TGH conveniently fails to mention that the process to agree on operating rules started on May 14, 2008, when the CNEE sent EEGSA the initial proposed regulations for the Expert Commission containing 17 articles that would govern the creation and operation of this body.[474] These regulations, if adopted via due formalities, would be permanent in nature, meaning they would apply to all future procedures of this type. These regulations only assigned the Expert Commission the duty to pronounce itself [*se pronunciará*] on discrepancies[475] and two of its

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474 E-mail from Melvin Quijivix to Miguel Francisco Calleja, attaching the Proposed Operating Rules for the Operation of the Expert Commission, May 14, 2008, **Exhibit R-70**. Articles 1 and 17 stipulated:

> **Article 1. Nature and functions.** The Expert Commission is a body created in the Articles 75 and 77 of the General Law of Electricity and the Article 98 of Regulations of the Law, with limited competence, formed by three professional experts whose function is to pronounce itself, by non-binding reports, on those discrepancies that may arise due to the revision of the Five-Year Tariff Studies.
>
> **Article 17.** The reports of the Expert Commission are not binding to all those participating in the respective procedure and no type of action, judicial or administrative, ordinary or extraordinary, will proceed in its respect […].

(Bold emphasis in original, underlined emphasis added).

475 *Ibid*, Article 12; see Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Tr., Day Three, Colom, 769:9-22

> We sent to Empresa Eléctrica an initial version with the proposal of regulations for the operation of the Expert Commission. It was a

articles (the first and last) explained the non-binding nature of the Expert Commission's opinion.[476]

361. EEGSA opposed the proposed regulations and suggested agreeing on certain specific rules for the 2008 review instead of general regulations. The CNEE agreed to this and, in a meeting at the CNEE on May 19, 2008, Mr. Calleja of EEGSA submitted a printed proposal containing 17 suggested rules for the future Expert Commission.[477]

362. This first version of the rules circulated by EEGSA mentioned that the Expert Commission would issue a "Ruling" [*Sentencia*] and that it would be in charge of the "resolution of disputes."[478] The CNEE rejected this proposal because it contradicted the LGE and the RGLE, which provide that the Expert Commission's task is to pronounce itself [*se pronunciará*] on the discrepancies as it is not a tribunal or organ that resolves disputes. EEGSA agreed to remove this language from its proposal and the wording never appeared again in successive communications circulated among the parties.[479]

> proposal of regulations. It was the first version that was circulated because the law did not contemplate any form in which the procedure had to be for this commission to operate.
>
> The law in fact was very clear; it is always been clear that the function of the Expert Commission is that of pronouncing itself on discrepancies. And for that reason we sent an initial draft and this draft is quite clear in two of its articles where it says that the commission is nonbinding, the ruling of the Expert Commission is not binding..

476 Therefore, TGH's criticism in its Memorial of the CNEE, in which it accuses Mr. Colom of wanting to undermine "the Commission's authority" for having responded to the media interrogation regarding the interpretation that the CNEE gave to the duties of the Expert Commission is false and unjust. Claimant's Memorial, paras. 151-154. Engineer Colom was simply expressing the interpretation that the body made of its duties according to the current regulatory framework. This is the same interpretation, is it important to note, that the highest judicial authority of Guatemala, the Constitutional Court, would have in studying this specific point of the regulatory framework, as explained in Section IV.B.5.

477 Proposed Rules for the Expert Commission, May 19, 2008, **Exhibit R-73**; Colom, **Appendix RWS-1**, para. 125.

478 Proposed Rules for the Expert Commission, May 19, 2008, **Exhibit R-R-73**, rules 8, 12 and 13; Colom, **Appendix RWS-1**, para. 126.

479 E-mail from Melvin Quijivix to Miguel Francisco Calleja, attaching the Operating Rules Proposed for the Operation of the Expert Commission, May 21, 2008, **Exhibit R-74**; E-mail from Melvin

363. Further, this proposal was the first to include what would later be identified as Rule 12. This rule stipulated that, once the Expert Commission issued its pronouncement, Bates White would correct the tariff study accordingly and resubmit the study for the Expert Commission to review and confirm whether said corrected study faithfully reflected the elements of the pronouncement.[480] As TGH acknowledges in its Claimant's Memorial, the parties did not reach an agreement on this point.[481]

364. As indicated above, the primary reason for the CNEE's objection was that neither the LGE nor the RLGE established an additional role for the Expert Commission after its pronouncement on the discrepancies. To allow the Expert Commission to review the study, supposedly corrected by the distributor, to confirm whether it was consistent with its pronouncement would have meant reversing the roles of the CNEE and the Expert Commission. Only the CNEE has the authority to determine the admissibility of the tariff study and approve it.[482] This was also impossible from a practical perspective, as the Expert Commission could not approve a tariff study that it had not reviewed in its entirety. As Mr. Bastos confirmed when asked about this issue at the Hearing of the Iberdrola case, the Expert Commission only considered points of disagreement, but did not review the tariff study in its entirety nor did it have the means to do so.[483]

365. After the draft rules were delivered by Mr. Calleja on May 19, various meetings were held with EEGSA at the CNEE to discuss the text of the operating rules;[484]

Quijivix to Luis Maté and Miguel Francisco Calleja, attaching the Proposed Operating Rules for the Expert Commission, May 23, 2008, **Exhibit R-75**; E-mail from Melvin Quijivix to Luis Maté and Miguel Francisco Calleja, May 28, 2008, **Exhibit R-77;** Colom, **Appendix RWS-1**, para. 126.

480 Proposed Rules for the Expert Commission, **Exhibit R-73**, rule 14.

481 Claimant's Memorial, para. 129.

482 RLGE, **Exhibit R-36**, art. 98. ("[…] [L]a [CNEE] resolverá sobre la procedencia o improcedencia de los estudios efectuados por los consultores […]").

483 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit 140**, Tr., Day Two, Bastos, 647:14-648:12.

484 Claimant's Memorial, paras. 128-130, 132, 137.

Mr. Melvin Quijivix, as meeting secretary, circulated various drafts of operating rules reflecting the status of the discussions between the parties after each meeting. This included the drafts of May 21, 23 and 28, 2008.[485] The May 28 draft (sent by Mr. Quijivix to Mr. Calleja) was the last document regarding which the parties attempted − unsuccessfully − to reach agreement.

366. By reviewing the aforementioned drafts circulated, one clearly sees that there was never a final agreement between the parties regarding the operating rules. The May 28 draft and its earlier versions are typical documents for a "*work in progress*," all using a very similar format, reflecting slight changes in the discussions following each meeting. Moreover, there is no evidence of an agreement in this respect. The following is a detailed description of these drafts:

Document	Date	Subject heading from the e-mail	Text heading the list of rules under discussion
E-mail from Engineer Melvin Quijivix to Mr. Miguel Calleja, attaching a new version of the rules under discussion (R-74)	May 21, 2008	PROPOSED RULES FOR THE EXPERT COMMISSION	PROPOSED OPERATING RULES FOR THE OPERATION OF THE EXPERT COMMISSION
E-mail from Engineer Melvin Quijivix to Mr. Miguel Calleja, attaching a new version of the rules under discussion (R-75)	May 23, 2008	EC RULES	PROPOSED OPERATING RULES FOR THE OPERATION OF THE EXPERT COMMISSION

485 E-mail from Melvin Quijivix to Miguel Francisco Calleja, attaching the Operating Rules Proposed for the Operation of the Expert Commission, May 21, 2008, **Exhibit R-74**; E-mail from Melvin Quijivix to Luis Maté and Miguel Francisco Calleja, attaching the Proposed Operating Rules for the Expert Commission, May 23, 2008, **Exhibit R-75**; E-mail from Melvin Quijivix to Luis Maté and Miguel Francisco Calleja, May 28, 2008, **Exhibit R-76** (this e-mail was later re-sent by M. Calleja to G. Pérez).

E-mail from Engineer Melvin Quijivix to Mr. Miguel Calleja, attaching a new version of the rules under discussion (R-76)	May 28, 2008	PROPOSED OPERATING RULES FOR THE EXPERT COMMISSION	PROPOSED OPERATING RULES FOR THE OPERATION OF THE EXPERT COMMISSION

367. As the preceding table shows, all of the versions of the rules circulated by Mr. Quijivix indicated that they constituted a proposal: all of them, in fact, used the word "PROPOSED" in the text heading. Furthermore, the "Subject" of the e-mails of May 21 and 28 specifically included this term. The fact that in each of these occasions Mr. Quijivix wrote "proposed" confirms that the rules were still under discussion between the parties when the e-mails were written. The text from the "subject" line in the e-mails reflected slight changes in each e-mail sent, which shows that Mr. Quijivix had to retype the text in the subject heading and did not simply "resend" or "respond" to a previous e-mail.

368. Consequently, it is clear that Mr. Quijivix did not send the May 28 e-mail as a final agreement between the parties as TGH alleges.[486] Not only was Mr. Quijivix not authorized to sign any agreement in this regard,[487] but it is implausible that he would include the word "proposal" if the intention was, as TGH claims, for this e-mail to be the culmination of an arduous process of negotiation over Rule 12.[488] Moreover, Mr. Quijivix's e-mail does not contain any mention of a supposed agreement reached nor does it indicate that it involves a final or binding document, which would be expected under such circumstances (also note that EEGSA did not respond to this e-mail in these terms). What is true, as we will see, is that the parties continued with the procedure before the Expert Commission without agreeing on Rule 12 as TGH claims.

(ii) Behind the CNEE's back, EEGSA sent the operating rules (including Rule 12) to the President of the Expert Commission,

486 Claimant's Memorial, para. 137.

487 This task corresponds exclusively to the Board of Directors; LGE, **Exhibit R-8**, art. 5.

488 Claimant's Memorial, paras. 129-130, 132, 137.

falsely indicating that they had been agreed upon with the CNEE

369. Despite the lack of agreement between the parties, on June 2, 2008, Mr. Calleja re-sent to the president of the Expert Commission, Mr. Bastos—behind the CNEE's back, without notifying it or cc-ing it—the e-mail with the draft under discussion that Mr. Quijivix had sent to EEGSA on May 28.[489] To better understand: EEGSA unilaterally communicated with the President of the Expert Commission and sent him the operating rules (including Rule 12), telling him that these had been agreed upon, which was false. In his witness statement, Calleja makes an untruthful statement that, after sending an e-mail to Mr. Bastos, he "informed Mr. Quijivix that I had done so."[490] He does not offer any proof of this, nor does he explain the manner in which such contact took place. It is notable that Mr. Calleja never mentioned this supposed communication with Mr. Quijivix in his witness statement in the Iberdrola case. The reality is that the CNEE only learned of the existence of this unilateral submission from Mr. Calleja to Mr. Bastos with the launch of the respective arbitrations by Iberdrola and TGH.[491]

370. A few days later, unaware of the irregular and unilateral action by Mr. Calleja, the CNEE agreed to a conference call with EEGSA and Mr. Bastos to discuss administrative questions regarding the procedure.[492] In this discussion, Mr. Quijivix and Mr. Calleja mentioned to Mr. Bastos that operating rules had been discussed, with the beginnings of an agreement,[493] given that such rules could be

489 E-mail from Miguel Francisco Calleja to Carlos Bastos, June 2, 2008, **Exhibit R-79**; Colom, **Appendix RWS-1**, para. 132.

490 Calleja, **Appendix CWS-3**, para. 42. Note that the witness Calleja had not referred to this supposed communication with Mr. Quijivix in his testimonial statement in the Iberdrola case. *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statement of Miguel Francisco Calleja, October 14, 2009, **Exhibit R-150**, para. 41.

491 Colom, **Appendix RWS-1**, para. 132.

492 *Ibid.*, para. 131.

493 In Rules 1 to 11, the operating rules included questions of procedure entirely consistent with the provisions of the LGE and the RLGE.

useful to the Expert Commission.[494] But at no time was it represented to Mr. Bastos that there was an agreement on Rule 12.[495]

371. On this point it is important to remember one essential element: the CNEE does not operate nor does it make its decisions in the way a private entity does; rather, it is governed by precise rules of public law.[496] One of the basic principles of administrative law governing its conduct is the publication of official documents, which ensures that the CNEE only exercises its authority through official resolutions (or official records) signed by its Directors and with proper support.[497] This, of course, was not new to EEGSA and its attorneys, who had spent ten years operating in Guatemala under the supervision of the CNEE and who knew that any agreement by the CNEE regarding operating rules had to be formalized in this way in order to be valid.

372. Furthermore, as is evident, no operating rules, much less ones that had not passed the discussion stage between two parties, could amend the letter and spirit of the LGE, the RLGE or the Agreements (which required that any change in the conditions of the legal framework be agreed upon in writing). Rule 12 had no legal basis, and in fact, would effectively amend the RLGE by introducing a third version of the tariff study and a second pronouncement from the Expert Commission not provided for in the LGE or the RLGE.[498] Mr. Bastos himself acknowledged at the Hearing in the Iberdrola case that the last word regarding

494 Colom, **Appendix RWS-1**, para. 131.

495 *Ibid.*

496 *Ibid.*, para. 129.

497 *Ibid.*, para. 129. The CNEE only expresses itself through resolutions passed by the majority of its members, meaning Article 5 of the LGE, and it cannot nor should it be construed that an e-mail implies approval from the CNEE, an e-mail that, in any case, does not even indicate that was approval had been given and which indicates that it is proposed text.

498 RLGE, **Exhibit R-36**, art. 98; LGE, **Exhibit R-8** art. 75.

whether the tariff study was approved or rejected needed to be that of the CNEE and not of the Expert Commission.[499]

(iii)The Act of Appointment of the Expert Commission

373. On June 6, 2008, the Act of Appointment of the Expert Commission (the ***Act of Appointment***)[500] was signed by Carlos Colom, representing the CNEE, and by Luis Maté, representing EEGSA. In the document, the two parties appointed their respective experts for the Expert Commission and gave their consent for Mr. Carlos Bastos to preside over the Expert Commission. Article One of the Act of Appointment made the mandate of the Expert Commission very clear:

> The undersigned state that the **Expert Commission** is constituted to pronounce itself on the discrepancies regarding the Distribution Value Added (VAD) Study of Empresa Eléctrica de Guatemala, Sociedad Anónima, contained in resolution CNEE – ninety-six – two thousand eight (CNEE-96-2008), as well as regarding the responses from Empresa Eléctrica de Guatemala, S.A. and its consultant for same, in accordance with what is set forth in article seventy-five (75) and ninety-eight (98) of the General Law of Electricity and the Regulations of the General Law of

499 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 593:8-20.

> A: […] "The exact instructions are that all of the calculations and modifications that must be made in the models are done, is necessary **to make that everything can be corroborated by the CNEE**."
>
> Q: Then there exists a role for the CNEE still after that supposed -- of the work that you say must be done by the consultant. **They have to be corroborated by the National Electric Energy Commission.** Right?
>
> A: That's what we are saying.
>
> Q: And all this before 1 August
>
> A: Exactly. **Everything has to be after our final report.**

(Emphasis added).

500 Notarial Act of Appointment of the Expert Commission, June 6, 2008, **Exhibit R-80**.

> Electricity, respectively, which establishes that in the event of discrepancies made in writing, the Commission and the distributors shall agree on the appointment of an Expert Commission of three members, one appointed by each party and the third one by mutual agreement.[501]

374. There was no mention of a second round of comments by the Expert Commission. The Letter of Appointment was the only official document issued by both parties pursuant to Resolution 96-2008, which ordered that the Expert Commission be created. It did not stipulate, explicitly or implicitly, any duty or task for the Expert Commission other than its pronouncement on the discrepancies. Nor did it make any reference whatsoever to the operating rules. Nor could it have done so since there was no such agreement and Rule 12 would have represented an overstepping of authority with respect to "what is set forth in article seventy-five (75) and ninety-eight (98) of the [LGE] and the [RGLE]."[502]

375. Subsequently, on June 12, 2008, the three experts gave notice that they were assuming their duties on the Expert Commission in a note confirming their understanding with respect to the scope of their work.[503]

(iv) The contracts signed between Mr. Bastos and the CNEE and between him and EEGSA

376. On June 26, 2008, Mr. Bastos signed separate contracts with the CNEE and EEGSA, which, in accordance with the provisions of RLGE Article 98, were each obligated to pay half of Mr. Bastos' fees (set at US$ 100,000 for the entire assignment).

377. It is important to emphasize that the contract signed between the CNEE and Mr. Bastos expressly defined his duty in detail (which he would later unilaterally

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501 Notarial Letter of Appointment of the Expert Commission, June 6, 2008, **Exhibit R-80**, clause 1 (Bold emphasis in original, underlined emphasis added).

502 *Ibid*. **Exhibit R-80**.

503 Letter from Jean Riubrugent, Carlos Bastos and Leonardo Giacchino to Carlos Colom Bickford and Luis Maté, June 12, 2008, **Exhibit R-83**.

modify in the opinion; see paragraph 414 below), which was to verify the proper application of the Terms of Reference:

> **THIRD: PURPOSE.**
>
> […]In his conduct as "EXPERT", he must verify the correct application of the methodology and criteria established in the Terms of Reference (Resolutions CNEE-124-2007 and CNEE-05-2008) in the Distribution Value Added Study of Empresa Eléctrica de Guatemala, Sociedad Anónima, indicating his position in relation to each discrepancy set forth in Resolution CNEE-96-2008; as well as on the responses to same from Empresa Eléctrica de Guatemala, Sociedad Anónima and its Consultant.
>
> **FOURTH: SCOPES.**
>
> **The EXPERT** must comply with the following:
>
> a) Join the Expert Commission as third member, which expert Commission shall be responsible to pronounce itself on the discrepancies with the Distribution Value Added Study of Empresa Eléctrica de Guatemala, Sociedad Anónima, established in Resolution CNEE-96-2008, dated May 15, 2008, Resolution which was notified to such Distributor on May 16, 2008, which, according to the applicable law, is firm; on the replies to same, from Empresa Eléctrica de Guatemala, Sociedad Anónima and its Consultant;
>
> b) To perform a technical analysis of the discrepancies established in Resolution CNEE-96-2008, arising with the Distribution Value Added Study of Empresa Eléctrica de Guatemala, Sociedad Anónima, by applying his knowledge and experience in the determination of the position of the Expert Commission, in relation to each discrepancy, according to the Terms of Reference;
>
> c) To verify the correct application of the Terms of Reference (TOR) approved by the [CNEE], in relation to the Distribution Value Added Study;
>
> d) To learn and use the applicable legislation on the points under discrepancy identified precisely in Resolution CNEE-96-2008, and the replies to same by

> Empresa Eléctrica de Guatemala, Sociedad Anónima and its Consultant;
>
> e) Issue its pronouncement on the discrepancies, according to the current law and the Terms of Reference approved by CNEE for the Distribution Value Added Study of Empresa Eléctrica de Guatemala, Sociedad Anónima.[504]

378. There is no mention in the contract of a supposed second round of comments nor does it make reference to the operating rules that were supposedly agreed to.

379. The contract between Mr. Bastos and EEGSA, to which the CNEE was not a party and in which it had no involvement whatsoever, presents some peculiarities that deserve pointing out. On one hand, it includes a version of the operating rules, indicating that they "had been agreed to by the CNEE and EEGSA." However, the content and order of the rules included in Mr. Bastos' contract are materially different from the last version thereof that was discussed—without agreement—by the parties (see paragraph 368 above). Thus, in Mr. Bastos' contract, EEGSA did not include several of the rules that TGH now asserts were agreed upon by the parties on May 28.[505]

380. It must also be noted that, when Mr. Bastos signed his contract with EEGSA, both parties made clear their understanding that the Expert Commission would issue a first and only "Final Report." In point of fact, this contract provided for the payment of the balance of 70 percent of Mr. Bastos' fees upon delivery of the Expert Commission's Final Report.[506] The term "Final Report" is used in that

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504 Contract between Carlos Bastos and the CNEE, June 26, 2008, **Exhibit R-85**, clauses 3 and 4 (Bold emphasis in original, underlined emphasis added).

505 This includes Rule 1, which required that all meetings be held with a full quorum of the three Expert Commission members; Rule 2, which required that the first and last meeting be held in Guatemala City; Rule 3, which required that the members of the Expert Commission prepare a calendar and send it to the parties; Rule 4, which prohibited private communication addressed [to] two members of the Expert Commission and required that it always be addressed to all of them; and Rule 6, which prohibited third parties from attending different staff meetings. See Contract between Carlos Bastos and the CNEE, June 26, 2008, **Exhibit R-85**, clause 3. Contract between Carlos Bastos and the CNEE, June 26, 2008, **Exhibit R-84**, clause 3.

506 Contract between Carlos Bastos and EEGSA, July 26, 2008, **Exhibit R-84**, clause 3.

contract to refer to the pronouncement of the Expert Commission.[507] This was also consistent with Mr. Bastos' financial proposal, which stipulated that the work of the Expert Commission would be complete upon delivery of this pronouncement. Once this was done, Mr. Bastos remained, according to the agreement, available to the parties only on a personal basis to make clarifications or to perform other work:

> My performance […] shall run […] until the pronouncement of the Expert Commission communicated officially to the [CNEE] and the Distributor though a final report. However, I shall remain at your disposal for any additional clarification or task arising from such pronouncement, and which is necessary for the effective application thereof.[508]

(v) The reference to the proposal by Mr. Bastos in his contract with the CNEE does not reflect an agreement on Rule 12

381. In the absence of any evidence other than the word of its own witnesses Mr. Mate and Mr. Calleja, TGH attempts to prove that there was a supposed agreement on Rule 12 based on a double cross reference in the contract between the CNEE and Mr. Bastos to the financial proposal sent by him to the parties in relation to his role as president of the Expert Commission.[509]

> THIRD: FORM OF PAYMENT.
>
> EEGSA shall make a first payment to Carlos Manuel Bastos in the net amount of FIFTEEN THOUSAND U.S. DOLLARS (US$15,000.00) as of the signature of this contract. Such amount constitutes 30% of EEGSA's payment obligation.
>
> The remaining 70%, equal to the net amount of THIRTY-FIVE THOUSAND U.S. DOLLARS (US$35,000.00) shall be paid by EEGSA to the Third Member of the Expert Commission, once the latter pronounces itself in the Final Report, regarding the discrepancies for which it was constituted. (Bold emphasis in original).

507 *Ibid.*, clause 4, rule 6.

508 Letter from Carlos Bastos to Melvin Quijivix and Miguel Francisco Calleja, June 6, 2008, **Exhibit R-81** (Emphasis added).

509 Claimant's Memorial, para. 141.

382. Let us review this argument. According to TGH: Clause twenty-two (b) of the contract between the CNEE and Mr. Bastos included a "financial offer" of Mr. Bastos of June 6, 2008 as a document forming part of the contract[510] (*reference number 1*). In turn, the last paragraph of said financial proposal, which essentially described the fees to be earned for serving as the president of the Expert Commission, stipulated that his performance would be subject to some "Arbitration Rules that were delivered to me in a timely manner"[511] (*reference number 2*).

383. Thus, TGH tries to argue that the CNEE accepted the operating rules as valid in its contract with Mr. Bastos since the contract makes references to the financial proposal which, in turn, refers to some "arbitration rules" not attached and without further description. The argument lacks any weight, especially if we consider that both TGH and Mr. Bastos acknowledge that the reference to Mr. Bastos' financial proposal to the "Arbitration Rules that were delivered to me in a timely manner"[512] is actually a reference to the e-mail that Mr. Calleja sent to Mr. Bastos behind the CNEE's back, representing to him a false agreement between the parties regarding the operating rules as discussed in paragraphs 369 to 372 below.

384. It is important to clarify that Mr. Bastos' financial proposal, which was attached to the contract with the CNEE, was never studied nor discussed between the parties before it was sent by Mr. Bastos. Mr. Bastos expressly conceded this fact in the hearing in the Iberdrola case upon being questioned by the President of the Tribunal.[513] In fact, as Mr. Colom explains, in signing the contract with Mr.

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510 Contract between Carlos Bastos and the CNEE, June 26, 2008, **Exhibit R-85**, clause 22, para. b.

511 Letter from Carlos Bastos to Melvin Quijivix and Miguel Francisco Calleja, June 6, 2008, **Exhibit R-81**.

512 *Ibid.*, **Exhibit R-81**.

513 During the Hearing in the Iberdrola case, Mr. Bastos admitted that the letter in question, in which some "arbitration rules" were mentioned, had been a document that he himself prepared, without having discussed or negotiated it with the parties:

Bastos, he understood the reference to "financial offer" as merely the inclusion of the financial terms of Mr. Bastos' proposal[514] (the "amount of the bid" as it was referred to by Mr. Bastos in the hearing in the Iberdrola case). Mr. Colom would never have agreed to include the operating rules that had not been approved[515] and that would have violated the regulatory regime.

385. If one carefully reads Mr. Bastos' financial proposal, it is clear that, at the time of his proposal, he believed that the work of the Expert Commission would be complete upon delivery of its pronouncement. Once this was done, Mr. Bastos was only available to the parties on a personal basis in order to make clarifications or perform other tasks:

> My performance […] shall run […] until the pronouncement of the Expert Commission communicated officially to the National Electric Energy Commission and the Distributor though a final report. However, I shall remain at your disposal for any additional clarification or task arising from such pronouncement, and which is necessary for the effective application thereof.[516]

386. If it was Mr. Bastos' understanding that the mission of the Expert Commission included an entire second round of review and approval of a corrected study, he would have said so in his proposal as part of his duties.

> PRESIDENT ZULETA: When you say that you attached what you call the Rules of Arbitration, was there any negotiation over this proposal? That proposal was accepted just as you presented it, was there any discussion?
>
> MR. BASTOS: No, just as I presented it. Actually, we discussed the amount of the bid by telephone, and the letter, let's say, confirmed the formality.

Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 651:15-652:2.

514 Colom, **Appendix RWS-1**, paras. 135.

515 *Ibid.*, paras. 135-136.

516 Letter from Carlos Bastos to Melvin Quijivix and Miguel Francisco Calleja, June 6, 2008, **Exhibit R-81** (Emphasis added).

387. Finally and even more importantly, the CNEE's agreement with Mr. Bastos contains specific procedural rules that they must apply, with priority over any rule included by double reference.[517]

8. The Expert Commission's delay in delivering the opinion

388. As Mr. Bastos confirms in his statement, the agreed delivery date for the Expert Commission's pronouncement was set for mid-July 2008, specifically for July 18.[518] This would give the CNEE time to review the pronouncement and to approve or reject the Bates White study before August 1, the date that the new tariff schedule was to take effect.

389. However, after it was formed, the Expert Commission requested an extension of the deadline for its pronouncement, which was ultimately set for the week of July 24.[519] Clearly, this hindered the CNEE's review of the pronouncement by reducing the amount of available time prior to August 1, the date on which the new tariff schedule was to take effect. This situation was aggravated when the Expert Commission actually delivered its pronouncement on the discrepancies to the parties on Friday, July 25, 2008,[520] this being just three business days before the effective date of the new tariffs.

9. The Expert Commission's pronouncement confirmed that the tariff study of May 5 was not suitable for setting the tariffs

390. Without prejudice to the irregularities discussed in the preceding section, it is worth spending some time on the Expert Commission's pronouncement, in which it studied the discrepancies between the parties regarding the May 5 study. Contrary to TGH's assertions,[521] the Expert Commission issued a pronouncement

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517 Contract between Carlos Bastos and the CNEE, June 26, 2008, **Exhibit R-85**, clause 4.

518 Bastos, **Appendix CWS-1**, para. 9.

519 Giacchino, **Appendix CWS-4**, para. 39. See also Colom, **Appendix RWS-1**, para. 122; Bastos, **Appendix CWS-1**, para. 16.

520 Expert Commission Report, July 25, 2008, **Exhibit R-87**.

521 Claimant's Memorial, para. 158.

on most of the discrepancies (58 percent)—including on the most important ones—in favor of the CNEE.[522] Let us study the most relevant flaws in the Bates White study as identified by the Expert Commission.

a. Auditability of the models

391. One of the most important discrepancies submitted to the Expert Commission was the issue of whether or not the Bates White models were auditable. Despite having received criticism from the CNEE regarding the inauditability of the models for the stage reports and the March 31 study, Bates White in its May 5 study presented un-linked spreadsheets, pasted values, calculations and adjustment factors without justification, among other things.[523] Bates White attempted to justify its failure to present auditable models based upon limited computer capacity and the number of people simultaneously working on the study.[524]

392. In response to the CNEE's objections, Bates White presented the following diagram with its May 5 report, to show how the spreadsheets from the various stages of the study were interrelated.[525] The consultant maintained that the traceability requirement had thus been met:

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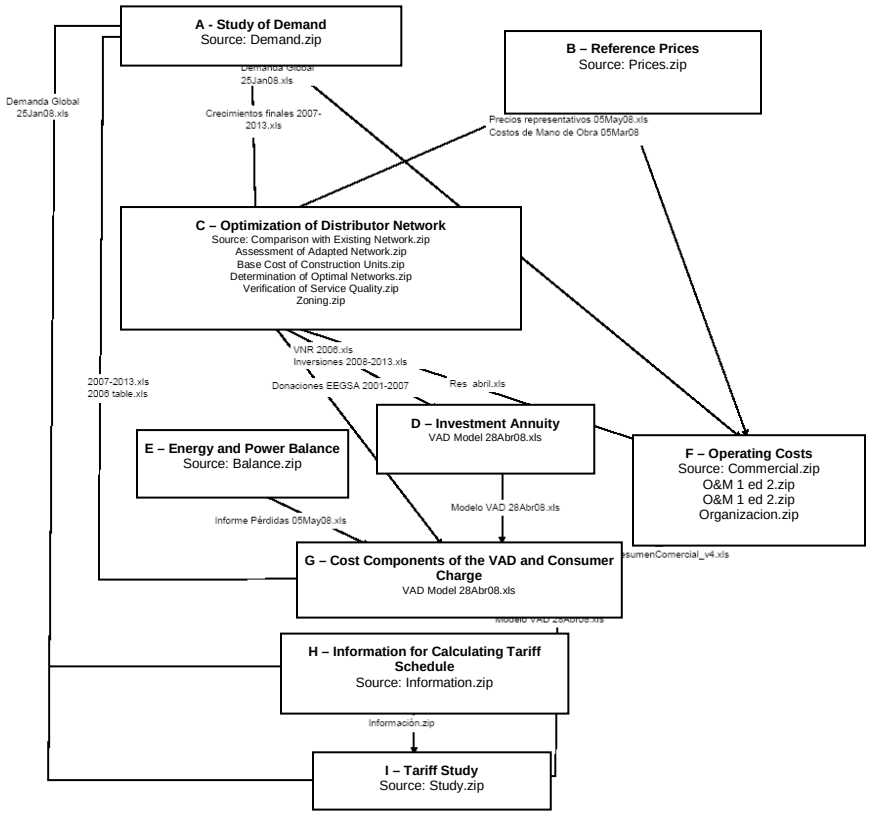
522 Of the 72 final decisions considered by the CNEE, 42 favored the CNEE's objections and 30 favored the Bates White tariff study. See **Appendix I**; Colom, **Appendix RWS-1**, para. 140.

523 CNEE Resolution 96-2008, May 15, 2008, **Exhibit R-71**, pg. 3; Damonte, **Appendix RER-2**, Section 4.1.1.

524 Letter from Leonardo Giacchino to Carlos Colom Bickford and Miguel Francisco Calleja, May 5, 2008, **Exhibit R-68**, pgs. 4-5.

525 *Ibid.*, pg. 5.



393. Clearly, this diagram did not allow the CNEE to reproduce calculations or make a sensitivity analysis of the model. Moreover, the complexity of this diagram did nothing more than emphasize how essential it was to have an interlinked electronic model. In addition, Bates White's persistence in presenting inauditable models obviously created serious doubts about the content of the information provided and the good faith of EEGSA's consultant.

394. The Expert Commission studied the arguments of each of the parties and unanimously, meaning even with the vote of the study's author, Mr. Giacchino, issued a pronouncement in favor of the CNEE.[526] This pronouncement was vital to the CNEE; as the only body liable (*accountable*) to third parties for setting the tariffs, it had to be able to justify the results of the study if questioned.[527]

526 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pgs. 15-17.

527 See Section III.B.2.b above.

b. Justification of efficient prices

395. With respect to the justification of efficient prices, the CNEE had observed that, with the May 5 Study EEGSA still: (i) had not submitted the national and international comparables necessary for the CNEE to be able to corroborate the efficiency of the prices included in the model; and (ii) had neither delivered a database containing systematized price information, nor a benchmarking study.[528] Bates White, for its part, argued that it was difficult to obtain comparables and that the data had been presented in an acceptable format.[529]

396. The Expert Commission studied both parties' arguments and again pronounced itself in favor of the CNEE. The Commission expressly indicated the inadmissibility of prices based on the distributor's actual prices. More importantly, the Commission expressed its concern regarding excess prices derived from agreements with local suppliers as well as possible transfers of profits involving related companies:

> **DISCREPANCY 3, STAGE "B" – REFERENCE PRICES […] The EC pronounces itself in favor of CNEE's objection, by majority vote**.[530]
>
> The controversy posed by CNEE is based on insufficient reference prices, especially in the requirement for two international prices, as set forth in the TOR.
>
> In the Tariff Study, the lack of more reference prices is justified by providing a broad explanation of how

528 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pgs. 33-35 and 40-41; *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statements of Leonardo Giacchino, October 19, 2009 and September 22, 2010, **Exhibit R-151**,, footnote 93 ("Documentation for the domestic prices is found in the invoices and the quotations sent on paper on July 28, 2008, whereas documentation for the international prices is found in the documents 'Prices Database' and 'Quotation"). See also CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pgs. 25-26; See Damonte, **Appendix RER-2**, section 4.1.2, "Reference Prices".

529 Bates White, Value-Added for Distribution Study for EEGSA - Stage B Report: Benchmark Prices, May 5, 2008, **Exhibit R-69**, paras. 27-29 and 40-43; see also Expert Commission Report, July 25, 2008, **Exhibit R-87**, pg. 163.

530 El experto Giacchino votó en disidencia sobre esta cuestión. Informe de la Comisión Pericial, 25 de julio de 2008, **Anexo R-87**, págs. 33-36 (Énfasis en el original).

> markets operate and the validity of comparing prices from other markets, to end up justifying that the only valid prices are those in the Guatemalan market. Besides, it is explained that in some cases, there are no more than two or three vendors, which is why these would be the values to be taken, justifying not including three quotes as required in the TOR.
>
> To resolve this controversy, it must be recalled that what is being analyzed is a Tariff Study based on the mechanism of maximum income permitted based on the costs of an efficient model company. This is a matter of extreme relevance since in the method followed, the study of the purchase expenses of the regulated company warrant a special chapter since the materials purchase mechanism may be a venue for the company to derive profits. […]
>
> In the analysis of the purchase process of a company that is not obligated to compete, it must be taken into account that, hypothetically, there may be agreements with the vendors of equipment and materials, in the sense of paying higher prices.
>
> The circumstance that the Guatemalan vendor market is limited may lead to situations of collusion and consequently, there is a greater possibility for prices to be greater. Therefore, there is more reason to consider that the international reference prices are mandatory.
>
> Consequently, the Tariff Study must complete the international price references and to perform the calculations of the VAD, it must adopt the lower of all prices informed for each material.[531]

397. With regard to the need for a database format that would allow prices presented to be audited, the Expert Commission also pronounced itself unanimously in favor of the CNEE.[532] With respect to the benchmarking study, the Expert Commission also pronounced itself unanimously in favor of the CNEE, requiring that Bates White conduct a comparison of costs, at least (i) with the model company which it

531 *Ibid.*, pg. 33-35 (Emphasis added).

532 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pg. 41.

constructed in the prior period's Tariff Study; (ii) with the model company constructed in the present tariff study; and (iii) with the actual company.[533]

c. Calculating the return on the depreciated capital base (VNR)

398. Another relevant discrepancy was the way in which the investor's return was to be calculated. As explained in Section I.B above, according to the regulatory framework and basic principles of economics, the investor's return is calculated based on the depreciated capital base, meaning the net depreciations already taken by the investor. Otherwise, the investor would be remunerated for capital that was not available to the Concession.[534] Thus, the Terms of Reference considered that EEGSA's capital base was depreciated by 50 percent.[535]

399. In calculating EEGSA's return, Bates White ignored the Terms of Reference and considered that the capital base to be used should be "gross" (that is, without taking into account the accumulated depreciations). As justification for not adhering to the Terms of Reference, the consultant indicated that it considered there to have been a "typographic error" in the formula included in the Terms of Reference.[536] This unusual position was not only contrary to the regulatory framework, the Terms of Reference and principles of basic economics;[537] it was

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533 *Ibid.*, pg. 164.

534 Damonte, **Appendix RER-2**, paras. 66-70.

535 Terms of Reference for the Performance of the Value-Added Distribution Study for Empresa Eléctrica de Guatemala, S.A., CNEE Resolution 124-2007, January 2008, **Exhibit R-53**, art. 8.3.

536 Bates White, Value-Added for Distribution Study for EEGSA - Stage D Report: Annuity of the Investment, February 29, 2008, reviewed on March 31, 2008, corrected on May 5, 2008, **Exhibit R-69**, pg. 11.

537 See para. 90 above. AE Kahn, *The Economics of Regulation, Principles and Institutions* (1996) Vol. 1, (excerpts) **Exhibit R-7**, pg. 32:

> The return to capital, in other words, has two parts: the return *of* the money capital invested over the estimated economic life of the investment and the return (interest and net profit) *on* the portion of investment that remains outstanding. The two are arithmetically linked, since according to the usual (but not universal) regulatory practice the size of the net investment, on which a return is permitted, depends at any given time on the aggregate amount of depreciation expense allowed in the previous years—that is, the amount of investment that remains depends on how much of it has

also inconsistent with the practice of Mr. Giacchino himself who, in 2003, when working for NERA, had calculated the return based on a capital base net of depreciations.[538]

400. If EEGSA believed that it was incorrect that its network was depreciated by 50 percent, as it had been stipulated in the Terms of Reference, EEGSA should have contested the Terms of Reference before they became final or at least have submitted information indicating the correct level of depreciation. In fact, the two other distributors, Deorsa and Deocsa, did so, and the CNEE adjusted their depreciation factor (from fifty percent, meaning a depreciation factor of 2, to forty-two percent, or a factor of 1.73).[539] However, in all their studies and despite the CNEE's comments, Bates White insisted on the return being calculated on the basis of the undepreciated capital base without offering an alternative to the depreciation level proposed in the Terms of Reference.[540] The insistence on obtaining a return based on the gross VNR, contrary to any basic principle and the practice of Mr. Giacchino himself, does nothing more than demonstrate the consultant's lack of credibility.

> been recouped by annual depreciation charges previously"); Asimismo, al describir los costos a ser recuperados por el inversor, el testigo de TGH, Lic. Giacchino, explica en su libro Fundamentals of Energy Regulation: "The cost of doing business will also include a fair return on the firm's undepreciated capital investment, which is called the rate base, including interest payments on short- and long-term debt and a return on equity capital.

538 Damonte, **Appendix RER-2**. It was also inconsistent with the writings of Mr. Giacchino. JA Lesser and LR Giacchino, *Fundamentals of Energy Regulation* (1st ed. 2007) (excerpts), **Exhibit R-34**, pgs. 56-57 and 99.

539 Moller, **Appendix RWS-2**, para. 50; Quantum and Union Fenosa, DEOCSA: Stage G Report: Cost Components of the VAD and the Charge to the Consumer, November 2008, **Exhibit R-98**, Section 4.1; Damonte, **Appendix RER-2**, para. 192.

540 Bates White, Value-Added for Distribution Study for EEGSA - Stage D Report, February 29, 2008, reviewed on March 31, 2008, **Exhibit R-61**, pgs. 4-9; Bates White, Value-Added for Distribution Study for EEGSA - Stage D Report: Annuity of the Investment, February 29, 2008, reviewed on March 31, 2008, corrected on May 5, 2008, **Exhibit R-69**, pgs. 6-12

401. This discrepancy was also brought to the Expert Commission which, as TGH admits,[541] confirmed that depreciations had to be taken into account in calculating the return.[542] Nonetheless, as explained in greater detail below, even though the Expert Commission's mandate was restricted to pronouncing on whether or not the consultant's study conformed to the Terms of Reference, [543] it exceeded the scope of its authority and proposed a formula for the recuperation of capital as an alternative to the formula set forth in the Terms of Reference. Even Mr. Bastos himself affirmed in his witness statement in the Iberdrola arbitration (excluded from his statement in the present arbitration) that the Expert Commission had decided to far exceed said mandate.[544] On top of exceeding its mandate, it is worth mentioning that this formula cannot be applied as it contains basic technical errors, as Mr. Damonte explains (see Section V.B.1 below)[545] In any case, what is

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541 Claimant's Memorial, para. 161.

542 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pgs. 104-106.

543 Section III.B.2.e above.

544 *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statement of Carlos Bastos, May13, 2009, **Exhibit R-102**, para. 44 :

> A simple solution which the Expert Commission could have made use of, would have been to say **whether or not** the consultant, in view of the regulatory model and current regulations, had justifiably departed from the guidelines contained in the TR [Terms of Reference]; thereby concluding the controversy by acknowledging that one of the parties was right. However, proceeding in this way, it would have resulted in a false solution as this would not have shown the consultant how it should correct the study and therefore stalled the procedure for approving the new tariff. As a all three experts agreed, our duty as experts was to make a determination on the content of the discrepancies and decide if what the consultant had done was right or, otherwise, to indicate to the latter how it should redo the study in the particular area that we were examining.

(Emphasis added).

This position was later confirmed by the experts in the introductory section of their pronouncement:

> For that reason, the Expert Commission shall resolve the discrepancies considering the positions of the Parties, or adopting a third position besides those of the Parties, always to the best of the knowledge and understanding of its members.

545 Damonte, **Appendix RER-2**, Chapter 6.2.

important is that the Expert Commission also concluded that Bates Whites' position was incorrect.

d. Non-optimal Construction Units

402. The CNEE had a great many comments regarding the construction units used to create the model company. The CNEE considered that many of the construction units were not optimal, meaning that their cost was not justified for the Guatemalan market or their quantity was excessive for the network.[546] This overvaluation of construction units substantially increased the VNR (capital base) used in calculating the tariffs. Given the quantity and technical complexity of these issues, we will next mention a few examples.

(i) Underground networks

403. As previously mentioned, Bates White constructed a model company in which all of the existing aerial networks were replaced by underground networks, which cost far more. Moreover, in its model company, Bates White installed these networks in concrete pipes,[547] instead of burying them directly, which is even done in developed countries such as Canada.[548] As Mr. Damonte explains, such pipeline construction is extremely costly, and therefore economically unjustifiable except in cases in which it is impossible to break ground to make repairs, such as under protected historical sites or major road intersections. Most egregious, however, is that no known EEGSA work plan as of that date even contemplated replacing the aerial networks with underground ones. Therefore, the additional cost would be added to the tariff without the infrastructure being improved for the consumer. Although Bates White, in line with the CNEE's comments on its March 31 study, had excluded a certain portion of the underground networks in

546 *Ibid.*, Chapter 4.1.3.

547 The pipes proposed by Bates White are described in its Value-Added for Distribution Study for EEGSA - Stage C Report: Network Optimization, May 5, 2008, **Exhibit R-69**, pg. 81, paras. c and d. They comprise 120 psi, 4" diameter PVC pipes. One cable per pipe is installed, and these pipes are connected to underground chambers.

548 Damonte, **Appendix RER-2**, para. 178.

the May 5 study, the CNEE decided that its comments were not complied with until all of the underground networks, except for those existing in the current network, were removed.

404. After studying both parties' arguments regarding this matter, the Expert Commission unanimously pronounced in favor of the CNEE, requiring that Bates White remove all of the underground networks as requested by the CNEE in order to fully comply with the opinion.[549] More importantly still, the Expert Commission confirmed that the inclusion of these costs had generated extraordinary profits for EEGSA:

> The inclusion of these underground grids in the VNR, which finally leads to the VAD, would give the company an extraordinary income if the underground facilities are not performed and the company remains with the aerial facilities.[550]

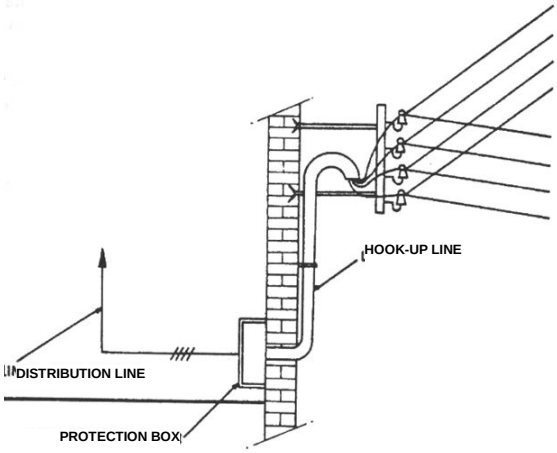
405. The unjustified insistence of EEGSA's consultant on including underground networks that did not exist in the current network and that had been repeatedly rejected is a clear example of a lack of good faith on the part of Bates White.

(ii) Low-voltage hook-ups

406. As the following figure illustrates, a hook-up is the connection line that runs from the distribution network to the house.

549 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pg. 83.

550 *Ibid.*, **Exhibit R-87**, pg. 83.



407. In its model, Bates White used hook-ups with longer lengths and larger calibers than necessary, which were therefore not optimal. In particular, the consultant over-dimensioned the units and thereby doubled the capacity of the hook-ups for some 300,000 users,[551] thereby increasing the unit costs of these units. This issue, along with the irregularities in the reference prices applied to these units, was studied by the Expert Commission. The Commission again pronounced itself [*se pronunció*] in favor of the CNEE.[552]

(iii) Number of outlets per transformer center

408. The following photograph shows a transformer center. This installation has, among other things, a transformer that makes it possible to convert medium voltage to low voltage. Each transformer, in turn, has various outlets connecting the transformer to the network:

551 Damonte, **Appendix RER-2**, para. 149-153.

552 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pg. 94.

409. The number of outlets for each transformer is crucial in determining the value of the networks and of the transformers.[553] In its model, Bates White proposed that each transformation center have two outlets. As Mr. Damonte explains, with four outlets, it is possible to cover more blocks and save money since a single, more powerful transformer is more economical than two, less powerful ones.[554] Therefore, the CNEE objected to the Bates White model on the grounds that it was not optimal.[555] The Expert Commission accepted the CNEE's concern and ordered Bates White to propose other alternatives to make it possible to select the most optimal.[556]

410. Although these examples only represent a small portion of the 58 percent of discrepancies that were confirmed as being overvalued in the Bates White model, they serve to illustrate that in no way could the CNEE set tariffs based on this tariff study. With only a few days before the due date for setting the new tariff

553 Damonte, **Appendix RER-2**, paras. 142-146.

554 *Ibid.*

555 CNEE Resolution 63-2008, April 11, 2008, **Exhibit R-63**, pgs. 9-10; CNEE Resolution 96-2008, May 15, 2008, **Exhibit R-71**, pgs. 9-10.

556 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pgs. 78-79.

schedule, the Expert Commission confirmed the inadmissibility of most of the study.

10. The dissolution of the Expert Commission

411. TGH argues that once the Expert Commission issued its pronouncement, Bates White was to revise the study and resubmit it to the Expert Commission for approval pursuant to Rule 12.[557] As explained earlier,[558] there was never an agreement between the CNEE and EEGSA regarding this rule, which moreover is contrary to the regulatory framework,[559] and TGH has not been able to provide any evidence to the contrary. Therefore, once the Expert Commission's pronouncement on the discrepancies was received and the duties assigned to it in the Notarized Act of Appointment were completed, the CNEE proceeded on July 25, 2008 to dissolve the Expert Commission.[560]

412. Contrary to TGH's arguments, this conduct was not illegal or arbitrary,[561] but rather is plainly consistent with LGE Article 75, which established that the Expert Commission is only to pronounce itself on the discrepancies. It is also consistent with the contract signed between EEGSA itself and Mr. Bastos, which stipulated payment of his final fee upon submission of this report.[562] As Dr. Aguilar explains:

> The dissolution of the EXPERT COMMISSION occurs by "**operation of law**," following the exhaustion or fulfillment of the function for which it was constituted, which, as previously indicated, may not extended beyond sixty days from the time it was constituted. Consequently, it was not against the law for the CNEE

557 Claimant's Memorial, para 167.

558 See Section III.F.7.c above.

559 Pursuant to Articles 4(c) and 63 of the LGE, norms not included in the LGE or the RLGE, could not be incorporated into the tariff review process. LGE, **Exhibit R-8**, arts. 4(c) and 63.

560 CNEE Resolution GJ-Judicial Decision-3121, July 25, 2008, **Exhibit R-86**; Colom, **Appendix RWS-1**, para. 138.

561 Claimant's Memorial, para 167.

562 See para 419 above.

> to have ordered the dissolution of the Expert Commission, given that such decision was based on the provisions of LGE Articles 75 and RLGE 98BIS;
>
> The CNEE did not unilaterally dissolve the EXPERT COMMISSION, as stated by the expert Alegría Toruño, because said dissolution occurred pursuant to the "**operation of law**" following the fulfillment of its function, and after the lapse of the sixty-day term established in the LGE and RLGE.[563]

413. Upon providing notice of the dissolution of the Expert Commission, the CNEE informed experts Jean Riubrugent and Carlos Bastos that "the activities relating to the execution" of their respective contracts had concluded with the submission of the pronouncement and that it would proceed to process payment for their respective expert fees.[564]

414. For its part, EEGSA did not pay Mr. Bastos the balance owed as was stipulated in his original contract upon submission of the "Final Report" (in other words, the pronouncement, see paragraph 377 above). Instead, EEGSA withheld the payment and conditioned it on the signing of a favorable addendum,[565] in which it was recorded that payment was to take place after the expert issued the note of "approval" of the July 28 study discussed below in Section III.F.12 below.[566]

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563 Aguilar, **Apéndice RER-3**, párrs. 56-57.

564 The proof of service along with delivery of this document to Carlos Bastos was received at 1:40 p.m. on Monday, July 28. Jean Riubrugent received proof of service at 1:45 p.m. that same day, July 28. Proof of Service issued by the CNEE, July 28, 2008, **Exhibit R-92**.

565 Agreement between Carlos Bastos and EEGSA, June 26, 2008, **Exhibit R-84**, clause 3. Modification of the Contract between Carlos Bastos and EEGSA, for the Retribution of the Third Member of the Expert Commission, September 3, 2008, **Exhibit R-302**.

566 The original contract between Mr. Bastos and EEGSA provided for payment of 70 percent of his fees upon submission of the Final Report of the Expert Commission. Contract between Carlos Bastos and EEGSA, June 26, 2008, **Exhibit R-84**, clause three. The term "Final Report" is used in this agreement in referring to the opinion of the Expert Commission, see **Exhibit R-84**, clause four, Rule 6, and, consistent with this, Mr. Bastos has explained that the "Final Report" of the Expert Commission was delivered on July 25, 2008. *Iberdrola Energía, S.A. v. the Republic of Guatemala* (ICSID Case No. ARB/09/05), Witness Statement of Carlos Bastos, May 13, 2009, **Exhibit R-102**, para. 49. What is surprising is that EEGSA did not pay Mr. Bastos the balance owed after said Final Report was issued on July 25, but rather made him sign an *addendum* as a condition for payment stipulating that the outstanding balance would be paid in full once "the Expert Commission had been reinstated" and when procedures subsequent to the Final Report, not

11. The CNEE set tariffs based on the Sigla study in view of the Expert Commission's opinion

415. Due to the late delivery of the pronouncement of the Expert Commission,[567] the CNEE had only three business days from its receipt on Friday, July 25, 2008 to analyze it and set the tariffs. Considering that the new tariff schedule had to take effect on August 1, it therefore had to be published in the Diario de Centroamérica by Thursday, July 31 at the latest.[568]

416. Given these circumstances, the Tariff Division team worked vigorously that weekend in order to report its conclusions to the CNEE Board of Directors first thing on Monday, July 28.[569] That Monday, the Board of Directors was informed that the Expert Commission had found in favor of the CNEE in more than 58 percent of cases,[570] and that this favorable percentage included key discrepancies such as the issues of model traceability/auditability and absence of price justification, among other things.[571] Faced with this scenario, the CNEE concluded that the May 5 Bates White study could not serve as a basis for setting the tariff schedule.[572]

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previously mentioned in the agreement, had been carried out. In exchange for signing that *addendum* (surely drafted by EEGSA, judging from the reproaches regarding the CNEE's conduct and legal interpretations regarding the mission of the Expert Commission it contains), Mr. Bastos received an advance for a substantial part of what was owed to him. Modification of the Contract between Carlos Bastos and EEGSA, for the Payment of the Third Member of the Expert Commission, September 3, 2008, **Exhibit C-302**, clause 2. Conscious of this irregularity as pointed out by Guatemala in the *Iberdrola* arbitration, in the present arbitration, Mr. Bastos has eliminated each and every one of the multiple mentions to the "Final Report" of July 25, which he now refers to simply as the "Report."

567 See para. 391.

568 Colom, **Appendix RWS-1**, para. 139.

569 See Agenda of meetings held by the tariffs division of CNEE between Friday 25 and Monday 28, June 25-28, 2008, **Exhibit R-88**; Colom, **Appendix RWS-1**, para 139.

570 Of the 72 decisions finally considered by the CNEE, 42 favored the CNEE's objections and 30 favored the Bates White tariff study (see **Appendix R-I**). As previously explained (see the footnote in paragraph 390), the parties differed on the manner in which to count the opinions. Aside from these differences, the importance is that the Expert Commission confirmed that the CNEE was correct in more than 50 percent of the discrepancies, including the most relevant, such as the issue of traceability.

571 Expert Commission Report, July 25, 2008, **Exhibit R-87**, pgs. 15-17, 33-34, 40-41.

572 Colom, **Appendix RWS-1**, para. 145.

417. Thus, the CNEE analyzed the available options.[573] One possibility was to correct the study. However, given the magnitude of comments confirmed by the Expert Commission, in terms of both quantity and substance, it was impossible to correct the study within the remaining available time.[574] Moreover, certain pronouncements by the Expert Commission required a greater degree of information (comparable national and international prices, optimal configurations, the installation of transformers, etc.). Even after receiving this information, it would have to be analyzed and incorporated into the model. This would take weeks. Finally and most importantly, because the Bates White model was not "*linked*," it was impossible to incorporate changes and make these adjustments.[575] Under these circumstances, the CNEE decided that the most reasonable option would be to use the tariff study prepared by the Sigla consultant to set the tariffs.[576] Thus, on that same day, the 28th, the CNEE's Department of Tariff Studies began analyzing the latest version of the Sigla study, which would be discussed by the Board of Directors the next day. This was a relatively simple task given that the CNEE had reviewed all of the stage reports and final reports submitted by Sigla since 2007[577] which had also been reviewed by other consultants.[578] It is important to clarify that Sigla also provided the CNEE with

573 Colom, **Appendix RWS-1**, para. 145.

574 *Ibid.*, paras 145-147.

575 *Ibid.*, paras 89 and 146.

576 *Ibid.*, para. 147.

577 See, e.g., Email from Gerardo Manhard a Marcela Paláez, RE: EEGSA - Specialized Consultant Info - Reference Prices, December 20, 2007, **Exhibit R-50** (asking that Gerardo Manhard send an Excel file to be able to "compare the unit prices calculated by SIGLA and those used in the previous study"). CNEE, Department of Tariff Studies, Technical Opinions on Tariff Schedules for Users not Affected by EEGSA's Social Tariff and the Tariff Schedule for EEGSA's Social Tariff for the five-year period of 2008-2013, **Exhibit R-93**, pg. 2; CNEE, Legal Department, GJ-Opinion-1287 and GJ-Opinion-12-88. Base Terms for the EEGSA Non-social Tariff and Base Terms for the EEGSA Social Tariff, 29 July 2008, **Exhibit R-94**, pg. 2.

578 Colom, **Appendix RWS-1**, para 150.

supporting tariff studies for the reviews of the two other large distributors, Deorsa and Deocsa.[579]

418. That same afternoon of the 28th, however, the CNEE received a new version of the Bates White tariff study that supposedly corrected the May 5 study and complied with the pronouncements of the Expert Commission. The VNR from this study still amounted to US$ 1,053 million. The speed with which all of the pronouncements were supposedly incorporated attracted the CNEE's attention.[580] Even if – as TGH alleges – the Bates White technical team was receiving information from Mr. Giacchino while the Expert Commission was deliberating.[581]

419. After a preliminary review by the CNEE's Department of Tariff Studies, it was confirmed, for example, that the models were still not linked nor completely supported, and the database remained an Excel file with no kind of automatization to allow quick access to the source of efficient prices.[582] Auditing the model remained impossible. Moreover, the CNEE had by now lost confidence in the study conducted by Bates White, who had been unwilling to submit a transparent report for over seven months. For this reason, and because there was no legal authority under the LGE and the RGLE to review the distributor's study for a third time, the CNEE decided to proceed with the plan to analyze the Sigla tariff study for approval.[583] Later on, two external expert reports commissioned by the CNEE to analyze whether Bates White July 28 study complied with the Expert Commission's pronouncement confirmed that very many pronouncements were never incorporated (see Section III.F.13 below).

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579 These backup studies by the CNEE's consultant were not necessary during these reviews because the studies submitted by the distributor's consultant complied with the applicable Terms of Reference. See Colom, **Appendix RWS-1**, para. 50; see also Moller, **Appendix RWS-2**, paras. 42-50.

580 Colom, **Appendix RWS-1**, para. 148.

581 Claimant's Memorial, para 168.

582 Colom, **Appendix RWS-1**, para. 149.

583 *Ibid.*

420. Thus, on Tuesday, July 29, the Tariff Division submitted to the Board of Directors an analysis of the Sigla study based on two legal opinions and two technical opinions.[584] The CNEE then issued CNEE Resolution 144-2008 approving the Sigla study in order to set the tariff schedule.[585] Proceeding with the legal procedure, on July 30, 2008, the CNEE approved the new tariff schedules for EEGSA for the five-year period of 2008-2013, which would be published the following day, July 31,[586] and would take effect on August 1, thereby meeting all deadlines set by the LGE. As explained in Section III.F.14 below, the tariffs set on the basis of the Sigla study are reasonable in that they reflect the efficient cost of the electricity distribution service.

12. Letters by Mr. Giacchino and Mr. Bastos dated August 1, 2008

421. Despite the dissolution of the Expert Commission, Mr. Giacchino insisted on obtaining approval for his July 28 study. The irrelevance of such efforts was indicated to him by Mr. Bastos in an e-mail sent to Mr. Giacchino that same day, July 28:

> Leo, I'm forwarding this e-mail for your information. I think this is an obstacle to what we have talked about and I don't want you to embark on a senseless task. I

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584 CNEE, CNEE, Department of Tariff, Technical Opinions on the Tariff Structure for the Users not affecting EEGSA's Tariff Sheets of the Social Tariff and EEGSA's Social Fee for the five years 2008-2013, July 29, 2008, **Exhibit R-93**, pg. 15:

> **Recommendations**
>
> Based on the technical analysis of the above we recommended, with the prior relevant legal analysis, the repeal of resolutions CNEE-66-2003, CNEE-67-2003 and CNEE-69-2008; and the issuing of the base rate schedules […] in accordance with the results obtained from the Study performed by the Business Association [Sigla] and approved by the CNEE through Resolution CNEE-144-2008.

CNEE, Legal Department, GJ- Opinion-1287 and GJ-Opinion-12-88. Base Terms for the EEGSA Non-social Tariff and Base Terms for the EEGSA Social Tariff, 29 July 2008, **Exhibit R-94**.

585 CNEE Resolution 144-2008, July 29, 2008, **Exhibit R-95**.

586 CNEE Resolution 145-2008, July 30, 2008 published in the Diario de Centro América on July 31, 2008, **Exhibit C-273**, and CNEE Resolution 146-2008, July 30, 2008, published in the Diario de Centro América on July 31, 2008, **Exhibit C-271**.

> think you should coordinate your work with Bates White with EEGSA. Let me know if you need any help.[587]

422. However, Mr. Giacchino insisted and, accepting the "help" offered to him by Mr. Bastos in his e-mail, Bates White paid for Mr. Bastos to travel to Washington DC to meet in the offices of EEGSA's consultant to review his own July 28 study.[588] This insistence was not by chance. Mr. Giacchino had a contractual obligation to EEGSA to "present and defend the Tariff Study, and in general pursue approval thereof, until final approval thereto is given by the CNEE."[589] Accordingly, Bates White had an economic interest in such approval given that, in the event that the study was not approved, EEGSA could refuse to pay its fees.[590]

423. Thus, according to TGH,[591] on July 30 and 31 (interrupted on various occasions by attempts to summon Mr. Riubrugent as well as several exchanges with EEGSA), Mr. Giacchino "reviewed" with Mr. Bastos how the Expert Commission's pronouncement had been incorporated in his own study. As a result of this review, on August 1, both Mr. Giacchino and Mr. Bastos sent letters to the CNEE, confirming that the July 28 study incorporated all of the pronouncements. Given the volume and complexity of the model (according to Mr. Bastos, it was 137 Excel spreadsheets and more than one thousand pages),[592] it is clear that Mr. Bastos did not have time to review the model, but rather was limited to listening to and relying on Mr. Giacchino's explanations. In fact, he himself made this clear

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587 Email from Carlos Bastos to Leonardo Giacchino, July 28, 2008, **Exhibit C-250**.

588 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 631:17-632:1 ("Q: On what date did you meet with Leonardo Giacchino? – A: Between 30 and 31 July. – Q: And where did you meet? – A: Here in Washington. – Q: And who paid for the trip for this visit? – A: Bates and White").

589 Contract between EEGSA and Bates White LLC for performance of the 2008-2013 Tariff Study, January 23, 2008, **Exhibit R-55**, clause 5, number 12, Obligations of the Consultant Firm.

590 *Ibid.*, clause four, letter D, Invoicing and Form of Payment.

591 Claimant's Memorial, para. 178.

592 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 635:3-636:4.

when he sent his letter to the CNEE "approving" the study of the 28th and confirming that it was impossible for him to go further:

> The size and complexity of the model in itself prevent me from following in detail all the steps in the calculation that was performed. However, it is possible to state that the results of the VAD calculated in your study are calculated with a model that incorporates the decisions made by the Expert Commission[593]

424. As this text illustrates, Mr. Bastos only confirmed that pronouncements were incorporated into the model, he does not know how those incorporations were accomplished or the veracity of the calculations. It is important also to note that, as can be seen in Annex 4 of his letter containing all the reviewed pronouncements, Mr. Bastos had not noticed that he failed to review all of the pronouncements,[594] nor that in some cases, the July 28 study indicated that certain pronouncements stated to be in EEGSA's favor were in reality issued in favor of CNEE.[595]

425. In addition, as mentioned earlier,[596] some of the pronouncements of the Expert Commission would require more information in order to (i) to confirm that the prices submitted were efficient or (ii) analyze whether more optimal construction

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593 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 635:3-9 (Emphasis added); see also Letter from Carlos Bastos to Carlos Colom Bickford and Luis Maté, August 1, 2008, **Exhibit R-97**.

594 See Letter from Carlos Bastos to Carlos Colom Bickford and Luis Maté, August 1, 2008, **Exhibit R-97**, pg. 4; Chart of Corrections Required by Expert Commission (attached as Exhibit 4 to the Letter from Carlos Bastos to Carlos Colom Bickford and Luis Maté, August 1, 2008), **Exhibit C-289**; Bastos, **Exhibit CWS-1**, paras. 35-36:

> I reviewed the corrected Bates White tariff study and confirmed that it had fully incorporated the decisions of the Expert Commission […]For each discrepancy for which a correction was required, I have noted where in the Excel spreadsheets the correction had been incorporated by Bates White into its model.

(Emphasis added).

595 The "Chart of Corrections Required by Expert Commission" fails to include three discrepancies – C.9.b., C.4, and E.4 – each of which were decided in favor of the CNEE by the Expert Commission. *Ibid.*

596 See Section III.F.9 above.

units existed than those proposed. It is clear that Mr. Bastos did not analyze these issues. Furthermore, once all the changes were incorporated, the model was still to be optimized. At no point does Mr. Bastos mention whether he was able to confirm that such optimization was performed. It is clear that in two days, he did not do so. Examined during the hearing in the Iberdrola case regarding the nature of his "review," Mr. Bastos explained the true reach of his work:

> R. The last paragraph of the letter says: The size and complexity of the model in itself prevent me from following in detail all the steps in the calculation that was performed. However, it is possible to state that the results of the VAD calculated in your study is are calculated with a model that incorporates the decisions made by the Expert Commission. […] For me it was impossible to corroborate all of the stages of calculation of the model.[597]

426. For these reasons, the final value of the July 28 study was not, and could not be, validated for approval by Mr. Bastos, which was in any event carried out in his "personal capacity" and not on behalf of the Expert Commission.[598] In addition, the approval of Mr. Giacchino, as both judge and party, with a contractual obligation to defend the study, does not merit further consideration.

427. To claim, as TGH does, that the approval by two members of the Expert Commission was "binding" upon the CNEE and obligate it to set the tariffs based on the July 28 study lacks any merit.

13. The report of July 28 did not incorporate the totality of the Expert Commission pronouncements

428. In addition to its preliminary review prior to establishing the tariffs based on the aforementioned Sigla study, the CNEE later submitted the Bates White July 28 study for review by the independent consultant firm, Mercados Energéticos.

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597 Transcript of the final hearing in ICSID Case No. ARB/09/5 (excerpts), **Exhibit R-140**, Day Two, Bastos, 635:3-636:4 (Emphasis added).

598 *Ibid.*, Day Two, Bastos, 580:22-581-2 ("And I did the análisis of the corrections made by the consultant in a personal capacity.").

Mercados Energéticos concluded that the July 28 study did not incorporate the totality of pronouncements issued by the Expert Commission.[599]

429. With respect to the models, Mercados Energéticos concluded that they were neither traceable nor auditable, and lacked the required support:

> "With respect to the models, it may be concluded that EEGSA has submitted a set of Excel spreadsheets grouped in folders called 'models', which have the following problems: […]
>
> The set of Excel spreadsheets submitted does not constitute a model and therefore does not permit an orderly and systematic review that would make it possible to corroborate and reproduce all the calculations made.
>
> […]
>
> The Study submitted by EEGSA, on July 28, 2008, is factually insusceptible of verification and correction, in two days, in accordance with the Terms of Reference prepared by the CNEE and the VAD of the EC, due to the fact that the aforementioned technical inconsistencies make it incalculable. Therefore it can consequently be concluded that this Study is not suitable, or conclusive.[600]

430. Even in those cases where Bates White gave its assurance that it worked to "link and document" the model, Mercados Energéticos observed that:

> It is worth noting in the first place that with respect to the links, the scheme presented in Annex D of Stage C in the EEGSA Consultant Report, which provides a description of the support file for the tariff study, bears no relation to the calculation spreadsheets and support

599 Mercados Energéticos Consultant Firm, "Review of EEGSA's Value-Added for Distribution Study in Relation to the Expert Commission Opinion," July 2009, **Exhibit R-103**, pgs. 5-6 and 13. See also Witness Statement of Alejandro Alberto Arnau Sarmiento, Mariana Álvarez Guerrero and Edgardo Leandro Torres of Mercados Energéticos S.A., 24 January 2012 (hereinafter ***Mercados Energéticos***), **Appendix RWS-3.**

600 Mercados Energéticos Consultant Firm, "Review of EEGSA's Value-Added for Distribution Study in Relation to the Expert Commission Opinion," July 2009, **Exhibit R-103**, pgs. 5 and 13. See also Mercados Energéticos, **Appendix RWS-3**.

> files that were actually sent. The files are comprised of calculation spreadsheets with some relation to one another, but do not form an integrated and ordered model that allows for its adequate traceability. The organization of the files and directories bears no apparent logic in relation to the different stages of the Tariff Study.
>
> Additionally, the review found values that were copy-pasted, and formulas that cannot be understood.
>
> It was not possible to find calculation files that reflected the numerical assessment to economically justify the adapted technology in the revised version.
>
> With respect to the documentation, no documentation was found to justify and support the calculations related to the selection of the chosen optimal technologies, either within the Stage C Report, or the support files.[601]

431. With respect to the Expert Commission's pronouncement ordering that the international price references be completed and that the lowest price be used in carrying out the calculations, Mercados Energéticos confirmed that there still remained irregularities in the reference prices. Among the irregularities was the lack of supporting documentation, which made it impossible to "ensure that the price adopted for the VAD components constituted the lowest of the reported prices."[602] As for the remainder of the study, Mercados Energéticos concluded that it did not reflect 64 percent of the pronouncements of the Expert Commission (25 out of 39 issues, most of which corresponded to opinions favoring the CNEE).[603] It further concluded that the pronouncements relating to discrepancies C.3.c; C.3.f and C.4, decided in favor of the CNEE, were misrepresented (that is, even though these were decided in the CNEE's favor, Bates White presented them as opinions in favor of EEGSA and therefore did not make the required changes);

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601 Mercados Energéticos Consultant Firm, "Review of EEGSA's Value-Added for Distribution Study in Relation to the Expert Commission Opinion," July 2009, **Exhibit R-103**, pg. 28. See also Mercados Energéticos, **Appendix RWS-3**.

602 Mercados Energéticos Consultant Firm, "Review of EEGSA's Value-Added for Distribution Study in Relation to the Expert Commission Opinion," July 2009, **Exhibit R-103**, pgs. 16 and 17. See also Mercados Energéticos, **Appendix RWS-3**.

603 *Ibid*, **Exhibit R-103**, pgs. 6 and 12; Mercados Energéticos, **Appendix RWS-3**.

even in cases in which the Expert Commission issued a pronouncement against the CNEE, the study discovered that the consultant made changes that were not required.[604]

432. The failure to incorporate all of the pronouncements was also confirmed by Mr. Damonte, who, after including all possible pronouncements (excluding those for which additional information was required and without being able to optimize the Bates White model), obtained a VNR figure of US$ 629 million instead of the US$ 1,053 million estimated by Bates White in its July 28 report..[605]

433. TGH, with support from its expert Mr. Kaczmarek,[606] principally tries to justify the substantial increase in the 2003 VNR and those proposed in the July 28 study based on inflation. Besides the fact that not all of the elements included in the inflation index used by Kaczmarek are applicable to Guatemala or to EEGSA, but are rather applicable to the United States,[607] and that the analysis assumes that the 2003 values are efficient,[608] the most important issue is that this analysis completely disregards the principle foundations of the model company system. The model company system does not take the preceding tariff base and adjust it for inflation. The model system constructs a new company (a new tariff base) every five years and tries to make it more efficient.[609]

434. As Kaczmarek well indicates, the methodology used in the 2003 study was based on the actual company, adjusted for some efficiencies (*SER top-down approach*). That methodology was set aside in 2008 and was replaced by the *bottom-up approach* that creates a model company from scratch (*green field*). The *top-down*

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604 *Ibid*, **Exhibit R-103**, pgs. 6 and 12; Mercados Energéticos, **Appendix RWS-3**.

605 Damonte, **Appendix RER-2**, para 173.

606 Kaczmarek, **Appendix CER-2**, paras. 104-106.

607 Damonte, **Appendix RER-2**, para. 224.

608 As already explained by Damonte in his report, aside from the fact that adjustment for inflation are not an acceptable approach in the model company methodology, it is important to note that there is no evidence showing that the VNR in the 2003 NERA study was efficient. Giacchino himself recognizes in his witness statement that the study contained substantial errors. *Ibid.*, chapter 7.2.

609 *Ibid.*, chapter 7.2.

system necessarily replicates some of the basic inefficiencies of the actual company's structure. In the *bottom-up* system, on the other hand, these inefficiencies are not taken into consideration since a model company is constructed from scratch.[610] For this reason, by creating an efficient model company completely from scratch (disregarding all inefficiency reflected in the previous tariff review), one would expect that the base values and updated values would be less than the previous tariff base indexed for inflation.[611]

14. The tariffs set by the CNEE are reasonable in that they reflect the efficient cost for electricity distribution

435. In addition to the previously described issues that prompted the CNEE to declare the Bates White study inadmissible and set tariffs based on the Sigla study, it is important to note that these tariffs were established using technical criteria in accordance with the procedure and principles of the LGE and the RLGE. The tariffs were calculated by an independent, prequalified consultant who had previously and satisfactorily worked for EEGSA.[612] More importantly, Sigla based its calculations on the Terms of Reference timely accepted by EEGSA.

436. TGH claims in its Claimant's Memorial that it did not participate in the preparation of the Sigla study.[613] This argument is unfounded, precisely because this involvement is not provided for in the LGE or the RLGE. The regulatory framework provides for using the tariff study of the CNEE consultant as a tool of last resort, to be used only if (i) the distributor's consultant refuses to "implement" the corrections to the study; and (ii) the study was not suitable for

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610 Kaczmarek, **Appendix CER-2**, para. 98; see also Damonte, **Appendix RER-2**, paras. 37-38.

611 Damonte, **Appendix RER-2**, paras. 35-43. As Damonte explains, we note that both methods are used by different countries and are equally valid. For example, the Top Down approach has more been used in the past in Argentina, Chile, Peru, El Salvador, and Guatemala. The Bottom Up approach has been used by Argentina, Chile, Peru, El Salvador, Uruguay, and Guatemala. The changes in methodology took place because regulators were searching for safer methodologies, based on economic theory and mathematical tools of optimization an above all capable of producing reproducible results.

612 See para. 324 above.

613 Claimant's Memorial, para. 197.

modification. Likewise, TGH's allegation that commissioning an independent study from Sigla at the start of the tariff review is evidence of the CNEE's pre-established intention to reject the EEGSA study cannot be taken seriously.[614] As explained earlier, the CNEE commissioned independent studies for the tariff reviews of EEGSA, Deorsa, and Deocsa to serve as a *benchmark* when reviewing these distributors' studies, in accordance with recommendations of the Chilean expert, Mr. Bernstein. In the case of Deorsa and Deocsa, because these companies adhered to legal procedure and to the applicable Terms of Reference, the CNEE had no need to use the Sigla study to set their respective tariffs. To argue that the CNEE was only to commission its supporting study once the distributor's study was rejected, meaning once the deadline for publishing the new tariff schedule was to expire, is contrary to all logic. Not only would this entail the late publication of the new tariffs, it would imply a serious impediment in the CNEE's analytical capacity given that the independent consultant's study is possibly the best tool that the CNEE has when analyzing the tariff studies prepared by the distributors.

437. In addition to adhering to legal principles, it is even more important to note that, unlike the values proposed in the Bates White July 28 study, the tariffs set according to the Sigla study reflect efficient values.

438. Kaczmarek tries to discredit the Sigla tariff study by, among other things,[615] only comparing the evolution of EEGSA's tariffs at the medium voltage level to companies in El Salvador. According to Kaczmarek, the VADs resulting from the tariffs set on the basis of the Sigla study are two or three times lower than those of distributors in El Salvador that were "potentially" comparable.[616]

614 Calleja, **Appendix CWS-3**, para. 49.

615 For a detailed analysis of Kaczmarek's other arguments related to the tariff level established in 2008, see Damonte, **Appendix RER-2**, Chapter [7.2].

616 Kaczmarek, **Appendix CER-2**, para. 124

439. This approach is wrong. First, the expert, in a biased manner, shows only the evolution of EEGSA's tariff for medium voltage levels, completely ignoring those for low voltage, which clearly invalidates his analysis.[617] Second, the "potentially" comparable companies from El Salvador that he uses are not comparable to EEGSA, as further explained by Damonte.[618] Last, Kaczmarek is being partial by not comparing the tariffs arising from Bates White's tariff study, which he insists should be applied, but which significantly exceed the tariff levels of El Salvador.[619]

440. Contrary to Kaczmarek's allegations,[620] the Sigla values are primarily in line with the VAD of CAESS, the El Salvadorian distributor most comparable to EEGSA.[621] The following graphic shows this consistency in the case of low voltage, and, in turn, the disproportionality of the VAD proposed by EEGSA in the July 28 study.

617 Kaczmarek, **Appendix CER-2**, para. 124

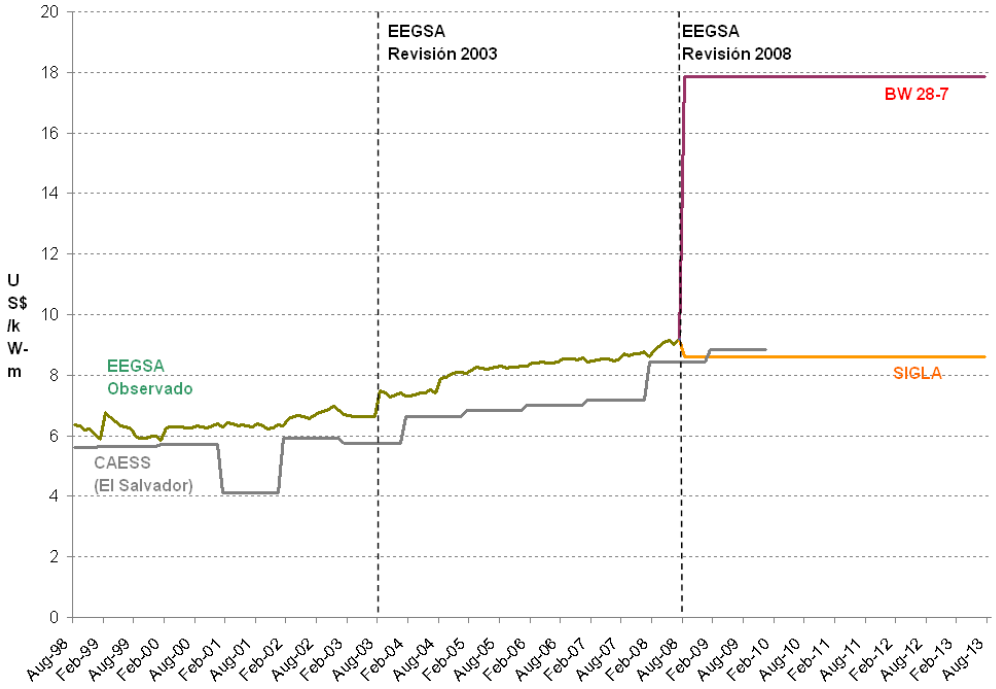
618 Damonte, **Appendix RER-2**, para. 231.

619 See section V.B below.

620 Kaczmarek, **Appendix CER-2**, para. 124. Kaczmarek alleges that the tariffs of comparable companies in El Salvador are double or triple that of those set by EEGSA. As previously explained by Damonte (Damonte, **Appendix RER-2**, para [215]) Kaczmarek uses companies that are not comparable to EEGSA; instead, the company most appropriate to make this comparison with is CAESS. Calleja, **Appendix RER-2**, para. 215.

621 Damonte, **Appendix RER-2**, para. 234.

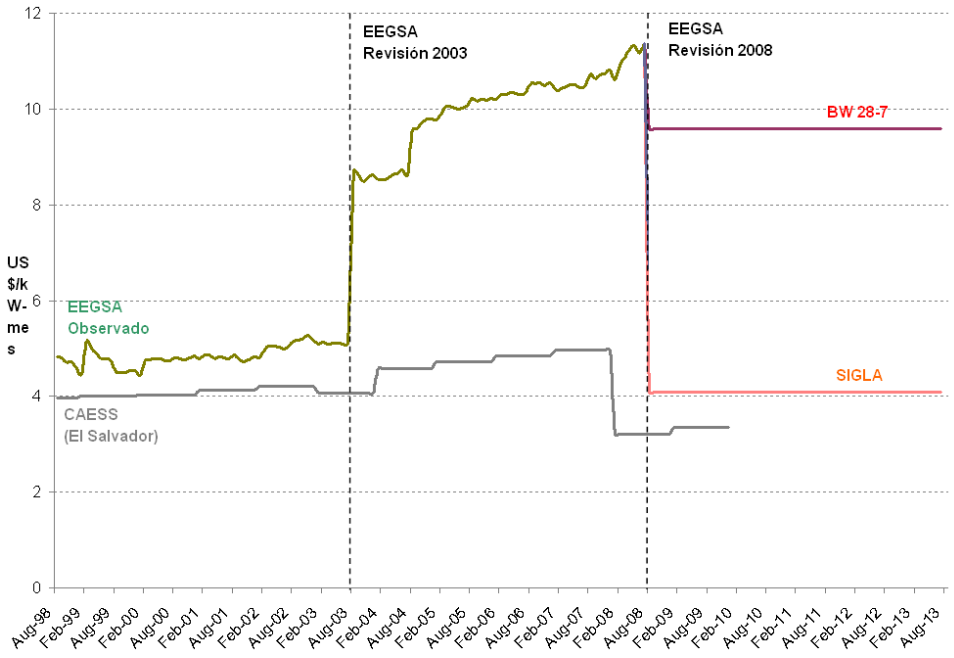
VAD Low Voltage (LV) - EEGSA vs. CAESS (El Salvador)[622]



441. As shown above, in the case of medium voltage, the VAD resulting from the Sigla study is much higher than that of CAESS. The disproportionality of the tariffs sought by Bates White is apparent in the following:

622 M Abdala and M Schoeters, **Appendix RER-1**, Section IV.2.2.

VAD Medium Voltage (MV) - EEGSA vs. CAESS (El Salvador)[623]



442. More illustrative still, the values are in line with the entire region. According to a benchmarking study carried out by Damonte in which he compared the VNRs of 60 Latin American distributors, the VNR for EEGSA based on the Sigla study coincided with the VNR of the benchmark (only 1 percent less).[624] Likewise, the book value of EEGSA's asset base (including merchant credit, which is the difference between the book value and the full value paid for by Teco for its shares in EEGSA),[625] results in a value that is very similar to the benchmark and that of Sigla, which also confirms its reasonableness.[626] It is important to clarify, as Damonte explains, that except in limited exceptions, the accounting VNR is almost always lower than the regulatory VNR, given that the latter must be more

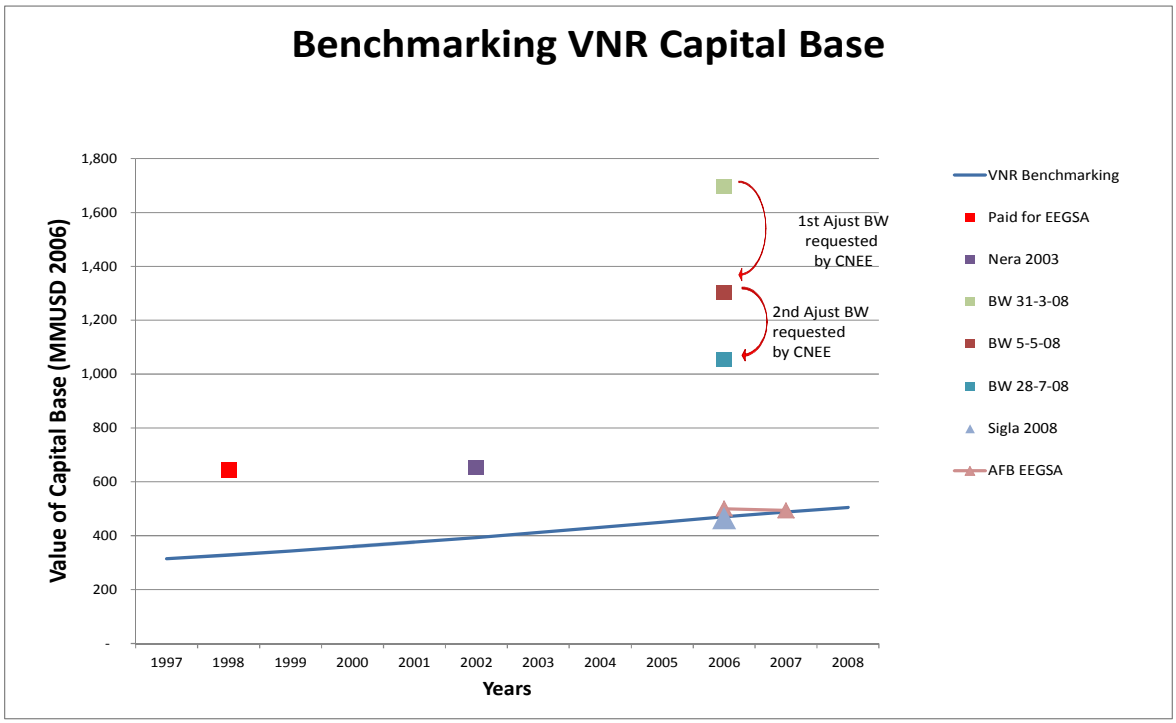
623 *Ibid.*

624 Damonte, **Appendix RER-2**, para. 247. We note that the Terms of Reference required presentation of a benchmark study which Bates White never submitted; furthermore, the Expert Commission unanimously pronounced itself on the necessity of presenting comparisons to validate the calculations in the study. Expert Commission Report, July 25, 2008, **Exhibit R-87**, pg. 164.

625 Higher than the inventory value. We note that this is a conservative analysis given that the value offered by Teco in the privatization is itself a risk (the premia eventually paid by the offeror cannot be passed on to the consumer). Damonte, **Appendix RER-2**, para. 251.

626 Damonte, **Appendix RER-2**, para. 251.

efficient.[627] By providing an additional comparison, we note that the VNR proposed by Bates White on July 28 is, in turn, 124 percent higher than the benchmark VNR.[628] The following graphic illustrates these values:[629]



627 Damonte, **Appendix RER-2**, paras. 27-30 and 39:

> [T]he Regulator always takes into consideration the real company, when it comes to judging the reasonableness of the VNR and the costs of the Model Company to be used for the tariff calculation. The costs and facilities of the real company (not only in Guatemala but in most of Latin America) represent an upper limit to the costs of the Model Company that will be used in calculating tariffs. The reason-ableness of this principle is obvious, since the main aim of regulation is equity, both for consumers and for the service provider. If the Regulator recognizes a cost that is higher than reality, it would be allowing the company to earn revenue above its costs, so the company would achieve above normal profitability. Moreover, this implies that consumers would be paying tariffs higher than those necessary to provide the service efficiently. […] It is important to consider that the unit VNR of the Model Company will always be less, or at most equal to that of the real company, unless the greater value is more than off-set by associated lower costs of the other components.

(Emphasis added).

628 Damonte, **Appendix RER-2**, para. 250.

629 We note the high level of the VNR in 2003 compared with the benchmarking (72 percent higher). *Ibid.*, para. 249.

a. The current tariffs attracted buyers to EEGSA's shares

443. Kaczmarek alleges that the tariffs adopted by the CNEE do not allow EEGSA to receive the return on investment contemplated by the LGE.[630] The reasoning of Kaczmarek, however, is plagued by fatal errors and is based on false assumptions.

444. First, as already explained, Kaczmarek conducted his profitability analysis on the amounts invested in EEGSA shares,[631] even though the LGE does not recognize profits over the real investment nor the price paid for shares, but rather over the capital base of the model company. Therefore, the profit rate of between 7 and 13 percent provided for by the LGE must be measured on the basis of the regulated capital base during the concession period, as it is a long-term investment. Finally, and most importantly, Kaczmarek in his analysis completely ignores the restructuring of EEGSA's business activities, including the transfer of infrastructure, of the transportation business from EEGSA to Trelec, and of other activities to affiliated companies.[632]

445. Additional evidence that the tariffs that the CNEE set based on the Sigla study did not, as TGH claims, adversely affect EEGSA or its shareholders, is the sale by Teco of its shares in EEGSA to Empresas Públicas de Medellín (***EPM***) after the new tariffs were established. The total sum paid (in cash) by EPM for 100 percent of the shares in DECA II was US$ 605 million, a price that included the buyer assuming the debt previously incurred by DECA II and its subsidiaries.[633] Upon presenting EEGSA to the interested parties, members of the Consortium

630 Kaczmarek, **Appendix CER-2**, paras. 230-231.

631 *Ibid.*, para. 230.

632 See section III.C.1 above and M Abdala and M Schoeters, **Appendix RER-1**, Section III.2.5.

633 In the case of EEGSA, the debt assumed was US$ 87.6 million. See Binding Offer presented by Empresas Públicas de Medellín, E.S.P. to Iberdrola Energía, S.A., TP de Ultramar LTD y EDP – Energías de Portugal, S.A. (redacted version), October 6, 2010, **Exhibit C-352**, annex 2.

characterized the company as nothing less than "one of the best and most solid companies of the country."[634]

446. As EEGSA's buyers fully confirmed at the time, they bought EEGSA because they considered it to be "the biggest and strongest energy distribution and marketing business in Central America."[635] Furthermore, as EPM executive Federico Restrepo confirmed, he bought EEGSA "on the basis that the current tariff model and layout is the one that exists […] and we don't have any expectations that it will be modified in any other direction."[636] EPM is one of the largest public utility companies in Latin America, with broad experience in the sector, and is an example of management and operation in the region. Its acquisition of EEGSA is a show of confidence and an endorsement of the regulatory and tariff-related management performed by the CNEE.

447. It is worth highlighting that, while TGH claims in its Memorial that its sale of shares in EEGSA was motivated by alleged mistreatment on the part of Guatemala, the press releases issued by TGH and its partners in EEGSA make no reference to this. To the contrary, TGH publicly announced that the sale of its share in EEGSA was due to its interest in concentrating its power generating assets in Guatemala, emphasizing its "continued good operations and strong earnings and cash flow."[637] In keeping with this position, Iberdrola and EDP, for their part, explained to their shareholders that the sale of EEGSA was exclusively

634 DECA II Management Presentation, September 2010, **Exhibit R-127**, pg. 22 (Emphasis in bold in the original).

635 EPM Informative Newsletter, "EPM acquires largest and most solid energy marketing and distribution business in Central America," October 21, 2010, **Exhibit R-129**.

636 "We carry no flag, we respect roots," *Prensa Libre*, October 23, 2010, **Exhibit R-133**; Letter from EPM to Iberdrola regarding the non-binding offer, July 26, 2010, **Exhibit R-126**. Suffice it to say that when accepting the price offer, TGH relied on the favorable opinion of its financial consultants at Citi, which disregarded any tariff increases before 2014. See Letter of Citi to the Management of Teco Energy, Inc., October 14, 2010, **Exhibit R-128**.

637 Teco Press Release: "TECO Energy reports third quarter results", October 28, 2010, **Exhibit R-134**, pg. 1.

due to corporate policies that were in no way related to the EEGSA tariff review process in 2008.[638]

448. Furthermore, Teco has recently acquired the bidding rules for a major investment in Guatemala's electricity sector, which demonstrates that its decision in 2010 had no relation to a discrepancy with the regulatory framework or the authorities in that sector.[639]

G. EEGSA AND ITS SHAREHOLDERS FULLY EXHAUSTED THEIR REMEDY TO JUDICIALLY CHALLENGE THE TARIFFS

449. As TGH explained in its Claimant's Memorial,[640] EEGSA and its shareholders decided to judicially challenge the CNEE's decisions. In particular, EEGSA decided to present an *amparo* against CNEE Resolution CNEE 144-2008 which

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638 Iberdrola explained to its shareholders that the sale of EEGSA was due to the need to ensure the availability of capital necessary for investing in Mexico and Brazil:

> The objective of IBERDROLA is to focus on its Latin American presence in Mexico and Brazil, which have become key countries in the future growth of the Group, as this is one of the most dynamic regions of the world. […]
>
> The sale of investee companies in Guatemala is defined in IBERDROLA's divestment plan, the purpose of which is to maintain the Group's financial strength, optimize capital structure and ensure the pace of investments committed to the markets.
>
> The operation is in addition to others announced in 2010 by IBERDROLA […] in the United States, in Chile, and in [Guatemala].

Press release of Iberdrola Energía S.A., October 22, 2010, **Exhibit R-132** (Emphasis added).

EDP, for its part, explained that the sale was in line with its strategy of divestiture in non-strategic assets over which the company could not exercise control. EDP told its investors:

> "The sale of these assets is in line with EDP's strategy of divesting non-core assets, such as minority stakes with no synergies with other assets in EDP and where EDP cannot have a relevant role in the management of the company."

EDP Press Release: "EDP sells its stake in DECA II," October 21, 2010, **Exhibit R-130** (Emphasis added).

639 Colom, **Appendix RWS-1**, para. 163.

640 Claimant's Memorial, paras. 204-219.

established the tariffs for the five-year period from 2008 to 2013, and against CNEE Resolution No. GJ-Providencia 3121 that dissolved the Expert Commission.[641] Even though the courts of first instance ruled in EEGSA's favor, the CNEE appealed these decisions resulting in their reversal by the Constitutional Court of Guatemala in decisions of November 18, 2009 and February 24, 2010.[642]

450. TGH and its legal expert, Professor Alegría, criticize the decisions of the Constitutional Court of Guatemala rejecting EEGSA's claims, as incorrect and politically biased.[643] However, as explained below, these accusations are groundless. The process and the foundation underlying these Constitutional Court decisions respected the rights of TGH and EEGSA, as already analyzed above and reiterated below.[644]

451. TGH's criticism of the Constitutional Court is opportunistic and unfounded, revealing a profound lack of understanding with regard to the relationship between the Constitutional Court, the CNEE, and the Government of Guatemala.

452. As already explained, the CNEE does not have any political or other interests in preventing an increase in distribution tariffs. Its only obligation is to ensure compliance with the LGE. Strong evidence that neither CNEE nor the Guatemalan State politically intervene in the determination of tariffs is that in 2010, the CNEE, under the same Board of Directors that set the tariffs in 2008, approved a quarterly tariff increase in favor of EEGSA, Deocsa, and Deorsa, simply because it was in compliance with the LGE's terms. In EEGSA's case, this amounted to a 9.8 percent increase in unsubsidized tariffs and a notable 30

641 Claimant's Memorial, paras. 207 and 209.

642 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, November, 18 2009, **Exhibit R-105**; Decision of the Constitutional Court, February 24, 2010, **Exhibit R-110**.

643 Claimant's Memorial, para. 275; Alegría, **Appendix CER-1**, paras. 75-76. We note that, while the way to challenge the decision of the highest court of Guatemala before an International tribunal would be via alleging a denial of justice, TGH has not invoked, nor could it invoke, a violation of that standard. -78. See section IV.B.2 and IV.

644 See Sections II.B.2 and IV.

percent increase in subsidized tariffs (the subsidized tariff is for the country's poorest demographic).[645] Not only did the CNEE approve these increases, but it also actively intervened to defend them when a legal battle ensued with the Ombudsman for Human Rights, who requested and obtained an *amparo* that provisionally suspended this increase. Following an appeal, the Constitutional Court heard arguments by EEGSA and the CNEE against this provisional *amparo*, and revoked it, thus allowing implementation of the tariff increases as established by the CNEE.[646] It is important to note that in this case, the President of Guatemala himself publicly opposed the judicial suspension of the electricity tariff increases. [647]

453. As another example of the Constitutional Court's independence, on February 25, 2010, only a day after issuing its judgment revoking the *amparo* of which TGH complained, the Court upheld the removal of the Minister of Education, Bienvenido Argueta, one of the most visible ministers in the government, on account of his failure to submit reports on education plans, as required by a member of Congress.[648]

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645 "[Álvaro] Colom deplores decision by judge that suspends increases in electricity", *Publimetro*, May 12, 2010, **Exhibit R-117**:

> The CNEE approved an increase of between six and 30 percent in electricity prices for the May–June–July quarter. It was rejected by broad sectors of the population.
>
> Human Rights attorney Sergio Morales filed an appeal against the measure, believing it would increase the cost of the basic goods.

In EEGSA's case, this amounted to 9.8 percent increase in unsubsidized (now 1,94 Q/kWh) and a notable 30 percent increase in subsidized tariffs (now 1,68 Q/kWh), this being the tariff subsidized for the country's poorest demographic. "Social electricity tariff rises between 25 and 30 percent starting in May", *Prensa Libre*, April 29, 2010, **Exhibit R-114**.

646 Decision of the Constitutional Court, Consolidated Case Files 719-2010, 721-2010, 722-2010, 723-2010 and 724-2010, Direct Appeal, March 3, 2010, Exhibit **R-113**, pg. 6.

647 "[Álvaro] Colom deplores decision by judge that suspends increases in electricity", *Publimetro*, May 12, 2010, **Exhibit R-117**.

648 Decision of the Constitutional Court, Case File 4255-2009, February 25, 2010, **Exhibit R-111**.

454. Finally, this same Constitutional Court recently terminated the presidential aspirations of the former wife of former President Álvaro Colom, by rejecting her candidacy.[649]

H. TGH'S ATTEMPTS TO "POLITICIZE" THE PRESENT DISPUTE IN ORDER TO RAISE IT TO THE INTERNATIONAL PLANE

455. Finally, it is necessary to briefly refer to TGH's attempts to politicize this dispute to give it an international "color." To this end, in its Claimant's Memorial, TGH refers to Guatemala's alleged pressure and harassment campaigns against EEGSA and its executives. Nonetheless, there is a complete lack of substantial evidence to prove its allegations.

1. (Private) criminal charges filed against EEGSA executives

456. In its desperate attempt to politicize this dispute, TGH refers to a supposed criminal prosecution in which two of EEGSA's executives in Guatemala were victims. TGH explains that, due to certain charges filed in August 2008 by Generadora del Sur S.A. (a private Guatemalan power-generating company), a criminal trial court in the small town of Amatitlán on the outskirts of Guatemala City, issued an arrest warrant for two EEGSA employees: Luis Maté, EEGSA's General Manager, and Gonzalo Gómez, a former company employee.[650]

457. The story presented by TGH regarding this situation is completely false and is worth briefly clarifying. The arrest warrants for Mr. Maté and Mr. Gómez, issued in late August 2008, resulted from EEGSA's dispute with a private company, Generadora del Sur S.A., which lasted several months. At the time these arrest warrants were issued, the tariff schedule had already been in force for almost a month. In any case, only days after the warrants had been issued, they were suspended by the Third Chamber of the Court for Criminal Appeals in Guatemala

649 Decision of the Constitutional Court, Case File 2906-2011, August 8, 2011, **Exhibit R-141**.

650 Claimant's Memorial, para. 205; Judgment of the First Instance Criminal Court for Narcoactivity and Crimes Against the Environment, Arrest Warrants against Luis Maté and Gonzalo Gómez, August 26, 2008, **Exhibit C-296**; Maté, **Appendix CWS-6**, paras. 66-72; Calleja, **Appendix CWS-3**, para. 55.

City and eventually dismissed.[651] In his witness statement, Luis Maté recognizes that criminal charges were filed by an individual, and that the Public Ministry had been dismissing each of those charges.

458. Demonstrative of the fact that such charges, initiated by individuals, are beyond the CNEE's control, is the fact that Moller himself, as well as other Directors, have also been victims of such baseless charges by a company that has a transmission contract with Generadora del Sur S.A. [652] The duty to submit to judicial proceedings is an inevitable consequence of living under the rule of law and performing duties associated with public utilities. The State, to the contrary, and as acknowledged by the witness Mr. Maté, protected these EEGSA executives by way of its Judicial Branch.

2. The theft of Mr. Calleja's laptop

459. If TGH's claims regarding the private complaints filed against EEGSA directors are strikingly groundless, TGH's complaint involving the theft of Mr. Calleja's laptop is even less plausible. According to TGH, on September 1, 2008, after Mr. Calleja gave a radio interview, "[w]hen he returned to his car after giving the interview, he discovered that his car had been broken into and his laptop computer had been stolen."[653] Mr. Calleja submits no documentary evidence of any police report issued after the alleged theft. Anyone knows that leaving a laptop in a parked automobile, even in a developed country, means assuming the risk of theft. This is even more so in a Latin American capital. The frivolity and absurdity of attempting to hold the Guatemalan government responsible for a theft in a parking lot requires no further comment.

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651 Maté, **Appendix CWS-6**, paras. 71-72.

652 "Commercial firm accuses EEGSA of monopolistic practices", El Periódico, June 9, 2008, **Exhibit R-82**; Moller, **Appendix RWS-2**, paras. 51.

653 Claimant's Memorial, para. 206.

IV. GUATEMALA HAS NOT BREACHED THE INTERNATIONAL MINIMUM STANDARD OF TREATMENT UNDER ARTICLE 10.5 OF THE TREATY

A. THE INTERNATIONAL MINIMUM STANDARD DOES NOT CENSURE REGULATORY OR CONTRACTUAL CONDUCT THAT IS ALLEGEDLY CONTRARY TO DOMESTIC LAW, EXCEPT IN THE CASE OF DENIAL OF JUSTICE

1. The international minimum standard only provides protection from gross conduct, such as conduct that is manifestly arbitrary or that flagrantly repudiates the regulatory framework

460. The text of Article 10.5 of the CAFTA-DR makes clear that the guaranteed standard of treatment is the customary international law minimum standard. Article 10.5 reads:

> Minimum Standard of Treatment
>
> 1. Each Party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security.
>
> 2. For greater certainty, paragraph 1 prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. The concepts of "fair and equitable treatment" and "full protection and security" do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights. The obligation in paragraph 1 to provide:
>
> (a) "fair and equitable treatment" includes the obligation not to deny justice in criminal, civil, or administrative adjudicatory proceedings in accordance with the principle of due process embodied in the principal legal systems of the world; and
>
> (b) "full protection and security" requires each Party to provide the level of police protection required under customary international law.

> 3. A determination that there has been a breach of another provision of this Agreement, or of a separate international agreement, does not establish that there has been a breach of this Article. (Emphasis added).

461. Therefore, under Article 10.5 of the Treaty, what the State must guarantee is the minimum standard of treatment, that is, "the customary international law minimum standard of treatment of aliens." It is expressly stated that the concept of "fair and equitable treatment" that is invoked by TGH, as well as the concept of "full protection and security," "do not require treatment in addition to or beyond that which is required by that standard, and do not create additional substantive rights."

462. In Annex 10-B of the Treaty, the parties also:

> [C]onfirm their shared understanding that "customary international law" generally and as specifically referenced in Articles 10.5, 10.6, and Annex 10-C results from a general and consistent practice of States that they follow from a sense of legal obligation. With regard to Article 10.5, the customary international law minimum standard of treatment of aliens refers to all customary international law principles that protect the economic rights and interests of aliens. (Emphasis added).

463. TGH must therefore show that Guatemala has breached the customary international law minimum standard of treatment of aliens. In order to provide content to the minimum standard of treatment, evidence must be presented of the "general and consistent practice of States that they follow from a sense of legal obligation." As has been made clear by international tribunals, the burden of proof with respect to customary international law is on the Claimant.[654] TGH presents absolutely no argument, much less evidence, of what is the general and consistent practice followed by the United States and Guatemala from a sense of legal

654 *Cargill, Incorporated v. United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009, **Exhibit CL-12**, para 273; *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit CL-23**, para 601.

obligation regarding the minimum standard of treatment. Therefore, from the outset, TGH's argument lacks any basis in law.

464. TGH limits itself to citing cases that refer to the international minimum standard of treatment, and does so without a careful analysis.[655] In particular, TGH omits any reference to the rulings of international tribunals that have confirmed that in order to constitute a violation of the international minimum standard under customary international law, the State's conduct must be extreme and outrageous. This was, for instance, the conclusion reached by the tribunal in *Cargill v. Mexico* after conducting a detailed analysis of the content of the international minimum standard, including the decisions of other tribunals on the subject.[656] In the words of the *Cargill* tribunal:

> To determine whether an action fails to meet the requirement of fair and equitable treatment, a tribunal must carefully examine whether the complained of measures were grossly unfair, unjust or idiosyncratic; arbitrary beyond a merely inconsistent or questionable application of administrative or legal policy or procedure so as to constitute an unexpected and shocking repudiation of a policy's very purpose and goals, or to otherwise grossly subvert a domestic law or policy for an ulterior motive […].[657]

465. The tribunal in *Glamis Gold v. the United States* ruled in a similar manner. The question in *Glamis Gold* was whether a refusal to grant a mining permit that was allegedly contrary to the administration's previous practice constituted a violation of the fair and equitable treatment standard. The tribunal stated:

> [T]o violate the customary international law minimum standard of treatment codified in Article 1105 of the NAFTA, an act must be sufficiently egregious and shocking – a gross denial of justice, manifest arbitrariness, blatant unfairness, a complete lack of due

655 See Claimant's Memorial, paras 232-234, 240-243.

656 *Cargill, Incorporated v. United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009, **Exhibit CL-12**, paras 284-286.

657 *Ibid.*, para 296. (Emphasis added).

> process, evident discrimination, or a manifest lack of reasons – so as to fall below accepted international standards and constitute a breach of Article 1105(1).
>
> […] a breach requires something greater than mere arbitrariness, something that is surprising, shocking, or exhibits a manifest lack of reasoning.[658]

466. The tribunal in *Thunderbird v. Mexico* also required that the State's conduct be extreme and outrageous:

> Notwithstanding the evolution of customary law since decisions such as *Neer Claim* in 1926, the threshold for finding a violation of the minimum standard of treatment still remains high, as illustrated by recent international jurisprudence. For the purposes of the present case, the Tribunal views acts that would give rise to a breach of the minimum standard of treatment prescribed by the NAFTA and customary international law as those that, weighed against the given factual context, amount to a gross denial of justice or manifest arbitrariness falling below acceptable international standards.[659]

467. Tribunals outside the context of the NAFTA have also required that the conduct be extreme and outrageous. For example, in *Genin v. Estonia* the tribunal was presented with allegations of improper conduct on the part of Estonia's financial services regulator, the Central Bank of Estonia, including with respect to the revocation of a banking license. The tribunal rejected the claim, holding that the minimum standard does not censure merely irregular conduct: "Acts that would violate this minimum standard would include acts showing a willful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith."[660]

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658 *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit Exhibit [sic] CL-23**, paras 616-617.

659 *International Thunderbird Gaming Corporation v. United Mexican States* (UNCITRAL Case) Award, 26 January 2006, **Exhibit CL-25**, para 194. (Emphasis added).

660 *Genin et al. v. Republic of Estonia* (ICSID Case No. ARB/99/2) Award, 25 June 2001, **Exhibit RL-3**, paras 365, 367. TGH cites cases such as *Biwater Gauff v. Tanzania*, *Rumeli v. Kazakhstan*, *Azurix v. Argentina* and *Saluka v. Czech Republic* to support its position that the minimum

2. The international minimum standard does not cover conduct that is not more than a supposed violation of domestic law; much to the contrary, it accords the State an ample margin of appreciation, leaving the task of redressing mere irregularities to the local courts and tribunals

468. TGH argues that "numerous tribunals found the Host State liable" in a situation "such as the case at hand."[661] Nothing could be further from the truth. Case law is clear in affirming that it is not for international courts and tribunals to decide disputes regarding nothing but supposed regulatory irregularities, such as disputes over the interpretation and application of a regulatory framework. Tribunals are required to accord an ample margin of appreciation to the State when a party's claims are based on such irregularities.

469. The decision of the NAFTA tribunal in *SD Myers v. Canada* is relevant in this regard. In *SD Myers,* the claimant argued that Canada breached the fair and equitable treatment standard when it imposed restrictions on the transport of hazardous substances, causing damage to the claimant's waste treatment business:

> When interpreting and applying the "minimum standard," a Chapter 11 tribunal does not have an open-ended mandate to second-guess government decision-making. Governments have to make many potentially controversial choices. In doing so, they may appear to have made mistakes, to have misjudged the facts, proceeded on the basis of a misguided economic or sociological theory, placed too much emphasis on some social values over others and adopted solutions that are ultimately ineffective or counterproductive. The

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standard under customary international law is nothing more than the standard of fair and equitable treatment. However, in none of these cases did the treaties in question contain language similar to that of Article 10.5 of the DR-CAFTA with regard to customary international law. The tribunals focused their analyses on the meaning of the expression "fair and equitable treatment" and mentioned the international minimum standard only fleetingly *in dicta* (*Rumeli Telekom A.S. and Telsim Mobil Telekomikasyon Hizmetleri A.S. v. Republic of Kazakhstan* (ICSID Case No. ARB/05/16) Award, 29 July 2008, **Exhibit CL-39**, paras 609-611; *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania* (ICSID Case No. ARB/05/22) Award, 24 July 2008, **Exhibit CL-10**, paras 591-592; *Saluka Investments B.V. v. Czech Republic* (UNCITRAL Case) Partial Award, 17 March 2006, **Exhibit CL-42**, paras 296-309; *Azurix Corp. v. Republic of Argentina* (ICSID Case No. ARB/01/12) Award, 14 July 2006, **Exhibit CL-8**, paras 359-361).

661 Claimant's Memorial, title of Section III.B.

> ordinary remedy, if there were one, for errors in modern governments is through internal political and legal processes, including elections.
>
> [...]
>
> The Tribunal considers that a breach of Article 1105 occurs only when it is shown that an investor has been treated in such an unjust or arbitrary manner that the treatment rises to the level that is unacceptable from the international perspective. That determination must be made in the light of the high measure of deference that international law generally extends to the right of domestic authorities to regulate matters within their own borders.[662]

470. In *Thunderbird v. Mexico*, a dispute arose over a ban imposed by the government (SEGOB) on the betting games that the investor's local subsidiary (EDM) was planning to distribute. The investor argued that the ban constituted unfair and inequitable treatment. The tribunal rejected the claim as follows:

> In the present case, the Tribunal is not convinced that Thunderbird has demonstrated that Mexico's conduct violated the minimum standard of treatment, for the following reasons.
>
> […]
>
> The Tribunal does not exclude that the SEGOB proceedings may have been affected by certain irregularities. Rather, the Tribunal cannot find on the record any administrative irregularities that were grave enough to shock a sense of judicial propriety and thus give rise to a breach of the minimum standard of treatment. […] [I]t does not attain the minimum level of gravity required under Article 1105 of the NAFTA under the circumstances.[663]

471. A similar conclusion was reached in *GAMI v. Mexico* with respect to an investor's claims regarding the way in which the Mexican authorities had applied a domestic

662 *SD Myers Inc v. Canada* (UNCITRAL Case) First Partial Award, 13 November 2000, **Exhibit CL-41**, paras 261, 263.

663 *International Thunderbird Gaming Corporation v. United Mexican States* (UNCITRAL Case) Award, 26 January 2006, **Exhibit CL-25**, paras 195, 200. (Emphasis added).

regulation concerning sugarcane production. Referring to *Waste Management II* the tribunal concluded that a "failure to fulfill the objectives of administrative regulations" and the "requirements of national law" "does not necessarily violate international law."[664] Instead, in determining whether a breach of the fair and equitable treatment standard has taken place, the fundamental issue is whether a "claim of maladministration […] amount[s] to an 'outright and unjustified repudiation' of the relevant regulations."[665] Accordingly, maladministration alone is not enough to establish a breach of the standard.

472. The *GAMI* tribunal's analysis of the facts presented to it provides further support to the conclusion that mere irregularities in the application of domestic law do not result in a breach of the international minimum standard. According to the tribunal:

> GAMI has demonstrated clear instances of failures to implement important elements of Mexican regulations.
>
> It has adduced eminent evidence to the effect that the Mexican government is constitutionally required to give effect to its regulations.[666]

473. However, the tribunal concluded that:

> Claims of maladministration may be brought before the Mexican courts. Indeed as breaches of Mexican administrative law they could be brought nowhere else. […]
>
> GAMI has not been able to show anything approaching "outright and unjustified repudiation" of the relevant regulations.[667]

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664 *GAMI Investments, Inc v. Mexico* (UNCITRAL Case) Final Award, 15 November 2004, **Exhibit RL-7**, para 97. (The tribunal's translation to Spanish in *Cargill, Incorporated v. United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009, **Exhibit CL-12**, para 287).

665 *Ibid.*, para 103.

666 *Ibid.*

667 *Ibid.*, paras 103-104.

474. The conclusions of the tribunal in *GAMI* were cited with approval by the tribunal in *Cargill,*[668] which further added:

> The Tribunal agrees with Respondent that even the unlawfulness of a municipal law does not necessarily mean that the act is unlawful under international law.[669]

475. The case of *ADF v. United States* is also relevant. The issue in *ADF* was whether a public authority had correctly applied the relevant U.S. regulations to a project involving the construction of a highway:

> [E]ven if the U.S. measures were somehow shown or admitted to be *ultra vires* under the internal law of the United States, that by itself does not necessarily render the measures grossly unfair or inequitable under the customary international law standard of treatment embodied in Article 1105(1). An unauthorized or *ultra vires* act of a governmental entity of course remains, in international law, the act of the State of which the acting entity is part, if that entity acted in its official capacity. But something more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the customary international law requirements of Article 1105(1), even under the Investor's view of that Article. That "something more" has not been shown by the Investor.[670]

476. In *Genin v. Estonia*, to give another example, the tribunal held that the fact that the conduct of a regulatory authority may be subject to criticism does not by itself support a finding of violation of the treaty and, in particular, of the international minimum standard of fair and equitable treatment:

> [W]hile the Central Bank's decision to revoke the EIB's license invites criticism, it does not rise to the level of a violation of any provision of the BIT.

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668 *Cargill, Incorporated v. United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009, **Exhibit CL-12**, para 287.

669 *Ibid.*, para 303.

670 *ADF Group Inc v. United States of America* (ICSID Case No. ARB(AF)/00/1) Award, 9 January 2003, **Exhibit CL-4**, para 190.

> […]
>
> Article II(3)(a) of the BIT requires the signatory governments to treat foreign investment in a "fair and equitable" way. […] Acts that would violate this minimum standard would include acts showing a willful neglect of duty, an insufficiency of action falling far below international standards, or even subjective bad faith. […].[671]

477. Accordingly, although a decision of a regulatory body may be subject to criticism or even be contrary to the law from the perspective of the relevant domestic legislation, it does not for that reason alone violate the international minimum standard. For this, more is required: the conduct must constitute a deliberate violation of the regulatory authority's duties and obligations or an insufficiency of action falling far below international standards.

478. *Glamis Gold* is also relevant; it summarizes the issue clearly:

> [T]he Tribunal first notes that it is not for an international tribunal to delve into the details of and justifications for domestic law. If Claimant, or any other party, believed that [the] interpretation of [the civil servant of] the undue impairment standard was indeed incorrect, the proper venue for its challenge was domestic court.
>
> […]
>
> It is not the role of this Tribunal, or any international tribunal, to supplant its own judgment of underlying factual material and support for that of a qualified domestic agency.[672]

479. In sum, a government authority does not violate the international minimum standard when it commits mistakes, makes questionable decisions, commits errors of judgment, or adopts misinformed or misguided measures. In determining

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671 *Genin et al. v. Republic of Estonia* (ICSID Case No. ARB/99/2) Award, 25 June 2001, **Exhibit RL-3**, paras 365, 367. (Emphasis added).

672 *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit CL-23**, paras 762, 779.

whether there was a breach of the minimum standard of treatment, international tribunals are not supposed to make such decisions, determinations or opinions *de novo*. Administrative errors must instead be remedied by recourse to the domestic judicial system. In light of the margin of appreciation that must be accorded to the State, it is not any administrative irregularity, wrongful application of the law, or acts of maladministration that result in a violation of the standard; instead, for a violation to take place, the actions in question must constitute a clear and manifest repudiation of the relevant domestic laws. This is clearly not the case when the dispute concerns a difference of opinion between the investor and the regulator regarding the scope of the applicable rules, as is the case before this Tribunal. As the tribunal stated in *EnCana v. Ecuador*: "governments do not repudiate obligations merely by contesting their existence."[673]

3. When irregularities of a domestic law nature are alleged, in order to raise a valid claim of violation of the international minimum standard, the claimant must also allege that the local courts have denied it justice

480. A dispute of a regulatory or contractual nature such as that submitted by TGH can under no circumstances give rise to a violation of the international minimum standard. According to the margin of appreciation and deference that the State is given under the international minimum standard, such disputes are an issue of domestic law which must be submitted to the local courts. Only if the local courts have committed a denial of justice may a claim of unfair and inequitable treatment be submitted to an international tribunal.

481. Case law is clear in this respect. In *Waste Management*, the tribunal examined the case law on the international minimum standard of fair and equitable treatment and defined the standard as follows:

> […] Taken together, the *S.D. Myers*, *Mondev*, *ADF* and *Loewen* cases suggest that the minimum standard of

673 *EnCana Corporation v. Republic of Ecuador* (LCIA Case No. UN3481, UNCITRAL Rules) Award, 3 February 2006, **Exhibit RL-9**, para 194.

> treatment of fair and equitable treatment is infringed by conduct attributable to the State and harmful to the claimant if the conduct is arbitrary, grossly unfair, unjust or idiosyncratic, is discriminatory and exposes the claimant to sectional or racial prejudice, or involves a lack of due process leading to an outcome which offends judicial propriety […].[674]

482. Accordingly, the obligation to accord treatment in accordance with the international minimum standard is breached when the conduct attributable to the State is "arbitrary, grossly unfair, unlawful or idiosyncratic," "discriminatory," or "involves a lack of due process leading to an outcome which offends judicial propriety," such as a manifest lack of natural justice. An administrative, regulatory or contractual irregularity does not violate the standard of minimum treatment.

483. The tribunal then examined the municipal measure that had been challenged and, even though the measure violated the contractual framework of the investment, the tribunal noted that, although it violated the contractual framework:

> [I]s not to be equated with a violation of Article 1105 [NAFTA's fair and equitable treatment provision], provided that it does not amount to an outright and unjustified repudiation of the transaction and provided that some remedy is open to the creditor to address the problem. […]
>
> The importance of a remedy, agreed on between the parties, for breaches of the Concession Agreement bears emphasis. […] [T]he availability of local remedies to an investor faced with contractual breaches is nonetheless relevant to the question whether a standard such as Article 1105(1) have been complied with by the State. Were it not so, Chapter 11 would become a mechanism of equal resort for debt collection and analogous purposes in respect of all public (including municipal) contracts, which does not seem to be its purpose.

674 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, 30 April 2004, **Exhibit CL-46**, para 158. (Emphasis added).

> For these reasons the Tribunal is not satisfied that the City's breaches of contract rose to the level of breaches of Article 1105(1) of NAFTA.[675]

484. Therefore, a violation of domestic law by a government authority does not lead to a violation of the international minimum standard of treatment unless it is a manifest and unjustified repudiation of a right and there is no remedy available to the aggrieved party, that is, there is no access to the local courts and tribunals.

485. After making the statements above, the tribunal in *Waste Management* conducted an analysis of the local judicial proceedings with a view to determining "whether th[o]se proceedings involved a denial of justice in terms of Article 1105."[676] The tribunal concluded:

> Turning to the actual reasons given by the federal courts, the Tribunal would observe that it is not a further court of appeal, nor is Chapter 11 of NAFTA a novel form of *amparo* in respect of the decisions of the federal courts of NAFTA parties. Certain of the decisions appear to have been founded on rather technical grounds, but […] [i]n any event, and however these cases might have been decided in different legal systems, the Tribunal does not discern in the decisions of the federal courts any denial of justice as that concept has been explained by NAFTA tribunals, notably in the *Azinian*, *Mondev*, *ADF* and *Loewen* cases. The Mexican court decisions were not, either *ex facie* or on closer examination, evidently arbitrary, unjust or idiosyncratic. There is no trace of discrimination on account of the foreign ownership of Acaverde, and no evident failure of due process. The decisions were reasoned and were promptly arrived at. Acaverde won on key procedural points, and the dismissal in the second proceedings, in particular, was without prejudice to Acaverde's rights in the appropriate forum.[677]

675 *Ibid*, paras 115-117. (Emphasis added).

676 *Ibid*, para 128.

677 *Ibid*, paras 129-130.

486. In sum, when the claim relates to a regulatory or contractual dispute, the claimant can allege a violation of the international minimum standard only if the local courts and tribunals have denied it justice.

4. These same conclusions have been reached by tribunals that have found that the standard of fair and equitable treatment is an autonomous standard

487. The Treaty's fair and equitable treatment standard is the standard of customary international law, i.e., the so-called international minimum standard.[678] The fair and equitable treatment standard when interpreted independently from customary international law is more demanding on the State than the international minimum standard.

488. This is explained by the tribunal in *Saluka v. Czech Republic*, which TGH cites as if it supported its position:[679]

> [T]he minimum standard of "fair and equitable treatment" may in fact provide no more than "minimal" protection. Consequently, in order to violate that standard, States' conduct may have to display a relatively higher degree of inappropriateness.
>
> […] [I]nvestors' protection by the "fair and equitable treatment" standard is meant to be a guarantee providing a positive incentive for foreign investors. Consequently, in order to violate the standard, it may be sufficient that States' conduct displays a relatively lower degree of inappropriateness.[680]

489. The tribunal in *Suez and others v. Argentina* ruled in the same manner with respect to a fair and equitable treatment clause that referred to "international law," but did not specify – as is the case with Article 10.5 of the CAFTA-DR – that the standard was that has developed in customary international law:

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678 See Section IV.A.1 above.

679 Claimant's Memorial

680 *Saluka Investments B.V. v. Czech Republic* (UNCITRAL Case) Partial Award, 17 March 2006, **Exhibit CL-42**, paras 292-293.

> [T]he Tribunal is of course bound by the specific language of each of the applicable BITs. With respect to the Argentina-France BIT, it is to be noted that the text of the treaty refers simply to "the principles of international law," not to "the minimum standard under customary international law." The formulation "minimum standard under customary international law" or simply "minimum international standard" is so well known and so well established in international law that one can assume that if France and Argentina had intended to limit the content of fair and equitable treatment to the minimum international standard they would have used that formulation specifically. [...]
>
> [...] The Tribunal therefore rejects the Respondent's argument that the content of the fair and equitable treatment standard in the Argentina-France BIT is limited to the international minimum standard.[681]

490. Accordingly, when the treaty's language is clear, as is the case here, the content of the fair and equitable treatment standard cannot go beyond that of the international minimum standard.

491. In any event, the tribunals that have interpreted the fair and equitable treatment standard as being a separate standard from that required by customary international law have rejected the possibility that regulatory disputes as the one submitted by TGH can give rise to a violation of the standard.

492. In *Saluka*,[682] for example, the tribunal found that the fair and equitable treatment standard of the BIT in question was not the international minimum standard because there was no reference to customary international law in the relevant clause of the BIT (in the present case, however, there is such a reference and it is

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681 *Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A. v. Argentina* (ICSID Case No. ARB/03/19) and *AWG Group v. Argentina* (UNCITRAL Case), Decision on Liability, 30 July 2010, **Exhibit RL-16**, paras 184-185; *Suez, Sociedad General de Aguas de Barcelona S.A. e InterAgua Servicios Integrales del Agua S.A. v. Argentina* (ICSID Case No. ARB/03/17) Decision on Liability, 30 July 2010, **Exhibit RL-17**, paras 177-178.

682 *Saluka Investments B.V. v. Czech Republic* (UNCITRAL Case) Partial Award, 17 March 2006, **Exhibit CL-42**.

very clear).[683] However, even though the tribunal interpreted the standard separately from customary international law, it concluded that the fair and equitable treatment standard is not violated by mere administrative or regulatory irregularities, which must instead be submitted to the local courts.[684]

493. The same conclusion was reached in *Parkerings*, in which the tribunal interpreted and applied the fair and equitable treatment standard without making any reference to the international minimum standard. The tribunal rejected the argument that certain irregularities committed by a municipality in the process of verifying the investor's compliance with the terms of a contract and in the subsequent termination of the contract could give rise to a violation of the fair and equitable standard treatment in the absence of an allegation of denial of justice.[685]

494. In sum, when a claim relates to a regulatory or contractual dispute involving the application of domestic law, there is no basis for a finding of unfair and inequitable treatment unless the dispute was submitted to the domestic courts and they failed to dispense justice to the claimant. The same conclusion holds true for both the minimum standard of customary international law and the fair and equitable treatment standard interpreted independently from customary international law.

B. IN THE ABSENCE OF ALLEGATIONS OF DENIAL OF JUSTICE, TGH'S CLAIM THAT THE SUPPOSED IRREGULARITIES COMMITTED BY THE CNEE BREACHED THE INTERNATIONAL MINIMUM STANDARD HAS NO BASIS

495. As noted above, TGH's claim is based on supposed irregularities – which in TGH's words constitute arbitrary and illegal conduct – committed by the CNEE

683 *Ibid*, para 294. See Section IV.A.1, above.

684 *Ibid*, paras 442-443. ("The Treaty cannot be interpreted so as to penalise each and every breach by the Government of the rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State"). See paras. 85 and 553.

685 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No. ARB/05/8) Award, 11 September 2007, **Exhibit RL-10**, paras 315-320. ("many tribunals have stated that not every breach of an agreement or of domestic law amounts to a violation of a treaty. […] In most cases, a preliminary determination by a competent court as to whether the contract was breached under municipal law is necessary. […]"). See paras 95 and 553.

in the application of the Guatemalan regulatory framework during EEGSA's tariff review in 2008.[686] Section III.C of the Claimant's Memorial explains how in TGH's view Guatemala has violated the international minimum standard. The first paragraph of that section summarizes TGH's arguments as follows:

> […] The CNEE thus arbitrarily and unlawfully imposed its own VAD, rather than the VAD that it was required to apply according to the law. In so doing, the CNEE deliberately ignored both the Expert Commission's Report and Bates White's revised tariff study, and instead relied on its own commissioned study […]. The result was a VAD that did not provide EEGSA's foreign investors with a rate of return within the range guaranteed by the LGE. Both the process and the result of the tariff review were unlawful and arbitrary, and contravened TECO's legitimate expectations […].[687]

496. This indicates that in TGH's view the following would constitute a breach of the international minimum standard:

(a) The fact that the CNEE considered the Expert Commission's opinion to be not binding for the determination of the VAD and the tariffs, and that the duties of the Expert Commission did not extend to approving the Bates White study;

(b) The fact that the CNEE concluded that it had the prerogative to reject the Bates White study and approve the Sigla study;

(c) The fact that the VAD approved by the CNEE was too low.

497. All of these questions relate to the interpretation and application of the regulatory framework, which tasks fall within the competence and responsibility of the CNEE. Even if the CNEE made a mistake with respect to any of these questions (which is not the case), the CNEE's conduct could at most be characterized as

686 Claimant's Memorial, title of Section III.C and paras 228, 259, 268, 270-273, 280.

687 *Ibid.*, para 259. See also, paras 228, 268, 270-273, 280.

contrary to domestic law; such conduct could not, however, be the basis for a claim that Guatemala breached the international minimum standard.

498. The supposed irregularities committed by the CNEE were submitted to the courts with jurisdiction over these questions, i.e., the Guatemalan courts, which ruled in favor of the CNEE. Under these circumstances, only if EEGSA/TGH had been denied justice could Guatemala be found to have breached the international minimum standard. The three questions raised above, as well as the relevant decisions of the Constitutional Court, are discussed in further detail below.

1. TGH's allegations regarding the Expert Commission relate to the interpretation of the regulatory framework and cannot constitute a breach of the standard

499. TGH's allegations regarding the Expert Commission are based on events that have not taken place: the use of the procedure set forth in Article 98 *bis* to appoint the third member of the Expert Commission, and the submission to the Expert Commission of questions that had not been discussed by the parties before. According to TGH: "if the CNEE's list of discrepancies had been accepted" and if Article 98 *bis* had been applied, there "would have" been "manipulat[ion]" of the process.[688] The use of the conditional tense is telling: none of this actually took place and, therefore, TGH's allegations are completely unfounded.

500. In truth, TGH's case is based on the fact that the CNEE understood that the opinion of the Expert Commission was only a technical opinion that did not bind the CNEE into accepting the Bates White study revised according to that opinion, and the fact that the CNEE understood that the duties of the Expert Commission did not include the approval of that study.[689]

501. The position adopted by the CNEE is correct according to the regulatory framework. The role of the Expert Commission is set forth in LGE Article 75 in

688 Claimant's Memorial, para 267.

689 *Ibid.*, paras 267, 268, 273.

the following words "the Expert Commission shall pronounce itself [*pronunciarse*] an opinion on the discrepancies." This is all that is said in the regulatory framework about the role of the Expert Commission. TGH would like the regulatory framework to contain a provision requiring the CNEE to accept the VAD that would result from the revision of the distributor's tariff study according to the opinion of the Expert Commission. It would also like that the regulatory framework contain provisions establishing that it is for the Expert Commission to review and approve the VAD study, thereby relegating the CNEE to being a mere executor of the decisions of the Expert Commission with respect to the tariffs.

502. However, the regulatory framework contains no such provisions; much to the contrary, it limits the role of the Expert Commission to the elaboration of a technical opinion, and does not establish any other duties for the Expert Commission beyond the issuance of its report, such as approving the tariff study. Dr Aguilar explains this in detail in his report.[690]

(a) According to the regulatory framework, it is the CNEE (in its capacity as the regulator of the sector) that has the power and responsibility to approve the tariffs (LGE Articles 61 and 71, and RLGE Articles 3, 82 and 99) and the VAD (LGE Article 60, and RLGE Articles 83, 92, 98(3), and 99), is responsible for ensuring compliance with and enforcement of the LGE (LGE Article 4), and is the organ in charge of applying the LGE and the RLGE (RLGE Article 3) and, accordingly, is also responsible for ensuring that the VAD is determined in accordance with the law;

(b) In fact, the LGE establishes in precise terms the definition of the VAD ("it corresponds to the average cost of capital and operation of the distribution network of an efficient company," Article 71); it also requires the CNEE to use the VAD to determine the tariffs and to ensure that the tariffs meet the requirements set out in the LGE ("These tariffs must strictly reflect the economic cost of acquiring and distributing electricity," Article 76).

690 Aguilar, **Appendix RER-3**, paras 10, 28-29, 46-58.

Therefore, the CNEE is the organ that must ensure that the VAD approved is correct and complies with the requirements of the LGE. If it fails to do so, the CNEE is not in compliance with its legal mandate. Such responsibility cannot be delegated to any other organ or entity;

(c) To the contrary, there is no specific provision in the LGE or the RLGE establishing that the opinion of the Expert Commission is binding for the determination of the VAD and the tariffs. In order for the opinion of the Expert Commission to be binding, an express provision to this effect would be absolutely necessary since this would have an impact on the duties and responsibilities of the CNEE, which include establishing a VAD and tariffs in accordance with the law;

(d) The Guatemalan regulatory framework must be interpreted in accordance with the principles of interpretation set out in the Law of the Judicial Organism. This law establishes that legal rules must be interpreted primarily according to their text but also according to their context.[691] It refers to the Dictionary of the Royal Spanish Academy (RAE Dictionary) for the determination of the meaning of the text.[692] The term "*pronunciarse*" (pronounce itself) in LGE Article 75 means in its pronominal version, according to the RAE Dictionary, "to declare or show oneself to be in favor or against someone or something"[693] and, according to the Pan-Hispanic Dictionary of Doubts of the Royal Spanish Academy, "to give an opinion on something";[694]

(e) The term "*pericial*" (expert-related) in LGE Article 75 derives from "*perito*" (expert), a term that, again, according to the RAE Dictionary, means a "person who, being possessed with certain scientific, artistic and technical knowledge and

691 Law of the Judicial Organism, Decree 2-89, 4 February 2005, **Exhibit R-31**, art 10.

692 *Ibid.*, art 11.

693 Dictionary of the Royal Spanish Academy, **Exhibit R-153.**

694 Royal Spanish Academy, Pan-Hispanic Dictionary of Doubts, **Exhibit R-154.**

techniques or practices reports, under oath, to the Court regarding litigious points as they relate to his or her special knowledge or experience";[695]

(f) An expert opinion in Guatemalan civil procedural law is, by definition, advisory in nature;

(g) According to LGE Article 75, the role of the Expert Commission is to pronounce itself [*pronounce itself*] on the discrepancies presented to it, nowhere does the LGE confer on the Expert Commission the power to approve the distributors' tariff studies. It is the responsibility of the CNEE, as the regulator of the sector, to make such a decision. The responsibility for making this decision falls to the CNEE in exercising its duties as regulator. TGH claims that the duties of the Expert Commission under the LGE were expanded in this case by means of the "Operating Rules" supposedly agreed upon between EEGSA and the CNEE; however, there was no such agreement and, moreover, it is inconceivable that a private agreement could have amended the LGE.

503. Therefore, TGH wrongly conceives the role of the Expert Commission in general as well as in this specific case. As Dr Aguilar explains:

> The LGE could not have provided that the EXPERT COMMISSION has the power to approve the tariff studies to be used by the CNEE to set the tariffs. This would be against the fundamental principles embodied in the LGE, according to which the CNEE is the body responsible for its enforcement, including calculating the VAD and setting tariffs. At the very least, any interpretation to the contrary would require explicit language to that effect. Instead, LGE Article 75 clearly limits the role of the EXPERT COMMISSION to pronouncing itself on the "discrepancies." It is for the CNEE, as the body responsible for the determination of the tariffs and the legality of the VAD, to determine the effects of the EXPERT COMMISSION's report. Even if the opinion of the EXPERT COMMISSION were binding, after it issues its pronouncement on the discrepancies it is the CNEE that is responsible for the

695 Dictionary of the Royal Spanish Academy, **Exhibit R-153**.

> application of the law, including for deciding – based on the law – whether the tariff study submitted by the Distributor's consultant should be modified according to the EXPERT COMMISSION's pronouncement, and whether said study can be used to determine the tariffs;[696]

504. The Expert Commission pronounced itself that the Bates White study did not incorporate the modifications legitimately required by the CNEE. For example, the Expert Commission found that the study was neither auditable nor traceable, as explained before.[697] It was then for the CNEE to make a decision regarding the consequences of the Expert Commission's pronouncement, in particular, whether the Bates White study was to be modified or whether the independent study commissioned by the CNEE was to be adopted instead.

505. All this, however, is irrelevant to this Tribunal. What is important here is that TGH has essentially submitted to this Tribunal a dispute under Guatemalan law, that is, a dispute regarding the scope of certain provisions of the LGE and the RLGE. TGH presents its own interpretation of such provisions and argues that they support its position. The CNEE interpreted the same provisions, in conjunction with others, and concluded that they supported the position that it adopted. Leaving aside the terms that TGH uses such as "arbitrary," "manipulate," alteration of the "commercial and legal environment," "mockery," etc.,[698] this dispute actually relates to differences of opinion regarding how certain provisions of the LGE and the RLGE should have been interpreted and applied.

506. Notably, TGH refers many times to *Waste Management* to support its position.[699] TGH, however, does not mention that in that case the tribunal concluded that violations of the contractual and regulatory framework by an administrative body

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696 Aguilar, **Appendix RER-3**, para 48.

697 See Section **Error! Reference source not found.**.

698 E.g., Claimant's Memorial, paras 269, 270, 272, 273.

699 Claimant's Memorial, paras 233-234, 236-237, 243.

do not lead to a violation of the international minimum standard.[700] This will only occur when there is a denial of justice.[701]

507. TGH also cites *CMS v. Argentina* and *LG&E v. Argentina*;[702] in these cases Argentina had completely dismantled the established tariff regime for the gas transportation sector through emergency legislative measures passed in 2002.[703] These cases are examined in further detail below.[704] These cases, however, are very different from the present case in which the allegations relate to a mere disagreement regarding the interpretation and application of certain provisions concerning the tariff review process, rather than the complete elimination or a substantial modification of the regulatory framework as was the case in *CMS* and *LG&E*. Moreover, none of those cases involved the application of the international minimum standard, but rather the fair and equitable treatment standard that is autonomous from customary international law.

508. TGH also cites *CME v. Czech Republic* and *PSEG v. Turkey*,[705] but these cases do not involve the application of the international minimum standard either.[706] Moreover, in *CME* there were fundamental legislative changes that made the contract between the foreign investor and its local partner illegal, which led to the rescission of the contract. In *PSEG*, the tribunal found problematic the "continuing legislative changes" regarding the corporate and tax structure of the investment as well as the constant changes to the concession agreement and the

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700 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, 30 April 2004, **Exhibit CL-46**, para 115.

701 *Ibid*, paras 129-130.

702 Claimant's Memorial, paras 270-271.

703 *CMS Gas Transmission Company v. Republic of Argentina* (ICSID Case No. ARB/01/8) Award, 12 May 2005, **Exhibit CL-17**; LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Republic of Argentina (ICSID Case No. ARB/02/1) Decision on Liability, 3 October 2006, **Exhibit CL-27**.

704 See Section IV.C.2.b

705 Claimant's Memorial, paras 269-270.

706 *CME Czech Republic B.V. v. Czech Republic* (UNCITRAL Case) Partial Award, 13 September 2001, **Exhibit CL-16**; *PSEG Global Inc. and Konya Ilgin Electrik Üretim ve Ticaret Limited Şirketi v. Republic of Turkey* (ICSID Case No. ARB/02/5) Award, 19 January 2007, **Exhibit CL-37**.

project status required by the government, which eventually left the investor with no option other than the complete abandonment of the project.[707] None of this has occurred in this case. Nor is this a case in which the administrative authority has "simply ignored" a "Constitutional Court decision upholding the rights under a contract."[708] Quite the contrary, the decisions of the Constitutional Court upheld the position adopted by the CNEE.

509. In contrast, the present case relates to a dispute regarding the interpretation and application of the regulatory framework by the regulator – in particular, the role of the Expert Commission – in which the regulator's position has been supported by the domestic courts; moreover, the regulatory framework remains in force and with no fundamental changes. The cases mentioned above make clear that a purely regulatory dispute does not constitute a breach of the international minimum standard, except when denial of justice is involved, which TGH has not alleged.

2. TGH's allegations that the CNEE mistakenly interpreted its mandate so as to include the power to reject the Bates White study and approve the Sigla study are also regulatory in nature and do not give rise to breach of the standard

510. TGH argues that the LGE and the RLGE, particularly RLGE Article 98, required the CNEE to approve the Bates White VAD study and prevented the CNEE from approving an independent study prepared by another prequalified consultant, i.e., the Sigla study.[709] Interestingly, TGH also complains about the 2007 amendment to Article 98.[710] This, however, goes against TGH's argument that the amended RLGE Article 98 did not give the CNEE the power to reject the Bates White study. This demonstrates that TGH's complaint relates to the manner in which the

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707 *PSEG Global Inc. and Konya Ilgin Electrik Üretim ve Ticaret Limited Şirketi v. Republic of Turkey* (ICSID Case No. ARB/02/5) Award, 19 January 2007, **Exhibit CL-37**, paras 250, 254.

708 *Ibid.*, para 249.

709 Claimant's Memorial, paras 266-274.

710 *Ibid.*, para 264.

CNEE interpreted Article 98, rather than its amendment. As noted previously, the 2007 amendment of RLGE Article 98 did not alter the fundamental principles of the regulatory framework.

511. TGH is wrong when it argues that the CNEE did not have the power to reject the Bates White study and approve the Sigla study. TGH misinterprets the mandate, duties, and responsibilities of the CNEE. The CNEE is the body in charge of the regulation of the electricity sector. It is the body responsible for ensuring that the LGE and the RLGE are correctly applied and complied with.[711] Pursuant to the LGE and the RLGE, the CNEE is the body responsible for: (i) defining the methodology for the calculation of the tariffs; [712] (ii) revising that methodology every five years;[713] (iii) preparing the Terms of Reference;[714] (iv) hiring professional advisors to assist in the establishment of the tariffs;[715] (v) approving or rejecting the VAD study prepared by the distributor, taking into consideration the Expert Commission's pronouncement; [716] (vi) calculating, determining, establishing, setting and structuring the electricity distribution tariffs;[717] and (vii) ensuring that the tariffs reflect "in strict form the economic cost of acquiring and distributing electric energy", that is, that the VAD meets the requirements set out in the LGE.[718] In short, the CNEE is not allowed to approve a VAD that in its view does not meet the requirements of the LGE.

512. As Dr Aguilar explains:

> The CNEE is the regulatory body that must "comply with and enforce" the LGE and RLGE (LGE Article

711 LGE, **Exhibit R-8**, art 4(a); RLGE, **Exhibit R-12**, art 3.

712 LGE, **Exhibit R-8**, arts 4(c) and 61; RLGE, **Exhibit R-12**, art 97.

713 LGE, **Exhibit R-8**, art 77.

714 *Ibid.*, art 74; RLGE, **Exhibit R-12**, art 98.

715 LGE, **Exhibit R-8**, art 5; RLGE, **Exhibit R-12**, art 32.

716 LGE, **Exhibit R-8**, art 76; RLGE, **Exhibit R-12**, arts 92, 98.

717 LGE, **Exhibit R-8**, arts 4(c), 61, 71, 76; RLGE, **Exhibit R-12**, art 99.

718 LGE, **Exhibit R-8**, art 76.

> 4(a)) and is the body responsible for the application of the LGE and RLGE (RLGE Article 3), including the legal principles and requirements that must be met by the VAD according to law. Therefore, the CNEE is the body that must ensure compliance with the LGE and RLGE, including all matters concerning the VAD, and this responsibility cannot be delegated to any other body or entity. [...]
>
> [...] The LGE thus assigned to the CNEE the role of regulator and of ensuring compliance with and the enforcement of the law and its regulation, including the responsibility of ensuring that the tariffs, in all their components, including the VAD, meet the criteria established in the law. Therefore, according to the structure of the LGE, the CNEE is the one responsible for the approval of the VAD studies and the tariffs. LGE Article 76 is clear in requiring that the tariffs approved by the CNEE "shall strictly reflect the economic cost of acquiring and distributing electric energy", which means that the CNEE is responsible for ensuring that the tariffs are established on the basis of a VAD that is correctly determined according to the LGE;[719]

513. In this case, EEGSA and Bates White were not cooperative during the tariff review process, which cast doubt on the reliability of the Bates White study. It is worth summarizing a few episodes:

(a) From the start, EEGSA and Bates White refused to submit supporting information and documentation, despite of the fact that the Terms of Reference required them to submit such documentation prior to the submission of the stage reports; without said documentation the CNEE was not able to conduct an adequate review of the distributor's study. In other words, the CNEE was not able to perform an audit of the study;[720]

(b) The Bates White study, in its different versions, was never traceable. That is to say, the cells of the Excel spreadsheets were not interlinked and,

719 Aguilar, **Appendix RER-3**, paras 10(n), 28.

720 See paras. 391-393.

moreover, contained pasted data that made it impossible to know the source of "such data". This made it impossible for the CNEE to assess the study;[721]

(c) The studies contained serious technical flaws, such as the calculation of the costs to be inputted in EEGSA's VAD (and, therefore, in the tariff), the costs of building and maintaining underground electrical networks (far more expensive than aerial networks), which, moreover, do not exist in EEGSA's actual network and were not foreseen in the Terms of Reference;[722]

(d) The studies produced absurd results, making it impossible to take them into account. The first study, dated 31 March 2008, led to a 245% increase in EEGSA's VAD (meaning that it would require tripling the tariff); one month later, a second study resulted in a 184 percent increase in the VAD; in the interim, the Chairman of EEGSA's Board of Directors, Mr. Gonzalo Pérez, made a strange visit to the CNEE during which he stated that EEGSA would consent to a 10% increase in the VAD.[723] Therefore, the CNEE could not rely on studies that produced diverging results and that did not reflect in any way the increase that EEGSA was prepared to accept by direct "negotiation" with the CNEE.

514. These non-transparent actions of EEGSA and Bates White marked the preparation of the Bates White study and illustrate the problems faced by the CNEE in supervising the study. It is paradoxical that TGH complains of the CNEE's actions, when EEGSA and Bates White themselves failed to comply with regulations.

515. The Expert Commission confirmed that the Bates White study was flawed. In particular, it noted that that study was not reliable because neither the model nor

721 *Ibid.*

722 See paras 403-405.

723 See Section III.F.6.c.

the database submitted by Bates White was auditable, they were not traceable and interlinked[724] and were not accompanied by a supporting database.[725] In its pronouncement, the Expert Commission stated that "there must be links among all of the models made so that these calculations can be reproduced" and it must be possible for them "to be corroborated by the CNEE."[726] Likewise, the study did not include the international reference prices which were necessary for the CNEE to evaluate the prices computed by Bates White in the model.[727] Moreover, the VNR was overvalued.[728]

516. In the light of this, the CNEE concluded that it was not possible to use the Bates White study to establish the VAD and the tariffs. As the CNEE could not, among other things, perform an audit of the model, compare the costs used against the database, and verify the prices used, it could not approve the Bates White study and become responsible for its flaws. The CNEE believed that the regulations not only allowed, but also required it to approve a tariff study that was reliable.

517. The VAD approved by the CNEE was calculated according to strictly technical criteria, based on a study prepared by an independent and prequalified consultant, the well-known company Sigla, which had satisfactorily prepared other studies for EEGSA in the past.[729] In its decisions of 18 November 2009 and 24 February 2010, the Constitutional Court ruled in favor of the position adopted by the CNEE.

518. In any event, TGH's allegations relate to supposed irregularities and the incorrect application of the regulatory framework by CNEE. According to the jurisprudence, this is not enough to establish a violation of the fair and equitable treatment standard. These are questions of domestic law that must be submitted to

724 Report of the Expert Commission, 25 July 2008, **Exhibit R-87**, pp 15-17, 41, 71.

725 *Ibid*, p 41.

726 *Ibid*, p 17.

727 *Ibid*, pp 34-36.

728 See Report of the Expert Commission, 25 July 2008, **Exhibit R-87**, p 83 (Underground Networks); p 78-79 (Outlets by Transformation Center) and p 94 (Service Connections).

729 See para. 319.

the local courts. Only if the courts fail to dispense justice can an investor present a claim of violation of the international minimum standard.

519. As the tribunal stated in *Waste Management*, incorrect application of the law "is not to be equated with a violation of Article 1105 [fair and equitable treatment]" if "some remedy is open to the [claimant] to address the problem," and if it is not possible to "discern in the decisions of the [local] courts any denial of justice."[730] TGH, however, does not claim denial of justice.

3. Likewise, TGH's allegations regarding the VAD's calculation concern a regulatory question that does not give rise to a breach of the standard

520. TGH argues that the VAD approved by the CNEE was too low. As explained above, TGH is mistaken.[731]

521. The calculation of the VAD is technically complex and is regulated by the LGE as follows: the VAD must reflect the "average cost of capital and operating costs of a distribution network of a reference efficient company, operating within an area of specific density" (Article 71); it must include as basic components the "[c]osts associated with the user, regardless of his demand for power and energy," "[a]verage distribution losses," "[c]osts of capital, operation and maintenance associated with the distribution" (Article 72); the cost of capital is calculated on the basis of the "New Replacement Value of an economically-dimensioned distribution network" (Article 73).[732]

522. It is noteworthy that TGH, while complaining about the VAD approved by the CNEE and basing its claim for damages on the VAD which, according to it, should have been adopted instead,[733] does not submit evidence from an expert on

730 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, 30 April 2004, **Exhibit CL-46**, paras 115, 130.

731 See Section III.F.

732 LGE, **Exhibit R-8**, arts 71-73.

733 Claimant's Memorial, paras 288-292.

electricity tariffs and VNR calculation for a distribution network explaining how the provisions listed above should be applied. This issue is dealt with only in the report of TGH's financial and valuation expert who limits himself to applying, without a critical analysis, the Bates White study of 28 July 2008.[734] Guatemala, on the other hand, has presented Engineer Damonte's report, which concludes:

> The main findings of this report are that, having studied the history of the Case, especially the Memorial and B. Kaczmarek's Report, I reach the following conclusions:
>
> a) That the BW 5-5-08 study is inapplicable for the calculation of EEGSA tariffs, since it repeatedly violates the CNEE Terms of Reference applicable
>
> b) That the BW 5-5-08 study violates a basic principle of financial math: It calculates EEGSA's return on a capital base without depreciating.
>
> c) That the BW 5-5-08 study, as a result of applying a number of unacceptable assumptions, results in a notably overvalued VNR and VAD
>
> d) That the BW 28-7-08 study did not comply properly with incorporating all the pronouncements of the Expert Commission, and therefore its results cannot be applied for EEGSA's tariff determination. The failure to apply several of the pronouncements and the misapplication of others, perpetuates some of the significant overvaluations of the VNR and the VAD found in the earlier BW studies, so that the application of BW 28-7-08 would produce unwarranted and significant financial damage to the consumers at-tended by EEGSA.
>
> e) That having analyzed the VNR and VAD values sanctioned by the CNEE for the third tariff period, using benchmarking tools based on a representative sample of 67 Latin American companies, the following conclusions are reached:
>
> The values applied by the CNEE in the third tariff period are reasonable

734 Kaczmarek, **Appendix CER-2**, para 153.

- The VNR value of the EEGSA study conducted by NERA in 2003, as well as the VNR of the three studies presented by BW in 2008, are clearly well above the results of the Benchmarking applied to EEGSA.[735]

523. Accordingly, the VAD approved by the CNEE was correct. In any event, it is clear again that the controversy revolves around the interpretation and application of the regulatory framework – in this specific instance, with respect to technical issues such as calculation of the economic cost of the service and the normal profitability that an investor should obtain. The essence of TGH's argument is that the CNEE set a VAD that is not in accordance with the provisions of the regulations. This allegation is unfounded, but even if it were not, it would have led to nothing but a breach of the provisions of domestic law in question. It would not have led to a violation of the international minimum standard.

524. It is important to note that the Constitutional Court, in its decision of 18 November 2009, reaffirmed EEGSA's right to a fair tariff established in accordance with the regulatory framework.[736] This framework has not changed in any significant manner; EEGSA continues to enjoy its tariff-related rights. EEGSA's acquisition by EPM is evidence of this.

4. Aware of the problems with its claim, TGH attempts to label CNEE's conduct as "arbitrary" without in any way defining this concept or providing support for its broad allegations

525. TGH's sensational allegations that the conduct of the CNEE was "arbitrary," without even elaborating on the concept of arbitrariness, constitute a clear sign that TGH is aware of the flaws in its argument.

735 Damonte, **Appendix RER-2**, para 8.

736 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, 18 November 2009, **Exhibit R-105**, p 32-33.

526. TGH uses the term arbitrariness no fewer than twenty times to characterize the measures at issue.[737] The concept of arbitrariness is a central part of its argument. Such is the case that the title of the section in which TGH presents its allegations that Guatemala has violated the Treaty is "Guatemala failed to fulfill the obligation set forth in the Treaty to give TECO's investment fair and equitable treatment by ignoring the Expert Commission's report and setting tariffs based on its own studies in an arbitrary manner and ignoring the corresponding legal framework."[738]

527. The absence of a more elaborate analysis regarding the concept of arbitrariness and its application to the facts of this case is revealing. It is clear that there is no substance whatsoever behind this sensationalist label. Knowing that the facts do not favor its position, TGH hopes that the use of the word "arbitrary" will suffice to transform its claim into a Treaty claim.

528. In any case, there has been no arbitrariness in this case. First, it is important to define the concept of arbitrariness in international law. With respect to this concept, the International Court of Justice (ICJ) stated in the *ELSI* case that:

> Arbitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law […].
>
> Thus, the Mayor's order was consciously made in the context of an operating system of law and of appropriate remedies of appeal, and treated as such by the superior administrative authority and the local courts. These are not at all the marks of an "arbitrary" act.[739]

529. The Court held that acts of a public body that are irregular or breach a legal provision are not *per se* arbitrary. In order to be arbitrary, such acts must be

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737 Claimant's Memorial, paras 6, 10, 108, 167, 189, 225, 227, 228, 258, 259, 263, 266-268, 272, 276 and titles of Sections II.F.3, III.A, III.C.

738 *Ibid.*, title of Section III.C. (Emphasis added).

739 *Elettronica Sicula S.p.A. (ELSI) (USA v. Italy)* [1989] ICJ Rep 15, 20 July 1989, **Exhibit RL-1**, paras 128-129.

contrary to the rule of law. In particular, there is no arbitrariness when the acts, although subject to criticism, were carried out in the context of a functioning legal system with appropriate legal remedies available.

530. Moreover, the jurisprudence has rejected the possibility of speaking of arbitrariness when the act in question "constituted the normal exercise of the regulatory duties"[740] or is the product of "a rational decision-making process,"[741] or was made "in the course of exercising its statutory obligations to regulate."[742]

531. As explained above,[743] and summarized below, the CNEE's actions upon which TGH bases its claim are well grounded in the LGE and principles of Guatemalan law. This has been confirmed by the highest judicial authority in Guatemala, the Constitutional Court.

532. Even if the CNEE were to have committed an error, irregularity, or illegality, which is not the case, this would not constitute arbitrariness under international law for the following reasons:

(a) The CNEE acted in the exercise of its regulatory powers, duties, and responsibilities;

(b) Its decisions were the result of rational decision-making processes;

(c) The CNEE interpreted and applied the regulatory framework according to its best understanding and followed at all times the rule of law principles, including by defending its position before the Guatemalan courts;

740 *Lauder v. Czech Republic* (UNCITRAL Case) Final Award, 3 September 2001, **Exhibit CL-38**, para 255.

741 LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Republic of Argentina (ICSID Case No. ARB/02/1) Decision on Liability, 3 October 2006, **Exhibit CL-27**, para 158.

742 *Genin et al. v. Republic of Estonia* (ICSID Case No. ARB/99/2) Award, 25 June 2001, **Exhibit RL-3**, para 370.

743 See Section III.F.

(d) The decisions of the CNEE were made in the context of a functioning legal system with appropriate legal remedies available; and

(e) The CNEE's position was endorsed by the Constitutional Court in well reasoned and supported decisions.

533. All of these are not, as noted by the ICJ in *ELSI*, "the marks of an 'arbitrary' act."[744]

534. Moreover, the international minimum standard is not breached by any arbitrariness, but only that which is particularly manifest and shocking. As the tribunal stated in *Glamis Gold v. the United States*:

> [T]o violate the customary international law minimum standard of treatment codified in Article 1105 of the NAFTA, […] a breach requires something greater than mere arbitrariness, something that is surprising, shocking, or exhibits a manifest lack of reasoning.[745]

5. The decisions of the Constitutional Court are correct. Moreover, TGH does not allege denial of justice

535. TGH complains about the decisions of the Constitutional Court of 18 November 2009 and 24 February 2010,[746] but, as already noted, it does not allege denial of justice. Apart from stating that the Court "appears to have been 'influenced by political considerations […]'",[747] without elaborating or providing supporting

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744 *Elettronica Sicula S.p.A. (ELSI) (USA v. Italy)* [1989] ICJ Rep 15, 20 July 1989, **Exhibit RL-1**, para 129.

745 *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit CL-23**, paras 616-617. Also see *Cargill, Incorporated v. United Mexican States* (ICSID Case No. ARB(AF)/05/2) Award, 18 September 2009, **Exhibit CL-12**, para 293 (in which the tribunal held that, in order for there to be arbitrariness, there must be "an unexpected and shocking repudiation of a policy's very purposes and goals," or a gross subversion of "a domestic law or policy for an ulterior motive.").

746 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, 18 November 2009. **Exhibit R-105;** Decision of the Constitutional Court, Case File 3831-2009, 24 February 2010, **Exhibit R-110**.

747 Claimant's Memorial, para 212. See also, paras 275, 277.

evidence, TGH limits itself to alleging that the Court ruled "wrongly."[748] As explained above, even if this were true, a mere judicial error does not suffice to establish a violation of an investment treaty. The claimant must prove that there was denial of justice,[749] which TGH has not alleged, and which did not occur.

536. TGH makes another mistake when it seeks to question the decisions of the Constitutional Court on the basis of the report of Mr Alegría. Mr Alegría focuses his report on the manner in which the Constitutional Court interpreted the expression "pronounce itself" in LGE Article 75, which concerns the role of the Expert Commission.[750] According to Mr Alegría, the ordinary meaning of "pronounce itself" is to hand down a final decision.[751]

537. As noted above,[752] in matters of textual interpretation, Guatemalan law refers to the RAE Dictionary.[753] The RAE Dictionary gives six definitions for the verb "to pronounce." The RAE dictionary explains that "meaning" is "[e]ach meaning of the word according to the context in which it appears."[754] Accordingly, it is clear that the correct meaning of any word depends on the context in which it is used.

538. An examination of the meanings listed for "to pronounce" by the RAE Dictionary reveals that the only pronominal meaning ("pronounce itself," as stated in LGE Article 75) of the verb is "[t]o declare or show oneself to be in favor of or against someone or something."[755] This was the meaning to which the Constitutional

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748 Claimant's Memorial, para 218. See also, paras 212, 213, 215.

749 *Robert Azinian et al. v. United Mexican States* (ICSID Case No. ARB(AF)/97/2) Award, 1 November 1999, **Exhibit RL-2**, para 99 ("The possibility of holding a State internationally liable for judicial decisions does not, however, entitle a claimant to seek international review of the national court decisions as though the international jurisdiction seised has plenary appellate jurisdiction. This is not generally, and it is not true for NAFTA. *What must be shown is that the court decision itself constitutes a violation of the treaty.* Even if the Claimants were to convince this Arbitral Tribunal that the Mexican courts were wrong with respect to the invalidity of the Concession Contract, this would not *per se* be conclusive as to a violation of NAFTA. More is required; the Claimants must show either a denial of justice, or a pretence of form to achieve an internationally unlawful end." (Emphasis in the original).

750 Alegría, **Appendix CER-1**, paras 76–78. Also see above, paras 79–80

751 *Ibid.*, para 76.

752 See para. 502

753 Law of the Judicial Organism, Decree 2-89, 4 February 2005, **Exhibit R-31**, art 11.

754 Dictionary of the Royal Spanish Academy, **Exhibit R-153**. (Emphasis added).

755 Diccionario de la Real Academia Española, **Anexo C-50**. (Emphasis added).

Court referred when it analyzed the text of LGE Article 75.[756] Similarly, the Pan-Hispanic Dictionary of Doubts of the RAE explains that to "pronounce itself" means "to manifest an opinion about something."[757] That is precisely the task of a commission of experts; this is also in line with the views and the declaration of Mr Bastos in his testimony at the hearing in the *Iberdrola* case.[758]

539. Professor Alegría makes a mistake when he favors the meaning of "pronounce itself" that defines this term as "to publish the ruling or lawsuit" for the mere fact that the RAE Dictionary states that this meaning applies in the legal context. As previously explained,[759] the rule of contextual interpretation requires interpreting the expression "pronounce itself" together with the word "expert." This is so because according to LGE Article 75 it is an expert commission that pronounces itself; it is not the role of an expert to issue a ruling or binding decision, but only "[t]o declare or show itself to be in favor of or against someone or something."[760]

540. The Constitutional Court interpreted the role of the Expert Commission in the only manner possible in the light of the responsibilities of the CNEE in tariff matters and the determination of the VAD; this is the conclusion of Dr Aguilar:

> In summary, the Decisions of the Constitutionality Court dated November 18th, 2009 and February 24th, 2010 are properly reasoned and well founded and, in my opinion, absolutely correct from the standpoint of the regulatory framework and the Guatemalan legal system in general. The decisions are based on the undisputable principle that the CNEE is the regulatory body that must "comply with and enforce" the LGE and its regulations (LGE Article 4(a)), including the legal principles and criteria that must be met by the VAD according to the law. According to LGE Article 76, the

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756 Decision of the Constitutional Court, Consolidated Case Files 1836-1846-2009, 18 November 2009, E**xhibit R-105**, p 23.

757 Royal Spanish Academy, Pan-Hispanic Dictionary of Doubts, **Exhibit R-154**.

758 Transcription of the final hearing for ICSID Case No. ARB/09/5, **Exhibit R-140**, Tr., Day Two, Bastos, p 650:8–11 ("The truth is that the mistake comes from saying "arbitration" instead of "expert report." The truth is that our work was not arbitration: it was an expert report.").

759 See above, para. 212.

760 Dictionary of the Royal Spanish Academy, **Exhibit R-153**. (Emphasis added).

> rates approved by the CNEE "shall strictly reflect the economic cost of acquiring and distributing electric energy". The CNEE could not fulfill this function if it were the Expert Commission the one that were in charge of approving the VAD studies and if the CNEE had to accept the EXPERT COMMISSION's decision.[761]

C. TGH FAILS TO DEMONSTRATE THAT ITS LEGITIMATE EXPECTATIONS HAVE BEEN VIOLATED BY A FUNDAMENTAL CHANGE TO THE REGULATORY FRAMEWORK

1. TGH refers to supposed legitimate expectations that it would have acquired at the time of EEGSA's privatization when TGH did not exist yet

541. TGH also alleges that the CNEE violated its legitimate expectations and thereby violated the international minimum standard of fair and equitable treatment.[762] Oddly, TGH refers to supposed legitimate expectations that it would have acquired or that would have been created at the time that EEGSA was privatized, when TGH had yet to come into existence.

542. Guatemala became aware of this fact during the document production process conducted pursuant to point 14 of the Minutes of the First Session of the Tribunal. In its Notice of Arbitration, TGH limited itself to stating that its investment in EEGSA was "indirect," without providing any explanation or supporting evidence in that regard.[763] In its Memorial, TGH did not even mention this matter. In light of this, Guatemala requested the production of documents on the corporate structure of the investment.[764] TGH submitted several diagrams without providing any additional explanation.[765] From those diagrams, Guatemala was able to conclude that the corporate structure of the investment had undergone broad

761 Aguilar, **Appendix RER-3**, para 68.

762 Claimant's Memorial, paras 259–280.

763 Notice of Arbitration, paras 14, 26.

764 Letter from Freshfields to White & Case, 7 November 2011, **Exhibit R-142**.

765 Letter from White & Case to Freshfields, 18 November 2011, **Exhibit R-143**. See the diagrams in **Exhibit R-158**.

changes since EEGSA's privatization in 1998. In particular, Guatemala discovered that TGH was only created in 2005, and that it acquired its indirect shareholding in EEGSA that same year.

543. Guatemala brought this fact to TGH's attention and requested additional documents on the corporate changes that took place,[766] noting the incorrectness of the statement contained in TGH's Notice of Arbitration that "[s]ince 1998, TGH, together with Iberdrola and EDP, have held an approximately 81% controlling interest in EEGSA.[767]

544. Given TGH's refusal to provide those documents,[768] Guatemala submitted an application to the Tribunal according to point 14 of the Minutes of the First Session of the Tribunal requesting the Tribunal to order TGH to provide the relevant documents.[769] Only then, in a letter submitted on 13 January 2012, did TGH agree to provide documents and recognize that it had previously made "inadvertent misstatements" when it asserted that it had held its share in EEGSA since 1998.[770]

545. Whatever the case, due to its insistence Guatemala was able to clarify this issue, and also to realize that the error recognized by TGH is not the only one that TGH has committed with respect to the issue of the time at which it made its investment. TGH's Memorial is plagued with incorrect statements regarding TGH's supposed actions and presumed expectations in 1998. For instance, statements using the terms "the Claimant" and "TECO" to refer to TGH:[771]

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766 Letter from Freshfields to White & Case, 29 December 2011, Exhibit R-145.

767 Notice of Arbitration, para 14.

768 Letter from White & Case to Freshfields, 3 January 2012, Exhibit R-146.

769 Letter from Freshfields to White & Case, 4 January 2012, Exhibit R-147.

770 Letter from White & Case to Freshfields, 13 January 2012, Exhibit R-148.

771 According to paragraph 1 of the Claimant's Memorial, the Claimant is also referred to as "TECO" throughout the Memorial.

- "[I]n the late 1990s, Guatemala sought – and obtained from Claimant [TGH] […];"[772]
- "Claimant [TGH] decided to invest in EEGSA as part of a consortium […];"[773]
- "In April 1998, Salomon Smith Barney prepared a Preliminary Information Memorandum […], which was sent to the strategic investors, including TECO [TGH]."[774]
- "TECO [TGH] was interested in investing in EEGSA and 'believed that its privatization […]';"[775]
- "'The laws [...] were central to [TGH's] decision to participate in the bid to privatize EEGSA.';"[776]
- "TECO [TGH] performed extensive due diligence […];"[777]
- "[I]n promoting EEGSA's privatization, Guatemala informed potential investors, including TECO [TGH] […]."[778]

546. In fact, all expectations TGH claims to have with respect to the regulatory framework are apparently based on its supposed understanding of that framework in 1998, as well as the presumed guarantees or promises made to TGH when EEGSA was privatized. It is clear that this is not possible. TGH could not have had any expectation, nor could it have received any guarantee, security or promise

772 Claimant's Memorial, para 3.

773 *Ibid.*, para 45.

774 *Ibid.*, para 49.

775 *Ibid.*, para 56.

776 *Ibid.*, para 57. See the English version of the Claimant's Memorial where it becomes clear that "our decision" refers to TECO.

777 *Ibid.*, para 59.

778 *Ibid.*, para 278.

dating back to the time of EEGSA's privatization; this is so because TGH did not yet exist at that time.

547. In its letter of January 13, 2012, TGH suggests that none of this is important and that the expectations held by other companies in its group in 1998 are automatically and retroactively transferred to TGH.[779] TGH does not explain how this could have occurred.

548. The legitimate expectations theory is fundamental to TGH's claim. It is not possible to attempt to solve an issue that is so central to this case, even according to TGH itself, with an unheard of and unexplained theory of transferred expectations. Case law is clear that the legitimate expectations that are protected by international law are those of each individual investor at the time that the initial investment is made.[780]

549. In sum, TGH does not allege or prove the existence of any legitimate expectation of its own in this case.

6. In any event, TGH's arguments regarding legitimate expectations do not have any legal or factual basis

550. In its analysis of the issue of legitimate expectations, TGH does not cite even one case in which a tribunal found that the international minimum standard was violated due to a violation of legitimate expectations. It only cites cases regarding the fair and equitable treatment standard that is autonomous from customary international law.[781]

551. In any event, the jurisprudence does not recognize a violation of legitimate expectations in cases where, at most, there was a failure to comply with the regulations (assuming TGH were correct on this issue, which is not the case); nor

779 Letter from White & Case to Freshfields, 13 January 2012, Exhibit R-148.

780 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No. ARB/05/8) Award, 11 September 2007, **Exhibit RL-10**, para 331.

781 Claimant's Memorial, paras 245–258.

when, at most, there have been isolated amendments to the regulatory framework that have not derogated or abolished the basic premises of such framework. This is true regardless of whether the case law relates to the fair and equitable treatment standard as part of the international minimum standard or as a separate standard that may be more demanding of the State.

a. The fair and equitable treatment standard does not protect just any expectation, but rather only those based on specific commitments of legal stability, which are not present in this case

552. In any event, the autonomous fair and equitable treatment standard (which is not the standard applicable in this case) does not protect simply any expectation of the investor. In particular, it does not protect an investor's ordinary expectation that a government authority will not breach an administrative contract or will not commit any irregularities in the application of the relevant regulations. These are disputes of domestic law over which the domestic courts have jurisdiction.

553. This is what stems from the case law mentioned above, in which it is held that the misapplication of domestic law on the part of a regulator does not lead to a violation of the international minimum standard or of the fair and equitable treatment standard:[782]

(a) *Genin v. Estonia*:

> [W]hile the Central Bank's decision to revoke the EIB's license invites criticism, it does not rise to the level of a violation of any provision of the BIT.[783]

(b) *ADF*:

> [S]omething more than simple illegality or lack of authority under the domestic law of a State is necessary to render an act or measure inconsistent with the

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782 See Section IV.A, above.

783 *Genin et al. v. Republic of Estonia* (ICSID Case No. ARB/99/2) Award, 25 June 2001, **Exhibit RL-3**, para 365.

> customary international law requirements of Article 1105(1). […].[784]

(c) *SD Myers*:

> [A] Chapter 11 tribunal does not have an open–ended mandate to second–guess government decision–making.[…] The ordinary remedy, if there were one, for errors in modern governments is through internal political and legal processes […].[785]

(d) *Thunderbird*:

> [A]cts that would give rise to a breach of the minimum standard of treatment prescribed by the NAFTA and customary international law as those that, weighed against the given factual context, amount to a gross denial of justice or manifest arbitrariness falling below acceptable international standards.[786]

(e) *Saluka*:

> […] The Treaty cannot be interpreted so as to penalize each and every breach by the Government of the rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State.[787]

(f) *GAMI*:

> GAMI has given clear examples of the failure to apply important elements of Mexican regulations. […] Suits on the grounds of maladministration could be filed with Mexican courts and tribunals. In fact, as failures to comply with Mexican administrative law, they cannot be filed in any other jurisdiction. […] GAMI has not in

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784 *ADF Group Inc v. United States of America* (ICSID Case No. ARB(AF)/00/1) Award, 9 January 2003, **Exhibit CL-4**, para 190.

785 *SD Myers Inc v. Canada* (UNCITRAL Case) First Partial Award, 13 November 2000, **Exhibit CL-41**, paras 261-263.

786 *International Thunderbird Gaming Corporation v. United Mexican States* (UNCITRAL Case) Award, 26 January 2006, **Exhibit CL-25**, para 194.

787 *Saluka Investments B.V. v. Czech Republic* (UNCITRAL Case) Partial Award, 17 March 2006, **Exhibit CL-42**, para 442.

> the least been able to prove that there has been an "outright and unjustified repudiation" of the pertinent provisions. […].[788]

(g) *Waste Management*:

> [Failure to perform] is not to be equated with a violation of Article 1105, provided that it does not amount to an outright and unjustified repudiation of the transaction and provided that some remedy is open to the creditor to address the problem. […].[789]

(h) *Parkerings*:

> [M]any tribunals have stated that not every breach of an agreement or of domestic law amounts to a violation of a treaty. […] In most cases, a preliminary determination by a competent court as to whether the contract was breached under municipal law is necessary. […].[790]

554. If BITs protected any given expectation, then any regulatory and contractual breach or small amendment to a regulation would automatically be a violation of international law. This is not the case, as otherwise the international law protections would have the same reach and content as domestic law; moreover, this would prevent any adaptation or evolution of a regulatory framework.

555. *Parkerings v. Lithuania* illustrates this point. In *Parkerings*, the tribunal examined the question of whether the fact that a municipality had committed certain irregularities in the process of verifying the investor's compliance with the terms of a contract and in the subsequent termination of that contract constituted a breach of the fair and equitable treatment standard on the grounds that it frustrated the investor's legitimate expectations. The tribunal stated:

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788 *GAMI Investments, Inc v. Mexico* (UNCITRAL Case) Final Award, 15 November 2004, **Exhibit RL-7**, paras 100, 103, 104.

789 *Waste Management Inc. v. United Mexican States* (ICSID Case No. ARB(AF)/00/3) Award, 30 April 2004, **Exhibit CL-46**, para 115.

790 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No. ARB/05/8) Award, 11 September 2007, **Exhibit RL-10**, paras 315-316.

The Claimant alleges a violation by the Municipality of Vilnius of its obligation to use its best efforts to ensure that the Government's laws and decrees furthered the successful development of the parking system. The Claimant alleges that following the different modifications of laws, it was deprived of various sources of income in violation of the Agreement. Moreover, the Claimant accuses the Representative of the Municipality and notably the Mayor of failing to act in good faith to protect and respect the Agreement and especially the economic interest of the Claimant in the performance of the Agreement.

It is evident that not every hope amounts to an expectation under international law. The expectation a party to an agreement may have of the regular fulfillment of the obligation by the other party is not necessarily an expectation protected by international law. In other words, contracts involve intrinsic expectations from each party that do not amount to expectations as understood in international law. Indeed, the party whose contractual expectations are frustrated should, under specific conditions, seek redress before a national tribunal. As stated by the Tribunal in *Saluka*, "*[t]he Treaty cannot be interpreted so as to penalize each and every breach by the Government of the Rules or regulations to which it is subject and for which the investor may normally seek redress before the courts of the host State*."

In the case at hand, the Claimant alleges that the Municipality of Vilnius frustrated its legitimate expectation in violation of Article III of the Treaty […] However, the Tribunal considers that the Claimant's expectations are, in substance, of a contractual nature. The acts and omissions of the Municipality of Vilnius, in particular any failure to advise or warn the claimant of likely or possible changes to Lithuanian law, may be breaches of the Agreement but that does not mean they are inconsistent with the Treaty.

> In conclusion, the Arbitral Tribunal finds that the Claimant has not been deprived of any legitimate expectation in violation of Article III of the Treaty.[791]

556. The foregoing is applicable to the case at hand. Every person expects the other party to an agreement or regulatory procedure to follow the applicable rules and provisions. This expectation is not the legitimate expectation that is protected under international law pursuant to the fair and equitable treatment standard. When this type of contractual or regulatory expectation is frustrated, the remedy is access to the domestic courts.

557. As the tribunal stated in *Glamis Gold*, "[m]erely not living up to expectations cannot be sufficient to find a breach of Article 1105 of the NAFTA. […]."[792]

558. The legitimate expectations that are protected by the fair and equitable treatment standard are something entirely different. In order for these expectations to arise, the investor must have received specific promises or guarantees that the State would not make any changes to the legal framework existing at the time that the investment was made. The classic example is a legal stability clause contained in an investment contract. In the words of the tribunal in *Parkerings*:

> It is each State's undeniable right and privilege to exercise its sovereign legislative power. A State has the right to enact, modify or cancel a law at its own discretion. Save for the existence of an agreement, in the form of a *stabilization* clause or otherwise, there is nothing objectionable about the amendment brought to the regulatory framework existing at the time an investor made its investment. As a matter of fact, any businessman or investor knows that laws will evolve over time. […]

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791 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No. ARB/05/8) Award, 11 September 2007, **Exhibit RL-10**, paras 343-346. (Underlining added; italics in the original). Also see *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana* (ICSID Case No. ARB/07/24) Award, 18 June 2010, **Exhibit RL-14**, paras 335-337.

792 *Glamis Gold Ltd. v. United States of America* (UNCITRAL Case) Award, 8 June 2009, **Exhibit CL-23**, para 620. (Emphasis added).

> […] an investor must anticipate that the circumstances could change, and thus structure its investment in order to adapt it to the potential changes of legal environment.[793]

559. Similarly, the tribunal in *EDF v. Romania* stated:

> The idea that legitimate expectations, and therefore FET, imply the stability of the legal and business framework, may not be correct if stated in an overly-broad and unqualified formulation. The FET might then mean the virtual freezing of the legal regulation of economic activities, in contrast with the State's normal regulatory power and the evolutionary character of economic life. Except where specific promises or representations are made by the State to the investor, the latter may not rely on a bilateral investment treaty as a kind of insurance policy against the risk of any changes in the host State's legal and economic framework. Such expectation would be neither legitimate nor reasonable.
>
> Further, in the Tribunal's view, the FET obligation cannot serve the same purpose as stabilization clauses specifically granted to foreign investors.[794]

560. There was no specific commitment of legal stability in the present case. In this regard, the Contracts literally and expressly provide that EEGSA:

> [I]s obligated to fulfill all provisions set forth in the *Law of General Electricity* and its Regulations, or <u>any amendments thereto, as well as other regulations and provisions of general application</u>. […].[795]

561. In short, there is no legal stability clause. Much to the contrary, EEGSA, and therefore TGH, have expressly agreed that any legislative and regulatory changes

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793 *Parkerings-Compagniet AS v. Lithuania* (ICSID Case No ARB/05/8) Award, 11 September 2007, **Exhibit RL-10**, paras 332-333. (Emphasis in the original).

794 *EDF Services (limited) v. Romania* (ICSID Case No. ARB/05/13) Award, 8 October 2009, **Exhibit RL-13**, paras 217-218.

795 Authorization Agreements for the Departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, 15 May 1998, **Exhibit C-31**, Clause 20**;** Final Electricity Authorization Agreement for the Departments of Chimaltenango, Santa Rosa and Jalapa, 2 February 1999, **Exhibit R-20**, Clause 20.

undertaken are fully applicable to them. Such flexibility is important in a contract that covers a period of 50 years, since it will be necessary in this period to introduce changes to improve the regulatory framework according to the lessons learned through its operation.

562. In view of this, TGH invokes the Preliminary Informative Memorandum and the Memorandum of Sale prepared by Salomon Smith Barney, and the *Roadshow* Presentation.[796] Apart from the fact that these are non-binding documents,[797] they do not address the issues raised by TGH. These documents merely contain a general description of the regulatory framework. Therefore, they are not a stability clause, nor do they have the function of one. There is nothing in these documents stating:

(a) That the CNEE does not have authority to approve independent tariff studies that in its view better conform to the regulations; or

(b) That the Expert Commission's pronouncement is binding or that the Expert Commission is the body responsible for approving the tariff studies; or

(c) Much less, what the specific outcome of each tariff review must be by providing in advance the VAD or VNR amounts.

563. Quite to the contrary, the documents in question emphasize the CNEE's authority to approve the VAD studies and set the tariffs. For instance, the Memorandum of Sale explained in clear terms that the CNEE, a technical body independent from

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796 Claimant's Memorial, paras 260-261, and footnotes 994, 1001.

797 As stated in the Sales Memorandum:

> Only such representations and warranties as contained in a final purchase agreement shall have legal effects. No information contained herein is or should be regarded as a future promise or statement. […] Potential buyers shall carry out their own research, conducting an analysis of the terms of the corporate capitalization and the sale of EEGSA's shares owned by the State, in addition to the assets, the business and the market described herein.

Solomon Smith Barney, "EEGSA: Memorandum of Sale," May 1998, **Exhibit R-16**, p 2.

the MEM (in terms of its functions and budget), would be the sector's regulatory and monitoring body, having the authority to enforce the LGE and set the tariffs.[798]

564. TGH claims that it understood these documents to mean that the Expert Commission's opinion was binding, and that the CNEE could not reject the report of the distributor's consultant. However, despite the fact that Guatemala requested TGH to produce documents demonstrating TGH's understanding of the regulatory framework at the time the investment was made,[799] TGH did not produce even a single document. TGH claims to have performed a due diligence assessment of the Guatemalan regulatory framework,[800] but it has refused to produce relevant information and documents in this regard.

565. For these reasons, it is difficult to understand how TGH could have developed any expectation of stability in the present case. Clause 20 of EEGSA's Authorization Contracts makes it crystal clear that there is no stability clause. In the absence of supporting documents, it is also difficult to understand how TGH could have developed its understanding of the regulatory framework 14 years ago. At no point did anyone or any document state that the CNEE could not as the regulator exercise its role in determining the VAD in accordance with its view of the proper interpretation of the regulatory framework. Nor did they state that the CNEE should delegate this responsibility to a temporary body such as the Expert Commission.

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798 Solomon Smith Barney, "EEGSA: Memorandum of Sale," May 1998, **Exhibit R-16**, p 54-55, where it explains:

> The basic duties of the [CNEE] are, among others, […] to set the tariffs determined by the law […]. The Commission, formally, is a technical body of the MEM with independence in terms of function and budget[;] it is the regulatory and monitoring body of the electricity sector. The basic duties of the Commission are: (1) to enforce the Law […], (4) regulate the transmission and distribution tariffs […].

799 Letter from Freshfields to White & Case, 7 November 2011, **Exhibit R-142**, Documentation A.2.

800 Claimant's Memorial, para 59; Gillette, **Appendix CWS-5**, para 8.

566. Dr Aguilar, who participated in the drafting of the LGE, explains this clearly in his expert opinion. The "depoliticization" of the tariff determination process under the new Guatemalan regulatory framework was ensured by the creation of the CNEE as a independent technical body with the responsibility of setting the tariffs and determining the VAD; not by the delegation of these functions to an expert commission. An investor could not have had any legitimate expectation in this regard:

> In order to ensure transparency in the enforcement of the law, the CNEE was created as a technical body of the MINISTRY OF ENERGY AND MINES (MEM), which was entrusted, among others, with the function of "determining tariffs for the transmission and distribution of electric energy and the methodology for its calculation," as well as the function of approving the costs of the distribution activity.
>
> The creation of the CNEE, along with its powers and functions, had the objective of ensuring the depoliticization of the enforcement of the law in the country's electricity sector;
>
> As a part of its "**functional independence**," according to the LGE, its regulations and other applicable legal provisions, **no** entity or body other than the CNEE has the power to determine or limit its functions, and much less to seize such functions, which includes, but is not limited to, the EXPERT COMMISSION referred to in LGE Article 75.[801]

b. The fair and equitable treatment standard only prohibits changes to the regulatory framework that are fundamental and that affect the legitimate expectations of an investor, which is not the case here

567. In addition to the fact that specific commitments are required to generate legitimate expectations, the frustration of those expectations requires a fundamental change to the legal framework. The premises upon which the investment was made must be dismantled by legislative or regulatory measures

801 Aguilar, **Appendix RER-3**, paras 10(b), (c), (f).

such that it can be concluded that the stability of the legal system, which had been guaranteed by a specific commitment, has been compromised. In this case, there are no such specific promises, nor have there been legislative and regulatory changes that could have dismantled the fundamental premises of the legal framework.

568. The cases related to the 2002 Argentine emergency legislation are representative. These cases illustrate the type of measures that can frustrate the legitimate expectations of the investor. Notably, TGH cites many of these awards as if they supported its position;[802] this, however, is not the case. It is worth examining the Argentinean cases in more detail.

569. In the Argentinean cases, the claims related to the dismantling of the regulatory and contractual framework for public utilities (including electricity transmission and distribution services) were caused by the adoption of emergency legislation. This legislation abolished the provisions regarding the calculation of public utility tariffs and the adjustment of the same to take into account devaluation and inflation. Accordingly, those cases involved a far more serious scenario than the one here. TGH's claims in this case relate to a dispute over the interpretation and scope of the distributor's rights (and those of the regulator) in the context of tariff reviews, rather than the abolition of such rights.

570. The first award issued against Argentina (*CMS v. Argentina*) concerned a dispute related to the gas transportation sector tariff regime. In analyzing international case law dealing with the fair and equitable treatment standard, the *CMS* tribunal stated:

> The measures that are complained of did in fact entirely transform and alter the legal and business environment under which the investment was decided and made. The discussion above, about the tariff regime and its relationship with a dollar standard and adjustment mechanisms unequivocally shows that these elements

802 Claimant's Memorial, paras 249-252, 270-271.

> are no longer present in the regime governing the business operations of the Claimant. […]
>
> […]
>
> It is not a question of whether the legal framework might need to be frozen as it can always evolve and be adapted to changing circumstances, but neither is it a question of whether the framework can be dispensed with altogether when specific commitments to the contrary have been made. The law of foreign investment and its protection has been developed with the specific objective of avoiding such adverse legal effects.[803]

571. As the tribunal noted, in *CMS* the regulatory and contractual framework had been "entirely transform[ed]" or "dispensed with altogether." It is these fundamental derogations – which in *CMS* involved the elimination of the tariff regime that provided for the calculation of tariffs in dollars as well as adjustment mechanisms – that frustrate legitimate expectations and result in a breach of the fair and equitable treatment standard.

572. It is also worth noting that the *CMS* tribunal distinguishes these fundamental changes from normal and necessary reforms and adaptations to a regulatory framework: "[i]t is not a question of whether the legal framework might need to be frozen as it can always evolve and be adapted to changing circumstances."[804] Regulations cannot remain frozen for 50 years and will, necessarily, undergo modifications and adaptations, especially during the first years of a new regulatory framework.

573. Similarly, in *LG&E v. Argentina*, the tribunal held that Argentina violated the fair and equitable treatment standard by introducing fundamental changes to the regulatory and contractual framework that frustrated the investor's legitimate expectations:

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803 *CMS Gas Transmission Company v. Republic of Argentina* (ICSID Case No. ARB/01/8) Award, 12 May 2005, **Exhibit CL-17**, paras 275, 277. (Emphasis added).

804 *Ibid.*, para 277. (Emphasis added).

> Specifically, it was unfair and inequitable to pass a law discarding the guarantee […] that the tariffs would be calculated in U.S. dollars and then converted into pesos. […]
>
> Argentina acted unfairly and inequitably when it prematurely abandoned the PPI tariff adjustments and essentially froze tariffs […] and when it refused to resume adjustments […] History has shown that the PPI adjustments that initially were supposed to be postponed have been abandoned completely and are now being "negotiated" away.
>
> […]
>
> Likewise, the Government's Resolution No. 38/02 issued on 9 March 2002, which ordered ENARGAS to discontinue all tariff reviews and to refrain from adjusting tariffs or prices in any way, also breaches the fair and equitable treatment standard.
>
> […] But here, the Tribunal is of the opinion that Argentina went too far by completely dismantling the very legal framework constructed to attract investors.[805]

574. Likewise, we can cite the *BG Group v. Argentina* award:

> Argentina […] entirely altered the legal and business environment by taking a series of radical measures, starting in 1999 […] Argentina's derogation from the tariff regime, dollar standard and adjustment mechanism was and is in contradiction with the established Regulatory Framework as well as the specific commitments represented by Argentina, on which BG relied when it decided to make the investment. In so doing, Argentina violated the principles of stability and predictability inherent to the standard of fair and equitable treatment.
>
> […]
>
> […] the Emergency Law and subsequent legislation were enacted to promote a new deal with the licensees,

805 *LG&E Energy Corp., LG&E Capital Corp. and LG&E International Inc. v. Republic of Argentina* (ICSID Case No. ARB/02/1) Decision on Liability, 3 October 2006, **Exhibit CL-27**, paras 134, 136, 138-139. (Emphasis added).

> impeding the application and execution of the original Regulatory Framework. […]
>
> In summary, […] Argentina fundamentally modified the investment Regulatory Framework […].[806]

575. Therefore, it is clear that only fundamental changes to the legal framework can result in a violation of the fair and equitable treatment standard.[807] There is no breach of legitimate expectations in a case in which, at most, there was a failure to comply with regulations (assuming TGH were correct on this issue, which is not the case). Nor is there a breach when, at most, there have been partial reforms to the regulatory framework that have not resulted in a derogation or abolishment of the basic premises of the regulation.

576. TGH has no basis to claim that the regulatory framework has been dismantled. As previously explained, TGH argues that Guatemala failed to fulfill the obligation of minimum treatment "when it arbitrarily and in complete disregard of its legal framework ignored the Expert Commission's Report and set the tariffs on the basis of its own study."[808] All of this, according to TGH, was contrary to "TECO's legitimate expectations."[809] In the words of TGH, it was the manner in which the CNEE interpreted and applied the regulatory framework that led to the frustration of TGH's legitimate expectations – not the fundamental alteration or abolition of said regulatory framework.

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806 *BG Group Plc. v. Republic of Argentina* (UNCITRAL Case) Final Award, 24 December 2007, **Exhibit CL-9**, paras 307, 309-310. (Emphasis added).

807 TGH cites *Biwater Gauff v. Tanzania*. Claimant's Memorial, paras 257, 280. This case concerns a radical change in the regulatory framework where rather than assigning an independent regulatory as required by law, Tanzania no less appointed a minister and member of Parliament as regulator. *Biwater Gauff (Tanzania) Ltd. v. United Republic of Tanzania* (ICSID Case No. ARB/05/22) Award, 24 July 2008, **Exhibit CL-10**, paras 537-539, 542, 610, 615. In no way has this occurred in the present case. TGH also cites *ADC v. Hungary* (Claimant's Memorial, para 254), which also lacks commonality with this case. In *ADC*, there was a clear legislative change resulting in the cancellation of agreements with the investor, causing a complete loss of investment. *ADC Affiliate Ltd. and ADC & ADMC Mgmt. Ltd v. the Republic of Hungary* (ICSID Case No. ARB/03/16) Award, 2 October 2006, **Exhibit CL-3**, paras 181, 184-189.

808 Claimant's Memorial, title of Section III.C.

809 Claimant's Memorial, para 259.

577. The only amendments made to the regulation in this case were those related to RLGE Articles 98 and 98 *bis* (and the latter was never applied to EEGSA). These modifications did not alter the substance of the original legal framework or the nature, powers, or role of the CNEE, as TGH claims.[810]

i. The reform of Article 98

578. As previously explained,[811] the Article 98 amendment was an ordinary regulatory evolution to put the text of that article in line with the principles of the LGE. In fact, the 2007 amendment to RLGE Article 98 relates to a subject which had already been addressed in the 2003 amendment to RLGE Article 99. Thus, as already foreseen in Article 99 since 2003, the amended Article 98 established that in the event of obstructive conduct on the part of the distributor, "the CNEE is authorized to issue and publish the corresponding tariff schedule, based on the tariff study it may independently carry out, or by making corrections to the studies initiated by the distributor."

579. Although the aforementioned change had been in effect since 2003, EEGSA never challenged that amendment before the local courts. Yet TGH now claims that the amendment was "at odds with the LGE's express provisions" and "unconstitutional" and that, therefore, it constitutes a modification of the regulatory framework.[812] It is also notable that no other distributor challenged the amended rule. Contrary to what TGH says, there is no "express provision" in the LGE that would be against that amendment. In fact, TGH admits that it is not complaining about the amendment *per se*, but rather about the manner in which the CNEE applied Article 98: "the CNEE later would interpret and apply amended RLGE Article 98 contrary to its plain meaning."[813] If TGH's claim is

810 Claimant's Memorial, paras. 264-267.

811 Cross-ref III.E.

812 Claimant's Memorial, para. 264.

813 Claimant's Memorial, para. 93.

that the CNEE erred in applying Article 98, it is then clear that it was not the amendment itself that caused harm to TGH.

580. Not only there was no alteration of the regulatory framework, but the CNEE's application of the provision in question was consistent with the fundamental principles of the LGE. The CNEE's power and responsibility for approving the distributors' tariff studies – including, therefore, the eventual rejection of said studies – is part of its functions as the regulator to "enforce" the LGE and be "responsible" for the application thereof.[814] Any given VAD is legal only to the extent that it meets the efficiency criteria set out in the Terms of Reference. The CNEE only has the authority to approve a tariff study that meets the requirements of the LGE; it cannot approve a study that does not do so. It is must be noted that the Constitutional Court backed the CNEE's conduct in this case on the grounds that the conduct in question fell within the CNEE's sphere of authority as the decision-making body in tariff-related matters, and also on the basis that the Expert Commission's pronouncement is non-binding; the Court's decision was not based on text of Article 98 as amended in 2007.

581. As Dr Aguilar explains:

> This amendment – which in no way decreases, increases, distorts, or contradicts the LGE's provisions regarding the CNEE's powers to set tariffs for the distribution of electricity – was aimed at preventing the Distributors from manipulating, determining or limiting the CNEE's powers by **failing to submit or make corrections to the tariff studies** in order to continue to benefit from the application of the tariffs in force at the time when their validity period expires. This amendment has thus complied with the legal mandate established in: i) LGE Article 60, which provides that the VAD (costs inherent to distribution activities) approved by the Commission shall correspond to the standard distribution costs of efficient companies; ii) LGE Article 61, which provides that tariffs shall be structured so as to promote the sector's economic

814 LGE, **Exhibit R-8**, Art 4(c); RLGE, **Exhibit R-12**, Art 3. See paras. 56, 202, 501, 510 above.

> efficiency; and iii) LGE Article 76, which provides that tariffs must strictly reflect the economic cost of acquiring and distributing electricity.[815]

582. Once again, one must keep in mind that amendments to regulations are normal and necessary in the case of long-term concessions (50 years, in this case). In fact, amendments were foreseen and accepted by EEGSA itself in Clause 20 of the Authorization Contracts.[816] International law does not prohibit these adaptations in any way. As the tribunal stated in *CMS*: "the legal framework […] can always evolve and be adapted to changing circumstances."[817]

ii. The amendment to Article 98 bis

583. In 2008, the RLGE was amended by the addition of Article 98 *bis.*[818] As previously explained, this article filled a lacuna in the RLGE.[819] Up until then, the constitution of the Expert Commission could be blocked if the parties (the CNEE and the distributor) did not come to an agreement regarding the third member of the Expert Commission. Pursuant to the reform, the parties must propose three candidates each, who must meet certain independence criteria with respect to the parties. If no agreement can be reached, the Ministry of Energy and Mines makes the appointment from amongst the persons nominated by the parties.

584. As the expert, Dr Aguilar, explains, this reform does not contradict the principles of the LGE, among other reasons, because the role of the Expert Commission is of technical nature and intended to assist the CNEE, which is the decision-making entity:

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815 Aguilar, **Appendix RER-3**, para 38(c).

816 Authorization Agreement for the Departments of Guatemala, Sacatepéquez and Escuintla, signed by EEGSA and the Ministry of Energy and Mines, May 15, 1998, **Exhibit C-31**, clause 20; Final Electricity Authorization Agreement for the Departments of Chimaltenango, Santa Rosa and Jalapa, February 2, 1999, **Exhibit R-20**, clause 20.

817 *CMS Gas Transmission Company v. Republic of Argentina* (ICSID Case No. ARB/01/8) Award, May 12, 2005, **Exhibit CL-17**, paras. 277.

818 Resolution No. CNEE-145-2008, May 19, 2008, published in the Diario de Centro América on July 31, 2008, **Exhibit R-72**.

819 See section III.F.7.b above.

> With regard to the procedure for selecting the third member of the EXPERT COMMISSION, it must be noted that the amendment filled a gap that, until that point, existed in the RLGE. The RLGE was silent about how to proceed if the parties failed to appoint the third member of the EXPERT COMMISSION by mutual agreement. The process could thus be blocked. Article 98BIS remedied this situation, making the constitution of the EXPERT COMMISSION possible. In any case, the MEM may appoint the third member only in the event of disagreement between the parties, and only from the candidates previously proposed by them, who must meet certain requirements of independence. Furthermore, the appointment by the MEM is a logical solution, given the EXPERT COMMISSION's role as advisor to the CNEE.[820]

585. In any event, as TGH recognizes,[821] Article 98 Bis was never applied to EEGSA in the present case, and therefore could not have caused it harm.

D. CONCLUSION: GUATEMALA HAS NOT VIOLATED THE INTERNATIONAL MINIMUM STANDARD OF TREATMENT OF TREATY ARTICLE 10.5

586. In sum, the international minimum standard – which is not the same as the autonomous fair and equitable treatment standard – protects investors only against extreme and outrageous conduct, such as conduct that is manifestly arbitrary or that constitutes a flagrant repudiation of a regulatory framework. Except in cases of denial of justice, that standard does not censure regulatory conduct that is allegedly against domestic law. The international minimum standard provides the State a broad margin of appreciation; any irregularities under domestic law are a matter to be solved by the local courts.

587. TGH's claims relate to conduct of the CNEE that is allegedly against the provisions of the regulatory framework. TGH's allegations are erroneous; but even if the CNEE had committed a mistake in interpreting the regulatory framework, this could not under any circumstances constitute a violation of the

820 Aguilar, **Appendix RER-3**, para. 44.

821 Claimant's Memorial, para. 135.

international minimum standard. The supposed illegalities were challenged before the local courts and the court of last resort on the subject, the Constitutional Court, ruled in favor of the CNEE's position. TGH, however, does not allege denial of justice, which would be the only grounds on which TGH could have claimed a violation of the standard – assuming of course that denial of justice had taken place, which is not the case here.

588. As regards its legitimate expectations argument, TGH refers to supposed expectations that it would have developed at the time of EEGSA's privatization – a point in time in which TGH did not even exist yet. These are not therefore expectations that TGH can invoke in these proceedings. In any case, TGH does not explain the basis for an expectation that the CNEE would not have the power to approve independent tariff studies that in its view better reflected the provisions of the regulations. Nor does TGH demonstrate where it is stated that the pronouncement of the Expert Commission is binding or that it is the Expert Commission that approves the tariff studies. There is nothing in the LGE and the RLGE to this effect. In fact, the powers of the CNEE, which were well known to TGH, do not allow the development of such expectations.

589. The legal reasoning behind TGH's theory of legitimate expectations is also flawed. TGH does not cite even one case involving the application of the international minimum standard of treatment in which the tribunal found that that standard was breached by a violation of the investor's legitimate expectations. Moreover, the cases on the autonomous fair and equitable treatment standard make clear that this standard does not protect just any expectation, but rather only those that are based on specific commitments of legal stability (which is not the case here). Much to the contrary, EEGSA explicitly accepted in the Authorization Contracts that any amendments to the LGE and its regulations would apply to it.

590. Apart from all this, the autonomous fair and equitable treatment standard is violated only by fundamental changes to the regulatory framework that frustrate legitimate expectations, which again is not the case here. The comparison with the

Argentinean cases invoked by TGH is illustrative: the tariff regime in this case has not been dismantled or destroyed; the only changes were those made to the RLGE, which could not logically have modified the principles embodied in the LGE – which understanding is in fact shared by TGH.

V. THE CALCULATION OF TGH'S ALLEGED DAMAGES

591. Based upon the factual and legal considerations presented in this Counter-Memorial (both jurisdictional and substantive), it remains clear that Guatemala has not breached the Treaty. However, even if this Tribunal were to consider that (i) it has jurisdiction to hear this claim; and (ii) that Guatemala violated international law by defining tariffs for the 2008-2013 period based upon the Sigla study, TGH has not suffered any damage, as we will explain in this section.

A. THE CALCULATION METHODOLOGY USED BY MR. KACZMAREK

592. TGH's expert, Mr. Brent Kaczmarek of Navigants Consulting Inc. (***NCI***), has divided the alleged damages to TGH into historical and future damages.

593. The historical damages (which the expert refers to as "lost cash flow"), includes the damages supposedly suffered between August 1, 2008 (the moment that the tariff schedule for 2008-2013 entered into effect) and October 21, 2010 (the date of the sale of Teco's shares in EEGSA). In making these calculations, the TGH expert used the discounted cash flow (***DCF*** or ***cash flow***) method in two different scenarios.

594. The *but for* scenario, which assumes that the CNEE applied the Bates White study of July 28, 2008 to determine the 2008–2013 tariffs. Mr. Kaczmarek bases his DCF calculation on a combination of the results of that study and his own projections regarding the evolution of the principal cash flow components.[822]

822 Kaczmarek, **Appendix CER-2**, paras. 153-155 and Chapter IX.

595. The actual scenario, which is the scenario in which the CNEE approves the tariffs based on the Sigla study. In the actual scenario, the expert primarily bases his DCF calculation on EEGSA financial statements.[823]

596. The future damage (called "lost value" by the expert), is the alleged difference in value of Teco's shareholdings in EEGSA as of October 21, 2010, considering EEGSA's situation as of that date to be: (i) the *but for* scenario (i.e. if the tariffs based on the Bates White study of July 28, 2008 had been approved); and (ii) the actual scenario (i.e. with the tariffs approved by the CNEE based on the Sigla study). To calculate the value of EEGSA, and TGH's participation in EEGSA in these scenarios, Kaczmarek uses the following valuation methods:

- DCF; and
- Comparable companies or comparable transactions (using publicly-traded companies and comparable transactions) (***Comparables***).

597. To calculate future damages, Kaczmarek then averages the results obtained using these two valuation methods (DCF and Comparables) in both the actual and *but for* scenarios, based on a series of *ad hoc* weighting factors.[824]

598. Based on these calculations, Kaczmarek estimates the historical damages as US$ 17.8 million and future damages as US$ 219.3 million, for a total of TGH's alleged damages amounting to US$ 237.1 million.[825]

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823 Kaczmarek, **Appendix CER-2**, paras. 153-155 and Chapter IX..

824 *Ibid.*, para. 218. Kaczmarek assigns the DCF method a weight of 60 percent, the comparable publically-traded companies method a weight of 30 percent and the comparable transaction method the remaining 10 percent. The expert justifies these values on the basis of his level of confidence in each method, which is related to the amount of available information to which he had access to for calculating each of the methods. However, he does not justify quantifiably the selected weights.

825 *Ibid.*, para. 17.

B. THE PRINCIPAL ERRORS IN MR. KACZMAREK'S VALUATION

1. DCF Valuation (*But for* scenario)

599. The principal problem with the valuation carried out by Mr. Kaczmarek is his over-estimation of EEGSA's value in the *but for* scenario. In other words, he over-estimates the value that EEGSA would have had if the CNEE had set tariffs based on the July 28 Bates White study rather than on the Sigla study.

600. As Messrs. Abdala and Schoeters explain in their report, Mr. Kaczmarek's valuation has three fundamental flaws with respect to the premises he applies in the DCF method.[826]

a. Operating Costs and Costs of Investment Projected by Mr. Kaczmarek

601. In order to calculate the historical and future damages for his *but for* scenario, Mr. Kaczmarek uses the income projections from the July 28 Bates White study as the principal premise upon which to define income.[827] This income is calculated, theoretically, to allow EEGSA to bear the operating and investment costs expected in the future. Curiously, however, when he later calculates the costs that EEGSA will actually incur in the future, Mr. Kaczmarek assumes operating and investment costs that are significantly lower (around 65 percent lower for investments and 26 percent lower for operating costs). This results in an artificial increase in the company's value. In other words, Mr. Kaczmarek's "sleight of hand" is that he requires a certain level of operating and investment costs to calculate the tariff income, but later assumes that costs would not actually be so high, thus saving the company costs and yielding an unjustified profit.

602. For example, with respect to investment costs, he over-estimates income by more than US$50 million per year.[828] Given that, as explained, the Guatemalan

826 M Abdala and M Schoeters, **Appendix RER-1**, section III.2.1.

827 *Ibid.*, para. 41.

828 M Abdala and M Schoeters, **Appendix RER-1**, para. 20

regulatory system strives for efficiency, it is clear that the regulator would not grant EEGSA a tariff based on investments that exceed efficient values to such an extent.[829] The TGH expert should have used both the income and the expenditures reflected in the tariff studies for his valuation.[830]

b. Kaczmarek's projections based on the VAD from the July 28 Bates White study in the but for scenario

(i) Mr. Kaczmarek uses the July 28 study without analyzing its reasonableness

603. Mr. Kaczmarek uses the VAD from the July 28 Bates White study as a basis for his DCF projections in order to calculate the historical and future damages in the *but for* scenario. The expert, however, uses this study without verifying whether its premises are reasonable or whether it properly includes the pronouncements of the Expert Commission in their entirety.[831] As previously explained in Section III.F.14, this study does not properly reflect the totality of the pronouncements. This was confirmed by both of the consultants to the CNEE, Mercados Energéticos,[832] and Mr. Damonte, who conducted an exhaustive analysis of the matter. By incorporating the feasible pronouncements into the May 5 Bates White study, Mr. Damonte arrives at a VNR that is approximately 40 percent lower than that of the July 28 Bates White study, which directly results in a substantial

829 *Ibid.*, para. 43.

830 *Ibid.*, paras. 45.

831 *Ibid.*, section III.2.2.

832 Mercados Energéticos Consultant Firm, "Review of EEGSA's Value-Added for Distribution Study in Relation to the Expert Commission Opinion," July 2009, **Exhibit R-103**; Witness Statement of Mercados Energéticos, signed by Alejandro Aberto Arnau, Mariana Álvarez Guerrero and Edgardo Leandro Torres, January 24, 2012 (hereinafter ***Mercados Energéticos***), **Appendix RWS-3**.

reduction in the VAD.[833] We reiterate that this value only reflects the incorporation of "feasible" pronouncements.[834]

(ii) Mr. Kaczmarek uses an inappropriate level of depreciation for the VNR

604. As previously explained, the Expert Commission rejected Bates White's position throughout the tariff review process, which was that EEGSA's return had to be calculated on a gross capital base (VNR) (that is, not accounting for accumulated depreciation).

605. However, the Expert Commission also rejected the formula in the Terms of Reference, which considered that the capital base upon which EEGSA's return should be calculated had been depreciated by 50 percent. Instead, the Expert Commission proposed an alternative formula that only considered depreciations for five years, but thereafter uses the new value of the installations.

606. By using the July 28 Bates White study, Mr. Kaczmarek accepted, without analysis, the alternative capital return formula proposed by the Expert Commission. As previously explained,[835] in proposing an alternative formula for calculating EEGSA's return on investment, the Expert Commission exceeded its authority. More importantly, as Mr. Damonte[836] and Messrs. Abdala and Schoeters[837] explain, this formula contains serious technical errors and over-compensates the investor. In Mr. Damonte's words:

> Conceptually this means that each tariff period will begin with accumulated depreciation at zero, and it will be depreciated over five years only. In the next period

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833 Damonte, **Appendix RER-2**, chapter 5; and M Abdala and M Schoeters, **Appendix RER-1**, para. 50.

834 As Mr. Damonte explains in detail in his report, the inclusion of many of the pronouncements required additional information and optimizations that were impossible to achieve within the available time frame. Damonte, **Appendix RER-2**, para. 176.

835 See section III.F.9.c above.

836 Damonte, **Appendix RER-2**, chapter 6.

837 M Abdala and M Schoeters, **Appendix RER-1**, section III.2.3.

> the cycle will repeat. My conclusion is that, by applying it during various tariff periods, assets will be being depreciated over five years and then all the depreciation accrued over the five years is reincorporated in the assets in the tariff period. This procedure is clearly wrong, as evidenced by the Net Present Value Test.[838]

607. Because the formula proposed by the Expert Commission results in an over-compensation of EEGSA in the long term, and because EEGSA never submitted the estimated level of depreciation of its capital base, Mr. Damonte proposes calculating EEGSA's return using an alternative formula: the theoretical Constant Annuity formula. This is a method commonly used in regulations and, in particular, it was used in EEGSA's 2003 tariff review. Mr. Damonte's calculations result in a depreciation factor of 1.42 for EEGSA's capital base, which means that the network's accumulated depreciation is 30 percent (meaning, the return is calculated based on the remaining 70 percent that has not been depreciated).[839]

608. As previously explained,[840] if EEGSA had furnished the depreciation value of its capital base instead of insisting that it be remunerated based on the gross value of its capital base, this estimation would not have been necessary. The approach that Mr. Damonte used is conservative when compared to the values that CNEE agreed to with Deorsa and Deocsa when they questioned the 50 percent depreciation established in the Terms of Reference. In the words of Mr. Damonte:

> […] Note that in the case of the tariff review of Deorsa and Deocsa of 2008, in which my consultancy Quantum participated as a consultant of those distributors, we believe that 50 percent of depreciation established in the ToR did not reflect the reality of the companies. In this context, we presented the relevant explanations to the CNEE and the CNEE agreed to change the level of

838 Damonte, **Appendix RER-2**, paras. 178–179; see also chapter 6.2.

839 1.42 in low voltage and 1.41 in medium voltage. M Abdala and M Schoeters, **Appendix RER-1**, section III.2.3 and para. 71; Damonte, **Appendix RER-2**, chapter 6.3.

840 See para. 400 above.

> accumulated depreciation to 42.2%, equivalent to a f=1.73. I understand that EEGSA never conducted a similar analysis, given that its aim was not to obtain recognition of a higher level of depreciation but it simply aimed to calculate the rent on the gross value of the Capital Base without depreciating.[841]

2. Valuation using Comparables (*but for* and actual scenarios)

609. In addition to the aforementioned problems, the Kaczmarek report contains errors in its valuation of future damages based on Comparables in the *but for* and actual scenarios. Although such methods may be useful within certain contexts, they are not relevant in this case for the following reasons:[842]

(a) The small sample size used by Mr. Kaczmarek in each of his valuations using Comparables (i.e., 12 publically-available companies and 9 comparable transactions) make them volatile and rather unreliable;[843]

(b) The companies and transactions selected are far-fetched comparables with characteristics different from those of EEGSA. This was even recognized by TGH in the annual reports of its head office;[844]

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841 Damonte, **Appendix RER-2**, para. 192.

842 M Abdala and M Schoeters, **Appendix RER-1**, section III.2.4.(a)

843 *Ibid.*, para. 73. Even Mr. Kaczmarek himself acknowledges that he does not fully trust his calculations of valuations based on comparables due to the unavailability and the poor quality of the information. Kaczmarek, **Appendix CER-2**, para. 218.

844 Annual Report 10-K report of TECO Energy, Inc. for 2009, February 29, 2010, **Exhibit R-112**, p.117 ("While quoted prices in active markets provide the best evidence of fair value, these are not available since TECO Guatemala has not received any offers for the purchase of its investment in DECA II. Additionally, multiples of earnings or another performance measure to determine fair value is not available since there are no comparable entities in Guatemala that have recently been sold. While there have been similar sales in Central America, these sales are not comparable to TECO Guatemala's investment due to the differing regulatory, economic and growth environments throughout Central America. Therefore, in conducting the impairment assessment for the company's investment in DECA II, the company used discounted cash flows of the business model of each of DECA II's significant group of assets."). M Abdala and M Schoeters, **Appendix RER-1**, paras. 73 and 76.

(c) The valuations using Comparables in the *but for* scenario are based on the EBITDA estimated by Mr. Kaczmarek using the DCF method which, as explained previously, suffers from errors that make it invalid to use;[845]

(d) The *ad hoc* weighting factors used by Mr. Kaczmarek in averaging the DCF and Comparables methods are not only unjustified, but biased. Mr. Kaczmarek assigns a greater weight to companies or transactions with high valuation multiples, thereby producing a higher valuation for EEGSA, which results in an artificial increase in his estimate of the alleged damage.[846]

610. In conclusion, the use of Comparables is not advisable in this case. Since EEGSA is a highly regulated company, once the differences in the key parameters of the tariff review have been resolved, the DCFs can be projected with an acceptable degree of certainty and, therefore, should be the preferred method.

3. The sale of DECA II reflects the correct value for EEGSA in the actual scenario

611. As previously explained, Mr. Kaczmarek calculates EEGSA's value in the actual scenario using (i) cash flow projections based on EEGSA's financial statements for the historical damages; and (ii) a weighted combination of cash flow projections based on the Sigla study and Comparables for the future damages. Considering that an actual sale transaction took place in the present case, there is no need to incur the unnecessary assumptions and uncertainties, on top of the other problems mentioned above, which are inherent to Kaczmarek's valuation.

612. As mentioned earlier, in 2010, EPM acquired Teco's indirect interest in EEGSA. In this context, the price paid by EPM to acquire the DECA II block of shares is the best available reference for EEGSA's value, because it was agreed upon

845 M Abdala and M Schoeters, **Appendix RER-1**, para. 74

846 *Ibid.*, para. 75.

between independent parties under free market conditions (*i.e.*, at "arm's length"). Further, this transaction was free from possible errors based on assumptions used in the DCF valuation. More importantly, such a transaction is free from the possible errors that are inherent in the assumptions used in the DCF method. In particular, such a transaction is free from the disadvantages of the lack of an adequate comparison for EEGSA among the companies selected in the Comparables method. Therefore, as Messrs. Abdala and Schoeters explain, information regarding the sale to EPM should be used as primary data in calculating EEGSA's value in the actual scenario, instead of the methods used by Mr. Kaczmarek.[847]

613. Having clarified this point, we must analyze how EEGSA's value may be determined based on the price EPM paid for the DECA II holding. In its initial presentations, TGH (like its associate Iberdrola in its pending arbitration) refused to provide internal or external valuations reflecting the price that EPM paid for EEGSA. Both TGH and Iberdrola maintained that the buyer's offer was a "global value" for a larger asset, and it was impossible to identify the price paid for EEGSA in this transaction. In this regard, both claimants in their respective arbitration proceedings asked their experts to estimate the implicit value of EEGSA in the sale of EEGSA.[848]

614. Mr. Kaczmarek calculated this value as US$498 million.[849] As Messrs. Abdala and Schoeters explain, the TGH expert underestimated EEGSA's value. By relying on EEGSA's EBITDA information for the 2009 fiscal year, the expert neglected to use more current information available at the time of the DECA II sale that more precisely and timely reflects the reality of EEGSA's business. Using the available EBITDA information from the twelve months' immediately

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847 M Abdala and M Schoeters, **Appendix RER-1**, para. 80. Although Mr. Kaczmarek acknowledges that the price paid by EPM is a good approximation of EEGSA's value in the actual scenario and uses it as a benchmark to justify his valuations, he discards it in calculating the alleged damage, with no justification whatsoever.

848 Claimant's Memorial, para. 305; Kaczmarek, **Appendix CER-2**, para. 241.

849 Kaczmarek, **Appendix CER-2**, para. 241.

preceding the sale of DECA II, Messrs. Abdala and Schoeters calculated the value of EEGSA as US$ 518.0 million.[850]

615. Furthermore, as part of the document production (and at the express request of Guatemala), TGH produced a document that its financial adviser Citibank prepared in the context of the sale of Teco's shares in EEGSA; this document shows EEGSA's value as US$582 million.[851] Thus, this value ought to be used as EEGSA's value in the actual scenario since it is the value furnished by TGH itself. As explained in detail below, using this value in the actual scenario shows that TGH did not suffer any damage. In any case, Messrs. Abdala and Schoeters conducted the inferred calculation based on the sale as proposed by TGH, but with updated information (US$518 million), in case the Tribunal were to decide to use an inferred value for EEGSA, rather than the value provided by TGH's own financial advisor Citibank in the actual context of the sale of TGH's participation in EEGSA.[852]

C. CORRECTED VALUATION BASED ON THE DAMAGE ALLEGED BY TGH

616. As we explained in the preceding section, TGH's valuation suffers from several fundamental errors.[853]

617. To correct these errors, Messrs. Abdala and Schoeters did the following:[854]

(a) *But for* scenario: they replaced Mr. Kaczmarek's projections based on the July 28 Bates White study with projections based on the May 5 Bates White study as recalculated by Mr. Damonte, incorporating all of the

850 M Abdala and M Schoeters, **Appendix RER-1**, para. 81.

851 This arises from considering the share of the valuation of EEGSA's capital (minimum of US$ 373.2 and maximum of US$ 448.2) in the capital of DECA II (minimum of US$ 572.1 and maximum of US$ 669.6). See Letter of Citi to the Management of Teco Energy, Inc., October 14, 2010, **Exhibit R-128**, p. 7; M Abdala and M Schoeters, **Appendix RER-1**, para. 82.

852 M Abdala and M Schoeters, **Appendix RER-1**, para. 81.

853 Experts M Abdala and M Schoeters have identified the other, less relevant errors, and analyze them in detail in their report. M Abdala and M Schoeters, **Appendix RER-1**, section III.2.4.c..

854 M Abdala and M Schoeters, **Appendix RER-1**, para. 81.

"feasible" pronouncements of the Expert Commission. Instead of using the FRC proposed by the Expert Commission, they used the FRC calculated by Mr. Damonte based on the Constant Annuity method.[855] Furthermore, in their projections they used a level of investment and operating costs that is consistent with the tariff study used, thereby avoiding overestimating EEGSA's value in this scenario.

(b) Actual scenario: they used the value of EEGSA furnished by Citibank and provided, as an alternative, the value derived from the actual transaction, calculated using the EBITDA methodology proposed by Mr. Kaczmarek, but using more current data.

618. Having amended these errors, the alleged damage originally calculated by Kaczmarek as US$237.1 million is reduced to zero if EEGSA's value as furnished by Citibank is applied. Using the inferred value of the Sale in the actual scenario, the damages are reduced to US$5.3 million, measured in US dollars as of October 2010. A summary of the results obtained after making the necessary corrections to the Kaczmarek valuation is provided below:[856]

855 M Abdala and M Schoeters, **Appendix RER-1**, para. 37–38 and 58 and Damonte, **Appendix RER-2**, chapter 6.

856 M Abdala and M Schoeters, **Appendix RER-1**, para. 95.

Corrected Valuation of Alleged Damage: A&S Base Case – October 2010 US$ MM

Valuación de EEGSA (al 21-oct-10)	Contra-fáctico	Real	
		FFD Citibank	EBITDA pro-rata
Valor Empresa	587,6	582,0	518,2
Deuda Neta de EEGSA	87,6	87,6	87,6
Valor del Capital Accionario	500,0	494,4	430,6
Valor del Capital Accionario de TGH (24,26%)	**121,3**	**120,0**	**104,5**
Flujos a TGH			
Flujos Históricos	12,8	24,4	24,4
Flujos Futuros	121,3	120,0	104,5
Total	**134,1**	**144,3**	**128,8**
Presuntos Daños Totales a TGH		**0,0**	**5,3**

Source: M Abdala and M Schoeter
Note: Totals may differ from the sum of the individual components due to rounding.

619. Furthermore, if this Tribunal accepts that EEGSA and its consultant had a legal obligation to present information that would justify a modification of the FRC of 50 percent depreciation as established in the Terms of Reference (as Deorsa and Deocsa did), and unjustifiably sought to be remunerated for the gross value of their assets, rather than one reduced by the accumulated depreciation, the damages would also be null.[857]

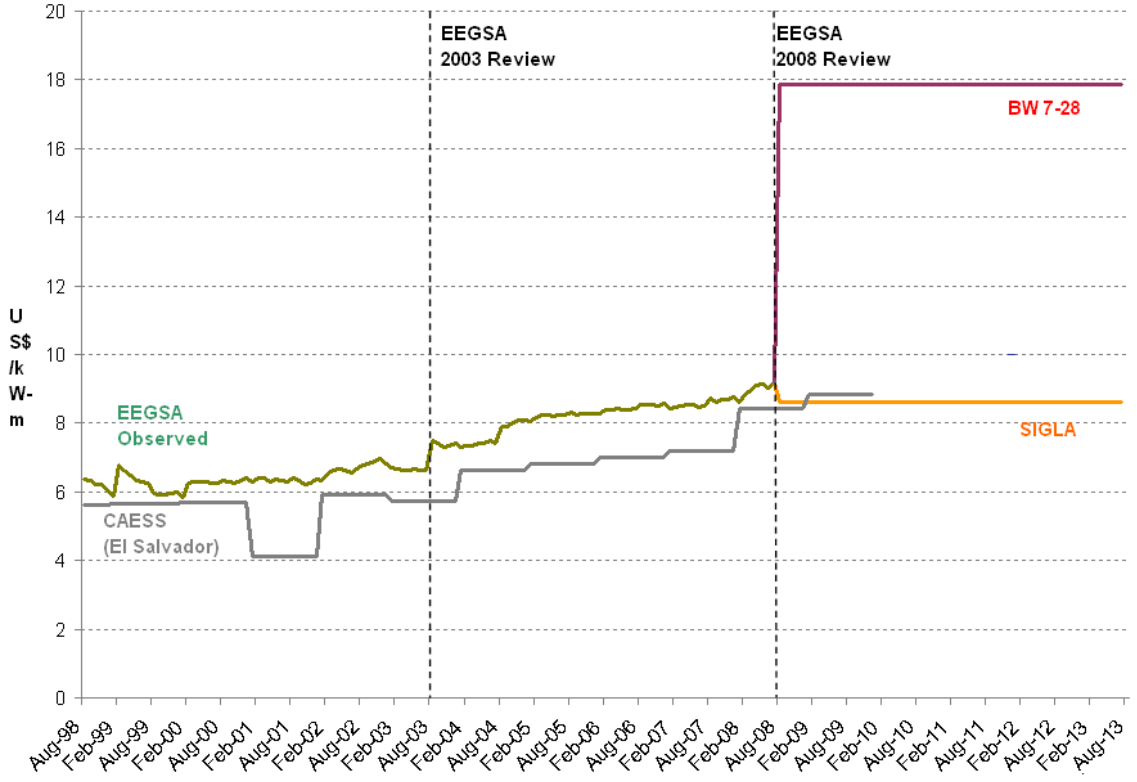
D. THE REASONABLENESS OF MESSRS. ABDALA AND SCHOETERS'S VALUATION

620. In order to give the Tribunal an objective means to assess the reasonableness of their valuation, Messrs. Abdala and Schoeters compared the tariffs resulting from their valuation with those of a comparable company in El Salvador. Thus, Messrs. Abdala and Schoeters present a comparison of EEGSA's historical low-voltage VAD in force up until the 2008 tariff review, with the low-voltage VAD underlying the tariffs calculated by Mr. Kaczmarek, Sigla and themselves.

857 M Abdala and M Schoeters, **Appendix RER-1**, para. 96.

621. As can be seen in the following graph, the VAD that results from the approach proposed by Messrs. Abdala and Schoeters follows the historical trend, while the VAD obtained by Bates White, and used by Mr. Kaczmarek in his valuation, is far higher than EEGSA's historical VAD. To put these results into context, the graph also compares these two VADs (both before and after the rates were set in 2008) to the VAD of CAESS, the principal electricity distributor of El Salvador, the country used as a reference for setting EEGSA's tariffs in the first five-year period of 1998-2003.[858] As is evident, both EEGSA's historical VAD and the VAD used in Messrs. Abdala and Schoeters's analysis are in line with those of CAESS.[859]

Value Added for Distribution (VAD) – Low Voltage



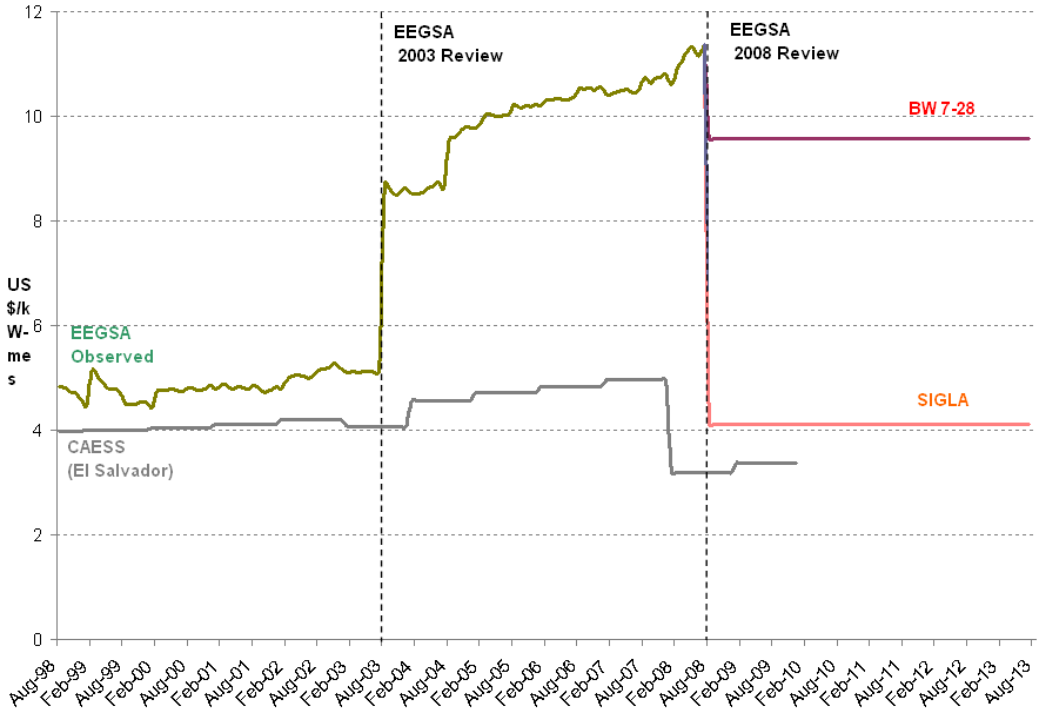
Source: M Abdala and M Schoeter
Note: As of August 2008, tariffs correspond to the initial tariff expressed in August 2008 in US$.

858 Damonte, **Appendix RER-2**, para. 234.

859 M Abdala and M Schoeters, **Appendix RER-1**, paras. 104-105.

622. The following graph, which shows the medium-voltage VAD, demonstrates that when the tariffs were set in 2003, the VAD was much greater than in previous years. Further, the VAD calculated by Damonte and used by Messrs. Abdala and Schoeters, although lower than the VAD of the tariffs set for 2003–2008, is in line with the trend of previous years, but with a slight increase. Furthermore, the VAD that Damonte calculated by implementing corrections to the May 5 study, as well as the VAD calculated by Sigla and used by the CNEE, are both above that of CAESS.[860]

Value Added for Distribution (VAD) – Medium Voltage



Source: M Abdala and M Schoete
Note: As of August 2008, tariffs correspond to the initial tariff expressed in August 2008 in US$.

E. PRE- AND POST-AWARD INTEREST

623. To actualize the presumed damages to their value as of the award date, Mr. Kaczmarek proposes three alternatives, yet none explains nor justifies the criteria

860 M Abdala and M Schoeters, **Appendix RER-1**, para. 863.

he used to select them, nor does he favor any one in particular. These alternatives would use the following as an interest rate:[861]

- The performance of Guatemala's sovereign bonds;
- The rate that US banks charge to the most solvent companies in the country ("preferred rate") plus a 2% premium;[862] or
- The LIBOR plus a 4% premium.[863]

624. To update the losses to their currency value as of October 21, 2010, it is necessary to actualize the presumed damages calculated by the DCF method from the date the damages occurred until the aforementioned date. As Messrs. Abdala and Schoeters explain, in order to do so, it is necessary to apply an actualization factor based on EEGSA's cost of capital (best represented by the "WACC"), which correctly reflects the risks that EEGSA faced when the company was still operating within the market.[864]

625. The logic of this reasoning is based on the premise that, if Guatemala had adopted the Bates White tariff study with the corrections made by Damonte, EEGSA would have earned more money than it did under the tariff schedule implemented in August 2008 (based on the Sigla study). These sums would have been applied

861 Kaczmarek, **Appendix CER-2**, paras. 221–223.

862 Mr. Kaczmarek acknowledges that the interest rate is not widely applicable and, to make it a rate that is more applicable within the market, adds a 2% premium to it. However, the expert does not present any additional information to support this adjustment.

863 Mr. Kaczmarek mentions that, historically, LIBOR plus 2% has closely followed the prime rate. This is why he includes an additional 2% to reach LIBOR plus a 4% premium. Mr. Kaczmarek has presented no evidence whatsoever of the aforementioned historical pattern. Even if this pattern were correct, Mr. Kaczmarek does not explain why this rate should be presented as an alternative to the prime rate plus 2%.

864 M Abdala and M Schoeters, **Appendix RER-1**, section V.

to its respective businesses, receiving a normal return on these funds equivalent to the WACC.[865]

626. On the contrary, from October 21 until the date of the award, the alleged damages need to be updated using an actualization factor that is based on a risk-free rate, in order to reflect that, starting the moment when TGH relinquished its indirect participation in EEGSA, it was no longer exposed to the risk of operating that company.[866]

VI. RESPONDENT'S REQUEST FOR RELIEF

627. The Republic of Guatemala respectfully requests that this Tribunal:

(a) DECLARE that it does not have jurisdiction over the controversy submitted by TGH and/or that the claim of TGH is inadmissible.

(b) Alternatively to the request (a) above, REJECT each and every one of the claims made by TGH on the basis of the facts;

(c) GRANT any other compensation to Guatemala that the Tribunal believes to be opportune and appropriate; and

(d) ORDER that TGH pay all costs of this procedure, including the costs of legal representation for Guatemala, with interest.

(e) Respectfully presented by the Republic of Guatemala on January 24, 2012.

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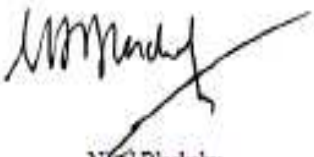
865 The techniques for a standard valuation presume the reinvestment of cash flows at the cost of capital rate. In other words, the firm's value remains constant over time, expressed in terms of year 0, only if the historical cash flows are invested earning a rate that equals the cost of capital.

866 M Abdala and M Schoeters, **Appendix RER-1**, section V.



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