

**INTERNATIONAL CENTRE FOR SETTLEMENT
OF INVESTMENT DISPUTES
WASHINGTON, D.C.
CASE NO. ARB/01/7
MTD EQUITY SDN. BHD. AND MTD CHILE S.A.
(CLAIMANTS)**

V.

**REPUBLIC OF CHILE
(RESPONDENT)**

AWARD

Date of dispatch to the parties: May 25, 2004

Before the Arbitral Tribunal comprised of:

President:	Mr. Andrés Rigo Sureda
Members of the Tribunal:	Mr. Marc Lalonde Mr. Rodrigo Oreamuno Blanco
Secretary of the Tribunal:	Mr. Ucheora Onwuamaegbu

I. PROCEDURE

1. Registration of the Request for Arbitration

1. By letter of June 26, 2001, MTD Equity Sdn (“MTD Equity”), a Malaysian company, and MTD Chile S.A (“MTD Chile”), a Chilean company, (collectively “the Claimants” or “MTD”) filed a request for arbitration with the International Centre for Settlement of Investment Disputes (“ICSID” or “the Centre”) against the Republic of Chile (“the Respondent” or “Chile”). The request, invoked the ICSID Arbitration provisions of the 1992 Agreement between the Government of Malaysia and the Government of the Republic of Chile for the Promotion and Protection of Investments (“the BIT”).

2. The Centre, on June 27, 2001, in accordance with Rule 5 of the ICSID Rules of Procedure for the Institution of Conciliation and Arbitration Proceedings ("Institution Rules") acknowledged receipt of the request and on the same day transmitted a copy to the Republic of Chile and to the Chilean Embassy in Washington, D.C. 3.
3. On July 17, 2001, the Centre requested further information from the Claimants, with regard to the fulfillment by both Claimants of the requirement set forth in Articles 6(3)(i) and (ii) of the BIT concerning an attempt to resolve the dispute amicably through consultation and negotiation at least three months before the request for arbitration. The Centre also sought confirmation from the Claimants that neither of them had submitted the dispute to courts or administrative tribunals of Chile, as precluded by Article 6(3)(ii) and (iii) of the BIT; and that the majority of the shares in the second Claimant, MTD Chile were, for purposes of Article 6(2) of the BIT, owned by investors of Malaysia before the dispute arose. The Claimants responded by a letter of July 30, 2001.
4. The request was registered by the Centre on August 6, 2001, pursuant to Article 36(3) of the ICSID Convention, and on the same day the Acting Secretary-General, in accordance with Institution Rule 7, notified the parties of the registration and invited them to proceed to constitute an Arbitral Tribunal as soon as possible.

2. Constitution of the Arbitral Tribunal and Commencement of the Proceeding

5. There were two successive arbitral tribunals in this case, the present Tribunal having been appointed upon the joint resignation of the first set of arbitrators.
6. Following the registration of the request for arbitration by the Centre, the parties agreed on a three-member Tribunal. The parties had agreed that each would appoint an arbitrator and that the third arbitrator, who would be the president of the Tribunal, would be appointed by agreement of the parties.
7. The Claimants appointed Mr. James H. Carter Jr., a national of the United States of America, and the Respondent appointed Professor W. Michael Reisman, also a national of the United States of America. By agreement, the parties appointed Mr. Guillermo Aguilar Alvarez, a national of Mexico, as the presiding arbitrator.

8. All three arbitrators having accepted their appointments, the Centre by a letter of March 5, 2002, informed the parties of the constitution of the Tribunal, consisting of Mr. James H. Carter Jr., Professor W. Michael Reisman, and Mr. Guillermo Aguilar Alvarez ("the first Tribunal"), and that the proceeding was deemed to have commenced on that day, pursuant to ICSID Arbitration Rule 6(1).
9. As agreed between the first Tribunal and the parties, in consultation with the Centre, the first Tribunal held its first session in New York on May 29, 2002, with the parties attending.
10. In advance of that session, the parties, by a joint letter dated May 24, 2002, communicated to the Tribunal their agreement on several items on the agenda proposed for the session. Those agreements by the parties were affirmed at the meeting and incorporated in the minutes.
11. Arbitrators had requested a rate of remuneration higher than the Centre's current rate. The Respondent and the Claimants, by letters dated September 17, 2002 and September 24, 2002, respectively, advised the Tribunal that they were unable to offer the rate of remuneration proposed by the Tribunal members.
12. By a letter dated October 2, 2002, the Tribunal notified the parties that it would not be able to serve on the basis of the fees agreed by the parties and that each of its members would be resigning his appointment. By a joint letter of October 17, 2002, members of the first Tribunal tendered their resignation to the Secretary-General of the Centre.
13. On October 18, 2002, the Centre notified the parties of the resignations of Mr. Aguilar Alvarez, Mr. Carter and Professor Reisman and informed them that the proceeding was suspended pursuant to ICSID Arbitration Rule 10(2). In accordance with Arbitration Rule 11, the parties were by that letter invited to appoint new arbitrators by the same method by which the initial arbitrators were appointed.

3. Appointment of the present Tribunal

14. By a letter of November 26, 2002, the Claimants informed the Centre of their appointment of Mr. Marc Lalonde, a Canadian national, to fill the vacancy created by the resignation of Mr. James H. Carter, and invited the Respondent to appoint a replacement for Professor W. Michael Reisman and to engage in consultations aimed at reaching an

agreement on the person to replace Mr. Guillermo Aguilar Alvarez as the presiding arbitrator.

15. By a letter of December 16, 2002, the Respondent notified the Centre that it had appointed Mr. Rodrigo Oreamuno Blanco, a national of Costa Rica, to fill the vacancy created by the resignation of Professor W. Michael Reisman.
16. The parties, by separate letters of January 23, 2003, notified the Centre of their appointment, by agreement, of Mr. Andrés Rigo Sureda, a national of Spain, to fill the vacancy created by the resignation of Mr. Guillermo Aguilar Alvarez as the presiding arbitrator.
17. All three arbitrators accepted their appointments and, on January 29, 2003, the Centre notified the parties that the Tribunal had been reconstituted and the proceeding recommenced on that day, in accordance with ICSID Arbitration Rule 12.

4. *Written and Oral Procedure*

18. At the first session of the first Tribunal on May 29, 2002, it was agreed that the proceeding would be in English and Spanish. Documents filed in one language would be followed within five business days by a translation in the other language. The procedural arrangements agreed by the first Tribunal have been adhered to by the Tribunal.
19. The following schedule was also agreed for the exchange of written submissions: the Claimants to file their Memorial by October 1, 2002; the Respondent to file its Counter-Memorial by February 1, 2003; the Claimants to file their Reply by April 15, 2003; and the Respondent to file its Rejoinder by July 1, 2003.
20. It was also agreed that a hearing would be held from Monday August 4 to Thursday, August 14, 2003, including Saturday, August 9, 2003.
21. The Claimants filed their Memorial on October 1, 2002, followed on October 8, 2002 by a Spanish language translation. These submissions were not transmitted to the first Tribunal but were sent to the present Tribunal after it was constituted.
22. Upon the resignation of the members of the first Tribunal, the proceeding was suspended on October 18, 2002, pursuant to ICSID Arbitration Rule 10(2) which provides:

“Upon the notification by the Secretary-General of a vacancy on the Tribunal, the proceeding shall be or remain suspended until the vacancy has been filled.”

23. Arbitration Rule 12 further provides:

“As soon as a vacancy on the Tribunal has been filled, the proceeding shall continue from the point it had reached at the time the vacancy occurred. ...”

24. On December 26, 2002, the Respondent wrote to the Centre suggesting that the effect of ICSID Arbitration Rules 10(2) and 12 was that suspension of the proceeding upon the resignation of the first Tribunal meant a suspension of the schedule established for the filing of submissions, and requested an extension for the filing of its Counter-Memorial. The Claimants in a letter of January 10, 2003 rejected the Respondent’s interpretation of Arbitration Rule 10(2), but agreed with the Respondent that the matter should be determined by the new Tribunal upon its constitution.

25. After the present Tribunal was constituted, by Procedural Order No. 1 of February 3, 2003, issued in English and Spanish, the Tribunal requested the parties to present, no later than by February 14, 2003, any observations that they may have on the effect of the suspension of the proceeding on time limits for filing pleadings. On that day, the parties simultaneously filed submissions.

26. On February 18, 2003, the Claimants requested the Tribunal “to address one new argument” asserted in the Respondent’s submission of February 14, 2003.

27. By Procedural Order No. 2, dated February 20, 2003, the Tribunal decided:

“that the meaning of the term ‘suspension’ in Rules 10 and 12 of the [ICSID] Arbitration Rules applies to all matters related to the proceeding, including time limits, and not only to matters related to action required from the Tribunal, that the time limit to present the counter-memorial originally fixed [for] February 1, 2003 [be] extended by 103 days [the duration of the suspension] to May 15, 2003.”

28. The Tribunal in that Order then directed the parties:

“(a) to consult each other on the subsequent schedule of the proceeding and other pending matters, including the matter related to business records, and
(b) advise the Tribunal of the result of their consultations not later than March 14, 2003.”

29. By a letter of March 14, 2003, the Claimants notified the Tribunal that the parties were still in discussions on the modified schedule.
30. By a letter of March 17, 2003, the Claimants advised the Tribunal of their agreed schedule for the submission of the remaining pleadings and notified the Tribunal that the parties had resolved the matter related to the business records referred to in Procedural Order No. 2. The Respondent in a letter of March 18, 2003, confirmed the agreement of the parties as communicated in the Claimants’ letter of the previous day.
31. Following a request by the Tribunal that the hearing commence a day later than that proposed by the parties, and correspondence with the parties in that regard, the Tribunal, by a letter dated April 21, 2003, formally took note of the agreed schedule for the submission of the remaining pleadings and proposed dates of the hearing from December 9, 2003 to December 19, 2003, including Saturday, December 13.
32. On June 9, 2003, the Respondent filed its Counter-Memorial in English and the Spanish version on June 16, 2003.
33. By letters of July 11, 2003 and July 14, 2003, respectively, the Claimants and the Respondent notified the Tribunal of each other’s witnesses and experts that should be made available for cross examination at the oral hearing.
34. On September 15, 2003, the Claimants filed their Reply in English language, followed on September 23, 2003 by Spanish translations.
35. On October 14, 2003, counsel for the Respondent wrote to the Tribunal concerning their participation in the proceeding stating that:
- “due solely to budgetary constraints faced by the Republic of Chile, White & Case LLP must withdraw as counsel of record

for the Respondent in respect of [this] case. For the avoidance of doubt we wish to emphasize that our withdrawal does not relate in any way to the merits of the issues raised in the case. We shall assume limited role as advisor to the Republic of Chile with regard to this matter. All communications and service of documents henceforth may continue to be addressed to us, as well as the other advisors of the Republic in regard to this matter”.

36. On November 21, 2003, the Respondent filed its Rejoinder in Spanish language, followed by the English language version on December 1, 2003.
37. As previously agreed, the hearing on merits was held from December 9 to 19, 2003, in Washington, D.C., at the seat of the Centre. The hearing was conducted in English and Spanish and full verbatim transcripts in both languages were made and distributed to the parties.
38. Pursuant to Rule 38(1) of the Arbitration Rules, on March 26, 2004, the Tribunal declared the proceeding closed, having deliberated by various means.

II. THE FACTS

39. The facts described below follow the narrative of the Claimants and, unless noted, have not been contested by the Respondent.
40. In 1994 Dato¹ Nik of MTD visited Chile as a member of a trade delegation organized by the Malaysian Ministry of Public Works. During this visit, he met with government officials and business leaders who emphasized Chile’s encouragement of foreign investment. Dato’ Nik so reported to the Management Committee of MTD. He also met with Mr. Musa Muhamad, the Malaysian External Trade Commissioner in the Malaysian embassy in Santiago, who encouraged MTD to invest in Chile.²
41. In April 1996, Dato’ Nik heard from Mr. Muhamad about “an opportunity to build a large planned community near Santiago.” Dato’ Nik informed Dato’ Azmil Khalid who at the time was traveling in the

¹ “Dato” is a Malaysian title of honor.

² Memorial, para. 13.

United States. Dato' Azmil Khalid traveled directly from the United States to Chile to investigate this opportunity. There he met with Messrs. Muhamad and Antonio Arenas, a local businessman. They informed Dato' Khalid that they had found "the perfect location for a planned community."³

42. Dato' Khalid visited the site in the small town of Pirque and met with the owner of the land, Mr. Jorge Fontaine Aldunate. Mr. Fontaine is reported to have said that "he would like to work with MTD to build a mixed-use planned community on the Malaysian model". Although the site was zoned for agricultural use, Mr. Fontaine is alleged to have said that the land was unproductive and "could readily be rezoned, particularly if it would attract foreign investment."⁴
43. Dato' Khalid returned to Malaysia and reported to MTD's Management Committee about this opportunity in Chile. The Management Committee decided to investigate it further. For this purpose, Messrs. Lee Leong Yow (Vincent Lee), MTD's Group General Manager and Head of Operations, and Nazri Shafiee, expert in land valuation, traveled to Chile from May 14 to May 18, 1996. Dato' Nik was also in Chile on May 16-17, 1996. He visited the project site and met with Mr. Fontaine and his family.⁵
44. Messrs. Lee and Shafiee visited the Foreign Investment Commission (FIC) on May 16, 1996. There they met with Mr. Joaquín Morales Godoy, Senior Legal Counsel.⁶ The next day, Mr. Shafiee met with Mr. Fernando Guerra Francovich, the head of Servicio de Vivienda y Urbanización ("SERVIU").⁷ After these meetings, Messrs. Lee and Shafiee concluded that MTD should pursue the investment opportunity and so reported to MTD's Management Committee.⁸ Based on their report, the Management Committee decided "to pursue negotiations with Mr. Fontaine while continuing to study the feasibility of a joint venture to develop the Project."⁹

³ Ibid., paras. 14-15.

⁴ Ibid., para. 16

⁵ Ibid., para. 13.

⁶ Ibid., paras. 20-22.

⁷ Ibid., para. 23.

⁸ Ibid., paras. 25-26.

⁹ Ibid., para. 27.

45. MTD engaged Banco Sud Americano in Santiago to appraise the land. In September 1996, the appraisers submitted their report valuing the land of Mr. Fontaine, 3000 hectares, at \$34,385,487. The appraisal assumed that the land could be developed as an upscale community after changing the existing zoning for agricultural use.¹⁰
46. In September 1996, the negotiations of MTD with Mr. Fontaine appeared to have reached a dead end because of disagreement on which hectares to develop and the control of the joint venture: Mr. Fontaine wanted: (i) to develop all 3000 hectares while MTD wished to develop first the 600 located at the lowest elevations; and (ii) a 50/50 split of the equity while for MTD it was essential to have control.¹¹
47. Negotiations resumed in November 1996. The law firm Vial & Palma represented MTD, specifically attorneys Alberto Labbé Valverde and José Miguel Olivares. The parties prepared a "Promissory Contract" dated as of November 21, 1996.¹²
48. On November 6, 1996, according to the Respondent, a meeting took place between Mr. Edmundo Hermosilla, Minister of MINVU, Mr. Sergio González Tapia, Secretario Regional Ministerial ("SEREMI"), and representatives of MTD.¹³ That this meeting took place, who attended and what was said at the meeting is a matter of controversy between the parties.
49. In December 1996, Messrs. Dato' Azmil Khalid and Lee negotiated the documents implementing the Promissory Contract and signed them on December 13, 1996.¹⁴ The Promissory Contract would take effect only after FIC's approval of the MTD's investment and provided for: (i) development of the land at first in two tranches of 600 and 630 hectares, the second tranche at the option of MTD; and (ii) the creation of a Chilean corporation, "El Principal Inversiones S.A." ("EPSA"), to be owned 51 per cent by MTD Chile S.A. and 49 per cent by Mr. Fontaine.¹⁵

¹⁰ Ibid., para. 28.

¹¹ Ibid., para. 29.

¹² 12 Ibid., para. 30.

¹³ Counter-Memorial, para. 24.

¹⁴ 14 Memorial, para. 30.

¹⁵ Ibid., para. 31.

50. On December 13, 1996, after signature of the Promissory Contract, Dato' Khalid and Mr. Labbé met with Mr. Eduardo Moyano, Executive Vice President of the FIC.¹⁶
51. On January 14, 1997, MTD filed an application with the FIC for approval of an initial investment of US\$ 17.136 million. The application described the project as follows:
- “[D]evelop a township of 600 hectares of Fundo El Principal de Pirque, which will be a self-sufficient satellite city, with houses, apartments for diverse socioeconomic strata, schools, hospitals, universities, supermarkets, commerce of all sorts, services, and all other components necessary for self-sufficiency” (Exhibit 12 at 3. Translation of the Claimants).”
52. The application specified the location as “Pirque, Metropolitan Region” and that “the investment would provide initial capital to a newly formed corporation named MTD Chile S.A., which would use the capital to acquire a 51 percent stake in El Principal S.A., which would own the land and develop the Project.”¹⁷
53. The application was approved by the FIC at its session of March 3, 1997. The following members of FIC attended: the President of FIC (the Minister of Economy, Development and Reconstruction), the President of the Central Bank, the Undersecretary of Finance, the Undersecretary of Mining, and the Undersecretary of Planning and Cooperation. The FIC informed MTD of the approval by letter dated March 6, 1997 and enclosed the standard contract used by Chile for these purposes.¹⁸
54. The Foreign Investment Contract was signed on March 18, 1997 by the President of FIC on behalf of Chile and Mr. Labbé on behalf of MTD. The Foreign Investment Contract provides that MTD will develop “a real estate project on 600 hectares of Fundo El Principal de Pirque. The aforementioned project consists of the construction of a self-sufficient satellite city, with houses, apartments, schools, hospitals, commerce, services, etc.” (“the Project”).¹⁹

¹⁶ *Ibid.*, para. 32.

¹⁷ *Ibid.*, para. 33.

¹⁸ *Ibid.*, paras. 35 and 36.

¹⁹ Exhibit 14 to the Memorial at 2.

55. After signature of the Foreign Investment Contract, MTD injected US\$ 8.4 million into EPSA as a capital contribution and with US\$ 8.736 million MTD purchased 51% of the EPSA shares from Mr. Fontaine “who was receiving them in return for his contribution to EPSA of 600 hectares of land.”²⁰ The funds contributed by MTD came from the resources of the MTD group and US\$ 12 million from a loan made to MTD by the Arab-Malaysian Bank in Kuala Lumpur.²¹
56. In March 1997, MTD representatives met three architectural firms of Santiago “to assist in the design work, performing engineering studies and obtaining regulatory approvals”²²; Darraidou, Larrain & Uranga (DLU), San Martín & Pascal and URBE. In April 1997, MTD selected DLU “to assist in obtaining zoning changes, subdividing the land, and designing prototype models of the houses and other structures.”²³ According to the Claimant, all three firms confirmed that the process to change the zoning would need to be initiated by the Municipality of Pirque and the change would need to be endorsed by the Ministry of Housing and Urban Development (“MINVU”).²⁴
57. MTD submitted a second application to FIC on April 8, 1997 for approval to invest additional working capital of US\$ 364,000. The second application was approved by FIC and MTD informed by letter dated April 22, 1997. The letter of approval enclosed the form of the standard foreign investment contract. The contract for this additional investment was signed on May 13, 1997. Its second clause provides that the investment will be used “[t]o make capital contributions and/or increases to the Chilean receiving company called MTD Chile S.A., which is developing a real estate project on 600 hectares of the Fundo El Principal de Pirque.”²⁵
58. On April 22, 1997, representatives of MTD and Mr. Labbé met with Messrs. Alberto Carbacho Duarte, the MINVU architect with overall responsibility for the Southern region of Santiago, which includes Pirque, and Mr. Sergio Lepe Corvalán, an official in the same office. According to the Claimants, Messrs. Carbacho and Lepe explained that

²⁰ Ibid., para. 43.

²¹ Ibid., para. 43.

²² Ibid., para. 44.

²³ Ibid.

²⁴ Ibid.

²⁵ Memorial, para. 39.

“because Pirque was covered by the Plano Regulador Metropolitano de Santiago (PMRS) [...] the MINVU would need to coordinate and approve the necessary zoning changes for the Project...the review process would be handled at the MINVU by the Secretario Regional Ministerial (SEREMI).”²⁶

59. On May 16, 1997, representatives of MTD met with the Mayor of Pirque, Mr. Manuel José Ossandón .²⁷
60. On May 20, 1997, Dato' Azmil Khalid met with Minister Edmundo Hermosilla. The same day, the MTD team met with Mr. Ricardo Lagos Escobar, then Minister of Public Works.
61. The Mayor of Pirque formally endorsed the Project by a letter dated August 14, 1997 and offered his assistance in obtaining approvals.²⁸
62. During this period, Minister Hermosilla was replaced by Mr. Sergio Henríquez Díaz.
63. On September 29, 1997, at an official state dinner on the occasion of the visit of the Prime Minister of Malaysia to Chile, President Eduardo Frei Ruiz-Tagle of Chile delivered a toast making reference, inter alia, to “the innovative real estate project in Pirque” Memorial, para. 51.²⁹ The next day appearance of the President at the inauguration of the Project was cancelled because of an alleged meeting with the President of Brazil. According to the Respondent, the speech to be read by the President, that was already in the hands of the Claimants, was withdrawn. This fact is contested by the Claimants.
64. Around November, 1997, “MTD heard from its consultants that SEREMI González of the MINVU was showing reluctance about modifying the PMRS for Pirque.”³⁰
65. On December 12, 1997, the Diario Oficial published the approval of the modification of the PMRS to include the Chacabuco area, North of

²⁶ Ibid., para. 45.

²⁷ Ibid., para. 46.

²⁸ Ibid., para. 50.

²⁹ Ibid., para. 51.

³⁰ Ibid., para. 54.

Santiago, in order to permit its development under the system of Zonas de Desarrollo Urbano Condicionado ("ZDUCs").³¹

66. In early 1998, MTD engaged the services of Mr. Pablo Heilenkötter, an attorney with expertise in land use regulation and real estate development. Since SEREMI González was unwilling to initiate the process to change the zoning, Mr. Heilenkötter and other consultants considered other alternatives under the *Ley General de Urbanismo y Construcción* ("LGUC"): "(i) the preparation of a sectional plan limited to a modification for the zoning in the area of the Project; (ii) the preparation of a communal plan for the Municipality of Pirque that would also include a zoning change for the area of the Project; and (iii) an application under article 55 for the construction of housing to complement a pre-existing activity."³²
67. Mr. Heilenkötter met with Mr. Lepe on March 6, 1998, and two weeks later with Mr. González together with other consultants of MTD. According to the Claimants, Mr. González informed them that he did not wish to undertake another modification to the PMRS "because it had just been changed in December 1997 to incorporate the Chacabuco area."³³
68. As MTD understood the LGUC, it was possible to pursue a change by way of a sectional plan and the Consejo Regional de la Región Metropolitana ("CORE") would "ultimately decide whether to approve the sectional plan, and it could do so over the MINVU's objection."³⁴
69. At this point, the Mayor of Pirque proposed to the Municipal Council to prepare a sectional plan to obtain a change in zoning. The Council approved such approach and the Mayor informed EPSA on March 31, 1998.
70. On April 13, 1998, MTD representatives and consultants met with Mr. Quintana, the CORE President. He suggested that, since Pirque did not have a Communal Regulatory Plan, the Municipality should submit with its sectional plan a strategic plan outlining Pirque's anticipated growth.³⁵

³¹ *Ibid.*, para. 54.

³² *Ibid.*, para. 55.

³³ *Ibid.*, paras. 56-57.

³⁴ *Ibid.*, para. 58.

³⁵ *Ibid.*, para. 60.

71. Sometime in April 1998, Dato' Azmil Khalid met with FIC Executive Vice-President Moyano "to discuss the slow progress of the zoning change request". Mr. Moyano reportedly said that he would make inquiries.³⁶
72. On April 16, 1998, the Mayor of Pirque, and MTD representatives and consultants met with Mr. Sergio González who informed them that the Project was inconsistent with MINVU's urban development policy.³⁷ After the meeting, the Mayor wrote to SEREMI González asking for "guidance about presenting a sectional plan to the MINVU for the development of the Project."³⁸
73. On April 20, 1998, Mayor Ossandón requested a meeting with the new MINVU Minister, Mr. Henríquez. The meeting took place on May 6, 1998 and it was also attended by representatives and consultants of MTD.³⁹
74. The SEREMI's office responded to the letter of April 16 on June 3, 1998 and explained: that "it would be inconvenient to initiate any changes to the PMRS pending completion of studies aimed at revising the Plan Regional de Desarrollo Urbano (PRDU)"; that "a sectional plan could not be used to obtain a change in zoning for the Project because only the SEREMI could initiate changes to the PMRS"; and that "before the investment contracts were signed, Minister Hermosilla had informed Mr. Fontaine and the Malaysian businessmen that it would not be possible to develop the Project in Pirque."⁴⁰
75. At the request of MTD and as a consequence of the letter of June 3, another meeting with Minister Henríquez took place on June 12, 1998. The Minister endorsed the letter of SEREMI González and confirmed that the MINVU would "neither initiate nor support any modification to the PMRS that would allow the Project to proceed."⁴¹
76. The same day, Mr. Heilenkötter met with Mr. Banderas of the FIC who informed him that "the FIC could not assist MTD and that its role is

³⁶ *Ibid.*, para. 66.

³⁷ *Ibid.*, para. 61.

³⁸ *Ibid.*, para. 63.

³⁹ *Ibid.*, para. 62.

⁴⁰ *Ibid.*, para. 63.

⁴¹ *Ibid.*, para. 64.

strictly limited to approving the inflow of foreign investment funds into Chile".⁴² At the request of Mr. Labbé, another meeting took place with Messrs. Moyano and Banderas. Mr. Moyano confirmed at the meeting that the approval of the FIC was without prejudice to other necessary approvals and that the FIC's authority was limited to the approval of the flow of funds into the country.⁴³

77. The Council of the Municipality of Pirque approved the Sectional Plan on July 3, 1998 and the Mayor submitted it to the SEREMI of MINVU on August 11, 1998. On September 8, 1998, the Mayor also submitted an Environmental Impact Study ("EIS") to the Comisión Regional del Medio Ambiente, Región Metropolitana ("COREMA"). On September 15, 1998, the COREMA informed the Municipality that it would review the EIS and announced the review in a public statement.⁴⁴
78. MTD's representatives held meetings with Mr. José Miguel Insulza, Minister of Foreign Affairs, who suggested that the Malaysian Government write him and President Frei requesting assistance to address MTD's situation. The Minister of Foreign Affairs of Malaysia wrote to Mr. Insulza and the Malaysian Prime Minister to President Frei on September 11 and September 15, 1998, respectively.⁴⁵
79. On September 25, 1998, the SEREMI of the MINVU returned the sectional plan to the Mayor of Pirque without evaluating the plan on its merits. The letter of SEREMI González indicated that "only the SEREMI could change the PRMS, that doing so would be 'inconvenient', and that a sectional plan could not be used to modify the PMRS."⁴⁶
80. On October 19, 1998, MTD's representatives and their advisors met with the MINVU Minister, Mr. Henríquez, and SEREMI González. Mr. Henríquez re-affirmed that the policy of the Government was to encourage development of Santiago towards the North and not the South where Pirque is located. Hence, he would not support the required zoning change, and the Project should be built elsewhere in Chile. On October 27, 1998, Mr. Shafiee sent Mr. Henríquez a letter

⁴² Ibid, para. 66

⁴³ Ibid., para. 67.

⁴⁴ Ibid., paras. 70-71.

⁴⁵ Ibid., para. 69.

⁴⁶ Ibid., para. 72.

thanking him for the meeting and including draft minutes of the meeting. The Minister responded on November 4, 1998 formally rejecting the Project. He stated that the SEREMI of the MINVU "will not initiate a change to the Regulating Plan for the Santiago Metropolitan Region to make this project possible". In a press release of the same day, MINVU indicated that it had rejected the Project because it conflicted with existing urban development policy and that the Mayor of Pirque no longer supported the Project.⁴⁷

81. On November 26, 1998, the COREMA rejected the EIS because the sectional plan was incompatible with the existing zoning for the land.⁴⁸
82. On December 15, 1998, the MINVU issued a more detailed press release about the rejection of the Project.⁴⁹
83. On June 2, 1999, MTD notified the Respondent that an investment dispute existed under the Malaysia-Chile Bilateral Investment Treaty (the BIT). At the end of the three-month negotiation period required by the BIT before the dispute may be brought to arbitration, no solution to the dispute had been found.⁵⁰ At the request of the Respondent, the parties agreed to a 30-day extension of the negotiation period. Negotiations continued without an agreement being reached at the expiry of the extension.⁵¹
84. On September 9, 1999, a third Foreign Investment Contract was signed between Chile and MTD for the purpose of providing an additional US\$ 25,000 of working capital to MTD Chile. As stated in the Memorial, "The third Contract was executed after the State of Chile had announced that the Project was incompatible with its urban-development policy and does not reference the Project in Pirque."⁵²
85. On October 8, 1999, MTD informed representatives of the Respondent that it would pursue this matter in formal dispute settlement proceedings under the auspices of ICSID. MTD continued to meet with repre-

⁴⁷ *Ibid.*, paras. 74-75.

⁴⁸ *Ibid.*, para. 77.

⁴⁹ *Ibid.*, para. 75.

⁵⁰ *Ibid.*, para. 80.

⁵¹ *Ibid.*, para. 81.

⁵² *Ibid.*, para. 40.

sentatives of the Respondent until it filed the request for arbitration in June 2001.⁵³

III. PRELIMINARY CONSIDERATIONS

1. *Applicable Law*

86. Article 42(1) of the Convention is the relevant provision for determining the law applicable to the merits of the dispute between the parties. This article requires the Tribunal to “decide a dispute in accordance with such rules of law as may be agreed by the parties”. This being a dispute under the BIT, the parties have agreed that the merits of the dispute be decided in accordance with international law. Applicable law has not been a matter of controversy between the parties except as it pertains to the issue of whether the Respondent has failed to meet its obligations, under the Foreign Investment Contracts, to grant the necessary permits for the Claimants to carry out their investment in Chile. The Claimants argue that the alleged failure of the Respondent has to be considered under international law because Article 3(1) of the Bilateral Investment Treaty between Chile and Denmark (the “Denmark BIT”) has the effect of internationalizing the obligations of the Respondent under the Foreign Investment Contracts. The Respondent denies that Article 3(1) of the Denmark BIT had such effect and maintains that Chilean law applies on the basis of Article 42(1) of the Convention. The Respondent affirms that, in the absence of agreement between the parties, “The applicable law in regard to the foreign investment contracts is Chilean domestic legislation, according to the provisions of the Washington Convention.”⁵⁴

87. At this point, the Tribunal will limit itself to note that, for purposes of Article 42(1) of the Convention, the parties have agreed to this arbitration under the BIT. This instrument being a treaty, the agreement to arbitrate under the BIT requires the Tribunal to apply international law. The Tribunal will analyze further this issue when considering the effect of Article 3(1) of the Denmark BIT.

⁵³ *Ibid.*, paras. 82 and 84.

⁵⁴ Rejoinder, para. 126 and footnote 61.

2. Significance of an Investment Dispute

88. At the beginning of its Counter-Memorial, Chile has made statements and provided statistics in support of Chile as “a place to invest”. Indeed, between 1974 and 2001, US\$ 82.9 billion in foreign investment were authorized, and more than four thousand companies invested in Chile. Chile has also pointed out that the case before the Tribunal is the first time that foreign investors appear before ICSID claiming that Chile violated DL 600⁵⁵ and engaged in discriminatory practices.⁵⁶
89. The Tribunal, in noting the success of the Respondent in attracting foreign investment, wishes to record its understanding that a dispute before an ICSID Tribunal is not necessarily a black mark on the record of a country or an investor. Bilateral investment treaties are relatively new and it is not unreasonable that their application or the many factors that affect foreign investment be a source of disagreement. The fact that disagreements are brought to the decision of a third party, such as an ICSID arbitral tribunal, and that a country has offered to do so in a treaty strengthens rather than detracts from a country’s endeavor to attract foreign investment and treat investors fairly and equitably.

3. Jurisdiction

90. As regards the jurisdiction of the Centre and the competence of this Tribunal, the Claimants maintain that their dispute with the Respondent is a legal dispute that arises out of an investment made in Chile by a national of another Contracting State, Malaysia. The Respondent has not raised any objections about this matter.
91. The Respondent consented to ICSID arbitration under the BIT and the Claimants consented when they filed their request for arbitration.
92. Article 6(1) of the BIT provides:

“Each Contracting Party consents to submit to the International Centre for the Settlement of Investment Disputes [...] any dispute arising between that Contracting

⁵⁵ Decree Law 600, the Foreign Investment Law of the Republic of Chile.

⁵⁶ Counter-Memorial, paras. 1 and 2.

Party and an investor of the other Contracting Party which involves:

(i) an obligation entered into by that Contracting Party with the investor of the other Contracting Party regarding an investment by such investor, or (ii) an alleged breach of any right conferred or created by this Agreement with respect to an investment by such investor.”

93. MTD Equity is a “national of another Contracting State”: it is a corporation organized under the laws of Malaysia and has its seat and operations in Malaysia. It is also an “investor” under the terms of Article 1(c)(ii) of the BIT, which defines investor as including:

“any corporation, partnership, trust, joint venture, organization, association or enterprise incorporated or duly constituted in accordance with applicable laws of that Contracting Party and have their seat and operations in the territory of that same Contracting Party.”

94. MTD Chile is wholly owned by MTD Equity and is a corporation organized under the laws of Chile. Under Article 25(2)(b) of the ICSID Convention and Article 6(2) of the BIT, such a corporation is to be deemed as a Malaysian national for purposes of arbitration proceedings under the ICSID Convention.

95. The dispute between the parties qualifies as a dispute under each of the categories of Article 6(1) of the BIT. It involves an obligation entered into by the Respondent with the Claimants regarding their investment in Chile and an alleged breach of their rights under the BIT in respect of such investment.

96. The requirement of Article 6(3)(i) of the BIT that the parties try to solve the dispute “amicably through consultation and negotiation” for at least three months before resorting to arbitration has also been satisfied. Negotiations took place for a period exceeding three months and through a one-month extension after the Claimants notified, on June 2, 1999, the President of Chile and the Minister of Economy that a dispute had arisen and invoked Article 6 of the BIT.

97. The Tribunal is satisfied that the dispute between the parties arises out of an investment made by MTD Equity, a national of Malaysia, in Chile and that the investment so made qualifies as such under the Convention and the BIT.

4. *The Right of States to adopt Policy and enact Legislation*

98. The Tribunal concurs with statements made by the Respondent to the effect that it has a right to decide its urban policies and legislation. Indeed, the States parties to the BIT have agreed that their commitment to encourage and create favorable conditions for investors and admit their investments is "subject to [each party's] rights to exercise powers conferred by its laws, regulations and national policies."⁵⁷ Furthermore, in the definition of investment, the term "investment" is understood to refer to "all investments approved by the appropriate Ministries or authorities of the Contracting Parties in accordance with its legislation and national policies."⁵⁸

99. Thus, by entering into the BIT, the Contracting Parties did not limit the exercise of their authority under their national laws or policies except to the extent that this exercise would contravene obligations undertaken in the BIT itself. An arbitral tribunal in the specific case of ICSID would not consider the policies or legislation of a country and changes thereto unless a connection can be established with the investment concerned. This connection may be "established if those general measures are adopted in violation of specific commitments given to the investor in treaties, legislation or contracts. What is brought under the jurisdiction of the Centre is not the general measures in themselves but the extent to which they may violate those specific commitments."⁵⁹

5. *The Most-Favored-Nation (MFN) Clause*

100. The Claimants have based in part their claims on provisions of other bilateral investment treaties and have alleged that these provisions apply by operation of the MFN clause of the BIT. The Respondent has not argued against the application of these provisions but, in the case of Article 3(1) of the Denmark BIT and Article 3(3) and (4) of the bilateral investment treaty between Chile and Croatia ("the Croatia BIT"), the Respondent has qualified its arguments by stating that, even in the event that the clause concerned would apply, the facts of the case are such that it would not have been breached. Because of this qualification in the Counter-Memorial and the Rejoinder, the Tribunal consid-

⁵⁷ Article 2(1).

⁵⁸ Article 1(b).

⁵⁹ CMS Gas Transmission Company v. The Republic of Argentina. Case No. ARB/01/8. Decision on Jurisdiction, para. 27.

ers it appropriate to examine the MFN clause in the BIT and satisfy itself that its terms permit the use of the provisions of the Denmark BIT and Croatia BIT as a legal basis for the claims submitted to its decision.

101. The first paragraph of the MFN clause of the BIT - (Article 3(1)) - reads as follows:

“1. Investments made by investors of either Contracting Party in the territory of the other Contracting Party shall receive treatment which is fair and equitable, and not less favourable than that accorded to investments made by investors of any third State.”

102. The other provisions of this Article extend the clause to compensation related to losses suffered because of wars or like events or limit its application by excluding benefits provided in regional cooperation and taxation related agreements.

103. The question for the Tribunal is whether the provisions of the Croatia BIT and the Denmark BIT which deal with the obligation to award permits subsequent to approval of an investment and to fulfillment of contractual obligations, respectively, can be considered to be part of fair and equitable treatment.

104. The Tribunal considers the meaning of fair and equitable treatment below and refers to that discussion. The Tribunal has concluded that, under the BIT, the fair and equitable standard of treatment has to be interpreted in the manner most conducive to fulfill the objective of the BIT to protect investments and create conditions favorable to investments. The Tribunal considers that to include as part of the protections of the BIT those included in Article 3(1) of the Denmark BIT and Article 3(3) and (4) of the Croatia BIT is in consonance with this purpose. The Tribunal is further convinced of this conclusion by the fact that the exclusions in the MFN clause relate to tax treatment and regional cooperation, matters alien to the BIT but that, because of the general nature of the MFN clause, the Contracting Parties considered it prudent to exclude. A contrario sensu, other matters that can be construed to be part of the fair and equitable treatment of investors would be covered by the clause.

IV. CONSIDERATIONS ON THE MERITS

105. The Claimants allege that the Respondent has breached:

- (i) Articles 2(2) and 3(1) of the BIT and Article 4(1) of the Croatia BIT by treating their investment unfairly and inequitably;
- (ii) Article 3(1) of the Denmark BIT by breaching the Respondent's obligations under the Foreign Investment Contracts;
- (iii) Article 3(2) and (4) of the Croatia BIT by impairing through unreasonable and discriminatory measures the use and enjoyment of the Claimants' investment and by failing to grant the necessary permits to carry out an investment already authorized; and
- (iv) Article 4 of the BIT by expropriating their investment.

106. The alleged breaches of the Denmark and Croatia BITs are based on the MFN clause of the BIT. The Tribunal will now consider each of these claims and the allegation made by the Respondent that the Claimants acted irresponsibly and contrary to the prudent and diligent standard of behavior expected from an experienced investor.

1. Fair and equitable treatment

(i) Meaning of "fair and equitable treatment"

107. Article 2(2) of the BIT requires that "Investments of investors of either Contracting Party shall at all time be accorded fair and equitable treatment [...]" The Croatia BIT provides that the right to fair and equitable treatment shall "not be hindered in practice" (Article 4(1)). There is no dispute between the parties about the applicability of these provisions, but they disagree on key facts to determine whether the standard of fair and equitable treatment has been breached. They also disagree on the significance of actions taken by the Respondent in relation to the approval of the investment and the execution of the Foreign Investment Contracts, and the significance of the conduct of the Claimants in reaching and executing their decision to invest in Chile.

108. The parties appear to agree on the meaning of fair and equitable treatment, but in view of comments made by them in the memorials, the Tribunal will address this matter first and then will consider the

facts underlying the Claimants' submission for purposes of applying this standard of treatment.

109. The parties agree that there is an obligation to treat investments fairly and equitably. The parties also agree with the statement of Judge Schwebel that "the meaning of what is fair and equitable is defined when that standard is applied to a set of specific facts"⁶⁰ As defined by Judge Schwebel, "fair and equitable treatment" is "a broad and widely-accepted standard encompassing such fundamental standards as good faith, due process, nondiscrimination, and proportionality".⁶¹
110. The parties have commented on whether the fair and equitable standard is part of customary international law or additional to customary international law in reference to recent awards of arbitral tribunals established under NAFTA before and after the interpretation of Article 1105(1) by the NAFTA Free Trade Commission. The Free Trade Commission has interpreted "fair and equitable treatment" as not requiring treatment in addition to or beyond that which is required by the international law minimum standard.
111. The Tribunal notes that Chile has not argued that this is how "fair and equitable treatment" should be understood under the BIT. Chile has simply drawn attention to this interpretation and the consequences it had on the application of the standard of fair and equitable treatment by NAFTA arbitral tribunals. The Tribunal further notes that there is no reference to customary international law in the BIT in relation to fair and equitable treatment.
112. This being a Tribunal established under the BIT, it is obliged to apply the provisions of the BIT and interpret them in accordance with the norms of interpretation established by the Vienna Convention on the Law of the Treaties, which is binding on the State parties to the BIT. Article 31(1) of the Vienna Convention requires that a treaty be "interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

⁶⁰ Opinion of Judge Steven Schwebel, para. 23. Witness Statement submitted with the Memorial.

⁶¹ *Ibid.*

113. In their ordinary meaning, the terms “fair” and “equitable” used in Article 3(1)⁶² of the BIT mean “just”, “even-handed”, “unbiased”, “legitimate”.⁶³ These terms are also used in Article 2(2) of the BIT entitled “Promotion and Protection of Investments”.⁶⁴ As regards the object and purpose of the BIT, the Tribunal refers to its Preamble where the parties state their desire “to create favourable conditions for investments by investors of one Contracting Party in the territory of the other Contracting Party”, and the recognition of “the need to protect investments by investors of both Contracting Parties and to stimulate the flow of investments and individual business initiative with a view to the economic prosperity of both Contracting Parties”. Hence, in terms of the BIT, fair and equitable treatment should be understood to be treatment in an even-handed and just manner, conducive to fostering the promotion of foreign investment. Its terms are framed as a pro-active statement –“to promote”, “to create”, “to stimulate”- rather than prescriptions for a passive behavior of the State or avoidance of prejudicial conduct to the investors.

114. Faced with a similar task, the tribunal in *TECMED* described the concept of fair and equitable treatment as follows:

“[...] to provide to international investments treatment that does not affect the basic expectations that were taken into account by the foreign investor to make the investment. The foreign investor expects the host State to act in a consistent manner, free from ambiguity and totally transparently in its relations with the foreign investor, so that it may know beforehand any and all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. Any and all State actions conforming to such criteria should relate not only to the guidelines, directives or requirements issued, or

⁶² Article 3(1): “Investments made by investors of either Contracting Party in the territory of the other Contracting Party shall receive treatment which is fair and equitable, and not less favourable than that accorded to investments made by investors of any third State.”

⁶³ The Concise Oxford Dictionary of Current English, fifth edition.

⁶⁴ Article 2(2): “Investments of investors of either Contracting Party shall at all time be accorded fair and equitable treatment and shall enjoy full protection and security in the territory of the other Contracting Party.”

the resolutions approved thereunder, but also to the goals underlying such regulations. The foreign investor also expects the host State to act consistently, i.e. without arbitrarily revoking any preexisting decisions or permits issued by the state that were relied upon by the investor to assume its commitments as well as to plan and launch its commercial and business activities. The investor also expects the state to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments, and not to deprive the investor of its investment without the required compensation.”⁶⁵

115. This is the standard that the Tribunal will apply to the facts of this case. The facts or their significance are controversial and the Tribunal will first describe the allegations of the parties as they relate to them.

(ii) Allegations of the Parties

116. According to the Claimants, the Respondent breached the fair and equitable treatment provisions of the BIT and the Croatia BIT when it “created and encouraged strong expectations that the Project, which was the object of the investment, could be built in the specific proposed location and entered into a contract confirming that location, but then disapproved that location as a matter of policy after MTD irrevocably committed its investment to build the Project in that location.”⁶⁶ Furthermore, to the extent that, as alleged by MINVU, the Respondent was always opposed to the Project even before the signing of the Foreign Investment Contracts, then the Respondent acted “dupliciously and in bad faith, for at that time - according to the MINVU’s argument - the State of Chile had already made a decision to block the Project.”⁶⁷ The Respondent disputes such allegations by referring to meetings the Claimants had with Government officials and by questioning the significance attributed by the Claimants to the approval of their investment by the FIC.

⁶⁵ Técnicas Medioambientales TECMED S.A. v. The United Mexican States, ICSID Case No. ARB(AF)00/2, award dated May 29, 2003, para. 154. See also Waste Management, Inc. v. United Mexican States, ICSID Case No. ARB(AF)00/3, para. 98.

⁶⁶ Memorial, para. 102.

⁶⁷ Ibid., para. 103.

117. The Respondent places great significance on the November 6, 1996 meeting with Minister Hermosilla and SEREMI González. The Claimants deny that such meeting ever took place. According to the Respondent, in this meeting, the Chilean officials warned Claimants' representatives that "the PMRS, which categorically forbade urban development in Pirque, posed a serious impediment to the Project", and that "because the Project was inconsistent with the goals of the PMRS, one of which was to promote urban densification, the office of the SEREMI would not be able to sponsor the project before the CORE."⁶⁸ The Respondent concludes the narrative of the November 6 meeting by saying that that meeting "should have left MTD with grave doubts about the viability of a real estate project in Pirque. At this point, a reasonable investor would have undertaken rigorous due diligence as to whether, among other things, any further developmental costs were warranted. Instead, despite having been put on clear notice that its proposed Project faced serious risks, MTD proceeded to enter into a joint venture agreement, further solidifying its commitment to the El Principal Project."⁶⁹
118. The Respondent maintains that, through the many meetings that representatives of the Claimants had with officials of the Chilean Government, the Claimants were informed about the difficulty of achieving a change in the PMRS, that the SEREMI of MINVU had the initiative to propose such change, and that a sectional plan was not the proper vehicle to change the PMRS because it is an instrument hierarchically lower from a normative point of view. The meetings that the Claimants had with various urban planning firms in March 1997 and related correspondence show that already at that time they were aware of the need to re-zone El Principal.⁷⁰
119. The Respondent further alleges that the role of the FIC is only to approve the capital transfer and not the details of the project itself, hence the limited nature of the description of the purpose of the investment. The Foreign Investment Contracts guarantee the foreign investor the same treatment as a national investor and provide that the authorization to import capital into Chile is "without prejudice to any others which, pursuant to such laws and regulations must be granted by the competent authorities." Therefore, the Foreign Investment Contracts

⁶⁸ Counter-Memorial, paras. 25-27.

⁶⁹ *Ibid.*, para. 27.

⁷⁰ *Ibid.*, paras. 48-96.

required "MTD to obtain zoning permits, environmental approvals and other applicable authorizations relating to the Project."⁷¹

120. As regards claims of Chile's extra-contractual liability, the Respondent alleges that they "betray a fundamental misunderstanding of the FIC approval process and other provisions of Chilean law", and contests even the existence of a possibility of extra-contractual liability: if a contract exists, "a claim may only be brought alleging the contractual breach; an additional claim alleging quasi-contractual liability is inadmissible."⁷²
121. According to the Respondent, the FIC is not obliged under article 15(c) of DL 600, as the Claimants maintain, to obtain reports prior to deciding on foreign investment applications except in limited circumstances required by legislation other than DL 600 itself. There is no legal norm or regulation that imposes upon the FIC the obligation to obtain from any other authority a report or pre-approval of a real estate project such as the proposed investment of the Claimants.⁷³ The FIC is not required either to seek a change in the PMRS after the approval of the foreign investment application. If this were the case, then Article 9 of DL 600 and Clause Four of the foreign investment contracts would be rendered meaningless and the FIC would operate outside the scope of its authority.⁷⁴
122. The Respondent explains that the FIC's jurisdiction does not "extend to determining the legal, administrative, technical or economic feasibility of those investments, nor does it restrict or limit the authority or jurisdiction of any government agency. The jurisprudence of domestic courts has uniformly recognized the limited jurisdiction of the Committee and the limited scope of the Investment Contract."⁷⁵ According to the Respondent, the Claimants have completely misrepresented the functions of the FIC by assigning to it the character of a "one-stop window". As explained by expert Feliú, in public law the "principle of lawfulness" requires that, in order for a public body to act as a "one-stop window", it needs to be so authorized.⁷⁶ It was not the

⁷¹ *Ibid.*, paras. 31-32.

⁷² *Ibid.*, para. 129 quoting expert Feliú's opinion.

⁷³ *Ibid.*, para. 131.

⁷⁴ *Ibid.*, para. 133.

⁷⁵ Rejoinder, para. 37.

⁷⁶ *Ibid.*, paras. 40-41.

FIC's "duty to reject MTD's Foreign Investment Application due to restrictions of land use, because the Committee did not have the legal authority to carry out such an evaluation. MTD chose to take the risk associated with its investment, which involved executing an urban development project in a restricted area, while speculating that the policies regarding land use in Chile would be modified in its favor."⁷⁷ The Respondent maintains that the reference to the Municipality of Pirque in the Application does not modify "the authority of the Committee, nor does it make the Committee the underwriter of the viability of the project."⁷⁸

123. The Respondent also dismisses the argument that it is extra-contractually liable because the Minister of MINVU, as "relevant Minister" under article 13(d) of the DL 600, did not attend the meeting which approved the Claimants' request. The Respondent maintains that this argument has no basis because under Article 14 the only requirement for a meeting is that a certain quorum be achieved with or without the "relevant Minister". In any case, it is the SEREMI of MINVU who is responsible for recommending the modification of the PMRS and the SEREMI acts independently of the MINVU Minister. The Respondent affirms further that, if the Minister of MINVU had attended the meeting, the outcome would have remained the same. He would presumably have commented that the project was risky but that in itself would not have been grounds for rejecting the application since the investor had the right to seek a modification of the PMRS:

"It is not within the FIC's authority or mandate to perform a risk assessment with respect to the investments that are the subject of the capital inflows it approves. The resolution of questions involving risk is wholly within the investor's sphere, and such issues have no bearing on the FIC's approval or disapproval of foreign investment applications."⁷⁹

124. The Claimants deny that the November 6, 1996 meeting ever took place and consider that the meeting is "crucial to the Respondent's case: this is the sole warning that MTD is alleged to have received before committing its investment". The documents presented as evidence of what was said at the meeting were written in 1998, not in

⁷⁷ *Ibid.*, para. 47.

⁷⁸ *Ibid.*, para. 50.

⁷⁹ Counter-Memorial, paras. 134-137. See also Rejoinder para. 68.

1996.⁸⁰ There are no contemporaneous records of the meeting except for the word "Malaysia" in the appointment book of Minister Herмосilla. The Claimants note that "It is striking that the Respondent's witnesses – without contemporaneous documentary record of the meeting – now remember details of the discussion so well seven years later, but are unable to recall who attended."⁸¹

125. The Claimants point out that the warnings that MTD allegedly received from architects, urban planners and government officials after signing the first Foreign Investment Contract would have come too late.⁸² The Claimants also note that, in its Reply, the Respondent does not acknowledge that the President of Chile praised the Project as innovative in September 1997 and the Claimants were never informed that the cancellation of the President's appearance the next day related to the withdrawing of support for the Project.⁸³ In fact, the reason given was that the President could not attend because of a conflicting meeting with the President of Brazil.

126. According to the Claimants, it was only in 1998 that they were informed about the meeting of November 6, 1996, and that the approval of the investment application only meant that MTD could import funds and that Chilean officials first began to raise environmental concerns: "The Respondent does not explain why these supposedly long-standing and important governmental positions and policies were not communicated to MTD before 1998."⁸⁴

127. The Claimants address the Respondent's assertion that, if they had acted diligently, they "would quickly have discovered that its [their] Project was unfeasible" by pointing out the following flaws: "First, if it was indeed so clear that the Project was not feasible, why did none of the many officials with whom MTD representatives met inform MTD of this impossibility until 1998? Second, the Respondent's 'due diligence' argument is premised on the warnings supposedly given to MTD at the phantom meeting of 6 November 1996."⁸⁵ In any case, "If the Project was in fact 'unfeasible' from the beginning, the State of Chile should not

⁸⁰ Reply, para. 4.

⁸¹ *Ibid.*, para. 18.

⁸² *Ibid.*, para. 7.

⁸³ *Ibid.*, para. 8.

⁸⁴ *Ibid.*, para. 9.

⁸⁵ *Ibid.*, para. 28.

have misled MTD by approving MTD's investment application and entering into Foreign Investment Contracts with MTD based on the illusory promise of a housing project in Pirque. If, on the other hand, the Project was not an impossibility, the Respondent should not have rejected MTD's requests for necessary approvals on the pretext that the applicable norms necessarily preclude any urban development in Pirque.⁸⁶

128. The Claimants also note that the Counter-Memorial overlooks the description of the Project in the application to the FIC, and, instead, focuses on the capital contribution section. It is clear from the project description section and the Second Clause of the Foreign Investment Contract, which are essentially the same, that the project and its location are clearly identified and the contract states that the purpose of the investment is exclusive and it could only be modified with the prior authorization of FIC.⁸⁷

129. The Claimants address the Respondent's explanation that the specific identification of the project in a foreign investment contract lacks significance and state that: "No Governmental official told MTD of any such limitation before signing the Foreign Investment Contracts." The opinions of the experts submitted with the Counter-Memorial and the testimony of Mr. Moyano focus on the fact that a foreign investment contract does not automatically provide all governmental approvals necessary to realize a project, but "they do not address the different question presented by this case: Whether the state of Chile may properly enter into a binding foreign investment contract that specifies the purposes and location of a particular investment project while, at the same time, knowing (and not telling the investor) that the Government will never allow the investor to carry out the project that is the premise of the contract."⁸⁸

130. The Claimants point out that although the Respondent refused to provide copies of the minutes of the FIC meetings, it did provide records of attendance that show that Ministers who were not permanent members of the FIC attended some meetings, "presumably to discuss and vote upon foreign investment applications that were relevant to their areas of responsibility, as required by Article 13 of DL 600."⁸⁹

⁸⁶ *Ibid.*, para. 12.

⁸⁷ *Ibid.*, paras. 31-34.

⁸⁸ *Ibid.*, para. 36.

⁸⁹ *Ibid.*, para. 41.

According to the Claimants, if “the role of the FIC were simply to approve the inflow of funds (as opposed to approving an investment for a particular project), then it would have been unnecessary and illogical for DL 600: (i) to provide that a Minister who is not a permanent member of the FIC is nevertheless a member for purposes of considering applications that are relevant to that Ministry’s work; and (ii) to require the Executive Vice President of the FIC to coordinate with other government agencies concerning information and authorizations.”⁹⁰ Furthermore, the Respondent is obliged to ensure under article 15(a) of the DL 600 that the FIC coordinates and consults with Ministries concerned. Although requested by the Claimants, the Respondent was not able to find any “responsive” documents.⁹¹

131. The Claimants argue that the Respondent’s position is inconsistent with the availability of other procedures for bringing foreign capital into Chile without signing a foreign investment contract and without necessarily identifying the object and purpose of their investment: “If the FIC’s role were limited to approval of the inflow of funds there would be no need for the FIC, because the Central Bank of Chile already has authority to [sic] the inflow of funds without consideration of the underlying project.”⁹² The position of the Respondent is also inconsistent with the terms of the Foreign Investment Contract: “If the object of the contract were limited to the inflow of funds, the contract would not need to specify the purpose of the investment, or provide that the purpose of the investment can be changed only with the FIC’s approval.”⁹³
132. As regards Clause Four of the Foreign Investment Contract, the Claimants point out that “It is one thing to argue that MTD must still satisfy norms and other requirements in the process of realizing the [P]roject – which MTD always understood. It is quite another matter for the Respondent to argue that Clause Fourth [sic] entitled it to approve and accept MTD’s investment in Chile while knowing that the premise of the contract could never be realized.”⁹⁴
133. The Claimants note that the Respondent has not presented contemporaneous evidence to support the alleged actual reasons for the with-

⁹⁰ Ibid., para. 42.

⁹¹ Ibid., para. 49.

⁹² Ibid., para. 43.

⁹³ Ibid., para. 44.

⁹⁴ Ibid., para. 46.

drawal of the speech of the President at the inauguration of the Project: "If the President's office had "withdrawn" the text of a presidential speech that he sent to be read at the inauguration ceremony, it would be reasonable to expect some record of such withdrawal. And if MTD had used a presidential speech without permission, surely the Chilean Government would have taken some action at least to indicate its displeasure. By contrast, the Claimants have submitted to the Tribunal a copy of the fax that they received from the Government with the approved words of President Frei's message."⁹⁵

134. The Claimants take issue with the statement of the Respondent that "the laws and regulations that govern urban planning and development in Chile – and in particular modifications to the PMRS – are simple and transparent."⁹⁶ It is the opinion of the Claimants that contrary to what the Respondent maintains, a sectional plan was an appropriate instrument to modify the PMRS. According to them, this instrument proposed by a municipality is not dependent on the MINVU for its initiation or completion: "When a sectional plan is filed with the MINVU, the SEREMI is required to analyze the request and forward it to the CORE with a favorable or unfavorable report."⁹⁷

135. The Claimants point out that uncertainty and confusion in the urban planning and development are also evident in respect of the recently proposed Modification No. 48 to the PMRS.⁹⁸ The CORE approved said modification by Resolution No. 14/2003. However, the Contraloría General has refused to accept the legality of the resolution "ruling that the CORE exceeded its authority by attempting to regulate rural lands located outside of the established urban limits."⁹⁹ The decision has been appealed by CORE.

136. In the opinion of the Claimants, Modification No. 48 contradicts the arguments of the Respondent as regards the uniqueness of Pirque from an environmental point of view: "It demonstrates that Pirque is not a unique "key sector" that must be exempted from urban development to protect the so called "environmental filter" of the Santiago met-

⁹⁵ *Ibid.*, para. 58.

⁹⁶ *Ibid.*, para. 70.

⁹⁷ *Ibid.*, para. 71.

⁹⁸ This modification of the PMRS permits Zonas de Desarrollo Urbano Condicionado in the area South of Santiago that includes Pirque.

⁹⁹ Reply, para. 72.

ropolitan region.”¹⁰⁰ The Claimants point out that it is striking that “MINVU chose to submit a Declaración de Impacto Ambiental (“DIA”), which involves a lower level of environmental analysis than an EIS, even though Modification No. 48 would introduce sweeping changes to the use of land throughout the Santiago Metropolitan Region, affecting over 34,000 hectares in comparison with the 600 hectares covered by the Municipality of Pirque’s sectional plan. Further, the MINVU’s DIA is much more vague and general than the EIS submitted with the sectional plan. Yet, in stark contrast to the way the COREMA treated the EIS submitted by the Municipality of Pirque, the COREMA concluded, after evaluating the DIA submitted by MINVU, that the proposed modification of the PMRS would not generate any relevant adverse environmental impacts.”¹⁰¹

137. The Claimants consider “disingenuous” the argument put forward by the Respondent to the effect that the Claimants should have requested an amendment of the PMRS instead of designing a sectional plan “because the Respondent made clear that it would not allow realization of the Project under any procedure. MTD and the Municipality of Pirque attempted the procedure of a sectional plan only after the MINVU indicated that it would not initiate such a change itself and the Respondent, through the MINVU, declined repeatedly to provide any guidance regarding the proper procedures to be followed to modify the PMRS.”¹⁰²
138. The Respondent argues that the Claimants cannot excuse their failure to comply with the law by alleging ignorance of the law. The law was clear, the plot of land in the Fundo El Principal was exclusively for silvoagropecuario use and the foreign investment contracts grant investors only the authorizations provided therein.¹⁰³ Referring to the cases decided by other arbitral tribunals relied on by the Claimants, the Respondent affirms that “[i]n contrast, MTD never had any right to carry out its Project, which was always contingent on the obtaining of the relevant authorizations by means of the procedure established by law. MTD did not understand or did not want to understand the regulations in force, choosing instead to follow procedures clearly contrary to the law.”¹⁰⁴

¹⁰⁰ Ibid., para. 84.

¹⁰¹ Ibid., para. 85.

¹⁰² Ibid., para. 118.

¹⁰³ Rejoinder, paras. 5-7.

¹⁰⁴ Ibid., para. 9.

139. The Respondent points out that the two communications of 1998 that refer to the November 6, 1996 meeting “were prepared and sent before any controversy existed between MTD and the Government, which thus belying [sic] MTD’s argument that this meeting has been fabricated by the Government.”¹⁰⁵ The Respondent also addresses the Claimants’ assertion that they did not receive any warning regarding the feasibility of their investment project before signing the Foreign Investment Contract and that if “MTD had been told in 1996 that the Project was not feasible, it would never have invested in the Project.” The Respondent comments that “this argument is based on an erroneous assumption that the Government of Chile had the obligation to warn MTD about the feasibility of its project before it invested. In fact, it was MTD that had the obligation to obtain the necessary information regarding the legal and technical feasibility of its project. This is particularly true, given that this information was public, transparent, and readily available.”¹⁰⁶ The Respondent points out the failure of the Claimants to mention that, “under the legislation in force at that time, it was possible, though difficult and not guaranteed, to obtain a modification of the PMRS, and that MTD tried to obtain such a modification by means of an erroneous procedure that necessarily led to its rejection.”¹⁰⁷
140. The Respondent rebuts the argument that their officials were unresponsive to the Claimants’ requests for assistance. In fact, “Due to the evident lack of competence of MTD’s consultants, Mr. Carvacho and Mr. Leppe offered to assist the company by guiding them through the steps necessary to attempt a modification of the PMRS, but MTD never took them up on this offer.”¹⁰⁸
141. The Respondent reaffirms that it had no obligation to modify the PMRS and to allow the Project to proceed. Every step taken by the Respondent’s officials was taken in accordance to the law, including the rejection of the Sectional Plan. Sectional plans cannot alter or modify the norm established by instruments of a higher hierarchy and the modification of the PMRS was inconvenient because the MINVU SEREMI was undertaking the study of the Regional Plan of Urban Development (“PRDU”). As explained by the Respondent, “The PRDU is

¹⁰⁵ *Ibid.*, para. 27.

¹⁰⁶ *Ibid.*, para. 30.

¹⁰⁷ *Ibid.*, para. 36.

¹⁰⁸ *Ibid.*, para. 69.

the urban planning instrument that establishes the roles of the urban centers, their gravitational areas of reciprocal influence, gravitational relations, and growth targets, among others."¹⁰⁹ The study of PRDU for the Santiago Metropolitan Region had begun in 1994 after the entry into force of the PMRS, and "it was being analyzed in 1998."¹¹⁰

142. The contention that, according to Chilean law, the SEREMI had an obligation to forward the sectional plan to the CORE contradicts the LGUC which establishes the legal procedure for the elaboration of the norms of the PMRS, "what the CORE approved or rejected was a proposal of the SEREMI and not a proposal of any other agency. The CORE did not have the power to consider or approve planning proposals of any other entities, including the sectional plans presented by the municipalities."¹¹¹

143. The Respondent admits that "Chilean urban planning regulations are complex, given their highly technical nature, but they are comprehensible, a diligent investor would require competent professional assistance, as would a domestic investor."¹¹² In any case, the Respondent argues that "complexity neither excuses MTD's negligence nor justifies MTD's attempts to circumvent the legally established procedures. MTD never followed these procedures but rather chose to evade them. MTD presented a Sectional Plan, through the Municipality of Pique, to modify the provisions of the PMRS, even though it was well informed that [sic] procedure was contrary to the regulations in force."¹¹³

144. Respondent defends Modification No. 48 as proof of the evolution of the urban planning framework in Santiago: "Land use regulation and the policies adopted in these matters in the Santiago Metropolitan Area can evolve over time. That evolution is carried out within a transparent administrative system, which mandates consultation with, and approval of, multiple government agencies [...] All the modifications [between 1997 and 2002] were the result of the procedures established under Chilean law and sought the public welfare of all the population."¹¹⁴

¹⁰⁹ *Ibid.*, para. 83.

¹¹⁰ *Ibid.*

¹¹¹ Rejoinder, para. 75.

¹¹² *Ibid.*, para. 93.

¹¹³ *Ibid.*

¹¹⁴ *Ibid.*, para. 95.

145. Chile argues that “The fact that the General Finance office of the Republic¹¹⁵ has formulated observations to the resolution [sic] approves [sic] that Modification No. 48 does not demonstrate to the ‘uncertainty and confusion related to the rules governing development and urban planning in Chile, [...] it demonstrates the functioning of the administrative regime and the Chilean democracy, and that the mere fact that the authority proposes modifications to the norm is no guarantee they will be implemented. This does not imply arbitrary conduct, but the normal process of creation of standards under a democratic and transparent system.”¹¹⁶
146. According to the Respondent, it is wrong to characterize Modification No. 48 as a means to allow large-scale urban development in the area of Pirque. The Respondent maintains that “MTD diminishes the impact of the conditions imposed on the development of new projects. In fact, Modification No. 48 would eventually allow the implementation of Conditional Urban Development Projects, only after the fulfillment of much stricter requirements than those previously imposed on any other housing project in the Santiago Metropolitan Area; the projects would have to be subjected to feasibility studies regarding basic conditions of location, size and profile of the proposal. These studies would be carried out by the municipalities where the project is located, by the SEREMI of Agriculture and the SEREMI of Housing. Subsequently, with the unanimous approval of those three agencies, the project would enter a technical evaluation phase by the SEREMI of Housing, which would have to determine if seven determinant conditions are fulfilled...the mere fulfillment of the requirements established in Modification No. 48 would not authorize the modification of land use.”¹¹⁷
147. For the Respondent, it is clear that Modification No. 48 would make it more difficult for large-scale real estate projects to be carried out in areas currently outside urban limits, since, as the Respondent explains, they “would have to go through two different and consecutive stages: first, they will have to fulfill the new requirements established in Modification No. 48 and, second, they will have to abide by the rules currently in place for PMRS modification. Between 1996 and 1998, however, MTD would only have had to fulfill this second stage.”¹¹⁸

¹¹⁵ Contraloría General de la República.

¹¹⁶ Rejoinder, para. 96.

¹¹⁷ *Ibid.*, paras. 99-100.

¹¹⁸ *Ibid.*, para. 101.

148. In the Rejoinder, Chile re-affirms its right to require that MTD comply with Chilean environmental and urban planning regulations. The Project “constituted an inappropriate attempt to use a Sectional Plan to modify the land use restrictions established by the PMRS for that Municipality”. This was correctly pointed out by the COREMA and “under article 16 of the General Law on the Environment, COREMA had the obligation to reject it.”¹¹⁹
149. From these allegations, three key issues emerge: the significance of the November 6, 1996 meeting, the scope of the approval by the FIC, and the conduct of the Claimants as diligent investors. The Tribunal will now consider them in that sequence.

(iii) The November 6, 1996 meeting

150. The Respondent has attributed particular importance to the meeting allegedly held with “Malaysian businessmen” on November 6, 1996 in order to show the reckless behavior of the Claimants in proceeding to invest notwithstanding warnings of the obstacles that their investment would face. The Claimants contest that such meeting ever took place. As proof of that meeting, there is the word “Malaysia” in the calendar of Minister Hermosilla and reference made to the meeting in two documents of the Respondent dated two years later. There are no briefings prior to the meeting, nor written record of what was discussed, nor any contemporaneous written record of who attended the meeting. Neither Minister Hermosilla nor SEREMI González could determine whether any of the MTD representatives who attended the hearings in Washington were one of the “Malaysian businessmen” that allegedly attended the November 6, 1996 meeting.
151. This notwithstanding, the Respondent has described in considerable detail the terms of the exchanges that took place at such meeting in the Counter-Memorial and the Rejoinder and so did Messrs. Hermosilla and González in their testimony. The Malaysian representatives of the Claimants, except for Mr. Lee, have presented their passports as proof that none of them was in Chile at the time. Mr. Lee lost his passport, but he was present at the Washington hearings when Messrs. Hermosilla and González testified.

¹¹⁹ Ibid., para. 105.

152. Given the factual controversy surrounding this meeting, the Tribunal will analyze the situation with and without the meeting and to what extent the conduct of the parties is consequent with the statements allegedly made by Chilean officials and the Claimants' representatives.
153. The alleged meeting of November 6, 1996 is one of many meetings that took place before and after that date between representatives of the Claimants and Chilean Government officials. Representatives of the Claimants met with Mr. Morales of the FIC on May 16 and with Mr. Guerra of SERVIU on May 17, 1996. The timing of the November 6 meeting coincides with the resumption during that month of negotiations of MTD, through the firm Vial & Palma, with Mr. Fontaine, which led to the signature of the Promissory Contract on November 21, 1996. Hence, the importance attributed to the meeting by the Respondent to show that the Claimants had been warned about the existing difficulties to build the Project by Chilean officials at the highest level and at an early stage of the Claimants' decision-making on the Project.
154. According to the Counter-Memorial, "Upon hearing that MTD had selected Pirque as the location for its Project, SEREMI González informed Minister Hermosilla that the Project was not feasible. Minister Hermosilla conveyed this point to MTD, explaining that the PMRS, which categorically forbade urban development in Pirque, posed a serious impediment to the Project. He added that the PMRS could not be circumvented and that the only way to develop a real estate project in Pirque was by modifying the PMRS."¹²⁰ Allegedly, the process for modifying the PMRS was explained to the Claimants at their own request. SEREMI González, "the official with sole authority to initiate the modification process,"¹²¹ explained that "because the Project was inconsistent with the goals of the PMRS, one of which was to promote urban densification, the office of the SEREMI would not be able to sponsor the project before CORE."¹²² Mr. Hermosilla also suggested that "MTD find an alternative location for its Project."¹²³
155. This record of the meeting provided by the Respondent will be considered by the Tribunal in the context of the subsequent conduct of the parties.

¹²⁰ Counter-Memorial, para. 25.

¹²¹ *Ibid.*, para. 27.

¹²² *Ibid.*

¹²³ *Ibid.*

156. The FIC approved the first request of the Claimants for foreign investment related to the Project on March 3, 1997. On March 18, 1997, the corresponding Foreign Investment Contract was signed. A second request for investment was approved by the FIC on April 8, 1997 and another Foreign Investment Contract signed on May 13, 1997. On September 29, 1997, the President of Chile at a state dinner in honor of the Prime Minister of Malaysia praised the Project as innovative and "a tangible demonstration that people may fully profit from the favorable conditions that the governments are creating". Then the next day the office of the President of Chile sent a public statement in similar terms to be read at the ceremony to inaugurate the Project in Pirque after canceling his appearance because of a meeting with the President of Brazil.
157. The Respondent alleges that the statement of the President intended to be read at the inauguration had been officially withdrawn. There is no evidence of such withdrawal nor of any disclaimer to this effect after the statement was actually read at the inauguration. It is also claimed now by the Respondent that the President cancelled his attendance at the inauguration at the request of the new Minister of MINVU, Mr. Henríquez, and that the actual reason for the cancellation of the President's attendance was that: "Having learned of the difficulties that MTD's project faced and of the warnings that his predecessor had imparted to MTD, Minister Henríquez believed that President Frei's presence at the ceremony could be misinterpreted, and therefore urged the President not to attend."¹²⁴ It is undisputed that the Claimants were not informed at the time of the real reason for the cancellation of the President's appearance or the alleged withdrawal of his statement. They have apparently learned about it during the course of these proceedings. Given that President Frei spoke at the state dinner only the evening before, there was no reason to suspect that there were other reasons for the cancellation of the President's appearance. The Respondent does not seem to have acted in accordance with the allegedly clear warnings given to representatives of the Claimants on November 6, 1996.
158. The Claimants' own actions contradict also the allegation of what was said at the November 6 meeting assuming that it took place. Irrespective of the inconsequent business decisions taken notwith-

¹²⁴ Counter-Memorial, para. 59.

standing the alleged clear warnings of the Respondent, a matter to which the Tribunal will turn later, the Claimants, in their dealings with Mr. Fontaine, sought protection in respect of the approval of their investment by the FIC. They conditioned the taking effect of the Promissory Contract to the FIC's approval of the transfer of funds. It would seem reasonable to assume that, if the statements made to them by Minister Hermosilla and SEREMI González had been as clear as alleged, the Claimants would have protected themselves accordingly by looking for another site or canceling the proposed investment altogether. It would have been equally inconsequential for the Claimants to seek the FIC's approval for an investment considered unfeasible by high level officials of the Respondent. The Tribunal will have further to say about the Claimants' diligence.

159. The scope of the approval of the first two investments of the Claimants by the FIC is a key element in the consideration of whether the Respondent fulfilled its obligation to treat the Claimants fairly and equitably and the Tribunal will turn to this question now. At this point, the Tribunal is only concerned with the actual approval of the inflow of funds for the Project and with the fact that Chile entered into the Foreign Investment Contracts with the Claimants. The Tribunal will discuss later the claim that Chile breached the Foreign Investment Contracts and, by operation of the MFN clause, the BIT.

(iv) Significance of the Approval of the FIC

160. The parties disagree on the meaning of the approval of the investment by the FIC under DL 600 and the significance of the absence of the Minister responsible for the sector of the proposed investment from the meeting where the investment was approved. Chile maintains that approval by the FIC does not mean more than an authorization to import funds into the country. The description of the project in the application to the FIC is too brief for it to be significant to the approval of the investment and it would be, in any case, beyond the scope of the FIC's authority to attribute to its approval any other meaning.

161. According to Chile, who attends the meeting of the FIC is not important provided there is a quorum for the meeting and the provisions of DL 600 do not require that the sector Minister concerned be part of the quorum. In fact, according to the Respondent, the practice of the FIC is that the sector Ministers do not attend the FIC meetings except in the case of some sectors, e.g. mining, and that the documents related

to an investment are not distributed to the sector Ministers before a FIC meeting nor is notice of the meeting sent to the non-permanent members of the FIC. In any case, argues Chile, even if the Minister of MINVU had attended, the outcome would have been the same given the limited role that the FIC plays. On the other hand, the Claimants consider the approval of the FIC to be the approval of the investment and of the Project at the described location, and to give them the right to develop the site. They attribute to the absence of the Minister of MINVU from the meeting of the FIC that approved the Project, the subsequent obstacles against which otherwise they would have been alerted.

162. DL 600 confers on the FIC the power to approve on behalf of "the Chilean State the inflow of foreign capital under this Decree-Law and to stipulate the terms and conditions of the corresponding contracts" (Article 12). The FIC members are all at the ministerial level except for the president of the Central Bank (Article 13). Decisions are taken by simple majority and a quorum for a meeting requires only the presence of any three members (Article 14). In order for the FIC to exercise its functions, the Executive Vice-Presidency is responsible, *inter alia*, for the coordination of foreign investments and to carry out and expedite the procedures required by public institutions that must report or grant their authorization prior to the approval of the applications submitted to the FIC (Article 15). The applications require the investor to specify the location of the investment and the requirement is repeated in the non-negotiable standard foreign investment contract. It is this contract that, in terms of DL 600, evidences the authorization of the FIC (Article 3). A change in the location of the investment would require a change in the contract and hence, the approval of the FIC.

163. The Tribunal considers that the ministerial membership of the FIC is by itself proof of the importance that Chile attributes to its function, and it is consequent with the objective to coordinate foreign investment at the highest level of the Ministries concerned. It is also evident from the DL 600 that the FIC is required to carry out a minimum of diligence internally and externally. Approval of a Project in a location would give *prima facie* to an investor the expectation that the project is feasible in that location from a regulatory point of view. The practice whereby the non-permanent member of the FIC is not notified of the FIC meetings and no information is distributed to the Minister concerned prior to the meetings, when followed consistently, may impair seriously the coordination function of the FIC. This is not to say that approval of a project in a particular location entitles the investor to develop that site

without further governmental approval. The Foreign Investment Contracts are clear in that respect and this matter is dealt with separately in this award. What the Tribunal emphasizes here is the inconsistency of action between two arms of the same Government vis-à-vis the same investor even when the legal framework of the country provides for a mechanism to coordinate. This is even more so, if, as affirmed by the Respondent, the presence of the MINVU Minister in the FIC meeting where the investment was approved would not have made a difference.

164. Chile has argued that each organ of the Government has certain responsibilities, that it is not its function to carry out due diligence regarding the legal and technical feasibility of a project for investors, and that this is the investors' responsibility. The Tribunal agrees that it is the responsibility of the investor to assure itself that it is properly advised, particularly when investing abroad in an unfamiliar environment. However, in the case before us, Chile is not a passive party and the coherent action of the various officials through which Chile acts is the responsibility of Chile, not of the investor. Whether the Claimants acted responsibly or diligently in reaching a decision to invest in Chile is another question.
165. The Claimants contacted officials of the Respondent from the very beginning in May 1996. It is only in June 1998, almost two years after the supposed November 6, 1996 meeting, that the SEREMI González informed the Claimants in writing about the policy against changing the zoning of El Principal and modifying the PMRS, and Minister Henríquez rejected the Project. Chile claims that it had no obligation to inform the Claimants and that the Claimants should have found out by themselves what the regulations and policies of the country were. The Tribunal agrees with this statement as a matter of principle, but Chile also has an obligation to act coherently and apply its policies consistently, independently of how diligent an investor is. Under international law (the law that this Tribunal has to apply to a dispute under the BIT), the State of Chile needs to be considered by the Tribunal as a unit.
166. The Tribunal is satisfied, based on the evidence presented to it, that approval of an investment by the FIC for a project that is against the urban policy of the Government is a breach of the obligation to treat an investor fairly and equitably. In this respect, whether the meeting of November 6, 1996 took place or not does not affect the outcome of

these considerations. In fact, if it did take place, it is even more inexplicable that the FIC would approve the investment and the first two Foreign Investment Contracts would be signed. Minister Herмосilla and the FIC were different channels of communication of the Respondent with outside parties, but, for purposes of the obligations of Chile under the BIT, they represented Chile as a unit, as a monolith, to use the Respondent's term.

167. This conclusion of the Tribunal does not mean that Chile is responsible for the consequences of unwise business decisions or for the lack of diligence of the investor. Its responsibility is limited to the consequences of its own actions to the extent they breached the obligation to treat the Claimants fairly and equitably. The Tribunal will now address the alleged Claimants' lack of diligence and of prudent business judgment raised by the Respondent.

(v) The issue of the Claimants' diligence

168. The lack of diligence of the Claimants alleged by the Respondent rests on the trust placed in Mr. Fontaine, the lack of adequate professional advice in the urban sector and the acceptance of an exorbitant land valuation at the time they made the investment.

169. The Respondent contends that the Claimants decided to invest in Chile without conducting meaningful due diligence. They relied on self-serving statements of Mr. Fontaine that the land was unproductive and could be readily re-zoned, "particularly if it would attract foreign investment."¹²⁵ If the Claimants had made "even the most rudimentary of inquiries" they would have learned that Pirque actually possesses high-quality agricultural land and plays an important role in the environmental health of the Metropolitan Region. They would have also learned about the PMRS adopted just two years earlier which "expressly prohibited urban development in Pirque and designated it as an exclusive silvoagropecuaria zone."¹²⁶ The Respondent finds it striking that the two-man team of the Claimants arrived at its favorable recommendation to invest in Chile after only four days in the country, particularly when it is considered that the investment in El Principal "appears to have been MTD's first venture outside of Southeast Asia."¹²⁷

¹²⁵ *Ibid.*, para. 8.

¹²⁶ *Ibid.*, para. 9.

¹²⁷ *Ibid.*, paras. 9 and 11.

170. The Respondent contrasts the practices of the Claimants with those followed by diligent foreign investors. Normally, “foreign investors routinely seek contractual protections against losses arising from difficulties in obtaining governmental authorizations by incorporating related representations and warranties, covenants, conditions precedent or subsequent, or other protective provisions”.¹²⁸ The Claimants proceeded to enter into the Promissory Contract “despite a cursory understanding of Chile’s foreign investment laws, a flawed land appraisal, warnings from government officials regarding land use issues, and apparently no additional professional advice regarding the risks inherent to its proposed development of a satellite city on land restricted to urban development.”¹²⁹
171. The Respondent draws attention to other arbitral awards not mentioned in Judge Schwebel’s opinion. The Respondent refers to the need of an arbitral tribunal to take into account, quoting from the award in *American Manufacturing & Trading v. Republic of Zaire*, the “existing conditions of the [host] country”¹³⁰ when applying the standards of a bilateral investment treaty: “In Chile, zoning modifications, such as those required for the PMRS, involve a lengthy administrative process – a process that Chilean Government officials explained to MTD at length.”¹³¹ The Respondent also refers to *Azinian*¹³² to emphasize that the Claimants, like the claimants in that case, were “alien to the host State’s business environment, had not secured the resources and services needed to implement the Project, and had not commissioned “any feasibility study worth the name.”¹³³
172. The Respondent emphasizes that the Claimants accepted as true the representations made by Mr. Fontaine that the land use restrictions on the Fundo El Principal could be modified and did not carry any further investigation to verify their validity.¹³⁴ They also accepted the valuation of the land done by Banco Sud Americano on the assumption that the land would be re-zoned for urban use and without specific identification of the 600 hectare plot that the Claimants were interested in buying.¹³⁵

¹²⁸ *Ibid.*, para. 29.

¹²⁹ *Ibid.*

¹³⁰ ICSID Case No. ARB/93/1, 36 I.L.M. 1531, at 1553 (1997).

¹³¹ Counter-Memorial, para. 109.

¹³² *Robert Azinian et al. v. The United Mexican States*, ICSID (AF) Case N. ARB (AF)97/2, ICSID REV. –Foreign INV. L.J. 538 (1999).

¹³³ Counter-Memorial, para. 111.

¹³⁴ Rejoinder, para. 14.

¹³⁵ *Ibid.*, paras. 24-25.

173. The Respondent criticizes the assumptions underlying the valuation of Mr. Fontaine's land done by Banco Sud Americano. In the first place, the valuation ignored the limitations imposed by the PMRS and "the appraisers assumed, without any analysis or explanation, that the land in El Principal would be re-zoned for urban use." According to the Respondent, had the Claimants made "even the most primitive attempt to conduct reasonable due diligence and consult with any urban planner, environmental expert, architect, or, at the very least, a lawyer experienced in real estate development issues, the erroneous nature of the appraisal's re-zoning assumption would have been imparted to MTD's representatives."¹³⁶
174. The appraisal also assumed that the road known as the Paseo Pie Andino would be built within five years, and "improperly suggested that the mere proposal of the unrealized Project raised the value of the land and erroneously assumed that the land could be divided into "parcelas de agrado" of 0.5 hectares." In fact, after the passage of the PMRS, the minimum subdivision possible was four hectares.¹³⁷
175. The Claimants decided on the value of the land only on the basis of that appraisal without considering the specific value of the 600 hectares that would be the basis of the initial investment, or how the value of the land was affected by the existing road system, or applicable zoning restrictions. According to the Respondent, if a more "exact-ing land appraisal" had been conducted, the Claimants, would have discovered that the value of the 600-hectare area proposed for development under the Project was between US\$ 4.1 and US\$ 4.6 million.¹³⁸
176. It is clear from the record that no specialist in urban development was contacted by the Claimants until the deal had been closed. The firms contacted thereafter, to the extent that there is a contemporary written record, do not seem to have been as clear as they are now in their testimony about the difficulty of changing the zoning. The only thing that emerges with certainty is that the Claimants were in a hurry to start the Project.
177. The Claimants apparently did not appreciate the fact that Mr. Fontaine may have had a conflict of interest with the Claimants for

¹³⁶ Counter-Memorial, para. 20.

¹³⁷ Ibid., para. 22.

¹³⁸ Ibid., para. 23.

purposes of developing El Principal. He played lightly to them the significance of the zoning changes and they seem to have accepted at first hand Mr. Fontaine's judgment. The price paid for the land was based on the Project going ahead and it was paid up-front without any link to the progress of the Project.

178. The BITs are not an insurance against business risk¹³⁹ and the Tribunal considers that the Claimants should bear the consequences of their own actions as experienced businessmen. Their choice of partner, the acceptance of a land valuation based on future assumptions without protecting themselves contractually in case the assumptions would not materialize, including the issuance of the required development permits, are risks that the Claimants took irrespective of Chile's actions.

2. Breach of the BIT by Breach of the Foreign Investment Contracts

179. The Claimants argue that the Respondent's failure to observe its contractual obligations, "constitutes a breach of its treaty obligation to observe the contractual obligations it undertook regarding MTD's investment. Because the breach at issue is a breach of an international obligation, the matter is governed, first and foremost, by international law. To the extent that the issue turns on the scope of the obligations arising out of the Foreign Investment Contracts, the Contract must be interpreted in accordance with its plain language and the general principles of contract law, in keeping with the internationalization of contract obligations [...] This conclusion is particularly relevant in this case, because the Foreign Investment Contracts do not contain a choice-of-law clause."¹⁴⁰

180. The Claimants emphasize the fact that the Foreign Investment Contracts were contracts of adhesion because their terms were not negotiable.¹⁴¹ The location of the Project in Pirque was "a fundamental assumption of the bargain between MTD and the State of Chile. MTD had a right to that location, and the State of Chile had a correlative

¹³⁹ "the Tribunal must emphasize that Bilateral Investment Treaties are not insurance policies against bad business judgments." *Emilio Agustín Maffezini v. The Kingdom of Spain*, ICSID Case No. ARB/97/7 para. 69.

¹⁴⁰ Reply, para. 104.

¹⁴¹ Memorial, para. 109.

obligation to take such steps as might be necessary to permit the use of that location for the development of the Project. The State of Chile breached that obligation by blocking the development of the Project on the ground that it was to be located in the very place designated in the Contracts.¹⁴² The refusal of the Respondent to re-zone the area concerned "frustrated the rights and legitimate expectations of MTD under the Foreign Investment Contracts and treated the entire Foreign Investment Application procedure as an empty formality."¹⁴³

181. The Claimants also argue that the approval of the investment in Pirque has the effect of approving the location of the Project and that the reference in clause Four of the Foreign Investment Contracts to "other" authorizations refers to authorizations other than those granted in the Foreign Investment Contracts themselves: "it would be the height of bad faith to construe Clause Fourth [sic] as giving the State of Chile the power to destroy the basis of the bargain by erasing, after the fact, the very object of the investment as specified in the Contracts."¹⁴⁴
182. As regards the obligation to grant the necessary permits for an authorized investment, the Claimants affirm that "the Respondent is obligated under the Treaty to grant the necessary permits to the extent that doing so is consistent with its laws and regulations. The Respondent cannot seriously contend that modifying the PMRS to permit large-scale urban development project in Pirque would have been inconsistent with Chilean laws and regulations, for that is precisely what the Respondent is trying to do, on a far larger scale, through Modification No. 48."¹⁴⁵
183. Chile argues that, even if Article 3(1) of the BIT between Chile and Denmark were applicable, it has not been proven by the Claimants that Chile has violated its obligations under that provision and "under international law, the violation of a contract does not suppose an ipso facto violation of an international treaty."¹⁴⁶

¹⁴² Ibid., para. 110.

¹⁴³ Ibid.

¹⁴⁴ Ibid., para. 111.

¹⁴⁵ Reply, para. 117.

¹⁴⁶ Rejoinder, para. 126.

184. Chile considers that it has complied with its obligations under the Foreign Investment Contracts and that the mere mention of El Principal in the Foreign Investment Contracts did not grant the Claimants an unfettered right to develop the Project in that location. The authorization granted by the FIC under DL 600 is only an authorization to transfer capital and it is without prejudice and independent from other authorizations that may be required under Chilean law. Foreign investors have no right to a preferential treatment vis-à-vis local investors: “Just as a domestic investor cannot obtain a waiver of the PMRS by executive fiat, neither could MTD.”¹⁴⁷
185. Based on statements made by Chile in the Counter-Memorial, the Claimants point out that the Respondent refused “for reasons of ‘inconvenience’” even “to consider taking the administrative actions necessary to permit urban development on the piece of land designated in the Contracts, a result that was entirely in its power and discretion to achieve [...] To this it may now be added that, under the Respondent’s own version of the facts, the State of Chile entered into Foreign Investment Contracts with the intent that it would not allow the Project to be built in Pirque.”¹⁴⁸
186. The Claimants contest that the scope of the Foreign Investment Contracts is governed by Chilean law and that under that law the FIC did not have “the capacity or authority to approve the nature and location of the investment project”.¹⁴⁹ The Claimants state that “Under basic principles of international law, the State of Chile may not evade its international responsibility by invoking any alleged insufficiency in the authority of the organ through which it acted.”¹⁵⁰ The Claimants also contest the argument that DL 600 guarantees treatment as a national investor and that they would have received better treatment if authorization of the investment and the Foreign Investment Contract would have given them the right to the modification of the PMRS. The Claimants argue that, under the BIT, they are “entitled to certain standards of treatment even if the State of Chile chooses not to extend the same treatment to its own national investors [...] [L]ocal investors are not eligible to enter into foreign investment contracts and hence can-

¹⁴⁷ Counter-Memorial, para. 124.

¹⁴⁸ Reply, para. 105.

¹⁴⁹ *Ibid.*, para. 107.

¹⁵⁰ *Ibid.*, para. 108.

not receive any of the special guarantees or advantages that DL 600 authorizes [...] [T]he principle of non-discrimination under Article 9 of DL 600 protects foreign investors from worse treatment than that accorded to national investors; it does not prevent them from receiving the benefits provided in the foreign investment contracts.¹⁵¹

187. The Tribunal considers the legal basis of the claim valid based on the wide scope of the MFN clause in the BIT, as already discussed. The Tribunal notes the statement of the Respondent that under international law the breach of a contractual obligation is not *ipso facto* a breach of a treaty. Under the BIT, by way of the MFN clause, this is what the parties had agreed. The Tribunal has to apply the BIT. The breach of the BIT is governed by international law. However, to establish the facts of the breach, it will be necessary to consider the contractual obligations undertaken by the Respondent and the Claimants and what their scope was under Chilean law.

188. The Tribunal has found that Chile treated unfairly and inequitably the Claimants by authorizing an investment that could not take place for reasons of its urban policy. The Claimants have based their arguments on the fact that "the location of the Project was a fundamental assumption of the bargain between MTD and the State of Chile. MTD had a right to that location, and the State of Chile had a correlative obligation to take such steps as might be necessary to permit the use of that location for the development of the Project."¹⁵² The Tribunal accepts that the authorization to invest in Chile is not a blanket authorization but only the initiation of a process to obtain the necessary permits and approvals from the various agencies and departments of the Government. It also accepts that the Government has to proceed in accordance with its own laws and policies in awarding such permits and approvals. Clause Four of the Foreign Investment Contracts would be meaningless if it were otherwise. Therefore, the Tribunal finds that Chile did not breach the BIT on account of breach of the Foreign Investment Contracts.

189. As already discussed under fair and equitable treatment, what is unacceptable for the Tribunal is that an investment would be approved for a particular location specified in the application and the subse-

¹⁵¹ *Ibid.*, para. 109.

¹⁵² Memorial, para. 110.

quent contract when the objective of the investment is against the policy of the Government. Even accepting the limited significance of the Foreign Investment Contracts for purposes of other permits and approvals that may be required, they should be at least in themselves an indication that, from the Government's point of view, the Project is not against Government policy.

3. Unreasonable and Discriminatory Measures

190. The argument of the Claimants regarding unreasonable and discriminatory measures is based on Article 3(3) of the Croatia BIT. This Article provides: "Each Contracting Party shall protect within its territory investments made in accordance with its laws and regulations by investors of the other Contracting Party and shall not impair by unreasonable or discriminatory measures the management, maintenance, use, enjoyment, extension, sale and liquidation of such investments."
191. The Claimants allege that the unfair and inequitable measures described earlier are also unreasonable and that the Respondent's "refusal to re-zone the El Principal Estate in Pirque to permit construction of the Project is discriminatory because the State of Chile has permitted construction of other large-scale real-estate projects in the Chacabuco area, north of Santiago."¹⁵³
192. Furthermore, the Claimants maintain that the acceptance and approval of an environmental impact declaration (DIA) by COREMA in support of Modification No. 48 "illustrates the State of Chile's unreasonable and discriminatory treatment of the EIS submitted by the Municipality of Pirque in support of the proposed Sectional Plan."¹⁵⁴
193. According to the Respondent, none of the modifications to the PMRS referred to by the Claimants were achieved through sectional plans and followed the standard PMRS modification procedure. Furthermore, Modification No. 48 "will make the completion of large real estate projects more -- rather than less -- difficult in the Metropolitan Region of Santiago."¹⁵⁵

¹⁵³ Memorial, para. 115.

¹⁵⁴ Reply, para. 115.

¹⁵⁵ Rejoinder, paras. 5-7.

194. The Respondent finds also inadmissible the comparison of the EIS with the DIA prepared for Modification No. 48. An EIS is only required by the existing environmental regulation when projects entail significant environmental impacts.¹⁵⁶ In contrast to the environmental consequences of the Project, "Modification No. 48 would not generate direct impacts on the environment, it would set out conditions for the development of future Urban Conditional Development Projects". Projects presented under Modification No. 48 will still need an EIS and satisfy "a more demanding environmental evaluation than that applied to the Sectional Plan for Pirque."¹⁵⁷
195. The Respondent explains the justification given by COREMA to reject the EIS. First of all, the COREMA followed the prescribed procedure. It accepted the EIS for review within five days of receipt because prima facie there were no evident administrative errors. The next step was to consult with other Government agencies with jurisdiction over environmental matters. This is what COREMA did in the case of MTD's EIS. COREMA issued a negative evaluation regarding the substance of the EIS only after "consulting with other agencies about the environmental impacts of MTD's Project."¹⁵⁸ The Project was inconsistent with the PMRS, which for purposes of evaluating an environmental impact study is considered an environmental regulation, and, hence, the Project failed to comply with environmental regulations. The EIS also failed to address identified environmental obstacles and was extremely vague.¹⁵⁹
196. To a certain extent, this claim has been considered by the Tribunal as part of the fair and equitable treatment. The approval of an investment against the Government urban policy can be equally considered unreasonable. On the other hand, the changes of the PMRS related to Chacabuco or more recently Modification 48, as explained by the Respondent, do not dispense with specific changes of the PMRS when the land is zoned of "silvoagropecuario interest". Therefore, there is no basis for considering the modifications made to PMRS as discriminatory. The Tribunal is also satisfied by the explanation regarding the rejection of the EIS by COREMA.

¹⁵⁶ Ibid., para. 108.

¹⁵⁷ Ibid., paras. 110-111.

¹⁵⁸ Counter-Memorial, para. 153.

¹⁵⁹ Ibid., para. 154.

4. Failure to Grant Necessary Permits

197. This claim is based on the Croatia BIT by way of the MFN clause of the BIT. Article 3(2) of the Croatia BIT reads as follows: "When a Contracting Party has admitted an investment in its territory, it shall grant the necessary permits in accordance with its laws and regulations."
198. The Claimants consider that this "clause obligates the State, once the investment is approved, to grant the necessary permits to the investor, in accordance with the country's laws and regulations."¹⁶⁰ And further, "At the very minimum, this provision obligates the [S]tate of Chile to grant to MTD such permits as may be necessary to cover those aspects of the investment that were specifically considered by the [S]tate admitting the investment. Accordingly, if a formal re-zoning permit required for the development of the Project and if that permit can only take the form of an amendment of the PMRS, the [S]tate of Chile is required by the quoted provision [Article 3(2)] to grant such permit by adopting such an amendment to the PMRS."¹⁶¹
199. While the Claimants realize that permits must be granted in accordance with the laws and regulations of the State and that the PMRS is one such regulation, they consider that, to use such reasoning, misses the point: "It is the modification of the PMRS – which is entirely within the State of Chile's discretion – that is at issue here. There is nothing in the State of Chile's laws or regulations that would prevent the [S]tate of Chile from modifying the PMRS to allow the Project to be fulfilled [...] The State of Chile refused to make such modification not because it lacked the power to do so, but because it chose not to do it for reasons of policy. Any interpretation that allowed the State to do just that would turn the treaty obligation to grant necessary permits for an approved investment into a dead letter."¹⁶² On the other hand, when Chile had the will to modify the PMRS, it found a way to justify it.
200. The Respondent dismisses the Claimants' statement that no legal norm prevented Chile from modifying the PMRS to allow the carrying out of the Project.¹⁶³ If the argument presented by the Claimants were

¹⁶⁰ Memorial, para. 118.

¹⁶¹ *Ibid.*, para. 119.

¹⁶² *Ibid.*, para. 120.

¹⁶³ Counter-Memorial, para. 143.

correct, it would “render meaningless that clause of the Chile-Croatia Treaty and the Foreign Investment Contracts – clauses found in countless other bilateral investment treaties and foreign investment contract worldwide – requiring foreign investors to comply with domestic laws and regulations.”¹⁶⁴ Under such theory, “a foreign investor would be able [sic] circumvent the PMRS modification process, while domestic investors could not – a result that would contravene the non-discrimination provision of DL 600.”¹⁶⁵

201. As to the modifications made to the PMRS, the Respondent affirms that they reflect minor changes that underscore the firm commitment of Chile to respect this instrument. The most significant modification of land use involved re-designating land at La Platina from Ecological Preservation to a Complementary Green Area to allow the construction of a zoological park. The modification introduced by Resolution 39 in 1997 incorporated new lands in the PMRS rather than changed the use of land already in the PMRS, the municipalities of Colina, Lampa and Til-Til in the Province of Chacabuco.

Furthermore, “The incorporation of Chacabuco [...] was wholly consistent with the original purpose of the PMRS, which was to allow urban development in Santiago’s north, where Chacabuco is located, rather than in the southeast, where Pirque is located.”¹⁶⁶ Chile does not deny that it can change the PMRS but asserts that it is not obliged to do so, “[t]he simple fact that the PMRS could be modified did not mean that MTD was entitled to its proposed modification.”¹⁶⁷

202. Chile points out that it is an unexplained indictment of the Claimants that Chile adhered to its urban planning policy: Chile – like any other sovereign State - has the power to establish its policies. In fact, it is a Government’s *raison d’être* to enact laws that reflect policy choices. MTD was aware of Chile’s policy before it purchased El Principal and has “no credibility to decry that policy now and argue –without support – that Chile was somehow automatically obligated as a matter of law to change a policy benefiting the millions of residents of [sic] Metropolitan Region.”¹⁶⁸

¹⁶⁴ Ibid., para. 144.

¹⁶⁵ Ibid., para. 145.

¹⁶⁶ Ibid., paras. 147-149.

¹⁶⁷ Ibid., para. 150.

¹⁶⁸ Ibid., para. 151.

203. The Respondent contests the argument that it failed to give the necessary permits and hence it violated Article 3(2) of the Croatia BIT: “Even assuming that article 3(2) [...] is applicable to the present case, Chile has not violated that obligation. Chile has demonstrated that the actions of its officials were not carried for [sic] for extra-legal reasons such as the particular preferences or whims of government officials.”¹⁶⁹ The permits needed for the Project, as found by the tribunal in *TECMED* in interpreting a similar provision, need to be granted in accordance with the laws of the State concerned,¹⁷⁰ and there is no merit to the contention of the Claimants that, “Because the breach at issue is a breach of an international obligation, the matter is governed, first and foremost, by international law.”¹⁷¹

204. The Tribunal considers the legal basis of the claim valid based on the wide scope of the MFN clause in the BIT, as already discussed. The Tribunal disagrees with the Respondent’s statement that there is no merit to the contention of the Claimants that, if there is a breach of an international obligation, “the matter is governed, first and foremost, by international law”. The breach of an international obligation will need, by definition, to be judged in terms of international law. To establish the facts of the breach, it may be necessary to take into account municipal law. In the instant case, the Tribunal will need to establish first whether the Respondent’s failure to modify the PMRS to the benefit of the Claimants was in accordance with its own laws.¹⁷²

205. The Tribunal draws a distinction between permits to be granted in accordance with the laws and regulations of the country concerned and those actions that require a change of said laws and regulations. To the extent that the application for a permit meets the requirements of the law, then, in accordance with the BIT and Article 3(2) of the Croatia BIT, the investor should be granted such permit. On the other hand, said provision does not entitle an investor to a change of the normative framework of the country where it invests. All that an investor may expect is that the law be applied.

¹⁶⁹ Rejoinder, para. 130

¹⁷⁰ *Environmental Techniques TECMED S.A. v. the Mexican United States*, ICSID Case No. ARB(AF)/00/2, Decision of May 29, 2003.

¹⁷¹ Rejoinder, paras. 131-132.

¹⁷² Memorial, para. 127.

206. As explained by the Respondent, the carrying out of the investment would have required a change in the norms that regulate the urban sector in Chile. The PMRS forms part of this normative framework, as repeatedly stated by the Respondent. Laws and regulations may be changed by a country but it is not an entitlement that can be based in Article 3(2) of the Croatia BIT. This clause is an assurance to the investor that the laws will be applied, and to the State a confirmation that its obligation under that article is confined to grant the permits in accordance with its own laws. The Tribunal concludes that the Respondent did not breach the BIT by not changing the PMRS as required for the Project to proceed.

5. Expropriation

207. The Claimants affirm that MTD made its investment “after receiving authorization to do so from the State; was forced to halt the execution of its project because it was informed that it lacked a necessary permit; attempted to obtain such permit but the attempts were rebuffed; as a result it was unable to continue with the Project and essentially lost the value of its investment. In these circumstances, the treatment suffered by the investor constitutes an indirect expropriation.”¹⁷³

208. The Claimants argue that their investment has been expropriated by the Respondent in breach of Article 4 of the BIT. The Claimants allege indirect expropriation resulting from actions and failure to act by the Respondent, irrespective of whether “the State intended or not to cause an indirect expropriation.”¹⁷⁴ In making this argument, the Claimants rely on definitions of indirect expropriation by arbitral tribunals in the cases of *Metalclad Corp. v. United Mexican States*¹⁷⁴ and *CME Czech Republic B.V. (The Netherlands) v. Czech Republic*¹⁷⁵ and consider that

¹⁷³ *Ibid.*, para. 124.

¹⁷⁴ “covert or incidental interference with the use of property which has the effect of depriving the owner, in whole or in significant part, of the use or reasonably-to-be-expected economic benefit of property even if not necessarily to the obvious benefit of the host state.” (*Metalclad Corp. v. United Mexican States*, ICSID Case No. ARB(AF)/97/1, Award, 30 August 2000, 103, 16 ICSID Rev.-FILJ 165 (2001)).

¹⁷⁵ “De facto expropriation or indirect expropriation, i.e. measures that do not involve an overt taking but that effectively neutralize the benefit of property of the foreign owner, are subject to expropriation claims. This is undisputed under international law.” (*CME Czech Republic B.V. (The Netherlands) v. Czech Republic*, Partial Award, 13 September 2001, 604 available at <http://www.cnts.cz/doc10/en/pdf/cme-cr-eng.pdf> (citing Sacerdoti, J., *Bilateral Treaties and Multilateral Instruments on Investment Protection*, 1997 *Recueil des Cours* 382 (1998)).

the facts of their case are analogous to *Metalclad* and *Biloune*¹⁷⁶: in these two cases “arbitral tribunals have found that the failure or refusal of the host State to provide a necessary permit to the investor constituted an indirect expropriation.”¹⁷⁷

209. Chile is “bewildered” by this claim because “MTD continues to enjoy full ownership of its interest in EPSA, and still has the right to seek zoning and other permits and approvals required under Chilean law [...] MTD remains able to explore investment opportunities in Pirque and has the right to seek a modification of the PMRS, and other urban planning regulations.”¹⁷⁸ The Respondent draws attention to the award in *Feldman v. Mexico* which found that “not all governmental regulatory activity that makes it difficult or impossible for an investor to carry out a particular business, change in the law or change in the application of existing laws that makes it uneconomical to continue a particular business, is an expropriation.”¹⁷⁹ The instant case does not concern “the change of an existing law or the application thereof. To the contrary, this case merely involves the Republic of Chile’s consistent application of its policies, regulations and laws.”¹⁸⁰

210. In the same vein, the Respondent contests the reliance of the Claimants on *Biloune*. There the arbitral tribunal held that “the combination of measures used against the investor constituted constructive expropriation”. In the case before this Tribunal, the Respondent argues that “*Biloune* simply does not support the theory that the denial of a permit alone or, as in the case of MTD, the absence of a change in zoning, constitutes a constructive expropriation [...] contrary to the facts in *Biloune*, Chilean Government officials never assured MTD that a change in zoning would be unnecessary or that MTD could proceed with its Project without modifying the PMRS.”¹⁸¹

211. The Claimants respond to Chile’s bewilderment about their expropriation claim by pointing out that, by definition, an indirect expropriation claim “takes place when the State deprives the investor of the use

¹⁷⁶ *Biloune and Marine Drive Complex Ltd v. Ghana Investments Centre and the Government of Ghana*, 95 I.L.R. 183 (1994).

¹⁷⁷ Memorial, para. 126.

¹⁷⁸ Counter-Memorial, para. 114 and Rejoinder, para. 10.

¹⁷⁹ Counter-Memorial, para. 115.

¹⁸⁰ *Ibid.*

¹⁸¹ *Ibid.*, para. 118.

and benefit of the investment without formally depriving the investor of title.”¹⁸²

212. The Claimants also contest the interpretation given by the Respondent to Metalclad and Biloune: “MTD received authorization from the [S]tate of Chile to make an investment to develop a project in Pirque, but was denied the ability to proceed with the development because the State denied a key permit [...] Biloune is not a case about the number of acts that a State must undertake against an investment [...] It is the overall impact of the state action on the investment that determines the existence of indirect expropriation. In this case, the refusal of the State of Chile to provide the key permit to allow the development of the Project in Pirque resulted in a complete frustration of the Project and a complete loss of in [sic] the value of MTD’s investment.”¹⁸³

213. The Respondent contests again in the Rejoinder the arguments presented by the Claimants on expropriation and insists on the irrelevance of the cases relied on by the Claimants (Middle East Cement, TECMED) because no license was revoked or permit renewal denied: “MTD has not identified any property right that has been seized by Chile. Moreover, MTD has admitted that it has been judicially compelled to accept an offer ‘approximately equivalent to US \$10.069.206’ for its shares in EPSA, which hardly supports their claim that these are essentially without value.”¹⁸⁴

214. As already stated, the Tribunal agrees with the argument of the Respondent that an investor does not have a right to a modification of the laws of the host country. As argued by the Respondent, “every State has the power to amend any of its laws. The mere fact that Chile can change the PMRS does not mean, however, that Chile is obligated to do so.”¹⁸⁵ The issue in this case is not of expropriation but unfair treatment by the State when it approved an investment against the policy of the State itself. The investor did not have the right to the amendment of the PMRS. It is not a permit that has been denied, but a change in a regulation. It was the policy of the Respondent and its right not to change it. For the same reason, it was unfair to admit the investment in the country in the first place.

¹⁸² Reply, para. 123.

¹⁸³ Reply, footnote 35 at pages 54-55.

¹⁸⁴ Rejoinder, para. 142.

¹⁸⁵ Counter-Memorial, para. 144.

V. DAMAGES

215. The Claimants seek “full compensation for the damage they have sustained as a consequence of the State of Chile’s treaty violations, so that the Claimants are restored to the position they would be in had those treaty violations not occurred.”¹⁸⁶ This entails the recovery of : “(i) the full cost of their investment (minus any remaining value), (ii) pre-award compound interest at a commercially reasonable rate, and (iii) the costs and expenses associated with this proceeding.”¹⁸⁷
216. Chile contends that the Claimants have failed to prove the alleged losses and their causal link to the alleged breaches. Chile points out several fundamental flaws in their claim. First, they failed to mitigate their losses by entering into the Promissory Contract notwithstanding Minister Hermosilla’s warning in the November 6, 1996 meeting that their project faced serious regulatory obstacles and without protecting themselves against the risks posed by these obstacles. The failure of the Claimants to mitigate losses is a cause of loss not attributable to the Republic of Chile.¹⁸⁸
217. Chile affirms that preparatory expenses till March 18, 1997 (date of signature of the first Foreign Investment Contract) should not be recoverable. As regards the other claimed losses, almost 80% occurred by transferring the funds to Chile between March 19, 1997 and the meeting held with Minister Hermosilla on May 20, 1997. During that period, architects, urban planners and governmental officials warned MTD that the Project faced serious difficulties and Mr. Hermosilla repeated his early warning.¹⁸⁹ After May 20, 1997 and until September 25, 1998 when the SEREMI confirmed that the sectional plan could not be used to amend the PMRS, the Claimants spent more than US\$ 1.4 million: “any reasonable investor would have long since developed serious reservations about allocating additional funds to a questionable investment”.¹⁹⁰ Even after September 25, 1998, the Claimants continued to spend more than US\$ 3.2 million on the Project and then declined to take advantage of an opportunity to recover about half their

¹⁸⁶ Memorial, para. 129.

¹⁸⁷ *Ibid.*, para. 130.

¹⁸⁸ Counter-Memorial, para. 165.

¹⁸⁹ *Ibid.*, para. 167.

¹⁹⁰ *Ibid.*, para. 168.

losses when they rejected the offer made by Mr. Fontaine to buy their shares of EPSA on November 24, 2001.¹⁹¹

218. Chile also questions whether the Claimants themselves actually incurred the losses: "Most of the alleged losses – including equity injections, debt servicing, salary payments and various other expenses – are supported by documents relating to MTD Construction or MTD Capital."¹⁹² Chile also finds that the Claimants have failed to substantiate the fate of the amount injected in EPSA or "explain whether the use of those funds constitutes recoverable losses."¹⁹³

219. The Respondent contends that there is no legal basis for the claim of interest or bank guarantee charges related to the loan used to finance the investment. Chile relies on the finding of the tribunal in *Middle East Cement* that "denied costs related to a bank loan taken out by the claimant itself because such costs 'are normal commercial risks for the Claimant. They could only be claimed if, it were shown that they were caused by conduct of the Respondent which was in breach of the BIT'". Chile argues that, "[i]n the present case, Claimants not only did not take out the bank loan, but they also failed to demonstrate how a 'loss' relating to debt service was a direct¹⁹⁴ result of actions or in actions by the Republic of Chile. Claimants fail to show that they incurred any losses related to debt servicing."¹⁹⁵

220. Chile contests the entitlement of Claimants to pre-award interest and maintains that "international law, as a rule, does not allow compound interest", and that, if the Tribunal should find that compound interest is allowed, then it would be "required to take into account the circumstances of the case and not award compound interest."¹⁹⁶

221. As regards the level of the rate of interest, Chile offers the alternative of the average dollar-based "interés corriente"¹⁹⁷ used for bank lending

¹⁹¹ *Ibid.*, para. 169.

¹⁹² *Ibid.*, para. 172.

¹⁹³ *Ibid.*, para. 173 and Rejoinder, para. 153.

¹⁹⁴ *Middle East Cement Shipping and Handling Co. S.A. v. Arab Republic of Egypt*, ICSID CASE No. ARB/99/6, Award, 12 April 2002, paras. 153-154. Quoted in para. 178 of the Counter-Memorial.

¹⁹⁵ *Ibid.*, para. 178.

¹⁹⁶ *Ibid.*, para. 183.

¹⁹⁷ The statutory interest rate applied by courts in Chile.

in Chile or the annual average of the London Inter-Bank Offering Rate ("LIBOR") as more reasonable alternatives to the 8% claimed by the Claimants.¹⁹⁸

222. Chile also argues that it is unclear how expenses under "salaries", "travel expenses" or "other" relate to the Project, and why they should be its responsibility.¹⁹⁹

223. The Respondent considers that the Claimants grossly understate the current value of their investment, particularly the value of the land that according to the valuation of the Claimants' expert is twenty times less than it was at the time they bought it.²⁰⁰

224. The Respondent requests that "the Tribunal order Claimants to bear the expenses incurred by the Republic of Chile in connection with these proceedings, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre, in their entirety."²⁰¹

225. The Claimants note that the Respondent does not dispute the standard of compensation advanced in the Memorial.²⁰² They object to the interpretation given by the Respondent to the Mihaly award on the issue of preparatory costs. In that case, the tribunal found that "certain preparatory expenses incurred by the investor did not give rise to an 'investment' for purposes of ICSID jurisdiction, in circumstances in which the State had made it clear that it did not intend to admit any investment from the claimant until execution of a binding investment contract."²⁰³ In the instant case, there is no dispute that the investment was approved and three Foreign Investment Contracts executed.

226. The Claimants also comment on the issue of mitigation of damages that precisely "because the great majority of MTD's expenses are evidenced by its initial investment in early 1997, it was reasonable and consistent with MTD's obligation to mitigate damages for MTD to continue seeking Government approvals even after it became apparent

¹⁹⁸ Counter-Memorial, para. 184.

¹⁹⁹ *Ibid.*, paras. 179, 180 and 182.

²⁰⁰ *Ibid.*, paras. 185-189.

²⁰¹ *Ibid.*, para. 191.

²⁰² Reply, para. 127.

²⁰³ *Ibid.* para. 130.

that Government officials were opposing the Project."²⁰⁴ As for the failure to accept the buy-out offer of Mr. Fontaine, the Claimants maintain that such offer was illusory because of the terms of payment. In neither of the payment alternatives offered by Mr. Fontaine, the Claimants would be able to "cash out" their holdings in EPSA.²⁰⁵

227. The Claimants reaffirm that MTD Equity and MTD Chile directly made the initial investment with funds supplied to MTD Equity by MTD Capital: "Contrary to the Respondent's assertions, MTD Equity directly incurred all other Project-related expenses, either directly through its owned subsidiary MTD Construction or by incurring legally enforceable obligations to its parent, MTD Capital, to repay expenditures that it made on MTD Equity's behalf."²⁰⁶
228. The Claimants maintain that the debt service and bank guarantee fees claimed as part of the damages are "directly related to the State of Chile's actions destroying the value of MTD's investment and denying MTD any opportunity to recoup its costs and earn a return on capital. Because the Respondent's conduct breached its obligations to MTD under the Treaty, these payments fall squarely into the exception the Middle East Cement tribunal carved out for commercial risk costs that are incurred as a direct result of the State's misconduct."²⁰⁷
229. The Claimants argue that compound interest is not unfair or inappropriate in the circumstances of this case because "the State of Chile cannot escape the fact that it approved MTD's application to invest in a project in Pirque and then frustrated that investment. MTD's possession of the land does not diminish its losses. In contrast to the land owner in the Santa Elena case, which was 'able to use and exploit [the property] to some extent,' MTD has not been able to use its investment in the land held by EPSA for any kind of profitable activity."²⁰⁸
230. As regards the interest rate applicable to pre-award interest, the Claimants recall that the dispute is not governed by Chilean law and therefore the *interés corriente* applied by Chilean courts is not appropriate. Similarly, it is not appropriate to apply LIBOR since they invest

²⁰⁴ *Ibid.*, para. 131.

²⁰⁵ *Ibid.*, paras. 132-135.

²⁰⁶ *Ibid.*, para. 139.

²⁰⁷ *Ibid.*, para. 148.

²⁰⁸ *Ibid.*, para. 157.

their dollars in local Malaysian markets: "At a minimum, MTD should be awarded US\$ 8.782 million in simple interest at its requested rate of 8 percent."²⁰⁹ The Claimants also find no merit to "Chile's argument that the 'constructive value' of MTD's 51 percent share in EPSA should be US\$ 12.8 million, which is based on a highly inflated estimate of land values and disallowance of most of MTD's investment expenses."²¹⁰

231. The Claimants contest the current valuation of the land in the Sánchez Report commissioned by the Respondent. They allege that the Sánchez Report relies on valuation data for land that is not comparable to the land that EPSA owns. In particular, "Sánchez relies on land values that he acknowledges have been affected by speculation about the pending Modification No. 48, which would permit urban development in Pirque."²¹¹ The Claimants argue that "by relying on prices that may reflect speculation about potential opportunities for urban development if Modification No. 48 comes into effect, the Respondent is permissibly trying to capitalize on the effects of its own actions upon market values. Having denied MTD the opportunity to develop its Project on the ground that no urban development may be allowed, it cannot now take actions encouraging a speculative increase in price and thereby reduce MTD's compensation."²¹² The Claimants allege that the "PIX assessment,"²¹³ which values land at US\$ 1.27 million, is a more reliable measure of the impact of the State of Chile's refusal to allow development on the land."²¹⁴

232. The Claimants consider faulty the argument that MTD overpaid for its shares in EPSA based on 1996 land values: "To begin with, MTD did not simply buy land; it bought stock in a joint venture engaged in development of a business. The 1996 Palma Kitzing²¹⁵ value analysis was based on the valuation of the assets to be used in such a venture, not bare land values, and assumed that the Project would be built. Ironically, the Respondent itself submitted (for very different purposes) the 1995 URBE Report, which estimated the value of the land for

²⁰⁹ *Ibid.*, para. 158.

²¹⁰ *Ibid.*, para. 159.

²¹¹ *Ibid.*, para. 162.

²¹² *Ibid.*, para. 163.

²¹³ Commissioned by the Claimants.

²¹⁴ Reply, para. 163.

²¹⁵ Palma Kitzing is the firm contracted by Banco Sud Americano.

investment purposes in 1995-1996 at more than US\$ 25 million.”²¹⁶ In any case, “relying on the Sánchez Report’s post hoc analysis as a basis to assess the value of the land in 1996 would be inconsistent with the practice of other international tribunals, which have rejected appraisals that were not prepared at the time the investor was injured.”²¹⁷

233. As regards Claimants’ costs, the Claimants consider that the Respondent should bear all the costs associated with them because MTD’s large investment losses were caused by the Respondent’s improper actions.²¹⁸

234. In its Rejoinder, the Respondent contests the additional claim of US\$ 3.2 million in interest for “delay resulting from Chile’s request for an extension to file its Counter-Memorial.”²¹⁹ The Respondent argues that “the Tribunal decided [...] that by application of Rules 10 and 12 of the Rules of Arbitration, the ‘suspension’ included all the issues related to the procedure, including time limits and the actions of the Tribunal. For that reason, the sum of US\$ 3.2 million in interest that the Claimants attribute to the State must be rejected, since the procedure was suspended for all the ‘issues related to the procedure.’”²²⁰

235. The Respondent also points out that: (i) the Claimants are entitled to collect damages from their partner, Mr. Fontaine, in the amount offered by him to buy the Claimants’ shares of EPSA; and (ii) the Claimants’ concerns about the economic difficulties and solvency issues of their partner are of no relevance. The sum offered by Mr. Fontaine must be deducted from the amount claimed, as well as interest from November 24, 2001, the date of Mr. Fontaine’s offer.²²¹

236. The Respondent clarifies that, in the URBE report, the land was not appraised and this report only calculated the value of the project minus the costs, including the cost of land, a fact omitted by MTD. In contrast, Mr. Sánchez appraised the 600 hectares in El Principal and not the current value of the project, therefore, a comparison between

²¹⁶ *Ibid.*, para. 164.

²¹⁷ *Ibid.*, para. 166.

²¹⁸ *Ibid.*, para. 169.

²¹⁹ *Ibid.*, para. 147.

²²⁰ *Ibid.*

²²¹ *Ibid.*, paras. 150-151.

the two is “deceptive and inaccurate.”²²² The Respondent also finds that MTD has not been able to substantiate the fate of the US\$ 8.4 million injected into EPSA.²²³

237. The Tribunal will address the following issues regarding damages that emerge from the parties’ allegations:

- 1) Eligible expenses for purposes of calculating damages;
- 2) Damages attributable to business risk;
- 3) Date from which interest should accrue; and
- 4) Applicable rate of interest.

238. The Tribunal first notes that the BIT provides for the standard of compensation applicable to expropriation, “prompt, adequate and effective” (Article 4(c)). It does not provide what this standard should be in the case of compensation for breaches of the BIT on other grounds. The Claimants have proposed the classic standard enounced by the Permanent Court of Justice in the *Factory at Chorzów*: compensation should “wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that had not been committed.”²²⁴ The Respondent has not objected to the application of this standard and no differentiation has been made about the standard of compensation in relation to the grounds on which it is justified. Therefore, the Tribunal will apply the standard of compensation proposed by the Claimants to the extent of the damages awarded.

1. Eligible Expenditures

239. The Tribunal considers that the Claimants have proven that the expenditures related to the Project were made by them or on their behalf and that they were made for purposes of the investment in Chile.

240. The Tribunal considers as eligible for purposes of the calculation of damages the following expenditures:

²²² *Ibid.*, paras. 176-177.

²²³ Counter-Memorial, para. 173.

²²⁴ Quoted in Reply, para. 127.

(i) Expenditures related to the initial investment in the amount of US\$ 17,345,400.00.

(ii) The Tribunal has found that Chile's responsibility is related to the approval of the transfer of funds by the FIC in spite of the policy of the Government not to change the PMRS. Therefore, the Tribunal considers that expenditures for the Project prior to the execution of the first Foreign Exchange Contract on March 18, 1997 are not eligible for purpose of the calculation of damages even if they could be considered part of the investment. For the same reason, expenditures made after November 4, 1998—the date on which Minister Henríquez informed the Claimants in writing that the PMRS would not be changed – are also to be excluded from said calculation. The total of expenditures during this period on account of salaries, travel, legal services and miscellaneous items, as detailed in Exhibit 93A submitted with the Reply, amount to US\$ 235,605.37.

(iii) The Tribunal considers the financial costs related to the investment made to be part of a business decision on how to finance the investment. As stated by the tribunal in Middle East Cement and referred to by the parties in their allegations:

“They could be claimed, if it were shown that they were caused by conduct of the Respondent which was in breach of the BIT.”²²⁵ Since the Tribunal has found that Chile breached its obligation to treat the Claimants' investment fairly and equitably and this treatment is related to the decision of the Claimants to invest in Chile, the Tribunal considers that the financial costs related to the investment in the amount of US\$ 3,888,582.95 are part of the eligible expenditures for purposes of the calculation of damages.

241. The aggregate of the above eligible expenditures amounts to US\$ 21,469,588.32. However, the residual value of the investment and the damages that can be attributed to business risk need to be deducted from such amount. The Tribunal will now turn its attention to these matters.

²²⁵ Middle East Cement, para. 154.

2. Damages Attributable to Business Risk. Residual value of the Investment

242. The Tribunal decided earlier that the Claimants incurred costs that were related to their business judgment irrespective of the breach of fair and equitable treatment under the BIT. As already noted, the Claimants, at the time of their contract with Mr. Fontaine, had made decisions that increased their risks in the transaction and for which they bear responsibility, regardless of the treatment given by Chile to the Claimants. They accepted to pay a price for the land with the Project without appropriate legal protection. A wise investor would not have paid full price up-front for land valued on the assumption of the realization of the Project; he would at least have staged future payments to project progress, including the issuance of the required development permits.

243. The Tribunal considers therefore that the Claimants should bear part of the damages suffered and the Tribunal estimates that share to be 50% after deduction of the residual value of their investment calculated on the basis of the following considerations.

244. Mr. Fontaine has made an offer for MTD's EPSA shares of US\$ 10,069,206. The Claimants are, by the terms of their shareholders' arrangements with Mr. Fontaine and as decided by an arbitral tribunal and confirmed by the Chilean courts, obliged to accept this offer or buy him out. For this reason, the Tribunal considers that the price offered by Mr. Fontaine for the shares of EPSA currently held by the Claimants constitutes the residual value of the investment. Because only part of the offer is in cash, the cash value of the remainder on a present value basis is US\$ 9,726,943.48.²²⁶

245. The Tribunal notes that the Claimants had not accepted Mr. Fontaine's offer because it is not a full cash offer and are concerned about the uncertain financial situation of Mr. Fontaine. This is of no relevance to this Tribunal, since the risk of having chosen Mr. Fontaine as a partner should be borne by the Claimants. Chile had no partici-

²²⁶ For purposes of this calculation, the Tribunal has used the US dollar two-year swap rate of May 6, 2004 for a two-year swap effective May 21, 2004 published by Bloomberg. The two-year swap rate represents an interest rate at which semiannual cash flows may be discounted until the maturity of the swap. There are no LIBOR rates for period of more than one year.

pation in his selection nor has it been claimed that the financial difficulties of Mr. Fontaine can be attributed to Chile. The Claimants themselves have manifested that they knew all along about his financial difficulties. This is a business risk that the investors shall bear.

246. To conclude, the Claimants should bear the risk inherent in Mr. Fontaine's offer and 50% of the damages after deducting the present value of such offer from the total amount calculated in Section 1 above.

3. Date from which pre-award interest should accrue

247. The Tribunal considers that interest on the amount of damages for which Chile is responsible should accrue from November 5, 1998, the day after Minister Henríquez notified the Claimants that it was against his Government's policy to modify the PMRS.

248. The Claimants in their Reply increased the amount of their claim with the interest accrued during the extension granted by the Tribunal to the Respondent to file the Counter-Memorial. Chile has argued that the additional interest should not be awarded since the suspension was for all the "issues related to the procedure."²²⁷ The Tribunal has awarded interest from November 5, 1998 for the reasons stated above and considers that the extension of the term for the submission of the Counter-Memorial does not have a bearing on this matter.

4. Applicable Rate of Interest

249. The Claimants have requested that the Tribunal apply a compound annual interest rate of 8%. The Respondent has proposed the dollar-based annual rate of interest applicable in Chile or the average annual LIBOR. The Respondent has objected to a compound interest rate as not being in accordance with international law.

250. This being an international tribunal assessing damages under a bilateral investment treaty in an internationally traded currency related to an international transaction, it would seem in keeping with the nature of the dispute that the applicable rate of interest be the annual LIBOR on November 5 of each year since November 5, 1998 until payment of the awarded amount of damages. Based on the rates published daily

²²⁷ Counter-Memorial, para. 147.

by Bloomberg, the annual LIBOR on November 5 of each year since November 5, 1998 are as follows: (i) 5.03813 % in 1998, (ii) 6.16 % in 1999, (iii) 6.71625 % in 2000, (iv) 2.24625 % in 2001, (v) 1.62 % in 2002, and (vi) 1.4925 % in 2003.

251. The Tribunal considers that compound interest is more in accordance with the reality of financial transactions and a closer approximation to the actual value lost by an investor. As expressed by the tribunal in Santa Elena:

“Where an owner of property has at some earlier time lost the value of his asset but has not received the monetary equivalent that then became due to him, the amount of compensation should reflect, at least in part, the additional sum that his money would have earned, had it, and the income generated by it, been reinvested each year at generally prevailing rates of interest.”²²⁸

VI. COSTS

252. Taking into account that neither party has succeeded fully in its allegations, the Tribunal decides that each party shall bear its own expenses and fees related to this proceeding and 50 % of the costs of ICSID and the Tribunal.

VII. DECISION

253. For the reasons above stated the Tribunal unanimously decides that:

- 1) The Respondent has breached its obligations under Article 3(1) of the BIT.
- 2) The Claimants failed to protect themselves from business risks inherent to their investment in Chile.
- 3) The Respondent shall pay the Claimants the amount of US\$ 5,871,322.42.

²²⁸ *Compañía de Desarrollo de Santa Elena, S.A. v. Republic of Costa Rica*, ICSID Case No. ARB/96/1, Final Award, 17 February 2000, para. 104.

4) The Respondent shall pay compound interest on such amount from November 5, 1998 and determined as set forth in paragraphs 249- 251 above until such amount has been paid in full.

5) The parties shall bear all their respective expenses and fees related to this proceeding.

6) The parties shall share equally the fees and expenses incurred by ICSID and the Tribunal.

7) All other claims filed in this arbitration shall be considered dismissed.

Done in Washington, D.C., in English and Spanish, both versions being equally authoritative.

Text Box: signed

Andrés Rigo Sureda
President of the Tribunal
Date: May 21, 2004

Text Box: Signed

Marc Lalonde
Arbitrator
Date: May 13, 2004

Text Box: Signed

Rodrigo Oreamuno Blanco
Arbitrator
Date: May 21, 2004