

NAFTA ARBITRATION UNDER THE UNCITRAL ARBITRATION RULES  
AND THE  
NORTH AMERICAN FREE TRADE AGREEMENT

INTERNATIONAL THUNDERBIRD GAMING CORPORATION

Claimant

versus

THE UNITED MEXICAN STATES

Respondent

PARTICULARIZED STATEMENT OF CLAIM  
OF CLAIMANT  
INTERNATIONAL THUNDERBIRD GAMING CORPORATION

15 August 2003

## TABLE OF CONTENTS

I.	<u>INTRODUCTORY STATEMENT AND SUMMARY OF ARGUMENT</u> .....	1
II.	<u>STATEMENT OF FACTS</u> .....	3
	A. <u>International Thunderbird Gaming Corporation</u> .....	3
	B. <u>Initiation of Thunderbird’s Investments in Mexico</u> .....	3
	C. <u>Gaming Activities in Mexico</u> .....	5
	D. <u>Initiation of Government Contacts Concerning Thunderbird’s Proposed Skill Machine Operations</u> .....	5
	E. <u>Thunderbird Preparations to Commence Skill Machine Operations</u> .....	6
	F. <u>Mexico’s Approval of Thunderbird’s Proposed Skill Machine Operations</u> .....	8
	G. <u>Thunderbird’s EDM Skill Machines Operations</u> .....	12
	1. EDM-Matamoros.....	12
	2. EDM-Laredo.....	13
	3. EDM-Reynosa.....	14
	4. EDM-Puebla.....	15
	5. EDM-Monterey.....	15
	6. EDM-Juarez.....	16
	7. Other Potential Locations.....	16
	H. <u>Mexico’s Destruction of Thunderbird’s EDM Investments in Mexico</u> .....	17
	I. <u>The October Administrative Findings and Order</u> .....	27
	J. <u>Post-Seizure Activities</u> .....	29
	K. <u>Thunderbird’s Investment Enterprises Pre- and Post-Seizure</u> .....	31
	L. <u>Guardia and Other Skill Machine Operators Presently Operating in Mexico</u> .....	34
III.	<u>INTERPRETATION AND GOVERNING PRINCIPLES OF NAFTA CHAPTER 11</u> .....	35
IV.	<u>THUNDERBIRD’S CLAIM MEETS THE REQUIREMENTS OF NAFTA CHAPTER 11</u> .....	38

A.	<u>NAFTA Articles 1001 and 1117</u> .....	38
B.	<u>Thunderbird is an Investor of a Party under Article 1117</u> .....	39
C.	<u>Thunderbird May Proceed Under Article 1117</u> .....	39
D.	<u>Thunderbird’s Claims Involve Measures Adopted or Maintained by Mexico</u> .....	39
E.	<u>Thunderbird Suffered Losses Arising from Mexico’s Treaty Breaches</u> .....	40
F.	<u>Thunderbird Brought Its Claims Within the Required Three Year Period</u> .....	40
V.	<u>MEXICO BREACHED THE “NATIONAL TREATMENT” STANDARD UNDER NAFTA ARTICLE 1102 IN ITS DESTRUCTION OF THE THUNDERBIRD INVESTMENTS</u> .....	41
A.	<u>Article 1102 and the “National Treatment” Standard</u> .....	41
1.	Article 1102.....	41
2.	The “National Treatment’ Standard.....	41
3.	Identification of Appropriate Comparators.....	43
4.	Treatment No Less Favorable.....	46
5.	Like Circumstances.....	49
B.	<u>Mexico Breached the Article 1102 “National Treatment” Standard</u> .....	52
1.	Identification of Appropriate Comparators.....	52
2.	Treatment No Less Favorable.....	56
3.	Like Circumstances.....	57
VI.	<u>MEXICO BREACHED THE “MINIMUM STANDARD OF TREATMENT” UNDER NAFTA ARTICLE 1105 IN ITS DESTRUCTION OF THE THUNDERBIRD INVESTMENTS</u> .....	57
A.	<u>Article 1105 and the “Minimum Standard of Treatment”</u> .....	57
1.	Article 1105.....	57
2.	“Minimum Standard of Treatment”.....	58
3.	Denial of Justice.....	61
4.	Procedural Denials of Justice.....	65

5.	Substantive Denials of Justice.....	71
6.	The Abuse of Rights Doctrine.....	74
7.	Detrimental Reliance.....	77
B.	<u>Mexico breached the Article 1105 “Minimum Standard of Treatment”</u> .....	79
1.	Detrimental Reliance.....	79
2.	Denial of Justice and Abuse of Rights.....	85
3.	Conclusion.....	98
VII.	<u>MEXICO EXPROPRIATED THE THUNDERBIRD INVESTMENTS WITHOUT COMPENSATION IN VIOLATION OF NAFTA ARTICLE 1110</u> .....	99
A.	<u>Article 1110 and “Expropriation”</u> .....	99
1.	Article 1110.....	99
2.	Article 1110 “Expropriation” Standards.....	100
B.	<u>Mexico Expropriated the Thunderbird Investments</u> .....	105
VIII.	<u>DAMAGES</u> .....	106
A.	<u>The International Law of Damages</u> .....	106
1.	The Requirement of Full Restitution Value.....	106
2.	Causation and Remoteness.....	109
3.	Full Restitution Value is the Fair Market Value of Any Frustrated Investment Business.....	113
4.	Valuation Factors and the DCF Method.....	115
5.	Interest.....	119
6.	Costs.....	121
B.	<u>Application of the International Law of Damages to the Facts of this Case</u> .....	122
1.	10 Year Scenario With No Expansion at the Existing Matamoros, Nuevo Laredo and Reynosa Locations.....	122

2.	10 Year Scenario With Expansion at the Existing Matamoros, Nuevo Laredo and Reynosa Locations.....	123
3.	10 Year Scenario With Expansion at the Existing Matamoros, Nuevo Laredo and Reynosa Locations and Developments at the Puebla, Ciudad Juarez and Monterrey locations.....	123
IX.	<u>CONCLUSION</u> .....	123

1 I.

2 **INTRODUCTION AND SUMMARY OF ARGUMENT.**

3 In October, 2001, The United Mexican States (“Mexico”) forcibly seized the investment  
4 enterprises of International Thunderbird Gaming Corporation (“Thunderbird”). At the same time, it  
5 provided, and still provides, favorable treatment to its own investors undertaking identical investment  
6 activities. Mexico reneged upon promises made to Thunderbird. Mexico arbitrarily and unjustifiably  
7 discriminated against a foreign investment. Mexico breached its NAFTA treaty obligations. Mexico  
8 destroyed investment enterprises worth tens of millions of dollars.

9 Thunderbird wished to undertake investment activities in Mexico. In good faith and seeking  
10 “certainty” as to the propriety of its proposed enterprise, Thunderbird made full disclosure to Mexico  
11 of its intended business activities. Thunderbird sought and obtained from the highest levels of the  
12 Mexican government an official opinion attesting to the propriety and legality of its intended operations.  
13 In reliance upon that official opinion, Thunderbird and its investors formed a series of Mexican entities  
14 to open and operate entertainment facilities where customers played “skill machines”. Three facilities  
15 were opened. Others were in various stages of preparation. The opened facilities were highly successful.

16 After a change of government, Mexico reversed course and reneged upon its prior approval of  
17 Thunderbird’s activities. Mexico embarked upon an aggressive course of action, employed through the  
18 arbitrary actions of its newly-appointed director of gaming, J. Guadalupe Vargas Barrera, to shut down  
19 the skill machine operations and destroy Thunderbird’s investment enterprises. Mexico succeeded in  
20 that effort. It forcibly seized, closed and sealed Thunderbird’s skill machine facilities. They remain  
21 seized and closed. At the same time it was seizing Thunderbird’s skill machine operations, Mexico was  
22 allowing its own investors to operate identical skill machine facilities. Those facilities remain open and  
23 operating.

24 Thunderbird brings this claim under Article 1117 as an investor of a Party (Canada) on behalf  
25 of enterprises of another Party (Mexico). Thunderbird brings this claim under Article 1117 on behalf  
26 of the following enterprises of Mexico:

- 27 - Entertainmens de Mexico S. de R. L. De C. V.
- 28 - Entertainmens de Mexico Laredo S. de R. L. de C.V.

- 1 - Entertainmens de Mexico Reynosa S. de R.L. de C.V.
- 2 - Entertainmens de Mexico Puebla S. de R.L. de C.V.
- 3 - Entertainmens de Mexico Monterey S. de R.L. de C.V.
- 4 - Entertainmens de Mexico Juarez. S. de R.L. de C.V. <sup>1</sup>

5 Thunderbird asserts that Mexico breached its treaty obligations as follows:

6 **Article 1102** - National Treatment.

7 Mexico breached its obligation under Article 1102 by failing to provide to the investments of  
8 an investor of another Party (Thunderbird of Canada) treatment no less favorable than it accords, in like  
9 circumstances, to investments of its own investors with respect to the establishment, acquisition,  
10 expansion, management, conduct, operation, and sale or other disposition of investments.

11 **Article 1105** - Minimum Standard of Treatment.

12 Mexico breached its obligation under Article 1105 by failing to accord to the investments of an  
13 investor of another Party (Thunderbird of Canada) treatment in accordance with international law,  
14 including fair and equitable treatment and full protection and security.

15 **Article 1110** - Expropriation and Compensation.

16 Mexico breached its obligation under Article 1110 by directly or indirectly expropriating  
17 investments of an investor of another Party (Thunderbird of Canada) in its territory in the absence of  
18 a public purpose, on a discriminatory basis, without due process of law and not in accordance with  
19 Article 1105(1), and without payment of compensation equivalent to the fair market value of the  
20 expropriated investments.

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27 <sup>1</sup>Thunderbird will proceed only under Article 1117. Concurrent with the filing and service of this Claim, Thunderbird  
28 provided additional waivers under Article 1121 2.(b) for Entertainmens de Mexico Puebla, Entertainmens de Mexico  
Monterey, Entertainmens de Mexico Juarez. Waivers were previously served for the other named Mexican enterprises.

1 II.

2 STATEMENT OF FACTS

3 **A. International Thunderbird Gaming Corporation.**

4 Claimant International Thunderbird Gaming Corporation (hereinafter “Thunderbird”) is a  
5 publicly held Canadian corporation. Thunderbird has approximately twenty-four million outstanding  
6 shares; approximately eight million of which are held each by Canadian residents, United States  
7 residents, and European residents. Thunderbird’s Chief Executive Officer and President of its board is  
8 Jack Mitchell. Its general counsel is Albert Atallah. *[Atallah, paras. 5, 6, 7; Ex. 1; Mitchell, para. 1]*<sup>2</sup>

9 Thunderbird is an owner and operator of international gaming facilities. In the early 1990's,  
10 Thunderbird was involved in Indian gaming activities in California. In the late 1990's, Thunderbird  
11 shifted its activities to exclusive involvement in Latin American gaming and entertainment operations.  
12 *[Atallah, para. 9; Mitchell, paras. 4-7]*

13 Thunderbird presently owns and operates gaming facilities in Guatemala, Panama, Nicaragua,  
14 and Venezuela. From 2000 to 2001, it owned, controlled and operated “skilled machine” facilities in  
15 the Mexico cities of Matamoros, Nuevo Laredo, and Reynosa. The wrongful seizure of those facilities  
16 by Mexico is the subject of this claim. *[Atallah, paras.10, 11; Mitchell, para. 7]*

17 **B. Initiation of Thunderbird’s Investments in Mexico.**

18 Beginning in late1999 and early 2000, Peter Watson, a lawyer from Minnesota, U.S.A., initiated  
19 discussions with Jack Mitchell, President and CEO of Thunderbird. Those discussions concerned  
20 potential gaming opportunities in Mexico. Watson had previously represented a U.S. investor in a  
21 Mexican gaming operation. Through that effort, he had gained considerable expertise and experience  
22 with respect to investments in Mexico and with respect to its gaming laws. Mitchell had significant  
23 knowledge concerning gaming activities throughout Latin America. *[Watson para. 3; Mitchell, paras.*  
24 *4-7]*

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25  
26 <sup>2</sup>References to declarations shall state the last name of the declarant and the numbered paragraph. For example, a reference  
27 to paragraph 6 of the “DECLARATION OF ALBERT ATALLAH IN SUPPORT OF PARTICULARIZED STATEMENT  
28 OF CLAIM OF CLAIMANT INTERNATIONAL THUNDERBIRD GAMING CORPORATION” will be stated as follows:  
“Atallah, para. 6”. All declarations are located in Binder C-II. References to exhibits shall state the abbreviation “Ex.” and  
exhibit number. For example, a reference to Exhibit 6 will be stated as follows: “Ex. 6”. All Exhibits are located in Binders  
C-III through C-VI and arranged in numerical order.



1 Mitchell and Watson looked at a number of investment possibilities, partnership arrangements  
2 and prospects for Thunderbird to establish gaming operations in Mexico. Thunderbird initially  
3 considered acquisition of a horse track facility and sports book operation in Nuevo Laredo.  
4 Thunderbird's lawyer in Mexico, Luis Ruiz de Velasco of Baker & McKenzie in Mexico City, reviewed  
5 proposed acquisition documents. Thunderbird ultimately decided not to pursue that investment.  
6 *[Watson para.5, Mitchell, paras. 8, 9, 10; Velasco, paras. 1, 2, 3]*

7 Mitchell and Watson were contacted by Doug Oien and Ivy Ong ("Oien/Ong"). Oien/Ong were  
8 involved in various gaming activities inside and outside of Mexico. They represented to Watson and  
9 Mitchell that they had made an investment in a sports book and skill game facility operated by Jose  
10 Guardia in Juarez, Mexico. *[Watson para. 6; Mitchell, para. 8, 9, 10]*

11 "Skill games" or "skill machines" are commonly understood in the international gaming industry  
12 as differing from slot machines in that the skill machine player is able to start and stop the activity at  
13 play, to make decisions about which games and which symbols to hold, and to effect, through his skill  
14 and dexterity, the outcome of the game. None of these elements are present in a "slot machine". There,  
15 the player simply pulls the handle and waits to see if he has won anything. Further, in the international  
16 arena of gaming activities, there is a clear distinction between traditional "casinos" and video gaming  
17 parlors. *[Atallah, para. 14; McDonald, para. 10, 11; Ex 69, Maida Dec.]*

18 Mitchell and Watson met with Oien/Ong in the Nuevo Laredo to discuss potential skill machine  
19 operations in Mexico. Present at that meeting were two Mexican lawyers, Julio Aspe and Oscar Arroyo.  
20 Aspe and Arroyo had represented Jose Guardia with respect to his skill machine operations in Mexico.  
21 Aspe and Arroyo stated that Guardia had a significant legal altercation with Gobernacion concerning  
22 his skill machine operations. Gobernacion is Mexico's Department of the Interior. It regulates and  
23 controls all gaming activities. Aspe and Arroyo stated that Gobernacion had entered Guardia's facility  
24 and sealed off the skill machines. Aspe and Arroyo, representing Guardia, had obtained an "amparo"  
25 (judicial injunctive relief) allowing use of the machines and had recently won the underlying court case

1 establishing the legality of skill machine operations in Mexico.<sup>3</sup> [Watson, para. 7; Mitchell, para. 11]

2 Oien/Ong were looking for investors to open and operate a skill machine facility similar to  
3 Guardia's. They proposed a revenue-sharing arrangement under which Thunderbird would back  
4 financially and operate one or more skill machine parlors in Mexico. Aspe and Arroyo would be  
5 utilized to obtain necessary local permits and deal with Gobernacion. During these meetings, Watson  
6 and Mitchell developed the idea that Thunderbird would raise capital to create, own and control a  
7 Mexican entity or a series of entities to operate skill machine parlors in Mexico. [Watson, para. 8]

8 **C. Gaming Activities in Mexico**

9 When Watson and Mitchell commenced their discussions concerning operation of skill machines  
10 in Mexico, they understood that even though Mexican law prohibited games of chance, it did not, and  
11 still does not, prohibit other related activities. In Mexico, there are bingo parlors, sports book operations  
12 where customers wager on sporting events and horse and dog racing operations with betting on race  
13 outcomes, jai lai with wagering, and various other gaming-related activities. There are skill machine  
14 operations at various location in Mexico, the most prominent of which are Guardia's facilities in  
15 Mexico City and Juarez<sup>4</sup>. [Watson, para. 4, 7, 57; Velasco, para. 25; Montano, para.19; Luz A. Armas  
16 Sawin, para. 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres; Gomez, paras. 27-29; Exs. 82-85]

17 **D. Initiation of Government Contacts Concerning Thunderbird's**

18 **Proposed Skill Machine Operations.**

19 Thunderbird, through Watson and Mitchell, sought assistance from Thunderbird's Baker &  
20 McKenzie attorneys in Mexico. In April and May, 2000, Baker & McKenzie lawyer Luis Ruiz de  
21 Velasco, Mitchell, Watson and Mauricio Girault met several times with Aspe and Arroyo. Girault was  
22 a long-time friend of Watson. He became an investor in Thunderbird's skill machine enterprises and  
23 a director of Thunderbird. Aspe and Arroyo generally explained the process used by Guardia to fend  
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25  
26 <sup>3</sup> Guardia subsequently obtained a favourable higher court ruling establishing the legality of his skill machine operations.  
Guardia's skill machine facilities are open and operating in Mexico today. [Watson, para. 57; Velasco, para. 25]

27 <sup>4</sup> Guardia's skill machine facilities remain open and operating. Thunderbird's skill machine facilities were seized and remain  
28 closed by Mexico government order. This disparate treatment provides the basis for claimant's Article 1102 "National  
Treatment" claim.

1 off Gobernacion with respect to his skill machine operations in Juarez and Mexico City. De Velasco  
2 analyzed the procedures utilized by Aspe and Arroyo; i.e., to simply open a skill machine facility and,  
3 if Gobernacion took action as it had with Guardia, defend by amparo proceedings. Velasco concluded  
4 that while this procedure had been effective for Guardia, it would not provide Thunderbird with the  
5 certainty necessary to proceed with the significant investment. *[Watson, paras. 9, 10, 11, 12; Mitchell,*  
6 *para. 12; Velasco, paras. 3, 4]*

7 In July 2000, Velasco, Girault, Aspe and Watson met in Mexico City. Aspe advised that he had  
8 several conversations with the Director of Juegos y Sorteos<sup>5</sup> within Gobernacion. He stated that he had  
9 described to the director what Thunderbird intended to do. Aspe indicated that he felt it might be  
10 possible to obtain an opinion letter from Gobernacion attesting to the legality of the skill machines.  
11 Thunderbird decided to request the official opinion from Gobernacion concerning the legality of its  
12 skill machines and proposed operations. If the response was favorable, Thunderbird would proceed with  
13 the opening and operation of its skill machine facilities in Mexico. *[Watson, paras. 11, 12; Mitchell,*  
14 *para. 12; Velasco, para. 5]*

15 Over the next few weeks, Aspe and Arroyo continued to speak with their contacts in  
16 Gobernacion. There were numerous contacts between the Thunderbird group and Gobernacion by and  
17 through Aspe and Arroyo. Those contacts concerned the nature and operation of the skill machines,  
18 Thunderbird's proposed operation and the text of a formal application to be presented to Gobernacion  
19 for consideration. Drafts of the proposed application were exchanged and discussed. Ultimately, Aspe  
20 indicated that Gobernacion was willing to consider and issue the opinion letter attesting to the legality  
21 of the skill machines. *[Watson, para. 11, 12, 13, 14; Mitchell, para. 12; Velasco, para. 5]*

22 **E. Thunderbird Preparations to Commence Skill Machine Operations.**

23 During this same period, and in anticipation of Gobernacion's approval of its intended  
24 operations, Thunderbird proceeded with preparations to open its first skill machine facility.

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27 <sup>5</sup>The Director of Juegos y Sortereos was, and is, the government representative within Gobernacion (Mexico's Department  
28 of Interior) with direct authority over of all games in Mexico in which betting is involved, including games of chance  
("Juegos de Azar"). *[Velasco, para. 8.]*

1 In April, the Oien/Ong had incorporated an entity known as Entertainmens de Mexico S.A. de  
2 C.V. (hereinafter “EDM”). In May, EDM had entered into a lease for a location in Matamoros. In June,  
3 2000, discussions began for acquisition of EDM by subsidiaries of Thunderbird. On June 20, 2000,  
4 EDM executed a modification of the Matamoros lease. Under that modification, EDM secured a  
5 voluntary five year extension of the lease through 2006. *[Watson, para. 18; Atallah, para. 15, 25;*  
6 *Gomez, para.47; Exs. 2, 3, 4, 5].*

7 On June 27, 2000, EDM opened bank accounts for both U.S. dollars and pesos. On June 30,  
8 2000, EDM secured a license for land use which specifically referred to the intended use as “video  
9 games of skill and dexterity”. On June 29, 2000, EDM noticed its intended business operations to local  
10 authorities. *[Gomez, paras. 48-50; Exs. 6, 7, 8].*

11 On July 27, 2000, EDM imported 50 Bestco Model MTL19U-8L video gaming machines.  
12 *[Gomez, para. 51; McDonald, paras. 4, 7, 9, 10, 12; Exs. 9. 36].*

13 On August 10, 2000, EDM provided notice of its intended operations to local authorities. That  
14 notice specified the following activities: “restaurant, bar, and video games were skill and  
15 abilities”.*[Gomez, para. 52; Ex. 10].*

16 On August 10, 2000, Thunderbird, through two wholly-owned subsidiaries, Juegos de Mexico,  
17 Inc. and International Thunderbird Brazil, acquired all outstanding shares of EDM. Mitchell, Watson,  
18 and Atallah were designated as the board of directors of EDM. *[Atallah, para. 26; Exs. 11, 12, 13].*

19 On August 11, 2000, Thunderbird acquired the EDM shares of International Thunderbird Brazil.  
20 Thunderbird, through its direct ownership and that of its subsidiaries, Juegos de Mexico, Inc., held the  
21 majority of EDM shares. Mitchell, Thunderbird’s president and CEO, was designated president of  
22 EDM’s board of directors. *[Atallah, para. 26; Ex. 14].*

23 On August 14, 2000, EDM imported 30 SCI model 17" UR video game machines. *[Gomez,*  
24 *para. 53; McDonald, paras. 4, 7, 9, 10, 12; Exs. 15. 36].*

25 Thunderbird obtained NOMS (Mexican consumer protection registration required for all  
26 imported products) for the imported machines. The machines had to be tested, analyzed and verified  
27 in order to obtain the NOMs. The NOMs specifically identified the imported machines as skill  
28 machines. *[Gomez, para. 54; Ex. 16; Watson; para. 19; Mitchell, para. 13].*

1 Thunderbird and EDM were prepared to open the Matamoros “skill machine” facility upon  
2 expected issuance of formal Mexican government approval.

3 **F. Mexico’s Approval of Thunderbird’s Proposed Skill Machine Operations.**

4 On August 3, 2000, and after extensive discussions between the Thunderbird representatives  
5 and Gobernacion, EDM presented a formal request, or “solicitud” to Gobernacion concerning the  
6 proposed skill machine operation. [*Ex. 16; Velasco, para. 6; Watson, para. 15; Atallah, para. 16*]. The  
7 application notified Gobernacion of EDM’s intention to operate 2,000 machines at various locations  
8 in Mexico. The application contained a detailed description of the machines, their method of operation,  
9 and the manner by which prizes were obtained by the players. The application identified the precise  
10 make and model number of the machines to be used. The application clearly and directly stated its  
11 purpose:

12 “. . . we are requesting an opinion from this Dirreccion General so the entity I represent has  
13 the certainty that the commercial exploitation of video game machines for games of skill  
and ability is legal..” [*English translation*]

14 The application was a direct request to the Director General of Gobernacion for an official opinion that  
15 the identified machines were not prohibited by Mexican law.

16 For that declared above, we have concluded that our operation is not of the type  
17 prohibited by *La Ley Federal de Juegos y Sorteros* since our video game machines do  
18 not use chance, bets or wagers, and these video games are only for the purpose of  
entertainment in which the users can obtain prizes fir their skills and abilities, and I’m  
requesting from this Direccion General your opinion about this. [*English translation*]

19 The full text (English Translation) of EDM’s August 3, 2000 application to Gobernacion is as follows:

20 JÚAN JOSÉ MENÉNDEZ TLACATELPA, legal representative of ENTERTAINMENS  
21 DE MÉXICO, S.A DE C.V. which accredits his personality by a certified copy of a  
22 notarized document attached hereby, and who has as conventional address, for receiving  
and hearing any type of communication and documents, Plaza Inverlat piso 12, Blvd. M.  
Avila Camacho n° 1, C.P. 1 1009, Mexico D.F., authorizes, for this purpose, Mr. Luis  
Ruiz de Velasco y P. and with all respects I appear before you to say:

23 By the means of these writings, I come to request from you that this Dirección General  
24 give an opinion about the activities that the party I represent is carrying out and which  
25 consist in the commercial exploitation of video game machines for games of skills and  
ability in accordance with the following:

26 1. - Entertainmens de México, S.A. de C.V., is a legal entity incorporated in accordance  
27 with the Laws of the Republic of Mexico with the public deed 38,765, which was issued  
and granted by the Public Notary Number 53, Mr. Rodrigo Orozco Perez, in Mexico  
28 D.F. as in proven by the attached notarial affidavit; and which is also registered in the  
Federal Registry of Taxpayers under the symbol EME-000405 -LQ7.

1 2. - The entity which I represent opened a business, at Av. de las Rosas N° 70-A,  
2 Colonia Jardin in the city of Matamoros, Tamaulipas, under the commercial name “La  
3 Mina de Oro”, which operates video game machines for games of skills and ability, and  
4 complies with all Municipal requirements.

5 3. - The video game machines for games of skills and ability, which the entity I represent  
6 commercially exploits, are devices for recreation which have been designed for the  
7 enjoyment and entertainment of its users. In these games, chance and wagering or  
8 betting is not involved, but the skills and abilities of the user who has to align different  
9 symbols on the machine screen by touching the screen or pushing buttons in order to  
10 stop the wanted symbol from several other symbols which spin in a sequential manner  
11 in each of the lanes or squares of each video game. The user has to align symbols in an  
12 optimum combination to receive a ticket with points which can be traded for goods or  
13 services; as this is already done at different locations in the country.

14 4.-The video game machines for games of skills and ability which we operate, at this  
15 present time at the place indicated above on this writings, are trademark Bestco, model  
16 MTL19U-8L and S.C.I. model 17”UR; and the entity I represent is trying to place about  
17 2,000 (two thousand) more machines at other locations in the Republic of Mexico and  
18 these machines are of the same identical mechanical nature and functioning as those  
19 described in point 3, above.

20 For all I have declared above, I come to this *Dirección General* requesting your opinion  
21 about the commercial activities which hereby I have detailed, and, therefore, you can  
22 express your opinion about the video game machines for games of skills and ability,  
23 which we have referred hereby, in order to determine if these games are regulated by the  
24 Ley Federal de Juegos y Sorteos.

25 We are requesting an opinion from this *Dirección General* so the entity I represent has  
26 the certainty that the commercial exploitation of video game machines for games of  
27 skills and ability is legal; after an analysis of the nature of our machines, and the legal  
28 dispositions, we have concluded that our machines are not bound by *Ley Federal de  
Juegos y Sorteos* and, therefore, are not regulated by *Secretaría de Gobernación* or any  
other federal authority since the activity which this company is engaged in is not found  
within the faculties foreseen in Article 73, of *Constitution General de la República* and  
which in its Fraction X clearly indicates that the Congress of the Union has exclusive  
authority to legislate, in the whole of the Republic, about games with bets, wagers and  
drawings, and that the Executive Federal has the authority to regulate these activities;  
but in entertainment where skills and ability is involved, it is logical that these are not  
under federal authority since *La Constitución General de la República* doesn't indicate  
that the Congress of the Union can exclusively legislate in such matters. Consequently,  
the authority to regulate this type of entertainment is not granted exclusively to the  
Federation, and, therefore, this is excluded from *La Ley Federal de Juegos y Sorteos*.

The nature of video game machines for games of skills and ability is not games of  
chance or games with bets, wagers or drawings, since, in the operation of these  
machines, the player seeks entertainment and is playing with our machines assuming an  
active position where his intelligence, his willpower, his experience and his skills to  
optimally answer to specific stimulus with the object of finding a combination, effect  
or boast on the machine, intervene; which can only be possible with ability, experience  
and control over the machine, and all of this is for the purpose of entertainment and  
enjoyment, and at the time, the player can receive points that he can trade for a prize as  
a reward for the skills achieved and in no way as the result of chance.

1 For this, it is clear to us, that is the skills and ability of the person who produces the  
2 effect over the videogame machine, and it is not the chance, the possibility, the fortune,  
3 or bet since the determinant to get results is the skills and ability of players; something  
4 very different from games of bets and wagers where there is a previous pact or covenant  
between the company and the user and, therefore, there is an agreement to handle an  
amount of money or any other thing, and all of this depends on a chance, on the  
unforeseen, or is not subject to the willpower or control of the user.

5 For that declared above, we have concluded that our operation is not of the type  
6 prohibited by *La Ley Federal de Juegos y Sorteos* since our video game machines do not  
7 use chance, bets or wagers, and these video games are only for the purpose of  
entertainment in which the users can obtain prizes for their skills and abilities, and I'm  
requesting from this Dirección General your opinion about this.

8 *[Ex. 17; Velasco, para. 6; Watson, para. 15]*

9 On August 15, 2000, Gobernacion issued the official letter. *[Ex. 18; Velasco, para. 7; Watson,*  
10 *para. 16; Atallah, para. 17.]* The letter was signed by Rafael de Antunano Sandoval, Director de  
11 Juegos y Sorteos in the name of, and on behalf of, Mr. Sergio Orozco Arceves, Director General of  
12 Gobernacion. These are the officials in charge at the highest levels of the Mexican government with  
13 direct authority over all games in which betting is involved, including games of chance. *[Velasco, para.*  
14 *8]* Gobernacion's official letter stated that the machines identified in EDM's August 3, 2000 solicitud  
15 are:

16 “. . recreational video game devices for purposes of enjoyment and entertainment of its  
17 users, with the possibility of obtaining a prize, without the intervention of luck or  
gambling, but rather the user's ability and skillfulness.”

18 The letter concluded that if the identified machines:

19 “. . operate in the form and conditions stated by you, this governmental entity is not able  
20 to prohibit its use. .”<sup>6</sup>

21 The full text of Gobernacion's August 15, 2000 official letter is as follows:

22 Regarding your letter dated August 3, 2000, received on August 8, 2000 by the  
23 Directorate of Games and Sweepstakes, entity that depends from this Directorate,  
24 whereby you request this entity to issue a response regarding your representative's  
exploitation of machines that operate under the concept of ability and skillfulness of its  
users, please be advised as follows:

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27 <sup>6</sup> Thunderbird through its Mexican entities imported and operated the precise machines identified in the August 3 solicitud  
28 and addressed in Gobernacion's official response and, at all times, operated them in the fashion described in that letter.  
Mexico has never produced evidence to the contrary.

1 As you may be aware, the Federal Law of Games and Sweepstakes, establishes with  
2 precision diverse dispositions that prohibit gambling and luck related games within the  
3 Mexican territory. Article I of such law establishes that “. . - All gambling and luck  
4 related games are prohibited within the Mexican territory, under the disposition of this  
5 law.”

6 Likewise, Article 3 of such law establishes that, “The federal executive branch, by  
7 means of the Ministry of State, shall supervise the regulation, authorization, control and  
8 vigilance of all games when such games contact gambling of any kind; as well as the  
9 sweepstakes, with the exception of the National Lottery, which shall be governed by its  
10 own law.”

11 In the same light, Article 4 of such law establishes that “in order to establish or operate  
12 any open or closed place, in which gambling games or sweepstakes take place, the  
13 Ministry of State shall authorize such establishments or operations, specifying the  
14 corresponding requirements and conditions to be fulfilled in every case.”

15 According to the above mentioned, the provisions established under the Federal Law of  
16 Games and Sweepstakes are enforceable legal dispositions that specifically prohibit  
17 gambling and luck related games within the Mexican territory; notwithstanding the  
18 above mentioned, according to your statement, the machines that your representative  
19 operates are recreational video game devices for purposes of enjoyment and  
20 entertainment of its users, with the possibility of obtaining a prize, without the  
21 intervention of luck or gambling, but rather the user’s ability and skillfulness.

22 In this light, it is important to clarify that, if the machines that your representative  
23 exploits operate in the form and conditions stated by you, this governmental entity is not  
24 able to prohibit its use, in the understanding that the use of machines known as “coins-  
25 swallowers,” “token-swallowers” or “slot machines,” in which the principal factor of the  
26 operation is luck or gambling and not the user’s ability of skillfulness as you stated,  
27 could constitute any of the hypothesis described under the Federal Law of Games and  
28 Sweepstakes, with the corresponding legal consequences that may be derived therefrom,  
under article 8 of such law.

In that view, and based on articles 27, section XXI of the Organic Law of the Federal  
Government; 1, 2, 3, 4, 5, 7, 8 and other articles related and applicable to the Federal  
Law of Games and Sweepstakes; as well as articles 8 and 14, Section XVII of the  
Interior Regulations of the Ministry of State, this Directorate, in accordance with the  
faculties previously conferred for such effect; warns you that in the machines that your  
representative operates there shall be no intervention of luck or gambling; warning that  
will not be in effect if the machines to be operated are video game devices that operate  
under the concept of ability and skillfulness.

Please be advised that, even though the machines of your representative operate under  
the concept of the user’s ability and skillfulness, it is necessary that the obligations and  
requirements set by the laws and regulations of each state and/or municipality be met.

*[Ex. 17; Velasco, para. 7; Watson, para. 16; Atallah, para. 17.]*

Based upon Gobernacion’s official opinion letter, Thunderbird and its counsel concluded that  
Thunderbird could proceed with skill machine operations in Mexico. *[Velasco, paras. 8, 9; Watson,  
para. 17; Atallah, paras. 17-20]*. In reliance upon Gobernacion’s stated official opinion, Thunderbird



1 moved forward with its plans to operate skill machine facilities in Mexico. *[Atallah, paras. 19-23]*.

2 Two days after Gobernacion issued its opinion, EDM opened at Matamoros. \_\_\_\_\_

3 **G. Thunderbird's EDM Skill Machines Operations**

4 **1. EDM - Matamoros**

5 The Matamoros facility ("La Mina de Oro") opened with approximately 80 machines. It was an  
6 immediate success. Thunderbird and EDM quickly brought the facility up to full operation. On August  
7 21, 2000, EDM provided notice to the municipality of added activities specifying "video game machines  
8 for skills and dexterity". On September 8, 2000, EDM registered with the Federal Registry of  
9 Taxpayers. EDM paid local municipality machine fees. On September 19, 2000, EDM filed employer  
10 registration documents. On September 19, 2000 EDM applied for workers' insurance. *[Gomez, paras.*  
11 *55-59; Exs. 19-23]*.

12 In January, 2000, "La Mina de Oro" underwent inspections by the health department. In  
13 February, 2001, it received compliance certifications from the fire and hazard department. In March,  
14 2001, EDM secured a liquor license. *[Gomez, paras. 60-62; Exs. 24-26]*.

15 On December 14, 2000, EDM was renamed "Entertainments de Mexico, S. de R. L. De C. V."  
16 and converted it to an "SRL". Thunderbird, through its direct ownership and that of its subsidiary,  
17 maintained majority ownership. Mitchell maintained his position as President of the Board of Directors  
18 of EDM. *[Atallah para. 28; ex. 27]*.

19 Thunderbird secured new investors into EDM. Those investors were uniformly advised of and  
20 relied upon Gobernacion's August 15 official opinion. In June 2001, EDM and investors executed a  
21 "Subscription and Investment Representation Agreement" and a "Members Quota Agreement" under  
22 which the investors secured various percentage interests in EDM. Membership certificates were issued  
23 to each of the investors indicating their share or quota percentages. Thunderbird maintained its  
24 significant ownership interest in EDM. Further, pursuant to the agreements, Thunderbird retained  
25 complete control over EDM's operations. The subscription agreement reflected and acknowledged  
26 Thunderbird's control of the investment:

27 "Thunderbird, through its key executives and management including  
28 Messrs. Watson and Girault will manage all aspects of the development  
and ongoing operation of the company.

1 The non-Thunderbird investors in EDM were “passive”. They exercised no control whatsoever over  
2 EDM or its operations. Thunderbird secured additional investors and acted to open new skill machine  
3 facilities. Those investors were uniformly advised of and relied upon Gobernacion’s August 15 official  
4 opinion. *[Atallah, paras. 21-24, 28-30; Exs. 28, 29; Velasco, para. 11]*

5 **2. EDM-Laredo**

6 In November, 2000, Thunderbird formed Entertainmens de Mexico Laredo S. de R. L. De C.  
7 V. (“EDM-Laredo”). *[Atallah, para. 31; Gomez, para. 64; Ex. 31; Velasco, para. 12]*. Thunderbird  
8 directly and through subsidiaries held a significant percentage interest in the entity. On November 17,  
9 2000, EDM Nuevo Laredo entered into a lease for a location in the city of Nuevo Laredo, Mexico. That  
10 one year lease granted EDM-Laredo voluntary extensions for a total lease term of nine years. On  
11 November 17, 2000, EDM-Laredo registered with the Federal Registry of Taxpayers. EDM-Laredo  
12 secure necessary permits and licenses.<sup>7</sup> *[Watson, paras. 22, 23, 24; Gomez, para. 65; Exs. 32, 33;*  
13 *Atallah, para. 58 b]*.

14 EDM-Laredo and various investors executed a “Subscription and Investment Representation  
15 Agreement” and a “Members Quota Agreement” under which the investors held their various percentage  
16 interests in EDM-Laredo. Membership certificates were issued to each of the investors indicating their  
17 share or quota percentages. Thunderbird maintained its significant ownership interest in EDM-Laredo.  
18 Thunderbird retained complete control over EDM- Laredo’s operations. The “Subscription and  
19 Investment Representation Agreement” acknowledged Thunderbird’s control of the investment.

20 “Thunderbird, through its key executives and management including  
21 Messrs. Watson and Girault will manage all aspects of the development  
and ongoing operation of the company.”

22 Further, Thunderbird maintained control over EDM-Laredo and its operations through a “Management  
23 Agreement”. Under that agreement, Thunderbird had direct control, through a managing director, of  
24 the development and operations of EDM-Laredo. The non-Thunderbird investors in EDM-Laredo were  
25 “passive”. They exercised no control whatsoever over EDM-Laredo or its operations. *[Atallah, paras.*

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26  
27 <sup>7</sup> Licenses ,permits and other EDM-Laredo documentation were sealed in the Nuevo Laredo facility upon closure and have  
28 been unavailable to claimant. Mexico disclosed during these proceedings that the Nuevo Laredo facility had been looted.  
The present location of such EDM-Laredo records is unknown. *[Crosby, para..5;Exs. 80, 81]*.

1 21-24, 32, 38; Exs. 34, 35, 37; Velasco, para. 12].

2 On February 9, 2001, EDM-Laredo opened its skill game facility in Nuevo Laredo. [Watson,  
3 para.24].

4 **3. EDM-Reynosa**

5 In June 5, 2001, Thunderbird formed Entertainmens de Mexico-Reynosa S. De R.L. de C.V..  
6 (“EDM-Reynosa”). [Atallah, para. 34; Gomez, para. 66; Ex. 39; Velasco, para. 13]. Thunderbird  
7 directly and through subsidiaries held a significant percentage interest in the entity. EDM-Reynosa  
8 secured a location with a two year lease. The lease had two voluntary extensions for a total lease term  
9 of fifteen years. EDM- Reynosa secured various permits and licenses.<sup>8</sup> [Watson, para. 31; Exs. 40, 41;  
10 Atallah, para. 58 c].

11 EDM-Reynosa and various investors executed a “Subscription and Investment Representation  
12 Agreement” and a “Members Quota Agreement” under which the investors held their various percentage  
13 interests in EDM-Reynosa. Membership certificates were issued to each of the investors indicating their  
14 share or quota percentages. Thunderbird maintained its significant ownership interest in EDM-Reynosa.  
15 Thunderbird retained complete control over EDM-Reynosa’s operations. The “Subscription and  
16 Investment Representation Agreement” acknowledged Thunderbird’s control of the investment.

17 “Thunderbird, through its key executives and management including  
18 Messrs. Watson and Girault will manage all aspects of the development  
and ongoing operation of the company.”

19 Further, Thunderbird maintained control over EDM-Reynosa and its operations through a “Management  
20 Agreement”. Under that agreement, Thunderbird had direct control, through a managing director, of  
21 the development and operations of EDM-Reynosa. The non-Thunderbird investors in EDM-Reynosa  
22 were “passive”. They exercised no control whatsoever over EDM-Reynosa or its operations. [Atallah  
23 para. 21-24, 35, 36; Exs. 42, 43, 45; Velasco, para. 13].

24 In August, 2001, EDM-Reynosa opened its skill game facility in Nuevo Laredo. [Watson, para.  
25 42].

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27  
28 <sup>8</sup>Licenses ,permits and other EDM-Reynosa documentation were sealed in the Nuevo Laredo facility upon closure and have been unavailable to claimant.



1 EDM-Monterey and various investors were circulating and reviewing a “Subscription and  
2 Investment Representation Agreement” and a “Members Quota Agreement” under which the investors  
3 would hold their various percentage interests in EDM-Monterey. Due to government interference and  
4 seizure of the other operations, the Monterey transactions were never finalized. The intended Monterey  
5 facility never opened. *[Atallah, para. 42, 43; Ex. 55, 56]*.

6 **6. EDM-Juarez**

7 In 2000, Thunderbird formed Entertainmens de Mexico-Juarez S. De R.L. de C.V. (“EDM-  
8 Juarez”). *[Atallah, para. 44; Gomez, para. 71; Ex. 57]*. Thunderbird, directly and through subsidiaries,  
9 held a significant percentage interest in the entity. By mid 2001, Thunderbird had located a suitable  
10 location for a skill machine facility in Juarez, Mexico. Lease negotiations were ongoing. The lease  
11 under negotiation would have provided EDM-Jaurez with a one year term with two five year extensions  
12 thereafter. *[Watson, para. 46 C; Ex. 58]*.

13 EDM-Juarez and various investors were circulating and reviewing a “Subscription and  
14 Investment Representation Agreement” and a “Members Quota Agreement” under which the investors  
15 would hold their various percentage interests in EDM-Monterey. Due to government interference and  
16 seizure of the other operations, the Jaurez transaction were not completed. The intended Juarez facility  
17 never opened. *[Atallah, para.45, 46; Ex. 59, 60]*.

18 **7. Other Potential Locations**

19 **Playa de Carmen**

20 \_\_\_\_\_Thunderbird has negotiations ongoing for a location in Playa de Carmen, Mexico. A lease  
21 proposal was under consideration and Watson was dealing with architects and builders. *[Watson, para.*  
22 *46 D; Exs. 61, 62]*.

23 **Puerta Vallarta**

24 Lease negotiations were ongoing for a location in Puerta Vallarta. Letters of intent encompassing  
25 formation of an EDM-Puerta Vallarta were under discussion. *[Watson, para. 47 E; Ex. 63, 64]*.

26 **Veracruz**

27 Thunderbird had investor interest and a lease under discussion in Vera Cruz, Mexico. *[Watson*  
28 *para. 47 F; Ex. 65]*.

1           **Chihuahua**

2           Thunderbird had executed of a letter of intent with investors for formation of one or more  
3 entities (“EDM de Mexico-Chihuahua”) to open skill machine operation in Chihuahua, Mexico.

4           *[Watson, para. 46 G; Ex. 66]*

5           **H. Mexico’s Destruction of Thunderbird’s EDM Investments in Mexico.**

6           Mexico held general elections in July, 2000. Vicente Fox’s administration came into office in  
7 December, 2000. J. Guadalupe Vargas Barrera (“Guadalupe Vargas”) was appointed the new Director  
8 de Juegos y Sorteos. That position had been held by Antunano Sandoval. He had signed, on behalf of  
9 Juegos y Sorteros and Gobernacion the August 15 official letter approving EDM’s operation of skill  
10 machines. Through Guadalupe Vargas, Mexico began aggressive efforts to disrupt Thunderbird’s skill  
11 machine operations. *[Velasco, para. 7, 15; Ex. 17; Watson, para. 16].*

12           Nuevo Laredo opened on January 21, 2001. Two weeks later, on February 9, 2001, Guadalupe  
13 Vargas closed the facility. He did so after conducting a personal “visual inspection” of the operation.  
14 *[Velasco, para. 15; Watson, para. 26; Atallah, para. 47; Mitchell, para. 18].*

15           Peter Watson was at home in Minnesota when Nuevo Laredo was closed. Watson received a  
16 telephone call from Steve Sawin, a manager at the facility. Sawin advised Watson that the new Director  
17 de Juegos y Sorteos, Guadalupe Vargas, had arrived at Nuevo Laredo with local police and was closing  
18 down the facility. Watson spoke directly with Guadalupe Vargas over the phone. Guadalupe Vargas  
19 stated that he was closing down the facility because "lo que veo aqui son tragamonedas." (“What I see  
20 before me are slot machines”). Watson described the August 15 official letter from Gobernacion. He  
21 explained the difference between skill machines and slot machines. Finally, Guadalupe Vargas simply  
22 said, “Look, I would like to help you but I am just following orders from my boss and I have an order  
23 here to close you down and that is that.” *[Watson, para. 26].* Another employee of the Nuevo Laredo  
24 facility specifically advised Guadalupe Vargas and the local authorities that Director General of  
25 Gobernacion Sergio Orozco Eschevez had granted permission for operation of the skill machine facility.  
26 That statement is expressed in the closure documents. *[Ex. 44].*

27           Thunderbird’s representatives flew to Mexico City the next day and with their lawyers from  
28 Baker & McKenzie. The lawyers filed for an amparo. Thunderbird they secured a meeting with Orozco

1 Aceves. He was now the outgoing Director General of Gobernacion. At that meeting for Thunderbird  
2 and the EDM entities were Girault, de Velasco, Mitchell and Jorge Montano<sup>9</sup>. Orozco Aceves stated that  
3 he was aware of the August 15 letter granting permission to operate the skill machines. He agreed with  
4 the Thunderbird representatives that Guadalupe Vargas had not followed proper procedure. He stated  
5 that he had given Guadalupe Vargas complete freedom to operate as the new director. Orozco Aceves  
6 said it was clear the order of closure had been signed prior to any inspection. He conceded there were  
7 many irregularities in the closure of the Nuevo Laredo facility. Orozco Aceves arranged an immediate  
8 meeting with a Mr. Alcantaro, head of the Amparo Division of Gobernacion. Alacantro and Orozco  
9 Aceves both expressed great concern about the closing and about the procedures used. They agreed to  
10 review the matter on an expedited basis. *[Watson, para. 27; Velasco, para. 16; Montano, paras. 8, 9,*  
11 *10; Atallah, para. 44].*

12 As a result of these meetings and other contacts, an agreement was reached. EDM would  
13 dismiss the Amparo proceeding. Gobernacion would lift the seals and allow operation of the Nuevo  
14 Laredo facility provided Thunderbird would enter into an administrative review proceeding to  
15 determine whether the machines did in fact comply with or violate Mexican law. In reaching that  
16 agreement, Thunderbird believed it would get fair treatment from the government. The Nuevo Laredo  
17 and Matamoros skill machines were being operated exactly as represented to Gobernacion in the August  
18 3 solicitud. Gobernacion had approved operation of the skill machines in response to that solicitud.  
19 *[Watson, para. 28; Velasco, para. 16; Montano, para. 11; Atallah, para. 48, 49].*

20 Thunderbird withdrew the amparo claim. Gobernacion lifted the seals. Laredo reopened on  
21 March 20, 2001. *[Watson, para. 29].*

22 Evidence indicates outright misrepresentation the part of Guadalupe Vargas as to the closure  
23 of Nuevo Laredo. In a March 9, 2001 letter to Daniel F. Cabeza de Vaca, Director General Asuntos  
24 Juridicos, the legal department of Gobernacion, Guadalupe Vargas explained his reasons for closing  
25 Nuevo Laredo. *[Ex. 67].* In doing so, he misrepresented the August 15 official letter. He explained that  
26

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27 <sup>9</sup>Jorge Montano is a career diplomat. He served as Mexico's Ambassador to both the United Nations and the United States.  
28 In both capacities, he served on Mexico's NAFTA negotiating team. He acted as a consultant to Thunderbird after the  
February, 2001 closure of Reynosa. *[Montana, paras. 3, 4, 5, 6, 7, 8]*

1 he closed the Nuevo Laredo facility because he had found 120 “slot machines”<sup>10</sup> operating without  
2 authorization or permit. He identified the August 3 solicitude and the August 15 official letter as the  
3 origin of the matter. But, in describing the August 15 letter to his superior, Guadalupe Vargas  
4 misrepresented it as denying authorization to Thunderbird’s EDM entity to operate skill machines. He  
5 stated as follows:

6       The matter in question has its origin in the petition submitted by C. Juan Jose Menendez  
7 Tlascaltepa, representing the company “Entertainments de Mexico, S.A. de C.V.”, by  
8 means of a document dated 3<sup>rd</sup> August, 2000, which prompted us to reply in our official  
9 letter No. DGG/SP/1057/2000, dated 15<sup>th</sup> August, 2000, in which authorization was  
10 denied to the petitioner for the operation of the above mentioned machines, explaining  
11 that their operation is not permitted within the national territory.

12       The company referred to nevertheless decided to start operations going beyond that  
13 which is prevented by the Federal Law of Gaming and Raffles and in contravention of  
14 the criteria communicated by the administrative authority, flagrantly violating the  
15 provisions of the law in question.

16 This an outright misrepresentation. In fact, the August 15 letter specifically stated that the identified  
17 machines were not games of chance and were not prohibited by Mexican law<sup>11</sup>. [*Ex. 17; Velasco, para.*  
18 *7; Watson, para. 16*].

19       Gobernacion, by means of an official letter, requested the presence of EDM’s legal  
20 representatives at a hearing on July 10, 2001. The official notice, executed by Aguilar Coronado, the  
21 new Director General of Gobernacion, requested the company’s legal representative to present all  
22 necessary proof and evidence concerning the machines installed in the facilities at Matamoros and  
23 Nuevo Laredo. The notice specifically stated that Guadalupe Vargas would be present at the meeting  
24 assisting Gobernacion in the process. In fact, he presided over the meeting. [*Watson, para.34; Velasco,*  
25 *para. 17; Ex. 68*].

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26 <sup>10</sup>There is no evidence that Guadalupe Vargas had the requisite experience or knowledge to even distinguish between skill  
27 machines and slot machines. In its document request, claimant requested production of “All documents relating to the  
28 qualifications and training of Jose Guadalupe Vargas Barrera in 2001 concerning the use, operation and legality of “skill  
machines” and/or slot machines in Mexico.” No documents were produced by Mexico. [*Crosby, paras.3,4; Exs. 78, 79*]

<sup>11</sup>This pattern of actively misrepresenting the text of Gobernacion’s official opinion letter was present in the subsequent  
administrative hearing and the findings arising therefrom. That pattern continued in post-seizure comments by Mr. Cabeza  
de Vaca, head of the Gobernacion’s legal department. After the seizures, de Vaca stated that the author of the opinion letter  
had, in a formal statement, disavowed the meaning Thunderbird had placed upon it. de Vaca would not provide the alleged  
statement at the time. [*Watson, para. 57*]. Thunderbird requested production of the alleged statement in these proceedings.  
Nothing was produced. [*Crosby, paras.3,4; Exs. 77, 78*]



1 At about the same time, representatives of Thunderbird and its EDM entity were noticed by the  
2 Attorney General (“PRG”) in Matamoros to appear and address a pending criminal investigation  
3 resulting from an earlier inspection of the Matamoros site. Carlos Gomez, a lawyer retained by  
4 Thunderbird, together with a Baker & McKenzie lawyer, met with the prosecutors. The prosecutors  
5 proposed to select an expert who would inspect the Matamoros machines and determine if there was  
6 an element of skill in their operation. The prosecutors selected an expert who analyzed the machines  
7 in Matamoros. That expert made a sworn report to the PGR that the Matamoros machines were indeed  
8 skill machines and not games of chance. The criminal investigation was concluded. Thunderbird felt  
9 the expert report and the investigation would have precedential effect in the upcoming administrative  
10 proceeding. Thunderbird and EDM prepared for the July 10 administrative hearing. *[Watson, para.*  
11 *33; Gomez, para. 21-22; Mitchell, para 19].*

12 Shortly before that hearing, Thunderbird representatives met with the new Director General  
13 Gobernacion, Umberto Aguilar Coronado. He had replaced Orozco Aceves. Aguilar Coronado received  
14 the Thunderbird representatives in the same office where they had previously met with Orozco Aceves.  
15 The Thunderbird representatives explained who they were and the nature of their operations. Aguilar  
16 Coronado stated that Thunderbird and its Mexican entities were “the good guys”, the only ones who had  
17 sought permission for their skill machine activities. Aguilar Coronado promised to set up a procedure  
18 to get the problems out in the open and resolved. After that meeting, the Thunderbird representatives  
19 felt confident that somebody was in charge who clearly understood the situation. *[Watson, para. 35;*  
20 *Mitchell, para. 21].*

21 Thunderbird prepared for the administrative hearing. It obtained and prepared the following  
22 evidence in booklet form for presentation to Gobernacion *[Watson, para. 36, 37; Atallah, para. 50; ;*  
23 *Velasco, para. 18; Montano, para. 16; Ex. 69].*

24 - The certified expert report obtained at the request of the Procuraduria General de la Republica  
25 (“PGR”) attesting to the operation of the Matamoros machines. *[Ex. 69 a]*. The expert stated as follows:

26 WE CONCLUDE THAT ALL OF THE MACHINES WHICH OPERATE IN THE  
27 BUSINESS “LA MINA DE ORO” LOCATED IN THIS CITY, ONLY INVOLVE  
28 ABILITY AND SKILL, BY REASON OF THE FACT THAT THEIR COMPONENTS  
KNOWN AS “LOGIC BOARDS” (TABLES OR CARDS OF LOGIC) DO NOT  
CONTAIN CIRCUITS WHICH RANDOMLY CONTROL THE RESULTS, that is to

- 1 say they are machines for games of ability and skill.
- 2 - Certification de Equip Nuevo de Conformidad con Norma Oficial Mexicana (“NOMS”). [Ex.
- 3 69 b]. Those official government certifications described the Thunderbird machines as games
- 4 of skill and dexterity.
- 5 - Gobernacion’s official opinion letter concerning the proposed use of “skill machines”. [Ex. 69
- 6 c].
- 7 - The expert declaration of James R. Maida, President of Gaming Laboratories International and
- 8 a world renowned expert on gaming. [Ex. 69 d]. Mr. Maida stated the following:

9 Based upon my review of the law in several jurisdictions a skill game is

10 a game in which the participant may affect the outcome of the game or

11 have the ability to improve the outcome of the game over time. For

12 example, in certain known to me games, the player may engage the game

13 and start the symbols spinning. The player must then use a combination

14 of visual and motor skill dexterity to choose a point to stop each

15 individual column in an attempt to line up a winning combination of

16 symbols for one to eight of the paylines. The Players' decision, based on

17 utilization of his sight, motor skills, and dexterity, is the determinative

18 factor in order to win any prize. Another example of a game know to me

19 is a three or five-column game with one payline. The game requires

20 analytical skill from the player. The player is given five symbols and has

21 the opportunity to lock down (hold) any or all symbols in an attempt to

22 create a winning combination on the payline. When the unlock icon is

23 engaged the columns that are not locked down flip over to a new symbol

24 to complete the game

25 I understand that the Mexico Federal law of Games and Sweepstakes

26 prohibit gambling and luck related games within the Mexican territory

27 but that games involving the user's ability and skill are not prohibited.

28 Skill games which I described herein may require significant decisions

by the player, which affect the result of the game. In addition, players'

will increase their return over time on both of the described games as a

result of their increase of skill.

- 29 - The expert declaration of Carlos Lozano, a consultant to the gaming and lottery industries with
- 30 over twenty years experience. [Ex. 69 e]. Mr. Lozano stated as follows:

31 That with respect to the issue of skill machines, I have a broad

32 background analysis of the meanings and definition of skill machines, as

33 well as technical expertise to make certain that machines which I have

34 analyzed comply with all of the technical requirements in order to meet

35 the definition of skill machines.

36 That although the technical definition of a skill machine may vary

37 slightly from jurisdiction to jurisdiction, the definition which is

38 commonly accepted worldwide is that a skill machine is a machine

1 which allows the player to interact with the machine, to push buttons in  
2 order to make choices and decisions, and which he may thereby affect  
3 the outcome or result more favorably than a slot machine, where no such  
4 decisions are made. Further, a person who plays continually can  
5 generally improve their skill and thus win more often than an unskilled  
6 person.

7 That I have read, in preparation for making this sworn declaration, the  
8 affidavit of James Maida of Gaming Laboratories Inc. and reviewed his  
9 definition of skill machines and skill games. Mr. Maida is, in my  
10 professional opinion, an expert in the field of skill and slot machines and  
11 other games and is recognized all over the world as such. I hereby declare  
12 that I agree with the definition of skill machines contained in his  
13 affidavit and I find it to be true and correct. It does not differ at all from  
14 my own understanding.

15 Further, in preparation for making this sworn declaration, I have visited  
16 the manufacturer site of Summit Amusement & Distributing in Billings  
17 Montana and reviewed similar types of machines as those which were  
18 shipped to Matamoros, and Nuevo Laredo, Tamaulipas, more  
19 specifically identified as under the NOMS attached hereto submitted  
20 herewith and incorporated herein and designated as exhibit B

21 That I have reviewed the technical data relating to said machines, I have  
22 examined and operated the actual machines, and I do hereby certify and  
23 declare that said machines comply with all accepted standards and  
24 definitions of skill machines within the meaning of skill machines for  
25 most jurisdictions in which I have reviewed the applicable law.

26 Further, I have reviewed a synopsis, translated into English, of the  
27 litigation in the Federal Court in the state of Chihuahua (60/99-III/99,  
28 January 4th, 1999), in which the court provides for a general definition  
of skill machines. In that case the proponent presented two machines:  
Sharp Image and BVC Technologies. I find that based on the definition  
provided by the Mexican court, the machines I have examined and which  
are similar to those being operated in Matamoros and Nuevo Laredo fit  
within the definition provided by the Mexican court

In conclusion, it is my professional opinion that all of the machines  
identified in exhibit B of this sworn declaration comply with the  
definitional requirements of a "skill machine" within the meanings given  
in most jurisdictions in which such machines are in use. Other such  
jurisdictions include, or have in the past included, Switzerland, North  
Carolina, Texas, and Oklahoma.

24 - The declaration Albert Atallah, General Counsel to Thunderbird. [ *Ex. 69 ff.* Mr. Atallah stated  
25 as follows:

26 That I am the general corporate counsel for International Thunderbird  
27 Gaming and I therefore deal with legal compliance issues in all of the  
28 jurisdictions in which International Thunderbird Gaming operates or  
conducts gaming activities.

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That I am generally familiar with the regulations governing gaming activities in several states within the United States of America, as well as Latin America, including Mexico.

That International Thunderbird Gaming ("Thunderbird") manages, maintains and operates all of the skill machine operations on behalf of Entertainmens de Mexico, Entertainmens de Mexico de Laredo, and will operate all future locations which other franchisee Entertainmens de Mexico might conduct in the future in other cities in Mexico. Thunderbird is a publicly traded company with our stock traded on the Toronto Stock Exchange (TSE-INB). Thunderbird, as a public company is under obligations to the TSE and various regulators to comply with all disclosure, transparency, accounting and financial regulations and to publish all information about our activities for access by the general public. The names of individual partners, investors and participants is all fully disclosed.

In my capacity as general counsel and in preparation for demonstration to the *Director of Juegos y Sorteos of Gobernacion* and their general counsel, I have researched jurisdictions which permit skill machines, but which do not permit slot machines or other types of gambling activities.

That the best cases in point, as illustrative examples are perhaps Texas (see affidavit of attorney Ramie Griffin in that regard), and North Carolina.

That the state of North Carolina has a law very similar to the *Ley de Juegos y Sorteos* in Mexico, namely, that all games, machines, electronic devices, slot machines or other games of chance are strictly prohibited and to conduct such activities could subject a person doing so to criminal and civil penalties. See exhibit A, attached hereto submitted herewith and incorporated by reference herein, which I certify as a true and correct copy of the General Law of Games and Drawings of North Carolina, provided to me by Westlaw, a legal research tool which is recognized in the United States as the premier method of obtaining accurate infonnation as to statutes and case law.It is clear that this statute, as stated above, prohibits gaming activities, as above, similar to the Law of Mexico

However, see Exhibit B, attached hereto submitted herewith, and incorporated by reference herein, which is the opinion of the North Carolina Attorney General, and which creates an exception for the operation of skill machines. I certify this document as true and correct also as having been obtained through the Westlaw research engine.

Furthermore, it is important to note, in connection with the use and operation of skill machines in North Carolina, the following:

- A) That Mr. James Maida, principal owner and director of Gaming Technology Inc and recognized as the world expert on electronic gaming devices, and the differences between skill and slot machines, testified before the North Carolina Tribal State Compact Certification Commission to assist them in properly defining the difference between a skill and a slot machine. (Please

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note that *Gobernacion* has, as part of the record we have submitted, a sworn declaration of Mr. James Maida as to the meaning and definition of what a skill machine is, and how it is different from a slot machine)

B) That at the present time, as a result of those hearings and the definitional guidelines provided by Mr. Maida, the Cherokee Indian Tribe of North Carolina operates skill machines at their casino located in North Carolina.

In conclusion, your affiant, Albert Atallah believes that North Carolina is a very similar case in point with respect to International Thunderbirds Gaming's operation of skill machines in Mexico, in which the player can interact with the machines, make choices with respect to the game played, and can affect the outcome of the play in accordance with his level of skill. Obviously the distinction between the general prohibition against games of chance and skill games is legally recognized both in Texas and in North Carolina, as well as other jurisdictions which vary only slightly but allow skill machines to operate, or have in the past. These include South Dakota, Oklahoma, and Switzerland.

- The declaration of Ramie H. Griffin addressing the comparative law of Texas re “skill machines” [Ex. 69 g].

- The declaration of Wendy Reeve, an employee of Thunderbird attesting that the “machines currently in operation in Matamoros and Nuevo Laredo have been certified by the Manufacturer as being skill machines and have been approved and certified for their NOMs by the testing lab “Laboratorio De. Laredo S.A. de C.V.” [ Ex. 69 h].

- The declaration of Kevin McDonald, President of Support Consultants, Inc., the manufacturer of the subject machines. [ Ex. 69 I]. McDonald describes in detail the machines and then states

The games described herein require significant decisions by the user which could substantially or greatly affect the result of the games. The games require the used to make independent judgments in the progressive play of the games. Each game is an active game requiring both decisions and active participation by the user as opposed to passive games such as slot machines

Each game described herein involves skill and dexterity  
[Atallah, para. 47, Ex. 69]

In addition to these materials, Kevin McDonald, agreed to appear and provide a laptop-sized machine for demonstration. Francisco Ortiz, the manager of Nuevo Laredo, agreed to appear and demonstrate the machine. [Watson, para. 36, 37; Atallah, para. 50; Velasco, para. 18; McDonald, paras. 15, 16, 19].

1           The hearing took place on July 10, 2001 at the offices of Director de Juegos y Sorteos in Mexico  
2 City. Gobernacion was represented by Guadalupe Vargas and Mr. Alcantara, one of the general counsels  
3 of Gobernacion in charge of the Ampara proceedings. No other representatives of Gobernacion were  
4 present. A stenographer was present. Thunderbird was represented by Peter Watson, Jorge Montoyo,  
5 Mauricio Gauralt, Carlos Gomez and Luis de Ruiz Velasco of Baker & McKenzie. The meeting was  
6 presided over by Guadalupe Vargas, the same individual who had previously closed down the Nuevo  
7 Laredo. *[Watson, para. 38; Velasco, para. 18 ; McDonald, para. 16; Atallah, para. 51, 52; Gomez,*  
8 *para. 23].*

9           Guadalupe Vargas looked at the materials for a matter of seconds. He threw the booklet off to  
10 the corner of the desk and said “this is just a thesis, and means nothing”. Throughout the hearing,  
11 Guadalupe Vargas exhibited a prejudice towards the foreign investment. He was “nasty and  
12 disrespectful” of the Thunderbird representatives. Although the Thunderbird representatives explained  
13 and demonstrated everything possible to Guadalupe Vargas, he, from the beginning of the hearing until  
14 the end, steadfastly represented that the machines were “slot machines” and nothing else. Guadalupe  
15 Vargas had clearly made up his mind long before the hearing and nothing Thunderbird could say would  
16 change his personal opinion regarding the operation of the machines. Gobernacion presented no  
17 evidence at the hearing relating to the operation of the machines, no evidence that the machines were  
18 being operated in a manner different than as represented in the August 3 solicitud, and no evidence  
19 establishing in any respect that the machines were anything other than legally-operating skill machines.  
20 More simply stated, Gobernacion presented no evidence. *[Watson, paras. 38,39, 45; Velasco, para.*  
21 *18; Montano, para. 17; Gomez, para. 24]*

22           Sometime after the hearing, Thunderbird representatives sought and obtained another meeting  
23 with Aguilar Coronado . Aguilar Coronado stated that he felt the administrative hearing would turn out  
24 well. But, he did imply that Guadalupe Vargas had direct connections to the highest levels of the  
25 Mexican government and to President Fox himself. Otherwise, Aguilar Coronado said little about the  
26 way that the matters were being handled by Guadalupe Vargas. *[Watson, para. 40]*

27           Thunderbird representatives also had a meeting with Mr. Cabeza de Vaca, head of the legal  
28 department for Gobernacion. de Vaca said that Thunderbird and its entities had done things right, that

1 they were working through the system, that the administrative decision was his and not that of the  
2 Director de Juegos y Sorteos. de Vaca assured them the decision would be made on a strictly legal  
3 basis, but it was also clear that de Vaca had a very limited understanding of the situation. *[Watson,*  
4 *para. 41]*

5 The summer of 2001 ended with Thunderbird and its entities not knowing exactly where they  
6 stood. They did not know when they would hear anything from the government or whether it would  
7 be favorable. Thunderbird pushed slowly ahead with its plans. It opened Reynosa in August, 2001 and  
8 moved forward with the Puebla and Monterey sites, but slowed down with the other projects. *[Watson,*  
9 *paras. 42,43; Atallah, para. 53, 54]*

10 On October 11, 2001, without prior notice, the Mexican government closed down and seized  
11 the Thunderbird/EDM skill machine operations at Matamoros and Nuevo Laredo. Mr. Alcantaro on  
12 behalf of Gobernacion, appeared at Luis de Ruiz Velasco's office in Mexico City and personally served  
13 him with administrative findings and an order for the closure at Matamoros and Nuevo Laredo. While  
14 the administrative findings and order specifically represented that an appeal could be taken,  
15 Gobernacion acted immediately to shut down and seize the facilities. Within an hour of service of the  
16 administrative findings and order in Mexico City, Guadalupe Vargas, with the assistance of federal and  
17 local police, seized and sealed the Matamoros and Nuevo Laredo facilities. The event was carefully  
18 designed for high publicity. Members of the press were present. The federal and local police who closed  
19 the facilities were armed. Employees of the facilities were arrested and taken away.*[Watson, para.44;*  
20 *Atallah, para. 55; Velasco, para. 19; Sawin, para. 6; Exs. 70, 71, 72; Gomez. Para. 26]*

21 Thunderbird closed the Reynoso facility for a period of time but then re-opened because the  
22 October 10, 2001 administrative order only affected Matamoros and Nuevo De Satero. On January 21,  
23 2002, the Mexican government seized and sealed the Reynosa facility. A video taken at the time of the  
24 closure indicates the public fashion in which the Mexican government acted against the Reynosa facility  
25 and Thunderbird's investments. More than 100 state and local law police appeared at Reynosa. At gun  
26 point, they closed the facility and arrested and arrested many employees.*[Watson, para. 44; Atallah,*  
27 *para. 56; Luz A. Armas Sawin, para. 3; Ex. 77; Sawin, para. 7; Gomez. Para. 27; Ex. 73]*

1 The Matamoros, Nuevo Laredo and Reynosa have remained closed. As of the date of these  
2 closures, Mexico had not sought, obtained or provided a single expert or other evidence to establish that  
3 the machines were not, in fact, skill machines. In fact, the only expert evidence obtained on that point  
4 by Mexico was the analysis obtained by the PGR attesting that the machines were in fact skill machines  
5 and not games of chance<sup>12</sup>. [Ex. 69a] Further, Mexico had not and, to date, has not provided any  
6 evidence that the machines were operating in any manner different than that described in the August  
7 3, 2002 solicitud. All of the actions taken by Gobernacion resulting in seizure of the three facilities were  
8 the result of Guadalupe Vargas' "visual inspection" and subjective opinion. There is no evidence that  
9 Guadalupe Vargas had or has any experience with, or clear understanding of, the operation of skill  
10 machines.

11 **I. The October Administrative Findings and Order.**

12 The administrative findings and order issued on October 10, 2001 under which Mexico seized  
13 the Thunderbird /EDM operations was issued and signed by Umberto Aguilar Coronado, Director  
14 General Secretary of Gobernacion. [Velasco, para. 20; Ex. 70]. While Aguilar Coronado signed  
15 findings and order, he was not present at the hearing. The findings and order were based entirely on the  
16 personal subjective beliefs and understandings of Guadalupe Vargas. [Watson, para. 38; Velasco, para.  
17 18 ; Atallah, para. 52, 52].

18 A significant portion of the administrative findings dealt with exclusion of all of the evidence  
19 provided by Thunderbird/EDM at the July 10 administrative hearing. At the outset of the findings, all  
20 of the evidence was excluded because it was allegedly provided in photostatic copy form as opposed  
21 to original documents.

22 Declarations provided by Thunderbird/EDM were rejected and excluded because they were  
23 offered in English and because they were offered by employees of Thunderbird. Thunderbird  
24 representatives had supplied the report obtained by the Attorney General of Mexico attesting that the  
25 machines operated at Matamoros were skill machines. [Ex. 69a]. The administrative findings addressed  
26 this report by stating it was not exactly the expert testimony of the Attorney General of the Republic

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28 <sup>12</sup>That report, obtained by an agency of the Mexican government itself, was summarily rejected as evidence in the October 10, 2002 administrative findings and order.



1 but rather an expert opinion requested by the Attorney General. It was therefore a private document and  
2 not a public document. The findings concluded that because it was a private document and not a public  
3 document, it had no value as evidence.

4 As to the declaration testimony of experts James Maida and Carlos Lozano, the findings and  
5 order simply noted their expert opinions contained subjective personal evaluations and therefore had  
6 no value.

7 As to Gobernacion's August 15 official letter, the administrative findings and order stated the  
8 following:

9 Public Document DGG/SP/1057/200 of 15<sup>th</sup> August, 2000, signed by the then Director  
10 of Games and Raffles, in the absence of the Director of Games and Raffles, is not an  
11 obstacle to the above, in that the contents of the said document in no way constitute an  
12 authorization for the operation of cash slot machines which are the subject of this  
13 resolution, as in a mistaken way, the company involved in this administrative procedure  
14 is trying to demonstrate.

15 \_\_\_\_\_  
16 The fact does not pass unnoticed by the judge in this case, that the administrative  
17 authorities existing at that time would have stated that:

18 "IN THIS SENSE, IT IS IMPORTANT TO CLARIFY THAT IF THE  
19 MACHINES THAT ARE COMMERCIALY EXPLOITED BY YOUR  
20 PRINCIPLE ARE OPERATED ACCORDING TO THE FORM AND TERMS  
21 STATED BY YOU, THIS ADMINISTRATIVE AUTHORITY IS NOT  
22 COMPETENT TO PROHIBIT THEM, KNOWING THAT IF WE ARE  
23 REFERRING TO MACHINES KNOWN AS 'CASH SLOT MACHINES',  
24 'TOKEN SLOT MACHINES' OR 'SLOT MACHINES', IN WHICH THE  
25 PREDOMINANT FACTOR OF OPERATION IS CHANCE AND THE  
26 PLACING OF BETS, AND NOT ABILITY AND SKILL, AS YOU STATE,  
27 SOME OF THE PROVISIONS ESTABLISHED BY FEDERAL LAW COULD  
28 BE INVOKED, WITH THE LEGAL CONSEQUENCES SET OUT IN  
ARTICLE 8 OF THE SAID LAW."

It is stated that such assertions do not constitute any type of permit, because present in  
the drafting is the conditional word "if" which logically requires in addition the presence  
of a determining situation or fact, which necessarily and without doubt must be adjusted  
to the terms of the condition proposed, which will never be interpreted as a permit, and  
most important of all in the said paragraph, the authority makes reference to the possible  
violation of the Federal Law on Gaming and Lottery.

For a better understanding of what is explained here, looking again at what is stated in  
the Document referred to, it is worth reviewing the following syllogisms

*If the machines operated by Entertainments de Mexico are not for chance or for  
purposes of gaming, they remain outside the competency of this administrative  
authority.*

1 To the contrary;

2 *If the machines operated by Entertainments de Mexico are for chance or for purposes*  
3 *of gaming, they remain within the competency of this administrative authority.*

4 Here it is clear that there is no implicit permission, and on the contrary, this only opens  
5 two possibilities as to the functioning of the machines, and consequently, two possible  
ways of exercising the administrative function (to act within its competency, or to  
refrain from acting, for lack of competency).

6 The foregoing explanation is corroborated in the same Document, in which is stated that  
7 “THIS GENERAL DIRECTORATE OF THE INTERIOR, IN CONFORMITY WITH  
8 THE ATTRIBUTES PREVIOUSLY CONFERRED TO THAT EFFECT, ORDER  
9 THAT IN THE OPERATION OF THE MACHINES THERE MUST NOT BE  
INTRODUCED THE CHARACTERISTICS OF CHANCE OR BETTING WHICH  
ORDER HAS NO EFFECT IF THEY ARE VIDEO GAME MACHINES OPERATED  
IN ACCORDANCE WITH THE CONCEPTS OF ABILITY AND SKILL.”

10 *[English Translation][Velasco, para. 20; Ex. 69].*

11 The administrative findings and order do not mention nor discuss the determinative paragraph  
12 in the August 15 letter which provides as follows:

13 “According to the above-mentioned, the provisions established under the federal laws  
14 of gaming and sweepstakes are enforceable legal dispositions that specifically prohibit  
15 gambling and luck related games within the Mexican territory; **notwithstanding the**  
16 **above-mentioned, according to your statement, the machines that your**  
17 **representatives operate are recreational video game devises for purposes of**  
18 **enjoyment and entertainment of its users with the possibility of obtaining a prize**  
19 **without the intervention of luck or gambling, but rather the users ability and**  
20 **skillfulness.”**

21 *[English Translation][Ex. 17; Velasco, para. 7; Watson, para. 16; Atallah, para. 16.]*

22 Further, there is no evidence cited in the administrative findings and order that the machines were any  
23 different than those specifically identified in, or operated in any manner different from that described  
24 in, the original August 3 solicitud in response to which the August 15 official opinion letter was issued.

#### 25 **J. Post-Seizure Activities**

26 Thunderbird, through its Mexican EDM entities, appealed the closure of the facilities as well  
27 as the order issued by Gobernacion through “amparos” in the courts of Reynosa and Matamoros and  
28 an appeal before the tax courts in Mexico City. The amparos were successful at the courts of first  
instance, but were denied at the “Colegiado” level. During the amparo process in Matamoros and  
Reynosa, government lawyers had lengthy ex-parte sessions with judges in charge of the cases without  
the presence of Thunderbird lawyers. The tax court appeal of the administrative order was also

1 unsuccessful. *[Watson, para. 49; Velasco, paras. 21, 22, 23]*

2 While the various legal claims were in process, Thunderbird’s representatives had several  
3 meetings with Cabeza de Vaca, the head of the legal department of Gobernacion, Umberto Aguilar the  
4 new Director General of Gobernacion and Arturo Chavez Chavez, the Internal Controller of  
5 Gobernacion. In those meetings, Thunderbird representatives were advised that Gobernacion would  
6 reconsider its position with respect to the closures but nothing ever occurred. Thunderbird  
7 representatives were repeatedly told that Mexico would agree to submit the machines to independent  
8 analysis and that if they were determined to be skill machines, the facilities could be re-opened. That  
9 analysis never took place. *[Watson, paras. 55, 56, 57]*

10 Thunderbird representatives met with Guillermo Flores, the individual in charge of creating a  
11 new gaming law in Mexico. He was a private citizen but Thunderbird understood he was a very good  
12 friend and the former campaign manager of Martin Huerta, the second in command at Gobernacion  
13 (Aguilar is third). Flores acknowledged Gobernacion’s opinion letter. He proposed that he would act  
14 as liaison, or conciliator, between Thunderbird and Gobernacion. He said he didn't see a reason why  
15 it could not be worked out amicably. Thunderbird/EDM were not, after all, “fly by night money  
16 launderers”. Thunderbird was “a public company and very transparent”. Nothing happened. *[Watson,*  
17 *para. 57]*

18 Simultaneously with these proceedings, Guardia obtained a federal decision upholding his right  
19 to operate skill machines. Thunderbird/EDM representatives met again with de Vaca to obtain an  
20 explanation of the disparate, discriminatory treatment received by the Thunderbird/EDM operations.  
21 de Vaca’s response was that Gobernacion believed the legal resolutions in favor of Guardia were wrong  
22 and that he would take a closer look at the matter. Nothing happened. Guardia’s skill machine facilities  
23 remain open and in operation. *[Watson, para. 56; Velasco, para. 25]*

24 In one meeting, de Vaca also stated that Gobernacion had interviewed Antunano, the former  
25 director of Juegos y Sorteos who had signed the opinion letter on behalf of Gobernacion. de Vaca stated  
26 that Antunano had provided them with a written statement indicating that what he had intended by the  
27 letter was not what Thunderbird had “inferred” from it. Thunderbird representatives were not allowed  
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1 to see the claimed statement. It has never been produced<sup>13</sup> [Watson, para. 57]

2 Jorge Montano, a career diplomat, served as Mexico's Ambassador to both the United Nations  
3 and the United States. In both capacities, he served on Mexico's NAFTA negotiating team. Concerning  
4 Mexico's treatment of Thunderbird's investment enterprises, Mr. Montano states that Mexico  
5 government acted "in "bad faith, clearly discriminating against foreign investment" and "completely  
6 disregarded NAFTA obligations". [Monatno, paras. 21, 22]

7 On March 21, 2002, Thunderbird initiated the present proceedings by serving Mexico with its  
8 "Notice of Intent to Submit Claim to Arbitration Under Section B of Chapter 11 of the North American  
9 Free Trade Agreement".

10 **K. Thunderbird's Investment Enterprises Pre- and Post-Seizure.**

11 **Matamoros**

12 At the time of seizure and closure on October 11, 2001, Matamoros was operating 80 video  
13 skill gaming machines. [Copeland, para. 12 ; Ex. 88 (Section II)]. Those machines had been generating  
14 significant revenues. Net wins (drops into the machines less prizes paid in U.S. dollars) for its initial  
15 months of operation were as follows:

16 August, 2000 - \$18,456.69  
17 September, 2000 - \$32,403.80  
18 October, 2000 - \$82,111.50  
19 November, 2000 - \$105,037.85  
20 December, 2000 - \$129,469.91  
21 January, 2001 - \$153,720.60  
22 February, 2001 - \$153,602.30  
23 March, 2001 - \$153,975.80

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25 <sup>13</sup>In its document request, claimant requested production of "All documents relating to meetings or discussions between  
26 Cabeza de Vaca and Rafael de Antunano Sandoval concerning the August, 15, 2000 letter issued by Rafael de Antunano  
27 Sandoval, Director de Juegos y Sorteos, in the representation of Sergio Orozco Arceves, Director General of Gobernacion,  
28 concerning the use and operation of skill machines in Mexico by Claimant" and "Any statements or correspondence provided  
by Rafael de Antunano Sandoval concerning the August, 15, 2000 letter issued by Rafael de Antunano Sandoval, Director  
de Juegos y Sorteos, in the representation of Sergio Orozco Arceves, Director General of Gobernacion, concerning the use  
and operation of skill machines in Mexico by Claimant." No documents were produced by Mexico. [Crosby, paras. 3,4;  
Exs. 78,79]

1 April, 2001 - \$148,994.70  
2 May, 2001 - \$154,968.40  
3 June, 2001 - \$148,074.55  
4 July, 2001 - \$119,299.70  
5 August, 2001 - \$227,038.60  
6 September, 2001 - \$158,619.30  
7 October, 2001 - \$48,027 (Open 10 days before closure on October 11, 2001)  
8 *[Copeland, para 12; Ex. 88]*

9 Matamoros has been closed and purportedly sealed since October 11, 2001 with Thunderbird/EDM's  
10 80 machines skill machines inside.<sup>14</sup> Thunderbird has sought and been denied access to the facilities<sup>15</sup>.  
11 Mexico divulged in these proceedings that Matamoros has apparently been looted. The facility now sits  
12 "without seals of closure and largely empty."*[English Translation] [Crosby, para. 5; Exs. 81, 82]*

13 **Nuevo Laredo**

14 At the time of seizure and closure on October 11, 2001 , Nuevo Laredo was operating 128 video  
15 skill gaming machines. *[Copeland, para.12; Ex. 88 (Section II)]* Those machines had been generating  
16 significant revenues. Net wins (drops into the machines less prizes paid in U.S. dollars) for its months  
17 of operation were as follows:

18 February, 2001 - \$23,8943.50  
19 March, 2001 - \$22,576.45  
20 April, 2001 - \$48,148.25  
21 May, 2001 - \$68,437.80  
22 June, 2001 - \$106,373.25  
23 July, 2001 - \$189,432.80  
24 August, 2001 - \$277,241.70

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26 <sup>14</sup>There is no dispute that machines were present and operating at the Matamoros, Nuevo Laredo and reynosa locations at  
27 the time of seizure by Mexico. Closure documents produced by mexico identify the mchanies present by serial number. *[Exs.*  
28 *71, 72, 73]*

<sup>15</sup>Thunderbird sought access through an Article 1134 motion for Interim Protective Measure in these proceedings. Mexico  
opposed that motion. *[Crosby, para. 5; Exs. 81, 82]*

1                   September, 2001 - \$336,735.00  
2                   October, 2001 - \$110,156.00 (Open 10 days before closure on October 11, 2001)  
3                   *[Copeland, para. 12; Ex. 88]*

4                   Nuevo Laredo has been closed and purportedly sealed since October 11, 2001 with  
5 Thunderbird/EDM's 128 machines skill machines inside. Thunderbird has sought and been denied  
6 access to the facilities. Mexico divulged in these proceedings that Nuevo Laredo has also been looted.  
7 The facility now also sits "without seals of closure and largely empty." *[English Translation] [Crosby,*  
8 *para. 5; Exs. 81, 82]*

9                   **Reynosa**

10                   At the time of seizure and closure on January 28, 2002, Nuevo Laredo was operating 80 video  
11 skill gaming machines. *[Atallah, para. ; Copeland, para.12; Ex. 88 (Section II)]* Those machines had  
12 been generating significant revenues. Net wins (drops into the machines less prizes paid in U.S. dollars)  
13 for its months of operation were as follows:

14                   August, 2001 - \$6,439.60  
15                   September, 2001 - \$103,026.15  
16                   October, 2001 - \$128,066.50  
17                   November, 2001 - \$185,653.50  
18                   January, 2002 - \$122,352.60 (Open only 10 days)  
19                   February, 2002 - \$23,843.50 (Month of closure)  
20                   *[Copeland, para. 12; Ex. 88]*

21                   Reynosa has been closed and purportedly sealed since January 28, 2002 with  
22 Thunderbird/EDM's 80 machines skill machines inside. Thunderbird has sought and been denied access  
23 to the facilities. The Reynosa apparently remains closed with seals intact. *[English Translation]*  
24 *[Crosby, para.5; Exs. 81, 82]*

25                   **Puebla, Monterey and Juarez.**

26                   \_\_\_\_\_Thunderbird had formed EDM entities for proposed facilities in each of these location and had  
27 made considerable progress towards opening operations. Due to Mexico's seizure and closure of three  
28 operating facilities, Puebla, Monterey and Juarez never opened..

1           **L. Guardia and Other Skill Machine Operators Presently Operating in Mexico**

2           Thunderbird was originally attracted to skill game operations in Mexico due to the success of  
3 Guardia’s skill machine facilities. Guardia was operating skill machine facilities at several locations in  
4 Mexico. These operations had withstood legal challenge by Gobernacion and were legally operating  
5 under existing Mexican law. *[Watson, para. 4, 7, 57; Velasco, para. 25; Montano, para.19; Luz A.*  
6 *Armas Sawin, para. 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres; Gomez, paras. 28-30. 72-73;*  
7 *Exs. 82-85, 94]*<sup>16</sup>

8           Throughout Thunderbird’s initial development and operation of its EDM Enterprises, throughout  
9 the period of seizures and legal challenges; throughout the present NAFTA proceedings, and up to the  
10 present, Guardia continued, and still continues, to operate his skill machine facilities in Mexico. He  
11 has done so in a very public fashion. Thunderbird witnesses played skill machines that Guardia facilities  
12 several years ago, several months ago, and several weeks ago. Several weeks before this filing, a  
13 Thunderbird witness also observed the operation of skill machines at a facility operated by another  
14 Mexican national in Rio Bravo, Tamaulipas, Mexico. *[Watson, para. 4, 7, 57; Velasco, para. 25;*  
15 *Montano, para.19; Luz A. Armas Sawin, para. 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres;*  
16 *Gomez, paras. 28-30, 72-73; Ex. 82-85, 94]*

17           In post-seizure discussions with Cabeza de Vaca, Thunderbird’s representatives pointed out that  
18 Guardia had obtained a favorable court decision allowing the operation of skill machines. A demand  
19 and an explanation as to the discriminatory treatment being accorded to Thunderbird’s investment  
20 enterprises in light of Guardia’s open and legally operating skill machine facilities. DeVaca stated  
21 Gobernacion felt the legal resolutions in favor of Guardia were against the law and that they would take  
22 “a closer look at this matter”. Guardia’s skill machine facilities remain open and operating to date.  
23 *[Velasco, para. 26]*

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<sup>16</sup>The legality of Guardia’s operations was in fact conceded by a high government official in post-seizure conversation with Peter Watson. *[Watson, para. 16]*

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**III.**

**INTERPRETATION AND GOVERNING PRINCIPLES OF NAFTA CHAPTER 11.**

NAFTA Article 1131 provides that Tribunals established to hear investor’s claims under Chapter 11 “shall decide the issues in dispute in accordance with [the NAFTA] and the applicable rules of international law.” Numerous tribunals have thus far concluded that, in terms of interpreting the NAFTA text, the applicable rules of international law are the customary international law rules of treaty interpretation.<sup>17</sup>

The customary international law rules of treaty interpretation have been codified in Article 31 of the *Vienna Convention on the Law of Treaties*, which states

1. A treaty shall 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.
2. The context for the purpose of the interpretation of a treaty shall comprise in addition to the text, including its preamble and annexes:
  - a) Any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;
  - b) Any instrument which was made by one of more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.
3. There shall be taken into account, together with the context:
  - a) Any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;
  - b) Any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;
  - c) Any relevant rules of international law applicable in the relations between the parties;
4. A special meaning shall be given to a term if it is established that the parties so intended.

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<sup>17</sup>23 May 1969, 1155 U.N.T.S. 331; 8 (1969) ILM 679 [TAB 1]. See, e.g. *United States – Standards for Reformulated Gasoline*, WT/DS2/AB/R, 20 May 1996, at 15 [TAB 2]; *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, 4 October 1996, at 9-12 [TAB 3]; and *Mondev International Ltd. v. U.S.A.*, ICSID No. ARB(AF)/99/2, Final Award, 11 October 2002, at para. 43 (www.naftalaw.org) [TAB 4]; *S.D. Myers, Inc. v. Canada*, NAFTA/UNCITRAL Tribunal, Award on the Merits, 13 November 2000, at para’s. 196-200 (www.naftalaw.org) [TAB 5]; or *Ethyl Corp. v. Canada*, NAFTA/UNCITRAL Tribunal, Award on Jurisdiction, 24 June 1998, at para’s. 25-29 (www.naftalaw.org) [TAB 6].



1 Article 31(1) of the *Vienna Convention* provides the golden rule of treaty interpretation. It  
2 requires a tribunal to focus upon the plain meaning of the text before it, while being mindful not only  
3 of its placement within the context of the treaty but also of the objects and purposes of that treaty. The  
4 textual focus will naturally predominate where the object and purposes of a treaty are not explicitly  
5 provided. This is not the case for the NAFTA, however, which provides tribunals with considerable  
6 guidance in this regard. The NAFTA provides both a list of its objectives and a prescription for how  
7 its text must be interpreted. Article 102 states:

- 8 1. The objectives of this Agreement, as elaborated more specifically through its  
9 principles and rules, including national treatment, most-favored-nation treatment  
10 and transparency, are to:
  - 11 (a) eliminate barriers to trade in, and facilitate the cross-border movement  
12 of, goods and services between the territories of the Parties;
  - 13 (b) promote conditions of fair competition in the free trade area;
  - 14 (c) increase substantially investment opportunities in the territories of the  
15 Parties;
  - 16 (d) provide adequate and effective protection and enforcement of intellectual  
17 property rights in each Party's territory;
  - 18 (e) create effective procedures for the implementation and application of this  
19 Agreement, for its joint administration and for the resolution of disputes;  
20 and
  - 21 (f) establish a framework for further trilateral, regional and multilateral  
22 cooperation to expand and enhance the benefits of this Agreement.
- 23 2. The Parties shall interpret and apply the provisions of this Agreement in the light  
24 of its objectives set out in paragraph 1 and in accordance with applicable rules  
25 of international law.

26 The first panel established to hear a NAFTA dispute noted Article 102 in concluding as follows:

27 The Panel also attaches importance to the trade liberalization background against which  
28 the agreements under consideration must be interpreted. Moreover, as a free trade  
agreement, the NAFTA has the specific objective of eliminating barriers to trade among  
the three contracting Parties. The principles and rules through which the objectives of  
the NAFTA are elaborated are identified in NAFTA Article 102(1) as including national  
treatment, most-favored nation treatment and transparency. Any interpretation adopted  
by the Panel must, therefore, promote rather than inhibit the NAFTA's objectives.<sup>18</sup>

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<sup>18</sup>Canada – Tariffs on Certain US - Origin Agricultural Products, CDA-95-2008-01, 2 December 1996, at 36. This was an  
arbitration panel established pursuant to NAFTA Article 2008 (<http://www.nafta-sec-alena.org/images/pdf/cb95010e.pdf>)  
[TAB 7].

1 This approach was echoed by the Tribunal in *Metalclad Corp. v. Mexico*, where the Tribunal  
2 noted in its Award that the principle of transparency and the objective of substantially increasing  
3 investment opportunities in the North American Free Trade Area were both important elements of its  
4 interpretative analysis.<sup>19</sup>

5 Article 102(1) is very specific in the manner in which it lays out the appropriate context for  
6 interpretation of the NAFTA text. It not only set out the goals of substantially increasing investment  
7 opportunities and promoting “conditions of fair competition” in the free trade area. It also provides that  
8 these objectives are “elaborated more specifically through its principles and rules,” which include:  
9 national treatment; most favored nation treatment; and transparency.

10 These three “principles and rules” represent the bedrock standards and principles of international  
11 economic law, which can be found within countless treaty provisions and throughout the burgeoning  
12 jurisprudence of international tribunals, such as the dispute settlement bodies of the World Trade  
13 Organization and other Chapters of the NAFTA. It is accordingly appropriate for a tribunal to have  
14 recourse to other trade and investment treaties, as well as the wider jurisprudence of international  
15 economic law, in interpreting the NAFTA text in a manner that is consonant with its broadly  
16 liberalizing objectives.

17 The Metalclad Tribunal also noted how the Parties agreed to “ENSURE a predictable  
18 commercial framework for business planning and investment” in the preamble of the NAFTA. As the  
19 Tribunal in *S.D. Myers, Inc. v. Canada* stated, the preambular language of a treaty shall be construed  
20 as part of the context in which the treaty text is situated.

21 Accordingly, as demonstrated in its preamble, the drafters of the NAFTA clearly designed an  
22 agreement which would permit the Parties to create a truly liberalized free trade and investment zone.  
23 The substantive protections granted to individual investors under NAFTA Chapter 11 operate as a  
24 bulwark against those who would attempt to weaken or subvert those goals. The only interpretation of  
25 the plain meaning of the NAFTA text which would be in accordance with the international law principle  
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28 <sup>19</sup>*Metalclad Corp. v. Mexico*, Final Award, NAFTA/UNCITRAL Tribunal, 2 September 2000, at para’s. 70-71  
(www.naftalaw.org) [TAB 8].

1 that treaties must be interpreted in good faith<sup>20</sup> is one that maximizes the liberalizing objectives  
2 contained therein.

3 **IV.**

4 **THUNDERBIRD'S CLAIM MEETS THE REQUIREMENTS OF NAFTA CHAPTER 11.**

5 **A. NAFTA Articles 1001 and 1117.**

6 Articles 1101 and 1117 are the pertinent jurisdiction-granting provisions of the NAFTA. Those  
7 articles provide, in pertinent part, as follows

8 Article 1101: Scope and Coverage

- 9 1. This Chapter applies to measures adopted or maintained by a Party  
10 relating to:
- 11 (a) investors of another Party;
  - 12 (b) investments of investors of another Party in the territory of the  
13 Party; and
  - 14 (c) with respect to Articles 1106 and 1114, all investments in the  
15 territory of the Party.

16 Article 1117: Claim by an Investor of a Party on Behalf of an Enterprise

- 17 1. An investor of a Party, on behalf of an enterprise of another Party  
18 that is a juridical person that the investor owns or controls  
19 directly or indirectly, may submit to arbitration under this  
20 Section a claim that the other Party has breached an obligation  
21 under:
- 22 (a) Section A or Article 1503(2) (State Enterprises), or
  - 23 (b) Article 1502(3)(a) (Monopolies and State Enterprises) where the  
24 monopoly has acted in a manner inconsistent with the Party's  
25 obligations under Section A, and that the enterprise has incurred  
26 loss or damage by reason of, or arising out of, that breach.2. An  
27 investor may not make a claim on behalf of an enterprise  
28 described in paragraph 1 if more than three years have elapsed  
from the date on which the enterprise first acquired, or should  
have first acquired, knowledge of the alleged breach and  
knowledge that the enterprise has incurred loss or damage.
- .....
4. An investment may not make a claim under this Section.

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<sup>20</sup> A.D. McNair, *The Law of Treaties* (Oxford: Clarendon Press, 1986) at 465 [TAB 9].

1           **B. Thunderbird is an Investor of a Party under Article 1117.**

2           Only an “investor of a Party” may bring a claim under NAFTA Article 1117. NAFTA Article  
3 1139 states that “investor of a Party means a Party or state enterprise thereof, or a national or an  
4 enterprise of such Party, that seeks to make, is making or has made an investment.” As a Canadian-  
5 incorporated company, Thunderbird is an enterprise of a NAFTA Party which made, and sought to make  
6 further, investments in the territory of Mexico. [ *Velasco, paras. 1-3, 9-14; Atallah, paras. 4, 5, 8, 9,*  
7 *11-13, 15-42; Mitchell, paras. 8-11, 15; Ex. 1; Watson, paras. 3, 5, 8-10, 17-19, 21-24, 29-32, 46,*  
8 *47.*

8           **C. Thunderbird May Proceed Under Article 1117.**

9           Under Article 1117, a claim can only be made by a NAFTA Investor in respect of the investment  
10 enterprise owned or controlled by an investor of a NAFTA Party. The Matamoros, Nuevo Laredo and  
11 Reynosa investment enterprises were all owned, in part, and controlled, completely, by Thunderbird.  
12 [*Atallah, paras. 15 -42; Exs. 11-14, 27-29, 31, 34-35, 37, 39, 42-45, 48-50, 52-53, 55-57*]

13           **D. Thunderbird’s Claims Involve Measures Adopted or Maintained by Mexico.**

14           NAFTA Article 1101 provides that Chapter 11 applies to measures adopted or maintained by  
15 a party relating to investors of another Party or investments of investors of another Party in the territory  
16 of the Party. NAFTA Article 201 defines “measure” as including “any law, regulation, procedure,  
17 requirement or practice.” The measures in this case include the following:

- 18           (I) The armed seizure, and subsequent closure, of the Matamoros, Nuevo Laredo  
19 facilities under the order of Mr. Barrera;
- 20           (ii) Guadalupe Vargas’ campaign to hinder, and ultimately destroy, Thunderbird’s  
21 business activities in Mexico, including the holding of an arbitrary and  
22 discriminatory administrative hearing resulting in a decision wholly unsupported  
23 by the evidence on the record;
- 24           (iii) The assurances made by other GOBERNACION officials that Thunderbird’s  
25 business undertakings were not proscribed under the applicable federal gaming  
26 laws or regulations;
- 27           (iv) The actions of various organs of the Mexican government which have had the  
28 effect of depriving Thunderbird of a fair hearing before Mexican administrative  
and court hearings, while simultaneously permitting its local competitors to  
remain in business; and
- (v) The actions taken, and acquiescence observed, by senior government officials,  
which effectively condoned the actions of Guadalupe Vargas and the unfair and  
inequitable treatment provided to Thunderbird and its investments.

1 In order for measures to be considered as *relating to* investors or their investments, it is  
2 necessary for a relationship of sufficient proximity to exist between the measures and the investor or  
3 its investments. The Tribunal in *Methanex Corp. v. U.S.A.* referred to this relationship of proximity as  
4 “legally significant connection” between the measure and the investor or its investments.<sup>21</sup>

5 Where a measure is aimed directly at the investor or investment, or if the measure can be seen  
6 as connected to the investment activities of the investor or its competitors, there is no controversy as  
7 to whether it relates to the investor or its investment<sup>22</sup>. In the present case, all of the measures in  
8 question either relate directly to the investor and its investments, or can be seen as connected to the  
9 business of Thunderbird and/or its competitors.

10 **E. Thunderbird Suffered Losses Arising from Mexico’s Treaty Breaches**

11 It is also necessary for an investor to have suffered a loss arising out of the treatment that it or  
12 its investment received that breached one of the relevant NAFTA provisions. As will be described in  
13 more detail below, the Investor has suffered considerable losses for which it is presently seeking relief.

14 **F. Thunderbird Brought Its Claims Within the Required Three Year Period.**

15 Finally, Articles 1116 and 1117 require that claims be brought in respect of breaches of the  
16 relevant NAFTA provisions by no later than three years after “the date on which the investor first  
17 acquired, or should have first acquired, knowledge of the alleged breach and knowledge that the  
18 investor has incurred loss or damage.” The measures at issue in this arbitration were first imposed in  
19 2001 and maintained thereafter. The investor launched this arbitration with the delivery of its Notice  
20 of Arbitration and Statement of Claim on August 1, 2002. Accordingly, the Investor launched its claim  
21 within the appropriate period of time required under the NAFTA.

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26 <sup>21</sup>*Methanex Corp. v. United States of America*, NAFTA/UNCITRAL Tribunal, Award on Competence and Jurisdiction, 7  
27 August 2002, at para. 147 [TAB 10].

28 <sup>22</sup>See, e.g., *Myers Merits Award*, at para’s. 233-236 [TAB 5].

V.

**MEXICO BREACHED THE “NATIONAL TREATMENT” STANDARD UNDER NAFTA  
ARTICLE 1102 IN ITS DESTRUCTION OF THE THUNDERBIRD INVESTMENTS.**

**A. Article 1102 and the “National Treatment” Standard**

**1. Article 1102**

Without justification, Mexico has accorded different treatment to the Investor and its investments than that which has been provided to domestic investors and investments operating in like circumstances. Such conduct constitutes a *prima facie* breach of the national treatment standard, which is found in NAFTA Article 1102. Article 1102 provides, in relevant part:

1. Each Party shall accord to investors of another Party treatment no less favorable than that it accords, in like circumstances, to its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
2. Each Party shall accord to investments of investors of another Party treatment no less favorable than that it accords, in like circumstances, to investments of its own investors with respect to the establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments.
3. The treatment accorded by a Party under paragraphs 1 and 2 means, with respect to a state or province, treatment no less favorable than the most favorable treatment accorded, in like circumstances, by that state or province to investors, and to investments of investors, of the Party of which it forms a part.

**2. The “National Treatment” Standard.**

NAFTA Article 102(1) provides that “national treatment” is one of the “principles and rules” of the Agreement which must be used to “elaborate” the objectives of the NAFTA set out in Article 102(1). Those objectives include “the promotion of conditions of fair competition in the free trade area” and “to increase substantially investment opportunities in the territories of the Parties.” Article 101(2) mandates that any interpretation and application of the NAFTA text must be undertaken “in light of” these objectives.

1 The national treatment standard appears in virtually all of the world's investment protection  
2 treaties.<sup>23</sup> The United Nations Conference on Trade and Development has defined the national treatment  
3 standard in investment treaties as follows:

4 National Treatment can be described as a principle whereby a host country  
5 extends to foreign investors treatment that is at least as favourable as the  
6 treatment it accords to national investors in like circumstances. In this way the  
national treatment standards seek to ensure a degree of competitive equality  
between national and foreign investors.<sup>24</sup>

7 "National treatment" is also a term which has been used repeatedly throughout the NAFTA,  
8 although never defined. It needs no definition because its *usus loquendi*, i.e. its common use, is well  
9 known among international lawyers. As the *Feldman* Tribunal noted in its recent award concerning the  
10 interpretation of application of NAFTA Article 1102, national treatment is a "fundamental obligation"  
11 of the NAFTA, which bears analogies to its use in other international trade agreements, such as Article  
12 III of *GATT 1947*.<sup>25</sup>

13 The *Pope & Talbot* Tribunal came to a similar conclusion about the over-arching nature of the  
14 national treatment standard, as demonstrated by its extensive analysis of applicable WTO jurisprudence  
15 on the national treatment standard.<sup>26</sup> The *Pope & Talbot* Tribunal has articulated a lucid and  
16 compelling analysis of the application of Article 1102 which has been implicitly observed by every  
17 NAFTA tribunal of panel to date.<sup>27</sup> This analysis be broken into three basic elements:

- 18 - Identification of the relevant subjects of the national treatment comparison;
- 19 - Consideration of the relative treatment received by each comparator; and
- 20 - Consideration of whether factors exist which could justify any difference in  
21 treatment so found.

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23 <sup>23</sup>United Nations Conference on Trade and Development, *National Treatment* (UN Publications, New York: 1999) at 1  
[TAB 11].

24 <sup>24</sup>*Id.*, at 1.

25 <sup>25</sup>*Marvin Feldman v. Mexico*, Final Award, Case No. ARB(AF)/99/1, at para. 165 (www.naftalaw.org) [TAB 12]

26 <sup>26</sup>See, e.g.: *Pope & Talbot, Inc. v. Canada*, NAFTA/UNCITRAL Tribunal, Final Merits Award, 10 April 2001, at para's.  
45-63 (www.naftalaw.org) [TAB 13].

27 <sup>27</sup>See, e.g.: *Pope & Talbot, Inc. v. Canada*, NAFTA/UNCITRAL Tribunal, Final Merits Award, 10 April 2001, at para's.  
45-63 (www.naftalaw.org) [TAB 13].

1           **3.       Identification of Appropriate Comparators.**

2           Article 1102 is a comparative standard. It requires a tribunal to compare the treatment being  
3 received by an investor or investment with that which is being received by the investors or investments  
4 of the host country. The scope for comparison is based upon the treatment in question. For example,  
5 to borrow from the context of a most-favored-nation treatment claim, if an investor under one treaty is  
6 entitled to certain protections not offered in a second treaty, the investor can obtain the benefits of the  
7 second treaty by operation of a MFN treatment clause contained within the first treaty<sup>28</sup>.

8           In cases where the treatment in question is particular to a certain industry, the source of  
9 comparison will naturally be between investors operating within that industry (rather than all investors  
10 in the territory). The basis for any comparison is based upon the likeness of the comparators.

11           The *Pope & Talbot* Tribunal concluded that, “as a first step, the treatment accorded to a foreign  
12 owned investment protected by Article 1102(2) should be compared with that accorded domestic  
13 investments in the same business or economic sector . . .,” although the Tribunal cautioned that this was  
14 but a first step. The Tribunal’s rationale for this first step can be found in the OECD *Declaration on*  
15 *National Treatment for Foreign-Controlled Enterprises*, which provides, in part:

16           As regards the expression “in like situations”, the comparison between foreign-  
17 controlled enterprises established in a Member country and domestic enterprises in that  
18 Member country is valid only if it is made between firms operating in the same sector.<sup>29</sup>

19           While not always noted explicitly, this first step can be seen in the reasons for decision of all  
20 other NAFTA tribunals. For example, in the *Feldman* case, the Tribunal started with a determination  
21 that the “applicable universe” of comparable investors and investments was made up of those businesses  
22 engaged in the purchase and reselling of cigarettes, rather than a wider group which would have  
23 included manufacturers, because the comparison was agreed as between the parties. The measure at

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24           <sup>28</sup>Emilio Agustin Maffezini and *The Kingdom of Spain*, Case No. ARB/97/7, January 25, 2000, *Decision of the Tribunal*  
25 *on Objections to Jurisdiction*, at para. 56 ([http://www.worldbank.org/icsid/cases/emilio\\_DecisiononJurisdiction.pdf](http://www.worldbank.org/icsid/cases/emilio_DecisiononJurisdiction.pdf)) [TAB  
26 14].

27           <sup>29</sup>Organization for Economic Co-operation and Development, *National Treatment for Foreign-Controlled Enterprises*  
28 (OECD, Paris: 1993) at 22 [TAB 15]. Mexico is an OECD Member country. As a consequence of Membership, Mexico  
is obliged to adhere to OECD declarations such as this one, pursuant to Article 5(b) of the 1960 *Convention on the*  
*Organization for Economic Co-operation and Development* [TAB 16].



1 issue in the *Feldman* case was a rebate on export taxes.<sup>30</sup>

2 In *US – Cross Border Trucking Services*, the Panel readily compared any trucking businesses  
3 operating, or desirous of operating, between points in the United States, regardless of business size or  
4 the particular type of service provided.<sup>31</sup> The measure at issue was a prohibition on most Mexican-  
5 owned carriers operating in all but a tiny fraction of the United States market.

6 The *ADF* Tribunal determined that the point of comparison for it under Article 1102(2) was  
7 between steel products held by the investor (a steel fabricator) versus steel products held by domestic  
8 investors, with respect to their potential use in a highway project.<sup>32</sup> By necessary implication, the  
9 Tribunal’s comparison focused on firms operating in the steel fabrication business as its “universe” of  
10 comparable investors under Article 1102(1).

11 And finally, in *S.D. Myers, Inc. v. Canada*, the Tribunal held that the appropriate basis for  
12 comparison – involving a measure which banned the export of PCB wastes from Canada in order to  
13 disadvantage the investor whose destruction facilities were located outside of Canada – was between  
14 the competitors for a share of the Canadian PCB waste destruction market.<sup>33</sup> It did so over the  
15 objections of Canada, which argued that the investor could only compare itself with PCB waste brokers  
16 because it did not completely actually destroy PCB wastes in Canada. This argument was rejected on  
17 the strength of the evidence, which clearly showed that it was Canada’s native PCB waste destruction  
18 firms who were most active in lobbying the Minister to impose an export ban and thereby keep Myers  
19 from entering the Canadian market, rather than any waste brokers (most of whom would welcome the  
20 work that increased competition could have brought).

21 This approach to the comparison required by Article 1102 is also sanctioned under WTO law,  
22 where numerous panels have commented on the goal of the national treatment standard as being to

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24 <sup>30</sup>*Feldman* Award, at para’s. 171-172 [TAB 12].

25 <sup>31</sup>*United States – In the Matter of Cross Border Trucking Services*, 252-257 & 291-294 [TAB 17].

26 <sup>32</sup>*ADF Group Inc. v. U.S.A.*, Final Award, NAFTA/ICSID(AF) Tribunal, Case No. ARB(AF)/00/1, 9 January 2003, at 155  
27 (www.naftalaw.org) [TAB 18].

28 <sup>33</sup>*ADF Group Inc. v. U.S.A.*, Final Award, NAFTA/ICSID(AF) Tribunal, Case No. ARB(AF)/00/1, 9 January 2003, at 155  
(www.naftalaw.org) [TAB 18].

1 promote and protect the conditions of competition as between individual economic actors. The  
2 following excerpts are illustrative of this theme in WTO national treatment jurisprudence:

3 The words “treatment no less favourable” in paragraph 4 call for effective equality of  
4 opportunities for imported products in respect of the application of laws, regulations and  
5 requirements affecting the internal sale, offering for sale, purchase, transportation,  
6 distribution or use of products. This clearly sets a minimum permissible standard as a  
7 basis. . . the purpose of Article III:2, dealing with internal taxes and other internal  
8 charges, is to protect “expectation on the competitive relationship between imported  
9 and domestic products.”<sup>34</sup>

10 The broad and functional purpose of Article III is to avoid protectionism in the  
11 application of internal tax and regulatory measures. . . Toward this end, Article III  
12 obliges members of the WTO to provide equality of competitive conditions for imported  
13 products in relation to domestic products . . . Moreover, it is irrelevant that the “trade  
14 effects” of the tax differential between imported and domestic products, as reflected in  
15 the volumes of imports, are insignificant or even non-existent; Article III protects  
16 expectations not of any particular trade volume but rather of the equal competitive  
17 relationship between imported and domestic products<sup>35</sup>.

18 The “no less favourite treatment obligation” in Article III:4 has been consistently  
19 interpreted as a requirement to ensure effective equality of competitive opportunities  
20 between imported products and domestic products. In this respect, it has been held that,  
21 since a fundamental objective of Article III is the protection of expectations on the  
22 competitive relationship between imported and domestic products, a measure can be  
23 found to be inconsistent with Article III:4 because of its potential discriminatory  
24 impact on imported products. The requirements of Article III:4 is addressed to “relative  
25 competitive opportunities created by the government in the market, not to actual choices  
26 made by enterprises in that market.”<sup>36</sup>

27 The lessons from the WTO jurisprudence are clear – the object of the national treatment  
28 comparison is to safeguard the competitive opportunities of an investor who claims its protection vis-a-  
vis its local competitors. Accordingly, the starting point for any national treatment comparison is to  
ensure that an appropriate “universe” of appropriate comparators is identified – based upon a definition  
which best protects the business activities of the investor in question. This universe can normally be  
drawn from the evidence of the private actors at issue, concerning with whom they believe they are in  
competition.

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34 *United States – Section 337 of the Tariff Act of 1930*, 36 (1989) B.I.S.D. 345 at para’s. 5.11-5.13 [TAB 19].

35 *Japan – Taxes on Alcoholic Beverages*, at 6 [TAB 3].

36 *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/R. WT/DS142/R, 31 January 2000, at para  
10.78 [TAB 20].

1           Where the measure is national in scope, but the nature of the business is either more localized,  
2 or there are more or less than a few easily identifiable competitors, the comparison can be based on an  
3 economic analysis of the industry within which the investor is situated. In other words, it is not  
4 necessary to demonstrate that the comparators are actually in direct competition with each other in any  
5 specific region. The analysis can be accomplished on a sectoral level. As the *Myers* Tribunal noted in  
6 its award:

7           The concept of “like circumstances” invites an examination of whether a non-national  
8 investor complaining of less favourable treatment is in the same “sector” as the national  
9 investor. The Tribunal takes the view that the word “sector” has a wide connotation that  
10 includes the concepts of “economic sector” and “business sector.”

11           From the business perspective, it is clear that SDMI and Myers Canada were in “like  
12 circumstances” with Canadian operators such as Chem-Security and Cintec. They all  
13 were engaged in providing PCB waste remediation services...<sup>37</sup>

#### 14           **4. Treatment No Less Favorable.**

15           The investor and its investment are entitled to the best level of treatment available to *any* other  
16 domestic investor or investment operating in like circumstances. This comparison is not limited to an  
17 evaluation of whether the treatment being received is substantially similar. It focuses on the result of  
18 the treatment being received. As the *Myers* Tribunal noted:

19           Intent is important, but protectionist intent is not necessarily decisive on its own. The  
20 existence of an intent to favour nationals over non-nationals would not give rise to a  
21 breach of [Article 1102] if the measures in question were to produce no adverse effect  
22 on the non-national complainant. The word “treatment” suggests that practical impact  
23 is required to produce a breach of Article 1102, not merely a motive or intent that is a  
24 violation of Chapter 11<sup>38</sup>.

25           A focus on the effects of treatment can also be found in GATT and WTO jurisprudence:

26           On the one hand, contracting parties may apply to imported products different formal  
27 legal requirements if doing so would accord imported products more favourable  
28 treatment. On the other hand, it also has to be recognized that there may be cases where  
application of formally identical provisions would in practice accord less favourable  
treatment to imported products and a contracting party might thus have to apply different  
legal provisions to imported products to ensure that the treatment accorded them is in  
fact no less favourable . . . In such cases, it has to be assessed whether or not such

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27 <sup>37</sup>Myers Merits Award, at para’s 250-251 [TAB 5].

28 <sup>38</sup>Id. at para. 254.

1 differences in the legal provisions applicable do or do not accord to imported products  
2 less favourable treatment.<sup>39</sup>

3 And the *Pope & Talbot* Tribunal has noted:

4 Canada contends that these [various WTO] cases are distinguishable because they  
5 involve *de jure*, rather than *de facto*, discrimination. We have already seen that it is not  
6 always clear whether a measure is a *de jure* or *de facto* case, but even if it were, Canada  
7 has presented no reasons to justify treating the two forms of disadvantage differently.  
8 Indeed, the recognition that national treatment can be denied through *de facto* measures  
9 has always been based on an unwillingness to allow circumvention of that right by  
10 skillful or evasive drafting. Applying Canada's proposed more onerous rules to *de facto*  
11 cases [which would require proof that foreigners, as a group, were proportionately  
12 disadvantaged in application of a measure] could quickly undermine that principle. That  
13 result would be inconsistent with Article 102(1)(b) and ©), to promote conditions of fair  
14 competition and to increase substantially investment opportunities.<sup>40</sup>

15 The test of "treatment no less favorable" is therefore, not a global comparison of treatment  
16 received, on the whole, by groups of domestic or foreign investors or investments. It is particular to the  
17 experience of the claimant. It does not matter if every other foreign investor is receiving treatment  
18 which is effectively identical to that which is provided to all domestic investors. It does not matter if  
19 there are other domestic investors who are also receiving less favourable treatment. The comparison  
20 is between the treatment being received by the claimant and the best treatment being received by a  
21 domestic investor operating in like circumstances. For example, in *United States – Section 337*  
22 interpreted the national treatment standard as follows:

23 The Panel did not consider relevant the fact that many of the state provisions at issue in  
24 this dispute provide the same treatment to products of other states of the United States  
25 as that provided to foreign products. The national treatment provisions require  
26 contracting parties to accord to imported products treatment no less favourable than that  
27 accorded to any like domestic product, whatever the domestic origin. Article III  
28 consequently requires national treatment of imported products no less favourable than  
that accorded to the most-favoured domestic products.<sup>41</sup>

29 Another application of this principle of comparison can be found in the WTO case of *Canada -*  
30 *Certain Automotive Measures*, which involved the application of the MFN treatment obligation.  
31 Canada argued that since its measure provided some luxury cars and some automotive distributors from

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32 <sup>39</sup>U.S. – Section 337, at para's. 5.13-5.14 [TAB 19].

33 <sup>40</sup>*Pope & Talbot* Final Merits Award, at para. 70 [TAB 13].

34 <sup>41</sup>*United States – Measures Affecting Alcoholic Beverages*, Panel Report, DS23/R, 19 June 1992, at para. 5.17 [TAB 23].

1 Japan, the United States and the European Union with the best possible treatment, it was not open to  
2 the European Communities or Japan to complain that other luxury cars and auto-distributors were not  
3 provided with that same quality of treatment. As long as somebody or something from Japan or the  
4 European Communities was receiving the best treatment, Canada reasoned, there could be no finding  
5 of discrimination in favour of anybody, or anything, from those countries. In rejecting this argument,  
6 the Panel determined that by not offering the best treatment available to all goods and all service  
7 providers from Japan or Europe, rather than just a closed list of goods and service providers, Canada  
8 breached its obligations to accord “treatment no less favourable” under both the GATS and GATT.<sup>42</sup>

9 As the *Pope & Talbot* Tribunal noted (in response to Canada’s argument that a single investor  
10 could not possibly claim entitlement to receive the most favorable treatment being received by any  
11 domestic competitor or competitors):

12 Canada has suggested no reason why the NAFTA Parties would have undertaken such  
13 an approach or any evidence of an intention to do so, and the Tribunal can see none.  
14 The Tribunal believes that the language of Article 1102(3) was intended simply to make  
15 clear that the obligation of a state or province to provide investments of foreign  
16 investors with the best treatment it accords *any* investment of its country, not just the  
17 best treatment it accords to investments of *its* investors. Since, as noted, the treatment  
18 of states and provinces in Article 1102(3) is expressly an elucidation of the requirement  
19 placed on the NAFTA Parties by Articles 1102(1) and (2), that interpretation lends  
20 support to the conclusion that, like states and provinces, national governments cannot  
21 comply with [the] NAFTA by according foreign investments less than the most  
22 favourable treatment they accord to their own investments.

23 ... The Tribunal thus concludes that ‘no less favourable ‘ means equivalent to, not better  
24 or worse than, the best treatment accorded to the comparator.<sup>43</sup>

25 It is also unnecessary to prove that the reason for any difference in treatment received by an  
26 investor or its investment was due to its nationality (i.e. its not being domestic). As the *Feldman*  
27 Tribunal has explained:

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28 <sup>42</sup>Canada – Automotive Industry, Panel Report, at para. 10.262 [TAB 20]. The Appellate Body overturned the Panel’s  
finding with respect to service providers as not being based on sufficient evidence that service providers, as opposed to the  
goods they distributed, were actually disadvantaged by the measure. The Appellate Body stressed, however, that it was not  
rejecting the Panel’s “treatment” analysis, only its reliance on insufficient evidence with respect to the GATS violation. See:  
*Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/AB/R & WT/DS142/AB/R, 31 May 2000, at  
para’s. 175-184 [TAB 22]

<sup>43</sup>*Pope & Talbot* Final Merits Award, at para’s. 41 & 42 [TAB 13].

1 It is clear that the concept of national treatment as embodied in [the] NAFTA and  
2 similar agreements is designed to prevent discrimination on the basis of nationality, or  
3 “by reason of nationality” . . . However, it is not self-evident, as the Respondent argues,  
4 that any departure from national treatment must be *explicitly* shown to be a result of the  
investor’s nationality. There is no such language in Article 1102. Rather, Article 1102  
by its terms suggests that it is sufficient to show less favorable treatment for the foreign  
investor than for domestic investors in like circumstances.<sup>44</sup>

5 **5. Like Circumstances**

6 Once a *prima facie* breach of Article 1102 has been proved by the claimant, NAFTA tribunals  
7 have consistently turned, in their analyses, to the question of whether the difference in treatment could  
8 be rationally explained as justifiable in the circumstances.

9 To the Panel in *U.S. Trucking Services*, this third prong of the national treatment test was as a  
10 *de facto* exception – by focusing on the phrase “treatment in like circumstances.” Much like the old  
11 adage about apples and oranges, the Panel wrote that differences in treatment could be justified if the  
12 comparators did not deserve to receive the same treatment. However, the Tribunal cautioned that it’s  
13 “like circumstances exception” must be construed narrowly so as not to strip the national treatment  
14 obligation of any true meaning.<sup>45</sup>

15 While it did not label its analysis under this third prong of the national treatment test as an  
16 “exception,” the *Pope & Talbot* Tribunal came to a similar conclusion:

17 Differences in treatment will presumptively violate Article 1102(2), unless they have a  
18 reasonable nexus to rational government policies that (1) do not distinguish, on their  
19 face or *de facto*, between foreign-owned and domestic companies, and (2) do not  
otherwise unduly undermine the investment liberalizing objectives of [the] NAFTA.

20 In one respect, this approach echoes the suggestion by Canada that Article 1102  
21 prohibits treatment that discriminates on the basis of the foreign investment’s  
22 nationality. The other NAFTA Parties have taken the same position. However, the  
23 Tribunal believes that the approach proposed by the NAFTA Parties would tend to  
24 excuse discrimination that is not facially directed at foreign owned investments. A  
25 formulation focusing on the like circumstances question, on the other hand, will require  
26 addressing *any* difference in treatment, demanding that it be justified by showing that  
27 it bears a reasonable relationship to rational policies not motivated by preference of  
28 domestic or other foreign owned investments. That is, once a difference in treatment  
between a domestic and a foreign-owned investment is discerned, the question becomes,  
are they in like circumstances? It is in answering that question that the issue of

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27 <sup>44</sup>Feldman Award, at 181[TAB 12]

28 <sup>45</sup>United States – Trucking Services, at 258-260 [TAB 17].

1 discrimination may arise.<sup>46</sup>

2 Once the Investor has made out its *prima facie* claim that it has received less favourable  
3 treatment than any of its domestic competitors, it is accordingly for the Respondent to justify such  
4 treatment as reasonable and justifiable in the circumstances. Such an approach is consistent with the  
5 general principles of international law and the applicable rules of evidence in customary international  
6 law. As a Majority of the Tribunal in *Feldman* noted:

7 On the question of burden of proof, the majority finds the following statement of the  
8 international law standard helpful, as stated by the Appellate Body of the WTO:

9 ... various international tribunals, including the International Court of Justice, have  
10 generally and consistently accepted and applied the rule that the party who asserts a fact,  
11 whether the claimant or respondent, is responsible for providing proof thereof. Also, it  
12 is a generally accepted canon of evidence in civil law, common law and, in fact, most  
13 jurisdictions, that the burden of proof rests upon the party, whether complaining or  
14 defending, who asserts the affirmative of a claim or defence. *If that party adduces  
15 evidence sufficient to raise a presumption that what is claimed is true, the burden then  
16 shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the  
17 presumption.* (Emphasis supplied.)

18 Here, the Claimant in our view has established a presumption and a *prima facie* case that  
19 the Claimant has been treated in a different and less favorable manner than several  
20 Mexican owned cigarette resellers, and the Respondent has failed to introduce any  
21 credible evidence into the record to rebut that presumption.<sup>47</sup>

22 The *Feldman* case involved a simple national treatment fact pattern. The investor was denied  
23 tax rebates that were enjoyed by domestic investors whose investments were operating in like  
24 circumstances. The investor was subjected to thorough audits at a time when domestic investors were  
25 left largely unmolested. While Mexico contended that none of the comparators actually should have  
26 received the rebates under the applicable domestic laws, the fact was that the rebates were received.  
27 A Majority of the Tribunal accordingly concluded that this obvious difference in treatment constituted  
28 a *prima facie* breach of Article 1102. It further concluded that Mexico failed to provide any evidence

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25 <sup>46</sup>Pope & Talbot Final Merits Award, at para's. 78-79 [TAB 13].

26 <sup>47</sup>Feldman Award, at 177 [TAB 12]. The accompanying note provides: "*United States – Measures Affecting Imports of  
27 Woven Wool Shirts and Blouses from India*, Adopted 23 May 1997, WT/DS33/AB/R, p. 14. Accordingly, *Asian Agricultural  
28 Products Limited v. Republic of Sri Lanka*, ICSID Reports, pp. 246, 272, 1990. ("In case a party adduces some evidence  
which prima facie supports his allegation, the burden of proof shifts to his opponent.") [See: TABS 23 & 24].

1 which could justify this difference in treatment.<sup>48</sup> The *Feldman* Tribunal also concluded that the audit  
2 activity which solely targeted the investor, rather than being applied evenly to all industry members,  
3 also violated Article 1102.<sup>49</sup>

4 The *Myers* Tribunal noted that the “overall legal context” of the NAFTA can be used to explain  
5 when apparently discriminatory treatment is actually justified under the circumstances.<sup>50</sup> Both the  
6 *Myers* Tribunal and the *US – Trucking* Panel focused on how environmental protection was woven into  
7 the context of the NAFTA to conclude that it could be a factor which could explain differences in  
8 treatment. In neither case, however, did these Tribunals determine that a *bona fide* environmental  
9 policy justification for was proved. For the *Myers* Tribunal, there were clearly less discriminatory  
10 measures available to Canada if it was really motivated by environmental concerns.<sup>51</sup> A similar  
11 conclusion seems implicit in the *US – Trucking* Panel Report.

12 The *Pope & Talbot* Tribunal entered into a thorough analysis of the measures and the  
13 justifications for their imposition before ultimately concluding that they were a reasonable response to  
14 political and economic realities which threatened the investor’s industry as a whole. The measure was  
15 an incredibly complicated export quota regime that allocated entitlement to export lumber – without  
16 the payment of an escalating scale of fees – based upon numerous factors, including the exporter’s  
17 performance in past years. The measure was imposed pursuant to an agreement between the Canadian  
18 and American governments which lifted the threat of US-imposed anti-dumping duties being imposed  
19 against industry members (including the investor).

20 The *Pope & Talbot* Tribunal ultimately determined that while the investor had received less  
21 favourable treatment than other domestic investors, there had always been a good reason for it. For  
22 example, because the investor was not in the process of expanding its facilities at the relevant times,  
23 it was not eligible to receive the portion of quota set aside for “new entrants” under the regime (even

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24 <sup>48</sup>Feldman Award, at para’s. 173-176 [TAB 12].

25 <sup>49</sup> Feldman Award, at para. 174 [TAB 12]. The *Pope & Talbot* Tribunal concluded that similarly selective, and arbitrary,  
26 auditing constituted a breach of Article 1105 in the case before it [TAB 13]

27 <sup>50</sup>Myers Merits Award, at para. 250; *Pope & Talbot* Final Merits Award, at para. 76 [TAB 13].

28 <sup>51</sup>Myers Merits Award, at para. 255 [TAB 5]



1 though the effect of the “new entrants” policy appeared to be a shift of quota from producers in British  
2 Columbia to producers in Quebec – thus disadvantaging the investor).

3 In each NAFTA case in which a *prima facie* claim of national treatment has been made out, the  
4 tribunal has turned to the respondent to justify its discriminatory actions – regardless of whether they  
5 were discriminatory on their face (such as in *US - Trucking*) or discriminatory in result or application  
6 (such as in *Feldman, Myers and Pope & Talbot*). To safeguard the liberalizing objectives of the  
7 NAFTA, this “like circumstances exception” must be construed narrowly. And any appreciation of the  
8 overall legal context of the NAFTA, in search for justification for an apparently discriminatory measure,  
9 must begin with an acknowledgment of the objectives contained within Article 102(1): to promote  
10 conditions of *fair competition* and substantially increase investment opportunities in the North  
11 American Free Trade Zone.

12 **B. Mexico Breached the Article 1102 “National Treatment” Standard.**

13 Application of the Article 1102 “National Treatment” standard is simple and straightforward  
14 under the facts of this case. Thunderbird’s EDM enterprises were seized and closed because of the  
15 machines the facilities were utilizing. Mexico asserted Thunderbird’s skill machines were illegal “cash  
16 slot machines” [*Ex. 70*]. Yet, domestic investors were, and are, open and operating essentially identical  
17 machines at locations in Mexico. Mexico breached its 1102 obligation of failing to provide claimant  
18 and its investments with treatment no less favorable than it provided to these domestic investors.

19 **1. Identification of Appropriate Comparators.**

20 \_\_\_\_\_Article 1102 requires a tribunal to compare the treatment being received by an investor or its  
21 investment with that which is being received by the investors or investments of that host country. The  
22 scope for comparison is the treatment in question. In cases where the treatment in question is particular  
23 to a certain industry, the source of the comparison will be between investors operating within that  
24 industry. The basis for any comparison is the likeness of the comparators. [*See Section V. A 3 above*]

25 In the present case, the identification of the appropriate comparators is straightforward and even  
26 more narrow than the comparison of investors in a particular industry described above. In this case, the  
27 treatment in question is particular to a certain business activity; i.e., the operation of skill machines.  
28 Thunderbird’s EDM enterprises were seized and closed by Mexico because the skill machines in

1 operation at those facilities were deemed illegal. Based upon the treatment in question [seizure and  
2 closure for operation of skill machines], the appropriate comparison to be made is to domestic investors  
3 undertaking that same business activity; i.e., the operation of skill machines.

4 **Guardia**

5 Guardia has long been operating, and continues to operate, skill machine facilities at several  
6 locations in Mexico. He is operating visibly and apparently under the protection of the Mexican law.  
7 In fact, Guardia's skill machine operations withheld legal challenge by Gobernacion and are apparently  
8 now deemed legal. [Watson, para. 4, 7, 57; Velasco, para. 25; Montano, para.19; Luz A. Armas Sawin,  
9 para. 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres; Gomez, paras. 28-30, 72-73; Ex. 82-85, 94]

10 Throughout Thunderbird's initial development and operation of its enterprises, throughout the  
11 period of seizures and legal challenges, throughout the present NAFTA proceedings, and up to the  
12 present time, Guardia has continued, and still continues to operate these skill machine facilities in  
13 Mexico. Eye witness testimony establishes that Guardia was operating skill machines several years ago,  
14 several months ago, and several weeks ago. [Watson, para. 4, 7, 57; Velasco, para. 25; Montano,  
15 para.19; Luz A. Armas Sawin, para. 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres; Gomez, paras.  
16 28-30, 72-73; Ex. 82-85, 94]

17 There is no doubt that Guardia is operating skill machines substantially similar, if not identical  
18 to the machines, operated by the now-closed Thunderbird EDM Enterprises. Luz A. Armas Sawin, para.  
19 4,5, 6, 7; Sawin, para. 8; Dec. of Cepeda y Torres; Ex. 82-85] The only apparent difference between  
20 the operation of the Guardia machines and those at the Thunderbird EDM facilities is described in the  
21 declaration of Steven Sawin.

22 In the development stages for the Thunderbird operations in Mexico, I had visited  
23 various gaming establishments within Mexico. In addition, since the date of the closures  
24 for the three Thunderbird facilities, I visited gaming establishments in Matamoros,  
25 Reynosa, and in Mexico City, that are competitive with the EDM operations that I  
26 managed. I determined that the machines located in Mexico City operation owned by  
27 Sr. Guardia were actually slot machines. Approximately two and ½ years ago, I visited  
28 a business owned by Guardia located in Mexico City and determined that the video  
machines were not "Skill Games" but slot machines. At playing the video game  
machines, I recognized that if I did not push the stop button on the machine within 30  
seconds of when I started the reels, the reels would stop automatically. Thus my opinion  
is that this feature turns the game from one of skill to a game of chance as the player  
could not affect the outcome of the game by the standards of the international  
community. The games operated at the EDM facilities did not have the automatic stop

1 feature as the reels continue to spin until the patron stopped the wheels by pressing the  
2 stop button. The EDM facilities also offered machines that were no different in concept  
3 to that of dominos which is a skill game. The various numerical combinations would  
4 result in a variety of credits depending upon the difficulty of the combination awarded.  
5 The player has the opportunity to utilize skill and gaming credits through the numerical  
6 combinations. After our operations were shut down by the Mexican government, I also  
7 visited other operators in Matamoros and Reynosa, whose owners were of Mexican  
8 descent. These facilities offered “skill stop” games very similar to those at the EDM  
9 facilities. These competitors also had video card (poker) games as well as the same type  
10 of games found in Guardia’s facility. [Sawin, para.8]

7 As far back as November, 2001, signage on the front of Guardia’s skill machine operation in Mexico  
8 City has referred to “betting with dollars” [Gomez, para. 74; Ex. 94]. Thus, not only is Guardia  
9 operating skill machines substantially similar to those operated by Thunderbird’s EDM enterprises,  
10 Guardia is also operating machines that are in effect traditional, and illegal, “slot machines”. Player  
11 involvement and the utilization of skill and dexterity by the player, or the claimed lack thereof, were  
12 prominent issues in the administrative findings and order which led to the closures of the Thunderbird  
13 EDM enterprises. [Ex. 70]

14 Further, the Guardia machines accept and utilize U.S. dollar bills. Declarant Luiz A. Armas  
15 Sawin describes operation of Guardia’s machine, observed in July 2003, as follows:

16 “On or about Tuesday, July 24, 2003, I visited a business which I understand is owned  
17 and operated by a company called Cesta Punta Deportes and is called Club 21 in Mexico  
18 City. I understand that this club is owned by a Mexican national whose last name is  
19 Guardia. The address is Interlomas number 5 Int. 20, Col. Lomas Anahuac,  
20 Huixquilucan de Degollado, Estado de Mexico. Within the premises I observed the  
21 following: there are 100 gaming machines. These gaming machines are Sharp Image  
22 manufactured white round top style. I had an opportunity to play these machines and  
23 recognized that there was a “skill feature” to the games just as the games we had at the  
24 EDM facilities. In order to play the game I had to insert U.S. dollars. I have attached  
25 some video footage and photographs of this operation that were taken on July 24, 2003.  
26 I have also attached a ticket voucher to my declaration.” [Luz A. Armas Sawin, para, 7]

22 The fact that Guardia’s machines utilize and accept dollars is critical because the administrative  
23 findings and order leading to closure of the EDM facilities at Matamoros, Nuevo Laredo and Reynosa  
24 emphasized the use of dollar bills and pesos in the Thunderbird machines.

25 “From the proofs put into the record as Appendices Three and Four, it seems that a  
26 machine that works by electricity effectively requires an interaction with the player for  
27 it to function.

27 In order for this player to have access to the machine, according to Mr. Francesco Ortiz  
28 he has to insert “dollar”, which is understood to mean the legal tender of the United

1 States of North America, as Mr. Ortiz declared that it accepted different denominations  
2 of the dollar.

3 It is logical that, in order to acquire these dollars, the player must pay out Mexican  
4 pesos, legal tender of the national territory, that is to say he must buy dollars with pesos,  
5 or otherwise he could not pay.

6 **Upon inserting the dollar in order to start the machine, one is in the presence of a  
7 “cash slot machine” and not a “token slot machine”.** *[English Translation]*  
8 *[Emphasis Added] [Ex. 70]*

9 Guardia has been allowed to operate, and is presently operating, skill machines which are essentially  
10 identical to those operated by the Thunderbird EDM enterprises and/or machines which are more akin  
11 to traditional and illegal slot machines. Guardia and his skill machine investments in Mexico are an  
12 appropriate comparator for Article 1102 analysis.

13 **de la Torre**

14 de la Torre owns and operates a business entitled Reflejos located in Rio Bravo, Tamaulipas  
15 Mexico which utilizes “skill machines”. The operation of the machines at Reflejos is described as  
16 follows:

17 “Most recently, I visited Rio Bravo, Tamaulipas, Mexico to observe and take  
18 photographs and videotape of the business being Reflejos. I understand that this business  
19 is owned by a Mexican national, Alphonso de la Torre. The business is located at  
20 Centros Comerciales Soriana, Francisco I Madera 1160, Col. Rio Bravo, C.P. 88900,  
21 Rio Bravo Tamaulipas. I visited the facility on July 22, 2003. There are 44 video  
22 gaming machines located on the premises. A patron plays the machine by inserting U.S.  
23 dollars and receives a ticket after finishing play which can be turned into U.S. dollars.  
24 The names of the machines included the Bestco manufactured game called Fantasy Five,  
25 the Leisure Time manufactured game called Pot of Gold and another game called Cherry  
26 Bonus. I videotaped and took pictures of this business operation. The video tape and  
27 photographs are attached to this declaration.

28 When I compare the machines that are being operated at this facility to the machines that  
were operated by patrons in the EDM facilities, I recognize just one difference in some  
of the machines. The patron does not need to push any buttons to stop the play as was  
the case with every machine at the EDM facilities. I understand that this difference is  
critical in comparing a skill machine from a slot machine. All of the games at the EDM  
facilities required player participation and the player was required to push a button to  
stop the play which called for skill and dexterity.

Thus, as do the Guardia operations, the de la Torre operations utilize skill machines which are  
substantially similar if not identical to the machines operated at Thunderbird’s EDM facilities. Also,  
like Guardia, some of de la Torre’s the machines operate on U.S. dollars and in a fashion that eliminates  
player participation and the utilization of skill and dexterity.

1           Because the de la Torre investment utilizes skill machines which are substantially similar if not  
2 identical to those used by the EDM Enterprises, and/or machines which are more akin to traditional and  
3 illegal slot machines, de la Torre and his skill machine investment are an appropriate comparator for  
4 1102 analysis

5           **2. Treatment No Less Favorable**

6           Under Article 1102, the investor and its investments are entitled to the best level of treatment  
7 accorded to any other domestic investor or investment operating under like circumstances. The test of  
8 treatment no less favorable is not a global comparison of treatment received, on the whole, by groups  
9 of domestic or foreign investors or investments. It is particular to the experience of the claimant. The  
10 comparison is between the treatment being received by the claimant and the best treatment received by  
11 a domestic investor operating in like circumstances. Further, the comparison is not limited to an  
12 evaluation of whether the treatment being received is substantially similar. It focuses on the result of  
13 the treatment being received. *[See Section V. A 4 above]*

14           The fact that Thunderbird and its EDM enterprises have been accorded less favorable treatment  
15 than domestic investors and investments under like circumstances is indisputable, both in the nature of  
16 the treatment received and in the effect of that treatment. Thunderbird's investment enterprises have  
17 been forcibly seized and closed. Domestic investors and investments operating under essentially  
18 identical circumstances (Guardia and de la Torre) remain open and operating, apparently under the  
19 protection of Mexican law. The discriminatory nature of the treatment accorded to Thunderbird and  
20 its investment enterprises, as compared to these domestic investors, is further exemplified by the fact  
21 that these domestic investors are allowed to operate not only skill machines substantially similar to  
22 those operated by Thunderbird's EDM facilities, they are also allowed to operate traditional and slot  
23 machines. They are also allowed to operate skill machines which utilize and accept U.S. dollars Yet,  
24 Mexico seized and closed the Thunderbird EDM facilities because, it contended, the skill machines  
25 utilized at those facilities were purportedly "cash slot machines". *[Ex. 70]*

26           Mexico has clearly breached its Article 1102 obligation to provide the investors and investments  
27 of another party treatment no less favorable than it accords, in like circumstances, to its own investors  
28 and their investments.



1 Each Party shall accord to investments of investors of another Party treatment in  
2 accordance with international law, including fair and equitable treatment and full  
protection and security.

3 **2. “Minimum Standard of Treatment”**

4 Pursuant to NAFTA Article 1131(1), this Tribunal shall decide the issues in dispute in  
5 accordance with the NAFTA and “the applicable rules of international law.” NAFTA Article 1105(1)  
6 specifically requires Parties to provide treatment that is “in accordance with international law.” For the  
7 purposes of interpreting NAFTA Article 1105(1), “the applicable rules of international law” include any  
8 international law obligations designed to protect and/or promote the interests of private actors, such as  
9 investors or their investments.

10 The *Myers* Tribunal implicitly recognized the Article 1131(1) requirement to consider the  
11 *applicable* rules of international law with its interpretation of Article 1105(1). The Tribunal noted that  
12 the provision expressed “an overall concept,” whereby the phrases “full protection and security” and  
13 “fair and equitable treatment” were to be read in conjunction with the introductory phrase: “treatment  
14 in accordance with international law.” The Tribunal stated:

15 The Tribunal considers that a breach of Article 1105 occurs only when it is shown that  
16 an investor has been treated in such an unjust or arbitrary manner that the treatment rises  
17 to the level that is unacceptable from the international prospective. That determination  
18 must be made in the light of the high measure of deference that international law  
generally extends to the right of domestic authorities within their own borders. The  
determination must also take into account any specific rules of international law that are  
applicable to the case.

19 In some cases, the breach of a rule of international law by a host Party may not be  
20 decisive in determining that a foreign investor has been denied “fair and equitable  
21 treatment”, but the fact that a host Party has breached a rule of international law that is  
specifically designed to protect investors will tend to weigh heavily in favor of finding  
a breach of Article 1105.<sup>52</sup>

22 The Tribunal in *Mondev v. U.S.A.* came to the same conclusion as did the *Myers* Tribunal.<sup>53</sup> It  
23 did so after the NAFTA Free Trade Commission issued a statement on the interpretation of 1105 which  
24 provided as follows:

25  
26  
27 <sup>52</sup>Myers Award on the Merits, at para’s. 263-264 [TAB 5].

28 <sup>53</sup>Mondev Award, at para. 120 [TAB 4].

1 B. Minimum Standard of Treatment in Accordance with International Law

- 2 1. Article 1105(1) prescribes the customary international law minimum standard  
3 of treatment of aliens as the minimum standard of treatment to be afforded to  
4 investments of investors of another Party.
- 5 2. The concepts of "fair and equitable treatment" and "full protection and security"  
6 do not require treatment in addition to or beyond that which is required by the  
7 customary international law minimum standard of treatment of aliens.
- 8 3. A determination that there has been a breach of another provision of the  
9 NAFTA, or of a separate international agreement, does not establish that there  
10 has been a breach of Article 1105(1).

11 NAFTA Article 1131(2) provides that interpretations issued by the Commission "shall be  
12 binding" upon Chapter 11 tribunals. In the opinion of the *Mondev* Tribunal – which counted both  
13 Professor Crawford and Judge Schwebel among its members – the Commission's statement had two  
14 primary effects. First, the statement confirmed that the standard of treatment recalled in Article 1105  
15 is a customary international law standard which would be required of the NAFTA Parties even in the  
16 absence of its codification through Article 1105. Second, the Tribunal confirmed that an investor cannot  
17 succeed in a claim under Article 1105 merely by proving that a NAFTA Party has breached an  
18 obligation contained within another treaty<sup>54</sup>.

19 With regard to the first issue, the *Mondev* Tribunal noted that all three NAFTA Parties were in  
20 agreement that Article 1105 conclusively recognized the existence of a customary international law  
21 minimum standard of treatment for foreign investors and their investments. They also were in  
22 agreement that the standard was an evolutionary one, whose content would be determined by recourse  
23 to modern international law standards. The Tribunal noted:

24 Thus, the question is not that of a failure to show *opinio juris* or to amass sufficient  
25 evidence demonstrating it. The question rather is: what is the content of customary  
26 international law providing for fair and equitable treatment and full protection and  
27 security in investment treaties?<sup>55</sup>

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28 <sup>54</sup>Mondev Award, at para. 121 [TAB 4]. This does not mean, however, that the existence of another treaty obligation is irrelevant to interpretation of the content of the Article 1105 standard in any given case (for example: as evidence of State practice)

<sup>55</sup>Id. at para's. 111-113 and 121-124.



1 The *ADF* Tribunal agreed with the *Mondev* approach to the customary international law  
2 standard contained within Article 1105, as mandated by the Commission. It provided the following  
3 approach to determining the appropriate content of that customarily-mandated standard:

4 We understand the *Mondev* Tribunal to be saying – and we would respectfully agree  
5 with it – that any general requirement to accord “fair and equitable treatment” and “full  
6 protection and security” must be based upon State practice and judicial or arbitral case  
7 law or other sources of customary or general international law.<sup>56</sup>

8 It is also important to note that the *ADF* Tribunal explicitly chose not to accept the US argument  
9 – which was supported by the two other NAFTA Parties – that “a specific rule of international law  
10 relating to foreign investors and their investments” must be proved (on the basis of providing evidence  
11 of both *opinio juris* and State practice) for an investor to succeed in an Article 1105 claim. The same  
12 arguments were made before, but clearly not accepted by, the *Mondev* Tribunal. Instead, the *ADF*  
13 Tribunal stated the following:

14 The Investor, of course, in the end has the burden of sustaining its charge of  
15 inconsistency with Article 1105(1). That burden has not been discharged here and hence,  
16 as a strict technical matter, the Respondent does not have to prove that current  
17 customary international law concerning standards of treatment consists only of discrete,  
18 specific rules applicable to limited contexts. It does not appear inappropriate, however,  
19 to note that it is not necessary to assume that the customary international law on the  
20 treatment of aliens and their property, including investments, is bereft of more general  
21 principles or requirements, with normative consequences, in respect of investments,  
22 derived from – in the language of *Mondev* – “established sources of international law.”<sup>57</sup>

23 Accordingly, to succeed in a claim for a breach of Article 1105, the investor will not need to  
24 prove the breach of some narrowly defined or historic rule of customary international law. It is the very  
25 existence of the minimum standard which has achieved the status of custom. To understand the content  
26 of this international law standard, one must provide proof – to be drawn from any one of the sources  
27 of international law set out in Article 38(1) of the *Statute of the Court of International Justice*. This  
28 proof will be used by a tribunal to consider how the terms “fair and equitable treatment and full  
protection and security” should be construed in light of the facts of any particular case.

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27 <sup>56</sup>*ADF* Award, at para. 184 [TAB 18].

28 <sup>57</sup>*Id.* at para. 185.

1 While the minimum standard remains a constant requirement of customary international law,  
2 the international law proof to be used in one Article 1105 case may not be relevant to another. For this  
3 case, there are three complementary international law doctrines which are helpful in understanding why  
4 Thunderbird and its investments were accorded treatment which fell below the international law  
5 standards.

- 6 - The doctrine of denial of justice;
- 7 - The theory of abuse of rights; and
- 8 - The theory of detrimental reliance.

9 All three doctrines can be used to inform the Tribunal’s interpretation of how “fair and equitable  
10 treatment” was not provided to Thunderbird or its investments.

### 11 **3. Denial of Justice**

12 As was confirmed in the recent *Loewen Award*,<sup>58</sup> the doctrine of denial of justice has a long  
13 history in customary international law and mixed-claims jurisprudence. This history extends beyond  
14 holding the acts of the domestic courts to the test of international law. One of the best encapsulations  
15 of the doctrine of denial of justice can be found than in the views contained within the 1961 *Harvard*  
16 *Draft Convention on Responsibility of States for Damage Done on Their Territory to the Person or*  
17 *Property of Foreigners*, which provides, in Article 7, that:

18 The denial to an alien by a tribunal or an administrative authority of a fair hearing in a  
19 proceeding involving the determination of his civil rights or obligations or of any  
20 criminal charges against him is wrongful if a decision or judgment is rendered against  
21 him or he is accorded an inadequate recovery. In determining the fairness of any hearing,  
22 it is relevant to consider whether it was held before an independent tribunal and whether  
23 the alien was denied:

- 24 (a) specific information in advance of the hearing of any claim or charge against  
25 him;
- 26 (b) adequate time to prepare his case;
- 27 (c) full opportunity to know the substance and source of any evidence against him  
28 and to contest its validity;

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27 <sup>58</sup>Raymond Loewen and The Loewen Group v. *United States of America*, Final Award, ICSID Case. No. ARB(AF)/98/3,  
28 25 June 2003, at para’s. 129 & 133 (www.naftalaw.org) [TAB 25]].

- 1 (d) full opportunity to have compulsory process for obtaining witnesses and  
evidence;
- 2 (e) full opportunity to have legal representation of his own choice;
- 3 (f) free or assisted legal representation on the same basis as nationals of the State  
4 concerned or on the basis recognized by the principal legal systems of the world,  
5 whichever standard is higher;
- 6 (g) the services of a competent interpreter during the proceedings if he cannot fully  
understand or speak the language used in the tribunal;
- 7 (h) full opportunity to communicate with a representative of the government of the State  
entitled to extend its diplomatic protection to him;
- 8 (I) full opportunity to have such a representative present at any judicial or administrative  
9 proceeding in accordance with the rules of procedure of the tribunal or administrative  
10 agency;
- 11 (j) disposition of his case with reasonable dispatch at all stages of the proceedings; or
- 12 (k) any other procedural right conferred by a treaty or recognized by the principal legal  
systems of the world.<sup>59</sup>

13 The *Harvard Draft* specifies that denials of justice may be perpetrated by “a tribunal or an  
14 administrative authority” that is charged with maintaining a proceeding “involving the determination  
15 of [a foreigner’s] civil rights or obligations.” The right to hold property has been explicitly recognized  
16 by Mexico through its ratification of the NAFTA, which provides for protection of a wide range of  
17 property interests included in the definition of “investment” under Article 1138.

18 Accordingly, any administrative proceeding maintained by a Mexican administrative authority  
19 must respect the investor’s property rights, in a manner which is consistent with “international law,  
20 including fair and equitable treatment and full protection and security.” The doctrine of denial of justice  
21 assists this tribunal in determining the content of this international law standard, involving both  
22 substantive and procedural denials of justice.

23 With the progress of time, the doctrine of denial of justice has evolved in a manner consistent  
24 with both international and domestic administrative law developments. The past hundred years has seen  
25 an exponential increase in the role of the State in economic and risk regulation. This development has  
26 necessarily extended the scope of how government decisions impact upon the rights and interests of

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27 <sup>59</sup>LB. Sohn & R.R. Baxter, “Responsibility of States for Injuries to the Economic Interests of Aliens” 55 (1961) *American*  
28 *Journal of International Law* 545 at 550 [TAB 26].

1 individual actors. International law has evolved to meet these developments. On a procedural level, the  
2 doctrine of denial of justice has been complemented by the rapid growth in protections afforded under  
3 various human rights treaties. On a substantive level, the doctrine has been enhanced by the  
4 development of international economic law treaties which prohibit the arbitrary or discriminatory  
5 treatment of foreigners or their investments.

6 Professor Garcia Amador's work on the minimum standard of treatment of aliens is widely  
7 regarded as an authoritative statement of customary international law standard as it existed thirty years  
8 ago. With respect to denials of justice, Professor Amador included numerous judicial, quasi-judicial  
9 and administrative or regulatory bodies within the scope of a denial of justice claim, noting:

10 A decision or judgment of a tribunal or an administrative authority rendered in a  
11 proceeding involving the determination of the civil rights or obligations of an alien or  
12 of any criminal charges against him, and either denying him recovery in whole or in part  
or granting recovery against him or imposing a penalty, whether civil or criminal, upon  
him is wrongful:

- 13 a) if it is a clear and discriminatory violation of the that law the State concerned;
- 14 b) if it unreasonably departs from the principles of justice recognized by the  
15 principal legal systems of the world; or
- 16 c) if it otherwise involves a violation by the State of a treaty.<sup>60</sup>

17 Similarly, although he was writing at a time predating the rise of the administrative state,  
18 Professor Freeman nonetheless noted that States may dispense regulatory functions in different ways,  
19 whether through courts or other bodies. In so doing, he noted:

20 It is not the *label* of the institution that matters, but the quality of the justice which it  
21 dispenses. If the procedure followed offers the same or as effective safeguards as that  
22 or ordinary courts; and if there is no question as to governmental control or absence of  
impartiality, no complaint may be made as to [the "exceptional character" of an  
administrative tribunal].<sup>61</sup>

23 At the present era of international relations, the submission of these cases to the scrutiny  
24 of an impartial body is the only sound assurance of an objective determination of the

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26 <sup>60</sup>V.F. Garcia-Amador, L.B. Sohn & R.R. Baxter, *Recent Codification of the Law of State Responsibility for Injuries to*  
27 *Aliens* (1974) at 196 [TAB 27].

28 <sup>61</sup>Alwyn Freeman, *The International Responsibility of States for Denial of Justice* (Kraus Reprint Co., New York: 1970)  
at 304 [TAB 28].

1 rights of aliens.<sup>62</sup>

2 In fact, as early as the opening decades of the 20<sup>th</sup> century, however, it was firmly established  
3 in the jurisprudence of mixed claims commissions that a denial of justice could be found in the  
4 administrative/regulatory decisions of the state, notwithstanding the existence of an exhaustion of local  
5 remedies rule.<sup>63</sup>

6 Of course, the NAFTA Parties have effectively annulled the application of the “exhaustion of  
7 local remedies” rule by providing investors with the choice of pursuing a claim for damages before a  
8 NAFTA Tribunal or a domestic tribunal, while permitting them to maintain domestic petitions for extra-  
9 ordinary relief pursuant Article 1121. Accordingly, unless the first and primary source of a NAFTA  
10 claim is the decision of a domestic court,<sup>64</sup> it will not be necessary to demonstrate that a claimant has  
11 exhausted its domestic legal remedies before seeking relief from a NAFTA tribunal.<sup>65</sup> The conclusion  
12 that denials of justice extend far beyond the domestic court room, besides being based on arbitral  
13 jurisprudence and the nullification of the exhaustion of local remedies rule for NAFTA claims, can also  
14 be based upon general principles of State responsibility. As Professor Bin Cheng noted about the actions  
15 of government officials, “whatever his rank, his act *qua* an official is an act of the Government and  
16 hence of the State.”<sup>66</sup> Professor Cheng’s view is supported by the tribunal in the *Moses* case, which  
17 concluded:

18 An officer or person in authority represents *pro tanto* his government, which in an  
19 international sense is the aggregate of all officers and men in authority.<sup>67</sup>

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21 <sup>62</sup>Id. at 545

22 <sup>63</sup>William Marion Gibson, *Aliens and the Law* (University of North Carolina Press, Durham: 1940) at 10 [TAB 29]; A. H. Feller, *The Mexican Claims Commission* (MacMillan, New York: 1935) at 133 [TAB 30].

23 <sup>64</sup>The *Loewen* Tribunal has clarified that the principle of finality will require a claimant to exhaust its appeals when the  
24 primary source of its complaint is the act of a court, rather than the acts of an administrator. This result is to be distinguished  
25 from the exhaustion of local remedies rule, as it goes to the nature of a court decision as a “measure” under the NAFTA.  
In application of the finality principle, a lower court’s decision does not constitute a “measure” under Article 1101 until  
appeals in respect of that decision have been exhausted. See: *Loewen* Award, at para’s. 143, 146, 148 and 156 [TAB 25]

26 <sup>65</sup>See, e.g.: *Feldman* Award, at para. 140 [TAB 12]

27 <sup>66</sup>Bin Cheng, *The General Principles of Law* (Stevens & Sons, London: 1953) at 196 [TAB 31].

28 <sup>67</sup>*Moses v. Mexico*, US-Mexico Claims Commission (1868), *Moore’s Digest*, 3127 at 3129 [TAB 32].

1           **4.       Procedural Denials of Justice**

2           The doctrine of denial of justice is composed of two categories: denials of procedural justice and  
3 denials of substantive justice. This distinction was best described in the celebrated *Cotesworth & Powell*  
4 judgement, which provided:

5                     The first occurs when the tribunals refuse to hear a complaint, or to the established  
6 forms of procedure, or when undue an inexcusable delays occur in rendering a  
7 judgement. The second takes place when sentences are pronounced and executed in  
open violation of the law, or which are manifestly iniquitous.<sup>68</sup>

8           Drawing upon centuries of international jurisprudence, numerous commentators have formulated  
9 expressions of how to recognize when procedural denials of justice may have occurred. For example,  
10 Professor Schachter has noted how the obligation of the host state includes the maintenance of  
11 “competent and independent tribunal” for the determination of a foreign investor’s rights.<sup>69</sup> Decades  
12 earlier, Professor Roth wrote that:

13                     International law grants the alien procedural rights in his State of residence as a primary  
14 protection against the violation of his substantive rights. These procedural rights amount  
15 to freedom of access to court, the right to fair, non-discriminatory and unbiased hearing,  
the right to a just decision rendered in full compliance with the laws of the State within  
a reasonable time.<sup>70</sup>

16           The kinds of activities which will constitute a denial of procedural justice would include, for  
17 example, an effective refusal to hear an interested party;<sup>71</sup> or “a continued absence of seriousness on the  
18 part of [the decision-maker].”<sup>72</sup> Professor Borchard, who authored the first *Harvard Draft*, summarized  
19 the content of the prohibition against procedural denials of justice as follows:

20                     On the procedural side, we are perhaps in less doubt of the content of the standard,  
21 although we must still be satisfied with general principles. Fair courts, readily open to  
22 aliens, administering justice honestly, impartially, without bias or political control, seem  
essentials of international due process. While the details of procedure necessarily vary

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23 <sup>68</sup>Moore’s 2057, at 2083 [TAB 33].

24 <sup>69</sup>Oscar Schachter, *International Law in Theory and Practice* (Kluwer, New York: 1991) at 312 [TAB 34].

25 <sup>70</sup>Andreas Hans Roth, *The Minimum Standard of International Law Applied to Aliens* (University of Geneva: 1949) at 185  
26 [TAB 35].

27 <sup>71</sup>*Cotesworth & Powell*, at 2083 [TAB 33].

28 <sup>72</sup>*United States (Chattin) v. United Mexican States*, 22 (1928) American Journal of International Law 677 (Mexico-US  
General Claims Commission) [TAB 36]; See: Roth at 183 [TAB 35].

1 considerably from country to country, certain essential elements of fair trial and  
2 objective justice are required of all systems. It is probably less difficult to apply than  
3 to define these principles, and we have in their application the aid of innumerable  
4 precedents from international practice. In spite of the legislative effort strictly to narrow  
the conception of denial of justice and the privilege of diplomatic interposition, few  
foreign countries have been willing to abandon their nationals to the arbitrariness of  
corrupt courts or administrative bodies<sup>73</sup>

5 Borchard's use of the term "due process" is telling, not only because it appears in NAFTA  
6 Article 1110 with explicit reference to the application of Article 1105 in terms of the expropriation of  
7 an investment, but also because it has appeared in numerous draft conventions on the protection of  
8 foreign property and in many bilateral investment treaties.<sup>74</sup> It connotes a fundamental respect for the  
9 Rule of Law, which must be present in the decision-making processes under review.

10 In his comparative study of due process and procedural fairness in the United States, in the  
11 United Kingdom and Commonwealth countries (such as Canada) and in the European Union, Professor  
12 Galligan has noted that the concepts of "due process" (as understood in the U.S. context) and  
13 "procedural fairness" (as understood in the common law process of the U.K. and Commonwealth  
14 countries) clearly "cover the same ground," with "the core idea" being "common to both ... that certain  
15 procedures are needed to give effect to the ends of justice within legal decisions."<sup>75</sup>

16 Professor Galligan states that the idea of procedural fairness is a general principle which applies  
17 across the spectrum of administrative processes in the common law of Commonwealth countries, "with  
18 its precise content to be determined in each context."<sup>76</sup> He similarly notes a conception of a sliding  
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21 <sup>73</sup>Edwin Borchard, "The 'Minimum Standard' of the Treatment of Aliens" 38 (1940) *Michigan Law Review* 445 at 460  
22 [TAB 37].

23 <sup>74</sup>In his treatise on the subject of these draft conventions, Professor Schwarzenberger hypothesized that with the inclusion  
24 of the term "due process of law" that the drafters of such codifying instruments as the *Abs-Shawcross Convention* and the  
*OECD Draft Convention* were attempting to acknowledge the role of the minimum standard in consideration of the  
25 lawfulness of a taking, as such a principle embodies elements of the Rule of Law. However, he suggested that they would  
26 have done better to state more precisely what they had in mind. See: Georg Schwarzenberger, *Foreign Investments and  
International Law* (Stevens & Sons, London: 1969) at 119 and 172 [TAB 38]; and D.J. Galligan, *Due Process and Fair  
Procedures: A Study of Administrative Procedures* (Clarendon, Oxford: 1996) at 170 [TAB 39].

27 <sup>75</sup>Galligan, at 170 [TAB 39].

28 <sup>76</sup>*Id.* at 186.

1 scale for the application of procedural principles, under the rubric of due process, in the U.S. context.<sup>77</sup>  
2 He recounts the kinds of due process (or procedural) safeguards which will be relevant in an  
3 administrative context as including: “the giving of notice, an oral hearing, an impartial adjudicator, the  
4 calling of witnesses and cross examination, the right to counsel, the compiling of a record, the basing  
5 of a decision on the record, and the giving of reasons.”<sup>78</sup>

6 In the European context, Professor Galligan notes how Article 6(1) of the *European Convention*  
7 *on Human Rights* stipulates that individuals are “entitled to a fair and public hearing within a reasonable  
8 time by an independent and impartial tribunal established by law.” He concludes that the “impartiality”  
9 mentioned above has connotations similar to those of English law and emphasizes the need to dispel  
10 the appearance of bias as well as actual bias.”<sup>79</sup>

11 The concepts of due process and procedural fairness can also be found within modern  
12 international economic law. For example, Article X:3 of the GATT, which the WTO Appellate Body  
13 has explicitly recognized as granting a minimum standard of procedural fairness which all WTO  
14 Member States (including Mexico) must obey,<sup>80</sup> provides:

- 15 (a) Each contracting party shall administer in a uniform, impartial and reasonable  
16 manner all its laws, regulations, decisions and rulings of the kind described in  
17 paragraph 1 of this Article.
- 18 (b) Each contracting party shall maintain, or institute as soon as practicable, judicial,  
19 arbitral or administrative tribunals or procedures for the purpose, *inter alia*, of  
20 the prompt review and correction of administrative action relating to customs  
21 matters. Such tribunals or procedures shall be independent of the agencies  
22 entrusted with administrative enforcement and their decisions shall be  
23 implemented by, and shall govern the practice of, such agencies unless an appeal  
24 is lodged with a court or tribunal of superior jurisdiction within the time  
25 prescribed for appeals to be lodged by importers; Provided that the central  
26 administration of such agency may take steps to obtain a review of the matter in  
27 another proceeding if there is good cause to believe that the decision is  
28 inconsistent with established principles of law or the actual facts.

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24 <sup>77</sup>Id. at 198.

25 <sup>78</sup>Id. at 208

26 <sup>79</sup>Id. at 220-221

27 <sup>80</sup>*United States – Import Prohibition on Certain Shrimp and Shrimp Products*, WT/DS58/AB/R, 12 October 1998, at para.  
28 183 [TAB 40].



1 In order to relate the content of the minimum standards contained in GATT Article X:3 to the  
2 content of the international law minimum standard memorialized in Article 1105, it is essential to  
3 demonstrate how the obligation has been undertaken by a State in the interests of private actors, such  
4 as investors and their investments. The WTO Panel in the *US – Section 301* case explained the  
5 connection between the obligations contained with multilateral trade agreements, such as the GATT,  
6 and individual economic actors in the following manner:

7 Trade is conducted most often and increasingly by private operators. It is through  
8 improved conditions for these private operators that Members benefit from WTO  
9 disciplines. The denial of benefits to a Member which flows from a breach is often  
10 indirect and results from the impact of the breach on the market place and the activities  
11 of individuals within it. Sections 301-310 themselves recognize this nexus. One of the  
12 principal triggers for US action to vindicate US rights under covered agreements is the  
13 impact alleged breaches have had on, and the complaint emanating from, individual  
14 economic operators...

15 In treaties which concern only the relations between States, State responsibility is  
16 incurred only when an actual violation takes place. By contrast, in a treaty the benefits  
17 of which depend in part on the activity of individual operators the legislation itself may  
18 be construed as a breach, since the mere existence of legislation could have an  
19 appreciable "chilling effect" on the economic activities of individuals.

20 Thus, Article III:2 of GATT 1947, for example, would not, on its face, seem to prohibit  
21 legislation independently from its application to specific products. However, in light of  
22 the object and purpose of the GATT, it was read in GATT jurisprudence as a promise  
23 by contracting parties not only that they would abstain from actually imposing  
24 discriminatory taxes, but also that they would not enact legislation with that effect.<sup>81</sup>

25 While it is not possible for an investor to use the NAFTA to submit a claim for breach of GATT  
26 Article X:3 on its own behalf, the content of the minimum standard contained within this obligation is  
27 certainly relevant in determining the content of the customary international law standard contained  
28 within Article 1105.

29 Similarly, while it is not possible for an investor to submit a claim for a breach of NAFTA  
30 Articles 1804 or 1805, it is certainly appropriate for this Tribunal to consider these obligations as part  
31 of the treaty context within which the meaning of the phrase "treatment in accordance with international  
32 law, including fair and equitable treatment and full protection and security" can be discerned (and the

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33 <sup>81</sup>*United States – Sections 301-310 of the Trade Act of 1974*, WT/DS152/R, 22 December 1999, at para's. 7.77 & 7.81-7.82  
34 [TAB 41].

1 content of the NAFTA minimum standard can thus be identified).<sup>82</sup> NAFTA Articles 1804 and 1805  
2 provide:

3 Article 1804: Administrative Proceedings.

4 With a view to administering in a consistent, impartial and reasonable manner all  
5 measures of general application affecting matters covered by this Agreement, each Party  
6 shall ensure that in its administrative proceedings applying measures referred to in  
7 Article 1802 to particular persons, goods or services of another Party in specific cases  
8 that:

- 7 (a) wherever possible, persons of another Party that are directly affected by a  
8 proceeding are provided reasonable notice, in accordance with domestic  
9 procedures, when a proceeding is initiated, including a description of the nature  
10 of the proceeding, a statement of the legal authority under which the proceeding  
11 is initiated and a general description of any issues in controversy;
- 10 (b) such persons are afforded a reasonable opportunity to present facts and  
11 arguments in support of their positions prior to any final administrative action,  
12 when time, the nature of the proceeding and the public interest permit; and
- 12 (c) its procedures are in accordance with domestic law.

13 Article 1805: Review and Appeal

- 14 1. Each Party shall establish or maintain judicial, quasi-judicial or administrative  
15 tribunals or procedures for the purpose of the prompt review and, where  
16 warranted, correction of final administrative actions regarding matters covered  
17 by this Agreement. Such tribunals shall be impartial and independent of the  
18 office or authority entrusted with administrative enforcement and shall not have  
19 any substantial interest in the outcome of the matter.
- 18 2. Each Party shall ensure that, in any such tribunals or procedures, the parties to  
19 the proceeding are provided with the right to:
- 20 (a) a reasonable opportunity to support or defend their respective positions;  
21 and
- 21 (b) a decision based on the evidence and submissions of record or, where  
22 required by domestic law, the record compiled by the administrative  
23 authority.
- 23 3. Each Party shall ensure, subject to appeal or further review as provided in its domestic  
24 law, that such decisions shall be implemented by, and shall govern the practice of, the  
25 offices or authorities with respect to the administrative action at issue.

25 Numerous NAFTA tribunals have recently confirmed that a denial of due process rights  
26 constitutes a breach of Article 1105. For example, the *Loewen* Tribunal identified serious deficiencies

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27 <sup>82</sup>This was the approach taken in the *Metalclad* Claim [TAB 8]. A similar approach was adopted by the *ADF* Tribunal in  
28 determining the meaning of “procurement” under Chapter 11 (with reference to its construction in Chapter 10) [TAB 18].

1 in the manner in which a civil claim was prosecuted against the investment as evidence of a failure to  
2 respect the due process rights required under Article 1105.<sup>83</sup> Similarly, the *ADF* Tribunal stated that if  
3 it were to make a finding in favor of the investor in spite of sufficient evidence on the record, such  
4 actions could constitute a denial of due process required under international law.<sup>84</sup>

5 In citing the same judgment of the International Court of Justice, both the *Mondev* Tribunal and  
6 the *Pope & Talbot* Tribunal have noted that failures to provide sufficient due process to an investor (in  
7 any government decision-making context) may evidence the kind of arbitrariness that falls below  
8 international law standards.<sup>85</sup> In this regard, the *Mondev* Tribunal stated:

9 In the *ELSI* case, a Chamber of the Court described as arbitrary conduct that which  
10 displays “a wilful disregard of due process of law, . . . which shocks, or at least surprises,  
11 a sense of judicial propriety”. It is true that the question there was whether certain  
12 administrative conduct was “arbitrary”, contrary to the provisions of an FCN treaty.  
13 Nonetheless (and without otherwise commenting on the soundness of the decision itself)  
14 the Tribunal regards the Chamber’s criterion as useful also in the context of denial of  
15 justice, and it has been applied in that context, as the Claimant pointed out. The Tribunal  
16 would stress that the word “surprises” does not occur in isolation. The test is not  
17 whether a particular result is surprising, but whether the shock or surprise occasioned  
18 to an impartial tribunal leads, on reflection, to justified concerns as to the judicial  
19 propriety of the outcome, bearing in mind on the one hand that international tribunals  
20 are not courts of appeal, and on the other hand that Chapter 11 of NAFTA (like other  
21 treaties for the protection of investments) is intended to provide a real measure of  
22 protection. In the end the question is whether, at an international level and having regard  
23 to generally accepted standards of the administration of justice, a tribunal can conclude  
24 in the light of all the available facts that the impugned decision was clearly improper and  
25 discreditable, with the result that the investment has been subjected to unfair and  
26 inequitable treatment. This is admittedly a somewhat open-ended standard, but it may  
27 be that in practice no more precise formula can be offered to cover the range of  
28 possibilities.<sup>86</sup>

20 Given the authority of arbitral jurisprudence, the work of the most noted publicists, and the  
21 current content of international economic law instruments, it is possible to provide a list of basic  
22 principles of procedural fairness, the denial of which may result in a finding that a NAFTA Party has  
23 breached the standards contained within Article 1105 and customary international law generally. These

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24 <sup>83</sup>Loewen Final Award, at para’s 87 and 119 [TAB 25].

25 <sup>84</sup>ADF Final Award, at para. 143 [TAB 18].

26 <sup>85</sup>*Pope & Talbot Inc. v. Government of Canada*, Damages Award, NAFTA/UNCITRAL Tribunal, 31 May 2002 at para’s  
27 63-65 (www.naftalaw.org) [TAB 42]

28 <sup>86</sup>Mondev Final Award, at para. 127[TAB 4].

1 principles would apply to all manner of judicial, quasi-judicial or administrative decision-makers, with  
2 the latter being provided with the greatest degree of deference.<sup>87</sup> For administrative decision-makers,  
3 such principles include:

- 4 (a) The provision of notice of a decision-making process that could materially affect  
5 the rights or interests of an investor or investment;
- 6 (b) The opportunity to be made aware of, and freely contribute to the assembly of,  
7 all of the evidence at issue;
- 8 (c) The opportunity to make one's case before an independent and impartial official;
- 9 (d) The promise of fair treatment by the decision-maker, including a prohibition on  
10 unnecessary or inappropriate *ex parte* communications; and
- 11 (e) The compilation of a record of proceedings and the issuance of satisfactory  
12 reasons for decision which are based upon that record.

#### 11 **5. Substantive Denials of Justice**

12 It is a well-established principle of international law that a claim may be founded upon  
13 substantive denials of justice, separate and apart from any serious defects of procedural law. Early in  
14 the last century, Professor Borchard wrote that: "As a rule, unjustified discrimination will be found an  
15 ingredient in sustainable claims [for substantive denials of justice]."<sup>88</sup> Desvernine also cited Borchard  
16 for the maxim that "a grossly unfair or notoriously unjust decision may be and has been considered as  
17 equivalent to a denial of justice." Noting the case of *Bronner v. Mexico*, he indicated that an  
18 adjudicative decision can be found "so unfair" as to constitute a denial of justice (in that case, involving  
19 a finding of fact that invoices evidenced fraud when they clearly did not).<sup>89</sup>

20 Sir Robert Jennings and Sir Arthur Watts have come to a similar conclusion about arbitrariness  
21 and the minimum standard of treatment of foreign investors:

22 An alien must in particular not be wronged in person or property by officials or courts  
23 of a state. Thus the police must not arrest him without cause, administrative officials  
24 must not treat him arbitrarily and courts must treat him justly and in accordance with the

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25 <sup>87</sup>Domestic courts are deserving of the highest level of deference in this regard because they are designed to provide the  
26 greatest degree of institutionalized protection to individuals in order to safeguard their rights and liberties.

27 <sup>88</sup>Borchard, at 458 [Tab 37].

28 <sup>89</sup>Raoul E. Desvernine, *Claims Against Mexico* (New York: Private Edition, 1921) at 79-80 [TAB 43].

1 law.<sup>90</sup>

2 The hallmark of a substantive denial of justice can be found in the arbitrariness of the decision  
3 in question. A decision is arbitrary, and accordingly a substantive denial of justice, if it is “manifestly  
4 unjust or one-sided.”<sup>91</sup> There are numerous arbitral decisions which consider applicability of customary  
5 minimum standards of treatment in terms of the arbitrariness of the government actions in question.  
6 For example, in the *BP Oil* case, the sole arbitrator found that the State’s actions violated public  
7 international law because its taking of the investor’s property “was made for purely political reasons  
8 and arbitrary and discriminatory in character.”<sup>92</sup>

9 Professor Mann has also confirmed that “...arbitrary, discriminatory or abusive treatment is  
10 contrary to customary international law...”<sup>93</sup> and the *Mondev* Tribunal has cautioned that “[to] the  
11 modern eye, what is unfair or inequitable need not equate with the outrageous or the egregious. In  
12 particular, a State may treat foreign investment unfairly and inequitably without acting in bad faith.”<sup>94</sup>  
13 The *Loewen* Tribunal has agreed, stating that proof of discriminatory intent or bad faith are not  
14 necessary to establish a breach of fair and equitable treatment under international law.<sup>95</sup>

15 The principle of protection against arbitrary State acts can also be found in the practice of the  
16 United Nations bodies. For example, the UN Human Rights Commission concluded that a membership  
17 allocation scheme for seats in a legislative press gallery impinged upon the claimant’s right to have  
18 access to information because the “operation and application” of the scheme could not be “shown as  
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<sup>90</sup>*Oppenheim’s International Law*, 9<sup>th</sup> ed., Vol. 1 – Peace, Parts 2-4 at 910-911 [TAB 45]

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<sup>91</sup>This is the formulation of a substantive denial of justice provided by Vattel, *Le Droit des Gens* (1758) Book II, Chapter 18, at para. 350; translated by C.J. Fenwick in: J.B. Scott, ed., *Classics of International Law* (Washington, Carnegie Institution: 1916) [TAB 46].

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<sup>92</sup>*British Petroleum Exploration Co. v. Libyan Arab Republic*, Final Award of Arbitrator Lagergren, 53 (1973) *International Law Reports* 297 at 329 [TAB 47].

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<sup>93</sup>*F.F.A. Mann*, “British Treaties for the Promotion and Protection of Investments” 52 [1981] *British Yearbook of International Law* 241 at 243 [TAB 48].

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<sup>94</sup>*Mondev Award*, at para. 116 [TAB 4].

<sup>95</sup>*Loewen Award*, at para. 132.

1 necessary and proportionate to the [legislative] goal in question and not arbitrary.”<sup>96</sup>

2 For its part, the United Nations General Assembly has issued a *Declaration on the Human*  
3 *Rights of Individuals Who Are Not Nationals of the Country in Which They Live*, which provides in  
4 Article 9 that:

5 No alien shall be arbitrarily deprived of his or her lawfully acquired assets.<sup>97</sup>

6 The WTO Appellate Body has twice considered what constitutes “arbitrary discrimination” in  
7 terms of the application of an otherwise justifiable government measure. In *US – Shrimp*, the Appellate  
8 Body determined that the regulatory process in question was non-transparent, did not provide the  
9 opportunity for a fair hearing of the issues, or an effective administrative means of review or appeal.  
10 Because the effect of these procedural weaknesses was to advantage some private actors over other  
11 ones, the measure was found to have been applied in a manner that resulted in arbitrary discrimination.<sup>98</sup>  
12 In *US – Reformulated Gasoline*, the Appellate Body made a similar finding, where the measure was  
13 applied in a manner which inexplicably disadvantaged the goods manufactured by firms in certain  
14 countries over those from other countries.<sup>99</sup>

15 Thus, it would appear that whether one focuses upon the procedural aspects of an investor’s  
16 treatment, or the substantive result, the teachings of the doctrine of “denial of justice” provide this  
17 Tribunal with an objective standard of “fair and equitable” treatment against which to judge the  
18 treatment received by an investment regardless of whether than level of treatment is no better than what  
19 local competitors receive. Both the procedural principles contained within this doctrine, and the  
20 substantive prohibition of arbitrary results, have been received into the modern practice of states and  
21 jurisprudence of international tribunals.<sup>100</sup>

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23 <sup>96</sup>United Nations, Human Rights Committee, Communication No. 633/1995: Canada 05/05/99, CCPR/C/65/D/633/1995  
24 at para.13.6 [TAB 49].

25 <sup>97</sup>A/RES/40/144, 13 December 1985 [TAB 50].

26 <sup>98</sup>*US - Shrimp*, at 177-183 [TAB 40].

27 <sup>99</sup>*United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/9, 29 May 1996, at pp. 16-19 [TAB  
51].

28 <sup>100</sup>See, e.g., the *Myers Award*, at para. 260 [TAB 5].

1           **6. The Abuse of Rights Doctrine**

2           The doctrine of abuse of rights is based upon the general principle of international law  
3 commonly known as good faith. The doctrine is based upon the premise that a State will not exercise  
4 any right under international law, including the liberty to exercise its sovereign regulatory authority, in  
5 an arbitrary, discriminatory or otherwise abusive manner.

6           As an elemental principle in the ordering of relations between states, good faith provides the  
7 glue which holds the international order together. Section 711 of the *Third Restatement of the Foreign*  
8 *Relations Law of the United States* establishes the principle of good faith in state responsibility provides  
9 that “a state is responsible under international law for injury to a national of another state caused by an  
10 official act or omission that violates... a personal right that, under international law, a state is obligated  
11 to respect for individuals of foreign nationality.”<sup>101</sup>

12           In its Merits Award, the ICSID Tribunal in *AMCO Asia v. Indonesia* has even determined that  
13 good faith is a general principle upon which an investor could found its claim, concluding that an  
14 investor should be entitled: “to realize the investment, to operate it with a reasonable expectation to  
15 make profit and to have the benefit of the incentives provided by law” without suffering the arbitrary  
16 exercise of a right which would prevent such enjoyment<sup>102</sup>

17           Professor Cheng devoted an entire chapter of his renowned treatise on the principles of  
18 international law to the manner in which the doctrine of abuse of rights rises from the principle of good  
19 faith. He summarized his view of the doctrine as follows:

20           ... discretion must be exercised in good faith, and the law will intervene in all cases  
21 where this discretion is abused. ... Whenever, therefore, the owner of a right enjoys a  
22 certain discretionary power, this must be exercised in good faith, which means that is  
must be exercised reasonably, honestly, in conformity with the spirit of the law and with

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24           <sup>101</sup> Commentary (e) to Section 711 confirms that this provision refers both to the interests of individuals and to “a juridical  
25 person of foreign nationality also enjoy some protection, for instance, against denials of procedural justice” and that “for  
26 a juridical person, such violations would normally result in economic injury and fall within clause ©)),” which provides that  
27 responsibility attaches for acts that unreasonably interfere with “a right to property of other economic interest that, under  
international law, a state is obligated to respect for persons, natural or judicial, of foreign nationality, as provided in section  
712.” [TAB 52].

28           <sup>102</sup> *AMCO Asia v. Indonesia*, 1 ICSID Reports, 377 at 490 & 493 [TAB 54]. See, also: the Sapphire Award (1963) 35 ILR  
136 at 181 [TAB 55].

1 due regard to the interest of others.<sup>103</sup>

2 And with respect to the application of the *Anglo-Norwegian Fisheries* case, Cheng noted:

3 The exercise of a right – or a supposed right, since the right no longer exists – for the  
4 sole purpose of causing injury to another is thus prohibited. Every right is the legal  
5 protection of a legitimate interest. An alleged exercise of a right not in furtherance of  
such interest, but with the malicious purpose of injuring others can no longer claim  
protection of the law.<sup>104</sup>

6 The principle of good faith requires every right to be exercised honestly and loyally.  
7 Any fictitious exercise of a right for the purpose of evading either a rule of law or a  
contractual obligation will not be tolerated. Such an exercise constitutes an abuse of the  
8 right, prohibited by law.<sup>105</sup>

9 For his part, Professor Schwarzenberger argued that the theory of abuse of rights was so well-  
10 ensconced in the principle of good faith and in the customary international law minimum standard of  
11 treatment of aliens that it was not even necessary to refer to it as a separate standard (or international  
12 tort) – except for the “hard core” of the theory. He considered the hard core to include: “the arbitrary  
13 or unreasonable exercise of rights or powers within the exclusive jurisdiction of States.”<sup>106</sup> Professor  
14 Schwarzenberger accordingly stated:

15 Arbitrariness in any form is – or ought to be – abhorrent to *homo juridicus*. His whole  
16 professional outlook is dominated by the attitude that, in the eyes of the law, equal  
situations require equal remedies.

17 Yet, anybody who is acquainted with the techniques by which judicial precedents are  
18 applied and distinguished is aware of the element of subjectivity which is inseparable  
from deciding even on a judicial level what situations are supposed to be equal.

19 In the fields of quasi-judicial, administrative or political decisions, it is even more  
20 difficult to verify the arbitrary exercise of discretion. The wider the scope of discretion,  
21 the easier it is to find plausible arguments to hide irrelevant or objectionable reasons  
behind such reasons. If discretion is exercised within as wide a framework of territorial  
22 jurisdiction, only the most potent abuses of sovereignty could possibly be caught by any  
prohibition of the arbitrary use of sovereign right.<sup>107</sup>

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24 <sup>103</sup>Bin Cheng, at 132-134 [TAB 31].

25 <sup>104</sup>Id. at 122

26 <sup>105</sup>Id. at 123

27 <sup>106</sup>Georg Schwarzenberger, *International Law and Order* (1971) at 89-90 & 99-100 [TAB 56].

28 <sup>107</sup>Id. at pp. 100-101.



1 Of course, Professor Schwarzenberger was not questioning whether it should be considered an  
2 international law tort for discretion to be exercised arbitrarily, capriciously, or unreasonably. Rather,  
3 he was concerned that international tribunals may not be able to spot the cases in which discretion has  
4 been exercised behind closed doors, but which leads to a manifestly discriminatory, or otherwise unfair  
5 or inequitable, result. In this regard, Sir Hersch Lauterpacht once stated:

6 ... the [international] law of torts is confined to very general principles, and the part  
7 which the doctrine of abuse of rights is called upon to play is therefore particularly  
8 important.<sup>108</sup>

8 Professor Amador also concluded that “the basic principle of the prohibition of abuse of rights  
9 is applicable in international relations” as a matter of customary international law. He cites no less  
10 authority than the PCIJ and ICJ for this proposition.<sup>109</sup> After reviewing the available jurisprudence and  
11 evidence of State practice, Professor Amador concludes:

12 In view of the foregoing, it seems obvious that the doctrine of the abuse of rights finds  
13 its widest application in the context of the so-called “unregulated matters,” which are  
14 found, especially, in those matters which are “essentially within the domestic  
15 jurisdiction” of States... And if there is a field in which States necessarily enjoy wide  
16 discretionary powers it is the field of treatment of aliens... Whatever the aspect of the  
17 “treatment” to which aliens are entitled under the principles governing state  
18 responsibility, it is recognized that the State possesses powers to take measures  
19 restricting even human rights and fundamental freedoms for reasons of internal security,  
20 the economic well-being of the nation, to ensure order, to protect health and morals, etc.  
21 Consequently, where such powers are not subjected to explicit and precise rules, the  
22 international responsibility which may be incurred by the State for injuries sustained by  
23 aliens, could only rest on an “arbitrary,” “abusive” exercise of the discretionary power.<sup>110</sup>

19 Given Professor Amador’s insights about the arbitrary or abusive exercise of discretionary  
20 authority by government officials, it is clear that the evidence of an “abuse of right” is not unlike the  
21 evidence of a substantive denial of justice. In fact, it would seem that every abuse of right is, by  
22 definition, a substantive denial of justice. Accordingly, it only makes sense that the touchstone for  
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24 <sup>108</sup>H. Lauterpacht, *The function of Law in the International Community* (1933) at 298 [TAB 57]

25 <sup>109</sup>F.V. Garcia-Amador, *The Changing law of International Claims*, Vol. I (Oceana, New York: 1984) at notes 139-141,  
26 citing: *Case Concerning Certain German Interests in Polish Upper Silesia*, PCIJ Series A7, at 30; *Case Concerning the Free*  
27 *Zones of Upper Savoy and the District of Gex* (1932), PCIJ Series A7, A/N 46, at 167; and *Anglo-Norwegian Fisheries*, at  
28 142 [TAB 58].

<sup>110</sup>*Id.* at 112-113.

1 liability under either theory is evidence of an arbitrary decision – i.e. a decision which cannot be  
2 explained on a reasoned basis as being fair and equitable.

3 It should not be generally necessary for an investor to prove conclusively whether a plainly  
4 arbitrary decision was in fact based upon an abuse of right, discrimination, or some other improper  
5 motive. The very existence of an arbitrary (i.e. not reasonably explainable) decision is evidence that  
6 an international wrong has been committed. Once an investor has established its *prima facie* case that  
7 a patently arbitrary decision has been made, and it has suffered damages as a result, it will be for the  
8 State to explain its conduct, and rebut the allegation that the seemingly arbitrary result falls below the  
9 standard of fair and equitable treatment required under NAFTA Article 1105.

10 Finally, it must be stressed that one does not need to allege the existence of bad faith to prove  
11 out a claim based upon the operation of the general international law principle of good faith. Abuses  
12 of right can be evidenced in the manifest arbitrariness of a process or a result, although any proof of  
13 discriminatory animus or bad faith, when available, can also serve the basis of a successful claim.

#### 14 **7. Detrimental Reliance**

15 One other particular species of international *delict*, which has repeatedly been seen as falling  
16 below international law standards, is the detrimental reliance of a claimant on assurances provided by  
17 a State official or agent.

18 In *Metalclad*, the Investor relied on advice from federal officials that its investment did not  
19 require the municipal construction permit which was demanded, and eventually refused, by municipal  
20 officials. The Tribunal concluded that Metalclad relied upon this advice to its considerable detriment.  
21 It accordingly concluded that - regardless of whether the advice that Metalclad received from federal  
22 officials was actually correct – the investor was entitled to rely upon it and seek damages for its  
23 detrimental reliance. Because the investment suffered as a result of this advice, Mexico was found to  
24 have breached the standard of fair and equitable treatment provided under Article 1105 and international  
25 law.<sup>111</sup>

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27  
28 <sup>111</sup>Metaclad Award, at para's 88-89 [TAB 8].

1 While not finding any such breach in the case before it, the *ADF* Tribunal noted that detrimental  
2 reliance is a legitimate ground of complaint under Article 1105, by stating that “any expectations that  
3 the Investor had with respect to the relevancy or applicability of the case law it cited were not created  
4 by any misleading representations made by authorized officials...”<sup>112</sup>

5 In the recent ICSID case of *Wena Hotels v. Egypt*, the Tribunal similarly held that senior  
6 government officials breached the standard of fair and equitable treatment by providing assurances to  
7 the investor to safeguard its imperiled investment and then failing to act upon them – leaving the  
8 investor in the lurch.<sup>113</sup>

9 In a recent ICSID arbitral proceeding involving Mexico, the Tribunal succinctly placed the  
10 doctrine of detrimental reliance into the overarching obligation of fair and equitable treatment.

11 “This arbitral tribunal considers that this provision of the agreement, examined in the  
12 light of the good faith requirements imposed by international law, demands that the  
13 Contracting Parties to the Agreement treat the foreign investment in a manner such that  
14 it will not detract from the basic expectations on the basis of which the foreign investor  
15 decided to make its investment. Part of these expectations is that foreign investors  
16 assumption that the State receiving the investment will act consistently, without any  
17 ambiguities, and transparently in its relation with the foreign investor, so that the latter  
18 may know in advance (and thus plan its activities and define its course of action) not  
19 only the rules and regulations that shall govern such activities but also the policies  
20 pursued by such rules and regulations and the administrative practices or guidelines that  
21 are relevant in connection therewith. It is therefore expectable that the State will act in  
22 accordance with these standards, both as to the guidelines, instructions or requirements  
23 established or given - or the decisions made in compliance with - as to the reasons and  
24 purposes underlying them. The foreign investor also expects the recipient State not to  
25 act in a contradictory manner; this means, among other things, that the State will not  
26 arbitrarily reverse prior or pre-existing State-made decisions or approvals upon which  
27 the investor relied and on the strength of which it took on its commitments and planned  
28 and set in motion its economic and business operation. The investor also trusts the State  
to use the legal instruments governing the investors performance or the investment in  
accordance with the function that is typically predictable in such instruments, and at all  
events, never to use them in order to deprive the investor of its investment without  
compensation. In point of fact, the non-observance by the State receiving the investment  
of the above-mentioned standards is applicable to its relationship with the foreign  
investor or its investments impair the ability of the foreign investor to assess the kind  
of treatment and the degree of protection actually afforded by the recipient State, as well  
as its ability to determine up to what extent the conduct of such State is in keeping with  
the warranty of fair and equitable treatment. Consequently, the observance by the  
recipient State of the above mentioned standards is inextricably linked to this warranty,  
to the actual chances that it be enforced, and to the exclusion of any possibility that any

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112 *ADF* Award, at para. 189 [TAB 18].

113 *Wena Hotels Ltd. V. Egypt*, ICSID Case No. ARB/98/4, Final Award, 8 December 2000, 41 (2002) I.L.M. 896 at para’s  
85-87 [TAB 59].

1 action taken by the State would be regarded as arbitrary - in other words, when the  
2 State's conduct is pregnant with such deficiencies that they would be discerned "...by  
3 any reasonable and impartial man", or when such conduct, even if not necessarily in  
breach of specific legal provisions is contrary to law because "it shocks or at least  
surprises a sense of judicial propriety."<sup>114</sup>

4 Accordingly, as a general statement on the responsibility of States, it can be said that an investor  
5 or investment should reasonably rely on the representations of government officials. If damages are  
6 suffered as a result of such reliance, the responsibility of the State is engaged under international law.  
7 Such treatment falls below international law standards, including fair and equitable treatment, as  
8 required under customary international law and NAFTA Article 1105.

9 **B. Mexico breached the Article 1105 "Minimum Standard of Treatment"**

10 All the above-described indicia of a breach of the Article 1105 "Minimum Standard of  
11 Treatment" (denials of justice, both procedural and substantive; abuse of rights; and detrimental  
12 reliance) are present in Mexico's treatment of Thunderbird and its EDM enterprises. In making this  
13 statement, Thunderbird does not mean to imply that all of these indicia are required to establish a treaty  
14 breach under Article 1105. To the contrary, as stated above, any of these various indicia alone could  
15 be sufficient to establish a treaty breach. But, in point of fact, all of these indicia are present in Mexico's  
16 treatment of Thunderbird and its EDM enterprises. The arbitrary and unjust actions of Guadalupe  
17 Vargas taken in direct contravention to the promises and commitments made by Mexico and upon  
18 which Thunderbird and its EDM enterprises relied clearly establish Mexico's breach of its Article 1105  
19 "Minimum Standard of Treatment" obligation.

20 **1. Detrimental Reliance**

21 A clearer case of detrimental reliance would be difficult to formulate. Seeking certainty as to  
22 the propriety and legality of its intended operations, Thunderbird and EDM solicited the Mexican  
23 government for an official opinion. The August 3 solicitude [*Ex. 17*] clearly and directly stated its  
24 intention and purpose.

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26 <sup>114</sup>*Técnicas Medioambientales Tecmed, S.A. v. United Mexican States*, Merits Award, SMFTA/ICSID(AF) Tribunal, Case  
27 No. ARB(AF)/00/2; ([www.http://www.worldbank.org/icsid/cases/tecmed-award.pdf](http://www.worldbank.org/icsid/cases/tecmed-award.pdf)). Unofficial English translation, at  
28 para. 154 [TAB 60] Add case citation

1 “...We are requesting an opinion from this *Direccion General* so the entity I represent  
2 has the certainty that the commercial exploitation of video gaming machines for games  
of skill and ability is legal.” [English Translation]

3 In presenting the solicitude, Thunderbird and EDM were seeking certainty as to the legality and  
4 propriety of their proposed skill game operation before proceeding with significant investments in  
5 Mexico. Thunderbird sought an official statement upon which it could rely in pursuing those  
6 investments in Mexico. Thunderbird proceeded with this solicitude only after discarding a more  
7 adversarial approach, that of simply opening the facilities and defending against government action.  
8 [Watson, paras. 9-12; Mitchell, para. 12; Velasco, paras. 3, 4]. Thunderbird’s efforts to secure prior  
9 governmental approval of its operations were even commented upon by Mexican authorities after  
10 seizure of its facilities.

11 EDM was also very clear in what they were requesting from Mexico. The solitud stated as  
12 follows:

13 For that declared above, we have concluded that our operation is not of the type  
14 prohibited by *La Ley Federal de Juegos y Sorteros* since our video game machines do  
15 not use chance, bets or wagers, and these video games are only for the purpose of  
entertainment in which the users can obtain prizes for their skills and abilities, and I’m  
requesting from this *Direccion General* your opinion about this. [English translation]

16 The solitud described the machines to be operated:

17 The video game machines for games of skills and ability which we operate, at this  
18 present time at the place indicated above on this writings, are trademark Bestco, model  
19 MTL19U-8L and S.C.I. model 17”UR; and the entity I represent is trying to place about  
20 2,000 (two thousand) more machines at other locations in the Republic of Mexico and  
these machines are of the same identical mechanical nature and functioning as those  
described in point 3, above

21 The solitud specifically described the manner in which the machines were to be operated.

22 The video game machines for games of skills and ability, which the entity I represent  
23 commercially exploits, are devices for recreation which have been designed for the  
24 enjoyment and entertainment of its users. In these games, chance and wagering or  
25 betting is not involved, but the skills and abilities of the user who has to align different  
26 symbols on the machine screen by touching the screen or pushing buttons in order to  
27 stop the wanted symbol from several other symbols which spin in a sequential manner  
28 in each of the lanes or squares of each video game. The user has to align symbols in an  
optimum combination to receive a ticket with points which can be traded for goods or

1 services; as this is already done at different locations in the country.<sup>115</sup>

2 Thunderbird and EDM also directed the solicitud to the highest levels of the Mexican  
3 government which had direct authority over application of Mexico's gaming laws. [*Velasco, para. 8*].  
4 The solicitud was presented only after months of discussions with representatives of Gobernacion and  
5 exchanges of drafts of the document. [*Velasco, paras. 6, 7; Watson, paras. 12-15*].

6 Mexico's official response to the solicitud [*Ex. 18*] was direct and unambiguous. It stated that  
7 in its opinion:

8 . . . the machines that your representative operates are recreational video game devices  
9 for purposes of enjoyment and entertainment of its users, with the possibility of  
10 obtaining a prize, without the intervention of luck or gambling, but rather the user's  
11 ability and skillfulness.

12 Mexico further stated that as follows

13 In this light, it is important to clarify that, if the machines that your representative  
14 exploits operate in the form and conditions stated by you, this governmental entity is not  
15 able to prohibit its use. . . ,

16 An more appropriate basis for reliance upon Government statements and pronouncements would  
17 be difficult to formulate. EDM stated its desire for "certainty" as to the legality and propriety of  
18 intended operations. EDM described in detail it's intended operations. EDM detailed by make and  
19 model the precise equipment it intended to operate. EDM stated it's intention to operate as many as  
20 2000 of the identified machines throughout Mexico. EDM stated its opinion that the identified machines  
21 were not prohibited by Mexican law and directly requested the government's opinion and  
22 pronouncement upon that issue. In direct response to that solicitud, Mexico stated that if the machines  
23 were as represented in the solicitud, they were recreational devices not prohibited Mexican law and the  
24 government had no authority to prohibit their use.

25 There can be no doubt that Gobernacion knew that Thunderbird intended to rely to its detriment

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26  
27 <sup>115</sup> To this day, Mexico has produced no evidence that the machines in use at Matamoros, Nuevo Laredo, and/or Reynosa  
28 were anything other than those machines identified in the letter or that they were operating in a fashion that was in any  
respect different from that identified in the solicitud.

1 upon Mexico's response to the solicitud.<sup>116</sup> The solicitud is clear in that respect. Further, Gobernacion  
2 well understood the exact nature of the machines and their operation at the time it issued its official  
3 opinion letter. The solicitud identified the machines at issue and the nature of their operation. Further,  
4 Gobernacion had recently been involved in the Guardia litigation. That litigation established the  
5 legality of Guardia's skill machine operations. It had involved technical information and expert  
6 testimony concerning the nature and operation of skill machines. [*Watson, para. 15*].

7 In October, 2000, attorney Carlos Gomez requested permission from Gobernacion and the  
8 Department of Interior on behalf of a client other than claimant to operate skill machines. In response,  
9 Gobernacion, in a letter signed by the same individual who signed the August 15, 2000 opinion letter  
10 concerning Thunderbird's machines, requested specific information about the machines to be utilized,  
11 including make and model numbers, methods of operation, and other detailed information. [*Gomez,*  
12 *paras. 3, 4, 5; Ex. 93*]. This was the same exact information provided by Thunderbird in its August 3,  
13 2000 solicitud and in response to which Gobernacion opined that it did not have the authority to prohibit  
14 use of the machines. In both these cases, Gobernacion had sufficient knowledge and understanding of  
15 skill machines to require production of specific information about the machines in order to assess their  
16 legality.

17 Based upon the content of the solicitud, the government's apparent understanding of the nature  
18 and operation of skill machines, the content of the government's response and the level of government  
19 from which that response issued, Thunderbird and EDM had every right to rely upon Mexico's official  
20 opinion letter and were clearly reasonable in doing so. Based upon the strength of the solicitud and the  
21 government's response, Baker & McKenzie, Thunderbird's lawyers in Mexico, issued its own letter  
22 confirming Thunderbird's ability to proceed with operations. That letter stated as follows:

23 As requested, we hereby give you our opinion with respect to the official letter dated  
24 August 15, 2000, (the "Official Letter") issued by the Mexican Ministry of Interior  
25 ("Secretaria de Gobernacion") in favor of Entertainmens de Mexico, S.A. de C.V.

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26  
27 <sup>116</sup>While the evidence here indicates that Mexico knew and understood the reliance Thunderbird/EDM intend to place upon  
28 the its response to the solicitud, such knowledge and understanding by Mexico is not necessary to establish Thunderbird's  
detrimental reliance. The determinative factor is the reasonable expectation of the investor in reliance upon government  
assurances, not the intent of the state in making those assurances. [*See Section VI A 6 above*]

1 (“EDM”), and which refers to the operation in Mexico of video game skill machines.  
2 Copy of the Official Letter and the English translation thereof is attached hereto.

3 Based on the principal terms of the Official Letter, the Ministry of Interior states that it  
4 does not have any jurisdiction over the operation of said machines, since in accordance  
5 with the representations made by EDM in its application, the video games skill  
6 machines to be operated by EDM do not fall into the classification of “slot machines”,  
7 which are forbidden in Mexico pursuant to the applicable laws, in view of the fact that  
8 they are considered to be as gaming and/or betting machines.

9 Furthermore, under the Official Letter the Ministry of Interior emphasizes that EDM can  
10 operate the video games skill machines as long as they do not become, in any manner  
11 whatsoever, as gaming or betting machines; provided, however, that EDM complies  
12 with the states and/or municipal laws or regulations in Mexico.

13 Based upon the foregoing, we are of the opinion that EDM is allowed to operate in  
14 Mexico the video game skill machines as long as EDM complies with the administrative  
15 requirements set forth by the state or municipal laws and regulations in Mexico.

16 Even more, in the event the Ministry of Interior intends to close down EDM’s  
17 operations, EDM will be able to appeal, since the Official Letter allows it to operate the  
18 skill machines as such; in the understanding, that EDM must comply at all times with  
19 each and everyone of the requirements set forth by the competent authorities where the  
20 machines are operating.

21 In his declaration filed in these proceedings, attorney Ruiz de Velasco described the justifiable basis  
22 for Thunderbird’s and Baker & McKenzie’s reliance upon Gobernacion’s official opinion:

23 8. Since the official letter from Gobernacion referred to above was signed by Mr.  
24 Sergio Orozco Aceves, at that time General Director of “Gobierno”, and the “Direccion  
25 de Juegos y Sorteos”, from the Ministry of Gobernacion, which is the appropriate  
26 authority in charge of the authorization, control and surveillance of all games in which  
27 betting is involved, including games of chance (“Juegos de Azar”) and that such  
28 authority expressly states that in view of the characteristics mentioned in the application,  
the machines could not be considered as slot machines, (in which case they would fall  
as a forbidden machine), the skill machines could be operated by the Mexican company,  
it was concluded by Thunderbird to proceed to operate these machines in Mexico.

9. Based on the foregoing facts, and at the request of Thunderbird, Baker &  
McKenzie, in turn, issued a legal opinion stating that, in its opinion, and based on the  
terms and conditions contained in the official letter referred to above EDM could  
operate the skill machines in Mexico; provided, however, that in the operation of the  
machines, the Mexican company complies with the state and municipal administrative  
laws and regulations of Mexico. It should be noted that in the official letter,  
Gobernacion did not forbid the operation of the skill machines, but rather specifically  
states that Gobernacion does not have jurisdiction or authority over their operation.

The fact of, and the reasonableness of, Thunderbird’s reliance upon the August 15 official  
opinion is buttressed by the post-seizure actions and statements of Mexican officials. In a post-seizure  
meeting with Thunderbird representatives, Mr. Cabeza de Vaca, the Director of the Legal Department



1 of Gobernacion, stated that Gobernacion had interviewed Attauano, the individual who had signed the  
2 official opinion letter. de Vaca stated that Gobernacion had secured a statement from him indicating that  
3 he had not intended by the official letter what Thunderbird had inferred from it [*Watson, para. 57*].  
4 That alleged statement was not provided to the Thunderbird representatives. A copy of the alleged  
5 statement was requested in these proceedings. Mexico did not produce such a statement [*Crosby, para.*  
6 *3,4; Exs. 78, 79*]. This evidence provides a clear indication that Mexico knew that Thunderbird had  
7 reasonably relied upon that official opinion. If the opinion was not worthy of Thunderbird's reasonable  
8 reliance, why attempt to recast its meaning after the fact? If the issue truly was one of interpretation,  
9 why wasn't it raised at the outset or much earlier? in the

10 Further, de Vaca's claim of a statement from Attuanao re-casting the meaning of the August 15  
11 official opinion coupled with Mexico's repeated failure to produce such a document evidences  
12 Mexico's bad faith and lack of truthfulness in its treatment of Thunderbird. If the Attuanao statement  
13 existed, why wasn't it produced? One can only conclude that de Vaca, a high official of the Mexican  
14 government, was lying in an effort to dissuade Thunderbird from pursuing its remedies<sup>117</sup>.

15 In reliance upon Gobernacion's official opinion letter as to the propriety and legality of its  
16 intended operations, Thunderbird and its EDM entities invested millions of dollars in Mexico and  
17 created investment enterprises worth tens of millions of dollars. Thunderbird did so in full view of the  
18 Mexican government. By public documents, it created, owned and controlled a series of Mexican  
19 entities (Entertainmens de Mexico S. de R. L. De C. V., Entertainmens de Mexico Laredo S. de R. L.  
20 de C.V., Entertainmens de Mexico Reynosa S. de R.L. de C.V., Entertainmens de Mexico Puebla S. de  
21 R.L. de C.V., Entertainmens de Mexico Monterey S. de R.L. de C.V., Entertainmens de Mexico Juarez.  
22 S. de R.L. de C.V) . Those entities secured government permits and licenses. They registered with the  
23 National Registry of Taxpayers. They executed leases. They operated in full view of, and with  
24 cooperation from, local authorities. They opened skill machine facilities which catered to thousands

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25  
26 <sup>117</sup>De Vaca's misrepresentation is part of larger pattern of deceit by Mexican officials. Before the final closures, Guadalupe  
27 Vargas actively misrepresented the content of the official opinion letter. The administrative findings arising from the July  
28 hearing falsely stated that Thunderbird has not offered original documents at the hearing. The findings used that basis to  
exclude all of Thunderbird's evidence. Original documents had, in fact, been provided. Further, the signatory to those  
findings was not even present at the hearing. Post-seizure, numerous offered assistance and promised help. None was  
forthcoming.

1 of customers in highly visible downtown areas of Matamoros, Nuevo Laredo and Reynosa. [Watson,  
2 paras. 17-24, 29-32, 46; Velasco, paras. 10-14; Atallah, paras. 17-43; Ex. 19-66, 86-91].

3 Fourteen months after it's issuance of the opinion letter, Gobernacion unilaterally reversed its  
4 position and forcibly closed the facilities at Matamoros, Nuevo Laredo and Reynosa. In doing so,  
5 Mexico destroyed investment enterprises, created in reliance upon the word of the Mexican government,  
6 worth tens of millions of dollars. Thunderbird's detrimental reliance upon Mexico's official opinion  
7 and Mexico's subsequent actions against Thunderbird and its EDM entities in direct contravention to  
8 the content of that official opinion letter alone establish a clear breach of Mexico's treaty obligation of  
9 "fair and equitable treatment and full protection and security" under Article 1105.

10 "The foreign investor also expects the recipient State not to act in a contradictory  
11 manner; this means, among other things, that the state will not arbitrarily reverse prior  
12 or pre-existing State-made decisions or approvals upon which the investor relied and on  
the strength of which it took on its commitments and planned and set in motion its  
economic and business operation."<sup>118</sup>

13 But, the unjust and arbitrary manner in which Mexico proceeded against Thunderbird and its EDM  
14 enterprises serves to reinforce the lack of "fair and equitable treatment" and acts as its own independent  
15 basis for finding a breach of Article 1105 treaty obligations.

## 16 **2. Denial of Justice and Abuse of Rights**

17 Mexico's destruction of Thunderbird's investment enterprises was largely carried out through  
18 by the actions of J. Guadalupe Vargas Berrara, the Director of Juegos Y Sorteros appointed shortly after  
19 Fox took office in December, 2002. [Velasco, para. 7, 15; Watson, para.16] His actions were unjust,  
20 arbitrary and deceitful.

21 In February, 2001, Guadalupe Vargas appeared at and closed the Nuevo Laredo facility after  
22 conducting a personal, visual inspection. Based solely upon that inspection, he concluded the  
23 Thunderbird machines were "slot machines". In a telephone conversation with Peter Watson at the time  
24 of closure, Guadalupe Vargas stated he was closing the facility down because "lo que veo aqui son  
25 tragamonedas." ("What I see before me are slot machines"). [Watson, para. 26] There is no evidence  
26 that Guadalupe Vargas had any knowledge or expertise in the operation of skill machines to as to allow  
27

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28 <sup>118</sup>TecMed Award, at [TAB 60] at para. 154.

1 him to even make that determination.<sup>119</sup> Watson attempted to advise him of the difference in the  
2 operation of the two types of machines. He wouldn't listen and closed the facility anyway. He was  
3 advised of Gobernacion's official opinion letter addressing operation of the machines. He closed the  
4 facility anyway. [*Velasco, para. 15; Watson, para. 26; Atallah, para. 47; Ex. 44*].

5 When the irregularities of the closure became clear, Gobernacion and Thunderbird reached an  
6 agreement allowing Nuevo Laredo to reopen. Thunderbird and its EDM entities agreed to enter an  
7 administrative process and again address operation of the machines. Thunderbird agreed to so proceed  
8 only because it was confident the outcome could only be favorable. Thunderbird and the EDM entities  
9 were operating exactly as represented to Gobernacion in the August 3 solicitude. [*Watson, paras. 28,*  
10 *29; Velasco, para. 16; Montano, para. 11; Atallah, paras. 48, 49*]. Gobernacion had stated that such  
11 operations were not prohibited by Mexican law. [*Ex. 18*]. As such, how could Gobernacion now close  
12 them down? How could the Mexican government simply reverse course in such arbitrary fashion?

13 In a March 9, 2001 correspondence (produced by Mexico in these proceedings), Guadalupe  
14 Vargas explained his reasons for closing Nuevo Laredo. Writing to Cabeza de Vaca, Guadalupe Vargas  
15 stated as follows:

16 I am writing to inform you that this Office of Games and Raffles under my  
17 responsibility, in attention to the functions to be carried out by the Government General  
18 Directorate, in accordance with the powers granted by the Organic Law of Public  
19 Federal Administration; the Interior Regulation of the Secretary of the Interior and the  
20 Federal Law of Gaming and Raffles, articles 27, section XXII, 14 section XVII and 8  
21 respectively, carried out an inspection at the residence located in Calle Guerrero No.  
1601, corner of Maclovio Herrera, central sector of the city of Nuevo Laredo,  
Tamaulipas; and by such action secured the shutting down and closure of the location  
on the basis that we had found 120 betting machines, known as "slot machines",  
operating without the authorization of the Secretary of the Interior.

22 I The matter in question has its origin in the petition submitted by C. Juan Jose  
23 Menendez Tlcaltepa, representing the company "Entertainmens de Mexico, S.A. de  
24 C.V.", by means of a document dated 3<sup>rd</sup> August, 2000, which prompted us to reply in  
our official letter No. DGG/SP/1057/2000, dated 15<sup>th</sup> August, 2000, in which  
authorization was denied to the petitioner for the operation of the above mentioned  
machines, explaining that their operation is not permitted within the national territory.

25 II. The company referred to nevertheless decided to start operations going beyond  
26 that which is prevented by the Federal Law of Gaming and Raffles and in contravention

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27 <sup>119</sup>Mexico was asked to documents establishing such expertise and experience on the part of Guadalupe Vargas. Nothing  
28 was produced. [*Crosby, paras. 3,4; Exs. 78, 79*].

1 of the criteria communicated by the administrative authority, flagrantly violating the  
2 provisions of the law in question.

3 III. Upon becoming aware of the illegal operation, we met up at the residence in  
4 which the machines were found to be operating, and proceeded immediately to shut  
5 down, close and seal the location; notwithstanding it is worth pointing out that the  
6 company in question, considering that the act of closure was to the detriment of the  
7 individual guarantees established in articles 5, 14, 16 and 22 of the Political Constitution  
8 of the United States of Mexico, filed a proceeding for constitutional protection before  
9 the Judge of the Fifth District of the State of Tamaulipas, residing in the City of  
10 Matamoros, entered into the file under defence number 71/2000-VII-B.

11 In support of the above written, and based on article 13 section I and III of the Internal  
12 Regulation of the Secretary of the Interior, I am kindly requesting you to commence  
13 whatever actions you consider to be appropriate, using the powers conferred by the  
14 applicable norms, and for which purpose I am attaching to this letter all of the  
15 documentary background to this case. [Ex. 67].

16 The arbitrary and unjust nature of Guadalupe Vargas' actions are clearly manifested in this letter.  
17 First, Guadalupe Vargas actively misrepresents the content of Gobernacion's official opinion letter as  
18 prohibitory in nature; i.e., as denying to EDM authorization "for operating the above mentioned  
19 machines." Guadalupe Vargas sets up this misrepresentation by stating, in the first paragraph, that "we  
20 had found 120 betting machines, known as slot machines." Nowhere in this letter does Guadalupe  
21 Vargas address the permissive nature of the opinion letter. Nowhere does he address or explain whether  
22 the alleged slot machines were something other than the specific machines identified in the August 3  
23 solicitude. The August 15 opinion letter can be characterized as prohibitory only if Thunderbird and  
24 EDM-Laredo were using machines other than those identified in the official opinion letter, or in a  
25 manner different than that described in that opinion letter. Guadalupe Vargas omits any consideration  
26 of this issue.

27 This letter also clearly evidences Guadalupe Vargas' utter lack of impartiality as to the nature  
28 of the Thunderbird machines. He had clearly concluded that at the time of his first inspection, or  
perhaps before, that the machines were "slot machines". That conclusion is articulated as the basis for  
his March 9, 2001 letter to de Vaca. This evidence of pre-judgment and lack of impartiality is critical  
because Guadalupe Vargas ultimately presided over the administrative hearing out of which issued  
orders for the permanent closure of the proceedings.

Despite promises made by government officials both before and after the hearing that it would  
be conducted fairly and that its determinations would be made on a fair and just basis, the administrative

1 hearing was an unjust, arbitrary and unfair exercise of government authority by Guadalupe Vargas.

2 The arbitrary and unjust nature of these proceedings is evident simply by the fact that Guadalupe  
3 Vargas was presiding over them. *[Watson, para. 38; Velasco, para. 18; McDonald, para. 16; Atallah,*  
4 *paras. 51, 52]*. Guadalupe Vargas was an individual who had originally closed Nuevo Laredo based  
5 upon his own personal subjective beliefs about the nature of the operation. His closure of the  
6 proceedings had given rise to the administrative hearing and the reconsideration of the nature and  
7 operation of the skill machines. His pre-judgment upon that issue and lack of impartiality are  
8 established by his statements made before the hearing. At the time he initially closed Nuevo Laredo,  
9 he had stated:

10 "lo que veo aqui son tragamonedas." ("What I see before me are slot machines").

11 *[Watson, para. 26]*.

12 In his March 9, 2001 letter to de Vaca, he had stated:

13 ". . .we had found 120 betting machines, known as "slot machines", operating without  
14 the authorization of the Secretary of the Interior.

15 *[Ex. 67]*.

16 Simply the fact that Guadalupe Vargas was presiding over the hearing undercuts any notions of  
17 fairness and impartiality. The fact that he had clearly pre-judged the issues before him destroys any  
18 argument that Thunderbird and its EDM entities were provided with any manner of "fair and equitable  
19 treatment" in the administrative process leading to closure of its facilities.

20 Guadalupe Vargas' lack of impartiality was made clear by his own actions at the time of the  
21 hearing. Thunderbird and EDM had prepared a significant amount of proof, including various expert  
22 declarations attesting to the nature and operation of the Matamoros and Nuevo Laredo machines. At the  
23 commencement of the hearing, Guadalupe Vargas looked at this evidence for a matter of seconds, threw  
24 it to the corner of the desk and stated "this is just a thesis, it means nothing." Throughout the hearing,  
25 Gaudalupe Vargas repeatedly stated: "These are slot machines and nothing else." Throughout the  
26 hearing, he was nasty and disrespectful. He evidenced a clear prejudice against the foreign investment.  
27 *[Watson, paras. 38, 39, 45; Velasco, para. 18; Montano, para. 17; Gomez, para. 24]*.

28

1           The July 10 administrative hearing was far from a fair consideration of evidence and a  
2 determination by an impartial decision maker, it was an exercise in arbitrariness and pre-judgment. It  
3 was a sham proceeding. As stated above, “the opportunity to make one’s case before an independent  
4 and impartial official” is a general tenet of the due process rights to accorded a foreign investor under  
5 the Article 1105 obligation of “fair and equitable treatment”. The arbitrary and unfair nature of the July  
6 10 administrative proceeding is evidenced most clearly by the character of the authority before whom  
7 it was conducted. Guadalupe Vargas was not only acting as prosecutor and judge, he was doing so based  
8 upon his own, uninformed pre-judgment of the issues before him and a pre-determined conclusion,  
9 expressed repeatedly before the proceeding, adverse to the foreign investor before him. Again, a more  
10 clear denial of procedural due process would be difficult to articulate. This lack of impartiality directed  
11 towards a foreign investor acts as its own breach of Mexico’s Article 1105 obligation of “fair and  
12 equitable treatment”.

13           At the July 10 hearing, Thunderbird and EDM presented significant and substantial evidence  
14 attesting to the nature and operation of the skill machines. [Ex. 69]. That evidence included  
15 declarations from experts testifying to the difference between slot and skill machines and establishing  
16 that the machines used at Matamoros and Nuevo Laredo were indeed “skill machines” as originally  
17 represented in the August 3 solicitude.

18           Among the declarations provided by Thunderbird at the time of the hearing was a report secured  
19 at the request of Mexico’s own PGR, the equivalent of the U.S.’s attorney general. [Ex. 69 a] To date,  
20 this remains the only expert evidence ever provided by any agency of the Mexican government  
21 addressing the operation of the Thunderbird machines. In that report, an expert selected by PGR  
22 officials, after inspecting and analyzing the machines at Matamoros and Nuevo Laredo, stated the  
23 following:

24           WE CONCLUDE THAT ALL OF THE MACHINES WHICH OPERATE IN THE  
25 BUSINESS “LA MINA DE ORO” LOCATED IN THIS CITY, ONLY INVOLVE  
26 ABILITY AND SKILL, BY REASON OF THE FACT THAT THEIR COMPONENTS  
27 KNOWN AS “LOGIC BOARDS” (TABLES OR CARDS OF LOGIC) DO NOT  
28 CONTAIN CIRCUITS WHICH RANDOMLY CONTROL THE RESULTS, that is to  
say they are machines for games of ability and skill. [English Translation]

1 In his declaration, Kevin McDonald, the President of SCI, the manufacturer of the machines stated as  
2 follows:

3 The games described herein require significant decisions by the user which could  
4 substantially or greatly affect the result of the games. The games require the used to  
5 make independent judgments in the progressive play of the games. Each game is an  
6 active game requiring both decisions and active participation by the user as opposed to  
7 passive games such as slot machines

8 Each game described herein involves skill and dexterity

9 In his declaration, expert James Maida described and attested to the operation of skill machines as  
10 opposed to traditional slot machines. Expert Carlos Lozano stated as follows stated as follows in his  
11 declaration:

12 Further, in preparation for making this sworn declaration, I have visited the  
13 manufacturer site of Summit Amusement & Distributing in Billings Montana and  
14 reviewed similar types of machines as those which were shipped to Matamoros, and  
15 Nuevo Laredo, Tamaulipas, more specifically identified as under the NOMS attached  
16 hereto submitted herewith and incorporated herein and designated as exhibit B

17 That I have reviewed the technical data relating to said machines, I have examined and  
18 operated the actual machines, and I do hereby certify and declare that said machines  
19 comply with all accepted standards and definitions of skill machines within the meaning  
20 of skill machines for most jurisdictions in which I have reviewed the applicable law.

21 Further, I have reviewed a synopsis, translated into English, of the litigation in the  
22 Federal Court in the state of Chihuahua (60/99-III/99, January 4th, 1999), in which the  
23 court provides for a general definition of skill machines. In that case the proponent  
24 presented two machines: Sharp Image and BVC Technologies. I find that based on the  
25 definition provided by the Mexican court, the machines I have examined and which are  
26 similar to those being operated in Matamoros and Nuevo Laredo fit within the definition  
27 provided by the Mexican court

28 In conclusion, it is my professional opinion that all of the machines identified in exhibit  
B of this sworn declaration comply with the definitional requirements of a "skill  
machine" within the meanings given in most jurisdictions in which such machines are  
in use. Other such jurisdictions include, or have in the past included, Switzerland, North  
Carolina, Texas, and Oklahoma.

Despite this evidence and throughout the hearing, Guadalupe Vargas repeatedly stated: "These are slot  
machines and nothing else."

The hearing ultimately resulted in issuance of administrative findings and orders for closure of  
the facilities. [Ex. 70]. Based upon those orders, Mexico forcibly seized, closed and sealed  
Thunderbird's investment enterprises at Matamoros, Nuevo Laredo and Reynosa. The manner in which  
Thunderbird's evidence, and the official opinion letter, were dealt with in the findings again clearly

1 establishes the arbitrary and unjust nature of those proceedings.

2 First and foremost, the administrative findings and order were not even signed by an individual  
3 present at the hearing. Guadalupe Vargas presided over the hearing. Also present for the Mexican  
4 government was an attorney from the Ampara division of Gobernacion. But, the administrative findings  
5 and order leading to the final closure of the three facilities was signed by Aguilar Coronado. Further,  
6 the administrative findings and order are written in a fashion that refers, in the first person, to evidence,  
7 argument and demonstrations presented at the hearing. It is unclear how any reasonable trier of fact  
8 could reach the determination that a hearing was just, fair and impartial when the individual issuing  
9 the findings arising from that hearing was not even present.

10 Thunderbird's evidence was uniformly excluded and rejected in the administrative findings and  
11 order. At the outset, the findings excluded all evidence presented by Thunderbird and EDM because  
12 such evidence was purportedly presented, not in the form of original documents, but as photostatic  
13 copies. The findings [English translation] state as follows:

14 I) Therefore, from one or other document, it follows that the essence of this resolution  
15 is to determine whether the machines operated by Entertainments de Mexico, S. de R.  
16 L. de C. V. in the national territory fall within the scope of those prohibited by Federal  
Law on Gaming and Lottery or those which do not have a permit issued by the Secretary  
of the Interior.

17 SIXTH: In consequence, in order to reach this point, based on articles 50 and 51 of the  
18 Federal Law of Administrative Procedure, in relation to sections 79, 197, 198 and the  
19 rest relating and applicable to the Federal Code of Civil Procedure, of supplementary  
application to this law, the analysis of the evidence already submitted for the record, has  
to commence.

20 SEVENTH: Thus, in principal, it is important to point out that all documents submitted  
21 by Entertainments de Mexico S. de R.L. de C. V. by means of the deed of the 10th of  
22 July of the current year, issued by Mr. Luis Ruiz de Velasco were presented in ordinary  
photocopy.

23 In view of the above, in terms of article 217 of the Federal Code of Civil Procedure,  
24 supplementary to the Federal Order of Administrative Procedure, it is concluded that the  
25 above-mentioned documents lack clear probatory value, as a result of which they should  
26 proceed to be dismissed as such.  
27  
28



1 The factual assertion that Thunderbird and EDM presented anything other than original documents at  
2 the hearing is simply false<sup>120</sup>. Original documents were provided. [*Velasco, para. 18; Watson, para. 39*]  
3 Further, participants at the hearing on Thunderbird’s recall no issue over the admissibility and  
4 consideration of Thunderbird’s evidence. [*Watson, para. 39; Velasco, para. 18*] . But, even assuming  
5 for the purposes of argument that photocopies had been provided as opposed to original copies, for  
6 Mexico forcibly seize and close substantial foreign investments based, even in small part, on such a  
7 finding is an extraordinary denial of due process.

8 The findings go on to state that notwithstanding that the documentary proof provided by  
9 Thunderbird and EDM was “dismissed because it did not achieve the status of full proof”, it would still  
10 be given “indicative value”. The findings then proceeded to again exclude Thunderbird’s evidence on  
11 a variety of grounds.

12 Thunderbird and EDM had presented the official NOMS for the imported machines. Those  
13 documents established government knowledge of and participation in importation of the machines. The  
14 findings rejected those documents as follows:

15 The document identified by Entertainments de Mexico S. de R.L. de C.V. as “Certificate  
16 of equipment of conformity with Official Mexican Norms lacks clear probatory value,  
and neither can be given the character of presumption, because it should be treated as  
an invalid document.

17 In effect, according to what is noticed as an ordinary photo copy which exists on the  
18 files, the Director General of Electronic Normalization and Certification A.C issued  
19 Certificate No. 0002C05336, on 17<sup>th</sup> May 2000, in which was expressly pointed out that  
said document has a validity of one year, for the information of those interested parties.

20 Therefore, if such document was issued on 17<sup>th</sup> May 2000, it is logical that its validity  
21 ended on 17<sup>th</sup> May 2001, being that which was presented to this authority up to the  
following 10<sup>th</sup> July, that is to say, when it had lost its temporary validity.

22 Portions and attachments to the Declaration of Albert Atallah were excluded because they were  
23 not translated into Spanish.

24 The report secured at the request of the PGR, the equivalent of the U.S.’s attorney general  
25 attesting that the machines were in skill machines was rejected as follows:.

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27 <sup>120</sup>Perhaps this statement derives from the fact the signatory of the findings was not at the hearing and perhaps did not  
28 ultimately see original evidence.

1 In respect of the first of the abovementioned documents, it should be noted that the  
2 description provided by the company which is subject to administrative procedure tends  
3 to generate confusion as it is not exactly an expert testimony of the Attorney General of  
4 the Republic, as wrongly stated, but rather of an expert testimony requested by the  
5 Attorney General of the Republic written by personnel of a private company called  
6 NetComm Systems and Telecommunications according to the ordinary photo static copy  
7 attached to the file.

8 Consequently, it is evident that we are in the presence of a private document and not a  
9 public document, which fact could be misinterpreted in this matter

10 The declaration of Kevin McDonald, attesting to the nature and operation of the machines and that they  
11 were in fact skill machines was excluded as follows

12 Referring to the second of the documents mentioned, as well as being an ordinary  
13 photocopy, it is assumed that it had expired by the 5<sup>th</sup> of July of this year, that is to say  
14 before having being offered as evidence in this matter.

15 In light of the foregoing, in the Spanish translation of the document can be seen an  
16 inscription in a foreign language, apparently inserted by Vicky A. Diaz, who it is  
17 presumed is a Notary Public in California, together with a seal on which appears the  
18 inscription "COMM. EXP. JULY 5, 2001" and that Mr. Kevin McDonald signed it on  
19 the 7<sup>th</sup> of March of the current year, the date on which he apparently appeared before  
20 said Notary Public, who, it is clear, does not have any legal competence in the national  
21 territory.

22 As to the expert declarations of Maida, Lozano, Griffin and Reeves, the findings excluded as follows:

23 In relation to all of the foregoing information, the conclusion is that, to begin within one  
24 of those who signed such documents guarantee that they are who they say they are, even  
25 in a presumptive manner, and as such this authority finds it to be legally and materially  
26 impossible to recognize the truth of her statement.

27 In addition, the majority of those persons are recognized as having knowledge of the  
28 legislation of other countries. None of them admit to having experience of the Federal  
29 Law on Gaming and Lottery, which is the only law that governs in this matter in the  
30 national territory.

31 Corroborating this information it is noticed that the majority conclude that a game of  
32 skill is that in which the player plays an active role and his decisions have an effect on  
33 the result of the game.

34 Nevertheless, it may go unnoticed that in conformity with article 27, section XXII of the  
35 Organic Law of Federal Public Administration, it falls to the Secretary of the Interior to  
36 regulate, authorize and inspect the game, the bets, lotteries and raffles, in terms of the  
37 relative laws.

38 In the same way, they all forget that article 3 of the Federal Law on Gaming and Lottery  
39 establishes that the regulation, authorization, control and vigilance of games which  
40 involve betting of any type, is the responsibility of the Federal Executive, acting through  
41 the Secretary of the Interior.

1 Therefore, their definitions of games of chance and gambling games, deal only with their  
2 own personal subjective valuations, which lack the basis to link them with the decision  
3 adopted in the current resolution, as they are not issued by any authority referred to in  
4 the legislation noted in the preceding paragraphs.

5 In addition to the foregoing, in as much as reference is made to a document identified  
6 in numeral IV above, it is worth noting that, not only do the assertions come from an  
7 employee of the artificial company which is today the subject of these proceedings,  
8 which shows a certain burden of subjectivity in his declarations, neither these, nor the  
9 accompanying documents merit any consideration whatsoever by this authority, because  
10 the fact that he is an employee does not give him any legitimacy to provide documents  
11 which, in any case, must only be provided by the legal representative, and not by a  
12 different person with the characteristic of “employee”.

13 Finally, and in any case, it should be recalled that article 203, second paragraph of the  
14 Federal Code of Civil Procedures, which is supplementary to the Federal Law on  
15 Administrative Procedure, remarks that a private document which contains a declaration  
16 of the truth, certifies the existence of the declaration, but not the facts declared.

17 The findings ultimately rejected all expert testimony.

18 For this reason, as a result of the considerations noted in this WHEREAS the outcome  
19 is to deny expert on the matters, which he addresses.

20 Having dispensed with any actual, or expert, testimony as to the true manner of operation of the  
21 machines, the findings proceed with a description as to why the machines are illegal:

22 Now, Entertainments de Mexico S. de R.L. de C.V. will be asking itself why the legal  
23 dispositions which have been elaborated in the current case are applicable.

24 From the proofs put into the record as Appendices Three and Four, it seems that a  
25 machine that works by electricity effectively requires an interaction with the player for  
26 it to function.

27 In order for this player to have access to the machine, according to Mr. Francisco Ortiz  
28 he has to insert “dollar”, which is understood to mean the legal tender of the United  
States of North America, as Mr. Ortiz declared that it accepted different denominations  
of the dollar.

It is logical that, in order to acquire these dollars, the player must pay out Mexican  
pesos, legal tender of the national territory, that is to say he must buy dollars with pesos,  
or other wise he could not pay.

Upon inserting the dollars in order to start the game, one is in the presence of a “cash  
slot machine” and not a “token slot machine”.

According to what was observed in the case of the cash slot machine that was exhibited  
in the current administrative procedure, there appeared on the screen some figures,  
which the player had to match in order to win.

Nevertheless, the form in which the figures appear on the screen is not according to the  
wishes of the player, but rather in a manner displayed by the machine, which is

1 considered to be an event, which does not depend on the skill of the one operating the  
2 machine, but rather on the working of the machine itself.

3 In other words, the player does not enjoy the freedom to make the figures appear on the  
4 screen in such a way that they match, but rather, in every case a chance or coincidental  
5 event is what allows them to match and thus for the player to win.

6 Therefore, it cannot be validly affirmed that cash slot machines operate on the basis of  
7 ability or skill of the player, as none of his senses will allow him to order the machine  
8 to display figures for his convenience.

9 In effect, the player cannot manipulate the machine either with sight, smell, enjoyment,  
10 touch or hearing in order to win. The speed of his hands only allows him to gain time  
11 over another player in order to stop the figures, and never to achieve his wish that they  
12 match with those shown by the machine, so as can be seen, this circumstance is subject  
13 to the operation of the machine and not the will of the player.

14 Therefore, we are in the presence of games of chance, in which fortune, the  
15 unpredictable, the indeterminate, coincidence and luck are the elements that operate the  
16 machine in question.

17 In this sense, as the player has no control over the machine, it is obvious that luck is  
18 what makes him win on some occasions and lose on others. On either assumption, in  
19 order to play again, he has to buy dollars, which generally implies using Mexican Pesos  
20 in his purchase.

21 Further, if he wins, he makes a profit; if he loses the player's capital will be diminished.

22 The fact that in certain types of people, games of this type create an addiction, and  
23 therefore cause excessive expenditure in the purchase of dollars in order to play, is in  
24 the public domain, and does not require any proof.

25 It follows that the thesis previously upheld by the First Chamber of the Supreme Court  
26 of Justice of the Nation, published in the Judicial Federation Weekly, Volume CXIX,  
27 page 3521, must be taken account, in which the intention of the legislator in regulating  
28 games of chance and games involving betting, was to eliminate those games which  
promote an excessive or prohibited profit, as well as large losses which cause the  
financial ruin of the players, to the detriment of the national economy.

21 These findings are counter to all the evidence provided by Thunderbird and EDM at the hearing  
22 and are clearly designed to make reach the pre-ordained conclusion that the machines are illegal. It must  
23 pointed that these conclusions can be based only upon the personal observations of Guadalupe Vargas,  
24 who presided over the hearing and whose lack of impartiality is clearly established by his own  
25 statements and writings made before the hearing. The signatory to the findings and order was not  
26 present at the hearing. How he could opine upon the operation of the demonstration machine when he  
27 was not present at the hearing is unexplained. The nature of any post-hearing communications between  
28 Guadalupe Vargas and the signatory of the findings as well as the events leading to actual drafting of

1 the findings is also unexplained. Further, Mexico presented no evidence at the hearing and none is cited  
2 in the findings and order.

3 The finding's summary discussion of the government's official opinion letter simply carried  
4 forward the mis-characterization of that opinion first set forth in Guadalupe Vargas 's earlier letter to  
5 de Vaca. The findings state:

6 Public Document DGG/SP/1057/200 of 15<sup>th</sup> August, 2000, signed by the then Director  
7 of Games and Raffles, in the absence of the Director of Games and Raffles, is not an  
8 obstacle to the above, in that the contents of the said document in no way constitute an  
9 authorization for the operation of cash slot machines which are the subject of this  
10 resolution, as in a mistaken way, the company involved in this administrative procedure  
11 is trying to demonstrate.

12 Having already subjectively characterized the machines as illegal slot machines, the findings falsely  
13 characterized the official opinion letter as prohibitory in nature and precluding use of the subject  
14 machines by Thunderbird and EDM. Nowhere in the administrative findings and order is any evidence  
15 cited to the effect that Thunderbird and EDM were operating the machines in a fashion which in any  
16 way differed from that described in the August 3 solicitude. The administrative findings were simply  
17 a re-statement, in a legalistic format, of the pre-conceived subjective opinion of Guadalupe Vargas that  
18 the machines were slot machines.

19 - Guadalupe Vargas, upon closing the Nuevo Laredo in February, 2001:

20 ***"lo que veo aqui son tragamonedas."*** (***"What I see before me are slot machines"***).  
21 *[Watson, para. 26]*

22 - Guadalupe Vargas, in March, 2001 correspondence to de Vaca:

23 ***". . .we had found 120 betting machines, known as "slot machines", operating***  
24 ***without the authorization of the Secretary of the Interior.***  
25 *[Ex. 67].*

26 - Guadalupe Vargas, commenting upon Thunderbird's evidence at the commencement of  
27 the July 10, 2001 administrative hearing over which he presided:

28 ***"this is just a thesis, it means nothing."***  
*[Watson, para. 26].*

1 - Guadalupe Vargas, throughout the course of the July 10, 2001 administrative hearing  
2 over which he presided:

3 ***“These are slot machines and nothing else.”***

4 *[Watson, para. 26; Velasco, para. 18; Montano, para. 17].*

5 - The October 10, 2001 administrative findings:

6 **Finally, having confirmed that the prohibition of games of betting and raffles,**  
7 **subject to the exceptions and conditions established by law, and the issuing of**  
8 **discretionary powers to this authority, have the objective of avoiding prohibited**  
9 **profit for the organizers and the financial ruin of the players, it is concluded that**  
10 **the cash slot machines operated by Entertainments de Mexico S. de R.L. de C.V.,**  
11 **in the national territory, fall within the prohibitions of the Federal Law on Gaming**  
12 **and Lottery, and further, that they are operated without the permission of the**  
13 **Secretary of the Interior, in terms of the legislation applicable to the case in point.**

14 *[Ex. 70].*

15 The hearing and the findings arising from it were a sham. There was no impartiality, no consideration  
16 of Thunderbird’s evidence, no affirmative evidence of illegality, no objective analysis of the facts and  
17 circumstances and no fair consideration of the government’s prior opinion letter. There was just the  
18 personal opinion of a biased government official reaching a pre-conceived conclusion.

19 Even the manner in which the administrative findings and order were served acts to illustrate  
20 the unjust and arbitrary nature of the Mexican government actions towards Thunderbird and its EDM  
21 enterprises. The administrative findings and order were served upon Thunderbird’s Mexico counsel  
22 on the afternoon of October 11, 2001. While EDM should have been allowed an appeal, the order was  
23 executed almost immediately. Within an hour, Mexico law enforcement officials in a highly publicized  
24 fashion, seized, closed and sealed the facilities at Matamoros and Nuevo Laredo. It seized, closed and  
25 sealed the facilities at Reynosa several months later in similar fashion.

26 Mexico’s arbitrary actions continued after it’s seizure and closure of the facilities. Thunderbird  
27 was repeatedly offered assistance by various government officials. None was forthcoming. Thunderbird  
28 was promised an independent analysis of its machines and the right to re-open if the machines proved

1 to be, in fact, skill machines. That analysis never occurred. Evidence suggests improper efforts to  
2 influence the judges hearing Thunderbird’s post-seizure legal cases. Thunderbird representatives were  
3 told they were the “good guys”, “the only ones sought prior approval” for their skill game operations.  
4 Yet, no actions were taken to fairly address Thunderbird’s situation. In the end, Cabeza de Vaca went  
5 so far as to suggest that Thunderbird had mis-interpreted the official opinion letter. He claimed to have  
6 a statement from the author indicating that he did not mean what Thunderbird had inferred from the  
7 letter. No such statement was ever produced.

### 8 **3. Conclusion**

9 These facts clearly establish a breach of the “Minimum Standard of Treatment” obligation under  
10 Article 1105 of NAFTA. Thunderbird and its EDM entities detrimentally and reasonably relied upon  
11 the actions and statements of the Mexican government in pursuing its investment enterprises. Over a  
12 year later, Mexico reversed course and reneged on its official statements causing Thunderbird and its  
13 EDM enterprises to lose investments worth tens of millions of dollars. Through arbitrary actions lacking  
14 any notions of impartiality, Mexico seized, closed and sealed these investment enterprises.<sup>121</sup> The  
15 reasons behind Mexico’s reversal of position and subsequent destruction of Thunderbird’s investments  
16 enterprises are unknown. The timing of the actions (i.e., commencing shortly after a change of  
17 administration), the acquiescence of high government officials in the actions of Guadalupe Vargas and  
18 the favorable treatment given to its own investors undertaking identical activities clearly suggest a  
19 conscious governmental directive by Mexico to single out and proceed against a foreign investor.

20 Mexico did not provide “fair and equitable treatment” to Thunderbird and its EDM entities in  
21 relation to their investment enterprises. Mexico has breached its Article 1105 obligation and should be  
22 held responsible for damages arising from that breach.

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27 <sup>121</sup>It should be noted that Thunderbird is not required to establish **both** detrimental reliance **and** the unjust and arbitrary  
28 denial of justice or abuse of rights. Thunderbird may prevail on an Article 1105 claim on facts establishing **either**  
detrimental reliance **or** an abuse of rights or denial of justice. But, what is clear from the evidence is that all of these potential  
bases establishing a treaty breach under Article 1105 are present

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VII.

**MEXICO EXPROPRIATED THE THUNDERBIRD INVESTMENTS WITHOUT  
COMPENSATION IN VIOLATION OF NAFTA ARTICLE 1110.**

**A. Article 1110 and “Expropriation”**

**1. Article 1110**

NAFTA Article 1110 provides for the payment of compensation for any expropriation, regardless of whether such a taking is lawful under international law. This is because Article 1110(1) provides that, under all circumstances, regardless of whether the taking is for a public purpose, non-discriminatory or otherwise in accordance with the minimum standard of treatment, compensation must be paid in accordance with the other paragraphs of this provision. Article 1110 states, in relevant part:

1. No Party may directly or indirectly nationalize or expropriate an investment of an investor of another Party in its territory or take a measure tantamount to nationalization or expropriation of such an investment ("expropriation"), except:
  - (a) for a public purpose;
  - (b) on a non-discriminatory basis;
  - (c) in accordance with due process of law and Article 1105(1); *and*
  - (d) on payment of compensation in accordance with paragraphs 2 through 6.
2. Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place ("date of expropriation"), and shall not reflect any change in value occurring because the intended expropriation had become known earlier. Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.
3. Compensation shall be paid without delay and be fully realizable.
4. If payment is made in a G7 currency, compensation shall include interest at a commercially reasonable rate for that currency from the date of expropriation until the date of actual payment.
5. If a Party elects to pay in a currency other than a G7 currency, the amount paid on the date of payment, if converted into a G7 currency at the market rate of exchange prevailing on that date, shall be no less than if the amount of compensation owed on the date of expropriation had been converted into that G7 currency at the market rate of exchange prevailing on that date, and interest had accrued at a commercially reasonable rate for that G7 currency from the date of expropriation until the date of payment.



1           6.       On payment, compensation shall be freely transferable as provided in Article  
2           1109.

3           **2.       Article 1110 “Expropriation” Standards.**

4           Five NAFTA Tribunals have considered the meaning of this provision, and have together  
5 provided a clear view of how it should be interpreted and applied. The first significant award was made  
6 by the *Pope & Talbot* Tribunal, which began by determining that the object of an expropriation under  
7 Article 1110 is the “investment of an investor of a NAFTA Party.” This term is defined under Article  
8 1138, and includes any of tangible or intangible property interests included there in. It is not limited  
9 to any particular form of property, such as an interest in land, and is intimately tied to the nature of the  
10 business in question.<sup>122</sup>

11           Next, the *Pope & Talbot* Tribunal confirmed that the kinds of interference envisaged in NAFTA  
12 Article 1110 (including direct nationalization, indirect expropriation and measures tantamount to  
13 expropriation) do not depart from that which is available under customary international law.<sup>123</sup> It also  
14 concluded that merely because a State claims that its actions are not overtly discriminatory and are  
15 justified as an exercise of its “police” (or regulatory) power, does not mean that compensation does not  
16 need to be paid under Article 1110(1). In doing so, the Tribunal noted:

17           Indeed, much creeping expropriation could be conducted by regulation, and a blanket  
18 exception for regulatory measures would create a gaping loophole in international  
19 protections against [uncompensated] expropriation.<sup>124</sup>

20           Finally, the Tribunal provided an excellent articulation of the current test of what kind of  
21 interference constitutes a taking under modern international law, in stating:

22           While it may sometimes be uncertain whether a particular interference with business  
23 activities amounts to an expropriation, the test is whether that interference is sufficiently  
24 restrictive to support a conclusion that the property has been “taken” from the owner.  
25 Thus the *Harvard Draft* defines the standard as requiring interference that would justify  
26 the inference that the owner will not be able to use, enjoy or dispose of the property...”  
27 The *Restatement*, in addressing the question of whether regulation may be considered

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28           <sup>122</sup>*Pope & Talbot, Inc. v. Canada*, Interim Merits Award, NAFTA/UNCITRAL Tribunal, 26 June 2000, at para’s. 95 & 96-98 [TAB 61].

27           <sup>123</sup>*Id.* at 96 & 103-104.

26           <sup>124</sup>*Id.* at 99.

1           expropriation, speaks of “action that is confiscatory, or that prevents, unreasonably  
2           interferes with, or unduly delays, effective enjoyment of an alien’s property.” Indeed,  
3           at the hearing, the Investor’s counsel conceded, correctly, that under international law,  
4           expropriation requires a “substantial deprivation.”<sup>125</sup>

5           The Tribunal in *Myers* concluded that an expropriation “usually amounts to a lasting removal  
6           of the ability of an owner to make use of its economic rights although it may be that, in some contexts  
7           and circumstances, it would be appropriate to view a deprivation as amounting to an expropriation, even  
8           if it were partial or temporary.” In the case before it, the *Myers* Tribunal determined that the measure  
9           only delayed Myers’ entry into the Canadian market for 14 months, rather than completely frustrating  
10          it.<sup>126</sup> Accordingly there was no expropriation.

11          By contrast, in *Wena Hotels*, the Tribunal noted that being deprived of access to its investment  
12          for only one year was sufficient to have deprived the investor of its enjoyment of the investment in a  
13          manner which was more than “ephemeral.”<sup>127</sup> The hotel had been appropriated by a State-sponsored  
14          tourist agency, and although control was eventually relinquished, the condition of the facilities upon  
15          return was poor.

16          The “merely ephemeral” standard can be found in the oft-quoted Iran-US Claims Tribunal case,  
17          *Tippets, Abbett, McCarthy, Stratton v. TAMS-AFFA*, which the *Wena Hotels* Tribunal cited at  
18          paragraph 98 of its award:

19               [W]hile assumption of control over property by a government does not automatically  
20               and immediately justify a conclusion that the property has been taken by the  
21               government, thus requiring compensation under international law, such a conclusion is  
22               warranted whenever events demonstrate that the owner has been deprived of  
23               fundamental rights of ownership and it appears that this deprivation is not merely  
24               ephemeral.<sup>128</sup>

25          After reviewing the expropriation findings including in these NAFTA cases, Professor

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26               <sup>125</sup>*Id.* at 102.

27               <sup>126</sup>*Myers* Merits Award, at 283 & 287 [TAB 5].

28               <sup>127</sup>*Wena Hotels* Award, at para. 99 [TAB 59].

<sup>128</sup>*Tippets, Abbett, McCarthy, Stratton v. TAMS-AFFA Consenting Engineers of Iran et al.*, Iran-U.S. Claims Tribunal,  
Award No. 141-7-2, June 22, 1984, at para. 225 [TAB 62].

1 Loewenfeld has adroitly observed about BIT practice (in which he includes the NAFTA Chapter 11  
2 jurisprudence):

3 It seems clear from the cases here excerpted and others that expropriation as governed  
4 by the BITs is defined by the deprivation to the investor, not by the gain to the host state.  
5 Thus destruction of the investor's property may come within the definition of  
6 expropriation if the actions are attributable to the host state, even if the state does not  
7 acquire the property in question. Further, intangible rights, such as the right to import  
8 or export a given product or to participate in a given industry, may be subject to the  
9 constraints on expropriation set out in the BITs. However, a regulation of temporary  
10 duration, or a regulation that reduces the profitability of an investment but does not shut  
11 it down completely and leaves the investor in control, will generally not be seen as  
12 expropriation, even when it gives rise to liability on the part of the host state for  
13 violation of national treatment and fair and equitable treatment clauses.<sup>129</sup>

9 The *CME* Tribunal has also similarly held:

10 The expropriation claim is sustained despite the fact that the Media Council did not  
11 expropriate CME by express measures of expropriation. De facto expropriations or  
12 indirect expropriations, i.e. measures that do not involve an overt taking but that  
13 effectively neutralize the benefit of the property of the foreign owner, are subject to  
14 expropriation claims. This is undisputed under international law (G. Sacerdoti page 382  
15 as cited above, referring to numerous precedents such as the German Interests In Polish  
16 Upper Silesia case, 1926, PCIJ, Series A, No. 7, reprinted in M. Hudson, ed., I World  
17 Court Reports 475 (1934); see also Southern Pacific Properties (Middle East) Ltd. v.  
18 Egypt, ICSID Case No. ARB/84/3 (1992), 32 I.L.M. 993, 1993, dealing also with the  
19 expropriation of contractual rights of the operating company).<sup>130</sup>

16 The *CME* Tribunal also cited, with approval, the reasoning of the *Metalclad* Tribunal that an  
17 expropriation under Article 1110:

18 ... included not only open, deliberate and acknowledged takings of property, such as  
19 outright seizure or formal or obligatory transfer of title in favor of the host State, but  
20 also covert or incidental interference with use of property which has the effect of  
21 depriving the owner, in whole or in significant part, of the use or reasonably to be  
22 expected economic benefit of property even if not necessarily to the obvious benefit of  
23 the host State.<sup>131</sup>

22 The *Metalclad* Tribunal was presented with a situation where the investor was led to believe that  
23 it had all the necessary federal and state authorizations to operate its newly constructed facility – only  
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25 <sup>129</sup>Andreas F. Lowenfeld, *International Economic Law* (Oxford, Cambridge: 2002) at 479-480 [TAB 63].

26 <sup>130</sup>*CME Czech Republic B.V. (The Netherlands) v. Czech Republic*, Partial Award, UNCITRAL Tribunal, 3 September 2001,  
27 at para. 604 [TAB 64].

28 <sup>131</sup>Id. at para. 606; citing the *Metalclad* Award at para. 103 [TAB 8]

1 to be prevented from doing so through political intrigue and the questionable legal tactics of local and  
2 state officials. It was also presented with a bold “ecological decree” issued by the governor during his  
3 last days in office which was admittedly designed to ensure that the facility was never operated. The  
4 Tribunal accordingly found that the business of the investor had been taken without the payment of  
5 appropriate compensation, contrary to NAFTA Article 1110, on both counts.<sup>132</sup>

6 With respect to the expropriatory impact of the so-called ecological decree, the *Metalclad*  
7 Tribunal also noted that it did not need to consider the motivation or intent behind its imposition. While  
8 Article 1110(1) provides that an expropriation can be undertaken “for a public purpose” it also provides  
9 that, in any case, prompt, adequate and effective compensation shall be paid.

10 The *Feldman* Tribunal has also found that:

11 If there is a finding of expropriation, compensation is required, *even if* the taking is for  
12 a public purpose, non-discriminatory and in accordance with due process of law and  
Article 1105(1).<sup>133</sup>

13 However the Tribunal has also noted that not all regulatory actions which indirectly confiscate  
14 a business are compensable takings under the customary international law of expropriation, as expressed  
15 in Article 1110.

16 In order to discern the line between legitimate acts of governmental regulation and compensable  
17 takings under international law, the *Feldman* Tribunal found assistance in commentary (g) to Section  
18 712 of the *Third U.S. Restatement on International Law*, which provides:

19 A state is responsible as for an expropriation of property under Subsection (1) when it  
20 subjects alien property to taxation, regulation, or other action that is confiscatory, or that  
21 prevents, unreasonably interferes with, or unduly delays, effective enjoyment of an  
22 alien’s property or its removal from the state’s territory... A state is not responsible for  
loss of property or for other economic disadvantage resulting from bona fide general  
taxation, regulation, forfeiture for crime, or other action of the kind that is commonly  
accepted as within the police power of states, if it is not discriminatory....<sup>134</sup>

23 Finding support in the notes of the *Restatement’s* author, the *Feldman* Tribunal resolved that  
24 the determination of whether an expropriation has taken place must be performed on a case-by-case

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26 <sup>132</sup>*Metalclad* Award, at para’s. 102-112 [TAB 8].

27 <sup>133</sup>*Feldman* Award, at 98 [TAB 12].

28 <sup>134</sup>*Id.* at 105.

1 basis, in view of the totality of the facts. For the *Feldman* Tribunal the key factor appeared to be the  
2 same one found by the *Pope & Talbot* Tribunal – that because the investment enterprises of each  
3 investor were still “in business” and under the control of their respective investors, the interference with  
4 these investments had simply not been *substantial* enough to constitute a taking under international  
5 law.<sup>135</sup> Nonetheless, the *Feldman* Tribunal also noted that:

6 not all government regulatory activity that makes it difficult or impossible for an  
7 investor to carry out a particular business, change in the law or change in the application  
8 of exiting laws that makes it uneconomical to continue a particular business, is an  
9 expropriation under Article 1110.

10 Besides the obvious question of whether there exists “a substantial interference with the  
11 investment,” the *Restatement* commentary mentioned above can also provide some direction as to how  
12 to decide whether the interference in question constitutes a compensable taking under international law.  
13 One should consider the overall “reasonableness” of the taking, including the manner of its imposition,  
14 and whether there were any discriminatory results. As the *Feldman* Tribunal suggests: the more  
15 arbitrary or discriminatory the measure which takes an investor’s business without providing  
16 compensation, the more likely that there is a breach of Article 1110.<sup>136</sup>

17 Another factor is whether the taking is general or specific in application. The *Feldman* Tribunal  
18 was presented with the impact of a tax measure of general application, rather than a regulatory activity  
19 which was directed at any particular enterprise or individual. Also, the *Feldman* Tribunal was presented  
20 with an investor that did not take advantage of administrative procedures which would have provided  
21 considerable certainty as to whether the business activity in which it was engaged was properly subject  
22 to the tax treatment that the investor sought to receive.<sup>137</sup>

23 Accordingly, the general rule for consideration of whether government action constitutes a  
24 compensable taking, under Article 1110, is based upon an objective analysis of the facts of each case,  
25 with an emphasis on determining whether there exists some sort of “substantial” and unreasonable (or

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26 <sup>135</sup>*Pope & Talbot* Interim Merits Award, at 103-104 [TAB 61]; *Feldman* Award, at 102, 106 & 111 [TAB 12].

27 <sup>136</sup>*Feldman* Award, at 99 [TAB 12]

28 <sup>137</sup>*Id.* at 134.

1 perhaps unjustifiable) interference with the business of the investment in question.

2 **B. Mexico Expropriated the Thunderbird Investments.**

3 Article 1110 provides that no NAFTA party may directly or indirectly expropriate, or take  
4 measures tantamount to the expropriation of, an investment of an investor of another party unless (a)  
5 for a public purpose; (b) on a non-discriminatory basis; (c) in accordance with due process of law and  
6 Article 1105(1); and (d) upon payment of compensation. NAFTA Article 1110.

7 The threshold issue under 1110 analysis is to determine whether an expropriation has occurred.  
8 The *Pope and Talbot* Tribunals stated that the test is whether the government interference “is  
9 sufficiently restrictive to support a conclusion that the property has been taken from the owner” and “as  
10 requiring interference that would justify the inference that the owner will not be able to use, enjoy or  
11 dispose of the property.”<sup>138</sup> The *Myer* tribunal concluded that expropriation usually amounts to “a  
12 lasting removal of the ability the owner and make use of its economic rights although it may be that,  
13 in some context and circumstances it would be appropriate to view deprivations amounting to an  
14 expropriation, even if it were partial or temporary”.<sup>139</sup> [See Section VII A 2 above]

15 Applying these standards, it is clear that Mexico has expropriated Thunderbird’s EDM  
16 investment enterprises. Mexico forcibly seized, closed and sealed the Thunderbird EDM facilities at  
17 Matamoros, Nuevo Laredo and Reynosa. It did so pursuant to an administrative edict that effectively  
18 prohibits any further development of skill game operations by Thunderbird and its various EDM  
19 enterprises. This is not a case of “creeping regulatory action” or “merely ephemeral“ deprivation of an  
20 investment. In this case, Mexico acted directly against Thunderbird’s EDM enterprises, seizing and  
21 permanently closing its facilities. Thunderbird’s machines, equipment and other property remain seized  
22 and sealed in Mexico beyond Thunderbird’s control or that of the EDM entities.

23 For the reasons stated above [See Section VI B above], Mexico will not be able to establish that  
24 this taking was for a public purpose and on a non-discriminatory basis and in accordance with due  
25 process of law. Mexico’s expropriation of Thunderbird’s investment enterprises was unjust, arbitrary

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27 <sup>138</sup> *Pope & Talbot* Interim Merits Award, at para. 102 [TAB 61]

28 <sup>139</sup> *Myers* Merits Award, at para. 283 [TAB 5].

1 and blatantly discriminatory. But, even assuming solely for the purpose of argument that Mexico could  
2 establish a public purpose for and a non-discriminatory basis for the taking and that the taking was  
3 undertaken in accordance with due process, Mexico would still be required to pay compensation  
4 equivalent to the fair market value of the expropriated investment as of the date of expropriation.

5 “If there is a finding of expropriation, compensation is required, even if the taking is for  
6 a public purpose, non-discriminatory and in accordance with due process of law and  
Article 1105(1).”<sup>140</sup> [*Feldman award at 98*]

7 Mexico expropriated Thunderbird’s investment enterprises without compensation in violation of  
8 NAFTA 1110. It is required to pay compensation for that taking.

## 9 VIII.

### 10 DAMAGES

#### 11 A. The International Law of Damages

##### 12 1. The Requirement of Full Restitution Value

13 The appropriate principles to be employed to compensate a foreign investor for the illegal  
14 treatment of its investment can be found in the decision of the Permanent Court of Justice in the  
15 *Chorzow Factory* case.<sup>141</sup> In the *Chorzow Factory* case, the Permanent Court addressed the question  
16 of quantification of damages arising from an unlawful expropriation. The Permanent Court stated that:

17 The essential principle contained in the actual notion of an illegal act ... is that  
18 **reparation must, as far as possible, wipe-out all the consequences of the illegal act**  
19 **and reestablish the situation which would, in all probability, have existed if that**  
20 **act had not been committed.** Restitution in kind, or, if this is not possible, payment  
21 of a sum corresponding to the value which a restitution in kind would bear; the award,  
if need be, of damages for loss sustained which would not be covered by restitution in  
kind or payment in place of it - such are the principles which should serve to determine  
the amount of compensation for an act contrary to international law.<sup>142</sup> [**emphasis**  
**added**]

22 Thus, the Permanent Court enunciated the principle that the goal for a trier of fact is to put a  
23 claimant back into the same position that it would have been “but for” the occurrence of the illegal act  
24 and that the amount of compensation to be provided. Accordingly, the quantum of damages “...is not

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25 <sup>140</sup> *Feldman Award*, at 98 [Tab 12].

26 <sup>141</sup> *Myers Award*, at para’s. 311 - 315 [TAB 5]; See, also: *S.D. Myers, Inc. v. Canada*, NAFTA/UNCITRAL Tribunal,  
27 Damages Award, 21 October 2002 [TAB 65].

28 <sup>142</sup> *Case Concerning the Factory at Chorzow (Merits)* PCIJ, Series A, No. 7, 13 September 1928 at 47 [TAB 66].

1 necessarily limited to the value of the undertaking at the moment of dispossession, plus interest to the  
2 day of judgment.”<sup>143</sup> This approach has been endorsed by many mixed claims tribunals. For example,  
3 the ICSID Tribunal in *Amco Asia Corp. v. Indonesia* noted that the reasoning adopted in the *Chorzow*  
4 *Factory* case constitutes the fundamental precedent on the law of compensation in international  
5 claims.<sup>144</sup>

6 In its partial award on liability and the theory of damages, the Tribunal in *S.D. Myers, Inc. and*  
7 *Canada* (“*Myers* Tribunal”) stated that, in addition to the compensation principles espoused in the  
8 *Chorzow Factory* Case, the following principles also apply to an investor-state claim brought under the  
9 NAFTA:

- 10 (I) compensation is payable only in respect of harm that is proved to have a  
11 sufficient causal link with the specific NAFTA provision that has been breached;  
12 the economic losses claimed by [the Investor] must be proved to be those that  
13 have arisen from a breach of the NAFTA, and not from other causes; [and]  
14 (ii) damages for breach of any one NAFTA provision can take into account any  
15 damages already awarded under a breach of another NAFTA provision; there  
16 must be no “double recovery”.<sup>145</sup>

17 To wipe out the consequences of the illegal acts, and to re-establish the situation that would have  
18 existed “but for” those acts, it is necessary to determine a “full restitution value” in respect of the  
19 harmed investor and investment. This value takes into account the extent of economic benefits that  
20 the investor and its investment would have realized in all probability if the acts had not been committed.  
21 Such benefits would include lost profits and consequential losses (in particular related to the loss of  
22 competitive advantage and market share), as well as all costs of defending against the illegal acts and  
23 an appropriate rate of interest thereupon.

24 The principle of integral restitution espoused by the Permanent Court in the *Chorzow Factory*  
25 case has been supported by a number of contemporary international tribunal decisions. For example,  
26 the Iran–US Claims Tribunal supported the compensation approached taken in the *Chorzow Factory*

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27 <sup>143</sup> *Id.* at 47. This Tribunal has recognized that the *Chorzow Factory* case supports the principle that “compensation should  
28 undo the material harm inflicted by a breach of an international obligation; See: *Myers* Award, at para 315 [TAB 5].

<sup>144</sup> *Amco Asia* Merits Award, at 500 [TAB 54].

<sup>145</sup> *Myers* Award, at para. 316 [TAB 5].



1 case.<sup>146</sup> The chamber in the *Amoco* case noted the distinction that would arise from whether the act  
2 complained of is unlawful or lawful, as follows:

3 ... The difference is that if the taking is lawful the value of the undertaking at the time  
4 of dispossession is the measure and the limit of compensation, while if it is unlawful,  
5 this value is, or may be, only part of the reparation to be paid. In any event, even in a  
6 case of unlawful expropriation the damage sustained is the measure of the  
7 reparation....<sup>147</sup>

8 In the *Amoco case*, the government measure at issue was determined to be a lawful one. This  
9 resulted in an award in which the Iran-US Claims Tribunal extended its analysis of the *Chorzow*  
10 *Factory* case to determine principles related to lawful acts. Judge Charles Brower took the opportunity  
11 in his Concurring Opinion to further clarify the decision of the *Chorzow Factory* case, in particular  
12 dealing with acts found to be contrary to international law. Judge Brower's analysis is particularly  
13 applicable in the context of a modern business valuation analysis when he states:

14 I agree that in the case of any taking, lawful or unlawful, 'the value of the enterprise at  
15 the moment of the dispossession' is to be awarded (additional remedies being available  
16 in the case of an unlawful expropriation).<sup>148</sup> ...

17 In my view *Chorzow Factory* presents a simple scheme: If an expropriation is lawful,  
18 the deprived property is to be awarded damages equal to 'the value of the undertaking'  
19 which it has lost, including any potential future profits, as of the date of taking; in the  
20 case of an unlawful taking, however, either the injured party is to be actually restored  
21 to enjoyment of his property, or, should this be impossible or impractical, he is to be  
22 awarded damages equal to the greater of (I) the value of the undertaking at the date of  
23 loss (again including lost profits), judged on the basis of information available as of that  
24 date, and (ii) its value (likewise including lost profits) as shown by its probable  
25 performance subsequent to the date of loss and prior to the date of the award, based on  
26 actual post-taking experience, plus (in either alternative) any consequential damages.  
27 Apart from the fact that this is what *Chorzow Factory* says, it is the only set of principles  
28 that will guarantee just compensation to all expropriated properties.

The substantive test of the judgment of *Chorzow Factory* is consonant with the  
conclusion that the 'value of the undertaking' includes its potential for earning profits.  
The Court thus described such value as including 'the cessation of the working and the  
loss of profit which have accrued' as encompassing all elements of damages except  
those that are 'outside the undertaking itself;' and as embracing 'the worth of the  
enterprise as a whole' or 'the total value of the undertaking' including 'profit'.

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<sup>146</sup> *Amoco International Finance Corp. and The Government of the Islamic Republic of Iran, et al.* (1987) 15 Iran-US CTR  
189, 246-52 [TAB 67]

<sup>147</sup> *Id.* at para. 197.

<sup>148</sup> *Id.*, Concurring Opinion of Judge Brower, at para. 17.

1 In summary, in order to provide the restitution value mandated in the *Chorzow Factory* case for  
2 a state act contrary to international law, consideration of the following elements of any potential  
3 damages claim is required:

4 a. The fundamental objective is to wipe-out all the consequences of the illegal act  
5 and reestablish the situation which would have existed if that act had not been  
6 committed;

7 b. The award of compensation is not limited to the value of the undertaking at the  
8 date of loss;

9 c. Restitution value is shown by demonstrating the “probable performance  
10 subsequent to the date of loss and prior to the date of the award, based on actual post-  
11 taking experience”;

12 d. Compensation for lost profits are included in the calculation of restitution value  
13 for unlawful acts; and

14 e. Consequential damages resulting from the unlawful act should be included in the  
15 calculation of restitution value.

## 16 **2. Causation and Remoteness**

17 Before a restitution value can be assigned to any loss claimed, however, two simple tests must  
18 be met. First, there must be a direct causal link between the unlawful international conduct and the  
19 damages incurred.<sup>149</sup> Second, the damages claimed must be a reasonably foreseeable consequence of  
20 the act that constituted the breach. The first test is a matter of causation. The second test is a matter  
21 of proximate cause (also known as “remoteness”). As the *Myers* Tribunal noted:

22 ... compensation is payable only in respect of harm that is proved to have a sufficient  
23 causal link with the specific NAFTA provision that has been breached; the economic  
24 losses claimed by SDMI must be proved to be those that have arisen from a breach of  
25 the NAFTA, and not from other causes<sup>150</sup>

26 This finding was further confirmed in the dispositive provisions of the *Partial Award*, when  
27 the Tribunal ordered:

28 CANADA shall pay to SDMI compensation for such economic harm as is established  
legally by SDMI to be directly as a result of CANADA’s breach of its obligations under

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29 <sup>149</sup> Id., Concurring Opinion of Judge Brower, at para. 51.

30 <sup>150</sup> *Myers* Partial Award, at 316 [TAB 5].

1 Articles 1102 or 1105 of the NAFTA.<sup>151</sup>

2 Accordingly, the simple test for proving damages in a claim brought under NAFTA Article 1117  
3 is: (1) to establish that *causation* exists between the alleged breach and the alleged harm, and (2) to  
4 ensure that the damages claimed are not too remote from the act or acts which constituted the treaty  
5 breach.<sup>152</sup>

6 In *Myers*, the investor sought to recover the present value of the net income stream that it lost  
7 due to the fourteen month period it and its investment were delayed from entering the Canadian market  
8 for the destruction of PCB wastes.<sup>153</sup> Myers' business model was simple: to attend at an industrial site;  
9 to remove any trace of PCB wastes from that site; and then to permanently and safely dispose of those  
10 wastes. Because the part of this business plan involved the destruction of some of these wastes in the  
11 USA, a protectionist Canadian politician was able to frustrate the investment by imposing an absolute  
12 ban on their export.<sup>154</sup>

13 In establishing the appropriate quantum of damages for this illegal act, the *Myers* Tribunal  
14 adopted the standard "but for" test of causation. It concluded that, but for the illegal imposition of a  
15 ban on the export of PCB wastes to the USA, the business established by the investor in Canada would  
16 have resulted in profits for it and the investment it controlled in Canada.

17 Regarding remoteness, the Tribunal heard from Canada that Myers could not recover any  
18 damages as a result of lost profits because they were too remote to the actual breach. This was because  
19 Myers planned to undertake final destruction of the wastes in the USA, rather than in Canada where the  
20 wrongful conduct was committed by the Canadian government<sup>155</sup> This argument was predicated on the

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22 <sup>151</sup> *Id.* at 325.

23 <sup>152</sup> *Id.* at 33-37.

24 <sup>153</sup> *Id.* at 34.

25 <sup>154</sup> The ban breached Articles 1102 and 1105 because it was designed to prevent Myers from running its business, and thus  
26 protect Canadian companies. It had nothing to do with protecting the environment.

27 <sup>155</sup> *Id.*, at para's. 34-35. Canada had also tried to argue that, to the extent the business planned by the investor and investment  
28 could be seen as the provision of a cross-border service, no recovery was possible because such activity would be covered  
under NAFTA Chapter 12 (which contains rules governing the regulation of cross-border services that are not subject to  
investor-state arbitration). The Tribunal obviously dismissed this argument because it was based on the faulty proposition

1 novel theory that NAFTA Chapter 11 does not contemplate payment of damages for losses suffered by  
2 an investor outside of the territory in which it has invested. The *Myers* Tribunal rejected this theory out-  
3 of-hand, stating that there is absolutely no reason to limit recovery on the basis of the territory where  
4 the loss was suffered.<sup>156</sup> Rather, the question of remoteness is merely one of considering whether the  
5 damages claimed are a foreseeable result of the action that led to the breach. For example, the Tribunal  
6 concluded that Myers could not receive damages for the independent, intervening act of the US  
7 government in closing its borders to PCB waste imports from Canada (thus reducing the length of time  
8 for which any deserved profits could be awarded).<sup>157</sup>

9 Decisions made by international tribunals in both the *Asian Agricultural Products* case,<sup>158</sup> and  
10 the *Shufelt Case*,<sup>159</sup> confirm the principle that the damages for anticipated future profits must not only  
11 be direct, but must also be foreseeable. As Professor Whiteman has suggested, the assessment of  
12 prospective profits requires proof that they are “reasonably anticipated.”<sup>160</sup> As Professor Schacter  
13 characterizes the issue as a matter of determining the extent of the “legitimate expectations” of an  
14 investor – concerning profitability of the expropriated business undertaking – before its seizure or  
15 effective destruction.<sup>161</sup>

16 Similarly, the *Amco Asia* Tribunal recognized the role of remoteness in any damages analysis,  
17 noting:

18 ... the Tribunal has to state that here again, according to principles and rules common  
19 to the main national legal systems and to international law, the damages to be awarded  
20 must cover the *direct* and *foreseeable* prejudice. The requirement of *directness* is but

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21 that merely because two treaty obligations overlap, one must be presumed to somehow “trump” the other – rather than merely  
22 applying simultaneously. *See id.* at 35 n

23 <sup>156</sup> *Id.* at para. 37.

24 <sup>157</sup> See, also: *Myers* Damages Award at 94 [TAB 65].

25 <sup>158</sup> *Asian Agricultural Products*, at para. 104 [TAB 24].

26 <sup>159</sup> *Shufelt v. Guatemala* (1930), 11 RIAA 1081 [TAB 68]; as cited in *LIAMCO v. Libya* (1981) 20 ILM 1, at 51-53 [TAB  
69]

27 <sup>160</sup> As cited in *Asian Agricultural Products*, at para. 104 [TAB 24].

28 <sup>161</sup> O. Schacter, *International Law in Theory and Practice* (Boston: Dordrecht, 1991) at 324 [70].

1 a consequence of the requirement of a causal link between the failure and the prejudice;  
2 and the requirement of *foreseeability* is met practically everywhere.<sup>162</sup>

3 Accordingly, in addition to being concerned with the existence of independent, intervening  
4 causes, one must also be concerned with the reasonable foreseeability of the damages claimed – as of  
5 the time of the act or acts which constituted a treaty breach (where foreseeability lies in the eyes of an  
6 objective observer, attempting to place himself in the shoes of the investor, often with the assistance  
7 of expert and/or contemporaneous evidence).

8 For example, the *Asian Agricultural Products* Tribunal confirmed that “uncertain” or  
9 “speculative” profits should be disallowed.<sup>163</sup> The *Amoco* Tribunal was similarly concerned about the  
10 speculative nature of long term profit projections sought by the claimant.<sup>164</sup> And the *Metalclad* Tribunal  
11 denied the recovery of future profits because the investment had not been a “going concern” before its  
12 expropriation, and because there was no other way to verify that they could have been legitimately  
13 expected.<sup>165</sup> A similar conclusion was reached by the Tribunal in *Feldman*.<sup>166</sup>

14 Accordingly, in a nutshell, if the damages claimed include profits which were not reasonably  
15 foreseeable as of the time of the breach, damages cannot be awarded for them. Instead, in order to  
16 award “full restitution value” or the investment, a tribunal must discount the claim for profits to a level  
17 which is adjudged to have been reasonably foreseeable as of the date of the breach.

18 Despite the fact that the investment was essentially frustrated before it could become a going  
19 concern, the *Myers* Tribunal awarded damages for lost profits, properly discounted to take various  
20 industry-specific contingencies into account. It was able to do so with the assistance of an expert report  
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24 <sup>162</sup>*Amco Asia* (Merits Award) at 501 [TAB 54]. The Tribunal cites in support of this proposition: D.P. O’Connell,  
*International Law*, 2nd ed., Vol. 2, at 117 ff, and the case cited at footnote 24.

25 <sup>163</sup>*Asian Agricultural Products*, at para. 104 [TAB 24].

26 <sup>164</sup>*Amoco*, at para. 238-239 [TAB 67]

27 <sup>165</sup>*Metalclad*, at para. 120- 122 [TAB 8]

28 <sup>166</sup>*Feldman* Final Award, at para. 198, note 41 [TAB 12].

1 and the past performance of the Myers companies in PCB waste remediation in the US market.<sup>167</sup>

2 **3. Full Restitution Value is the Fair Market Value of Any Frustrated Investment**

3 **Business**

4 NAFTA Article 1110(2) provides:

5 Compensation shall be equivalent to the fair market value of the expropriated  
6 investment immediately before the expropriation took place ("date of expropriation"),  
7 and shall not reflect any change in value occurring because the intended expropriation  
8 had become known earlier. Valuation criteria shall include going concern value, asset  
9 value including declared tax value of tangible property, and other criteria, as appropriate,  
10 to determine fair market value.

11 No particular analysis is dictated for breaches of NAFTA provisions such as Articles 1102 or  
12 1105, and tribunals have thus far confirmed that they accordingly retain discretion to apply an analysis  
13 which is in accordance with the principles of international law.<sup>168</sup> As the *Myers* case demonstrates, the  
14 overall objective of any damages analysis under international law is to provide full restitution value for  
15 losses attributable to the wrongful conduct of a State. Regardless of whether the wrongful act  
16 constitutes a breach of Article 1110 or another NAFTA provision, if the business of the investment  
17 enterprise has been effectively frustrated the only way to provide full restitution value is to award the  
18 fair market value of the business immediately prior to its frustration. Accordingly, international law  
19 jurisprudence concerning the value of compensation for expropriation will be as relevant for breaches  
20 of NAFTA Articles 1102 and 1105 as they are for Article 1110.

21 In the cases of the Iran - US Claims Tribunal, the compensation to be paid for the lawful  
22 expropriation of "going concerns" was generally set to an amount equal to the fair market value  
23 ("FMV") of those concerns at the date of expropriation. This value approximated what a willing buyer  
24 would reasonably have expected to pay for the expropriated business on a date immediately prior to the  
25 expropriation. Generally such an amount would include not only the net value of the concern's  
26 assets,<sup>169</sup> but also the value of its goodwill and its future profitability. The Tribunal uniformly rejected

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28 <sup>167</sup>Id. at 195; citing the *Myers Merits Award* at para's. 303-319 [TAB 5]

<sup>168</sup> *Myers Merits Award* at para's. 309, 311 & 318 [TAB 5]; and *Myers Damages Award* at 159-160, 167 & 173-174 [TAB 65]

<sup>169</sup>"Net Book Value" could also be termed as the going concern value at the date of the expropriation and would exclude compensation for future profits. The traditional latin terms would be the provision of *damnum emergens* (the value at the

1 the use of the net book value method as the proper method for valuing a going concern.<sup>170</sup>

2 In the *Amoco Case*, the Tribunal provided the following definition of going concern value:

3 Going concern value encompasses not only the physical and financial assets of the  
4 undertaking, but also the intangible valuables which contribute to its earning power,  
5 such as contractual rights ... as well as goodwill and commercial prospects. Although  
6 those assets are closely linked to the profitability of the concern, they cannot and must  
7 not be confused with the financial capitalization of the revenues which might be  
8 generated by such a concern after the transfer of property resulting from the  
9 expropriation (*lucrum cessans*).

7 The value of a going concern - of Khemco in this case - is 'made up of the values of the  
8 various components of the undertaking separately considered, and of the undertaking  
9 itself considered as an organic totality - or going concern - therefore as a unified whole,  
10 the value of which is greater than that of its components parts' to take the words of the  
11 award in the *AMINOIL* case. *AMINOIL, supra*, para. 178, 21 *Int'l Legal Mat'ls* at 1041.  
12 The arbitral tribunal in that case added that account should also be taken 'of the  
13 legitimate expectation of the owners.' This last remark, however, has to be understood  
14 in relation to a previous finding of that tribunal, which noted that this concept of  
15 'legitimate expectations' had been used by the parties in their contractual relations with  
16 a specific meaning. In the present Case, the legitimate expectations of the Parties can  
17 only be deduced from the history of the concern and from its various components, as  
18 well as from the terms of the Khemco Agreement, taking into account the circumstances  
19 prevailing at the time of the taking. Finally, the liabilities of Khemco at the valuation  
20 date have to be deducted from the total value so determined.<sup>171</sup>

15 In the Iran-US Claim Tribunal award in *INA Corporation v. Iran*, the Iran-US Claim Tribunal  
16 defined the term "fair market value" as follows:

17 'Fair market value' may be stated as the amount which a willing buyer would have paid  
18 a willing seller for the shares of a going concern, disregarding any diminution of value  
19 due to the nationalization itself or the anticipation thereof, and excluding consideration  
20 of events thereafter that might have increased or decreased the value of the shares.<sup>172</sup>

20 In the *American International Group Case*, the Iran-US Claims Tribunal held that:

21 ... the appropriate method is to value the company as a going concern, taking into  
22 account not only the net book value of its assets but also such elements as good will and  
23 likely future profitability, had the company been allowed to continue its business under

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24 time of the taking) as distinct from *lucrum cessans* (lost future profits and value from the date of the taking to the date of  
25 the expert opinion)

26 <sup>170</sup>For example, see discussion in the *Amoco* Award, at para's. 249-259 [TAB 67], where the Tribunal rejected the  
27 submission of the Respondent to use the net book value method as the proposed basis of valuation.

27 <sup>171</sup> *Amoco* Award, at para's. 264-265 [TAB 67]..264-265.

28 <sup>172</sup>(1985) 8 Iran-US CTR 373 at 380, at para. 10 [TAB 71].

1 its former management.<sup>173</sup>

2 **4. Valuation Factors and the DCF Method**

3 The quantification of fair market value relates directly to the lost past and future economic  
4 benefits to the investor and its investments in the context of a notional market place that would include  
5 all potential purchasers. This concept has frequently been referred to in international law under the  
6 rubric of “anticipated future profits.” Damages for lost profits may be awarded when the loss of profits  
7 is a foreseeable consequence of an international law breach and when such profits can be calculated  
8 with reasonable certainty.<sup>174</sup> Under international law, there have been an array of awards that have  
9 provided the aggrieved party compensation not only for actual losses suffered (*damnum emergens*), but  
10 also for consequential damages such as the loss of possible business profits (*lucrum cessans*).<sup>175</sup>

11 The Iran - US Claims Tribunal addressed these issues in numerous cases.<sup>176</sup> In addition, the  
12 decisions in a number of oil arbitrations may be relevant for their consideration of general principles  
13 of valuation. In these cases, valuation principles are addressed that are directly applicable to the  
14 Investor’s claim concerning factors such as anticipated future profits and the use of calculating such  
15 values by means of the discounted cash flow (“DCF”) method.

16 In the *LIAMCO v. Libya* case, the single member international Tribunal provided an analysis  
17 of the quantum of compensation with reference to future profits on a DCF basis. The Respondent’s  
18 position was derived from a speech of the Libyan oil Minister which suggested compensation on a net  
19 book value.<sup>177</sup> The sole arbitrator, Professor Mahmassani, awarded full compensation for the physical  
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23 <sup>173</sup>(1983) 4 Iran-US CTR 96 at 109, at para. 21 [TAB 72].

24 <sup>174</sup>*Sea-Land Service, Inc. v. Iran* (1984) 6 Iran-US CTR at 294 [TAB 73].

25 <sup>175</sup> *Myers* Damages Award, at para. 152 [TAB 65].

26 <sup>176</sup> The *Amoco* Case, the *Phillips* Case (discussed below) and the *Starret Housing* Case (1987) 16 Iran-US CTR 112 [Tab 74],  
27 are the most often cited examples. *Starret Housing* involved the termination of a building project contract part way through  
construction

28 <sup>177</sup> *LIAMCO Case*, at 55.



1 plant as well as compensation for future profits.<sup>178</sup>

2 In *Kuwait v. Aminoil*<sup>179</sup>, the Tribunal examined various elements of value including  
3 acknowledging that “...the reasonable rate of return, assessed on a somewhat more liberal scale,  
4 constitutes one of the elements of compensation.”<sup>180</sup> The Tribunal further stated that:

5 Having thus described the place occupied by the notion of a reasonable rate of return in  
6 the indemnification of Aminoil, the Tribunal must now indicate what principles are, in  
7 its view, valid for determining the compensation due in respect of the Company’s assets.  
8 As the Tribunal has stated earlier, it considers it to be just and reasonable to take some  
9 measure of account of all elements of an undertaking. This lead to separate appraisal  
10 of the value, on the one hand of the undertaking itself, as a source of profit, and on the  
11 other of the totality of assets, and adding together the results combined.<sup>181</sup>

12 In the Iran-US Claims Tribunal award in the *Amoco Case*, the Tribunal specifically addressed  
13 the question of anticipated future profits in the context of the DCF method. As the *Amoco Case* dealt  
14 with the case of a lawful expropriation, the Tribunal did not adopt the DCF method as an appropriate  
15 basis of compensation. Nevertheless, the *Amoco Case* is useful because of its detailed discussion of  
16 the DCF method. In that case, the claimant proposed a method of valuation that did not utilize a net  
17 book value of the going concern, also known as *damnum emergens*, but favoured a method which the  
18 Tribunal held amounted solely to be *lucrum cessans*. This method was the DCF method and was  
19 described by the Tribunal as follows:

20 229. ...The Claimant’s method is instead a projection into the future to assess the  
21 amount of the revenues which would possibly be earned by the undertaking, year  
22 after year, up to eighteen years later in this Case. These forecasted revenues are  
23 actualized at the time by way of a discounting calculation, and capitalized as a  
24 measure of the compensation to be paid, as well as the alleged market value of  
25 the enterprise. With such a method, *lucrum cessans* becomes the sole element  
26 of compensation.

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27 <sup>178</sup> Somewhat surprisingly, despite the arbitrator’s detailed discussion of these international decisions involving the  
28 appropriate theory of damages and valuation method, his compensation award in *LIAMCO* was made without detail and on  
the basis of “equitable compensation” for the lump sum of \$66,000,000 for the lost profits related to the nationalization of  
concession rights. See: *Liamco Case*, at 58 - 60 under the title: “Indemnification for expropriation of Petroleum Concession  
20-Raguba field.”

<sup>179</sup> (1982) 21 ILM 976, also at (1982) 66 ILR 518 [TAB 75].

<sup>180</sup> *Id.* at para. 163.

<sup>181</sup> *Id.* at para. 164.

1 In the *Amoco Case*, the Tribunal was particularly concerned about the speculative nature of long-  
2 term projections under the DCF method<sup>182</sup> but this was mainly in the context of a lawful expropriation  
3 that it rejected the use of this method. The Tribunal did not express an opinion on the question of the  
4 use of the DCF method in the case of an unlawful expropriation,<sup>183</sup> although it can be inferred from the  
5 extensive discussion by the Tribunal that it would have considered the DCF method appropriate in the  
6 case of an unlawful expropriation.

7 In the *Amco Asia* case, the Investor was deprived of its potentially profitable investment rights  
8 in Indonesia, and in particular

9 ... the right to operate the Kartika Plaza [a hotel], that is to say the loss of a *going*  
10 *concern*.

11 Now, while, there are several methods of valuation of going concerns, the most  
12 appropriate one in the present case is to establish the *net present value* of the business,  
13 based on a reasonable projection of the foreseeable net cash flow during the period to  
14 be considered, said net cash flow being then discounted in order to take into account the  
15 assessment of the damages at the date of the prejudice, while in the normal course of  
16 events, the cash flow would have been spread on the whole period of operation of the  
17 business....

18 Accordingly, it is this method (namely, the valuation of the net present value of the lost  
19 business, as resulting from the discounted net cash flow) that will be applied by the  
20 Tribunal in order to assess the damages to be awarded to the Claimants.<sup>184</sup> [emphasis  
21 in original]

22 In the *Phillips Petroleum Case*, the Iran - US Claims Tribunal relied primarily upon the DCF  
23 method.<sup>185</sup> The Tribunal in the *Phillips Case* sets out its valuation approach as follows:

24 The Tribunal recognizes the determination of fair market value of any asset inevitably  
25 requires the consideration of all relevant factors and the exercise of judgment. In the  
26 absence of an active and free market for comparable assets at the date of taking, a  
27 tribunal must, of necessity, resort to various analytical methods to assist it in deciding  
28 the price a reasonable buyer could be expected to have been willing to pay for the asset  
in a free market transaction, had such a transaction been possible at the date the property  
was taken. **Any such analysis of a revenue-producing asset, such as the contract  
rights in the present Case, must involve a careful and realistic appraisal of the  
revenue-producing potential of the asset over the duration of its term, which**

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25 <sup>182</sup> *Amoco Case*, at para. 238 - 239 [TAB 67].

26 <sup>183</sup> *Amoco Case*, at para. 240.

27 <sup>184</sup> *Amco Asia* - Merits Award, at 501 [TAB 54].

28 <sup>185</sup> (1989) 21 Iran - US CTR 79. In particular, see: discussion at para. 111 - 116, and 154 - 158 [TAB 76].

1 **requires appraisal of the level of production that reasonably may be expected, the**  
2 **costs of operation, including taxes and other liabilities, and the revenue such**  
3 **production would be expected to yield, which, in turn, requires a determination of**  
4 **the price estimates for sales of the future production that a reasonable buyer would**  
5 **use in deciding upon the price it would be willing to pay to acquire the asset.**  
Moreover, any such analysis must also involve an evaluation of the effect on the price  
of any other risks likely to be perceived by a reasonable buyer at the date in question,  
excluding only reductions in the price that could be expected to result from threats of  
expropriation or from other actions by the Respondent relates thereto.

6 One such method of analysis, and the method used by the Claimant, is the Discounted  
7 Cash Flow ('DCF') analysis, which calculates the Claimant's prospective net earnings  
8 over the term of the JSA and discounts them to give their value at the date of taking,  
using a discount rate that takes into account the perceived risks. [emphasis added in  
bold]<sup>186</sup>

9  
10 In contrast to the approach of the *Amoco* Tribunal, the *Phillips* Tribunal then goes on to state  
11 that the analysis of anticipated revenues was not a distinct head of damages of lost future profits, but  
12 was simply a factor inherent in the calculation of the fair market value of the undertaking at the date of  
13 taking:

14 The Tribunal recognizes that a prospective buyer of the asset would almost certainly  
15 undertake such DCF analysis to help determine the price it would be willing to pay and  
16 that DCF calculations are, therefore, evidence the Tribunal is justified in considering in  
17 reaching its decision on value.<sup>187</sup>

18 In summary, the DCF method includes, as recognized by the *Phillips Case* Tribunal, the  
19 following factors:

- 20 a) consideration of all relevant factors and circumstances;
- 21 b) An appraisal of revenue-producing potential of the asset over the relevant time  
22 period, which includes an appraisal of:
  - 23 I. the level of production that may reasonably be expected,
  - 24 ii. the costs of operation, including taxes and other liabilities, and
  - 25 iii. the revenue that such production would be expected to yield, including  
26 a determination of the price estimates for sales of the future production;  
and
- 27 c) An evaluation of the effect on the price of any other risks likely to be perceived

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28 <sup>186</sup> Id., at para's. 111-112.

<sup>187</sup> Id. at para. 112.

1 by a reasonable buyer.

2 **5. Interest**

3 The *Metalclad* Tribunal cited the *Asian Agricultural Products* case for the principle that  
4 “interest becomes an integral part of the compensation itself, and should run consequently from the date  
5 when the State’s international responsibility is engaged.”<sup>188</sup> The Tribunal accordingly awarded the  
6 investor pre-judgment interest, running from the date that Metalclad was wrongly denied its application  
7 for a construction permit by the local municipal government to 45 days after the award was rendered  
8 – at a rate of 6% compounded annually; as well as post-judgment interest of 6% compounded annually  
9 from the 45 day mark after the award.

10 Other international arbitral awards have expressly allowed compound interest to be paid on the  
11 award of damages and the recent trend appears to be towards the provision of compound interest.<sup>189</sup> Dr.  
12 Mann and Professor Gaetano Arangio-Ruiz have similarly concluded that compound interest should be  
13 awarded to the claimant as an integral part of damages awards by international tribunals.<sup>190</sup>

14 The recent ICSID arbitration case of *Compania del Desarrollo de Santa Elena, S.A. v. The*  
15 *Republic of Costa Rica*,<sup>191</sup> provides a comprehensive review of the international arbitral case law  
16 concerning whether compound interest should be awarded. In the *Santa Elena* case, the Tribunal  
17 awarded compound interest to the claimant. The Tribunal explained its decision as follows:

18 Even though there is a tendency in international jurisprudence to award only simple  
19 interest, this is manifested principally in relation to cases of injury or simple breach of  
20 contract. The same considerations do not apply to cases relating to the valuation of  
property and property rights. In cases such as the present, compound interest is not  
excluded where it is warranted by the circumstances of the case.<sup>192</sup>

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21  
22 <sup>188</sup> *Metalclad*, at para. 128 [TAB 8]; *Asian Agricultural Products*, at para. 114 [TAB 24]. The Tribunal in *Asian*  
*Agricultural Products* quotes R. Lillich in his essay “Interest in the Law of International Claims”, *Essays in Honor of Vade*  
*Saario and Toivo Sainio* (1983) at 55-56.

23  
24 <sup>189</sup> *Fabiani’s Case*, *Moore’s Digest of International Law* (1905) at 4878-4915 [TAB 77]; *Aminoil* at 613 [TAB 75]

25 <sup>190</sup> F.A. Mann, “Compound Interest as an Item of Damage in International Law”, *Further Studies in International Law* (1990)  
at 380 [TAB 78].

26 <sup>191</sup> *Compania del Desarrollo de Santa Elena, S.A. and The Republic of Costa Rica*, Final Award, Case No. ARB/96/1,  
27 February 17, 2000 (“*Santa Elena*”) [TAB 79].

28 <sup>192</sup> *Id.* at para 97; citing with approval *Flexi-Van v. Iran* (1987) 9 Iran - US CTR 206, which stated that: “Most awards  
allocate only simple interest, but occasionally compound interest has been awarded.”

1  
2 ... where an owner of property has at some earlier time lost the value of his asset but has  
3 not received the monetary equivalent that then became due to him, **the amount of**  
4 **compensation should reflect, at least in part, the additional sum that his money**  
5 **would have earned, had it, and the income generated by it, been reinvested each**  
6 **year at generally prevailing rates of interest.** It is not the purpose of compound  
7 interest to attribute blame to, or to punish, anybody for delay in the payment made to the  
8 expropriated owner; it is a mechanism to ensure that the compensation awarded the  
9 Claimant is appropriate in the circumstances.<sup>193</sup> [emphasis added]

10 In the Iran-US Claims Tribunal, the *Sylvania v. Iran* case is cited as the standard with respect  
11 to the assessment of interest and costs.<sup>194</sup> It was cited by the Iran-US Claims Commission Tribunal in  
12 other cases, such as the *Sola Tiles* case, as ensuring that commercial interest rates should be used by  
13 international tribunals. The Tribunal stated:

14 In accordance with the approach developed and applied by this Chamber since its award  
15 in the *Sylvania Technical Systems, Inc. v. Islamic Republic of Iran*, Award No. 180-64-1  
16 (27 June 1985), **the Claimant is entitled to interest on the amount awarded, at a rate**  
17 **based approximately on the amount that it would have been able to earn had it had**  
18 **the funds available to invest in a form of commercial investment in common use in**  
19 **its own country.**<sup>195</sup> [emphasis added]

20 Other NAFTA Tribunals have displayed a marked preference for awarding compound interest  
21 from the date of the breach. The *Pope* Tribunal concluded that international law principles require an  
22 “appropriate” award of interest,<sup>196</sup> which it determined to be 5%, compounded quarterly.<sup>197</sup> The *Myers*  
23 Tribunal similarly awarded interest at a rate of 1% above the Canadian prime rate, compounded  
24 annually.<sup>198</sup>

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25 <sup>193</sup> Id. at para. 104.

26 <sup>194</sup> *Sylvania Technical Systems v. Iran* (1985) 8 Iran-US CTR 298 at 320-324 [TAB 80].

27 <sup>195</sup> *Sola Tiles, Inc. v. The Government of the Islamic Republic of Iran* (1987) 14 Iran-US CTR 223, at para. 66 [TAB 81].

28 <sup>196</sup> Both of the *Pope* and the *Myers* tribunals acknowledged that the governing law for their consideration of interest must be international law, as required under NAFTA Article 1131(1). Without mentioning Article 1131(1), the *Feldman* Tribunal apparently observed Mexican domestic law in designating a simple rate of interest (at para. 205 of its Award). This decision appears closely related to the facts of the case, involving qualification for tax rebates wrongfully withheld.

<sup>197</sup> *Pope* Damages Award, at para’s. 90-9.

<sup>198</sup> *Myers* Second Partial Award on Damages, at para’s. 303-306. Without explanation, the Tribunal awarded interest from the date of the notice of arbitration.

1           **6.     Costs**

2           Article 38 of the UNCITRAL Rules provides as follows:

3           The arbitral tribunal shall fix the costs of arbitration in its award. The term ‘costs’  
4           includes only:

- 5           (a)     The fees of the arbitral tribunal to be stated separately in the award as to each  
6           arbitrator and to be fixed by the tribunal itself in accordance with article 39;
- 7           (b)     The travel and other expenses incurred by the arbitrators;
- 8           (c)     The costs of expert advice and of other assistance required by the arbitral  
9           tribunal;
- 10          (d)     The travel and other expenses of witnesses to the extent that such expenses are  
11          approved by the arbitral tribunal;
- 12          (e)     The costs for legal representation and assistance of the successful party if such  
13          costs were claimed during the arbitral proceedings, and only to the extent that  
14          the arbitral tribunal determines that the amount of such costs is reasonable;
- 15          (f)     Any fees and expenses of the appointing authority as well as the expenses of the  
16          Secretary-General of the Permanent Court of Arbitration at The Hague.

17          Article 40 of the UNCITRAL Rules provides:

- 18          1.     Except as provided in paragraph 2, the costs of arbitration shall in principle be  
19          borne by the unsuccessful party. However, the arbitral tribunal may apportion  
20          each of such costs between the parties if it determines that apportionment is  
21          reasonable, taking into account the circumstances of the case.
- 22          2.     With respect to the costs of legal representation and assistance referred to in  
23          article 38, paragraph (e), the arbitral tribunal, taking into account the  
24          circumstances of the case, shall be free to determine which party shall bear such  
25          costs or may apportion such costs between the parties if it determines that  
26          apportionment is reasonable.

27          No NAFTA provisions exist which would modify the application of these arbitration rules.  
28          Accordingly, it lies within the discretion of this Tribunal to award costs in the manner which it  
29          determines to be the most appropriate and reasonable in the circumstances.<sup>199</sup>

30          Two awards have been rendered in favor of NAFTA claimants who chose the UNCITRAL  
31          Rules: *Pope & Talbot* and *Myers*. In both cases, the claimants were awarded a greater portion of the  
32          costs of the proceedings, based upon the principle that the losing party should normally bear the costs

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33          <sup>199</sup> NAFTA Article 1120(2) states: “The applicable arbitration rules shall govern the arbitration except to the extent modified  
34          by this Section.” The Claimant selected the UNCITRAL Rules for this arbitration.

1 of the arbitration. Operating under different arbitral rules – which do not explicitly recognize the “loser  
2 pays” principle – the *Metalclad* and *Feldman* Tribunals did not award costs to the victorious claimants.  
3 Thus far, no NAFTA Tribunal has rendered an award of costs against an unsuccessful claimant.

4         These previous NAFTA awards establish a practice which can provide some guidance for this  
5 Tribunal in exercising its discretion to award costs. Essentially, absent any indication that a successful  
6 claimant is undeserving of a full costs award, one should be made. Such indications would include  
7 inappropriate conduct during the arbitral proceedings or a lack of success in relation to any key element  
8 of the alleged claim. If such factors are not present, a complete award of costs should be made.

9         Otherwise, an apportionment of costs between the claimant and the respondent NAFTA Party  
10 may be appropriate, given the circumstances of the particular case and the conduct of those particular  
11 arbitration proceedings. Also, given the unequal relationship that exists in any arbitration between an  
12 individual claimant and a respondent State, it is rarely appropriate for costs to be awarded to an  
13 unsuccessful NAFTA claimant. Such circumstances would include a finding that a claim, or key  
14 portions of a claim, were frivolous and vexatious.

15         **B. Application of the International Law of Damages to the Facts of this Case**

16         Exhibit 91 is the “Valuation Analysis of International Thunderbird’s Skill Gaming Operations  
17 in Mexico” provided by the Innovation Group of New Orleans, Louisiana. That valuation analysis  
18 provides back up and analysis supporting the opinions of Steven Rittvo as to the value of Thunderbird’s  
19 investment enterprises under several different scenarios. Those valuations are calculated based upon  
20 projected income streams for the various locations over stated periods of time reduced to present value  
21 at appropriate discount rates. This “NPV” (net present value) model is intended to provide the best  
22 analysis of the full restitutionvalue of Thunderbird’s investment enterprises at the date of seizure and  
23 closure by Mexico. Claimant is presenting three different damage calculations for the full  
24 restitutionvalue of Thunderbird’s investment enterprises under different assumptions

25         **1. 10 Year Scenario With No Expansion at the Existing Matamoros, Nuevo and**  
26         **Reynosa Locations.**

27         This damage calculation assumes that the cumulative number of machines located at  
28 Matamoros, Nuevo and Reynosa as of the time of closure remain constant over the projected ten years

1 of income analysis. In other words, the three facilities continued to operate as they were constituted at  
2 the time of the closures for a period of ten years. Claimant's damages under this scenario are **\$23.2**  
3 **million dollars (U.S)**. With interest compounded quarterly based upon the Mexican prime rate,  
4 claimant's damages under this scenario increase to **\$24.0 million dollars (U.S)**.

5 **2. 10 Year Scenario With Expansion at the Existing Matamoros, Nuevo and**  
6 **Reynosa Locations.**

7 This damage calculation assumes that the cumulative number of machines located at  
8 Matamoros, Nuevo and Reynosa as of the time of closure is increases to a collective 1,000 over the  
9 projected ten years of income analysis. Claimant's damages under this scenario are **\$66.0 million**  
10 **dollars (U.S)**. With interest compounded quarterly based upon the Mexican prime rate, claimant's  
11 damages under this scenario increase to **\$67.9 million dollars (U.S)**.

12 **3. 10 Year Scenario With Expansion at the Existing Matamoros, Nuevo Laredo and**  
13 **Reynosa Locations and Developments at the Puebla, Ciudad Juarez and Monterrey**  
14 **locations.**

15 This damage calculation assumes that the cumulative number of machines located at  
16 Matamoros, Nuevo Laredo and Reynosa as of the time of closure is increases to a collective 1,000 and  
17 an additional 1000 machines are spread equally over the Puebla, Ciudad Juarez and Monterrey locations  
18 over the projected ten years of income analysis. Claimant's damages under this scenario are **\$171.2**  
19 **million dollars (U.S)**. With interest compounded quarterly based upon the Mexican prime rate,  
20 claimant's damages under this scenario increase to **\$175.4 million dollars (U.S)**.

21 **IX.**

22 **CONCLUSION**

23 The facts of this case clearly establish breaches by respondent The Untied Mexican States if its  
24 NAFTA Article 1102, 1105 and 1110 obligations owed to claimant International Thunderbird Gaming  
25 Corporation and its Mexican investment enterprises, Entertainmens de Mexico S. de R. L. De C. V.,  
26 Entertainmens de Mexico Laredo S. de R. L. de C.V., Entertainmens de Mexico Reynosa S. de R.L. de  
27 C.V., Entertainmens de Mexico Puebla S. de R.L. de C.V., Entertainmens de Mexico Monterey S. de  
28 R.L. de C.V. and Entertainmens de Mexico Juarez. S. de R.L. de C.V.



1 Claimant respectfully requests that the Tribunal award damages in amount representing the full  
2 restitutionvalue of Thunderbird's investment enterprises at the date of seizure by Mexico.

3  
4 Date: August 14, 2003

5 James D. Crosby, Lead Counsel for the Claimant  
International Thunderbird Gaming Corporation

6 James D. Crosby  
7 Attorney at Law  
13400 Sabre Springs Parkway, Suite 160  
8 San Diego, Ca. 92128  
9 Phone: (858) 486-0085  
Fax: (858) 486-2838  
E-Mail: crosby@crosbyattorney.com

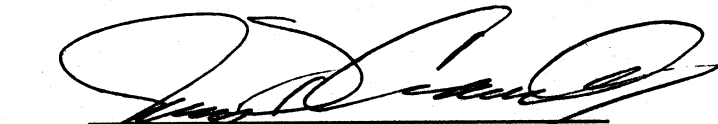
10  
11 Co-Counsel for Claimant

12 Professor Todd Weiler  
13 University of Windsor Law School  
401 Sunset Avenue  
14 Windsor, Ontario  
N9B 3P4  
15 Phone: (416) 575-4574  
Fax: (416) 577 2751

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Claimant respectfully requests that the Tribunal award damages in amount representing the full restitution value of Thunderbird's investment enterprises at the date of seizure by Mexico.

Date: August 14, 2003



James D. Crosby, Lead Counsel for the Claimant  
International Thunderbird Gaming Corporation

James D. Crosby  
Attorney at Law  
13400 Sabre Springs Parkway, Suite 160  
San Diego, Ca. 92128  
Phone: (858) 486-0085  
Fax: (858) 486-2838  
E-Mail: crosby@crosbyattorney.com

Co-Counsel for Claimant

Professor Todd Weiler  
University of Windsor Law School  
401 Sunset Avenue  
Windsor, Ontario  
N9B 3P4  
Phone: (416) 575-4574  
Fax: (416) 577 2751