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INTERNATIONAL CENTRE FOR SETTLEMENT OF

INVESTMENT DISPUTES

ICSID Case No ARB/19/28

between

LATAM HYDRO LLC and CH MAMACOCHA SRL

Claimants

- and -

REPUBLIC OF PERU

Respondent

The Tribunal

Professor Albert Jan van den Berg, President

Professor Dr Guido Santiago Tawil - Arbitrator

Professor Raúl E Vinuesa - Arbitrator

VIDEOHEARING ON JURISDICTION AND MERITS

Wednesday, 16 March 2022

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I N D E X

(9.00 am EST, Wednesday, 16 March 2022)

PRESIDENT: Mr Zeballos, is everybody accounted for on your side?

MR ZEBALLOS: Yes, Mr President.

PRESIDENT: Mr Grané for the Respondent, or Ms Endicott, who is the spokesperson for your side?

MR GRANÉ: Ms Endicott will be the spokesperson as to the damages portion, but we are ready to go and also look forward to the US intervention later today.

PRESIDENT: Very good. Everybody accounted for on your side, Mr Grané?

MR GRANÉ: Yes, we are all here. Thank you.

PRESIDENT: Thank you. Any procedural point, admin point, household? Mr Zeballos?

MR ZEBALLOS: No, Mr President.

PRESIDENT: Mr Grané?

MR GRANÉ: Nothing from our side. Thank you.

PRESIDENT: Then we can move to the experts for Respondent. Ms Endicott, you will introduce them?

MR MATTHEW SHOPP and MR KIRAN SEQUEIRA

MS ENDICOTT: Thank you, Mr President. **09:01**
Hello to the Tribunal. We have with us today Matthew Shopp and Kiran Sequeira from Versant Partners, who are available to present and answer questions.

PRESIDENT: Thank you, Ms Endicott. May I first ask, Mr Shopp and Mr Sequeira, who is the lead person?

MR SHOPP: I will be the lead person today.

PRESIDENT: Let's start, then, with you. Mr Shopp, can you please state your full name for the record?

MR SHOPP: My name is Matthew David Shopp.

PRESIDENT: Mr Shopp, you appear as an expert witness for the Respondent.

MR SHOPP: I do.

PRESIDENT: If any question is unclear to you please seek a clarification, if you don't do so the Tribunal assumes you have understood the question and that your answer responds to the question.

MR SEQUEIRA: Yes.

PRESIDENT: Mr Shopp, you will appreciate that appearing before a court or an arbitral tribunal and testifying there is a very serious matter. In that connection the Tribunal expects you to give the statement, the text of which will now appear on the screen.

MR SHOPP: I solemnly declare upon my honour and conscience that my statement will be in accordance with my sincere belief.

PRESIDENT: Then I move to Mr Sequeira. Can you please state your full name for the record?

MR SEQUEIRA: Yes, it's Kiran Peter Sequeira.

PRESIDENT: You also appear as an expert witness for Respondent. If any question is unclear to you, please do seek a clarification, because if you don't do so the Tribunal assumes you have understood the question and that your answer responds to the question.

MR SEQUEIRA: Yes, of course. Thank you, Mr President.

PRESIDENT: And, Mr Sequeira, you will also appreciate that appearing before a court or an arbitral tribunal and testifying there is a very serious matter. In that connection the Tribunal expects you to give the statement, the text of which is in front of you.

MR SEQUEIRA: I solemnly declare upon my honour and conscience that my statement will be in accordance with my sincere belief. **09:03**

PRESIDENT: Thank you. Then, Mr Shopp and Mr Sequeira, could you please confirm that you are alone -- together alone in the room or you are in separate rooms? Because I see two different paintings behind you.

MR SHOPP: We are in separate but adjacent rooms, and I am alone and Mr Sequeira can confirm the same.

MR SEQUEIRA: Yes, I am alone as well in my office, which is adjacent to Mr Shopp's office.

PRESIDENT: If anyone enters your room, please alert the Tribunal and refrain from testifying until the person has left the room.

MR SEQUEIRA: Yes.

MR SHOPP: Yes.

PRESIDENT: Mr Shopp, can I invite you first to scan the room where you are?

MR SHOPP: Yes. [Pause]

PRESIDENT: Mr Sequeira, may I invite you to do the same?

MR SEQUEIRA: Yes. [Pause]

PRESIDENT: Thank you. For the record,

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Mr Shopp, can you confirm the location from which you are testifying?

MR SHOPP: Washington DC.

PRESIDENT: Mr Sequeira?

MR SEQUEIRA: Washington DC as well.

PRESIDENT: Before you start with your presentation, I have to draw your attention to a provision in Procedural Order No 6 about the manner of testifying. So this paragraph 23, and I read it to you: "Experts who have presented joint reports will be examined simultaneously, that means" -- and then your names appear, Mr Shopp and Mr Sequeira -- "For the cross-examination of these experts, the questions will be directed to the lead expert in the group designated by the Claimants/Respondent that previously selected lead expert". The lead expert, that is you, Mr Shopp?

MR SHOPP: Correct.

PRESIDENT: "That expert will be responsible for determining which expert among the two should respond to the question. Only one expert can respond to each question. Each testifying expert should log into the virtual platform separately and refrain from interacting with the other testifying experts during the examination,

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unless invited to do so by the questioning counsel or Tribunal member".

So, gentlemen, then the last question I have for you is could you please shut down your iPhones or other mobile devices?

MR SEQUEIRA: Mine are shut down.

MR SHOPP: Mine is shut down and in a drawer.

PRESIDENT: Then may I invite you for direct examination? Ms Endicott, you would like to invite?

MS ENDICOTT: I would like to invite Mr Shopp and Mr Sequeira to please proceed with their presentation that they've prepared for you today. Thank you.

PRESIDENT: 45 minutes you have, gentlemen.

Presentation
by Mr Shopp

MR SHOPP: I will be doing a share screen, if that is OK.

Thank you, Mr President, members of the Tribunal, for allowing us the chance to present to you today. My colleague, Mr Sequeira, and I will be going over some of the key issues in damages in this

09:07

arbitration.

Starting first with briefly a comparison of the experts' results, as you can see on slide 4, there's a summary of the experts' respective damages conclusions. BRG concludes total damages of 47.6 million US dollars with pre-award interest updated through 1 March 2022. This is comprised, as you'll see in the sort of orange and reddish row, a $31.8 million for the fair market value of Claimants' investments as of 14 March 2017, $2.4 million in damages for what has been called the additional costs and expenses, along with $13.4 million of pre-award interest through 1 March 2022.

Our damages conclusion is significantly lower. We reached total damages in the range of $10.9 to $11.4 million under the fair market value standard, and that includes 7.5 million US dollars for the value of Claimants' investments as of March 2017. We used the same $2.4 million in additional costs and expenses, and we calculate lower pre-award interest of roughly 1 million or so US dollars through March 2022.

So how are our results different? Well, it's not due to our valuation approach. Both

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experts agree that damages for an expropriation or a full deprivation should be based on the fair market value, or FMV, standard.

We also both agree on the use of a discounted cash flow, or DCF valuation method, supported by third-party offers to determine the fair market value, and we similarly agree that the Claimants' sunk costs do not represent fair market value.

However, despite this common approach, again we reached significantly different conclusions. BRG calculates the fair market value of Claimants' investments as of March 2017 of $31.8 million, whereas we calculate the same at $7.5 million. BRG's valuation, as we've explained in our reports, is three to four times higher than the third-party offers for Claimants' investments which range from $7 to $9 million, and BRG's conclusions are based on highly flawed DCF inputs that are irreconcilable, we would say, with basic financial principles.

Our valuation, on the other hand, is consistent with these third-party offers and is based on a DCF which uses inputs that align with basic financial principles. And as to pre-award interest, again, a big difference in our results. That is because BRG relies upon high risk, economically irrational interest rates that are tied to Claimants' cost of capital, whereas we use economically rational pre-award interest rates, including Respondent's cost of borrowing, the yield on investment grade bonds, and the US dollar risk free rates.

Turning first to an issue that's been discussed at length in our reports and yesterday, what is the fair market value of Claimants' investments implied by third-party offers made for either some or all of their stake in CHM?

Well, in this case we're fortunate to have five third-party offers that each provide evidence of the fair market value of Claimants' investments, and all five of these offers which are listed in the table at the bottom of the slide imply a fair market value of between $7 and $9 million for Claimants' investments, and all five offers are representative of the value in the but-for scenario. In other words, they are unaffected by the breaches.

So turning, first, to the February 2017 Innergex offer, this is one that was first discussed by BRG in its initial report and then it's been continued to be discussed since then. Just to recap, what was this offer? Well, it called for Innergex to invest $17.8 million of cash into CHM over time to earn a 70 per cent stake in the company. Innergex also would pay a $1.5 million development fee to Latam Hydro. And importantly this offer was a subscription for new shares in CHM, it was a capital raise, to be completed via direct funding of up to $17.8 million in the project's construction costs.

BRG incorrectly interprets the Innergex offer. According to BRG the Innergex offer implies a value of $27 million, which they calculate as saying Innergex would invest $17.8 million for a 70 per cent stake, and they would pay a million and a half dollars to Claimants. But that math is incorrectly assuming that Innergex was purchasing existing shares from Claimants rather than subscribing to new shares in the company.

So what's the correct interpretation of the Innergex offer? It's that CHM would only be worth approximately $28 million -- so our math is a little bit different -- but would only be worth around $28 million after, and only after, Innergex injected this $17.8 million worth of cash into the company. The value of CHM before Innergex put in, or would have put in the $17.8 million was $8.8 million. And, in fact, Claimants' investments could only ever be worth $8.8 million regardless of whether they owned 100 percent of CHM before Innergex invested, in other words 100 percent of $8.8, or if they owned 30 per cent of CHM after Innergex invested, in other words 30 per cent of roughly $28 million.

So we're going to go into the details here because this has been such an issue of contention between the experts, and we'll take it back to basics and talk about pre-money and post-money value, and what those mean and when those terms apply.

Pre-money value is simply the value of a company before funds are received from a new share subscription. Post-money value, on the other hand, is referring to the value of a company after funds are received from a new share subscription. And when does this matter, this pre-money and post-money distinction? We heard yesterday that it's only for venture stage or early stage companies where it's two people in a garage. That is simply false. Pre-money and post-money is relevant any time there is a new share subscription that raises funds for 09:14 the company. It does not matter if the company is early stage, two guys in a garage, or a pre revenue series A, or if it's mature, if it's a bank that is getting recapitalised via a new equity investment, a bank that's worth billions of dollars and has been around for hundreds of years. Pre-money and post-money matters any time there is a new share subscription. And what then is the relationship between pre-money and post-money value?

Well, post-money value is simply the value on a pre-money basis plus the value of the new investment, so if you know what it was worth beforehand you add the new investment and you can come up with the post-money value. And, conversely, pre-money value, if you know what it's worth after the post-money value, you can simply subtract out the amount of the new investment to calculate pre-money value. And why is post-money higher? Why are these two amounts different? Well, that's because new investment, a new addition of capital into the company, increases the value of the company itself on a one-for-one, a dollar-for-dollar basis. Most share transactions, if I log on to Fidelity or my brokerage account and buy a share from another individual, we exchange money for a share. The company isn't involved at all. It doesn't get anything out of that transaction. That sale doesn't affect its value. But in these share subscriptions, it's the company itself who is receiving the funds; therefore this investment increases the value of the company on a one-to-one basis.

And it's also important to note, does a new share subscription, a new equity raise, increase value to existing shareholders? Well, the answer is no. Although the company receives money and its value increases, the existing shareholders get diluted. In other words, their percentage is decreased and the value of their equity remains the same. So it's a value neutral transaction, assuming it's sold at fair market value from the perspective of an existing shareholder. The company is worth more because of the new funds, but you have a lower percentage ownership in the company such that those two factors offset and your economic position stays the same.

A very, very simple example, we tried to keep it really easy, we had this in our report of pre-money/post-money value, and I won't go through this in too much detail, but assume you have a

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gentleman, Steve, who owns 100 percent of a piggy bank that has $10 in it, Steve's friend Mary is interested in buying the piggy bank but Steve says well, instead of buying it, why don't you contribute some new capital, subscribe for some new shares, if you put in $10, I will give you a 50 per cent share, or you will be able to earn via the purchase of new shares in the piggy bank, a 50 per cent share of the piggy bank, and what that leads to is a situation where Mary puts in her $10, that increases the value of the piggy bank from $10 to $20, and Steve and Mary then each have a 50 per cent share.

So the pre-money value of the piggy bank is just $10. That's what was in there before any transaction occurred. The post-money value of the piggy bank after Mary puts in the $10 is $20. 10 plus 10 is 20. But importantly Steve's investment, the original investor, his investment is only ever worth $10. He either owns 100 percent of the pre-money value or 50 per cent of the post-money value.

So this is just a very simple example of how pre-money and post-money works.

Turning to the specifics, then, of this

case, what did this look like with respect to the February 2017 Innergex offer? Well, in step 1, Claimants are owners of 100 percent of CHM, which had a pre-money value of $9.773 million. That includes the $930,000 of future investment that Claimants had yet to make, but that's the pre-money value and Claimants were 100 percent owners.

In step 2, Innergex would inject $17.8 million in cash into CHM in exchange for new shares and would also separately pay $1.5 million to Claimants, as I think they called it development fee or development premium. And in exchange Innergex would receive 40 million new shares representing 70 per cent of the company.

But as you see at the bottom of this sort of middle portion of the chart, again that $17.8 million that Innergex puts into the company increases the value of the company, because it's cash that's coming in.

So where, then, does that leave the two parties on a post-money basis? Well, that leaves CHM has a value of $27.576 million, including this new investment, the original pre-money value plus the new money that was put in, of which Innergex owns 70 per cent and Claimants own 30 per cent, and then Claimants, as you can see on the side, also have that $1.5 million they got separately from Innergex as a development fee.

So we can look at what this means for the value of Claimants' investments both ways, what was their value before the transaction, what was their value after the transaction, and, as we said it should be, the value of Claimants' investment is exactly the same at $8.843 million both before and after the Innergex transaction. It doesn't matter which way you look at this. Before the transaction Innergex recognised development costs that Claimants had put into the project of $7.63 million. They paid -- or were willing to pay -- a development premium for 100 percent of the project equivalent to $2.14 million. That gives you a total pre-money value of that $9.773. You subtract the remaining investment that Claimants had yet to make, that they would have had to make before Innergex put in the money, and that leaves you a net of $8.843 million. So that's the pre-money perspective of what this was worth, what Claimants' investments were worth.

Now let's look at it from a post-money basis. Here we start with well, what was Innergex willing to spend to earn -- to buy into 70 per cent of this project on a post-money basis. Innergex would put in $17.8 million, they would pay a $1.5 million development premium, so in total Innergex will have spent $19.3 million to earn a 70 per cent ownership stake in the post-money version of CHM and, again, here you can calculate by dividing 19.3 divided by 70 per cent, you get a $27.6 million post-money value, of which Claimants at that point would only own 30 per cent and that then gives them a value of their stake of $8.273, to which you add the development premium and subtract the remaining investment and get the same number, $8.843 million. So whichever way you look at this, before or after the transaction, you get to the same result.

In fact, this is pretty similar to what we later see, which are four offers to purchase 100 percent of Claimants' interest in CHM, from both Claimants made offers to sell, Innergex and Glenfarne made offers to buy, and all of these offers were in a range of $7 to $8.1 million, which is pretty similar to that Innergex offer from 2017. And again, importantly, all four of these offers were based on the same fundamental conditions as in the but-for scenario, which we list here and which

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I believe was acknowledged yesterday by BRG in its testimony.

So how does BRG get this so wrong? How do they say it's worth $27 million instead of $7 to $9? Well, they forget and they don't realise that the value of CHM would increase by $17.8 million only after those funds are invested into the company. BRG wrongly includes this nearly $18 million new investment as part of CHM's value as of March 2017. That is simply wrong.

As of March 2017, CHM's value should not include $18 million for a planned future cash injection. That is just incorrect. And in fact we would say that that approach is grossly incorrect and illogical. And here's a simple example to show you the flaw in this logic.

Imagine an investor comes to you and says I own a gold mine, I've done some feasibility studies, I have the rights to the concession, but that's where it stands. And there's a new investor who's planning to invest and spend $1 billion developing this gold mine, and he'll earn an equity share in the company by doing so. And, according to BRG, what that person should say is therefore I currently own a one billion dollar gold mine.

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That argument is nonsensical. The fact that someone eventually may put in a billion dollars or $18 million may increase the value of the company, but that doesn't change what the company is worth today before that money is invested. So, again, we would say, just based on all this evidence, it's clear that the value of CHM and Claimants' investments implied by these offers is in that $7 to $9 million range.

And if that weren't all, what we also have is Innergex's own financial model that they used to evaluate this project. This is a contemporaneous third-party analysis of the value in the but-for scenario. It includes a forecast of free cash flows to equity, and it specifies a discount rate -- not a hurdle rate, I don't believe it says hurdle rate anywhere in that model, it says discount rate -- specifies a discount rate of 8 per cent, and if you discount those free cash flows at that 8 per cent discount rate you get an implied DCF value of $7.231 million -- again, consistent with our view of these transactions and extremely inconsistent with BRG's view.

Here on slide 16 we just have a comparison of all these various offers and analyses which show

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that they're all in this tight range and they are generally consistent with our DCF, and extremely inconsistent with BRG's DCF valuation, which in our view demonstrates that our analysis is correct and BRG's DCF analysis is not.

Now, turning to the DCF valuation, I'll hand things over to my colleague, Mr Sequeira.

by Mr Sequeira

MR SEQUEIRA: Thank you, Mr Shopp. And good morning and good afternoon to members of the Tribunal.

As Mr Shopp explained, both sets of experts agree that the DCF method is an acceptable method to value the project, but our valuation conclusions are very different. Next slide.

So BRG calculates a fair market value for the project of $31.75 million as of March 2017. We conclude that this value is four times what it should be, or it is inflated by roughly 300 per cent, as you see in the box to the right, and there are five reasons that explain this poor valuation which we've listed here on the slide. I will cover the first two, the cost of equity and the performance bond, and then Mr Shopp will cover the next three, which relate to the actual cost offsets and the modelling of construction costs and sales revenues.

But when you correct for these five issues, the DCF value of the project changes to $7.5 million, which is right in line with the value that's implied by the Innergex offer that Mr Shopp just explained. Now, in the following slides I will address the cost of equity issue first, which is the most significant issue impacting value. Now, before we unpack the details of BRG's cost of equity calculation, there is a simple test you could run to see whether BRG's cost of equity is right or wrong, and that is simply comparing the project's cost of debt with BRG's cost of equity.

The Tribunal will have heard two terms used to describe cost of equity. One is the unlevered cost of equity, which implies the cost of equity where the project has no debt or is debt free, and the second is the levered cost of equity which is the cost of equity when the party has taken on debt. But regardless of whether you're talking about unlevered cost of equity or the levered cost of equity, that cost of equity is always higher than the cost of debt, and I'll explain this with a simple example.

Assume that you have a project that is debt free, that's unlevered, and it's an early stage project and you now have a $1 million debt investment coming into the project. Now, the project has a firm legal obligation to repay that debt with interest within a specified time frame. Now, in the alternative, instead of that debt investment let's assume you now have an equity investment of $1 million that is flowing into this debt free project.

In this case the project has no obligation to repay the equity, nor is there any obligation to pay dividends on the equity. That equity for this project is therefore more risky than the debt and the cost of this equity, this unlevered cost of equity, is therefore higher than the cost of debt. And this is a fundamental financial principle. We've explained this in detail in section 3A of our Second Report, and I invite the Tribunal to take a look that, but it is important to understand that this distinction between levered and unlevered cost of equity makes no difference when you value it whether it should be higher or lower than the cost of debt.

If you go to the next slide we show some numbers here. So the project cost of debt -- which both experts agree is in the range of 7.1 to 7.36 per cent -- is, as you can see here, higher than BRG's unlevered cost of equity of 5.79 per cent. So this is plainly incorrect. And yesterday we heard BRG sidestep and confuse this issue; they said this is a comparison of apples and oranges -- this is not an apples and oranges comparison. This is corporate finance 101. **09:29**

As you can see via the quotes we have on the right, I'll just go to the first two, the first quote says the cost of debt is always less than the cost of equity. It does not matter whether it's a levered cost of equity or an unlevered cost of equity.

The second box is a question posed by Dr Damodaran. The question is clear. It says can the cost of equity ever be lower than the cost of debt for any firm at any stage in its life cycle? And the answer is no, equity investors are always behind lenders in line for cash flows.

So this could not be more clear. It doesn't matter whether the project is in a concept stage, construction stage, operation stage, whether it's levered or unlevered, that cost of equity will always be higher than the cost of debt. And it is surprising to me that the experts have a disagreement on this issue. It's also somewhat troubling. We can have a debate about what the cost of equity should be but there should be no debate that the unlevered cost of equity has to be higher than the cost of debt.

So in my view this is a black-and-white issue, and BRG is dead wrong about this, but it is an important issue, and I welcome questions on this either on cross-examination or from the Tribunal. Next slide. [Slide 21]

So the logical question to ask is, having established that BRG's unlevered cost of equity is too low, the question is why is it so low, and in order to understand that we've got to look at the inputs to the CAPM formula that both experts use to calculate the cost of equity. And we've listed the build-up of the cost of equity calculation here, and we have a disagreement with BRG on three inputs shaded at the top, and we believe that BRG's values for each of these inputs is too low, and when you correct for these inputs the unlevered cost of equity increases to 7.48 per cent, which is above the cost of debt. So I will sequentially address

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each of these inputs in the following slides. Next slide. [Slide 22]

So the first input is the risk-free rate and both experts rely on the yields in the ten-year US Treasury bonds to establish the risk-free rate. The disagreement is the duration over which this yield should be measured. We use the prevailing yield as the valuation date, 14 March 2017, which is 2.6 per cent, but BRG takes a trailing 12-month average yield for the 12 months prior to the valuation date, which gives them a risk-free rate of 1.94 per cent. In our reports we have cited numerous authorities which explain that the risk-free rate should be based on the prevailing rate and prevailing expectations as at the valuation date, which is what we have done.

BRG says that we are using an arbitrary date where the risk-free rate was artificially high but this is simply incorrect. That date is not arbitrary. We are using the valuation date to set the risk-free rate. BRG also has a defence saying that the risk-free rate was on a downward market trend as the valuation date. This is also incorrect, and you can see this on the chart to the right. The vertical dotted black line is the

09:33

valuation date and you can see that in the run-up to the valuation date the yields were generally increasing. But more importantly, as of the valuation date you can see that dotted blue line which shows that the expectation for rates going forward were actually increasing and not decreasing, and therefore we believe our risk-free rate is reasonable, if not conservative, and BRG's risk-free rate is too low. Next slide.

The second input we disagree on is the beta which measures the volatility in the project's price or value relative to the market, and here both experts again agreed that we need to look at a peer group of publicly traded companies to measure this unlevered beta but we disagree on what the peer group should be. BRG relies on 52 companies in the US power sector, and these are all integrated power companies that are primarily focused on transmission and distribution, not on generation, and they have minimal, if any, hydroelectric power generation. We rely instead on 12 companies that operate in the Latin American market and they have a high focus on generation and within generation on hydro power generation. So we believe that is a better peer group that gives us a reliable estimate of beta, and you can also do a reasonableness check. We have here a company which is a subsidiary of Enel called Edegel. It's the largest electricity generator in Peru, and the analysts value this company on an ongoing basis, and they use an unlevered beta of 0.62 for this company, which is slightly higher than our unlevered beta, which again shows that our beta is reasonable if not conservative. 09:34

Next slide.

Here we drill down a little more into the peer group of companies that we use and you can see here that all of our companies have operations in Latin America, they have significant hydropower generation assets, whereas in BRG's peer set there are no companies with operations in Latin America and very few companies that have any significant hydropower generation. So again we maintain that our peer group is a better peer group, and gives you a reliable estimate of beta. Next slide.

The third input we disagree on is the equity risk premium, or the ERP, and we use an ERP of 5.5 per cent, which is based on current premiums, meaning expectations as of the valuation date based on guidance provided by Professors Damodaran and Fernandez and Duff & Phelps. BRG uses an historic average premium over an 80 or 90 year period, and uses a geometric mean for this data to calculate an ERP of 4.62 per cent based on data published by Professor Damodaran. **09:35**

Now, the problem with BRG's method is that Professor Damodaran himself states that reliance on such long running historical averages is not reliable; it's an inferior method because it's a poor predictor of expectations and movements going forward.

Another way to test whether the BRG ERP is reasonable is to look at the total market return, which is the sum of the risk-free rate and the ERP, and we have charted that on the graph to the right. And you can see when you add the risk-free rate and the ERP, the total return that BRG calculates is 6.56 per cent, which is towards the very low end of the range we see of benchmarks here, and our estimate is 8.1 per cent, which is more in line with the consensus view here, which is in the 8 to 9 per cent range. So again we believe that our ERP is reasonable and BRG's ERP is too low. Next slide.

So we've so far been looking at a bottom-up analysis of all the inputs that give us the cost of equity, but we could also look at this

09:37

top-down by comparing BRG's cost of equity and our cost of equity with other benchmarks for cost of equity that are in the record, and that's what we have done on this slide. The red bar shows you BRG's cost of equity over the life of the project. The blue bar shows our estimate of the cost of equity over the life of the project, and the three green bars are benchmarks we have. The first one is Innergex's discount rate, which is 8 per cent, and the next two green bars show you the cost of equity that had been calculated by analysts covering the two largest electricity generators in Peru, these are diversified generators with hydropower operations, and they calculate costs of equity of above 9 per cent for both these companies.

So this again shows that the cost of equity that we calculate is reasonable, if not conservative, and BRG's cost of equity is too low. Next slide.

So in this slide we show you the impact of correcting each of the three inputs I just discussed, so if you start with BRG's valuation in the far left, which is the red bar, $31.75 million, and you progressively correct for the risk-free rate, the equity risk premium and the unlevered beta, the corrected DCF value drops $15.7 million which is roughly a 50 per cent reduction in value so you can clearly see this is a significant factor impacting the valuation. Next slide. **09:38**

So the second area of disagreement is the performance bond, and here what we disagreed with is the way in which BRG models this in the but-for scenario versus the actual scenario because they are not consistent, so in the but-for scenario, in its DCF valuation, BRG assumes that the cash collateral of $5 million that was provided for the performance bond would be released, which is a fair assumption, we agree with that, but in the actual scenario they assume that that $5 million would not be released. But this is an incorrect assumption because in reality this performance bond has not been executed to date, nor will it be executed if Claimants prevail on their claims. Therefore, if Claimants prevail, BRG will claim the $5 million via the DCF valuation but then Claimants would also receive the cash released from the performance bond of $5 million to get a total of $10 million, which would result in a windfall to Claimants.

Now, BRG appears to acknowledge this in their Second Report where they say that, if the

09:39

performance bonds are released, they would reserve the right to update their analysis, but they have not done this as yet, so their analysis as it currently stands captures this additional $5 million value into the DCF model, which has a net effect of a $4 million increase in their DCF value. I'll now turn it back to Mr Shopp who will cover the remaining areas of disagreement.

by Mr Shopp

MR SHOPP: Thank you. So the third difference in our DCF models relates to the so-called actual cost offset. What this means is that BRG offsets the budgeted project construction costs, so in other words the costs that had to be incurred to get the project up and running; BRG reduces those costs which are negatives in the DCF by the amount that Claimants spent from March 2017 to December 2018, so after the valuation date, and in doing so BRG increases its DCF value by roughly $7.1 million based on actual costs in this sort of March 2017 to December 2018 period.

And while we agree sort of in principle that if these costs truly did reduce the budgeted cost, then it could be appropriate to include them in this damages calculation, however we would say that only those costs that serve to actually reduce the budgeted costs should be included as an offset.

So if they are over budget or if they weren't in the budget to begin with, then you can't say that they are reducing something that was in the budget that you're using to construct your DCF. And having looked at the budgeted expenditures versus these actual expenditures, categorising them to the best of our ability based on the information we had, we determined that, at most, $4.3 million of these costs were included in the project budget and should be considered or could be considered as an offset.

However, as we'll discuss later, we think that anything that's relying on Claimants' costs summaries is somewhat questionable due to discrepancies between their alleged cost and the underlying support that has been provided by Claimants. So this is truly an "at most" number, in our view.

Fourth, getting into some more minor issues now, BRG miscalculates the timing and amount of construction costs. For the timing BRG relies on a generic method which evenly spreads all costs over the 30.3 month remaining construction period. We rely on the specific cost allocation schedule as set out in the Hatch report, and we think that's a better method. Similarly, the access road contingency cost. This access road was the most significant construction risk, according to the various engineers and technical evaluators, but the 2017 Hatch report is the only source with a specific estimate of this access road contingency, and we would say that because this is really the only specific source, it's the best source and it contains a specific contingency of $1.316 million, which we apply, and we think that's preferable to BRG's approach, which relies on a generic civil and additional works contingency, sort of this categorical contingency percentage that BRG applies to just the access road, and they use that to come up with an estimate of roughly $0.4 million for this contingency cost.

And, fifth and finally, BRG overestimates electricity prices and sales revenues. These are relatively minor so I won't go into detail too much. I invite you to read our reports where we discuss these at length. But first BRG ignores the asymmetrical price penalty in the RER Contract in which the prices are reduced in years, we call them dry years, when CHM produces less than 130,000 megawatt hours. There's no corresponding price increase if they produce more than the 130 benchmark so that translates to, according to our detailed calculations, a 1.9 per cent average reduction over the life of the contract and, second, BRG assumes that the RER Contract end date is extended from 2036 to 2039, based on legal instruction from its counsel. We understand from our counsel that there is no legal basis to assume that this contract extension would have occurred.

Where does that leave us? Here's a chart that shows starting with BRG's total FMV as of March 2017 value of $31.75 million. Making these corrections, including the cost of equity, performance bond and so on, when these corrections are made you reach a value of $7.519 million which we say is the correct amount, and again is in line with the value implied by all the offers for Claimants' investments.

So, in addition to that, there's also what's been called damages for alleged additional costs. BRG adds $2.4 million for these additional costs and expenses which were incurred starting in January 2019. These include things like the costs of the Lima Arbitration, costs of criminal defence that were incurred by the company, costs of dismantling operations, and so on and so forth. We offer no opinion on the appropriateness of these costs having been incurred or the legal viability of the damages claim, so we just include this in our analysis but understand that it is in dispute between the parties whether this is a relevant damages figure. **09:45**

We would just again note that this $2.4 million number is based on the summary accounting spreadsheets provided by Claimants, but as we'll discuss in a later section, we find multiple issues with Claimants' cost documentation which calls into question, in our view, the reliability of this claim for $2.4 million.

Turning, then, to pre-award interest and the damages conclusion, BRG calculates pre-award interest based on the project's cost of debt of 7.06 per cent. Well, this cost of debt for the project was higher than junk bond rates due to its overall high level of risk. In our view, and as discussed by numerous authors on the topic, which we've quoted some of them on the right, it is economically illogical to award Claimants extra compensation via pre-award interest for undertaking but not having been required to successfully complete a high risk project. In other words, you should not reward the Claimant for a risk that they never took, in particular when it's a very high risk.

And we calculate as an alternative what we consider to be three economically rational potential pre-award interest rates which range from 2.3 to 3.4 per cent. These include Respondent's USD denominated government bond rate under the forced loan theory that Claimants should receive the same rate of return as other lenders to Respondent. We include the yield on investment grade corporate bonds as a proxy for a normal commercially reasonable rate, and, finally, under the risk-free rate theory under which Claimant should only be compensated for the time value of money, we calculate pre-award interest based on the yield on US Treasury bonds. And in our view, again, these are economically rational rates that do not reward Claimants the pre-award interest simply because the project was high risk.

Where does this leave us? We have nominal FMV damages totalling $9.931 million, as you can see in the table, comprised of $7.5 million as what we call the but-for value as of March 2017, $2.4 million in additional costs and expenses, and to those amounts we add pre-award interest calculated based on these three economically rational potential rates ranging from $0.9 to $1.4 million, and that results in total FMV damages as of 1 March 2022 of $10.827 to $11.284 million.

Now, very briefly on sunk costs, which was discussed a bit yesterday, here there is agreement between the experts that sunk costs do not represent the fair market value of Claimants' investments, and therefore if the appropriate standard of compensation is the fair market value of Claimants' investments, then sunk costs or the so-called investment value damages calculation are irrelevant because they don't measure FMV, and that's because sunk costs could be higher than FMV, for instance if there was overspending, or it could be lower than fair market value, for instance if there were positive market project-specific developments.

But in any case, if the goal here is fair market value, sunk costs isn't something that works.

We'd also note that Claimants' sunk costs remain unsupported. BRG has calculated $26.678 million in sunk costs, which we summarise in

09:49

this table to the right, based on accounting summary spreadsheets prepared by Claimants.

And while BRG says that the supporting documents, which is basically a 1400 page pdf that Claimants produced at one point, while BRG says that those supporting documents validate all expenses incurred by Claimants, they performed absolutely no analysis of this issue whatsoever, nor, as far as we're aware, was any analysis of this type of validation exercise presented by Mr Sillen. We heard yesterday that he had performed a reconciliation, but I don't believe we've seen any such reconciliation.

We did do a detailed analysis of this 1400 page pdf in an attempt to compare what Claimants say the costs were in their Excel spreadsheet versus what the underlying documents can support, and our analysis shows that nearly half of the alleged sunk costs remain unsupported. We talk about this in our report; it sort of summarised some of the issues that are summarised in the table to the right.

But what this means at the end of the day, in our view this is further sort of evidence/information that sunk costs would not be reliable even as an alternative damages remedy.

09:50

And finally, even ignoring all of that, all of the reliability concerns and the fact that it doesn't approximate FMV, even if you were to go to sunk costs still there are still a minimum of three necessary corrections to BRG's calculation. We show them here. First, remove the performance bond guarantee for the reasons Mr Sequeira discussed. Second, remove the upstream project costs on the basis that those were, we understand, unaffected by the breaches. And, third, apply a lower pre-award interest rate at the rates we discussed earlier, and what that would leave you with is total sunk costs with interest through March 2022 ranging from $23.5 to $25.1 million in damages.

And that concludes our presentation. We thank you again for the opportunity to discuss with you today, and we're happy to answer any questions you might have.

PRESIDENT: Before we move to the cross-examination, I have one question, Mr Shopp, and that is the last section where you address sunk costs and where you state you agree with BRG that sunk costs do not represent FMV, fair market value. But could they represent damages in general?

MR SHOPP: I think that may be more of an

09:52
issue for you to decide. I think we would say that if the goal is FMV, sunk costs don't necessarily approximate it. I think --

PRESIDENT: I do understand the theory being I've spent, according to your corrected -- what is it, depending where you look, from $25 to $23 million corrected. I spent this, and in any case, whatever may be else about valuations that you have, I spent it and I want my money back in case there's a breach.

MR SHOPP: If the theory is that compensation should be "give them their money back with interest" as opposed to "they're entitled to the value of their investment at the time of the deprivation or the expropriation", then sunk costs could be appropriate as damages in that context. Again, I think we would caution that there are some reliability concerns about these numbers but yes, that could be an appropriate damages remedy, if the idea is to just give them back any money that they put into the investment, rather than focusing on what the investment is worth.

PRESIDENT: I raise this point because most of these fair market valuations are done in the context of expropriation claims, also in FET claims as they call it, fair and equitable treatment treaty claims, but if you are under contract analysis there are various theories for what you call damages. But apparently you have not been instructed to do that? 09:53

MR SHOPP: No, we have not.

PRESIDENT: It may also not be a matter in this arbitration.

Thank you, Mr Shopp.

Mr Zeballos? Please proceed.

MR ZEBALLOS: Yes, I'm ready to move forward, Mr President.

PRESIDENT: In the meantime we've received another CD-05 from you?

MR ZEBALLOS: Yes.

PRESIDENT: Are you going to use that?

MR ZEBALLOS: Yes, I am going to use that today.

THE COURT REPORTER: Can I respectfully ask for people to remember the 3 to 5 second rule?

MR ZEBALLOS: I will do my best. I'm a Chilean raised in New York so it's a tall order to ask me to speak slowly, but I will do my best.

Cross-examination by Claimants

by Mr Zeballos

MR ZEBALLOS: Good morning, Mr Shopp.

MR SHOPP: Good morning. **09:55**

MR ZEBALLOS: Good morning, Mr Sequeira.

MR SEQUEIRA: Good morning, counsel.

MR ZEBALLOS: I'm going to address my questions to Mr Shopp primarily. Just as we did yesterday, if you feel your colleague, Mr Shopp, is more appropriate to answer the questions, just indicate that. It's not going to be an issue for me.

You've prepared two reports for this proceeding, right, Mr Shopp?

MR SHOPP: That's correct.

MR ZEBALLOS: And those reports provide two alternative damages approaches, correct?

MR SHOPP: I'm not sure to what you're referring.

MR ZEBALLOS: One of your approaches is a DCF analysis for damages, correct?

MR SHOPP: One of the approaches is what I would maybe term "fair market value" as opposed to "DCF".

MR ZEBALLOS: But your fair market value analysis uses a DCF approach, correct?

MR SHOPP: As part of it. Also the implied value from the offers.

09:55

MR ZEBALLOS: And the other approach you use, Mr Shopp, is a sunk cost analysis, right?

MR SHOPP: I wouldn't say we use that approach. BRG presented that as, in other words what I understand Claimants presented as an alternative damages remedy called -- they referred to it as investment value, so I wouldn't say that we presented that as a damages approach. That was responding to what BRG apparently based on instruction proposed as an alternative damages remedy.

MR ZEBALLOS: But you agree that the DCF approach is the appropriate means to determine the value of the Mamacocha Project, correct?

MR SHOPP: Yes, I mean the DCF approach is applicable here in our view under this sort of fair market value damages approach. That's right.

MR ZEBALLOS: And your DCF analysis relies on a valuation date of March 14, 2017, right?

MR SHOPP: Correct.

MR ZEBALLOS: And you assess damages in your DCF analysis as of that date, correct?

MR SHOPP: Yes and no, because BRG introduced this actual cost offset point. We are, of course, looking at costs that Claimant incurred

through December 2018 as a sort of part of that DCF, **09:57**
but generally speaking the idea is to assess the value as of March 2017.

MR ZEBALLOS: And the information you considered for your DCF analysis was information that existed on or before that date, right?

MR SHOPP: That should be the case, yes. I believe so.

MR ZEBALLOS: Mr Shopp, do you confirm that any documents material to your conclusion are attached to or referenced in your report?

MR SHOPP: Yes, that should be the case.

MR ZEBALLOS: And if you didn't attach or refer to documents in your reports, it's because they aren't material to the conclusions you reached in your report?

MR SHOPP: Not material enough that they were directly relevant to a footnote or something we were citing. Certainly we reviewed more documents than we cited in our reports but I would say the most material ones -- or everything we've cited is material and the most material -- that should include the most material ones, but not all that we reviewed.

MR ZEBALLOS: And you don't use the word

"Amparo" anywhere in your First Report at all, do you? 09:58

MR SHOPP: That's testing my memory. I'll take your word for it.

MR ZEBALLOS: I'll represent to you that I ran a word search and that it doesn't appear. That's a reasonable response, Mr Shopp.

And in your Second Report the word "Amparo", I'll represent to you I ran a word search in your Second Report, and the word "Amparo" appears only in one footnote, footnote 79.

MR SHOPP: That may be the case.

MR ZEBALLOS: I'd like to take you to paragraph 16 of your First Report. Can we put that up on the screen, Tom?

In this paragraph you describe BRG's approach to fair market damages as described -- sorry.

In this paragraph you describe BRG's approach to fair market damages as comprised of two elements. One is BRG's estimate of the value of the project, and two is Claimants' actual costs. Is that right?

MR SHOPP: That's right. That's not how BRG presented it, they didn't sort of split things

09:59

exactly that way, but we split them here in that manner.

MR ZEBALLOS: And in your Second Report you also consider the fair market value of the project on valuation date and Claimants' actual costs, right?

MR SHOPP: We'd have to look. I guess actual costs meaning the additional costs and expenses or this cost offset piece.

MR ZEBALLOS: Let's pull up appendix 7 of your Second Report.

MR SHOPP: Sure.

MR ZEBALLOS: Let's focus on line 10. Do you see where it says "but-for"?

MR SHOPP: Yes, that's excluding this actual cost offset, which is the next line down.

MR ZEBALLOS: Right. And the but-for refers to the fair market value on the valuation date, correct?

MR SHOPP: That's right, before accounting for any of these additional costs Claimants had incurred over that March 2017 to December 2018 period.

MR ZEBALLOS: And the figure in cell F10 is $3.402 million, correct?

MR SHOPP: That's correct.

MR ZEBALLOS: And that's the result your DCF model provided, correct?

MR SHOPP: That's right.

MR ZEBALLOS: And that constitutes your estimate of the fair market value of the project on March 14, 2017 based on your DCF methodology, correct?

MR SHOPP: Correct.

MR ZEBALLOS: Mr Shopp, your piggy bank hypothetical that you just described, in that hypothetical your piggy bank doesn't generate any revenue, does it?

MR SHOPP: Well, you can take money out of the piggy bank. That would be generating revenue. It's not a business, if that's what you mean. I could reach into a piggy bank, take out a dollar, and that would be revenue generation of a sort. It's something that has cash and can generate cash at its simplest level.

MR ZEBALLOS: This isn't a piggy bank that makes money, right? It doesn't print dollars, does it?

MR SHOPP: No. I would like that kind of piggy bank!

MR ZEBALLOS: I'd like to walk you through a hypothetical, Mr Shopp. My hypothetical is a revenue producing project. OK? **10:01**

MR SHOPP: Sure.

MR ZEBALLOS: And this revenue producing project in my hypothetical is a farm. OK? In year one I have $10 million in costs, and this includes all my costs -- seeds, et cetera, everything I need. OK? Are you following me?

MR SHOPP: Yes.

MR ZEBALLOS: In year 2 I have my harvest, and I also have a guaranteed buyer that will guarantee me $100 million of income net of costs. So far, so good?

MR SHOPP: Yes.

MR ZEBALLOS: So I'd like to run a fair market value analysis using the DCF method of my project. All right? And we're going to assume no externalities, no inflation, no completion risk, no other impacts. We're going to keep this very simple. For the sake of simplicity let's assume a discount rate of 10 per cent. OK?

MR SHOPP: OK.

MR ZEBALLOS: So on Day 1 the value of my farm project will be $80 million, which is my income discounted by 10 per cent to $90 million and subtracting my $10 million costs, right?

MR SHOPP: Yes, that sounds right.

MR ZEBALLOS: So the farm is worth $80 million on Day 1 even though the harvest isn't until year 2, correct?

MR SHOPP: Correct. That's the premise of DCF valuation for an early stage project.

MR ZEBALLOS: Let's change the hypothetical a little bit. Let's assume I have the money to develop the farm on my own, but you and I, we agree to be 50/50 partners. OK? And again, no externalities, nothing to suggest that you won't invest, so there's certainty that you and I are going to invest in this project together. OK?

MR SHOPP: OK.

MR ZEBALLOS: Now, the only change to my hypothetical is our partnership. Everything else we've discussed remains the same. The fair value of the farm in my hypothetical partnership, it would still be $80 million, right?

MR SHOPP: Yes. We could reach -- I suppose if you agreed to sell me half of your farm for $5 million that would probably call into question your alleged DCF value, but yes, adding a

10:04

new investor does not fundamentally change the value of the investment before that investor comes in. That's what we said earlier. Pre-money value is pre-money value. It's only new investment that adds to the value of the business.

MR ZEBALLOS: And so my $80 million farm, that's the value of my farm even though I've only invested $5 million and you've only invested $5 million. The fair market value of my farm on Day 1 remains $80 million, just as it has in every other scenario I've given you.

MR SHOPP: Yes. I mean again, I would agree with that hypothetical. I don't think it really goes to the issue at hand here, but I do agree with that hypothetical.

MR ZEBALLOS: And my 50 per cent share in that farm is $40 million, right? It's worth $40 million.

MR SHOPP: If I had agreed to buy 50 per cent from you for $40 million, I think you could reasonably say that your share is worth $40 million. On the DCF basis, that might be what you come up with as well.

MR ZEBALLOS: And the fair market value of both equity stakes together -- in other words, of

100 percent -- remains $80 million, right? I think you just said that. **10:05**

MR SHOPP: Yes.

MR ZEBALLOS: And that value wouldn't change if I was thinking of selling my interest, right?

MR SHOPP: No, not from thinking of selling. It would change if I, as this new investor, came in and actually spent $5 million, because then we would not have 10 million in expenses in year 1. Instead, we would only have another five because I would have at that point increased the value of the company by spending money.

MR ZEBALLOS: And the value of my $80 million farm wouldn't change if you were thinking of selling your 50 per cent share, would it?

MR SHOPP: Thinking of -- no.

MR ZEBALLOS: Give me one second. Let's make one last alteration in my hypothetical. Let's say at the last minute you pull out of my project unexpectedly but I want to go forward, but remember I can still put up the other $5 million. So I put up the rest of the money and the project goes forward. OK. In my hypothetical my farm is still worth $80 million on Day 1, right? 10:06

MR SHOPP: Yes. Pre-money value is pre-money value. The farm is worth what it's worth before a new investor comes in. Again, as a concept I agree with you.

MR ZEBALLOS: And it wouldn't make any difference that perhaps we'd only ever conceived of it as a 50-50 partnership between the two of us. As long as the project goes forward the value of a 100 percent equity stake in the project remains $80 million on Day 1, correct?

MR SEQUEIRA: Yes, that's right.

MR ZEBALLOS: And in the hypothetical I just gave you, we calculate the fair market value of the farm by applying a DCF analysis to the projected future cash flows of the farm, correct?

MR SHOPP: That's how you did it in your hypothetical. As I mentioned, if you had offered to sell me the farm or 50 per cent of the farm for $5 million, I think we could reasonably say it's probably not worth 80 at that point. So, yes, you could have a DCF. DCFs are -- come up with lots of different results based on different inputs, as we see here, but in your hypothetical you only talked about the DCF. If we had an offer, as we do here, obviously we would want to consider that as well. **10:08**

MR ZEBALLOS: Your DCF model -- your DCF model of the Mamacocha Project relies on projected future cash flows from that project, correct?

MR SHOPP: Correct, both negative in the early years for construction and debt repayment, and then positive through revenue generation.

MR ZEBALLOS: Right. And your model applies a DCF methodology to those future cash flows to determine fair market value, right?

MR SHOPP: We discount the future cash flows to equity and determine the value, yes.

INTERPRETER: Perdón que aproveche para interrumpir, les podría pedir a los participantes que hablen un poquito más despacio, que dejen una pequeña pausa entre las preguntas y respuestas para la interpretación. Gracias.

MR ZEBALLOS: Sí, por supuesto, lo siento.

Do we still have appendix M up on the screen here?

Just so we're clear, I think we've established that you conclude that your DCF value of the project representing the fair market value of the project on March 14, 2017 is $3.402 million.

So let's focus on the next line, which is the $4.117 million. 10:09

The $4.117 million represents actual costs and expenditures incurred in the project, as we discussed earlier today. Isn't that right?

MR SHOPP: It represents, based on our analysis, the portion of the costs incurred by Claimants from March 2017 to December 2018 that offset or were within the project's budget that's included in the DCF. It's not all of the costs they incurred according to their summary spreadsheets, but it is a subset of those.

MR ZEBALLOS: Let's pull up slide 4 of your presentation from this morning.

Do you see the line where it says "Fair market value of Claimants' investments as of 14 March 2017", and you have the number 7.5?

MR SHOPP: Yes, I see that.

MR ZEBALLOS: Yes. That number combines the fair market value which we just looked at, the $3.4 million, plus the $4 million and change from the actual costs and expenditures, correct?

MR SHOPP: That's right. And this is simply following BRG's approach. You could look at table 1 of their Second Report where they have what they call the but-for value of the Mamacocha Project as of 14 March 2017 and list $31.75 million, so we're not trying to hide this. This is literally using BRG's exact same format for demonstrating these numbers. So we're happy to split it further if you think that would be useful. **10:11**

MR ZEBALLOS: Yes, Mr Shopp. I'm just trying to make -- I think what you mean to say here is -- as you have this caption, it shouldn't say fair market value of Claimants' investment; it should say damages based on fair market value methodology or DCF methodology or however you want to say it, but it's a combination of fair market value and actual costs but the fair market value component of it, as we've just established, is 3.4. That's correct, right?

MR SHOPP: The DCF itself, excluding the sort of actual cost offset produces $3.4 million. That's right.

MR ZEBALLOS: Let's take a look at your assessment of actual costs. Please turn to paragraph 80 of your Second Report. Tom, if you could put that up, please. And, Mr Shopp, if at any time I'm referring to a paragraph or page in your report and I forget to pull it up, feel free to

10:12

interrupt me to ask me to pull the document up.

MR SHOPP: I have a hard copy of the reports here as well.

MR ZEBALLOS: Now, the $4.285 million referenced here, I'm going to refer to this as $4 million simply because I know that there's some adjustment with the DCF. When you run these numbers they might change marginally so I don't want to -- I'm not trying to trip you up on that difference, I'm just going to say 4 million. If you want me to be more precise, you can say so, but this $4 million in actual costs, you didn't include any of those actual costs in your First Report, right?

MR SHOPP: No, and as we explained in our First Report BRG really didn't say why they were doing this offset. It wasn't clear to us that this was sort of just a cost claim added to the DCF, or what we later found out, that they viewed it as an offset to construction costs. Again, it was a little unclear why costs such as these would be considered in what BRG called the but-for value as of March 2017. So we discussed them; we didn't ignore those costs and how they were incorporated; we sort of asked for clarification; BRG provided it; and we proceeded on that basis in our Second Report.

MR ZEBALLOS: And the actual costs that you do include in your Second Report -- and again I'm going to use a rounding figure here -- but are about 2 and a half million dollars less than the actual costs that BRG includes in its Second Report, right? **10:14**

MR SHOPP: That's right. I think it's -- let's call it 4 versus 6 and a half, I think is pretty close.

MR ZEBALLOS: OK. Let's turn to paragraph 79 in your Second Report, and you exclude this 2 and a half million dollars or so on the grounds that they were either over budget or not included in the budget at all, correct?

MR SHOPP: That's right. The idea is that if your DCF has a budget and the premise is that you are sort of avoiding having to incur those costs that are in the budget because they've already been spent by Claimants at a subsequent date, then it's necessary that they're included in the budget. If it's over budget then well, it turns out your budget was too low and should have been higher, if they're not in the budget at all then they again are just an extra cost that wasn't in the budget, and they can't be said to be an "offset" as BRG termed it.

MR ZEBALLOS: Let's take a look at the construction budget, which is table 6 at page 37 of your Second Report. 10:16

This table shows a total construction budget of $7,314,534, and actual expenditures through December of 2018 of $7,084,513, correct?

MR SHOPP: That's right, and I would say this isn't the total construction budget.
I believe -- and I don't know that we need to, we can turn to appendix O -- I think this may just be the project owner component of the construction budget, or some other subset that relates to this type of cost. But you are right, those two numbers are correct, $7.3 and $7.1 million.

MR ZEBALLOS: Right. And so actual expenditures are lower than the total budgeted expenditure here, right?

MR SHOPP: Which is unsurprising given they didn't actually start construction on the project. I would have expected them to be much lower still for that reason but yes, it is lower.

PRESIDENT: Gentlemen, may I remind you the plea of the court reporters and the interpreters to take a number of seconds between Q and A? Thank you.

MR ZEBALLOS: Yes, Mr President. **10:17**

And your table 6 contains a number of sub categories; technical employee, project administration, technical consulting, social, PR, et cetera, et cetera. Do you see those?

MR SHOPP: Yes, I do see those.

MR ZEBALLOS: And are these categories that you identified or categories that Claimants identified?

MR SHOPP: I'd have to check which of them matched one to one. Essentially what we had is you have a budget that splits it in a certain way according to categories, and then you have a spreadsheet of hundreds, if not thousands of different cost items which we had some where we had receipts or we had an invoice, which don't have obviously the same categories. There's not some uniform categorisation system. So the challenge here and what was necessary was to try to categorise both the budgeted and the actual expenditures according to some common system that was detailed enough to be meaningful but not so detailed that it was thousands of rows, and then do a comparison on that basis.

But I'd have to look at the budget to see

which of these were exactly the same categories. **10:18**
I know we probably combined a few or maybe reworded it just for ease of comparison given that we are looking at a budget which is very nice and neatly organised, versus thousands of costs which we have to sort of fit into one of those budget categories.

MR ZEBALLOS: But, Mr Shopp, these are your categories, right? These are your team's categories?

MR SHOPP: Again, I assume the budget may say something like "project admin" or it may have "social" or it may have "easements" as a category. So we did do a categorisation system and I think we tried to have them be corresponding where that was possible. I have to look at appendix O and the budgets to see kind of which of these are direct overlaps of categories and which are ones where we had to sort of combine categories from the budget to make the best comparison we could based on the underlying expense data.

MR ZEBALLOS: So based on your identification of these categories -- I'm trying to understand what you're saying. If I mis-state it please correct me.

But based on your understanding of the

hundreds of thousands of line items that you saw, you've tried to simplify this by putting it into these categories. Am I right so far?

MR SHOPP: That's right. I mean appendix O goes into this sort of exercise in some detail where we categorise each of the expense items -- I don't know if it's hundreds of thousands, certainly hundreds of expense line items -- and try to match that to an equivalent budget category, and this is because when BRG did this exercise, they just said Claimants spent $7 million, that's an offset to construction costs, and we looked at it and said well, a lot of these things appear to have nothing to do with construction costs, which again stands to reason as construction hadn't started yet. And this was our attempt to say, OK, which of these could conceivably be included in the construction budget versus which ones are outside of or above the construction budget, but it was an exercise necessitated by the nature of the data to try to sort of fit the cost with a budget line item as best we could.

MR ZEBALLOS: So you used your best judgment, for example, to determine what budget is, whether a line item fit, was a technical employee or a technical consultant or a project admin, you guys were the ones who figured out whether that expense should go into that category? **10:21**

MR SHOPP: To the best of our ability -- I apologise for the lack of a pause. We had invoices at times. You know, some of it is to an extent subjective. But, again, it's all set out in detail in appendix O of our report.

MR ZEBALLOS: OK. And the budgets -- the column where you have budgeted expenditures and you have it divided by these categories, so then you used the same exercise to determine what the budget was for these categories as well, correct?

MR SHOPP: Correct. Again, I would refer you to appendix O, which has all of this in detail, in sort of gory detail. It's quite a big appendix, I believe.

MR ZEBALLOS: And then my same question for actual expenditures. So once you determined what the budget was using the best of your ability, your best judgment, to try to fit individual expenses into these budgets, you looked at the actual expenditures and did the same exercise to determine whether something was over or under budget, correct?

MR SHOPP: We categorised the different expenses and then whether it's over or under budget just depends on what the sum for each category would have been. So we didn't look at an individual expense and say is this over or under budget; we grouped and categorised all of the expenses, grouped and categorised the budget items and compared them on a like-for-like basis as best we could. Again, because there's no sort of common categorisation system that naturally exists for accounting line items, you know, there is no common so we had to come up with something for that. And, again, that is documented in detail in our appendix O. **10:22**

MR ZEBALLOS: I see.

So let's take a look at the project administration line. So this is way over budget. This shows \$2.3 -- \$2.4 million if we round up, \$2.4 million in actual expenditures but only \$700,000 in budgeted expenditure, so this is one of the worst line items from your perspective, right? This is way over budget.

MR SHOPP: I don't think I would say "worst". It's one where I believe that's all the employees at sort of the corporate level who were in Miami who continued to draw salaries and benefits, you know, during this period and relatively high salaries and, again, it's higher than what appeared to be the equivalent line item in the budget itself. **10:24**

MR ZEBALLOS: And then let's take a look technical employees.

So technical employees, the project was way under budget here, almost a million dollars -- actually over a million dollars under budget here, right?

MR SHOPP: That's right. And that's, again, as I would expect, given that they hadn't actually started construction of the project. You would think that if you're not building a hydro plant, you're probably not going to be hiring too many technical employees at that point.

MR ZEBALLOS: So, Mr Shopp, if somebody is an engineer, if their professional title is engineer, do you put them in technical employee or do you put them in project administration or do you put them in technical consulting? How do you decide that?

MR SHOPP: Again, I think maybe we could go to appendix O. To the best of our ability we looked at people's job titles, we had invoices from various people, payroll records, so we tried -- if

10:25

it was clearly a line engineer or somebody who's at the plant day-to-day doing work, we would try to group them I assume with technical employee. If it was a -- you know, sort of the equivalent of a Hatch or a Pöyry who's doing consulting work, we would call that technical consulting. If it's somebody who we know was the CEO or CFO or some very high upper level management person who is not necessarily involved at the project level, they would have been grouped into project admin, or if it was rent for an office in Miami again -- or wherever.

So, again, this is looking at the individual expenses, trying to the best of our ability to categorise these expenses such that it can be compared with the budget, and again, for every line item this was an expensive exercise, we did this for every line item expense as set out in detail in appendix O.

MR ZEBALLOS: So if you didn't know you used your best judgment, is what you're telling me?

MR SHOPP: Yes, again, because nobody before us had tried to do this. The assumption was well, they spent it so it must be an offset to the budget when, based on this, that certainly appears to be unreasonable, and I think as a matter of kind of logic, that they hadn't actually started construction yet, also seems to be reasonable. **10:26**

MR ZEBALLOS: And it's your position that that's more reasonable than simply using the construction budget, its budgets that were produced to you that show that actual expenditures were less than budgeted expenditures?

MR SHOPP: Of course actual expenditures were less than budgeted within a construction -- but we are trying to give Claimants credit for all the work they've done if it conceivably fell within one of these categories. So, again, they had not started construction. They have management employees who are in Miami who presumably would have had to be there, you know, had construction been ongoing so we said, OK, that counts towards the budget. But $750,000 in legal fees, that's not something that's in the construction budget, as far as we could tell, so that's something that we would say shouldn't be in there. Or this extra -- apparent extra $1 point -- what, 6 million in project admin costs that is above what's in the budget. So we're not -- trying to compare the bottom line numbers ignores what those costs actually are, and that's our point. And to say that it's an offset, it's reasonable and we think necessary to try to establish that it's a cost that actually is in the budget such that it can be an offset to the budget.

MR ZEBALLOS: All right. We're almost done with this. I just want to move -- you just mentioned the legal expense. These legal expenditures, these include legal expenditures incurred by Claimants in the real world, right?

MR SHOPP: That's right. I believe so, yes.

MR ZEBALLOS: And Claimants allege that these are legal expenditures undertaken because of the measures, right?

MR SHOPP: I don't know about these specific legal expenses. Claimants may make that allegation for this $753,000. I don't know.

MR ZEBALLOS: Right but -- I'm sorry. 3-second rule.

But you don't dispute that those fees were incurred, right?

MR SHOPP: Well, there is an accounting summary spreadsheet that has those costs on it. In some cases there are invoices which support those amounts. On a global basis we do find that a lot of the costs are unsupported with that underlying detail, but there is a spreadsheet that says that those costs were incurred. That is true.

MR ZEBALLOS: But you put them in this line item instead of project admin so you did that for a reason I would think, right?

MR SHOPP: Yes, I think because they're identified as an invoice from a law firm and -- yes, I mean we could have put them in project admin and they would have been similarly over budget, but they were specified as legal expenses because the line item in the spreadsheet says "Invoice from" whatever law firm or whatever lawyer.

MR ZEBALLOS: And a portion of the RER fees are also excluded here because they were supposedly over budget, correct?

MR SHOPP: Yes, it appears that the budget had $250,000 over this roughly one year nine month period but according, again, to these cost spreadsheets there were $400 and roughly $78,000 worth of costs, so again it appeared to be over budget based on that.

MR ZEBALLOS: Right. And you don't dispute that those fees were incurred, right?

MR SHOPP: Again, they're in the

10:30

spreadsheet. I don't know that we've seen an underlying document for those specifically, but this would be an example of where, if you're calculating the DCF value based on a budget and you say the budget's 250 grand, $250,000, and then it turns out that that cost is $477,000 and that's what you deduct or add under this actual cost offset, well, that's wrong because your DCF budget was too low to start with, so you are overstating the but-for FMV by that delta, by that $227,000. That's why you -- for this to be an offset it has to offset a specific amount that is included in the budget.

MR ZEBALLOS: So when you removed actual expenditures from that additional cost analysis, did you account for them anywhere else in your report since they were actual expenses incurred by Claimants?

MR SHOPP: No, I think -- sorry.

MR ZEBALLOS: Or did you just remove them all together?

MR SHOPP: So we removed them from this valuation. We have a note, we say it twice, in which case these costs -- you know, if they're outside the budget could be claimed separately as an additional cost if Claimants can demonstrate they were caused by the alleged breaches. 10:32

So we're not saying they just should disappear into the ether if there is a legal basis put forward by Claimants for sort of recouping those costs, but to simply assume that well, it was spent, therefore it should be recouped within the context of the DCF model makes no sense. It has to be something that adds to the value of the project as sort of envisioned in this but-for world. So if Claimants can say there's 753,000 in legal fees, I can prove that that's the amount of them, I can prove that that total amount is strictly associated with the alleged breaches and here's my new damages claim for that, just like is done with this additional costs and expenses of $2.412 million, which is a separate claim, then that could be appropriate. I mean we acknowledge that in our report.

But to simply assume without that level of even sort of allegation that these specific costs were caused by the breaches, at least that we're aware of, BRG certainly didn't make any such link, then yes, we removed them from the analysis but acknowledged that if they are truly and directly and with support proved -- sorry, due to the alleged breaches, then Claimants could make a claim for them and then we'd discuss that on its terms. **10:33**

MR ZEBALLOS: Mr President, I think this would be a good place for a 15-minute break.

PRESIDENT: Good. Recess until 15.50 CET. Gentlemen, Mr Shopp and Mr Sequeira, you are not allowed to discuss this case with anyone because you are under testimony.

MR SEQUEIRA: Yes, of course.

MR SHOPP: We confirm.

(Short break from 10.33 EST to 10.50 EST)

PRESIDENT: Mr Zeballos, please continue the cross-examination, and please be mindful of the 3-second rule.

MR ZEBALLOS: Yes. Could you bear with me one second, Mr Shopp and Mr President? My live note isn't working. I just need to reset it.

MR SHOPP: If I may, if this is allowed, I don't know if it's a function of my failing eyesight or memory, but I referred to appendix O when we were talking about --

PRESIDENT: Before we do that, I think Mr Zeballos has a technical issue, and then we'll come back.

MR SHOPP: OK.

MR ZEBALLOS: Mr Shopp, I think I know where you're going. It's appendix Q. **10:51**

MR SHOPP: That's right.

MR ZEBALLOS: For the sake of the record there's an inadvertent error in the Versant report. Is it 2? It is Versant Report 2. The appendix refers to appendix O as support for additional costs. It should be appendix Q. We have no issue with it; that's an absolutely appropriate correction.

PRESIDENT: Mr Zeballos, you have overcome your technical --

MR ZEBALLOS: Yes, I have.

PRESIDENT: Please continue the cross-examination. Again, reminder, gentlemen, 1, 2, 3. Please continue.

MR ZEBALLOS: Thank you for your patience with my technical issue, Mr President.

Mr Shopp, we're going to move to a different topic. Your report highlights -- in your words highlights several issues with the BA Energy Solutions report. That's a quote from Versant 2, paragraph 95, if you want to see it. But essentially I want to get to the point that you raised some issues with the BA Energy Solutions report, correct?

MR SHOPP: That's right. In both our first and second reports we raised some issues regarding being able to review the detail underlying it, the results it produced. We didn't ever make a change to that but we do raise issues, I think is a good way to put it, about the BAES Report.

MR ZEBALLOS: And just to be clear, what we're talking about, BA Energy Solutions spot price forecast, correct?

MR SHOPP: That's correct. Spot -- it's the monomic price forecast which includes both the spot price and then the guaranteed capacity payment, and in particular for the sort of farther out years of the forecast when the RER Contract concludes and CHM would be selling in sort of this spot -- this monomic spot market.

MR ZEBALLOS: Yes, and to be clear, when I say spot price I'm referring to the monomic spot price. I may forget to use the word "monomic".

Mr Shopp, you're familiar with MINEM, the Peruvian Ministry of Energy and Mines, right?

MR SHOPP: Generally speaking, yes, I'm familiar with them and that they exist, and what they do broadly.

MR ZEBALLOS: Mr Shopp, did Respondents ever provide you with any spot price forecasts from MINEM? **10:54**

MR SHOPP: I would have to look back through the record. There may -- we looked on MINEM's sort of -- I don't know if it was their website or their publications at various points. I think there may be some of those even referred to within the BA Energy Solutions paper that they produced for BRG. I can't recall off the top of my head if Respondent ever sent us any of those or if we found them on our own or whether it was exactly a MINEM publication, so I think -- "I don't know" is probably the safest answer there.

MR ZEBALLOS: But you don't include any MINEM spot price forecast in your reports, correct?

MR SHOPP: No, we don't. The comparator we have to BAES is Innergex. There's a graph that shows that.

MR ZEBALLOS: And are you familiar with OSINERGMIN -- for the court reporter -- I think that's been one of the defined terms that's been provided. OSINERGMIN regulates and supervises the energy industry in Peru. Are you familiar with them, Mr Shopp?

10:55

MR SHOPP: Generally, yes.

MR ZEBALLOS: And did Respondent ever provide you with any spot price forecasts from OSINERGMIN?

MR SHOPP: Again, I think the safest answer to that is I don't know. I don't recall any off the top of my head.

MR ZEBALLOS: And did Respondent ever provide you with any spot price forecasts from OSINERGMIN?

MR SHOPP: As I said, I think the safest answer is I don't recall. I certainly don't recall any specifically, but "I don't know" is probably the safest answer. We don't include any in our comparison.

MR ZEBALLOS: And in my concern to count to three I asked you the same question twice.

What I meant to ask you was you don't refer to any OSINERGMIN spot price forecasts in your reports, correct?

MR SEQUEIRA: Yes, I don't believe that we do.

MR ZEBALLOS: Are you familiar with COES, which is the Comité de Operación Económica del Sistema Interconectado Nacional, which is

10:56

responsible for planning and co-ordinating the operation of the generation, transmission and distribution systems that form Peru's interconnected network?

MR SHOPP: I'm familiar. I know -- whether that was in our own research and looking for various tariff rates and looking for these capacity payment rates, or if it was discussed by BA Energy Solutions in their paper, I am familiar with COES -- not the full name and description that you gave it but yes, I've been on their website before I believe.

MR ZEBALLOS: And did you ever ask for any spot price forecasts from COES?

MR SHOPP: I don't believe we did, no.

MR ZEBALLOS: Did Respondent ever provide you with any spot price forecasts from any Peruvian State entity?

MR SHOPP: I don't know that -- I don't believe that Respondents did, to the best of my memory.

MR ZEBALLOS: And you were never provided with any COES spot price forecasts, right?

MR SHOPP: Not to the best of my memory.

MR ZEBALLOS: Did Respondent ever retain

10:58

an expert to provide an alternate spot price forecast?

MR SHOPP: No. Yes, no, there was no separate expert retained to address the BAES forecast.

MR ZEBALLOS: Did you ever ask respondents to retain an outside expert to determine a spot price forecast like the BA Energy Solutions report?

MR SHOPP: No, and I think again, that's somewhat of a function of the fact that we don't change the energy price forecast in the DCF model, so it's not -- we have questions about this forecast; it appears aggressive, certainly compared to Innergex, but ultimately we don't decrease the monomic price forecast used in the DCF.

MR ZEBALLOS: Let's pull up paragraph 61 of your First Report. Tom, can you pull it up on the screen, please?

If you look at paragraph 62 of your First Report, you state -- I'm sorry, paragraph 61 of your First Report right here.

Here you state that the BAES forecast is "extremely bullish compared to recent market trends in Peru and other contemporaneous price forecasts".

Do you see that?

MR SHOPP: That's right. **10:59**

MR ZEBALLOS: When you say contemporary price forecasts here, you mean price forecasts as of the valuation date, right?

MR SHOPP: Yes, I think we could probably say and Innergex's price forecasts. That would be a fine substitution in that sentence.

MR ZEBALLOS: Yes, so it wasn't multiple price forecasts. It was just the Innergex projections, correct?

MR SHOPP: Yes. The recent market trends, as the following sentence says what happened between 2012 and 2017, but for the forecast period Innergex is the comparator we have.

MR ZEBALLOS: OK. Let's take a look at paragraph 62 of your First Report. OK. Here you say, "Given the divergence with recent price trends and the Innergex forecast, it is hard to believe that the BAES"-- which is the BA Energy Solutions --"forecast accurately reflects the market's contemporaneous views regarding Peruvian electricity prices as of March 2017".

Do you see that?

MR SEQUEIRA: Yes.

MR ZEBALLOS: Mr Shopp, in your DCF model

I think you said you used the BA Energy Solutions' spot price forecasts to run that model, correct? **11:01**

MR SHOPP: That's right. We don't modify the price forecast.

MR ZEBALLOS: And using the BA Energy Solutions forecasts, you arrived at a fair market valuation of $3.4 million, correct?

MR SEQUEIRA: Yes, excluding the additional cost offset, that's right.

MR ZEBALLOS: Did you ever run your DCF model using the Innergex spot price forecasts?

MR SHOPP: We may have at some point. I don't recall the exact number.

MR ZEBALLOS: And if you did you would expect it to result in a lower fair market value, right?

MR SHOPP: Yes, lower, I think possibly slightly negative based on the forecast being lower. I mean, again, that's a reason not to just sort of pick and choose, cherry pick one variable and substitute it into a model. Innergex had its own model, which as we've said has an associated value/implied value of $7.2 million. Just cherry picking their price forecast we didn't think would be appropriate. That's why we didn't do it. But

11:02

sitting here now, I'm guessing that's a lower, if not slightly negative, FMV if you were to use Innergex, if I had to guess.

MR ZEBALLOS: Let's pull up --

PRESIDENT: Mr Zeballos, may I remind you about the three seconds?

MR ZEBALLOS: I'm sorry, Mr President.

PRESIDENT: I know you want to keep pace in the examination, which I understand, but please remind that we have court reporters and interpreters.

MR ZEBALLOS: Thank you. Old habits die hard, Mr President. I'll do my best.

PRESIDENT: I know, I know. We'll keep reminding you.

MR ZEBALLOS: Could we please pull up Claimants' demonstrative number 5?

Mr Shopp, this demonstrative shows the results of your DCF model after running it using the Innergex spot prices. Do you see that this results in a negative fair market value of $5 million -- $5.1 million, about?

MR SHOPP: I see what that says. I'll take it -- sort of take your representation that that number is correct and the model's been run correctly, but again, that's not a very surprising result. **11:03**

MR ZEBALLOS: No one would invest in a project with a negative DCF valuation, right?

MR SHOPP: No. And I think that would be a reason not to just substitute Innergex's spot price into our DCF, which is one of the reasons why we didn't do that or wouldn't do that. Innergex again had its own DCF that had its price forecast, all of its other assumptions regarding costs, growth, production, budget, discount rate, and if you run that on its own terms it's a DCF value/implied value of $7.2 million so -- but no, to your specific question, I don't think anyone would invest in a project with negative NPV.

MR ZEBALLOS: Tom, you can take this down.

Let's pull up paragraph 3 of your First Report. So, Mr Shopp, this is paragraph 3 of your First Report, and it defines the measures at issue in this dispute, and those measures are the lawsuit by the Regional Government of Arequipa on 14 March 2017, which sought to revoke certain environmental permits previously granted to Mamacocha; 2, the filing of criminal charges by Arequipa's environmental prosecutor in March 2017;

3, the denial of Mamacocha's civil works authorisation in May of 2017; and, 4, MINEM's refusal to grant extensions to account for the delays caused by the lawsuit and its commencement of an arbitration in Lima to nullify prior extensions.

Do you agree that these are the measures alleged by Claimants for the purposes of -- that you referred to for the purposes of preparing your First and Second Reports?

MR SHOPP: That's right. This is sort of a background section. I don't know that we intended for this to be the be-all/end-all. Obviously these are Claimants' allegations and for factual and legal issues we are just summarising what we understood to be the breaches alleged that were relevant but -- to the best of our understanding and ability.

MR ZEBALLOS: And, Mr Shopp, have you reviewed the full factual record and testimony in this case to form an opinion as to the potential impacts of the measures on your valuation?

MR SHOPP: I'm not entirely sure. Have I read every page of every exhibit and legal authority and witness statement and expert report? I don't believe so. We certainly looked at the index of documents and tried to identify everything that could be relevant. I think it's a pretty big record in this case. There was document production, there were lots of other things, so I don't know that I can say I've read every page, no. **11:06**

MR ZEBALLOS: Let's pull up paragraph 129 of your First Report. In this paragraph you cite to a separate paragraph from an e-mail for Mr Sillen to support your contention, "that Innergex later became concerned that the project was not as attractive as it had been initially thought".

Do you see that? It's in the paragraph above the quote.

MR SHOPP: That's right. It appeared that appeared to be the case. I'm not testifying on matters of fact, but that's what appeared to be the case based on that e-mail.

MR ZEBALLOS: Let's turn to exhibit C-168, which is the e-mail cited in paragraph 129 of your report.

Mr Shopp, who provided you with this exhibit?

MR SHOPP: I don't recall. I don't remember if that was something from the record or if it was from something Claimants had produced or from Respondent to the lawyers. I can't recall. We didn't have it on our own to start with. **11:08**

MR ZEBALLOS: And did anyone tell you how to interpret the meaning of this e-mail?

MR SHOPP: No. I don't really understand what you mean by that.

MR ZEBALLOS: Did anyone tell you how to interpret the meaning of this e-mail?

MR SHOPP: No.

MR ZEBALLOS: Let's turn to paragraph 130 of your report.

Here in this section -- this paragraph immediately follows the paragraph that we just discussed. Here in this paragraph you imply that Mr Sillen's testimony is referring to revisions by Pöyry to the project's average electricity generation, correct?

MR SHOPP: No, that's not correct. I think those are separate. Mr Sillen appeared to be saying they are less positive about the project, and we are saying separately from his e-mail, or what he might have thought, that there was one potentially meaningful or meaningful development during this period, which was this decrease in the expected generation capacity from 140,000-megawatt hours per year to roughly 135.

So we're not trying to suggest that that's what Mr Sillen meant or that's what Innergex meant, just that it appeared that there was some concern on Innergex's part that it wouldn't be as attractive as originally conceived, and that this is one potential development that appeared meaningful given that it's -- you know, a decrease in revenues without any change in costs, using, I don't know, what is that, 3 and a half, 4 per cent of revenues because of the lower generation potential, but we're not trying to put words in Mr Sillen's mouth. We're just observing that this was a change that occurred during that period of time. **11:09**

MR ZEBALLOS: Right. When you quote Mr Sillen in 129 and you say the project was not as attractive as initially thought, one of the reasons you think that Innergex might have thought the project was not as attractive as originally thought is Pöyry's forecast revision that's referenced in 130. Am I understanding you right?

MR SHOPP: That could be a reason. We see that Mr Sillen -- and I think that's a direct quote -- their main concerns are time and that the project is not as attractive to them as they thought it was when they started negotiations, indicating that they would like to improve the deal.

So we said, OK, what could explain this change in perceived value that they wanted to maybe renegotiate terms, and one thing that would somewhat obviously have an effect on Innergex's evaluation of the project is a 4 per cent revenue drop without a corresponding decrease in costs or any other change. That's really just a direct hit to value. So we're not suggesting that is what specifically they meant; Mr Sillen doesn't say what they meant; I don't know that he says one way or another, but we're not trying to put words in his mouth, we're just saying this is a development which would have been -- or at least very likely could have been viewed negatively by Innergex during that intervening period that's referred to.

MR ZEBALLOS: But you acknowledge, Mr Shopp, that Innergex knew about this no later than March 1, 2017, right?

MR SHOPP: I think we know that that's when Pöyry -- sort of the report is dated or maybe it was mailed. I don't know if and when -- or at least when that would have been delivered to Innergex by the Claimants. I think what we know is that the Pöyry report, or the estimate was revised on March 1. As to when it was delivered to Innergex, that I don't know. Probably around that date, I would think. **11:12**

MR ZEBALLOS: And March 1, 2017, Mr Shopp, that's prior to the valuation date while Innergex's offer was pending, right -- Innergex's 2017 offer was pending, right?

MR SHOPP: Yes, that's what I understand to be the case. The valuation date is I think March 14, 2017?

MR ZEBALLOS: That's correct, Mr Shopp. And you don't identify any report -- I'm sorry. And you don't identify in your report any document in the record that suggests that the terms of Innergex's pending offer changed between March 1 and March 14, 2017, right?

MR SHOPP: No. I think, you know, when we look at the Innergex deal we look at the February 2017 proposed terms. So what we're looking at here is kind of what might explain that gap between this $3.4 and roughly $8 million that is the correct value implied by the Innergex deal, and this is one potential explanation of that. We're not trying to change the Innergex offer; it was what it was in February 2017. This is just an attempt to say why might those numbers be that sort of 4-ish million dollar difference at that point.

MR ZEBALLOS: I'm just trying to understand what you just said. So it's your position that the project lost more than half of its value between February 2017 and March 14, 2017?

MR SHOPP: No, that's not my position. Innergex value is one marker/indicator of value. The value implied by the Innergex February 2017 offer was 8-ish million dollars. Our DCF comes up with $3.4 million. This is saying well, is there something that might sort of bridge some of that gap between these numbers, and one thing is that our DCF, which uses the lower generation amount from Pöyry of 135,000, which is lower than the generation amount that Innergex would have used in its evaluation in February, that may explain some of the gap. And if you were to go into Innergex's financial model, which previously had a value of $7.2 million, change the generation capacity, that would reduce their DCF from $7.2 to $4.9 million, so again saying our DCF relies on up-to-date numbers in March, Innergex's offer and DCF relied on older previous numbers, if you correct that one element of their DCF, update it, our results become more in line. They're still not perfectly in line, you wouldn't expect two values to be exactly the same developed using different models and different methods, but they're reasonably close.

MR ZEBALLOS: Innergex never decreased its offer, right?

MR SHOPP: Other than this e-mail saying that they are saying the project's not as attractive as they thought and they would like to improve the deal, I'm not aware of any sort of firm conclusion to that, but yes, I mean, there's an indication they were looking to do that. But when we talk about the Innergex offer, we're talking about the February 2017 offer.

MR ZEBALLOS: Mr Shopp, are you aware that the RGA Lawsuit was filed on March 14, 2017?

MR SHOPP: Yes.

MR ZEBALLOS: And are you aware that the Arequipa environmental prosecutor filed a criminal lawsuit based on the allegations in the RGA Lawsuit on March 24, 2017?

MR SHOPP: I'll take your word on that exact date. I'm aware of that general time frame certainly.

MR ZEBALLOS: And are you aware that

on May 16, 2017 the regional water authority, the AAA, denied the project its civil works authorisation? **11:16**

MR SHOPP: Again, I'll take your word on the date. We may refer to that specifically somewhere in our report.

MR ZEBALLOS: And are you aware that Claimants contend that each one of these actions that I just described to you comprise at least one of the measures alleged in this case?

MR SHOPP: Yes.

MR ZEBALLOS: So you agree that each of the measures I just referenced took place between March 14, 2017 and May 16, 2017, correct?

MR SHOPP: Assuming the dates you gave are correct. I apologise, I don't have them memorised, but I'll take your word for it.

MR ZEBALLOS: Let's pull up C-0168 again.

Mr Shopp, the date of this e-mail is May 17, 2017, correct?

MR SHOPP: Correct.

MR ZEBALLOS: And that's after all of these three events had occurred?

MR SHOPP: Chronologically that would be true, yes.

MR ZEBALLOS: And all of these occurred after the valuation date, right? **11:17**

MR SHOPP: Yes, they're after March 14th.

MR ZEBALLOS: Are you aware that this exhibit C-168 was included as part of Mr Sillen's testimony in this case, in his first witness statement?

MR SHOPP: I should have checked the cite. Maybe that's what we cited it to. Yes, I believe so. We would have reviewed his witness statement and the associated documents.

MR ZEBALLOS: Let's turn to Mr Sillen's first witness statement at paragraph 133. In paragraph 133 Mr Sillen says, "I kept Innergex and DEG informed of these events as they transpired. Both entities were sympathetic, but neither wanted to move forward with their respective agreements with Latam Hydro until a resolution to the RGA Lawsuit was reached. Even if we could somehow obtain a resolution to the RGA Lawsuit, the existence of the criminal investigation and the issues with the AAA permit made it difficult, if not unlikely, for Innergex and DEG to restore their faith in the project. In May 2017, Innergex confirmed to us that the regional opposition meant that the project was 'not as attractive to them as they thought it was' earlier in the year". 11:19

Do you see that?

MR SHOPP: I see that's his witness statement, yes.

MR ZEBALLOS: I think you just said you would have considered Mr Sillen's testimony when you prepared your reports, is that right?

MR SHOPP: We certainly reviewed it, yes.

MR ZEBALLOS: But you don't mention Mr Sillen's testimony in paragraph 129 or paragraph 130 of your report?

MR SHOPP: I'll have to check the cites, but no, we may not. And again, the concluding part of that e-mail is indicating that they would like to improve the terms of the deal, so it didn't seem to be a total lack of interest. You know, it's not that they were walking away apparently; they wanted to improve the terms of the deal, which we assumed meant commercially.

MR ZEBALLOS: Give me one second.

I have no further questions, Mr Shopp. Thank you.

PRESIDENT: Thank you, Mr Zeballos. Ms Endicott, are you still on line?

MS ENDICOTT: I'm here, just trying to minimise the number of video windows you need to have open, because I know it makes them so small. **11:20**

PRESIDENT: I understand. Do you need time to review the questions you want to ask in redirect, or do you have any questions actually for redirect?

MS ENDICOTT: I may have just a couple. With the Tribunal's indulgence could I have, say, ten minutes to confer with my team briefly?

PRESIDENT: By all means. Normally we would have lunch time in your time zone, dinner in my time zone, but it's pretty early, I can tell you, so if we can adapt the schedule, take your ten minutes, and then come back and tell us how you would like to proceed.

MS ENDICOTT: Thank you. Appreciate that.

PRESIDENT: Ten minutes recess until 16.35 CET.

(Short break from 11.21 EST to 10.31 EST)

PRESIDENT: I see everybody is back. Ms Endicott, for the Respondent, redirect, any questions?

MS ENDICOTT: Yes, just one.

PRESIDENT: OK, please go ahead.

Re-examination by Claimants 11:32

by Ms Endicott

MS ENDICOTT: Today, during your cross-examination, Mr Shopp, Mr Zeballos posed a hypothetical to you at page 49, line 16 of the transcript about a revenue producing project that was a farm. At page 52, line 1, of the transcript you responded that you don't really think that the hypothetical goes to the issue at hand here.

Could you explain why not?

MR SHOPP: Sure. So in that hypothetical what was being compared was sort of the future DCF value of a farm compared to what it would cost to get it up and running, and I don't think there's any dispute that that's how projects work. You pay something upfront and you get benefits later on. But that's not what we're talking about here. We're talking about assessing the implied value from a known series of offers for this specific project and figuring out what we can do with the value using that data. It's not projecting cash flows, it's not a DCF versus costs, you know revenues versus costs. We know for a fact that Claimants were offered somewhere between $7 and $8 million for their project. We know that in the sort of February 2017

Innergex offer, Innergex was willing to invest $17.8 million to receive a 70 per cent share in what would become, post investment, a $28 million project.

So the sort of general hypothetical of costs upfront and cash flows later and whether somebody invests or doesn't invest, that's really not what we're talking about here. We're talking about assessing known offers that imply values in a very tight range of $7 to $9 million, and that farm example doesn't get to that point because it sort of assumes that the DCF is what matters, when what we're talking about is the offers themselves in that case.

MS ENDICOTT: Thank you. I have no further questions.

PRESIDENT: Thank you, Ms Endicott. Professor Tawil, any questions from the Tribunal?

PROFESSOR TAWIL: Thanks, Mr President. I just want a clarification. Only one clarification.

Questions by the Arbitral Tribunal

PROFESSOR TAWIL: Could I ask if Versant could put in the screen, or someone -- Tom, I don't know, slide 18 of their presentation today?

MR SHOPP: I'm happy to if you'd like me to do it. **11:35**

PROFESSOR TAWIL: Please.

MR SHOPP: I need to open it up. Sorry.

PROFESSOR TAWIL: If -- and I'm going to start with a question. If I understood correctly, the main questioning of BRG said DCF was the issue that they took into account, sort of the value, not taking into account that Innergex had not injected the money to the project, so that it was sort of inflated because it was concerning money that was not yet injected.

Now the question is how does this slide 18 relate with the other thing? I mean you're saying here that the BRG's valuation is inflated by 322%. Which valuation? The valuation where you already deleted the $17 or $18 million? Because I mean I just don't understand how you say it's inflated if you have already discounted the $18 million of Innergex not in the project.

MR SHOPP: Think of them as two completely separate things. There's BRG's assessment of the Innergex offer, which they say implies a value of $27 million. That's where we would say you've incorrectly included $18 million in costs, or in

11:36

funds that Innergex would invest. That version, that analysis by BRG, correcting the Innergex no investment, decreases it from $27 to roughly $9. This is separate to that. This is BRG's DCF, which doesn't incorporate Innergex. Innergex isn't part of this DCF. It just assumes Claimants would fund any equity investment, they would get future revenues, so there is no Innergex in this DCF world.

PROFESSOR TAWIL: I understand now. If you deduct the Innergex investment not made, are we still having a valuation inflated by 322 per cent?

MR SHOPP: Their DCF valuation, which doesn't consider Innergex at all, is still inflated because they use a discount rate which is too low, a performance bond, et cetera. Kind of mechanically you could get to almost the same place if you just deducted $18 million from it, but that's not -- that's coincidental. These are truly separate analyses. The $18 million subtraction only applies to BRG's assessment of the Innergex offer. Separately in BRG's DCF, which does not consider Innergex as part of it, the reason that analysis is inflated is because of these five discrete what we would call errors in their DCF.

So you can sort of forget about Innergex when you're talking about the DCF model, because it's not modelled in there. **11:38**

PROFESSOR TAWIL: Thank you. I have no further questions, Albert Jan.

PRESIDENT: Thank you. Professor Vinuesa, any questions?

PROFESSOR VINUESA: No, I have no questions. Thank you.

PRESIDENT: I have also no questions. Ms Endicott, any follow-up questions from questions arising from the Tribunal?

MS ENDICOTT: No, thank you.

PRESIDENT: Mr Zeballos, any questions arriving? Mr Zeballos, you are on mute.

MR ZEBALLOS: No, Mr President. I have no further questions, thank you. At least I enforced the three second rule.

PRESIDENT: Well, at the end we got it all right. Mr Shopp and Mr Sequeira, thank you for testifying as an expert witness. You are now excused.

MR SEQUEIRA: Thank you.

MR SHOPP: Thank you very much.

PRESIDENT: Ms Endicott and Mr Grané, for the Respondent, and Mr Zeballos, so what the

Tribunal proposes is now also to have the presentation by the United States, the NDP presentation, because then we can conclude the day in, say, 30 to 40 minutes. Is that acceptable to the parties? It's acceptable to the United States. I inquired with them.

MR ZEBALLOS: I will need a few minutes to consult with my team, Mr President. Is that OK? Could we have a --

PRESIDENT: It's an early day that you have then, so -- OK. Mr Grané, do you need also to consult?

MR GRANÉ: No, Mr President. We are perfectly fine to proceed. Of course, it's really the US who needs to tell us if they're ready, and they have, so we are ready to proceed.

PRESIDENT: I see Ms Thornton and Ms Grosh are online. Ms Thornton, bear with me for a second. Thank you for being prepared to do your presentation early, but we have to wait until Claimant has taken instructions internally.

MR ZEBALLOS: I'll be as quick as I can, Mr President.

[Pause]

MR ZEBALLOS: Mr President, apologise for the delay. We're ready to proceed. **11:42**

PRESIDENT: Thank you. Then with the consent of both parties we can proceed.

Ms Thornton, you have 30 minutes to make your oral presentation on behalf of the United States as a non-disputing party.

Presentation by Non-Disputing Party
by Ms Thornton

MS THORNTON: Thank you, Mr President and members of the Tribunal for this opportunity. Good morning. I will just make some very brief remarks on behalf of the United States today pursuant to article 10.20.2 of the US-Peru Trade Promotion Agreement, or TPA.

Today I will address five questions of treaty interpretation arising out of the parties' responses to the US written submission dated November 19, 2021. I will address first the weight of non-disputing party submissions; second, the relationship of the waiver requirement and claims that may be brought under article 10.16.1; third, the customary international law minimum standard of treatment; fourth, the most favoured nation treatment standard and the non-conforming measure exception in article 10.13.2 and annex 2 of the TPA; and, fifth, the meaning or lack thereof of silence on any topic in US non-disputing party submissions. 11:43

So I begin my remarks by addressing the weight due to US views on matters addressed in a non-disputing party submission.

States are well placed to provide authentic interpretations of their treaties including in proceedings before investor-state tribunals like this one. Article 10.20.2 ensures that the non-disputing party to a dispute under the US-Peru TPA can provide its views on the correct interpretation of the TPA. The TPA parties consider non-disputing party submissions to be an important tool in this respect, and the United States consistently includes non-disputing party provisions in its investment agreements to reinforce the importance of these submissions in the interpretation of the provisions of these agreements, and we routinely make such submissions.

Article 31 of the Vienna Convention on the Law of Treaties recognises the important role that the states parties play in the interpretation of their agreements. Although the United States is not a party to the Vienna Convention, we consider that article 31 reflects customary international law on treaty interpretation. Article 31, paragraph 3 states that in interpreting a treaty there shall be taken into account, together with the context, any subsequent agreement between the parties regarding the interpretation of the treaty or application of its provisions, and any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation. 11:45

Article 31 is framed in mandatory terms. It is unequivocal that subsequent agreements between the parties and subsequent practice of the parties shall be taken into account. Thus, if the Tribunal concludes there is either a subsequent agreement between the parties or a subsequent practice that establishes such an agreement regarding the interpretation of a treaty provision, the Tribunal must take that into account in its interpretation of the provision.

Where the submissions by the two TPA parties demonstrate they agree on the proper interpretation of a given provision, the Tribunal must, in accordance with article 31.3A take this agreement into account. In addition, the TPA parties' concordant interpretations may also constitute subsequent practice under 31.3B.

In response to arguments that non-disputing party submissions are not entitled to deference because they are made in the course of arbitration, this is simply not true. The TPA parties expressly included the mechanism to provide interpretations to investor-state tribunals in the course of an arbitration for a reason. Indeed, the International Law Commission has commented that subsequent practice may include statements in the course of a legal dispute.

Accordingly where the TPA party submissions in an arbitration evidence the common understanding of a given provision, this constitutes subsequent practice that must be taken into account by the Tribunal under article 31.3B.

Now I would note as well that in its written observations on a non disputing party submission Peru agreed that the TPA parties have reached either a subsequent agreement or subsequent practice with respect to those treaty provisions on which they have evidenced their common understanding through their submissions in this proceeding.

Additionally, investment tribunals have

agreed that submissions by the NAFTA parties in arbitrations under NAFTA Chapter 11, including non-disputing party submissions, may serve to form subsequent practice. For example, the Mobil v Canada Tribunal found that arbitral submissions by the NAFTA parties constituted subsequent practice and observed that "the subsequent practice of the parties to a treaty, if it establishes the agreement of the parties regarding the interpretation of the treaty, is entitled to be accorded considerable weight".

I'm quoting from paragraph 158 of the Mobil v Canada decision on jurisdiction and admissibility dated July 13, 2018, and I would point you also to paragraphs 103, 104, and 158-160 of that decision for context.

The Tribunal in Canadian Cattlemen for Fair Trade of course reached a similar conclusion at paragraphs 188-189 of its award on jurisdiction dated January 28, 2008.

I would also note in response to comments on this issue that TPA article 10.22.3, which concerns interpretations by the Free Trade Commission, and article 10.20.2, which concerns non-disputing party submissions, merely establish separate mechanisms for the parties to provide interpretations of the treaty. Nothing in the TPA's texts -- [loss of sound] -- to binding authoritative interpretations of the TPA that the parties intended to preclude themselves from issuing non-binding but nevertheless authentic means of interpretation of the TPA provisions. 11:48

PRESIDENT: Ms Thornton, there was an issue with the sound. Could you please repeat the last sentence as of "Nothing in the TPA text".

MS THORNTON: Thank you. I hope it's not my bandwidth. Apologies for that.

PRESIDENT: It's OK.

MS THORNTON: Nothing in the TPA's text suggests that in granting the Free Trade Commission the ability to issue binding authoritative interpretations of the TPA that the parties intended to preclude themselves from issuing non-binding, but nevertheless authentic, means of interpretation of TPA provisions through their submissions to investor-state tribunals, or to preclude a tribunal from giving such submissions the weight to which they would otherwise be entitled.

To sum up on this first point, whether the Tribunal considers that the interpretations presented by the two TPA parties as a subsequent agreement under 31.3A, as a subsequent practice under 31.3B, or both, on any particular provision the outcome is the same. The Tribunal must take the TPA parties' common understanding of the provisions of their treaty into account. **11:50**

The next topic I will address concerns the relationship between the TPA's waiver requirement and claims brought under 10.13.1. Article 18.2B --

THE INTERPRETER: Perdón, disculpe que interrumpa, soy el estenotipista en español. Hay un problema con el sonido y está siendo difícil la interpretación, y además va un poco rápido tambien. No sé si es un problema con el micrófono.

COURT REPORTER: I'm sorry to interrupt. There's a problem with Ms Thornton's sound and it's very difficult to interpret her. Plus she is going quite fast. It might be a problem of bandwidth indeed.

PRESIDENT: Two questions by the interpreters. One is could you please slow down a little bit.

MS THORNTON: I got that, yes.

PRESIDENT: If you go to 50 per cent, that's OK, I grant you more time then, so don't worry that you then have to complete in 30 minutes. I will give you more time because then you have a better transcript and better interpretation. And point 2 is that there is an issue still with your bandwidth, I guess, so could you start again at when you said "The next topic is". Then you started to waver. **11:51**

MS THORNTON: I will. Thank you. And if I continue to have difficulties I apologise, I may need to ask my colleague to step in, but I will continue until you tell me otherwise.

PRESIDENT: Don't worry. I will monitor the situation.

MS THORNTON: Thank you.

The next topic I will address concerns the relationship between the TPA's waiver requirement and claims that may be brought under article 10.16.1. Article 10.18.2(b) requires that Claimants waive any right to initiate or continue before any administrative tribunal or court under the law of any party, or other dispute settlement procedures, any proceeding with respect to any measure alleged to constitute a breach referred to in article 10.16.

In our November submission, the United States stated that the waiver provision does not preclude the concurrent submission of treaty and contract claims under article 10.16.1 before one tribunal, provided that issues such as potential double recovery and inconsistent findings are otherwise addressed.

Under article 10.16.1, however, only the Claimant on its own behalf, or the Claimant on behalf of an enterprise of the Respondent that it owns or controls directly or indirectly, may submit to arbitration a claim that the Respondent has breached an obligation of section A of the TPA's investment chapter, an investment authorisation, or an investment agreement.

Thus, while the TPA contemplates that certain treaty claims may be brought together with certain contract claims, such claims may not be brought under article 10.16.1 -- they may only be brought under 10.16.1 by a Claimant investor.

Article 10.16.1 does not provide standing to a domestic enterprise of the Respondent that the investor owns or controls for the enterprise to bring a claim itself. Nor does it provide for the joinder of other Claimants.

The third topic of my remarks concerns the customary international law minimum standard of treatment. TPA article 10.5 provides that each party shall accord to covered investments treatment in accordance with customary international law, including fair and equitable treatment and full protection and security. This provision prescribes the customary international law minimum standard of treatment of aliens as the minimum standard of treatment to be afforded to covered investments. **11:54**

Annex 10A to the Agreement addresses the methodology for determining whether a customary international law rule covered by article 10.5 has crystallised. The annex expresses the parties' shared understanding that customary international law generally and is specifically referenced in article 10.5, results from a general and consistent practice of states that they follow from a sense of level obligation.

Thus, in annex 10A the parties confirmed their understanding and application --

PRESIDENT: Sorry, Ms Thornton, can you please repeat the last sentence? "Thus, in annex 10A"?

MS THORNTON: Yes. In annex 10A the parties confirmed their understanding and application of this two-element approach, state practice and opinio juris which is the standard practice of states and international courts, including the International Court of Justice. **11:55**

As the United States observed in our written submission, decisions of international courts and arbitral tribunals interpreting fair and equitable treatment as a concept of customary international law are not themselves instances of State practice for purposes of evidencing customary international law, although such decisions can be relevant for determining State practice when they include an examination of such practice. A formulation of a purported rule of customary international law based entirely on arbitral awards that lack this examination of State practice and opinio juris fails to establish a rule of customary law as incorporated by article 10.5.

The United States therefore does not assert that arbitral awards are without relevance. Our submissions do cite to arbitral awards concerning the minimum standard, but we cite to certain awards such as Glamis because they correctly observe that arbitral awards do not constitute State practice and cannot by themselves create or prove customary international law.

11:57

We acknowledge that arbitral awards can be relevant and illustrative where they have examined State practice and opinio juris in order to determine whether a purported element of fair and equitable treatment has crystallised into a rule of customary international law within the minimum standard.

Finally, on this topic, I would also note that while the TPA parties consented to allow investor-state tribunals to decide issues and dispute in accordance with the agreement and applicable rules of international law, they did not consent to delegate to Chapter 10 Tribunals the authority to develop the content of customary international law, which must be determined solely through a thorough examination of State practice and opinio juris.

The fourth topic I will address elaborates on the US interpretation of the most favoured nation treatment standard contained in article 10.4.

As stated in our written submission, for a claimant to establish a breach of the most favoured nation treatment obligation under article 10.4, the investor has the burden of proving that it or its investments, 1, were accorded treatment; 2, were in like circumstances with identified investors or investments of a non party or another party; and, 3, received treatment less favourable than that accorded to those identified investors or investments.

This means that if the claimant does not identify treatment that is actually being accorded with respect to an investor or investment of a non party or another party in like circumstances, no violation of article 10.4 can be established. In other words, the claimant must identify a measure adopted or maintained by a party through which that party accorded more favourable treatment as opposed to speculation as to how a hypothetical measure might have applied to investors or investments of a non party or another party.

Moreover, a party does not accord treatment through the mere existence of provisions and as other international agreements, such as umbrella clauses or clauses that impose autonomous fair and equitable treatment standards. Treatment accorded by a party could include, however, measures adopted or maintained by a party in connection with carrying out its obligations under such provisions.

As we additionally observed in our written

12:00

submission, a Claimant must establish that the alleged non-conforming measures that constituted less favourable treatment are not subject to the exceptions contained in annex 2 of the TPA. In that annex, both parties reserve, in accordance with articles 10.13 and 11.6, the right to adopt or maintain any measure that accords differential treatment to countries under any bilateral or multilateral international agreement in force or signed prior to the date of entry into force of this agreement.

Annex 2 does not require the State's parties to affirmatively exercise an annex 2 reservation for a generally applicable measure.

As the explanatory notes to annex 2 provide in accordance with TPA article 10.13.2, the articles specified under the heading "Obligations concerned" in a State party's entry to annex 2 simply do not apply to the sectors, sub sectors, and activities identified in that entry. No further action by a State party with respect to the non-conforming measures described is required.

Moreover, annex 2 provides that the States parties reserve the right to adopt or maintain measures according differential treatment. This

12:01

provision excludes pre-existing non-conforming measures and not just ones adopted in the future from the obligations listed. This -- [loss of sound] -- entry in investment agreements is intended to recognise that the parties to such --

PRESIDENT: Ms Thornton, can you repeat the last sentence? You faded.

MS THORNTON: Yes.

PRESIDENT: Thank you.

MS THORNTON: So I was noting that the language is that the parties reserve the right to adopt or maintain measures according differential treatment, and that that provision excludes pre-existing non-conforming measures and not just ones adopted in the future from the obligations listed.

This construction, common in trade and investment agreements, is intended to recognise that parties to such negotiations commonly have existing measures that they are not agreeing to remove, and the formulation was necessary to avoid a situation where a state might be in non-compliance with its obligations as soon as the treaty entered into force.

Requiring a state party to affirmatively exercise such a reservation of rights would be nonsensical -- [loss of sound] -- and language, context, and purpose of annex 2.

THE REPORTER: I did not get the last sentence.

MS THORNTON: Sorry about that. The last sentence was requiring a state party to affirmatively exercise such a reservation of rights would be nonsensical and contrary to the language, context, and purpose of annex 2.

I am quite close to done, so hopefully we can get through this.

Finally, I would just emphasise that the United States stands by the interpretations set forth in its written submission, although we did not address all of those issues today. And this brings me to my final topic, the issue of silence and issues of interpretation in which a US non-disputing party submission, whether written or oral, does not reach.

In every non-disputing party submission we make, and we do so here, the United States explains that the submission takes no position on the application of the treaty to the facts of the dispute, and that no inference should be drawn from the absence of comment on any issue not addressed in it. **12:04**

Rather, a non-disputing party submission aims to share the proper interpretation of disputed treaty provisions in a way that is helpful to the Tribunal. In any given case there may be numerous interpretative issues in dispute that the United States chooses not to address. We make it perfectly plain that it would be incorrect to read into our silence any particular position on the topics not addressed.

As the standard US assertion on silence makes clear, silence is not acquiescence to any interpretative position advanced by either disputing party in a case.

And with that final observation I will close my remarks, and thank the Tribunal again for the opportunity to present the views of the United States on these important interpretative issues.

PRESIDENT: Thank you, Ms Thornton, for presenting the view of the United States as a non-disputing party. You may stay on, of course, online as a non-disputing party.

I point now back to counsel for the Claimants. I see Mr Grané for Respondent, OK.

12:05

Mr Reisenfeld? Basically we come to the conclusion of the day. Unless there are other businesses to transact, we can then adjourn until Friday, but are there any points you would like to raise, Mr Reisenfeld, of procedure, admin or household?

MR REISENFELD: Claimants do not have anything to raise at this time.

PRESIDENT: Thank you. Mr Grané?

MR GRANÉ: Nothing at this time, Mr President. In the unlikely event that something arises before our closing arguments on Friday, we'll be sure to write to the Tribunal and hopefully I will try to resolve any issue with opposing counsel before we do so. But this moment we have nothing, thank you.

PRESIDENT: I look to my co-arbitrators. Professor Tawil, anything further?

PROFESSOR TAWIL: No, Mr Chairman. Thanks.

PRESIDENT: Professor Vinuesa?

PROFESSOR VINUESA: No, no. Thank you.

PRESIDENT: Ana, is there anything from ICSID's perspective?

MS CONOVER: Nothing from our end. Thank you.

PRESIDENT: Thank you. Then I close for today and we see each other on Friday. And if there's a question that arises in the meantime from the parties, please feel free to contact us, with always a copy to the other side. **12:07**

MR REISENFELD: Thank you.

MR GRANÉ: Thank you.

(The hearing was adjourned at 12.07 pm EST)