BEFORE THE HONORABLE TRIBUNAL ESTABLISHED PURSUANT TO CHAPTER ELEVEN OF THE NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)

MARVIN ROY FELDMAN KARPA
CLAIMANT

v.

THE UNITED MEXICAN STATES,
RESPONDENT

ICSID Case No. ARB(AF)/99/1

ADDITIONAL OBSERVATIONS ON THE PRELIMINARY QUESTIONS

COUNSEL FOR THE RESPONDENT:
Hugo Perezcano Díaz

ASSISTED BY:

Secretaría de Comercio y Fomento Industrial
Máximo Romero Jiménez
Fernando Reséndiz Wong

Shaw Pittman
Stephan E. Becker

Thomas & Davis
Christopher Thomas
J. Cameron Mowatt

ADDITIONAL OBSERVATIONS ON THE PRELIMINARY QUESTIONS

PART I: INTRODUCTION

1. In Procedural Order No. 4, the Tribunal directed the Respondent to file its Counter-memorial on the preliminary questions by 8 September 2000 and to provide any additional observations by 22 September 2000.

2. This submission consists of the Respondent's additional observations on arguments made in the Memorial on Preliminary Issues and the Counter-memorial on Preliminary Questions.

3. Although the Respondent submits that the Tribunal should dismiss this claim, this submission also addresses, in the event that the Tribunal holds otherwise, the appropriate form and content of future requests for production of documents and witnesses, and directions of the Tribunal that may assist the parties in the orderly and efficient conduct of this proceeding.

4. The headings and terminology used in this submission correspond with the headings and terminology used in the Counter-memorial on Preliminary Questions.

PART II: THE TRIBUNAL'S JURISDICTION *RATIONE PERSONAE*

5. The Claimant argues that, for the purposes of the NAFTA, he is both an national of the United States and a national of Mexico and thus, on a simplistic reading of the applicable provisions of Chapter Eleven, he could be an "investor of another Party" and thereby have standing to sue Mexico.

6. The Claimant makes the point, which is not disputed, that Chapter Eleven does not contain an express provision prohibiting a "dual national"— an individual holding citizenship in two NAFTA Parties or an individual holding citizenship in one Party and permanent resident status in another—from commencing arbitration against any Party in which he holds NAFTA nationality.

7. The Claimant notes the anomaly of the simplistic interpretation he propounds—that he would equally be entitled to sue the United States under Chapter Eleven—but tries to avoid the issue by arguing that citizenship, not permanent resident status, should be the determinative factor. Significantly, he says nothing of the dilemma that would arise in a case of dual citizenship.

8. Under the NAFTA, "national means (not "includes" as the Claimant says in the Memorial[1]) a natural person who is a citizen or permanent resident of a Party...". The NAFTA

---

1. Memorial, paragraph 90.

places citizens and permanent residents on an equal footing. There is no basis to infer that citizenship should "trump"[2] permanent residency in the application of any provision of the NAFTA.

9. The clear effect of the simplistic interpretation the Claimant urges the Tribunal to accept is that a dual national may sue either party in which he holds nationality, a proposition that would lead to manifestly absurd and inequitable results.

10. For example, should Mr. Feldman's Mexican grandson—who apparently will obtain U.S. citizenship by virtue of Mr. Feldman's U.S. citizenship—be able to reside all of his life in Mexico and establish a business in Mexico with Mexican capital, and still be entitled to sue Mexico under Chapter Eleven on the premise that he is an investor of another Party?

11. Or, should the California-born daughter of a Canadian mother and American father who holds dual citizenship be entitled to sue the United States under Chapter Eleven, if she was raised and educated entirely in California and invested in a business there that has no connection whatever to Canada?

12. Or, should a U.S. citizen who sought refuge in Canada and settled in Ontario to avoid compulsory military service during the Vietnam War be entitled to sue Canada in respect of an investment made in Ontario thirty years later, even if he applied for and obtained landed immigrant status, married a Canadian citizen, fathered Canadian children, and enjoyed publicly-funded health care, education and pension benefits as a permanent resident of Canada?

13. These and any number of other examples demonstrate the absurdity of the interpretation of "investor of a Party" that the Claimant urges the Tribunal to accept. The more rational and equitable result follows the interpretation propounded by the Respondent—that a national of a Party, whether a citizen or permanent resident, cannot be an "investor of another Party" under Chapter Eleven.

14. The Respondent accordingly submits that there is no policy reason why a citizen of a Party, upon acquiring the rights associated with permanent residency in another Party, should be entitled to initiate a Chapter Eleven claim against that Party in respect of investment made in the territory of that Party. The NAFTA establishes a line between investors who have standing under Chapter Eleven and those who do not. Once the line is crossed —by becoming a permanent resident or citizen of the Party in which the investment is made— an investor's ability right to invoke Section B of Chapter is lost.

---

2. A term borrowed from the Claimant. See Memorial, paragraph 102.

PART III: THE REMAINING PRELIMINARY QUESTIONS

A. Question (a): Failure to Submit a Claim for Denial of National Treatment

15. The Claimant contends that by stipulating in his Article 1119 notice of intent that Article 1102 (among others) was a provision of Chapter Eleven that had been breached, and by alleging in his notice of claim that has been the victim of "discrimination" (among other things), he has submitted to arbitration a point of claim that he may now pursue in this proceeding, notwithstanding that the claim of denial of national treatment now asserted is based on an alleged measure that he did not know of and had not occurred when he filed his notice of intent or when he submitted this claim to arbitration.

16. The Claimant relies on the Award on Jurisdiction in *Ethyl Corporation v. The Government of Canada* in support of his argument that having "cited Article 1102 as one basis for his claim in the Article 1119 Notice ... the Article 1102 claim was made at that time"[3] and that Article 48 of the Arbitration Rules entitles him to advance the claim of denial of national treatment he now asserts.

17. In *Ethyl*, Canada complained, *inter alia*, that the Claimant submitted its claim to arbitration after the measure complained of (the MMT Act) had been passed by the House of Commons and the Senate but 11 days before it received Royal Assent. Canada made the point that the alleged breach was a "proposed measure", not a measure within the meaning of Article 1101 (1), at the time the claim was submitted to arbitration and the arbitral tribunal accordingly lacked jurisdiction over the claim.

18. The arbitral tribunal noted that although Canada's argument was "not without effect", its complaint was, in essence, that the claimant had "jumped the gun" and having done so should be required to commence an entirely new arbitration. The tribunal went on to note that Royal Assent is "granted as a matter of course when the Government has requested it", that the MMT Act was a reality within 11 days of the submission of the claim, and thus the tribunal had been "presented with a claim based on a 'measure' which has been 'adopted or maintained' within the meaning of Article 1101"[4].

19. Canada also complained that the claimant had not complied with the procedural requirements of Chapter Eleven, which in include "a series of steps which must be taken before a claim is submitted to arbitration", including compliance with Articles 1116(1), 1120, 1119, and 1121[5]. Mexico supported Canada's position on this point, stating in pertinent part:

> Mexico is also of the view that arbitral tribunals established under Chapter Eleven must adhere to the requirements of Section B for the initiation of arbitration proceedings. By

---

3. Memorial, paragraph 20.
4. Ethyl, paragraphs 68, 69.
5. Ibid, paragraph 45.

> entering into the Agreement, the NAFTA Parties have given a general consent to submit to all arbitrations commenced against them. Having done so, this places a special duty upon tribunals to ensure that claimants comply with the necessary requirements set out in the Chapter. ... The language of Articles 1119 and 1120 is clear. The Agreement has to have allegedly been breached at the time that the Notice of Intent is filed and six months must have elapsed "since the events giving rise to the claim". Section B of Chapter Eleven is a significant remedy from the perspective of all three NAFTA Parties, and it is one which calls for the observance of such requirements by prospective claimants.[6]

20. The United States did not make a submission under Article 1128 in *Ethyl*.

21. The arbitral tribunal in *Ethyl* posed the question: "to what extent, if any, is Canada's consent to arbitration in Chapter 11 conditioned absolutely on the fulfillment of specified procedural requirements at a given time?[7]"

22. After dealing with Canada's submissions on a separate point (that the MMT Act was a measure affecting trade in goods, not investment) the tribunal considered the question of "whether the NAFTA Parties intended that any of these conditions must be fulfilled prior to or simultaneously with delivery of the Notice of Arbitration in order for the Tribunal's jurisdiction to attach"[8].

23. The tribunal did not answer this question directly. Instead it found that the procedural requirements had been fulfilled in effect, albeit belatedly, noting (*inter alia*) that consultations had been held previously, that six months had long since elapsed since the MMT Act had received Royal Assent, and that the claimant's waiver and consent had been delivered with the Statement of Claim rather than the Notice of Arbitration as would have been the better practice.

24. In the result the tribunal noted that "dismissal of the claim at this juncture would disserve, rather than serve, the object and purpose of the NAFTA" and held:

> In the specific circumstances of this case the Tribunal decides that neither Article 1119 nor Article 1120 should be interpreted to deprive this Tribunal of jurisdiction[9].

25. The tribunal ordered that the costs of the Government of Canada and of the Tribunal attributable to the jurisdictional proceedings relating to issues raised under Articles 1119, 1120, and 1121 be borne by the claimant.

26. As noted in the Counter-memorial, the view that procedural requirements of Section B are prerequisites to obtaining the disputing NAFTA Party's consent to arbitration is shared by all

---

6. Ibid, paragraph 48.
7. Ibid, paragraph 60.
8. Ibid, paragraph 74.
9. Ibid, paragraph 85.

three NAFTA Parties, as evidenced by their submissions to the arbitral tribunal in *Pope & Talbot, Inc. v. The Government of Canada*.[10]

B. Question (b): The Claimant's Request to Amend to Assert a New Claim of Denial of National Treatment

27. The Claimant contends that having submitted a point of claim under Article 1102 —by merely mentioning it in his notice of intent— he is entitled to advance an additional claim of denial of national treatment pursuant to Article 48 of the Arbitration Rules.

28. If the Claimant is correct, then it follows that any prospective claimant may deliver a notice of intent alleging that the disputing Party has breached all of its substantive obligations under Section A of Chapter Eleven and thereafter expect to invoke Article 48 as a means of pursuing any claim that later comes to mind, whether or not the measure subsequently complained of occurred prior to submission of the claim and whether or not the new claim bears any relationship to a claim properly identified in the notice of intent and submitted to arbitration in accordance with the procedures prescribed in Section B.

29. All of the NAFTA Parties have objected to the contention that the arbitration rules can take precedence over the procedures and other requirements of Section B. They relied on the language of Articles 1122 (1) and 1120 (2), respectively:

> Each Party consents to the submission of a claim to arbitration in accordance with the procedures set out in this Agreement[11].
>
> The applicable arbitration rules shall govern the arbitration except to the extent modified by this section[12].

30. The Respondent submits that it did not consent to arbitration of the claim of denial of national treatment the Claimant now seeks to assert by reason of his failure to comply with Articles 1119, 1120 and 1121 or satisfied the requirements of Article 1117 in respect of such claim.

31. The Respondent further submits that Article 48 of the Arbitration Rules is modified by the requirements of Articles 1119, 1120, and 1121 and can be of no avail to the Claimant, at least until he complies with those requirements, assuming he could satisfy Article 1117.

32. Arbitral tribunals in two previous Chapter Eleven proceedings have taken the view that the amendment provisions of the applicable arbitration rules (Article 20 of the UNCITRAL Arbitration Rules in *Ethyl*[13] and Article 48 of the ICSID (Additional Facility) Rules in

---

10. Counter-memorial, paragraphs 175-177.
11. Article 1122 (1).
12. Article 1120 (2).
13. *Ethyl*, supra, paragraphs 91, 94.

Metalclad)[14] are not modified by Articles 1119, 1120 and 1121. They have also postulated that the NAFTA Parties did not intend to limit the jurisdiction of Chapter Eleven tribunals in this way.

33. The Respondent submits, with respect, that both tribunals were wrong on both points. In fact, the three NAFTA Parties have advanced the position that the fulfillment of the requirements of Articles 1119, 1120 and 1121 is a mandatory pre-requisite to invoking their consent to arbitrate in a given case and must be complied with before new claims are admitted.

34. The fact that nothing in Section B expressly purports to modify the amendment provisions in the various arbitration rules is of no consequence. If the fulfillment of the procedural requirements of Section B is mandatory (as the NAFTA Parties say it is), the amendment provisions are inoperative until such time as the disputing investor has complied with the requirements of Section B.

35. This approach does not create hardship for a disputing investor. It would result only in modest delay in adding new claims —in order to give the 90 days' notice, and the lapse of six months from the date of implementation of the measure complained of, that the disputing Party is entitled to the benefit of under Articles 1119 and 1120.

36. In this case the Claimant has failed to properly identify the basis of his new claim of denial of national treatment, let alone comply with Articles 1119, 1120 and 1121. He testifies that he believes, through an unidentified source, that Mercados received IEPS rebates in 1999 and 2000 and that such payments were terminated when the *Secretaría de Hacienda y Crédito Público* (SHCP) found out as a result of counsel's requests for documents in this proceeding. Through counsel he also asserts the right to demand discovery documents to "find out" whether SHCP has given IEPS rebates to any other cigarette reseller since 1990.

37. Simply put, the Respondent has not been given proper notice of the issues and factual basis for the claim, the relief sought, the injury suffered by CEMSA as a result of the alleged violation or the approximate amount of damages claimed.

C. Question (c): The Three Year Limitation Period and Alleged Estoppel

38. The Claimant contends that the three year limitation period prescribed by Articles 1116 and 1117 "tolls" from the date that the investor delivers a notice of intent to submit a claim to arbitration pursuant to Article 1119. The Respondent's view is that, upon a proper interpretation of Articles 1116 and 1117 (and the other applicable provisions of Section B), an investor is required to submit its claim to arbitration within three years of the date that the investor first acquired knowledge, or should have acquired knowledge, of the alleged breach and that the investor (or an enterprise owned or controlled by the investor) has incurred loss or damage.

---

14. *Metalclad Corporation v. The United Mexican States*, ICSID Case No. ARB(AF)/97/1, Award, August 30, 2000, paragraph 67.

39. If the Claimant's position is correct, then it would be open for any prospective claimant to eliminate the running of the limitation period by delivering a notice of intent and simply sitting on it.

40. The Respondent submits that the time limitations and procedural requirements prescribed by Section B are not unfair or draconian as the Claimant suggests. On the plain language of the applicable provisions, a prospective claimant can ascertain that he must give notice under Article 1119 at least 90 days before submitting a claim to arbitration, that he must allow six months to elapse from the occurrence of the events giving rise to the Claim as required by Article 1120, and that he must submit the claim to arbitration within three years of being charged with knowledge of the alleged breach and resulting damage. In effect, it means that the investor must begin the process within two years and nine months of learning of the measure complained of.

41. The three year limitation presents no hardship to the Claimant. He gave notice of intent within three months of the primary measures complained of —the denial in December 1997 of IEPS rebates claimed for exports in October and November 1997 and the January 1998 amendment to the IEPS law— and thereafter sought a determination of the competent authorities pursuant to Article 2103 (6) as to which of his claims of expropriation could be submitted to arbitration.

42. Because he did not make a submission to the United States Department of Treasury until August 18, 1998, the determination of the competent authorities (which must be issued within six months) was not issued until February 18, 1999[15]. On April 30, 1998 he submitted his claim to arbitration by delivery the Notice of Arbitration to the Secretary General of the ISCID.

43. It is only because the Claimant now seeks to assert claims which pre-date the measures initially complained of, in some cases by many years, that the three year limitation presents a problem to him. The Claimant has testified that in June 1995 he obtained the agreement of SHCP officials to allow CEMSA to apply for and obtain IEPS rebates for cigarette exports and that CEMSA resumed that activity in May 1996[16], almost a year later.

D. Question (d): Relevance of Claims Pre-dating NAFTA's Entry into Force

44. The Memorial and Mr. Feldman's declaration in support thereof contend that SHCP "shut down" CEMSA's cigarette exporting business on three occasions:

a) first, in 1991, when SHCP "took administrative steps ... to deny rebates for exports for cigarette exports in November 1990 and to cut-off further exports by CEMSA";

---

15. Notice of Arbitration, p. 4.

16. First Feldman Declaration, paragraph 14.

b) second, between 1993 and 1995, when SHCP "stopped making IEPS rebates to CEMSA"; and

c) third, and finally, in late 1997 when SHCP "refused to pay the rebates requested for cigarette exports in October and early November 1997".

45. As noted in the Counter-memorial, the Claimant does not identify with precision what "measures" caused any of these alleged events, nor does he indicate how, if at all, such measures were a breach of any of the Respondent's obligations under Section A of Chapter Eleven. Instead, he now characterizes these alleged events as forming a pattern of conduct amounting to "creeping expropriation" which "culminated in the final extinction of CEMSA's cigarette export business in late 1997".

46. The Claimant's purpose is obvious —he seeks to avoid the determination of the competent authorities that the 1 January 1998 amendment to the IEPS law was "not an expropriation". That is the operative measure in this case. It expressly provided that IEPS rebates may only be claimed by the producer and first purchaser of cigarettes manufactured in Mexico, putting a certain end to the Claimant's alleged ability to claim IEPS rebates upon presentation of self-made invoices that purported to separate the amount of IEPS incorporated in the price of cigarettes purchased from secondary vendors.

47. The Respondent submitted in the Counter-memorial that, objectively characterized, the alleged events of 1991 to 1995 cannot be construed as a progressive series of hostile measures that culminated in the *de facto* expropriation of CEMSA (or its "cigarette export business") in late 1997 as the Claimant now contends.

48. The Respondent need only refer the Tribunal to the Claimant's own allegations that:

a) he obtained the agreement of senior SHCP officials in June 1995 to allow CEMSA to receive IEPS rebates upon exporting cigarettes,

b) pursuant to this alleged agreement CEMSA began exporting cigarettes and receiving IEPS rebates in May 1996, about a year later, and that

c) in continuance of this alleged agreement, CEMSA applied for and received payment of 83, 454,763 pesos in IEPS rebates for cigarettes exported from May 1996 to September 1997.

49. The Claimant has thus described a period of about two and a half years (June 1995 through September 1997) when, according to him, SHCP agreed that CEMSA's was entitled to receive IEPS rebates for cigarette exports. Accordingly, he cannot at the same time contend through counsel that:

> ...facts and circumstances dating back to 1990 demonstrate a sustained campaign by senior Mexican officials to drive CEMSA out of the cigarette export business by illegal and discriminatory manipulation of the IEPS tax law that culminated in the measures

taken by Respondent in 1997 to shut down CEMSA's cigarette export business for the third time[17].

50. The Respondent accordingly submits that alleged measures affecting the Claimant that pre-date NAFTA's entry into force (or that were implemented more than three years before this claim was submitted to arbitration) are not relevant to the claim or claims that are admissible in this proceeding.

51. The Respondent acknowledges that evidence as to the history of the implementation and administration of the IEPS law may be tangentially relevant to SHCP's decision to disallow CEMSA's rebate claims for cigarettes exported in October and November 1997 and to the 1 January 1998 amendment to the IEPS law. However, the Respondent submits that SHCP's alleged treatment of CEMSA prior to NAFTA's entry into force, whether positive or negative, is not relevant and requests for production of documents and witness statements should be circumscribed accordingly.

PART IV: THE POSSIBLE MERITS OF ADMISSIBLE CLAIMS

52. The Respondent has endeavored to answer questions (a) to (d) without contesting the Claimant's allegations of fact. The Respondent does not admit these allegations in connection with the claim on the merits. Rather, recognizing that the Tribunal is not in a position to make findings of fact in connection with questions (a) to (d), the Respondent has presumed the truth of the testimony given by Marvin Feldman in his two declarations for the purpose of making its submissions on those issues.

53. The submissions below discuss in a non-exhaustive manner the possible merits of admissible claims if this Tribunal determines that it has jurisdiction in this arbitration.

A. The Claimant's Allegations in Proper Perspective

54. In reality, the Claimant complains that taxation measures implemented by Mexico's taxation authorities have impaired CEMSA's ability to profitably engage in parallel marketing, euphemistically known as "gray marketing", of brand name cigarettes manufactured in Mexico.

55. In the context of this case, the Claimant seeks to engage in parallel marketing of "Marlboro" cigarettes, a brand owned by Philip Morris Corporation. Marlboro cigarettes are manufactured under license in Mexico by Cigatam who, like the licensed manufacturers and distributors of Philip Morris products in other countries, is contractually obliged not to produce cigarettes for export to countries where other licensed manufacturers and distributors have paid for territorial rights to use the Marlboro brand.

---

17. Memorial, paragraph 46.

56. In this case the Claimant, through CEMSA, has sought to take advantage of differences in the retail price of Marlboro cigarettes between Mexico and certain other countries, including the United States. Rebate of the IEPS enhances the profit margin that CEMSA can earn by engaging in such transactions.

57. In fact, CEMSA's website indicates that it continues in business today, offering for sale "transnational brands" of a wide variety of products including four brands of cigarettes, three brands of alcoholic beverages, and a host of other products ranging from diapers and toiletries to batteries and Volkswagen "Beetles". Marlboro cigarettes are given special attention:

> **Marlboro Cigarettes:**
>
> **We export only Mexican Made Marlboro cigarettes. 60 cartons to a Mastercase. Not 50 as in the USA.**
>
> **Samples are free.**
> **Send your FEDEX account mumber. (sic)**[18]

58. The Tribunal will note that the Claimant initially notified the Respondent of a claim for 13 million dollars for the alleged "value of CEMSA", a claim reiterated in the Notice of Arbitration which claimed 50 million dollars for (among other things) "the value of CEMSA as a going concern in December 1997". However, since receiving the Respondent's request for production of documents and information concerning CEMSA's trade in other goods, the Claimant has retreated, now speaking of the "destruction of CEMSA's cigarette exporting business".

59. Query whether this is true, given the fact that CEMSA continues to offer Marlboro and three other brands of cigarettes for sale on its website. Query further whether, even if CEMSA's ability to profitably engage in gray marketing of cigarettes has been substantially eliminated, there has been an expropriation of his enterprise CEMSA contrary to Article 1110. The Respondent will address this issue in further detail below.

B. The Respondent's Position on the Merits

60. If this proceeding is continued, the Respondent's Counter-memorial on the merits will answer any allegation that SHCP has implemented or administered the IEPS law in a manner calculated to "destroy CEMSA" at the behest of Cigatam, or to protect an "illegal monopoly" on the export of cigarettes, an allegation Mr. Feldman has made repeatedly in paid advertisements in the Wall Street Journal and Mexican newspapers, an allegation he reiterates in this proceeding, based only on his "information and belief".

61. Depending on the Tribunal's answers to the five preliminary questions and the nature of the Claimant's case as finally framed in his Memorial on the merits, the Respondent expects to adduce evidence and make legal submissions that will establish the following:

---

18. http://www.cemsamex.com.mx/. See Exhibit 1.

a) the IEPS has been implemented and administered according to the law and prevailing tax policy, not to obey the commands of Mr. Carlos Slim, Cigatam or anyone else;

b) the Claimant's contention that the 1993 *amparo* judgment thereafter entitled CEMSA to export cigarettes is wrong as a matter of fact and Mexican law;

c) the Claimant's contention that SHCP had a legal duty and the legal means to compel cigarette producers and subsequent purchasers to ensure that they separately stated and transferred the amount of IEPS paid on cigarettes that were ultimately purchased by CEMSA from "Sam's Club" is wrong as a matter of fact and Mexican law;

d) even if the Claimant could establish that SHCP did have the legal duty and means to ensure the every party in the chain of distribution issued invoices, its alleged failure to enforce the law in CEMSA's favor does not amount to a breach of Section A of Chapter Eleven; and

e) SHCP lawfully refused to IEPS pay rebates claimed by CEMSA for cigarettes it claimed to have exported in October and November 1997.

C. Possible Merits of Claims that Are Admissible in this Proceeding

62. The Respondent submits there are two claims of "expropriation" that are conceivably admissible in this proceeding:

a) SHCP's alleged refusal to implement a 1993 decision of the Mexican Supreme Court of Justice in favor of CEMSA concerning the rebate of certain excise taxes imposed on the sale of cigarettes; and

b) SHCP's refusal to provide rebates of excise taxes to CEMSA for cigarettes allegedly exported in October and November 1997.

63. The Respondent has addressed the possible merits of these claims in paragraphs 259 to 266 of the Counter-memorial.

64. There are additional conceptual problems with the claims of expropriation that the Respondent wishes to put on the record to avoid again being accused of raising a defense that is a "weak after-thought (sic)"[19].

65. As noted above, the Claimant has shifted his claim that CEMSA was expropriated to an allegation that CEMSA's cigarette exporting business was expropriated. This is because CEMSA has engaged, and apparently continues to engage, in the export of a broad variety of

---

19. Memorial, paragraph 111.

"transnational brands", including alcoholic beverages, diapers, toiletries, automobiles, auto parts, and cigarettes.

66. The Respondent will submit that CEMSA's "cigarette exporting business" is not an "investment of an investor" within the meaning of Article 1110 (1). CEMSA is the investment (if Mr. Feldman is an investor of another Party).

67. The Respondent will further submit that, consistent with the position of all three NAFTA Parties, a measure "tantamount to expropriation" must be equivalent, in all material respects, to an expropriation of an investment of an investor[20]. This requires a measure that has the effect of "taking" an investor's interest in its investment. A reduction in profitability is not enough[21].

68. This is consistent with the compensation prescribed by Article 1110 (2). It requires payment of the fair market value of the investment, not a diminution in value or profits lost as a result of the measure complained of.

69. The Respondent also expects the Claimant will encounter significant problems in establishing a plausible claim for compensation. Without being exhaustive, the Respondent notes that the cigarette exporting business that CEMSA claims to have lost was based on a totally insecure premise —the alleged ability to export "tax free" cigarettes without a distribution agreement with a cigarette producer or licensed distributor.

70. As events have shown, CEMSA's ability to carry on business in that manner —which only existed because of a deal Marvin Feldman says he made with SHCP officials— was eliminated by the January 1998 amendment to the IEPS law, a taxation measure that the Government of Mexico was lawfully entitled to implement and which the competent authorities have ruled was "not an expropriation".

71. No market value based on future profits or goodwill could therefore be ascribed to CEMSA's cigarette export business, let alone the 50 million dollars that the Claimant says he is entitled to be paid.

PART V: PRODUCTION OF DOCUMENTS AND WITNESS STATEMENTS

72. The disputing parties are at odds as to the proper scope of production of documents and witness information. This may have resulted in part from the fact that Claimant's counsel is immersed in the legal tradition of the United States, where broad-based discovery of documents and witnesses is an institutionalized procedure; whereas in Mexico, as in other civil law jurisdictions, production of documents and witnesses at the request of the opposing party is not enshrined in the legal process.

---

20. See *Pope & Talbot, Inc. v. The Government of Canada*, Interim Award, June 26, 2000, paragraphs 96-105.

21. Ibid.

73. The Claimant, notwithstanding an avowed intention to refrain from engaging in discovery "anything like Federal Rules of Civil Procedure"[22], has done exactly that—he has issued very broad, non-specific demands for discovery of documents which, taken has a whole, cover virtually all documents created since 1990 which relate, in any way, to the implementation and administration of the IEPS law and SHCP's dealings with CEMSA, and to any other entity which sought or obtained IEPS rebates on cigarettes during the same ten year period.

74. In its approach to this issue, the Respondent has endeavored to apply concepts recognized by leading commentators as being appropriate to international arbitral proceedings—particularly where the disputing parties come from different legal systems—and that are consistent with its prior experience in three Chapter Eleven arbitrations under the ICSID Arbitration (Additional Facility) Rules (the "Arbitration Rules").

75. The Respondent notes that, notwithstanding the Claimant's repeated references to his rights of "discovery", it is not a word that appears anywhere in Section B of the Chapter Eleven, the Arbitration Rules, or any procedural order issued by the Tribunal. Production of requested documents in international arbitration is a much narrower concept than "discovery". The two should not be confused.

76. The Respondent cited the observations of leading commentators in its submission to the Tribunal dated 14 July 2000 and will not repeat them here. In summary, it is expected that request for production of documents will be consist of a "limited and specific request" for documents that are:

a) described with sufficient particularity to enable the responding party to identify, locate and produce them;

b) relevant to matters properly in issue in the proceeding; and

c) necessary to the proper resolution of the dispute.

77. Accordingly, in its request for production of documents the Respondent endeavored to:

a) identify the requested documents by name or, failing that, by their legal effect and/or expected content;

b) identify the legal issue to which each request pertained; and

---

22. See page 52 of the record of the First Session of the Tribunal. Counsel for the Claimant stated:

> Now, I want to make it clear from the outset that we are not proposing common-law style discovery. We are not proposing to use anything like the Federal Rules of Procedure in an arbitration. In our view, that is completely inappropriate. We are not proposing a fishing expedition, we are not looking for information at large, which may, in the words of the Federal Rules, be relevant to the proceeding.

c) indicate the evidentiary purpose of the documents requested.

78. By comparison, the Claimant's requests for documents—from 1991 to date—make repeated use of the phrase "all documents relating to ...". These are not limited and specific requests for documents or requests for specific documents. Moreover, when the Respondent asked the Claimant to advise as to the legal relevance and necessity of its requests, the Claimant's response was confined for the most part to bare assertions such as "measures tantamount to expropriation under NAFTA Article 1110". There was virtually no effort to describe the legal issue or evidentiary purpose of such documents.

79. The Respondent was similarly concerned that the Claimant was misusing the procedural order to force the Respondent to present all of its evidence first—before knowing the case that it is expected to answer—contrary to the order of presentation contemplated in the Arbitration Rules and the usual expectation that the Claimant bears the onus and burden of proof, and basic principles of fairness that underlie the proper conduct of the proper conduct of the arbitration and upon which the Tribunal's jurisdiction rests.

80. Having expected to receive up to three requests for witness statements as proposed by the Claimant in his letter to the Tribunal dated 22 March 2000, the Respondent received requests for statements from twenty-two witnesses, including President Zedillo, former President Salinas, four Secretaries of State, and the Ambassador to the United Kingdom.

81. The majority of the witness statement requests were not requests for "written statements on specific points by witnesses ... with an indication of their relevance". Rather, they were broadly worded interrogatories that amounted, in sum, to pre-pleading deposition of witnesses, a procedure not authorized by the Arbitration Rules and one which is inappropriate for international arbitration.

A. Directions Concerning Production of Documents and Witness Statements

82. In the words of a leading text on ICC arbitration, "arbitration is inherently a consensual process"[23]. The Respondent respectfully submits that the Tribunal should be mindful of differing legal customs and sensitivities in order preserve the integrity and efficacy of the arbitral process.

83. The Respondent has attempted to communicate with the Claimant, in good faith, with a view to achieving agreement on what has proven to be a highly disputed and time-consuming matter—the proper form and scope of requests for production of documents and witness information. The Respondent regrets this has led the Claimant to accuse it of "refusing to comply" with the Tribunal's procedural orders, engaging in "tactics designed to delay the proceedings" and otherwise acting in "bad faith".

---

23. Craig, Park and Paulsson, *International Commercial Arbitration*, Section 26.01, p. 406.

84. Mexico has said that it believes the disputing parties should be able resolve issues relating to document production without having to resort to the Tribunal for directions. However, the Mexico has now come to the view that, in the current circumstances of this case, the Tribunal stipulate the general rules to be applied, in addition to answering the questions that will assist the parties in determining which claims are admissible in the proceeding.

85. The Respondent submits that the general principles described above—that requested documents must be sufficiently described and be demonstrably relevant and necessary to the proper conduct of the proceeding—should adopted by the Tribunal in this case. They are consistent with the Arbitration Rules and international arbitration practice.

B. Request for Confidentiality Order

86. The Claimant has recently resorted to publication in the news media of matters that are *sub judice* in this proceeding.

87. In an advertisement published in *Reforma* on 28 August 2000, he purported to inform Canadian and United States "investors" residing in Mexico that the Government of Mexico seeks to abrogate their rights under the NAFTA[24].

88. Quite apart from the inaccuracy of Mr. Feldman's accusation, his actions are inconsistent with the general expectation of confidentiality in arbitral proceedings. In the Respondent's view, they indicate an intention to abuse the arbitral process.

89. The Respondent has in the past chosen not to respond to Mr. Feldman's paid notices and advertisements, notwithstanding their objectionable content. However, his misuse of this arbitral proceeding to stage a further publicity campaign calculated to embarrass the Mexican government is unacceptable.

90. The Respondent objects to breaches of the applicable arbitration rules and the general expectation of confidentiality that apply to both parties, particularly those which appear calculated to subvert the arbitral process.

91. The Respondent accordingly requests that the Tribunal direct, in the exercise of its jurisdiction to control the proceeding and preserve the integrity of the arbitral process, that neither party shall publish any matter that is before this Tribunal without the prior agreement of the other party or the prior approval of the Tribunal.

92. The Respondent further requests the Tribunal to direct that all documents, witness testimony and other evidence produced or disclosed by either party shall be treated in confidence and shall not be published or disclosed to any third party (except the other NAFTA Parties pursuant to Articles 1127 and 1129) unless the parties agree to such disclosure or the Tribunal so directs.

---

24. Exhibit 2.

93. The Respondent further requests Tribunal to direct that a breach of its confidentiality directions by either party will result in the imposition of such sanctions that the Tribunal sees fit in the circumstances, including, but not limited to, suspension of the proceedings for period of time to be determined by the Tribunal.

PART VI: ADDITIONAL OBSERVATIONS ON RELIEF REQUESTED

1. Answers to the Five Questions Posed by the Tribunal

94. The Respondent respectfully reiterates its the request for answers to the preliminary questions as stated in paragraph 267 of the Counter-memorial.

95. The Respondent requests the Tribunal to dismiss the proceeding on the ground that the Claimant, as a national of Mexico, is not entitled to submit a claim as an "investor of another Party".

96. Alternatively, the Respondent submits the Tribunal should to dismiss the claim on basis of the evidence before it which, in the Respondent's submission, establishes indicates that the Claimant's dominant and effective nationality, for the purposes of Chapter Eleven of the NAFTA, is that of Mexico.

97. Alternatively, the Respondent submits that if the Tribunal determines that it is unable to determine the Claimant's dominant and effective nationality on the evidence before it, then the Tribunal should hold a hearing on that question. In such case the Claimant and any other witness proffered by either party should be required to attend for cross-examination.

98. The Respondent submits that joining the dominant and effective nationality issue to the merits would put both parties to the inconvenience and expense of dealing with other complex factual and legal questions, including expert opinion evidence on the question of damages, all of which would be wasted if the Respondent ultimately succeeds on the standing issue. This issue is distinct and separate from all other issues that arise in this proceeding and should be dealt with separately.

99. The Respondent will provide any further submissions the Tribunal may require to address the five preliminary questions or any other matter raised by the parties, including oral submissions if so directed.

2. Observations as to Claims that are Properly Admissible

100. The Respondent respectfully submits that it would assist the parties in the orderly and efficient conduct of this proceeding if the Tribunal would express its views, on a without prejudice basis, as to the claims that are properly admissible in this proceeding.

3. Directions Concerning Requests for Production of Documents and Witness Statements

101. The Respondent respectfully submits that it would assist the parties in the orderly and efficient conduct of this proceeding if the Tribunal would give directions as to:

a) the proper form and content of requests for production of documents, encompassing the principles described above; and

b) the requirement for confidentiality of documents and witness statements produced by the parties, in terms similar to those proposed above.

102. The Respondent also notes that, depending on the Tribunal's decision on the five preliminary questions, it will assist the parties if the Tribunal takes an active role in reviewing and approving their requests for production of documents and witness information. The Respondent will make further submissions on this point after the Tribunal's award has been issued, if such assistance is considered necessary.

All of which is respectfully submitted:

_____

Stephan E. Becker

SHAW PITTMAN
2300 N Street, NW
Washington, DC 20037

Counsel for the United Mexican States