

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

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Commerce Group Corp. and)	
San Sebastian Gold Mines, Inc.)	
)	
Claimants,)	
)	ICSID Case No. ARB/09/17
v.)	(Annulment Proceeding)
)	
Republic of El Salvador)	
)	
Respondent.)	
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EL SALVADOR'S APPLICATION FOR SECURITY FOR COSTS

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I. INTRODUCTION

1. This application for security for costs is based on circumstances that, to our knowledge, have not been present in any other application for security for costs submitted under the ICSID Convention. Without making any reference to the merit (or lack of merit) of Claimants' application for annulment, this application for security for costs is based solely on Claimants' irresponsible decision to start an annulment proceeding for which they had no funds. Claimants demonstrated their financial irresponsibility when they defaulted on their very first advance payment to ICSID, and only managed to make that payment when faced with the discontinuance of the proceeding, after a seven-month suspension and ten months after their original default. Claimants then admitted that they cannot meet their obligation under ICSID Administrative and Financial Regulation 14(3)(e) to pay for this annulment proceeding unless they secure third-party financing.

2. Claimants made the first advance payment to ICSID only with great difficulty, and apparently still have not secured third-party financing. Claimants have thus placed El Salvador, the Centre, and the Committee in the position of having to expend significant resources in a proceeding that will most likely be abandoned for lack of funding. Even if Claimants do find a third-party financier, they may have to abandon the proceeding if the financier decides to pull out partway through after mounting legal fees and expenses.

3. Under these circumstances, Claimants must guarantee that not only El Salvador, but the Centre and the Committee as well, are reimbursed for their expenses if Claimants do not follow through. The risk for all involved is evidenced by the circumstances created by Claimants' actions thus far in these proceedings. According to the information provided by the Centre on

August 2, 2012, by the time Claimants made their first payment on the final day of the final extension, the Centre and the Committee had already accumulated unreimbursed fees and expenses in an amount exceeding \$71,000. The unreimbursed expenses for all involved will be significantly greater if Claimants ultimately fail to respond to the Centre's next call for funds. El Salvador submits that these insolvent Claimants should not be able to force the State, the Centre, and the members of this Committee to invest time and resources into a proceeding under these circumstances unless there is a guarantee that Claimants will not abandon the proceeding for lack of payment and fail to comply with an award of costs.

4. Therefore, El Salvador requests that the *ad hoc* Committee exercise its inherent powers to protect the integrity of this proceeding, to require Claimants to provide security for costs as a condition to continue with this annulment proceeding. This application is not a request for provisional measures intended to safeguard a particular right of a party. This request is made to safeguard the integrity of the proceeding because Claimants are admittedly unable to fund it to its conclusion.

II. SECURITY FOR COSTS IS NECESSARY

A. El Salvador is not responsible for Claimants' insolvency

5. Claimants' own documents demonstrate that their troubled financial situation existed long before their dispute with El Salvador, which according to Claimants' allegations began in 2006. Claimants ceased their activity in El Salvador in 1999, not because of anything the Government

did or failed to do, but because "the price of gold suffered a severe decline."¹ Commerce Group Corp. admits in its annual reports that it "has not had any revenues since April 1, 2000."²

Claimants have made no claim that the Government is responsible for their cessation of activities in 1999 or their lack revenue beginning in 2000.

6. After 1999, despite obtaining new permits and licenses from the Government, Claimants never managed to re-initiate their gold mining and processing activities. In 2002, Claimants explained that they had no revenue because of the "need to rehabilitate, overhaul and expand" the processing facilities, and stated that they hoped to resume their activities "when adequate funding becomes available."³ They never obtained the funding they needed to reinitiate activities after 1999 and they therefore failed to fulfill their investment commitments to El Salvador.

7. In fact, two years ago, Commerce Group Corp.'s 2010 Annual Report stated that the company had more than \$33 million in debt, including decades of accrued salaries, rent, legal fees, and deferred Directors' fees.⁴ Claimants' decades-old utter lack of financial resources—for which El Salvador bears no responsibility—has not changed since this report was filed. In 2011, Claimants failed to file an Annual Report and notified the SEC that the audit reports they filed in 2010 and prior years were "no longer effective" because their auditors' registration had been permanently revoked by the relevant oversight board.⁵ On June 29, 2011, less than two weeks before filing their application for annulment, Claimants explained that their Annual Report

¹ Commerce Group Corp., Annual Report (Form 10-K), at 41 (July 15, 2010). This document was submitted with El Salvador's Preliminary Objection and, for ease of reference, is included with the exhibits to this application as **Exhibit R-1**.

² Commerce Group Corp., Annual Report (Form 10-K), at 94 (July 15, 2010).

³ Commerce Group Corp., Annual Report (Form 10-K), at 45-46, 66 (May 28, 2002). This document was submitted with El Salvador's Reply (Preliminary Objection) and, for ease of reference, is included with this application as **Exhibit R-2**.

⁴ Commerce Group Corp., Annual Report (Form 10-K), at 31, 36, 63-65 (July 15, 2010) (R-1).

⁵ Commerce Group Corp., Current Report (Form 8-K), at 2 (July 14, 2011) (**Exhibit R-3**).

would be late and that they expected that their reported net loss for 2011 would be "significantly higher" than the previous fiscal year.⁶ It appears that Claimants have not filed their Annual Report following this notification. Clearly, El Salvador cannot be blamed for the fact that Claimants took nearly a year to come up with \$150,000 to meet their obligation to make the initial advance payment for these proceedings or for the fact that they have no funds with which to make future payments.

B. Claimants initiated an arbitration they could not fund

8. It is now clear that Claimants also started their original CAFTA arbitration against El Salvador in 2009 without having first secured adequate financing. In light of their statements in filings with the Government of the United States cited above that they have been accumulating heavy debt with no revenues since 2000, and the failure of their attempts to obtain funding since at least 2002, it is indisputable that Claimants were well aware of their decades-old financial problems when they initiated arbitration against El Salvador. Claimants' financial irresponsibility did not become evident during the arbitration only because El Salvador brought its Preliminary Objection that ended the arbitration at the earliest possible time, limiting unnecessary waste of expense to the parties. Even though the arbitration was terminated quickly, Claimants imposed significant costs on El Salvador by submitting an inaccurate factual account, making unsubstantiated arguments, and changing their positions.⁷

⁶ Commerce Group Corp., Form 12b-25 (Notification of Late Filing), at Part IV(3) (June 29, 2011) (**Exhibit R-4**).

⁷ As just one example, Claimants at first based their main defense to the Preliminary Objection on the argument that, in spite of its title, the waiver requirement was not a condition to consent. (Claimants' Response to Preliminary Objection, para. 32.) El Salvador had to spend considerable time and resources to respond to this argument, which was so frivolous that Claimants abandoned it in their Rejoinder. (Claimants' Rejoinder to Preliminary Objection, para. 5.) Unfortunately, it was easier, and significantly less costly, for Claimants to make inaccurate factual statements and unsubstantiated allegations without checking the facts, and then backtrack, than it was for El Salvador to research and respond to each frivolous argument put forward.

9. Considering the high cost to El Salvador of Claimants' irresponsible actions thus far, El Salvador is justifiably concerned that Claimants are now trying to string along an annulment proceeding that they admittedly cannot fund.

C. Claimants initiated an annulment proceeding they could not fund

10. One year ago, on August 17, 2011, ICSID first requested that Claimants make the initial advance payment of \$150,000 for the annulment proceeding within 30 days.⁸ Claimants failed to respond and did not make the necessary payment. After Claimants defaulted, ICSID sent a second letter on October 24, 2011, asking either party to pay the outstanding \$150,000.⁹

11. Claimants responded on November 17, 2011, advising that they were "unable to pay the requested advance at this time" and that they had been trying, unsuccessfully, to "muster their resources and move forward" ever since filing the application for annulment.¹⁰ El Salvador also responded, declining to make the advance payment that only Claimants, as applicants for annulment, were obligated to make and noting its concerns about keeping a proceeding alive when Claimants would likely have to abandon it when the next advance would be requested.¹¹

12. On December 19, 2011, the Centre, pursuant to the Rules, notified the parties of the suspension of the proceedings due to Claimants' failure to pay the initial advance.¹² Five months later, ICSID notified the parties that the Secretary-General would move to discontinue the proceedings if payment was not received by June 19, 2012.¹³

⁸ Letter from ICSID to the Parties, Aug. 17, 2011 (**Exhibit R-5**).

⁹ Letter from ICSID to the Parties, Oct. 24, 2011 (**Exhibit R-6**).

¹⁰ Letter from Claimants to *ad hoc* Committee, Nov. 17, 2011, at 1-2 (**Exhibit R-7**).

¹¹ Letter from El Salvador to *ad hoc* Committee, Dec. 15, 2011 (**Exhibit R-8**).

¹² Letter from ICSID to the Parties, Dec. 19, 2011 (**Exhibit R-9**).

¹³ Letter from ICSID to the Parties, May 22, 2012 (**Exhibit R-10**).

13. Claimants responded to this fourth request for the initial advance payment on the eve of the deadline, explaining that they were unable to make the payment and requesting more time to "secur[e] financing from third-parties for the continuation of these proceedings."¹⁴ They ultimately received an extra month and, on the last possible date, wired two separate payments totaling \$150,000 to the Centre to keep the proceeding alive.¹⁵ Claimants have thus bought themselves some time to try to convince a third-party to finance their endeavor. But they have done so by placing El Salvador in the untenable position of having to expend very significant resources to prepare its counter-memorial and otherwise defend itself in these proceedings while they continue to seek financing, with the substantial risk that when the Centre issues the next call for funds, Claimants will be unable to pay and the proceeding will be terminated.

14. In fact, there is every reason to doubt that Claimants will be able to secure the financing they need and, therefore, every reason to believe that they will have to abandon their application for annulment. In their June 18, 2012 letter, Claimants explained that they had been "diligently working on securing financing from various third parties" for the past six months, with daily contacts with potential lenders, and had thus far been refused.¹⁶ Although they indicated that another potential financier was reviewing the file at the time of their letter, there is no reason to believe that financier will reach a different conclusion than the others who had already reviewed the file. It is perhaps not surprising that third-party financiers hesitate to fund annulment proceedings because applications for annulment are less likely to be successful than arbitration

¹⁴ Letter from Claimants to Secretary to the *ad hoc* Committee, June 18, 2012, at 1 (**Exhibit R-11**).

¹⁵ Letter from ICSID to the Parties, July 23, 2012 (**Exhibit R-12**).

¹⁶ Letter from Claimants to Secretary to the *ad hoc* Committee, June 18, 2012, at 1 (R-11).

claims.¹⁷ Potential financiers, weighing their chances for financial gain, have little incentive to fund an annulment proceeding.

D. Claimants should be responsible for all costs if they abandon this proceeding

15. If the annulment proceeding is abandoned, El Salvador should be entitled to reimbursement of its costs. This is the fair result, correctly recognized by *ad hoc* committees and arbitral tribunals. When RSM Production Corporation abandoned its annulment proceeding against Grenada shortly before the scheduled hearing, the committee relied, *inter alia*, on its inherent power to take measures to protect the integrity of the proceedings and ordered that the applicant pay the respondent's costs.¹⁸ The committee favorably cited ICSID tribunal decisions holding claimants responsible to pay the costs for abandoning proceedings. As cited by the *RSM ad hoc* committee, an ICSID tribunal discontinuing an arbitration against Costa Rica because of the claimants' inability to pursue their claim and pay the advance requested by ICSID awarded costs to the State, noting that if the claimants had adequately considered "the consequences of their actions" in the arbitration, they could have saved much of the respondent's and the Centre's costs, as well as the tribunal members' time.¹⁹ The tribunal in that case sought to spare the respondent State the consequence of the claimants' irresponsible actions:

[C]onsidering Claimants' insistence o[n] continuing this arbitration at a time and circumstance when they could have averted such procedural expenditure, Claimants cannot expect Respondent to carry the burden of the costs of defending claims that Claimants decided to abandon. Accordingly, equity and fairness mandate that

¹⁷ See The ICSID Caseload – Statistics (Issue 2012-2) at 13, 15 (**Exhibit R-13**).

¹⁸ *RSM Production Corporation v. Grenada* (Annulment Proceeding), ICSID Case No. ARB/05/14, Order of the Committee Discontinuing the Proceeding and Decision on Costs, Apr. 28, 2011 (**Authority RL-1**).

¹⁹ *Quadrant Pacific Growth Fund LP and Canasco Holdings Inc. v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/08/1, Order of the Tribunal Taking Note of the Discontinuance of the Proceeding and Allocation of Costs, Oct. 27, 2010, para. 70 (**Authority RL-2**).

Claimants should bear the expenses and costs incurred by the Respondent in this arbitration.²⁰

16. Here, Claimants have insisted on pursuing an annulment application which they admittedly do not have the funds to pursue and will have to abandon if they cannot convince a third party to provide financing. They have done this even though other potential financiers have already reviewed the case and refused to finance it.

17. Claimants' actions have had serious consequences beyond leaving the Committee and the Centre with unpaid fees and expenses for several months. Claimants' failure to pay has already delayed this proceeding for more than seven months, sustaining a "pending" case against El Salvador instead of the final Award in El Salvador's favor. The pending proceeding and publicity negatively impact El Salvador's reputation for international investment.

18. El Salvador recalls that Claimants also let the underlying arbitration remain idle until ICSID notified the parties of its intention to terminate the arbitration after six months of inactivity in accordance with ICSID Arbitration Rule 45.²¹ Only when faced with ICSID's termination of the arbitration, and after the domestic judicial proceedings in El Salvador were completed, did Claimants respond and request constitution of the tribunal, having kept the State in limbo while figuring out how they would proceed.

19. Under these circumstances, and in light of the jurisprudence cited above, should this proceeding be terminated because of Claimants' failure to meet their obligation to provide funds,

²⁰ *Quadrant Pacific v. Costa Rica*, Order of the Tribunal Taking Note of the Discontinuance of the Proceeding and Allocation of Costs, para. 71 (RL-2). See also *Piero Foresti, Laura de Carli and others v. Republic of South Africa*, ICSID Case No. ARB(AF)/07/1, Award, Aug. 4, 2010, para. 132 (**Authority RL-3**) (noting that "the Claimants pressed ahead with the arbitration at a time and in circumstances where it was in a position to avert the need for some part of the Parties' expenditure", and commenting that claimants cannot expect respondent States to bear the costs of defending abandoned claims).

²¹ El Salvador's Reply (Preliminary Objection), paras. 129-130.

it is evident that Claimants should be responsible for all costs they force upon El Salvador, the Centre, and the Committee.

E. Without security for costs, Claimants could abandon this annulment proceeding and ignore an order for costs

20. Claimants have repeatedly ignored the consequences of their actions for El Salvador. Unless Claimants are required to provide security for costs, the Centre, the Committee, and El Salvador will unfairly bear the risk of this proceeding being abandoned. Having barely managed to keep this proceeding going, after a suspension of seven months, Claimants should now guarantee that they will not abandon the proceeding when the next advance is due and leave the Centre, the Committee, and El Salvador with unreimbursed expenses.

21. As indicated above, El Salvador's concerns about Claimants' financial record and their penchant for initiating proceedings they cannot fund are fully justified. The fact that insolvent Claimants are struggling to find third-party financing for this proceeding only heightens the risks for El Salvador.

22. Security for costs is especially warranted under these circumstances because a third-party financier, being an undisclosed non-party, could influence the proceedings. If Claimants secure third-party financing, the financier would likely reserve its right to discontinue financing at its discretion. If financing is withdrawn, Claimants would be forced to abandon the proceeding partway through. In that case, El Salvador would be entitled to have its costs reimbursed, but Claimants would inevitably be without funds to pay such costs. El Salvador will only be able to recover the costs Claimants intend to impose on the State if security for costs is provided.

23. It should be noted that any third-party financier would certainly enter into an agreement with the expectation of obtaining a return if Claimants eventually were to win an award against El Salvador, but the financier would not be liable to pay any costs that could be ordered against Claimants. Thus, the risks imposed on El Salvador by Claimants' pursuit of the annulment proceeding despite their admitted lack of financial capacity are only increased by the prospect of third-party financing because such financing would enable Claimants' to impose substantial burdens on El Salvador, with no prospect of collecting an award of costs from Claimants or the entity that provided the financing for Claimants' actions against El Salvador. In fact, the speculation for financial gain with no corresponding risk to pay costs has been described as "arbitral hit and run," and recognized "by arbitrators and commentators alike as particularly compelling grounds for security for costs."²²

24. Without security for costs, these insolvent Claimants will thus be in a position to benefit from third-party financing while they unfairly burden El Salvador and risk undermining the international arbitration system by frustrating a costs award.²³ Security for costs is thus required in order to preserve any future award for costs the Committee may choose to make and to protect the integrity of the international arbitration process. El Salvador is no stranger to the empty

²² J.E. Kalicki, *Security for Costs in International Arbitration*, TDM, Vol. 3, issue 5 (2006), www.transnational-dispute-management.com (**Authority RL-4**).

²³ See Noah Rubins, *In God We Trust, All Others Pay Cash: Security for Costs in International Commercial Arbitration*, 11 Am. Rev. Int'l Arb. 307, 359 (2000) (**Authority RL-5**) ("When claimants are defeated in arbitration and default with impunity on costs payments, international businesspeople are deprived of the assurance of even that institution's effectiveness. The risks of doing business across borders rise, the cost of capital for the initiation of international ventures rises, and global expansion is checked to some degree.").

relief of being awarded costs against an insolvent claimant that did not honor its commitment to comply with the award.²⁴

III. THIS *AD HOC* COMMITTEE HAS THE POWER TO ORDER SECURITY FOR COSTS

25. It is beyond contention that this Committee, being indisputably an international tribunal, has inherent powers to issue orders in circumstances not provided for in the express terms of the ICSID Convention and Arbitration Rules.²⁵ It is also beyond contention that such powers include the power to protect the integrity of its own proceedings and sanction breaches of the parties' obligation to arbitrate in good faith,²⁶ including by granting a request for security for costs where the applicants initiated a proceeding that they admittedly cannot fund.²⁷

²⁴ In *Inceysa Vallisoletana v. El Salvador*, El Salvador was awarded partial costs by the tribunal, but the insolvent claimant never reimbursed El Salvador, and it would have been a waste of more money to sue a claimant that did not have any liquid assets. See *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, ICSID Case No. ARB/03/26, Award, Aug. 2, 2006 (**Authority RL-6**).

²⁵ *RSM Production Corporation v. Grenada*, ICSID Case No. ARB/05/14 (Annulment Proceeding), Decision on RSM Production Corporation's Application for a Preliminary Ruling, Dec. 7, 2009, para. 20 (**Authority RL-7**).

²⁶ *Libananco Holdings Co. Limited v. Republic of Turkey*, ICSID Case No. ARB/06/8, Decision on Preliminary Issues, June 23, 2008, para. 78 (**Authority RL-8**) ("parties have an obligation to arbitrate fairly and in good faith and . . . an arbitral tribunal has the inherent jurisdiction to ensure that this obligation is complied with; this principle applies in all arbitration, including investment arbitration, and to all parties, including States."). See also *Hrvatska Elektroprivreda d.d. v. Republic of Slovenia*, ICSID Case No. ARB/05/24, Decision on the Participation of Counsel, May 6, 2008, para. 33 (**Authority RL-9**) ("as a judicial formation governed by public international law, the Tribunal has an inherent power to take measures to preserve the integrity of its proceedings"); *EDF (Services) Limited v. Romania*, ICSID Case No. ARB/05/13, Procedural Order No. 2, May 30, 2008, para. 46 (**Authority RL-10**) ("It is part of the inherent procedural powers of an arbitral tribunal, be it acting within the framework of an international commercial arbitration or of an investment treaty arbitration under the ICSID Convention, to ensure that the proper functioning of the dispute settlement process is safeguarded.").

²⁷ El Salvador is not requesting security for costs as a provisional measure under Article 47 of the ICSID Convention. Accordingly, the Committee need not decide whether it has the power to recommend provisional measures regardless of the fact that Article 52(4) of the ICSID Convention does not refer to Article 47, or whether the general reference in Article 44 of the ICSID Convention to the Arbitration Rules, as read together with Rules 39 and 53 of the Arbitration Rules, provides the Committee with such competence. See *Libananco Holdings Co. Limited v. Republic of Turkey*, ICSID Case No. ARB/06/8 (Annulment Proceeding), Decision on Applicant's Request for Provisional Measures, May 7, 2012, para. 15 (**Authority RL-11**). El Salvador's application for security for costs, based on Claimants' inability to fund the proceeding they initiated, is designed to protect the integrity of the proceeding, not just the rights of one party, and thus it is not a request for provisional measures, formally or otherwise.

26. The Committee's inherent power to preserve the integrity of its own process is confirmed by Article 44 of the ICSID Convention, which applies *mutatis mutandis* to annulment proceedings according to Article 52(4), and explicitly authorizes the annulment committee to decide any procedural questions that arise that are not covered by the Convention or other applicable rules. According to the ICSID tribunal in *Abaclat and others v. Argentina*, Article 44 is a "mere expression of the inherent power of any tribunal to resolve procedural questions in the event of lacunae."²⁸ Other tribunals have noted that their inherent power to take measures to preserve the integrity of proceedings "finds a textual foothold in Article 44 of the Convention."²⁹

27. As the committee in *RSM v. Grenada* explained, the inherent powers of an *ad hoc* committee must be exercised where such powers are "necessary to ensure the performance of functions that have been expressly conferred."³⁰ The committee's primary function is to determine the applicant's application for annulment. Where, as here, the orderly resolution of the application for annulment and compliance with any future orders of the Committee are in doubt, the Committee can take reasonable steps to protect the proceeding by filling the "gaps" in its mandate,³¹ in the interests of fairness and the orderly administration of justice.³²

²⁸ *Abaclat and others v. Argentine Republic*, ICSID Case No. ARB/07/5, Decision on Jurisdiction and Admissibility, Aug. 4, 2011, para. 521 (**Authority RL-12**).

²⁹ *Hrvatska Elektroprivreda d.d. v. Republic of Slovenia*, para. 33 (RL-9).

³⁰ *RSM Production Corporation v. Grenada* (Annulment Proceeding), Decision on RSM Production Corporation's Application for a Preliminary Ruling, para. 20 (RL-7).

³¹ The *Abaclat* tribunal explained that, based on its inherent powers and Article 44, it could deal with "specific problems arising in the proceedings at hand" and found that it "ought to fill gaps left where the application of existing rules are not adapted to the specific dispute submitted." *Abaclat and others v. Argentine Republic*, paras. 523, 525 (RL-12).

³² *Waguieh Elie George Siag and Clorinda Vecchi v. Arab Republic of Egypt*, ICSID Case No. ARB/05/15, Award, June 1, 2009, para. 365 (**Authority RL-13**) ("The Tribunal has an overriding duty to preserve the integrity of the proceedings and ensure fairness to both parties.").

28. For example, neither the Convention nor the Arbitration Rules expressly mention the posting of security in connection with a stay of enforcement under Article 52(2).³³ Yet despite the lack of an express provision in the Convention, *ad hoc* committees have still proceeded to order the posting of security. And they have done so on several occasions.³⁴ Writing in 2008, the *Enron* annulment committee noted that there existed a "*jurisprudence constante* to the effect that a stay [of enforcement] may be made conditional upon the provision of security."³⁵ Thus, the requirement to post security as a condition of a stay of enforcement is implicitly permitted, but not required, by the Convention and the Arbitration Rules.³⁶ Quite simply, it is a matter within the inherent powers of *ad hoc* committees.³⁷

29. Claimants have the obligation to initiate and orderly pursue their application in good faith. Claimants have already frustrated the dispute resolution process by delaying the proceeding for more than seven months while they sought funding. Now they are asking El Salvador, the Centre, and the Committee to assume the further risk of expending time and resources in this proceeding without knowing whether or not Claimants will obtain third-party financing, without which they will eventually have to abandon the proceeding. Even if

³³ Christoph H. Schreuer et. al., *The ICSID Convention: A Commentary* 1076 (2d. ed., 2009) (**Authority RL-14**).

³⁴ See, e.g., *Amco Asia Corporation and others v. Republic of Indonesia*, ICSID Case No. ARB/81/1 (Annulment Proceeding) Decision, May 17, 1985 ("Amco I") (unpublished); *AMCO v. Indonesia*, ICSID Case No. ARB/81/1, Resubmitted Case: Interim Order No. 1 of the *ad hoc* Committee concerning the Stay of Enforcement of the Award, Mar. 2, 1991, 9 ICSID Rep. 59 (2006) ("Amco II") (**Authority RL-15**); *Wena Hotels Limited v. Arab Republic of Egypt*, ICSID Case No. ARB/98/4 (Annulment Proceeding), Procedural Order No. 1, Apr. 5, 2001 (**Authority RL-16**); *CDC Group plc v. Republic of the Seychelles*, ICSID Case No. ARB/02/14 (Annulment Proceeding), Decision on Whether or Not to Continue Stay and Order, July 14, 2004 (**Authority RL-17**); *Sempra Energy International v. Argentine Republic*, ICSID Case No. ARB/02/16 (Annulment Proceeding), Decision on the Argentine Republic's Request for a Continued Stay of Enforcement of the Award, Mar. 5, 2009 (**Authority RL-18**).

³⁵ *Enron Corp. Ponderosa Asset, L.P. v. Argentine Republic*, ICSID Case No. ARB/01/3 (Annulment Proceeding), Decision on the Argentine Republic's Request for a Continued Stay of Enforcement of the Award, Oct. 7, 2008, para. 33 (**Authority RL-19**) (emphasis in original).

³⁶ Paul D. Friedland, *Stay of Enforcement of the Arbitral Award Pending ICSID Annulment Proceedings*, in *Annulment of ICSID Awards* 177, 177 (Emmanuel Gaillard & Yves Banifatemi eds., 2004) (**Authority RL-20**).

³⁷ *Id.*

Claimants do secure financing, any potential third-party financier would only be involved as long as this serves its own financial gain, and would have no obligation to see the proceeding to completion or comply with any orders of the Committee. Claimants' admitted lack of funds and possible reliance on an unknown third-party financier thus jeopardize the integrity of this proceeding. In these circumstances, the Committee must exercise its inherent powers to ensure the performance of the functions that have been expressly conferred on it by the ICSID Convention.

30. By exercising its power to protect the integrity of its own proceedings by granting El Salvador's request for security for costs, the Committee will not be acting inconsistently with the terms of the ICSID Convention and Arbitration Rules.

31. El Salvador understands that this is the first time an *ad hoc* committee is called upon to make a decision on security for costs. If the Committee's power to issue such an order becomes a contested issue, and should the Committee have any doubts about this power, this would be too important a decision to make with only one round of pleadings. Accordingly, should Claimants question the Committee's power to issue an order for security for costs, and should the Committee have any doubts about its power to issue such order, El Salvador respectfully requests the opportunity to respond.

IV. THE CURRENT SITUATION BEFORE THE *AD HOC* COMMITTEE IS SIGNIFICANTLY DIFFERENT FROM PREVIOUS APPLICATIONS FOR SECURITY FOR COSTS

32. This application for security for costs is unique because it is not based on hypothetical and subjective factors, such as Claimants' likelihood of success, but rather on the fact of Claimants' evidenced inability to fund the proceeding, a fact admitted by Claimants, which has

already caused significant delay and prejudiced El Salvador by unduly prolonging a public investment arbitration proceeding.

33. Whereas tribunals have been hesitant to prejudge the merits of a dispute,³⁸ or make a subjective determination about the likelihood that costs will be awarded to the respondent and the claimants' ability or willingness to pay a potential award on costs,³⁹ this Committee can decide to protect the integrity of this proceeding based on undisputed facts in the record before it. Unlike a tribunal facing a new case that does not wish to prejudge the case before hearing the evidence, here the Committee already has direct, uncontroverted evidence, including the experience of the parties' behavior, demonstrating Claimants' inability to fund this proceeding with the accompanying unfairness of making El Salvador, the Centre, and the Committee assume the risk of expending substantial resources to continue a proceeding that will either be abandoned or funded by a third party. Moreover, the request for security for costs justified by this evidence is unrelated to the merits of Claimants' application for annulment.

34. Claimants' financial situation is not hypothetical or the subject of conjecture. Claimants admittedly have no funds and needed an extension just to pay the first advance. Immediately

³⁸ *Emilio Agustín Maffezini v. Kingdom of Spain*, ICSID Case No. ARB/97/7, Procedural Order No. 2, Oct. 28, 1999, paras. 15, 19-21 (**Authority RL-21**); *Alasdair Ross Anderson and others v. Republic of Costa Rica*, ICSID Case No. ARB(AF)/07/3, Award, May 19, 2010, para. 9 (**Authority RL-22**); *World Duty Free Company Limited v. Republic of Kenya*, ICSID Case No. ARB/00/7, Award, Oct. 4, 2006 (**Authority RL-23**); *Inceysa Vallisoletana S.L. v. Republic of El Salvador*, Award (RL-6); *Plama Consortium Limited v. Republic of Bulgaria*, ICSID Case No. ARB/03/24, Award, Aug. 27, 2008 (**Authority RL-24**); *Biwater Gauff (Tanzania) Limited v. United Republic of Tanzania*, ICSID Case No. ARB/05/22, Award, July 24, 2008 (**Authority RL-25**); *Bayindir Insaat Turizm Ticaret Ve Sanayi A.S. v. Islamic Republic of Pakistan*, ICSID Case No. ARB/03/29, Decision on Jurisdiction, Nov. 14, 2005 (**Authority RL-26**); *Cementownia "Nowa Huta" S.A. v. Republic of Turkey*, ICSID Case No. ARB(AF)/06/2, Award, Sept. 17, 2009 (**Authority RL-27**); *Europe Cement Investment and Trade S.A. v. Republic of Turkey*, ICSID Case No. ARB(AF)/07/2, Award, Aug. 13, 2009 (**Authority RL-28**); *Saba Fakes v. Republic of Turkey*, ICSID Case No. ARB/07/20, Award, July 14, 2010 (**Authority RL-29**); *RSM Production Corporation and others v. Grenada*, ICSID Case No. ARB/10/6, Decision on Application for Security for Costs, Oct. 14, 2010 (**Authority RL-30**).

³⁹ *Víctor Pey Casado and President Allende Foundation v. Republic of Chile*, ICSID Case No. ARB/98/2, Decision on Provisional Measures, Sept. 25, 2001, para. 89 (**Authority RL-31**); *Libananco Holdings Co. Limited v. Republic of Turkey*, Decision on Preliminary Issues, paras. 57-59 (RL-8); *Gustav F W Hamester GmbH & Co KG v. Republic of Ghana*, ICSID Case No. ARB/07/24, Award, June 18, 2010, paras. 14-17 (**Authority RL-32**).

following that payment is the proper time for El Salvador to submit this request. The Committee does not need to wait for additional information to make an informed and fair decision, and we are not at a point in the proceeding where requiring security is impracticable. The timing of El Salvador's request is intended to prevent any unnecessary expense by ensuring that Claimants demonstrate that they can afford to continue this proceeding now, before the Centre, the Committee, and El Salvador invest more time and resources in a proceeding that the evidence currently before the Committee clearly indicates will likely be abandoned.

35. Claimants' new counsel, who in this case are advocating in favor of Claimants' bid to keep their proceeding going by securing third-party financing, will no doubt recognize that El Salvador's request is amply justified—their law firm has represented the State requesting security for costs in nearly half of the known cases where such requests have been made.⁴⁰ Indeed in *Libananco*, they recognized the threat to the integrity of proceedings inherent in third-party funding, arguing that the tribunal had before it "an exceptional case in which security for costs should be allowed because the Claimant [wa]s a shell company . . . with a wealthy third party ('the Third Party') funding the arbitration with no intention to pay any costs awards ('arbitral hit and run')." ⁴¹ Counsel thus viewed the presence of a third-party financier as justifying security for costs. Here, El Salvador is in the exceptional circumstance of facing insolvent applicants seeking funding from a third-party who would have no obligation to even see the proceeding through to completion. Unlike the *Libananco* tribunal, however, the Committee does not have to worry about prejudging the outcome of this proceeding.⁴² This Committee can take steps to

⁴⁰ Indeed, Claimants' new counsel probably has clients in the same unfortunate position as El Salvador regarding the *Inceysa* arbitration—unable to collect an outstanding award from an insolvent claimant after the tribunal did not order the requested security for costs.

⁴¹ *Libananco v. Turkey*, Decision on Preliminary Issues, para. 35 (RL-8).

⁴² *Libananco v. Turkey*, Decision on Preliminary Issues, para. 59.

protect the integrity of the proceeding based on the events that have already played out in this proceeding—namely, that Claimants in this case already defaulted on their first advance payment to ICSID and stated that they have no funds to make future payments.

36. Thus, given Claimants' documented financial irresponsibility, which has already irreparably harmed El Salvador with the expense of defending against multiple proceedings and the impact on its reputation for international investment, as well as the prospect that this proceeding—currently unfunded—may be abandoned, this Committee should take steps now, before it is too late, to protect the integrity of this proceeding. Neither El Salvador nor the Centre should be left with unreimbursed costs for this proceeding if Claimants are unable to obtain the funding they need just to meet their minimum obligations to fund the costs of the Centre and the Committee.

V. THE AMOUNT PROVIDED FOR SECURITY FOR COSTS MUST BE SUFFICIENT TO COVER ALL EXPECTED FEES, COSTS, AND EXPENSES, AND MUST BE PROVIDED PROMPTLY

37. El Salvador is including in this application an amount sufficient to cover not only its own legal fees and costs, but also any unpaid fees, costs, and expenses owed to ICSID at the end of the proceeding, which El Salvador would commit to pay if this application is granted and the guarantee is executed.

38. According to the August 2, 2012 e-mail from the Secretary to the Committee, the average cost of an ICSID annulment proceeding is \$350,000. In the same e-mail, the Secretary informed the parties that the fees and expenses for this proceeding, following the suspension of the proceeding for seven months, already exceeded \$71,000. At this point, the proceeding has only included the constitution of the Committee, the first procedural session of the Committee by

teleconference, and correspondence related to the funding of the proceeding. The Committee has not yet begun to review the pleadings or otherwise become involved with the substance of the case. At Claimants' request, there will be two rounds of written submissions. Then there will be a two-day hearing in Paris, probably post-hearing briefs, deliberations, and the drafting of the decision. Claimants have engaged new counsel, an international law firm, to assist them. It appears, therefore, that this proceeding will be more expensive than the average annulment proceeding. Under the circumstances, El Salvador considers that it would be prudent to set aside \$300,000 for future fees, costs, and expenses of ICSID and the Committee.

39. With regard to El Salvador's own costs, El Salvador had \$800,000 in legal fees and expenses in the underlying arbitration, which ended at the preliminary objection phase under the expedited procedure of CAFTA. That was a relatively simple case. In fact, El Salvador had made Claimants (and the ICSID Secretariat) aware of the fundamental jurisdictional problem manifest in the Notice of Arbitration, even before the case was registered. As stated in the communication by the Attorney General of El Salvador, which was completely ignored by Claimants, the Notice of Arbitration should not have even been registered by ICSID.⁴³ Then, immediately after the case was registered, El Salvador gave Claimants the opportunity to walk away from the arbitration without any significant costs to either party by providing its advance consent to the termination of the arbitration proceeding, if Claimants so requested before the

⁴³ Letter from Attorney General of El Salvador to Secretary-General of ICSID, Aug. 14, 2009. This document was submitted with El Salvador's Preliminary Objection and, for ease of reference, is included with this application as **Exhibit R-14**.

constitution of the Tribunal.⁴⁴ But Claimants made the conscious choice to move forward with the case.

40. Now, based on its expenses in the underlying arbitration, and taking into account the more complicated nature of any annulment proceeding with multiple alleged grounds for applying for annulment, and a two-day hearing to be held in Paris, El Salvador estimates its legal fees and expenses in the amount of \$1.7 million, excluding all fees and costs related to ICSID and the Committee. El Salvador requests that the security cover the anticipated full amount of its expenses because Claimants' default on payment of costs could take place near the very end of the proceedings, after El Salvador has incurred the expense to defend the process through the hearing.

41. Therefore, El Salvador requests that the security to be provided by Claimants be in the amount of \$2.0 million, in the form of an unconditional and irrevocable bank guarantee issued by a reputable international bank. Any amount still remaining after making the payments ordered by the Committee would be refunded to Claimants.

42. El Salvador further requests that the Committee set a reasonable time limit by which the bank guarantee must be provided. El Salvador considers that a time limit not exceeding thirty days would be sufficient for Claimants to provide the bank guarantee. First, Claimants have known since July 3, 2012, that El Salvador would apply for security for costs. Second, the 60-day extension Claimants requested on June 18, 2012, to pursue an additional third-party financier, will be over by the time the Committee decides on this application. Claimants will

⁴⁴ Letter from counsel for El Salvador to ICSID Senior Counsel, Aug. 24, 2009. This document was submitted with El Salvador's Preliminary Objection and, for ease of reference, is included with this application as **Exhibit R-15**.

know by then if they have secured the financing and thus whether they are able to continue with this proceeding. Finally, a time limit not exceeding thirty days would allow El Salvador sufficient time following the posting of security to begin substantial work preparing its counter-memorial on annulment, due on October 19, 2012.

VI. REQUEST

43. For the reasons stated above, El Salvador requests the Committee to order Claimants to submit, as a condition to the continuation of the annulment proceeding, an unconditional and irrevocable bank guarantee issued by a reputable international bank in the amount of \$2.0 million to cover the costs of this proceeding and ensure compliance with an award of fees and expenses.⁴⁵

44. El Salvador further requests that the Committee set a time limit not exceeding thirty days by which the bank guarantee must be provided.

45. In the event that Claimants are unwilling or unable to provide the bank guarantee by the date ordered by the Committee, El Salvador requests that the Committee order the termination of this annulment proceeding without further delay.

46. In the event that Claimants question the Committee's power to issue an order for security for costs, and should the Committee have any doubts about its power to issue such order, El Salvador requests an opportunity to respond.

⁴⁵ El Salvador estimates that this amount would cover two rounds of written pleadings, a two-day hearing on annulment in Paris, any post-hearing briefing, and any payments Claimants fail to make to the Centre. Any amount still remaining after making the payments ordered by the Committee would be refunded to Claimants.

47. Finally, in the event the Committee is not inclined to issue an order for security for costs for any reason, El Salvador reserves the right to request an alternative remedy.

Dated: August 10, 2012

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Derek Smith", written over a horizontal line.

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