

# DEWEY & LEBOEUF

Dewey & LeBoeuf LLP  
1101 New York Avenue, NW  
Suite 1100  
Washington, DC 20005-4213

tel +1 202 346 8769  
fax +1 202 956 3242  
dsmith@dl.com

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By e-mail

Members of the Tribunal  
Professor Albert Jan van den Berg  
Dr. Horacio A. Grigera Naón  
Mr. J. Christopher Thomas, Q.C.

c/o Mr. Marco Tulio Montañés-Rumayor  
Secretary of the Tribunal

Re: Commerce Group Corp. and San Sebastian Gold Mines, Inc. v.  
Republic of El Salvador (ICSID Case No. ARB/09/17)

Dear Members of the Tribunal,

In response to the Tribunal's invitation on January 27, 2011, El Salvador submits its comments on Claimants' Application for Fees and Costs of November 30, 2010.

On November 17, 2010, the Secretary of the Tribunal transmitted to the parties the Tribunal's invitation to submit: "by Tuesday, November 30, a statement of costs." As noted by El Salvador in its letter to the Tribunal of December 1, 2010, a statement of costs, as its name indicates, is simply a list of a party's arbitration costs. However, in response to the Tribunal's invitation to submit a *statement* of costs, Claimants submitted an *application* for fees and costs that included additional legal arguments on the merits of the Preliminary Objection, as well as Claimants' statement of costs. Claimants' application for fees and costs was unsolicited and should be rejected by the Tribunal on that basis.

However, the Tribunal could also consider Claimants' Application for Fees and Costs as further evidence in support of El Salvador's own application for fees and costs, as explained below.

**1. CAFTA Article 10.20.6 requires that Claimants pay the costs of this arbitration**

Pursuant to Article 61(2) of the ICSID Convention, unless the parties agree otherwise, the Tribunal shall decide how and by whom the costs of a proceeding should be paid.

The present Preliminary Objection phase is governed by CAFTA Article 10.20.5. CAFTA Article 10.20.6 provides:

When it decides a respondent's objection under paragraph 4 or 5, the tribunal may, *if warranted*, award to the *prevailing disputing party* reasonable costs and attorney's fees incurred in submitting or opposing the objection. *In determining whether such an award is warranted, the tribunal shall consider whether either the claimant's claim or the respondent's objection was frivolous, and shall provide the disputing parties a reasonable opportunity to comment.*<sup>1</sup>

If warranted, the Tribunal may award costs and fees to the prevailing party. In making a determination as to whether an award of costs and fees is warranted, the Tribunal shall consider whether Claimants' claim is frivolous.

In this case, it was clear from the beginning that Claimants' claim was frivolous. It is also clear that El Salvador informed Claimants about the problem with their case and gave Claimants two opportunities to reverse their conduct without adverse consequences, but Claimants willfully ignored those opportunities and pressed ahead with the case.<sup>2</sup>

Claimants brought this arbitration under CAFTA knowing that they had proceedings pending before the Supreme Court of El Salvador based on the same measures complained of in this arbitration. In fact, Claimants referred to the pending litigation related to the same measures in the Notice of Arbitration.<sup>3</sup> Claimants therefore knew or should have known that they were in violation of the CAFTA waivers the moment they were submitted.

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<sup>1</sup> CAFTA Article 10.20.6 (emphasis added).

<sup>2</sup> Preliminary Objection, paras. 88-93.

<sup>3</sup> NOA, para. 22 ("On December 6, 2006, Commerce/Sanseb's legal counsel filed with the El Salvadoran Court of Administrative Litigation of the Supreme Court of Justice two complaints relating to this matter, one for the San Sebastian Gold Mine and the other for the San Cristobal Mill and Plant. These legal proceedings have not been resolved.").

Giving Claimants the benefit of the doubt, El Salvador made Claimants aware, both before and immediately after registration of their Notice of Arbitration, that Claimants were in violation of the CAFTA waivers. In addition, El Salvador communicated to the ICSID Secretariat its advance consent to discontinue the case, with no adverse consequences to Claimants, if Claimants requested discontinuance before the constitution of the Tribunal.<sup>4</sup>

El Salvador further communicated to Claimants that if they chose to continue with their arbitration even after being made aware that they had violated the waivers, El Salvador would be forced to request that the Tribunal order Claimants to pay for El Salvador's legal fees and costs that would be unnecessarily generated during the Preliminary Objection phase.<sup>5</sup>

Finally, the Tribunal will recall that Claimants' pursuit of this arbitration has been timed based on the parallel proceedings before the Supreme Court of El Salvador that were related to the same measures Claimants complained of in this CAFTA proceeding. The Supreme Court cases were finally decided in February and March of 2010, and the parties were notified of the judgments on April 29, 2010.<sup>6</sup> It was only after the cases had been decided, and after the ICSID Secretariat warned Claimants that it intended to apply the provisions of ICSID Arbitration Rule 45 to discontinue the arbitration due to inactivity in the case for more than six months, that Claimants requested the constitution of this Tribunal. Because both proceedings related to the same measures, this order of events is clear evidence that Claimants' intention all along was to wait for the Supreme Court to issue its decisions and to keep the CAFTA arbitration open in case they lost in El Salvador. This is precisely one of the abuses CAFTA's waiver requirement is intended to prevent.<sup>7</sup>

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<sup>4</sup> Letter from counsel for El Salvador to ICSID Senior Counsel, Aug. 24, 2009 (R-10). Claimants acknowledged this offer at the hearing: "it's still . . . 'We still have the choice to . . . request discontinuance of the arbitration.' That was the drive at that point in time, that we were jurisdictionally defective from the beginning, that there is nothing we could do to fix it." Transcript of Hearing on Preliminary Objections, Nov. 15, 2010 ("Transcript"), at 117: 14-22.

<sup>5</sup> Letter from counsel for El Salvador to ICSID Senior Counsel, Aug. 24, 2009 (R-10).

<sup>6</sup> Supreme Court Decision, Case 308-2006, Feb. 26, 2010 (R-5); Supreme Court Decision, Case 309-2006, Mar. 18, 2010 (R-6).

<sup>7</sup> Claimants' desire to continue their domestic litigation until a final decision and, at the same time, not lose the right to initiate a CAFTA arbitration is also clear from their comments at the hearing. There, Claimants explained their view of El Salvador's letters: "So we're looking at this from our practical standpoint. Here we are in August of 2009. We certainly don't want to get into a statute of limitations question. This is three years after. And what they are saying is, you have to dismiss your CAFTA proceedings, and then go through the some process in El Salvador before you could even -- an unknown time frame before you can start it." Transcript, at 115: 2-10.

Under these circumstances, the fact that Claimants did not request discontinuance of the arbitration but instead requested the constitution of the Tribunal is also evidence of bad faith, which is an additional reason why El Salvador should be awarded its costs and attorney's fees.<sup>8</sup>

**2. Claimants' arguments during the arbitration were frivolous and their conduct was improper**

As the Tribunal will recall, Claimants 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.<sup>9</sup> 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 two weeks later.<sup>10</sup>

The Tribunal will also recall that Claimants then made another frivolous argument that the waiver requirement in CAFTA did not require Claimants to do anything, but instead, to make the waiver effective, a Respondent State would have had to go before any court, tribunal, or other forum where a claimant may continue overlapping proceedings with a copy of the waiver to request termination of those cases.<sup>11</sup>

In addition, Claimants, after consistently representing themselves as two U.S. companies acting together to pursue a joint venture in El Salvador, suddenly changed course in the middle of the written procedure and argued that San Sebastian was not a party to the domestic proceedings.<sup>12</sup> As described by El Salvador at the hearing, either San Sebastian was involved in everything Commerce Group did (as suggested in Claimants' Notice of Arbitration), including the domestic proceedings, because the two

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<sup>8</sup> El Salvador's Reply, paras. 128-132.

<sup>9</sup> Claimants' Response, para. 32 ("The text of Article 10.18 does not operate as a condition precedent to consent. If the treaty drafters had intended Article 10.18 to apply as conditions precedent, they would have provided so expressly. They did not. Although Article 10.18 is called 'Conditions and Limitations on Consent of Each Party', the treaty text does not expressly create conditions precedent to consent; rather it identifies procedural requirements for the submission of a claim to arbitration.").

<sup>10</sup> Claimants' Rejoinder, para. 5 ("Although the Claimants argued in their Response that the text of CAFTA Article 10.18 establishes procedural requirements for the submission of claims, the Claimants accept that the submission of a waiver under CAFTA Article 10.18 is a condition and limitation on consent and thus a jurisdictional requirement.").

<sup>11</sup> Claimants' Rejoinder, paras. 23, 25.

<sup>12</sup> Claimants' Response, paras. 87-88.

companies were registered as a joint venture under the name "Commerce Group,"<sup>13</sup> or San Sebastian has no standing to bring claims as it is not authorized to do business in El Salvador and did not receive or apply for any of the licenses or permits, or the very concession involved in this dispute.<sup>14</sup> Claimants simply chose to invent another frivolous argument that seemed expedient at the time, unnecessarily increasing the costs of the arbitration for El Salvador.

Claimants not only initiated an arbitration while refusing to comply with a condition to El Salvador's consent to arbitrate and then increased the costs of the proceedings by presenting frivolous arguments, but Claimants then conducted themselves in the arbitration in a manner that was unhelpful to the Tribunal and insulting to other State Parties. Claimants failed to provide helpful responses to the Tribunal's requests for information about issues of Salvadoran law. Claimants' self-serving arguments lacked legal foundation, to the extent of not bothering to verify that the law to which they cited had been repealed.<sup>15</sup> Finally, when two CAFTA Parties made non-disputing Party submissions as it was their right to do, Claimants disparaged them by publicly impugning their motives when they chose to exercise their Treaty rights as non-disputing Parties.<sup>16</sup>

### **3. Claimants' Application for Fees and Costs is also frivolous**

At paragraph 8 of their Application for Fees and Costs, Claimants set forth the central premise of their application for costs based on an alleged lack of merit of El Salvador's Objection:

Simply stated, the Respondent claimed that the Tribunal lacked jurisdiction because the Claimants failed to obtain the dismissal of pending domestic proceedings in the Republic of El Salvador before they filed a Notice of Arbitration with ICSID. However, the Respondent has failed to bring to the attention of the Tribunal any authority supporting this argument. Furthermore, the argument is at odds with the plain language of CAFTA.

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<sup>13</sup> Commerce Group Entry into Commercial Registry, Apr. 11, 1991 (R-22).

<sup>14</sup> Transcript, at 86-95.

<sup>15</sup> Letter from Claimants to the Tribunal, Nov. 23, 2010.

<sup>16</sup> Transcript, at 221: 18-22 (Mr. Machulak: "As to the other two states that we have in connection with these proceedings, it doesn't escape notice, looking at the Dewey & LeBoeuf web site, that their law firm is representing those two countries. So to sit here and listen, in all fairness to my clients, that everybody else in the world is against us in our interpretation of the treaty is just plain not true.").

Claimants not only misstate El Salvador's position, but make the surprising argument that El Salvador's position is not supported by any authority or the text of CAFTA. Making such an assertion after the briefing and hearing in this arbitration is frivolous.

First, El Salvador's position is that Claimants violated the waivers by continuing the domestic judicial proceedings with respect to the same measures they alleged constituted breaches of CAFTA, and thus failed to meet a condition to consent, as a result of which there is no jurisdiction.<sup>17</sup> El Salvador's position is not that this Tribunal lacks jurisdiction because Claimants failed to obtain the dismissal of the pending domestic proceedings. *Claimants did not even request the dismissal of the pending domestic proceedings.*

Second, whereas Claimants were forced to abandon their initial position that Article 10.18.2, despite its title: "Conditions and Limitations on Consent of Each Party", was not a condition to consent,<sup>18</sup> El Salvador's argument that a good faith reading of the text of CAFTA requires conduct consistent with the waiver has remained the same since its letters during the registration phase of this arbitration.<sup>19</sup>

Third, El Salvador's position is supported by CAFTA and NAFTA precedent as well as other CAFTA Parties. In contrast, Claimants rely exclusively on an unrelated case decided under a bilateral investment treaty where the claimants did withdraw their domestic claims and the waiver requirement was not a condition to consent, as well as on the dissenting opinion of Mr. Keith Highet in the *Waste Management v. Mexico* arbitration.<sup>20</sup> As Claimants should have been aware since before initiating this arbitration, the NAFTA tribunal in *Waste Management* and the CAFTA tribunal in *RDC v. Guatemala* both decided that the waiver requirement is a condition on consent and that

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<sup>17</sup> Preliminary Objection, para. 87 ("In sum, the absence of a valid waiver means that El Salvador's consent to CAFTA arbitration was not perfected. Therefore, there is no jurisdiction and this Tribunal has no competence to decide this case. As a consequence, the entire arbitration must be dismissed.").

<sup>18</sup> Claimants' Response, para. 32; Claimants' Rejoinder, para. 5.

<sup>19</sup> Letter from Attorney General of El Salvador to Secretary-General of ICSID, Aug. 14, 2009 (R-8) ("The waivers required by article 10.18.2 of CAFTA-DR, and a corresponding conduct consistent with those waivers, are conditions precedent to the Republic's consent to arbitration under CAFTA-DR; part of a sub-section titled 'conditions and limitations on consent of each party'.").

<sup>20</sup> Claimants' Response, paras. 43-44, 60-62. Mr. Highet's opinion in the *Waste Management* arbitration has not been followed by subsequent tribunals nor has it been endorsed in commentary.

a claimant must act consistently with the waiver.<sup>21</sup> El Salvador's view is further reinforced by the position taken by all three State Parties to NAFTA, as well as the positions of Guatemala, the Dominican Republic, Nicaragua, and Costa Rica in the context of CAFTA. In sum, El Salvador's position is supported by the text of CAFTA, the positions of the State Parties to CAFTA and NAFTA, and considerable arbitral authority. Claimants' position is not.

Another misrepresentation in Claimants' Application for Fees and Costs is Claimants' implication that El Salvador's letters in August 2009, rather than alert Claimants to the fatal defects in their Notice of Arbitration, somehow caused them not to seek termination of the domestic proceedings or comply with CAFTA.<sup>22</sup> El Salvador merely informed Claimants that the current arbitration, with the waiver violations, could not proceed. El Salvador said nothing about Claimants' ability to start a new arbitration after terminating the local proceedings. It should be recalled that Claimants, not El Salvador, initiated this arbitration. Prior to doing so and at all times thereafter, Claimants had full access to the text of CAFTA and existing legal authority, and, like El Salvador, had every opportunity to seek independent legal advice from experienced international counsel. El Salvador was in no position to cause Claimants to make any particular decision or act in any particular way. Claimants appear now to regret that they chose to ignore El Salvador's letters, as well as the authority cited in the letters, and that they did not do what they had to do to properly initiate arbitration. But El Salvador bears absolutely no responsibility for Claimants' decisions.

Of course El Salvador was under no obligation to tell Claimants how to cure their waiver violation and initiate a valid arbitration against El Salvador. Claimants were free to withdraw their Notice of Arbitration before it was registered or seek discontinuance after registration (for which they already had El Salvador's advance consent), and to request termination of the domestic legal proceedings and then file a new Notice of Arbitration. Now Claimants' bad faith in refusing to act in accordance with CAFTA as pointed out in El Salvador's letters is compounded by their attempt to blame El Salvador for their refusal to terminate the domestic proceedings before initiating CAFTA arbitration.

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<sup>21</sup> Preliminary Objection, paras. 41, 65.

<sup>22</sup> Claimants' Application for Fees and Costs, Nov. 30, 2010, para. 13 ("The import of these letters was that the claimed lack of jurisdiction could not be cured by dismissing the then pending domestic proceedings and that efforts to do so would be pointless.").

#### 4. Conclusion

Whatever lack of knowledge Claimants and their counsel may have had before initiating this arbitration, El Salvador informed them early on that they had violated the waivers and that they should discontinue the case. Any excuse for lack of knowledge Claimants may have had before submitting the Notice of Arbitration was eliminated when Claimants' counsel stated at the hearing that, even then, he was glad Claimants had not listened to El Salvador's admonition and had continued with the arbitration in spite of El Salvador's warning.<sup>23</sup>

El Salvador was forced to bring this Preliminary Objection even though it provided Claimants with early notice of the defects in their Notice of Arbitration and two clear opportunities to avoid incurring these costs. Claimants chose to ignore the notice and continued with this arbitration knowing that they had pending proceedings before the Supreme Court of El Salvador based on the same measures complained of in this arbitration, in violation of the text of CAFTA Article 10.18.2, and Claimants now admit that they feared that otherwise they could run into a statute of limitations problem.<sup>24</sup>

Furthermore, having been forced to respond to Claimants' frivolous allegations concerning the waiver requirement in CAFTA, including Claimants' surprising position that the waiver requirement is not a condition to consent, El Salvador now responds to this equally frivolous submission of an Application for Fees and Costs.

El Salvador does not know whether Claimants would voluntarily comply with an Award of costs, or whether legal action to enforce the Award would result in its complete satisfaction. However, El Salvador believes it is important to send a strong message to Claimants that they cannot expect to intentionally violate an express waiver required as a condition to consent by the Treaty under which they are seeking protection.

In its Preliminary Objection, El Salvador included a request for the Tribunal to "[i]ssue an order awarding the Republic of El Salvador its share of the arbitration costs and its attorney's fees incurred related to this Objection, plus interest from the time of the decision until payment is made, at a rate to be established at the appropriate time."<sup>25</sup>

El Salvador reaffirms its request for costs and fees plus interest.

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<sup>23</sup> Transcript, at 224: 13-15 (Mr. Machulak: "In fact, I'm glad we did not follow El Salvador's advice, because I think we would be in a very poor, poor position here today.")

<sup>24</sup> Transcript, at 115: 2-10.

<sup>25</sup> Preliminary Objection, para. 126.

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To encourage prompt compliance with the Award, El Salvador requests that interest be awarded at a rate the Tribunal decides is appropriate,<sup>26</sup> beginning to accrue sixty days after the Award is dispatched to the parties, and compounded semi-annually until the Award is satisfied in full.

Sincerely,



Derek C. Smith

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<sup>26</sup> El Salvador notes that the interest rate used by ICSID tribunals for post-Award interest is commonly the rate of LIBOR in effect as of the date of the Award plus either four percent (4%) or two percent (2%). In this case, El Salvador respectfully suggests that the applicable rate could be the six-month term LIBOR rate for U.S. dollar deposits published by the Wall Street Journal as of the date of the Award, plus four percent (4%), beginning to accrue sixty days after the Award is dispatched to the parties, and compounded semi-annually until the Award is satisfied in full.