IN THE ARBITRATION UNDER CHAPTER 11
OF THE NORTH AMERICAN FREE TRADE AGREEMENT
AND UNDER THE UNICITRAL ARBITRATION RULES
BETWEEN

- - - - - - - - - - - - - - - - -x
METHANEX CORPORATION,

Claimant/Investor,

and

UNITED STATES OF AMERICA,

Respondent/Party.

- - - - - - - - - - - - - - - - -x Volume 2

SECOND FINAL AMENDED TRANSCRIPT

Tuesday, June 8, 2004

The World Bank
1818 H Street, N.W
MC Building
Conference Room 13-121
Washington, D.C.

The hearing in the above-entitled matter
came on, pursuant to notice, at 9:35 a.m. before:

V. V. VEEDER, Q.C., President

PROF. W. MICHAEL REISMAN, Arbitrator

J. WILLIAM ROWLEY, Q.C., Arbitrator

Also Present:

SAMUEL WORDSWORTH,
Tribunal Legal Secretary

MARGRETE STEVENS,
Senior ICSID Counsel
Tribunal Administrative Secretary

Court Reporter:

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PROCEDINGS

PRESIDENT VEEDER: Good morning, ladies and gentlemen. This is day two of the main hearing, and under our schedule it's now for the United States to make its oral submissions, and we hand the floor over to you, Mr. Taft.

OPENING STATEMENTS BY COUNSEL FOR RESPONDENT/PARTY

MR. TAFT: Thank you, Mr. President.

Mr. President, members of the Tribunal, it's my privilege to open the United States's presentation of its case-in-chief at this hearing, and I speak on behalf of the entire U.S. team arrayed to my right in saying that we are honored to appear before you today.

This morning I will make some general remarks and provide an overview of the U.S. presentation and then summarize how we intend to divide the presentation among the members of our team. I regret that I will not be able to stay with you during the course of the day. In fact, I have to leave right after.

There seem to be two hearings this week in Washington that have not been cancelled as a result of President Reagan's ceremonies, and this is one,
and the other is the hearing of the Senate Select Committee on Intelligence on the Law of the Sea Treaty at which I'm scheduled to testify, so I will have to go and attend to that, but I'm glad to be able to start off here.

In its first pleading in this case, the statement of defense of August 2000, the United States stated that, and I quote, Methanex's claim does not remotely resemble the type of grievance for which the state parties to the NAFTA created the investor-state dispute resolution mechanism of Chapter 11, unquote.

Several years have passed, and many pages of pleadings and evidentiary materials have been prepared and filed since then, but the passage of time has only served to underscore the fact that Methanex's claims, no matter how cast or recast, do not fit the NAFTA's investment chapter. They're not the kind of claims that the parties contemplated would be subject to the jurisdiction of investor-state dispute resolution panels, and they are not, on their merits, entitled to any of the remedies of Chapter 11.

First, Methanex's claims do not fall within the scope of Chapter 11. As a result, this Tribunal does not have jurisdiction to resolve them. Article 1101(1) of the Treaty provides that Chapter 11 only applies to those of a party's measures relating to, first, investors of another
party; or two, the investments of those investors in the territory of the first party. I understand that yesterday Methanex did not address this issue directly, suggesting that it would come to jurisdictional issues only in its closing. For the moment, it only put forward its belief that the challenged measures related to Methanex and methanol. But the measures Methanex complains of relate to a product, MTBE, that Methanex doesn't manufacture and in the production of which it has made no investment at any time.

As the First Partial Award in this case held, this ban could not be said to relate to Methanex or relate to its investments within the meaning of Article 1101(1) under the facts alleged in Methanex's written pleadings.

In our presentation, we will show that Methanex's points have no merit. The Tribunal did, in its First Partial Award, leave a narrow jurisdictional window open to Methanex. It held that if Methanex could prove that the measures it challenges were intended to harm foreign methanol producers, including Methanex and its investments in this country, then it could make its case on the merits. The First Partial Award thus declined to dispose of the case on the pleadings based on Methanex's representation that it could prove that by banning MTBE, California secretly intended to...
harm methanol producers. All of the evidence is now in, however, and that evidence falls far short of showing such an intent.

The evidence submitted by Methanex consists, in major part, of opinion pieces published in petrochemical industry newsletters, uncorroborated double hearsay statements by interested witnesses, sheer speculation about what must have been discussed at a dinner meeting with gubernatorial candidate Davis, and a series of expert reports and witness statements that provide unsupported post hoc criticisms of California's policy decision to ban MTBE, reports and statements that were not available to California decision makers at the time that the measures in question were adopted.

Far from establishing any secret intent to harm methanol producers, the record shows that California's intent in banning MTBE was precisely what the measures said it was: To protect California's public water resources from MTBE's contaminating effects on the taste and the smell of drinking water.

In light of this failure of proof, the holdings of the First Partial Award, therefore,
The ban of MTBE in California gasoline relates to producers of California gasoline and producers of MTBE. It does not relate to Methanex, which does not make or market either gasoline or MTBE. Because Methanex has failed to establish that the measures relate to it within the meaning of Article 1101(1), its claims must be dismissed.

Methanex’s claims also fail on their merits. Methanex has not established that it has suffered any loss proximately caused by the measures or, indeed, that it has suffered any loss at all.

First, the claims are too remote. They depend upon the effects of the MTBE ban on suppliers of California gasoline, who will buy less MTBE from MTBE producers, who, in turn, will allegedly buy less methanol from methanol producers like Methanex. It is well settled under customary international law that claims premised on such remote effects cannot stand.

In its first memorial in this case submitted in November of 2000, the United States collected numerous international case authorities. Those authorities established that claims based on the effects of state action upon the claimant’s contractual counterparty are too remote to satisfy the international law principle of proximate causation. Methanex has never identified any
international authority to dispute the holdings of those cases which we put forward.

Secondly, Methanex has also failed to prove that it suffered any loss at all as a result of the ban of MTBE. As the President and now Chief Executive Officer of Methanex advised Methanex investors earlier this year, in only one of many similar statements by Methanex officials, the MTBE ban has—and I'm quoting him—really had no impact on our industry, unquote. And he was referring to the methanol industry.

To the contrary, the years since California's ban on MTBE have been golden ones for Methanex. Methanol prices have been high and supplies tight in all markets, including in the United States. Methanex's stock price has increased by 425 percent over the last four years. Methanex's failure to prove any loss on this record is not surprising. It is, nonetheless, fatal to every one of Methanex's claims.

Beyond these threshold problems posed to its case under Article 1101, Methanex's specific claims fare no better. The national treatment claim under Article 1102 fails on the undisputed facts in the record. It is not contested that there is a substantial methanol industry in the United States and that U.S. investors own methanol marketing and production units just like Methanex.
It is also not disputed that California's MTBE ban, to the extent it constitutes treatment of the methanol industry at all, accords Methanex's investments precisely the same treatment as that accorded to the U.S.-owned methanol industry. California, therefore, accorded to Methanex treatment no less favorable than that it accorded in like circumstances to U.S. investors. Article 1102 requires no more than this. Nor has Methanex made any serious effort to support its claim under Article 1105(1). That Article requires treatment in accordance with international law. In its Amended Statement of Defense, the United States comprehensively showed how Methanex's claim that customary international law prohibits discrimination against foreign goods, has no support whatsoever. Methanex has made no answer to that showing. Its Article 1105(1) claim is baseless. Methanex's claim of expropriation is similarly without merit. The parties' pleadings raise interesting issues with respect to the law of expropriation, but these issues are really beside the point, given the evidentiary record. Methanex has not attempted to prove that anything at all was taken away from it by California's measures. But
without a taking, a question of whether there has been an expropriation does not arise. Because the record here does not begin to show an expropriation, Methanex's Article 1110 claim should be dismissed.

Finally, I would to say just a word about costs. First, as noted, Methanex avoided dismissal of its claims based on its commitment that it would provide evidence of California's secret intent, a commitment that it has not kept. As the Tribunal stated in its procedural order of June the 2nd, 2003, and I'm quoting it, the Tribunal is not disempowered from making an order for costs against Methanex if the Tribunal should decide that the Tribunal had no jurisdiction over the disputing parties' dispute.

We respectfully submit that given Methanex's failure to produce evidence the Tribunal deemed essential to its jurisdiction, in light of Methanex's conduct in these proceedings, and considering the stark inconsistencies between Methanex's claims of loss and what it has repeatedly told to its shareholders about its prosperity, it is appropriate for the Tribunal to award full costs to the United States.

Each of my colleagues will address the points that I've just made in greater detail. The U.S. presentation will proceed as follows: First,
Mark Clodfelter will summarize the principal facts relevant to the Tribunal's decision, and in doing so will show that the measures at issue here were based upon genuine concern about the threat that MTBE use poses to public water resources.

Bart Legum, David Pawlak and Andrea Menaker will address Article 1101(1)'s requirement that the measure complained of relate to the investment or the investor. Bart Legum and Mark McNeill will present the United States's case on proximate causation.

That will conclude our presentation for today. Tomorrow morning, we will turn to the specific claims of breach made by Methanex. Mark Clodfelter and Andrea Menaker will present the United States's case on national treatment. Carrielyn Guymon will examine Methanex's claim under Article 1105(1), and Andrea Menaker will then address the issue of Methanex's claiming of expropriation under Article 1110. Jennifer Toole will review Methanex's failure to prove its ownership of investments in the United States.

Ron Bettauer, who will be our impresario throughout and introduce these different presentations separately, will then conclude the U.S. presentation tomorrow. I now invite the Tribunal to turn the floor over to Mr. Clodfelter who will provide the
summary of the salient facts, and again, I appreciate the opportunity to appear before you, and I apologize that I'm not able to stay with you longer.

Thank you.

PRESIDENT VEEDER: Thank you, Mr. Taft.

We apologize if by starting slightly late because

of our administrative meeting we've delayed you from your other duties, but in accordance with your request, we hand over the floor either to the impresario or to Mr. Clodfelter.

(Pause.)

MR. CLODFELTER: Mr. President, members of the Tribunal, yesterday you heard Methanex's version of events: Convoluted, conspiratorial, and largely speculative, a version based on overreading of thin evidence, giant leaps of inference, nonexistent and meaningless admissions, and calls for adverse inferences on such meritless grounds as our determination that none of their witness testimony merited cross-examination; a version based, in part, on documents of suspect origin, the first explanation of which we received for the first time in three years just last week, and a firsthand account of which we still await.

Methanex's version of events ignores the fundamental facts surrounding California's decision to ban the use of MTBE in gasoline. Therefore,
before we present our case-in-chief in response to Methanex's arguments, we want to provide an overview of some of those fundamental facts, which are, by and large, undisputed.

With the aim of restoring a measure of perspective to the California measures, one more formerly rooted in what actually happened, I'll cover three basic topics. First, I'll briefly review the history of the use of MTBE as an oxygenate additive in California gasoline. Second, I'll outline the background of the problem of MTBE contamination of California water supplies. And finally, I will describe in somewhat greater detail the measures that California took in response to that contamination problem. Of course, additional details of the factual record will be discussed during our presentations of the legal issues.

Let's begin with how MTBE came to be used in California gasoline. MTBE is a manufactured chemical compound made from ethanol and isobutylene. MTBE is not methanol. MTBE is an ether; methanol is an alcohol. MTBE is not even a version of methanol, no more than water is a version of hydrogen. The two chemicals are distinct and separate products, with distinct and separate properties and molecular structures. The method of combining them is a
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MTBE came into use in the United States in the 1970s. First, it was used as a source of octane in gasoline to replace lead, which was being phased out under Federal Government regulations aimed at reducing air pollution. MTBE's use as a fuel additive increased in response to amendments documented in 1990 to the U.S. Clean Air Act, amendments that required a higher oxygen content in gasoline.

The 1990 Clean Air Act amendments created two programs: The winter Oxyfuel program and the year-round reformulated gasoline program, or RFG program. Both of these programs require that in certain metropolitan areas with severe ozone or carbon monoxide levels, gasoline must contain a minimum of 2 percent oxygen by weight. Several areas of California are subject to this requirement, including Los Angeles, San Diego, and Sacramento.

The Clean Air Act amendments do not mandate which oxygenate additives must be used to achieve the new higher oxygen level, but the United States Environmental Protection Agency, the EPA, does impose requirements for fuel additives. The EPA requires fuels and fuel additives to satisfy certain specifications relating to vehicle emission standards.
In addition, as of 1994, fuel additives above a certain baseline level are required to undergo testing for health effects before they can be used commercially.

In practice, ethanol has been the principal oxygenate additive used in the winter Oxyfuel program. MTBE has been the principal oxygenate additive used in the RFG program. Now, the greater Los Angeles area is the exception. It uses MTBE, or has, for both the winter Oxyfuel program and the RFG program.

Other oxygenate additives, including additives known as TAME, ETBE, DIPE and TBA, have been used little, if at all.

So, this is how MTBE came to be used in California gasoline. It can fairly be said that MTBE owes its very market existence to government measures aimed at limiting the harmful effects of gasoline use. But what was the effect of using MTBE as an additive in California gasoline? That's the second topic I want to review.

MTBE had two effects: First, it helped reduce air pollution, at least in the earlier years of its use. But as sometimes happens with complex public policy decisions, MTBE also had an unintended consequence; namely, that minute amounts of gasoline containing MTBE polluted large volumes of water to the point where that water was no longer drinkable.
gasoline sometimes spills and leaks into the environment. Spills of conventional gasoline generally do not threaten drinking water supplies because the chemical components of gasoline biodegrade or break down before they have time to migrate into water resources. Spills of gasoline containing MTBE, however, do threaten drinking water. MTBE is highly soluble in water. It travels through soil rapidly. Compared to other components of gasoline, MTBE is highly resistant to biodegradation. Therefore, MTBE can, and does, enter sources of public water even when other components of a gasoline leak or spill do not.

Once in drinking water, MTBE gives the water a foul taste and odor. MTBE-contaminated well water smells and tastes like turpentine, making it undrinkable. Even at relatively low concentrations, MTBE's taste and odor can be detected.

As can you see in my first slide, in controlled studies, MTBE's taste is detectible at levels as low as two parts per billion. MTBE's odor is detectible at levels as low as 2.5 parts per billion.
California law prohibits state public drinking water agencies from delivering drinking water with an MTBE concentration of over five parts per billion, twice the level at which some people can taste and smell it.

So, as you can see on this screen, five parts per billion is the legal limit of MTBE in California water. And as was pointed out yesterday, the health limit in California is 13 parts per billion.

Unfortunately, California has experienced some of the worst and most widespread MTBE contamination in the United States. Let me give you a few examples. The City of Santa Monica, a city with a population of over 80,000 people, lost half its drinking water supply when it had to close contaminated wells in 1996. Some of those wells had concentrations as high as 610 parts per billion. Compare that to the five parts per billion legal limit. As shown on the slide, that's over 100 times the California limit.

In Glennville, California, contaminated residential drinking water wells had concentrations of MTBE of up to 20,000 parts per billion, 20,000 parts per billion. This proportion is shown in the slide. That is 4,000 times the California legal limit. And since 1997, Glennville has had to rely
on alternative sources of drinking water.

Another example: In a study published in July 1999, it was determined that in Santa Clara, California, underground fuel tanks that had been upgraded to comply with California's then new regulations continued to leak, resulting in MTBE contamination of groundwater. Levels found there were as high as 200,000 parts per billion, or 40,000 times the legal limit.

Well, there are many other instances of such contamination. In the south Lake Tahoe area, for example, the public utility district shut down 35 of its public drinking water wells due to MTBE contamination. In Santa Rosa, California, a fuel distribution company contaminated nine residential and business wells resulting in the detection in 1999 of MTBE at concentrations as high as 240 parts per billion in one of those wells.

In Los Gatos, California, it was determined that the Loma Prieta Elementary School had been serving trace amounts of MTBE to 400 school children.

Being forced to shut down water supplies has not been the only problem of course. Cleaning up contaminated wells has proven to be a very expensive undertaking in California. For example, a treatment facility for just five MTBE contaminated wells in Santa Monica has been estimated to cost up to $520 million.
So, the notion that public and official concern about MTBE was nothing more than hysteria whipped up by ethanol producers is a fiction. MTBE contamination was found in public water supplies throughout California. Mr. Pawlak will have more to say about the incidence of such contamination.

Not surprisingly, California's government took action, and the action taken to address the MTBE problem was the third topic I want to address this morning. This topic will take a little longer in light of Methanex's presentation yesterday.

First, in October 1997, California enacted Senate Bill 521. There's a lot about this bill that is relevant to Methanex's allegations, beginning with the process by which it became law. Notably, it was adopted unanimously; that is to say, every member voting on it in both chambers of the California Legislature from both political parties represented in those chambers voted in favor of enacting it. Not a single legislator of the 114 voting members dissented. That kind of bipartisan unanimity on any public policy measure is extremely rare these days, in California or any other state.
Moreover, the bill was signed into law not by Governor Gray Davis, but by his predecessor, Governor Pete Wilson, the same Governor who Mr. Dugan told us yesterday opposed ethanol. Davis was not even elected Governor until more than a year later and did not take office for another 15 months.

Now, these facts about how Senate Bill 521 became law are significant because of what that bill did. First, as can you see on the screen, Section 2 of the bill stated that its purpose was to provide what it termed a, quote, thorough and objective evaluation of the human health and environmental risks and benefits, if any, of the use of methyl tertiary-butyl ether, MTBE, unquote, compared to other mentioned additives.

To accomplish this purpose, Section 3(a) of the bill appropriated $500,000 to be used by the University of California to carry out this thorough and objective evaluation.

Now, that is not an extraordinary sum to be sure, but the Legislature knew what it was doing by designating a state institution like the University of California, since much of the work would be conducted on the University’s time by faculty experts. So, the Legislature was able to leverage the $500,000 into a much more valuable product.
Section 3(d) of the bill required that the evaluation be peer reviewed and subject to public hearings. In a key provision, Section 3(e) of the bill required whoever was Governor when the study and hearings were completed to make a determination. First, as you can see on the screen, that determination was to be based solely on the conclusions and recommendations of the study and the testimony presented at the public hearings. The Governor could not consider other sources of information, only the study and the testimony.

And second, the determination had to be one of two listed alternative possibilities. The two alternatives specified, as can you see, one, and I quote, that on balance, there is no significant risk to human health or the environment of using MTBE in gasoline in this state, unquote. Or two, and I will quote again, that on balance, there is a significant risk to human health or the environment of using MTBE in gasoline in this state, unquote.

There were no other options. In essence, the bill provided the Governor with a binary choice, if you will. Either MTBE did not pose a significant risk or it did. And whoever was Governor, 10 days after the public hearings were completed, had to choose one or the other determination. It wasn't a free choice, remember, since it had to be based solely on the report and
There were consequences, depending on which determination was made. As can you see on the screen, Section 3(f) of the bill required that if the Governor made the second determination, that

MTBE did pose a significant risk, then, and I quote, notwithstanding any other provision of law, the Governor shall take appropriate action to protect public health and the environment, unquote. Now, it's true, as Mr. Dugan stated in reply to Professor Reisman's question yesterday, that Section 3(f) did not specify exactly what action the Governor had to take. Mr. Dugan suggested that he could have gotten by by doing as little as banning two-cycle engines on surface water. But that option is not even mentioned in the bill. The only specific possible course of action mentioned in Senate Bill 521 was to ban the use of MTBE in gasoline.

As can you see on the screen, the very next section of the bill, Section 4, provided that, quote, If the sale and use of MTBE in gasoline is discontinued pursuant to subsection F of Section 3, unquote, the state under subparagraph A was prohibited from relaxing requirements of MTBE and was required to notify the EPA under subsection B.
Thus, discontinuance of MTBE use was the only action mentioned in the entire bill. So, that's the first thing that the state did in response to the MTBE contamination problem. It passed Senate Bill 521. That bill essentially prewired the public policy decision on how to handle MTBE. First, an objective study and hearing, and then if the study and hearing gave MTBE a thumbs up, the Governor could certify no significant risk. But, if the study and testimony gave MTBE a thumbs down, the Governor had no real choice. He had to certify that there was a significant risk. And in that case, he also had to take action. And the only action contemplated anywhere in the bill was a ban on MTBE use. And what is even more significant, this preprogrammed, almost mechanical process either—leading either to no action or to a ban on MTBE was the unanimous public policy choice of the California Legislature and that supposedly antiethanol Governor, Pete Wilson.

Well, the study was conducted, and in November 1998 the University of California issued the report required by Senate Bill 521. The UC report comprised 17 independently prepared papers, filling five volumes and spanning more than 600 pages. More than 60 highly credentialed
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researchers authored the report.

PRESIDENT VEEDER: Just before we move on with the report, can I take you back to the passage you read in Section D, that's Section 2(d) of the Senate Bill. And if you have it before you, but I can read out the relevant words. It was the deadline of the 1st of January 1999, the university shall submit a draft report, and then upon receiving the draft report, the Governor shall take all of the following actions. Under (d)(1) he transmits the draft report, without any alteration, to two institutions for comments, and then he issues a notice of intent to hold two public hearings.

And if you look at the end of that paragraph two, the draft report apparently becomes a report, and then in E the Governor has to act solely upon the assessment and report submitted pursuant to the previous provisions.

There's nothing in this particular bill to explain how the draft report becomes a report; is that right? Or am I missing something?

MR. CLODFELTER: I believe that you're correct, that the bill is silent on that, but I believe that this process is known, and I do not believe that the report was changed after the assessment.

PRESIDENT VEEDER: We could come back to it later. I don't want to interrupt you.
MR. CLODFELTER: I will just note one thing. It's actually in Section 3(d) as opposed to Section 2(d).

Ms. Menaker will give an answer to your question.

MS. MENAKER: Thank you. After the draft report was issued, then it could be revised based on the peer review comments received, and also based on comments received during the public testimony.

MR. CLODFELTER: To continue, Mr. President, the conclusions of the 60 highly credentialed researchers in the UC report were firm. First, MTBE's pollution-reducing benefits had pretty much run their course. Reports stated, as you can see on the screen, MTBE and other oxygenates were found to have no significant effect on exhaust emissions from advanced technology vehicles. So, as the technology of automobile engines advanced, the additives had less and less pollution-reducing benefits.

The report concluded that the use of MTBE in gasoline poses significant risks and costs due to water contamination, and found that continued use of MTBE would increase the danger of water contamination. It's worth considering this finding in full, and so with your indulgence, I'm going to take the time to read that entire significant
finding, which you can see on the screen as well. There are significant risks and costs associated with water contamination due to the use of MTBE. MTBE is highly soluble in water and will transfer readily to groundwater from gasoline leaking from underground storage tanks, pipelines, and other components of the gasoline distribution system. In addition, the use of gasoline containing MTBE in motor boats, in particular those using older two-stroke engines, results in the contamination of surface water reservoirs. The extent of MTBE contamination is discussed in more detail in Section 5, but it is clear that we are placing our limited water resources at risk by using MTBE.

MTBE has been detected in several water supply systems, which have shut down the contaminated sources, resorting to alternative supplies or treatment. Since both groundwater wells and surface water reservoirs have been contaminated, alternative water supplies may not be an option for many water utilities. If MTBE continues to be used at current levels and more sources become contaminated, the potential for regional degradation of water resources, especially
groundwater basins, will increase. Severity of water shortages during drought years will be exacerbated.

The report also found that the cost of treating MTBE-contaminated water resources would be enormous. And again, I would like to read the entire finding, which you can see on the screen.

The cost of treatment of MTBE-contaminated drinking water sources in California could be enormous. In addition, the cost of remediating underground storage tank and pipeline leaks and spills could be on the order of tens to hundreds of millions of dollars per year. There are other significant costs to the economy, which may be in the tens of millions of dollars per year, in terms of monitoring of surface water resources for MTBE and potential losses in recreational income to surface water reservoirs that ban or restrict the use of gasoline-powered boats. We believe that the use of either nonoxygenated reformulated gasoline, or ethanol as an oxygenate in CaRFG2 would result in much lower risk to water supplies, lower water treatment costs in the event of a spill of either of these alternative RFG formulations, and lower monitoring costs.

These were the report's principal findings. The recommendations of the report were equally as straightforward. To remedy the problem, the report recommended the phasing out of the use of gasoline-powered boats.
of MTBE in gasoline over the course of several years. As you can see on the screen, the report recommended rather than an immediate ban on MTBE, we recommend consideration of phasing out MTBE over an interval of several years.

In other words, the, quote, thorough and objective evaluation, end quote, required by Senate Bill 521, on the basis of which the Governor was required to act, stated unequivocally that the

answer to the real and threatened problem of MTBE use was to end its use as an oxygenate additive in California gasoline.

The report had something to say as well about switching to ethanol in lieu of MTBE. As Mr. Dugan pointed out yesterday, the report's ninth recommendation, which we have put up on the screen, urged caution and further study before substituting ethanol for MTBE in California gasoline. It did not recommend the substitution of ethanol for MTBE. It did not call for the establishment of a California ethanol industry.

In fact, the report's second recommendation called for the state to obtain a waiver of the Federal requirement that RFG gasoline sold in California have an oxygen content, a waiver that would allow the use of RFG gasoline without ethanol or any other oxygenate additive.

Public hearings were held on the draft UC
At those hearings, the report's authors made presentations and government officials and public citizens had an opportunity to ask questions. Members of public also testified at the hearing, several of them relating their firsthand experiences with the negative effects of MTBE contamination. In all, a majority of those testifying supported the report's conclusions and recommendations.

It should also be noted that the report was peer-reviewed, as required by the U.S. Geological Survey and the Centers for Disease Control. Both agencies reviewed the report favorably.

Now, what happened next could not have been a surprise. You didn't have to be a weather man to know which way the wind was blowing, and Senator Burton did not have to be a seer to have foreseen the upcoming action to ban MTBE use. It was essentially preordained. Senate Bill 521, signed by ethanol opponent Pete Wilson, directed the Governor to follow the lead of the report and the hearings. And the ethanol averse report itself required a determination of significant risk. And the bill and the report together left no serious
alternative to banning MTBE use.

So, in the face of the UC report and the hearings, Governor Gray Davis took action as Senate Bill 521 required. A few weeks after the hearings, Governor Davis issued the 1999 Executive Order. First, the Executive Order made the determination, as it had no choice but to do based on the UC report and public testimony, that there was on balance a significant risk to the environment from using MTBE in California gasoline.

Second, it directed the responsible California agencies to develop a timetable for the removal of MTBE from gasoline. The Executive Order directed that MTBE be discontinued as soon as it was feasible, but no later than the end of 2002.

Third, as the UC report recommended should be done, the Executive Order required state agencies to seek a waiver from the EPA of the Federal RFG oxygenate requirement so that California could use gasoline that met air quality standards without using any oxygenate, including ethanol.

Finally, the order directed state agencies to prepare reports on the effects of using ethanol as an oxygenate additive in gasoline.

Subsequently, as shown on the screen, as you know, the state did seek a waiver from the EPA, as the UC report recommended and as Governor Davis directed. The Legislature also took further action
after the UC report was issued.

In October 1999 the Legislature passed, and Governor Gray Davis signed into law Senate Bill 989. That bill imposed new requirements to prevent leaks from underground storage tanks that were more stringent in many respects than Federal regulations. And it also required the responsible state agencies to develop a timetable for the removal of MTBE from gasoline at, quote, the earliest possible date, unquote.

In response to this legislation, in June 2000, the California Air Resources Board promulgated the reformulated gasoline Phase III regulations, prohibiting the use of MTBE in gasoline after December 31st, 2002.

The regulations also required reductions in sulfur and benzene levels in California gasoline. And in 2001, EPA denied California's request for the oxygenate waiver.

In response, Governor Davis brought an action in U.S. Federal court to challenge that denial. In March of 2002, he also issued another Executive Order, this one postponing the MTBE ban for one additional year. The order noted that insufficient ethanol supplies would lead to a gasoline shortage if the ban went forward as scheduled at the end of 2002. The California reformulated gasoline Phase III regulations were
amended accordingly to postpone the ban until the end of 2003.

And then again, as can you see on the screen, last year the Ninth Circuit Court of Appeals overturned EPA’s denial of California’s waiver request, ruling that it was an abuse of discretion not to grant the waiver. And California has since renewed that request, which is now pending.

Finally, the ban on MTBE use in California gasoline took effect at the beginning of this year. These, in short, are the undisputed facts, and the story they tell about the ban on MTBE use is impossible to reconcile with the story Methanex would have you believe. Methanex’s theory of a conspiracy to harm foreign methanol producers is contradicted at every turn by these facts, by the real and widespread and persistent contamination of California water resources by MTBE, by the fact that the California Legislature passed Senate Bill 521 unanimously, and by the fact that that bill left whoever was serving as Governor with little choice but to do exactly what the 1999 Executive Order did, in fact, do.

Methanex’s theory of a conspiracy to
advance the cause of ethanol is also contradicted by these facts, by the fact it was Governor Davis's antiethanol predecessor who signed that bill into law, by the fact that in recommending an MTBE ban, the UC report also cautioned again a switch to ethanol, by California's request for a waiver of the EPA's oxygenate requirement for RFG gasoline, and by California's continued pursuit of that waiver in court, and even now after the MTBE ban has gone into effect.

The real story of the MTBE ban is really quite simple. Just seven years after MTBE came into widespread use, California found itself suffering serious problems with public water contamination. It commissioned a major study of those problems and was told by objective and highly respected experts that the way to solve them was to end the use of MTBE in gasoline. California did this. Even as it sought to be relieved of the Federal requirement to use any oxygenate additive at all, including ethanol, in RFG gasoline.

We will have a lot more to say about the proven facts in the case as we present our case-in-chief in greater detail, but unless you have questions now, I propose to turn the chair over to Mr. Bettauer, who will introduce our presentation on the legal issues in the case.

PRESIDENT VEEDER: We just have one question, and I wonder if you could help us about

And if you look at the third preamble which refers to the findings and recommendations of the UC report and public testimony, it continues, and regulatory agencies, while MTBE has provided California with clean air benefits because of leaking underground fuel storage tanks, MTBE poses an environmental threat to groundwater and drinking water.

Now, at a later stage, could you just help us identify what are the findings and recommendations of the regulatory agencies there described.

And the other question, you heard yesterday Mr. Dugan make a point that this was an Executive Order based upon an environmental threat. And indeed, if you look at the fourth paragraph, the certification or the finding by the Governor, and this is the passage in quotes, is a reference to the significant risk to the environment from using MTBE in gasoline in California, and not to the other phrase we saw in the Senate Bill health.

First of all, as regards to the latter, do you accept that there is this distinction?

MR. CLODFELTER: Mr. President, we doubt that there is a mutually exclusive distinction, and environmental concerns subsume many public health
concerns, so we would not read too much into the certification for environmental purposes and all as excluding concern for the health effects. With respect to your first question, I believe the reference to regulatory agencies is the reference to the peer review agencies which were required to review the draft report and make comments. But I also know that state agencies appeared at the public hearings and offered testimony, so that could be merely redundant of the reference to public testimony. The content of those recommendations we will summarize and get to you in response to your question later, if that's okay.

PRESIDENT VEEDER: Thank you. It's been suggested by my colleagues this would be a good time to break for coffee, but you are the masters of the situation. Will this be a good time or a bad?

MR. CLODFELTER: It's a good time.

(Brief recess.)

PRESIDENT VEEDER: Let's resume.

MR. BETTAUER: Thank you. Mr. President, members of the Tribunal, you've now heard Mr. Taft's introduction and Mr. Clodfelter's summary of the facts. Since the United States will have a number of presenters on each of the major
topics, I will intervene from time to time to draw this together and to give you a brief overview of how the parts of our presentation fit together. Tomorrow, I will do the same at the beginning of our presentation, and then we'll conclude the U.S. first round presentation.

We now turn to our presentation on jurisdiction. Our presentation will first address the issue under Article 1101(1) left open by the First Partial Award, whether Methanex has met the requirement of that award to show that the ban of the sale of California gasoline containing MTBE relates to methanol producers like Methanex.

We will divide our treatment of this issue into three parts. First, Mr. Legum will take the floor. He will show that there is no evidence to suggest that California intended to harm methanol producers by banning MTBE. He will also demonstrate that methanol does not compete with ethanol in any sense relevant here.

Second, Mr. Pawlak will address the scientific evidence in this case. He will show that contrary to Methanex's arguments, the scientific evidence supports California's action. The record cannot sustain Methanex's contention that science was a pretext for harming methanol producers.
At this point, it will likely be time for the lunch break.

The third point, the third part of our presentation on this issue will be given by Ms. Menaker. She will show that contrary to Methanex’s contention, the record does not support Methanex’s suggestion that the ban was intended to provide a gift to the ethanol industry. Instead, California’s intent was precisely what it said it was, to protect the state’s groundwater resources from a contaminant that made water undrinkable.

At the end of those three parts, I will return to provide a brief conclusion to this part of the presentation.

Mr. President, I now request that you call on Mr. Legum.

PRESIDENT VEEDER: Thank you very much, and we do, indeed, call upon Mr. Legum.

MR. LEGUM Mr. President, members of the Tribunal, I will now begin the United States’s presentation on the jurisdictional issue left unresolved by the First Partial Award in this case, whether the ban of MTBE relates to Methanex and its investments, as required by NAFTA Article 1101(1). My remarks this morning will be divided into three parts. First, I will briefly review the holdings of the First Partial Award and the limited jurisdictional issue that the Award left for
resolution in this phase of the proceedings. I will demonstrate that under the First Partial Award, only a showing that the ban of MTBE was intended to harm or at least address methanol producers like Methanex could establish the legally significant connection between measure and investment that the Tribunal found to be lacking.

Second, I will examine the evidence of record presented by the disputing parties on this subject. I will demonstrate that the evidence in no way suggests, much less establishes, that California intended to get at methanol producers by banning MTBE.

Finally, I will address the latest version of Methanex's argument that methanol competes with ethanol in the market for oxygenate additives in California. I will show that the Tribunal already rejected that argument in its First Partial Award and that in any event, Methanex has failed to prove any such competition.

I turn now to my first topic, a review of the jurisdictional issue that the First Partial Award left unresolved. Article 1101(1) of the NAFTA, and this is my first slide, although I suspect that everyone in this room has memorized it by now, that Article delineates the scope of the investment Chapter as follows: Quote, This Chapter applies to measures adopted or maintained by a party relating to investors of another party and
investments of investors of another party in the territory of the party. The First Partial Award found that the measures at issue on their face did not relate to Methanex or to its investments. The measures banned the sale of California gasoline containing MTBE. Methanex does not produce or market California gasoline. It does not even produce or market MTBE. Instead, it makes methanol. While, as the First Partial Award noted, methanol is a feedstock for the production of MTBE, this fact was not sufficient to establish that the ban of MTBE related to methanol producers as required by Article 1101(1). But, as the Tribunal noted, Methanex also alleged that even though on its face the measures related only to MTBE, California, according to Methanex, secretly intended to harm methanol producers and marketers by banning MTBE. The Tribunal held that if Methanex could establish that the ban of MTBE was really intended to address methanol producers, even though this was not apparent on the face of the measures for the facts alleged, then Methanex could establish that the ban related to it and its investments.
I'll turn to my next slide. Only this specific showing could establish jurisdiction in this case, as the Tribunal unambiguously held in the operative part in the First Partial Award. Only, quote, certain allegations relating to the intent underlying the U.S. measures could potentially meet the requirements of Article 1101(1).

And as the Tribunal explained in its September 25, 2002, letter to the disputing parties, which is my next slide, the Tribunal, and I quote, has already decided that its jurisdiction can exist only in respect of that part of the claim alleging an intent underlying the U.S. measures to benefit the U.S. ethanol industry and to penalize foreign methanol producers such as Methanex, closed quote.

I wish to highlight--

PRESIDENT VEEDER: Just before you move on, what paragraph of that is in our letter?

MR. LEGUM: It appears at the bottom of the slide that you have. It looks like paragraph seven, from here.

PRESIDENT VEEDER: Proceed.

MR. LEGUM: I wish to highlight that in rendering this ruling, the First Partial Award made clear that the showing required was one concerning intent to address methanol producers. The Award
made clear in its discussion at paragraphs 153 to
157 that a showing of intent to address or harm
MTBE producers and benefit ethanol producers would
not be sufficient. The proof required under the
Award, therefore, is proof that the intent
underlying the ban of MTBE was to address methanol
producers.

Mr. President, members of the Tribunal,
Methanex has not remotely come close to the
required showing. Reviewing the evidentiary

materials offered by Methanex on the measure's
supposed intent to harm methanol producers does not
take long, for there is little of it. Methanex
offers five pieces of evidence that, according to
it, show a link between the measures and Methanex
or methanol producers as opposed to MTBE or
ethanol. This is, under the First Partial Award,
the evidence on which Methanex's case hinges.

To review the materials highlighted by
Methanex as supporting this point is to confirm
that there is no substance to this allegation, and
it is to that task that I now turn.

The first material that Methanex offers to
show a specific intent to address methanol
producers is the testimony of Robert Wight.
Mr. Wight is a governmental affairs officer for
Methanex. In his November 2002 statement, he
recounts a conversation that he says took place in
years before the date of Mr. Wright's statement, unidentified persons recounted to him a conversation they allegedly had with Senator John Burton of the California Senate.

In that conversation, Mr. Wright says they said Senator Burton said that he recommended shorting Methanex's stock. The Senator also supposedly gave his views on how likely it was that the Governor would not find MTBE to be a risk to drinking water, but that statement on MTBE could not show an intent to address methanol producers in any event.

Mr. Wright's testimony is entitled to no weight for several reasons. First, it is hearsay upon hearsay. International tribunals have repeatedly declined to rely upon such statements, as the United States demonstrated in paragraph 127 of the Amended Statement of Defense.

Second, although Methanex in its reply at paragraph 37 attempted to shore up Mr. Wright's testimony by offering two unauthenticated memos written by unidentified persons to unidentified persons a few days after the supposed conversation, neither memo contains any reference to Senator Burton's supposed remark about shorting Methanex.
Far from confirming the reliability of Mr. Wright's recollection of this conversation about a conversation four years before, the memoranda raised more questions about it.

Now, yesterday during the course of Methanex's presentation, the President asked the question about the word "your" in the two-word phrase allegedly uttered by the Senator. The President asked whether the use of that word in that phrase could suggest a focus on Methanex or methanol, and Mr. Dugan essentially replied yes. Well, that does not appear to be the way that the people who were there perceived that supposed remark, at least according to the memoranda from unidentified persons that Methanex has supplied.

This is my next slide from the first memorandum, the one that Methanex referenced yesterday in its presentation. That person in that memorandum said, quote, Burton was perhaps the most candid legislator to date, suggesting in only two words that a phaseout was inevitable, closed quote. This statement suggests that the Senator provided a view on the likelihood of a ban, not on its impact on MTBE producers, much less on methanol producers. My next slide is the conclusion of the second memorandum that Methanex supplied. Quote, I think John Burton's comments accurately reflected
the general belief in the Legislature that MTBE will be phased out within a fairly quick time frame, closed quote.

Again, nothing in this statement suggests that the impact of the ban on producers of MTBE or methanol was the thrust of the Senator's remarks. The supposed contemporaneous notes do not corroborate Mr. Wright's statement.

My third point about Mr. Wright's statement is that it supplies no context or foundation for Senators' supposed statement about shorting stock. Notably, it does not suggest that

the Senator understood what Methanex was, or, notably, that it produced methanol rather than MTBE.

Fourth, even taken at face value, Senator Burton's supposed remark about shorting does not show an intent to address methanol producers. At best, the statement would suggest an understanding that a ban of MTBE might have an impact on methanol producers like Methanex. As the First Partial Award makes clear, however, there is a world of difference between a measure that affects a person and a measure intended to harm or address a person.

Finally, and in any event, Senator Burton was but a single government actor in a very large government. He was one of 35 members of the California Senate. As the Tribunal observed in its First Partial Award, and this is my next slide,
PRESIDENT VEEDEER: I'm just querying whether Senator Burton was an actor at all. If you go to page 28 of Mr. Clodfelter's charts, where he has the timeline running from SB521 in 1997, to the date when the ban went into effect, I think Senator Burton was in the Senate and presumably voted on SB521 with his colleagues. But after that did he take any further part in the events that followed, as a legislator?

MR. LEGUM: The next legislative action was Senate Bill 989, which was enacted, my recollection is, in November of 1989, but I could be off by a few months.

PRESIDENT VEEDEER: I see. So, he would have taken part in--

MR. LEGUM: Did I say '89? '99.


MR. LEGUM: Yes, and I must say that we have not gone back to looked at the records to see whether he voted for or against that bill. There were a few dissenting votes for that bill.

PRESIDENT VEEDEER: We can take it he was a still a member of the California Senate in November
As the Tribunal observed in the First Partial Award, it does not necessarily follow that the views of a single governmental actor can be attributed to the entire government. The evidence must, as the Tribunal noted, prove such a thing. Even if Senator Burton did think it wise to short Methanex stock in early 1999, nothing suggests that he influenced any relevant government body or officer to act in accordance with that view.

In sum, Mr. Wright's statement does nothing to advance Methanex's case.

The second piece of evidence that Methanex relies upon is a single sentence published by the U.S. Federal Environmental Protection Agency on page 68,350 of the 1993 volume of the Federal Register. The text in question is my next slide.

The publication proposed a rule that would have required that 30 percent of reformulated gasoline contain oxygenate additives produced from renewable resources—renewable sources. U.S. EPA predicted in 1993 that this proposed regulation would have an impact on methanol producers, and there is the statement that Methanex relies on.
Revenues and net incomes of domestic methanol producers and overseas producers of both methanol and MTBE would likely decrease due to reduced demand in prices.

This piece of evidence does nothing to show California's intent in banning MTBE over half a decade later. First, nothing suggests that California officials were even aware of this sentence in this Federal notice from years before the decision to ban MTBE. This Federal statement says nothing about California's intent.

Now, in its motion on evidentiary matters, Methanex argues that this is a conclusive admission irrevocably binding on the United States. It is nothing of the kind, and the authorities Methanex cites to support the proposition do not support it.

Under U.S. law, which Methanex references in its motion, a statement of a party opponent is admissible evidence under an exception to the hearsay rule. All this means is that it may be considered by the trier of fact. It does not mean that the statement has any special significance beyond its ordinary context.

The two international authorities referenced by Methanex address very different kinds of statements, statements made in the realm of foreign relations by the President or the Foreign Minister of a country. That is not what we are talking about here.
Putting it a slightly different way, the United States, as a state in international law, may be responsible for the acts of its subnational government units, but that does not make the intent or knowledge of one governmental unit attributable to another unit. The issue here is California's intent. This U.S. EPA statement sheds no light on California's intent.

Second, as with the supposed Burton statement, all this statement does is show an understanding that the proposed regulation might have an impact on methanol producers. It does not even suggest that the Federal Government's purpose was to address methanol producers, much less that the California government had such a purpose. Indeed, Methanex's reliance on this sentence highlights a fundamental defect in Methanex's approach. It's equating foreseeability with intent. It may well be foreseeable, for example, if I have a large dinner party at a restaurant owned by a friend, that that will have a beneficial impact on my friend's restaurant and a detrimental impact on other restaurants of its class in the city. That does not mean, however, that I intend to act to the detriment of other restaurants in the city by having dinner at my friend's restaurant. Foreseeability may be necessary to a finding of
Moreover, as both of the submissions amicus curiae here have pointed out, it is good public policy for governments issuing regulations to try to assess all possible consequences before adopting a measure. Equating foreseeability and intent, as Methanex suggests, could chill this useful practice. Methanex's approach fails on policy grounds as well.

The fourth—-the third and fourth pieces of evidence Methanex offers is a transcript of a 1992 interview that Dwayne Andreas gave on television and a copy of a 1998 letter by Doug Vind. I note that the Doug Vind letter is one of the pieces of evidence admitted by the Tribunal de bene esse subject to further order by this Tribunal.

Each of these materials briefly refers to foreign methanol production, albeit in different contexts. Dwayne Andreas was the Chairman of Archer Daniels Midland, ADM, and is a relative of Alan Andreas and Marty Andreas. Those two people were present at the August 1998 dinner with gubernatorial candidate Davis. Doug Vind is the son of Richard Vind, who was also present at that dinner.

Here is what Methanex's argument is.
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Methanex argues based on these two statements, that, quote, it is overwhelmingly likely, closed quote, that at the August 1998 dinner with Gray Davis, Dwayne Andreas and Richard Vind talked about methanol and inevitably described it as a foreign product. This argument is ill conceived for several reasons.

First of all, neither of the speakers whose prior statements Methanex references were even present at the dinner. Dwayne Andreas was not there. Doug Vind wasn't there, either.

Methanex is asking the Tribunal to speculate that because these relatives of the people who were there at the dinner had made certain statements on two isolated occasions before those people who were at the dinner must have said something similar. This case, however, must be decided on the basis of the evidence, not on speculation.

The evidence that is of record, three witness statements by people who were there, unanimously confirmed that there was no discussion of Methanex or methanol at that dinner.

Now, yesterday Methanex also showed slides of statements concerning imported methanol by various persons or organizations who also were not at the August 1998 dinner. Citizen Action, which was Tab 53 of the presentation yesterday, they weren't at the dinner. Representative Jim Nussle
of Iowa—that's Tab 50—he wasn't there. Senator Tom Daschle of South Dakota, Tab 51, he wasn't at that dinner either. The record shows no connection between any of these people and the California measures at all. These additional statements add nothing.

My second point is that in any event, Methanex's whole premise concerning the August 1998 dinner is misconceived. Methanex's premise seems to be that if constituents or supporters tell an elected official their views on a subject, the official necessarily becomes hypnotized and is compelled to act in accordance with the views expressed. This premise is supported neither by the record nor by common sense. Elected officials are constantly exposed to a wide range of views on a variety of subjects. The mere fact that an official hears any particular point of view says nothing about whether the official will act in reliance on those views.

Thus, the record does not support Methanex's allegations that methanol was discussed at the dinner, but in any event, the record does not support the underlying notion that a candidate like Mr. Davis is necessarily brainwashed by views expressed by a supporter or constituent. I would note that Andrea Menaker will have more to say on the subject of the 1998 dinner when she addresses...
Methanex's allegations of an intent to benefit

ethanol.

I'd now like to turn to the final piece of evidence that Methanex relies upon, to support its claim that California decision makers had methanol in mind in banning MTBE. This is the conditional prohibition of about a dozen listed compounds subject to thorough testing for their impact on the environment. One of the compounds listed was methanol. Methanex argues that this separate conditional prohibition shows that the absolute ban of MTBE was intended to address methanol. The record does not support this argument.

The Tribunal will recall that California's actions here had essentially four components. First, California thoroughly tested MTBE and found it to pose a serious threat to the state's drinking water resources. It, therefore, banned MTBE. That ban is the measure alleged here to breach the NAFTA.

Second, in order to ensure that it did not repeat the mistake made by using MTBE without sufficient testing in advance, California mandated that no other oxygenate could be added to its gasoline without the same thorough testing and
evaluation that MTBE had undergone.

Third, California thoroughly tested ethanol and found that ethanol did not pose the threat that MTBE did. It, therefore, did not ban ethanol.

And finally, California sought a waiver of the Federal oxygenate requirement so that clean-burning gasoline not containing either MTBE or ethanol could be used. It is California's second action, the conditional prohibition of other oxygenates, that Methanex points to as evidence that California banned MTBE in order to get at methanol producers.

I will make two points concerning this prohibition. First, contrary to what Methanex asserted for the first time yesterday, this prohibition does not establish the legally significant connection between measure and investment that is otherwise lacking here. Second, the prohibition does not show that California intended to harm methanol producers by banning MTBE.

My first point, the conditional prohibition is not the measure that is at issue in this case. The prohibition did not exist when Methanex submitted its claim to arbitration. It did exist in general form that is, without the definition that specifically listed 11 compounds. It did exist in general form at the time when
Methanex submitted its amended statement of claim, but Methanex made no reference to it. The amendment, that's the one that provided the definition that specifically listed the 11 compounds, that was not in force when Methanex submitted its second amended statement of claim. Methanex has asserted no claim in this case based on the conditional prohibition, and in its reply Methanex made clear that the only measure at issue for purposes of Article 1101(1) is the ban of MTBE, and I would refer the Tribunal to the discussion on this subject in paragraphs 199 to 202 of our rejoinder.

If Methanex had asserted a claim based on the conditional prohibition, that claim would be barred for the reasons set forth in our Amended Statement of Defense at part six, which deals with the new jurisdictional objection, which the Tribunal will recall we withdrew in the rejoinder on the understanding that Methanex was no longer asserting that it had a claim to assert based on the conditional prohibition.

In sum, the question of whether the conditional prohibition relates to Methanex is not before the Tribunal since there is no claim asserted based on that prohibition. The only question presented is whether the conditional prohibition of these 11 compounds suggests that...
California's purpose in banning MTBE was other than what it said it was, and this is my second point: The record supports no such suggestion.

The record clearly establishes that the purposes of the MTBE ban and the conditional prohibition were distinct. California banned MTBE because scientific research showed that it was a serious threat to drinking water resources. It conditionally prohibited the use of these other compounds because it did not know whether they posed a risk to public health or the environment, and did not wish to take the chance of using them without testing them first. The purpose of the conditional prohibition in no way suggests that California banned MTBE to get at methanol producers.

Second, the record is clear, and indeed uncontradicted, as to California's reasons making those 11 compounds subject to the conditional prohibition. This is my next slide. The reason was simple. Those are the compounds listed in the industry standard testing method that California relied upon to detect the presence of relevant compounds in gasoline. Methanol is included among
the compounds listed, as is ETBE, an ether made from ethanol, and a number of other ethers and alcohols that had not been thoroughly tested by California.

My next slide shows that--

MR. DUGAN: Is there any evidence in the record that supports that last statement? I know you cited to this list of compounds, but the stuff about the previous stuff, is there any evidence in the record? If there is, I would just like the citation to it, please.

MR. LEGUM: The citation to the record for what proposition?

MR. DUGAN: The standard that this was an industry standard for detection.

MR. LEGUM: Yes, Amended Statement of Defense, paragraph 149, note 267, which quotes 14 JS Tab 19 at 540.

MR. DUGAN: I'm sorry, could you say that one more time, because it's not on this slide.

MR. LEGUM: Amended Statement of Defense, paragraph 149, note 267, quoting 14 JS, Tab 19, at 540.

MR. DUGAN: Thank you.

MR. LEGUM: Of the compounds listed, and what we have on the screen is the list of 11 compounds that were included in the California conditional prohibitions definition, of those compounds, only four could legally be added to
gasoline under Federal law to satisfy the oxygenate requirement. Those compounds are the three ethers and TBA, which is tertiary butanol.

Again, nothing in this background suggests that the intent behind the MTBE ban was to harm methanol producers.

And finally, the inclusion of methanol in that list of conditionally prohibited compounds had no impact on methanol producers. This is because methanol cannot legally be used as an oxygenate additive to gasoline under Federal law, as Jim Caldwell established in his undisputed witness statement. Nor can methanol practically be so used in today's automobile fleet.

Intent to harm methanol producers by a different ban can hardly be inferred from a conditional prohibition that had no impact on methanol producers whatsoever.

Mr. President, members of the Tribunal, that is it. We have just reviewed all of the evidence offered by Methanex specifically to show that California intended for the MTBE ban to harm methanol producers. Just to recap, we reviewed Robert Wright's uncorroborated double hearsay statement that California Senator John Burton told unidentified persons to short Methanex's stock. We examined the single line in a 1993 U.S. EPA publication that predicted an impact on methanol
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producers from a different regulation proposed by

U.S. EPA at that time.

We considered Methanex's suggestion that

it was inevitable that methanol was discussed at

the August 1998 dinner because two relatives of

some of the persons at the dinner had once made

statements about methanol in the past. And we

reviewed the conditional prohibition of the use of

untested oxygenates as evidence of a secret intent

behind the MTBE ban.

All of the rest of Methanex's evidence

either deals with ethanol or with MTBE. My

colleague, Andrea Menaker, will address that

evidence in a little while, but my point here is

that none of that evidence addresses either

methanol or Methanex. It therefore cannot, by

definition, supply the showing of intent to address

methanol producers or Methanex required by the

First Partial Award. The United States

respectfully submits that the evidence we have just

reviewed does not even begin to overcome the

presumption of regularity of governmental acts that

attaches to the California measures as a matter of

international law. This failure of proof alone is

sufficient to compel dismissal of Methanex's claims

in their entirety.
Unless the Tribunal has any questions, I would now like to turn to my second main point:

Methanex errs in suggesting that even though it has no direct evidence that California intended to harm methanol producers, the Tribunal should consider its evidence on ethanol relevant because ethanol and methanol compete as products in some sense relevant here. I will show that this suggestion by Methanex fails on legal and factual grounds.

First, I will show that this assertion of competition is no different from that originally pleaded by Methanex and rejected by the Tribunal in the First Partial Award. I will also demonstrate under this head of argument that the holdings of the First Partial Award are final and binding and not subject to reconsideration.

Second, I will demonstrate that the record does not show the competition Methanex alleges in any event.

Before starting, however, it's useful briefly to recall the evolution of Methanex's allegations of competition in these proceedings.

This is my first slide on this subject. A Keystone of both Methanex's original Statement of Claim and its Amended Statement of Claim was that methanol was sold for use as a feedstock in the production of MTBE.

As my next slide shows, similarly
Methanex's allegations of competition, however, were based entirely on methanol's status as a feedstock for MTBE production. It did not dispute that MTBE and ethanol were the products that directly competed with each other in the market for additives to California gasoline. My next slide shows the Tribunal recognized these undisputed facts in the First Partial Award. It recognized that, quote, Ethanol is an oxygenate that competes directly with MTBE, closed quote, whereas methanol is a feedstock for MTBE, closed quote. These were among the allegations that the Tribunal assumed to be correct for purposes of its jurisdictional analysis. Yet the Tribunal, and this would be my next slide, in the First Partial Award found these allegations to be insufficient to establish the legally significant connection required by Article 1101(1) between the MTBE ban, Methanex, and its investments. Instead, the Tribunal found that only part of Methanex's case could fall within its jurisdiction, that part relating to the intent underlying the MTBE ban.
Methanex's allegations concerning methanol and ethanol sales did not comprise part of the case that provisionally survived the First Partial Award. The Award thus necessarily rejected the notion that mere cross-elasticity of demand between a feedstock, like methanol, and a downstream product, like ethanol, could supply the legally significant connection that was otherwise lacking here.

Methanex, then in its fresh pleading for the first time asserted that methanol directly competed with ethanol. It asserted that methanol, like MTBE and ethanol, could be added to gasoline by itself to satisfy the oxygenate requirements of the Clean Air Act. We have on the screen a sample of one of Methanex's assertions to this effect. It suggested that methanol therefore competed directly with methanol and MTBE in the market for oxygenate additives to gasoline. The United States demonstrated in its Amended Statement of Defense and accompanying witness statements and expert reports that Methanex's new assertion was novel. The witness statement of Jim Caldwell in Volume 13 of the joint submission of evidence showed that methanol could not be legally used as an oxygenate additive in the United States under Federal law. The expert report of Bruce Burke in that same volume showed that because of its particular
properties, methanol could be not practically be added to gasoline to satisfy the oxygenate requirement in today's conditions. Messrs. Burke and Caldwell demonstrated that there was, and could be, no competition between ethanol and methanol in the United States.

In the face of this showing, Methanex, in its reply, effectively withdrew its assertion of direct competition between ethanol and methanol. The reply no longer contends that methanol can be, quote, splash-blended or otherwise mixed into gasoline as an oxygenate additive in the United States.

The reply narrowed its contention on competition to one subcategory of the market, those integrated refiners in California that own gasoline refining, MTBE production, and gasoline distribution facilities. It posited that because such refiners would have previously bought some methanol as a feedstock for MTBE production and will now buy ethanol to add to gasoline, methanol and ethanol therefore compete.

Now, Methanex's reply attempts to blur this reality by arguing that methanol and ethanol are both just ingredients used in the manufacture of gasoline, but that is not what the record shows.
The record shows that there are two very different kinds of oxygenated gasoline in use in the United States today. One is gasoline containing MTBE. The other is gasoline containing ethanol.

To put it in simple terms, methanol may be, as a technical matter, part of the large class of chemicals classified as oxygenates, but you can't add it to gasoline. If you do at the levels required to satisfy the Federal oxygenate requirement, you will violate Federal law as shown by the witness statement of Jim Caldwell, and you will void the warranty of most cars on the market in the United States, as shown by the expert report of Bruce Burke.

The measures at issue here address gasoline containing a specific oxygenate. That oxygenate is MTBE. It is not methanol. Methanol's only role is as a feedstock for MTBE.

We thus find ourselves having gone full circle on Methanex's theory of competition. The theory of competition advanced in Methanex's reply is precisely the same as that advanced during the jurisdictional phase. It is also, as I have shown, precisely the same as that rejected by the Tribunal in its First Partial Award.

Given this state of affairs, it is perhaps not surprising that Methanex has requested the Tribunal to reconsider the First Partial Award for
the terms of that award squarely disallow Methanex's current argument on competition. I will now, therefore, briefly address Methanex's request for reconsideration.

PRESIDENT VEEDER: Just before you do that, can we raise a question as to how you see the nature of the exercise you've just gone through. If this were a jurisdictional phase, we would be looking at the Amended Statement of Claim for Methanex, the so-called fresh pleading, and adopting the approach that we outlined in the First Partial Award based upon the ICJ's decision in the oil platforms case. We would be making certain factual assumptions in favor of Methanex, and on the basis of those assumptions we might or might not assume and exercise jurisdiction in regard to the merits.

If we did assume jurisdiction on the basis of assumed facts on the basis of a pleading only, and we then got to the merits, we wouldn't then make a decision to unmake our decision on jurisdiction. The Tribunals tend, when they get to the merits, decide the cases on the merits.

Now, in the procedure we've had to follow in this case, what's the test on Article 1101? Do we look at the fresh pleading and make certain factual assumptions, or do we deal with it essentially on findings of fact, on evidence that we now have before us?
I will give a provisional answer at this time because I'd like to get the views of my colleagues on this question, but my understanding of where we are is that the Tribunal has joined the jurisdictional issue to the merits, and the Tribunal's decision will be based on evidence of record on this issue as it is on other issues; but I would like to visit that issue with my colleagues, and perhaps we will have a more educated answer after the lunch break.

On the subject of reconsideration, the United States's position on this subject is set forth in its letter of March 30, 2004. Under Article 32(2) of the UNCITRAL Rules, the Tribunal's award is final and binding and not subject to reconsideration, as the first slide shows.

Methanex's first argument in response is that Article 32(2) of the UNCITRAL Rules applies only to final awards, not to interim or partial awards. The United States demonstrated the error of that view at some length in its March 30 letter. I will only briefly recap our points here.

My next slide: Although paragraph one of Article 32 separately references the final award and interim interlocutory or partial awards, the
rest of the UNCITRAL Rules do not. By using the
generic term "the Award," Article 32(2) makes clear
that its terms encompass each of the species of
award referred to in Article 32(1).

Indeed, Methanex recognized that the First
Partial Award was an award within the meaning of
the UNCITRAL Rules by requesting interpretation of
it under Article 35(1). The text of Article 35(1)
is now displayed on the screen below that of
Article 32(2). Methanex's current position would
ascribe a different meaning to the same words, "the
Award," in different articles of the same rules.
Elemental principles of textual interpretation do
not support such an approach.

Moreover, the travaux preparatoires and
arbitral jurisprudence confirm that the UNCITRAL
Rules' reference to "the Award" includes partial
awards. Displayed on the screen is commentary on

the travaux for Article 32, which states that
paragraph one of that Article was included
precisely to make clear that the term "award" does
encompass partial awards, and the Iran-U.S. claims
Tribunal in the Ford Aerospace case expressly
addressed whether interim awards on jurisdiction
were final and binding within the meaning of
Article 32(2).

As shown in my next slide, the Tribunal
concluded that an interim award on jurisdiction,
Now, Methanex had an opportunity in its April 14th letter to address the points I have just restated from our March 30 letter. It did not. It made no response because there is no response.

Partial awards are clearly final and binding under the UNCITRAL Rules.

The argument that does get considerable attention in Methanex's April 14 letter is a different one, that the Tribunal has the authority to sit in judgment of a two-year-old challenge to one of its own members and reconsider the Award on the basis of Methanex's challenge. That argument fails, as a matter of law and fact.

First, the law. Methanex points to no provision in the UNCITRAL Rules authorizing other members of a Tribunal to address a challenge made to one member. The UNCITRAL Rules, in fact, provide precisely to the contrary. Rules grant in Article 12 the appointing authority an exclusive role in deciding such challenges.

And my next slide shows that, as Jacomijn van Hof notes in her discussion of the traveaux preparatoires to Article 12 in her commentary, quote, The underlying principle of this Article is that a neutral third party should decide a challenge, closed quote. In fact, the drafters specifically considered and rejected the notion...
that challenges should be decided by the other members of the Tribunal. Methanex's attempt to ascribe such a role to the members of this Tribunal is without support in the governing rules.

Second, contrary to Methanex's argument, the UNCITRAL Rules expressly provide that no negative inference may be drawn by the fact that an Arbitrator withdraws after a challenge. My next slide shows Article 11(3) of the UNCITRAL Rules. That Article, as is clear from the text, provides that no implication of acceptance of the grounds for the challenge may be entertained.

Third, Methanex's claim that Mr. Christopher was biased is without support in any--in fact. My next slide shows Methanex's argument. Quote, Mr. Christopher personally pitched a case to Governor Davis after this case had commenced, and Governor Davis personally decided, over the objection of his Attorney General, to award a lucrative representation to Mr. Christopher's firm, closed quote.

My next slide shows what the record shows in the form of Mr. Christopher's signed statement. Quote, I did not make a personal appeal to the Governor to obtain that representation for
O’Melveny over the opposition of the Attorney General, and, indeed, I have never spoken to Governor Davis about the case, closed quote. The competent evidence of record provides no support here, as elsewhere, for the charges Methanex advances.

Methanex makes two other arguments on consideration that I will address briefly. The first is based on a single paragraph in its fresh pleading of November 2002; that paragraph complained about the reasoning of the First Partial Award. It is now displayed on the screen in my next slide.

Note that the statement—note the statement which we have underlined that, quote, Methanex does not seek to relitigate that decision, closed quote. Methanex now contends that this paragraph was an objection, to use their words, that amounted to a request for reconsideration, even though no reconsideration was requested anywhere in that pleading.

My next slide shows Methanex’s argument quoted from their April 14 letter. I will pause for a moment to allow the Tribunal to digest it. Here is what they are arguing. Even though Methanex did not ask for reconsideration, even though the UNCITRAL Rules do not provide for reconsideration, and even though the very paragraph
that they rely upon expressly says they don't want to relitigate the First Partial Award, the Tribunal should have, sua sponte, divined that this single paragraph in their fresh pleading nonetheless was, in fact, an attempt to relitigate the Award and ruled upon it. And, they assert, the United States waived any objection by similarly failing to recognize that this single paragraph was a request for reconsideration.

Merely to state this argument is to reveal its lack of merit. It has become a familiar tactic for Methanex to blame the Tribunal or the United States for its own failure to press its case within the limits set by the governing Arbitration Rules and the Tribunal's order. The tactic is as regrettable as it is unmeritorious.

The final argument by Methanex in support of the Tribunal's authority to reconsider the First Partial Award is that neither disputing party supports the legal standard adopted by the Tribunal in that award. As the United States's rejoinder makes abundantly clear, however, it is the United States's view that the First Partial Award correctly states the law on Article 1101(1). We fully support the standard that was adopted.

There is, in sum, no support for Methanex's assertion that the Tribunal has authority to reconsider the First Partial Award. That award is final and binding. Its reasoning...
disposes of Methanex’s claim that methanol as a feedstock for MTBE competes with ethanol as an additive to gasoline. That claim, therefore, is without merit, as a matter of law.

Unless the Tribunal has any questions on the subject of reconsideration or the finality of the First Partial Award, I will move to my final point.

Methanex has, in any event, made no serious attempt to prove the competition it asserts between methanol or ethanol in a market for integrated refiners in California. The record notably is silent on a number of points essential to this assertion. First, the record does not establish that there are refiners in California that are integrated in the sense that the same company owns refineries, MTBE production facilities, and distribution terminals. What the record does show is that those--that both the physical structure of the California gasoline distribution system and its ownership structure are highly complex. There is no basis for assuming here what the record does not show.

Second, the record does not establish that there is a market with respect to any such integrated refiners in which methanol and ethanol
can be considered to compete in an economic sense. Notably absent here is the kind of comprehensive economic testimony that is familiar in those contexts, such as some competition law applications, where it may be appropriate to consider an upstream input for a product to compete with downstream finished products. It is difficult to take seriously Methanex's desire to engraft a competition law approach onto the investment chapter when that attempt is not accompanied by any supporting economic evidence.

Third, what evidence there is merely confirms that participants in the market view methanol as no more than a feedstock with gasoline containing MTBE and gasoline containing ethanol. The single unsigned, undated contract with one refiner that Methanex offers makes clear that the methanol to be sold was for use in Valero's, and I'm quoting the contract, production of or demand for MTBE in California, close quote. And the chart that Methanex offered yesterday at Tab 7 of its hearing book, the Tribunal will recall that it was the one with lines for methanol and ethanol that crisscrossed each other, that chart was based solely on data for MTBE and ethanol, on data for use of those two substances in California.

It is telling that Methanex--
ARBITRATOR REISMAN: Would you tell us that again.

MR. LEGUM: It was at Tab 7 of Methanex's hearing book yesterday.

The chart relied on data from a California governmental study of ethanol, which is in the record, and it also relied on a February 2004 document that is not in the record that is a California government document addressing MTBE use in California.

PRESIDENT VEEDER: Could you take your criticisms of this a little bit more slowly.

MR. LEGUM: Oh, sorry.

PRESIDENT VEEDER: No, no, it's helpful, but let's just look at Tab 7 that we had yesterday.

MR. LEGUM: I remember it fairly well.

PRESIDENT VEEDER: And it's entitled Binary Choice, and the red line is marked ethanol, but the blue line is marked methanol, not MTBE.

MR. LEGUM: That's correct. And if you look at the source for that information, the source is a study of ethanol, which is in the record, there is a record cite for that, and then there is a quarterly report on MTBE that is not in the record, but there are earlier versions of that same report that are in the record.

What Methanex did, as I understand it, is they said, well, methanol is used as a feedstock for MTBE, and there is roughly .34 units of
methanol for every unit of MTBE, so they've backed out from the figures for MTBE how much methanol would have been used as a feedstock to produce that MTBE.

As I was saying, Methanex relied on data for MTBE to arrive at this conclusion because it couldn't find the document, it seems, that shows

comparative data for methanol and ethanol use in the California gasoline market. That is because methanol and ethanol are not seen by participants to compete in that market.

Mr. President, members of the Tribunal, the U.S. rejoinder details a number of other ways in which the evidentiary record fails to support Methanex's claim of competition in the market for integrated refiners, but unless the Tribunal has any further questions, I would propose now to turn the floor over to Mr. Pawlak, who will address the scientific evidence and its relevance to the issues here.

PRESIDENT VEEDER: We have no questions at this stage, Mr. Legum. It's now 12:20, and if Mr. Pawlak wants to start now, he can start now, or we can break and try to resume earlier.

MR. LEGUM: Time flew, and I think that we should break now. So, we'll resume at what time?

PRESIDENT VEEDER: Let's break now and resume, then, at 20 past two, but we may want to
bring our meeting forward by a few minutes if we could meet at 10 to two on the tenth floor for the matter which concerns us.

MR. LEGUM Thank you very much.

(Whereupon, at 12:22 p.m., the hearing was adjourned until 2:20 p.m., the same day.)

AFTERNOON SESSION

PRESIDENT VEEDE: Let's resume.

MR. BETTAUER: It is now Mr. Pawlak's turn to continue on the relating to argument.
Good afternoon, Mr. President, members of the Tribunal. As Mr. Bettauer mentioned this morning, I will address the scientific evidence in the record before you. As I will demonstrate, there is no basis to question the soundness of the science before the California officials that form the basis for their decision to ban MTBE.

Before I begin, it is important that I put my review of the science in its proper context. The time that will be devoted to the science underlying the MTBE ban during this hearing is disproportionate to its relevance to the issues in this case. In addition to my presentation today, later in these proceedings, the Tribunal will hear from four U.S. witnesses who have addressed the science underlying California's decision. On Friday, Drs. Anne Happel and Graham Fogg will be present to respond to questions regarding their respective expert reports on MTBE's contamination of groundwater.

Also on Friday, the Tribunal is scheduled to hear from Dean Simeroth of California's Air Resources Board regarding air quality issues. On Monday, economist Dr. Ed Whitelaw will testify regarding the economics of the MTBE ban. Despite the substantial time devoted to a review of the science supporting the ban, the
United States reiterates its view that the scientific record regarding the ban is, at best, of very limited relevance to the issues before this Tribunal.

Allow me to explain.

There is no dispute between the parties that the UC report did, in fact, support the 1989 Executive Order's finding that MTBE posed a significant risk to the environment. The Governor's decision to request a timetable for the phaseout of MTBE, therefore, was in full accord with the scientific conclusions in the record before the Governor's office.

We address here today the scientific basis for the California measures only because Methanex has alleged that California officials were secretly out to get methanol producers, even though those officials said they adopted the measures out of concern over the MTBE contamination of California's groundwater.

To maintain its theory, Methanex would have to prove two theses: First, that the science regarding MTBE before the decision makers was a sham, a sham that merely covered up the secret intent of the ban. And, second, that the Governor, and other California officials knew that the science was lacking foundation, but proceeded with the decision to eliminate MTBE anyway. Methanex
As I will demonstrate, Methanex has not established any basis to question the science of the scientific conclusions. Similarly, Methanex has not established any basis to question the California decision makers' good-faith reliance on those scientific conclusions in taking action to protect California's groundwater.

During the next several minutes, I will highlight the record on the scientific evidence. In the first part of my presentation, I will establish the bona fides of the UC report which amply supported the decision to ban MTBE.

To conclude the first part of my presentation, I will rebut the claim advanced by Methanex that California improperly singled out MTBE for regulation. In the second part of my presentation, I will consider the reports offered by the scientific experts. Those reports support the conclusion that the MTBE ban was intended to address water contamination.

Allow me to begin by considering the UC report. Mr. Clodfelter, as you'll recall from this morning, reviewed some of the findings and recommendations of that report. I will revisit the
report explaining that there is no basis to question its conclusions or findings.

I will also highlight in somewhat greater detail some of the key findings in the UC report.

As we have heard, Methanex has not disputed that a highly credentialed, multi-disciplinary team of more than 60 tenured researchers authored the UC report.

Nor does Methanex dispute that the UC reports' authors worked independently and in good faith in preparing 17 distinct papers that were compiled in five volumes. Each of those papers covered distinct issues relevant to the determination of the severity of the threat posed by MTBE to California's water resources. Methanex nevertheless complains that the report was underfunded, incomplete, and wrong on many critical points. These complaints, none of which Methanex has begun to prove, could not establish a finding that the science underlying the MTBE ban was a sham, much less that Governor Davis and many other California officials knew of but ignored that fact.

In any event, for the reasons that I now will explain, there is no support for Methanex's assertions. First, several other highly respected sources contemporaneously issued similar research results and thus confirmed the good-faith nature of the UC report. For example, if you will look to the screen or turn to the slide numbered number
five in your packets, by July 1999, the United States Environmental Protection Agency's Blue Ribbon Panel on Oxygenates and Gasoline had issued conclusions and recommendations similar to those of the UC report. As you see on the next slide, so too did the Northeast States for Coordinated Air Use Management, also in 1999.

And in April 2000, Denmark's Environmental Protection Agency added MTBE to its list of undesirable substances, indicating its view that, quote, Use of the substance should be limited as much as possible, end quote.

The fact that these other esteemed scientific research groups reached similar conclusions confirms that the UC report was no pretextual exercise.

Second, despite Methanex's assertions to the contrary, other government agencies in the United States widely praised the UC report. The California Senate bill calling for the study of MTBE, that is, Senate Bill 521, explicitly required that appropriate federal agencies have an opportunity to review and comment on the UC report. Those agencies' comments became part of the public record. Let me highlight a few of those comments for you.

As you will see on slides eight and nine, as well as on the screen at your right, the U.S.
Geological Survey, for example, congratulated the University of California faculty on the UC report, noting that it contains an impressive amount of information and research that will prove useful in addressing the complex issues associated with MTBE use.

On the next pair of slides, we see that the U.S. Department of Health and Human Services stated that the UC report was very well written and very thoughtful in its presentation of the most currently available information. And on the next slide we see that the Oak Ridge National Laboratory reported that, quote, It is clear that the salient references are cited and that detailed analyses have been performed.

The reviews of the UC report, such as those that I have highlighted here, make it clear that its scientific conclusions were no sham. Finally, Methanex's complaints that the UC report was underfunded and incomplete provide no basis for finding any violation of international law. International law does not set minimum amounts that states must spend on scientific research before science-based regulatory measures
may be adopted. Indeed, given the limited resources available to many states, the approach suggested by Methanex would effectively bar many developing states from adopting measures to protect the environment.

That is not, however, the law. In any event, the amount appropriated for the UC report, $500,000, was far from insubstantial. Methanex itself has not disputed that the funding for the UC report was sufficient to address two principal areas of inquiry, one, the human health impacts of MTBE, and two, the environmental impacts and benefits of MTBE.

More importantly, the report addressed the problem of MTBE contamination in a systematic manner. Substantively the UC report provided ample scientific evidence supporting the ban of MTBE. California officials were well aware that gasoline containing MTBE was stored in volume underground, in close proximity to water resources at tens of thousands of locations throughout the state.

Allow me to highlight on the projection screen at your right the record on these points. If you would like to refer to your packet, page 14 of the packet is the first slide.

First, in 1998 and '99, the California fuel supply consumed each day on average over 4.3 million gallons of MTBE. That daily volume of consumption would fill more than five Olympic-size
swimming pools or about half of an oceangoing supertanker.

Next, on slide 15, you see as of 1999, California was home to more than 45,000 operating underground storage tank systems, and by that I mean tanks used as a source for refueling.

On the next slide, slide 16, it is clear, that in addition, as of early 1999, just seven years after widespread use of MTBE had begun in California, MTBE had been shown to have polluted groundwater and more than 4,000 underground fuel tank sites. Allow me to take a minute to explain what this slide represents. The dots on the map reflect leaking underground fuel tank sites.

Leaking underground fuel tank sites are those that were identified to have released gasoline into the subsurface environment and thus became subject to regulation and monitoring. The color coding of these dots reflects the status of testing for MTBE in groundwater at those leaking fuel tank sites. And as you will see, the red dots represent the 4,000-plus tank sites where MTBE had been shown to have polluted groundwater. These are actual detections. As of 1999, nearly 10,000 leaking tank sites had not yet even been analyzed for MTBE, and that is reflected in the yellow dots.

Now, as you will see on the next slide, more than 50 percent of those 4,000-plus leaking
tank sites were located within one-half mile of a public drinking water well. Again, allow me to explain this slide. The dots here, on slide 17, reflect something different than they do on the previous screen. Here, the dots represent public drinking water supply wells. There are about 22,000 such public wells in California. The darker red dots reflect a well that is within just one-half mile of ten or more tank sites that leaked MTBE into groundwater. Similarly, the lighter red dots reflect a public drinking well within one-half mile of four to nine tank sites that leaked MTBE into groundwater.

In short, the point here on this slide is a vulnerability analysis, as Dr. Fogg explains in his expert reports. The arrival of just a fraction of the known thousands of instances of MTBE contamination to nearby water supply wells would result in a serious drinking water contamination problem for affected communities.

Finally, as Dr. Happel has explained in her written testimony, despite California's strict requirements for underground storage tanks, upgraded underground storage tank systems were continuing to leak. Additionally, again, as reflected on the projection screen to your right, or slide 18 in the packet, the UC report made it
clear to California officials what effect MTBE had
on the state's water resources and consumers. The
UC report stated: The taste of MTBE has been
described as objectionable, bitter, solvent-like,
and nauseating.
And in the next slide, the taste and odor
properties of fuel oxygenates in drinking water is
of primary importance to the consumers as well as
suppliers of drinking water. The report further
informed California officials that members of the
public may become worried or stressful over the
safety of contaminated water. For example, a
parent may be hesitant to use water with a strong
taste and odor for children because of safety
concerns. Subjective acute effects may result from
public reaction to the unpleasant taste and odor of
MTBE-containing drinking water.
As the United States has demonstrated in
its written submissions, as of January 1999,
California law prohibited its public water agencies
from delivering to consumers drinking water that
contains MTBE in excess of five parts per billion.
Five parts per billion is the equivalent of merely
one and one-half tablespoons in an Olympic-size
swimming pool. As the United States has also set
out in its written submissions, California
officials were aware that concentrations of MTBE
Page 86
much greater than five parts per billion had been detected in several areas of California.

For example, in a 1999 study, as we heard briefly from Mr. Clodfelter this morning, the Santa Clara Valley Water District detected MTBE at levels as high as 200,000 parts per billion, and that detection was in groundwater underneath gasoline service stations that had already upgraded their underground storage tanks to comply with California's strict 1998 tank regulations.

Contrary to Methanex's suggestion yesterday, a focus on upgrading underground storage tanks would not have solved the MTBE problem. For the record, I note that the Tribunal may find a discussion of the Santa Clara study in Dr. Happel's rejoinder expert report, 24 JS tab C at pages 10 and 11.

As U.S. experts Dr. Fogg and Happel explain, California has seen only the beginning of MTBE's impacts to groundwater. Recall that it was only in 1992 that MTBE became widely used as an oxygenate additive in California. As those impacts are fully realized, increasing numbers of Santa Clara and others throughout California risk finding that water runs putrid every time that they take a glass of water, wash their clothes, water their lawns, boil their vegetables or bathe their children. California's ban on the use of MTBE in
gasoline merely eliminated a source of future additional MTBE contamination of California's water resources. Given the findings of the UC report, and the consistent results from several other research efforts that I highlighted a moment ago, the Tribunal should reject Methanex's claim that California singled out one contaminant among many.

To support its assertion, you'll note a familiar slide from yesterday on the screen and at pages 21 and 22 of your packet. This appears at page 39 of Methanex's reply brief. Methanex relies on this single table listing contaminants in California groundwater to claim essentially that California's adopting an MTBE ban without first enacting a ban of other contaminants somehow evidences that California improperly targeted MTBE. Methanex is mistaken for several reasons. First, California has acted to protect its groundwater from benzene by imposing restrictions on the benzene content of gasoline that are more severe than those imposed by the Federal Government. In addition, benzene is a fundamental component of gasoline, whereas MTBE is not. As expert witness Bruce Burke testified in his rejoinder report, the complete removal of benzene from gasoline would be cost-prohibitive.

Additionally, consider, for example, the
testimony on the screen at your right that was presented to the California Senate in December 1997. This is at page number 23 of your packet. Santa Monica's Director of Environmental and Public Works Management testified to the California Senate, quote, It is important to note that benzene, which has been a constituent in gasoline for several decades, is rarely detected in wells, yet MTBE in a few short years of use has already managed to knock out 71 percent of Santa Monica's wells.

Dr. Anne Happel's expert report confirms the findings now presented on the screen. As Dr. Happel also confirmed, quote, Data from many sources demonstrate that MTBE poses a risk of contaminating groundwater, a higher risk of contaminating groundwater than other gasoline constituents, end quote. As a result, Methanex is wrong to suggest that California somehow was obligated to address other groundwater contaminants in the same manner as it addressed MTBE.

Finally, even assuming Methanex had established its assertion that California acted against MTBE to the exclusion of other contaminants--and, of course, it has
not--California could not be faulted. To do so would preclude governments from responding to any problem without responding to all problems of a similar type. Methanex does not offer any international law support for such a proposition.

In summary, there is no basis for Methanex's claims that California officials somehow improperly singled out MTBE. California officials had ample reason to accept the soundness of the scientific conclusions regarding MTBE that were before them. No evidence even remotely suggests that the science underlying the ban was a sham.

Allow me now to turn to the disputing parties' scientific expert testimony. As I mentioned, the Tribunal will hear from experts Dr. Anne Happel and Graham Fogg, as well as Dean Simeroth of the California Air Resources Board on Friday and Dr. Ed Whitelaw next Monday. However, as I mentioned at the outset of the presentation, the disputing parties' scientific expert reports are irrelevant to the question of intent before this Tribunal. None of the California decision makers had access to the expert reports when the measures were adopted.

As was pointed out in a question put to Methanex yesterday, even assuming Dr. Williams's analyses are correct--and we submit that they are seriously flawed--California was not acting on
Dr. Williams's analyses. It was acting on the conclusions of the UC report and its related public testimony.

The criticisms of the UC report, in the report submitted by Methanex, shed no light, therefore, on the motivations behind the challenged measures. The reports of U.S. experts Dr. Fogg, Happel and Whitelaw, as well as the statement of Dean Simeroth, each demonstrate that the central conclusions contained in the UC report were valid and provided an appropriate basis for California's action. Each responds in detail to the contrary assertions and conclusions asserted by Methanex's experts.

Dr. Fogg, our first witness, whom I believe will testify in the afternoon on Friday, is Professor of Hydrogeology at the University of California at Davis. He is one of the world's leading authorities on the fate and transport of contaminants in groundwater. Among his many accomplishments, Dr. Fogg was the geological Society of America's 2002 Birdsall-Dreiss distinguished lecturer, which is awarded to one hydrologist each year. Just a few years before receiving that distinguished award, Dr. Fogg completed his work as co-author of the UC report.

As Dr. Fogg stated in his December 2003 expert report, his, quote, general opinions and conclusions regarding past, present, and potential...
MTBE impacts on groundwater remain unchanged from those that I presented in the UC report, end quote.

In this case Dr. Fogg's expert reports make clear that Methanex's critique of the UC report ignores the unique demands placed on groundwater in California, with its desert climate and exploding population. Dr. Fogg demonstrates that thousands of public drinking water wells are vulnerable to MTBE contamination. He also explains that Methanex's experts ignore entirely the more than 450,000--that is 450,000 private water wells located in California. The UC report made clear that private wells are even more vulnerable to MTBE contamination than public wells, and those private wells are generally not monitored in the California Department of Health Services database, which is analyzed by Dr. Williams.

It is Dr. Fogg's view that Methanex's expert reports underestimate the MTBE problem. Regarding MTBE remediation from groundwater, Dr. Fogg's written testimony concludes, quote, Cleanup of groundwater contamination is difficult, costly, and sometimes impossible, end quote.

Dr. Happel's written testimony concurs as
to the gravity of the MTBE problem. Dr. Happel earned her doctorate from Harvard University, and she will be here to testify on Friday. Prior to her service, as just one of 14 members of the U.S. EPA’s Blue Ribbon Panel on Oxygenates, Dr. Happel produced a ground-breaking study of MTBE while serving as a tenured scientist at the Lawrence Livermore National Laboratory. It is on account of that study that Dr. Happel became a nationally recognized expert on MTBE in California groundwater.

Dr. Happel’s Lawrence Livermore National Lab research on MTBE was broadly supported. That research was funded by, among others, the Western States Petroleum Association and the American Petroleum Institute. As Dr. Happel points out in her expert report, her 1998 Lawrence Livermore research served in part to inform California EPA, and, in turn, Governor Davis’s office regarding the MTBE issue prior to the ban.

In this case, Dr. Happel’s expert reports detail California’s role in leading the nation in the regulation and testing of underground storage tanks. Like Dr. Fogg, she confirms that even upgraded, strictly monitored tanks could and do continue to leak. Dr. Happel also addresses Methanex’s claims that MTBE contamination of California groundwater is not widespread.
As you see up on your right, as well as on slide 24 in your packet, by reviewing actual California data, Dr. Happel finds that there are nearly 10,000 sites reporting MTBE pollution in groundwater. Based on that data, Dr. Happel estimates that 10,000 to 15,000 leaking underground storage tank sites have polluted groundwater throughout California. Dr. Happel thus concludes the extent and magnitude of MTBE pollution in California’s groundwater is indeed significant, widespread, and worse than predicted by the UC report.

The United States third witness is Dean Simeroth of California’s Air Resources Board. Mr. Simeroth’s written testimony rebutted Methanex’s claim that the ban of MTBE is suspect because it will negatively impact air quality in California. As Mr. Simeroth explained, California’s regulations required that the use of ethanol-oxygenated gasoline not result in any backsliding in California’s emissions standards. In its reply, Methanex did not dispute that its earlier allegations of increased air pollution associated with ethanol were erroneously based on an analysis of gasoline that did not meet California’s specifications. Dr. Williams’s reply report stated, quote, California’s stringent air quality standards may, in fact, prevent ethanol fuel blends from producing
negative air quality impacts. Methanex's assessment yesterday of the increased air pollution associated with ethanol use is not borne out by the record.

The United States's fourth expert witness is economist Dr. Ed Whitelaw. Dr. Whitelaw rebuts Methanex's claims that the MTBE ban was not cost-beneficial and, therefore, must reflect a nefarious intent. He will testify on Monday of next week. Dr. Whitelaw, Professor of Economics, at the University of Oregon, earned his Ph.D. from MIT in 1968. His reports in this case establish that California's decision to ban MTBE is consistent with the information available on costs and benefits in 1999 and 2000. Dr. Whitelaw also establishes the limitations of cost-benefit analysis as a policy-making tool where policy choices based on substantial unquantified or non-monetized factors must be made.

In Dr. Whitelaw's rejoinder report he reviews the substantial downside risks of the continued use of MTBE that were recognized by California decision makers prior to the ban. Dr. Whitelaw then frames the question presented to California officials this way, and you can look at
slide 26 or at the screen to your right, for the excerpt from Dr. Whitelaw's rejoinder report: He writes: Is the benefit of eliminating once and for all the considerable uncertainty surrounding MTBE's future ability to contaminate California's groundwater assets worth the risk of increasing gasoline prices by about three cents per U.S. gallon. California, Dr. Whitelaw explains, answered, yes, it is beneficial to eliminate the risk posed by MTBE at a cost of a mere three cents per gallon of gasoline. Dr. Whitelaw's reports detail that California's decision was economically wise and rational.

In summary, substantively there is no question that the reports offered by the United States's experts have rebutted those offered by Methanex. The MTBE problem was no illusion.

Further, contrast Methanex's expert submissions to those offered by the United States. By its order of June 1, 2004, the Tribunal admitted into evidence Methanex's reports that were the subject of the United States's motion to exclude. However, the many defects in Methanex's reports remain, and those defects substantially diminish their weight. Consider, for example, that Dr. Williams's firm has been retained by Methanex since at least 1989. Consider, also, that it is principally Dr. Williams on whom Methanex has
relied, essentially, to claim that more than 60 professors who authored the UC report engaged in a vast conspiracy.

The United States respectfully submits that the Tribunal should take into account Dr. Williams's failures of disclosure in assessing the weight that is due the several reports authored in whole or in part by Dr. Williams.

The submissions of Methanex's cost-benefit analyst, Dr. Gordon Rausser, also are suspect. His report in this case is virtually the same as one he prepared for an MTBE producer in 2001. As you will see on the screen, or on slide 28 in your packet, Dr. Rausser, quote, accidentally included in the

Methanex report information based largely on the earlier estimate of the costs of an MTBE ban in California. He had prepared that estimate for the MTBE producer.

A Federal Court recently held that Dr. Rausser's testimony in support of other MTBE interests on the economic impacts of a New York law banning MTBE was, quote, speculative and has insufficient evidentiary support, end quote.

Although the slide is not particularly clear there, the one in your packet should make clear the excerpt from Dr. Rausser's reply report.

PRESIDENT VEEDE: Just help us with the reference there.

MR. PAWLAK: Certainly. That is from 20
MR. PAWLAK: Oh, certainly. There it is.

PRESIDENT VEEDER: Thank you very much.

MR. PAWLAK: There have been several other courts that have rejected Dr. Rausser's testimony as unreliable, speculative, and unsubstantiated by the evidence. Similarly, Dr. Rausser's reports in this case are due little, if any, weight.

In summary then, to the extent the scientific expert reports have any relevance to the question of California's intent in adopting the MTBE ban, they support a finding that California's intention was just what California officials said it was, to protect Californians from a significant threat to their water resources. Methanex's competing reports do not begin to establish a record on which this Tribunal could conclude that California adopted the ban to target methanol producers.

Before I conclude, I will address briefly two additional points that Methanex raised yesterday. First, I'll explain that Methanex's
reliance to the European Union's approach to the MTBE issue is misplaced. Second, I will address Methanex's statements of yesterday that there is no credible evidence that MTBE poses a health concern.

First, the European Union. Contrary to Methanex's suggestion, the European commission did, in fact, find that, quote, There is a need for specific measures to limit the risks, end quote, of MTBE contamination of groundwater. Thus far, the EU has taken a different approach to the recognized threat of MTBE, based on that region's topography, climate, population, and other factors. Europe's approach says nothing about the appropriateness of California's ban. The evidence of record identifies the unique circumstances confronted by California decision makers. For example, in dry years, Californians can rely on groundwater for up to two-thirds of their total water consumption. With California's population expected to grow by more than 30 percent by the year 2020, the state's reliance on groundwater resources will increase dramatically.

Moreover, Methanex is wrong in its claims that, in some places in Europe, MTBE is used more widely than in the U.S. Unlike U.S. legislation, EU legislation does not mandate the use of
oxygenates in gasoline. In Europe, MTBE is used primarily as an octane booster and at substantially lower concentrations than it was used in California.

Consider the graphic up at your right or at page 29 of your packet. California's consumption of MTBE amounted to almost double the volume consumed by 16 European countries combined. Further, Methanex's claim yesterday that Finland uses MTBE, quote, at substantially higher concentrations than the United States, end quote, is not accurate.

Slide 30 in the packet as well as the slide up at your right, makes this fact plain. This figure is found in Dr. Fogg's expert rejoinder report at 24 JS tab B, page 84. As you will see,

its average MTBE content of gasoline in Finland in 1997 was only 8.5 percent by weight. Finland's range concentration is much greater than the 1.9 percent by weight, European Union average. In contrast, the MTBE content in California gasoline was about 11 percent by weight. So, clearly Methanex's assertions yesterday are not correct.

Methanex has offered no basis to conclude that California was required to address MTBE's recognized risks to groundwater in the same manner that European Union policy makers have decided to address those risks.

Finally, allow me to turn now to address
briefly Methanex's claims that MTBE is neither toxic nor carcinogenic.

Of course, it bears emphasis that California banned MTBE principally because of its threat to the potability of drinking water, not because of findings that MTBE was toxic or carcinogenic. However, yesterday Methanex was asked to explain how California's primary maximum contaminate level for MTBE of 13 parts per billion squares with its statements that MTBE is not a health threat.

In response, Methanex stated, among other things, I would be willing to say, this is quoted, I would be willing to say, there is no credible evidence that anybody has gotten sick or adversely affected by MTBE in the water, end quote. Methanex reiterated. But, again, I don't think there is any credible evidence that anyone has been adversely affected by drinking water at this level, end quote.

Contrast Methanex's assertions to the views of the Board of Scientific Counselors to the United States National Toxicology Program. For the record, the Tribunal may find a set of the meeting minutes of the Board that I will refer to at 25 JJS Tab 19 at page 3124. At the Board's meeting held in December 1998, five out of 12 scientists with one abstention on the National Toxicology Program's
Board of Scientific Counselors Voted to list MTBE in their report on carcinogens as, quote, reasonably anticipated to be a human carcinogen. Similarly, a review committee for that report at the National Institute of Environmental Health Sciences voted four to three to recommend listing MTBE in the report as reasonably anticipated to be a human carcinogen. The Tribunal may find this document in the record at 25 JS tab 19 at 3123.

Thus, contrary to Methanex's assertions yesterday that there is no credible evidence that MTBE has adverse health effects, recognized experts in the field are divided as to whether MTBE may be carcinogenic. In any event, there is no requirement that a state deem a chemical to be carcinogenic or even toxic before banning it. To the contrary, California has every right to protect itself by regulating chemicals that render water undrinkable, even assuming their presence in water do not result in other adverse health effects.

In short, Methanex's contentions on toxicity are wrong, but they are also beside the point. California's basis for the ban of MTBE was its capacity to render water unpotable.
That concludes my presentation, and I would now like to turn the floor over to Ms. Menaker, who will address Methanex's assertion that the purpose of the MTBE ban was to benefit ethanol.

PRESIDENT VEEDE: Thank you very much indeed. Ms. Menaker.

MS. MENAKER: Thank you.

Mr. President, members of the Tribunal, I will now address the final portion of the United States's arguments under Article 1101. My colleagues have already demonstrated that California did not intend to harm Methanex or methanol producers when it banned MTBE in gasoline. I will now show that California did not intend to benefit ethanol producers when it adopted the ban. As we have shown, it would be legally irrelevant even if California did have this purported intent. Methanol and ethanol do not compete with each other in the gasoline oxygenate market. Therefore, even if California had intended to benefit ethanol producers, this Tribunal could not draw the inference that it intended to harm methanol producers like Methanex.

In any event, Methanex's assertion is baseless. California did not enact the ban in order to benefit ethanol producers. To the contrary, the inference that Methanex asks you to draw is belied by the undisputed facts in the
I will first show how California's own actions are inconsistent with an intent to benefit ethanol. I will then address Methanex's suggestion that this Tribunal should infer such an intent based on the fact that Governor Davis attended a dinner with certain persons involved in the ethanol industry and accepted campaign donations from ADM. I will demonstrate that such an inference is unwarranted. The purpose of the 1989 Executive Order is clear on its face. I have placed the pertinent language with which you are undoubtedly very familiar by now on the screen, and this is also slide one in the packet you have received.

Yesterday, Methanex argued that, and I quote, It is the tendency of governments to use environmental regulations as a pretense to dress up what are actually other reasons for doing it, end quote.

Methanex may have indicated one or two examples where a Tribunal found that that was the case. There is, however, no presumption that governments tend to adopt pretextual regulations.
Methanex has it precisely backwards. The presumption is that measures are not pretextual. The Tribunal in its First Partial Award recognized this when it stated that governmental acts are entitled to a presumption of regularity. The statement of purpose in the 1999 Executive Order, along with the rest of the Executive Order, therefore, is entitled to a presumption of regularity. Methanex has offered no evidence to overcome that presumption.

Methanex’s argument that California’s true intent was to benefit ethanol finds no support in the record. Contrary to Methanex’s argument, California did not rush to embrace ethanol. In fact, rather than accept that ethanol would replace MTBE in California gasoline, the Executive Order, in accordance with the recommendation made in the UC report, announced that California would seek a waiver from the Federal oxygenate requirement. I have placed the pertinent language from the Executive Order on the screen, and that is also slide two in your packet.

If granted, the use of ethanol in California gasoline would substantially decrease.

The waiver request is inconsistent with any effort
to increase the use of ethanol in California. This provision of the Executive Order demonstrates that benefiting ethanol producers was not California's intent in banning MTBE.

California has vigorously pursued this waiver. Governor Davis wrote letters to the Administrator of the United States Environmental Protection Agency and to the President of the United States urging that California's request be granted.

When California's request was denied, California filed suit against the U.S. EPA in Federal Court. California's request is now under consideration once again and is being pursued by California with continued vigor.

Methanex has argued that even if the waiver were granted, California gasoline would likely still contain some ethanol. There is no question, however, that a far smaller amount of ethanol will be used than if the waiver were not granted. That is why, as Methanex itself concedes, and I quote from its Second Amended Statement of Claim at paragraph 131, the U.S. ethanol industry bitterly opposed the waiver, end quote.

If California's intent was to provide a gift to the ethanol industry, it would not have sought this waiver. And if California's intent was to provide a gift to the ethanol industry, it would not have continued to pursue this waiver after it
was initially denied. California's actions are fundamentally at odds with Methanex's proposition that California was motivated by an intent to benefit ethanol producers.

California has done more than just seek a waiver from the Federal oxygenate requirement. In March of 2002, Governor Davis issued an Executive Order directing the Air Resources Board to adopt regulations postponing the ban on MTBE for one year.

The Governor issued this order after the United States Environmental Protection Agency had initially denied California's waiver request. If the ban were to have gone into effect as planned, ethanol would have had to have been added to almost all gasoline sold in California in order to comply with the Federal regulations.

The Governor determined that mandating such a large increase in ethanol supply in such a short period of time would cause substantial price increases, severe shortages in gasoline, and economic havoc.

As you can see on the slide that I have placed on the screen, in his press release announcing the postponement, the Governor explained his decisions as follows: He said, and I quote, I am not going to allow Californians to be held hostage by another out-of-state energy cartel, end
He was referring, of course, to the ethanol industry. This statement dispels any notion that Governor Davis was motivated by an intent to benefit the ethanol industry.

Not surprisingly, ethanol proponents soundly criticized the Governor's action postponing the ban. The Renewable Fuels Association is a national trade association for the ethanol industry. It issued a press release denouncing the decision. The RFA accused Governor Davis of making, quote, a horrible decision for California, end quote.

It characterized the postponement as--and again, I have placed this quote on the screen and also in your package--a callous breach of faith with California consumers that want MTBE out of their drinking water now. Gasoline refiners and marketers that have invested to meet the original deadline, and farmers across the country that have added more than a billion gallons of ethanol capacity to enable the timely transition away from MTBE.

In fact, according to documents submitted by Methanex, the Governor's action postponing the MTBE ban resulted in an oversupply of ethanol that
consequently dragged down ethanol prices to historic lows. While the ethanol industry criticized the Governor's actions, the MTBE industry, on the other hand, had lobbied for the postponement and applauded the Governor's move. Today, the MTBE ban is in effect in California, and there is an adequate supply of ethanol, and, yet, California is still seeking the waiver. Methanex's proposition that Governor Davis requested the waiver for political expediency is not borne out by the undisputed facts in the record.

Thus, contrary to Methanex's contention, California did not rush to embrace ethanol. Before accepting that ethanol would be accepted for use in even larger amounts of California gasoline, the 1999 Executive Order directed the California Air Resources Board, the State Water Resources Control Board, and the Office of Environmental Health Hazard Assessment to conduct studies on ethanol. Those studies were peer-reviewed and presented to the California Environmental Policy Council at the end of 1999, before the regulation banning MTBE went into effect. After public hearings, the California Environmental Policy Council unanimously approved of the report and passed a resolution. I have placed language from that resolution on the screen.
That resolution stated, and I quote, There
will not be a significant adverse environmental
impact on public health or the environment
including any impact on air, water, or soil that is
likely to result from the change in gasoline that
is expected to be implemented to meet the
California RFG3 regulations approved by the ARB,
end quote.
Nor were the amendments made to the Phase
III California reformulated gasoline regulations
that Methanex mentioned yesterday intended to
benefit ethanol. Mr. Dean Simeroth, who, as my
colleague, Mr. David Pawlak, mentioned, will be
testifying on Friday, and who is the Chief of the

Criteria Pollutants Branch of the California Air
Resources Board for the California Environmental
Protection Agency, explained in his first witness
statement that those amendments were intended to
provide refiners with maximum flexibility in
producing gasoline while subjecting that gasoline
to the same stringent emission requirements which
ensures that air quality benefits are maintained.
Mr. Simeroth's testimony refutes any alleged intent
on behalf of California to benefit ethanol
producers.
What does Methanex ask this panel to rely
on to reach a conclusion at odds with all of this
evidence and assume that California intended to
benefit ethanol producers? Two events. One is a dinner that occurred in August 1998, and the other is ADM's campaign contributions to Governor Davis's election campaign. From these two quite ordinary events, Methanex asks the Tribunal to draw the following extraordinary inferences: First, that as a result of certain remarks made at the dinner,

Governor Davis was persuaded to ban MTBE in order to benefit ethanol producers. And second, that in exchange for campaign contributions from ADM, Governor Davis signed the Executive Order. There is no basis to support such speculation.

I will first discuss the dinner and then the campaign contributions.

My colleague, Mr. Legum, has already discussed the August dinner and shown how it provides no evidence to support Methanex's claim that California's ban was intended to harm Methanex or methanol producers. I will now discuss that dinner again in light of Methanex's claim that the dinner is evidence that Governor Davis intended to benefit ethanol producers.

Methanex attempts to cast the August 1998 dinner in a sinister light by repeatedly referring to it as the secret meeting. There was, however, nothing secret about it. Yesterday Methanex focused on the campaign form that I have placed on the screen. As the Tribunal can see, this form is
a disclosure form for campaign expenditures. When candidates spend funds that they have raised for their campaigns, they have an obligation to disclose how they are spending those funds. The public can then confirm that campaign donations are indeed being spent for campaign-related purposes and not for private purposes. That is what this form is. It discloses that Governor Davis used some of his campaign funds to purchase an airplane ticket to attend a meeting in Chicago to meet with labor representatives.

PRESIDENT VEEDEER: Before you move on, do we know what the code name "T" means in the middle column? It's my way of saying I don't know, but I wondered whether you do.

MS. MENAKER: I don't know offhand, although I can attempt to find out.

PRESIDENT VEEDEER: Thank you very much.

My colleague says it may mean "T" for travel.

MS. MENAKER: That would be, I think, a very good guess.

Methanex argued that while Governor Davis disclosed his trip to Chicago to meet with labor leaders, he did not disclose his trip to Decatur, Illinois. This is simply untrue.

I have placed on the screen another slide.
Because this image was taken from a PDF image, it may be difficult to read, although certainly the one in your JS files is clear. This is a form for reporting campaign donations received by the candidate. Both monetary and in-kind donations must be disclosed. In accordance with that law, Governor Davis reported that he flew on ADM’s private plane, free of cost, from Chicago to ADM’s headquarters in Decatur, Illinois, on the evening of the dinner. That is public information, and as the Tribunal correctly noted yesterday, there is absolutely no evidence that ADM denied meeting with Governor Davis, nor is there any evidence that anybody else denied the fact that the meeting had occurred. There was nothing secret about this dinner.

PRESIDENT VEEDER: Just pausing there, is it right to go as far as you go? If you look at the entry for Archer Daniels Midland and the Decatur address, that relates to the full name and address of the contributor. Where would you get from this entry that this covered a flight from Chicago to Decatur?

MS. MENAKER: Well, it took place on the same day, it’s on August 4, 1998, which is the same day he was in Chicago, where he put in his expense form for the meeting that he flew to, to attend with labor representatives.
PRESIDENT VEEDER: You say reading them together you'd be able to work out that he hadn't taken a private plane to Chicago, he'd taken a United Airways flight, and therefore, he must have used the flight to go from Chicago to somewhere else?

MS. MENAKER: Well, he would not—if he had not taken a United Airlines flight or a public carrier, he would not have had to have disclosed it on his expenditures form, which is what he did for the Chicago meeting. On this, this form indicates that he received something by a contributor, and what he received here was the use of a plane. So I think that is a fair inference to draw, that he was using ADM's private plane on the same day where he was scheduled to be in Chicago, but nevertheless, there is no requirement that candidates disclose meetings that they hold with potential supporters. All they need to disclose is contributions that they receive, whether those contributions be monetary contributions or in-kind contributions. And here, the value that ADM gave him was the use of the plane, which its fair market value was considered to be $2,400, which is why he needed to make that disclosure, and I certainly think there is nothing surprising about the fact that if he is in Chicago, and ADM's headquarters are in Decatur, and he is using that private plane, that he traveled to Decatur on their private plane.
This was nothing more than a routine dinner attended by a candidate with potential supporters. As I said, Governor Davis was in Chicago meeting with labor union representatives on the date the dinner occurred. After his meetings in Chicago, he flew to Decatur.

This was just one of innumerable meals that the Governor attended while campaigning. Press conferences are not held announcing events like these, and no inference of wrongdoing can be made on the basis that they occurred. Nor does the discussion, the content of the discussion at that dinner support the inferences that Methanex seeks to draw.

First, no evidence supports the inference that the focus of the dinner discussion was the MTBE problem and that the Governor's decision was influenced by anything said at that dinner. All of the evidence in the record supports the opposite conclusion. We have in the record the witness statements of three persons who attended that dinner. First, there is the witness statement of Roger Listenberger, who was an ADM employee and who will be cross-examined on Thursday. Mr. Listenberger stated that ADM discussed its
presence in California, and that ADM’s ethanol business was only briefly discussed.

Mr. Listenberger testified that neither methanol nor Methanex was discussed, and he recalled the issue of MTBE arising only once, when he asked the Governor whether he thought the issue might arise in his campaign. Mr. Listenberger testified that the Governor said no.

Second, Richard Vind, who was with Regent International, an ethanol company, and who will also be cross-examined on Thursday, also submitted a witness statement. Mr. Vind testified that the dinner conversation focused on Governor Davis’s campaign. He recalled that ADM’s business was discussed, but that neither methanol nor Methanex was discussed. He had no recollection of MTBE having been discussed.

Finally, Daniel Weinstein, who will also be cross-examined on Thursday, submitted a witness statement. Mr. Weinstein is with Weatherly Capital Investments Group. He similarly recollected that the conversation at dinner was a general one. He recalled that ADM representatives talked about their company and their business in California. He did not recall any discussion of methanol, Methanex, or MTBE.

Methanex has introduced no evidence to call into doubt this testimony. It nevertheless
asks you to draw an inference at odds with this evidence. According to Methanex, you should assume that the conversation at dinner focused on ethanol and how the Governor could support ethanol because a majority of the attendees at dinner were involved in the ethanol industry. This inference is not only contrary to all of the evidence in the record, it is based on an erroneous assumption.

In his statement, Mr. Vind identifies the persons who he recalled being at the dinner. From the list of attendees, it is apparent that despite

Methanex's repeated allegations, the majority of the attendees were not primarily responsible for ethanol-related matters. Mr. Vind, of course, himself was involved in the ethanol industry at the time.

As far as the ADM attendees were concerned, however, only one attendee, Mr. Roger Listenberger, could be described as someone whose job focused on ethanol. The other attendees from ADM were all senior officers whose responsibilities spanned a wide range of ADM's business. These people included ADM's Chief Executive Officer and an ADM Senior Vice President.

In addition, the other attendee mentioned by Mr. Vind, and that is Mr. Daniel Weinstein, has no connection with the ethanol industry. At the end of the day, that makes two persons, only one of whom is from ADM out of a total of six attendees
who could be said to be primarily in the ethanol business. That is not by any count a majority of participants.

It is not at all unreasonable that the senior ADM executives who are responsible for many aspects of ADM’s business would speak generally about ADM’s business, and particularly about ADM’s presence in California when meeting with a candidate for Governor of California. That accords with the evidence in the record and is entirely reasonable.

In any event, even if the dinner conversation had focused on ethanol, or even if MTBE, methanol, or Methanex had been discussed, that would in no way establish the illicit intent asserted. There is no requirement that politicians be hermetically sealed off from the public. To the contrary, politicians routinely interact with members of the public and listen to what the public has to say.

In fact, the record contains evidence that just days before the Governor signed the Executive Order, one of the Governor’s top aides went on a tour of Arco’s refinery in California. Arco’s

Chief Executive Officer also phoned the Governor to
defend the use of MTBE in California gasoline.

When asked to explain Arco's behavior, its lobbying and public affairs manager was quoted as saying, and I quote, The most important thing is we want to be able to discuss these issues and get our views on the table, end quote.

We all know that politicians are likely to be exposed to various viewpoints. Arco's interaction with the Governor's office demonstrates this reality. The mere fact that an interested party has expressed its views to a politician does not give rise to any inference of impermissible conduct.

I will now examine Methanex's hypothesis that ADM contributed to Governor Davis's campaign with the expectation that the Governor would take action to benefit ethanol producers and that in exchange for these campaign contributions, the Governor directed that MTBE be banned from California gasoline.

Of course, if Governor Davis had signed the Executive Order explicitly or implicitly in exchange for ADM's campaign contributions, that would constitute a crime under U.S. law. Methanex does not dispute this. Yet, Methanex has repeatedly disavowed any claim that Governor Davis committed a crime.

Herein lies an insurmountable
contradiction in Methanex's case. It is asking this Tribunal to draw an inference that it can only draw if it assumes facts that Methanex has conceded are not existent. By conceding that Governor Davis did nothing illegal, Methanex has conceded that the Governor did not take any action in exchange for donations or the promise of donations. If Governor Davis was not influenced to sign the Executive Order because of ADM's campaign contributions, those contributions are completely irrelevant, and indeed, that is the case. Even if Methanex were to back away from its earlier concession, however, there is no evidence in the record to support an inference that Governor Davis was improperly influenced by campaign contributions made by ADM.

Methanex has relied principally on a recent U.S. Supreme Court case, McConnell versus Federal Elections Commission, to support the inference it asks you to draw, and Methanex's reliance is misplaced. As we explained in our rejoinder, there are laws in the United States regulating political contributions. The legislative history of those laws show that Congress found that political contributions created a sufficient danger of corruption, as well as an appearance of corruption, that regulation of such contributions was justified. The Supreme Court upheld the regulation at issue in the McConnell case, finding that they did
not run afoul of U.S. constitutional protections for free speech. Congress did not determine that all campaign contributions were corrupting. It did not outlaw all such campaign contributions. That the possibility or appearance of corruption justified regulation does not and cannot support a finding that by virtue of making or receiving a lawful contribution there is corruption.

Let me provide an analogy. Like campaign finance, the field of securities is also highly regulated in the United States. It would however, be unreasonable to suggest that the mere fact that the securities field is highly regulated is cause for inferring wrongdoing with respect to any particular sale of securities, especially where there is agreement that all such regulations were respected in relation to that sale. And that is the case here. It is uncontested that the ADM contributions in question complied with all applicable U.S. laws.

Assume for the moment that Methanex's premise were accepted. Under Methanex's theory, if Governor Davis had reached a different determination in the Executive Order, this Tribunal would be justified and, in fact, compelled to find that the Governor was improperly influenced by
Arco. After all, the record contains evidence showing that Arco contributed approximately the same amount as did Methanex to the Governor Davis's gubernatorial campaign.

Excuse me, I'm sorry. The record contains evidence—let me correct that—the record contains evidence showing that Arco contributed approximately the same amount as did Methanex—no, ADM, excuse me, to Governor Davis's campaign.

Arco's CEO apparently called the Governor just days before the Governor signed the Executive Order to defend the use of MTBE, and one of the governor's top aides took a tour of Arco's refinery days before the Executive Order was signed. Under Methanex's theory, this would mean that the Governor had been improperly influenced by Arco.

Of course, such an inference would be unwarranted. Equally unwarranted is the inference that Methanex asks you to draw regarding ADM's influence over Governor Davis.

The only so-called evidence of corruption on Governor Davis's part that Methanex has submitted are newspaper articles. All but one of these articles are opinion pieces. No international Tribunal nor competent domestic court, for that matter, would or could base an inference of wrongdoing solely on reports in
newspapers without any documentary evidence or
witnesses to corroborate any of the allegations
that might have been repeated in those reports.

All of the remaining evidence proffered by
Methanex relates not to Governor Davis, but to the
ethanol industry. This evidence is irrelevant.
Neither ADM, Regent, Richard Vind, nor the ethanol
industry in general is on trial here. Nor can the
United States be held responsible for ADM’s,
Regent’s, or Richard Vind’s conduct.

In any event, Methanex’s own arguments
only confirm California’s good faith. Yesterday
Methanex repeated arguments previously made in
Mr. Wright’s supplemental affidavit. Methanex
claimed that the ethanol industry was, and I quote,

involved with the manipulation of the public
opinion and the whipping up of the degree of
concern about MTBE that simply wasn’t merited by
the facts, end quote. The fact that public opinion
supported the ban only confirms California’s good
faith. As the United States noted in its Amended
Statement of Defense, it is legitimate and
unremarkable that elected officials take action in
response to public opinion. If the public believed
that its drinking water was endangered because of
MTBE contamination, and the Governor acted in
response to those concerns, that dispels any
illicit intent on Governor Davis’s part.

Finally, even assuming for the sake of
argument that ADM did intend to improperly influence Governor Davis, and there is no such evidence here, that cannot bear on Governor Davis’s motivation absent evidence that, as I have just demonstrated, is wholly lacking here. It is ironic that Methanex’s claim centers on the lobbying activities and campaign contributions made by Regent and ADM. Methanex does not deny that it too engages in lobbying. After all, it was Methanex’s lobbyists who were purportedly at the meeting with Senator Burton on which Methanex relies. Yesterday, Methanex also conceded that after the UC report was issued, the methanol lobby, and I quote, launched a vigorous lobbying campaign to try to convince Governor Davis that the report was wrong and that the ban on MTBE was the wrong solution, end quote. Methanol (sic) has issued memoranda showing that its lobbyists held over 20 meetings with California legislators, and it bears noting that there is no indication that Methanex or the methanol lobby or anyone else felt it was necessary to publicly announce that those meetings were held. Those meetings are no more or less secret than the meeting ADM held with Governor Davis, and in addition to its lobbying activities, the evidence shows that Methanex has also made donations to U.S. political parties. Yet--
PRESIDENT VEEDER: I thought it was an offer to make? Did they actually make them? I thought they had to repay the money?

MS. MENAKER: There is--they did have to repay one of the contributions that was listed in the article, but nevertheless they did make the contribution. It was later deemed to be an illegal contribution and was returned to them.

Yet, while attacking ADM’s and Regent International’s legitimate activities and accusing ADM of spying on its competitors, Methanex, at best, hired individuals to sift through the garbage dumpster behind Mr. Vind’s office and salvage his personal files, and it appears this was not done in connection with any litigation, but rather was a systemic effort to dig up dirt for use for political advantage. I understand that the Tribunal is going to schedule argument on whether these documents should be excluded from evidence, so I will defer making those arguments until that time. I pause here only to note the tension between Methanex’s attacks on the U.S. political system and the ethanol lobby’s legitimate activities and its own behavior.

Finally, it’s important to keep in mind
that almost all of Methanex's allegations relate
solely to influence that ADM or the ethanol lobby
supposedly had over Governor Davis. As
Mr. Clodfelter noted this morning in his
presentation of the facts, Governor Davis did not
have a lot of discretion insofar as the MTBE ban
was concerned. Senate Bill 521 had been
unanimously passed by the California Legislature
and signed by the previous Governor in office.
That bill required the Governor to make one of two
determinations. Once again I have put this
language on the screen for you to look at. He
could decide, one, that on balance, there is no
significant risk to human health or the environment
of using MTBE in gasoline in the state, or, two,
that on balance, there is a significant risk to
human health or the environment of using MTBE in
gasoline in the state.

The bill required the Governor to make
determination within ten days after the
completion of public hearings on the UC report.
Senate Bill 521, as you've heard, also required
that the Governor's determination be based on the
UC report, its assessment, and the public hearings.
You've just heard my colleague, Mr. Pawlak,
describe the recommendations of the UC report, as
well as the peer-reviewed comments and some of the
testimony that was offered at the public hearings.
It is undisputed that the UC report concluded that
there was a significant risk to human health or the environment from using MTBE. Taking this information into account, what would have been surprising would have been if the Governor had come to an opposite conclusion, at odds with the recommendation proposed by the UC report.

Governor Davis's subsequent actions also conformed with the expectations in Senate Bill 521 and the recommendations in the UC report. Methanex argued yesterday that even if the Governor was justified in making his determination, his action banning MTBE was somehow unjustified. But again, the facts are to the contrary. Senate Bill 521 directed the Governor to take appropriate action to protect public health and the environment to the extent he made the determination that MTBE did pose a significant risk.

Immediately following Section 3, which directs the Governor to take appropriate action, the next two provisions evidence that the only action envisioned by the Legislature that had unanimously passed Senate Bill 521 was banning MTBE. Those provisions state that if the sale and use of MTBE in gasoline is discontinued pursuant to subdivision (f), then the State shall not thereafter adopt or implement any rule or regulation that permits or requires the use of MTBE in gasoline. The following provision similarly
states that if the sale and use of MTBE is to be discontinued pursuant to subdivision (f), then the Air Resources Board shall notify the Environmental Protection Agency that MTBE will be discontinued in the state. In addition, the UC report concluded the following, and I've also placed the language on the screen, quote, We recommend consideration of phasing out MTBE over an interval of several years, end quote. As you can see, insofar as his determination was concerned, the Governor's discretion was quite limited. He was required to take action based on the UC report, its assessment, and the public hearings. The determination he made was consistent with the UC report's recommendation. The action he took in response also accorded with the expectations set forth in Senate Bill 521, as well as with the recommendation of the UC report. For this reason alone, the emphasis that Methanex places on ADM's supposed influence over Governor Davis is misplaced. In conclusion, there is no evidence that even suggests, never mind proves, that Governor Davis intended to benefit the ethanol industry when
he made his determination that MTBE posed a risk to California's drinking water. The Governor's actions in seeking a waiver of the oxygenate requirement and postponing the effective date of the ban belie any supposed intent to benefit the ethanol industry. Those actions were taken at the same time by the same individual in relation to the same problem and were harshly criticized by ethanol proponents. In light of this evidence, and the absence of any other evidence, it is not plausible to conclude that the Governor intended to benefit the ethanol industry.

Unless the Tribunal has any questions, I would ask to turn the floor over to Mr. Bettauer.

PRESIDENT VEEDER: Just before we take a break, Ms. Menaker, there is one thing we would like to raise, and if you want to come back to this question later, please do. But Governor Davis is no longer an officer in the government of California, he is a private citizen, and some very harsh things are being said about him in these proceedings to which he is not a party, and where he is not legally represented. We understand that he is not a witness being called by the United States Government, but has he been approached or advised that there is an opportunity for him to give evidence if he were to be called by the United States?

MS. MENAKER: If I may take a moment?
(Pause.)

MS. MENAKER: I can tell you that when the Governor was Governor, we had spoken to the Governor's office, not to the Governor personally, but to individuals who worked in his office, and he was not interested in participating. Since he has left the governorship, we have not contacted him.

PRESIDENT VEEDE: Let's take a ten-minute break, and then we will come back here at quarter past four. But before that, we'll hear Mr. Legum.

MR. LEGUM: Would it be convenient for Mr. Bettauer to give a short, a very short conclusion—I retract that. Thank you.

PRESIDENT VEEDE: Having retracted that, we will have a ten-minute break and come back at quarter past four. Thank you very much.

(Brief recess.)

PRESIDENT VEEDE: Let's proceed.

MR. BETTAUER: Thank you, Mr. President and members of the Tribunal.

I would like to briefly pull together a few of the key points that have been made in the last three presentations dealing with Article 1101. First, you have seen that there is very little evidence before the Tribunal concerning methanol as opposed to ethanol and MTBE. None of the evidence supports Methanex's assertion that California intended to harm methanol producers by...
banning MTBE. As Mr. Legum demonstrated, this failure of proof by itself is fatal to all of Methanex's claims.

Second, methanol and ethanol do not compete with each other, in any sense, relevant for the purposes of any ban of MTBE in California gasoline. Methanol is, as this Tribunal observed in the First Partial Award, a feedstock for MTBE. Ethanol is a gasoline additive that directly competes with MTBE. Methanol, unlike MTBE or ethanol, cannot be added to gasoline to meet the oxygenate requirements of the Clean Air Act. Under the reasoning of the First Partial Award, and on the evidence in this case, there is no relevant competition between methanol and ethanol, period.

Third, Mr. Pawlak demonstrated that the science on which the MTBE ban was based is, at best, of tangential relevance to this case. There is no dispute that the conclusions of the UC report supported Governor Davis's finding, that MTBE posed a significant threat to the state's drinking water resources. The only way in which the science could be relevant here is that if Methanex had established that the science was a sham or a pretext, and that the decision makers in fact knew
this. But the record does not remotely show any such thing.

Fourth, Ms. Menaker showed that the record does not support Methanex's assertion that California intended to provide a gift to the ethanol industry by banning MTBE. To the contrary, the record shows that California took numerous actions that were detrimental to ethanol interests, including seeking a waiver of the oxygenate requirement from the U.S. EPA, and postponing the ban by one year. The evidence Methanex relies on, the August 1998 dinner and campaign contributions, do not show what Methanex says they show. Again, the record establishes that the purpose of the ban was exactly what California said it was, to protect California's groundwater resources from a contaminant that made water undrinkable.

In sum, the record simply does not sustain Methanex's allegation that the MTBE ban was intended to hurt foreign methanol and benefit domestic ethanol. The measures did not relate to

Methanex or its investments. Methanex's claims do not fall within the scope of Chapter 11, and they do not fall within the scope of the U.S. consent to arbitrate set forth in that Chapter. It is clear there is no jurisdiction over this case.

We now turn to a different reason why all of Methanex's claims should be dismissed. Methanex has not demonstrated that it suffered any loss
proximately caused by the measure at issue. Again, we will divide our presentation on this subject, this time into two parts. First, Mr. Legum will focus on the chain of causation in this case. He will show that any effect on Methanex from the measures at issue, if there was any effect at all, is too remote to give rise to a cognizable claim. Any impact on Methanex could only occur as the result of the measures' effects on Methanex's contractual counterparties under settled international law, incorporated into the NAFTA. This kind of remote effect through third parties does not establish loss that can sustain a NAFTA claim.

Second, Mr. McNeil will discuss the allegations of loss that Methanex makes. He will demonstrate that Methanex has failed to establish any loss or damage at all within the meaning of Articles 1116 or 1117 of the NAFTA. This lack of evidence of any loss or damage is fatal to all of Methanex's claims.

Mr. President, I now ask you to call on Mr. Legum to begin our discussion of this part of our presentation.

PRESIDENT VEEDEER: Thank you, Mr. Bettauer.

MR. LEGUM: Thank you, Mr. President.
I will now address the chain of causation in this case. I will demonstrate that the loss alleged by Methanex is far too remote to be recognized under applicable principles of international law.

Methanex has at no point in the past four years disputed the nature of the causal chain in this case. The measure at issue regulates the sale of California gasoline containing MTBE. There is no dispute—and I have a little graphic going on the screen there—there is no dispute that the first link in this causal chain is the impact of the measure on sellers of California gasoline, the persons who are directly regulated by the measure at issue.

Methanex's allegation is that these sellers will, as a result of the ban, buy less MTBE to use in the California gasoline that they produce. Methanex alleges, and this is the second link in the chain, that these decreased purchases will create an adverse impact on producers of MTBE, the second link, as I said before, in the causal chain.

According to Methanex, the producers of MTBE will manufacture less MTBE as a result of the ban, and therefore, need to buy less methanol to produce MTBE. This will, assuming that the supply
of methanol remains constant, according to them, result in lower worldwide methanol prices. This is the third link.

And finally, if worldwide methanol prices did in fact decrease, that would have an adverse impact on Methanex and its investments.

It is, therefore, apparent that the causal chain in this case depends upon the impact of the measures on suppliers, Methanex, to suppliers, MTBE producers, to the persons directly regulated by the ban, sellers of California gasoline. It is equally undisputed that under established principles of international law, a remote chain of causation cannot give rise to state responsibility. The United States collected numerous authorities to support this proposition. At pages 16 to 30 of its November 2000 memorial on jurisdiction and admissibility.

Methanex has at no point in the intervening four years, attempted to disprove the principle of proximate causation recognized by these international law authorities. If these authorities apply to this case, then Methanex's claims must be dismissed in their entirety under the holding of these cases.

Now, while Methanex does not dispute the principle, it does dispute the application of the principle.
principle. It advances two arguments for the non-application of the principle of proximate causation. I will, with my remaining time today, show that each of these arguments is without merit. Methanex's main argument for non-application of the principle is that NAFTA Articles 1116(1) and 1117(1) dispensed with the normal requirement of proximate cause by using the word "by reason of," and the words that Methanex highlights, "or arising out of a breach." The text of Article 1117(1) is on the screen. The text of Article 1116(1) is, for these purposes, identical. Methanex concedes that the words "by reason of" signify proximate causation, but it argues based on municipal law cases in the insurance context that the words "arising out of" embody a different, more expansive approach to causation, never before seen in international law. This argument is without substance for several reasons. First of all, it is international law, not municipal insurance law, that governs this case. Under international law, the phrase "arising out of," or similar formulations, have repeatedly been held to reflect a proximate cause standard. The United States demonstrated this at pages 9 to 13 of its reply on jurisdiction three years ago. The Algiers Accords provide one example. As the Iran-U.S. Claims Tribunal has repeatedly and
unambiguously held, those accords use the words "arising out of" to signal proximate cause.

Another example is the Mexico-U.S. General Claims Convention of 1923, which use the words "originating from" to the same effect as the claims commission established by that treaty found. Methanex has never offered a response to the United States showing concerning these accords. This is, we submit, because there is no response.

Now, Methanex does complain that under this interpretation, "by reason of" means pretty much the same thing as "arising out of." This complaint, however, is without merit. Treaty negotiators, particularly in the context of negotiations among parties with different languages and different legal traditions, treaty negotiators often use equivalent phrases as "belts and suspenders" to ensure that the desired concept gets across. Articles 1116 and 1117 themselves provide another example of such an approach. We have the text on the screen in slide six. They use the words "loss" or "damage." Now, if there is a difference between "loss" or "damage"--loss and damage for purposes of this provision, it is too subtle for us to be able to perceive. "Loss" or "damage," both words are used there in order to signal in a clear way the same concept. There is nothing incongruous about the NAFTA parties' use of two equivalent expressions for proximate causation.

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My second point is if ever there were any doubt as to the NAFTA parties' intent to incorporate the traditional standard of proximate causation by the clause "by reason of" or "arising out of," that doubt has been dispelled by the NAFTA parties' submissions to this Tribunal in this case. As Mexico notes in its fourth submission--and we have the text on the screen now--Mexico has expressly agreed that those articles incorporate the standard of proximate causation. And Canada, as demonstrated in slide eight, has similarly stated its view that, quote, the ordinary meaning of the words "by reason of" or "arising out of," establishes that there must be a clear and direct nexus between the breach and the loss for damage incurred, close quote.

Under Article 31(3)(a) of the Vienna Convention on the Law of Treaties, or to be more precise, the rule of customary international law reflected in that provision, such a subsequent agreement on the interpretation of a treaty by its parties shall be taken into account. Finally, the only other NAFTA Tribunal to address the question to date also reads Article 1116 and 1117 as reflecting a standard of proximate causation.
causation. Slide nine shows a quote from the Tribunal in the S.D. Myers versus Canada case which in its award on damages concluded that, quote, The breach of the specific NAFTA provision, must be the proximate cause of the harm. In sum, nothing supports Methanex's assertion that NAFTA adopted a previously unknown standard of causation. The overwhelming weight of international claims authority, the unanimous views of the NAFTA parties, and the only other NAFTA Tribunal to address the question all agree.

Articles 1116 and 1117 incorporate the familiar principle of proximate causation. That principle compels dismissal of Methanex's case. Methanex's second argument for non-application of the principle of proximate causation in no way changes this result.

Methanex's second argument is that its allegations that California acted intentionally change the equation. This argument fails on several levels. First, as we demonstrated in our presentation earlier today, the record in no way supports Methanex's allegations that California intended to harm or even address methanol producers by banning MTBE. Methanex has failed to prove the intent upon which this argument is premised. Second, Methanex's own authority, the Dix case, suggests that intentional harm is relevant to
the causation analysis only where it is directed both at the claimant and at the specific harm alleged. There is no evidence in the record showing that California had Methanex in mind when it adopted the ban, let alone that it specifically intended harm to Methanex's goodwill or any of the other losses alleged by Methanex. The lack of proof of specific intent further defeats this argument by Methanex.

Finally, even if Methanex could support its intent allegations, which it has not, and it cannot, that would not relieve it of the burden of showing losses proximately caused by the breach. A showing that a tortfeasor specifically intends an indirect injury may allow a Tribunal to overlook the indirect nature of the injury, but such a showing in no way abolishes the rule that a loss caused by the breach must be shown.

The NAFTA itself confirms that a showing of loss caused by the breach is required. Slide ten shows again the text of Article 1117. It unequivocally requires a showing of, quote, loss or damage and requires that that be, "by reason of" or "arising out of" the breach. The text of the treaty in no way supports Methanex's suggestion that the universal requirement of proof of loss and causation is suspended when a claimant alleges an intentional breach.

Now, as I already noted, the record here
doesn't show intent to harm Methanex or to cause the specific harm that's alleged. Under classic principles of proximate causation, therefore, the chain of causation is too indirect to impose state responsibility, but, as my colleague, Mr. McNeil, will demonstrate in a few moments, even if Methanex's claims were not remote, they would still fail for lack of evidence of any loss at all caused by the breach.

I would like to conclude my presentation by addressing Methanex's contention that the undated, unsigned contract with Valero that I referenced this morning establishes proximate causation. It establishes precisely the opposite. It is clear from that contract that the party directly affected by a ban of the use of MTBE in California gasoline would be Valero, the party that produced California gasoline containing MTBE. It, that is, Valero, would have a lesser demand for MTBE as a result of the ban. Because it would need less MTBE, it would buy less methanol as a feedstock for MTBE production. Methanex, a supplier of methanol, would be impacted by the ban only as a result of its impact on its contractual counterparty. This is precisely the scenario that
the international case law authorities collected in our briefs have held not to satisfy the requirement of proximate causation.

I have a quote from the Tribunal in the Dickson Car Wheel case on the screen now which summarizes the holding of these cases. Quote, A state does not incur international responsibility from the fact that an individual or company of the nationality of another state suffers a primary injury as the corollary or result of an injury which the defendant's state has inflicted upon an individual or company, irrespective of nationality, when the relations between the former and the latter are of a contractual nature.

I would note that paragraph 225 of the Amended Statement of Defense provides a number of other examples of cases directly supporting this point.

The Valero contract is, if it were ever signed, evidence of a contractual relation with Methanex. The primary impact of the measure would fall on Valero. Any impact on Methanex would only be a corollary or result of the impact on Valero. There is, under established international law recognized by these cases, no international responsibility here.

Unless, the Tribunal has any questions on the causal chain or the principle of proximate
10 causation, I would turn the floor over to
11 Mr. McNeil.
12
13 PRESIDENT VEEDER: Thank you very much,
14 Mr. Legum We have no questions at this stage. We
15 hand the floor to Mr. McNeil.
16
17 MR. MCNEILL: Thank you.
18 Mr. President, members of the Tribunal, as
19 Mr. Legum mentioned, I will be addressing
20 Methanex's failure to prove any loss or damage in
21 this case. I will demonstrate the record in this
22 arbitration lacks any evidence of any loss to
23 Methanex or its U.S. investments as a result of the
24 California ban.
25
26 This lack of evidence is easy to explain.
27 There is no loss. In fact, Methanex has repeatedly
28 told its investors and the public that it has not
29 been affected by the California ban. As recently
30 as February of this year, Methanex's CEO told
31 investors that the ban has, and I quote, really had
32 no impact on our industry. That is at 25 JS tab 2,
33 and I will return to that later.
34
35 Even without these admissions of no loss,
36 it is clear from the factual record in this case
37 that Methanex and its U.S. investments have not
38 been adversely affected by the ban. The record
39 shows that Methanex's methanol plant in Fortier,
40 Louisiana, was closed before the ban was even
41 announced and was kept idle for economic reasons
42 having nothing to do with the ban. The record also
shows that Methanex's marketing operation in Dallas, Texas, Methanex-U.S. suffered no loss of goodwill or market share as a result of the ban, and was, in fact, a thriving and profitable operation during the relevant period.

The record showing an alleged decline in Methanex's exports from Canada to California occurred years before and was unrelated to the California ban, and in any event, is not a claim that can be submitted under the investment chapter of the NAFTA.

And finally, the record shows that a temporary decline in Methanex's stock price, long prior to the ban taking effect, is not attributable to the ban, but more importantly, cannot be a legal matter--cannot as a legal matter serve as the basis for a claim of loss to the corporation. Methanex's failure to prove any loss or damage caused by the measures requires dismissal of all of its claims.

I will briefly review the requirements under the NAFTA. I will then review Methanex's admissions that it has no loss. Finally I will demonstrate that each of Methanex's damage claims with respect to its investments, with respect to Methanex-Fortier, Methanex-U.S., and also with
First, let’s look at the requirements under the NAFTA. Kindly draw your attention to the first slide. NAFTA Articles 1116 and 1117 require as an element of a claim that an investor demonstrate that it, quote, has incurred loss or damage by reason of or arising out of an alleged breach. The text, you will notice, is phrased in the past tense. It requires that a claimant produce evidence of an existing loss. As one NAFTA Tribunal has held the failure to produce evidence that an actual loss has been incurred is fatal to a claim of liability. In ADF versus United States, the Tribunal dismissed certain of ADF’s claims because the claimant failed to produce any evidence that it had incurred an actual loss.

As here, the quantum of damages was reserved for a later phase in the proceedings. And that case is at Tab 2 in the U.S. Amended Statement of Defense. As I will demonstrate, the same result is called for here.

I will now address Methanex’s statements to its shareholders and to the public that it has suffered no loss from the California ban. The first example is from Methanex’s earnings conference call for the second quarter 2002. Kindly draw your attention to the screen.
As you can see in that call, Methanex's CEO, Pierre Choquette, stated that, quote, We don't expect the impact of this change—referring to California refiners no longer purchasing methanol—to have much of an impact on pricing, if any at all—and by "pricing," Mr. Choquette was referring to methanol pricing.

In the next slide, there is a quotation from the same conference call. As you can see Mr. Choquette likewise stated that, quote, It, referring to the loss of California MTBE market, just happens to be coming at a time—

MR. DUGAN: Can I register an objection?

He is reading into what Mr. Choquette is saying.

Mr. Choquette's not a witness here, and he has never put anything into the record.

PRESIDENT VEEDER: I think it is a function of counsel in making submissions to a Tribunal on the existing material before the Tribunal.

MR. DUGAN: We don't know what that Mr. Choquette actually intended what they say he's intended.

PRESIDENT VEEDER: Are you objecting to the previous interpolation?

MR. DUGAN: Yes, I'm objecting to the interpolations. I think he has to have the language up just as it was said.

PRESIDENT VEEDER: Well, I think we can
MR. MCNEILL: To return to this quote, as Methanex’s CEO Pierre Choquette stated, Clearly in the market we are in today, if the conversion in California took place overnight, it would be fully absorbed.

Methanex’s earnings conference call for the first quarter of 2003, as you can see on the screen, Methanex’s CEO stated, and I quote, The reduction in consumption—referring to MTBE consumption—in the United States, is taking place, but, of course, it is overshadowed by supply constraints, so it is hard to see the impact of the reduction, close quote.

And here is a statement made by Mr. Choquette, Methanex’s CEO, at an investor conference in Canada in June 2003. At that conference Mr. Choquette stated that, quote, I always like to say that I wish they would eliminate it—referring to MTBE—from the U.S. market tomorrow morning, so we can get on with life, because it is not that big a deal, close quote.
Finally, as you can see on the screen, at an investor conference in February of this year, Bruce Aitken, Methanex's President and now CEO, stated that, quote, We have already had big reductions in MTBE demand in the U.S., and it's really has had no impact on our industry, close quote.

We don't expect an impact on pricing if at all. It is unlikely to have any significant impact. It would be fully absorbed. It is hard to see the impact of the reduction. It is not that big a deal. And it has really had no impact on our industry.

The timing of this latter statement in February of 2004--February of this year, is particularly significant. MTBE, as Mr. Aitken notes, had already declined significantly across the United States. As you can see from Methanex's Exhibit 7, which we have up on the projection screen, it is not in your packets, we discussed this slide this morning, you can see from the blue line that demand for methanol, for MTBE in the California market, had been fully--had completely disappeared by 2004. You can see by the beginning of 2003, it was almost completely out of the market, but by 2004, it had been completely phased.
Thus, if there is to be any effect on Methanex from the California ban, it would certainly have been felt by the time Methanex's President made this statement in February of this year.

Methanex has no explanation for the discrepancy between these statements that it has no loss, and its damage claims in this case. Methanex has nearly a $1 billion damage claim which is approximately the value of the entire company, suggests not just a severe loss but a catastrophic loss. Methanex offers no explanation because it is impossible to reconcile these two things.

Methanex's response to these admissions of no loss is to claim that they must have been taken out of context. The citation in the record for each statement is at the lower right-hand corner of the handouts. We invite the Tribunal members to see for themselves that in their full context, these statements mean exactly what they say, and I include the statement that Mr. Dugan referred to earlier about methanol pricing.

The only statement that Methanex actually addresses in substance, and that Methanex mentioned yesterday, is the one from mid-2003, that the elimination of MTBE across the entire United States would not be that big a deal. Notably Methanex does not refute that Methanex had no loss as of
that date. Rather, in the third Macdonald affidavit Methanex expressly confirms that it had no loss. The statement is on the screen. Mr. Macdonald stated, paragraph 35, quote, By mid-2003, the methanol market had changed for the better, and supply and demand were in a balance to tight situation. Because of the strong price, the immediate damage of the MTBE ban was not felt,

close quote.

This is a remarkable admission. Methanex concedes that four years after commencing this arbitration, it still had not felt a loss from the MTBE ban. Methanex's damage claim thus boils down to this. It argues that it is only because of the tight market situation and high methanol prices that it has no injury. If market conditions were different, or if they change sometime in the future, Methanex suggests, perhaps it might have a loss.

Mere hypothetical losses or mere speculation about possible future losses cannot be the basis for a claim under Articles 1116 and 1117 of the NAFTA. Those articles require that a claimant demonstrate an actual, existing loss. Methanex's admissions that it had no existing loss by themselves are fatal to Methanex's claims. In the remainder of my presentation, I will address the factual record in this case with
I noted moments ago that it was not possible to reconcile Methanex’s admissions of no loss with its damage claims. Those admissions are, however, easy to reconcile with one thing in this case, the evidentiary record, for that record shows exactly what Methanex’s CEO, President, and now its Senior Officer, Michael Macdonald, have all said: The ban has had no impact on Methanex.

I will first address Methanex’s claim with respect to its plant in Fortier, Louisiana. I’ll then discuss its claim with respect to Methanex-U.S., its marketing in Dallas, Texas, and finally I’ll address Methanex’s claim based on its stock price and its debt rating.

As you heard yesterday, Methanex alleges in this case the ban injured its methanol plant in Fortier, Louisiana. Methanex converted that plant from an idle ammonia factory in 1994. It ran that plant for only four and a half years, and it closed it down in March 1999, before the California ban was even announced.

In assessing the Fortier claim it is helpful to bear in mind some important facts about the U.S. methanol industry. Methanol is made
primarily from natural gas, which in the North American market constitutes up to 90 percent of the production cost of methanol. The Fortier plant's natural gas costs were significantly higher than those in Chile or Trinidad where Methanex has several methanol plants.

If I may draw your attention again to the screen, as you see from this chart, in 1999, for example, natural gas costs at the Henry Hub in Louisiana, where Fortier obtained its natural gas, were around $2.25 for a million BTUs, for a million units, more than four times the 50 cents for a million units in Chile. The Fortier plant's natural gas costs were also higher than those for Methanex's Canadian plants, all of which, incidentally, closed due to their high natural gas costs.

The chart on the screen now is from Methanex's 1997 annual report. As you can see on the far right of this chart, natural gas costs at the Henry Hub where Fortier was located were $2.47 for 1996. It's more than two and a half than the price for Methanex's plants in Medicine Hat. For 1997, it is the same story. You see the natural gas costs were $2.45 in 1997, almost double the costs at Medicine Hat and significantly higher than the natural gas costs from Methanex's plant in Kitimat, British Columbia.

The Fortier plant could not operate
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profitably with such high input costs. Methanex ran its plant well below its capacity, as low as 50 percent in 1998, and by comparison, Methanex ran its methanol plants worldwide at an average rate of between 96 and 98 percent over the last several years. Methanex shut the plant down in 1999 because it was losing money. As Methanex stated in its 1999 annual report, you can see on the screen, Methanex estimated that it saved approximately $9 million per year while the Fortier plant remained idle.

On this next slide, there is a quote from Methanex's Senior Officer, Michael Macdonald. At the time of the Fortier closing Mr. Macdonald explained, referring to Fortier, quote, We are not making money there. In fact, we are hurting. If it were within our control, we would have had the plant down earlier, close quote.

To be clear, Methanex's claim is not that it closed the Fortier plant because of the California measures; rather, it claims that the measures contributed to its decision to keep the plant closed. In other words, Methanex suggests that it might have reopened the plant and run it profitably but for the ban. Methanex, however, provides no documentary evidence for this speculative claim. This is a remarkable omission, given that such a major corporate decision would
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19 surely be reflected in Methanex’s corporate 
20 documents.
21 Rather, as we saw yesterday, Methanex
22

1 relies exclusively on a single line in its 2002 
2 annual report warning, in boilerplate language, 
3 that an MTBE ban across the entire United States 
4 could affect its North American operations, 
5 including its Fortier plant. Methanex’s evidence 
6 is at 19 JS tab 2.
7 Mere speculation as to possible future 
8 events, as I noted, does not establish that 
9 Methanex has incurred a loss as required by Chapter 
10 11. Furthermore, it is hard to see how 
11 Methanex—excuse me—furthermore, it hard to see 
12 how the California ban could have had any material 
13 effect on the Fortier plant, let alone the decisive 
14 effect alleged by Methanex.
15 First, there is no evidence of record that 
16 Fortier ever supplied methanol used to produce MTBE 
17 for California gasoline. On this next slide, there 
18 is a map from Methanex’s 1999 annual report. You 
19 can see the Fortier plant located in Louisiana near 
20 the Gulf of Mexico. The Fortier plant served 
21 customers in the southeastern United States and

454

1 along the Mississippi River, that predominantly

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produced chemical derivatives, not MTBE. If you look at the small arrow just to the left of center of this map, you can see that the California market was served instead by Methanex's plant in Kitimat, British Columbia in Canada. It is difficult to see how an MTBE ban in California could impact a plant in Louisiana that never served the California market.

Second, there is no evidence that the measures indirectly injured the Fortier plant by lowering the global price of methanol, as Methanex contends. In fact, let's be clear: Methanex has admitted that there was no such effect on the global price of methanol. I showed you this slide previously. Methanex's CEO stated in 2002, earnings conference call, quote, We don't expect the impact of this change, referring again to California refiners, no longer purchasing ethanol, to have much of an impact on pricing, if any at all. And again, by pricing Mr. Choquette was referring to methanol pricing.

Furthermore, there is no evidence that the ban caused any depression in the global price of methanol. To the contrary, methanol prices have increased substantially since 1999. If I may draw your attention again to the screen, as you can see from this chart, based on data from Methanex's 2003 annual report, Methanex's average realized methanol price in 1999 was about $105 per metric ton. By
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2003, that had more than doubled to about $220 per metric ton, and it remains at about that level today. So it is hard to see how Fortier was supposedly injured by low methanol pricing as Methanex contends.

Finally, as a factual matter, Methanex's claim that it would have reopened Fortier is implausible as well as speculative. Methanex has for years been telling its investors of its relentless drive to lower production costs by withdrawing its production from the North American market. In fact, this is what Methanex said when it took a write-off on the Fortier plant in 2002.

I draw your attention to the screen. Quote, The Fortier plant has been mothballed since March 1999. The write-off of the Fortier facility reflects our low-cost strategy of reducing our reliance on North American production by expanding our production capacity in Trinidad and Chile. No mention is made of the California ban as a factor in the decision to write off the Fortier plant.

More importantly, Fortier's natural gas prices, which as I noted were already high in 1999, only increased substantially thereafter. As you can see from this chart from Methanex's 2002 annual report, natural gas prices at the Henry Hub near Fortier more than doubled around $2.25 for a million units to around $6. Today that price is
nearly triple the 1999 price at around $6.50. And
I will draw your attention to the yellow line at
the bottom of this chart. That represents
Methanex’s average natural gas costs at around $1.
In other words, as of 2002, Methanex had

1 the option of producing methanol based on natural
gas at a dollar or less in Trinidad or Chile, or it
could have reopened the Fortier plant at a
substantial cost, and produced methanol from
natural gas at $6 or more.
U.S. natural gas prices not only increased
after 1999, they also became increasingly volatile,
making it in the words of one industry leader,
quote, virtual impossible, end quote, to produce
methanol in North America, and that is at 16 JS tab
48 at 1420.
If in 1999 the Fortier plant was, to use
Methanex’s words, hurting economically. It appears
highly doubtful it would have fared any better
thereafter had it been reopened. As we saw
methanol prices increased after 1999, the increase
was not nearly enough to offset the far greater
increases in the cost of natural gas.
In sum, Methanex has failed to produce any
evidence showing that the measures caused any loss
or damage to its closed Fortier plant. Its
unsupported and speculative contention that it might have reopened that plant and somehow run it profitably falls far short of its evidentiary burden under Chapter 11.

Next, I will address Methanex's claim with respect to Methanex-U.S.'s goodwill, customer base, and market share.

The record in this arbitration lacks any competent evidence of Methanex-U.S.'s goodwill. Methanex told us yesterday that it purchased two customer lists in 2002, one for $25 million, and one for $10 million. That is at page 202 of the transcript. That is not evidence of Methanex's goodwill. And the lists allegedly purchased in 2002, well after the ban was announced. Any effect on those customer lists from the California ban, and there is no such evidence, would have been anticipated at the time of purchase. Methanex, in fact, does not demonstrate at all how Methanex-U.S.'s goodwill was supposedly affected by the California measures. This failure of proof by itself is fatal to Methanex's goodwill claim.

Furthermore, Methanex's testimony shows that Methanex-U.S.'s business was thriving after the ban was announced. For example, according to the third Macdonald affidavit, Methanex's revenues increased from $228 million in 1999, to over $300 million in 2002. That is at the third Macdonald
affidavit paragraph 14, 19 JS at eight.

And Methanex-U.S.'s profitability remained basically unchanged during that period. It is thus difficult to understand as a factual matter how Methanex-U.S.'s intangible assets were supposedly severely impaired. Methanex sheds no light on this mystery.

Next, I will address Methanex's claims concerning a loss of the California MTBE market. On the screen you can see a chart we created based on Methanex's export figures for the California market. I will ask you to focus for now just on the dotted line. I will return to this chart a little later and describe the other information in the chart. The dotted line is a graphical representation of evidence provided by Methanex in the second Macdonald affidavit. The line represents Methanex's exports from Kitimat, British Columbia in Canada, to California, and it shows exports declining from around 132,000 metric tons in 1998, to a little more than 50,000 metric tons by 2001. This is Methanex's evidence that it lost a valuable market as a result of the ban. This evidence fails to establish any loss to Methanex for several reasons.

First, as a matter of law, such a claim cannot establish a breach under Chapter 11 of the NAFTA, which pertains solely to investments in the
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territory of the respondent party, not to trade in goods. These sales figures given by Methanex represent cross border trade in goods. Trade in goods is expressly excluded from ambit of Chapter 11 and is covered in other chapters of the NAFTA. This reason alone is sufficient to dismiss Methanex's claims.

Second, there is a critical distinction between revenues and profits. Looking at the dotted line, the decrease in Methanex's exports as shown here only tells us what happened to Methanex's revenues with respect to the California market. The record is silent as to any lost profits as a result of the ban. And, in fact, it is highly doubtful that the California market was profitable for Methanex. As I pointed out on the map I showed you earlier, Methanex exported methanol to California from its plant in Kitimat, British Columbia. Methanex closed that plant in mid-2000 because it was losing money. Let me draw your attention again to the screen. This is what Methanex stated in its May 2000 press release. The Kitimat methanol plant has been losing substantial sums of money for some time primarily due--there's a typo there--primarily due to very high natural gas costs. Furthermore, Methanex has not even alleged that it had a net decrease in revenues. Rather,
Methanex concedes that it simply sold any methanol it would have sold in California elsewhere. As you can see from this quote on the screen, from the third Macdonald affidavit, Mr. Macdonald states that, quote, After the California ban was announced, Methanex largely moved its sales out of the California MTBE sector and restructured its sales to other U.S. MTBE producers.

Furthermore, in the very tight market conditions prevailing in 2002 and 2003, Methanex was running its plants at very close to full capacity. In fact, Methanex was struggling to meet its existing contractual commitments and could only do so by purchasing additional methanol on the spot market at a considerable loss. As Methanex's CEO described the situation to the company shareholders in early 2003, quote, and I have the quote up on the screen, We currently are on order control. In other words, Methanex wasn't able to accommodate more orders for methanol. Thus, while Methanex's sales may have shifted from one market to another, there was no net decrease in revenues and no production capacity that went unused as a result of the California ban.

Finally, the record belies Methanex's contention that it exported less methanol to
Mr. Miller's data shows that demand was, in fact, increasing in those years. There is, thus, no causal relationship between what was happening in the California MTBE market and Methanex's decision to export less methanol to that market.

Methanex has not disputed Mr. Miller's data. As a matter of fact, Methanex has not referenced Mr. Miller at all. Instead, Methanex alleges, again, without any evidence, that it simply was mitigating its damages by withdrawing from the California market. We submit that
Methanex's contention that it was mitigating damages by withdrawing from a growing market years before the ban is simply implausible. The far more likely explanation is that Methanex exported less methanol to California because it was losing money on every gallon of methanol it produced at its money-losing plant in Kitimat, British Columbia, and sold into that market.

As a final note, while we have this chart in front of us, I would just like to give you a sense of the size of the methanol market at issue. Methanex has labored to create the impression in this case that it lost an enormous and valuable market. For instance, Methanex yesterday stated that, quote, California, in and of itself, is a very big market. It is one of the biggest markets for methanol in the world because it is a huge economy, and the market for MTBE in California itself is a very big market. So, the loss of the market, in and of itself, is a big loss for a company like Methanex, and that is at pages 204 and 205 of the transcript. Methanex also noted at page 140 of the transcript that the California ethanol market was about $1.8 billion. The impression that Methanex seeks to create is false.

As you see from this chart, Methanex alleges that it sold 50,000 metric tons of methanol in 2001. Methanex did not provide any data after...
21 2001, so these are the most recent figures we have.

1 How much is that market worth to Methanex? Well,
2 Methanex sold approximately 7.4 million metric tons
3 of methanol that year, so the California market at
4 issue was less than one percent of Methanex's
5 global sales. It was around 0.7 percent. In
6 dollar terms, that market was less than $9 million
7 in revenue, and more importantly, the market was
8 not profitable. From this perspective, it is easy
9 to see why Methanex has been telling its investors,
10 it's been telling its shareholders, for years, that
11 it has not felt any impact from the loss of the
12 California MTBE market, and the California ban is
13 no big deal.
14 Finally, I will address Methanex's stock
15 price and credit rating claims. As you heard
16 yesterday, Methanex alleges that its average stock
17 price declined about 20 percent in early 1999.
18 Methanex also alleges injury based on the downgrade
19 of its long-term credit rating, also in early 1999.
20 These claims are without merit for the following
21 reasons: First, with respect to the stock price

claim Methanex points to no case in which an
international Tribunal has awarded damages based on
its radical theory that states are responsible to
corporations for fleeting changes in the price of their shares. Such an event on its face is not a loss to the corporation. The corporation does not own stock in itself.

In fact, Methanex has previously stated that it does not base any claim on its share price. Let me draw your attention again to the screen. In paragraph 86, to its reply to the statement of defense from August of 2000, Methanex states, quote, Methanex's damage claim is not based on a loss of share value. Because Methanex has expressly disavowed any stock price claim in this case, it is unclear why Methanex continues to discuss it here.

Even if the Tribunal were to consider this allegation, however, it is without merit for several other reasons. First, there is a significant causation problem. The stock price change alleged by Methanex occurred years before the ban. Methanex said yesterday they didn't think that was a problem. We think that presents a big problem to Methanex's claim. At best, a minor price movement years before the ban reflects investors' mere concern about the possible future effects on the company, an effect that Methanex has later confirmed time and time again to its shareholders did not occur.

In fact, nothing demonstrates the
impossibility of attributing a temporary stock
price movement to the ban more clearly than the
fact that throughout this arbitration Methanex has
been unable to settle on which stock price
movements it seeks to use.

I have on the screen a chart showing
Methanex's stock price from mid-1998 to the end of
2000. In Methanex's reply to the U.S. Statement of
Defense at paragraph six, Methanex alleged a
one-day drop, on March 26, 1999, the day after the
announcement of the ban. That is represented by

the yellow line. That was the first iteration of
Methanex's claim. In its Second Amended Statement
of Claim, Methanex decided, without explanation, to
expand its claim to the ten-day period following
the March 25 announcement. And that is represented
by the red bar. That was Methanex's second
 iteration of its claim. Incredibly, yesterday,
Methanex showed you a slide suggesting that they
now base their claim on a seven-day period in
January 1999, even before the ban was announced.
That was Methanex's third iteration of its claim

PRESIDENT VEEDE: Do you have a
transcript reference?

MR. McNELL: It was Exhibit 73, and I
don't have a transcript reference, but I can
provide that.

It is clear that Methanex has no idea what
price movements it thinks were actually caused by

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the ban. Methanex's stock price claim has other serious problems as well. Methanex showed us yesterday a number of analysts' reports suggesting concern over a nationwide MTBE ban that allegedly put downward pressure on Methanex's stock price. Professor Reisman asked Methanex how it accounted for the contribution from California, and the contribution from the rest of the United States. Methanex's response, incredibly, was that it was claiming for all bans across the United States. California, says Methanex, is an, quote, environmental front runner and other U.S. state legislatures mindlessly follow California on environment matters. All the bans, says Methanex, should be laid at California's doorstep. And that is at page 206 of the transcript.

That proposition is, of course, absurd. The fact is, Methanex cannot separate out concern over California versus concern over what might happen in the rest of the country.

Furthermore, as you can see, the alleged periods of decline occurred during a significant downtrend in Methanex's stock price caused by the cyclical decline in methanol prices. In early 1999, methanol prices were, in fact, at their
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lowest level in more than ten years. Methanex offers no explanation of how it could possibly separate out any effects from concern over MTBE in California, from effects due to the historically low methanol prices.

Finally, as you can see, Methanex's stock price recovered fairly quickly to about $12. This is $12 Canadian, by the end of 2000. That price, as you can see, is higher than the stock price before the ban was announced.

Yesterday, Methanex's stock price was trading around $17 on the Toronto exchange. The 20 percent drop has thus been recovered many times over. Methanex does not explain how an alleged minor and temporary decline in 1999 could possibly be quantified today.

Finally, Methanex's claims with respect to the temporary downgrade in its long-term debt rating fail for many of the same reasons. First, Methanex points to no case in which an international Tribunal has awarded damages based on a temporary downgrade. Second, there is no basis for attributing the downgrade solely or even primarily to the California measures.

Let's take a look at the 1999 Fitch IBCA report that Methanex showed you yesterday. That report directly refutes that the ban was the primary reason for the rating action. As you can
see on the screen, that report states, quote, This
erating action is primarily due to deterioration of
methanol price caused by oversupply. In fact, this
was the first line of the report. Methanex skipped
over that first line and showed you a few snippets
that dealt with MTBE.

Finally, Methanex is unable to produce any
evidence that the corporation was actually injured
by the downgrade. Rather, by Methanex's own
admission, it is merely a hypothetical loss. This
is what the third Macdonald affidavit says: The
practical impact of the downgrades was to increase
the cost of any new debt the company might have

Notably Methanex offers no evidence to
suggest that it did, in fact, raise new debt at any
relevant time, or that the downgrade had any
adverse effect on the terms of that debt. Methanex
cannot state a claim under Articles 1116 and 1117,
based on hypothetical or speculative losses.

Those articles require actual existing
losses. Because Methanex has not produced any
evidence of actual existing losses and it has
admitted that no losses exist, its claims, we
submit, should be dismissed in their entirety.

If the Tribunal has any questions, I would
be pleased to answer them. Otherwise, I will turn
the matter over to Mr. Bettauer.

PRESIDENT VEEDER: Thank you very much.
We have no questions at this stage.

MR. MCNEILL: Okay. May I just add that the citation you requested was page 213, lines nine through 19. That is related to tab 73 or Exhibit 73, which I noted.

PRESIDENT VEEDER: Thank you very much.

MR. BETTAUER: Since it is late, I will take two minutes and wrap up our presentation for today. The presentation on proximate cause has not been lengthy, and I don't intend to repeat it. Suffice it to say, in this part of our presentation we have established two additional grounds for dismissal of the case before us. First, Mr. Legum showed that the chain of causation in this case is an extraordinarily weak one. Methanex's claim depends upon the impact of the ban upon suppliers, to suppliers, to persons directly affected. The impact alleged here is far too remote to stand under established principles of international law.

Second, Mr. McNeil demonstrated that the record shows no loss to Methanex caused by the measures in any event. The Fortier plant was idle before the 1999 Executive Order and did not even serve the California market before it was idled. There is no evidence of record to support Methanex's implausible contention that it might
have reopened the plant and run it profitably but for the ban.

With respect to Methanex-U.S., Methanex has provided no evidence of any loss of goodwill or market share. In fact, Methanex's own testimony demonstrates that Methanex-U.S.'s revenues have only increased since the ban was announced. Methanex's inability to demonstrate any loss or damage resulting from the California ban should come as no surprise. As Mr. McNeil pointed out, Methanex's senior officers have repeatedly represented to its investors and the public that the MTBE ban had no impact on the company. Methanex's failure to prove any loss caused by the measures by itself requires dismissal of all its claims.

Mr. President, this concludes our presentation for today. We will resume tomorrow morning by addressing each of Methanex's claims under Articles 1102, 1105(1), and 1110, as well as Methanex's failure to provide appropriate proof of ownership of investments in the United States.

Thank you for your attention.

PRESIDENT VEEDER: Thank you. My colleague has, I think, one question to raise.

ARBITRATOR ROWLEY: Mr. Legum, this morning the President asked you with respect to the
jurisdictional issue, which we have joined to the merits, whether we were to decide that on the basis of assuming the pleading to be true, and I believe you gave a provisional answer which I understood to be, no, we were to decide it on the evidence, not on the pleadings and you said you were going to consult further. First, have I understood your answer correctly, and secondly, have you consulted further, and are you in a position to speak to that point?

MR. LEGUM I have, and the answer that I gave earlier stands. At least our understanding is that the procedure is that the jurisdictional issue has been joined to the merits; and therefore, as part of the merits, the Tribunal will address it based on the evidence that the parties have compiled, rather than based on assumptions and inferences from lines in the pleadings. Of course, to the extent that the First Partial Award assumed facts that are consistent with the facts that have been demonstrated in the record, such as the competition between methanol as a feedstock and ethanol as a finished product, to the extent the Tribunal assumed facts and decided based on those assumed facts in a certain way, our view is that that is the binding law to the extent that the facts that have been proven turn out to be, as we believe they are, fully consistent with the facts that the Tribunal has assumed.
I hope that didn't add more confusion than enlightenment to the question.

ARBITRATOR ROWLEY: Thank you very much.

PRESIDENT VEEDE: We come to the end of day two, and as Mr. Bettauor has indicated, we will start again with the further oral submissions for the United States tomorrow morning.

Unfortunately, as you all know, we have another matter to deal with and we break now for ten minutes and we will resume on the tenth floor for a further meeting in regard to this other matter. Thank you.

(Whereupon, at 5:41 p.m., the hearing was adjourned until 9:30 a.m. the following day.)
CERTIFICATE OF REPORTER

I, David A. Kasdan, RDR-CRR, Court Reporter, do hereby testify that the foregoing proceedings were stenographically recorded by me and thereafter reduced to typewritten form by computer-assisted transcription under my direction and supervision; and that the foregoing transcript is a true record and accurate record of the proceedings.

I further certify that I am neither counsel for, related to, nor employed by any of the parties to this action in this proceeding, nor financially or otherwise interested in the outcome of this litigation.

DAVID A. KASDAN, RDR-CRR

CERTIFICATE OF REPORTER

I, Cathy Jardim RPR, Court Reporter, do hereby testify that the foregoing proceedings were
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5 stenographically recorded by me and thereafter
6 reduced to typewritten form by computer-assisted
7 transcription under my direction and supervision;
8 and that the foregoing transcript is a true record
9 and accurate record of the proceedings.
10 I further certify that I am neither
11 counsel for, related to, nor employed by any of the
12 parties to this action in this proceeding, nor
13 financially or otherwise interested in the outcome
14 of this litigation.

--- CATHY JARDIM, RPR ---