

**In the Matter of the Arbitration Proceedings Pursuant to NAFTA Chapter 11 and the  
UNCITRAL Arbitration Rules between:**

**GAMI INVESTMENTS, INC.**

**Claimant/Investor,**

**AND**

**THE GOVERNMENT OF THE UNITED MEXICAN STATES**

**Respondent/Party.**

---

**GAMI'S REPLY  
TO  
MEXICO'S STATEMENT OF DEFENSE**

---

Guillermo Aguilar Álvarez  
Lucía Ojeda  
Elsa Ortega  
Itziar Esparza

**SAI ABOGADOS**  
Edificio Plaza Reforma  
Prol. Paseo de la Reforma #600-103  
Mexico, D.F. 01210

Charles E. Roh, Jr.  
Adam P. Stochak  
J. Sloane Strickler  
Alicia Cate

**WEIL GOTSHAL & MANGES LLP**  
1501 K Street, N.W.  
Suite 100  
Washington, D.C. 20005

Attorneys for Investor  
*GAMI Investments, Inc.*

February 5, 2004

## TABLE OF CONTENTS

	<b>Page</b>
I. INTRODUCTION .....	1
II. CORRECTING THE FACTUAL RECORD.....	4
A. Mexico Was Responsible For Its Own Failure To Enforce And Implement Its Sugar Program .....	4
B. Mexico’s Operation of the Sugar Program .....	8
1. Reference Price System And Its Adjustment.....	8
2. Export Of Surplus Sugar.....	13
a. Mexico Was Responsible Under The 1997 Acuerdo For Allocating Export Quotas .....	14
b. Mexico’s Failure To Enforce The Export Requirements.....	15
c. Wholly Mexican-Owned Mills Were Obligated To Comply But Did Not.....	17
d. Grupo CAZE.....	18
e. Action by Mexico .....	20
3. Base Production Levels.....	20
C. Factors Beyond Mexico’s Control Do Not Explain Mexico’s Failure To Protect The Domestic Price Of Sugar As Required By The Sugar Program.....	24
D. The Expropriation Of GAM’s Mills Was Unjustified And Discriminatory .....	27
1. Mexico Incorrectly States GAM’s Debt to the Cañeros .....	27
a. 1999/2000 Harvest.....	27
b. 2000/2001 Harvest.....	29
2. Suspensión de Pagos .....	32
3. The Administrative Record Fails To Support The Government’s Rationale For Expropriation .....	33
III. LEGAL ARGUMENT.....	38
A. The Tribunal Has Jurisdiction Over Each Of GAMI’s Claims.....	38
B. ARTICLE 1105.....	39
1. Mexico Arbitrarily Implemented And Enforced The Sugar Regime.....	39
a. It Is Irrelevant That Surpluses And Depressed Prices Are Not A Violation Of International Law .....	40

**TABLE OF CONTENTS**  
**(continued)**

	<b>Page</b>
b. A Measure May Be Found To Be Arbitrary Without First Being Challenged As Illegal Under Domestic Law In The Host State’s Courts .....	40
c. Mexico’s Failure to Implement And Enforce The Sugar Regime .....	42
(1) Mexico Is Legally Responsible For The Failure Of The Sugar Regime.....	42
(2) Mexico’s Arbitrary Implementation Of Its Sugar Regime Constitutes A Breach Of Article 1105.....	44
2. Mexico Arbitrarily Expropriated GAMI’s Investment .....	46
C. ARTICLE 1102.....	49
1. In Like Circumstances .....	50
2. It Is Not necessary To demonstrate Intent To Discriminate Based On Nationality To Establish A Violation Of Article 1102 .....	54
D. ARTICLE 1110.....	57
1. Mexico’s Own Courts Have Determined That The Expropriation Decree Did Not Delineate A Valid Public Purpose .....	58
2. Mexico Expropriated GAMI’s Shares In GAM In A Discriminatory Manner .....	59
3. The Expropriation Was Not Carried Out In Accordance With The Minimum Standards of Article 1105 .....	60
4. Mexico Has Not Provided The Required Compensation.....	60
5. The Tribunal Is Fully Competent To Evaluate Article 1110 Claims.....	61
6. Regardless of Domestic Law And Domestic Proceedings, GAMI’s Claims Remain Valid and Pertinent.....	61
7. GAM’s Entry Into Suspensión De Pagos Does Not Negate GAMI’s Claim To Compensation Or Violate The Rights Of Creditors .....	64
E. GAMI Did Not Assume The Risk That Mexico Would Breach Its Treaty Obligations.....	65
IV. VALUATION .....	68
A. Legal Principles Relating to Valuation and Calculation of Damages.....	68
1. Navigant’s Valuation Is Appropriate .....	69
2. FGA’s Methodologies Are Fatally Flawed.....	72

**TABLE OF CONTENTS**  
**(continued)**

	<b>Page</b>
V. CONCLUSION.....	73

## I. INTRODUCTION

1. GAMI Investments, Inc. (“GAMI”) submits this reply to the United Mexican States’ (“Mexico,” “the Government,” or “Respondent”) Statement of Defense (*Escrito de Contestación*) dated 24 November 2003.<sup>1</sup>

2. Mexico acknowledges that the sugar industry is unique, both in Mexico and globally, characterized by extraordinary levels of Government economic regulation designed to protect important social interests such as nutritional security and the health of the agricultural economy. There is no dispute that *cañeros* and mills exist in a situation of mutual dependence, yet can have opposing interests. Mexico further concedes that it has undertaken significant economic regulation of the Mexican sugar industry to ensure that critical national interests are protected and to regulate the economic relation relationship between the *cañeros* and the mills.

3. Notwithstanding these undisputed facts, however, Mexico attempts to absolve itself of any responsibility for economic regulation of its domestic sugar industry, urging that Mexico’s sugar program “is not based on Government leadership,” but rather on negotiation between the mills and the *cañeros*.<sup>2</sup> Alternatively, Mexico tries to blame external problems in global markets and in U.S. policies. These arguments defy both logic and law. If the regulation of sugar production were simply a matter of commercial negotiations between the mills and the *cañeros*, there would be no need for the Sugarcane Decree<sup>3</sup> and its implementing *acuerdos*.<sup>4</sup> These

---

<sup>1</sup> Henceforth, we shall refer to Mexico’s submission of 24 November 2003 as “Statement of Defense” and to this memorial as “GAMI’s Reply.”

<sup>2</sup> Statement of Defense, para. 77.

<sup>3</sup> *Decreto por el que se declaran de interés público la siembra, el cultivo, la cosecha y la industrialización de la caña de azúcar* (31 May 1991) (Exh. C-20) and later amended by *Decreto por el que se reforma el diverso por el que se declara de interés público la siembra, el cultivo, la cosecha y la industrialización de la caña de azúcar* (27 July 1993) (Exh. C-21).

<sup>4</sup> *Acuerdo por el que se establecen reglas para la determinación del precio de referencia del azúcar para el pago de la caña de azúcar* (25 March 1997) (Exh. C-23) (the “1997 Acuerdo”); *Acuerdo que reforma al diverso que establece las reglas para la determinación del precio de referencia del azúcar para el pago de la caña de azúcar* (31 March 1998) (“1998 Acuerdo”)

documents are not merely frameworks for negotiations among the parties. They are binding legal requirements of Mexican law, created by the government and subject to enforcement by the government, as explained in the attached Expert Opinion of Ulises Schmill, former Chief Justice of the Supreme Court of Mexico.<sup>5</sup> And blame cannot be shifted to external pressures, when the sugar program, properly carried out, has all the tools needed to offset those external pressures.

4. GAMI invested US\$30 million in the Mexican sugar industry, relying on the international commitments of the Mexican Government in NAFTA, and the domestic commitment of the Government to a strong sugar program. The Mexican program should have worked to regulate domestic supply and demand for cane and sugar, but did not. Essentially, the Government assured prices to *cañeros* for cane well above what would result from market forces without government intervention. The Government failed, however, to implement and enforce the measures that would have result in a domestic price of sugar sufficient to provide a reasonable margin for the mills. Having driven the industry into economic difficulties, the Government abruptly and arbitrarily expropriated 27 mills.

5. Mexico is a sovereign nation and it has substantial leeway to regulate its sugar industry as it sees fit to protect whatever national, local, collective, or individual interests it deems most important, but only in conformance with the norms of international conduct and its treaty obligations. What it cannot do, however, is what has happened here: turn the voluntary investment of a U.S. investor into an involuntary contribution of its capital into whatever domestic social or political group the Mexican Government wishes to favor. The facts here are unambiguous. GAMI's US\$30 million investment in Grupo Azucarero Mexico, S.A. de C.V.

---

(Exh. C-25); *Acuerdo por el que se ponen a disposición de los ingenios azucareros las cuotas de exportación por ingenio para la zafra 1999-2000 y los niveles de producción base por ingenio que surtirán efectos a partir de la zafra 2000-2001* (9 March 2000) (the "2000 Acuerdo") (Exh. C-33).

<sup>5</sup> Expert Opinion of Former Chief Justice Ulises Schmill Ordoñez (Exh. C-11D) ("Schmill Opinion").

(“GAM”) was used to reduce debt and improve productivity at GAM’s sugar mills. The effect of Mexico’s Governmental conduct was to transfer that capital to the *cañeros* in the form of inflated payments for cane and, finally, to the Mexican Government itself via the expropriation. There can be no serious doubt that NAFTA requires compensation under these circumstances.

6. As argued in the Statement of Claim, this case is, at its core, a simple one, for there is no dispute that Mexico expropriated GAM’s five sugar mills and thereby indirectly expropriated GAMI’s minority shareholder interest in the company by making it worthless.<sup>6</sup> GAMI further argued in its Statement of Claim that the only matter properly in dispute with respect to the expropriation claim under Article 1110 is, or should be, the measure of damages, and provided an expert valuation opinion by Navigant Consulting supporting its claim for damages of not less than US\$27.8 million.<sup>7</sup> Faced with the irrefutable fact of the expropriation, Mexico offers no defense to GAMI’s claim under Article 1110, except to repeat its previously asserted – and refuted – objections to the jurisdiction of the Tribunal.<sup>8</sup> Mexico likewise has no real defense for its breaches of the standards of treatment required under Article 1102 and 1105. Mexico presents no new evidence or argument in its Statement of Defense sufficient to overcome GAMI’s *prima facie* claim of liability for breaches of Article 1110, 1105, or 1102.

7. Mexico chooses to address the fundamental question of the quantum of damages due by ignoring it, offering no valuation of its own. Mexico’s valuation expert, Fausto García Lopez, expressly states that he was not asked to provide a valuation of GAM, or GAMI’s interest in GAM, and his report is limited to a critique of the assumptions underlying the Navigant

---

<sup>6</sup> Statement of Claim, para. 2.

<sup>7</sup> *Id.* at paras. 2, 149.

<sup>8</sup> This is in direct contravention of the Tribunal’s direction to the parties, in paragraph 3 of Procedural Order No. 4, that they make no further submissions on jurisdictional issues absent an invitation to do so from the Tribunal.

valuation.<sup>9</sup> As discussed below, the assumptions underlying the Navigant valuation are wholly appropriate under NAFTA and properly control for the damage to GAMI's investment caused by Mexico's failure to implement and enforce its own laws and rules relating to economic regulation of the Mexican sugar industry, resulting in a valuation that measures the "fair market value of the expropriated investment immediately before the expropriation took place" in accordance with Article 1110(2). The Rebuttal Report of Navigant Consulting, submitted herewith, amply demonstrates that the FGA critique is factually incorrect and methodologically flawed.

8. This Reply demonstrates that Mexico's arguments are factually incorrect and legally flawed, and that its valuation evidence is insufficient and methodologically unsound. Section II addresses the factual inaccuracies in Mexico's Statement of Defense. In Section III, we respond to Mexico's legal defenses and explain why Mexico has failed to refute GAMI's claims under Articles 1102, 1105, and 1110 of NAFTA. Finally, section IV addresses the critical question of valuation.

## **II. CORRECTING THE FACTUAL RECORD**

9. Mexico's response to most of GAMI's claims is based on simple misrepresentations of fact. To avoid repetition of common points of fact under each claim in the legal argument, this Section t of GAMI's Reply addresses Mexico's most important factual errors and omissions with respect to Mexico's sugar laws and the Government's powers and responsibilities, as well as the status of GAMI, GAM and the Mexican and world sugar markets.

### **A. Mexico Was Responsible For Its Own Failure To Enforce And Implement Its Sugar Program**

10. Mexico devotes a large part of its answer to an effort to shift the blame for the failure of its sugar program to the private sector or external factors.<sup>10</sup> Mexico asserts that it acted merely

---

<sup>9</sup> F. García Asociados, *Análisis y Comentarios Sobre La Valuación Presentada Por: "Grupo GAM"* (SOD Exh. R-16) ("FGA Report").

<sup>10</sup> See, e.g., Statement of Defense, paras. 3-54, 171-177.

as an observer in the application and enforcement of the Mexican sugar program.<sup>11</sup> The facts, as set out in GAMI's Statement of Claim and in Mexico's own answer and public documents, belie this effort to avoid responsibility.

11. The Mexican sugar program is essentially set out in five legal instruments issued by the Executive Branch of the Mexican Government and published in the *Diario Oficial de la Federación*: the 1991 Sugarcane Decree, its amendments of 1993 and the 1997, 1998 and 2000 *Acuerdos*.<sup>12</sup> As testified by Former Chief Justice Schmill,<sup>13</sup> the pervasiveness of the Government's role in the Sugar Program is evident from consideration of the legislative and executive grant of authority to the *Secretaría de Agricultura, Ganadería, Desarrollo Rural, Pesca y Alimentación* ("SAGARPA"),<sup>14</sup> the *Secretaría de Economía* ("SE")<sup>15</sup> and the *Secretaría de Hacienda y Crédito Público* ("SHCP").<sup>16</sup>

12. Mexico does not dispute the basic legal framework, all of which devolves from the Mexican State:

- The Mexican sugar industry operates subject to legal framework created by the Sugarcane Decree published in 1991, which declared that the sowing, cultivation, harvest and industrialization of sugarcane has been declared to be "of public interest" by the Mexican Government.<sup>17</sup>

---

<sup>11</sup> *See id.*, paras. 112, 119-120, 128, 131.

<sup>12</sup> Schmill Opinion, paras. 100-101 (Exh. C-110).

<sup>13</sup> *See id.* paras. 23-35 and 101.

<sup>14</sup> "Ministry of Agriculture, Livestock, Rural Development, Fish and Nutrition." SAGARPA was formerly known as "SAGAR."

<sup>15</sup> The *Secretaría de Economía* ("Ministry of the Economy") was known as the *Secretaría de Comercio y Fomento Industrial* ("Ministry of Commerce and Industrial Promotion") ("SECOFI") until 2000. Because the decrees and *acuerdos* cited herein refer to SECOFI, both names are used interchangeably in this brief.

<sup>16</sup> Ministry of Finance and Public Credit.

<sup>17</sup> Sugarcane Decree, art. 1 (Exh. C-20). Former Chief Justice Schmill has testified as to the implications of this declaration. *See* Schmill Opinion, paras 38, 39 and 103 (Exh. C-110).

- The Sugarcane Decree and its implementing regulations and resolutions were issued by the Executive Branch of the Mexican Government to establish a regime governing the economic relationship between the *cañeros* and the mills;<sup>18</sup>
- Both the CAA and the JCACA, which are bodies designed to implement the objectives of the Sugarcane Decree, have been created by regulatory action of the Executive Branch of Government;
- The Government holds two of the six seats in both the CAA and the JCACA; and holds the deciding votes in each;

13. Under this framework, the Mexican Government had the responsibility to:

- Act in a manner that would result in “strict compliance” with the Sugarcane Decree and its implementing rules;<sup>19</sup>
- Issue rules and guidelines to regulate the relationship of mutual dependence between *cañeros* and mills; and<sup>20</sup>
- Issue such rules as may be required to effectively implement the Sugarcane Decree.<sup>21</sup>

14. Finally, the Government had the responsibility under the different regulations to generate or maintain and publish the following reliable data required for the adequate operation of the sugar program: domestic production and consumption (Article 3(III) of the 1997 *Acuerdo*; third paragraph of Article 1 of the 2000 *Acuerdo*); export quotas (Articles 4(III) and 5(II) of the 1997 *Acuerdo* and Article 5(IV) of the 1998 *Acuerdo*); sugar export volumes and prices (Article 4(II) of the 1997 *Acuerdo*); mill base production levels (Article 3(II) of the 1998 *Acuerdo* Article 2d of the 2000 *Acuerdo*).<sup>22</sup>

---

<sup>18</sup> *Id.*, para. 68.

<sup>19</sup> Sugarcane Decree, art. 4(a) (Exh. C-20).

<sup>20</sup> *Id.*, art. 4(b).

<sup>21</sup> *Id.*, art. 4(c).

<sup>22</sup> See Exh. C-23 (1997 *Acuerdo*); Exh. C-25 (1998 *Acuerdo*); Exh. C-33 (2000 *Acuerdo*);

15. It is also true that the implementation of the Sugarcane Decree and *Acuerdos* called for involvement of both the *cañeros* and the mills, the key private sector participants in the industry. As described in Mr. Antonius' Report submitted as part of GAMI's Statement of Claim, given the semi-perennial nature of sugar cane and the need for this raw material to be processed in adjacent mills, the *cañeros* and the mills live in a situation of mutual dependence.<sup>23</sup> Their interests conflict, however, as a higher price for *cañeros* means higher costs and less profit for mills. One of the motivations for a governmentally enacted sugar program is to deal with the inevitable tensions in that relationship.<sup>24</sup> The history of the industry in Mexico attests to the fact that, absent centrally enforced and transparent public rules, achievement of this equilibrium is impossible.

16. The Government has, and must have, the decisive role in the implementation of the law. Private sector actors may be consulted, and the decisions may be portrayed as a consensus, but the Government's deciding vote is what controls when *cañeros* and mills are unable to agree due to the natural tension in their interests.<sup>25</sup> Further, all participants know that the availability of other discretionary Government benefits (and disincentives), as well as the political power of the *cañeros*, means that mills in effect must acquiesce to Government wishes.

17. Former Chief Justice Schmill confirms that the Government had the necessary authority to secure protection of the domestic price of sugar and that, given the Government's own declaration that the sugar sector was of public interest, it was required to directly and

---

<sup>23</sup> See Andrés Antonius González, *The Mexican Sugar Industry 1991-2001*, p. 6 (January 2003) (Exh. C-19) ("Antonius First Report").

<sup>24</sup> Both Mr. Santos, a former mill owner, and Mr. Cruz, a *cañero* representative, attest to this acrimony. See Witness Statement of Alberto Santos, para. 6 (Exh. C-114) ("Santos Statement"); Witness Statement of José Cruz Romero Romero, p. 12 (Exh. C-113) ("Cruz Statement").

<sup>25</sup> See Santos Statement, paras. 6-8 (Exh. C-114); Cruz Statement, pg. (Exh. C-113).

permanently intervene to enforce the objectives of the Sugarcane Decree and the 1997, 1998 and 2000 *Acuerdos*.<sup>26</sup>

## **B. Mexico's Operation of the Sugar Program**

18. There is no dispute between the parties as to the existence of at least three instruments in the Mexican sugar program to ensure that all participants be profitable and remain viable: (i) the reference price formula and its adjustments for determination of prices that mills would pay to the *cañeros* for their cane; (ii) the requirement for the mills to export surplus sugar; and (iii) the enforcement of per mill base production program. These elements are supposed to operate to assure a fair price to *cañeros* for their cane, and a fair domestic Mexican price for sugar, so that the mills have a sufficient refining margin. In reality, these three elements of the sugar program were implemented and enforced in way that resulted in a relatively high compensation to the *cañeros* that was not balanced by enforcement of measures to provide a commensurate return for sugar mills. In particular, the pricing formulas favored the *cañeros*, but the export control and production control mechanisms were enforced arbitrarily or not at all, leading to surpluses of sugar in the domestic market and a depressed domestic price.

### **1. Reference Price System And Its Adjustment**

19. As explained in paragraph 44 of the Statement of Claim, the 1997 *Acuerdo* introduced a formula to calculate a national reference price for sugar that would serve to determine the price for sugarcane in a manner that was responsive to actual market conditions.<sup>27</sup> The reference price was to be determined by a weighted average of the sugar prices received in the domestic market, the price for the exports to the United States market within the restricted U.S. quota and the prices from exports of surpluses to the (low-priced) world market. Under the formula, if production increased so that a higher proportion of that production was sold in the low-priced

---

<sup>26</sup> Schmill Opinion, paras. 100-101 (Exh. C-110).

<sup>27</sup> See 1997 *Acuerdo*, art. 3 (Exhibit C-23).

world markets, the reference price would decrease as well. To the extent that *cañeros* were to receive a percentage of the reference price for their sugarcane, return to the *cañeros* would consequently also decrease. Accordingly, *cañeros* and mills would always share both in the upside and in the downside of the prices at which sugar was effectively sold.

20. Mexico asserts that the reference price formula was merely a mathematical exercise using objective data published in the Official Journal,<sup>28</sup> but the facts show that a critical factor was what estimated price data was put into the formula. That choice of price data resulted in a reference price considerably higher than the market reality in the crucial two years prior to the expropriation.

21. Thus, under pressure from the *cañeros*,<sup>29</sup> the Government revised the reference price for the 1998-1999 harvest upwards to \$3,688.43 pesos per ton from 3,515.83 per ton.<sup>30</sup> In addition, the Government further inflated the reference price in a manner inconsistent with the reference price formula of Article 3 of the 1997 *Acuerdo* by ordering mills to make additional payments for sugarcane as follows:

- an added 1.38 percent for the 1997-1998, 1998-1999 and 1999-2000 harvest seasons;<sup>31</sup> and
- an extra 2.0 percent for the 1997-1998 harvest season.<sup>32</sup>

Accordingly, the reference price which resulted from application of the formula set out in Article 3 of the 1997 *Acuerdo* was inflated as indicated below:

#### **Comparative Reference Price Figures per Harvest Year**

---

<sup>28</sup> Statement of Defense, para. 118.

<sup>29</sup> See, e.g., Press Release from *Cañero* Unions (18 November 1998) (Exh. 123).

<sup>30</sup> See Reference Price for 1998/1999 Harvest (Exh. C-121).

<sup>31</sup> See *id.*; 1998 *Acuerdo* (Exh. C-25).

<sup>32</sup> 1998 *Acuerdo* (Exh. C-25).

(Pesos/Ton)

Harvest Season	Reference Price by Application of the Reference Price Formula	Reference Price After Government Mandated Increase	Difference
1997 – 1998 <sup>33</sup>	3,512.63	3,632.33	119.70
1998 – 1999 <sup>34</sup>	3688.43	3,739.33	50.90
1999 – 2000 <sup>35</sup>	4,295.21	4,354.49	59.28

22. In and of itself, this departure by the Government from the mandatory reference price formula set out in the 1997 *Acuerdo* defeated the vital purpose of tying the price of sugarcane to the price of sugar. While the price of sugar would continue to respond to actual market forces, the price of sugarcane was, once again, arbitrarily fixed by the Government at levels inconsistent with the published reference price formula.

23. The inflation of the reference price was aggravated because the adjustment mechanism, which was supposed to deal with situations when the actual market price of sugar did not conform to the reference price, in practice did not function. Article 4 of the 1997 *Acuerdo* requires that the reference price formula be run with actual numbers at the end of the harvest year. It also requires per mill calculations and industry-wide data to be provided by the SHCP.

24. In turn, Article 5 provides a mechanism to adjust the pre-liquidation reference price to calculate the price for the final liquidation of the sugarcane. Accordingly, Article 5:

---

<sup>33</sup> *Actas de las Reuniones del Grupo de Trabajo del Balance Azucarero de 1996 a 2001* (SOD Exh. R-48).

<sup>34</sup> *Determinación del precio de referencia del azúcar para el pago la caña de azúcar durante la zafra 1998/1999*, Diario Oficial (15 January 1999) (“Reference Price for 1998/1999 Harvest”) (Exh. C-121).

<sup>35</sup> *Determinación del precio de referencia del azúcar para el pago la caña de azúcar durante la zafra 1999/2000*, Diario Oficial (28 October 1999) (“Reference Price for 1999/2000 Harvest”) (Exh. C-122).

- entitles a mill to an adjustment in the event that the *actual* price of a kilogram of base standard sugar observed for each mill is lower than the reference price calculated for pre-liquidation purposes; and
- requires that the reference price for mills that did not comply with their exports be adjusted to account for a 2.5 penalty factor.<sup>36</sup>

25. As declared by Mr. Cruz, Mexico never provided the data required under article 4 to run the reference price formula with actual figures.<sup>37</sup> Furthermore, Mexico did not provide the export quota compliance information that would have permitted assessment of the penalty for failure to export.<sup>38</sup> In this situation, the mills could not benefit by lowering their final payment to the *cañeros* to reflect the lower market prices actually prevailing, because the *cañeros* were denied information to corroborate whether mills were complying with the export requirement. As a result, the *cañeros* and the mills were unable to make the calculations and adjustments required by Articles 4 and 5. This situation penalized mills which, like GAM, had complied with their export obligations, but yet continued to have to sell their sugar at depressed prices while rewarding non-complying mills (which included the Government-owned mills). The nominal right of the mills to reduce the final payment to *cañeros* to the extent that the actual prices were less than the reference price was in practice an illusion. The Government did not provide data that would permit its enforcement. Though actual prices were well below the theoretical reference price and mills were suffering in consequence, there never were adjustments, nor could there be without the requisite government support in the face of the diametrically interests of mills and *cañeros*.

26. The following graph illustrates the effects of the Government induced breakdown of the system:

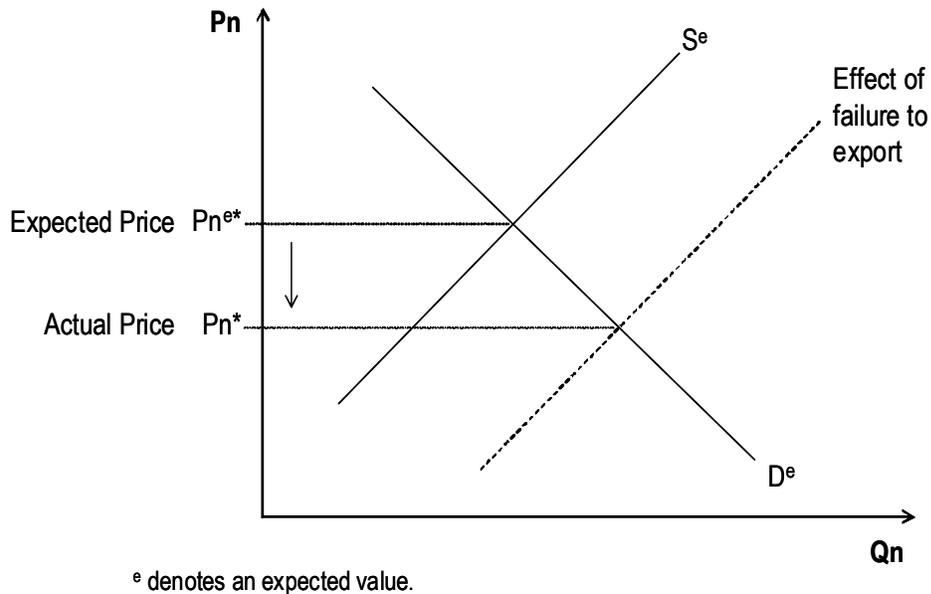
---

<sup>36</sup> See Exh. C-23.

<sup>37</sup> See Cruz Statement, p. 6 (Exh. C-113).

<sup>38</sup> See *id.*, at 6 (Exh. C-113); Second Witness Statement of Juan Cortina, p. 6 (Exh. C-115) (“Cortina Second Statement”).

27. **Graph 1: Effect of Failure to Require Export of Surplus Sugar**



28. As a result of the situation created by Mexico’s arbitrary application of the reference price formula and its failure to provide the data required to perform the adjustments required by Articles 4 and 5 of the 1997 *Acuerdo*, GAM paid for sugarcane based on the  $Pn^e$  reference, while only receiving  $Pn^*$  for the sugar that it sold. Thus, sugarcane would no longer be responsive to market forces and the *cañeros* would no longer share in the downside of the prices at which sugar actually was sold. The entire purpose of the reference price formula was thus defeated and the first crucial element of the Mexican sugar program was lost.

29. After the expropriation, however, Mexico intervened to secure compliance with the requirement to adjust the reference price. On April 14, 2003, Mexico announced that the *Secretaría de Economía* and SAGARPA would jointly make this adjustment.<sup>39</sup> This measure, will only benefit the Government as owner of 27 expropriated mills – not GAM or its minority shareholder, GAMI.

<sup>39</sup> See *Determinación del Precio de Referencia del Azúcar para el Pago de la Caña de Azúcar Durante la Zafra 2002/2003*, Diario Oficial (14 April 2003) (“Reference Price for 2002/2003 Harvest”) (Exh. C-152).

## 2. Export Of Surplus Sugar

30. Domestic sugar prices are driven by supply and demand. When supply exceeds demand, as it did in Mexico during the second half of the 1990s, prices will decrease. Mexico does not dispute that the 1997 *Acuerdo* addresses this basic problem by requiring that each mill export a percentage of its output proportional to its share in total production and that the consequence of not doing so was to pay a substantial penalty price equal to 2.5 times the difference between Mexican and world prices for sugarcane.<sup>40</sup> Mexico further concedes that there was noncompliance in the industry and it has not disputed the validity of export quota compliance data provided by GAMI in paragraph 53 of its Statement of Claim and in Exhibits C-31 and C-32.<sup>41</sup> Mexico has also admitted that the two Government-owned mills failed to export their quota.<sup>42</sup>

31. Rather, Mexico adopts the untenable position that: (i) it was not responsible for setting export quotas;<sup>43</sup> (ii) short of expropriating half of the industry, it did not have any enforcement authority;<sup>44</sup> (iii) it did not matter that most non-complying mills, including the Government's, ignored their export obligations;<sup>45</sup> (iv) Grupo CAZE was actively pursued and punished for submitting fraudulent documents showing compliance with its quota requirements;<sup>46</sup> and (v)

---

<sup>40</sup> See Statement of Defense, para. 103.

<sup>41</sup> See *id.*, paras. 126-127.

<sup>42</sup> See *id.*, para. 126.

<sup>43</sup> See *id.*, para. 106 (“The CNIAA was responsible for calculating the quota for each mill.”)

<sup>44</sup> See *id.*, para. 128, 105 (“Enforcement of the 1997 *Acuerdo* came under the responsibility of the two productive sector involved.”).

<sup>45</sup> See *id.*, paras. 126 and 127.

<sup>46</sup> See *id.* at paras. 130 and 131.

other factors, not the sugar glut, had an effect on the domestic price of sugar.<sup>47</sup> Mexico is wrong on all counts.

**a. Mexico Was Responsible Under The 1997 Acuerdo For Allocating Export Quotas**

32. Articles 4 and 5 of the 1997 *Acuerdo* unequivocally establish that SECOFI (now *Secretaría de Economía*) was legally responsible for allocating export quotas to individual mills.

Article 4 states:

Prior to the final payment of sugarcane, the Sugarcane Production Committees of the National Sugar Mills shall calculate the bulk price per kilogram of standard sugar observed by each sugar mill, and the calculation of the difference between the definitive sugar exports of each sugar mill *with respect to the export quota assigned by the Department of Commerce and Industrial Development*.<sup>48</sup>

33. In accordance with this requirement, section II of Article 4 of the 1997 *Acuerdo*, requires the SHCP to provide information on export prices and quantities captured in the *Sistema Automatizado Aduanero Integral*.<sup>49</sup> As discussed below, absent the publication of the data, the *cañeros* could not assess the 2.5 penalty factor against specific delinquent mills and adjustment of the reference price under Articles 4 and 5 became impossible.<sup>50</sup> Mexico's only rebuttal to this clear legal requirement is that it asserts that the *Cámara Nacional de las Industrias Azucareras y Alcoholeras* ("CNIAA") was responsible for creating the export quotas.<sup>51</sup> However, Mexico can only cite as support an agreement between the CNIAA and SECOFI that was completed *prior* to

---

<sup>47</sup> See, e.g., *id.* at para. 134.

<sup>48</sup> Exh. C-23 (emphasis added).

<sup>49</sup> Integral Customs Computer System.

<sup>50</sup> See Cruz Statement, p. 6 (Exh. C-113).

<sup>51</sup> See Statement of Defense, para. 106 ("The CNIAA was responsible for calculating the quota for each mill, which it made known to the SECOFI.").

the publication of the 1997 *Acuerdo*.<sup>52</sup> Mexico can not provide, however, any explanation as to why Mexico is not required to produce the export quotas given the language of the 1997 *Acuerdo*.

**b. Mexico's Failure To Enforce The Export Requirements**

34. As indicated above, Mexico had both the authority and the duty to act in a manner that would result in strict compliance with the Sugarcane Decree and its implementing provisions, including by issuing such rules as may be required to effectively implement the sugar program.<sup>53</sup> Furthermore, and as also explained above, the major disincentive of failing to export was the requirement of the 1997 *Acuerdo* that the mills would have to pay a penalty price to the *cañeros*.<sup>54</sup> Article 7 of the Sugarcane Decree designated the JCACA as the competent authority to resolve all economic disputes between the mills and the *cañeros*, including enforcing the penalty price against non-compliant mill.<sup>55</sup> Although Mexico argues that it does not control the JCACA, this is clearly wrong:

---

<sup>52</sup> *See id.*, note 102.

<sup>53</sup> Sugarcane Decree, art. 4(a)(c) (Exh. C-20). Moreover, the *cañeros* shared this same view. For instance, on June 14, 2001, GAM, its *cañeros* and Mr. Ignacio Lazcano Martinez, a SAGARPA representative, signed the minutes of a meeting which clearly spells out how the participants in the meeting understood the role of the Government:

The Grupo GAM representative indicated that [GAM] had complied with the volume of exports that it had been allocated for the 200/2001 harvest. Consequently, *the Industrial Sector and the Cañero Sector demand that the corresponding authorities oversee strict compliance with allocated export quotas and [that] they apply the corresponding sanctions in case of non compliance.*

SOD Exh. R-52, para. 6 (emphasis added). The SAGARPA representative who signed these minutes did not take exception to the characterization of the Government's role in overseeing strict compliance with the export quotas and applying the 2.5 penalty factor to delinquent mills.

<sup>54</sup> 1997 *Acuerdo*, art. 5(II) (Exh. C-23).

<sup>55</sup> Exh. C-20.

- The JCACA was created by the Sugarcane Decree to insure its proper implementation;
- SAGARPA controls the budget of the JCACA;<sup>56</sup>
- As Mexico concedes, the Government held two of the six seats in the JCACA, including the deciding vote;<sup>57</sup>
- The JCACA's decisions are binding by virtue of the law;<sup>58</sup> and
- The JCACA's decisions may be challenged in an *amparo* procedures because they constitute “authority acts.”<sup>59</sup>

35. However, as GAMI explained in the Statement of Claim,<sup>60</sup> the JCACA failed to adjudicate the lawsuits brought before it brought by the *cañeros* to enforce the penalty price against non-complying firms, thus rendering the entire export regime worthless.<sup>61</sup> According to Mr. Cruz, the *cañero* suits were effectively blocked by the Government when it refused to

---

<sup>56</sup> See, e.g., *Juez Séptimo de Distrito en Materia Civil en el Distrito Federal* (“Seventh Civil District Judge”), Proceeding No. EXP 133/99, pp. 7-8 (2 December 1999) (Exh. C-124), where in a submission to a federal judge, the President of the JCACA characterized the institution’s role as follows: “...the economic resources that make up the budget assigned to [JCACA] by the *Comité de la Agroindustria Azucarera*...come entirely from the budget of [SAGARPA] and this gives [the JCACA] absolute and total independence to act as arbitrator in the final resolution of disputes between suppliers of sugarcane and the industrial unites.”

<sup>57</sup> Statement of Defense, para. 74. The President of the JCACA in fact has recently referred to this authority to cast the deciding vote in a submission to a federal judge. *Juez Séptimo de Distrito en Materia Civil en el Distrito Federal* (“Seventh Civil District Judge”), Proceeding No. EXP 133/99, pp. 7-8 (2 December 1999) (Exh. C-124).

<sup>58</sup> Sugarcane Decree, art. 5 and 7 (Exh. C-20); Amendment to Sugarcane Decree, clause 29 (Exh. C-21).

<sup>59</sup> Schmill Opinion, para. 44.

<sup>60</sup> Statement of Claim, para. 56.

<sup>61</sup> The two *cañero* lawsuits were filed against the entire industry on 4 December 2000. See Exh. C-28, 29.

produce the official export data on which the JCACA could determine which mills would pay the penalty price.<sup>62</sup>

36. Mexico responds to this allegation by stating that GAM itself was a defendant in similar proceedings before the JCACA and that in those proceedings GAM contested the jurisdiction of the JCACA, thereby “oppos[ing] the proper functioning of the JCACA and the mechanism established to assure compliance with export requirements.”<sup>63</sup> Mexico's response merely distracts from the issue at hand. Although it is true that GAM was named as a defendant in the proceedings, this was only because the *cañeros* were forced to name every mill as a defendant in suits before the JCACA as the Government had failed to produce the data showing which mills were in compliance and which were not.<sup>64</sup> Notably, Mexico does not dispute that GAM had fully complied with its export obligations and that accordingly, GAM had every right to challenge the jurisdiction of the JCACA over it.<sup>65</sup>

**c. Wholly Mexican-Owned Mills Were Obligated To Comply But Did Not**

37. Mexico does not deny that prior to the expropriation it owned two sugar mills: Santa Rosalía and La Joya.<sup>66</sup> In addition, Mexico concedes that these two mills fell considerably short of their export obligations as set out in paragraph 53 of GAMI's Statement of Claim.<sup>67</sup> Mexico discounts the failure of its own mills to comply on grounds that they accounted for a small portion of domestic production.<sup>68</sup> That misses the point. Failure of the Government-owned mills

---

<sup>62</sup> Cruz Statement, pp. 6-7 (Exh. C-113).

<sup>63</sup> See Statement of Defense, para 123.

<sup>64</sup> See Cruz Statement, pp. 5-7 (Exh. C-113).

<sup>65</sup> See *id.*

<sup>66</sup> See Statement of Defense, para. 126.

<sup>67</sup> See *id.*

<sup>68</sup> See *id.*

to set a positive example led an increasing number of private mills to believe that they too would be permitted to sell surplus sugar in the higher priced domestic market without having to pay the penalty price.

38. Mexico undermined the rule of law by setting an example that resulted in non-compliance by other mills. During the 1997-1998 harvest, 10 mills (including the two Government-owned mills) failed to export their respective quotas.<sup>69</sup> By the next harvest (1998-1999) the number had increased to 19<sup>70</sup> and by the 2000-2001 season it had reached 30,<sup>71</sup> always including La Joya and Santa Rosalía.<sup>72</sup> In fact, GAM's mills were the only mills that complied in full with their export requirements every year from 1996 to 2001.

#### **d. Grupo CAZE**

39. The failure to take timely action against Grupo CAZE also sent a negative signal to the Mexican sugar industry. As GAMI established in the Statement of Claim, Mexico further exaggerated the problem by not sanctioning CAZE officials for fraudulently submitting export figures.<sup>73</sup> Mexico, however, fails to rebut this allegation. Specifically, Mexico does not deny

---

<sup>69</sup> La Joya, Santa Rosalía, Calipam, El Carmen, Dos Patrias, Azuremex (Tenosique), Adolfo López Mateos, Tres Valles, Independencia and Los Mochis. *See* Export Quota Compliance Chart 1996/1997 – 1997/2000 (Exh. C-31).

<sup>70</sup> La Joya, Santa Rosalía, Calipam, El Carmen, Dos Patrias, Azuremex (Tenosique), Independencia, Los Mochis, Atencingo, Casano La Abeja, El Modelo, El Potrero, Emiliano Zapata, La Providencia, Plan de San Luis, San Cristobal, San Miguelito, El Molino and La Concepción. *See id.*

<sup>71</sup> La Joya, Santa Rosalía, Calipam, El Carmen, Dos Patrias, Azuremex (Tenosique), Independencia, Los Mochis, Atencingo, Casano La Abeja, El Modelo, El Potrero, Emiliano Zapata, La Providencia, Plan de San Luis, San Cristobal, San Miguelito, El Molino, La Concepción, Eldorado, Central Progreso, José María Morelos, Pablo Machado, Zapoapita, Alianza Popular, Cuatotlapam, Pedernales, Plan de Ayala, San Gabriel and Santo Domingo. *See* Export Quota Compliance Chart 2000/2001 (Exh. C-32).

<sup>72</sup> *See* Santos Statement, para. 11 (Exh. C-114).

<sup>73</sup> *See* Statement of Claim, para. 55.

that it was aware of CAZE's fraud at least as early as October of 1999 when the CNIAA notified SECOFI that CAZE had tried to establish compliance with its export requirements by submitting false documents.<sup>74</sup>

40. It is a fact that the CNIAA drew the attention of the Minister of Trade to this situation by letter of 27 October 1999.<sup>75</sup> Moreover, Mr. Alberto Santos, the Chairman of *Ingenios Santos, S.A. de C.V.*, another expropriated Mexican sugar company, and the President of the CNIAA from 1998-2000, testifies that the CAZE situation was further discussed at a meeting held in November of 1999 with the participation of the Ministers of SECOFI, SAGARPA, Finance and Labor.<sup>76</sup> At the meeting, the Government officials indicated that no action could be taken against CAZE before the end of the fiscal year.<sup>77</sup> On 14 December 1999, the CNIAA yet again addressed a letter to the Minister of Trade confirming its request for Government action.<sup>78</sup> By the end of 1999, the Government had still taken no action, despite the fact that it was by that time clear that CAZE had simulated exports by producing false documents.<sup>79</sup>

41. Commercial reality requires swift action against participants in a managed supply system who refuse to comply with their export obligations. Although Mexico purports to have taken action,<sup>80</sup> that action was not timely and therefore not effective. Mr. Santos, the former President

---

<sup>74</sup> See Statement of Defense, paras. 130-131.

<sup>75</sup> Letter from the CNIAA to the Ministers of Commerce (27 October 1999) (Exh. C-126) (requesting that SECOFI “. . . take the action necessary to clearly establish the responsibility of [CAZE] and the corresponding authorities in connection with this regrettable matter.”). A copy of this letter was delivered to the Ministers of Finance, SAGARPA, Labor and Civil Service.

<sup>76</sup> Santos Statement, para. 10 (Exh. C-114).

<sup>77</sup> See *id.*

<sup>78</sup> Letter from CNIAA to Minister of Commerce (14 December 1999) (Exh. C-127).

<sup>79</sup> Santos Statement, para. 10 (Exh. C-114).

<sup>80</sup> Statement of Defense, para. 130.

of the CNIAA, testifies that he is unaware of any action by the Mexican Government prior to the expropriation,<sup>81</sup> almost two years after the CNIAA's first complaint of October 1999.<sup>82</sup>

**e. Action by Mexico**

42. Mexico contends that SECOFI took legal action to promote compliance with export quotas,<sup>83</sup> a statement which itself contradicts Respondent's earlier position that the 1997 *Acuerdo* does not create an obligation for mills to export surplus sugar.<sup>84</sup> Mexico indicates its action included: (i) restricting exports to guarantee domestic supply, but allowing some duty free exports; (ii) eliminating official prices in 1995; (iii) subsidizing inventories in 1998 and 1999; and (iv) considering compliance with export quotas in allocating access to the U.S. market.<sup>85</sup>

43. Regardless, Mexico cannot deny that whatever measures were taken were a failure. Prices remained low, the price penalty for sugarcane was unenforced, and non-compliance with export requirements was rampant.

**3. Base Production Levels**

44. The 1998 *Acuerdo* amended the 1997 *Acuerdo* to provide for each mill to be assigned base production levels which would limit the number of hectares a mill could produce from, thus reducing production. As amended, Article 3 of the 1997 *Acuerdo* provides that:

---

<sup>81</sup> This statement is not contradicted by Mexico's Exhibit R-37.

<sup>82</sup> The fact, however, that the *Procuraduría General de la República* may have acted against CAZE after the expropriation is of course irrelevant to this dispute for, by that time, the adverse effect on the market had gone unchecked, and further, GAM's mills, and GAMI's investment, had already been taken by Mexico.

<sup>83</sup> Statement of Defense, para. 107.

<sup>84</sup> *See id.*, para. 103.

<sup>85</sup> *See id.*, para. 107.

SECOFI and SAGAR, hearing the opinion of the [CAA] shall determine a per mill base production level as of the 1997/1998 harvest. . . .<sup>86</sup>

45. The Government was thus obligated to establish base production levels for each mill, an important measure because, left to its own device, each mill had a natural tendency to produce as much as possible, which would mean surpluses and unremunerative prices. The private sector had a right to be consulted under Article 3, but had no veto. The Government has an obligation to act, even without industry agreement.

46. In the expert opinion of former Chief Justice Schmill, the definition of base production levels under this provision is binding.<sup>87</sup> The testimony of Mr. Adalberto Gonzalez that SECOFI required the agreement of CAA to issue base production levels is thus wrong on the face of the law.<sup>88</sup> Nothing in this amended *Acuerdo* requires that the CAA provide a unanimous opinion to SECOFI and SAGARPA, and there is no limitation to their authority to proceed with definition of base production levels where no agreement emerges at the CAA level. As testified by former Chief Justice Schmill, the provisions of the 1997 and 1998 *Acuerdos* “. . . are not mere invitations or the certification of private arrangements . . . between private industrial or *campesino* individuals . . . they have been issued by State entities in the exercise of their authority . . . .”<sup>89</sup>

47. Mexico does not deny that Article 6 of the 1998 *Acuerdo* requires SECOFI and SAGARPA to establish the base production levels by 1 October of every year.<sup>90</sup> Likewise,

---

<sup>86</sup> Exh. C-23.

<sup>87</sup> Schmill Opinion, para. 85 (Exh. C-110).

<sup>88</sup> Testimonio de Adalberto Gonzalez Hernández, para 22 (SOD Exh. R-28).

<sup>89</sup> Schmill Opinion, para. 103 (Exh. C-110).

<sup>90</sup> See Statement of Defense, paras. 109-110.

Mexico does not dispute that it never published base production levels.<sup>91</sup> Instead, the Government argues that it did not have to comply with its obligation under the 1998 *Acuerdo* because the *cañeros* and the mills could not reach agreement as to how the production levels should be fixed.<sup>92</sup> As testified by Mr. Santos, instead of stepping in to resolve this disagreement by fixing the base production levels as required by law, the Government did nothing for over two years.<sup>93</sup> The testimony of Mr. Cruz also confirms this account, and Mexico does not disagree that base production levels were not established for the 1998/1999 and 1999/2000 harvests.<sup>94</sup>

48. Mexico further asserts that base production levels were "implemented" through the 2000 *Acuerdo*. Specifically, Mexico alleges that:

The CAA [calculated] the base production level for each mill. As required by the 2000 *Acuerdo*, both SECOFI and the CAA made the base production levels available to all interested parties ... In fact, Mr. Alejandro Hidalgo Prieto, the GAM foreign trade representative, showed for GAM at the SECOFI offices. . . .<sup>95</sup>

49. This account is both inaccurate and legally irrelevant: (i) the 1998 *Acuerdo* calls for determination of the base production levels by SECOFI and SAGARPA by October 1 of 1998, not March of 2000; (ii) the 1998 *Acuerdo* does not require CAA to "calculate" the base production levels; (iii) pursuant to the 2000 *Acuerdo*, base production levels for all mills were to be made available at the offices of the CAA, not SECOFI;<sup>96</sup> and (iv) the base production levels

---

<sup>91</sup> *See id.*

<sup>92</sup> *See id.*, para. 110.

<sup>93</sup> Santos Statement, para. 13 (Exh. C-114).

<sup>94</sup> *See id.*; *see also* Cruz Statement, pp. 9-10 (Exh. C-113).

<sup>95</sup> Statement of Defense, para. 112.

<sup>96</sup> 2000 *Acuerdo*, art. 2 (Exh. C-33).

table attached to Mr. Adalberto Gonzalez' testimony (SOD Exh. R-28) was never made available to GAM.<sup>97</sup>

50. In any event, this is yet another example of lack of transparency and failure of the Government to fulfill its duties under the law. Mexico has failed to explain why base production levels were not published, or how its practice to secretly "make available" partial information to individual mills advances the rule of law. Also, Mexico implemented the base production levels late and in a way that guaranteed they would not be enforced.<sup>98</sup> Enforcement of production limitations was further jeopardized because Mexico never promulgated the regulations required by Article 2 of the 2000 *Acuerdo*.<sup>99</sup>

51. Moreover, Mexico attempts in its Statement of Defense to claim credit for a reduction in harvested surface of two GAM mills: Tala, from 24,297 hectares in the 1997/1998 harvest to 22,894 hectares for the 1998/1999 harvest; Lázaro Cárdenas, from 4,119 hectares in the 1998/1999 harvest to 3,848 hectares in the 1999/2000 harvest.<sup>100</sup> However, Mexico cannot claim that 1997-99 harvested surface were reduced as a result of base production levels since those levels were not "made available" to mills and *cañeros* in any way until March of 2000.<sup>101</sup> In

---

<sup>97</sup> See Cortina Second Statement, para. 6-7 (Exh. C-115). Mexico argues that SECOFI "directly attended" to GAM's representative on March 16, 2000 and that "GAM's representative appeared, and was informed of GAM's production levels." Statement of Defense, para. 112. While Alejandro Hidalgo Prieto of GAM did attend a meeting at SECOFI in early 2000, during that meeting Mr. Hidalgo was shown but never given any copy of proposed production levels for only GAM's mills. See Cortina Second Statement, paras. 6-7 (Exh. C-115). No final and official base production levels for all mills in the sugar industry were ever provided. See *id.*

<sup>98</sup> See generally Cruz Statement, pp. 9-10 (Exh. C-113).

<sup>99</sup> See *id.*

<sup>100</sup> Statement of Defense, note 119.

<sup>101</sup> The reality is that the surface area under cultivation for a number of mills actually increased, not the decreased, after Mexico's purported implementation of base production levels. For instance, San Nicolas, El Carmen and La Gloria mills actually exceeded their base production level by 816, 978 and 340 hectares respectively. Compare Table Re: Base Production Levels for 1997/1998-1998/1999 Harvests (Exh. C-128) (originally part of SOD Exh. R-18), with CAA Chart Re: Base Production Levels for 1998-2002 (Exh. C-129).

addition, by March of 2000 the fields were already planted and in the process of being harvested. As the record shows, GAM lost its mills in September of 2001 and for this reason any reduction of production levels after this date benefited Mexico only.

**C. Factors Beyond Mexico's Control Do Not Explain Mexico's Failure To Protect The Domestic Price Of Sugar As Required By The Sugar Program**

52. Mexico asserts, essentially, that GAM's financial difficulties are attributable to forces beyond Mexico's control – either exogenous factors or GAM's own putative failings.<sup>102</sup> None of the factors cited by Mexico, however, stand up to scrutiny. First, Mexico asserts that the financial crisis of 1995 “worsened” the “financial conditions” of the mills.<sup>103</sup> The crisis, however, preceded the expropriation by a full six years and by that time, according to Mexico's own figures, inflation had returned to under five percent per year and the crisis had completely subsided. Further, to the extent that the crisis did affect the mills, Mexico certainly could have more adequately addressed these issues through the proper management of the sugar regime.

53. Second, Mexico implies that GAMI's investment suffered because GAM's mills were inefficient.<sup>104</sup> As a factual matter, Mexico's contention is completely untrue – according to the figures published by both the Government and the CNIAA, the GAM mills were efficient.<sup>105</sup> In fact, even Mexico's own expert, Mr. Luis Ramiro García, acknowledges that GAM's mills

---

<sup>102</sup> See, e.g., Statement of Defense, para. 27; *id.* at para. 228 (stating that, “the numerous factors that influenced the Mexican sugar market, including the reasons for privatizing the industry, the financial crisis Mexico experienced, the characteristics of world sugar markets, the conditions of bilateral trade between Mexico and the United States during the relevant period and the dispute between the two countries over sweeteners, as well as competition from fructose”).

<sup>103</sup> *Id.* para. 32.

<sup>104</sup> *Id.* at para. 142.

<sup>105</sup> See Antonius Antonius González, Rebuttal – Expert Report, pp. 5-6 (January 2004) (Exh. C-112) (“Antonius Second Report”) (noting both that the L.R. Garcia Report classifies only one of the GAM's five mills as inefficient and that the CNIAA's figures show that four of five GAM mills saw an improvement in sucrose yield while all five saw a decrease in the amount of fuel oil consumed per ton of milled cane).

operated at efficiency levels close to the average of all mills.<sup>106</sup> Interestingly, in Mr. García's analysis, GAM mills fared as well, if not better, than the mills of Beta San Miguel (BSM), a company that was not expropriated.<sup>107</sup>

54. Third, Mexico repeatedly asserts that the inability to export sugar to the United States and the importation of HFCS from the United States caused further damage to the industry generally.<sup>108</sup> The influx of high fructose corn syrup to the Mexican sweetener market is just one more factor to be taken into consideration in the Government's balancing of the supply and demand for sugar. The undisputed fact is that Mexico undertook to regulate the supply of sweeteners in the domestic market. It had ample power to include fructose in the national sugar balance and to regulate it in order to maintain supply and demand for sweeteners in equilibrium. Indeed, it affirmatively took this step after the expropriation when it imposed a tax on the use of fructose as a sweetener in beverages.<sup>109</sup> There is a risk that Mexico will respond by saying that the U.S. fructose industry has initiated a NAFTA Chapter 11 case against Mexico for having taken the very action that we, also as Chapter 11 Claimants, believe to be appropriate.

55. Fourth, Mexico offers no evidence that GAM lowered its prices due to its liquidity problems. But even if GAM had lowered its prices, both GAM's liquidity problems and the need to lower prices were caused fundamentally by the Government's own failures to implement and enforce the sugar program.

56. Finally, Mexico implies that the fall in sugar prices in the American and world markets contributed to the condition of GAM and GAMI's investment in GAM.<sup>110</sup> As Mr. Antonius

---

<sup>106</sup> L. R. García Report, table 9 (SOD Exh. R-12).

<sup>107</sup> *Id.* at 5.

<sup>108</sup> *See, e.g.*, Statement of Defense, paras. 174, 177.

<sup>109</sup> *See Ley del Impuesto Especial sobre Producción y Servicios*, Diario Oficial (1 January 2002) (Exh. C-130).

<sup>110</sup> *See* Statement of Defense, para. 142.

notes, however, that although world price for sugar dropped 22.7% between January 1997 and September 2001, prices in the United States dropped only 4.6% during the same period, thereby confirming that functioning domestic sugar markets operate independent of the other domestic markets or the world market.<sup>111</sup> Thus, according to Mr. Antonius:

[I]f the *Acuerdos* had been applied, the domestic price in Mexico would have been greater than it was (as sugar would have been exported), and the price of cane would have been lower (through the application of the weighted average formula). The key factor behind the deterioration in the viability of the Mexican sugar sector during the period of the GAMI investment continues to be the lack of application of the *Acuerdos*.<sup>112</sup>

57. In summary, none of the factors that Mexico blames for the failings of the sugar program and GAM's financial difficulties withstand scrutiny. To the extent any of these factors had validity and had an effect, the proper implementation of the sugar program would have offset the factor and prevented the adverse effect on Mexican prices and on GAM and other sugar mills. The point of Mexico's sugar laws was precisely to protect against the vicissitudes of external

---

<sup>111</sup> See Antonius Second Report, pp. 3-5 (Exh. C-112). GAMI further notes that Mexico has not provided a single document that denies the simple proposition that Mexican sugar prices are a function of internal supply and demand. In fact, Mexico's own experts and documents confirm this fundamental economic principle. See, e.g., L.R. García Report, pp. 4, 7, 12, 15, 48 (SOD Exh. R-12); SOD Exh. R-71, p. 9. In particular, Mr. García testified that ". . . [sugar] price fluctuations are associated with the lack of equilibrium between production and consumption more than with the amount offered in the world market." L. R. García Report, p. 15 (SOD Exh. R-12). GAM's SEC filings are also clear on this point: ". . . 70% of world sugar sales are at each individual country's domestic price. Mexican sugar prices are primarily driven by the demand for and domestic supply of sugar as well as export requirements which result in the support of domestic prices." SOD Exh. R-49, p. 1. Finally, the 26 June 2001 *Acuerdo* is unambiguous: "[p]roduction of sugar has generated excess supply which has resulted in the decrease of the domestic price of such product . . ." SOD Exh. R-59.

<sup>112</sup> Antonius Second Expert Opinion, p. 5 (Exh. C-112). Of course, the same point is true for Mexico's contention that indebted companies tend to lower their prices. See, e.g., Statement of Defense, para. 134. That is, Mexico is trying to shift blame to the failing firms themselves even though it was Mexico that had both the authority and the responsibility to rectify the problems in the industry.

factors. GAMI does not fault Mexico for global surplus production or competition from high fructose corn syrup or other such factors. However, Mexico had the tools at its disposal and the responsibility to use those tools so that both millers and *cañeros* could survive. Mexico's failure to do so is attributable to no one but itself.

**D. The Expropriation Of GAM's Mills Was Unjustified And Discriminatory**

58. In GAMI's Statement of Claim, GAMI demonstrated that the facts and the record did not support Mexico's stated reasons for expropriating GAM's mills, or explain why mills of GAM were expropriated while other mills in similar circumstances were not. Mexico's Statement of Defense simply ignores evidence adduced by GAMI, while adducing evidence itself that is either incomplete, irrelevant or simply wrong.

**1. Mexico Incorrectly States GAM's Debt to the Cañeros**

**a. 1999/2000 Harvest**

59. Mexico states in its Statement of Defense that "[d]uring the 99/00 harvest, GAM paid its suppliers for only part of their sugarcane."<sup>113</sup> On the contrary, as discussed below, GAM fully paid its debt to the *cañeros* for the 1999/2000 harvest.<sup>114</sup>

60. Mexico also states that GAM reached agreements with the *cañero* unions to schedule the payments of its outstanding debt, and that in one of these agreements, on 18 August 2000, GAM requested a credit from the *Fondo de Capitalización y Modernización del Campo Cañero* (FOCAM) to pay its *cañeros*.<sup>115</sup> It is true that GAM did enter into those agreements with the *cañeros*, and pursuant to one of them, signed with the UNPC-CNC on 18 August 2000, GAM requested and obtained a credit from FOCAM for the payment of its debt to the *cañeros*.

---

<sup>113</sup> Statement of Defense, para. 148.

<sup>114</sup> Cortina First Statement, para. 27 (Exh. C-18).

<sup>115</sup> See Statement of Defense, para. 148; SOD Exh. R-54.

61. What is not true, however, is Mexico's statement that the mills were unable "to obtain credit due to their suspension of payments."<sup>116</sup> As stated by Mr. Darío Oscós in his Expert Opinion, a company in *suspensión de pagos* may receive credit upon judicial authorization.<sup>117</sup> Each of the five GAM mills received the requisite authorization. Between 25 August and 11 September 2000, Judge Cervantes issued interlocutory judgments authorizing each mill to pay pre-petition debt to its *cañeros*<sup>118</sup> and to receive credit from FOCAM for payment of post-petition obligations to cane growers.<sup>119</sup>

62. Accordingly, on 6 September 2000, FOCAM and each of GAM's mills signed a credit agreement, by which GAM's mills received from FOCAM sufficient credit to pay the amount of \$84.25 million pesos as stated in the 18 August 2000 agreement with the UNPC-CNC.<sup>120</sup> GAM guaranteed its credit to FOCAM with promissory notes (*pagarés*)<sup>121</sup> and immediately deposited the money in a specially created bank account administered by one representative of GAM and

---

<sup>116</sup> See Statement of Defense, para. 148.

<sup>117</sup> Oscós Opinion, para. 31 (Exh. C-111); see also Authorizations from Judge Cervantes for post-petition credit for each of GAM's mills (25 August 2000) (Exh. C-131).

<sup>118</sup> See Authorizations from Judge Cervantes for pre-petition payment for each of GAM's mills (Exh. C-132).

<sup>119</sup> See Authorizations from Judge Cervantes for post-petition credit for each of GAM's mills (25 August 2000) (Exh. C-131).

<sup>120</sup> See SOD Exh. R-54.

<sup>121</sup> See Exh. C-133 (4 promissory notes from the Tala mill in the amounts of 10,059,347.00, 5,867,952.50, 5,867,952.50, 6,454,748.00 for a total of 28,250,000.00 pesos); Exh. C-134 (4 promissory notes from the Lázaro Cárdenas mill in the amounts of 2,136,498.50, 1,246,291.00, 1,246,291.00, 1,370,920.00 for a total of 6,000,000.50 pesos); Exh. C-135 (4 promissory notes from the San Francisco mill in the amounts of 2,670,623.00, 1,557,863.50, 1,557,863.50, 1,713,650.00 for a total of 7,500,000 pesos); Exhibit C-136 (4 promissory notes from the San Pedro mill in the amounts of 5,163,205.00, 3,011,869.50, 3,011,869.50, 3,313,056.50 for a total of 14,500,000.50 pesos); Exh. C-137 (4 promissory notes from the Benito Juárez mill in the amounts of 9,970,326.00, 5,816,023.50, 5,816,023.50, and 6,397,626.00 for a total of 27,999,999.00 pesos). The total amount of all 20 promissory notes is 84,250,000.00 pesos, thereby indicating that GAM paid the debt in full.

one representative of the *cañeros* on behalf of FOCAM, ensuring that the funds would be directly allocated to the payment of the *cañeros*' debt.

63. Thus, with regard to the debt to the *cañeros* for the 1999/2000 harvest, GAM fully paid its credit with FOCAM. GAM did request an amendment to its payment schedule and FOCAM agreed to the extension. In accordance with the amended payment schedule, GAM complied with its obligations to FOCAM, paying in full its debt before the date of expropriation.<sup>122</sup> Thus, the promissory notes issued by GAM's mills were immediately cancelled to denote payment had been made.<sup>123</sup>

#### **b. 2000/2001 Harvest**

64. As to the 2000/2001 harvest, due to the lack of adequate Government protection of domestic sugar prices, GAM had to delay payments to its *cañeros*.<sup>124</sup> Consequently, as was previously done for the 1999/2000 harvest, GAM's mills, like other mills, including Beta San Miguel (BSM),<sup>125</sup> entered into agreements with *cañeros* for the payment of their debts in 2000/2001. Mexico attached to its Statement of Defense, and also included in the Administrative Record for purposes of its decision to expropriate GAM's mills, an agreement between GAM and its *cañeros* dated 14 June 2001.<sup>126</sup> However, Mexico ignores that the 14 June Agreement

---

<sup>122</sup> See *Comunicación de GAM a FOCAM* (31 May 2001) (SOD Exh. R-56).

<sup>123</sup> Each promissory note is stamped "PAGADO" or paid. See Exh. C-133-137.

<sup>124</sup> See Statement of Claim, para. 103.

<sup>125</sup> See Statement of Claim, para. 120; see also Cruz Statement, p. 10 (Exh. C-113) (noting that the vast majority of mills had arranged for extended payment schedules as well as stating that that the BSM mills in particular signed agreements with their *cañeros* on 27 July 2001 and that these agreements provided for payment to *cañeros* during the months of August to October of that year).

<sup>126</sup> See SOD Exh. R-60.

was superseded by an Agreement of 14 August 2001, as GAMI discussed in its Statement of Claim and Mr. Cortina's Witness Statements.<sup>127</sup>

65. The 14 August 2001, agreement, called the *Convenio de Pago*, demonstrates not only that GAM continued to make arrangements for payment to the *cañeros*, but also that the amount of debt which Mexico states in the Administrative Record is incorrect.<sup>128</sup> At page four of the *Convenio de Pago*, the top chart shows the total amounts GAM owed to the *cañeros* two weeks prior to the expropriation. That amount, 368.4 million pesos, is 94.6 million pesos, or 20 percent less than the amount Mexico reported as the basis for expropriating GAM's mills (*i.e.*, 463 million pesos). In addition, the *Convenio de Pago* shows that GAM had agreed to provide *cañeros* with certificates of deposit of sugar inventories to guarantee payment.<sup>129</sup> This mechanism had already been successfully used a year earlier.

66. GAM made the agreed-upon payments to the *cañeros* in the following two weeks of August, thereby further reducing its outstanding debt.<sup>130</sup> The only obligations that GAM had for payments prior to the date of expropriation were to the *cañeros* associated with Lázaro Cárdenas and Tala mills, and GAM met those obligations on time. On 27 August 2001, an agreement was made for payment of the pre-liquidation amount to the *cañeros* of the Lázaro Cárdenas mill.<sup>131</sup>

---

<sup>127</sup> See Statement of Claim, para. 103; Cortina First Statement, para. 28 (Exh. C-18); Cortina Second Statement, paras. 10-13 (Exh. C-115).

<sup>128</sup> See *Convenio de Pago* (14 August 2001) (attached to Cortina Second Statement at Exh. C-115).

<sup>129</sup> See Certificates of deposit for each of GAM's mills showing that sugar was deposited with *Almacenador Gómez, S.A. de C.V.* to guarantee payment to the *cañeros* (Exh. C-138).

<sup>130</sup> The latest of these agreements (between 28 and 31 August 2001), were consummated in SAGARPA's offices. Mexico thus cannot plead ignorance of the existence of such agreements, and its submission of only the superceded 14 June 2001 Agreement in these proceedings demonstrates less than good faith and candor to the Tribunal.

<sup>131</sup> Cane payments are made in two steps. The pre-liquidation payment of 80-85% is made shortly after delivery of each shipment during the harvest season. The liquidation payment of the remaining 15-20% is made at the end of the harvest. See Cortina Second Statement, para. 12 (Exh. C-115).

GAM agreed to pay the amount between 27 and 31 August 2001, and in fact, did so in the amount of \$2,069,862 pesos.<sup>132</sup> For the Tala mill, on 29 August 2001 an agreement was made for payment to the *cañeros* of the pre-liquidation amount as well. GAM agreed to pay 30 million pesos between 27 August and 31 August 2001, and GAM did so. Exhibit C1-39 shows that GAM transferred an amount of more than 38 million pesos to BBVA Bancomer bank for payment to the *cañeros*.<sup>133</sup>

67. As a result, by 31 August 2001, GAM's debt to the *cañeros* was less than 330 million pesos, in sharp contrast to the 463 million pesos Mexico asserted in the Administrative Record.<sup>134</sup> Furthermore, all remaining payments to *cañeros* for the 2000/2001 harvest were guaranteed with GAM's own sugar inventories with the certificates of deposit.<sup>135</sup>

68. The payment schedule set out in the August 2001 agreements provided that payments of the final twenty percent (*liquidacion*) owed to the *cañeros* would begin on 3 September 2001 and would be completed during the Fall of 2001.<sup>136</sup> Thus, GAM had a plan of payment which would and could have worked were it not for the expropriation of the mills on 2 September 2001. Mills such as those of BSM and others who also had arranged delayed payment schedules with the *cañeros* were not expropriated.

---

<sup>132</sup> GAMI does not have access to the actual document as if the property of the mill, which, of course, is currently an asset of Mexico. *See id.*, para. 11 (Exh. C-115).

<sup>133</sup> Internal invoices of GAM demonstrate that GAM made transfers to the bank for payment of the *cañeros* in the total amount of 38,644,040.68 pesos. The dates of the internal invoices do not reflect the actual date of payment, which had occurred earlier Cortina Second Statement, para. 12 (Exh. C-115).

<sup>134</sup> *See* Administrative Record – Technical File, p. 3 (Exh. C-50).

<sup>135</sup> *See* Statement of Claim, para. 103, n. 134. The certificates of deposit (CEDES) had a commercial value of more than 360 million pesos.

<sup>136</sup> *See id.*, para. 119; *see also* Exh. C-52 to C-55.

## 2. Suspensión de Pagos

69. Mexico, in its Statement of Defense at paragraph 272, implies that GAM was expropriated in part because it was in *suspensión de pagos*:

The expropriation was executed on those mills whose precarious financial situation compromised production . . . endangered the work and livelihood of a large number of cane growers, as well as the economic stability of several regions of the country. While suspension of payments allowed GAM to attempt to restructure its debt and possibly avoid bankruptcy, its financial situation was not consequently less precarious. GAM and the five mills it owned were the only companies in the sugar sector in suspension of payments. No other such company was in the same situation.

70. Mexico's heavy reliance upon GAM's status as an entity under *suspensión de pagos* as a justification for expropriating mills of GAM is completely contrary to the facts and to the purpose of the Mexican law of *suspensión de pagos*. According to the expert opinion of Mr. Darío Oscós, entry into *suspensión de pagos* does not compromise an entity's financial status.<sup>137</sup> If anything, *suspensión de pagos* allows an entity time to reorganize its finances to better pay that which is owed.<sup>138</sup> Furthermore, while *suspensión de pagos* may allow an entity to temporarily stop payments to certain creditors, it does not stay the post-petition obligations of an entity.<sup>139</sup> Thus, the *cañeros* were in a better position to receive any payments owed them *after* GAM was declared in *suspensión de pagos* on 9 May 2000.<sup>140</sup> As Mr. Oscós notes:

[T]he suspension of payments was a diligent decision to avoid deterioration of GAM's mills temporary financial distress during the Mexican sugar industry crisis. In fact, the suspension of payments adjudication ensured that GAM's mills continued to operate a viable business, that payments were made to cane

---

<sup>137</sup> See Oscós Opinion, paras. 9-10 (Exh. C-111).

<sup>138</sup> See *id.* at para. 9.

<sup>139</sup> See *id.* at para. 23.

<sup>140</sup> GAMI sought and obtained judicial authorization to pay pre-petition debt. See *supra*, note 119.

growers, preserved the jobs of mill workers, and preserved value and optimal assets for the benefit of all interested parties, including creditors.<sup>141</sup>

71. Mexico's assertion that GAM, "due to its *suspensión de pagos* condition, is not eligible for credit," also is incorrect.<sup>142</sup> A company in *suspensión de pagos* may receive credit once it gains authorization from a judge.<sup>143</sup> As noted above, each of the five GAM mills received the requisite authorization.<sup>144</sup>

72. Mexican law provides for a system of *suspensión de pagos* precisely so that entities such as GAM have an opportunity to restructure and reorganize in order to continue as viable, going concerns. Nowhere in the law does it state that entities that enter into *suspensión de pagos* are potentially subject to expropriation.

### **3. The Administrative Record Fails To Support The Government's Rationale For Expropriation**

73. Article 3 of the Expropriation Law of Mexico requires that Government decisions to expropriate be based on evidence compiled in an Administrative Record.<sup>145</sup> The Administrative Records here, however, contain very little information regarding GAM's mills, and that which it does contain is either incorrect, out-of-date or lacking evidentiary support.

74. To demonstrate this point, Claimant provides the Administrative Record for the expropriation each mill to the Tribunal.<sup>146</sup> While voluminous, a review of the Administrative

---

<sup>141</sup> Oscós Opinion, para. 39 (Exh. C-111).

<sup>142</sup> Statement of Defense, paras. 153-154; *see also* Administrative Record – Technical File, p. 3 (Exh. C-50) (“... *no pudo tomar crédito por la vía fideicomiso que se está instrumentando (por su condición de suspensión de pagos, no es sujeto de crédito) pra liquidar sus adeudos con los cañicultores: . . .*”).

<sup>143</sup> Oscós Opinion, para. 31 (Exh. C-111).

<sup>144</sup> *See supra* notes 119-120.

<sup>145</sup> *See* Statement of Claim at para. 98 (citing Expropriation Law, art. 3 (Exhibit C-34)).

<sup>146</sup> *See* Exh. C-116 (Administrative Record – Tala); Exh. C- 117 (Administrative Record – Lázaro Cárdenas); Exh. C-118 (Administrative Record – Benito Juárez); Exh. C- 119

Records reveals that each contains essentially the same information most of which pertains to other mills and only a fraction of which specifically relates to GAM's mills (see blue pages in each Administrative Record).<sup>147</sup>

75. Interspersed throughout each Administrative Record, one finds significant portions of the “*Estudio de la Industria Azucarera Mexicana*” (the “Sparks Report”), which is dated 31 July 1998. This information was more than three years old at the time that Mexico expropriated the sugar mills and therefore could not possibly have served as a reliable basis for determining which mills it should expropriate.

76. In addition to the Sparks Report, each Administrative Record also contains a document entitled “Administrative Record – Technical File” (*Expediente Administrativo – Técnico*).<sup>148</sup> This document, also provided as Exhibit C-50, is exactly the same in all five Administrative Records and summarizes in six sentences the alleged facts Mexico asserts as the basis for expropriation of GAM's mills. The reasons outlined by Mexico in the Administrative Record are listed:

- (1) GAM produces approximately 9% of the country's sugar.
- (2) As of 30 June 2001, GAM's 6 mills owed the Federal Government approximately 450 million pesos.
- (3) GAM could not receive credit due to its entry into *suspensión de pagos* on 2 May 2000.
- (4) GAM could not pay its debts to the cane producers, which totaled approximately 463 million pesos.

---

(Administrative Record – San Francisco); and Exh. C-120 (Administrative Record – San Pedro) (each one consisting a large three-ring binder with over 600 pages).

<sup>147</sup> See Exhibits C-116-120 (containing blue pages in each denoting those documents that relate to GAM's mills).

<sup>148</sup> See Exh. C-116, pp. 008-012 (Administrative Record – Tala); Exh. C-117, pp. pp. 006-010 (Administrative Record – Lázaro Cárdenas); Exh. C-118, pp. 008-012 (Administrative Record – Benito Juárez); Exh. C-119, pp. 007-011 (Administrative Record – San Francisco); and Exh. C-120, pp. 007-011 (Administrative Record – San Pedro).

- (5) GAM was involved in serious difficulties related to the issuance of bonds to foreign investors in Europe and had to repurchase those bonds with serious losses for the investors that acquired those instruments.
- (6) The foregoing events affected and continue to affect confidence in the national sugar industry.
- (7) GAM's financial problems jeopardize the milling of nearly 4 million tons of sugarcane in the next harvest.
- (8) The Mexican Central Bank classified GAM's mills with "Letter E" signifying that they cannot be granted credit nor guarantees.<sup>149</sup>

We address each of these points below:

77. Point 1: Mexico's statement that GAM produces 9 percent of the sugar in the country is not supported by any evidence found in the Administrative Record, but is not disputed.

However, size is not a relevant expropriation factor. Mexico left approximately half of the nation's sugar production in private hands and other industry participants, such as BSM, had shares of national sugar production comparable to GAM's, but were not expropriated.<sup>150</sup>

78. Point 2: GAM had only five mills, not six, and the Administrative Record erroneously counted Eldorado as one of GAM's mills.<sup>151</sup> In addition, the Administrative Record states the debt of GAM's mills at different levels in different places, and is consistent only in always being wrong, always overstating the debt and never providing the basis of its calculations.<sup>152</sup> The only evidence of any debt of GAM in the Administrative Record is 46,240,000 pesos (approximately

---

<sup>149</sup> Administrative Record – Technical File, page 3, paras. 4-8, and page 4 at para. 1 (Exh. C-50).

<sup>150</sup> Statement of Claim, para. 117.

<sup>151</sup> Although Mexico states, correctly, at one point in its brief that GAM owned five mills, *see* Statement of Defense, para. 272, it continues to rely on the erroneous inclusion of the Eldorado mill in its analysis. *See* L.R. Garcia Report, at 35 ("The Benito Juárez, Eldorado and the San Pedro mills that belong to GAM are in group 'R.'").

<sup>152</sup> *See Annex I - Cartera de Créditos de los Ingenios Azucareros con Fina al 30 Junio 2001, con Base en los Estados de Cuenta* ("Annex I"). This document appears at, for example, Exh. C-120, p. 243; at Exh. C-119, p. 245.

US\$4.6 million), and Mexico itself has said that only information in the Administrative Record was considered in making the expropriation decisions.<sup>153</sup>

79. Point 3: GAM had signed a series of agreements with the *cañeros* to make payments for the 2000/2001 harvest.<sup>154</sup> The Administrative Records contain only the 14 June 2001 Agreement and ignore the 14 August 2001 Agreement that, but for the expropriation, would have resolved all of GAM's debts to the *cañeros*.

80. Point 4: Mexico's statement that GAM was not eligible for credit due to *suspensión de pagos* is incorrect. *Suspensión de pagos* did not preclude GAM from receiving post-petition credit, which it received with authorization from the court.<sup>155</sup>

81. Points 5-7: The Administrative Records contain no supporting evidence for points 5-7 of the Technical Administrative File, nor are those points true.

82. Point 8: As to Mexico's final point, there is no supporting documentary evidence in the Administrative Records as to the rating for any of GAM's mills. Moreover, the Administrative Record itself demonstrates that Mexico did not follow its own criteria in the Record. Mexico did not expropriate other mills which had the very same "Letter E" rating attributed to GAM. Other mills that also received a "Letter E" rating and yet were not expropriated include: Puga, El Refugio, Motzorongo and Santo Domingo.<sup>156</sup> In addition, the chart, at or around page 606 of each Administrative Record, contains the following footnote:

---

<sup>153</sup> See *id.* (adding the data in Annex I for each of the five mills: Benito Juárez (4,594,000); Lázaro Cárdenas (1,806,000); San Francisco (2,678,000) San Pedro (9,582,000); and Tala (27,580,000). The total comes to 46,240,000 pesos.

<sup>154</sup> See *supra* Section II.D.1.

<sup>155</sup> See *supra* Section II.D.2.

<sup>156</sup> See, e.g., Administrative Record – San Pedro, p. 261 (Exh. C-120).

Important Note: When a group or sugar mill has a zero in any of its estimated areas or is in suspension of payment or bankruptcy, the system shall grant it a classification of “E.”<sup>157</sup>

However, in that same chart there are several instances, such as that of Calipam, El Carmen, Dos Patrias, Los Mochis, Bellavista, and Cuatotolapam, where the group or mill received a zero, and yet it was *not* marked with the classification rating of “E”. Instead, those mills simply received an “ND” or “Not Determined” rating and they were not expropriated.

83. Mexico in most instances expropriated all mills of common ownership, rather than evaluating each mill on its own merits, as might have been expected if Mexico’s criteria were as claimed in the Administrative Record. The exception to Mexico’s policy of making expropriation decisions by owner was the Machado I group. All five mills of the Machado I Group had a “Letter E” rating; however, Mexico only expropriated four of those mills. Mexico’s own expert, L.R. Garcia, includes a chart that demonstrates that Mexico expropriated the four best performing mills within the Machado I Group, leaving the worst performer in the hands of the original owners.<sup>158</sup> This result is the opposite of Mexico’s claimed criteria.

84. The very same chart relied on by Mexico’s expert also demonstrates that GAM’s mills were in comparable or better operational condition, than many of the mills that were not expropriated.<sup>159</sup> For example, mills such as Dos Patrias and Independencia, which were performing worse than GAM’s mills according to Mr. L.R. Garcia’s information, were not expropriated.<sup>160</sup>

---

<sup>157</sup> See, e.g., Exh. C-117, p. 606; Exh. C-118, p. 606; Exh. C-119, p. 603; and Exh. C-120, p. 606.

<sup>158</sup> See SOD Exh. R-12, p. 33.

<sup>159</sup> See *id.*

<sup>160</sup> See Cruz Statement, pp. 10-14 (Exh. C-113); see also SOD Exh. R-12, p. 33.

85. There is also indication that the rating system itself was flawed. For example, Independencia, although classified according the Administrative Record with a “Letter C” rating, was actually in worse financial condition than GAM at the time of the expropriation. In fact, despite the recent recovery in the sugar regime which has brought success to most mills in the sugar industry, Independencia is now in bankruptcy proceedings (“*concurso mercantil*”).<sup>161</sup>

### **III. LEGAL ARGUMENT**

86. Just as the factual record corroborates GAMI’s position rather than supporting Mexico’s effort to defend its actions, Mexico’s legal arguments similarly lack merit. This part addresses those arguments. Where appropriate, this part makes cross references to Part III above, which has already addressed most of the alleged factual bases for Mexico’s defenses.

#### **A. The Tribunal Has Jurisdiction Over Each Of GAMI’s Claims**

87. In Mexico’s Statement of Defense,<sup>162</sup> Mexico reiterates the jurisdictional arguments that it submitted and GAMI rebutted in two rounds of written jurisdictional briefs and in the oral hearing on jurisdiction on September 24, 2003. In Procedural Order No. 4, the Tribunal made clear that it did not require further argument on these issues:

For the avoidance of doubt, the Arbitral Tribunal emphasizes that it is satisfied with the thorough and cogent presentations by both sides with respect to the issues of jurisdiction and admissibility, and invites no further submissions in this regard (subject to the arbitrators’ discretion to ask of specific observations or clarifications as may appear appropriate in light of future developments).<sup>163</sup>

---

<sup>161</sup> See SOD Exh. R-12, p. 33; 2001 Financial Statement of Independencia Mill (Exh. C-140).

<sup>162</sup> See Statement of Defense, paras. 161-168, 198-206, 230-235, 259-267.

<sup>163</sup> Tribunal’s Procedural Order No. 4, para. 3 (25 September 2003).

88. Accordingly, GAMI refers the Tribunal to its Procedural Order No. 4 and to GAMI's refutation of Mexico's position as set out in GAMI's previous submissions, and will not repeat those submissions here.

## **B. ARTICLE 1105**

89. In the Statement of Claim, GAMI established that Mexico committed two independent breaches of Article 1105. First, Mexico treated GAMI's investment unfairly and inequitably when it flagrantly failed to implement and enforce Mexican sugar laws, with the effect of substantially reducing the value of GAMI's investment. Second, Mexico also breached Article 1105 when it expropriated GAMI's shares based on an arbitrary and unsubstantiated application of its own criteria for expropriation under the Expropriation Decree.

90. Mexico's response to GAMI's claim misrepresents both the salient facts and the law with regard to GAMI's claims under Article 1105. In Section II above, GAMI has set out in some detail most of the numerous factual elements on which GAMI's claim is founded. Accordingly, this Section will focus on refuting Mexico's misinterpretation of the requirements of Article 1105, while noting those portions of the factual summary that respond to Mexico's erroneous assertions of fact.

### **1. Mexico Arbitrarily Implemented And Enforced The Sugar Regime**

91. Mexico argues three basic points, each either irrelevant or without merit, in response to GAMI's claim that Mexico breached Article 1105 through its flagrant failure to implement and enforce its sugar laws. Mexico contends that:

- (1) the surpluses and depressed prices that prevailed in Mexico's market are not a violation of international law;<sup>164</sup>
- (2) a measure may not be held to be an Mexican court has yet found that measure to be illegal under domestic law;<sup>165</sup> and

---

<sup>164</sup> Statement of Defense, para. 238.

<sup>165</sup> *See id.*, paras. 240-242.

(3) Mexico did not manage the sugar regime in an arbitrary manner.<sup>166</sup>

92. GAMI responds to each of these points in turn.

**a. It Is Irrelevant That Surpluses And Depressed Prices Are Not A Violation Of International Law**

93. Mexico first argues that “NAFTA does not prohibit, but rather recognizes, the legality of surplus production.”<sup>167</sup> Mexico’s argument is irrelevant. GAMI has never alleged that countries have an international law obligation to control surpluses or otherwise support or stabilize domestic production of any product. However, Mexico, having undertaken by law to do so, does have an obligation under Article 1105, which embraces the international law minimum standard, to follow the rule of law, and not to arbitrarily enforce or fail to enforce that law.<sup>168</sup> The arbitrariness in this case is aggravated because Mexico did enforce the law to sustain the price of sugar cane, but then left the millers to absorb that high price without enforcing the provisions that would have sustained the millers. The law required balanced intervention, not just intervention for the *cañeros*.

**b. A Measure May Be Found To Be Arbitrary Without First Being Challenged As Illegal Under Domestic Law In The Host State’s Courts**

94. Mexico next argues that because GAMI has not first challenged the measures in Mexican courts, GAMI “cannot pursue this claim.”<sup>169</sup> This argument is nothing more than an attempt to impose a requirement upon the investor to exhaust its local remedies. However, Chapter 11 of

---

<sup>166</sup> *See id.*, paras. 243-258.

<sup>167</sup> *Id.*, para. 238.

<sup>168</sup> *See, e.g., Asylum Case*, 1950 I.C.J. 266, 284 (20 November 1950) (Exh. C-141).

<sup>169</sup> Statement of Defense, paras. 169(b), 240-242; *see also id.* at para. 249 (“Absent a ruling of illegality at the level of Mexican law, the Tribunal cannot proceed to analyze whether the conduct of the Mexican authorities can be characterized as arbitrary in accordance with international law.”).

the NAFTA, like most modern investment treaties, waives the exhaustion requirement of customary international law. Article 1121 plainly does not require investors to challenge the offending measures in national courts before submitting the claim to international arbitration.<sup>170</sup>

95. Where, an international tribunal has jurisdiction over a claim, as is the case here, the tribunal is not obligated to wait for a domestic court ruling, but rather must make a definitive determination of those claims. According to the *Vivendi Annulment* Committee:

In the Committee’s view, it is not open to an ICSID tribunal having jurisdiction under a BIT in respect of a claim based upon a substantive provision of that BIT, to dismiss the claim on the ground that it could or should have been dealt with by a national court. In such a case, the inquiry which the ICSID tribunal is required to undertake is one governed by the ICSID Convention, by the BIT and by applicable international law. Such an inquiry is municipal law, including any municipal law agreement of the parties.<sup>171</sup>

96. Mexico argues that both the ICJ’s Opinion in the *Case Concerning Elettronica Sicula S.p.A. (ELSI)* (“ELSI”) and the NAFTA Award in *ADF Group Inc. v. United States of America* (“ADF”) support its argument, but that is not so. In *ADF*, the investor did not challenge the alleged measure in the U.S. courts prior to challenging the measure as a breach of Article 1105.<sup>172</sup> Nevertheless, the *ADF* tribunal fully addressed the merits of the investors claim.<sup>173</sup>

---

<sup>170</sup> Article 1121(1) states:

1. A disputing investor may submit a claim under Article 1116 to arbitration only if:

....

(b) the investor waives their right *to initiate or continue* before any administrative tribunal or *court* under the law of any Party . . . any proceedings with respect to the measure of the disputing Party . . . (emphasis added)

<sup>171</sup> *Compañía de Aguas del Aconquija S.A. v. Argentine Republic*, Decision on Annulment, ICSID Case No. ARB/97/3, para. 102 (3 July 2002), *reprinted in* 41 ILM 1135 (2002) (Exh. C-143) (“Vivendi Annulment”).

<sup>172</sup> *See ADF*, paras. 44-55 (Exh. C-46).

Likewise, *ELSI* does not support Mexico's argument. Rather, the *ELSI* Court held that finding a breach of international law is not dependent on finding a breach in municipal law and vice versa.<sup>174</sup>

97. Not only is there no obligation to exhaust local remedies, it is far from clear that GAMI or any other person would be able to force the Government to implement properly the sugar regime. Chief Justice Schmill states:

Now, it is important to note that the Mexican legislation do not provide any remedy for the individuals to force the Government to act in a manner that assures the accomplishment of the objectives of the 1991 Decree, its modifications of 1993 and the 1997, 1998 and 2000 Acuerdos.<sup>175</sup>

**c. Mexico's Failure to Implement And Enforce The Sugar Regime**

**(1) Mexico Is Legally Responsible For The Failure Of The Sugar Regime**

98. In paragraphs 170 to 177, Mexico argues, as a general defense to GAMI's first claim under Article 1105, that the failure of the sugar regime is not "imputable" to it because the conduct or inaction alleged to breach NAFTA was done (or not done) by "private entities," for which the "State is not responsible."<sup>176</sup> This attempt to deny its responsibility and shift the

---

<sup>173</sup> See *id.*, paras. 175-192.

<sup>174</sup> *ELSI*, para. 73 (Exh. C-144), stating:

Compliance with municipal law and compliance with the provisions of a treaty are different questions. What is a breach of treaty may be lawful in the municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision. Even had the Prefect held the requisition to be entirely justified in Italian law, this would not exclude the possibility that it was a violation of the FCN Treaty.

*See also Vivendi Annulment*, para. 97 (Exh. C-143) (finding same).

<sup>175</sup> Schmill Opinion, para. 102 (Exh. C-110).

<sup>176</sup> Statement of Defense, paras. 170-172; *see also id.*, para 189, stating:

blame elsewhere is refuted in Section II.B.2 above, where GAMI explains the responsibility of the Government to enforce the law and the disingenuousness of the effort to shift that responsibility.

99. Other international arbitral bodies have properly held governments responsible for measures that, although superficially appearing to be “voluntary” actions or a product of consensus, in fact had the effect of mandatory measures. In numerous GATT/WTO cases, panels have made clear that nominally “voluntary” private actions in substance have been compelled, and that governments may be held responsible for measures that lack the formality but not the effect of compulsory regulation.<sup>177</sup> In doing so, panels have consistently looked

---

The legal instruments to which GAMI refers as the applicable “Law”, and which establish the provisions GAMI accuses Mexico of violating, are the product of an agreement between the three sectors involved. These instruments do not establish the obligations for the federal Government that GAMI accuses Mexico of having breached: calculating the reference price, export requirements, and basic production levels. The industry participates in determining these three elements through the CNIAA. In fact, both export volumes and base production levels result from commitments assumed by the mills and noncompliance gives rise to contractual penalties demandable by the productive sectors themselves, and under no circumstances by the Government.

<sup>177</sup> See, e.g., *Japan – Trade in Semi-conductors*, BISD 35S/116, para. 109 (adopted 4 May, 1988) (Exh. C-145) (finding that administrative guidance constitutes “measures” under Article XI:1 and stating that the “two essential criteria” are that: (1) “there were reasonable grounds to believe that sufficient incentives or disincentives existed for non-mandatory measure to take effect”; and (2) “was the operation of the measure to restrict export[s] . . . essentially dependent on Government action or intervention”); *Canada – Certain Measures Affecting the Automotive Industry*, where the panel found that commitments made among four automobile manufacturers constituted “requirements” as understood by Article III:4 of GATT where:

In sum, the evidence before the Panel shows that: (i) in making the undertakings contained in the Letters, the companies *acted at the request* of the Government of Canada; (ii) the anticipated conclusion of the Auto Pact was a key factor in the decision of the companies to submit these undertakings; (iii) the companies *accepted responsibility* vis-à-vis the Government of Canada with

beyond formalistic textual arguments to determine the true impact of the instrument on the Government and participants.<sup>178</sup>

100. Likewise, in this dispute, GAMI has demonstrated that the provisions for industry “consultation” or “consensus” are of little or no weight in the face of the Government’s power to guide and control that consensus.

**(2) Mexico’s Arbitrary Implementation Of Its Sugar Regime Constitutes A Breach Of Article 1105**

101. In defense of its non-compliance with the law, Mexico, citing three previous NAFTA awards, asserts that NAFTA tribunals have “consistently maintained” that the mismanagement of government programs is not a violation of customary international law and therefore, presumably not a violation of Article 1105.<sup>179</sup>

102. It is uncontested, as noted in both the *Azinian* and *Feldman* awards, that not every business problem of a foreign investor, and not every governmental failing, is necessarily a

---

respect to the implementation of the undertakings contained in the Letters, which they described as "obligations" and in respect of which they undertook to provide information to the Government of Canada and indicated their understanding that the Government of Canada would conduct yearly audits; and (iv) at least until model year 1996, the Government of Canada *gathered information on an annual basis* concerning the implementation of the conditions provided for in the Letters.

WT/DS/139/R, para. 10.122 (AB Report adopted June 19, 2000) (emphasis added) (Exh. C-146); *Japan – Measures Affecting Consumer Film and Photographic Paper*, WT/DS44/R, paras. 10.298-10.299 (adopted April 22, 1998) (finding that decisions made by “councils” composed of private actors that are “largely the product of decisions by private industry associations,” are nevertheless “requirements” attributable to the Government where the councils were required to “liaise with the competent Government authority,” and where the councils’ decisions have a “sufficient connection to administrative guidance of the Japanese Government”) (Exh. C-147).

<sup>178</sup> *See id.*

<sup>179</sup> Statement of Defense, paras. 253-255 (quoting *S.D. Myers v. Government of Canada*, *Azinian v. United Mexican States*, and *Feldman v. Mexico*).

breach of an investment treaty.<sup>180</sup> The *Feldman* Tribunal correctly recognized that governments do not necessarily breach Chapter 11 “in their exercise of regulatory power,” or in changing “their laws and regulations in response to changing economic circumstances or changing political, economic or social considerations.”<sup>181</sup> However, the holding that not every governmental regulatory deficiency rises to the level of a breach of the international law obligation to accord fair and equitable treatment does not suggest that host states are free to act arbitrarily in disregard of their own legal regimes to the detriment of foreign investors. In the Statement of Claim, GAMI explained how Article 1105, as well as past arbitral awards, support a finding that Mexico's behavior in this case breaches the standards of Article 1105 with respect to GAMI's investment.<sup>182</sup> Recent arbitral awards that have appeared since GAMI filed its Statement of Claim have articulated a standard of fair treatment of investors that, if anything, even more strongly support a finding that Mexico has breached the international minimum standard in the measures that are the subject of GAMI's complaint here.<sup>183</sup>

---

<sup>180</sup> See *Azinian v. Mexico*, Award, ICSID Case No. ARB(AF)/97/2, Award, (1 November 1999), paras. 83-84 (Exh. C-148); see also *Feldman v. Mexico*, Award, ICSID Case No. ARB(AF)/99/1, para. 112 (16 December 2002) (Exh. C-73).

<sup>181</sup> *Feldman*, para. 112 (Exh. C-73).

<sup>182</sup> Statement of Claim, paras. 75-81 (citing *Mondev* (Exhibit C-44), *ADF* (Exhibit C-46), and the Third Restatement (Exhibit C-48)); see also S. Vasciannie, *The Fair and Equitable Treatment Standard in International Investment Law and Practice*, 70 *BYIL* 99, 133 (1999) (Exh. C-149) (stating that “if there is discrimination on arbitrary grounds, or if the investment has been subject to arbitrary or capricious treatment by the host State, then the fair and equitable treatment standard has been violated. This follows from the idea that fair and equitable treatment inherently precludes arbitrary and capricious actions against investors”).

<sup>183</sup> *Técnicas Medioambientales Tecmed S.A. v. The United Mexican States* Case No. ARB (AF)/00/2, Award, para. 154, (May 29, 2003) (Exh. C- 150) (finding that the fair and equitable treatment standard requires the state “to provide treatment that does not affect the basic expectations” of the foreign investor, including that the State will act “in a consistent manner” and “totally transparently” so that the investor “may know beforehand . . . all rules and regulations that will govern its investments, as well as the goals of the relevant policies and administrative practices or directives, to be able to plan its investment and comply with such regulations. . . . The investor also expects the State to use the legal instruments that govern the actions of the investor or the investment in conformity with the function usually assigned to such instruments,

103. In sum, the Statement of Defense does not credibly explain and cannot justify Mexico's failure to implement and enforce the law with respect to the matters set out in detail by GAMI. Instead, Mexico tries to defend its actions, not on the merits, but with redundant jurisdictional objections or obviously unfounded legal theories, such as the doctrine of exhaustion of local remedies or the untenable denial of the Government's responsibility for the implementation and enforcement of the laws it creates. Mexico, however, is simply unable to provide any coherent justification for its flagrant failure to follow and enforce its own law. It is telling that Mexico, having used the Government-caused difficulties of the milling industry as a pretext for expropriation of 27 mills, has found a way to bring a strong recovery to the industry since the expropriation. This improvement has happened even though exogenous pressures have scarcely changed and provides powerful evidence that through both its own conduct and inaction, Mexico treated GAMI's investment unfairly and inequitably in violation of international law and Article 1105.

## 2. Mexico Arbitrarily Expropriated GAMI's Investment

104. As GAMI explained in the Statement of Claim, Mexico justified the expropriation of the 27 mills based on four criteria: 1) whether the mills were being honestly managed; 2) whether the financial state of a mill was such that the livelihood of those that depended on the mill had been put at risk; 3) whether the financial state of the mill was such that the mill would be unable to make the necessary repairs prior to the 2001/2002 harvest; and 4) whether the owners are the ones which the local *cañeros* have indicated that they will not continue to work.<sup>184</sup>

---

and not to deprive the investor of its investment without the required compensation); *see also Metalclad v. United Mexican States* (Exh. C-79) (finding that Mexico breached Articles 1105 where “Mexico failed to ensure a transparent and predictable framework for Metalclad’s business planning and investment”); *Maffezini v. Spain*, ICSID Case No. ARB/97/7, Award on the Merits, para 83 (November 13, 2000) (Exh. C-151) (holding that “lack of transparency . . . is incompatible with Spain’s commitment to ensure the investor a fair and equitable treatment in accordance with Article 4(1) of the same treaty”).

<sup>184</sup> *See* Statement of Claim, para, 97 (citing Expropriation Decree, paras. 1-7 (Exhibit C- 15)).

105. GAMI established in the Statement of Claim that none of GAM's mills qualify for expropriation under any of these criteria.<sup>185</sup> In this regard, GAMI noted that at the time Mexico seized the five GAM mills, GAM had made all agreed upon payments to the *cañeros*.<sup>186</sup> Accordingly, GAMI established that Mexico has seized the GAM mills (thereby indirectly expropriating GAMI's investment) without basis and therefore in violation of international law and Article 1105.

106. In its Statement of Defense, Mexico did not even attempt to justify the expropriation of the GAM mills under most of its own criteria. Mexico does not contest that the GAM mills were being honestly managed, that the mill workers' livelihoods were never at risk, that GAM had sufficient cash reserves and a sound financial plan to ensure the maintenance of the mills during the off-season, and that the *cañeros* would continue to work with GAM and its investors. Instead, Mexico tries to defend its action based on GAM's entry into *suspensión de pagos* and general and ill-founded allegations regarding GAM's debt and the implication for *cañeros* associated with GAM.

107. First, Mexico repeatedly asserts that the GAM mills were expropriated because GAM was in *suspensión de pagos*.<sup>187</sup> This rationale itself is so arbitrary and unfounded that it alone constitutes a breach of Article 1105. Under Mexican law, at the time GAM became insolvent, GAM had a statutory right to enter into *suspensión de pagos*.<sup>188</sup> Mexico now asserts GAM's exercise of this right as the primary justification for the expropriation. Mexico's actions are both illogical and deeply unfair to GAM, to its shareholders such as GAMI, and to GAM's creditors, and to its associated *cañeros*.

---

<sup>185</sup> See *id.*, paras 96-107.

<sup>186</sup> See *id.*, paras 102-103.

<sup>187</sup> See Statement of Defense, paras. 153-154.

<sup>188</sup> See Oscós Statement para. 22 (Exh. C-11).

108. As explained above in Section II.D.2, the *suspensión de pagos* law exists so that indebted, but functioning companies may remain viable entities while they reorganize, their debt. Expropriating the assets of companies like GAM, however, defeats the entire purpose of the law, because a company whose assets are seized of course, cannot be viable and cannot satisfy its creditors. Further, nothing in the law of *suspensión de pagos* provides that entry into *suspensión de pagos* will justify expropriation of the company. It is a basic principle of law that a state may not discriminate against an enterprise that invokes legal protection from creditors.<sup>189</sup> By imposing without warning this arbitrary and unjustifiable penalty on GAM and its shareholders, Mexico breaches the minimum standard of Article 1105.

109. Mexico tries to support its thesis by unfounded and inaccurate claims that GAM had great trouble paying off its debts for the 1999/00 harvest as well as for the 2000/01 harvest.<sup>190</sup>

110. However, as explained in Section II.D.1 above, Mexico's allegations are based on inaccurate and unfounded information.

111. As also discussed above in Section II.D.3, Mexico's own evidence – or the lack thereof – confirms that the expropriation of GAM mills was not warranted under Mexico's own criteria, and thus was arbitrary, discriminatory and capricious:

- By including the Eldorado mill within GAM's group, Mexico continues to overstate materially GAM's debt.
- According to the evidence Mexico's expert used as a basis for his opinion, four of the five GAM mills qualified as "efficient" in at least their mill operations, yet all were expropriated.
- Mexico did not expropriate other mills which, like the GAM mills, had been classified as "E" mills and thus ostensibly qualified for expropriation. Other mills that also received a "Letter E" rating but which

---

<sup>189</sup> See, e.g., 11 U.S.C. § 525(a) (Exh. C-153) (statutory prohibition against governmental discrimination against any person or entity that is or has been a debtor under U.S. bankruptcy law).

<sup>190</sup> Statement of Defense, paras. 148, 149.

were not expropriated included: Puga, El Refugio, Motzorongo and Santo Domingo and four of the five Machado-owned mills.

- Mexico did not expropriate six other mills which, like the GAM mills, had qualified for an “E” rating by scoring a “0.00” in one category of their credit histories.<sup>191</sup>
- Mexico expropriated on a per-group basis instead of a per-mill basis in every case but one. In the case of the Machado I Group, Mexico expropriated only four of the five mills in the group, leaving the most at-risk mill while taking the most viable.
- At the time of the expropriation, the Independencia mill was in much worse financial shape than the GAM mills, yet it was not expropriated.

112. In sum, it is clear that Mexico expropriated GAMI’s investment without basis and in violation of Article 1105. As discussed, Mexico persists in trying to justify its actions based on the same inaccurate and incomplete information that it used in September of 2001 – even after being given notice that its data is insufficient and incorrect.

### **C. ARTICLE 1102**

113. In its Statement of Claim, GAMI argued that Mexico has breached Article 1102 in two expropriated respects. First, Mexico indirectly expropriated GAMI’s share in GAM while not expropriating the shares of other Mexican investors in other mills that were not expropriated, including a number of unexpropriated mills that fit Mexico's criteria for expropriation comparable or greater degree than mills of GAM.

114. Second, GAMI argued that Mexico failed to enforce the export regime against non-complying mills, while GAMI’s mills complied. Mexico has now come forward with evidence that Mexico did apply some of the penalties of the enforcement scheme, in that non-complying mills were deprived of benefits for financing inventories and access to the small quota into the U.S. market. Even accepting these facts as true, Mexico’s conduct was still discriminatory in

---

<sup>191</sup> As stated above, Mexico’s tables indicate that any mill with a “0.00” grade in any of the columns should be classified as an “E” mill and be should expropriated. However the following mills all received an “ND” or “no determinado” rating instead of an "E" rating and were not expropriated: Los Mochis, Calipam, El Carmen, Dos Patrias and El Molino.

that the most important sanction for non-compliance with export requirements – the penalty price to *cañeros* – remained a dead letter as a practical matter because the Government failed to provide information on a timely basis to enable enforcement against violators, increasing the disadvantage to mills such as those in which GAMI invested, which did comply. This is fully addressed in Section II.B.2; the remainder of this Section will address exclusively the breach of 1102 as a result of the discriminatory expropriation.

115. Mexico asserts two principal defenses to the Article 1102 claim. First, Mexico argues that GAMI is not “in like circumstances” with Mexican investors in other mills. Second, Mexico argues that any discriminatory treatment was not based on nationality. As GAMI will show, both of these arguments are without merit.

### 1. In Like Circumstances

116. With regard to the issue of like circumstances, Mexico’s primary contention is that, because GAM was the only sugar mill in *suspensión de pagos*, no company is in like circumstances with GAM and hence no investor in other companies is in like circumstances with GAMI.<sup>192</sup> Alternatively, Mexico argues that BSM’s investment was not in like circumstances with GAMI’s investment because BSM’s debt burden was different from GAM’s.<sup>193</sup>

117. As discussed above,<sup>194</sup> the fact that GAM was in *suspensión de pagos* cannot justify discriminatory action against GAM or GAMI’s investment, nor is it a basis for claiming that GAM or GAMI is not in like circumstances with those invested in mills not in *suspensión de pagos*.<sup>195</sup> *Suspensión de pagos* provides temporary legal protection from creditors precisely so

---

<sup>192</sup> See Statement of Defense, para. 272 (“GAM and the five mills it owned were the only companies in the sugar sector in *suspensión de pagos*. No other such company was in the same situation.”).

<sup>193</sup> See *id.*, para. 270; *id.* para. 271 (“Mexico further asserts that aside from its “enormous debt,” GAM had “default[ed] on payment to cane growers, and default[ed] on its credit obligations,” and thus was not “creditworthy.”).

<sup>194</sup> See *supra* Section II.D.3.

<sup>195</sup> See Statement of Defense, para. 272.

that an enterprise will be able to maintain normal operations. In GAM's case, *suspensión de pagos* made GAM better able to make payments to its *cañeros* and mill workers.<sup>196</sup> The report of Mexico's own expert assumes that Mexico would continue to make payments to *cañeros*,<sup>197</sup> and the witness statement of Mr. Cruz confirms what GAMI demonstrated in its Statement of Claim: GAM had reached agreement to satisfy its responsibilities to *cañeros* and was meeting those obligations at the time of the expropriation.<sup>198</sup> In citing *suspensión de pagos* as the justification for discriminatory expropriation, Mexico effectively is adding a punishment to GAM (and GAMI) in provisions of Mexican law that contain no such penalty. Indeed, it is the expropriation that has frustrated the very purpose of the Mexican law of *suspensión de pagos*, since the expropriation obviously made it impossible for GAM to continue in business and to satisfy its creditors.<sup>199</sup> In sum, there is no rational reason to distinguish between GAM and all other mills based on *suspensión de pagos*.<sup>200</sup>

118. Mexico also argues that GAM is not in like circumstances with BSM, because of GAM's debt. However, the evidence does not support Mexico and particularly does not demonstrate that GAM was less likely to meet its obligations to *cañeros*. As discussed in the Statement of Claim, BSM's finances were similar to GAM's as of the date of expropriation:

- BSM had an outstanding overall debt of US\$116,134,000 compared to GAM's overall debt of US\$139,540,000;

---

<sup>196</sup> See Oscós Report, para. 47 (Exh. C-111).

<sup>197</sup> See FGA Report, annex 2, p. 2 (Exh. R-16) (assuming for purposes of its analysis that GAM would not make any payment other than to *cañeros*).

<sup>198</sup> Cruz Statement, p. 11 (Exh. C-113); Statement of Claim, para 116.

<sup>199</sup> See Oscós Opinion, para. 39 (Exh. 111).

<sup>200</sup> See Statement of Defense, para. 277 ("all the shareholders of the rest of the holding companies whose mills were expropriated, and who, consequently, are in similar circumstances, also are Mexican nationals.").

- BSM had a debt to production ratio of \$278/ton, compared with GAM's ratio of \$325/ton; and
- both firms operated at a loss during 2001.<sup>201</sup>

119. Mexico responds to this point with the testimony of Mr. José Pinto Mazal, the Corporate Director of BSM, who simply declares that GAM's debts are greater than those of BSM.<sup>202</sup> Mr. Pinto, however, does not dispute any of the evidence that GAMI proffered establishing the similarity of the two companies at the time of expropriation.<sup>203</sup> Instead, he testifies in conclusory fashion that GAM's financial position was worse than BSM's as of December 31, 1999 - 20 months prior to the expropriation.<sup>204</sup> As explained in the Second Statement of Juan Cortina, Mr. Pinto's comparison is misleading and, in fact, demonstrates that GAM's finances were in some respects stronger than BSM's. For example, the most significant difference Mr. Pinto identifies is that GAM's ratio of foreign-currency denominated debt to total debt was much higher than BSM's.<sup>205</sup> All that this demonstrates, however, is that GAM had a high proportion of dollar-denominated debt as a result of its conscious, strategic decision to finance itself through issuance of public debt in the United States. This was a purposeful measure that allowed GAM to obtain more favorable interest rates, thus making its balance sheet stronger than BSM's in this respect.

120. Moreover, Mexico provides no evidence to refute that GAM met its obligations to the *cañeros* and mill workers in the same way as mills that were not expropriated. Mexico falsely contends that GAM had "default[ed] on payment to cane growers."<sup>206</sup> The reality is different. GAM, like unexpropriated mills reached agreement with the *cañeros* on a delayed payment

---

<sup>201</sup> See BSM and GAM Comparative Worksheet for the Third Quarter of 2001 (Exh. C-60).

<sup>202</sup> See Testimonial de José Pinto Mazal, para. 31 and annexed chart (SOD Exh. R-26).

<sup>203</sup> Statement of Claim, para. 118.

<sup>204</sup> SOD Exh. R-26.

<sup>205</sup> See Cortina Second Statement, paras. 2-5 (Exh. C-115).

<sup>206</sup> Statement of Defense, para. 271.

schedule for the 2000/01 harvest that stretched into the Fall of 2001. That is substantiated by documentary evidence and confirmed by both Mr. José Cruz and Mr. Cortina.<sup>207</sup> Further, many mills, including many that were not expropriated, such as Puga and Seoane, had reached similar agreements to delay their payment schedules to *cañeros* in same time period.<sup>208</sup> This extended payment schedule never resulted in the default of any obligation to the *cañeros* prior to the expropriation.

121. Thus, Mexico is simply wrong about GAM's alleged default, and Mexico has no answer or explanation at all for the similarity of GAM in this crucial respect to other companies whose mills were not expropriated. Mexico has conceded that the Administrative Record contains the entire record of the basis of which Mexico decided to expropriate some mills but not others.<sup>209</sup> That record, when compared to the evidence available, demonstrates Mexico's arbitrariness and discrimination.

122. Other evidence provided by Mexico confirms that GAMI is in like circumstances with investors in unexpropriated mills. Production figures provided by Mexico show that the production of GAM and BSM was practically identical,<sup>210</sup> while Mexico's own expert says that the overall productivity and efficiency of the two groups were very similar.<sup>211</sup>

---

<sup>207</sup> See Cruz Statement, p. 11 (Exh. C-113); see also Cortina Second Statement, p. 10-13 (Exh. C-115).

<sup>208</sup> Thus, BSM mills did not make its final payments for the 2000/01 harvest until between September 28 and October 24, 2001; the Puga mill did not make its final payments until October 31st, and the Seoane Group did not complete payments with their *cañeros* until August 31st. See GAMI's Statement of Claim, paras. 120-122. GAMI notes that there was a typographical error in paragraph 122 of its Statement of Claim. The sentence mistakenly refers to the Porres mills instead of the Puga mill. José Cruz likewise confirms that numerous unexpropriated mills negotiated similar delayed payment schedules. See Cruz Statement, p. 12-14 (Exh. C-113).

<sup>209</sup> See e.g., Letter from Hugo Perezcano to the Tribunal, p. 2 (26 August 2003) ("Hemos confirmado a GAMI que, respecto a la primer categoría de documentos solicitados, los que fueron considerados en conexión a la expropiación de los ingenios ya están integrados en el expediente administrativo de cada ingenio azucarero, mismos que le hemos proporcionado.").

<sup>210</sup> See Chamber production numbers for 1999/2000 Carte de la CNIAA a SECOFI de fecha 23 de marzo de 1998. (SOD Exh. R-41) (noting that GAM and BSM had very similar overall

123. Finally, as discussed in Section II.D.3, Mexico appeared to provide more favorable treatment to wholly Mexican-owned forms that qualified for expropriation but were not in fact seized by the Government.

**2. It Is Not necessary To demonstrate Intent To Discriminate Based On Nationality To Establish A Violation Of Article 1102**

124. Mexico also argues GAMI has failed to establish a breach of Article 1102 because GAMI has not proven that it was discriminated against because of GAMI's nationality.<sup>212</sup> Mexico notes in this regard that certain Mexican investors and their investments – notably those invested in GAM were treated in a similar fashion to GAMI and its investment.<sup>213</sup>

125. These arguments have no basis in the text of the Treaty or in relevant past awards. The text of Article 1102 prohibits treatment less favorable than domestic investors in like circumstances. It does not require demonstration of an intent to provide less favorable treatment, and it does not justify less favorable treatment of foreign investors if some domestic investors also get less favorable treatment. Mexico in effect tries to justify discriminatory treatment

---

production numbers); Carte de la CNIAA de fecha 22 de febrero de 2000; y documento titulado superficie de Caña de Azúcar, zafras 1997/1998 y 1999/2000 de fecha 29 de febrero de 2000. (SOD Exh. R-46) (noting that GAM and BSM's harvested acreage was very similar); *see also* Sparks October 1998 Report, p. 129 (Exh. R-11) (noting that production between the two groups was practically identical in the 1996/97 harvest).

<sup>211</sup> L. R. García Report, Table 9 (SOD Exh. R-12) (“In Table 9, it can be observed that the Grupo GAM mills operate under very similar conditions to those of the average of Mexican mills.”); *see also id.*, Table 6, stating that between 1989 and 1990 BSM and GAM had very similar productivity rates, with GAM having two mills with the highest efficiency rating, two mills with the middle rating and one mill with the lowest rating compared with BSM which had one or two mills qualify for the highest rating and three or four of its mills qualify for the middle rating. (examining mill productivity in the field and the factory between the 1989/90 and 1998/90 harvests). The uncertainty in these figures is due to the fact that there are two San Miguelitos, one owned by BSM and one formerly owned by CAZE and it is impossible to determine from the table which one is which.

<sup>212</sup> Statement of Defense, para 277.

<sup>213</sup> *Id.*, para. 277.

toward GAMI and its investment on grounds that Mexico also discriminated arbitrarily against some Mexican investors, while favoring others.

126. Mexico cites *Loewen v. United States*,<sup>214</sup> where, in *obiter dicta*, the Tribunal found that alleged anti-Canadian conduct in a court proceeding did not constitute – or more properly would not have constituted – a breach of Article 1102. The Tribunal stated:

The effect of these provisions [Article 1102(1) and (2)], as Respondent’s expert Professor Bilder states, is that a Mississippi court shall not conduct itself less favorably to Loewen, by reason of its Canadian nationality, than it would to an investor involved in similar activities and in a similar lawsuit from another state in the United States or from another location in Mississippi itself. We agree also with Professor Bilder when he says that Article 1102 is directed only to nationality-based discrimination and that it proscribes only demonstrable and significant indications of bias and prejudice on the basis of nationality, of a nature and consequence likely to have affected the outcome of the trial.<sup>215</sup>

127. The *Loewen* Tribunal was addressing allegations of misconduct of various kinds in a court proceeding, and had no evidence as to the treatment of local investors in such proceedings. This *dicta* cannot be stretched beyond its facts to mean that proof of intent to discriminate based on nationality is required to show a violation of Article 1102.<sup>216</sup>

128. In contrast, the *Feldman* tribunal, which addressed the identical argument that Mexico makes in this case,<sup>217</sup> found that Article 1102 by its terms suggests that it is sufficient to show less favorable treatment for the foreign investor than for domestic investors in like

---

<sup>214</sup> *Id.*, para. 273.

<sup>215</sup> *Loewen*, para. 139 (Exh. to Mexico’s Rejoinder on Jurisdiction).

<sup>216</sup> GAMI notes that the Tribunal decided this case on jurisdictional grounds.

<sup>217</sup> *See Feldman*, para. 163 (SOD Exh. C-73) (“Assuming, arguendo, that there is different treatment, Mexico argues that it is not sufficient under Article 1102 just to show different treatment for there to be a violation of Article 1102. Rather, any discrimination shown between the Claimant and domestically owned cigarette seller/exporters must be shown to be a result of the fact that the Claimant is a foreign national.”).

circumstances.”<sup>218</sup> The Tribunal further found strong policy concerns underlying this textual interpretation of Article 1102:

. . . requiring a foreign investor to prove that discrimination is based on his nationality could be an insurmountable burden to the Claimant, as that information may only be available to the Government. It would be virtually impossible for any claimant to meet the burden of demonstrating that a Government’s motivation for discrimination is nationality rather than some other reason. Also, as the Respondent argues, if the motives for a Government’s actions should not be examined, there is effectively no way for the Claimant or this Tribunal to make the subjective determination that the discriminatory action of the Government is a result of the Claimant’s nationality, again in the absence of credible evidence from the Respondent of a different motivation. If Article 1102 violations are limited to those where there is explicit (presumably *de jure*) discrimination against foreigners, e.g., through a law that treats foreign investors and domestic investors differently, it would greatly limit the effectiveness of the national treatment concept in protecting foreign investors.<sup>219</sup>

129. Citing the *Pope & Talbot* tribunal’s similar analysis of Article 1102,<sup>220</sup> the *Feldman* tribunal found that because “the treatment between the foreign investor and domestic investors in like circumstances is different on a *de facto* basis, and such discrimination is clearly in conflict with the investment liberalization objective found in Article 1102,” Mexico had violated Article 1102 based on evidence that a Mexican-owned investor had received more favorable treatment than its U.S. investor-owned competitor had.<sup>221</sup> A NAFTA government cannot justify its actions

---

<sup>218</sup> *Id.*, para. 181.

<sup>219</sup> *Id.*, para. 183.

<sup>220</sup> See *Pope & Talbot v. Government of Canada*, Final Merits Award, para. 79 (April 10, 2001) (Exh. C-47).

<sup>221</sup> *Feldman*, para. 184 (Exh. C-73).

by arguing that its discriminatory measures also provide adverse treatment to some or many domestic products.<sup>222</sup>

130. Accordingly, Mexico has failed to rebut GAMI's demonstration in its Statement of Claim that Mexico breached Article 1102 when it indirectly expropriated GAMI's investment in GAM.

#### **D. ARTICLE 1110**

131. Mexico offers little or no defense to GAMI's Article 1110 claim, except to repeat its objections to jurisdiction of the Tribunal. This is unsurprising because the facts relating to the expropriation are beyond any credible dispute and the law is unambiguous.

132. Article 1110 prohibits expropriation unless the expropriation is:

- (a) for a public purpose;
- (b) on a non-discriminatory basis;
- (c) in accordance with due process of law and Article 1105(1); and
- (d) on payment of compensation in accordance with paragraph 2 through 6.

A "legal" expropriation must meet all four of these criteria. Mexico has not met any of these four factors much less all of these factors and thus can not claim to have a "right to expropriate."<sup>223</sup> Because Mexico's conduct unambiguously is proscribed by NAFTA Article 1110, the only matter that should be at issue with respect to the expropriation is the measure of damages.

---

<sup>222</sup> See Statement of Claim, paras. 123-125 (citing *United States – Standards for Reformulated and Conventional Gasoline* (Exh. C-68), *Japan – Taxes on Alcoholic Beverages* (Exh. C-69), *United States – Measures Affecting Alcoholic and Malt Beverages* (Exh. C-71), and *Chile – Taxes on Alcoholic Beverages* (Exh. C-70), which stated, "it is sufficient to find that certain of the imports are taxed dissimilarly compared to certain of the domestic substitutable products. It is not necessary to show that all of the imports are taxed dissimilarly to all of the domestic products").

<sup>223</sup> See Statement of Defense, para. 196.

## 1. Mexico's Own Courts Have Determined That The Expropriation Decree Did Not Delineate A Valid Public Purpose

133. In the Statement of Claim, GAMI established Mexico's lack of a public purpose to justify the expropriation of GAM's mills.<sup>224</sup> Mexico, in its response claims that the Expropriation Decree establishes a valid reason of public utility, namely that the "financial health in the mills compromised their ability to obtain the necessary financial resources to process a significant portion of the sugarcane planted in the country [and] . . . endangered production of sugar, a necessary consumer commodity, and with it the jobs and livelihood of a large number of field workers as well as the economic activity of large regions of the country."<sup>225</sup> Mexico also argues that "[i]t is for the Mexican courts to determine whether the expropriation was or was not effected for reasons of public utility."<sup>226</sup>

134. These arguments fail on both legal and factual grounds. As to the law, this is a NAFTA Treaty claim and compliance is measured by Treaty standards not those of local law, though obviously a failure to meet local standards is a strong evidence of a failure to meet Treaty standards. But even if the standard were simply one of local rather than treaty law, Mexican courts in reality already have decided against Mexico on the question of whether Mexico issued the Expropriation Decree for a public purpose as a matter of Mexican law.<sup>227</sup> In the 19 August 2003 *amparo* decision related to GAM's mills, as well as two *amparo* proceedings completed involving unrelated mills, Mexican courts determined that the Respondent's rationale behind the Expropriation Decree either lacked evidence to establish a public purpose or was so ambiguous that it effectively would allow Mexico to expropriate at will, and found the expropriation

---

<sup>224</sup> See Statement of Claim, paras. 140-143.

<sup>225</sup> Statement of Defense, para. 202.

<sup>226</sup> *Id.*, para. 203.

<sup>227</sup> See Statement of Claim, paras. 140-143.

unlawful on these grounds.<sup>228</sup> This Tribunal should also find that Mexico's Expropriation Decree lacked a valid public purpose.

135. Referring to GAM's withdrawal of its writ of *amparo* in relation to San Francisco and San Pedro, Mexico also claims that "GAM itself has accepted the legality of the expropriation (at least with regard to two of the mills)."<sup>229</sup> Whether GAM has or has not accepted the legality of the expropriation of GAM's mills under Mexican law is irrelevant to GAMI's Treaty claim. GAMI's shares were indirectly seized by Mexico, and as a result, GAMI has a valid Treaty claim before this Tribunal. Further, the withdrawal of a writ of *amparo* does not signify GAM's acceptance of Mexico's expropriation. On the contrary, both GAM and GAMI continue to maintain that Mexico's expropriation of all of GAM's assets was illegal and based on an erroneous factual record.

## **2. Mexico Expropriated GAMI's Shares In GAM In A Discriminatory Manner**

136. As discussed in the Statement of Claim and in Section III.C above, Mexico did not expropriate the interests of other investors in mills in like circumstances, Mexico's expropriation of GAMI's shares was discriminatory.<sup>230</sup>

---

<sup>228</sup> See *Juicio de Amparo Indirecto* 863/200 1-III-A, 19 August 2003 (Exh. C-142); see also *Juez Séptimo de Distrito en Materia Administrativa en el Distrito Federal* ("Seventh Administrative District Judge"), 30 October 2002, Amparo Proceeding No. 851/2001 (Exhibit C-42) (noting that Mexico's proffered rationale for the expropriation – "for the benefit of the collective group" – is so broad that "any activity that generates a social benefit would fall within the meaning of the phrase."); *Juez Séptimo de Distrito en Materia Administrativa en el Distrito Federal* (Seventh Administrative District Judge), January 2, 2003, Amparo Proceeding No. 850/2001 at 10 (Exh. C-41) (holding that "no evidence has been provided that. . . prove the existence of a public purpose being performed. . .")

<sup>229</sup> Statement of Defense, para. 204 (emphasis in original).

<sup>230</sup> See Statement of Claim, paras. 110-131, 144.

### **3. The Expropriation Was Not Carried Out In Accordance With The Minimum Standards of Article 1105**

137. As GAMI pointed out in its Statement of Claim and in Section III.B.2 above, Mexico arbitrarily expropriated GAMI's investment in violation of Article 1105.

### **4. Mexico Has Not Provided The Required Compensation**

138. Even if the expropriation of GAMI's shares otherwise conformed to the requirements of Article 1110, which it does not, Mexico, more than two years after the expropriation, has still not compensated GAMI in accordance with Article 1110(2).<sup>231</sup>

139. Mexico claims that "the Expropriation Decree contains the federal Government's offer to pay the compensation required by law to those who accredit their legitimate right to it, subject to prior delivery of the *shares*, coupons or other instruments representing the capital of the expropriated companies."<sup>232</sup> Whatever Mexico's intentions to compensate GAM in accordance with Mexican laws, GAMI must be compensated in accordance with Article 1110. Having compensated GAMI, Mexico will be entitled to GAMI's shares in GAM.

---

<sup>231</sup> See *American International Group, Inc. v. Iran*, Award No. 93-2-3 (19 December 1983), reprinted in 4 Iran-U.S.C.T.R. 96, Section IV.2.a ("AIG") (Exh. C-80) ("[I]t is a general principle of public international law that even in a case of lawful nationalization the former owner of the nationalized property is normally entitled to compensation for the value of the property taken."). This was also recognized in *Phelps Dodge Corp. v. Iran*, Award No. 217-99-2, para. 22 (19 March 1986), reprinted in 10 Iran- U.S.C.T.R. 121, 130 (Exh. C-154):

The Tribunal fully understands the reasons why the Respondent felt compelled to protect its interests through this transfer of management, and the Tribunal understands the financial, economic and social concerns that inspired the law pursuant to which it acted, but those reasons and concerns cannot relieve the Respondent of the obligation to compensate Phelps Dodge for its loss.

<sup>232</sup> Statement of Defense, para. 205 (emphasis added). The word "shares" demonstrates that Mexico's own Decree belies Mexico's arguments before this Tribunal – a shareholder can be expropriated and has the right to compensation.

## 5. The Tribunal Is Fully Competent To Evaluate Article 1110 Claims

140. Article 1110 explicitly provides that direct as well as indirect expropriations constitute violations of the Agreement. It is irrelevant whether GAM is the only entity capable of bringing a claim for the *direct* expropriation of GAM's mills, since GAMI has made a valid claim for an *indirect* expropriation of its interest in GAM. The direct expropriation of GAM's mills has the effect of depriving GAMI of substantially all the value of its 14.18 percent minority share in GAM.<sup>233</sup>

141. As noted by the Tribunal in *Starrett Housing*, “[i]t is recognized in international law that measures taken by a State can interfere with property rights to such an extent that they must be considered to have been expropriated, even though the State does not purport to have expropriated them and the legal title remains with the original owner”.<sup>234</sup>

## 6. Regardless of Domestic Law And Domestic Proceedings, GAMI's Claims Remain Valid and Pertinent

142. In its Statement of Defense, Mexico argues that domestic law and domestic proceedings should be resolved before the Tribunal can make a finding on Claimant's expropriation claim under the Treaty. This argument has no basis in the NAFTA or prior awards. The very first award Mexico cites in its expropriation argument acknowledges that international tribunals are neither required nor expected to follow the decisions of domestic courts:

The Claimants have cited a number of cases where international arbitral tribunals did not consider themselves bound by decisions of national courts. Professor Dodge, in his oral argument, stressed

---

<sup>233</sup> See Statement of Claim, paras. 136-138. As a minority shareholder, GAMI is entitled to bring a claim under NAFTA for the expropriation of its 14.18 percent interest in GAM. See *id.*, para. 137, n.178. There is “no bar in current international law to the concept of allowing claims by shareholders independently from those of the corporation concerned, not even if those shareholders are minority or non-controlling shareholders.” *CMS Gas Transmission Company v. Republic of Argentina*, Case No. ARB/01/8, Decision of the Tribunal on Objections to Jurisdiction, para. 48 (July 17, 2003) (Exh. C-155).

<sup>234</sup> *Starrett Housing Corporation v. Iran*, Interlocutory Award No. ITL 32-24-1, o, 19 (19 December 1983) (Exh. C-156).

the following sentence from the well-known ICSID case of *Amco v. Indonesia*: “An international tribunal is not bound to follow the result of a national court.” As the Claimants argue persuasively, it would be unfortunate if potential claimants under NAFTA were dissuaded from seeking relief under domestic law from national courts, because such actions might have the salutary effect of resolving the dispute without resorting to investor-state arbitration under NAFTA.<sup>235</sup>

Moreover, there is no exhaustion requirement under NAFTA. As noted above in Section III.B.1.b, the Treaty claims brought by Claimant here should be resolved independently of any domestic proceeding.

143. Mexico also argues that “the municipal legal system determines whether or not the expropriation has been definitively consummated”<sup>236</sup> and that “[i]f the federal courts declare the decree illegal, then expropriation in the sense of Article 1110 will not have occurred.”<sup>237</sup> This is simply wrong as a matter of Treaty law. Whether there has been an expropriation under Article 1110 does not depend on Mexican law but on the Treaty. As Article 1131 makes clear, the governing law here is “this Agreement [NAFTA] and applicable rules of international law.”

144. Mexico also argues that “the municipal legal system establishes the legally protected property rights.”<sup>238</sup> This, too, is wrong. It is the Treaty that defines the legally protected rights. Specifically, Article 1110 protects the “investment of an investor”. Article 1139 defines “investment” and specifically includes within that definition the following:

(b) an equity security of an enterprise;

(e) an interest in an enterprise that entitles the owner to share in income or profits of the enterprise;

---

<sup>235</sup> *Azinian v. Mexico*, ICSID No. ARB(AF)/97/2, Award, para. 86 (November 1, 1999) (Exh. C-148).

<sup>236</sup> Statement of Defense, para. 209.

<sup>237</sup> *Id.*, para. 210.

<sup>238</sup> *Id.*, para. 209.

(f) an interest in an enterprise that entitles the owner to a share in the assets of that enterprise on dissolution, other than a debt security or a loan...

GAMI's 14.18 percent interest in GAM's mills falls within the definition of "investment" and is therefore protected from expropriation under NAFTA.

145. In addition, Mexico erroneously argues that GAMI's claim is untimely, apparently because Mexico thinks that GAMI should wait to see what compensation, if any, Mexico may one day offer GAM under Mexican law.<sup>239</sup> NAFTA imposes no requirement to wait for an offer under local law. NAFTA sets out all relevant timeframes for a Treaty claim, and, unlike Mexico, GAMI has complied with them.

146. It is well-settled in international law that a State may not avoid liability for compensation by showing that its actions were carried out pursuant to or in accordance with its own laws.<sup>240</sup> Given this universally-accepted principle, it is incongruous to argue, as Mexico does here, that a claim under international law is barred because a local tribunal may in the future conclude that the act complained of is illegal under local law. Mexico cannot elude its international obligation to pay GAMI compensation for the 14.18 percent interest that was indirectly expropriated simply because several years later its expropriatory actions may be deemed illegal under domestic law by its domestic courts.<sup>241</sup>

---

<sup>239</sup> *Id.*, para. 214.

<sup>240</sup> The Iran-U.S. Claims Tribunal confirmed this in *Birnbaum v. Iran*, Award No. 549-967-2, para. 35 (6 July 1993) (Exh. C-157):

The Respondent's reasons and concerns for taking control of [the company] cannot relieve it from responsibility to compensate the Claimant for the taking . . . Moreover, a Government cannot avoid liability for compensation by showing that its actions were taken legitimately pursuant to its own laws.

<sup>241</sup> President Paulsson aptly pointed out this issue at the hearing, stating that:

147. Mexico also quotes extensively from the hearing transcript regarding discussions of the return of GAM's mills under the domestic proceedings and the effect this might have on any potential award to GAMI under the Treaty.<sup>242</sup> GAMI seeks the compensation due it under NAFTA, not Mexican law. If this Tribunal awards compensation for the expropriation of GAMI's shares, Mexico will be entitled to those shares upon payment of the compensation. If Mexican courts awarded restitution or compensation to GAM prior to the Tribunal's award and that action does not make GAMI whole for the breaches of NAFTA, then the Tribunal should award GAMI the difference.<sup>243</sup>

**7. GAM's Entry Into Suspensión De Pagos Does Not Negate GAMI's Claim To Compensation Or Violate The Rights Of Creditors**

148. Mexico argues that “[c]ompensation for expropriation of the shares of the corporations that owned the mills is owed to GAM, not to its shareholders.”<sup>244</sup> Mexico then claims that even if GAM were provided compensation, “GAM cannot freely dispose of the compensation, for the same reason it cannot dispose of the rest of its assets as long as the state of *suspensión de pagos*

---

Since you invited us to ask questions at any time, with respect to your submissions about the conceivable effect of the pending court actions in Mexico, and you said that the circumstances are such that if the complaints about the expropriation measures succeed ultimately before the Mexican court — I think at one point you went so far as to say “no hai expropiacion” [ph] — couldn't it be said against you that it is an unattractive paradox to find that the liability under NAFTA of the Government depends on the alacrity of the victim of an unlawful expropriation in the sense that the Government benefits if the victim is more energetic than if the victim is passive?

English Transcript (Min-u-Script) of the Jurisdictional Hearing, p. 39-40.

<sup>242</sup> Statement of Defense, paras. 211-213.

<sup>243</sup> As noted, if the Tribunal makes its award first, Mexico will be entitled to GAMI's shares, thus also avoiding double compensation.

<sup>244</sup> Statement of Defense, para. 220.

persists.”<sup>245</sup> These arguments are not relevant to the issues of GAMI’s rights for the expropriation of GAMI’s interests under Article 1110. At best, they are jurisdictional arguments that the Tribunal already rejected preliminarily.

149. Mexico also professes concern for the rights of creditors of GAM in any compensation GAMI might be awarded. Mexico’s argument is based upon a mischaracterization of GAMI’s claim. GAMI seeks compensation not for the value of GAM’s assets, but rather for the value of its 14.18 percent shareholder interest in GAM. GAMI seeks compensation for the value of those shares in accordance with Article 1110 and international law.

150. Mexico in effect takes the position that GAMI is owed nothing because of the degree of GAM’s debt. Having operated its sugar program in a manner that did not support the industry but rather was driving it into crisis, Mexico now claims it owes no compensation because the mills it seized were so indebted.

151. GAMI’s claim to compensation is based on a conservative valuation of the mills had Mexico simply carried out its sugar program. Navigant’s conservative calculations did not assume away debt, but rather calculated GAM’s value, including the ability to liquidate debt, had Mexico carried out its responsibilities.

152. Creditors and other shareholders will not be disadvantaged if GAMI is properly compensated, since nothing will come from the assets or revenues of GAM. GAM shareholders, including Mexico which will be a 14.18 percent owner, will be entitled to the full amount of compensation that Mexico determines under its law is owed to GAM. Creditors will have whatever rights they have to the full settlement to GAM under Mexican law.

**E. GAMI Did Not Assume The Risk That Mexico Would Breach Its Treaty Obligations**

153. Mexico cites various disclosures that GAM made in filings with securities regulators in support of its argument that the risks of investing in the Mexican sugar industry were well-

---

<sup>245</sup> Statement of Defense, para. 220.

known and that GAMI assumed those risks when it invested in GAM.<sup>246</sup> No provision of NAFTA or international law, however, holds that a State may invoke disclosure by an issuer of securities of certain risks as a bar to a claim for damages on account of the State's failure to comply with an investment treaty. GAM's disclosures do not excuse Mexico's repeated and systematic breach of its obligations under NAFTA.

154. The fallacy of Mexico's argument is clear when the purposes of risk disclosure requirements are considered. The rationale behind securities disclosure requirements is to highlight for potential investors risk factors that may be associated with an investment in an issuer's securities. The enactment of securities laws in the United States in the 1930s began a trend away from strict adherence to the harsh doctrine of *caveat emptor* and toward a more regulated and comprehensive duty to disclose.<sup>247</sup> Risk factor disclosure Sections are now incorporated in virtually all equity and debt offerings.

155. Standard practice among issuers is to craft broad disclosures. Indeed, most issuers often include at least one or two broadly-worded risk factors which cover almost anything that could conceivably go wrong with an investment.<sup>248</sup> All of GAM's Form F-20 Annual Reports filed with the United States Securities and Exchange Commission contain one such catch-all disclosure that covers essentially any actions on the part of Mexico. This disclosure reads:

Mexican Government actions concerning the economy could have significant adverse effects on private sector entities in general and on the Company in particular. The Company cannot provide

---

<sup>246</sup> Statement of Defense, paras. 190-195.

<sup>247</sup> See Securities Act of 1933, 15 U.S.C. § § 77a et seq. (2003); see also *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963) (Exh. C-158) (noting that in enacting the securities statutes Congress sought to “substitute a philosophy of full disclosure for the philosophy of *caveat emptor* and thus to achieve a higher standard of business ethics in the securities industry”); *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 151 (1972) (Exh. C-159) (same).

<sup>248</sup> See Alan K. Austin, et al., *Risk Factors Disclosure and the Private Securities Litigation Reform Act*, 1392 PLI/Corp 751, 763 (October 2003) (Exh. C-160).

assurance that the future economic, political or diplomatic developments in or affecting Mexico over which the Company has no control will not impair the Company's business, results of operations, financial condition, liquidity (including the ability to obtain financing) or prospects, or adversely affect the market price of the Company's securities (including the Notes) or the ability of the Company to meet its obligations.<sup>249</sup>

156. Under Mexico's logic, Mexico could essentially have done anything it desired to GAMI's investment in the sugar mills and simply claimed that since GAMI was aware of and assumed the risks within the catch-all disclosure it should be foreclosed from pursuing any damages. Mexico cites no authority whatsoever for its novel assertion.

157. Disclosures are meant to put potential investors on notice of various risks and to provide the issuer with a defense to any claim against them that the risks of the investment were not disclosed or were misrepresented. The benefits of these disclosures run only to the investor and to the issuer. All disclosures of risk factors to investors were made by GAM, not Mexico. Mexico thus has no standing to assert the existence of these disclosures as a bar to its own liability under NAFTA.

158. Of course, the specific risk of expropriation by Mexico was never disclosed in any of GAM's prospectuses, registration statements or annual reports, but even if it had been this would not have foreclosed GAMI from seeking compensation for Mexico's unlawful conduct under the NAFTA. Even under securities law, upon the occurrence of any disclosed risk, investors may pursue all available remedies, except for a claim against the issuer for non-disclosure. Thus, GAM's disclosure of various risks including risk of behavior that also could violate NAFTA, does not remove Mexico of its liability for breach of any NAFTA obligation.

---

<sup>249</sup> GAM's Form F-20 Annual Report December 31, 2000, p. 15 (SOD Exh. R-57).

#### IV. VALUATION

##### A. Legal Principles Relating to Valuation and Calculation of Damages

159. Mexico affirmatively declines to present to the Tribunal any independent evidence regarding the valuation of the expropriated property.<sup>250</sup> The only proper expert opinion on valuation properly before the Tribunal therefore is the report of Navigant Consulting, GAMI's expert, that the fair market value of GAMI's interest in GAM on September 2, 2001, was not less than US\$27.8 million. Mexico's Statement of Defense, and the accompanying report of FGA, offer only a critique of the Navigant valuation, but no independent evidence of the proper value of GAMI's shares. We demonstrate below that Mexico's criticisms are legally and factually erroneous. As discussed in the Expert Valuation Reply of Navigant Consulting, the FGA critique is rife with conclusory suppositions and basic mathematical errors, and relies on speculation rather than rigorous financial analysis and the proper exercise of professional judgment.

160. GAMI's discussion of damages in its Statement of Claim was brief because this is not a complicated case. No legal authority is necessary beyond the plain language of NAFTA Article 1110(2). There is no dispute that the expropriation deprived GAMI's investment of substantially all its value. Accordingly, the task for the Tribunal is no more complex than determining the fair market value of the investment.

161. The Tribunal need not reach the question of damages for breach of Articles 1102 and 1105 if it awards compensation for the expropriation as GAMI requests. But even if the Tribunal were to reach the issue of damages for Mexico's breach of Articles 1102 and 1105, the measure of those damages is the same as the calculation of fair market value under Article 1110.<sup>251</sup> The

---

<sup>250</sup> Statement of Defense, para. 320.

<sup>251</sup> Mexico's citation of the *Feldman* case makes this point clear. Statement of Defense, para. 293. In discussing the measure of damages for breach of Article 1102, the *Feldman* tribunal specifically noted that, "*In the absence of any discrimination that also constitutes an indirect expropriation or is equivalent to an expropriation, the claimant would not be entitled to the total market value of an investment granted under NAFTA Article 1110.*" (emphasis added.). Here, in

action and inaction of the Mexican Government, including the unlawful and discriminatory expropriation, reduced the value of GAMI's investment to zero. The difference between the fair market value at the time GAMI initiated its claim (zero) and the fair market value at the time of expropriation (US\$27.8 million) is an appropriate measure of damages. As an alternative, it would be appropriate to calculate damages under Articles 1102 and 1105 as the difference between the actual value of the investment today (zero) and the hypothetical value that the investment would have in today's market. The hypothetical value of the investment today would be substantially higher in light of the improvements in domestic prices that have occurred since the expropriation because Mexico, now having a direct financial interest in the matter, began enforcing the laws.<sup>252</sup> That amount, as set forth in the Navigant Expert Valuation Reply, is \$US 29.41 million.<sup>253</sup>

### **1. Navigant's Valuation Is Appropriate**

162. Mexico's primary argument with respect to valuation is that Navigant's adjustment to GAM's historical financial statements was improper as a matter of law. This assertion is incorrect. Navigant's adjustments controlled for the effect on GAM's cash flow of Mexico's arbitrary and unlawful administration of its sugar program. It is wholly appropriate under NAFTA and general principles of international law to adjust the valuation of an expropriated

---

contrast, we have discriminatory conduct that did amount to an expropriation, so the proper measure of damages is the total market value of the investment.

<sup>252</sup> For instance, Mexico has caused the 27 mills that it now owns to comply with their export obligations. *See Exportaciones Realizadas en el Ciclo 2001/2002* ("Sugar Exports 2001/2002") (Exh. C-161). Mexico has also provided for adjustment of the reference price. *See* Exh. C-152. In addition, domestic sugar prices (SNIIM) have increased approximately 18 percent between the 2000/2001 harvest and the 2002/2003 harvest. *See* Expert Valuation Reply of Navigant Consulting, p. 9 (Exh. Vol. V to GAMI's Reply to the Statement of Defense).

<sup>253</sup> Expert Valuation Reply of Navigant Consulting, para. 22 (Exh. Vol. V to GAMI's Reply to the Statement of Defense).

asset to account for the effect of the improper conduct.<sup>254</sup> Article 1110(2) expressly provides flexibility to allow for adjustments like this: “Valuation criteria shall include going concern value, asset value including declared tax value of tangible property, *and other criteria, as appropriate*, to determine fair market value.” Declining to make adjustments, as Mexico urges, would be grossly unfair. Mexico’s theory of valuation would allow a state to drive an investment into economic distress, expropriate that investment, pay little or no compensation to foreign investors (because of the Government-induced distress), then privatize the industry once it recovered and earn windfall profits.

163. It is not disputed that the value of GAMI’s investment was severely impaired prior to the expropriation on account of GAM’s liquidity crisis and the depressed price of sugar on the domestic market. But these circumstances were the result of Mexico’s unlawful and arbitrary administration of the Mexican sugar program, as demonstrated by the evidence GAMI has adduced.<sup>255</sup> By expropriating GAM’s mills, Mexico deprived GAMI of all possibility that the value of its investment would increase when the Government finally began enforcing the law and corrected the problems in the industry.<sup>256</sup> Investors in non-expropriated mills, in contrast, were able to retain this upside potential. The appropriate measure of damages must also compensate GAMI for the loss of the upside potential.

164. Mexico asserts that the Navigant adjustments are impermissible because there is no proof of a precise correlation between those adjustments and Mexico’s wrongful conduct. This

---

<sup>254</sup> See, e.g., *Metalclad v. Mexico*, para. 122 (Exh. C-79) (“[W]here the state has acted contrary to its obligations, any award to the claimant should, as far as possible, wipe out all the consequences of the illegal act and reestablish the situation which would in all probability have existed if that act had not been committed (the status quo ante).”).

<sup>255</sup> See Witness Statement of Juan Cortina, paras. 17-20 (Exh. C-18); see also Andrés Antonius González, *The Mexican Sugar Industry 1991-2001*, pp. 29-34 (Exh. C-19).

<sup>256</sup> As demonstrated in the expert witness statement of Darío Oscós, GAM’s commencement of suspension of payments largely resolved its liquidity crisis, allowing for the payment of post-filing debts and permitting the company to receive post-filing credits. Thus, GAM was well on its way to financial rehabilitation at the time of the expropriation.

misperceives the fundamental nature of valuation, which, in the absence of purely objective data such as market capitalization of an actively traded, publicly-held corporation, is a modeling process. The assumptions and predictions that underlie the Navigant valuation are well-articulated, rational, conservative, and based on the proper exercise of professional judgment.<sup>257</sup> Navigant did not, as Mexico asserts, assume an “ideal world for GAM,” but rather made conservative and appropriate assumptions based on the specific evidence proffered with GAMI’s Statement of Claim. Mexico offers no evidence to rebut the contention that, but for the Government’s failures, GAM would have achieved financial results commensurate with those predicted by Navigant.

165. Even if the Tribunal were to conclude that there is some doubt about the ability to quantify precisely the economic effect of Mexico’s misconduct on the value of GAMI’s investment, that does not mean no damages should be awarded. Rather, the appropriate course of action in that situation is to find another measure of damages. Navigant provided exactly such an alternative in its initial report – calculation of the investment value.<sup>258</sup> Thus, if the Tribunal finds that the use of adjusted cash flow is too speculative, it should award GAMI its investment value of US\$22,537,691.<sup>259</sup> The tribunal in *Metalclad* did just that in circumstances where it concluded that any calculation of future profits was too speculative.<sup>260</sup>

---

<sup>257</sup> By considering debt, Navigant’s valuation also addresses the issue of protecting GAM’s creditors.

<sup>258</sup> See Navigant Valuation Report, para. 50 (Exh. C-26).

<sup>259</sup> In criticizing Navigant’s calculation of the initial value of GAMI’s investment, Mexico fundamentally misperceives the entire purpose of the exercise. See Statement of Defense, paras. 307-310. The calculation of initial investment value obviates the need to attribute the decline in the value of the investment to any particular factor. Thus, if the Tribunal determines that the effect of Mexico’s misconduct on the value of the investment cannot be separated from the effect of the other factors noted by Mexico (weather, competition, world sugar prices, lack of an active market for GAM shares after commencement of suspension of payments, etc.), the appropriate thing to do is to award the investor its initial investment value.

<sup>260</sup> See *Metalclad*, para. 122 (citing cases) (Exh. C-79).

166. Mexico's other criticisms on the Navigant valuation are equally unpersuasive. Contrary to Mexico's assertions, GAM had more than enough history of operations in the sugar industry to permit valuation on a cash flow basis, having been formed in the mid-1990s.<sup>261</sup> GAMI made its investment in 1996 and GAM went public in 1997. The *Metalclad* case, which Mexico cites at paragraph 292 of its Statement of Defense for the proposition that only a company that has been profitable for two or three years can be valued on a cash flow basis, simply does not stand for that proposition and, in any event, is readily distinguishable. *Metalclad* was a case where the business in question, a landfill, had *never* operated. In contrast, GAM had a long history of well-established business relationships and operations.

167. Mexico's contentions regarding Navigant's use of the comparable transaction and comparable publicly-held company valuation methodologies are equally unpersuasive, based as they are on conclusory assertions rather than empirical data or professional judgment. Indeed, while criticizing Navigant's selection of comparable transactions and comparable public companies, Mexico offers no alternative comparables of its own. Accordingly, there is no evidence in the record that better comparables transactions exist and, as Navigant explains in its rebuttal report, in the exercise of its professional judgment the comparables transactions utilized were in fact the best available and were reasonable.

## **2. FGA's Methodologies Are Fatally Flawed**

168. Mexico has chosen not to put forth a valuation of its own on the ground that doing so might "prejudice" the calculation of compensation to be paid in Mexico under the Expropriation Decree. It is impossible to see how a calculation here could be prejudicial to Mexico's position in domestic proceedings; it either believes a valuation submitted to this Tribunal to be correct, in which case there would be no prejudice, or it has doubts about its correctness, in which case

---

<sup>261</sup> Moreover, GAM is the successor to *Corporacion Industrial Sucrum, S.A. de C.V.*, which was formed in June of 1990 by a group of investors led by Juan Gallardo Thurlow, the current majority shareholder of GAM. See L. R. Garcia Report, p.2 (SOD Exh. R-33).

Mexico should not present it in the first place. In any event, in the absence of a well-reasoned expert opinion on valuation Mexico asks the Tribunal to consider only the critique by FGA of the Navigant valuation.

169. The Navigant rebuttal report, submitted herewith, analyzes the FGA report in considerable detail, and we draw the Tribunal's attention to that document for a point-by-point analysis of FGA's flawed methodology and basic errors in calculation. We summarize below the most significant flaws in FGA's work.

- FGA improperly fails to recognize that a discounted cash flow analysis is predictive rather than reactive. Thus, Navigant's valuation properly is based on a prediction of GAM's forward cash flow on September 2, 2001.
- FGA's inclusion of historic losses in its discounted cash flow analysis has the effect of double counting these losses because they had already been incurred.
- FGA committed a series of computational errors in its analysis of GAM's earnings before interest, taxes, depreciation, and amortization (EBITDA).
- FGA offers no alternative comparable transactions or comparable publicly-traded companies in its analysis.
- FGA criticizes the market multiples selected by Navigant based on nothing more than the conclusory assertion that they are "outside the range acceptable for the Mexican market," yet offers absolutely no empirical data or even a published source to support this opinion.

170. FGA erroneously calculates a negative market value, a circumstance that cannot exist because an investor cannot lose more than the value of its initial investment. The absurdity of FGA's conclusion of a value of negative US\$676 million is amply demonstrated by the simple fact that GAM's outstanding debt at the time of expropriation was less than one-third of this amount. Thus, FGA assumes that, leaving aside debt, GAM had negative value – in other words, that its mills and other fixed assets had negative value – an absurdity.

## **V. CONCLUSION**

171. GAMI has established beyond any doubt that Mexico expropriated GAMI's investment and that compensation must be awarded under Article 1110. GAMI likewise has shown, through

overwhelming documentary evidence and the testimony of both industry representatives and *caneros*, that Mexico's implementation and enforcement of its sugar program was inequitable and discriminatory in violation of the minimum standard of treatment required by Article 1105 of NAFTA, as well as the national treatment requirement of Article 1102. Against overwhelming factual evidence and legal authority, Mexico's defense is founded on baseless efforts to shift the blame and obsolete legal theories that are overruled by NAFTA and discredited by modern authority.

172. Countries commit to investment protections such as those of the NAFTA for purposes of encouraging foreign investment. The benefits of NAFTA, however, come with concomitant responsibilities and obligations. By signing the treaty, Mexico committed itself to treat U.S. investors in accordance with specified minimum standards of conduct. Mexico has breached those commitments, the treaty requires compensation to the investor.

173. In this matter, the effect of Mexico's actions was to undermine the value of GAMI's investment and then expropriate it in its entirety. GAMI thought it was investing in a privatized sugar industry that could thrive under a strong sugar program. In reliance on Mexico's commitment to afford U.S. investors these basic, minimum protections, GAMI invested US\$30 million in GAM. That US\$30 million was used to pay down GAM's government debt, to improve the efficiency of its mills, and to pay the operating costs of the enterprise, the largest portion of which were payments to *caneros* for sugarcane. Having reaped the benefits of NAFTA, Mexico must now honor its commitment to pay compensation for its breaches.

174. Mexico offers no valuation evidence on the question of damages and cites no credible evidence or authority in support of its position that damages are zero. In contrast, GAMI has presented a valuation demonstrating that, but for Mexico's wrongful conduct that resulted in depressed domestic sugar prices and a liquidity crisis in the industry, GAMI's investment would have been worth US\$27.8 million at the time of expropriation. Rebuttal evidence submitted with this Reply shows that valuation was indeed conservative, and that higher valuations would be fully justified.

175. For the reasons set forth in the Statement of Claim and this Reply, the Tribunal should award GAMI compensation in an amount not less than US\$27.8 million, plus interest in accordance with Article 1110(4) and the costs of this arbitration.

Respectfully submitted,

---

Guillermo Aguilar Álvarez  
Lucía Ojeda  
Elsa Ortega  
Itziar Esparza

**SAI ABOGADOS**  
Edificio Plaza Reforma  
Prol. Paseo de la Reforma #600-103  
Mexico, D.F. 01210

---

Charles E. Roh, Jr.  
Adam P. Stochak  
J. Sloane Strickler  
Alicia Cate

**WEIL GOTSHAL & MANGES LLP**  
1501 K Street, N.W.  
Suite 100  
Washington, D.C. 20005

Attorneys for Investor  
*GAMI Investments, Inc.*

February 5, 2004