

COURTESY TRANSLATION*

**IN THE MATTER OF THE ARBITRAL PROCEEDING PURSUANT TO
CHAPTER ELEVEN OF THE NORTH AMERICAN FREE TRADE
AGREEMENT**

**INTERNATIONAL THUNDERBIRD
GAMING CORPORATION,
CLAIMANT**

v.

**UNITED MEXICAN STATES,
RESPONDENT**

STATEMENT OF REJOINDER

COUNSEL FOR THE UNITED MEXICAN STATES:

Hugo Perezcano Díaz

ASSISTED BY:

Secretaría de Economía

Alejandra Galaxia Treviño Solís

Luis Ramón Marín Barrera

Shaw Pittman LLP

Stephan E. Becker

Sanjay Mullick

Thomas & Partners

J. Christopher Thomas, Q.C.

J. Cameron Mowatt

Alejandro Barragán

* Translation is provided as a courtesy only. The Spanish Rejoinder is the only authentic version and prevails over the translation for all purposes.

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I. INTRODUCTION AND SUMMARY OF THE KEY FACTUAL AND LEGAL ISSUES

1. The Claimant's Reply is replete with heated rhetoric and caustic accusations. It also contends that the Respondent has not answered various of its claims, even though the Statement of Defense actually contained extensive evidence and submissions responding to those claims.

2. This tactic appears intended to mask the Claimant's own deficiencies and omissions with the purpose of distracting attention away from the central issues. The Claimant chose not to admit or deny the Respondent's allegations of fact, and failed to even comment on a number of crucial facts proven by the Respondent. Thunderbird also attempts to divert attention from the weakness of its case by presenting long, academic discussions of legal principles that are not pertinent to the facts of this dispute.

3. The Government of Mexico also notes in addition, that the Claimant has erred in translating the Spanish language of the Statement of Defense, and as a result, has mischaracterized several of the Respondent's arguments.¹ Also, on other occasions it has misinterpreted the Respondent's objections.

4. As will be addressed below, the Claimant has asserted certain new facts in the Reply, although some are supported only by witness statements prepared by individuals who have some connection with the Claimant, and others are not supported by any evidence whatsoever. In the Respondent's view, the Claimant's descriptions of the key facts lack probative value.

5. The parties have framed the issues in different ways and focused on different aspects of the facts, but the Claimant now apparently agrees with the Respondent that it is not this Tribunal's role to make its own independent judgment on whether the machines were prohibited gambling equipment under the *Ley Federal de Juegos y Sorteos*.² Rather, the Tribunal must decide whether Mexico's treatment of Entertainments de México S. de R.L. de C.V., Entertainments de México-Laredo, S. de R.L. de C.V. and Entertainments de México-Reynosa S. de R.L. de C.V. (collectively "Las Sociedades de EDM")—*i.e.*, the conduct of the Secretaria de Gobernacion (Gobernacion) — was inconsistent with its Chapter Eleven, Section A obligations.

¹ For example, the Claimant unfoundedly alleges that the Respondent argued that Thunderbird, "appears to have consciously followed a business strategy which is against the law". Reply at 21. But what the Respondent in fact argued in the Statement of Defense is that Thunderbird "consciously followed a business strategy that was on the margins of the law" ("conscientemente seguía una estrategia de negocios que está en los márgenes de la ley"). Statement of Defense at 39. .

² See Reply at 5 ("The Tribunal's role in these proceedings is clearly not to independently determine whether the EDM skill machines are in fact legal, or illegal, under Mexican law.") However, the Claimant seems to resile from this position when it says in the following sentence: "Nor is it's [sic] role to simply defer to Mexico in its determinations on that point" — which implies that the Claimant believes that the Tribunal could determine that the machines were legal under Mexican law. Clearly the machines have been found illegal under Mexican law, and the Tribunal lacks authority to change that determination. The only questions validly before the Tribunal are whether the manner in which that determination was reached and the judicial remedies available to EDM to challenge that determination constituted a violation of NAFTA Chapter Eleven.

6. Although there has been voluminous argument and documentary evidence offered in this proceeding, this case will turn on several very specific and relatively narrow questions, some of which are closely inter-related:

- Can the Claimant be considered to have relied on the 15 August 2000 Gobernacion letter as the basis for its investment when it entered into lease agreements and imported gaming machines prior to the letter's issuance; when it expressly advised investors in EDM that the letter was "no specific entitlement" for EDM's operations; when it reported to its own shareholders that it had relied on private sector advisers in making the investment; and asserted in U.S. court proceedings that it was fraudulently induced to enter this business by Messrs. Oien and Ong?
- Is the Gobernacion letter, which is in the form of a general advisory opinion and expressly states that it would be applicable only "if" the machines operate as represented by EDM in its request, an "approval" for the operation of specific machines not described by EDM to Gobernacion in its solicitude, given that EDM failed to present any evidence on the operation of the machines, and given that Gobernacion clearly and expressly made known to EDM the nature of the machines that are prohibited by law?
- Can it be considered arbitrary and irrational that Gobernacion would consider the machines to be prohibited games when the Claimant itself knew their nature, and knew of the existing risk that they would be inspected by Gobernacion and it would reach that conclusion?
- Were the administrative proceedings in which EDM's machines were found to be illegal arbitrary or unfair so as to violate any standard of international law, when the decision itself indicates that EDM's evidence was taken into account even when not in strict accordance with the applicable domestic legal requirements, and when the decision sets out a reasoned basis for its conclusions? Can the administrative proceedings carried out by Gobernacion be considered arbitrary or unfair so as to violate any applicable standard of international law, when the procedure was transparent and in compliance with Mexican laws, validated by EDM's lawyers who were experts in Mexican law, and given that had there been a violation during these proceedings, there were appropriate judicial remedies available to challenge it?
- Can the Claimant claim a substantive violation of the NAFTA if EDM abandoned the available judicial remedies, particularly when the NAFTA did not require such abandonment as a condition precedent prior to the submission of the Claimant's NAFTA claim?
- Can Gobernacion be deemed to have discriminated against EDM when it has closed every similar facility of which it has become aware, and defended its actions in every court appeal initiated by the operators of machines similar or identical to those of EDM?

Other issues have also been raised, and Mexico will deal with each in this Rejoinder.

7. The key legal points are as follows:

- Mexican authorities have not accorded EDM less favorable treatment than that accorded to Mexican companies in like circumstances; there has been no discriminatory treatment of EDM on the basis of the Claimant’s nationality (nor for any other reason) in violation of NAFTA Article 1102. Gobernacion has acted consistently in enforcing the law against all persons, including Mexican nationals, who have attempted to operate facilities with so-called “skill” machines. EDM is not in “like circumstances” with the persons that have been able to continue operating under temporary injunctive relief while the merits of appeals against Gobernacion’s actions are decided.
- Thunderbird has not made out a violation of the “minimum standard of treatment” under the customary international law standard encompassed in Article 1105: (i) its complaints about the Gobernacion administrative proceedings are factually invalid and in any event are issues of purely domestic law, and (ii) it has not presented any evidence of any failures of the Mexican judicial system that it argues prejudiced it and constituted the principal reason why it withdrew its judicial appeals.
- Thunderbird cannot succeed in its claim of expropriation because: (i) it failed to present its claim under Article 1116 of NAFTA, (ii) *bona fide* law enforcement actions by Gobernacion, such as the closure of illegal gambling operations, do not amount to an expropriation, and (iii) EDM filed appeals in the national courts which it subsequently withdrew.
- Thunderbird cannot present a claim on behalf of companies over which it does not have ownership or control.

8. Mexico emphasizes that it re-affirms all of the facts and legal arguments contained in its Statement of Defense, including those that are not repeated in this Rejoinder.

II. RESPONSE TO THE CLAIMANT’S FACTUAL PRESENTATION

A. The Weighing Of The Evidence Presented In This International Arbitration

9. In the Reply, Thunderbird incorrectly assumes that this Tribunal should apply the rules that govern the presentation of evidence in the United States, and asserts that its arguments should be accepted because it has offered a series of witness statements of its employees,

consultants and investors that must be given great weight, and that conversely, the Respondent's submission must be discounted because it is not supported with numerous witness statements.³

10. Mexico's arguments are supported by pertinent evidence, particularly contemporaneous documents. Messrs. Redfern and Hunter have explained why contemporaneous documents are preferred evidence in international arbitration:

In international commercial arbitration, the best evidence that can be presented in relation to any issue of fact is almost invariably contained in the documents which came into existence at the time of the events giving rise to the dispute. This contrasts with the presentation of evidence in the courts in the common law system, where most facts are proved by direct oral testimony, and even documentary evidence must in principle be introduced by a witness in oral evidence.

It is not difficult to appreciate why reliance on documentary evidence is favoured by international arbitral tribunals. Its presentation is easier and less time consuming; and, in an environment in which cross-examination is regarded as an unreliable method of testing the evidence of a witness, the evidentiary weight of documentary evidence is clearly more substantial than that of oral evidence which is not tested by an effective challenge, either through lack of expertise on the part of the opposing party's advocate or lack of time during the course of the hearings.

However, the best reason for the practice of international arbitration tribunals in relying primarily upon evidence contained in contemporary documents is that the application of the so-called "best evidence rule" applies primarily to the weight of the evidence rather than to its admissibility, and the evidence of contemporary documents will invariably be regarded as being of great weight.⁴

³ See, e.g., Reply at 1 ("[the Claimant's] case was supported by multiple, detailed declarations from the principal participants in the Thunderbird EDM investments"); *Id.* at 4 ("Numerous witnesses provided statements describing the arbitrary and discriminatory July 10, 2001 administrative hearing"); *Id.* ("Mexico presents no declaration testimony from Aguilar Coronado"); *Id.* at 9 ("In support of its SoD, Mexico submits only two witness statements"); *Id.* at 14 ("Peter Watson stated *under oath* as follows" [emphasis in original]).

It is axiomatic that international arbitration involves a melding of the civil and common law systems. Civil law procedures give primary importance to documentary evidence, while under common law procedures testimonial evidence can, in some circumstances, be given as much importance as documentary evidence. See Alan Redfern & Martin Hunter, Law and Practice of International Commercial Arbitration, (Sweet and Maxwell 2d ed. 1991) p. 67.

In international arbitration, of course, the tribunal has broad discretion to admit into the record a broad range of evidence, both documentary and testimonial. The fact that evidence is admissible, however, has no bearing on its weight. In particular, having multiple witnesses say the exact same thing does not, in and of itself, make the testimony more compelling. Sandifer, *Durward: Evidence Before International Tribunals. Revised Ed., University Press of Virginia*, 1975, p. 18 ("Sandifer").

⁴ Alan Redfern & Martin Hunter, Law and Practice of International Commercial Arbitration (2d ed. 1991), pp. 329-30. Cf. Studer v. Great Britain (U.S. v. U.K.), 6 R.I.A.A. 149, 152 (American and British Claims

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11. Durward Sandifer similarly wrote:

Tribunals may refuse to base an award on evidence taken long after the event, if uncorroborated by other evidence. On the other hand, the tribunal is free to attach great weight to contemporary evidence if it bears intrinsic indications of veracity, even though given by an interested party.⁵ [citations omitted]

12. Bin Cheng commented upon these issues as follows:

“Generally speaking, ... the mere *ex parte* statements of the facts by the interested party in a dispute are not considered as evidence and do not constitute sufficient proof of the facts alleged.

“Personal interest of the deponent and the uncontrolled character of his affirmation are, therefore, important considerations which generally deprive a claimant’s affidavit of much of its probative force.”

“‘Testimonial evidence’, it has been said, ‘due to the frailty of human contingencies is most liable to arouse mistrust.’ On the other hand, documentary evidence stating, recording, or sometimes even incorporating the facts at issue, written or executed either contemporaneously or shortly after the events in question by persons having direct knowledge thereof, and for purposes other than the presentation of a claim or the support of a contention in a suit, is ordinarily free from this distrust and considered of higher probative value.”⁶

[citations omitted]

13. Below the Respondent provides certain examples of the facts that illustrate why the Respondent believes that the evidence presented with the Statement of Defense must be preferred over the evidence of the Claimant.

1. Nature of the Machines

14. A remarkable aspect of this case is that the Claimant has chosen to support its arguments regarding the operation of the machines at issue in this dispute with ambiguous characterizations

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Arbitration Tribunal 1925) (“Where a case rests so largely upon *ex parte* statements prepared many years after the event by the party in interest, for the express purpose of presenting his claim in the best possible light, allowances must be made for infirmities of memory as well as for a claimant’s natural sense of grievance amounting sometimes to almost an obsession.”)

⁵ Sandifer, *op cit*, p. 18.

⁶ Cheng, Bin, General Principles of Law As Applied By International Courts And Tribunals (Cambridge Grotius Publishing, Ltd., 1987) pp. 309, 311 and 319..

(e.g. “skill machines”) based simply on witness statements; but it has not offered a precise description of the machines and their operation, and it has not presented the manuals, instructions, catalogs, photographs, etc., (just as EDM did not do so when it submitted the solicitude to Gobernacion)⁷. It bears noting that Support Consultants, Inc. (SCI) – that claims that like Thunderbird it was a manufacturer of many of the machines – also has not presented blueprints, guidelines, instructions, manuals, catalogues, photographs etc. of its products to demonstrate it manufactured the machines in question specifically for the Mexican market in accordance with instructions or specific criteria, or to demonstrate they were different from the machines described by the Respondent.

15. The Respondent, on the other hand, has presented the operating manuals for EDM’s machines found in the facilities in which they operated.⁸ The operating manuals indicate, among other things, that EDM could set the odds for winning and the level of payouts. Moreover, the Respondent has identified cases in which machines with the same manufacturer and name (Bestco “Fantasy Five”) or with similar so-called “skill stop” buttons were described in detail and held to be gambling equipment in legal proceedings in the United States.⁹ Mexico has also submitted corporate reports of the Claimant showing that Thunderbird itself manufactured machines with the exact same names as machines used by EDM (“Very Cherry Bonus” and “Red White and Blue 7s”), and that Thunderbird itself called them gambling games.¹⁰ The Respondent’s photographs of the EDM machines further indicate that they were not manufactured for the Mexican market as the Claimant now argues, but instead were originally created for English-speaking customers and that the outside containers were modified for use by Spanish-speaking customers – even to the extent that the original serial number and manufacturer nameplates were removed and replaced with nameplates with SCI’s name.¹¹

⁷ In the petition dated August 3, 2000, EDM limited itself to referring to the alleged manufacturer of the machines, but, for example, it failed to specify the operation of the machines (e.g., the fact that the machines relied on the insertion of U.S. dollars in order to function, the fact that users played to win points with a certain value that would allow the player to continue playing the machine or redeem them for cash), or the types of games (e.g., Eight-liner, Fantasy Five, Video Poker, etc.).

⁸ See Exhibits R-011, R-012, R-015, and R-016. These operating manuals were found in the offices of EDM Nuevo Laredo, in the presence of EDM’s legal representative Carlos Gomez Alvarez Tostado (who previously submitted a witness statement on behalf of the Claimant). Copies of the manuals, as well as all other documents retrieved from EDM’s offices, were given to Sr. Gomez.

⁹ Statement of Defense at Section IV.

¹⁰ Statement of Defense at Section VI.

¹¹ Exhibit R-001, 12th photograph. See also Exhibit R-011. The Claimant did include with its Statement of Claim a compact disc with several photographs of the machines at EDM Matamoros taken while the machines were turned on. Exhibit C-30. The Respondent has printed three of those photographs because, it can be seen that the machines display “reels” just like a traditional slot machine. Exhibit R-094. For purposes of comparison, included in Exhibit R-123 are brochures of slot machines with “touchscreens” downloaded from the website of a major U.S. manufacture of slot machines, International Gaming Technology. Although the International Gaming Technology machines are more sophisticated than those used by EDM, they are similar in that they require the customer to “interact” with the machine by pushing buttons or touching the screen, either to stop moving video images or to play

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16. Further, two of the operating manuals found at EDM are practically identical: one of them actually has SCI's name on the cover, although there are only cosmetic differences between this manual and a Thunderbird equipment manual ("4205 Gameboard Series Instructions") also found at EDM, suggesting that SCI simply put its own name on the outside of the machines previously manufactured by Thunderbird.¹²

17. Additional documents just produced by Thunderbird pursuant to Procedural Order 5 provide further evidence of the nature of the equipment. For example, on 26 May 2000, when Thunderbird moved ahead with the venture by signing a Letter of Intent with the ONG Group, the agreement stated the parties would work together to establish facilities in Mexico that would operate "'Skill Games' (commonly known as 'VLTs')," *i.e.*, video lottery terminals.¹³ Albert Atallah testifies that the machines operated by Thunderbird in California were VLTs.¹⁴

18. Thunderbird also consistently treated the venture as a project to place slot machines in Mexico. For example, an 8 May 2000 email from Peter Watson to "Mauricio" (Girault) states as follows:

Dear Mauricio,

*Jack called me on Saturday, May 6th, to tell me about a potential opportunity for gaming in Mexico. An acquaintance of Jack's, Mr. Ivy Ong has acquired, through an Amparo, the right to operate four slot machine operations in Mexico!*¹⁵

[emphasis in original]

19. Moreover, the newly-produced documents make clear that the basis of the Revenue Sharing and Consulting Agreement between Juegos de Mexico, Inc. (JDMI) and A-1 Financial (Messrs. Oien's and Ong's company), entered into on 22 June 2000, was the sharing of the "Net Win" generated from the operation of the machines.¹⁶ The agreement even stated the parties

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video poker. International Gaming Technology presents these machines as games of chance and betting, and at no time refers to them as machines of skill and ability ("*habilidad y destreza.*")

¹² Exhibit R-011 and R-016.

¹³ Exhibit R-096. See also "Thunderbird Internal Control Minimum Standards." Exhibit R-097.

¹⁴ See Witness Statement of Albert Atallah. Exhibit C-V

¹⁵ Exhibit R-095.

¹⁶ The "Net Win" was defined as:

"Net Win" shall be defined as gross receipts from the operation of the Skill Video machines, less: (i) all amounts paid out to Skill Video Machine patrons in the form of winnings, and (ii) all existing and future enacted gaming taxes less (iii) a reserve for a change in progressives (if any) plus (iv) the amount of any

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would work together to develop a “casino.”¹⁷ The concept of a “net win” only makes sense in the context of an operation where the “payout” is expected.¹⁸

20. In Las Vegas, where games of chance and betting is allowed, and where traditional slot machines are used, the state requires that the machines generally pay out at least 75% of the money inserted into them.¹⁹ Data for 2002 shows that actual payouts were anywhere between 86% and 93%.²⁰ According to EDM’s own records, in 2000, its machines in Matamoros paid out, on a monthly basis, within a range of 65% to 73%.²¹ In other words, the chances of winning on a slot machine in Las Vegas were much greater than at one of EDM’s machines.

21. The response offered by the Claimant to the overwhelming photographic and documentary evidence provided by Mexico —most of it of the Claimant’s own making— has been to argue that the Respondent has not proven that the manuals found at EDM were actually for the machines it was using,²² and that the Respondent has not proven that games with identical names are actually similar.²³

22. The objective evidence —documents and photographs— provided by the Respondent, in contrast with the weak testimony, unsupported by any contemporaneous documentary or physical evidence, should compel the Tribunal to find that the EDM machines are similar or

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progressive jackpot when it is discontinued without being paid out. Not less than weekly, the Net Win account for each Skill Video Machines location shall be distributed as follows [between JDMI and A-1].

Revenue Share and Consulting Agreement Between Juegos de Mexico, Inc. and A-1 Financial International, Ltd., Article 6.2, 22 June 2000. Exhibit R-098.

¹⁷ Id., Article 7.6. Exhibit R-098.

¹⁸ The “Capital Equipment Budget” for EDM-Nuevo Laredo includes a “Slots Department,” which includes “Slot Machines” as Equipment, and its Consolidated Projected Cash Flows chart lists the “Net Win net of Allocation and Gaming Taxes” as being calculated by subtracting the “Net Win” by (i) the “Oien Group Allocation;” (ii) “IVA [value added tax];” and (iii) “Device Fee – Slot Machines.” Exhibit R-099, pp. 3 and 20.

¹⁹ Regulations of the Nevada Gaming Commission and State Gaming Control Board § 14.040. Exhibit R-100.

²⁰ Jeff Simpson, Turning ‘em Loose: Slot Payout Rankings Deal Casinos New Marketing Card, Las Vegas Review Journal, May 19, 2002, available at http://www.reviewjournal.com/lvrj_home/2002/May-19-Sun-2002/business/18686053.html (accessed March 12, 2004). Exhibit R-101.

²¹ Exhibit C-28.

²² Reply at 35 (“the argument is based upon the same faulty premise addressed above – that machines described in old Thunderbird manuals are the same machines operated at the EDM facilities. There is no evidence supporting that premise.”)

²³ Id. at 33 (“there is no evidence offered to support the assertion that the “eight-liner” game addressed in the Texas cases operated the same as, or even in a fashion similar to, the eight-line games operated at the EDM facilities”).

identical to machines that were held to be gambling equipment in U.S. legal proceedings, and previously described as gambling equipment by Thunderbird itself.

23. This evidence is pertinent to the issues of (i) whether Gobernacion could be deemed to have acted arbitrarily at international law in finding that such machines were prohibited equipment under Mexican law, after having concluded by means of a specifically regulated administrative procedure, subject to judicial review, that the machines were games of chance and betting; and (ii) whether Thunderbird could have had a reasonable expectation that Gobernacion would agree that the machines operated by EDM were not illegal gaming machines, when in its August 3, 2000 *solicitud* to Gobernacion, EDM failed to provide a detailed description of the operations of its facilities or of the manner in which the machines functioned failing to submit, for example, the operating manuals, or providing a description of the machines, of the manner in which it intended to obtain earnings, or of the alleged differences with the operations of typical slot machines, particularly when it knew that the operation in Mexico of “skill machines substantially similar, if not identical”²⁴ had been the source of “significant legal altercation with Gobernacion.”²⁵

2. Origin of EDM Machines: Used Or Manufactured For EDM

24. The following is an excerpt from the 2 February 2004 witness statement of Kevin McDonald submitted by the Claimant:

The games that were sold to the EDM operations either by SCI, Bestco or Summit were all games that were created for the Mexico market following Thunderbird’s submittal of its petition to Gobernacion and Gobernacion’s August 15, 2000 reply.²⁶

[emphasis added]

Mr. McDonald’s assertion must be compared to the following excerpt from EDM’s August 3, 2000 letter to Gobernacion:

The video game machines for games of skill and ability which we operate, at this present time at the place indicated above on this writings, are trademark Bestco, model MTL19U-8L and S.C.I. model 17”UR; and the entity I represent is trying to place about 2,000 (two thousand) more machines at other locations in the Republic of Mexico and these

²⁴ Statement of Claim, p. 53: “There is no doubt that Guardia is operating skill machines substantially similar, if not identical to, the machines operated by the now-closed Thunderbird EDM enterprises...”

²⁵ Id., p. 4.

²⁶ Witness Statement of Kevin McDonald. Exhibit C-HH.

machines are of the same identical mechanical nature and functioning as those described in point 3, above.²⁷

[emphasis added]

Mr. McDonald's statement contrasts with the following excerpt from the 5 October 2001 comments by Mauricio Girault Esteva (an investor in EDM) to Jack Mitchell commenting on operations of the "Competition" in Matamoros:

The machines are identical as ours (Steve told me they are surplus from Carolina, given very cheap to Don Bradley).²⁸

[emphasis added]

Similarly, the McDonald statement contrasts with this excerpt from a statement to Thunderbird shareholders issued by Mr. Mitchell after the Gobernacion closures:

The Company also wrote off \$209,000 in gaming equipment that was intended to be refurbished for the Mexican market.²⁹

25. The contemporaneous evidence contradicts Mr. McDonald's new assertions in this proceeding. The Respondent maintains that the Tribunal should prefer the weight of the contemporaneous documentary evidence.

3. Gobernacion's Administrative Determination

26. The Claimant persists in disregarding the content of the ruling issued by Gobernacion, which declares the illegality of EDM's machines. Instead, Thunderbird chooses to focus on complaints of its witnesses, recently prepared for the purpose of this proceeding, in reference to alleged irregularities committed during the administrative procedure, particularly during the administrative hearing carried out in July 2001.³⁰ It is well established that the best evidence of

²⁷ "The video game machines for games of skill and ability which we operate, at this present time at the place indicated above on this writings, are trademark Bestco, model MTL19U-8L and S.C.I. model 17"UR; and the entity I represent is trying to place about 2,000 (two thousand) more machines at other locations in the Republic of Mexico and these machines are of the same identical mechanical nature and functioning as those described in point 3, above."

In "Point 3" EDM states:

"In these games, chance and wagering or betting is not involved, but the skills and abilities of the user who has to align different symbols on the machines screen by touching the screen or pushing buttons in order to stop the wanted from several other symbols which spin in a sequential manner" [Emphasis added] See Exhibit C-17

²⁸ Exhibit R-102. See Statement of Defense p. 38, quoting from Thunderbird's corporate disclosures that it was withdrawing from its business in South Carolina due to threatened enforcement action.

²⁹ Exhibit R-057.

³⁰ Reply at 14-15.

judicial or administrative proceedings is the record of those proceedings, as well as the authority’s ruling.³¹

27. In this case the record is Gobernacion’s formal determination dated October 10 in which it set forth its analysis and findings —the determination explains in detail the considerations that went into the weighing of the evidence presented in the hearing, as well as the legal grounds on which the determination is based.

28. For example, the Claimant says that a witness statement prepared by Kevin McDonald was disregarded by Gobernacion because of a faulty notarization, and that an “expert” report prepared by Netcomm Systems & Communications was “rejected” only because Netcomm is a private company.³² However, the Claimant fails to refer the Tribunal to Gobernacion’s detailed evaluation of this evidence:

Notwithstanding the foregoing, there is an additional element which removes any remaining probatory value from the said documents, as it is a fact that they do not just retain some similarity, but rather are completely identical in the terms used, a situation that generates suspicion, and from which arises their dismissal.

To corroborate the foregoing, it is sufficient to refer to what was said in each one of these documents.

Expert testimony provided at the request of the Attorney General of the Republic prepared by personnel of a private company called NetComm Systems and Telecommunications	“Declaration by Mr. Kevin McDonald, President of Support Consultants Inc., manufacturers of, among other things, machines of ability and skill.”
These machines have (sic) the following (sic) hard/electronic parts: external case, monitor, glass, panel of buttons, ‘login board’ (card or logic board), cabling, printer, electricity supply and miscellaneous components. The user interacts with action of the machines by means of the use of buttons located on the panel of the machine. Touching the buttons sends signals to the logic board, which is completely dead, that is to say inactive until the user starts the process and sends signals to the logic board. The user presses the first button, and the machine is thereby activated. The user has between 3 and 5 buttons, depending on the game, to communicate with the machine by means of the ‘logic board’ (card or logic board); and this communication will determine the results of the game. The working of the game depends upon the orders of the	SCI produces, distributes and services various machines of skill. These machines have the following hard parts or hardware: external case, monitor, glass, panel of buttons, electronic board ‘logic board’, cabling, printer, an opening to receive notes, electricity supply and miscellaneous components which are more fully described in the List of Components. The user interacts with action of the machine by means of the use of buttons located on the panel of the machine. Touching the buttons sends signals to the logic board, which is completely dead, that is to say inactive, until the player starts the process and sends signals to the logic board. The player presses the first button, and the machine is there by activated. The user has between 3 and 5 buttons, depending on the game, to communicate with the machine by means of the ‘logic board’; and this

³¹ Sandifer, op. cit at 202-209.

³² See Reply, p. 7 fn. 5 (“That [Netcomm] report, obtained by an agency of the Mexican government itself, was summarily rejected as evidence”); and Statement of Claim p. 93.

<p>user, since the 'logic board' (card or logic board) is 'slave' to the user. When the user presses a button to print the ticket which indicates the prize or incentive, the interaction of the customer with the machine ends.</p>	<p>communication will determine the results of the game. The working of the game depends upon the orders of the user, since the logic board is 'slave' to the user. When the user presses a button to print the ticket which indicates the prize or incentive, the interaction of the customer with the machine ends."</p>
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According to what can be seen in the transcription, not only are the texts identical, when **compared** one with the other, since the clear intention also existed to perfect them, but while in the translated document the word "player" had appeared repeatedly, in the Expert Testimony, only the said word was changed to the of "user". Except for this question of form, the basis is identical.

From this basis flows the rejection of such documents, and this determination is supported by the Jurisprudence Thesis VI. 1.J/26, contained on page 668 of the Judicial Federation Weekly, Volume VI, Second Part-2, July to December, Eighth Session, Joint Circuit Tribunals, which states:

“SUSPICIOUS WITNESSES, THOSE WHICH USE IDENTICAL TERMS. If during their declarations, witnesses use almost the same terms, this provides the basis for suspicion that the witnesses may have been prepared; and if it is found that the evidence is uniform, this refers to the substance and the facts about which they are giving evidence, rather than the terminology used in the declarations.”

This is also covered in the Jurisprudence Thesis 1073, which is published on page 742 of the Appendix of 1995, Volume VI, Part TCC, Joint Circuit Tribunals, Eighth Session, which states:

SUSPICIOUS WITNESSES, THOSE THAT USE IDENTICAL TERMS. If during their declarations, witnesses use almost the same terms, this provides the basis for suspicion that the witnesses may have been prepared; and if it is found that the evidence is uniform this refers to the substance and the facts about which are giving evidence, rather than the terminology used in the declaration.

Finally, the consideration of this authority is supported by the Thesis in section 548 of the Judicial Federation Weekly, Volume IV, Second Part-1, July to December, 1989, Eighth Session, Joint Circuit Tribunals, which states:

“PREPARED TESTIMONIES, IF ALMOST IDENTICAL TERMS ARE USED AND ARE CONTRADICTED BY OTHER EVIDENCE. Declarations of those who testify in criminal proceedings, must be validated by the jurisdictional entity attending to the rules contained in the code relevant to the subject matter, and as such, if any contradiction is encountered in

any other proofs collected during the proceedings, and furthermore that the witnesses use almost identical terminology, that is sufficient to consider that the witnesses have been prepared; consequently, they cannot have any probatory value.”

TWELFTH: Having concluded the rejection of the documents relating to the above points of consideration, analysis commences of the rest of the documents alleged by the company to whom the present administrative procedure is directed.

29. The Respondent invites the Tribunal to read the administrative ruling dated 10 October 2001, which is part of the record of this arbitral proceeding³³. In the Respondent’s view, the determination speaks for itself.

30. The Claimant also minimizes the fact that the conduct of the administrative proceeding and ruling by Gobernacion were subject to judicial review before the federal courts, and, in fact, that EDM filed appeals available to it under domestic law. Specifically, EDM filed for nullification (*juicio de nulidad*) of Gobernacion’s ruling, which it lost, appealed, and finally withdrew.

4. Purported Reliance By Thunderbird on the 15 August 2000 Letter Issued by Gobernacion

31. The Claimant admits in its Statement of Claim that it undertook the following actions, all before 15 August 2000: (i) opened bank accounts; (ii) obtained local permits, such as for land use; and (iii) imported machines.³⁴ In fact, in its August 3, 2000 *solicitud* EDM stated to Gobernacion: “Las maquinas de video para juegos de habilidad y destreza que operamos actualmente en el local mencionado en este escrito...” (emphasis added).³⁵ However, Thunderbird now alleges in the Statement of Reply that it is false that EDM-Matamoros was already operating prior to Gobernacion’s August 15, 2000 letter.³⁶ It is Thunderbird’s own representations and EDM’s own documents –provided by the Claimant as exhibits— that contradict the allegations it now presents in the Statement of Reply, arguing that it invested in Mexico based on reasonable reliance on the August 15 letter from Gobernacion.

32. Thunderbird commits four pages of its Reply to the question of its “reasonable reliance” on Gobernacion’s 15 August 2000 letter.³⁷ It is evident that Gobernacion’s letter was a response to the petition presented by Juan José Menendez Tlacatelpa, the prior owner of EDM. Juegos de

³³ See Exhibit R-093 (which contains the Claimant’s English translation of the ruling).

³⁴ Statement of Claim, p. 7, cited by Respondent in the Statement of Defense at p. 50.

³⁵ Exhibit C-17.

³⁶ Reply at 18.

³⁷ Reply at 36-39.

México, Inc. acquired EDM's shares on 10 August 2000, after the petition had been presented. Even supposing that Thunderbird acquired EDM afterwards—which the Respondent does not admit—it cannot be said that Thunderbird acted in reasonable reliance on Gobernacion's letter, in light of the fact that the letter was not addressed to Thunderbird, nor to any subsidiary or any person involved with Thunderbird at the time.³⁸

5. Statements made by Thunderbird to its Investors

33. Actions taken by the Claimant and EDM after 15 August 2000 also contradict the claim of reliance on the Gobernacion letter. Gobernacion's letter plainly stated that “the Ley Federal de Juegos y Sorteos establishes with precision diverse dispositions that strictly prohibit games of chance and game of betting within the Mexican territory”, and that “the law is conclusive in forbidding that ‘there shall not be established any house, open or closed space in which gambling is carried out, or any other gaming activity, without express authorization from Gobernacion’” (emphasis added). Gobernacion clearly warned EDM “that the machines it operates may not involve elements of chance or betting” (emphasis added).³⁹ In contrast, the 20 June 2001 EDM-Matamoros Subscription and Investment Representation Agreement stated:

Currently, “slot machines” are not permitted in Mexico primarily because they are viewed as gaming and betting machines which are games of chance requiring no skill. If the game requires some degree of skill by the user, generally it will not be deemed a prohibited slot machine in Mexico. Through the Franchise Agreement with EDM, the Company will operate video game “skill machines” which require some degree of the user's ability and skillfulness to obtain a prize.⁴⁰

[Emphasis added]

34. Thus, the Subscription Agreement's description of the Mexican law was inconsistent with that of Gobernacion. In contrast with the text of the law and the Gobernacion opinion, which “strictly” and “conclusively” prohibit games of chance and games with betting, and even more the express warning that the games “may not involve elements of chance or betting”, the Subscription Agreement claimed that “if the game requires some level of skill by the user, generally it will not be deemed a prohibited slot machine.” Even more, the Subscription Agreement also suggests that games that involve any degree of skill are exempt from the requirement that there be no element of betting, which also conflicts with the Gobernacion opinion.

35. This characterization of Mexican law was not an incidental error by the Claimant. In his witness statement, Albert Atallah stated:

³⁸ The letter from Gobernacion is directed to Juan José Menéndez Tlacatelpa.

³⁹ Exhibit C-18.

⁴⁰ Exhibit C-28, section 3(b)(viii).

As a part of Thunderbird's due diligence into the potential skill game operations in Mexico, I became familiar with Mexico's gaming laws. My understanding was and still is that the law of Mexico permits an entertainment and gaming activity in which the player has some interaction with the machine, and can affect the outcome or the result of the play, i.e., a skill game.⁴¹

Moreover, even if it could somehow be "understood" that the Mexican law allows for games with a "some level of skill," or in which "the player has some interaction with the machine" — which is not admitted by the Respondent— EDM simply ignored that the law also strictly forbids betting games.

36. It is obvious that Thunderbird presented an erroneous characterization of the *Ley Federal de Juegos y Sorteos* and Gobernacion's letter to induce third parties to invest in EDM. Thus, it is not possible to attribute responsibility for this to Mexico.

6. Evidence on Thunderbird's Reliance on the Representations of Srs. Oien, Ong, Aspe and Arroyo

37. The evidence demonstrates that, to the extent Thunderbird itself relied on any other party in deciding to invest, that reliance was on the advice of its own business associates: namely, Messrs. Oien and Ong (of A-1 Financial) and Messrs. Aspe and Arroyo. In section VI.B of the Statement of Defense, the Respondent reviewed Thunderbird's statements, in which it indicated it had relied on representations made by Messrs. Oien and Ong. In filings with a U.S. court, and in a corporate disclosure statement provided in compliance with the *Ontario Securities Act*, the Claimant accused A-1 (and therefore, Messrs. Oien and Ong) of making statements that induced "Thunderbird and its investor group [to invest] well over \$6,000,000 in cash and \$2,000,000 in capital equipment" and to open three facilities in Mexico. Thunderbird also made known its intention to counterclaim for amounts paid to A-1 and "for damages arising from fraud and intentional misrepresentation", among other things.⁴² In its Reply, the Claimant disavows these as mere "posturing" statements⁴³, having resisted the Respondent's request for documents concerning the allegation, arguing that they were "irrelevant" to this proceeding.⁴⁴ The documents finally provided by the Claimant by order of the Tribunal leave no doubt that the

⁴¹ Exhibit C-E, ¶ 13.

⁴² See Exhibit R-019 and Exhibit R-120, pp. 16-17. Section 122(1) of the *Ontario Securities Act*, R.S.O. 1990 C-S5, provides that the making of a statement in any report or other document required to be filed or furnished under Ontario securities law that, in a material respect and at the time and in the light of the circumstances under which it is made, is misleading or untrue or does not state a fact that is required to be stated or that is necessary to make the statement not misleading, is an offense punishable by a fine of up to \$5 million and/or a term of imprisonment of up to five years less a day.

⁴³ Reply at 40.

⁴⁴ Letter from James D. Crosby to the Respondent dated 22 September 2003. Letter from James D. Crosby to the Tribunal dated 5 December 2003.

relationship between Thunderbird and Messrs. Oien and Ong is relevant: it disproves the Claimant's claim that it relied on Gobernación to carry out its investment in Mexico.⁴⁵

38. Specifically, on 26 May 2000, Thunderbird and Messrs. Oien and Ong (acting as the "ONG Group") entered into a "Letter of Intent," to collaborate in establishing gaming facilities in Mexico. Thunderbird's principal responsibility was (i) to form "Mexican Operating Companies ("MOCs") to operate "Skill Games" (which the Letter described as being "commonly known as VLTs"), and (ii) to supply up to 2000 VLTs. Messrs. Oien and Ong committed themselves to provide the following consultations:

3. *Obligations of ONG Group. The ONG Group shall be responsible for the following services to promote the business of the MOCs:*

(a) *consultation concerning the implementation and management of legal matters;*

(b) *consultation concerning obtaining all necessary federal, state and local permits and authorizations;*

(c) *consultation concerning locations, leases, and other local matters;*

(d) *consultation concerning the political affairs applicable to the contemplated business; and*

(e) *consultation concerning the type and specifications applicable to the permitted games.*⁴⁶

[Emphasis added]

39. On 22 June 2000, Juegos de Mexico, Inc. (JDMI) and A-1 Financial International Ltd. (A-1), which was formed by Messrs. Oien and Ong, entered into a "Revenue Share and Consulting Agreement." Similar to the Letter of Intent, the Agreement stated that JDMI's principal responsibility was "formation of Mexican Companies" to operate the facilities and "supply of SKILL VIDEO Machines."⁴⁷ The Agreement provided:

A-1 FINANCIAL intends to pursue all permits and licensing requirements so as to authorize the operation of Skill Video Machines in various MEXICO Municipalities and seek approval for such operation in accordance with MEXICO Law. A-1 FINANCIAL has the necessary knowledge and experience to monitor and control the licensing and approvals to enable JDMI to operate such Skill Video Machines in MEXICO. A-1 FINANCIAL will provide JDMI with all necessary

⁴⁵ Exhibit R-127.

⁴⁶ Exhibit R-096 ¶¶ 1-3.

⁴⁷ See Exhibit R-103 which contains an organizational chart for A-1 Financial. See also Exhibit R-098, articles 1.3 and 4.1, June 22, 2000.

government authorization to operate Skill Video Machines in Facilities throughout MEXICO.⁴⁸

[Emphasis added]

40. A-1's principal responsibilities were stated to be as follows:

3.1 Permits and Licensing. A-1 FINANCIAL shall provide JDMI with all the necessary permits and licensing to enable Skill Video Machines to operate in the Skill Game Facilities in the country of MEXICO. Such permitting and licensing shall be specific to each governmental entity with applicable jurisdiction including local, state and federal governments [it then reiterated the responsibilities provided in the Letter of Intent].

*3.2 Lawful Operation. A-1 FINANCIAL shall supervise, monitor, consult with any and all governmental agencies and personnel and otherwise keep JDMI fully informed on obtaining and maintaining all licenses and permits necessary to operate the Skill Video Machines. A-1 FINANCIAL shall keep JDMI informed of all relevant laws and market developments to continue the operation of Skill Video Machines placed hereunder. To the extent available, A-1 FINANCIAL shall assist JDMI in obtaining and maintaining all necessary permits and licenses required to permit the lawful operation of the Skill Video Machines at each Skill Video Machine Site. As necessary, A-1 FINANCIAL shall provide JDMI with written instructions in connection with importation, installation, and operation of the Skill Video Machines. Notwithstanding any provision of this Agreement to the contrary, in the event JDMI is clearly prohibited by operation of law from using the Skill Video Machines in MEXICO, this Agreement shall terminate as to such Skill Video Machines and neither party shall have any further obligations to the other under this Agreement. If particular Skill Video Machines are rendered unlawful in specific Skill Game Facilities, then such Skill Video Machines shall be removed and not be subject to this Agreement. Upon mutual agreement the parties may contest the unlawful determination, and, if successful, re-deploy the Skill Video Machines in an approved location.*⁴⁹

[Emphasis added]

41. The documents show that the Claimant had committed to invest in gaming facility operations in Mexico fully six weeks before the 15 August letter was issued from Gobernacion, and that it did so specifically on the basis that Messrs. Oien and Ong would take care of obtaining all necessary permits, approvals, and licensing requirements.

⁴⁸ Exhibit R-098, article 1.2.

⁴⁹ A-1 Financial was also responsible for paying certain unspecified taxes and for locating sites for the gaming facilities. *Id.*, articles 3.1-3.4.

42. An exhibit to the 22 June 2000 Agreement establishes that “JDMI shall acquire 100% of the shares/interest in Entertainments de México, S. de R.L., which operates that certain business commonly known as the Matamoros Operation from its existing owners.” It also states that, “[o]nce JDMI acquires 100% of the shares/interest in the S. de R.L., all provisions contained in the agreement shall apply equally to the Matamoros Operation, as if specifically set forth herein at length”.⁵⁰ The evidence shows that JDMI acquired EDM on 10 August 2000 —prior to obtaining Gobernacion’s letter.⁵¹ Therefore, even if it could be considered that Thunderbird was the owner of JDMI, Gobernacion’s August 15 letter could not have been the reason for the acquisition of EDM.

43. Messrs. Aspe and Arroyo were not the legal counsel for the Claimant (as it asserted), but instead, were representatives of Mr. Oien and Ong.⁵²

44. In its Reply, the Claimant argued that there Mexico had not demonstrated that the conduct of Messrs. Aspe and Arroyo had been improper, contending that they were simply paid a fee “for their work in helping to secure the August 15, 2000 SEGOB letter.”⁵³ The draft letter from Peter Watson is dated 10 August 2000, as noted by the Respondent in the Statement of Defense, which is one week after EDM had submitted its letter to Gobernacion.⁵⁴ Even more noteworthy is that, although the letter stated Thunderbird would pay Messrs. Aspe and Arroyo US \$300,000 to obtain a letter from Gobernacion stating “there is no opposition or limitation to operate our skill machine venture,” it agreed to pay them upwards of US \$1,000,000 if the letter were “granted exclusively for the benefit of Thunderbird.”⁵⁵ The Claimant has now produced a signed document dated 15 August 2000 issued from Thunderbird to Messrs. Aspe and Arroyo. It states:

⁵⁰ Id. Addendum A.

⁵¹ Exhibit R-036 and R-124.

⁵² The Claimant objected to the Respondent’s 29 August 2003 request for the communications between Thunderbird and Messrs. Aspe and Arroyo on the grounds that it sought production of “privileged attorney-client communications and/or privileged attorney work product.” Letter from James Crosby to Hugo Perezcano, 22 September 2003, p. 9. However, the documents produced by the Claimant in compliance with Procedural Order No. 5 demonstrate that Messrs. Aspe and Arroyo were attorneys to Mr. Ong, not Thunderbird. An 8 May 2000 e-mail from Peter Watson to Mauricio Girault states “I have left a call for Julio Aspe, and Oscar Arroyo, the attorneys for Mr. Ong. . . in order to provide them to Luis Ruiz Velasco [Thunderbird’s attorney]. Exhibit R-095. An 11 May 2000 fax from Mauricio Girault to Jack Mitchell states “I called Lic. Julio Aspe (lawyer of ivy ong). . .” Exhibit R-105. The Tribunal should note that the Claimant refused to provide the Respondent with these documents for over six months on the basis of a non-existent privilege.

⁵³ Reply at 40.

⁵⁴ Statement of Defense, p. 41. Exhibit R-027.

⁵⁵ “It is our mutual understanding that the above-mentioned letter will be granted exclusively for the benefit of Thunderbird and/or its subsidiaries or designees in Mexico, and that no other such permission will be granted to other potential competing parties.” Thunderbird offered to pay US \$1,000 for each of 700 machines. Exhibit R-027.

In accordance with our understanding, the official letter shall be granted exclusively in favor of ITG and/or its subsidiaries in Mexico and shall not be granted to any person or legal entity competing in the same field of business.⁵⁶

45. The issuance of an authorization such as that which EDM intended to obtain (essentially an authorization to establish a monopoly) is related to the legality or illegality of the gaming activities in question. If the activity were legal, any person could obtain a license by complying with the applicable requirements and following the corresponding procedures. If, as is the case, the activity is illegal, no person can obtain a license, much less an exclusive license such as that which Thunderbird wished to obtain. Therefore, Mexico does not understand Thunderbird's agreement to pay a success fee to Messrs. Aspe and Arroyo if it received an exclusive benefit for an activity which is prohibited by the law (as it would not make sense to pay a success fee to obtain authorization for an activity that is legal, since all this requires fulfillment of the filing procedures). This arrangement also plainly raises suspicions about the *bona fides* of the contracting parties, even if the gaming machines had been legal.

46. The Tribunal should note that neither Messrs Oien or Ong, nor Messrs. Aspe or Arroyo, either individually, through the ONG Group, A-1 Financial, or otherwise, were able to secure a permit or approval from Gobernacion for operation of the "skill machines." As repeatedly pointed out by the Respondent, Gobernacion's 15 August 2000 letter plainly did not provide specific authorization of any kind.⁵⁷ It is evident that Messrs. Oien and Ong did not fulfill their part of their agreement and the parties decided to terminate it.⁵⁸ The Respondent submitted a letter dated January 2001 (three months after closure of the facilities) from Thunderbird to A-1 Financial stating:

As we have already tried to make clear, this venture is far different, far more complex, and far more difficult than what A-1 represented it to be.⁵⁹

47. In Mexico's submission, the weight of the evidence strongly supports the view that the Claimant proceeded with the investment in reliance on the representations of Messrs. Oien and

⁵⁶ Exhibit R-106. Thunderbird provided a copy of an electronic wire transfer of funds from Thunderbird Greeley, Inc. to Consultoria Internacional Casa de Cambio, S.A. de C.V. for \$300,000 dated 16 August 2000, payable to a Rafael Ramos Velasco as the beneficiary. Exhibit R-107.

⁵⁷ Thunderbird also not does claim it is so. See Statement of Claim, p. 41: "*Claimant has never asserted that it obtained a government permit or specific formal authorization to operate with the August 15, 2002 [sic] letter.*"

⁵⁸ Cf. *Revenue Sharing and Consultation Agreement*. Exhibit R-098. Letter from Albert Atallah to A-1 Financial, 21 December 2000 ("*A-1 Financial and its principals are no longer authorized to represent International Thunderbird Gaming Corporation, its affiliates and subsidiaries (including Entertainments de Mexco) with respect to the Mexico Skill Game Operation. Furthermore, as stated in our discussions, Thunderbird does not believe that A-1 Financial met its obligations as contemplated by the original agreement.*" Exhibit R-108; Exhibit R-129.

⁵⁹ Exhibit R-109.

Ong private sector advisors and business partners, and not the Gobernacion letter. In fact, the Revenue Share and Consultation Agreement between Thunderbird and A-1 Financial states:

JDMI and A-1 FINANCIAL warrant that these Recitals are a material part of this Agreement and are true and correct. Both parties relied upon the recitals in entering into this Agreement.

...

1.2 Knowledge and experience. A-1 FINANCIAL is a limited partnership under the Texas law and wishes to participate in a Revenue Share and Consulting Agreement with JDMI to operate Skill Video Machines facilities in the MEXICO Market and is authorized to execute agreements on behalf of the partnership in accordance with Texas law. A-1 FINANCIAL intends to pursue all permits and licensing requirements so as to authorize the operation of Skill Video Machines in various Mexico Municipalities and seek approval for such operation in accordance with Mexico Law. A-1 FINANCIAL has the necessary knowledge and experience to monitor and control the licensing and approvals to enable JDMI to operate such Skill Video Machines in Mexico. A-1 FINANCIAL will provide JDMI with all necessary government authorization to operate Skill Video Machines in Facilities throughout MEXICO.

...

3.1 Permits and Licensing. A-1 FINANCIAL shall provide JDMI with all the necessary permits and licensing to enable Skill Video Machines to operate in the Skill Game facilities in the country of MEXICO. Such permitting and licensing shall be specific to each governmental entity with applicable jurisdiction including local, state and federal governments. A-1 FINANCIAL shall be responsible for the following services to promote the business of the MOCs:

- (a) the implementation and management of legal matters relating to the Skill Video Machines;*
- (b) obtaining all necessary federal, state and local permits and authorizations;*
- (c) selecting locations and negotiations of leases;*
- (d) advising of the political affairs applicable to the contemplated business; and*
- (e) advising on the type and specifications applicable to permitted games.⁶⁰*

⁶⁰

Exhibit R-098.

7. Reasons Why EDM Withdrew From Judicial Appeals Filed In Mexican Courts

48. In the Statement of Defense, Mexico reviewed the various judicial proceedings initiated by EDM to contest Gobernacion's ruling and the closure of the gaming facilities:

- Nuevo Laredo. EDM simultaneously filed a *juicio de amparo* (before a district judge) and for a nullification ("*juicio de nulidad*") (before the federal tax and administrative court) against the same actions, claiming the same alleged violation. Both claims were dismissed. To challenge the ruling of the district judge, EDM filed an appeal ("*juicio de revision*" en efecto una apelación). The Collegiate Tribunal (*Tribunal Colegiado*, in essence, a court of appeals) ruled against EDM. The ruling of this court is final; there is no further means of review. EDM filed a *juicio de amparo* against the ruling on nullification, but then withdrew.⁶¹
- Reynosa. Prior to the closure carried out by Gobernacion, EDM had filed two *juicios de amparo* from which it later withdrew. Against the closure, EDM filed a new *juicio de amparo* from which it withdrew, which was why the case was dismissed.⁶²
- Matamoros. In this case, EDM filed a *juicio de amparo* against the closure, which was dismissed because EDM withdrew.⁶³

49. In its Reply, the Claimant attempts to justify EDM's decision to withdraw, arguing that to continue the proceedings would have been "a futile exercise."⁶⁴ It contends:

Thunderbird did not lightly abandon any local avenues of judicial redress. The decision to direct the EDM's to cease court actions was based on a careful analysis of the relevant legal and political factors known to it at that time. These factors are addressed in the declaration of Javier Navarro submitted with this SoR. They included an evaluation of the likelihood of success, given evidence that the process was not being conducted fairly; and they included the decision to choose remedies available under the NAFTA instead of those available under domestic law.⁶⁵

50. However, in his witness statement, Mr. Navarro refers to the procedural violations allegedly committed by Gobernacion in the closures, regarding which the above appeals were

⁶¹ See Statement of Defense, Section VI.C.1.

⁶² Exhibit R-130.

⁶³ See Statement of Defense, Section VI.C.2.

⁶⁴ Reply at 48.

⁶⁵ Reply at 47.

filed. Contrary to the Claimant’s allegations, Mr. Navarro does not in fact argue that the courts treated EDM unjustly, nor that there might have been any kind of violations in the judicial proceedings. There is no evidence of unfair or unjust treatment in the judicial proceedings.

51. The “irregularities and violations” to which Mr. Navarro refers do not address the conduct of the judicial proceedings. They specifically concern the closure order that EDM challenged.⁶⁶ Even more, in his witness statement, Mr. Navarro limits himself to transcribing the claims made by EDM in the *juicio de amparo*:

Navarro Witness Statement ⁶⁷	Claims made in the Juicio de Amparo 471/2001 ⁶⁸
<p>a. La SEGOB no cumplió con todos los requisitos que establece la Constitución en los casos de los cateos, ya que si bien existe un oficio de fecha 10 de oct. 01, mediante el cual se le autorizó a los inspectores (nombres) proceder a intervenir los días 10, 11 y 12 de octubre de 2001 en la clausura que se llevara a cabo en el inmueble de EM, ésta quedó condicionada a que se detectase “la celebración de juegos prohibidos por la LFJS y/o que no se cuente con permiso de la SEGOB”; los inspectores en el acta de inspección y clausura se excedieron al asegurar y clausurar todos los bienes muebles y equipos dentro del interior del inmueble de referencia, así como impedir que la quejosa continuara en su caso con el negocio de restaurante-bar, para lo cual cuenta con los permisos estatales y municipales correspondientes, ya que sin establecer en el acta de manera clara y pormenorizada qué tipo de juegos prohibidos por la Ley encontraron en el lugar, procedieron a la clausura del negocio mercantil de la quejosa.</p>	<p>(...) Adicionalmente se podrá observar que la autoridad administrativa no cumplió con todos los requisitos que establece la constitución en los casos de los cateos, ya que si bien existe un oficio de fecha 10 de oct de 2001, mediante el cual se autorizó a los inspectores (nombres) proceder a intervenir los días 10, 11 y 12 de octubre de 2001 en la clausura que se llevara a cabo en el inmueble (ubicación) ésta quedó condicionada a que se detectase “la celebración de juegos prohibidos por la LFJS y/o que no se cuente con permiso de la SEGOB”; los inspectores en el acta de inspección y clausura se excedieron al asegurar y clausurar todos los bienes muebles y equipos dentro del interior del inmueble de referencia, así como impedir que la quejosa continuara en su caso con el negocio de restaurante-bar, para lo cual cuenta con los permisos estatales y municipales correspondientes, ya que sin establecer en el acta de manera clara y pormenorizada qué tipo de juegos prohibidos por la Ley encontraron en el lugar, procedieron a la clausura del negocio mercantil de la quejosa.</p>

52. The best evidence of why EDM withdrew from its appeals is contained in the court decisions themselves. The decisions indicate that EDM committed fundamental errors of litigation strategy by attempting to appeal Gobernacion’s actions simultaneously before two

⁶⁶ See pp. 7, 9 and 14 of the *juicio de amparo* indirecto 300/2001, Exhibit R-028(1). See also p. 7 of the *juicio de amparo* indirecto 471/2001, Exhibit R-030(1).

⁶⁷ See Javier Navarro Witness Statement, ps. and 9. Exhibit C-V.

⁶⁸ See Exhibit R-030, p. 7.

different tribunals.⁶⁹ In fact, the Respondent has submitted a document in this proceeding in which Thunderbird indicated dissatisfaction with the advice provided by Baker & McKenzie, the law firm representing EDM.⁷⁰

53. Thus, the evidence indicates that EDM withdrew from the appeals for its own tactical or business reasons, and not because of any problems experienced with the administration of the Mexican courts.

8. Investors In EDM Companies

54. The Claimant submits a series of witness statements from several individuals that affirm having invested in EDM as “passive investors”.⁷¹ It is important to note that the Claimant in its Reply, instead of analyzing the documents it provided with the Statement of Claim, which Thunderbird argued prove its ownership and control of EDM, it limits itself to providing a series of witness statements to support its position. However, a review of these statements and the lists of investors for each company show various inconsistencies. For example, Isabel Berger, representative of ANCAR, S.A., Aquilino de la Guardia, Carlos de la Guardia, Laurence Berger on behalf of Productos Superiores, and Harry Strunz assert that they invested in EDM Matamoros. However, their names do not appear in any documents pertaining to this company: the Subscription Agreement, Members Quota Agreement, list of shareholders, Board Meeting Minutes, etc. As a result, they cannot be considered investors of EDM Matamoros.

9. Motivation of Thunderbird to Withdraw From California

55. In paragraph 13 of his 6 February 2004 witness statement, Albert Attallah states:

The reason that Thunderbird disassociated itself from the California gaming market was that the company was asked by the United States District Attorneys to cease doing business with the tribes. This decision by Thunderbird was completely voluntaryThe management at Thunderbird at that time believed that because the company was involved in gaming in other parts of the world, it would be in the company's best interest to cooperate with the U.S. regulators even though ultimately had the company remained in California, the company's activities would have been completely legal.⁷²

56. However, an excerpt from Thunderbird's Minutes of a Board of Directors' Meeting held on 16 April 1998 states:

⁶⁹ See section VI.C of the Statement of Defense.

⁷⁰ See Exhibit R-018.,p. 3. Messrs. Luis Ruiz de Velasco and Javier Navarro are attorneys with Baker & McKenzie.

⁷¹ Reply at 28.

⁷² Exhibit C-V.

[Jack Mitchell] indicated further that the Attorney's Office advised that if the tribes did not choose either option, they will face criminal action. Similarly, any company dealing with them on any level, such as Thunderbird, will also be at risk for criminal and civil prosecution in California after the May date. The Company retained criminal counsel to provide assistance with respect to this matter. Mitchell said that the message from the four State's Attorneys for California was that they would be taking enforcement action immediately following the May deadline. He indicated that they had not been concerned with activities of vendors such as Thunderbird in the past but they would be so once the deadline passed. "The message was clear: if you are not doing business with compacted Tribes after the deadline, then you'd better not be doing business in California."⁷³

57. The Tribunal should give greater probative value to Mr. Mitchell's contemporaneous statement to the Thunderbird board in which he warns of the civil and criminal liability it could face, than the testimony of Mr. Atallah, prepared specifically for this arbitral proceeding.

10. Submission Of Identical Witness Statements Offered By Thunderbird

58. As Professor Sandifer wrote: "witnesses testifying in identical language concerning complex or remote facts will not ordinarily be considered entitled to belief."⁷⁴

59. The Claimant submitted with its Reply fourteen identical witness statements from alleged investors in EDM.⁷⁵ The witness statements of Tim Carson and Kevin McDonald testifying that the machines used by EDM were custom-made for the Mexican market are virtually identical (compare paragraphs 2 through 7 of Carson's statement to paragraphs 4 through 8 and 10 of McDonald's statement).⁷⁶

60. The Notary Public statements presented by the Claimant along with the Statement of Reply are also essentially identical. For example, Section VII of the certification of facts ("*acta de fe de hechos*") dated 16 January 2004, which describes the "Club 21" machines in

⁷³ Exhibit R-021 ps. 2-4

⁷⁴ Op. cit. p. 323.

⁷⁵ See witness statements of Peter Watson (Exhibit C-X); Isabel Berger (Exhibit C-Z); Aquilino de la Guardia (Exhibit C-AA); Frank Bennett (Exhibit C-BB); Michael Snow (Exhibit C-CC); Carlos de la Guardia (Exhibit C-DD); Max Joe Harari (Exhibit C-FF); Kevin McDonald (Exhibit C-GG); Lawrence Berger (Exhibit C-JJ); Wayne Rudd (Exhibit C-KK); Robert Ruyle (Exhibit C-LL); Harry Strunz (Exhibit C-MM); Mauricio Girault (Exhibit C-NN); and Tino Monaldo (Exhibit C-II) (the latter statement has some additional language but the key substantive paragraph is substantially identical to those in the other statements).

⁷⁶ See Exhibits C-EE and C-HH.

Huixquilucan is virtually identical to Section VII of the certification of facts for the Matamoros facilities issued by a different Notary Public, in a different location.⁷⁷

61. It is obvious that all of these statements were prepared by the Claimant and lack probative value as testimony of witnesses.

B. Response To Claimant's Submissions On the *Ley Federal de Juegos y Sorteos*

62. The Claimant complains that the Mexican law on gambling is unclear, and that Mexico provided little information in its Statement of Defense about Mexican law. For example, page 32 of the Reply states "*the lack of any significant discussion of Mexican law as it applies to the operation of skill machines*" and "*the SOD contains no discussion of Mexican law as it applies to the operation of skill machines*".

63. Apparently, the Claimant did not read pages 7 to 9 and 17 of the Statement of Defense, which discuss the *Ley Federal de Juegos y Sorteos*; pages 43 to 48, which explain the procedures before domestic tribunals; pages 50 to 52, which analyze the legal proceedings initiated by Messrs. Guardia and de la Torre regarding the closure of their facilities; and the expert legal report of Dr. José María de la Serna (Exhibit R-054).

64. In addition, the Respondent submits that the detailed legal arguments presented by Gobernacion in its ruling dated 10 October 2001 respond to the arguments then posed by EDM as well as those that Thunderbird presents in this claim. Since the Claimant has omitted to discuss most of Gobernacion's explanation, the Respondent has reproduced a portion of it below:

FOURTEEN: Having remained established that the substance of the present resolution is in order to determine whether the machines operated by Entertainmens de Mexico are or are not permitted under the Federal Law on Gaming and Lottery.

Along these lines, article 1 of the Federal Law on Gaming and Lottery, establishes that:

Art. 1.- Games of chance and games involving betting remain prohibited, in accordance with the terms of this law, in the whole national territory.

From the legal text as written, can be observed the prohibition of two types of games:

- a) Games of chance

⁷⁷ See Exhibit C-P, C-S and C-T. It should also be noted that the certification of facts carried out by Notary Public No. 160 of Matamoros, Tamaulipas, Mr. Guillermo Vázquez Cuevas, at the Matamoros facilities took place on the same day (27 January 2004) at practically the same time: one proceeding began at 11:00 a.m. and ended at 11:45 a.m.; while at the other facility it began at 11:00 and ended at 11:05. See Exhibits C-S and C-T.

b) Games involving betting

To achieve the correct interpretation of the said rule, it follows that the legislator used the conjunction “and” to determine the prohibited games. Two different types are dealt with; one in which chance intervenes, and the other in which betting appears. Both suppositions could be recognized individually, even though there is no obstacle to their being presented jointly, that is to say, games of chance involving betting, and a situation that obviously, and by extension, is also prohibited by law.

This situation is also recognized by the legal representative of the artificial [juridical?] person the subject of these proceedings, quoting from his document of 23rd March last, he maintained “With the objective that this authority entertains the possibility of confirming that the video game machines of ability and skill are not machines of chance or involving betting”.

Nevertheless it is not required sine qua non that both elements are present (chance and betting) for a game to be considered as prohibited in terms of the Federal Law on Gaming and Lottery, it is sufficient for one of those to be present in order to effect the prohibition that the legislator prepared in the order under consideration.

As established above, it is necessary to review the contents of article 2 of the actual legal text which concerns us, in which is stated:

“Art.2 – Those that alone are permitted:

I. The game of chess, the game of checkers and others similar to it; of dominos, of dice, of bowls, of skittles and of snooker; all types and descriptions of ball games; races for people, vehicles and animals, and in general, all types of sports.

II. Raffles The game which are not designated will be considered as prohibited for the effect of this law.”

From what is written, it is the intention of the legislator to designate, **in a limited way**, those games which the law itself permits.

Furthermore, in agreement with the foregoing, the last paragraph of the said legal precept is of utmost importance, in that it defines the **nature of the Federal Law on Gaming and Lottery as prohibitive, and not as constitutive of rights.**

For this reason it is valid to maintain that the machines operated by Entertainments of Mexico S. de R.L. de C.V, are not contemplated within the games set out in section I of article 2 of the Federal Law on Gaming and Lottery, as they have nothing to do with chess, neither of checkers nor any similar games; neither with these machines can dominos be played, nor dice, nor bowls, much less skittles or billiards; neither races

for people, vehicles or animals, nor with them can be played any type of sports.

For its part, article 3 of the legal order in question, establishes:

Art.3 The regulation, authorization, control and vigilance of games involving betting of any type, such as raffles, is the responsibility of the Federal Executive, acting through the Secretary of the Interior, with the exception of the National Lottery, which is governed by its own law.

The article under consideration stipulates the power of the Secretary of the Interior to:

- a) Regulate
- b) Authorize
- c) Control, and
- d) Inspect;
- e) Games where there exist betting of any time.

Note that the legal disposition does not restrict the betting to a particular assumption, but rather the generic phrase “of whatever type” opens it up, so that is not possible to accept the definition provided by the company which is participating in this administrative procedure, in the sense that the games involving betting” ...are those in which players agree among themselves in advance, the delivery of a quantity of money.. .” and as can be seen, the legislator foresaw that the bet is not only made in the legal tender of the country, but “of whatever type”, thus including all present or future possibilities.

The said legal precept also establishes the power of the Secretary of the Interior to **authorize** games when they involve betting of whatever type.

Therefore, in addition to the contents of article 2, section I, above written, the law delegates to administrative authority the responsibility to authorize the said games; and so we are in the presence of two conflicting interpretations of the legal text.

1. Those games prohibited by the same Federal Law on Gaming and Lottery.
2. Those games authorized by the Secretary of the Interior, when they involve betting of whatever type.

In the case before us, there is no compliance with either of these provision; according to what has been seen, we are dealing with games

prohibited by the Federal Law on Gaming and Lottery even though the Secretary of the Interior has not authorized them.⁷⁸

The determination goes on to analyze the factual nature of EDM's machines.

65. A key point – avoided by the Claimant – is that the prohibition established by the gaming law comes into effect with the involvement of either element: chance or betting. If a game involves betting, it is prohibited regardless of the degree of “ability or skill” required from the player. EDM's games operated based on risking a certain sum of money in order to win a greater amount as a result of obtaining a winning combination of figures in a machine.⁷⁹ This sole element was sufficient for Gobernacion to determine that the games involved betting and therefore were prohibited. Gobernacion did not only determine that “one is in the presence of games of chance” and not of skill, but also determined that they were games with betting.⁸⁰

66. As explained in the Statement of Defense, analogous rules apply in the United States.⁸¹ For example, in the state of North Carolina, even a machine that meets that state's requirements for being a “skill machine” is still regulated as gambling equipment if cash or prizes worth more than \$10 can be won. An EDM-type casino would be illegal in North Carolina unless it was located on an Indian reservation and was licensed as a casino by the state. Mexico's point has been that, in every jurisdiction in which it has examined the applicable law, the types of machines operated by EDM are treated as gambling equipment.

67. The Claimant has presented no evidence to the contrary, nor has it identified any other jurisdiction in which these types of machines are not considered gambling equipment. Where a jurisdiction allows gambling – such as in Las Vegas or on U.S. Indian reservations – these types of machines can be used legally in a casino, provided that the casino operator has obtained the

⁷⁸ Exhibit R-093.

⁷⁹ Specifically, the machine operates based on the insertion of dollar bills to begin the game, with the objective of earning points redeemable for cash. If the player loses the sum of money that had been inserted into the machine, the player may insert more to keep playing. When the player decides to end the game, the machine prints a ticket displaying the number of points accrued, which the player can then redeem for cash.

⁸⁰ Exhibit R-093 p. 23.

⁸¹ The Claimant now says that U.S. law is irrelevant. But as explained by the Respondent in the Statement of Defense:

Thunderbird's legal representative declares to have studied U.S. gaming laws, and concluded that games of skill are allowed. He bases his understanding of Mexican gaming law on this. The Claimant formerly was involved with the operation of these types of gaming machines in the United States, and has argued that U.S. law exempts “skill machines” from prohibition under gaming laws. However, the Claimant incorrectly interprets U.S. law, which is the exclusive basis for its interpretation of Mexican law. Thus, U.S. law is therefore relevant to this dispute, as it reflects on both the Claimant's genuine expectations and the credibility of its opinions on the Mexican law.

Statement of Defense p. 9.

necessary permits and submitted to the oversight of the pertinent government agency that regulates gambling establishments.

68. Accordingly, the Claimant is being disingenuous when it says that its machines were “legal” in the United States.⁸² They are legal only when used in a location where gambling is allowed and where appropriate permits have been issued. Here, a gambling game is not permitted in Mexico without authorization from Gobernacion. EDM did not have an authorization, and this was one of the reasons for the closure.

69. The Claimant is also evasive when it argues that its machines have never been “found illegal.”⁸³ The Respondent already submitted documentary evidence provided by the Claimant itself that demonstrates that it withdrew from various markets because it knew that its activities would be determined to be illegal.⁸⁴ Accordingly, the Respondent reaffirms its arguments.⁸⁵

70. For these reasons, the Claimant is incorrect when it claims on page 32 of the Reply that the application of the laws of the U.S. jurisdictions contained in the Statement of Defense “are not inconsistent in any respect with the statements made by Thunderbird to Mexican authorities or the positions taken by Thunderbird in the seizure and post seizure periods.” To the contrary, EDM claimed to Gobernacion that these types of machines were not treated as gambling equipment in the United States. The Respondent has demonstrated, with U.S. statutes and case law, that those representations were wrong.

71. Nelson Rose, a recognized expert in gambling law in the United States, testifies that machines of the nature described by Thunderbird itself—specifically, those with “skill stop” buttons”—have routinely been held to be gambling equipment in the United States, and that in

⁸² In his witness statement, Albert Atallah states that Thunderbird’s games “would have been completely legal” in California. Exhibit C-V.

⁸³ Reply p. 10.

⁸⁴ See Statement of Defense pp. 35-39, as well as Exhibit R-021.

⁸⁵ The Claimant displays indignation over its claim that the Statement of Defense said that Thunderbird had made a conscious decision to operate “against the law.” Reply p. 21 (“*Mexico feels compelled to slander the integrity of the claimant*”). Mexico did not make any such statement in the Statement of Defense. Rather, after presenting evidence from Thunderbird’s own corporate records that it had entered and withdrawn from several markets after the applicable laws had been clarified to prohibit gambling, the Respondent concluded that it appeared that Thunderbird had made “conscientemente seguía una estrategia de negocios que está en los márgenes de la ley.” Statement of Defense p. 39. Note also the following statement from Thunderbird’s own annual report:

The Company's prior activities in unsettled markets and its stipulated denial of a license in Colorado create challenges for it to be licensed in certain jurisdictions in United States. The Company has taken all steps possible to operate responsibly in regulated markets, including divestiture of its Internet business and removal of all officers and directors responsible for moving the Company into unsettled markets. The Company was conservative in ceasing its operations in May, 1998 in California and ceasing collection of substantial revenues from its Tribal clients.

Exhibit R-088. The Respondent reaffirms the arguments it made in its Statement of Defense.

fact he is unaware of any jurisdiction in which they have been found not to be gambling machines.⁸⁶ Mr. Rose also highlights that “In some jurisdictions, the degree of skill is totally irrelevant if the potential payouts are greater than a *de minimis* level.”⁸⁷ He adds that it is typical of these types of companies to operate in jurisdictions where the applicable law is unclear, with the intention of generating profits during the time they can operate before the authorities become aware and take appropriate measures.⁸⁸

72. Mr. Rose also testifies that the term “video lottery terminals,” used by Mr. Atallah in his description of the machines placed by Thunderbird in California, is synonymous with the term “video gaming terminals,” and that such machines are classified as slot machines under both California and U.S. federal law.⁸⁹ Mr. Rose states that the activities of Thunderbird in placing such machines with tribes that did not have Compacts with the state government put the company at serious risk of criminal prosecution.⁹⁰

C. Response to the Claimant’s Assertion That the 15 August Letter Was an “Approval” Of Its Activities

73. In the Reply, the Claimant has attempted to adjust its argument on the nature of the 15 August 2000 letter. In the Statement of Claim, Thunderbird characterized the 15 August 2000 letter as an authorization.⁹¹ It now admits:

*Claimant has never asserted that it obtained a government permit or specific formal authorization to develop its operations.*⁹²

74. The Claimant nonetheless goes on to assert that Gobernacion informed Thunderbird that its operations were not prohibited by Mexican law:

Whether the letter is characterized as an “approval” or a “government assurance”, there can be little doubt that it was intended by [Gobernacion], and understood by Thunderbird, to be a statement by the government of Mexico that the intended investment was not prohibited

⁸⁶ Statement of Nelson Rose at pp. 17-20, Exhibit R-110.

⁸⁷ Id. at p. 9.

⁸⁸ Id. at pp. 14-17.

⁸⁹ Id. p. 21.

⁹⁰ Id. pp. 20-21.

⁹¹ Statement of Claim pp. 18-19 (“In doing so, he [Vargas] misrepresented the August 15 official letter... in describing the August 15 letter to his superior, Guadalupe Vargas misrepresented it as denying authorization to Thunderbird’s EDM entity to operate skill machines... In fact, the August 15 letter specifically stated that the identified machines were not games of chance and were not prohibited by Mexican law.”).

⁹² Reply p. 41.

and could go forward without threat of government restriction or regulation.⁹³

1. The August 15 Letter Was An Advisory Opinion Based On The Information Provided By EDM In Its 3 August 2000 Solicitude

75. In its Statement of Defense, Mexico has explained the scope of the letter issued by Gobernacion on 15 August 2000 in response to the statements provided by EDM.⁹⁴ Mexico has also demonstrated that EDM did not operate the machines in the form or manner described in its August 3 solicitude, neither with respect to the element of “ability and skill” nor the betting.

76. In its *solicitud*, EDM emphatically states: “En estos video juegos no interviene ni el azar ni la apuesta...”. EDM failed to specify, as Thunderbird later did to its shareholders, that the games in question involved “some degree of skill”. The *solicitud* also states that the objective of the game is “que el operador del juego consiga ordenar signos en una combinación óptima y que le otorgue un ticket [sic] con puntos canjeables por bienes o servicios”⁹⁵. EDM did not point out that the “user” must insert dollar bills and that the “goods or services”, the “prize”, the “reward” is a payment in cash.

77. Gobernacion concluded as follows:

Public Document DGG/SP/1057/200 of 15 August 2000, signed by the acting Director of Games and Raffles, in the absence of the Director of Games and Raffles, is not an obstacle to the above, in that the contents of said document in no way constitute an authorization for the operation of cash slot machines which are the subject of this resolution, as in a mistaken way, the company involved in this administrative procedure is trying to demonstrate.

The fact does not pass unnoticed by the judge in this case, that the administrative authorities existing at that time stated that:

“IN THIS SENSE, IT IS IMPORTANT TO CLARIFY THAT IF THE MACHINES THAT ARE COMMERCIALY EXPLOITED BY YOUR PRINCIPAL ARE OPERATED ACCORDING TO THE FORMS AND TERMS STATED BY YOU, THIS ADMINISTRATIVE AUTHORITY IS NOT COMPETENT TO PROHIBIT THEM, KNOWING THAT IF WE ARE REFERRING TO MACHINES KNOWN AS ‘CASH SLOT MACHINES’, ‘TOKEN SLOT MACHINES’ OR ‘SLOT MACHINES’, IN WHICH THE PREDOMINANT FACTOR OF OPERATION IS CHANCE AND THE PLACING OF BETS, AND NOT ABILITY AND

⁹³ Id.

⁹⁴ Statement of Defense, Section VI.D.1.

⁹⁵ Exhibit C-17.

SKILL, AS YOU STATE, THE PROVISIONS ESTABLISHED BY FEDERAL LAW WILL APPLY, WITH THE CONSEQUENCES SET OUT IN ARTICLE 8 OF SAID LAW.

It is noted that such assertions do not constitute any type of permit, because present in the drafting is the conditional word “if” which logically requires in addition the presence of a determining situation or fact, which necessarily and without doubt must be adjusted to the terms of the conditions proposed, which will never be interpreted as a permit, and most important of all in the said paragraph, the authority makes reference to the possible violation of the Federal Law on Gaming and Lottery.⁹⁶

78. The August 15 letter is far from an “authorization” or from providing “assurances”; rather, it is clearly a warning that operations EDM was conducting, which it intended to expand, could be illegal.⁹⁷

79. Thus, it is clear that Thunderbird is seeking to have this Tribunal rule on the very same issue – an issue of purely domestic law – that has already been resolved by Gobernacion in an administrative proceeding and which was affirmed by the Mexican courts.

⁹⁶ Exhibit R-093, pp. 25-26.

⁹⁷ The Reply asserts that the Respondent has conceded that a Gobernacion official, “Francisco La Bastida,” who the Claimant alleges was the Secretary of Gobernacion when the 15 August 2000 letter was issued, orally told Peter Watson (an investor in EDM) in a “private meeting” that he was aware that since there was already a successful skill game and a precedential court case, the 15 August letter was an “appropriate response” to EDM’s letter. Reply p. 42; Declaration of Peter Watson ¶ 16 (Exhibit C-A). The Respondent wishes to point out that Sr. Labastida, who did serve as Secretary of Gobernacion, resigned in May 1999 to seek the PRI’s nomination as candidate for President of Mexico. Transcript of Francisco Labastida Resignation Press Conference, 21 May 1999. Exhibit R-111. Sr. Labastida did not return to work for the federal government after the elections of 2 July 2000, which were won by President Fox. The impossibility of Mr. Watson’s assertion with respect to Sr. Labastida casts serious doubts on the Claimant’s witness statements that claim numerous meetings with Gobernacion officials. It should be noted that the Respondent sought documentation from the Claimant evidencing the purported meetings it claims were held with Gobernacion officials, and the Claimant produced nothing in response.

By means of Oficio No. DGCJN.511.13.949.03 dated 29 August 2003, the Respondent asked the Claimant to provide copies of any documents evidencing discussions between any representative of Thunderbird or EDM with any Gobernacion official, specifically identifying Sr. Labastida Ochoa. Oficio No. DGCJN. 511.13.949.03 dated 29 August 2003, p. 4. The Claimant responded with a blanket objection that the request was “overly-broad and burdensome.” Letter from James Crosby to Hugo Perezcano, 22 September 2003. On 17 October 2003, the Respondent narrowed the request to such documents “referring to meetings identified by the Claimant in its Particularized Statement of Claim” which specifically discussed, among others, EDM’s request and SEGOB’s response. Oficio No. DGCJN.511.13.1095.03 dated 17 October 2003, pp. 1-2. The Claimant then objected that it was “not specifically designed to obtain particular documents.” Letter from James Crosby to Gonzalo Flores, 5 December 2003, p. 3.

2. EDM Did Not Treat the Letter As a Permit Or Authorization At the Time It Was Issued By Gobernacion

80. In its Reply, the Claimant states that Thunderbird chose “to hire the world’s largest law firm and the certainty of the solicitud process they advised to undertake.”⁹⁸ According to Jack Mitchell, Thunderbird’s lawyers determined that a solicitud to Gobernacion and the response would authorize it to operate in Mexico⁹⁹. It is important to review the legal opinion that attorney Luis Velasco of Baker & McKenzie issued regarding the 15 August 2000 letter:

Based on the principal terms of the Official Letter, the Ministry of Interior states that it does not have any jurisdiction over the operation of said machines, since in accordance with the representations made by EDM in its application, the video games skill machines to be operated by EDM do not fall into the classification of “slot machines”, which are forbidden in Mexico pursuant to the applicable laws, in view of the fact that they are considered to be gaming and/or betting machines.

Furthermore, under the Official Letter the Ministry of Interior emphasizes that EDM can operate the video games skill machines as long as they do not become, in any manner whatsoever, as gaming or betting machines; provided; however, that EDM complies with the states and/or municipal laws or regulations in Mexico.

Based upon the foregoing, we are of the opinion that EDM is allowed to operate in Mexico the video game skill machines as long as EDM complies with the administrative requirements set forth by the state or municipal laws and regulations in Mexico.

Evenmore, in the event the Ministry of Interior intends to close down EDM’s operations, EDM will be able to appeal, since the Official Letter allows it to operate the skill machines as such; in the understanding, that EDM must comply at all times with each and everyone of the requirements set forth by the competent authorities where the machines are operating.¹⁰⁰

[Emphasis added]

81. Ruiz de Velasco emphasized that EDM could operate so long as they did not become in any manner betting machines (“*emphasizes that EDM can operate the video games skill machines as long as they do not become, in any manner whatsoever, as gaming or betting*”

⁹⁸ Reply p. 65.

⁹⁹ Declaration of Jack Mitchell, 14 August 2003: “Through a “solicitud” process and an official response from Gobernacion, our lawyers determined that skill games could be operated under the laws of Mexico.” (emphasis added). Exhibit C-C.

¹⁰⁰ Exhibit R-112.

machines”,¹⁰¹ In the November 2003 visits to the EDMs, the Respondent was able to confirm that the machines had dollar bill acceptors, which made them *per se* “dollar-swallowers” (“maquinas tragadolares o tragabilletes”).¹⁰²

82. As previously noted, the fact that money is played with the aim of earning more money than the amount originally deposited into the machine (also considering that the full amount deposited may be lost), is sufficient to conclude that Gobernacion neither authorized, approved, nor consented to EDM’s operation, according to the simple and clear terms of the Gobernacion letter, particularly in light of the warning provided by EDM’s own attorney.

83. The 20 June 2001 EDM-Matamoros Subscription and Investment Representation Agreement also refers to the opinion to the Baker & McKenzie opinion: “[t]he Company has been advised by Baker & McKenzie... that the operation of ‘skill machines’ by EDM is not prohibited in Mexico.” Again, however, it is necessary to parse the text of the agreement carefully:

The entitlement also confirmed that so long as EDM operates “skill machines”, as described to the government by EDM, the government will not challenge EDM’s operations. Based on this letter, although no specific entitlement was granted to the Company either directly or indirectly by approving the EDM’s franchise System, the Company believes that its operations of the Business as contemplated will be permitted in Mexico.

There can be no assurance that the Mexican Government will continue to view EDM’s or the Company’s operations as permitted “skill machines” and not a game of chance.¹⁰³

[Emphasis added]

84. The Tribunal should note that EDM did not inform Gobernacion that its machines were fitted with dollar bill acceptors in order to allow the player to win a ticket with points redeemable for cash (“*obtenga un ticket con puntos canjeables*”), knowing this would be one element Gobernacion would take into consideration in its determination. Thus, the disclaimer provided by EDM to its investors that there could be “no assurance that the Mexican Government will continue to view EDM’s or the Company’s operations as permitted “skill machines” and not games of chance” was telling. It did not rule out the possibility that Gobernacion would take action under the gambling law (*Ley Federal de Juegos y Sorteos*) once it saw how the games actually operated.

^{101.} The Tribunal should note that Mr. Ruiz de Velasco was expressly authorized in the August 3 solicitude in which EDM affirmed categorically that in the games neither chance nor betting intervened, however, his opinion is focused only on the betting element.

¹⁰² An aspect also noted by Mr. Guadalupe Vargas during the inspection and closure of the Nuevo Laredo facility. Exhibit R-042.

¹⁰³ EDM-Matamoros Subscription and Investment Representation Agreement, section 3(b)(viii). Exhibit C-28.

3. Mr. Carlos Gómez Álvarez Tostado's Solicitud ("Amazing World")

85. In its Statement of Claim, and again in its Reply, the Claimant argues that Mr. Gomez requested from Gobernacion on behalf of a client other than EDM an authorization to operate skill machines ("attorney Carlos Gomez requested permission from Gobernacion and the Department of Interior on behalf of a client other than claimant to operate skill machines") and that Gobernacion required from him the exact same information that Thunderbird provided in the 3 August 2000 request ("was the exact same information provided by Thunderbird in its 3 August 2000 solicitude").¹⁰⁴ However, this is not the case.

86. On 9 October 2000, Carlos Gomez filed a letter with Gobernacion in which he inquired whether some special authorization was required to operate "*maquinas para juegos de destreza y video*", also recognized as "tragamonedas," that awarded prizes valued at less than 1,000 pesos to the players that won points based on ability and skill.

87. On 14 December 2000, Gobernacion responded to Sr. Gomez's letter, stating:

A este respecto resulta oportuno hacer las precisiones siguientes:

Con objeto de que esta autoridad administrative cuente con mayores elementos que le permitan valorar su peticion y emitir su criterio con relacion al asunto que nos ocupa, se hace necesario que nos envie informacion mas detallada acerca del prototipo de las maquinas, su funcionamiento, la mecanica de participacion de los usuarios, todo ello en razon de que usted manifiesta que estas son maquinas de juego de destreza y video y que en su opinion tambien se les conoce como "tragamondeas", lo cual refleja una clara confusion entre la diferencia de unas y otras, circunstancia que nos obliga a requerirle diversa informacion que aqui se detalla con objeto de saber a que equipo se refiere; esto es, fotografias, descripcion y operacion de las mismas y demas elementos que a su juicio sirvan de base para la plena identificacion de estas.

El requerimiento de merito se formula a efecto de determinar si en la operacion de estas maquinas intervienen de manera directa los elementos de azar y/o apuesta, toda vez que en nuestro pais se encuentran prohibidos los juegos de azar y los juegos con apuestas... [r]azon por la cual es indispensable que nos proporcione la informacion requerida a fin de determinar lo que corresponda conforme a derecho.¹⁰⁵

88. EDM never provided Gobernacion with detailed information on its machines, information regarding their operation, the mechanism of user participation, photographs, nor any

¹⁰⁴ Statement of Claim p 82; Reply pp. 41-42.

¹⁰⁵ Letter from Rafael de Antuñano Sandoval to C. Carlos G. Gomez Alvarez Tostado, 14 December 2000 (emphasis added), Exhibit C-93.

other element that would allow Gobernacion to plainly identify the machines and evaluate their legality. All this information was requested of Mr. Gomez by Gobernacion to in light of the fact that he had stated that the machines in question were skill video game machines, also known as dollar swallowers. Gobernacion leaves no room for doubt as it pointed out that the requested information was essential in order to determine if the machines involved elements of chance and/or betting, and thus, determine the games' legality.

D. Response To The Claimant's Argument On The Government of Mexico's Bad Faith

89. In the Reply, the Claimant presents a witness statement from Mr. Navarro who states that the Director of Legal Affairs for Gobernacion filed criminal charges before the Attorney General (P.G.R.) in April 2001, regarding the closure of an EDM facility that took place on 25 February 2001. According to Mr. Navarro, that preliminary investigation was numbered No. AP 546/2001-2. Mr. Navarro also says that "[Gobernacion] filed a claim against 'EM' before the Attorney General's office and kept the case on file until October 11, 2001".¹⁰⁶

90. Mr. Navarro's statement is without merit and its purpose is none other than to confuse the Tribunal. The preliminary investigation which Mr. Navarro refers to did exist; in fact, however, it began as a result of the claim filed by Gobernacion after the closure of the Nuevo Laredo facility in October 2001. The Respondent has no knowledge of the claim that Mr. Navarro alleges was filed in April 2001.

91. In the October 11, 2001 closure of the Nuevo Laredo facility, in addition to inspectors from Gobernacion, the *Agente del Ministerio Publico de la Federacion* (hereinafter *Ministerio Publico*) also participated. As a result of this intervention, on 15 October 2001 the *Ministerio Publico* requested that Gobernacion indicate whether it was planning to bring a complaint regarding the 11 October 2001 closure of the Nuevo Laredo facility.¹⁰⁷

92. On 18 October 2001, the General Director of Legal Affairs for Gobernacion filed a claim before the *Ministerio Publico* for the probable illegal activities carried out by EDM in Nuevo Laredo at the time of the facility's closure on 11 October 2001. The claim was registered under preliminary investigation number 546/01¹⁰⁸. Therefore, the criminal suit referred to by Mr. Navarro was filed in October 2001, not in April of the same year, and was certainly not "kept" by the PGR and Gobernacion for over six months.

93. In closing the Matamoros facility on 11 October 2001, Gobernacion also filed a claim before the *Ministerio Publico* for probable illegal activities.¹⁰⁹ The claim was registered under

¹⁰⁶ Witness Statement of Javier Navarro, p. 6. Exhibit C-U.

¹⁰⁷ Letter dated 16 October, 2001. Exhibit R-113.

¹⁰⁸ See Nuevo Laredo Claim. Exhibit R-113.

¹⁰⁹ See Matamoros Claim. Exhibit R-113.

preliminary investigation number M235/01-II. With respect to the Reynosa facility closure, Gobernacion filed a claim on 18 January 2002, which was registered under preliminary investigation number A.P.320/2003-II.¹¹⁰

94. The three preliminary investigations initiated by Gobernacion's claims of probable illegal activities have followed due course and are still pending.

95. In his witness statement, Mr. Navarro also alleges that Gobernacion carried out the claims under a framework of "hostile and aggressive actions" against EDM. It was Gobernacion's duty to file the claims for criminal activity which EDM committed by carrying out activities prohibited in Mexico.

E. Thunderbird Decided to Open the Reynosa Facility Even Though The Gobernacion Administrative Proceeding Was Still Pending.

96. In his witness statement, Mr. Atallah states that even though Thunderbird had knowledge of its competitors' practice of opening facilities and filing a *juicio de amparo* in case they were closed, the company, rather than acting in the same manner, opted to seek an "authorization" from Gobernacion to operate.¹¹¹ However, it seemed to have changed its mind with respect to opening the Reynosa facility.

97. The EDM facility in Reynosa began operating in August 2001, almost two months prior to Gobernacion's issuance of its ruling concluding the administrative procedure. Thunderbird did not expect Gobernacion to rule on the legality of EDM's gaming machines and followed the same path as its competitors: opening the Reynosa facility and filing *juicios de amparos* in case they were needed.

98. On 10 August 2001, Thunderbird's Board approved the decision to open the Reynosa facility—which was named "D'Stressa" instead of "Mina de Oro", which was the name used in the other two facilities that were closed—also deciding to file an amparo should it be necessary ("asked for a motion to use its discretion in opening Reynosa even under the amparo process if that is necessary...").¹¹²

99. EDM filed two different (on 23 October 2001 and 27 December 2001) *amparo* appeals against the possible "written or verbal" inspection and closure orders that could be issued against the Reynosa facility. EDM later withdrew both appeals.

¹¹⁰ See Reynosa Claim. Exhibit R-113.

¹¹¹ See Albert Atallah witness statement, ¶ 15. Exhibit C-V.

¹¹² See Thunderbird Board Meeting Minutes from August 10, 2001, p. 4. Exhibit R-104.

III. RESPONSE TO LEGAL ARGUMENT

A. Mexico Has Accorded The Same Treatment To Investors In Like Circumstances

100. In the Statement of Defense, Mexico explained that Gobernacion, using its administrative powers, had sought to close all the facilities identified that were operating machines the same as or similar to those used by EDM. It also noted that in some cases operators of these facilities have been able to continue operating by appealing closure orders and obtaining injunctions while their legal challenges were pending. The Claimant has avoided discussing the arguments and evidence presented by Mexico in relation to the closure of facilities and injunctive relief.¹¹³

1. Gobernacion Has Taken Equivalent Action In Every Case

101. The Claimant states that Mexico has made a “False Assertion That It Has Closed Down All Similar Gaming Facilities¹¹⁴” and adds “Numerous domestic skill machine facilities remain open and operating, including Guardia’s Club 21 and the Reflejos facilities”¹¹⁵. The Tribunal should note that Mexico affirms that Gobernacion has closed all the facilities of this kind of which it has become aware; and in the case of Club 21 there is a temporary injunction that permits it to operate while the *juicio de amparo* is pending. Mexico reiterates its position and re-affirms the arguments it made in its Statement of Defense¹¹⁶.

102. In an exhibit to its Statement of Defense, the Respondent presented copies of the certificates of 17 closures executed by Gobernacion —of all the facilities of which it was aware.¹¹⁷ It explained that the owners of the facilities challenged these closures in court and, in one case, the tribunal in question granted an injunction against the closure. The Respondent submitted all the corresponding evidence¹¹⁸. Thunderbird completely ignores those arguments and documentary evidence in the Reply.

103. In most of the cases appealed, the courts dismissed the claims and, as a result, the closures became final:

¹¹³ Statement of Defense sections III.C and IV.D.3. See also Exhibits R-009 and R-031-1.

¹¹⁴ Reply p. 18. See also *id.* pp. 42 et. seq.

¹¹⁵ *Id.* at 19.

¹¹⁶ See Section VI.D of the Statement of Defense.

¹¹⁷ See Exhibit R-009. This exhibit 18 closures; two of these refer to the same facility; “Reflejos” located at Plaza Fiesta in Matamoros (Exhibit R-009-K and R-009-P).

¹¹⁸ See Section VI.D.3.a of the Statement of Defense. See also Exhibit R-031.

Cases That are Resolved Definitively				
Facility	Business name	Date of closure	File	Current Status
Makrocentro de la suerte ¹¹⁹ Cancún, Quintana Roo	Magno Operadora S.A. de C.V.	August 21, 2001	Juicio de amparo 939/01	Case dismissed. Facility closed definitely.
Macrocentro de la Suerte ¹²⁰ Nuevo Laredo, Tamps.	Magno Operadora S.A. de C.V.	August 21, 2001	Juicio de amparo 241/01	Case dismissed. Facility closed definitely.
Makrocentro de la Suerte ¹²¹ Mérida, Yucatán	Magno Operadora S.A. de C.V.	August 21, 2001	Juicio de amparo 62/01	Case dismissed. Facility closed definitely.
Makrocentro de la Suerte ¹²² Monterrey, Nuevo León	Magno Operadora S.A. de C.V.	October 11, 2001	Juicio de amparo 1440/01	Case dismissed. Facility closed definitely.
La Mina de Oro ¹²³ Nuevo Laredo, Tamp.	Entertainmen s de México, S. de R.L. de C.V.	October 11, 2001	Juicio de amparo 300/01	Case dismissed ¹²⁴ . Facility closed definitely.
Makrocentro de la Suerte ¹²⁵ Monterrey, Nuevo León	Magno Operadora S.A. de C.V.	October 11, 2001	Juicio de amparo 1453/01	Case dismissed. Facility closed definitely.
La Mina de Oro ¹²⁶ Matamoros, Tamaulipas	Entertainmen s de México, S. de R.L. de C.V.	October 11, 2001	Juicio de amparo 471/01	Case dismissed ¹²⁷ . Facility closed definitely.

¹¹⁹ Exhibit R-009-C.

¹²⁰ Exhibit R-009-D.

¹²¹ Exhibit R-009-E.

¹²² Exhibit R-009-F.

¹²³ Exhibit R-009-G.

¹²⁴ Section VI.C.1.(a) Statement of Defense.

¹²⁵ Exhibit R-009-H.

Viva Cancún and Resorts de México ¹²⁸ Interior del Centro Comercial “Gran Sur México DF	Viva Gaming & Resort de México, S.A. de C.V.	November 1, 2001	Juicio de amparo 1068/01	Case dismissed. Facility closed definitely.
D’Stressa ¹²⁹ Reynosa, Tamps.	Entertainments de México, S. de R.L. de C.V.	18 January 2002	Juicio de amparo 64/2002	Case dismissed. Facility closed definitely.
Bellavista Centro de Entretenimiento ¹³⁰ Interior del Hotel Granada Inn. San Nicolás de los Garza, Nuevo León.	Inmobiliaria Cemarza, S.A. de C.V.	March 7, 2003	Juicio de amparo 532/2003	Case dismissed. Facility closed definitely.

104. In some cases, the individuals requesting review have obtained a judicial ruling granting a temporary injunction while the principal appeal remained pending. In other cases, the courts determined that there were irregularities in the proceeding during the closure and granted *amparos* in order to remand the issue to Gobernacion to correct those errors. Gobernacion closed these facilities once again, and the parties have again challenged the actions of Gobernacion.

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¹²⁶ Exhibit R-009-I.

¹²⁷ This *juicio de amparo* was dismissed because the company withdrew its claim. See Section VI.C.2 of the Statement of Defense.

¹²⁸ Exhibit R-009-J.

¹²⁹ Exhibit C-73.

¹³⁰ Exhibit R-009-O.

Appeals Pending				
Facility	Business name	Date of closure	File	Current Status
Club 21 ¹³¹ Centro Comercial Interlomas Huixquilucan, Edo. de México	Cesta Punta Deportes, S.A. de C.V.	July 12, 2001	Juicio de amparo 545/01	Claimant was granted injunctive relief. The appeal was dismissed in first instance. The judicial ruling was appealed. The appeal is pending. ¹³²
Reflejos ¹³³ Interior 2 del local Plaza Fiesta Matamoros, Tamps.	Operación y Distribución Total, S.A de C.V.	December 14, 2001	Juicio de amparo 7/02	Amparo was granted in order to amend errors in the closing procedure ¹³⁴ .
Cesta Punta Deportes S.A. de C.V. ¹³⁵ Ciudad Juárez, Chihuahua	Cesta Punta Deportes, S.A. de C.V.	April 15, 2002	Juicio de amparo 253/02	Dismissed in first instante. The Claimant appealed the ruling ¹³⁶ . Appeal remains pending.
Reflejos ¹³⁷ Blvd. Morelos y Américo Villarreal Subancla F Interior 1 Reynosa, Tamps.	Operación y Distribución Total, S.A. de C.V.	April 29, 2003	Juicio de amparo 233/2003	Amparo was granted in order to amend errors in the closing procedure. ¹³⁸

¹³¹ Exhibit R-009-B.

¹³² Section III.A.1.a of the Rejoinder, as well as Section VI.D of the Statement of Defense.

¹³³ Exhibit R-009-K. See Section III.A.1.c. of the Rejoinder

¹³⁴ Exhibit C-96. See Section III.A.1.b of the Rejoinder

¹³⁵ Exhibit R-009-L.

¹³⁶ Section VI.D.3.a.ii. of the Statement of Defense.

Reflejos ¹³⁹ Río Bravo, Tamps.	Operación y Distribución Total, S.A. de C.V	August 28, 2003	Juicio de amparo 407/2003	Temporary injunction granted. Ruling pending ¹⁴⁰
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105. The Claimant submitted statements of notaries public which contain statements of fact to support its argument that some entities are operating with machines the same as or similar to those of EDM.¹⁴¹ The manner in which Thunderbird describes the status of certain facilities in its Reply calls for a brief explanation of the legal status of each of the ongoing appeals, which the Claimant ignores completely.

a. Club 21: Huixquilucan, Estado de México

106. In the Reply, the Claimant repeats the same allegations from the Statement of Claim regarding the facility called Club 21 in Huixquilucan, Estado de Mexico. In the Statement of Defense, the Respondent provided a lengthy explanation of the legal proceedings initiated by Cesta Punta Deportes, S.A. de C.V. against the closure of the Club 21 facility. The Respondent was very clear in explaining the legal reasons why the facility remained open. Thunderbird has simply ignored to the arguments and evidence of Mexico.¹⁴²

107. The Respondent directs the Tribunal to the discussion of Club 21 in the Statement of Defense.¹⁴³

b. Reflejos: Río Bravo

108. The Reflejos facility was closed by Gobernacion on 28 August 2003.¹⁴⁴ Operación y Distribución Total, S.A. de C.V. (hereinafter “Operación y Distribución”) filed a *juicio de*

Footnote continued from previous page

¹³⁷ Exhibit R-009-Q.

¹³⁸ Exhibit R-131.

¹³⁹ Exhibit R-009-S.

¹⁴⁰ Section III.A.1.b of the Rejoinder.

¹⁴¹ In paragraph 61 and footnote 76, the Respondent described the deficiencies in the statements of the notaries public that affect their probative value.

¹⁴² Claimant presents as Exhibit C-97 to the Reply an article from the magazine Milenio. Exhibit R-114 contains other articles regarding Gobernacion’s closures of Mr. Guardia’s facilities. This exhibit also contains newspaper articles describing other recent actions by Gobernacion enforcing the Ley Federal de Juegos y Sorteos.

¹⁴³ Cesta Punta Deportes challenged the closure of Club 21 and obtained a temporary injunction. The trial court ruled against it, but it appealed the ruling. The case continues. See Statement of Defense, Section VI.D.

amparo against that closure. The court granted a temporary injunction. Mexico has already explained that injunctive relief is not a ruling on the legality of the machines. Injunctive relief constitutes a preventive judicial measure to maintain the status quo while the merits of the appeal are decided.¹⁴⁵

c. Reflejos: Matamoros

109. In the Reply, the Claimant identifies two facilities operating “skill machines” in Matamoros. It states that one of these, called “Reflejos” in Plaza Fiesta, operates under the protection of Mexican law (“under full protection of Mexican law”) because, as the Claimant argues, it obtained a final ruling recognizing the domestic investor’s right to operate skill machines (“a final and binding determination by a Mexican court of the domestic investor’s right to operate skill machines”).¹⁴⁶

110. However, the Claimant fails to mention to the Tribunal the true state of the matter: The court did not rule that the operation of “skill machines” was legal. Rather, the judge determined that there were procedural deficiencies in the closure¹⁴⁷ and awarded the *amparo para efectos* to have Gobernacion repeat the closure procedure.¹⁴⁸

111. Lic. Alberto Alcantara states that: “the *amparo* was decided only “*para ‘efectos’*,” which means that the merits of the case were not decided, but rather, the procedural issues of how the government actions in question were carried out, which means that the authority may carry out the actions once again so long as they are in compliance with the judicial ruling. It is also necessary to explain that the basis of the ruling is the procedural violations that were found, which allows the administrative authority to act once again, if it fulfills the legal requirements to do so...”¹⁴⁹.

112. Thus, Gobernacion closed the facility again.¹⁵⁰ Operación y Distribucion a Total filed a new *juicio de amparo*. The judge granted temporary injunctive relief.¹⁵¹ The court issued the

Footnote continued from previous page

¹⁴⁴ The Respondent notes that it previously stated incorrectly that the facility was closed in October 2001. Exhibit R-009-S.

¹⁴⁵ See footnote 137 of the Statement of Defense.

¹⁴⁶ Reply at 20, line 4

¹⁴⁷ See Exhibit R-009-K.

¹⁴⁸ The ruling shows that the closure procedure was illegal “*por incumplir con la comisión de inspección que les fuera encomendada*” and concluded that “*resulta procedente conceder a la impetrante el amparo y protección de la justicia*”, also adding “*estas condiciones, por el resultado de la conclusión arribada, resulta innecesario el estudio de los demás conceptos de violación...*”. Exhibit C-96, p. 24.

¹⁴⁹ Witness Statement of Alberto Alcantara, p. 4. Exhibit R-125.

¹⁵⁰ Exhibit R-009-P.

amparo on 23 October 2003 *para efectos*.¹⁵² On 4 December 2003 Gobernacion filed an appeal against the *amparo* ruling. This appeal is still pending.

d. The Remaining Facilities Identified By The Claimant

113. In the Statement of Defense, the Respondent noted that the illegal operation of these kinds of machines very often is carried out in a clandestine manner and is an ongoing problem. The record demonstrates that Gobernacion has closed all of the facilities of which it has become aware. For example, in the Notice of Arbitration and Statement of Claim submitted on 22 August 2002, the Claimant alleged that competitors of Thunderbird continued to operate. It specifically identified entities owned by Don Bradley. Mr. Atallah subsequently informed the Board of Thunderbird that Gobernacion had closed the facilities of Don Bradley (“Don Bradley’s places were in fact shut down this week”).¹⁵³

114. In its Reply, the Claimant identifies two new facilities. One is located at Avenida Jorge del Moral s/n Colonia Lomas del Roble in the city of San Nicolás de los Garza, Nuevo León. On 7 March 2003, Gobernación closed a facility called “Bellavista Centro de Entretenimiento” located in this very location. In response to this closure, the owner, Inmobiliaria Hotelera Cemarza, S.A. de C.V., filed a *juicio de amparo*, but it subsequently withdrew and the case was dismissed. The ruling has legal effect (that is, it was not appealed and is thus binding), and with it the closure remained final.¹⁵⁴

115. Gobernacion was not aware that another facility had opened in the same location.¹⁵⁵ Similarly, it was not aware of the existence of the facility called “Reflejos” in Plaza Comercial Soriana, located on Lauro Villar in Matamoros, which the Claimant identified in the Reply.¹⁵⁶ Gobernacion has now initiated appropriate action.¹⁵⁷

Footnote continued from previous page

¹⁵¹ Exhibit R-116.

¹⁵² Id.

¹⁵³ Thunderbird Board Meeting Minutes, 2 May 2003, p. 7. Exhibit R-118. . The Respondent notes that Mr. Bradley is a shareholder of Operación y Distribución Total S.A. de C.V., a company that owns the “Reflejos” facilities. Previously Mr. Bradley had provided his services to EDM.

¹⁵⁴ Exhibit R-117. Exhibit R-009-O.

¹⁵⁵ The Claimant provided a certification carried out by a Notary Public on 3 February 2004 at the request of Mr. Carlos Gomez Alvarez Tostado, legal representative of EDM. Exhibit C-Q. Gobernacion visited the location and verified that the facility remains closed. The facility identified by the Claimant is a different facility located in the same building.

¹⁵⁶ See Reply, p. 19, line 25.

¹⁵⁷ Exhibit R-128, Exhibit R-131.

2. The Claimant Has Not Proven Discriminatory Treatment Based On Nationality

116. The Claimant argues that there is no need for Thunderbird to show that there was discrimination against EDM based on nationality¹⁵⁸. In the Statement of Defense, the Government of Mexico demonstrated that Thunderbird has not succeeded in proving that there was any discrimination against EDM, whether based on nationality or otherwise.

117. At page 46 of the Reply, the Claimant contends that there is a “three-part test of national treatment applied consistently by past NAFTA tribunals”. In fact, the single award on which Thunderbird relies for the “three part test”, *Pope & Talbot, Inc. v. Government of Canada*, has been uniformly disavowed by all three NAFTA Parties and some of its findings rejected by subsequent Chapter Eleven tribunals.¹⁵⁹

118. The Claimant asserts that the Tribunal in *Pope & Talbot* held that an intent to discriminate against an investment by virtue of its foreign nationality is not required. In a subsequent case, *The Loewen Group, Inc. and Raymond L. Loewen v. United States*, the tribunal determined 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”¹⁶⁰. The Tribunal in *Loewen* agreed with the position of the three NAFTA Parties.

119. It is also important to note the context in which the *Pope and Talbot* tribunal made its ruling. The tribunal’s concern was that the national treatment obligation could be avoided by means of treatment that appeared neutral: “*the approach proposed by the NAFTA Parties would tend to excuse discrimination that is not facially directed at foreign owned investments*”¹⁶¹. Nonetheless, in applying the standard to the specific circumstances of the case, the tribunal in fact applied the standard as described by the NAFTA Parties: the Tribunal looked for discrimination based on nationality and specifically used the word “motivation” and other phrasing connoting the drawing of distinctions between foreign and domestic investors and their investments by reasons of nationality. It determined that:

- the imposition of export controls only on lumber originating in certain provinces did not violate Article 1102, since “the decision affects over 500 Canadian owned producers precisely as it affects the Investor, *it cannot reasonably be said to be motivated by discrimination outlawed by Article 1102*”¹⁶²;

¹⁵⁸ Reply pp. 45-47.

¹⁵⁹ *Pope & Talbot, Inc. v. Government of Canada*, Award on the Merits of Phase 2, April 10, 2001.

¹⁶⁰ *The Loewen Group, Inc. and Raymond L. Loewen v. The United States*, ICSID Case No. ARB(AF)/98/3, Award dated June 26, 2003, ¶ 139.

¹⁶¹ Award Regarding Phase II On the Merits of the Dispute in the case *Pope & Talbot*, ¶ 79. .

¹⁶² Id. ¶ 87.

- the administration of the granting of export quotas to “new entrants” did not violate Article 1102, stating that this “had a reasonable nexus with the rational policy of providing for new entrants and it had *no elements of discrimination against foreign-owned producers*”;¹⁶³
- a settlement of a lumber dispute between British Columbia and the United States did not violate Article 1102, the tribunal finding that “there is no convincing evidence that it was based on *any distinction between foreign-owned and Canadian owned companies*” and in a footnote elaborating on this finding, it stated that “there is no hint that the decision ... was *motivated by the nationality of one of those users, the Investment*”¹⁶⁴.

120. In a subsequent case, *Marvin Roy Feldman Karpa v. United Mexican States*, the tribunal was similarly concerned that facially neutral treatment that had the effect of denying national treatment not escape the article’s coverage. It recognized that a State may properly draw distinctions between classes of investors (“the concept of discrimination has been defined to imply *unreasonable* distinctions between foreign and domestic investors in like circumstances”¹⁶⁵) and that the drawing of distinctions generally is not unlawful. It fully understood that the article requires an inquiry into motivation or intent to draw unreasonable distinctions.

121. Like the *Pope & Talbot* tribunal, when the majority of the tribunal in *Feldman* applied the national treatment test, it looked for the existence of discrimination motivated by the nationality of the investor.¹⁶⁶

122. When carefully analyzed, therefore, and contrary to the Claimant’s assertion, the decided cases agree with the three NAFTA Parties’ interpretation that Article 1102 prohibits action that is motivated by nationality-based discrimination. When a measure is facially neutral and motivation is unclear, the analysis is focused on the elements that permit it to determine if less favorable treatment can be explained by an illegitimate distinction between nationals and foreigners.

3. EDM Is Not in Like Circumstances To Closed Facilities That Obtained Temporary Court Injunctions Of The Closures

123. The Claimant insists that Mexico has permitted Mexican nationals to continue to operate facilities with machines similar or identical to those of EDM. It states “*the bottom line, under*

¹⁶³ Id. ¶ 93.

¹⁶⁴ Id. ¶ 103 and footnote 86.

¹⁶⁵ *Marvin Roy Feldman Karpa v. United Mexican States*, ICSID Case No. ARD(AF)/99/1 Award, December 16, 2002, ¶ 170 (emphasis in original).

¹⁶⁶ Id. ¶¶ 174, 175, and 180.

1102, is that some local businesses, operating in like circumstances, are open today while Thunderbird's EDMs are not.”¹⁶⁷ Thunderbird argues that this is sufficient to prove a violation of Article 1102.

124. As Mexico has already explained¹⁶⁸, Gobernacion has closed all those businesses in which it detected the operation of illegal gaming machines, including those of EDM. The majority have filed appeals against these closures and some have obtained a temporary injunction to continue in business, at least on a temporary basis, while their court appeals are pending.

125. However, EDM is not in “like circumstances” with those other facilities, as even if it filed *juicios de amparo*, it was not granted injunctive relief¹⁶⁹. For example, in the case of Nuevo Laredo, the *juicio de amparo* was decided against EDM in a definitive manner; in the cases of the Reynosa and Matamoros facilities, EDM withdrew its appeals.

126. Thunderbird has not presented any evidence that proves that the decision of EDM to withdraw from the domestic judicial proceedings can be attributed to the Government of Mexico. In light of the rulings issued by domestic courts against EDM, and the fact that EDM withdrew from other appeals, Thunderbird has no basis to argue that Mexico did not fulfill its obligations under Article 1102.

127. Because the Statement of Defense demonstrated that EDM is not in like circumstances to the other entities operating “skill machines” to which it wants to be compared, in the Reply Thunderbird attempts to justify the withdrawal of EDM’s claims in domestic judicial procedures arguing that it would have been “futile” to continue “given evidence that these processes would not being [sic] conducted fairly” and that Thunderbird decided instead to “choose the remedies available under the NAFTA instead of those available under domestic law”¹⁷⁰. This justification fails.

128. Thunderbird uses the witness statement of Lic. Navarro to support its argument that there were “political factors” and “proof” that the proceedings would not be conducted fairly. Nonetheless, Sr. Navarro does not refer to “political factors” nor does he state that the proceedings were not conducted fairly. He states:

[EM] asked us to withdraw from the Amparos presented by its businesses located in the cities of Nuevo Laredo, Matamoros and Reynosa, Tamps., to comply with the requirements of the Free Trade

¹⁶⁷ Reply p. 49.

¹⁶⁸ See section III.A.1 of the Rejoinder.

¹⁶⁹ On two occasions EDM was granted a temporary injunction, however, this ruling was reversed after an appeal filed by Gobernación.

¹⁷⁰ Reply at 47.

Agreement and present an arbitral claim against the Mexican Government.¹⁷¹

129. There is no evidence that the Mexican courts acted in an incorrect or unfair manner – Thunderbird has not even alleged this. In fact, other tribunals –including appellate tribunals – located in various places, ruled unanimously against EDM, in accordance with the governing law¹⁷².

130. On the other hand, as already explained in the Statement of Defense,¹⁷³ NAFTA Article 1121 provides that a disputing investor must waive domestic judicial proceedings to file a NAFTA claim, “except for proceedings for injunctive, declaratory or other extraordinary relief, not involving the payment of damages.” The Claimant itself acknowledges that Article 1121 “provides investors with the option of simultaneously seeking ... injunctive relief in a domestic court”¹⁷⁴. *Juicios de amparo* are declarative proceedings, as their purpose is to rule on the legality of the authority’s actions – they may also include injunctive measures. They are not proceedings for damages. Thus, the Claimant cannot argue it was a “necessary prerequisite” to waive these proceedings to bring a claim under NAFTA Chapter Eleven.

131. The Claimant refers to Mexico’s objections in *Waste Management, Inc. v United Mexican States*¹⁷⁵ with respect to Article 1121 and the proceedings that company brought in the domestic courts. It incorrectly argues that the Government of Mexico “was possessed of a far different opinion of Article 1121 only a short time ago.”¹⁷⁶

132. In fact, the tribunal’s award in *Waste Management* is clear that the three domestic judicial claims that Waste Management, Inc. brought were: (i) “a claim for a monetary sum plus damages for non-payment of invoices;” (ii) a claim “for breach of payment of certain invoices;” and (iii) one “claiming damages for non-payment of services.”¹⁷⁷ All the proceedings brought in the domestic were for damages for which the waiver required by Article 1121 of the treaty was required. Mexico’s position in *Waste Management* does not contradicts its position in this case.

¹⁷¹ Exhibit C-U pp.10 and 11.

¹⁷². Both the *Amparo* tribunals as well as the Federal Tax and Administrative Court (*Tribunal de Justicia Federal y Administrativa*) dismissed the claims brought by EDM because EDM simultaneously filed a *juicio de amparo* and a claim for nullification against the same acts and for the same grievances. Mexican jurisprudence confirms that this is not admissible.

¹⁷³ Statement of Defense, p. 58.

¹⁷⁴ Reply p. 48.

¹⁷⁵ ICSID Case No. ARB(AF)/99/2.

¹⁷⁶ Reply p. 47, footnote 24.

¹⁷⁷ Award dated 2 June 2000, ¶ 25.

133. The Claimant's argument regarding some of the facilities operating under injunctive relief has several deficiencies. The Claimant limits itself to pointing out that some facilities currently operate machines similar or identical to those used by EDM. However, as previously explained, the Claimant does not respond to the Mexico's arguments and evidence that demonstrates some these facilities have been granted injunctive relief as a precautionary measure while their appeals are pending. The Claimant also ignores Mexico's arguments regarding the decisions of domestic courts against the Nuevo Laredo facility, resulting in the closure order remaining in place, in addition to the fact that EDM was not granted an injunction in those cases.

134. Therefore, it is clear that EDM is not in like circumstances to other facilities that have been granted temporary injunctions that temporarily suspended the closure orders. It should also be noted that it was EDM that defined its own procedural strategies and decided to simultaneously file incompatible appeals, as well as to later withdraw from the proceedings it had initiated.

B. The Claimant Has Not Identified Any Violation Of Article 1105

135. In the Statement of Defense, the Respondent provided a legal opinion regarding the Mexican law governing administrative procedures, prepared by Dr. Jose María Serna de la Garza¹⁷⁸. It should be noted that in the Reply, the Claimant makes no reference at all to that opinion.

136. The Claimant's response is focused on the completely ancillary question, the presence of Lic. Humberto Aguilar Coronado at the 10 July 2001 administrative hearing. The Claimant argues extensively and has presented numerous witness statements to try to establish that the Respondent has made a "false representation" that Lic. Aguilar Coronado was present at, and presided over, the hearing¹⁷⁹.

137. In the Statement of Defense, the Respondent stated that Mr. Aguilar Coronado presided over the administrative hearing, which remains true, even if he was not present.¹⁸⁰ According to the applicable law, it was the duty of the then *Direccion General de Gobierno* of Gobernacion to supervise, execute and authorize acts implementing the *Ley Federal de Juegos y Sorteos* and related applicable authority. As a result, the *Director General de Gobierno* was the official responsible for handling the various issues that were the responsibility of the administrative directorate under his supervision, although he was obviously assisted by several other administrative units assigned to that office, which were composed of different government officials of different rank. The *Direccion General de Gobierno* also received support from other branches of Gobernacion, for example, the legal advisory area then called *Direccion General de Asuntos Juridicos*.

¹⁷⁸ Exhibit R-054.

¹⁷⁹ Reply p. 14.

¹⁸⁰ Statement of Defense pp. 125 and 126

138. In this manner, Lic. Aguilar Coronado formally presided over the hearing, even if he was not present. Lic. Alberto Alcántara testifies that this is “a common and valid practice.”¹⁸¹ Mr. Alcántara participated in the hearing and in effect, was the individual who conducted the proceeding.¹⁸² Therefore, it is irrelevant that Mr. Aguilar Coronado was not present. In fact, EDM’s legal representative, Lic. Luis Ruiz de Velasco, who attended the hearing, signed the certificate of the hearing without declaring in any way that the absence of Mr. Aguilar Coronado was an irregularity, notwithstanding that the certificate clearly indicates that he presided over the hearing. Even more, EDM did not challenge these facts, even in the *juicios de amparo* and nullification it filed against the closure orders.

139. The Claimant persists in its claim regarding the alleged treatment received from Sr. Guadalupe Vargas and his alleged attitude during the hearing.¹⁸³ The Respondent reiterates that Mr. Vargas’ participation in the administrative proceedings was very limited¹⁸⁴. Mr. Alcántara denies that Mr. Vargas had the attitude described by the Claimant. In any event, the 10 October 2001 ruling contains a detailed legal analysis supporting the decision, carried out under the responsibility of Lic. Aguilar Coronado, who issued the ruling. Sr. Vargas did not issue the ruling.

1. There Is No Claim of Denial of Justice Attributable to the Mexican Courts

140. The Claimant admits that “[i]n this case, the measures at issue arise from the decisions of SEGOB officials, rather than those of a Mexican court.”¹⁸⁵ As discussed above, Mr. Navarro’s witness statement is directed at the purported conduct of Gobernacion. He does not mention any irregularities committed on the part of the Mexican courts. Specifically, he stated:

EM considered that SEGOB’s conduct consisted of a treatment unequal to that with Mexican investors because, contrary to how it conducted itself with them, in the Mexican Republic there are several adult entertainment centers with skill machines THAT OPERATE IN A MANNER IDENTICAL TO EDM’S MACHINES, that have not been closed down and sanctioned [resulting in the instruction to withdraw].¹⁸⁶

¹⁸¹ Second Witness Statement of Alberto Alcántara. Exhibit R-125.

¹⁸² Id.

¹⁸³ Reply p. 4.

¹⁸⁴ Statement of Defense p. 126. Sr. Vargas only had an active role in the first inspection and closure of Nuevo Laredo. Although he was present at the 10 July 2001 hearing, it was Lic. Alcantara who had the corresponding responsibility to conduct the proceeding. See also second witness statement of Alberto Alcantara, p. 1. Exhibit R-125.

¹⁸⁵ Reply p. 48, footnote 25.

¹⁸⁶ Witness statement of Javier Navarro, p. 10. Exhibit C-U.

141. Gobernación, the competent authority in this area, has been consistent in its interpretation that the *Ley Federal de Juegos y Sorteos* prohibits the gaming activities in question, as it concerns games that involve chance and games that involve betting. Gobernación has consistently closed down every facility of which it has become aware operated these type of games. Mexican courts have dismissed a majority of the *amparos* filed by these individuals against the closure orders; in two other cases the courts determined that the appropriate procedural closure requirements were not met by Gobernación, and thus, granted the *amparo* in order to reopen the case so that Gobernación could correct these procedural errors; and there are other cases in which the *amparos* have even been resolved. To this date, no court has ruled against Gobernación's interpretation of the law. Therefore, the only legal opinion on this issue is that of Gobernación. The Mexican courts have not overruled it, therefore, its position remains legally valid.¹⁸⁷

142. In the specific case of EDM, it is clear that the company simultaneously claim the same violations with respect to the same actions before different courts. It followed this strategy with respect to the closure of the Nuevo Laredo facility. The courts (both the *amparo* court as well as the court of nullity) ruled on the basis of clear legal provisions in accordance with the law. In the case of Nuevo Laredo, the *juicio de amparo* proceeded to the final stage. It was decided against EDM. The nullification proceeding was decided against EDM, which appealed with an *amparo* against the *Tribunal Federal de Justicia Fiscal y Administrativa*, but EDM withdrew it. In the cases of Reynosa and Matamoros, EDM also brought *juicio de amparo* for the closure of these facilities, but it withdrew before the trial courts ruled.

143. Thunderbird claims that the Mexican judicial system is “rudimentary” and suggests that it cannot provide fair and equitable treatment. However, setting aside the unfounded and coarse use of adjectives, the fact remains that the Claimant has not proven that the Mexican courts acted in an unfair, irregular or arbitrary manner. In fact, the Claimant does not even allege this.¹⁸⁸

2. The Claimant Did Not Challenge the Official Acts Concerning the Administrative Hearing

144. The Claimant alleges that it suffered an administrative denial of justice. However, the Claimant fails to address the full Gobernación administrative determination and it does not respond to the arguments presented at pages 60 to 64 of the Statement of Defense nor to Dr. Jose Maria Serna's expert legal opinion presented by Mexico. In light of the precise description of the administrative proceeding provided by Mexico, as well as the detailed explanation of the legal analysis contained in the ruling dated 10 October 2001 that supports the decision to close the EDM facilities, the Claimant has no argument other than to resort to simple labeling: accusing the administrative hearing of being a “farce”, the behavior of Gobernación officials as “manifestly arbitrary”, an “absurd” evaluation of the evidence presented, etc.

¹⁸⁷ See *Robert Azininan et al v. United Mexican States*, ICSID case no. ARB (AF)/97/2, Award 1, November 1, 1999, ¶ 78.

¹⁸⁸ See Statement of Defense, section VII.C.3.

145. However, Thunderbird's claims have no basis. It should be noted that, despite the complaints it now expresses with respect to the manner in which the administrative hearing was conducted, EDM did not file appeals to challenge Gobernacion's actions during the hearing. Lic. Ruiz de Velasco signed the certificate of the hearing, without claiming that there was any irregularity. Even more, when EDM filed a *juicio de amparo* to appeal the closure orders, it did not take issue with the actions taken during the hearing. As previously noted, the supposed irregularities to which Lic. Navarro alludes to relate to Gobernacion's actions in inspecting and closing the facilities, not to the prior administrative proceeding.

146. It is clear that when a denial of justice on the part of the State is claimed, the entire justice system must be examined.¹⁸⁹ Mexican law provides a means of defense and review against the actions taken by administrative authorities. Those measures of defense were available and, in fact, EDM utilized them. However, it did not challenge the actions that are the subject of this claim.

147. As a result, the claim simply has no basis. It should be dismissed.

3. The Claimant Cites Sources Out of Context

148. The Claimant's conclusions regarding the minimum standard of treatment under customary international law fail to properly examine the context of the cases that it cites. The Claimant proposes an broad standard of treatment and refers to the tribunal awards from the following cases: *Alex Genin, Eastern Credit Limited, Inc. and A.S. Baltoil v. The Republic of Estonia, Mondev International Ltd. v. United States of America*, and *ADF Group, Inc. v. United States of America* (although it acknowledges that in each case the tribunals rejected claims that there had been a breach of the minimum standard).¹⁹⁰

149. The Claimant also ignores the decision of a Chamber of the International Court of Justice in the *Case Concerning Elettronica Sicula S.P.A. (ELSI)*¹⁹¹. At issue in that case was whether the Mayor of Palermo's requisition of a factory – which was later held by a domestic court to be an excess of power at Italian law – amounted to an arbitrary act at international law. The Chamber stated:

128. *Arbitrariness is not so much something opposed to a rule of law, as something opposed to the rule of law. This idea was expressed by the Court in the Asylum case, when it spoke of "arbitrary action" being "substituted for the rule of law" (Asylum, Judgment, I.C.J. Reports 1950, p. 284). It is a willful disregard of due process of law, an act which shocks, or at least surprises, a sense of judicial propriety....*

¹⁸⁹. See generally *Loewen Award*, op cit.

¹⁹⁰ Reply pp. 50-54.

¹⁹¹. 1989 I.C.J. 15.

150. Even though the Mayor's actions were later found by the Italian courts to have been illegal under Italian law, the Court found that they were not arbitrary at international law. The ELSI case has been cited with approval by NAFTA tribunals.¹⁹²

151. The Claimant states that the EDM facilities were "inexplicably closed" and that "the results of the [administrative] hearing were shockingly arbitrary".¹⁹³ It bases on this its arguments of "manifest arbitrariness" contained at pages 60 – 63 of the Reply, which, notwithstanding, still lack any analysis. The Claimant once again resorts to mere labelings.

152. The evidence shows that Gobernacion carried out its actions in compliance with the laws that regulate administrative procedures¹⁹⁴ and based its decision on a detailed analysis of the facts, evidence, and the applicable law. Therefore, Gobernacion's actions were reasonable and predictable.

153. The Claimant also claims "detrimental reliance" on the 15 August 2000 Gobernacion letter. That argument is based on the – now disclaimed – factual premise that the 15 August 2000 Gobernacion letter represented some type of permit for specific activities or machines, rather than a general statement of the law based on the description set out by EDM of the machines in its August 3 solicitude. The Government of Mexico has already refuted that factual claim, and in addition the Claimant has admitted in the Reply that Gobernacion's letter was not a permit or authorization.

154. The Claimant argues that Gobernacion was "estopped" from finding that the machines were illegal. It should be noted that the term "estoppel" has a particular meaning in international law, which is shared by the municipal courts on matters involving the interpretation of domestic law. Namely, that the doctrine of estoppel is related to the determination of facts, not questions of law.

155. Professor Brownlie cites Professor Bowett on this subject in his Principles of Public International Law:

Professor Bowett has stated the essentials to be: (1) a statement of fact which is clear and unambiguous; (2) the statement must be voluntary, unconditional, and authorized; and (3) there must be reliance in good

¹⁹² Award of the Tribunal in *ADF*, ¶ 190. Award in *Mondev*, ¶ 108. The *Mondev* Tribunal cited Mexico's submission under Article 1128 with respect to the *ELSI* case and the concept of arbitrariness. It stated: "*The key point is that the Chamber accorded deference to the respondent's legal system in applying the standard, finding that even though the mayor's act of requisitioning the factory at issue in the case was unlawful at Italian law as an excess of power, mere illegality did not equate to arbitrariness at international law.*"

¹⁹³ Reply p. 62.

¹⁹⁴ Expert legal opinion, Dr. José María Serna. Exhibit R-054.

faith upon the statement or to the advantage of the party so relying on the statement.¹⁹⁵

[Emphasis added]

156. Brownlie continues with the cite to Bowett:

It is now reasonably clear that the essence of estoppel is the element of conduct which causes the other party, in reliance on such conduct, detrimentally to change its position or to suffer some prejudice. Without dissenting from this as a general and preliminary proposition, it is necessary to point out that estoppel in municipal law is regarded with great caution, and that the ‘principle’ has no particular coherence in international law, its incidence and effects not being uniform¹⁹⁶.

[Emphasis added]

157. The Gobernacion letter was not an opinion of fact that can give rise to an estoppel as described by Professor Bowett. Moreover, as the tribunal in *Feldman* recognized, an estoppel/reliance argument is inapposite when, as here, Gobernacion has interpreted and applied the law in a uniform manner, prohibiting these types of machines in every case. In addition, the Claimant was well aware of Gobernacion’s position with regards to this kind of business prior to EDM’s initiation of operations. The Claimant stated in its Statement of Claim that it was aware that Gobernacion’s position had led to a “significant legal altercation” between Gobernacion and Sr. Guardia with respect to the operation of facilities with “skill games.”¹⁹⁷

¹⁹⁵ Brownlie, Ian, *Principles of Public International Law*, (5th ed.), USA: Oxford University Press, 1998, p. 646.

¹⁹⁶ Id.

¹⁹⁷ In *Feldman* the tribunal noted:

148. The facts and the reasonableness of the Claimant’s reliance in *Metalclad*, are thus quite different from the instant case. The assurances received by the investor from the Mexican government in *Metalclad* were definitive, unambiguous and repeated, in stating that the federal government has the authority to authorize construction and operation of hazardous waste landfills, and that Metalclad had obtained all necessary federal permits and other permits for the facility... Nor is there any indication that the assurances received by Metalclad, despite some ambiguities, were inconsistent with Mexican law on its face. Finally, Metalclad was deprived of all beneficial use of its property, which was incorporated into an ‘ecological reserve’.

149. In contrast, in the present case, the Mexican government essentially opposed the Claimant’s business activities at every step of the way, notwithstanding a few periods when the rebates were granted. Also, in the present case the assurances allegedly relied on by the Claimant (which assurances are disputed by Mexico) were at best ambiguous and largely informal (since the Claimant never sought a formal written tax ruling on the Article 4 issue, or litigated the issue until 1998)...

Feldman Award at ¶¶ 148 and 149.

C. There Is No Cognizable Property Interest That Can Be Recognized

158. The Claimant now agrees with the Respondent that Mexico “*need not pay compensation for effectively neutralizing an unlawful business undertaking*”¹⁹⁸. It claims, however, that Thunderbird had an “acquired right” allowing EDM to use its machines without government interference, based on “*detrimental reliance*” on the 15 August 2000 letter. As Mexico stated in paragraphs 242-252 of the Statement of Defense, it is the Mexican legal system that defines the applicable rights. As a result, Gobernacion’s letter either does or does not establish a right to operate the machines. The alleged existence of a reasonable expectation cannot create rights where these do not exist under the local law. The absence of these reasonable expectations, as in this case, prevents an investor from claiming on the international plane that its rights have been violated.

159. The Respondent has explained at length the reasons why Thunderbird could not have had a reasonable expectation that EDM would be allowed to operate the machines in question.¹⁹⁹ However, another significant inconsistency that refutes its position should also be noted: the Claimant has explained that it was well aware that Gobernacion has closed the facilities of other operators, such as Sr. Guardia, and that they had filed legal challenges resulting in what the Claimant itself called a “significant legal altercation”. In fact, the totality of the claim for a violation of Article 1102 is based on the fact that the machines used by those operators are the same as those of EDM. How then could Thunderbird reasonably expect that Gobernacion would permit the EDM operation when it knew that it had prohibited “identical” operations of other facilities and that it was vigorously defending its position in the national courts to the degree that it found itself in a “significant legal altercation” with those operators?

160. With respect to the application of Article 1110, the Claimant argues that its claim and the *Feldman* claim are different because Feldman “never sought out the advice of Mexican officials, in order to confirm whether it properly qualified for the tax rebates that it would later be denied.”²⁰⁰ In fact, Feldman argued that, based on discussions with various officials, he actually did obtain an assurance that he could conduct his operations and obtain tax refunds.²⁰¹ It should not be overlooked EDM submitted the 3 August 2000 solicitude in an ambiguous manner - to say the least- especially when it knew that Gobernacion had prohibited the exact same operations and closed those facilities. If EDM desired to obtain a precise response from Gobernacion, it would have been sufficient for it to state in its solicitude that it intended to operate – indeed, that it was operating – machines “identical” to those of the contested facilities of Sr. Guardia.

161. The Claimant’s argument regarding detrimental reliance on the 15 August 2000 letter is simply not credible.

¹⁹⁸ Reply p 65.

¹⁹⁹ See Statement of Defense pp. 31-34.

²⁰⁰ Reply, p. 65.

²⁰¹ *Feldman*, Arbitral Award ¶ 18.

D. Jurisdictional Objection: Thunderbird’s Failure To Bring A Claim On Its Own Behalf Under Article 1116 Precludes It From Obtaining Compensation Under Article 1110

162. Regarding its failure to bring a claim on behalf of itself under Article 1116 (as opposed to the claim it brought under Article 1117 purportedly on behalf of EDM), the Claimant makes several arguments that are not clearly linked. First, it states that “a breach of Article 1110 will also constitute a breach of Article 1105, as a matter of simple logic.”²⁰² To the contrary, the Free Trade Commission issued a binding interpretation on 31 July 2001 that states that “[a] determination that there has been a breach of another provision of the NAFTA ... does not establish that there has been a violation of Article 1105(1).” Accordingly, on that basis alone, a breach of Article 1105 cannot be based on a breach of Article 1110.²⁰³

163. The Claimant also argues that Article 1110 is actually irrelevant on the theory that customary international law forbids expropriations without prompt, adequate and effective compensation, and “it accordingly does not matter whether Article 1110 exists.”²⁰⁴ It is unclear why the Claimant believes this argument advances its position that it is entitled to bring a claim under Article 1110.

164. Finally, the Claimant argues that because the definition of “investment” extends to objects that are not “enterprises,” the Claimant should be allowed to bring a claim on behalf of EDM for an alleged violation of Article 1110.²⁰⁵ In making this argument, the Claimant misinterprets this legal provision. Article 1110 imposes an obligation on the NAFTA Parties not to expropriate “an investment of an investor of another Party in its territory” without complying with the requirements set out therein. EDM is not an “investor of another Party,” and therefore Article 1110 does not impose an obligation on the Government of Mexico vis-à-vis EDM. In other words, Thunderbird cannot bring a claim on behalf of EDM for an alleged expropriation of EDM, or an alleged expropriation of any property interests of EDM.

165. It is important to note in this regard the distinction between Articles 1116 and 1117. Section B of Chapter Eleven permits international claims to be made only in circumstances of alleged violations of Section A of that Chapter. Consistent with long-standing rules of customary international law, Chapter Eleven does not permit an enterprise of a Party to commence an international claim against its own Party. Article 1117(4) states in this regard that: “An investment may not make a claim under this Section.”

166. Article 1117 differs from customary international law in that it permits a foreign investor to bring a derivative claim in the name of an enterprise that is a “juridical person” of the

²⁰² Reply, p. 66.

²⁰³ Statement of Defense, pp. 60-61.

²⁰⁴ Reply p. 67.

²⁰⁵ Reply pp. 67-69.

respondent State in respect of certain provisions of Chapter Eleven. Obligations owed to “investments” (as distinguished from “investors”) are set out in Articles 1102(2), 1103(2), 1105, and 1107. Thunderbird chose to present its claim exclusively as a derivative claim on behalf of EDM, and not to bring a claim in its own name as an investor.

167. The derivative nature of the claim must be maintained throughout the arbitration and be reflected in any relief that might be awarded by a tribunal. For example, Article 1135(2) requires that, in the event of a successful claim on behalf of the enterprise, restitution or damages must be “paid to the enterprise”. It also requires that the arbitral award “shall provide that it is without prejudice to any right that any person may have in the relief under applicable law”.²⁰⁶ This provision recognizes the enterprise and its legal relations as different entities. Paragraph 2 of Article 1117 is designed to ensure that the enterprise’s creditors, for example, are able to make a claim in respect of any damages that might be awarded to the enterprise under Article 1117.²⁰⁷ The Tribunal lacks authority to disregard the language of Chapter Eleven and to re-construe an Article 1117 claim as one brought under Article 1116.

168. Finally, in apparent recognition that its foregoing arguments are unsustainable, the Claimant seeks to amend its claim to include an allegation of a violation of Article 1110 on its own behalf as an investor of a Party under Article 1116. The Claimant’s suggestion that it be allowed to amend its claim at this extremely late date is simply unacceptable.

169. If the Tribunal were to decide to allow the claim of the Claimant under Article 1116, and if it decides it decides to award compensation under Article 1110, any evaluation of damages must be limited exclusively to Thunderbird’s own alleged investment in EDM.

IV. RESPONSE TO CALCULATION OF ALLEGED DAMAGES

A. Introduction

170. The following submissions are made without prejudice to Mexico’s defense to the claim on liability and its objections to jurisdiction.

171. The Claimant has failed to reply to the Respondent’s defense to the claim for damages. The Reply mis-describes Mexico’s legal arguments and fails to respond to the evidence and arguments presented on the facts.

172. The only evidence presented by the Claimant in response to Mexico’s defense to the claim for damages is in the second witness statement of Booker T. Copeland III.²⁰⁸ There is no reply report from the Claimant’s damages expert, The Innovation Group. Mexico will

²⁰⁶ NAFTA Article 1117(2).

²⁰⁷ No such provision is made for an Article 1116 claim because the legal interests being asserted differ from those of the enterprise.

²⁰⁸ See Exhibit C-W.

demonstrate below that Mr. Copeland’s main contention – that the audited financial statements of the EDM companies should not be used to project future profitability because they might be biased – is without merit.

B. Mexico’s Defenses on the Law

173. The Respondent’s analysis of damages is based on the ordinary meaning of Articles 1117 and 1110(2) and jurisprudence applicable to NAFTA. For the sake of certainty, Mexico confirms that it relies solely on the above.²⁰⁹

174. As to the interpretation of Article 1110(2), Mexico continues to agree with the observations of the *Metalclad* tribunal:

118. With respect to expropriation, NAFTA, Article 1110(2), specifically requires compensation to be equivalent to the fair market value of the expropriated investment immediately before the expropriation took place. This paragraph further states that the “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”

119. Normally, the fair market value of a going concern which has a history of profitable operation may be based on an estimate of future profits subject to a discounted cash flow analysis. *Benvenuti and Bonfant Srl v. The Government of the People’s Republic of Congo*, 1 ICSID Reports 330; 21 I.L.M. 758; *AGIP v. The Government of the People’s Republic of Congo*, 1 ICSID Reports 306.

120. However, where the enterprise has not operated for a sufficiently long time to establish a performance record, or where it has failed to make a profit, future profits cannot be used to determine the going concern or fair market value. In *Sola Tiles, Inc v. Iran* (1987) Iran-U.S.C.T.R. 224, 240-42; I.L.R. 460, 480-81, the Iran-U.S. claims Tribunal pointed to the importance in relation to a company’s value of “its business reputation and the relationship it has established with its suppliers and customers”. Similarly, in *Asian Agricultural Products v. Sri Lanka* (4 ICSID Reports 246 (1990) at 292) another Tribunal observed, in dealing with the comparable problem of the assessment of the value of goodwill, that its ascertainment “requires the prior presence on the market for at least two or three years, which is the minimum period needed to establish continuing business connections”.²¹⁰

175. As to the claims for damages arising from alleged breaches of Article 1102 and Article 1105, Mexico continues to agree with the observations of the *Feldman* tribunal:

²⁰⁹ Statement of Defense, ¶¶ 318-325.

²¹⁰ Award, August 30, 2000, at ¶¶ 118-120.

194. ...NAFTA provides no further guidance as to the proper measure of damages or compensation for situations that do not fall under Article 1110 (expropriation); the only detailed measure of damages provided in Chapter 11 is in Article 1110(2-3), “fair market value,” which necessarily applies only to situations that fall within that Article 1110. It follows that, in the case of discrimination that constitutes a breach of Article 1102, what is owed by the responding Party is the amount of loss or damage that is adequately connected to the breach. In the absence of discrimination that also constitutes indirect expropriation or is tantamount to expropriation, a claimant would not be entitled to the full market value of the investment which is granted by NAFTA Article 1110. Thus, if loss or damage is the requirement for the submission of a claim, it arguably follows that the tribunal may direct compensation in the amount of the loss or damage actually incurred.²¹¹

176. Mexico also continues to agree with the tribunal in *S.D. Myers*, that:

...damages may only be awarded to the extent that there is a sufficient causal link between the breach of a specific NAFTA provision and the loss sustained by the investor. Other ways of expressing the same concept might be that the harm must not be too remote, or that the breach of the specific NAFTA provision must be the proximate cause of the harm.²¹²

177. Thunderbird misquotes a passage from the Award in *Metalclad*. Thunderbird states in the Reply:

And unlike what took place in *Metalclad* – where the Tribunal stated that a DCF analysis would be inappropriate because “the property’s future profits were so dependent on as yet unobtained preferential treatment from the government that any prediction would be speculative” – Thunderbird officials did obtain assurances from SEGOB officials which confirmed to them that their proposed businesses could operate as profitably as they had planned.²¹³

[Emphasis in the original, footnote omitted.]

178. In the *Metalclad* Award, the quoted passage actually refers to the *Phelps Dodge Corp. et al. v. The Islamic Republic of Iran* case, where the tribunal held “the property’s future profits were so dependent on as yet unobtained preferential treatment”. The *Metalclad* tribunal cited *Biloune v. Ghana Investments Centre* as a similar case to that before it, where the investment at issue had never gone into operation. Moreover, the contention that Thunderbird officials

²¹¹ Award, December 16, 2002, at ¶194.

²¹² Second Partial Award, 21 October 2002, at ¶ 140.

²¹³ Reply at p. 72, lines 20-21.

obtained assurances from Gobernacion lacks evidentiary support. The Claimant has not adduced any evidence to prove that Mexican government officials might have provided any assurance that the EDM businesses could operate at all, let alone “operate as profitably as they had planned”²¹⁴.

179. Mexico submits that only the “going concern value” of a business, based on discounted cash flow, can be used as a valuation criterion where the enterprise in question has a sufficient track record of profitable operations, which applicable jurisprudence suggests requires a minimum period of two to three years (the Matamoros facility, which was in business the longest, was only open for 13 months). If there is such a history of operations, it must be used. It is not permissible to make projections based on an increase in earnings and the reduction of operation costs.

180. The Respondent does not believe that the remarks of Rosalyn Higgins, cited in the Reply, accurately describe the measure of indemnification under Article 1110(2). However, it is notable that even Rosalyn Higgins would remark that a discounted cash flow valuation is based on “the purchaser’s estimate of unspeculative profits...”²¹⁵

181. The Award of the Tribunal in *S.D. Myers*, also cited in the Reply, supports Mexico’s position in the sense that in international arbitration, the award of damages cannot be based on speculative profits.²¹⁶ A full review of the facts²¹⁷ will reveal that S.D. Myers, Inc. (SDMI) had been “an industry leader in the remediation of PCB-contaminated waste material in the USA”²¹⁸ for several years when it obtained permission from the United States to import PCB waste from Canada for destruction at its facility in Ohio. It also had “an excellent record of profitability, and an outstanding record of passing audits by regulators and customers”²¹⁹ when Canada imposed an export ban on PCBs waste that remained in place for 14 months.

182. With the assistance of its Canadian affiliate, Myers Canada, SDMI had secured 107 orders and 833 bids and quotes having a total value of CAN\$104 million²²⁰ which it was ready to perform but for the export ban. To determine the damages, the tribunal carefully assessed the number of contracts that would have been performed had the export ban not been adopted, taking suitable reductions for likely price degradation and other effects of competition, even when

²¹⁴ Id., p. 72, lines 21-22.

²¹⁵ Id., p. 71.

²¹⁶ Indeed, the *S.D. Myers* tribunal expressly cautioned against the use of speculative profits as a measure of compensation. Second Partial Award, ¶¶ 156 and 173.

²¹⁷ Id., at pp. 17-19, and 41-73.

²¹⁸ Id., at ¶ 83.

²¹⁹ Id., at ¶ 181.

²²⁰ These prospective Canadian customers had a legal obligation to either store or dispose of their stockpiles of PCB waste as set forth in the prevailing environmental laws and regulations. They were motivated to dispose of their PCB’s when the opportunity presented itself. Id., ¶ 198.

SDMI was found to have had significant timing advantages over its American competitors and a substantial price and location advantage over its Canadian competitors²²¹. The assessment of SDMI's lost stream of net earnings was based on SDMI's historical cost of sales for providing precisely the same services to its U.S. customers over a number of years.²²² Finally, the tribunal awarded slightly more than CAN\$6 million on SDMI's orders, bids and quotes of CAN\$104 million²²³.

183. The circumstances of the Claimant's gaming operations in Mexico were markedly different. They were in business only a short time (Matamoros 13 months, Nuevo Laredo 8 months and Reynosa less than 5 months), never earned a profit, and they carried on business (speaking most charitably) on the margins of the law.²²⁴ Thunderbird itself had a history of losses and had never paid a dividend.

184. The Claimant does not seek compensation based on the historical performance of any of the three facilities during the time that they operated. It seeks an award ranging from US\$24 million to US\$175 million based on massive projected revenue increases and assumed reductions in operating costs, unaffected by legislative or regulatory change or competition from other similar operators.

185. Based on the ordinary meaning of Article 1110(2) and the NAFTA jurisprudence, Mexico maintains that: (i) either the three facilities did not have sufficient track record to allow a discounted cash flow assessment of going concern value, or (ii) they did have a sufficient track record which can and should be used. What the Claimant cannot do is base a valuation on an imaginary track record that it wished it had, or rely on speculation as to enhanced profitability in the future.

186. As to the claims based on alleged breaches of Articles 1102 and 1105, the Claimant contends that the effects of the measures complained of are the same as the effects of the alleged breach of Article 1110 –“Thunderbird's EDM's are all out of business”.²²⁵ The Claimant has deliberately declined to offer evidence in support of any lesser claim that might arise for something less than the total loss of the benefit and value of the three EDM gaming facilities. Simply put, it has adopted an “all or nothing” approach.

187. The Claimant bears the onus of proving its claim for damages. It is not for the Respondent to offer alternate measures of damages for alternate grounds of liability that have not been pleaded. Moreover, it would be inappropriate for the Tribunal to search through the

²²¹ Id., ¶¶ 197-208, 249-281

²²² Id., ¶¶ 282-296.

²²³ Id., ¶¶ 300.

²²⁴ Mexico maintains the view that the EDM operations were unlawful.

²²⁵ Reply, p. 73 (emphasis in the original).

evidence for a measure of damages for something less than the “out of business” theory that the Claimant relies on. In such case the Respondent would not have an opportunity to answer.

C. Mexico’s Defenses On The Facts

1. The Second And Third Scenarios Are Abandoned

188. The expert opinion of The Innovation Group presented with the Statement of Claim allegedly assesses damages (excluding interest) for 10 years’ loss of profits under three different scenarios: (i) US\$23.2 million for the three existing EDM facilities with the existing number of machines at the date of closure, (ii) US\$66 million for the three existing EDM facilities with 333 machines each²²⁶, and (iii) US\$171.2 million for the existing EDM facilities, each with 333 machines plus three new (yet undeveloped) facilities also having 333 machines at each location.

189. The Respondent responded to the second scenario by observing that the record is devoid of any document or testimony to the effect that the companies actually intended to increase the number of machines at each facility to 333. More importantly, there is no evidence that the facilities had the physical capacity to accommodate any more machines. Mexico also adduced evidence of observations made during the recent inspection of the now-closed facilities: at Nuevo Laredo there was space for only a few additional machines and no additional space for expansion, Matamoros was smaller than Nuevo Laredo and had no room for expansion, and Reynosa was not significantly larger than Nuevo Laredo.

190. The Respondent responded to the third scenario by observing that if the Claimant had an equity interest in any newly established enterprises that were incorporated for the purpose of developing new facilities, it could contend there was an investment, but the fair market value of such investment at the date of alleged expropriation would be insignificant. The definition of “investment” under NAFTA Article 1139 does not include plans, intentions, hopes or aspirations. The newly incorporated enterprises could not have any going concern value or any significant asset value, because they had no business premises, gaming equipment, personnel or customer base. Moreover, Thunderbird’s Annual Information Forms filed for 2000, 2001 and 2002 made no mention of an investment interest in any Mexican enterprise other than the three existing companies.

191. The Reply does not address Mexico’s defense to the second and third scenarios. They are not even mentioned, let alone supported with new evidence or submissions. In fact, they have quietly been abandoned.

2. Deficiencies In The Innovation Group Report

192. In the Statement of Defense, Mexico established that the valuation evidence submitted by the Innovation Group had the following deficiencies:²²⁷

²²⁶ This would have tripled the number of machines at each of the three existing facilities.

²²⁷ Statement of Defense, p. 92.

- It is not a “fair market value” assessment of the subject investments immediately prior to the date of their alleged expropriation. It purports to be a “determination of the earnings lost as a result of [the] premature closure” of the three existing facilities, and three others that “were in various stages of initial conception and development”.
- Despite the absence of any track record of profitable operations, it purports to value the three facilities on a discounted cash flow basis. It does not offer other valuation criteria.
- The discounted cash flow valuation is based on assumed cost and revenue projections that are not supported by the audited financial statements of the three entities at issue. They have been estimated or are taken from sources that the Innovation Group has not disclosed.
- It does not take into account “any other risks likely to be perceived by a reasonable buyer at the date in question” which, in the circumstances of this case, must include the prospect of closure through regulatory or legislative enforcement action or, if the skill games are established as lawful under the Gaming and Lotteries Law, competition from other operators.
- It offers no alternate measure of damages suffered by reason of or arising out of alleged breaches of Articles 1102 and 1105.

193. No further report or witness statement from the Innovation Group or any other substantive response to any of these points has been provided. With respect to Mexico’s argument that the Innovation Group report does not assess “fair market value”, the Reply is limited to contending that “slavish reliance on the text of Article 1110(2)-(4) should not prevail over a common sense approach to determining the actual extent of damages...”²²⁸ In response to Mexico’s argument that the Innovation Group failed to take into account any negative contingencies, the Reply contends that “Mexico has provided no evidentiary basis upon which to justify the alleged, unconsidered risks it sets out at paragraphs 354 to 357 of the SoD”²²⁹. The Tribunal will appreciate that, in fact, these paragraphs repeat Thunderbird’s own admonitions to shareholders and future investors that its operations are dependent on favorable legislation and judicial regulatory rulings, and are exposed to competition from more experienced, better financed operators, two of whom are identified by name as likely future competitors in Mexico.

194. Mexico refers paragraphs 327 to 359 of the Statement of Defense for the Tribunal’s further consideration.

²²⁸ Reply, p. 71, lines 23-25.

²²⁹ Id., p. 73, lines 1-3.

D. Mexico's Response To Booker T. Copeland III's New Testimony

1. Thunderbird Is Not A "Great Company"

195. Mr. Copeland offers a spirited defense of Thunderbird's track record, saying "like any great company, we have experienced failure [but] our successes, which outnumber the disappointments, have sustained us".²³⁰ For the most part, the testimony tendered by the Claimant is inconsistent with incontrovertible facts. Thunderbird's disappointments are many and easily exceed its successes, both in number and effect.²³¹

196. This is reflected in the history of Thunderbird's stock price and its forced delisting from the Toronto Stock Exchange (TSE). The price of shares fell from US\$5.87 in February 1996 when Thunderbird was first listed on the TSE to US \$0.09 in November 2002, when it was suspended from trading for failing to maintain the TSE's market capitalization requirements.²³² It did not trade again until July 2003 when Thunderbird became listed on the newly established CNQ Exchange. By the end of 2003, the CNQ had only 13 listings and its average daily volume was only CDN\$16,232.00. As of March 2004, Thunderbird's stock price was only US\$0.38 per share, notwithstanding its supposed successes.

197. Thunderbird's successes and various other failures are relevant to two issues: (i) the wisdom of investing in "skill game" parlors in Mexico, and (ii) the credibility of its claim for damages.

198. As to the first issue, it can be seen that all of Thunderbird's investments that have enjoyed any measure of success – a total of 10 casinos in Panama, Venezuela and Nicaragua, and a VLT parlor in Guatemala – are located in countries where gaming is legal and Thunderbird enjoys vested legal rights as a licensee or through a licensee. By comparison, its most significant failures – California Indian gaming and South Carolina, its operations on the Internet and facilities in Mexico – are located in jurisdictions where gaming is (or was) illegal and Thunderbird did not have vested rights.

199. The Claimant itself recognized the peril of engaging in non-licensed gaming operations in November 1998, upon claiming to have adopted a more prudential approach:

The Company's prior activities in unsettled markets and its stipulated denial of a license in Colorado create a challenge for it to be licensed in certain jurisdictions in the United States. The Company has taken all steps possible to operate responsibly in regulated markets, including divestiture of its Internet business and removal of all officers and

²³⁰ See Second Witness Statement of Booker T. Copeland III, ¶ 17, Exhibit C-W.

²³¹ *Thunderbird's Investments and Dispositions* (1996-2002). Exhibit R-91.

²³² Exhibit R-55 and Thunderbird's stock price records provided with the letter DGCJN.511.13.058.04 dated 23 January 2004. Most of Thunderbird's loss of value occurred in 1997 and 1998. There is no perceptible decline in value following the announced closure of the Mexican gaming operations in September 2001 and January 2002.

directors responsible for moving the Company into unsettled markets. The Company was conservative in ceasing its operations in May, 1998 in California and ceasing collection of substantial revenues from its Tribal clients.²³³

200. However, contrary to its own purported prudential practice, Thunderbird did enter another so-called “unsettled market”²³⁴ in June 2000 when, having heard from Mr. Watson that “*Mr. Ivy Ong has acquired, through an Amparo, the right to operate four slot machine operations in Mexico!*”²³⁵, it negotiated an agreement with Mssrs. Ong and Oien to participate in “skill game” facilities in Mexico, in the expectation of operating under *amparo* judgments pending the anticipated passage of legislation that would allow the establishment of casinos.

201. As to the overall credibility of the claim for damages, it defies logic that three newly established facilities in a market identified by the Claimant as an “unsettled market” could be worth 2.5 times more than Thunderbird’s interest in 11 licensed gaming establishments in jurisdictions where licensed gambling is legal. But that is precisely what the Claimant seeks: US\$23.2 million,²³⁶ compared to its current market capitalization of US\$9.2 million²³⁷. Unlike the claimant in *S.D. Myers*, Thunderbird did not have “an excellent record of profitability, and an outstanding record of passing audits by regulators and customers.” To the contrary, Thunderbird’s corporate history is characterized by repeated annual losses and some very significant regulatory problems.

202. The claim for damages is grossly inflated and should be rejected in its entirety.

2. The Audited Financial Statements Must Prevail

203. The central contention in Mr. Copeland’s second witness statement is that the Finbridge report was wrong in finding that none of the three EDM facilities was profitable because the audited financial statements for 2001 do not cover a full year of operations (Matamoros and Nuevo Laredo having been closed down in October 2001) and that the results do not reflect the removal of certain non-recurring expenses. He does not identify these expenses, except to contend that some are development expenses and some comprise the continued payment of wages to employees. He does not refer to any exhibit or new document that would demonstrate the existence or amount of these alleged expenses.

204. Mr. Copeland appears to rely on financial reports prepared by management to conclude that the Matamoros facility had EBITDA of US\$344,000 for the first nine months of 2001.

²³³ Exhibit R-088-B, Press Release dated 6 November 1998, “Third Quarter Results and Company Update”.

²³⁴ Mexico would call it an illegal market or black market.

²³⁵ See *supra*, ¶ 18.

²³⁶ For the three existing “skill game” facilities with the existing number of machines at the time of closure.

²³⁷ 24,311,687 outstanding shares at US\$0.38, which is equal to \$9,238,441.81 as at 24 March 2004.

However, as explained in the Finbridge rejoinder report,²³⁸ there are serious unexplained differences between the audited financial statements and the financial statements prepared by management that preclude the latter from being used to project future profitability.

205. The Tribunal will be familiar with an auditor's obligation to be satisfied as to the reliability of information relied on before certifying that an annual financial statement fairly and accurately reflects the financial affairs of the subject entity. It is not appropriate for Mr. Copeland, CFO of Thunderbird, to refer to the financial statements audited by KMPG as "skewed" information that cannot be used to determine the value of the EDM enterprises. If there is some reason as to why management's financial statements should be preferred to audited financial statements, it should come from KPMG.

3. The Second Report Of Finbridge Consulting

206. The second report of Finbridge responds to Mr. Booker T. Copeland's second witness statement in which he criticizes the opinions offered by Finbridge for relying on EDM's audited financial statements, which he characterizes as being skewed because they include two and a half months of operations without income as a result of the closure of the facilities in October 2001.²³⁹

207. Finbridge explains that the use of audited financial statements to evaluate a company is standard practice and that the differences between the audited and unaudited financial statements are so great that the latter cannot be relied on. These differences are not related to the exchange rate used to convert pesos into dollars as Mr. Copeland claims.

208. Furthermore Finbridge also points out that no adjustments can be made to compensate for the referenced two and a half "months of no revenues" either because the adjustment would be inappropriate (as is the case of EDM Reynosa, which was not closed until 2002) or because they would require additional information that has not yet been provided by the Claimant (*i.e.*, a detailed breakdown of the costs and expenses).

209. Mr. Copeland disagrees with Finbridge's opinion regarding the precarious financial condition of the three EDM companies, pointing to their positive EBITDA as well as the cash they generated (USD \$754,000) during 2001 as evidence to the contrary. Mr. Martínez, author of the Finbridge report, explains that: (i) it is not appropriate to draw conclusions about the companies' financial stability and future performance based on 9 months of operation in the case of Matamoros, 8 months in Nuevo Laredo and only 3 months in the case of Reynosa, and (ii) the cash figure cited by Mr. Copeland refers to cash generated by the three EDM companies plus the cash generated by a fourth company: Servicios de Destreza S.A. de C.V., that should not have been included and that accounts for 37.3% of the total.²⁴⁰ This company, owned by Thunderbird,

²³⁸ Exhibit R-119.

²³⁹ See the Second Witness Statement of Booker T. Copeland, 9 February 2004, ¶ 15. Exhibit C-W.

²⁴⁰ See Audited Financial Statements of EDM. Exhibits R-061 and R-087.

provides personnel to the EDM companies as stated in the Subscription and Investment Representation Agreement:

Servicios de Destreza is owned and operated by International Thunderbird Gaming Corporation and is not a profit center, such that all costs of employees are paid by the company through a lease arrangement with Servicios de Destreza, which does not charge any fee for its services”.²⁴¹

[Emphasis added]

210. Finbridge explains why in its opinion a discounted cash flow approach is inappropriate in this case, namely, because there is not enough information to reliably project the companies’ future profits. It reiterates its opinion regarding the value of the companies based on alternative methodologies (book value and liquidation value) in the amounts shown in the following chart:

Summary of valuation results

<i>Cifras en miles de pesos</i>	VPN	Valor en libros	Valor de liquidación
EDM- Laredo	- 3,891	8,420	6,315
EDM-Reynosa	- 5,444	4,031	3,023
EDM-Matamoros	- 4,858	5,228	3,921
Total Empresas existentes	- 14,193	17,679	13,259
Puebla	-	-	-
Ciudad Juarez	-	-	-
Monterrey	-	-	-
Total Empresas proyectadas	-	-	-
Total	- 14,193	17,679	13,259

Preparado por: FinBridge Consulting S.C.

E. Damages Arising From Other Causes

211. The Claimant blames the actions of the Mexican government for its failure in the Mexican “skill game” business, when in fact, Thunderbird suffered similar losses as a result of its own so-called “first mover” approach to investment opportunities in nascent markets²⁴², ignoring the kind of prudential practices that would reasonably be expected. It also suffered from the apparent misrepresentations, fraudulent or otherwise, of Mssrs. Ong and Oien and perhaps other individuals, as it has contended in a corporate disclosure statement that was made under a legal duty of candor and complete disclosure. The Respondent submits that in the unlikely event of a finding of liability based on a breach of Articles 1102 or 1105, the Tribunal must consider to what extent the loss or damage complained of was the caused by the Claimant’s

²⁴¹ Exhibit C-28, p. 10.

²⁴² See Annual Information Forms for 2000, 2001 and 2002, Section II.B, Business Strategy. Exhibit R-20, R-26, and R-120.

own aggressive investment practices and/or its decision to proceed based on misrepresentations of third parties.

F. Conclusions

212. The Respondent reiterates the conclusions in paragraphs 365 to 369 of the Statement of Defense. The Claimant's share of any compensation based on valuation criteria that could be considered to be appropriate under Article 1110(2), in the circumstances of this case, is as follows:

- for the amount apparently invested in the EDM companies: USD \$1,440,850 (although the amount of money and/or money's worth contributed by the Claimant appears to be less);
- for the book value of the EDM companies: USD \$664,952; and
- for the liquidation value of the EDM companies: USD \$498,754.

213. As to the claims for damages arising from breaches of Articles 1102 and 1105, the Respondent reiterates its submissions contained in paragraphs 325, 358 and 359 of the Statement of Defense. Simply put, the Claimant has failed to meet the burden of proof.

V. JURISDICTIONAL OBJECTION

214. In its Statement of Defense, the Respondent argued the Claimant did not own or control any of the EDM companies that would entitle it to present a claim on behalf of them under NAFTA Article 1117. Thunderbird did not demonstrate (i) that it owned its Juegos de Mexico and Thunderbird Brazil; (ii) that these companies acquired the EDM companies; or (iii) that Juegos de Mexico and Thunderbird Brazil were the owners of the EDM companies.

215. In the Reply, the Claimant simply repeats its general argument that it held a significant level of ownership in, and had complete control over, the EDM companies during the pertinent time:.

Thunderbird does not claim that it owned more than 50% of certain EDM's (i.e. Nuevo Laredo, Matamoros & Reynosa) during the relevant times. Rather, it does claim to have held a significant level of ownership in all of the EDM's and to have exercised complete control over all of them at all relevant times. Thus, the question for this Tribunal to determine as regards to Thunderbird's ability to proceed under Article 1117 is *whether Thunderbird directly or indirectly controlled the EDM's at the relevant times.*²⁴³

[emphasis in original]

²⁴³ Reply p. 23.

216. The Claimant did not submit any additional documentary evidence to rebut the arguments made by the Respondent nor to explain the chronological discrepancies that Mexico identified in the documents provided by the Claimant to prove the relationship between Thunderbird and EDM.

217. The Claimant's acknowledgement that it did not own more than 50% of the shares of any of the EDM companies is significant. As Mexico discussed in detail in the Statement of Defense, the bylaws, Subscription and Investment Representation Agreement, and Members Quota Agreement for each of these facilities, required from share ownership of 51% to 65% to control corporate actions.²⁴⁴ Because the Claimant has admitted it did not own EDM for purposes of Article 1117, the Respondent will focus its discussion on the issue of control. For the reasons set out below, the Respondent re-affirms that Thunderbird has failed to establish a claim under Article 1117.

218. The Respondent notes that the Claimant characterizes the Respondent's jurisdictional objection as a "preliminary argument."²⁴⁵ Mexico has formally objected to the jurisdiction of this Tribunal to hear Thunderbird's claim under Chapter Eleven and maintains its objections.

A. The NAFTA's Requirements

219. Article 1101 requires that a measure adopted or maintained by a Party in its territory relate to "investments of investors" of another Party. Under Article 1139 an enterprise of a Party is an "investment." Similarly, "enterprise of a Party" is defined as "an enterprise constituted or organized under the law of a Party" Article 1139 defines an "investment of an investor of a Party" as one "owned or controlled directly or indirectly by an investor of such Party." Thus, for an investor to bring a claim under Article 1117 on behalf of an enterprise, as its investment, the NAFTA requires that: (i) the enterprise be a "juridical person" and (ii) the investor "own or control" it.

220. According to the definition of an "enterprise of a Party", an enterprise constituted or organized under the law of a NAFTA Party would be an enterprise of that NAFTA Party, and the domestic corporate law of that Party would apply.

221. Neither the NAFTA nor Chapter Eleven in particular provide a definition of "control". Absent such a guideline, international law refers to the applicable domestic law. The International Court of Justice described the relationship between international law and municipal corporate law as follows:

In the [field of diplomatic protection] international law is called upon to recognize institutions of municipal law that have an important and extensive role in the international field. All this means is that international law has to recognize the corporate entity as an institution

²⁴⁴ See Statement of Defense, Section VIII.

²⁴⁵ Reply p. 22.

created by States in a domain essentially within their domestic jurisdiction. This in turn requires that, whenever legal issues arise concerning the rights of States with regard to the treatment of companies and shareholders, as to which rights international law has not established its own rules, it has to refer to the relevant rules of municipal law.²⁴⁶

Thus, to determine what constitutes “control” of a corporation, it is necessary to look to the corporate law of the Party under whose laws the enterprise was incorporated, and specifically to the corporate law. In this manner, in considering the claim of the Claimant under NAFTA Article 1117, it is necessary to determine under Mexican corporate law whether it exercises control over the corporation.²⁴⁷

B. The Claimant Does Not Have Legal Control Of EDM

222. A review of the *Ley General de Sociedades Mercantiles* and the different EDM corporate agreements demonstrates that Thunderbird did not (and does not) have control of EDM-Matamoros, EDM-Laredo, or EDM-Reynosa.²⁴⁸ Because Mexico already described the provisions of these agreements in detail in the Statement of Defense, the discussion below will review them only in summary fashion, focusing on the most relevant portions of the provisions addressing control of these companies.²⁴⁹

1. *Ley General de Sociedades Mercantiles*

223. EDM-Matamoros, EDM-Laredo, and EDM-Reynosa were constituted under the *Ley General de Sociedades Mercantiles* (LGSM). The EDM-Matamoros Subscription and Investment Representation Agreement provided:

The Company is a Society of restricted Liability with variable capital (sociedad anonima de capital variable) organized under the laws of the

²⁴⁶ Case Concerning Barcelona Traction, Light and Power Company, Limited (Belgium v. Spain) (“Barcelona Traction”, ICJ Reports 1970, p. 3. See also Brownlie, Ian, Principles of Public International Law, 5th Ed., Oxford University Press (1988) p. 493 (quoting Barcelona Traction: “If the company is harmed... [t]he shareholders must look to the company and thence to the national state of the company for action.”).

²⁴⁷ Under Article 31 of the Vienna Convention on the Law of Treaties, the terms of a treaty should be given their ordinary meaning in their context. The context includes the text of a treaty, which in the case of NAFTA provides the definition of “enterprise of a party.” It refers to the law of the respective Party regarding the establishment and organization of a company. In this manner, under the rules of interpretation of treaties contained in the Vienna Convention, it should be concluded that NAFTA Article 1117, consistent with the criteria of international law, and as has been expressed by the International Court of Justice, requires that legal control be demonstrated under the Mexican corporate law.

²⁴⁸ Regarding the rest of the companies, the Respondent reaffirms its arguments presented in the Statement of Defense. The Claimant not succeeded in demonstrating it has made an “investment”, nor has it demonstrated that the Government of Mexico adopted measures in relation to those other facilities., The claim cannot include any of these other companies.

²⁴⁹ See Section VIII of the Statement of Defense.

United Mexican States (“Mexico”). The organization, operation and management of the Company will be subject to the General Law of Commercial Companies (“Ley General de Sociedades Mercantiles”) of Mexico and other applicable Mexican laws (collectively, the Mexican Laws”).²⁵⁰

224. Under the LGSM, in a limited liability corporation (*Sociedad de Responsabilidad Limitada*, one of the kinds of enterprises recognized by the law²⁵¹), the *Asamblea de Socios* is the highest authority of the company, in which company decisions are taken by a majority vote of the shareholders that represent at least half of the company shares²⁵². All shareholders have the right to participate in the decisions of the *Asamblea*, provided one vote per thousand pesos of participation in shares.²⁵³ The Board has a series of powers that are listed in Article 78 of the LGSM.²⁵⁴ The *Asamblea de Socios* has a series of powers that are enumerated in Article 78 of the LGSM, including naming and removing the managers on which the administration of the company depends.: The decisions taken by the managers must be by majority vote.

2. EDM Corporate Documents

225. The specific bylaws of each of the EDM facilities expressly described the criteria for control the company’s actions. They required that corporate resolutions be approved by greater than 65% of the company’s shareholders, including naming and removing managers, approval

²⁵⁰ EDM-Matamoros Subscription and Investment Representation Agreement, Article 3(b)(i). Exhibit C-28.

²⁵¹ EDM companies were companies or limited liability (*sociedades de responsabilidad limitada y de capital variable, S. R.L. de C.V.*). Enterntainmens de Mexico was constituted as a *sociedad anonima de capital variable*, and later changed to a limited liability corporation.

²⁵² Art. 77 of the LGSM.

²⁵³ Art. 79 of the LGSM.

²⁵⁴ Art. 78. Las asambleas tendrán las siguientes facultades:

- I. Discutir,aprobar, modificar o reprobar el balance general correspondiente al ejercicio social clausurado y de tomar con estos motivos, las medidas que juzguen oportunas;
- II. Proceder al reparto de utilidades;
- III. Nombrar y remover gerents;
- IV. Designar, en su caso, el consejo de vigilancia;
- V. Resolver sobre la decision y amortización de las partes sociales;
- VI. Exigir, en su caso, las aportaciones suplementarias y las prestaciones accesorias;
- VII. Intentar contra los porganos sociales o contra los socios, las acciones que correspondan para exigirles daños y perjuicios;
- .. VIII. Modificar el contrato social.
- IX. Consentir en las cesiones de partes sociales y en la admisión de nuevos socios;
- X. Decidir sobre los aumentos y reducciones del capital social;
- XI. Decidir sobre la disolución de la sociedad, y
- XII. Las demás que les correspondan conforme a la Ley o al contrato social.

and modification of financial statements, approving the business plan, and the designation of external auditors.²⁵⁵

226. Although there are various inconsistencies between the bylaws and other corporate instruments (the Subscription Agreement and Members Quota Agreement),²⁵⁶ they all generally required greater than 65% of the shares to approve resolutions regarding the administration of the companies, but in no case required less than 51%. In addition, at least 40% of the shares must be represented to constitute a quorum for the *Asamblea de Socios*.

227. Thunderbird had an ownership of 36.67% in EDM-Matamoros, 33.3% in EDM-Laredo and 40.1% in EDM-Reynosa.

228. In some cases, the series B shareholders had the right to name the president and secretary of the board of managers. However, Thunderbird did not have sufficient ownership to permit it to do so alone.²⁵⁷

229. Thunderbird has argued that although it had a partial ownership of the EDM companies, it controlled them. However, as discussed above, the documents provided by the Claimant indicate the contrary. The bylaws of the three companies required 51% to 65% ownership to adopt resolutions of the *Asamblea de Socios*, a percentage that Thunderbird alone did not have and thus prevents it from controlling the EDM companies.

230. It is in this manner that the very documents provided by Thunderbird show that in no case did it have sufficient ownership in the EDM companies to permit it to legally control them.

3. Inapplicability of *S.D. Myers*

231. Despite the NAFTA's specific requirements, the Claimant contends that the jurisprudence supports its argument that it may present a claim under Article 1117 without a showing of legal control over the companies in question.²⁵⁸ It argues that in *S.D. Myers and Government of Canada (S.D. Myers)*, the tribunal permitted the claim notwithstanding that the Claimant could not demonstrate its control of the investment.²⁵⁹ Even if *S.D. Myers* were considered applicable, the Claimant is not exempted from meeting the burden of proof to demonstrate that it had control of the EDM companies. It has not done so.

²⁵⁵ See Statement of Defense, Sections VIII.C.2 and VIII.C.3.

²⁵⁶ The Respondent identifies them in its Statement of Defense. *Id.*

²⁵⁷ *Id.*

²⁵⁸ Reply pp. 23-24.

²⁵⁹ *S.D. Myers, Inc. and Government of Canada*, Partial Award (Liability), 13 November 2000.

232. S.D. Myers, Inc. (which the tribunal referred to as SDMI) was an Ohio corporation. Mr. Dana Myers owned 51% of the shares and the rest was distributed among his three brothers.²⁶⁰ In 1993, the Myers brothers established “Myers Canada”. When SDMI filed its arbitral claim under the NAFTA, the Government of Canada argued that the Myers brothers, not SDMI, owned Myers Canada.²⁶¹ The tribunal concluded that SDMI was an “investor” for the purposes of Chapter Eleven of the NAFTA, and that Myers Canada was an “investment.”²⁶² The Tribunal permitted SDMI’s claim to proceed, stating:

[T]he Tribunal does not accept that an otherwise meritorious claim should fail solely by reason of the corporate structure adopted by a claimant in order to organize the way in which it conducts its business affairs.²⁶³

233. Nevertheless, as will be demonstrated below, the reasons on which the tribunal based its decision that SDMI had submitted an “otherwise meritorious claim” cannot be used to support the Claimant’s argument that Thunderbird may bring a claim on behalf of EDM without demonstrating legal control of it.

234. SDMI was majority owned by Dana Myers and the rest of the ownership was divided among his brothers. Therefore, the entire ownership of SDMI was divided among four individuals, all of whom were related. In fact, the tribunal repeatedly referring to SDMI as a family business.²⁶⁴ Thus, although SDMI was a corporation, in reality it was little more than the “alter ego” of the Myers brothers.

235. In addition, the corporate chronology in *S.D. Myers* was simple and straightforward: Stanley Myers founded the family business and then transferred it to his four sons.²⁶⁵ The tribunal noted:

The uncontradicted evidence before the Tribunal was that Mr. Stanley Myers had transferred his business to his sons so that it remained wholly within the family and that he had chosen his son Mr. Dana Myers to be the controlling person in respect of the entirety of the Myers family’s business interests.²⁶⁶

²⁶⁰ Id. at ¶ 89.

²⁶¹ Id. at ¶ 227.

²⁶² Id. at ¶ 231.

²⁶³ Id. at ¶ 229.

²⁶⁴ *S.D. Myers, Inc. and Government of Canada*, Second Partial Award, 21 October 2002, ¶¶ 109, 112.

²⁶⁵ Partial Award (Liability) at ¶ 89.

²⁶⁶ Partial Award (Liability) at ¶ 230.

[emphasis added]

There was no doubt Mr. Myers owned the business and transferred to his sons, nor that they were its owners.

236. The situation of Thunderbird and EDM is much different. According to the Claimant:

On August 10, 2000, Thunderbird, through two wholly owned subsidiaries, Juegos de Mexico, Inc. and International Thunderbird Brazil, acquired all outstanding shares of EDM... On August 11, 2000, Thunderbird acquired the EDM shares of International Thunderbird Brazil. Thunderbird, through its direct ownership and that of its subsidiaries, Juegos de Mexico, Inc., held the majority of EDM shares.²⁶⁷

The Claimant stated it acquired EDM via two of its British Virgin Islands subsidiaries, and then acquired the shares from one of those subsidiaries the next day. It should not be overlooked, however, that the Claimant has not demonstrated it acquired the shares of EDM. The Respondent reiterates that the Claimant has not provided any document to demonstrate that:

- Thunderbird owned Juegos de Mexico, Inc. The founding documents of Juegos de Mexico (“Memorandum and Articles of Association of Juegos de Mexico, Inc.”) provided by the Claimant do not identify the company’s shareholders nor do they contain information as to its ownership;²⁶⁸
- On 10 August 2000, Thunderbird owned Thunderbird BVI, or that Thunderbird BVI owned International Thunderbird Brazil;²⁶⁹
- International Thunderbird Brazil (BVI) had acquired EDM. The 10 August 2000 share purchase agreement states that Juegos de México, Inc. purchased and acquired all of the shares of EDM. The document does not make any mention of International Thunderbird Brazil (BVI).²⁷⁰

It is also not clear whether Juegos de Mexico, Inc. acquired EDM because the 10 August 2000 share purchase agreement is for the purchase of “Entertainments de Mexico, S.A. de C.V.”. However, on 2 June 2000, the company’s then owners approved the conversion of the company to a *responsabilidad* limitada, and a change of the name to Entretenimientos de Mexico.

²⁶⁷ Statement of Claim p. 7.

²⁶⁸ Exhibit C-11.

²⁶⁹ Exhibit C-12.

²⁷⁰ “Contrato de Compra de Acciones,” providing (“compra y adquiere de los Vendedores, exactamente 5 acciones de la Serie “A”... que representan exactamente 100% del capital social de Entertainments de México, S.A. DE C.V.”). Exhibit R-036.

This raises the question of whether Juegos de Mexico, Inc. purchased an entity that actually did not exist.²⁷¹

237. In *S.D. Myers*, uncontradicted evidence led the tribunal to conclude that SDMI was entitled to submit a claim to arbitration notwithstanding its corporate structure. In the case of Thunderbird, the documents provided do not demonstrate the acquisition of the supposed investment by Thunderbird by its subsidiaries or otherwise. Because Thunderbird that it either owned or controlled EDM, it cannot assert that it has a valid claim under the NAFTA.

238. Thunderbird entered into various agreements (“Subscription and Investment Representation Agreement” and a “Members Quota Agreement”) with different persons interested in investing in EDM-Matamoros, EDM-Laredo, and EDM-Reynosa. These establish the terms under which the companies in Mexico would carry out commercial activities, in Mexico, which the Tribunal should consider. As discussed above, despite the inconsistencies among the corporate documents, it is clear that Thunderbird did not have sufficient ownership to allow it to control the EDM companies. For example, the EDM-Matamoros Subscription and Investment Representation Agreement provides unequivocally:

Control of Company. The control of the Company is based upon equity ownership of the combined Class A and Class B Quotas, as more fully described in **Exhibit “A”**.²⁷²

[emphasis in original]

Exhibit “A” provides a chart (“EDM-Matamoros Division of Ownership and Cash Flows”) and indicates that Thunderbird had an ownership interest of 36.67%, much less than the 65% required to control the company.²⁷³ Thunderbird cannot seriously claim this fact is irrelevant to determining whether or not it controlled EDM-Matamoros. As already discussed, the situation of the other two companies is no different.

C. The Claimant Does Not Control EDM In Fact

239. Thunderbird rejects Mexico’s argument that the NAFTA requires a Claimant to prove it has legal control of the company to bring a claim on its behalf under Article 1117. However, the cases it cites do not support its argument that it has complied with the necessary requirements to demonstrate it has control of the investment.

240. According to the Claimant, the jurisprudence of the Iran-U.S. Claims Tribunal indicates that majority ownership is not a necessary requirement for establishing control.²⁷⁴ However, if it

²⁷¹ Exhibit C-11. This was discussed in further detail in footnote 239 of the Statement of Defense.

²⁷² EDM-Matamoros Subscription and Investment Representation Agreement, Article 3(b)(xv). Exhibit C-28.

²⁷³ Id.

²⁷⁴ Reply pp. 23, 24.

does not have ownership (majority ownership), it must demonstrate that it has control. The absence of legal control can be disregarded if control in fact is “shown”.²⁷⁵

241. The Claimant argues that the “legal” definition of control should not be considered. As it has already explained, Mexico maintains that the NAFTA requires that legal control be demonstrated. However, Thunderbird also has not demonstrated it had control of the companies in question even considering the term’s ordinary meaning.

242. The *Real Academia Española* defines “control” as having the dominion, the.²⁷⁶ Thunderbird contended that it actually exercised “complete” control over EDM.²⁷⁷ However, the facts do not support this position.

1. Prominent Role of Messrs. Watson and Girault

243. In the Reply, the Claimant focuses on a series of statements of the supposed investors of the various EDM companies in an attempt to counter Mexico’s objections to jurisdiction. According to Thunderbird:

These investors state, under oath, that they were and are passive investors in the EDM enterprises and, finally, that they relinquished control of their EDM investments and of the operations of the EDM entities to Thunderbird.²⁷⁸

244. Among these declarations are one from Peter Watson and one from Mauricio Girault. Mr. Watson’s declaration provides:

I completely understood then as I do now that I was and now am a passive investor in the Mexico Skill Game Operations. I fully understood then and I fully understand now that ITGC was the owner of a significant equity interest in the Mexico Skill Game Operations and that I relinquished control of my investment and control of the operations of EDM Matamoros to ITGC.²⁷⁹

[emphasis added]

²⁷⁵ Reply p. 23, citing Article VII(2) of the Claims Settlement Declaration at 24, quoting *Alcan*, 2 Iran-U.S.C.T.R. 294, 297 (1983)[emphasis added].

²⁷⁶ Real Academia Española, *Diccionario de la Lengua Española*, Tomo I, a-g, Madrid 1992. Exhibit R-126. In English, “control” is defined as: “Power or authority to manage, direct, superintend, restrict, regulate, govern, administer, or oversee. The ability to exercise a restraining or directing influence over something.” (*Black’s Law Dictionary*, Sixth Edition (1990), p. 329); “To exercise authoritative or dominating influence over.” (*The American Heritage College Dictionary*, 3d. Ed. (1997) p. 303). Exhibit R-126.

²⁷⁷ Reply pp. 23, 28-69.

²⁷⁸ Reply p. 28.

²⁷⁹ Peter Watson Witness Statement Exhibit C-X at ¶ 5.

Because Mr. Girault's declaration is verbatim identical to Mr. Watson's, it is not necessary to repeat it as well.²⁸⁰

245. It is generally understood that a "passive investor" is one that is not actively involved in the management or daily operations of the company in which it has invested. It concerns an investor who, "lets others be, without taking any action".²⁸¹ Black's Law Dictionary defines "passive income" as "income earned in an activity in which the individual does not materially participate."²⁸² Documents provided by the Claimant demonstrate that Messrs. Watson and Girault were not "passive investors".

246. According to the EDM corporate documents, Messrs. Watson and Girault played a central role in the management and operation of EDM. Both Peter Watson and Mauricio Girault were extensively involved in the founding of EDM-Matamoros, as well as in its management and operation, the opening of the facility, during and even after the entering into of the June 2001 EDM-Matamoros Subscription and Investment Representation Agreement. There is no evidence that Messrs. Watson or Girault sold or otherwise transferred ownership in EDM-Matamoros. To this day they maintain their status as Class B shareholders of EDM with the concomitant rights of the bylaws and other corporate documents (Annex A contains additional information regarding the role that Messrs. Watson and Girault played).

247. Under the Claimant's own interpretation of Article 1117, Thunderbird had to exercise total control of EDM to present the claim. However, Thunderbird shared the Class B quotas with Messrs. Watson and Girault, as well as the corresponding authority to appoint the Board of Managers. The documents also prove that Messrs. Watson and Girault carried out various activities on behalf of the company: pursuing financing; securing leases, negotiating contracts; obtaining licenses; approving and accepting payments; etc.

248. The evidence presented does not permit the Claimant to maintain that it exercised complete control over EDM during all of the pertinent period. There is no proof that Thunderbird had control in fact or at law over EDM.

2. Status Of Other Investors

249. From the time the Claimant submitted its notice of intent to submit a claim for arbitration in March 2002, the Respondent requested on numerous occasions the documents demonstrating that it had ownership or control of the EDM companies. It has taken almost two years for the Claimant to provide even basic information that, under the LGSM, any company should have, identifying the owners of the EDM companies, and to date it has not done so completely.²⁸³

²⁸⁰ Declaration of Mauricio Girault, Exhibit C-NN at ¶ 4, 17.

²⁸¹ Real Academia Española, Diccionario de la Lengua Española, Tomo II, h-z, Madrid 1992. Exhibit R-126.

²⁸² Black's Law Dictionary, Sixth Edition (1990) at 1124. Exhibit R-126.

²⁸³ See various communications from the Secretaria de Economia to Thunderbird. Exhibit R-002.

250. In the Reply, the Claimant presents a series of witness statements of persons who allegedly invested in EDM. However, a careful review of those witness statements indicates their probative value is limited, if they have any at all. They are not witness statements prepared by each person in which they provide their own version and explain the reasons they invested in EDM. They are identical witness statements prepared by the same person (probably by the legal representative of the Claimant) for the same purpose.²⁸⁴ In addition there are discrepancies between the witness statements and the EDM the EDM corporate documents. (See Section B of Annex A).

D. The Claimant Did Not File Waivers On Behalf Of Other Entities In Accordance With The NAFTA's Requirements

251. In the Reply, the Claimant argues that the NAFTA allowed it to submit the waivers required by Article 1121 at the time of the filing of the Statement of Claim. However, the Claimant confuses the UNCITRAL arbitration rules with NAFTA Chapter Eleven.

252. In particular, at pages 29-30 the Reply mischaracterizes a discussion held during the First Session of the Tribunal. As may be recalled, the Government of Mexico had objected to Thunderbird's Notice of Arbitration because: (i) it was not presented in the Spanish language, and (ii) Thunderbird had not presented even prima facie evidence that it had ownership or control over the EDM companies/entities. The Tribunal will recall that during the First Session the Government of Mexico stated that it would not object to the Notice of Arbitration solely because it was in English, without a translation, as required under the applicable law.²⁸⁵ However, Mexico has objected to the competence and jurisdiction of the Tribunal because, despite numerous and detailed requests for documents, Thunderbird did not prove it had ownership or control of the Mexican companies. This issue is still pending.

253. In the first session with the Tribunal, the Claimant urged the Tribunal to treat its Notice of Arbitration as the Statement of Claim and that it require Mexico to immediately file a Statement of Defense. Notwithstanding, the Tribunal ruled that Thunderbird should prepare a comprehensive Statement of Claim.²⁸⁶

254. The Reply relies on this discussion to argue that the Statement of Claim it submitted on 15 August 2003 should be treated as the Notice of Arbitration, and therefore, that the waivers presented be considered valid. However, Chapter Eleven sets forth specific rules that establish the conditions to submit a claim to arbitration, that in all cases prevail over the provisions of the UNCITRAL Arbitration Rules.

²⁸⁴ See Reply, Declarations AA-OO.

²⁸⁵ Transcript of First Session, English Language version at 88-89; Transcript of First Session, Spanish Language at 39-43.

²⁸⁶ Transcript of First Session, English Language version at 90-99; Transcript of First Session, Spanish Language at 39-43.

255. Specifically, NAFTA Article 1121, entitled Conditions Precedent to Submission of a Claim to Arbitration, provides that an investor may submit a claim to arbitration only if it consents to arbitration and waives its rights to initiate or continue domestic proceedings for damages. Article 1121(3) states that “[a] consent and waiver required by this Article shall be in writing, shall be delivered to the disputing Party and shall be included in the submission of a claim to arbitration.”

256. Article 1137(1) defines when a claim is considered “submitted to arbitration”:

A claim is submitted to arbitration under this Section when:

...

...

(c) the notice of arbitration given under the UNCITRAL Arbitration Rules is received by the disputing Party.

In this case, the claim was submitted to arbitration on 22 August 2002.²⁸⁷

257. The requirement to present the written waiver of the right to initiate or continue any actions in local courts or other fora should be complied with at the time of presenting the Notice of Arbitration under the UNCITRAL Arbitration Rules. In this respect, it is necessary to explain:

- a) Article 1121 establishes the “Conditions Precedent of Submission of a Claim to Arbitration”;
- b) Article 1121(1) and (2) state that a claim may be submitted to arbitration “only if” the waiver is given; and
- c) Article 1137 states that (in the case of the UNCITRAL Rules) a claim is submitted to arbitration when the Notice of Arbitration, contemplated in the UNCITRAL rules, is received by the Responding party.

258. As the plain text of the treaty and the interpretative statements of the other Parties show, through the waiver, the Parties wanted the assurance that, having given a general consent in advance to the arbitration of disputes arising from alleged breaches of Chapter Eleven, tribunals established under this Chapter would ensure that disputing investors would comply with the procedures set out in Chapter Eleven in order to validate a Party’s prior consent. In the contrary

²⁸⁷ The U.S. Statement of Administrative Action (see footnote 226 of the Statement of Defense) describes the waiver requirement under the heading “Jurisdictional Requirements”. Statement of Administrative Action p. 147. Canada’s Statement on Implementation, which is a document analogous to the U.S. Statement of Administrative Action, states: “The consent and waiver are to be included with the submission of the claim to arbitration”. CSI p. 154.

case, there would not exist consent of a Party to submit to arbitration, and the arbitral proceeding would be invalid *ab initio*.

259. A corollary to the general rules of interpretation set out in Article 31 of the Vienna Convention is the principle of effectiveness (*ut res magis valeat quam pereat*²⁸⁸):

[I]nterpretation must give meaning and effect to all the terms of the treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility.²⁸⁹

260. In accordance with the principle of effectiveness, this Tribunal must apply Articles 1121 and 1137 as they are written, and lacks discretion to waive or modify the requirements set out therein.

²⁸⁸ Meaning, “[t]hat the thing may rather have effect than be destroyed.” Black’s Law Dictionary op. cit. p. 1547. Exhibit R-126.

²⁸⁹ *United States - Standards for Reformulated and Conventional Gasoline*, (WT/DS2/AB/R), at 23 (May 20, 1996) (WTO Appellate Body). See also Interpretation, 14 Whiteman Digest of International Law §33, at 380-83 (1970).

261. For the reasons stated above, the Respondent reaffirms its request that the Tribunal dismiss the claim presented by International Thunderbird Gaming Corporation in its entirety, with a corresponding award of costs.

All of which is respectfully submitted for your consideration;

(signed in the original)

Hugo Perezcano Díaz
Agent and Counsel for the Respondent,
The United Mexican States
7 April 2004