

**Subject:** FW: PCA Case No. 2012-10: Merck Sharp & Dohme (I.A.) Corp. (U.S.A.) v. The Republic of Ecuador  
**Attachments:** 2016-02-05 MSDIA Letter\_(151704047)\_ (1).pdf; 2016-01-20 CC Decision (Spanish).pdf; 2016-01-20 CC Judgment (translation)\_ (151702165)\_ (1).pdf

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**Subject:** PCA Case No. 2012-10: Merck Sharp & Dohme (I.A.) Corp. (U.S.A.) v. The Republic of Ecuador

Dear Members of the Tribunal,

On behalf of Claimant MSDIA in the above-referenced arbitration, please see the attached letter and the recent Ecuadorian Constitutional Court decision (and translation) referenced therein.

Respectfully submitted,

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5 February 2016

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**VIA EMAIL**

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Re: ***MERCK SHARP & DOHME (I.A.) CORP.(U.S.A.) v. THE REPUBLIC OF ECUADOR***  
**(PCA CASE NO. 2012-10)**

Dear Sirs:

On 29 January 2016, MSDIA received notification that Ecuador's Constitutional Court issued a decision dated 20 January 2016, in which it annulled the 10 November 2014 judgment of the National Court of Justice ("NCJ") in the *PROPHAR v. MSDIA* litigation – a judgment of \$7.7 million that Ecuador's courts had fully enforced against MSDIA. The new Constitutional Court decision reinstates the \$150 million judgment against MSDIA issued by Ecuador's court of appeals in 2011 and returns the case for a third time to the NCJ for a new decision. As we will explain, the decision sends a message that the irrational \$150 million judgment should be sustained or—still more incredibly—increased. The Constitutional Court's decision and a translation are attached to this letter.

The Constitutional Court's decision exposes MSDIA to a risk of substantial and irreparable harm. As experience has shown, the timing of court decisions in Ecuador is impossible to predict, and the harm to MSDIA could come at any time, as soon as the NCJ issues its new decision. For the reasons set out below, MSDIA urgently requests interim measures of protection to preserve its investment in Ecuador pending this Tribunal's final resolution of the issues presented in this arbitration.

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## I. The Constitutional Court's Decision

As the Tribunal will recall from the parties' submissions and the March 2015 hearing in this arbitration, on 10 November 2014, the NCJ issued a second final award in the *PROPHAR v. MSDIA* litigation in Ecuador, holding that MSDIA was liable on a theory of pre-contractual liability and awarding Prophar (formerly NIFA) \$7,723,471.81 in damages. Ecuador's courts ordered MSDIA to pay, and it did pay, that amount to Prophar on 9 July 2015, deducting the \$1.57 million it had already paid in respect of the NCJ's first final decision (dated 21 September 2012), which had found MSDIA liable in that amount on the theory of "unfair competition."

Following the NCJ's 10 November 2014 decision, Prophar filed an Extraordinary Action for Protection ("EAP") in the Constitutional Court, arguing that the NCJ's decision was arbitrary and violated Prophar's constitutional rights to due process, effective legal protection and legal certainty. Prophar's EAP was pending at the time of the oral hearing in this arbitration in March 2015. As we previously notified the Tribunal, the Constitutional Court held an oral hearing on Prophar's EAP in January 2016, at which both MSDIA's counsel and a representative from the Attorney General's office, as well as counsel for Prophar, made oral submissions to the Court.

The Constitutional Court's 20 January 2016 decision granted Prophar's EAP and annulled the 10 November 2014 NCJ judgment.

With respect to the NCJ's finding on liability, the Constitutional Court rejected the NCJ's determination that the court of appeals judgment, which had awarded Prophar \$150 million on an antitrust theory, suffered from "defective substantiation." The NCJ decision had found that the court of appeals used "obscure, imprecise phrases, and confus[ed] concepts and application of rules with regards to matters such as free competition..."<sup>1</sup> The Constitutional Court held that the NCJ's analysis "fails to employ judicial, factual and evaluative premises" and that this "incomplete analysis" rendered the NCJ's judgment "illogical."<sup>2</sup> The Constitutional Court's decision thus rejects the legal analysis of the NCJ and reinstates a decision based on a theory of antitrust liability.

With respect to the NCJ's finding on damages, the Constitutional Court found that the NCJ had failed to provide an "adequate basis" for its \$7.7 million damages award, violating Prophar's "right to judicial security."<sup>3</sup> The Constitutional Court referred specifically to the expert report of Christian Cabrera that had been submitted in the underlying litigation by Prophar, in which Mr. Cabrera had calculated Prophar's lost profits damages to be \$204 million and found additional

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<sup>1</sup> Exhibit C-293, NCJ Judgment, *PROPHAR v. MSDIA*, dated 10 November 2014, at p. 25.

<sup>2</sup> Constitutional Court Decision, *PROPHAR v. NCJ*, dated 20 January 2016, at pp. 21-22.

<sup>3</sup> *Id.* at p. 15.

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damages to “the Ecuadorian people” in the amount of more than \$642 million.<sup>4</sup> The NCJ had specifically rejected Mr. Cabrera’s evidence, finding that it was “irrational and illogical.”<sup>5</sup>

The Constitutional Court strongly criticized the NCJ for having disregarded Mr. Cabrera’s evidence:

“[The Cabrera expert] report makes a determination about the losses suffered by the plaintiff based on real data and data projecting sales growth over fifteen years, that is, until the year 2018. Without giving a clear and adequate explanation in the judgment on appeal, the judges do not apply the statute requiring that the compensation be adequate to the damages, that is, that make the victim whole. It is strange how arbitrary the national judges’ reasoning is, given that in their determination of the amount of compensation [the respondent] is ordered to pay, they only consider the year 2003 and disregard the damages suffered by the respondent [sic] in the years following 2003.”<sup>6</sup>

The Constitutional Court’s decision thus directs the NCJ now to issue a new decision taking into account Mr. Cabrera’s evidence.

Moreover, the Constitutional Court found that the NCJ had violated Propfar’s constitutional rights by failing to consider Propfar’s petition for cassation, in which Propfar had asked the NCJ to review and reverse the reduction of damages from the \$200 million awarded by the first instance court to the \$150 million awarded by the court of appeals. The Constitutional Court’s judgment thus directs the NCJ now to consider whether the \$150 million judgment against MSDIA is in fact too low.

In light of its rejection of the NCJ’s decision on liability and damages, the Constitutional Court decision ordered as “measures of full reparation”:

1. “Vacate the judgment issued on November 10, 2014, by the [NCJ].

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<sup>4</sup> Exhibit C-42, Report of Cristian Augusto Cabrera Fonseca, *PROPHAR v. MSDIA*, Court of Appeals, dated 21 June 2011, at pp. 22-23, 30.

<sup>5</sup> Exhibit C-293, NCJ Judgment, *PROPHAR v. MSDIA*, dated 10 November 2014, at p. 80. The Tribunal will recall from the March 2015 hearing that Mr. Cabrera was designated an expert under highly questionable circumstances and his credentials were so lacking that the Council of the Judiciary later determined he should never have been designated an expert in the first place. It is because the NCJ had considered that disqualification in its initial decision reversing the court of appeals decision that the Constitutional Court had overturned the NCJ’s first final judgment in the case. Exhibit C-285, Constitutional Court Decision, *PROPHAR v. NCJ*, dated 12 February 2014, at pp. 21-22.

<sup>6</sup> Constitutional Court Decision, *PROPHAR v. NCJ*, dated 20 January 2016, at p. 15.

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2. “Retroact the effects of the proceedings until the moment before the issuance of the decision rendered on November 10, 2014, by the [NCJ].”
3. “Order, pursuant to the provisions of Article 201 number 1 of the Organic Code on Judicial Functions, that the Chamber of Associate Judges for Civil and Commercial Matters, National Court of Justice resolve the motion that has been filed for cassation, in accordance with the Constitution of the Republic, the law and comprehensive application of this Constitutional decision, that is, considering the *decisum* or resolution as well as the central arguments that formed the basis of the decision and constitute the rationale; under warning that the provisions of Article 86 number 4 of the Constitution of the Republic will be enforced if they do not do so.”

The “Chamber of Associate Judges” to whom the Constitutional Court has referred the case for a new decision are not the ordinary judges of the NCJ. The Associate Judges do not form part of the Civil and Commercial Chamber of the NCJ, from which the judges who issued the two prior final decisions in the *PROPHAR v. MSDIA* litigation were drawn. Rather, the Associate Judges ordinarily serve only as alternate judges when the ordinary judges of the NCJ are not available.

Article 86(4) of the Constitution provides, in part: “If the sentence or ruling is not complied with by the public servants, the judge shall order their dismissal from their job or employment, without detriment to the civil or criminal liabilities that might be applicable.”

## **II. MSDIA Is Entitled to Interim Measures of Protection**

While we are mindful of the Tribunal’s direction that the parties should report only on developments in the Ecuadorian courts and not argue in correspondence about the import of those decisions on the merits of MSDIA’s claims in the arbitration, the Constitutional Court’s decision is a dramatic and alarming change of circumstances that exposes MSDIA once again to the risk of imminent and irreparable harm. MSDIA therefore seeks interim measures of protection from this Tribunal. In support of its application, MSDIA offers the following observations about the Constitutional Court’s decision and its effects.

The Constitutional Court’s decision once again exposes MSDIA to the immediate threat of losing its business in Ecuador. The NCJ’s November 2014 decision no longer has legal effect in Ecuador (notwithstanding that MSDIA paid the judgment), and the \$150 million judgment of the court of appeals once again is the operative decision in the long-running *PROPHAR v. MSDIA* litigation. If the NCJ affirms that decision, MSDIA will face a final and immediately enforceable judgment against it that far exceeds the value of its assets in Ecuador. If Prophar takes steps to enforce that judgment in Ecuador, as it would almost certainly do, MSDIA would lose the business it has operated in Ecuador for more than forty years.

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For all the reasons MSDIA explained in connection with its prior interim measures application (which it withdrew in September 2012, after the NCJ issued its first final decision awarding damages of \$1.57 million), the risk that the NCJ will affirm the court of appeals judgment of \$150 million exposes MSDIA to the risk of substantial and irreparable harm. The requirements for awarding interim measures of protection – (i) a *prima facie* case on jurisdiction, (ii) that the requested measures are necessary to prevent a threat of substantial or irreparable harm, and (iii) urgency – are all met. In addition, to the extent the Tribunal regards there to be a fourth requirement of a *prima facie* case on the merits, MSDIA has easily met that requirement as well.

Indeed, the risk of substantial and irreparable harm to MSDIA is even greater now, following the Constitutional Court’s decision, than it was in September 2012 prior to the first NCJ decision.

In its recent decision, the Constitutional Court went far beyond merely annulling the NCJ’s second final judgment. In its 25-page decision, the Constitutional Court gave directions to the NCJ about how to decide the case when it is returned to that court for the third time.

Specifically, the Constitutional Court criticized the NCJ’s findings on liability, which had rejected the antitrust analysis on which the court of appeals decision rested, as “incomplete” and “illogical.” The Constitutional Court’s decision thus signals to the NCJ that it should uphold the court of appeals’ findings on liability. Notably, in the arbitration, Ecuador has never even tried to defend the court of appeals’ antitrust decision, arguing instead that:

“But the most important thing of course about the National Court of Justice second decision is it cured any problems that pre-existed its issuance. It is a new judgment where the parties had a full opportunity to present their cases, and because it is fully reasoned and cannot be impugned as irrational, it disposes of any question of wrongdoing or misapplication of the law below....”<sup>7</sup>

Now that the Constitutional Court has in fact impugned the NCJ’s second final decision as “illogical,” MSDIA faces the risk that the NCJ will uphold the court of appeals’ decision on liability.

The Constitutional Court also criticized the NCJ’s findings on damages, holding that the NCJ’s decision to award Prophar \$7.7 million was “arbitrary.” The Court went on to identify specific steps in the NCJ’s reasoning that it regarded as incorrect, including that the NCJ:

(i) ignored the expert report offered by Mr. Cabrera, which was grounded on an antitrust theory of damages, including the “real data and data projecting sales growth over fifteen years, that is, until the year 2018” included in Mr. Cabrera’s report and that were the

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<sup>7</sup> Day 2, Merits Hearing Full Transcript, at 20: 6-13.

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basis of his asserted damages of \$204 million (plus \$642 million in additional damages to “the Ecuadorian people”);

(ii) failed to apply the rule that “compensation [must] make the victim whole”;

(iii) “only consider[ed] the year 2003 and disregard[ed] the damages suffered by the respondent [sic] in the years following 2003”; and

(iv) “disregard[ed] the valuation of the damages that the company must have endured in subsequent years.”<sup>8</sup>

The Constitutional Court’s judgment directs the NCJ to issue a new decision “in accordance with the Constitution of the Republic, the law *and comprehensive application of this Constitutional decision, that is, considering the decimum or resolution as well as the central arguments that formed the basis of the decision and constitute the rationale.*”<sup>9</sup> In other words, the Constitutional Court directs the NCJ to award damages in accordance with the Constitutional Court’s reasoning that the NCJ should have given weight to the Cabrera report and should have awarded damages over a fifteen year period using the data and projections endorsed by Mr. Cabrera.

Notably, in the arbitration, Ecuador also has never sought to defend the court of appeals’ finding on damages or the reliability of the Cabrera report, arguing instead that the Cabrera report is irrelevant because it was rejected by the NCJ. Ecuador’s counsel stated at the March 2015 hearing that “the Cabrera report, which has been the biggest target of Merck’s complaints, was completely rejected by the NCJ, in NCJ 1, completely rejected.”<sup>10</sup> Similarly Ecuador’s counsel argued “[b]y reducing 95% of Merck’s damages, the NCJ wiped out any alleged vestiges of bias or impropriety reflected in the damages originally imposed by the lower courts.”<sup>11</sup> Now that the Constitutional Court has directed the NCJ to rely on the Cabrera report, which was the basis for the court of appeals’ irrational damages awards, Ecuador can no longer ignore the gross violations of MSDIA’s due process rights that result from reliance on that report or the risk of imminent and irreparable harm to MSDIA if the court of appeals’ decision is upheld.

The Constitutional Court also expressly criticized the NCJ for not having decided on Prophar’s cassation petition, which had sought review by the NCJ of the court of appeals’ decision to reduce the damages award from \$200 million to \$150 million. By directing the NCJ to decide Prophar’s cassation petition, the Constitutional Court has signaled to the NCJ that the award of \$150 million against MSDIA should be reexamined on the basis that it might insufficiently

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<sup>8</sup> Constitutional Court Decision, *PROPHAR v. NCJ*, dated 20 January 2016, at pp. 15, 16.

<sup>9</sup> *Id.* at p. 24.

<sup>10</sup> Day 2, Merits Hearing Full Transcript, at 219:6-9.

<sup>11</sup> Ecuador’s Rejoinder, paras. 442-443.

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compensate Prophar. Thus, the Constitutional Court's decision not only revives the risk that MSDIA will be subject to a final decision against it of \$150 million, but also raises the possibility of a final decision from the NCJ awarding Prophar \$200 million or more (including the ludicrous \$642 million in damages "to the Ecuadorian people" asserted by the Cabrera report).

The Constitutional Court also included in its judgment a threat to the judges of the NCJ that they will be exposed to personal liability if they fail to follow the Constitutional Court's directions. In its disposition, the Court warned that if the NCJ does not follow the Court's "resolution" and the "central arguments that ... constitute the rationale," the NCJ judges will be subject to penalty under Article 86(4) of the Constitution. Article 86(4) provides that a public official who does not comply with the ruling of an Ecuadorian court can be removed from office and subject to criminal and civil liability. The import of this threat is clear, and confirms the serious risk that the NCJ will this time affirm the judgment of the court of appeals.

But that is not all. The Constitutional Court's decision also expressly refers the *PROPHAR v. MSDIA* case to the Associate Judges of the NCJ, and not to the same Civil and Commercial Chamber that has twice before decided on MSDIA's cassation petition. The Constitutional Court's decision in this respect is highly unusual, and it is further evidence that the Court is seeking to engineer a different outcome to that which has come in the prior two decisions of the NCJ.

In light of the directions and threats made by the Constitutional Court to the NCJ, there is a serious risk that the NCJ will issue a final decision against MSDIA either affirming the \$150 million court of appeals judgment or awarding Prophar even more than that amount.

As MSDIA established in its first interim measures application in 2012, if the NCJ upholds the court of appeals' decision, MSDIA's ongoing business in Ecuador would be entirely destroyed. In brief:

- The total value of the assets of MSDIA's Ecuadorian branch is far less than \$150 million. Because MSDIA's Ecuador branch does not have cash or other liquid assets sufficient to satisfy the judgment, the judgment-creditor, Prophar, would have to ask the Ecuadorian courts to order the seizure of MSDIA's assets in Ecuador. These assets are necessary to the operation of MSDIA's business—indeed, apart from MSDIA's goodwill, good name, and relationships, these assets *are*, in effect, MSDIA's business. If the Ecuadorian courts order the seizure of MSDIA's assets in Ecuador to satisfy the judgment against it, this will completely destroy MSDIA's business in Ecuador.



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- MSDIA will suffer irreparable harm upon the issuance of an adverse NCJ judgment, even before its assets are seized to satisfy that judgment. If employees and business partners perceive that MSDIA will be put out of business in Ecuador by the judgment, they will act to protect their own interests. Key employees will seek and find other employment. Distributors will turn to other suppliers. Those from whom MSDIA leases facilities will look for other tenants likely to occupy the premises over the long term. These injuries will be immediate and produce irreversible consequences.
- The seizure of MSDIA's assets in Ecuador would have irreparable effects not only on MSDIA, which would be put entirely out of business in Ecuador, but also on MSDIA's employees in Ecuador, whom MSDIA would not be able to pay, and on the supply of essential pharmaceutical products to the Ecuadorian people.
- Moreover, unless Ecuador takes steps to prevent the enforcement of the disputed judgment outside of Ecuador, there is a significant risk that the judgment-creditor, Prophar, will take steps to enforce the judgment in other countries where MSDIA has assets, which will cause substantial and irreparable harm to MSDIA businesses in other countries outside Ecuador as well.

Numerous tribunals have found that the destruction of an ongoing business is an irreparable harm which warrants the issuance of interim measures.<sup>12</sup>

MSDIA therefore requests interim measures of protection directing Ecuador—including specifically its courts, its executive branch, and its national police—to take all steps within its power to prevent enforcement of any judgment against MSDIA in the *PROPHAR v. MSDIA* case, both within and outside of Ecuador.

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<sup>12</sup> See, e.g., Exhibit CLM-13, *Perenco Ecuador Ltd. v. Republic of Ecuador*, ICSID Case No. ARB/08/6, Decision on Provisional Measures (8 May 2009); Exhibit CLM-3, *Burlington Resources Inc. v. Republic of Ecuador*, ICSID Case No. ARB/08/5, Procedural Order No. 1 (29 June 2009); Exhibit CLM-7, *City Oriente Ltd. v. Republic of Ecuador*, ICSID Case No. ARB/06/21, Decision on Provisional Measures (19 November 2007); Exhibit CLM-8, *City Oriente Ltd. v. Republic of Ecuador*, ICSID Case No. ARB/06/21, Decision on Revocation of Provisional Measures and Other Procedural Matters (13 May 2008); Exhibit CLM-12, *Paushok v. Gov't of Mongolia*, UNCITRAL Arbitration Rules, Order on Interim Measures (2 September 2008). See also *CEMEX Caracas Investments B.V. v. Bolivarian Republic of Venezuela*, ICSID Case No. ARB/08/15, Decision on the Claimants' Request for Provisional Measures (3 March 2010), at para. 55 (noting that "the destruction of the ongoing concern that constituted the investment, would have created an 'irreparable harm.'").

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### **III. The Constitutional Court's Decision Is Also Relevant to the Merits of MSDIA's Claim in This Arbitration**

The Constitutional Court's 20 January 2016 decision is also highly relevant to the merits of MSDIA's claims before this Tribunal.

At the March 2015 hearing, MSDIA explained that it was caught in an endless spiral of litigation in Ecuador which violated Ecuador's obligations under the Ecuador-United States BIT not to deny justice to U.S. investors and to provide effective means of asserting claims and enforcing rights with respect to investments. The Constitutional Court decision confirms that MSDIA is being subjected to repeated denials of justice in Ecuador's courts and that the Ecuadorian judicial system fails to provide effective means of asserting and defending claims and enforcing rights.

In the arbitration, Ecuador vigorously disputed MSDIA's assertions. At the hearing, Ecuador's counsel stated:

“We heard multiple times about the treadmill that Merck appears to have found itself on, this endless loop of cases, and if that is what they have to expect, authorities say maybe you don't have to exhaust any more.... But again, Claimant has not shown that there is a serious risk that multiple EPAs would be entertained by the Constitutional Court in the same litigation, and upheld. As a matter of logic, it is unlikely that the same proceeding would give rise to repeated successive constitutional defects.... So it cannot be a ground to hold the EPA ineffective, that there is some theoretical possibility of multiple EPAs. There is simply no proof that that is a likely result.”<sup>13</sup>

Events in its own courts have proven Ecuador wrong. The Constitutional Court has entertained and upheld multiple EAPs in the same litigation, and MSDIA continues to find itself in an endless loop of judgments that deny it justice.

Moreover, the Constitutional Court's decision confirms that the Constitutional Court is not able to provide justice to MSDIA and cannot provide MSDIA an effective remedy for redressing violations of its due process rights at the hands of other courts. MSDIA explained in the arbitration that it did not file its own EAP in the Constitutional Court because doing so could not have remedied the harm to MSDIA and because it feared that doing so would only increase the damages resulting from denials of justice by the NCJ. The Constitutional Court's 20 January 2016 decision demonstrates that MSDIA's concerns were entirely justified.

Notably, the Constitutional Court has now done exactly what Ecuador and its legal experts said in the arbitration could not happen under Ecuadorian law. At the March 2015 hearing, Ecuador's

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<sup>13</sup> Day 5, Merits Hearing Full Transcript, at 110:6-24.

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expert on constitutional law, Dr. Guerrero del Pozo, testified that it “is not permitted given the nature of extraordinary protection action” for the Constitutional Court to indicate “how the judges of the National Court of Justice should decide in the case.”<sup>14</sup> With respect to the Cabrera report in particular, Ecuador’s counsel stated that the Constitutional Court “could not have directed the NCJ to ignore or not to ignore Mr Cabrera’s report in any way without exceeding its authority under Ecuador’s Constitution.”<sup>15</sup>

MSDIA’s constitutional law expert, Professor Rafael Oyarte, agreed with this assessment. He explained that, “[i]n keeping with this limited function, under no circumstances can the Constitutional Court order or instruct the NCJ how to decide a case. As the Constitutional Court itself has said, this would mean not only exercising jurisdictional authority that it does not have, but it would violate the principle of judicial independence.”<sup>16</sup> Professor Oyarte explained that “[t]he Constitutional Court does not analyze the facts of a case, does not evaluate evidence and does not interpret the law, nor does it apply the law to the facts of the case.”<sup>17</sup>

The limits of its jurisdiction did not matter to the Constitutional Court in its decision of 20 January 2016. In that decision, the Constitutional Court evaluated the evidence, issued factual and legal determinations, and directed the NCJ judges how to decide the case, threatening them with loss of their jobs and personal civil and criminal liability if they did not comply. This decision, like those that came before it, denies justice to MSDIA and violates Ecuador’s obligations under the Ecuador-United States BIT.

#### **IV. MSDIA Requests that the Tribunal Establish a Schedule for Written Submissions and a One-Day Hearing**

As discussed above, the Constitutional Court’s decision is a material development that gives rise to an urgent need for interim measures of protection to preserve the existence of MSDIA’s investment in Ecuador. That decision is also highly relevant to the merits of the claims before this Tribunal.

MSDIA therefore requests that the Tribunal establish a timetable for written submissions and schedule an oral hearing to address MSDIA’s request for interim measures and the effects of the Constitutional Court’s decision on the merits of MSDIA’s claims. In light of the urgency of the situation, MSDIA requests that the Tribunal establish an expedited timetable for written submissions and set a date for an oral hearing as soon as reasonably possible.

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<sup>14</sup> Guerrero del Pozo Expert Report, dated 18 February 2015, at para. 94.

<sup>15</sup> Day 2, Merits Hearing Full Transcript, at 191:7-11.

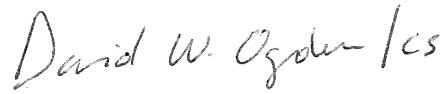
<sup>16</sup> Oyarte Expert Report, dated 7 August 2014, at para. 11.

<sup>17</sup> *Id.* at para. 12.

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Sincerely,

A handwritten signature in cursive script that reads "David W. Ogden /cs".

David W. Ogden

Enclosures

cc: Mr. Martin Doe  
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Mr. Mark Clodfelter  
Ms. Janis Brennan  
Ms. Diana Tsutieva  
Mr. Ronald Goodman  
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