IN THE MATTER OF AN ARBITRATION UNDER CHAPTER ELEVEN OF THE
NORTH AMERICAN FREE TRADE AGREEMENT

BETWEEN:

POPE & TALBOT, INC.

Claimant/Investor

and

THE GOVERNMENT OF CANADA

Respondent/Party

GOVERNMENT OF CANADA

CANADA'S SUBMISSION ARISING OUT OF ARTICLE 1128 SUBMISSIONS ON NOTES OF INTERPRETATION

(Damages Phase)

December 14, 2001

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1. Canada has reviewed the post-hearing submissions of the United Mexican States ("Mexico"),[1] and of the United States of America ("United States"),[2] submitted pursuant to Article 1128 following the Damages hearing, and makes the following comments.

PART A: THE TRIBUNAL'S OBLIGATION TO APPLY THE FREE TRADE COMMISSION'S INTERPRETATION OF ARTICLE 1105

2. Canada agrees with both submissions that the applicability of the Notes of Interpretation issued by the Free Trade Commission to the present case is governed by Article 1131 of NAFTA.[3] Under paragraph 1 of that article a tribunal must decide in accordance with the provisions of the NAFTA and applicable rules of international law. Specifically, under paragraph 2, an interpretation of the Commission is binding on a Chapter 11 tribunal.

3. Article 1131 sets out the governing law for a Chapter 11 tribunal. A tribunal must apply that law. It must accept an interpretation of the Commission as binding on it. It has no authority to go behind that interpretation and ask how it was effected, whether it was appropriate for any particular NAFTA Party to participate in the interpretation, or whether it thinks that the interpretation is consistent with its own reading of the provision in question. The treaty provides for the Commission to make such interpretations and the treaty provides for those interpretations to be binding on Chapter 11 tribunals. A tribunal cannot ignore the treaty and refuse to apply the governing law set out in Article 1131.

4. In the present case, the Tribunal has yet to rule on damages arising out of its conclusion in April 2001 that the verification review episode constituted a breach by Canada of its obligations under Article 1105. In making a

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[1] Post-Hearing Submission of the United Mexican States (Damages Phase), 3 December 2001 ("Mexico's Submission").
[2] Eighth Submission of the United States of America, 3 December 2001, attaching and incorporating the Response of Respondent United States of America to Methanex's Submission Concerning the NAFTA Free Trade Commission's July 31, 2001 Interpretation ("United States Methanex Submission").
[3] Mexico's Submission, para. 2; United States Methanex Submission, page 2.

determination of damages the Tribunal must apply the governing law as set out in Article 1131, which includes the obligation to treat any Commission interpretation as binding. As the United States pointed out,[4] there is nothing improper in applying the Commission's interpretation to a pending arbitration. It is simply an application of the requirements of the governing law.

5. Damages can only be awarded if, as provided in Articles 1116 and 1117, loss or damage has been incurred "by reason of or arising out of " a breach. The Tribunal thus can make an award of damages only if the actions of Canada that allegedly caused damage constituted a breach of Article 1105. Thus, the question for the Tribunal is whether it can award damages on the basis of an earlier finding of breach if that finding was based on an incorrect interpretation of Article 1105.

6. The issue here is not one of retroactivity or non-retroactivity. The requirement that a Commission interpretation of Chapter 11 is binding on a tribunal is a statement about the limits of a Chapter 11 tribunal's authority. A tribunal carrying out its functions under the Agreement cannot, at any stage of the process, act on or draw legal consequences from an interpretation of a provision of Chapter 11 that is inconsistent with the governing law including Article 1131(2).

7. Thus, if the Tribunal based its finding of breach in respect of the verification review episode on what the Tribunal now knows to be an incorrect interpretation of Article 1105, then it would not be applying the governing law in accordance with Article 1131 if it were to proceed to award damages on the basis of that "breach". The Tribunal cannot make an award of damages on the basis of what it now knows is not a breach of Chapter 11. For the Tribunal to do so would be to ignore the governing law set out Article 1131.

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[4] United States Methanex Submission, page 5.

8. As Mexico observed,[5] the Tribunal must consider whether each of the findings leading to the conclusion that Canada had violated Article 1105 was based on an incorrect interpretation of that provision. If the Tribunal concludes that its determination of breach was not based on an incorrect interpretation of Article 1105, then it can award damages. If the Tribunal concludes that its determination of breach was based on an incorrect interpretation of Article 1105, then it cannot award damages.

PART B: THE LEGAL STANDARD APPLICABLE UNDER ARTICLE 1105

9. If the Tribunal concludes, in the light of the Notes of Interpretation, that its finding that Canada breached its obligations in respect of the verification review episode was based on an incorrect interpretation of Article 1105, it must then apply the correct legal standard as set out in the Commission's interpretation.

10. That standard, as both Mexico and the United States have pointed out, is the international minimum standard recognized under customary international law.[6] This means the minimum standard of treatment in respect of fairness that any state could be expected to provide. It is not the best standard of treatment that might be expected under domestic systems.

11. In this regard, Canada agrees with Mexico[7] that the 1989 decision of the Chamber of the International Court of Justice in the *Case Concerning Elettronic Sicula S.P.A (ELSI)*[8] provides guidance. There it referred to arbitrary conduct as a "willful disregard of due process of law, an act which shocks, or at least surprises, a sense of judicial propriety....".[9]

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[5] Mexico's Submission, para. 5.
[6] Mexico's Submission, paras 7-11; United States Methanex Submission, page 5.
[7] Mexico's Submission, para. 9.
[8] [1989] ICJ 15.
[9] *Ibid*, p. 76.

12. As Mexico pointed out,[10] this is a high threshold. It is not a domestic law standard; it is an international minimum standard. A Chapter 11 tribunal must apply this standard. It cannot claim to sit as if it were a domestic court and apply a standard that it derives from the domestic law of a particular NAFTA Party or the domestic law of the NAFTA Parties as a whole. It is for that reason that the standard applied by the Tribunal to the verification review episode was not the international minimum standard.

13. Furthermore, the Notes of Interpretation make clear that the terms fair and equitable treatment and full protection and security do not add an additional standard to the international minimum standard. Thus, that standard has to be determined on the basis of customary international law. As Mexico points out,[11] that standard has to be determined independently of the standard set out in bilateral BITs and FIPAs.

14. In response to a question raised by the Tribunal, on 16 November 2001, about the number of bilateral investment agreements, counsel for Canada gave an incorrect answer.[12] As counsel for the Investor pointed out, the number of such agreements has been estimated to be 1800.[13] But no survey of the provisions of those agreements has been placed before the Tribunal. It is not possible for the Tribunal to determine whether there is commonality in the provisions of all of those agreements and what the relationship is between those provisions and the international minimum standard under customary international law.

15. As the United States points out,[14] the use of the term "fair and equitable treatment" in bilateral investment agreements establishes nothing about the content of that term. Certainly, no conclusions can be drawn from looking only at bilateral investment agreements entered into by the United

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[10] Mexico's Submission, para. 10.
[11] *Ibid*, para. 13.
[12] Arbitration Hearing Vol. 3, p. 730.
[13] *Ibid*, p. 767.
[14] United States Methanex Submission, page 6.

States. Indeed, again as the United States points out,[15] the evidence would suggest that the terms "fair and equitable treatment" and "full protection and security" in bilateral investment agreements were intended to reflect an existing customary international law standard, and not create a new and higher standard.

16. For the Tribunal to incorporate what it sees as a higher standard set out either in BITs or FIPAs and treat that standard as the international minimum standard is to undermine the Commission's interpretation. It would constitute a failure to apply the Commission's interpretation, which Article 1131(2) requires the Commission to apply. Accordingly, if the Tribunal is to consider again the applicability of Article 1105 to the verification review episode, it is the international minimum standard of treatment that must be applied.

17. Finally, Canada notes that the United States has provided the opinion of Sir Robert Jennings in the *Methanex* case. This opinion was prepared for one party in another case, and ought not to be given any weight in this case. In any event, the Jennings opinion is irrelevant. The Notes of Interpretation are binding on the Tribunal pursuant to Article 1131(2) and form part of the governing law for these proceedings.

PART C: THE REOPENING OF ARTICLE 1102

18. As Mexico has submitted, the tribunal cannot reconsider its determination in respect of Article 1102.[16] An interpretation by the Commission does not require a Chapter 11 tribunal to reopen all of its earlier determinations. If there is no action required by a tribunal in respect of a past determination, then there is no basis for the tribunal to reconsider that determination. Nothing in Article 1131 requires or authorizes the reopening of decisions on which no further action is necessary. Moreover, under the UNCITRAL

[15] *Ibid*, pages 9-11.
[16] *Ibid*, paras 16-20.

Rules, reopening of a decision is limited to the circumstances set out in Article 36, none of which is applicable in this case. There is, therefore, no legal basis for either Party to request a reopening of the Tribunal's conclusion in respect of Article 1102. Thus, the circumstances require no action by the Tribunal in relation to Article 1102.

19. In any event, even if there were some further action to be taken with respect to Article 1102, the Notes of Interpretation would be irrelevant. The Notes of Interpretation relate to Article 1105, not Article 1102. They do not purport to provide an interpretation of Article 1102. The link between Article 1105 and 1102 is of the Tribunal's making; it does not appear in the Commission's interpretation, and it is based on a misconception of the relationship of those articles.

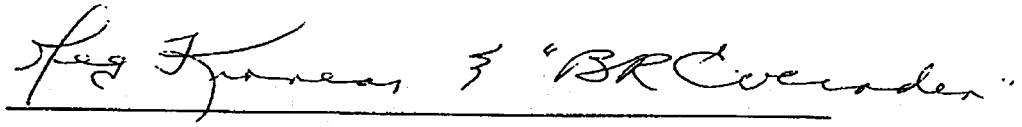
20. Furthermore, for the Tribunal to embark *proprio motu* on a reconsideration of its decision in respect of Article 1102 would be to assert a jurisdiction the Tribunal does not have. For the Tribunal to claim, as it did in the oral proceedings on November 15th,[17] that it had predicated its conclusion on Article 1102 on its ability to reach a finding against Canada on the basis of Article 1105, when such reasoning does not appear on the face of its decision, is to modify its original decision. There is no basis in law for the Tribunal to do this.

21. Finally, as Mexico has noted,[18] the Investor neither claimed that the verification review episode constituted a violation of Article 1102, nor adduced any evidence or presented any argument on the matter. There is, thus, no factual or legal basis for the Tribunal to reopen its conclusion reached on the basis of the claims made before it under Article 1102.

[17] Arbitration Hearing Vol. 3, p. 722.
[18] Mexico's Submission, para. 17.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

DATED at the City of Ottawa, the Province of Ontario, this 14th Day of December, 2001.



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